# BUSINESS, DEFAMATION, AND PRIVACY TORTS

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# BUSINESS, DEFAMATION, AND PRIVACY TORTS

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*Defamation, and Privacy Torts*
*over the past 20 years who've inspired us*

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# PREFACE

*Business, Defamation, and Privacy Torts* focuses on how individuals and businesses go about protecting intangible personal rights and recover for infringement of those rights, subject of course to the full range of defenses, some unique to this area, and some carryovers from physical and emotional torts. The thirteenth edition (2024) of our *Cases and Materials on Torts*, previewed the arrival of this advanced, companion casebook. It is our hope that these two books work a sensible division between the basic first-year torts course and an advanced, upper division course (or seminar) on torts.

This volume expands material previously covered in *Cases and Materials on Torts* (12th ed., 2020), specifically, Part Two, "Torts Against Nonphysical Interests," including the chapters on defamation, privacy, misrepresentation, and economic harms. We have inverted the order, so that we may highlight the general theme that connects these seemingly disparate areas of advanced tort law: When and why, if ever, are economic harms recoverable in tort? To begin, there are certain breaches of duty for which pecuniary losses must be honored, lest the common law fail in its promise to prevent force and fraud. More specifically, just as we all enjoy the right to be free from the threat of physical harm, so too we have the right to receive protection for the ability to make new contracts free from force and threats of force, and to be assured that others will not seek to knowingly induce breach of our existing contracts. By the same token, we also deserve to have our reputation, and those of our goods and services, protected from harmful falsehoods. Distinct privacy rights of two sorts also receive protection: first, the right to keep personal information about ourselves private, and second, to control the use of our name and likeness in commercial and business ventures.

Similar to our approach in *Cases and Materials on Torts*, our intention here has been to update the materials while preserving historical and conceptual continuity between the present and the past. In so doing, we have sought to keep one of the distinctive features of our casebooks, which is to stress the alternative visions of tort law as they developed in the nineteenth and twentieth centuries, along with the ever-larger footprint of the twenty-first century. Toward that end, we have retained in this first edition those great older cases, both English and American, that have proved themselves time and again in the classroom, and which continue to exert great influence on the modern law. By the same token, the Internet has ushered in new challenges across the board, including thorny issues of liability for actors in the "platform economy." We have sought to keep pace with these new developments, which occur both through common law and, increasingly, through legislation and regulation.



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In preparing the first edition of this casebook, we have been fortunate enough to draw on the comments of many teachers and students who have used our *Cases and Materials on Torts* casebook, now in its thirteenth edition. Over the years we have received additional assistance and suggestions on various points of chapters included in this volume from Kenneth Abraham, Cindy Estlund, and Rick Hasen. We should also like to thank, in addition, all the unnamed casebook users who have filled in their forms to explain what they did and did not like about *Cases and Materials on Torts.*

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# INTRODUCTION

The Economic Loss Rule(s) (ELR) set(s) out the fundamental choices in organizing the study of Business, Defamation, and Privacy Torts. It is here that courts most directly grapple with the question whether and why pecuniary losses must be honored, when they are no longer treated as some consequence of a physical or emotional wrong covered in the traditional first-year Torts curriculum. The ELR (Chapter 1) presents the problem of adapting familiar traditional torts to unfamiliar settings for damages and on occasion injunctive relief. It thus guides students through the complexities that follow both when the parties are in privity and when they are not. Products Liability (Chapter 2), in its modern, post-*Second Restatement* era, faced the problem forging a boundary line between contracts (dealing with disappointed expectations) and torts (dealing with bodily harms and property damage). The chapters that follow extend the analysis to more established areas of advanced tort law: misrepresentation (Chapter 3), economic harms (Chapter 4), public nuisance (Chapter 5), defamation (Chapter 6), and privacy (Chapter 7). But they all unfailingly present situations where the expansion of liability may at once be novel, dubious, and nonetheless potentially morally and socially desirable. Students must be able to appreciate the full policy and doctrinal challenges of these debates. Setting selective limits on the recovery of pecuniary losses is how the common law has adapted to economic advancements over the past 1,000 years, if not more. From the Statute of Labourers to artificial intelligence, students will encounter examples of such adaptation. Our overarching aim is to instill in you, the student, a healthy skepticism and critical engagement with advanced torts, so that even when presented with established areas like defamation, you consider why it exists at all and whether novel applications to, say, algorithmic speech comports with the fundamental aims of tort and indeed the common law.

Some final words on the organization of this book, as well as how it draws upon the material previously included in the 2020 *Cases and Materials on Tort* ("2020 CB"), as well as some overlap with Products Liability and Public Nuisance material covered in 2024 *Cases and Materials on Tort* ("2024 CB").

Chapter 1, The Economic Loss Rule(s), is entirely new. It incorporates some main cases from *2020 CB* to give the ELR its own standalone treatment. It refigures *Casa Clara* (Fla. 1993), for example, more explicitly as a case rooted in products liability, using that reasoning as a jumping off point for debating the merits, intent, and scope of the economic loss rule more generally. It also brings in more counterexamples from other states that do or do not adhere to a products-focused ELR, and also traces the ELR's roots back to the admiralty jurisprudence of the federal courts.

The chapter also makes explicit the conceptual framework of "contractual privity" and "stranger" economic loss rules (hence the "(s)" in the chapter title). The "web of contract" economic loss rule paradigm is a new addition to the book, making use of *Home Depot* (N.D. Ga. 2016) and *Schnuck* (7th Cir. 2018) to illustrate, even for proponents of the ELR, how far it may go and perhaps the limits of what courts can tolerate or manage. Finally, professional negligence is a new frontier for the ELR, showcasing *Ellis-Don Construction* (M.D.N.C. 2004) and *Terracon Consultants* (Nev. 2009). Professional malpractice is but one example of how



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broadly fraud has been interpreted, to encompass some types of negligent acts as well. In this way, wrongly asserting one's professional competence is itself a misrepresentation that must allow for appropriate recovery in tort, lest there be no recovery at all. As such, the ELR leads to an expanded economic recovery.

Chapter 2, Products Liability (an expanded version of Chapter 8 of the streamlined *2024 CB*), examines the evolution of products liability from its nineteenth-century preoccupation with privity to its modern applications in dealing with the three major classes of defects: namely those in manufacturing, design, and warning. It also addresses the ever more important question of whether, why, and when federal regulation displaces the private rights of action in duty to warn and design defect cases—the subject of intense litigation in the U.S. Supreme Court in recent years. Finally, it takes on the latest revolutions in product liability concerning dangerous products sold by online platforms.

The chapter features prominent additions in two areas: Who Is a Product Seller? and What Is a Product? The potential new era of products liability is expounded at length in the former, assessing whether Amazon and similar online retailers are sellers for goods that other parties sell on its website. The consequences of the dueling decisions of *Loomis* (Cal. Ct. App. 2021) and *McMillan* (Tex. 2021) are readily apparent: the Products Liability chapter delineates the expansion of liability from contract and privity to tort, foreseeability, and ultimately strict liability. The Amazon cases lay bare an underlying theme that can no longer be ignored: Does the expanding, unprecedented market power of a few actors make it appropriate for common law judges to expand traditional notions of duty in response to these challenges?

Separately, the *Social Media* MDL (N.D. Cal. 2023) serves as a case study on the possible extension of products liability to a growing online population, including the presence of an online student body. Design defects in algorithms now pose a novel set of challenges of addiction and exposure to third parties. The MDL judge methodically applies standard products liability doctrine to this untidy collection of issues that may shape how courts and legislatures try to deal with yet-unseen products on the market, in ways that interact with the expanded definitions of professional negligence addressed in Chapter 1 on the ELR. The prophetic remarks of Judge Traynor in *Escola* still haunt the debate some 80 years later.

Chapter 3, Misrepresentation, has undergone major revisions since *CB 2020* (Chapter 13). Section B, Fraud, now has four labeled subsections to better organize the additional material: (1) Misrepresentation and Scienter; (2) Reliance and Causation; (3) Proximate Cause; and (4) Relaxing Reliance: Securities Fraud, Class Actions, and Statutory Fraud Schemes. Relevant provisions from the *Restatement (Third): Liability for Economic Harms* have been added in the main text and in Notes where appropriate.

Section B features the most additions. To begin, the securities fraud materials have been divided and moved to each relevant subsection. Additional Notes introduce, *inter alia*, states' differing standards for "justifiable" reliance; proving reliance through circumstantial evidence and rebuttable presumptions; and contracting out of liability for fraud through no-reliance clauses. Subsection 3 (Proximate Cause) features a new main case, *Ernst & Young v. Pacific Mutual* (Tex. 2001), which considers a foreseeability-based limitation on liability for third-party reliance. Subsection 4 (Relaxing Reliance: Securities Fraud, Class Actions, and Statutory Fraud Schemes) introduces *Kaufman v. i-Stat Corp.* (N.J. 2000) as a main case, with a dueling majority and dissent squarely addressing the fraud-on-the-market theory of reliance in state law cases. The Notes explore the effect of consumer fraud class actions on reliance presumptions, and statutory fraud schemes that similarly relax or remove the reliance requirement. The *Trump* civil fraud case (N.Y. Sup. Ct. 2024) (on appeal as we go to press) is a new main case following *Kaufman*, providing one such example with major unfolding political implications.

Section C, Negligent Misrepresentation, features a new discussion of the economic loss rule in negligent misrepresentation cases. Short additional Notes include a persistent contemporary

split over whether privity is required in negligent misrepresentation, and another look at no-reliance clauses.

Chapter 4, Economic Harms, is an expanded version of Chapter 14 in *CB 2020*. In Section B, Inducement of Breach of Contract, following *Asahi* (Cal. Ct. App. 2014) there is a new Note detailing the case's relative lack of engagement in the past decade, with California courts accepting its holding perhaps without noting the alarm over "tortifying" contract law.

Section C is entirely new: Covenants Not to Compete. It presents the early case of *Mitchel v. Reynolds* (Eng. Rep. 1711) and the Federal Trade Commission's 2024 rule against non-compete agreements as main cases/authorities, and its Notes dive into the microeconomic debate underlying this area of law and policy. This section is significant as an example of the Federal Trade Commission finding a mixed reception to its effort to change the rule-of-reason approach at common law to a per se ban on the practice, a ruling that has been put on hold by the courts.

Section D, Intentional Interference with Prospective Advantage, has a new main case, *Korea Supply Co. v. Lockheed Martin Corp.* (Cal. Ct. App. 2003), which considers the level of intent required for this tort and whether the wrongfulness of the underlying action affects that inquiry. *KSC* is a significant addition, putting a spotlight on an embedded issue in intentional interference: whether the interference must be "independently wrongful" in order to be actionable.

Finally, for the new Section E, Unfair Competition, there are pending lawsuits pertaining to artificial intelligence (AI) that may be natural fits if they result in reasoned decisions. So far there is only briefing, so until then the Note material references the parties' arguments while acknowledging that it is a live issue. Moreover, the issue of federal preemption in the intellectual property arena is on the rise. *Theflyonthewall*'s (2d Cir. 2011) broad invocation of the Copyright Act reared its head prominently in the AI briefings, which is pointed out in those Notes, and will likely be in greater tension with common law unfair competition torts as time goes on.

Chapter 5, Public Nuisance, draws from and expands upon the discussion of the topic included in Chapter 7, Section E.2 of the *2024 CB*. The number of public nuisance lawsuits has ballooned in recent years, with more than 200 cases being filed since 2022 alone. Contributing to this massive increase in litigation is the expanding scope of issues that these public nuisance suits are intended to address. Traditionally, public nuisance suits were brought when the discrete actions of an individual or group affected another's ability to take advantage of a public right, typically in relation to accessing or enjoying land or water. Now, however, these suits are being brought against large multinational corporations, alleging that their actions have caused public nuisances by interfering with a far more expansive conception of public rights. This change in the focus of public nuisance lawsuits is readily apparent from the new cases added to this chapter: *City and County of San Francisco* (N.D. Cal. 2022) alleged that Walgreen's facilitated the opioid crisis and thus helped create a public nuisance, and *City of New York* (2d Cir. 2021) and *City and County of Honolulu* (Haw. 2023) alleged that a public nuisance resulted from marketing of fossil-fuels by major corporations has contributed to the climate crisis even if those emissions were from downstream parties. This theme is also apparent in Notes cases, with allegations that car companies have created a public nuisance because of a car-theft crisis, that beverage companies have created a public nuisance because their plastic bottling contributes to climate change, and that chemical companies have created a public nuisance on climate and health through the sales of their products.

Chapter 6, Defamation, updates Chapter 11 in *CB 2020*. There has been relatively little change in U.S. defamation law since 2020. The Communication Decency Act §230 still immunizes all Internet Service Providers that do not materially contribute to the illegality of the content posted on their platforms, and the Internet has made it so that more and more

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cases must meet *New York Times v. Sullivan*'s (U.S. 1964) actual malice standards (a high-bar to recovery) since it is easier than ever for people to be classified as public figures. Much of the material added to this chapter takes a prospective view of U.S. defamation law, asking how the law would look if *Sullivan* were overruled, or if §230 were amended or repealed. Many scholarly articles offer suggestions on how to improve our defamation regime, if *Sullivan* and §230 were both gone. Although U.S. Supreme Court Justices have become increasingly willing to criticize *Sullivan* and the actual malice standard, no case has as yet walked back *Sullivan*.

There have been a number of updates in defamation regimes abroad which informs the discussion of U.S. defamation law in this chapter. *Defteros* (Australia 2022) provides an interesting roadmap for handling Internet defamation cases in a purely common law regime. Beyond that, not much has changed abroad either. The UK's Defamation Act of 2013, heightening requirements to prevail in defamation suits in order to combat libel tourism, may have played a role in Johnny Depp's failure to prevail in his U.K. lawsuit, but this point is relatively tangential to the discussion of libel tourism in the present chapter.

Chapter 7, Privacy, updates Chapter 12 in *CB 2020*. Certain aspects of privacy law in the United States have changed as the expanding Internet has catapulted data privacy to the forefront of the conversation. The European Union has since enacted the General Data Protection Regulation (GDPR), which imposes a number of new duties on data processors and supplemented it with the Digital Services Act that imposes further legal obligations on the biggest search engines and online platforms. Certain states in the United States have followed the European Union's lead by enacting similar data-protective statutes (the California Consumer Privacy Act and California Privacy Rights Act of 2020, the Colorado Privacy Act, and the Consumer Data Protection Act in Virginia). While these state statutes are modeled after the GDPR, they are not quite as data protective. They do, however, place a greater emphasis on making decisions and profiling users based on artificial intelligence and automated processing of personal data, an area of privacy law that will only become more important in the coming years. While the discussions surrounding the collection and use of data by online platforms has become increasingly important in recent years, there have not been many developments in U.S. privacy law outside of these statutes, notwithstanding the many academic suggestions for change.

We have consciously edited the materials with an eye toward smoother reading. Unless the context otherwise seems to require, we have followed a loose convention of using the female pronoun for plaintiffs and the male pronoun for defendants. Citations to cases (and to cases within cases), footnotes, and other quoted material have been eliminated or simplified without any special indication, solely to remove clutter and preserve readability. The few footnotes that have been retained keep their original numbering for easier reference to the original materials. Footnotes added by the editors are indicated by an asterisk.

Richard A. Epstein
Catherine M. Sharkey
New York

December 2024

# TORTS: LIST OF CHAPTERS

***TORTS***
**Richard A. Epstein**
(Aspen Law & Business, 1999)


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# LIST OF ABBREVIATIONS

| **Abbreviation** | **Full Citation** |
| --- | --- |
| AC | Appeals Cases (to the House of Lords) |
| C.F.R. | Code of Federal Regulations |
| KB | King's Bench |
| MPC | Model Penal Code |
| QB | Queen's Bench |
| RT | REstatement of Torts |
| RLI | Restatement of the Law, Liability Insurance |
| RST | Restatement (Second) of Torts |
| RTT: IT | Restatement (Third) of Torts: Liability for Intentional Torts |
| RTT: LEH | Restatement (Third) of Torts: Liability for Economic Harm |
| RTT: LPEH | Restatement (Third) of Torts: Liability for Physical and Emotional Harm |
| RTT: PL | Restatement (Third) of Torts: Products Liability |
| RTT: UC | Restatement (Third) of Torts: Unfair Competition |



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# BUSINESS, DEFAMATION, AND PRIVACY TORTS

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## CHAPTER 1

# THE ECONOMIC LOSS RULE(S)

## SECTION A. INTRODUCTION

Our Business Torts Casebook begins with the many variations of the economic loss rule. This doctrine anchors the distinction between a course in business torts and the typical first-year semester-long torts course. Whereas 1L Torts focuses primarily on physical and emotional injuries, harms to purely *economic* or financial interests are no less significant, and these are potentially, but not uniformly, actionable in tort. These harms may arise from defective products, misrepresentations, public nuisances, defamatory statements, or invasions of privacy, among other sources of liability.

Two fundamental questions continue to vex common law courts today. Is recovery available for purely financial losses when the underlying tort is premised solely on negligence? What about when the harm arises between contracting private parties? Different iterations of the economic loss rule would say "no" to one or both of these propositions, in order to guard against potentially limitless liability for ordinary business actions, while simultaneously trying to set up a framework for the efficient negotiation of contracts.

The materials throughout this book address, through the lenses of various industries and technologies, these core issues of line-drawing. Where is the proper place to draw the line between tort and contract? How far should tort spread its wings to protect against purely financial losses? And from what sources?

## SECTION B. THEORETICAL UNDERPINNINGS AND PRODUCTS LIABILITY ROOTS

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§1. Liability for the Unintentional Infliction of Economic Loss: General Principles**

(a) An actor has no general duty to avoid the unintentional infliction of economic loss on another.

(b) Duties to avoid the unintentional infliction of economic loss are recognized principally on the terms stated [in further sections of the chapter].

### NOTES

**1.** ***Scope of Duties.*** Duties in tort "do not arise merely because an act creates a risk of economic loss to another; they require a more specific rationale." RTT: LEH §1, cmt. *a*. Why



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is negligence liability much narrower for economic harms, as compared to physical body and property harms?

**2.** ***"Indeterminate and Disproportionate Liability" Rationale.*** According to RTT: LEH §1, comment *c*:

> A single negligent utterance can cause economic loss to thousands of people who rely on it, those losses may produce additional losses to those who were relying on the first round of victims, and so on. Consequences of this sort may be at least generally foreseeable to the person who commits the negligent act. Defendants in such cases thus might face liabilities that are indeterminate and out of proportion to their culpability. Those liabilities may in turn create an exaggerated pressure to avoid an activity altogether.

Is this concern regarding ripple effects exclusive to the economic harms?

**3.** ***Deference to Contract Rationale.*** RTT: LEH §1, comment *c* adds:

> First, economic injuries caused by negligence often result from a decision by the victim to rely on a defendant's words or acts when entering some sort of transaction — an investment in a company, the purchase of a house, and so forth. A potential plaintiff making such a decision has a full chance to consider how to manage the risks involved, whether by inspecting the item or investment, obtaining insurance against the risk of disappointment, or making a contract that assigns the risk of loss to someone else. Second, money is a complete remedy for an economic injury. Insurance benefits, indemnification by agreement, or other replacements of money payments are just as good as the money lost in a transaction that turns out badly. This fungibility makes those other ways of managing risk — insurance, indemnity, and the like — more attractive than they might be to a party facing a prospect of personal injury.

How convincing are these alternative rationales for the economic loss rule?

**4.** ***How Are Economic Losses Defined?*** RTT: LEH §2 defines "economic loss" as "pecuniary damage not arising from injury to the plaintiff's person or from physical harm to the plaintiff's property." As you read the cases in this chapter, consider the extent to which this definition captures what is distinct about financial loss cases.

**Catherine M. Sharkey**

## *The Remains of the Citadel (Economic Loss Rule in Products Cases)*

100 Minn. L. Rev. 1845 (2016)

. . . By and large, "through the late 1950s and early 1960s defective product cases were controlled by contract law with its privity requirement and, to a substantially lesser extent, by negligence law." Moreover, as Prosser explained in *The Borderland of Tort and Contract*, concurrent remedies in implied warranty and negligence were commonly available; implied warranty was itself the "borderland" between tort and contract. Thus, when Prosser wrote *The Assault upon the Citadel* in 1960 — and decried, "the dam has busted, and . . . those in the path of the avalanche would do well to make for the hills" — he paid scant attention to the "refusal on the part of a few courts to allow recovery for pecuniary loss to the consumer caused by defects in the products itself, such as the cost of repairing it when it breaks down." He thus overlooked the significance of a handful of notable stalwarts, holding fast to privity in the realm of negligently-inflicted purely economic losses. . . .

[The early economic loss rule had two primary rationales.] The *Seely* [*v. White Motor Co.*] court raised a concern that liability imposed by law, that could not be disclaimed, would open the manufacturer to unknown and unlimited damages. Specifically, if a manufacturer could

not limit "the scope of his responsibility for harm caused by his products" he "would be liable for damages of unknown and unlimited scope." . . .

. . . The concern dates back to [*infra* Chapter 2, at 46]—the canonical case representing the strength of the privity barrier in the nineteenth century—where Lord Abinger warns that any plaintiff injured in any capacity by the product may be able to sue, leading to "the most absurd and outrageous consequences, to which I can see no limit." Other lords echoed this view, fearing that otherwise no limiting principle could be devised.

The floodgates concern is by no means unique to the realm of economic losses due to defective products. Indeed, it is a common fear whenever a tort right is expanded. . . . The concern of contract "drowning in a sea of tort," by contrast, moves the debate from the default of no liability in the absence of tort to the default of contract-based liability. . . .

. . . The U.S. Supreme Court picked up this rationale in *East River Steamship* [*Corp. v. Transamerica Delaval, Inc.*], when it concluded that "[d]amage to a product itself is most naturally understood as a warranty claim." . . .

. . . In other words, . . . "the courts should not ask tort law to perform a job that contract law might perform better." But what precisely falls within the wheelhouse of contract or warranty law and outside of tort?

## *Casa Clara Condominium Ass'n, Inc. v. Charley Toppino & Sons, Inc.*

620 So. 2d 1244 (Fla. 1993)

McDonald, J. . . . The issue is whether a homeowner can recover for purely economic losses from a concrete supplier under a negligence theory. We agree with the district court that such a recovery cannot be had. . . .

Charley Toppino & Sons, Inc., a dissolved corporation, supplied concrete for numerous construction projects in Monroe County. Apparently, some of the concrete supplied by Toppino contained a high content of salt that caused the reinforcing steel inserted in the concrete to rust, which, in turn, caused the concrete to crack and break off. The petitioners own condominium units and single-family homes built with, and now allegedly damaged by, Toppino's concrete. In separate actions the homeowners sued numerous defendants and included claims against Toppino for breach of common law implied warranty, products liability, negligence, and violation of the building code. The circuit court dismissed all counts against Toppino in each case. On appeal the district court applied the economic loss rule and held that, because no person was injured and no other property damaged, the homeowners had no cause of action against Toppino in tort. The district court also held that Toppino, a supplier, had no duty to comply with the building code.

Plaintiffs find a tort remedy attractive because it often permits the recovery of greater damages than an action on a contract and may avoid the conditions of a contract. The distinction between "tort recovery for physical injuries and warranty recovery for economic loss" rests

> on an understanding of the nature of the responsibility a manufacturer must undertake in distributing his products. He can appropriately be held liable for physical injuries caused by defects by requiring his goods to match a standard of safety defined in terms of conditions that create unreasonable risks of harm. *He cannot be held for the level of performance of his products in the consumer's business unless he agrees that the product was designed to meet the consumer's demands.*

Casa Clara Condominiums in Key Colony Beach, Florida
*Source: Google Maps*

Seely v. White Motor Co., 403 P.2d 145, 151 (Cal. 1965) (emphasis supplied). An individual consumer, on the other hand,

> should not be charged at the will of the manufacturer with bearing the risk of physical injury when he buys a product on the market. He can, however, be fairly charged with the risk that the product will not match his economic expectations unless the manufacturer agrees that it will.

*Id. Seely* sets out the economic loss rule, which prohibits tort recovery when a product damages itself, causing economic loss, but does not cause personal injury or damage to any property other than itself. E.g., East River Steamship Corp. v. Transamerica Delaval, Inc., 476 U.S. 858 (1986). . . .

Economic loss has been defined as "damages for inadequate value, costs of repair and replacement of the defective product, or consequent loss of profits—without any claim of personal injury or damage to other property." Note, Economic Loss in Products Liability Jurisprudence, 66 Colum. L. Rev. 917, 918 (1966). It includes "the diminution in the value of the product because it is inferior in quality and does not work for the general purposes for which it was manufactured and sold." Comment, Manufacturers' Liability to Remote Purchasers for "Economic Loss" Damages—Tort or Contract?, 114 U. Pa. L. Rev. 539, 541 (1966). In other words, economic losses are "disappointed economic expectations," which are protected by contract law, rather than tort law. This is the basic difference between contract law, which protects expectations, and tort law, which is determined by the duty owed to an injured party. For recovery in tort "there must be a showing of harm above and beyond disappointed expectations. A buyer's desire to enjoy the benefit of his bargain is not an interest that tort law traditionally protects." Redarowicz v. Ohlendorf, 441 N.E.2d 324, 327 (Ill. 1982).

The homeowners are seeking purely economic damages—no one has sustained any physical injuries and no property, other than the structures built with Toppino's concrete, has sustained any damage. They argue that holding them to contract remedies is unfair and that homeowners in general should be excepted from the operation of the economic loss rule. We disagree.

In tort a manufacturer or producer of goods "is liable whether or not it is negligent because 'public policy demands that responsibility be fixed wherever it will most effectively reduce the hazards to life and health inherent in defective products that reach the market.'" *East River*, 476 U.S. at 866 (quoting Escola v. Coca Cola Bottling Co. (Traynor, J., concurring)). . . . The purpose of a duty in tort is to protect society's interest in being free from harm, and the cost of protecting society from harm is borne by society in general. Contractual

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duties, on the other hand, come from society's interest in the performance of promises. When only economic harm is involved, the question becomes "whether the consuming public as a whole should bear the cost of economic losses sustained by those who failed to bargain for adequate contract remedies."

We are urged to make an exception to the economic loss doctrine for homeowners. Buying a house is the largest investment many consumers ever make, and homeowners are an appealing, sympathetic class. If a house causes economic disappointment by not meeting a purchaser's expectations, the resulting failure to receive the benefit of the bargain is a core concern of contract, not tort, law. There are protections for homebuyers, however, such as statutory warranties, the general warranty of habitability, and the duty of sellers to disclose defects, as well as the ability of purchasers to inspect houses for defects. Coupled with homebuyers' power to bargain over price, these protections must be viewed as sufficient when compared with the mischief that could be caused by allowing tort recovery for purely economic losses. Therefore, we again "hold contract principles more appropriate than tort principles for recovering economic loss without an accompanying physical injury or property damage." *Florida Power & Light*, 510 So. 2d at 902. If we held otherwise, "contract law would drown in a sea of tort." *East River*. We refuse to hold that homeowners are not subject to the economic loss rule.

The homeowners also argue that Toppino's concrete damaged "other" property because the individual components and items of building material, not the homes themselves, are the products they purchased. We disagree. The character of a loss determines the appropriate remedies, and, to determine the character of a loss, one must look to the product purchased by the plaintiff, not the product sold by the defendant. Generally, house buyers have little or no interest in how or where the individual components of a house are obtained. They are content to let the builder produce the finished product, i.e., a house. These homeowners bought finished products — dwellings — not the individual components of those dwellings. They bargained for the finished products, not their various components. The concrete became an integral part of the finished product and, thus, did not injure "other" property.

We also disagree with the homeowners that the mere possibility that the exploding concrete will cause physical injury is sufficient reason to abrogate the economic loss rule. This argument goes completely against the principle that injury must occur before a negligence action exists. Because an injury has not occurred, its extent and the identity of injured persons is completely speculative. Thus, the degree of risk is indeterminate, with no guarantee that damages will be reasonably related to the risk of injury, and with no possibility for the producer of a product to structure its business behavior to cover that risk. Agreeing with the homeowners' argument would make it difficult "to maintain a realistic limitation on damages." *East River*.

[Affirmed.]

Barkett, C.J., concurring in part, dissenting in part.

If the allegations of the homeowners in this case are true, their homes are literally crumbling around them because the concrete supplied by Toppino was negligently manufactured. The homeowners assert that the concrete is now cracking and breaking apart and poses a danger of serious injury. The courts, including this one, have said "too bad."

I find that answer unacceptable in light of the principle underlying Florida's access to courts provision: that absent compelling, countervailing public policies, wrongs must have remedies. Art. I, §21, Fla. Const. I understand and accept that sometimes the remedies provided cannot be in the full measure that pure justice unfettered by pragmatism can provide. Thus, some applications of the economic loss doctrine may have acceptable viability. But surely it stretches reason to apply the doctrine in this context to deny these homeowners any remedy.

Their claim for breach of implied warranty has been denied (they lack privity with Toppino); their claim that Toppino violated the Florida Building Codes Act has been denied (Toppino, as a material supplier, is not governed by the Standard Building Code); and now their claim in tort has been denied because, notwithstanding their alleged ability to prove that their houses are falling down around them, they have not suffered any damage to their property on the basis that homes are "products."

A key premise underlying the economic loss rule is that parties in a business context have the ability to allocate economic risks and remedies as part of their contractual negotiations. That premise does not exist here. Moreover, I cannot subscribe to the majority's view that the defective concrete has not damaged "other property" in the form of the houses' individual components. . . .

Shaw, J., concurring and dissenting . . .

While I agree with the majority opinion that parties who have freely bargained and entered a contract relative to a particular subject matter should be bound by the terms of that contract including the distribution of loss, I feel that the theory is stretched when it is used to deny a cause of action to an innocent third party who the defendant knew or should have known would be injured by the tortious conduct. Toppino knew that the concrete that was the subject matter of the bargain between Toppino and the general contractor would be incorporated into homes that would be bought and occupied by innocent third parties.

When the concrete proved to be contaminated, damages were not limited to simply the loss of concrete; innocent third parties suffered various degrees of damage to structures using the concrete. In my mind, the economic loss theory was never intended to defeat a tort cause of action that would otherwise lie for damages caused to a third party by a defective product.

## NOTE

***Tort or Contract?*** The economic loss rule in *Casa Clara* represents the majority position in the United States, and controls in admiralty cases as well. Thus in East River Steamship Corp. v. Transamerica Delaval, Inc., 476 U.S. 858 (1986), the Supreme Court refused to allow a tort action against the manufacturer of turbine engines that malfunctioned once installed into oil-transporting supertankers.

*Casa Clara* poses a provocative question: Why should the logic of contract apply only to economic losses but not personal injury or property damage? If contractual solutions bind parties for economic losses of $1,000,000, why do they break down for physical damage worth $1,000? Does it make a difference if the transactions are between merchants? With consumers? Conversely, if the bargaining impediments for physical damage justify overriding disclaimers for liability for physical injury, then why not for economic loss? Peters, J., dissenting in *Seely*, 403 P.2d at 153–54, so argued:

> Given the rationale of Greenman v. Yuba Power Products, Inc. [*infra* Chapter 2, at 62] it cannot properly be held that plaintiff may not recover the value of his truck and his lost profits on the basis of strict liability. The nature of the damage sustained by the plaintiff is immaterial, so long as it proximately flowed from the defect. What *is* important is not the nature of the damage but the relative roles played by the parties to the purchase contract and the nature of their transaction. . . .
>
> In *Greenman* we allowed recovery for "personal injury" damages. It is well established that such an award may include compensation for past loss of time and earnings due to the injury, for loss of future earning capacity, and for increased living expenses caused by the injury. There is no logical distinction between these losses and the losses suffered by plaintiff here. All involve

> economic loss, and all proximately arise out of the purchase of a defective product. I find it hard to understand how one might, for example, award a traveling salesman lost earnings if a defect in his car causes his *leg* to break in an accident but deny that salesman his lost earnings if the defect instead disables only his *car* before any accident occurs. The losses are exactly the same; the chains of causation are slightly different, but both are “proximate.” Yet the majority would allow recovery under strict liability in the first situation but not in the second. This, I submit, is arbitrary.

The Restatement Third of Torts: Products Liability follows *Casa Clara*. Section 1 limits the scope of the Restatement to “harms to persons or property,” which are defined in section 21 to include only “the plaintiff’s property other than the defective product itself.” See RTT: PL §21(a). In Saratoga Fishing Co. v. J.M. Martinac & Co., 520 U.S. 875 (1997), the Supreme Court treated the loss of “extra equipment (a skiff, a fishing net, spare parts) added by the initial user after the first sale and then resold as part of the ship” as “other property” for which a tort action was appropriate. Justice Breyer argued that the contractual remedy was ineffective in the context of resale after initial use “because, as other courts have suggested, the Subsequent User does not contract directly with the Manufacturer (or distributor).”

## SECTION C. “CONTRACTUAL PRIVITY” ECONOMIC LOSS RULE

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§3. Preclusion of Tort Liability Arising from Contract (Economic Loss Rule)**

Except as provided elsewhere in this Restatement, there is no liability in tort for economic loss caused by negligence in the performance or negotiation of a contract between the parties.

### NOTE

***An Economic Loss Rule for Contracting Parties.*** Instead of defining the economic loss rule to encompass a general lack of duty to avoid economic harm, RTT: LEH §3 instead drew the line closer by limiting it to contracting parties, as adopted by a majority of courts. The Restatement justifies this rule as follows:

> The rule of this Section serves several purposes. When a dispute arises, the rule protects the bargain the parties have made against disruption by a tort suit. Seen from an earlier point in the life of a transaction, the rule allows parties to make dependable allocations of financial risk without fear that tort law will be used to undo them later. Viewed in the long run, the rule prevents the erosion of contract doctrines by the use of tort law to work around them. The rule also reduces the confusion that can result when a party brings suit on the same facts under contract and tort theories that are largely redundant in practical effect . . .

RTT: LEH §3, cmt. *b*.

Some courts have adopted the economic loss rule for contracting parties grounded in deference to contract but refuse to extend it to third-party and stranger cases (discussed *infra* Section D). For example, Sullivan v. Pulte Home Corp., 306 P.3d 1, 3 (Ariz. 2013), held that while the economic loss rule between contracting parties served “to encourage the private

ordering of economic relationships, protect the expectations of contracting parties, ensure the adequacy of contractual remedies, and promote accident-deterrence and loss-spreading," those rationales did not extend to non-contracting parties.

## *Tiara Condominium Ass'n, Inc. v. Marsh & McLennan Companies, Inc.*

110 So. 3d 399 (Fla. 2013)

Labarga, J. This case is before the Court for review of a question of Florida law certified by the United States Court of Appeals for the Eleventh Circuit. . . . [T]he Eleventh Circuit certified the following question to this Court:

> DOES AN INSURANCE BROKER PROVIDE A "PROFESSIONAL SERVICE" SUCH THAT THE INSURANCE BROKER IS UNABLE TO SUCCESSFULLY ASSERT THE ECONOMIC LOSS RULE AS A BAR TO TORT CLAIMS SEEKING ECONOMIC DAMAGES THAT ARISE FROM THE CONTRACTUAL RELATIONSHIP BETWEEN THE INSURANCE BROKER AND THE INSURED?

Because the question as certified by the Eleventh Circuit is premised on the continued applicability of the economic loss rule in cases involving contractual privity, we restate the certified question as follows:

> DOES THE ECONOMIC LOSS RULE BAR AN INSURED'S SUIT AGAINST AN INSURANCE BROKER WHERE THE PARTIES ARE IN CONTRACTUAL PRIVITY WITH ONE ANOTHER AND THE DAMAGES SOUGHT ARE SOLELY FOR ECONOMIC LOSSES?

We answer this question in the negative and hold that the application of the economic loss rule is limited to products liability cases. . . .

### Facts and Procedural Background

. . . We summarize the facts here. Tiara Condominium Association (Tiara) retained Marsh & McLennan (Marsh) as its insurance broker. One of Marsh's responsibilities was to secure condominium insurance coverage. Marsh secured windstorm coverage through Citizens Property Insurance Corporation (Citizens), which issued a policy that contained a loss limit in an amount close to $50 million. In September 2004, Tiara's condominium sustained significant damage caused by hurricanes Frances and Jeanne. Tiara began the process of loss remediation. After being assured by Marsh that the loss limits coverage was per occurrence (meaning that Tiara would be entitled to almost $100 million rather than coverage in the aggregate, which would be half of that amount), Tiara proceeded with more expensive remediation efforts. However, when Tiara sought payment from Citizens, Citizens claimed that the loss limit was $50 million in the aggregate, not per occurrence. Eventually, Tiara and Citizens settled for approximately $89 million, but that amount was less than the more than $100 million spent by Tiara.

In October 2007, Tiara filed suit against Marsh, alleging (1) breach of contract, (2) negligent misrepresentation, (3) breach of the implied covenant of good faith and fair dealing, (4) negligence, and (5) breach of fiduciary duty. The trial court granted summary judgment in favor of Marsh on all claims and Tiara appealed to the Eleventh Circuit. The appeals court concluded that summary judgment was proper as to the breach of contract, negligent misrepresentation, and breach of implied covenant of good faith and fair dealing claims. However, the appeals court did not affirm the summary judgment granted by the trial court on the negligence and breach of fiduciary duty claims, which were based on Tiara's allegations that

Marsh was either negligent or breached its fiduciary duty by failing to advise Tiara of its complete insurance needs and by failing to advise Tiara of its belief that Tiara was underinsured. As to these two claims, the appeals court certified a question to this Court to determine whether the economic loss rule prohibits recovery, or whether an insurance broker falls within the professional services exception that would allow Tiara to proceed with the claims. We turn now to a discussion of the economic loss rule.

## Analysis

### Origin and Development of the Economic Loss Rule

. . . A historical review of the doctrine reveals that it was introduced to address attempts to apply tort remedies to traditional contract law damages. In *Casa Clara* [*supra* at 9] we recognized the economic loss rule as "the fundamental boundary between contract law, which is designed to enforce the expectancy interests of the parties, and tort law, which imposes a duty of reasonable care and thereby encourages citizens to avoid causing physical harm to others." *Id*. at 1246 (quoting Sidney R. Barrett, Jr., *Recovery of Economic Loss in Tort for Construction Defects: A Critical Analysis*, 40 S.C. L. Rev. 891, 894 (1989)). . . .

Simply put, the economic loss rule is a judicially created doctrine that sets forth the circumstances under which a tort action is prohibited if the only damages suffered are economic losses. *Indem. Ins. Co. of N. Am. v. Am. Aviation, Inc*., 891 So.2d 532, 536 (Fla. 2004). The rule has its roots in the products liability arena, and was primarily intended to limit actions in the products liability context. . . .

### Contractual Privity Economic Loss Rule

"The prohibition against tort actions to recover solely economic damages for those in contractual privity is designed to prevent parties to a contract from circumventing the allocation of losses set forth in the contract by bringing an action for economic loss in tort." . . . When the parties are in privity, contract principles are generally more appropriate for determining remedies for consequential damages that the parties have, or could have, addressed through their contractual agreement. Accordingly, courts have held that a tort action is barred where a defendant has not committed a breach of duty apart from a breach of contract. . . .

. . . Another situation in which this Court has determined that public policy dictates that liability not be limited to the terms of the contract involves cases such as those alleging neglect in providing professional services. . . .

### Products Liability Economic Loss Rule

Although the economic loss rule has, over time, been extended to the contractual privity context, the roots of the rule may be found in the products liability context. The products liability economic loss rule developed to protect manufacturers from liability for economic damages caused by a defective product beyond those damages provided by warranty law.

. . . Relying on the reasoning in *Seely* and *East River*, this Court adopted the products liability economic loss rule, precluding recovery of economic damages in tort where there is no property damage or personal injury, in *Florida Power & Light Co. v. Westinghouse Elec. Corp*., 510 So.2d 899 (Fla. 1987), our seminal case on the applicability of the economic loss rule. . . .

. . . We also noted that "the products liability economic loss rule articulated in *Seely* and *East River*, and adopted by this Court in *Florida Power*, applies even in the absence of privity of contract." *Id*. . . . *see also Casa Clara*, 620 So.2d at 1248 (holding cause of action against manufacturer of defective concrete was barred by the economic loss rule notwithstanding absence of privity).

Simply stated, "[t]he essence of the early holdings discussing the rule is to prohibit a party from suing in tort for purely economic losses to a product or object provided to another for consideration, the rationale being that in those cases 'contract principles [are] more appropriate than tort principles for resolving economic loss without an accompanying physical injury or property damage.'" . . .

### A Legacy of Unprincipled Expansion

For some time [describing prior cases] this Court has been concerned with what it perceived as an overexpansion of the economic loss rule. . . .

Having reviewed the origin and original purpose of the economic loss rule, and what has been described as the unprincipled extension of the rule, we now take this final step and hold that the economic loss rule applies only in the products liability context. We thus recede from our prior rulings to the extent that they have applied the economic loss rule to cases other than products liability. . . . Our experience with the economic loss rule over time, which led to the creation of the exceptions to the rule, now demonstrates that expansion of the rule beyond its origins was unwise and unworkable in practice. Thus, today we return the economic loss rule to its origin in products liability.

### Conclusion

Because we now limit the application of the economic loss rule to cases involving products liability, it is not necessary for us to decide whether the economic loss rule exception for professionals applies to insurance brokers. Based on the foregoing, we answer the rephrased certified question in the negative and hold that the application of the economic loss rule is limited to products liability cases. Having answered the rephrased certified question, we return this case to the Eleventh Circuit Court of Appeals.

It is so ordered.

Lewis and Labarga, JJ., concur.

Polston, C.J., dissenting.

The Eleventh Circuit certified the following question:

> Does an insurance broker provide a "professional service" such that the insurance broker is unable to successfully assert the economic loss rule as a bar to tort claims seeking economic damages that arise from the contractual relationship between the insurance broker and the insured?

No. This Court's controlling precedent clearly answers the certified question in the negative. But without justification, the majority greatly expands the use of tort law at a cost to Florida's contract law. Now, there are tort claims and remedies available to contracting parties in addition to the contractual remedies which, because of the economic loss rule, were previously the only remedies available.

. . . Instead of simply answering the certified question that our cases clearly control, the majority obliterates the use of the doctrine when the parties are in contractual privity, greatly expanding tort claims and remedies available without deference to contract claims. Florida's contract law is seriously undermined by this decision.

Accordingly, I respectfully dissent.

Canady, J., concurs.

Canady, J., dissenting.

For many years, this Court has recognized the vital role of the economic loss rule in maintaining the boundary between tort law and contract law. With today's decision, the majority repudiates our case law and sets a new course for the expansion of tort law at the expense of contract law. I agree with Chief Justice Polston's view that "Florida's contract law is seriously undermined by this decision," dissenting op. at 411 (Polston, C.J.), and I accordingly dissent.

[Canady, J., discusses prior precedents, including *Casa Clara*, as forging the boundary between tort law and contract law]:

> [E]conomic losses are disappointed economic expectations, which are protected by contract law, rather than tort law. This is the basic difference between contract law, which protects expectations, and tort law, which is determined by the duty owed to an injured party. For recovery in tort there must be a showing of harm above and beyond disappointed expectations. A buyer's desire to enjoy the benefit of his bargain is not an interest that tort law traditionally protects.

. . . Our cases thus have repeatedly recognized the economic loss rule as a rule that prevents contract law from "drown[ing] in a sea of tort." *Casa Clara*, 620 So.2d at 1247 (quoting *East River S.S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858, 866, 106 S. Ct. 2295, 90 L.Ed.2d 865 (1986)). The basis for this rationale—which the Court has repeatedly elaborated—is not limited to the products liability context. The application of the economic loss rule in the context of other relationships based on contract is not "unprincipled." Majority op. at 406–07. The goal of preventing contract law from drowning in a sea of tort is as compelling in the broader context of contract-based relationships as it is in the product liability context. The majority articulates no explanation of why the economic loss rule is appropriately applied in the products liability context but is unworkable or unwise in that broader context.

. . . The fact that the economic loss rule is subject to certain recognized exceptions—exceptions that are based on specific policy considerations—does not undermine the integrity of the general rule or obliterate the purpose on which it is based. On the contrary, the exceptions are predicated on the validity of the general rule. . . .

. . . With today's decision, we face the prospect of every breach of contract claim being accompanied by a tort claim. I strongly dissent from this decision. Based on the precedents explained in Chief Justice Polston's dissent, I would conclude that an insurance broker does not provide a professional service and thus is not precluded from asserting the economic loss rule as a bar to tort claims. I therefore would answer the certified question in the negative.

Polston, C.J., concurs.

## NOTES

**1.** ***Which Jurisdictions Follow* Tiara Condo *in Limiting the Economic Loss Rule to Products Liability Cases?*** Courts have lined up on both sides of *Tiara Condo*. Compare Com. Painting Co. v. Weitz Co. LLC, 676 S.W.3d 527, 540 (Tenn. 2023) ("In sum, the economic loss doctrine should only apply in products liability cases."); NM-Emerald, LLC v. Interstate Dev., LLC, 488 P.3d 707, 711 (N.M. 2021) ("In the three decades since [adopting the economic loss rule], application of the rule by New Mexico courts has occurred only in the context of strict products liability cases."); and Ellis-Don Constr., Inc. v. HKS, Inc., 353 F. Supp. 2d 603, 606 (M.D.N.C. 2004) ("[Defendant] argues that North Carolina's economic loss doctrine has expanded beyond its traditional realm of products liability and sales of goods to preclude Plaintiff's tort claim. The court disagrees."), with Holborn Corp. v. Sawgrass Mut. Ins. Co., 304 F. Supp. 3d 392, 400 (S.D.N.Y. 2018) (finding that "New York and Florida

employ different substantive rules" that are in direct conflict concerning the economic loss doctrine); Sharon Acad. v. Wieczorek Ins., 2013 Vt. Super. LEXIS 34, *5 ("While acknowledging that the [economic loss] rule had its roots in the product liability arena, Vermont has in the past declined to so restrict the doctrine [as Florida in *Tiara Condo*], holding that it now 'clearly applies to commercial disputes outside the confines of product liability.'").

**2. *Does* Tiara Condo*'s Narrow Rule Allow Creative Avoidance of the Economic Loss Rule?*** Consider In re Takata Airbag Products Liability Litigation, 193 F. Supp. 3d 1324, 1338–39 (S.D. Fla. 2016), where the plaintiffs asserted misrepresentation claims against Mazda, seeking recovery for financial losses resulting from defective airbags in their cars:

> The question before the Court, then, is whether Florida's Supreme Court, by its dicta [in *Tiara Condo*], intended to abridge the economic loss rule in the products liability setting to allow [fraud claims] even where the action for fraud depends upon precisely the same allegations as a warranty claim — i.e., a claim the product failed to work as promised.

The court concluded that because these fraud claims are "dependent on the same fundamental allegations" as products liability claims for economic loss, *Tiara Condo* implicitly barred them, in this way not "allow[ing] the economic loss rule to be manipulated." *Id*. Accord Stanley v. Nissan N. Am. Inc., 719 F.Supp.3d 786 (M.D. Tenn. Feb. 27, 2024).

What about failure-to-warn claims? Consider Nbis Construction & Transport Insurance Services v. Liebherr-America, Inc., 93 F.4th 1304, 1313–14 (11th Cir. 2024), where the plaintiff sued the distributor of a crane (which the parties stipulated was not defective) for its failure to alert the product owner of a known danger in its assembly, when the crane collapsed and destroyed itself. Given uncertainty as to whether *Tiara Condo* would allow such a claim to proceed, the Eleventh Circuit certified the question to the Florida Supreme Court. With regard to distributors of products, does it make sense for so much to turn on whether the underlying claims are framed as negligence as opposed to products liability claims? What about if the product services provider is outside the chain of product distribution?

**3. *Is* Tiara Condo*'s Approach to the Economic Loss Rule Justified?*** Is there a compelling rationale for applying the economic loss rule to products liability, but no further? Recall Catherine M. Sharkey, Remains of the Citadel, *supra* at 2, discussing the products liability origins of the economic loss rule. But in both that history and the Restatement's modern justifications, *supra* at 7, the "deference to contract" rationale does not seem logically limited to products liability; in fact it might seem strongest where the parties are in privity, which is canonically not the case in the products realm. Consider this framework while reading *Sheen*.

## *Sheen v. Wells Fargo Bank, N.A.*

505 P.3d 625 (Cal. 2022)

Cantil-Sakauye, C.J. Several years after purchasing his house, plaintiff Kwang K. Sheen used the home as collateral for two loans he took from defendant Wells Fargo Bank, N.A. (Wells Fargo). Plaintiff subsequently suffered financial setbacks and missed payments on these junior loans. He submitted applications to Wells Fargo to modify the loans, but Wells Fargo did not respond. Instead, it sent plaintiff letters informing him of the actions it might take because of the delinquency of his accounts. The letters did not specifically mention foreclosure. Plaintiff alleges that because "Wells Fargo did not provide [him] with a written determination regarding his eligibility for modification" of the loans prior to sending him the letters, plaintiff "believed the letters meant that the . . . [l]oans had been modified such that they were

unsecured loans" and his house "would never be sold at a foreclosure auction." Eventually, Wells Fargo sold plaintiff's debt. Four years later, the owner of the debt foreclosed on plaintiff's home. Plaintiff sued Wells Fargo.

Specifically, plaintiff asserted a negligence claim against Wells Fargo, alleging that the bank "owed Plaintiff a duty of care to process, review and respond carefully and completely to the loan modification applications Plaintiff submitted." . . . Wells Fargo demurred, arguing that it owed plaintiff no such duty. The Court of Appeal affirmed the lower court's decision to sustain the demurrer but noted that "[t]he issue of whether a tort duty exists for mortgage modification has divided California courts for years." (*Sheen v. Wells Fargo Bank, N.A.* (2019) 38 Cal. App. 5th 346, 348 (*Sheen*).)

In this case, we address the issue dividing the lower courts: Does a lender owe the borrower a tort duty sounding in general negligence principles to (in plaintiff's words) "process, review and respond carefully and completely to [a borrower's] loan modification application," such that upon a breach of this duty the lender may be liable for the borrower's economic losses — i.e., pecuniary losses unaccompanied by property damage or personal injury? We conclude that there is no such duty, and thus Wells Fargo's demurrer to plaintiff's negligence claim was properly sustained. . . .

## II. Discussion

. . . Plaintiff does not point to any specific language in his contract — which evidently contains no provisions obligating Wells Fargo to review or respond to plaintiff's modification application — as the source of this duty. Instead, he claims that the duty arises as a matter of law when a borrower submits a loan modification application to a lender, and that a lender's failure "to process, review and respond carefully and completely" to the application is actionable in tort.

Whether such a tort duty exists is an issue upon which the Courts of Appeal are divided. . . .

### A. Statutory Law

Plaintiff does not identify any statute or regulation that requires Wells Fargo to treat his modification applications with due care. . . .

### B. Common Law

Rather than focusing on any statute, plaintiff grounds his negligence claim in the common law. We conclude that this effort fails in light of the economic loss rule. . . .

#### 1. Economic Loss Rule

We begin with a review of the contours of the economic loss rule. The rule itself is deceptively easy to state: In general, there is no recovery in tort for negligently inflicted "purely economic losses," meaning financial harm unaccompanied by physical or property damage. . . .

The economic loss rule has been applied in various contexts. First, it carries force when courts are concerned about imposing "'liability in an indeterminate amount for an indeterminate time to an indeterminate class.'"

In another recurring set of circumstances, the rule functions to bar claims in negligence for pure economic losses in deference to a contract between litigating parties. Regarding this latter branch of the doctrine, one scholar has stated, "Using contract law to govern commercial transactions lets parties and their lawyers know where they stand and what they can expect to follow legally from the words they have written. But if a disappointed buyer has the option of abandoning the contract and suing in tort, the significance of the contract is diminished

and the doctrines that protect the integrity of the contractual process are reduced in importance. . . . (Farnsworth, *The Economic Loss Rule* (2016) 50 Val. U. L. Rev. 545, 553–554 (Farnsworth).) The Restatement states this form of the economic loss rule thusly: "[T]here is no liability in tort for economic loss caused by negligence in the performance or negotiation of a contract between the parties." (Rest., §3.)

Because it involves parties who are in contractual privity, this strand of the economic loss rule is sometimes referred to as the "contractual economic loss rule," "contractual rule," or "consensual paradigm." (See, e.g., Sharkey, *In Search of the Cheapest Cost Avoider: Another View of the Economic Loss Rule* (2018) 85 U. Cin. L. Rev. 1017, 1018–1019 (Sharkey); Dobbs, *An Introduction to Non-Statutory Economic Loss Claims* (2006) 48 Ariz. L. Rev. 713, 714.) . . .

#### *a. The Economic Loss Rule Bars Plaintiff's Negligence Claim*

Plaintiff and Wells Fargo had a contract. Plaintiff's complaint alleges that he "obtained a second-lien residential mortgage from Wells Fargo" that was "secured by the Property pursuant to a deed of trust." Plaintiff thus had an agreement with Wells Fargo that specified the parties' rights and obligations with respect to the mortgage loan and the collateral securing the loan. In particular, the fact that the mortgage was "secured by the Property pursuant to a deed of trust" (impliedly with the power of sale) means the parties agreed that Wells Fargo would have the right to seize and sell the property in satisfaction of the debt should plaintiff stop making payments on the loan. . . . These were the terms of the parties' agreement.

Plaintiff and Wells Fargo did *not* agree that should plaintiff default and attempt to renegotiate his loan by submitting a modification application, Wells Fargo would "process, review and respond carefully and completely to the . . . applications Plaintiff submitted," and could foreclose only after discharging such obligations. To impose a tort duty in such circumstances would go further than creating obligations unnegotiated or agreed to by the parties; it would dictate terms that are *contrary* to the parties' allocation of rights and responsibilities. . . .

#### *b. Policy Considerations*

. . . [T]he rationales behind the economic loss rule provide a compelling basis to reject "a duty of care to process, review and respond carefully and completely to . . . loan modification applications." . . .

Plaintiff raises two broad policy arguments. First, he argues that without the ability to bring a negligence claim, he would be left "without any remedy at all" and as such, a viable tort claim is needed to prevent injury to borrowers like himself. Yet there are causes of action *other* than a general claim of negligence for failing to exercise reasonable care in processing, reviewing, and responding to a borrower's loan modification application that may offer recourse to borrowers who suffer injury due to missteps by a lender (or loan servicer) in connection with the handling of a mortgage modification application. Two such causes of action are negligent misrepresentation and promissory estoppel. . . .

. . . Furthermore, even taking at face value plaintiff's argument that "no other source of law addresses the harm that [he] identifies," plaintiff is not limiting the sought-for tort duty to only those instances when other sources of law fall short. . . . In essence, even if plaintiff has identified a gap in the law, he is not proposing to fill that gap. Instead, he seeks to layer a new and expansive negligence cause of action atop all existing laws, imposing a tort duty with indefinite boundaries.

We are unpersuaded that such a remedy should be created by judicial fiat. Plaintiff recognizes that lawmakers at both the state and federal levels have been active in regulating the mortgage loan modification process. . . . In contrast with such detailed schemes, tort liability—with a yet-to-be articulated standard of care—is ill defined and amorphous. We remain uncertain how such differing regulatory and statutory frameworks will function in practice, much less that they might operate together to better serve the interests of borrowers,

lenders, or the public at large. The vagueness and breadth of plaintiff's proposed duty thus counsel against imposing that duty to correct for the problems he contends exist.

Plaintiff's second argument, that allowing his tort claim to go forward will "prevent[] future harm," relies on asserted market failures within the mortgage industry. . . . Such market failures, plaintiff argues, justify judicial intervention.

We observe at the outset that insofar as plaintiff has identified a problem, he is not proposing to tailor his proposed solution to the problem in any way. . . .

### III. Conclusion

We hold that when a borrower requests a loan modification, a lender owes no tort duty sounding in general negligence principles to "process, review and respond carefully and completely to" the borrower's application. Because the Court of Appeal's decision is in accord, we affirm the judgment below.

Liu, J., concurring. . . . [T]his case calls our attention to an important area that may warrant further consideration by the Legislature. As many reported decisions detail, borrowers seeking mortgage loan modifications may be strung along by loan servicers' incompetence, pursuit of fees, or improper incentives over the course of years, leading borrowers to forgo other remedies. According to Sheen, the California Homeowner Bill of Rights (HBOR), designed "to ensure that . . . borrowers are considered for, and have a meaningful opportunity to obtain, available loss mitigation options" (Civ. Code, §2923.4), "imposes a narrow set of duties on servicers"; its "protections are insufficient to cover the myriad ways in which a servicer's negligence can injure borrowers when it comes to loan modification." The frequency with which these issues are making their way through the courts — along with what the Civil Justice Association of California, California Chamber of Commerce, and Western Bankers Association as amici curiae call the "Damoclean repeat of the 2008–2012 foreclosure crisis [that] looms on the horizon" — suggests that legislative action may be warranted. . . .

## NOTES

**1.** ***To What Extent Is* Sheen *Supported by the Rationale of the Restatement (Third)?*** Recall that RTT: LEH §3 applies the economic loss rule only to "economic loss caused by negligence in the performance or negotiation of a contract between the parties." It does not say, as the *Sheen* majority implies, that a cognizable tort duty must be wholly "independent of the original . . . contract." The majority finds a sufficient relation between Sheen's claim and the mortgage contract; the claim "is based on an asserted duty that is contrary to the rights and obligations clearly expressed in the loan contract." But there are myriad non-waivable rights that undermine contracts in this way — for example, you generally cannot waive your right to bring a fraud claim arising out of that same contract, see *infra* Chapter 3. Was the asserted breach of duty in *Sheen*, then, "negligence in the performance or negotiation" of the mortgage contract, or does the majority have a broader conception of the economic loss rule?

In his concurrence, Liu, J., noted that the majority "does not state a broad rule against recovery for pure economic loss in tort in the context of a contractual relationship, and courts should not invoke the rule without considering the basis for its application." Is he advocating for a case-by-case approach, or invoking the Restatement's narrower scope of actions "in the performance or negotiation" of contracts? What should be done if the bank had explicitly refused to modify or otherwise renegotiate the loan after Sheen was in default?

**2. *A Traditional Tort Justification for the Economic Loss Rule.*** Catherine M. Sharkey, In Search of the Cheapest Cost Avoider: Another View of the Economic Loss Rule, 85 U. Cin. L. Rev. 1017, 1018–19 (2018) — cited by the *Sheen* majority — posits an efficiency rationale for the economic loss rule:

> A cheapest cost avoider framework highlights how the economic loss rule functions as an information-forcing default rule. It incentivizes the party with superior knowledge of the nature and depth of its potential injury to share that information with the party that may be liable for such harm. In other words, the victim often has superior information and ability to minimize financial losses. . . .
>
> . . . Unlike the primacy of contract rationale, the cheapest cost avoider rationale directs attention to the fact that the party in the best position to reduce economic risks should take responsibility for taking affirmative steps to avoid such losses, whereas imposition of tort liability could place the burden on a party who must either take difficult or expensive measures to ascertain the risks present.

Consider this efficiency framework in the "stranger" paradigm and in the context of professional negligence in the sections that follow.

## SECTION D. "STRANGER" ECONOMIC LOSS RULE

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§7. Economic Loss from Injury to a Third Person or to Property Not Belonging to the Claimant**

Except as provided elsewhere in this Restatement, a claimant cannot recover for economic loss caused by

(a) unintentional injury to another person; or

(b) unintentional injury to property in which the claimant has no proprietary interest.

### *People Express Airlines, Inc. v. Consolidated Rail Corp.*

495 A.2d 107 (N.J. 1985)

Handler, J. This appeal presents a question that has not previously been directly considered: whether a defendant's negligent conduct that interferes with a plaintiff's business resulting in purely economic losses, unaccompanied by property damage or personal injury, is compensable in tort. The appeal poses this issue in the context of the defendants' alleged negligence that caused a dangerous chemical to escape from a railway tank car, resulting in the evacuation from the surrounding area of persons whose safety and health were threatened. The plaintiff, a commercial airline, was forced to evacuate its premises and suffered an interruption of its business operations with resultant economic losses.

#### I.

. . . On July 22, 1981, a fire began in the Port Newark freight yard of defendant Consolidated Rail Corporation (Conrail) when ethylene oxide manufactured by defendant BASF

Wyandotte Company (BASF) escaped from a tank car, punctured during a "coupling" operation with another rail car, and ignited. The tank car was owned by defendant Union Tank Car Company (Union Car) and was leased to defendant BASF.

People Express airplanes dating from the 1980s, when the company was based in Newark, New Jersey. The company sold its fleet to Continental Airlines in 1987.

*Information source: History of People Express, AvStop.com, http://avstop.com/history/historyofairlines/peoplexpress.htm*
*Image source: Scott McKiernan / ZUMA Wire / zumapress.com / Alamy Live News*

The plaintiff asserted at oral argument that at least some of the defendants were aware from prior experiences that ethylene oxide is a highly volatile substance; further, that emergency response plans in case of an accident had been prepared. When the fire occurred that gave rise to this lawsuit, some of the defendants' consultants helped determine how much of the surrounding area to evacuate. The municipal authorities then evacuated the area within a one-mile radius surrounding the fire to lessen the risk to persons within the area should the burning tank car explode. The evacuation area included the adjacent North Terminal building of Newark International Airport, where plaintiff People Express Airlines' (People Express) business operations are based. Although the feared explosion never occurred, People Express employees were prohibited from using the North Terminal for twelve hours.

The plaintiff contends that it suffered business-interruption losses as a result of the evacuation. These losses consist of cancelled scheduled flights and lost reservations because employees were unable to answer the telephones to accept bookings; also, certain fixed operating expenses allocable to the evacuation time period were incurred and paid despite the fact that plaintiff's offices were closed. No physical damage to airline property and no personal injury occurred as a result of the fire.

According to People Express' original complaint, each defendant acted negligently and these acts of negligence proximately caused the plaintiff's harm. An amended complaint alleged additional counts of nuisance and strict liability based on the defendants' undertaking an abnormally dangerous activity, as well as defective manufacture or design of the tank car, causes of action with which we are not concerned here. . . .

## II.

The single characteristic that distinguishes parties in negligence suits whose claims for economic losses have been regularly denied by American and English courts from those who have recovered economic losses is, with respect to the successful claimants, the fortuitous occurrence of physical harm or property damage, however slight. It is well-accepted that a defendant who negligently injures a plaintiff or his property may be liable for all proximately caused harm, including economic losses. Nevertheless, a virtually per se rule barring recovery for economic loss unless the negligent conduct also caused physical harm has evolved throughout this century, based, in part, on Robins Dry Dock & Repair Co. v. Flint, 275 U.S. 303 (1927) and Cattle v. Stockton Waterworks Co., 10 Q.B. 453 (1875). This has occurred although neither case created

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a rule absolutely disallowing recovery in such circumstances. See, e.g., Stevenson v. East Ohio Gas Co., 73 N.E.2d 200 (Ohio Ct. App. 1946) (employee who was prohibited from working at his plant, which was closed due to conflagration begun by negligent rupture of stored liquified natural gas at nearby utility, could not recover lost wages); Byrd v. English, 43 S.E. 419 (Ga. 1903) (plaintiff who owned printing plant could not recover lost profits when defendant negligently damaged utility's electrical conduits that supplied power to the plant); see also Restatement (Second) of Torts §766C (1979) (positing rule of nonrecovery for purely economic losses absent physical harm). But see In re Kinsman Transit Co., 388 F.2d 821, 824 (2d Cir. 1968) (after rejecting an inflexible rule of nonrecovery, court applied traditional proximate cause analysis to claim for purely economic losses).

The reasons that have been advanced to explain the divergent results for litigants seeking economic losses are varied. Some courts have viewed the general rule against recovery as necessary to limit damages to reasonably foreseeable consequences of negligent conduct. This concern in a given case is often manifested as an issue of causation and has led to the requirement of physical harm as an element of proximate cause. In this context, the physical harm requirement functions as part of the definition of the causal relationship between the defendant's negligent act and the plaintiff's economic damages; it acts as a convenient clamp on otherwise boundless liability. The physical harm rule also reflects certain deep-seated concerns that underlie courts' denial of recovery for purely economic losses occasioned by a defendant's negligence. These concerns include the fear of fraudulent claims, mass litigation, and limitless liability, or liability out of proportion to the defendant's fault. . . .

The troublesome concern reflected in cases denying recovery for negligently-caused economic loss is the alleged potential for infinite liability, or liability out of all proportion to the defendant's fault. This objection is also not confined to negligently-caused economic injury. The same objection has been asserted and, ultimately, rejected by this Court and others in allowing recovery for other forms of negligent torts, see H. Rosenblum, Inc. v. Adler, 461 A.2d 138 (N.J. 1983), and in the creation of the doctrine of strict liability for defective products, see Feldman v. Lederle Laboratories, 479 A.2d 374 (N.J. 1984); Henningsen v. Bloomfield Motors, Inc., 161 A.2d 69 (N.J. 1960), and ultrahazardous activities, see Dep't of Envtl. Protection v. Ventron Corp., 468 A.2d 150 (N.J. 1983). The answer to the allegation of unchecked liability is not the judicial obstruction of a fairly grounded claim for redress. Rather, it must be a more sedulous application of traditional concepts of duty and proximate causation to the facts of each case.

It is understandable that courts, fearing that if even one deserving plaintiff suffering purely economic loss were allowed to recover, all such plaintiffs could recover, have anchored their rulings to the physical harm requirement. While the rationale is understandable, it supports only a limitation on, not a denial of, liability. The physical harm requirement capriciously showers compensation along the path of physical destruction, regardless of the status or circumstances of individual claimants. Purely economic losses are borne by innocent victims, who may not be able to absorb their losses. In the end, the challenge is to fashion a rule that limits liability but permits adjudication of meritorious claims. The asserted inability to fix crystalline formulae for recovery on the differing facts of future cases simply does not justify the wholesale rejection of recovery in all cases.

Further, judicial reluctance to allow recovery for purely economic losses is discordant with contemporary tort doctrine [with its twin objectives of legal redress for victims and deterrence of future harms by others].

**A.**

Judicial discomfiture with the rule of nonrecovery for purely economic loss throughout the last several decades has led to numerous exceptions in the general rule. Although the rationalizations for these exceptions differ among courts and cases, two common threads run throughout the exceptions. The first is that the element of foreseeability emerges as a more appropriate analytical standard to determine the question of liability than a per se prohibitory rule. The second is that the extent to which the defendant knew or should have known the particular consequences of his negligence, including the economic loss of a particularly foreseeable plaintiff, is dispositive of the issues of duty and fault.

One group of exceptions is based on the "special relationship" between the tortfeasor and the individual or business deprived of economic expectations. [The court then refers to liability for negligent misrepresentation under *Rosenblum, infra* Chapter 3, Note 2.]

Courts have found it fair and just in all of these exceptional cases to impose liability on defendants who, by virtue of their special activities, professional training or other unique preparation for their work, had particular knowledge or reason to know that others, such as the intended beneficiaries of wills or the purchasers of stock who were expected to rely on the company's financial statement in the prospectus (*Rosenblum*), would be economically harmed by negligent conduct. In this group of cases, even though the particular plaintiff was not always foreseeable, the particular class of plaintiffs was foreseeable as was the particular type of injury.

A very solid exception allowing recovery for economic losses has also been created in cases akin to private actions for public nuisance. Where a plaintiff's business is based in part upon the exercise of a public right, the plaintiff has been able to recover purely economic losses caused by a defendant's negligence [citing Union Oil Co. v. Oppen, 501 F.2d 558 (9th Cir. 1974) (fishermen making known commercial use of public waters may recover economic losses due to defendant's oil spill)]. . . .

These exceptions expose the hopeless artificiality of the per se rule against recovery for purely economic losses. When the plaintiffs are reasonably foreseeable, the injury is directly and proximately caused by defendant's negligence, and liability can be limited fairly, courts have endeavored to create exceptions to allow recovery. The scope and number of exceptions, while independently justified on various grounds, have nonetheless created lasting doubt as to the wisdom of the per se rule of nonrecovery for purely economic losses. Indeed, it has been fashionable for commentators to state that the rule has been giving way for nearly fifty years, although the cases have not always kept pace with the hypothesis. . . .

We hold therefore that a defendant owes a duty of care to take reasonable measures to avoid the risk of causing economic damages, aside from physical injury, to particular plaintiffs or plaintiffs comprising an identifiable class with respect to whom defendant knows or has reason to know are likely to suffer such damages from its conduct. A defendant failing to adhere to this duty of care may be found liable for such economic damages proximately caused by its breach of duty.

We stress that an identifiable class of plaintiffs is not simply a foreseeable class of plaintiffs. For example, members of the general public, or invitees such as sales and service persons at a particular plaintiff's business premises, or persons travelling on a highway near the scene of a negligently-caused accident, such as the one at bar, who are delayed in the conduct of their affairs and suffer varied economic losses, are certainly a foreseeable class of plaintiffs. Yet their presence within the area would be fortuitous, and the particular type of economic injury that could be suffered by such persons would be hopelessly unpredictable and not realistically foreseeable. Thus, the class itself would not be sufficiently ascertainable. An identifiable class of plaintiffs must be particularly foreseeable in terms of the type of persons or entities comprising the class, the certainty or predictability of their presence, the approximate numbers of those in the class, as well as the type of economic expectations disrupted.

B.

Liability depends not only on the breach of a standard of care but also on a proximate causal relationship between the breach of the duty of care and resultant losses. The standard of particular foreseeability may be successfully employed to determine whether the economic injury was proximately caused, i.e., whether the particular harm that occurred is compensable, just as it informs the question whether a duty exists. . . .

We conclude therefore that a defendant who has breached his duty of care to avoid the risk of economic injury to particularly foreseeable plaintiffs may be held liable for actual economic losses that are proximately caused by its breach of duty. In this context, those economic losses are recoverable as damages when they are the natural and probable consequence of a defendant's negligence in the sense that they are reasonably to be anticipated in view of defendant's capacity to have foreseen that the particular plaintiff or identifiable class of plaintiffs is demonstrably within the risk created by defendant's negligence.

III.

We are satisfied that our holding today is fully applicable to the facts that we have considered on this appeal. Plaintiff has set forth a cause of action under our decision, and it is entitled to have the matter proceed to a plenary trial. Among the facts that persuade us that a cause of action has been established is the close proximity of the North Terminal and People Express Airlines to the Conrail freight yard; the obvious nature of the plaintiff's operations and particular foreseeability of economic losses resulting from an accident and evacuation; the defendants' actual or constructive knowledge of the volatile properties of ethylene oxide; and the existence of an emergency response plan prepared by some of the defendants (alluded to in the course of oral argument), which apparently called for the nearby area to be evacuated to avoid the risk of harm in case of an explosion. We do not mean to suggest by our recitation of these facts that actual knowledge of the eventual economic losses is necessary to the cause of action; rather, particular foreseeability will suffice. The plaintiff still faces a difficult task in proving damages, particularly lost profits, to the degree of certainty required in other negligence cases. The trial court's examination of these proofs must be exacting to ensure that damages recovered are those reasonably to have been anticipated in view of the defendants' capacity to have foreseen that this particular plaintiff was within the risk created by their negligence.

We appreciate that there will arise many similar cases that cannot be resolved by our decision today. The cause of action we recognize, however, is one that most appropriately should be allowed to evolve on a case-by-case basis in the context of actual adjudications. We perceive no reason, however, why our decision today should be applied only prospectively. Our holdings are well grounded in traditional tort principles and flow from well-established exceptional cases that are philosophically compatible with this decision.

Accordingly, the judgment of the Appellate Division is modified, and, as modified, affirmed. The case is remanded for proceedings consistent with this opinion.

## NOTES

**1.** ***Tort Recovery for Economic Loss Between Non-Contracting Parties.*** As *People Express* indicates, the common law judges historically have been reluctant to allow any recovery for pure economic losses attributable only to the defendant's negligence. Most notably, in Byrd v. English, 43 S.E. 419, 420 (Ga. 1903), the defendant's negligent excavation severed the

power lines, owned by the electric company, that supplied the power to the plaintiff's plant. The plaintiff's cause of action against the contractor was denied on grounds reminiscent of Winterbottom v. Wright [*infra* Chapter 2, at 46]:

> According to this petition, the damage done by them was to the property of the Georgia Electric Light Company, which was under contract to furnish to the plaintiff electric power, and the resulting damage done to the plaintiff was that it was rendered impossible for that company to comply with its contract. If the plaintiff can recover of these defendants upon this cause of action, then a customer of his, who was injured by the delay occasioned by the stopping of his work, could also recover from them; and one who had been damaged through his delay could in turn hold them liable; and so on without limit to the number of persons who might recover on account of the injury done to the property of the company owning the conduits. To state such a proposition is to demonstrate its absurdity. The plaintiff is suing on account of an alleged tort by reason of which he was deprived of a supply of electric power with which to operate his printing establishment. What was his right to that power supply? Solely the right given him by virtue of his contract with the Georgia Electric Light Company, and with that contract the defendants are not even remotely connected. If, under the terms of his contract, he is precluded from recovering from the electric light company, that is a matter between themselves for which the defendants certainly can not be held responsible. They are, of course, liable to the company for any wrong that may have been done it, and the damages recoverable on that account might well be held to include any sums which the company was compelled to pay in damages to its customers; but the customers themselves can not go against the defendants to recover on their own account for the injury done the company.

Similarly, in Cattle v. Stockton Waterworks Co., [1875] 10 Q.B. 453, 457, the defendant waterworks company had negligently constructed and maintained its pipes on the land of one Knight. The plaintiff had been hired for a fixed reward to build a tunnel on Knight's land and incurred increased costs when the water from the defendant's leaky pipes flooded his operations. Blackburn, J., conceded that Knight could have recovered damage for the increased cost of the completion if he had constructed the tunnel himself, but he denied that this plaintiff could recover for those same costs. He argued that if the action were allowed

> we should establish an authority for saying that, in such a case as that of *Fletcher v. Rylands* the defendant would be liable, not only to an action by the owner of the drowned mine, and by such of his workmen as had their tools or clothes destroyed, but also to an action by every workman and person employed in the mine, who in consequence of its stoppage made less wages than he otherwise would have done.

A narrow view of recovery for economic loss was also taken in Robins Dry Dock & Repair Co. v. Flint, 275 U.S. 303, 308–09 (1927). The plaintiffs hired a boat on a time charter with the third-party owner. The terms of the time charter called for the boat to be docked for maintenance and repaired once every six months, with payments of money on the charter suspended until the boat was returned to service. While the boat was in the defendant's docks, the defendant negligently damaged the propeller, thereby causing the plaintiffs to lose the use of the boat for a two-week period while the necessary repairs were made. The defendant undertook repair of the boat in ignorance of the time charter or its terms. The accident took place in August 1917, shortly after the United States entered World War I, so the time charter gave the plaintiff highly favorable rates. In an earlier action arising out of the same incident, The Bjornefjord, 271 F. 682 (2d Cir. 1921), the plaintiff was not allowed to recover the lost value of his charter from the boat owner on a contract theory that the owner had discharged its obligation by selecting a competent independent contractor for the repairs. But in Flint v. Robins Dry Dock & Repair Co.,

13 F.2d 3, 5 (2d Cir. 1926), the Second Circuit awarded recovery to the plaintiff in tort. Mack, J., reasoned:

> Clearly, the result reached involves no injustice to respondent. Its liability for its tortious act is for the actual damage done to the combined interests in the ship. The measure of the total recovery is the market value of the loss of the use. If there had been no charter, the entire loss would have been sustained by the owner; therefore he could have recovered that amount himself. The wrongdoer has no interest in and should not benefit because of the contractual obligations of the shipowner to the charterer, or the absence of any liability of the owner to the charterer for respondent's negligence. This nonliability of the owner is neither a test nor a measure of the wrongdoer's liability, for, though the owner be not directly liable to the charterer, he may nevertheless be liable over to him as a trustee for so much of the recovery from the wrongdoer as exceeds his own personal loss.

Holmes, J., writing for a unanimous Supreme Court, reversed the Second Circuit and dismissed the plaintiff-respondent's cause of action:

> The question is whether the respondents [charterers] have an interest protected by the law against unintended injuries inflicted upon the vessel by third persons who know nothing of the charter. If they have, it must be worked out through their contract relations with the owners, not on the postulate that they have a right *in rem* against the ship.
>
> Of course the contract of the petitioner [Dry Dock Company] with the owners imposed no immediate obligation upon the petitioner to third persons, as we already have said, and whether the petitioner performed it promptly or with negligent delay was the business of the owners and of nobody else. But as there was a tortious damage to a chattel it is sought to connect the claim of the respondents with that in some way. The damage was material to them only as it caused the delay in making the repairs, and that delay would be a wrong to no one except for the petitioner's contract with the owners. The injury to the propeller was no wrong to the respondents but only to those to whom it belonged. But suppose that the respondent's loss flowed directly from that source. Their loss arose only through their contract with the owners — and while intentionally to bring about a breach of contract may give rise to a cause of action, no authority need be cited to show that, as a general rule, at least, a tort to the person or property of one man does not make the tortfeasor liable to another merely because the injured person was under a contract with that other, unknown to the doer of the wrong. The law does not spread its protection so far.

275 U.S. at 308–09.

Can Judge Mack's position be sustained if the contract between the charterer and the owner precludes recovery of lost profits attributable to the negligence of the owner? Can Justice Holmes's position be sustained if that contract allows expectation damages? For an argument that Holmes's rule is defensible so long as the charter arrangement is ignored, whether the rentals move up or down, see Victor P. Goldberg, Recovery for Pure Economic Loss in Tort: Another Look at *Robins Dry Dock v. Flint*, 20 J. Legal Stud. 249 (1991). In essence, the losses suffered in those cases when charter prices move up are offset by the windfall that is gained when the charterer is released from a losing contract by the wrongful act of a third party. The Holmes position remains the majority view today. See Nautilus Marine, Inc. v. Niemela, 170 F.3d 1195, 1197 (9th Cir. 1999), in which the court rebuffed the plaintiff's effort to escape *Robins* by pleading the defendant's recklessness. "The line between recklessness and negligence is sufficiently indistinct that extensive litigation would be likely to ensue before *Robins Dry Dock* could be applied in any case." Is it?

With *Robins*, contrast J'Aire Corp. v. Gregory, 598 P.2d 60, 64 (Cal. 1979), in which the plaintiff restaurant could not open for business because the defendant contractor failed to complete work on the heating and air conditioning system on premises owned by a third party and leased in part to plaintiff. The question before the court was "whether a contractor

who undertakes construction work pursuant to a contract with the owner of premises may be held liable in tort for business losses suffered by a lessee when the contractor negligently fails to complete the project with due diligence." The court answered the question in the affirmative for much the same reasons adopted in *People Express*.

> [T]his court finds that respondent [defendant] had a duty to complete construction in a manner that would have avoided unnecessary injury to appellant's business, even though the construction contract was with the owner of a building rather than with appellant, the tenant. It is settled that a contractor owes a duty to avoid injury to the person or property of third parties. As appellant points out, injury to a tenant's business can often result in greater hardship than damage to a tenant's person or property. Where the risk of harm is foreseeable, as it was in the present case, the injury to the plaintiff's economic interests should not go uncompensated merely because it was unaccompanied by any injury to his person or property.

Should the tenant in *J'Aire* be limited to an action against its landlord? After *J'Aire*, should construction companies insert clauses into their standard contracts that either require landlords to obtain waivers from actual or prospective tenants against the construction company or call on the landlord to indemnify the construction company for its expenses or losses? That strategy is not, however, open in cases such as *People Express*, in which the plaintiff and the defendant are total strangers. If the release of dangerous chemicals is a strict liability action, why require proof of negligence for recovery of economic loss in *People Express*? And why adopt more stringent tests of foresight? Are the results in any of these cases defensible under *People Express*?

**2.** ***An Economic Analysis of Economic Losses.*** Finding a theoretical justification for disallowing recovery for pure economic loss at common law has not been easy. The defendant is by hypothesis negligent; the plaintiff's harm is typically foreseeable, even if the precise identity of the plaintiff is not; rarely do any intervening acts or events sever the causal connection; and typically there are no affirmative defenses based on the plaintiff's misconduct. Why then the denial?

Apart from the administrative concerns, the law and economics literature has offered two explanations for the dominant legal rule. W. Bishop, Economic Loss in Tort, 2 Oxford J. Legal Stud. 1 (1982), suggests that the economic losses to the plaintiffs do not represent social losses because whatever business is lost by the plaintiff is picked up by some rival firm whose "excess capacity" can meet the increased demand. That argument is vulnerable on two separate grounds. First, some social loss always remains because the substitute performance is more costly than that originally contemplated—otherwise the plaintiff would not have obtained the business in the first place. Second, the unprotected plaintiff will take excessive precautions to avoid losses that are far more costly than the substitute precautions open to the negligent defendant.

An alternative explanation for the rule, suggested in Mario J. Rizzo, A Theory of Economic Loss in the Law of Torts, 11 J. Legal Stud. 281 (1982), is to reduce the number of potential suits by "channeling" tort liability through a small class of plaintiffs, typically those who have suffered physical injury. The property owner who recovers losses can reimburse the contractors and others for their increased costs of completion under contract, as may have been intimated, for example, in both Cattle v. Stockton Waterworks and Robins Dry Dock & Repair Co. v. Flint, discussed *supra* at 17.

Some support for this position comes from the application of the traditional privity limitation, which is intended to prevent the proliferation of possible plaintiffs in both *Byrd* and *Cattle*. That same issue arises in both regulatory and antitrust contexts, where the same privity limitation reasserts itself. Thus in Southern Pacific Co. v. Darnell-Taenzer Lumber Co., 245 U.S. 531, 533–34 (1918), Justice Holmes held that a shipper could recover an overcharge

from a regulated railroad even though it had itself recovered some of the excess costs from its customers. "The general tendency of the law, in regard to damages at least, is not to go beyond the first step. As it does not attribute remote consequences to a defendant so it holds him liable if proximately the plaintiff has suffered a loss." The corollary to this position is that the remote purchaser cannot recover for the same loss precisely because the immediate purchaser is entitled to recover the full loss without offset. See generally for its application in antitrust cases Illinois Brick v. Illinois, 431 U.S. 720 (1977). Note that the privity limitation couples strong deterrence with economic efficiency.

**Exhibit 1.1 Judith Smith Kaye**

Judith Smith Kaye (1938–2016) was the first woman and longest-serving chief judge to sit on the New York Court of Appeals, the state's highest court. Governor Mario Cuomo first appointed her to the bench in 1983, and she became chief judge in 1993 after her predecessor, Sol Wachtler, was forced to resign amidst scandal. A graduate of Barnard College and New York University School of Law, Chief Judge Kaye made her mark on criminal law, New York state constitutional law, and the legal rules surrounding attorney practice. Her state constitutional jurisprudence was characterized by a more expansive interpretation of individual rights relative to the U.S. jurisprudence. As chief judge, she also oversaw the entire New York state court system, spearheading initiatives to modernize the courts and championing access to justice for the citizens of New York. Kaye joined the firm Skadden, Arps, Slate, Meagher & Flom LLP after retiring from the Court of Appeals in 2009.

*Bio source: Crane, Judith Smith Kaye, Historical Society of the New York Courts*
*Image source: Wikimedia Commons*

## *532 Madison Ave. Gourmet Foods, Inc. v. Finlandia Center, Inc.*

750 N.E.2d 1097 (N.Y. 2001)

Kaye, C.J. The novel issues raised by these appeals — arising from construction-related disasters in midtown Manhattan — concern first, a landholder's duty in negligence where plaintiffs' sole injury is lost income and second, the viability of claims for public nuisance.

Two of the three appeals involve the same event. On December 7, 1997, a section of the south wall of 540 Madison Avenue, a 39-story office tower, partially collapsed and bricks, mortar and other material fell onto Madison Avenue at 55th Street, a prime commercial location crammed with stores and skyscrapers. The collapse occurred after a construction project, which included putting 94 holes for windows into the building's south wall, aggravated existing structural defects. New York City officials directed the closure of 15 heavily trafficked blocks on Madison Avenue — from 42nd to 57th Street — as well as adjacent side streets between Fifth and Park Avenues. The closure lasted for approximately two weeks, but some businesses nearest to 540 Madison remained closed for a longer period.

In *532 Madison Ave. Gourmet Foods v. Finlandia Ctr.*, plaintiff operates a 24-hour delicatessen one-half block south of 540 Madison, and was closed for five weeks. The two named

plaintiffs in the companion case, *5th Ave. Chocolatiere v. 540 Acquisition Co.*, are retailers at 510 Madison Avenue, two blocks from the building, suing on behalf of themselves and a putative class of "all other business entities, in whatever form, including but not limited to corporations, partnerships and sole proprietorships, located in the Borough of Manhattan and bounded geographically on the west by Fifth Avenue, on the east by Park Avenue, on the north by 57th Street and on the South by 42nd Street." Plaintiffs allege that shoppers and others were unable to gain access to their stores during the time Madison Avenue was closed to traffic. Defendants in both cases are Finlandia Center (the building owner), 540 Acquisition Company (the ground lessee) and Manhattan Pacific Management (the managing agent).

On defendants' motions in both cases, Supreme Court dismissed plaintiffs' negligence claims on the ground that they could not establish that defendants owed a duty of care for purely economic loss in the absence of personal injury or property damage, and dismissed the public nuisance claims on the ground that the injuries were the same in kind as those suffered by all of the businesses in the community. In *5th Ave. Chocolatiere*, plaintiffs' additional claims for gross negligence and negligence per se were dismissed on the ground that plaintiffs could not establish a duty owed by defendants, and their private nuisance cause of action was dismissed on the ground that they could not establish either intentional or negligent wrongdoing.

*Goldberg Weprin & Ustin v. Tishman Constr.* involves the July 21, 1998 collapse of a 48-story construction elevator tower on West 43rd Street between Sixth and Seventh Avenues—the heart of bustling Times Square. Immediately after the accident, the City prohibited all traffic in a wide area of midtown Manhattan and also evacuated nearby buildings for varying time periods. Three actions were consolidated—one by a law firm, a second by a public relations firm and a third by a clothing manufacturer, all situated within the affected area. Plaintiff law firm sought damages for economic loss on behalf of itself and a proposed class "of all persons in the vicinity of Broadway and 42nd Street, New York, New York, whose businesses were affected and/or caused to be closed" as well as a subclass of area residents who were evacuated from their homes. Plaintiff alleged gross negligence, strict liability, and public and private nuisance.

Noting the enormity of the liability sought, including recovery by putative plaintiffs as diverse as hot dog vendors, taxi drivers and Broadway productions, Supreme Court concluded that the failure to allege personal injury or property damage barred recovery in negligence. The court further rejected recovery for strict liability, and dismissed both the public nuisance claim (because plaintiff was unable to show special damages) and the private nuisance claim (because plaintiff could not show that the harm threatened only one person or relatively few).

The Appellate Division affirmed dismissal of the *Goldberg Weprin* complaint, concluding that, absent property damage, the connection between defendants' activities and the economic losses of the purported class of plaintiffs was "too tenuous and remote to permit recovery on any tort theory" (275 A.D.2d 614, 713 N.Y.S.2d 57). The court, however, reinstated the negligence and public nuisance claims of plaintiffs *532 Madison* and *5th Ave. Chocolatiere*, holding that defendants' duty to keep their premises in reasonably safe condition extended to "those businesses in such close proximity that their negligent acts could be reasonably foreseen to cause injury" (which included the named merchant plaintiffs) (272 A.D.2d 23, 712 N.Y.S.2d 8) and that, as such, they established a special injury distinct from the general inconvenience to the community at large. Two Justices dissented, urging application of the "economic loss" rule, which bars recovery in negligence for economic damage absent personal injury or property damage. The dissenters further concluded that the public nuisance claims were properly dismissed because plaintiffs could not establish special injury.

We now reverse in *532 Madison* and *5th Ave. Chocolatiere* and affirm in *Goldberg Weprin & Ustin*.

## Plaintiffs' Negligence Claims

Plaintiffs contend that defendants owe them a duty to keep their premises in reasonably safe condition, and that this duty extends to protection against economic loss even in the absence of personal injury or property damage. Defendants counter that the absence of any personal injury or property damage precludes plaintiffs' claims for economic injury.

The existence and scope of a tortfeasor's duty is, of course, a legal question for the courts, which "fix the duty point by balancing factors, including the reasonable expectations of parties and society generally, the proliferation of claims, the likelihood of unlimited or insurer-like liability, disproportionate risk and reparation allocation, and public policies affecting the expansion or limitation of new channels of liability." At its foundation, the common law of torts is a means of apportioning risks and allocating the burden of loss. In drawing lines defining actionable duty, courts must therefore always be mindful of the consequential, and precedential, effects of their decisions.

As we have many times noted, foreseeability of harm does not define duty. Absent a duty running directly to the injured person there can be no liability in damages, however careless the conduct or foreseeable the harm. This restriction is necessary to avoid exposing defendants to unlimited liability to an indeterminate class of persons conceivably injured by any negligence in a defendant's act.

A duty may arise from a special relationship that requires the defendant to protect against the risk of harm to plaintiff. Landowners, for example, have a duty to protect tenants, patrons and invitees from foreseeable harm caused by the criminal conduct of others while they are on the premises, because the special relationship puts them in the best position to protect against the risk. That duty, however, does not extend to members of the general public. Liability is in this way circumscribed, because the special relationship defines the class of potential plaintiffs to whom the duty is owed. . . .

Plaintiffs' reliance on *People Express* [*supra* at 16] is misplaced. . . . Allowing the plaintiff to seek damages for purely economic loss, the New Jersey court reasoned that the extent of liability and degree of foreseeability stand in direct proportion to one another: the more particular the foreseeability that economic loss would be suffered as a result of the defendant's negligence, the more just that liability be imposed and recovery permitted. The New Jersey court acknowledged, however, that the presence of members of the public, or invitees at a particular plaintiff's business, or persons traveling nearby, while foreseeable, is nevertheless fortuitous, and the particular type of economic injury that they might suffer would be hopelessly unpredictable. Such plaintiffs, the court recognized, would present circumstances defying any appropriately circumscribed orbit of duty. We see a like danger in the urban disasters at issue here, and decline to follow *People Express*.

Policy-driven line-drawing is to an extent arbitrary because, wherever the line is drawn, invariably it cuts off liability to persons who foreseeably might be plaintiffs. The *Goldberg Weprin* class, for example, would include all persons in the vicinity of Times Square whose businesses had to be closed and a subclass of area residents evacuated from their homes; the *5th Ave. Chocolatiere* class would include all business entities between 42nd and 57th Streets and Fifth and Park Avenues. While the Appellate Division attempted to draw a careful boundary at storefront merchant-neighbors who suffered lost income, that line excludes others similarly affected by the closures—such as the law firm, public relations firm, clothing manufacturer and other displaced plaintiffs in *Goldberg Weprin*, the thousands of professional, commercial and residential tenants situated in the towers surrounding the named plaintiffs, and suppliers and service providers unable to reach the densely populated New York City blocks at issue in each case.

As is readily apparent, an indeterminate group in the affected areas thus may have provable financial losses directly traceable to the two construction-related collapses, with no satisfactory way geographically to distinguish among those who have suffered purely economic losses. In such circumstances, limiting the scope of defendants' duty to those who have, as a result of these events, suffered personal injury or property damage — as historically courts have done — affords a principled basis for reasonably apportioning liability.

We therefore conclude that plaintiffs' negligence claims based on economic loss alone fall beyond the scope of the duty owed them by defendants and should be dismissed.

[The court's handling of plaintiffs' public nuisance claims is taken up in Chapter 5.]

## *Southern California Gas Co. v. Superior Court of Los Angeles County*

441 P.3d 881 (Cal. 2019)

Cuellar, J. This case concerns a massive, months-long leak from a natural gas storage facility located just outside Los Angeles. . . . [T]he accident severely harmed the economy of a nearby suburb. We must decide if local businesses — none of which allege they suffered personal injury or property damage — may recover in negligence for income lost because of the leak. Our decision turns on whether the entity that allegedly caused the leak had a tort duty to guard against what we and other courts have termed "purely economic losses." . . .

### I.

Near the northwestern corner of Los Angeles lies Porter Ranch, a residential neighborhood home to some 30,000 people. Southern California Gas Company (SoCalGas) stores vast amounts of natural gas in an underground facility [the "Aliso Facility"] in the hills surrounding the community. . . .

In October 2015, a leak happened — and people noticed. An uncontrolled flow of natural gas from the Aliso Facility coated nearby neighborhoods in an oily mist. At its peak, the leak released some 55 tons of natural gas every hour. Porter Ranch residents reported unpleasant odors, headaches, dizziness, and respiratory problems. In addition to those symptoms, students at local schools complained of nosebleeds and vomiting.

That November, the Los Angeles County health department directed SoCalGas to establish a relocation program available to Porter Ranch residents who lived within a five-mile radius of the leak site. . . . About 15,000 people were relocated in total, scattering to locations dozens — and in some cases hundreds — of miles away. . . .

Plaintiffs are Porter Ranch area businesses seeking to represent a class of "[a]ll persons and entities conducting business within five miles of the Facility from October 23, 2015 to [the] present." They allege that SoCalGas's negligence caused the leak. The resulting relocation of many Porter Ranch residents devastated the local economy: by depriving local businesses of customers, the environmental disaster cost local businesses considerable earnings. . . .

SoCalGas demurred, arguing that Plaintiffs' negligence claims failed as a matter of law because Plaintiffs were seeking to recover for purely economic losses. Overruling the demurrer, the trial court explained that companies "must face the full cost of accidents" they create, or else "they will underinvest in precautions." . . .

[The Court of Appeal reversed the trial court.]

## II.

. . . The issue here is whether SoCalGas—separate from other legal and practical reasons it had to prevent injury of any kind to the public—had a tort duty to guard against negligently causing what we and others have called "purely economic loss[es]." . . . [W]e conclude it had no tort duty to guard against purely economic losses.

In California, the "general rule" is that people owe a duty of care to avoid causing harm to others and that they are thus usually liable for injuries their negligence inflicts. . . . [W]e have frequently begun our analysis by presuming a duty of care. But we have not universally done so. A case in point is liability in negligence for purely economic losses, which is "the exception, not the rule" under our precedents. . . .

The primary exception to the general rule of no recovery for negligently inflicted purely economic losses is where the plaintiff and the defendant have a "special relationship" [citing *J'Aire*, *supra* at 22]. What we mean by special relationship is that the plaintiff was an intended beneficiary of a particular transaction but was harmed by the defendant's negligence in carrying it out. . . .

Concerned about line-drawing problems and potentially overwhelming liability, courts across the country have rejected recovery for purely economic losses stemming from man-made calamity. [The court discusses *532 Madison, supra* at 24, and several other cases that rejected recovery for purely economic losses.]

Against all these decisions, only the New Jersey Supreme Court's opinion in *People Express Airlines, Inc*. [*supra* at 16] cuts definitively the other way. . . . Yet decades after the demise of the airline that gave the case its name, *People Express* remains "a lonely outpost."

The allegations before us underscore the ineluctable difficulty associated with imposing a duty to guard against purely economic losses in negligence cases like this one. It may be possible to quantify the profits any one business lost because of an industrial accident, but imposing such a duty would nevertheless create line-drawing problems across—quite literally—space and time. . . . We lack clear spatial bounds within which to cabin claims like those asserted here.

This case does not involve a so-called special relationship under our precedents. Plaintiffs concede—as they must—that their only relevant ties to SoCalGas are having the misfortune of operating near the Aliso Facility. Accordingly, they propose to limit the class they seek to represent based on geographic proximity alone. Putative class members here are businesses operating "in the area within five miles" of the leak, a space which Plaintiffs characterize as "the precise area from which residents were evacuated." . . .

We see no workable way to limit geographically who may recover purely economic losses. Without one, the dangers of indeterminate liability, over-deterrence, and endless litigation are at their apex. Nor do we see a viable way to limit temporally what purely economic losses could be recovered here. . . . True: we could conceivably cabin recovery for purely economic losses to those suffered during the disaster alone. Or we could allow recovery only for such losses suffered during a business closure, not merely for systemic hits to economic demand. Yet upon closer inspection, the alluring simplicity of both approaches quickly proves to be a mirage. . . .

. . . [W]e recognize Plaintiffs' concern that SoCalGas's alleged negligent behavior will go insufficiently deterred if we deny recovery here. But SoCalGas is not getting off scot free. At oral argument, the company represented that some 50,000 claimants have alleged in other litigation that they suffered property damage caused by the leak—several hundred of whom are local businesses. It further informed us, and we have no reason to doubt, that the company has spent some $450 million on remedial measures and agreed to pay another $120 million as part of a settlement with local authorities. SoCalGas, operating in a heavily regulated domain, also remains under investigation—and may face further consequences in the future.

### III.

Risks from industrial accidents raise grave concerns for society, and we have no doubt the accident precipitating this case caused significant hardships. To compensate those harmed and to deter those who do the harming, our society assigns tort law a pivotal role. But that does not mean society's interests are best served by extending its scope indefinitely. Meaningful limits on tort liability, along with the incentives they set, are crucial to the functioning of our economy and of our courts. Where such limits leave gaps in our social fabric, tort does not stand alone: insurance also compensates, regulation also deters. And where gaps persist, the Legislature can act.

The better part of a century has passed since then-Judge Cardozo warned that permitting recovery in negligence for purely economic losses can threaten indeterminacy-cubed: "liability in an indeterminate amount for an indeterminate time to an indeterminate class." (Ultramares Corp. v. Touche [*infra* Chapter 3]). Courts across the country have since heeded that warning, by and large denying recovery in negligence cases like this one even though purely economic losses inflict real pain. That prevailing rule of no recovery is, like society itself, imperfect. Yet nearly everyone follows a rule that few (if any) entirely like. California does, too.

[Affirmed.]

## NOTES

**1.** ***Rejection of* People Express *and an Economic Loss Rule for Stranger Cases?*** Cuellar, J., declines to follow *People Express* and notes the near unanimous repudiation of the decision by the courts. In *532 Madison Ave.*, Chief Judge Kaye both rejects and distinguishes *People Express*. She suggests that the plaintiffs could not meet its "particular foreseeability" standard, where "the presence of members of the public, or invitees at a particular plaintiff's business, or persons traveling nearby, while foreseeable, is nevertheless fortuitous." Could a channeling rationale explain the different outcomes in *532 Madison Ave.* and *People Express*?

RTT: LEH §7 embraces the holding and rationale of *532 Madison Ave*. It rejects *People Express* as a "[c]ontrary position . . . taken only occasionally in the case law." RTT: LEH §7, cmt. *a*. The Restatement justifies its rule as follows:

> (1) "economic losses can proliferate long after the physical forces at work in an accident have spent themselves"; (2) "[r]ecognizing claims for those sorts of losses would greatly increase the number, complexity, and expense of potential lawsuits"; (3) "recognition of such claims would also result in liabilities that are indeterminate and out of proportion to the culpability of the defendant"; and (4) "victims of economic injury often can protect themselves effectively by means other than a tort suit [including "first-party insurance against their losses" or "recover[y] in contract"].

RTT: LEH §7, cmt. *b*.

The Restatement acknowledges the tradeoffs at play here:

> Denying claims by rule undeniably works a hardship on plaintiffs with claims that fall outside the policies that make the rule attractive — claims that do not lend themselves to solution by contract . . . or that present no problems of indeterminacy. But a rule against recovery has other advantages: predictability, clarity, and economy of application for courts, lawyers, and those attempting to plan their affairs and anticipate their liabilities.

*Id*. Should this rule be sensitive to the magnitude of these economic losses? How about a rule that allows only the first tier of aggrieved parties (the businesses, but not their customers and employees) to sue for their losses?

**2. *The Least Cost Avoider Framework.*** Union Oil Co. v. Oppen, 501 F.2d 558 (9th Cir. 1974), cited in *People Express*, recognized negligence and public nuisance claims by commercial fisherman who sued Union Oil for the loss of catch attributable to its pollution of the Santa Barbara Channel. The court adopted an economic approach that required it "to fix the identity of the party who can avoid the costs most cheaply. Once fixed, this determination then controls liability." See, e.g., Guido Calabresi, The Cost of Accidents 69–73 (1970). If the cheapest cost avoider cannot be determined, who is the "party who can best correct any error in allocation, if such there be, by acquiring the activity to which the party has been made liable"? Sneed, J., suggested that on this second criterion, "there is no contest — the defendants' capacity is superior." How is the buyout possible if the class of fisherman constantly shifts in its composition? Note the parallel to the farmer's difficulty in bargaining with ranchers under an open-range regime.

Consider now in the stranger context in Catherine M. Sharkey, In Search of the Cheapest Cost Avoider, *supra* at 14:

> In the stranger cases — such as *People Express* and *532 Madison Avenue Gourmet* — it could be argued that the business victims are in a better position than the potentially negligent stranger tortfeasor to assess the cost and to mitigate ex post any business interruption due to negligence. As an initial matter, business interruption insurance is readily available to the putative victims. Moreover, certain particular features of these economic losses likewise tip the balance in favor of the victim as cheapest cost avoider. First, business interruption losses are the kind of losses that occur regularly even absent any wrongdoing; putative victims thus develop experience and expertise in terms of managing and reducing them. Second, such losses tend to accumulate over time; as a result, victims tend to operate over a long term horizon in terms of mitigating them. Taken together, the victim can structure its operations — for example, by maintaining spare parts, excess capacity, and alternative operating modes — so as to minimize any compounding of losses. Seen in this light, the economic loss rule provides incentives for potential plaintiffs to exercise optimal care and to self-insure efficiently.
>
> But the case for a per se stranger economic loss rule based on cheapest cost avoider principles is not airtight. Such a blanket no-duty rule could lead unprotected plaintiffs to take excessive precautions that are far costlier than substitute precautions available to the negligent defendant tortfeasor.

**3. *Insurance and the "Stranger" Paradigm.*** Justice Cuéllar suggests that the economic loss rule incentivizes the acquisition of first-party insurance: "Now certain that a lawsuit seeking purely economic losses of this sort will not succeed, businesses operating near a natural gas storage facility — or a dam, shipping lane, oil well, and so forth — may be inclined to buy insurance covering profits they stand to lose if disaster strikes." 441 P.3d at 895. Does Justice Cuéllar blur the distinction between commercial property insurance, which covers only physical damage, and a more far-reaching form of insurance for pure economic losses? See Kenneth S. Abraham & Catherine M. Sharkey, The Glaring Gap in Tort Theory, 133 Yale L.J. 2165, 2214 n.194 (2024). Does the latter form of insurance even exist? The Southern California Gas Company contends it does. See Southern California Gas Co.'s Response to Briefs of Amicus Curiae, In re S. Cal. Gas Leak Cases, 441 P.3d 881 (Cal. 2019) (No. S246669) ("Moreover, Plaintiffs' 'particular foreseeability' test would if anything have a perverse effect. It would protect as 'particularly foreseeable' large companies like People Express, which have access to first-party insurance to protect against economic interruption. But it would fail to protect many smaller enterprises with fewer resources to insure against economic loss — especially mobile or itinerant business actors like taxi drivers, ice cream vendors or door-to-door salesmen, whose presence in any one location is not 'particularly foreseeable.'"). Does it make sense to encourage plaintiffs to insure against a substantial interference with a public right? Are public nuisances *ipso facto* unforeseeable?

## SECTION E. THIRD-PARTY OR "WEB OF CONTRACT" ECONOMIC LOSS CASES

### In re *The Home Depot, Inc., Customer Data Security Breach Litigation*

No. 1:14-md-2583-TWT, 2016 WL 2897520 (N.D. Ga. May 18, 2016)
(MDL Docket No. 2583)

Thrash, J. Between April 2014 and September 2014, the Defendant, The Home Depot, Inc., was the subject of one of the largest retail data breaches in history. Hackers stole the personal and financial information of approximately 56 million Home Depot customers across the country. The hackers then sold the information on the internet to thieves who made large numbers of fraudulent transactions on credit and debit cards issued to Home Depot customers.

The Defendant makes a large portion of its sales to customers who use credit or debit cards. Merchants such as the Defendant acquire large amounts of information about each customer when processing card transactions, including the card data and potentially personally identifiable information ("PII") such as financial data and mailing addresses. The Defendant has stored that data in its computer systems for years. In fact, the Defendant stores PII indefinitely. Starting in 2008, the Defendant identified the potential repercussions of a data breach as a risk factor for its business in its annual report and SEC filings. . . .

[After years of internal, external, and government warnings about the vulnerability of its systems, Home Depot did not enhance its cybersecurity, making it known that the company would not allocate funds for this purpose. A confirmed hack of at least eight point-of-sale terminals in one store led to further unheeded warnings about the company's firewall.]

Beginning in April of 2014, hackers gained access to the Defendant's computer systems using the credentials of a third party vendor, which they were able to do because of the firewall flaw. The hackers were able to freely access the network without triggering any alarms. Inside the network, the hackers targeted the point-of-sale systems at 7,500 self-checkout lanes. They installed malware on those systems that siphoned off the information from a payment card when it was used at a self-checkout lane. The malware remained on the self-checkout terminals until around September 7, 2014. Between September 1, 2014, and September 7, 2014, the credit and debit card information of the Defendant's customers was made available for sale on a black-market website. . . .

On September 2, 2014, a security blogger reported that banks were seeing evidence of fraud linked to cards that had made purchases at the Defendant's stores. The U.S. Secret Service also alerted the Defendant that its computer systems had likely been breached. At that point, the Defendant noted that it was looking into the situation, but did not confirm a breach. On September 6, 2014, the Defendant's investigators confirmed that a security breach had taken place, but did not publicly disclose that information. On September 8, 2014, the Defendant issued a news release that its systems had been breached, but failed to warn that its customers' information was for sale and being used by criminals. On November 6, 2014, the Defendant issued a news release announcing the results of its internal investigation; it admitted that data security should have been a higher priority and that its systems were woefully out of date.

The Plaintiffs here are a putative class of financial institutions that issued and owned payment cards compromised by the data breach. . . . The putative financial institution class alleges that it has been damaged by having to reimburse customers for the fraud losses suffered

due to the data breach as well as by other costs such as having to reissue payment cards. The putative class brings claims for negligence and negligence per se, as well as violation of eight state-specific consumer protection statutes. The putative class also seeks injunctive and declaratory relief. . . . The Defendant moves to dismiss. . . .

## III. Discussion

### B. Negligence and Negligence Per Se

. . . [T]he Defendant argues that the Plaintiffs' negligence and negligence per se claims are barred by the economic loss rule. "The 'economic loss rule' generally provides that a contracting party who suffers purely economic consequences must seek his remedy in contract and not in tort." In other words, "a plaintiff may not recover in tort for purely economic damages arising from a breach of contract." Where, however, "an independent duty exists under the law, the economic loss rule does not bar a tort claim because the claim is based on a recognized independent duty of care and thus does not fall within the scope of the rule." Here, even though there is a contract between the card issuers and the Plaintiffs, the independent duty exception would bar application of the economic loss rule. Georgia recognizes a general duty "to all the world not to subject them to an unreasonable risk of harm." A retailer's actions and inactions, such as disabling security features and ignoring warning signs of a data breach, are sufficient to show that the retailer caused foreseeable harm to a plaintiff and therefore owed a duty in tort. Here, the Plaintiffs have pleaded that the Defendant knew about a substantial data security risk dating back to 2008 but failed to implement reasonable security measures to combat it. This Court therefore finds that an independent duty existed, barring application of the economic loss rule.

The Court declines the Defendant's invitation to hold that it had no legal duty to safeguard information even though it had warnings that its data security was inadequate and failed to heed them. To hold that no such duty existed would allow retailers to use outdated security measures and turn a blind eye to the ever-increasing risk of cyber attacks, leaving consumers with no recourse to recover damages even though the retailer was in a superior position to safeguard the public from such a risk. The Defendant's motion to dismiss based on the economic loss rule should be denied. Additionally, the Defendant moves to dismiss the Plaintiffs' negligence claim on the ground that it owed no duty to the Plaintiffs. Because this Court finds that a duty does exist, the motion to dismiss on the ground that there was no duty should also be denied.

[Motion to dismiss granted in part and denied in part.]

## *Community Bank of Trenton v. Schnuck Markets, Inc.*

887 F.3d 803 (7th Cir. 2018)

Hamilton, C.J. In late 2012, hackers infiltrated the computer networks at Schnuck Markets, a large Midwestern grocery store chain based in Missouri and known as "Schnucks." The hackers stole the data of about 2.4 million credit and debit cards. By the time the intrusion was detected and the data breach was announced in March 2013, the financial losses from unauthorized purchases and cash withdrawals had reached into the millions. Litigation ensued.

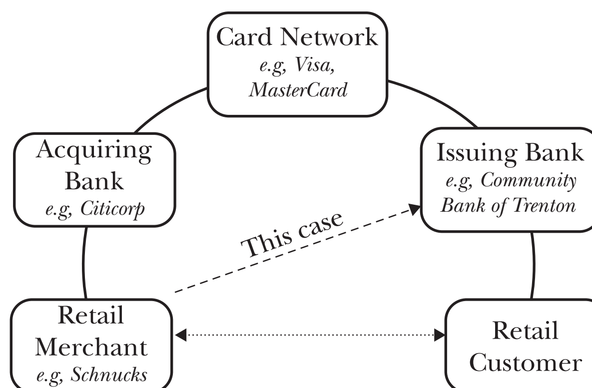
Like many other recent cases around the country, this case involves a massive consumer data breach. . . . Unlike most other data-breach cases, however, the proposed class of plaintiffs

in this case is comprised not of consumers but of financial institutions. Card-issuing banks and credit unions are required by federal law to indemnify their card-holding customers for losses from fraudulent activity, so our four plaintiff-appellant banks here bore the costs of reissuing cards and indemnifying the Schnucks hackers' fraud. See 15 U.S.C. §1643(a) (limiting credit-card-holder liability for unauthorized use); 12 C.F.R. §205.6 (limiting debit-card-holder liability for unauthorized use). The Article III standing and injury issues that arose in . . . many other data-breach cases with consumer plaintiffs are not issues in this case.

The principal issues in this case present fairly new variations on the economic loss rule in tort law. The central issue is whether Illinois or Missouri tort law offers a remedy to card-holders' banks against a retail merchant who suffered a data breach, above and beyond the remedies provided by the network of contracts that link merchants, card-processors, banks, and card brands to enable electronic card payments. The plaintiff banks assert claims under the common law as well as Illinois consumer protection statutes. Our role as a federal court applying state law is to predict how the states' supreme courts would likely resolve these issues. We predict that both states would reject the plaintiff banks' search for a remedy beyond those established under the applicable networks of contracts. Accordingly, we affirm the district court's dismissal of the banks' complaint.

## I. Factual Background and Procedural History

When a customer uses a credit or debit card at a retail store, the merchant collects the customer's information. This includes the card-holder's name and account number, the card's expiration date and security code, and, in the case of a debit card, the personal identification number. Collectively, this payment card information is known as "track data." At the time of purchase, the track data and the amount of the intended purchase are forwarded electronically to the merchant's bank (the "acquiring bank"), usually through a payment processing company. The acquiring bank then requests payment from the customer's bank (the "issuing bank") through the relevant card network — in this case, Visa or MasterCard. If the issuing bank approves the purchase, the transaction goes through within seconds. The customer's issuing bank then pays the merchant's acquiring bank the amount of the customer's purchase, which is credited to the merchant's account, minus processing fees. Contracts govern all of these relationships, although typically no contracts directly link the merchant (e.g., Schnucks) with the issuing banks (our four plaintiffs here). Here is a simplified diagram of this series of relationships:




In this case, Schnucks routed customer track data through a payment processor, First Data Merchant Services, to its acquiring bank, Citicorp. Citicorp then routed customer track data

through the card networks to the issuing banks (plaintiffs here), who approved purchases and later collected payments from their customers, the card-holders. This web of contractual relationships facilitates the dotted line above: the familiar retail purchase by a customer from a merchant. Because Schnucks was the weak security link in this regime, the plaintiff banks seek to recover directly from Schnucks itself, a proposed line of liability represented by the dashed line above. This new form of liability would be in addition to the remedies already provided by the contracts governing the card payment systems. . . .

## II. Analysis

### B. Common Law Claims

#### 1. Framing the Analysis

Courts invoking the economic loss rule trust the commercial parties interested in a particular activity to work out an efficient allocation of risks among themselves in their contracts. Courts "see no reason to intrude into the parties' allocation of the risk" when bargaining should be sufficient to protect the parties' interests, and where additional tort law remedies would act as something of a wild card to upset their expectations. East River S.S. Corp. v. Transamerica Delaval Inc., 476 U.S. 858, 872–73, 875–76 (1986) (adopting economic loss rule in admiralty cases). . . .

The doctrinal explanation is relatively simple: tort law often applies where there is "a sudden, calamitous accident as distinct from a mere failure to perform up to commercial expectations." . . . In the latter case, contract law should be sufficient because a sophisticated business plaintiff could "have protected himself through his contractual arrangements" ahead of time. . . .

. . . In deciding whether economic losses are recoverable in tort law, courts face a choice between what scholars have called the "stranger paradigm" and the "contracting parties paradigm." [citing, *inter alia*, Catherine M. Sharkey, Can Data Breach Claims Survive the Economic Loss Rule?, 66 DePaul L. Rev. 339, 344 (2017)]

The stranger paradigm fits "when an actor's negligence causes financial losses to a party with whom the actor has no pre-existing relationship." Catherine M. Sharkey, Can Data Breach Claims Survive the Economic Loss Rule, *supra*. The stranger paradigm seeks to set the "parameters of the duty of reasonable care . . . at physical injuries and property damage" and, traditionally, does not allow recovery for simple economic losses. *Id*. But some courts taking this approach in data breach cases have decided to allow tort recovery anyway, both for consumers and for sophisticated financial institutions. These courts, one scholar argues, "are doing so not only in an ad hoc manner, but also by stretching and misapplying the stranger paradigm" instead of taking a "broader regulatory perspective." *Id*. at 383.

The contracting parties paradigm approaches the problem differently. Under this paradigm, "the question is whether a duty should be imposed by [tort] law . . . over and above . . . any voluntary allocation of risks and responsibilities already made between the contracting parties." *Id*. at 344–45. In this approach, the presence of contract remedies sets a boundary for tort law. If "contract law purports to decide the case, the negligence paradigm . . . should stay in the background." *Id*. at 345 n.16.

Courts using the contracting parties paradigm first take into account the mechanisms the parties have chosen to allocate the risks they face. Courts then consider whether these mechanisms have sufficiently reduced the externalities visited upon third parties, or whether the breached entities need additional financial incentives to pursue better data security. *Id*. at 382–83. The ultimate question is whether these arrangements already place costs on "the cheapest cost avoider" or whether additional tort liability is necessary because the existing contracts "externalize significant risk onto hapless third parties." *Id*. at 383.

The plaintiff banks emphasize here that they have no direct contractual relationship with Schnucks. That's true, but it does not undermine use of the contracting parties paradigm. The plaintiff banks and Schnucks all participate in a network of contracts that tie together all the participants in the card payment system. That network of contracts imposes the duties plaintiffs rely upon and provides contractual remedies for breaches of those duties. Under these circumstances, we believe the Illinois and Missouri courts would most likely use the contracting parties paradigm.

As described above, in deciding to join the card payment system, Schnucks agreed to abide by the data security standards of the industry, the PCI DSS. Schnucks also agreed to be subject to assessments and fines from the card networks in the event that it was responsible for data breaches and unauthorized card activity. On their end, the plaintiff banks agreed to exceed federal requirements for indemnifying their card-holders and also consented to the remedial assessment and reimbursement process provisions and related risks.

Even if these issuing banks had heard of this particular merchant before its data breach was announced, parties to the card payment system are not ships passing (or colliding) in the night. All parties involved in the complicated network of contracts that establish the card payment system have voluntarily decided to participate and to accept responsibility for the risks inherent in their participation. This includes at least some risk of not being fully reimbursed for the costs of another party's mistake.

The details of these reimbursement remedies are not fully apparent from the contract excerpts presented in this case. But what matters is not the details of the remedies but their existence. Merchants and acquiring banks face the financial cost of data breaches through the card networks' reimbursement regime. That means the cheapest cost avoiders (the data handlers) already bear the cost of data security protocols and breaches. The plaintiff banks in this case make no effort to explain how this system is inadequate in providing reimbursement. They ask us, though, to predict the recognition of new theories of state tort liability through simplistic application of sweeping black-letter tort law principles, leaving the card network reimbursement systems to be considered as mere damage issues on remand.

Given this network of contracts and contractual remedies, we decline plaintiffs' invitation to apply a version of the stranger paradigm. We doubt the wisdom of recognizing new, supplemental liabilities without a clear sense of why they are necessary. It's not as if the banks have no rights or remedies at all. This is also not a situation where sensitive data is collected and then disclosed by private, third-party actors who are not involved in the customers' or banks' direct transactions. See, e.g., In re Equifax, Inc., Customer Security Data Breach Litigation, 289 F.Supp.3d 1322, 2017 WL 6031680 (J.P.M.L. 2017). The plaintiff banks seek additional recovery because they are disappointed by the reimbursement they received through the contractual card payment systems they joined voluntarily.

The legal issues raised by the plaintiff banks are similar to the issues that arise in large construction projects with layers of contractors, subcontractors, sub-subcontractors, and so on. There may be no direct contractual relationship between a negligent subcontractor and other businesses that suffer from delays and expenses it caused. Yet all participants are tied into a network of contracts that allocate the risks of sub-standard or slow work. [The court then discusses cases in Indiana, Illinois, and Missouri where such cases are treated under contract law.]

[Affirmed.]

## NOTE

***An Independent Duty to Protect Data?*** The economic loss rule stands as a formidable hurdle for victims of data breaches. Courts are split on whether recovery should be allowed.

Some courts focus on the breach of duty between the data custodian and data owner—see, e.g., Dittman v. UPMC, 196 A.3d 1036 (Pa. 2019) (finding that an employer has a legal duty to safeguard its employees' sensitive information)—whereas others recognize the important role contract law should play—see Fox v. Iowa Health System, 399 F. Supp. 3d 780, 795 (W.D. Wis. 2019) ("[T]he parties had an opportunity to include a remedy for data breaches as part of their contract but chose not to.").

How do different conceptions of data breach harms—a pure economic loss or invasion of privacy (see Chapter 7, *infra*)—impact the outcome of cases? Should the type of data—e.g., consumer credit card information or health information—make a difference? Should companies purchase cybersecurity insurance to cover data breaches? For a detailed discussion of data breaches and tort liability, see Catherine M. Sharkey, Can Data Breach Claims Survive the Economic Loss Rule?, 66 DePaul L. Rev. 339 (2017). Besides the economic loss rule, standing also presents a major obstacle to data breach claims. For discussion of cognizable harms suffered in data breaches, see Daniel J. Solove & Daniel Keats Citron, Risk and Anxiety: A Theory of Data-Breach Harms, 96 Tex. L. Rev. 737 (2018).

## SECTION F. PROFESSIONAL NEGLIGENCE RESULTING IN ECONOMIC LOSS

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§4. Professional Negligence Resulting in Economic Loss**

A professional is subject to liability in tort for economic loss caused by the negligent performance of an undertaking to serve a client.

### *Ellis-Don Construction, Inc., v. HKS, Inc.*

353 F. Supp. 2d 603 (M.D.N.C. 2004)

Bullock, J. This diversity action, filed May 27, 2004, arises out of a hospital construction project in which Ellis-Don Construction, Inc. ("Plaintiff") served as the general contractor and HKS, Inc. ("HKS") . . . and Corley Redfoot Zack, Inc. ("CRZ") (together, "Defendants") served as the design team, responsible for overall project design and management. Plaintiff alleges that Defendants performed their duties negligently and in bad faith, causing Plaintiff to suffer economic damages. Plaintiff seeks actual and punitive damages against the Defendants jointly and severally, alleging . . . tort liability against [both] Defendants. Before the court is CRZ's motion to dismiss the complaint pursuant to Federal Rule of Civil Procedure 12(b)(6). For the reasons set forth below, CRZ's motion will be denied.

#### Facts

The University of North Carolina Hospitals, a state "public body" and owner of the construction project at issue here, contracted with HKS to design and manage the construction of the North Carolina Children's Hospital and North Carolina Women's Hospital. HKS contracted with . . . CRZ to serve as consultants on the project, with . . . CRZ providing architectural services, including planning and design work, administration of the construction process, and

inspections. Plaintiff contracted directly with the owner to provide general contractor services for the construction of the hospitals. No contractual privity existed between Plaintiff and any of the Defendants.

CRZ, according to Plaintiff, was responsible for the preparation of the construction plans that the prime contractors, including Plaintiff, used to build the hospitals. CRZ was also responsible for coordinating the construction efforts of the various prime contractors, supervising their work, and administering the contracts under which each contractor operated. Plaintiff alleges that CRZ . . . performed these responsibilities negligently and in bad faith, resulting in construction delays and cost overruns that forced Plaintiff to incur economic losses in excess of $1,000,000. Plaintiff claims that [CRZ] breached the duty of care recognized under North Carolina law despite the absence of contractual privity between the parties. CRZ argues that Plaintiff cannot, in the absence of privity, maintain a tort action solely for economic damages because such claims are precluded by North Carolina's economic loss rule.

## Discussion

. . . Under the law of North Carolina, which controls in this diversity action, Plaintiff has asserted facts sufficient to withstand CRZ's motion to dismiss. In North Carolina, "in the absence of privity of contract an architect may be held liable to a general contractor and his subcontractors for economic loss resulting from breach of a common law duty of care." . . . Such duty of care "flow[s] from the parties' working relationship." . . . Indeed, the courts of North Carolina have stated that the "'power of economic life or death'" an architect holds over a contractor requires that such a duty of care be recognized, even in the absence of privity of contract. . . . Plaintiff has alleged facts indicating that CRZ acted in the capacity of an architect, with considerable control over Plaintiff's operations as general contractor on the hospital construction project. The complaint, therefore, alleges facts that give rise to an action in tort against CRZ under North Carolina law.

CRZ argues that North Carolina's economic loss doctrine has expanded beyond its traditional realm of products liability and sales of goods to preclude Plaintiff's tort claim. The court disagrees. The economic loss doctrine . . . was, and remains, firmly rooted in traditional concepts of warranty and contract law, and operates to "keep products liability and contract law in separate spheres and to maintain a realistic limitation on damages" in products liability cases. . . .

. . . The economic loss rule poses no obstacle to Plaintiff's claim. As noted, North Carolina's economic loss rule bars claims in tort for purely economic losses in the sale of goods covered by contract law, including the UCC. It does not limit tort actions that arise in the absence of a contract, nor is there any indication that the courts of North Carolina have expanded the rule beyond its traditional role in products liability cases. The privity requirement does, in some cases, preclude action in tort in the absence of a contractual relationship, but, as discussed above, North Carolina has expressly removed the privity requirement for tort actions by contractors against managing architects.

. . . Such a broad statement of the economic loss rule is entirely appropriate . . . to preclude recovery in tort for purely economic damages when a contract or the UCC operates to allocate the risk of such damages. That does not mean, however, that the doctrine has expanded to preclude all claims in tort for economic damages in the absence of a contract, or, more narrowly, outside the products liability context. The economic loss rule . . . in no way undermines or overturns the twenty-five years of case law recognizing the type of tort claim Plaintiff brings here. . . .

## Conclusion

. . . CRZ's motion to dismiss the complaint will be denied.

## *Terracon Consultants Western, Inc. v. Mandalay Resort Group*

206 P.3d 81 (Nev. 2009)

Gibbons, J. . . . Does the economic loss doctrine apply to preclude negligence-based claims against design professionals, such as engineers and architects, who provide services in the commercial property development or improvement process, when the plaintiffs seek to recover purely economic losses?

The answer to the question is yes. "Purely economic loss" has been defined as "'the loss of the benefit of the user's bargain . . . including . . . pecuniary damage for inadequate value, the cost of repair and replacement of [a] defective product, or consequent loss of profits, without any claim of personal injury or damage to other property.'" . . . After examining relevant authority and contemplating the policy considerations behind the economic loss doctrine, we have determined that the doctrine's purpose—to shield defendants from unlimited liability for all of the economic consequences of a negligent act, particularly in a commercial or professional setting, and thus to keep the risk of liability reasonably calculable—would be furthered by applying it to preclude the professional negligence claims at issue here. Thus, we conclude that the economic loss doctrine bars professional negligence claims against design professionals who provided services in the process of developing or improving commercial property when the plaintiffs' damages are purely financial.

### Procedural History and Facts

This matter arises from a removed diversity case in which a property owner brought a breach of contract and professional negligence action against certain design professionals (engineering and architectural firms). The property owner alleged that the design professionals provided negligent design advice upon which the property owner relied in making major improvements to its commercial real property, causing the property owner economic losses.

Respondents Mandalay Resort Group, Mandalay Development, and Mandalay Corporation (collectively, Mandalay) managed the construction of the approximately $1 billion Mandalay Resort and Casino (the resort) in Las Vegas. To complete the resort, Mandalay hired various subcontractors, including appellants Terracon Consultants Western, Inc., Terracon, Inc. (collectively, Terracon), Lochsa, LLC, and Klai-Juba Architects, Ltd. Mandalay entered into a written contract with Terracon, under which Terracon agreed to provide geotechnical engineering advice about the subsurface soil conditions and recommended a foundation design for the property. The parties do not dispute that Terracon's work was limited to providing professional engineering advice and that Terracon was not involved in physically constructing the property. . . .

In accordance with the written contract's terms, Terracon prepared a geotechnical report with its foundation design recommendations, which Mandalay implemented as it began erecting the resort. Based upon Terracon's soil analysis and the anticipated weight of the building, Terracon predicted a certain amount of settling underneath the foundation. According to Mandalay's complaint, however, the ultimate amount of settling exceeded Terracon's projections. Because Clark County believed that the settling presented a potential danger to the resort's structural integrity, the county required Mandalay to repair and reinforce the foundation before proceeding with the construction. Consequently, Mandalay sued Terracon for damages in state court, alleging that the deficient engineering advice caused the resort's foundation problems. Mandalay's theories of recovery included breach of contract, breach of the covenant of good faith and fair dealing, and professional negligence.

Terracon . . . moved for partial summary judgment on Mandalay's professional negligence claim, arguing that the claim was barred under the economic loss doctrine. Mandalay opposed the motion, arguing, among other things, that as a matter of law the economic loss doctrine did not apply to negligence claims against design professionals or contractors who solely provide services.

Terracon also filed a third-party complaint against, among others, Lochsa and Klai-Juba for negligence, contribution, and equitable indemnity. Terracon argued that if the economic loss doctrine did not bar Mandalay's negligence claim, then the doctrine likewise would not bar its claims against Lochsa and Klai-Juba. In response, Lochsa and Klai-Juba argued that the economic loss doctrine applied and moved the federal court to dismiss Terracon's third-party complaint on that basis.

The U.S. District Court denied without prejudice the motion[s] . . . after determining that Nevada law was unclear on whether the economic loss doctrine applied to bar a claim grounded on allegations that design professionals negligently rendered services when the plaintiffs sought to recover purely economic losses. The federal court thus asked this court to address the scope of Nevada's economic loss doctrine. . . .

. . . We . . . answer directly whether the economic loss doctrine bars professional negligence claims against design professionals who provide only their services in the commercial property development or improvement process, when the plaintiffs are seeking to recover purely economic losses. . . .

## Discussion

### The Economic Loss Doctrine

The economic loss doctrine is a judicially created rule that primarily emanates from products liability jurisprudence. This court has explained that "'[t]he economic loss doctrine marks the fundamental boundary between contract law, which is designed to enforce the expectancy interests of the parties, and tort law, which imposes a duty of reasonable care and thereby [generally] encourages citizens to avoid causing physical harm to others.'" Applying the economic loss doctrine to accomplish its general purpose, this court has concluded that the doctrine bars unintentional tort actions when the plaintiff seeks to recover "purely economic losses." Nevertheless, as set forth below, exceptions to the doctrine apply in certain categories of cases when strong countervailing considerations weigh in favor of imposing liability. . . .

### Policy Considerations Underlying the Economic Loss Doctrine

. . . In addition to balancing economic activity incentives against providing compensation to negligence victims, the economic loss doctrine is driven by financial considerations. In that regard, the doctrine works to reduce the cost of tort actions, but still provides tort victims with a remedy because less expensive alternative forms of compensation, such as insurance, generally are available to a financially injured party. Thus, when applied to foreclose tort liability at a certain point, the economic loss doctrine dispels the fear of creating victim compensation costs that are unnecessarily high, at least from an administrative standpoint.

Another consideration behind the economic loss doctrine is balancing the disproportion between liability and fault. *Id*. To that end, cutting off tort liability at the point where only economic loss is at stake without accompanying physical injury or property damage "provides . . . incentives and disincentives to engage in economic activity or to make it safer." On the other hand, imposing unbounded tort liability for pure financial harm could result in "incentives that are perverse," such as insurance premiums that are too expensive for the average economic actor to afford. For those reasons, courts have been reluctant to impose tort liability for purely financial harm. . . .

### The Economic Loss Doctrine Applies to Preclude Mandalay's Professional Negligence Claim

Guided by the doctrine's purpose—"to shield [defendants] from unlimited liability for all of the economic consequences of a negligent act, particularly in a commercial or professional setting, and thus to keep the risk of liability reasonably calculable," . . . and, after contemplating the competing policy reasons set forth above, we conclude that the economic loss doctrine should apply to bar the professional negligence claim at issue here.

In the context of engineers and architects, the bar created by the economic loss doctrine applies to commercial activity for which contract law is better suited to resolve professional negligence claims. This legal line between contract and tort liability promotes useful commercial economic activity, while still allowing tort recovery when personal injury or property damage are present. Further, as in this case, contracting parties often address the issue of economic losses in contract provisions. . . .

. . . We perceive no significant policy distinction that would drive us to permit tort-based claims to recover economic losses against design professionals, such as architects and engineers, who provided their professional services in the commercial property development and improvement process, when we have concluded that such claims are barred under the economic loss doctrine if brought against contractors and subcontractors involved in physically constructing improvements to real property. . . . The work provided by construction contractors or the services rendered by design professionals in the commercial building process are both integral to the building process and impact the quality of building projects. Therefore, when the quality is deemed defective, resulting in economic loss, remedies are properly addressed through contract law. . . . In that regard, we point out that economic losses for which no tort action will lie generally involve a buyer's "disappointed economic expectations." . . . In the commercial property development and improvement process, design professionals' duties typically are prescribed by the parties' contract, and therefore, any duty breached arises from the contractual relationship only, which "necessitates an analysis of the damages which were within the contemplation of the parties when framing their agreement." . . .

While the loss alleged here arguably was foreseeable, we do not read the rule as necessarily being dependent on foreseeability notions. . . . Instead, the economic loss doctrine cuts off tort liability when no personal injury or property damage occurred, with traditionally recognized exceptions for certain classes of claims. . . . Negligence claims against design professionals do not fall within those traditional exceptions, and we decline to make an exception here.

In this case, for purposes of the certified question, Mandalay suffered only economic loss without any attendant personal injury or property damage, and therefore, the economic loss doctrine bars Mandalay from proceeding with their negligence-based claims against Terracon. Thus, adhering to our general policy of applying the economic loss doctrine in a predictable and fair way, we answer the federal court's question affirmatively.

### Conclusion

We conclude that, in a commercial property construction defect action in which the plaintiffs seek to recover purely economic losses through negligence-based claims, the economic loss doctrine applies to bar such claims against design professionals who have provided professional services in the commercial property development or improvement process. Accordingly, we answer the U.S. District Court's certified question in the affirmative.

## NOTES

**1. *The Significance of the Contracting-Parties and Stranger Paradigms.*** What explains the different outcomes in *Ellis-Don* and *Terracon*? Is it that privity existed in one case and not the other? Should a court considering this issue analyze which professions create duties in tort, or only reach that question if the parties are strangers? Are these professional liability cases consistent with the third-party "web of contract" cases, *supra* Section E?

**2. *Why Treat "Professionals" Differently?*** According to RTT: LEH §1, comment *d*:

> First, the professional sued for malpractice by a client who has suffered economic loss is not likely to face an unusual risk of indeterminate or disproportionate liability. Second, the imbalance of knowledge between the typical professional and client makes contracts between them less trustworthy and important than usual: less trustworthy because one side is not in a position to negotiate effectively with the other, and less important because the right allocation of responsibility between the parties is clear enough as a matter of public policy.

**3. *Who Is a "Professional"?*** RTT: LEH §4, comment *b* takes a preliminary stab at answering this question:

> In defining which occupational groups are "professionals," courts consider whether the practice of the occupation requires formal training and a license issued by a public body, whether the occupation has an internal code of conduct and discipline, and whether there is a need for complex discretionary judgments in carrying out the work.

Are these factors suitable proxies for the policies (see *supra* Note 2) that lie behind the "professionals" exception to the economic loss rule? Do they translate to categorical judgments? According to RTT: LEH §4, comment *b*: "Lawyers, doctors, and accountants are invariably regarded by courts as professionals; insurance agents and architects are examples of additional parties this Restatement would so recognize, whereas construction contractors and tradesmen are on the other side of the line."

Have courts followed this categorization for purposes of economic harms? *Ellis-Don* and *Terracon*, *supra*, illustrate a split in authority regarding architects. Insurance agents have received more widespread recognition from courts. Many courts align with *Terracon* in recognizing tort liability against insurance agents. See Sharon Acad. v. Wieczorek Ins., Inc., 2013 WL 6631043, at *3–4 (Vt. Super. Ct. 2013) (recognizing insurance agents' "extra-contractual duty"); Kanter v. Deitelbaum, 648 N.E.2d 1137, 1139–40 (Ill. Ct. App. 1995) (same); Nelson v. Anderson Lumber Co., 99 P.3d 1092, 1100 (Idaho Ct. App. 2004); Cincinnati Ins. Co. v. Ruch, 940 F. Supp. 2d 338 (E.D. Va. 2013); Cleveland Indians Baseball Co., L.P. v. N.H. Ins. Co., 727 F.3d 633, 640 (6th Cir. 2013)). New York, in contrast, refuses to deem insurance agents professionals on account of their lack of "formal learning and training, licensure and regulation . . . [or] a code of conduct [or] a system of discipline." Chase Sci. Rsch., Inc. v. NIA Grp., Inc., 749 N.E.2d 161, 166 (N.Y. 2001).

The Vermont Superior Court in *Sharon Academy* advanced a powerful policy argument for recognizing insurance agents as professionals liable for economic harms: "It is hard to imagine how such a duty could ever be enforced if a suit for its breach required physical harm. By its nature, the injury for a failure to procure insurance will be solely economic: a lack of payment for financial losses. Thus, the economic loss rule, if applied here, would vitiate the existence of any such duty." 2013 WL 6631043, at *3. Is this distinction a defensible basis for departing from the economic loss rule? Or is it simply more reason to view this "professional" relationship as a creature of contract alone?

What about construction contractors and tradespeople (the final category in RTT: LEH §4, comment *b*)? Should they be considered "professionals" if licensed and subject to codes of conduct and disciplinary systems? New York cases (following *Chase Scientific*) have answered

"no" with regard to "project managers" (see CBH Med., P.C. v. Merit Sys., LLC, 178 N.Y.S.3d 418, 425–28 (Sup. Ct. 2022)) and actuaries (see Castle Oil Corp. v. Thompson Pension Emp. Plans., Inc., 299 A.D.2d 513, 514 (N.Y. App. Div. 2002)). Will categorization vary by state occupational licensing schemes?

Do these considerations advance the myriad policy rationales of the economic loss doctrine, or does this threshold definitional question risk becoming overly formalistic? What is a feasible alternative approach? Would an open-ended standard go too far in the opposite direction? See Santopietro v. City of New Haven, 682 A.2d 106, 115–16 (Conn. 1996) (deeming softball umpires professionals including within standard regarding "the failure of one rendering professional services to exercise that degree of skill and learning commonly applied under all the circumstances in the community by the average prudent reputable member of the profession").

**4. *Professional Liability Insurance and the Economic Loss Doctrine?*** Should courts consider the availability of insurance when considering professional liability for economic harm?

*Terracon* cites Barber Lines A/S v. M/V Donau Maru, 764 F.2d 50, 55 (1st Cir. 1985), for the following proposition: "[I]mposing unbounded tort liability for pure financial harm could result in 'incentives that are perverse,' such as insurance premiums that are too expensive for the average economic actor to afford." *Barber Lines* was a maritime economic loss case arising under federal admiralty jurisdiction, in which then-Judge Stephen G. Breyer took a pragmatic approach:

> . . . What, for example, in cases like this one, are the added administrative costs involved in allowing all persons suffering pure financial harm to sue the shipowner instead of "channeling" suits (perhaps via contract) through traditionally injured plaintiffs? Is there a problem of "disproportionality"? How far, for example, would additional, unbounded, pure financial loss liability for negligently caused oil spills, when added to the already large potential traditional liability, affect the type of insurance carried, the incentive to mitigate losses, the incentive to transport oil safely, the likelihood that shippers will use pipelines and domestic wells instead of ships and foreign wells, and the consequences of these and other related changes? We do not know the answers to these questions, nor can judges readily answer them in particular cases.

*Id*. at 55.

With regard to professional malpractice specifically, do these factors militate in favor of the economic loss rule, as the *Terracon* court concluded? How does, or should, the insurability of the risk influence whether to recognize a duty in tort? Should the availability of a uniform malpractice insurance policy influence whether a court recognizes an occupation as a "profession" at all?

**5. *Could Software Developers Be Deemed "Professionals"?*** Bryan H. Choi, in Software as a Profession, 33 Harv. J. L. & Tech. 557 (2020), argues that software developers should be legally classified as "professionals," with the attendant malpractice liability that attaches. To what extent does the discretionary judgment and need for an ethical code weigh in favor of this classification? Is the case stronger for software developers than for architects or engineers? How does artificial intelligence affect this discussion if software developers create algorithms that act unpredictably? See Bryan H. Choi, AI Malpractice, 73 DePaul L. Rev. 301 (2024).

# CHAPTER 2

# PRODUCTS LIABILITY

## SECTION A. INTRODUCTION

Products liability law has become so important that it is virtually a legal field unto itself.

As befits its complexity, products liability law has a rich and dense history, which can be roughly divided into four periods. The first period ran from approximately the mid-nineteenth century to the early twentieth century, when the major debate was whether to allow an injured party to sue either product manufacturers or sellers. Courts often held that the "privity" limitation prevented the injured party—whether consumer, user, or bystander—from suing the "remote" supplier of the product in question, that is, one who has no direct contractual relationship with the injured party. Instead an injured consumer or user could sue only the immediate vendor of the product; an injured bystander could sue only the party in possession of the product just before the injury occurred.

The last half of the nineteenth century witnessed a gradual erosion of this privity limitation, as exceptions were created for products known to hold hidden dangers that manifested themselves when either the plaintiff or some third party put them to ordinary use. This second period began when MacPherson v. Buick Motor Co., 111 N.E. 1050 (N.Y. 1916), rejected the privity limitation outright by imposing liability for negligence on a remote seller.

The third stage of products liability law was inaugurated by the famous concurring opinion of Justice Traynor in Escola v. Coca Cola Bottling Co., 150 P.2d 436, 440 (Cal. 1944), which argued that strict liability, not negligence principles, should govern the manufacturer's liability. Traynor's view steadily gained adherents and became the dominant view by 1965, when the American Law Institute incorporated a general principle of strict liability into section 402A of the Second Restatement. For a discussion of the early development of strict liability through the Second Restatement, see Richard A. Epstein, Modern Products Liability Law (1980); William L. Prosser, The Assault Upon the Citadel (Strict Liability to the Consumer), 69 Yale L.J. 1099 (1960).

Soon after the Second Restatement was adopted, products liability law entered a period of rapid expansion. The three dominant themes in debates leading up to the Second Restatement focused on the role of manufacturers: their market power, their capacity to obtain insurance, and their ability to internalize the costs of accidents associated with their products. Taken together, these three issues pointed to placing nearly "absolute liability" on the manufacturer, and perhaps others in the chain of distribution. As George L. Priest, The Invention of Enterprise Liability: A Critical History of the Intellectual Foundations of Modern Tort Law, 14 J. Legal Stud. 461, 527 (1985), laments, "[t]he presuppositions themselves do not incorporate any conceptual limit to manufacturer's liability."



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The fourth stage of products liability law began in the decade following the 1965 Restatement with a series of important decisions in "defective design" and "failure to warn" cases, as they are now commonly known. These cases, which somewhat ironically have expanded liability within the traditional negligence framework, form the centerpiece of modern products liability law.

In 1998, in response to these major developments, the American Law Institute issued a separate volume of the Third Restatement devoted exclusively to products liability law. "This [Third] Restatement is . . . an almost total overhaul of Restatement Second as it concerns the liability of commercial sellers of products." RTT: PL at 3. The Third Restatement has received a rather chilly reception in the courts and mixed reviews in the academy. Courts are still reacting unevenly to various provisions of the Third Restatement, and it remains unclear whether the longer Third Restatement will displace or supplement the earlier, but more concise, Second Restatement. It is therefore necessary to study both Restatements throughout this chapter. In any event, it is now evident that the fourth period has been a period of doctrinal consolidation, if not some modest retrenchment. The steady string of plaintiffs' breakthroughs that were par for the course between 1965 and 1980—the rise of crashworthiness theories, the decline of the open and obvious defense, and the expansive definitions of product defect—has slowed markedly since then. See James A. Henderson, Jr. & Theodore Eisenberg, The Quiet Revolution in Products Liability: An Empirical Study of Legal Change, 37 UCLA L. Rev. 479, 481 (1990); Gary T. Schwartz, The Beginning and the Possible End of the Rise of Modern American Tort Law, 26 Ga. L. Rev. 601, 604 (1992).

The newest developments in this field go beyond the traditional contours of the tort law. Consider, for example, the emergence of autonomous vehicles. Autonomous vehicles hold the promise of dramatically reducing automobile accident rates, roughly 98 percent of which are caused by human error. But what about crashes due to software glitches? Should these cases be handled under strict products liability? Also of immediate relevance is the question of whether online suppliers of goods (like Amazon) should be subject to the products liability legal regime when they act as an aggregator and conduit between other product sellers and their customers. These questions have momentous implications for the safety of products and the business models of sellers and distributors.

Another fast-developing area in tort law comes from government regulatory oversight. Today it is common for government agencies to launch extensive investigations of product defects, which can lead to major fines or criminal prosecutions, activities that are largely beyond the scope of this chapter. Relatedly, however, this chapter considers the extent to which direct forms of federal regulation can supersede private rights of action under state tort law, a legal concept known as preemption. The stakes here are enormous, as federal regulation affects products as varied as motor vehicles, pharmaceuticals, medical devices, and toxic chemicals. Without question, the major developments in products liability since 2000 have concerned the preemption question, which forces tort lawyers to negotiate the treacherous shoals of federalism and administrative law. See Catherine M. Sharkey, Products Liability Preemption: An Institutional Approach, 76 Geo. Wash. L. Rev. 449 (2008).

Products liability law is also inevitably bound up with mass tort litigation, including, but not limited to, class actions. Major class action suits dominate the headlines and capture the attention of political, corporate, and consumer actors. The 3M multidistrict litigation provides a high-profile example. Numerous federal cases that alleged that 3M's dual-ended

Combat Arms earplugs are defective and caused the plaintiffs to develop hearing loss were consolidated in a multidistrict litigation in Northern Florida under Judge M. Casey Rodgers. See *In re* 3M Combat Arms Earplug Products Liability, Case No. 3:19-md-2885. In a 2022 bellwether trial, a jury awarded a plaintiff $72 million in damages after concluding 3M was liable for defective design and failure to warn, among other claims. Verdict Form, Beal v. 3M Co., No. 7:20-cv-00006 (N.D. Fla. May 20, 2022), ECF No. 176. The parties have reached a $6 billion settlement agreement. See 3M Products Liability Litigation, MDL No. 2885, Master Docket No. 3:19md2885, https://www.flnd.uscourts.gov/3m-products-liability-litigation-mdl-no-2885.

**A billboard for a Texas law firm that sought plaintiffs after Vioxx was removed from the market**

*Source: Bob Daemmrich / Corbis*

These multifaceted legal developments demonstrate that products liability law is big business. In 2020, some 241,438 products liability tort suits were filed in U.S. federal district courts, a dramatic increase from the previous peak of 64,367 in 2010. This spike, likely a result of the COVID-19 pandemic, has tapered off a bit, with the numbers for 2022 reverting to 61,712, only slightly above pre-COVID levels. See Admin. Office of the U.S. Courts, 2022 Annual Report of the Director: Judicial Business of the United States Courts tbl. C-11 (Sept. 30, 2022), https://www.uscourts.gov/sites/default/files/data_tables/jb_c11_0930.2022.pdf. From these numbers, it should come as no surprise that personal injury products liability actions now constitute over 20 percent of the docket of new civil filings in federal district courts, up from under 5 percent in 1980.

Interestingly, the rapid increase in the overall level of products litigation has been matched by a long and steady decline in accident levels. From 1945 to 2021, fatal workplace accidents declined from 33 per 100,000 to 3.6 per 100,000, with home and vehicular accident rates falling dramatically as well. See Bureau of Labor Stat., U.S. Dep't of Labor, USDL-22-2309, National Census of Fatal Occupation Injuries (2022). On this issue, the relationship between the improved accident picture and the changes in the tort liability arena is unclear. The decline in accident rates started before the expansion in tort liability and has continued uniformly even as the doctrinal expansion in the field slowed around 1990. See generally George L. Priest, Products Liability Law and the Accident Rate, *in* Liability: Perspectives and Policy (Litan & Winston, eds., 1988).

Today, intense battles rage on about whether tort claims exert a positive influence in promoting safety and deterring accidents. Some scholars argue that the headline-grabbing pharmaceutical and medical-device cases of the past twenty years have highlighted the insufficiency of federal regulation; others claim that tort suits undermine the careful balancing done by the federal regulators, thereby exposing manufacturers to excessive risk. To understand the contemporary state of products liability, it is helpful to trace its origins back to the mid-nineteenth century.

## SECTION B. EXPOSITION

### *Winterbottom v. Wright*

(1842) 152 Eng. Rep. 402 (Ex.)

[The plaintiff brought an action on the case, i.e., in tort, based on the following undisputed facts. The defendant contracted with the Postmaster-General to supply coaches to carry mail and to see that the coaches would "be kept in a fit, proper, safe, and secure state and condition for said purpose." Under this contract the defendant assumed "the sole and exclusive duty, charge, care, and burden of the repairs, state, and condition" thereof. Atkinson, knowing of this contract, personally contracted with the Postmaster-General to supply horses and drivers for the defendant's coaches. The plaintiff, one of Atkinson's drivers, was driving a coach serviced by the defendant, and was hurt when a latent defect caused the coach to break down, throwing him to the ground and injuring him. The defendant demurred to the plaintiff's action.]

Abinger, C.B. I am clearly of opinion that the defendant is entitled to our judgment. We ought not to permit a doubt to rest upon this subject, for our doing so might be the means of letting in upon us an infinity of actions. This is an action of the first impression, and it has been brought in spite of the precautions which were taken, in the judgment of this Court in the case of Levy v. Langridge, [(1836) 150 Eng. Rep. 863 (Ex.)], a case of fraudulent representation by the seller to the purchaser, to obviate any notion that such an action could be maintained. We ought not to attempt to extend the principle of that decision, which, although it has been cited in support of this action, wholly fails as an authority in its favour; for there the gun was bought for the use of the son, the plaintiff in that action, who could not make the bargain himself, but was really and substantially the party contracting. Here the action is brought simply because the defendant was a contractor with a third person; and it is contended that thereupon he became liable to everybody who might use the carriage. If there had been any ground for such an action, there certainly would have been some precedent of it; but with the exception of actions against innkeepers, and some few other persons, no case of a similar nature has occurred in practice. That is a strong circumstance, and is of itself a great authority against its maintenance. It is however contended, that this contract being made on the behalf of the public by the Postmaster-General, no action could be maintained against him, and therefore the plaintiff must have a remedy against the defendant. But that is by no means a necessary consequence—he may be remediless altogether. There is no privity of contract between these parties; and if the plaintiff can sue, every passenger, or even any person passing along the road, who was injured by the upsetting of the coach, might bring a similar action. Unless we confine the operation of such contracts as this to the parties who entered into them, the most absurd and outrageous consequences, to which I can see no limit, would ensue. Where a party becomes responsible to the public, by undertaking a public duty, he is liable, though the injury may have arisen from the negligence of his servant or agent. So, in cases of public nuisances, whether the act was done by the party as a servant, or in any other capacity, you are liable to an action at the suit of any person who suffers. Those, however, are cases where the real ground of the liability is the public duty, or the commission of the public nuisance. There is also a class of cases in which the law permits a contract to be turned into a tort; but unless there has been some public duty undertaken, or public nuisance committed, they are all cases in which an action might have been maintained upon the contract. Thus, a carrier may be sued either in assumpsit [contract] or case [tort]; but there is no instance in which a party, who was not privy to the contract entered into with him,

can maintain any such action. The plaintiff in this case could not have brought an action on the contract; if he could have done so, what would have been his situation, supposing the Postmaster-General had released the defendant? That would, at all events, have defeated his claim altogether. By permitting this action, we should be working this injustice, that after the defendant had done everything to the satisfaction of his employer, and after all matters between them had been adjusted, and all accounts settled on the footing of their contract, we should subject them to be ripped open by this action of tort being brought against him.

## NOTE

***The American Reception of Winterbottom v. Wright.*** During the nineteenth century, Winterbottom v. Wright was a leading — albeit controversial — case both in England and in the United States. Negotiating the line between contracts and torts, *Winterbottom*'s requirement of privity between the parties provided a clear rule that limited the scope of tort duties owed to third persons who were not parties to the underlying contract, in this instance to repair the coach. According to one explanation, the result in *Winterbottom* had as much to do with procedure as with substance:

> The dominant focus of the pre-negligence era [before 1850 at the earliest] was fixed upon the different and difficult problem of concurrence [between tort and contract remedies]. The early common law was traditionally hostile to double remedies, and this attitude, though less intense in the 19th century, was still alive.

Vernon Palmer, Why Privity Entered Tort — An Historical Reexamination of *Winterbottom v. Wright*, 27 Am. J. Legal Hist. 85, 89 (1983).

Would this problem be so severe if the court in *Winterbottom* had limited tort remedies to defective products? That concept came to the fore in several late-nineteenth-century cases, which carved out significant exceptions to *Winterbottom*'s categorical prohibition. The overall position in the United States was summarized by Sanborn, J., in Huset v. J.I. Case Threshing Machine Co., 120 F. 865, 866–71 (8th Cir. 1903):

> [T]he natural and probable effect of the negligence of the contractor or manufacturer will generally be limited to the party for whom the article is constructed, or to whom it is first sold, and, perhaps more than all this, for the reason that a wise and conservative public policy has impressed the courts with the view that there must be a fixed and definite limitation to the liability of manufacturers and vendors for negligence in the construction and sale of complicated machines and structures which are to be operated or used by the intelligent and the ignorant, the skillful and the incompetent, the watchful and the careless, parties that cannot be known to the manufacturers or vendors, and who use the articles all over the country hundreds of miles distant from the place of their manufacture or original sale, a general rule has been adopted and has become established by repeated decisions of the courts of England and of this country that in these cases the liability of the contractor or manufacturer for negligence in the construction or sale of the articles which he makes or vends is limited to the persons to whom he is liable under his contracts of construction or sale. The limits of the liability for negligence and for breaches of contract in cases of this character are held to be identical. The general rule is that a contractor, manufacturer, or vendor is not liable to third parties who have no contractual relations with him for negligence in the construction, manufacture, or sale of the articles he handles. But while this general rule is both established and settled, there are, as is usually the case, exceptions to it as well defined and settled as the rule itself. There are three exceptions to this rule.

> The first is that an act of negligence of a manufacturer or vendor which is imminently dangerous to the life or health of mankind, and which is committed in the preparation or sale of an article intended to preserve, destroy, or affect human life, is actionable by third parties who suffer from the negligence. . . .
>
> The second exception is that an owner's act of negligence which causes injury to one who is invited by him to use his defective appliance upon the owner's premises may form the basis of an action against the owner. . . .
>
> The third exception to the rule is that one who sells or delivers an article which he knows to be imminently dangerous to life or limb to another without notice of its qualities is liable to any person who suffers an injury therefrom which might have been reasonably anticipated, whether there were any contractual relations between the parties or not.

The court then held that the plaintiff's complaint alleged a cause of action under the third exception: that the defendant's threshing machine was constructed so that the cylinder covering upon which its operator had to walk could not support his weight, that the defect was latent in that it could not be discovered by ordinary inspection, and that this defective condition was known by the defendant. The court remanded the case for trial, noting that it was "perhaps improbable" that the defendant had had knowledge of the imminently dangerous character of the machine at the time of delivery.

Some cases did succeed under this third exception. In Kuelling v. Roderick Lean Manufacturing Co., 75 N.E. 1098, 1101 (N.Y. 1905), the defendants sold a roller to a dealer who then resold it to the plaintiff. The roller was made out of weak wood and contained a knot that prevented a safe hook-up of the roller to the team of horses that pulled it. The defect was deliberately concealed by putty and paint. Bartlett, J., allowed the action:

> In the case at bar we have not only fraudulent deceit and concealment, but what amounts to an affirmative representation that the tongue of the roller was sound, as the manufacturer by filling the defect with putty and painting the entire surface so that the eye could not detect any weakness by reason of the knot, knothole filled up, the kind of wood employed and the fact that it was cross-grained, must be held to have represented that the roller as offered for sale was in a perfectly marketable condition.

## *MacPherson v. Buick Motor Co.*

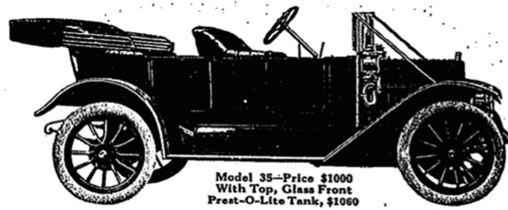
111 N.E. 1050 (N.Y. 1916)

Cardozo, J. The defendant is a manufacturer of automobiles. It sold an automobile to a retail dealer. The retail dealer resold to the plaintiff. While the plaintiff was in the car, it suddenly collapsed. He was thrown out and injured. One of the wheels was made of defective wood, and its spokes crumbled into fragments. The wheel was not made by the defendant; it was bought from another manufacturer. There is evidence, however, that its defects could have been discovered by reasonable inspection, and that inspection was omitted. There is no claim that the defendant knew of the defect and willfully concealed it. The case, in other words, is not brought within the rule of *Kuelling v. Lean Mfg. Co*. The charge is one, not of fraud, but of negligence. The question to be determined is whether the defendant owed a duty of care and vigilance to any one but the immediate purchaser.

The foundations of this branch of the law, at least in this state, were laid in Thomas v. Winchester (6 N.Y. 397 (1852)). A poison was falsely labeled. The sale was made to a druggist, who in turn sold to a customer. The customer recovered damages from the seller who affixed the label. "The defendant's negligence," it was said, "put human life in imminent danger." A poison falsely labeled is likely to injure any one who gets it. Because the danger is to be foreseen, there is a duty to avoid the injury. . . .

**Exhibit 2.1 1910 Buick Model 10**

"The Buick Model 10 was introduced in 1908. The Gentlemen's Light Four-cylinder Roadster body-style soon became the company's best seller. Over 4,000 examples were created during its first year and that figure doubled the following year to 8,100. The last year was in 1910, with production approaching 11,000 units." 1910 Buick Model 10, Conceptcarz, http://www.conceptcarz.com/vehicle/z7409/Buick-Model-10.aspx.




*Source: PF / Alamy*

*Thomas v. Winchester* became quickly a landmark of the law. In the application of its principle there may at times have been uncertainty or even error. There has never in this state been doubt or disavowal of the principle itself. The chief cases are well known, yet to recall some of them will be helpful. Loop v. Litchfield (42 N.Y. 351 (1870)) is the earliest. It was the case of a defect in a small balance wheel used on a circular saw. The manufacturer pointed out the defect to the buyer, who wished a cheap article and was ready to assume the risk. The risk can hardly have been an imminent one, for the wheel lasted five years before it broke. In the meanwhile the buyer had made a lease of the machinery. It was held that the manufacturer was not answerable to the lessee. Loop v. Litchfield was followed in Losee v. Clute (51 N.Y. 494 (1873)), the case of the explosion of a steam boiler. That decision has been criticised but it must be confined to its special facts. It was put upon the ground that the risk of injury was too remote. The buyer in that case had not only accepted the boiler, but had tested it. The manufacturer knew that his own test was not the final one. The finality of the test has a bearing on the measure of diligence owing to persons other than the purchaser.

These early cases suggest a narrow construction of the rule. Later cases, however, evince a more liberal spirit. First in importance is Devlin v. Smith (89 N.Y. 470 (1882)). The defendant, a contractor, built a scaffold for a painter. The painter's servants were injured. The contractor was held liable. He knew that the scaffold, if improperly constructed, was a most dangerous trap. He knew that it was to be used by the workmen. He was building it for that very purpose. Building it for their use, he owed them a duty, irrespective of his contract with their master, to build it with care.

From Devlin v. Smith we pass over intermediate cases and turn to the latest case in this court in which Thomas v. Winchester was followed. That case is Statler v. Ray Mfg. Co. (195 N.Y. 478, 480 (1909)). The defendant manufactured a large coffee urn. It was installed in a restaurant. When heated, the urn exploded and injured the plaintiff. We held that the manufacturer was liable. We said that the urn "was of such a character inherently that, when applied to the purposes for which it was designed, it was liable to become a source of great danger to many people if not carefully and properly constructed."

It may be that Devlin v. Smith and Statler v. Ray Mfg. Co. have extended the rule of Thomas v. Winchester. If so, this court is committed to the extension. The defendant argues that things imminently dangerous to life are poisons, explosives, deadly weapons — things whose normal function it is to injure or destroy. But whatever the rule in Thomas v. Winchester

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may once have been, it has no longer that restricted meaning. A scaffold (Devlin v. Smith, *supra*) is not inherently a destructive instrument. It becomes destructive only if imperfectly constructed. A large coffee urn . . . may have within itself, if negligently made, the potency of danger, yet no one thinks of it as an implement whose normal function is destruction. What is true of the coffee urn is equally true of bottles of aerated water (Torgeson v. Schultz, 192 N.Y. 156 (1908)). We have mentioned only cases in this court. But the rule has received a like extension in our courts of intermediate appeal. . . .

[Cardozo, J., then reviews the parallel English decisions.]

We hold, then, that the principle of Thomas v. Winchester is not limited to poisons, explosives, and things of like nature, to things which in their normal operation are implements of destruction. If the nature of a thing is such that it is reasonably certain to place life and limb in peril when negligently made, it is then a thing of danger. Its nature gives warning of the consequences to be expected. If to the element of danger there is added knowledge that the thing will be used by persons other than the purchaser, and used without new tests, then, irrespective of contract, the manufacturer of this thing of danger is under a duty to make it carefully. That is as far as we are required to go for the decision of this case. There must be knowledge of a danger, not merely possible, but probable. It is *possible* to use almost anything in a way that will make it dangerous if defective. That is not enough to charge the manufacturer with a duty independent of his contract. Whether a given thing is dangerous may be sometimes a question for the court and sometimes a question for the jury. There must also be knowledge that in the usual course of events the danger will be shared by others than the buyer. Such knowledge may often be inferred from the nature of the transaction. But it is possible that even knowledge of the danger and of the use will not always be enough. The proximity or remoteness of the relation is a factor to be considered. We are dealing now with the liability of the manufacturer of the finished product, who puts it on the market to be used without inspection by his customers. If he is negligent, where danger is to be foreseen, a liability will follow. We are not required at this time to say that it is legitimate to go back of the manufacturer of the finished product and hold the manufacturers of the component parts. To make their negligence a cause of imminent danger, an independent cause must often intervene; the manufacturer of the finished product must also fail in *his* duty of inspection. It may be that in those circumstances the negligence of the earlier members of the series is too remote to constitute, as to the ultimate user, an actionable wrong. . . . We leave that question open. We shall have to deal with it when it arises. The difficulty which it suggests is not present in this case. There is here no break in the chain of cause and effect. In such circumstances, the presence of a known danger, attendant upon a known use, makes vigilance a duty. We have put aside the notion that the duty to safeguard life and limb, when the consequences of negligence may be foreseen, grows out of contract and nothing else. We have put the source of the obligation where it ought to be. We have put its source in the law.

From this survey of the decisions, there thus emerges a definition of the duty of a manufacturer which enables us to measure this defendant's liability. Beyond all question, the nature of an automobile gives warning of probable danger if its construction is defective. This automobile was designed to go fifty miles an hour. Unless its wheels were sound and strong, injury was almost certain. It was as much a thing of danger as a defective engine for a railroad. The defendant knew the danger. It knew also that the car would be used by persons other than the buyer. This was apparent from its size; there were seats for three persons. It was apparent also from the fact that the buyer was a dealer in cars, who bought to resell. The maker of this car supplied it for the use of purchasers from the dealer just as plainly as the contractor in Devlin v. Smith supplied the scaffold for use by the servants of the owner. The dealer was indeed the one person of whom it might be said with some approach to certainty that by him the car

would not be used. Yet the defendant would have us say that he was the one person whom it was under a legal duty to protect. The law does not lead us to so inconsequent a conclusion. Precedents drawn from the days of travel by stage coach do not fit the conditions of travel today. The principle that the danger must be imminent does not change, but the things subject to the principle do change. They are whatever the needs of life in a developing civilization require them to be.

In reaching this conclusion, we do not ignore the decisions to the contrary in other jurisdictions. . . . The earlier cases are summarized by Judge Sanborn in Huset v. J. I. Case Threshing Machine Co. (120 Fed. Rep. 865). . . . Judge Sanborn says . . . that the contractor who builds a bridge, or the manufacturer who builds a car, cannot ordinarily foresee injury to other persons than the owner as the probable result. We take a different view. We think that injury to others is to be foreseen not merely as a possible, but as an almost inevitable result. Indeed, Judge Sanborn concedes that his view is not to be reconciled with our decision in Devlin v. Smith. The doctrine of that decision has now become the settled law of this state, and we have no desire to depart from it.

[Cardozo, J., then reviews the English cases from *Winterbottom* onward and continues:] From these cases a consistent principle is with difficulty extracted. The English courts, however, agree with ours in holding that one who invites another to make use of an appliance is bound to the exercise of reasonable care. That at bottom is the underlying principle of Devlin v. Smith. The contractor who builds the scaffold invites the owner's workmen to use it. The manufacturer who sells the automobile to the retail dealer invites the dealer's customers to use it. The invitation is addressed in the one case to determinate persons and in the other to an indeterminate class, but in each case it is equally plain, and in each its consequences must be the same. . . .

. . . Subtle distinctions are drawn by the defendant between things inherently dangerous and things imminently dangerous, but the case does not turn upon these verbal niceties. If danger was to be expected as reasonably certain, there was a duty of vigilance, and this whether you call the danger inherent or imminent. In varying forms that thought was put before the jury. We do not say that the court would not have been justified in ruling as a matter of law that the car was a dangerous thing. If there was any error, it was none of which the defendant can complain.

We think the defendant was not absolved from a duty of inspection because it bought the wheels from a reputable manufacturer. It was not merely a dealer in automobiles. It was a manufacturer of automobiles. It was responsible for the finished product. It was not at liberty to put the finished product on the market without subjecting the component parts to ordinary and simple tests. Under the charge of the trial judge nothing more was required of it. The obligation to inspect must vary with the nature of the thing to be inspected. The more probable the danger, the greater the need of caution. . . .

The judgment should be affirmed with costs.

Bartlett, C.J., dissenting. . . . [In Thomas v. Winchester,] Chief Judge Ruggles, who delivered the opinion of the court, distinguished between an act of negligence imminently dangerous to the lives of others and one that is not so, saying: "If A. build a wagon and sell it to B., who sells it to C. and C. hires it to D., who in consequence of the gross negligence of A. in building the wagon is overturned and injured, D. cannot recover damages against A., the builder. A.'s obligation to build the wagon faithfully, arises solely out of his contract with B. The public have nothing to do with it. . . . So, for the same reason, if a horse be defectively shod by a smith, and a person hiring the horse from the owner is thrown and injured in consequence of the smith's negligence in shoeing the smith is not liable for the injury." . . .

I do not see how we can uphold the judgment in the present case without overruling what has been so often said by this court and other courts of like authority in reference to the absence of any liability for negligence on the part of the original vendor of an ordinary carriage to any one except his immediate vendee. The absence of such liability was the very point actually decided in the English case of Winterbottom v. Wright, and the illustration quoted from the opinion of Chief Judge Ruggles in Thomas v. Winchester assumes that the law on the subject was so plain that the statement would be accepted almost as a matter of course. In the case at bar the defective wheel on an automobile moving only eight miles an hour was not any more dangerous to the occupants of the car than a similarly defective wheel would be to the occupants of a carriage drawn by a horse at the same speed; and yet unless the courts have been all wrong on this question up to the present time there would be no liability to strangers to the original sale in the case of the horse-drawn carriage.

## NOTES

**1. *A Landmark Case.*** The *MacPherson* trial record yields a somewhat different view of the facts of this case. The eyewitnesses all testified that MacPherson was traveling (in 1911) at over thirty miles per hour when the accident took place, not the leisurely eight miles per hour stated in the dissent. As James Henderson notes,

> [t]he problem with MacPherson's story was that it was premised on a physical impossibility. Uncontradicted expert testimony from defendant's experts showed that, at such a low speed in high gear, the Buick would have stalled in its tracks—the engine could not possibly have continued to operate in four inches of gravel—and the car would have come to a stop almost immediately.

James A. Henderson, Jr., *MacPherson v. Buick Motor Company*: Simplifying the Facts While Reshaping the Law, *in* Tort Stories 45–46 (Rabin & Sugarman eds., 2003).

The nature of the collision offers a compelling explanation as to why the wheel broke as it did. If the defect had been built in from the beginning, the wheel surely would have collapsed sooner under the pressure of driving on back-country roads. None of these details came out in the appellate litigation, as Buick preferred to concentrate on the privity defense on the appeal in the hopes of securing a categorical defense that did not turn on the condition of the wheel at the time of the accident. If the facts had come out, would the case for the privity limitation have been stronger or weaker? On its actual facts, could MacPherson get to the jury today?

**Exhibit 2.2 *MacPherson's* Facts: Not as Simple as Cardozo Suggests**

The few facts recited in Cardozo's *MacPherson* decision are "starkly simple" and "give[] no hint of the inherently controversial nature of the conclusions reached at trial." Henderson, *MacPherson v. Buick Motor Company*: Simplifying the Facts While Reshaping the Law, *in* Torts Stories 41, 51 (Rabin & Sugarman eds., 2003). By the time the case reached the Court of Appeals, the underlying facts of *MacPherson* had already been manipulated; Cardozo then altogether elided them in the course of reshaping the law of products liability. For instance:

- *Car Not New*. MacPherson's Buick Model 10 runabout "was not new, or even nearly new; the MacPhersons had owned it for over a year and had put it to hard use. . . . [They] had driven the car all over . . . upstate New York . . . on all kinds of surfaces, including rough country roads." Henderson, *supra*. They had used it, moreover, "with a lot of weight

aboard," to carry gravestones and markers, in connection with the family's gravestone and marker business. *Id.*

- *MacPherson No Novice*. By the time of the accident, MacPherson had "owned and operated several other automobiles . . . and was an experienced driver." *Id.*
- *Travel at High Gear*. The accident occurred on a "paved state road," on which MacPherson, according to "several disinterested eyewitnesses," "shifted the Buick into high gear and pushed the speed up to over 30 miles an hour." *Id.* at 42, 45. MacPherson testified that he was only going eight miles per hour—a speed at which the accident would have been, according to uncontradicted expert testimony, a "physical impossibility." *Id.* at 45.
- *When Did That Wheel Break?* The Buick ran into a "stretch of loose gravel" on the paved road, at which time MacPherson "lost control" of the car, which slid off the road to the right, and "struck a telephone pole with the front right bumper, spun around 180 degrees from its own momentum, and fell . . . into a three-foot ditch. When the automobile landed in the ditch, the left rear wheel broke under the sudden force of the impact. . . ." *Id.* at 43. MacPherson, however, testified that "the left rear wheel suddenly collapsed while the car was being driven," *id.* at 47—a rendition ostensibly endorsed in full by Cardozo. ("While the plaintiff was in the car, it suddenly collapsed. He was thrown out and injured. One of the wheels was made of defective wood, and its spokes crumbled into fragments." *MacPherson*, 111 N.E. at 1051.)

As argued on appeal, *MacPherson* counts as a landmark decision in the history of our law. Before *MacPherson*, Sanborn, J., in Huset v. J.I. Case, *supra* at 47, stated the law as it stood in virtually all jurisdictions, including New York. After *MacPherson*, one jurisdiction after another abandoned the privity rule in cases involving physical injuries caused by defective products. Subsequent cases incrementally extended the scope of *MacPherson*. Thus in Smith v. Peerless Glass Co., 181 N.E. 576 (N.Y. 1932), the court allowed a direct action for negligence to be brought against the manufacturer of a component part, such as the wheel maker in *MacPherson*. Today, every jurisdiction in the United States follows the *MacPherson* rule. Great Britain eventually abandoned *Winterbottom* as well in Donoghue v. Stevenson, [1932] AC 562 (HL) 580, 599 (appeal taken from Scot.), in which the plaintiff was allowed to sue, even without privity, the maker of a ginger beer bottle for the physical harm sustained when she drank the remains of a decomposed snail left in an opaque bottle of its brew. While the House of Lords went out of its way to avoid explicitly overruling Winterbottom v. Wright, it took exception to its view of privity:

> [A] manufacturer of products which he sells in such a form as to show that he intends them to reach the ultimate consumer in the form in which they left him, with no reasonable possibility of intermediate examination, and with the knowledge that the absence of reasonable care in the preparation or putting up of the products is likely to result in injury to the consumer's life or property, owes a duty to the consumer to take that reasonable care.

Could MacPherson have recovered under this formulation of the rule in light of his ability to inspect the wheel?

**2.** ***Privity in Contract Law: The Warranty Side of the Line.*** In *Huset*, Sanborn, J., noted that products liability claims frequently sounded in contract as well as in negligence. Often the plaintiff's strategy is to claim that the defendant made an express or implied warranty that the product sold was fit for its intended purpose. These contract theories must surmount two obstacles: privity and the intrinsic limitations of warranty law.

First, could the plaintiff rely on a warranty theory if she did not purchase the product directly from the defendant? In Chysky v. Drake Brothers Co., 139 N.E. 576, 577 (N.Y.

1923), the plaintiff, a waitress, was given a piece of the defendant's cake for lunch. She bit on a concealed nail that had been baked into the cake and suffered injuries to her mouth. Section 96 of the New York Personal Property Code provided that

> there is no implied warranty or condition as to the quality or fitness for any particular purpose of goods supplied under a contract to sell or a sale, except as follows: 1. Where the buyer, expressly or by implication, makes known to the seller the particular purpose for which the goods are required, and it appears that the buyer relies on the seller's skill or judgment (whether he be the grower or manufacturer or not), there is an implied warranty that the goods shall be reasonably fit for such purpose.

Even after *MacPherson*, the New York Court of Appeals held that the plaintiff's cause of action failed under this section, stating that

> [t]he general rule is that a manufacturer or seller of food, or other articles of personal property, is not liable to third persons, under an implied warranty, who have no contractual relations with him. The reason for this rule is that privity of contract does not exist between the seller and such third persons, and unless there be privity of contract, there can be no implied warranty.

*Chysky*, 139 N.E. at 578.

The privity barrier was overcome in Baxter v. Ford Motor Co., 12 P.2d 409, 412 (Wash. 1932). The plaintiff was injured in the eye when a small rock shattered the front windshield of his car, which was manufactured by Ford and sold to the plaintiff by the defendant dealer, St. John Motors. The Washington Supreme Court allowed the dealer to escape liability under a provision in the contract of sale that excluded all warranties. But relying on Thomas v. Winchester, the court held that Ford could be responsible for its representations in catalogues and printed materials that St. John distributed to customers about the car's "Tri-plex shatter-proof glass windshield."

> The rule in such cases does not rest upon contractual obligations, but rather on the principle that the original act of delivering an article is wrong, when, because of the lack of those qualities which the manufacturer represented it as having, the absence of which could not be readily detected by the consumer, the article is not safe for the purposes for which the consumer would ordinarily use it.
>
> Since the rule of *caveat emptor* was first formulated, vast changes have taken place in the economic structures of the English speaking peoples. Methods of doing business have undergone a great transition. Radio, bill boards and the products of the printing press have become the means of creating a large part of the demand that causes goods to depart from factories to the ultimate consumer. It would be unjust to recognize a rule that would permit manufacturers of goods to create a demand for their products by representing that they possess qualities which they, in fact, do not possess; and then, because there is no privity of contract existing between the consumer and the manufacturer, deny the consumer the right to recover if damages result from the absence of those qualities, when such absence is not readily noticeable.

Dealer liability on an implied warranty theory was also at issue in McCabe v. L.K. Liggett Drug Co., 112 N.E.2d 254, 256–57 (Mass. 1953), where the plaintiff was injured by a metal coffee maker, the "Lucifer Lifetime," sold (but not manufactured) by the defendant in a sealed cardboard box and assembled by the plaintiff in accordance with the instructions. The plaintiff's expert testified that the "notches" in the coffee maker's filtration system were "inadequate to provide for the release of the pressure which developed from the boiling water," especially if they became clogged by the "congealing" of the coffee grounds. As a result, the coffee maker blew up and injured the plaintiff. Williams, J., brushed aside other defenses as follows:

> The sale carried an implied warranty by the seller that the appliance was a coffee maker of merchantable quality. G. L. (Ter. Ed.) c. 106, §17 (2). Merchantable quality means that goods are reasonably suitable for the ordinary uses for which goods of that description are sold. . . .

The fact that the apparatus violently burst apart in the manner described showed that the accumulating pressure was not being released and in the absence of explanation was itself evidence of a defective condition. The jury could find that the explosion was caused by the failure of the water to rise into the upper bowl and from an examination of the notches in the filter that this failure was due to an inadequate outlet and the clogging effect of coffee grounds which would collect around the notches.

If the coffee maker was so imperfect in design that it could not be used without the likelihood of an explosion it could be found that the appliance was not reasonably fit for making coffee and therefore not merchantable. The plaintiff was not deprived of her right to rely upon the implied warranty either by a failure to inspect or by an inspection before use, as it could have been found that the defect in design would not be obvious to an ordinary person on inspection.

The judge was not justified in entering the verdict for the defendant on the ground that, as contended by the defendant, the notice required by G. L. (Ter. Ed.) c.106, §38, was insufficient, in not stating the exact date of the purchase or the name of the purchaser. Information as to the exact date of the sale was here of little if of any importance to the seller. The defendant had been selling these coffee makers over a period of a week. Presumably all were constructed alike. No claim was made that there was a defect in the particular appliance which was not common to all. The notice indicated a date of purchase within the period when they were being sold and was sufficient to enable the defendant to examine into any fault in their common design. The name of the person who actually made the purchase did not enter into the transaction with the defendant and the failure to state it did not invalidate the notice.

After *MacPherson*, how would a defense lawyer attack a plaintiff's story? Is there any difference between a defective and an unmerchantable appliance? Why shouldn't this action be brought against the manufacturer? How do the parallel lines of warranty and tort evolve?

## *Escola v. Coca Cola Bottling Co. of Fresno*

150 P.2d 436 (Cal. 1944)

[The plaintiff was a waitress. As part of her job, she was placing into the restaurant's refrigerator bottles of Coca-Cola that had been delivered to the restaurant at least 36 hours earlier. As she put the fourth bottle into the refrigerator, it exploded in her hand, causing severe injuries. The plaintiff alleged that the defendant had been negligent in selling "bottles containing said beverage which on account of excessive pressure of gas or by reason of some defect in the bottle was dangerous . . . and likely to explode."

The jury entered a verdict for the plaintiff that was affirmed on appeal. Gibson, J., wrote as follows: "The bottle was admittedly charged with gas under pressure, and the charging of the bottle was within the exclusive control of the defendant. As it is a matter of common knowledge that an overcharge would not ordinarily result without negligence, it follows under the doctrine of res ipsa loquitur that if the bottle was in fact excessively charged an inference of defendant's negligence would arise."]

Traynor, J. I concur in the judgment, but I believe the manufacturer's negligence should no longer be singled out as the basis of a plaintiff's right to recover in cases like the present one. In my opinion it should now be recognized that a manufacturer incurs an absolute liability when an article that he has placed on the market, knowing that it is to be used without inspection, proves to have a defect that causes injury to human beings. MacPherson v. Buick Motor Co. established the principle, recognized by this court, that irrespective of privity of contract, the manufacturer is responsible for an injury caused by such an article to any person who comes in lawful contact with it. In these cases the source of the manufacturer's liability was his negligence in the manufacturing process or in the inspection of component parts supplied by others. Even if there is no negligence, however, public policy

demands that responsibility be fixed wherever it will most effectively reduce the hazards to life and health inherent in defective products that reach the market. It is evident that the manufacturer can anticipate some hazards and guard against the recurrence of others, as the public cannot. Those who suffer injury from defective products are unprepared to meet its consequences. The cost of an injury and the loss of time or health may be an overwhelming misfortune to the person injured, and a needless one, for the risk of injury can be insured by the manufacturer and distributed among the public as a cost of doing business. It is to the public interest to discourage the marketing of products having defects that are a menace to the public. If such products nevertheless find their way into the market it is to the public interest to place the responsibility for whatever injury they may cause upon the manufacturer, who, even if he is not negligent in the manufacture of the product, is responsible for its reaching the market. However intermittently such injuries may occur and however haphazardly they may strike, the risk of their occurrence is a constant risk and a general one. Against such a risk there should be general and constant protection and the manufacturer is best situated to afford such protection.

The injury from a defective product does not become a matter of indifference because the defect arises from causes other than the negligence of the manufacturer, such as negligence of a submanufacturer of a component part whose defects could not be revealed by inspection, or unknown causes that even by the device of res ipsa loquitur cannot be classified as negligence of the manufacturer. The inference of negligence may be dispelled by an affirmative showing of proper care. If the evidence against the fact inferred is "clear, positive, uncontradicted, and of such a nature that it cannot rationally be disbelieved, the court must instruct the jury that the nonexistence of the fact has been established as a matter of law." An injured person, however, is not ordinarily in a position to refute such evidence or identify the cause of the defect, for he can hardly be familiar with the manufacturing process as the manufacturer himself is. In leaving it to the jury to decide whether the inference has been dispelled, regardless of the evidence against it, the negligence rule approaches the rule of strict liability. It is needlessly circuitous to make negligence the basis of recovery and impose what is in reality liability without negligence. If public policy demands that a manufacturer of goods be responsible for their quality regardless of negligence there is no reason not to fix that responsibility openly.

**Exhibit 2.3 Roger Traynor**

Justice Roger Traynor (1900–1983), whose 30-year tenure on the California Supreme Court encompassed 24 years as an associate justice (1940–1964) and 6 as chief justice (1964–1970), is the subject of Chapter 6 in G. Edward White, Tort Law in America: An Intellectual History (2003). According to White, the Traynor years were marked by "a strong interest in academic literature as source material; an effort to preserve, where possible, the lawmaking power of courts [in the face of "an increasingly detailed legislative apparatus"], and a search for a harmony of result and doctrine in his opinions." White, *supra*.

White further explains: "The basis for Traynor's faith in the judiciary as a lawmaking force . . . was his conviction that rationality could be achieved through enlightened judging." *Id.* at 188. Traynor, who "never departed from his belief that rationality was an achievable judicial goal . . . was not disturbed by the 'activist judge' label often attached to him." *Id.*

*Source: Law School Archives, University of California, Berkeley*

Indeed, and as shown by his concurrence in *Escola* and decision in *Greenman v. Yuba Power Products*, Inc., Traynor, "[i]n his activist conception of judging . . . was one of the pioneers of his time and one of the precursors of a 'policymaking' role for judges in tort cases. . . . Traynor was committed to using his powers as fully as possible to promote social policies in which he believed and to reorient the common law of California in directions he thought rational and desirable." *Id.* at 208.

In the case of foodstuffs, the public policy of the state is formulated in a criminal statute. . . . Statutes of this kind result in a strict liability of the manufacturer in tort to the member of the public injured.

The statute may well be applicable to a bottle whose defects cause it to explode. In any event it is significant that the statute imposes criminal liability without fault, reflecting the public policy of protecting the public from dangerous products placed on the market, irrespective of negligence in their manufacture. While the Legislature imposes criminal liability only with regard to food products and their containers, there are many other sources of danger. It is to the public interest to prevent injury to the public from any defective goods by the imposition of civil liability generally.

The retailer, even though not equipped to test a product, is under an absolute liability to his customer, for the implied warranties of fitness for proposed use and merchantable quality include a warranty of safety of the product. This warranty is not necessarily a contractual one; see 1 Williston on Sales, 2d ed., §§197–201, for public policy requires that the buyer be insured at the seller's expense against injury. The courts recognize, however, that the retailer cannot bear the burden of this warranty, and allow him to recoup any losses by means of the warranty of safety attending the wholesaler's or manufacturer's sale to him. . . . Such a procedure, however, is needlessly circuitous and engenders wasteful litigation. Much would be gained if the injured person could base his action directly on the manufacturer's warranty.

The liability of the manufacturer to an immediate buyer injured by a defective product follows without proof of negligence from the implied warranty of safety attending the sale. Ordinarily, however, the immediate buyer is a dealer who does not intend to use the product himself, and if the warranty of safety is to serve the purpose of protecting health and safety it must give rights to others than the dealer. In the words of Judge Cardozo in the *MacPherson* case: "The dealer was indeed the one person of whom it might be said with some approach to certainty that by him the car would not be used. Yet, the defendant would have us say that he was the one person whom it was under a legal duty to protect. The law does not lead us to so inconsequent a solution." While the defendant's negligence in the *MacPherson* case made it unnecessary for the court to base liability on warranty, Judge Cardozo's reasoning recognized the injured person as the real party in interest and effectively disposed on the theory that the liability of the manufacturer incurred by his warranty should apply only to the immediate purchaser. It thus paves the way for a standard of liability that would make the manufacturer guarantee the safety of his product even when there is no negligence.

This court and many others have extended protection according to such a standard to consumers of food products, taking the view that the right of a consumer injured by unwholesome food does not depend "upon the intricacies of the law of sales" and that the warranty of the manufacturer to the consumer in absence of privity of contract rests on public policy. Dangers to life and health inhere in other consumers' goods that are defective and there is no reason to differentiate them from the dangers of defective food products.

In the food products cases the courts have resorted to various fictions to rationalize the extension of the manufacturer's warranty to the consumer: that a warranty runs with the

chattel; that the cause of action of the dealer is assigned to the consumer; that the consumer is a third party beneficiary of the manufacturer's contract with the dealer. They have also held the manufacturer liable on a mere fiction of negligence: "Practically he must know [the product] is fit, or bear the consequences if it proves destructive." Such fictions are not necessary to fix the manufacturer's liability under a warranty if the warranty is severed from the contract of sale between the dealer and the consumer and based on the law of torts as a strict liability. Warranties are not necessarily rights arising under a contract. An action on a warranty "was, in its origin, a pure action of tort," and only late in the historical development of warranties was an action in assumpsit allowed. (Ames, The History of Assumpsit, 2 Harv. L. Rev. 1, 8; 4 Williston on Contracts (1936) §970.) . . .

As handicrafts have been replaced by mass production with its great markets and transportation facilities, the close relationship between the producer and consumer of a product has been altered. Manufacturing processes, frequently valuable secrets, are ordinarily either inaccessible to or beyond the ken of the general public. The consumer no longer has means or skill enough to investigate for himself the soundness of a product, even when it is not contained in a sealed package, and his erstwhile vigilance has been lulled by the steady efforts of manufacturers to build up confidence by advertising and marketing devices such as trademarks. (See Thomas v. Winchester, 6 N.Y. 697; Baxter v. Ford Motor Co.[, 12 P.2d 409 (Wash. 1932)].) Consumers no longer approach products warily but accept them on faith, relying on the reputation of the manufacturer or the trademark. Manufacturers have sought to justify that faith by increasingly high standards of inspection and a readiness to make good on defective products by way of replacements and refunds. (See Bogert and Fink, Business Practices Regarding Warranties in the Sale of Goods, 25 Ill. L. Rev. 400.) The manufacturer's obligation to the consumer must keep pace with the changing relationship between them; it cannot be escaped because the marketing of a product has become so complicated as to require one or more intermediaries. Certainly, there is greater reason to impose liability on the manufacturer than on the retailer who is but a conduit of a product that he is not himself able to test.

The manufacturer's liability should, of course, be defined in terms of the safety of the product in normal and proper use, and should not extend to injuries that cannot be traced to the product as it reached the market.

## NOTES

**1. *Rationales.*** At a factual level, does the switch to a theory of strict liability resolve the question of whether the Coca-Cola bottles were excessively charged in the factory or were mishandled by subsequent parties? As a theoretical matter, how sound are the various rationales for strict liability that Traynor, J., offers?

a. ***Loss Minimization.*** One rationale offered is that the manufacturer, rather than the unwitting consumer, is most knowledgeable and is therefore in the best position to minimize the losses that arise out of the general use of its product. If correct, should we also require strict liability for defective premises owned by commercial enterprises, or for that matter, strict liability for automobile accidents, at least when business enterprises are defendants? On this rationale, what adjustments should be made if the plaintiff or some downstream third party is in a better position to take the desired precautions? What if the plaintiff shook the bottle in use, or stored it in a hot place? Is it consistent with the loss minimization rationale to allow the manufacturer to contract out of liability with the consumer? Does a negligence rule fail to

create the necessary incentives for the manufacturer to take appropriate cost-justified precautions?

b. ***Loss Spreading.*** A second defense of the strict liability rule in *Escola* rests upon the ability of the defendant producer to spread the damages among many consumers, thus cushioning the "overwhelming misfortune" of the injured person or her family. This risk-spreading rationale for strict liability was challenged in Wights v. Staff Jennings, Inc., 405 P.2d 624, 628 (Or. 1965), where the court observed:

> The rationale of risk spreading and compensating the victim has no special relevancy to cases involving injuries resulting from the use of defective goods. The reasoning would seem to apply not only in cases involving personal injuries arising from the *sale* of defective goods, but equally to any case where an injury results from the risk creating conduct of the seller in any stage of the production and distribution of goods. Thus a manufacturer would be strictly liable even in the absence of fault for any injury to a person struck by one of the manufacturer's trucks being used in transporting his goods to market. It seems to us that the enterprise liability rationale employed in the *Escola* case proves too much and that if adopted would compel us to apply the principle of strict liability in all future cases where the loss could be distributed.

c. ***Elimination of Proof Complications.*** Traynor, J., also defends strict liability in *Escola* because it simplifies the law by eliminating the need to resort to res ipsa loquitur. In all contexts, a strict liability rule switches the residual risk of unavoidable accidents from the plaintiff to the defendant. With exploding soda bottles, that risk is generally quite small given the stringent quality control and inspection devices incorporated into the manufacturing process. How does res ipsa loquitur apply when misconduct by the plaintiff or a third party is also at issue? Should it make any difference that the plaintiff in *Escola* could not produce the pieces of the broken bottle for inspection and examination?

d. ***The Foodstuffs Analogy.*** A fourth defense of strict liability rests on the analogy between adulterated foodstuffs and product defects. In this regard, the law after *MacPherson* and before *Escola* drew a distinction between foodstuffs that were sold in sealed containers and those that were not. For goods sold in sealed containers, the law exempted the retailer from liability but allowed a direct suit against the manufacturer, albeit on a negligence theory. See, e.g., Richenbacher v. California Packing Corp., 145 N.E. 281 (Mass. 1924), sustaining the use of res ipsa loquitur when the plaintiff's mouth was cut by glass found in a container of spinach. In contrast, when goods were not packaged, the general rule imposed negligence liability, if at all, on the retailer, but not on the original food supplier. Is *Richenbacher* an easier case for res ipsa loquitur than *Escola*? Why?

e. ***Corrective Justice.*** Another argument for strict liability in products cases—one not pressed by Traynor—is that the loss should be placed upon the party who created the dangerous condition, not the party who suffered from it. This reasoning is similar to the argument for strict liability in ordinary trespass cases, or even under the rule in Rylands v. Fletcher: once the plaintiff establishes the causal connection to the defendant's act (in *Escola*, the defective bottling under pressure that caused harm), then, prima facie, the defendant should be held liable. Note, however, one structural difference between the two types of cases. With abnormally dangerous activities, the defendant is virtually always in possession of the dangerous instrumentality just before it causes the accident, so the class of defenses based upon plaintiff's conduct remains quite small. With products liability, the defendant is never in possession of the dangerous product when it causes injury, so that the older privity limitation

might be a sensible way for liability to track possession (and hence control), except in those few cases in which a party out of possession is in a better position to avoid the loss. See Richard A. Epstein, The Historical Origins and Economic Structure of Workers' Compensation Law, 16 Ga. L. Rev. 775, 806–08 (1982), defending privity for workplace injuries on the ground that employer's liability is both cheaper and more efficient than manufacturer's liability.

**2. *Criticisms.*** For an early criticism of strict liability in products cases, see Marcus L. Plant, Strict Liability of Manufacturers for Injuries Caused by Defects in Products — An Opposing View, 24 Tenn. L. Rev. 938, 945 (1957), in which it is noted that "[t]he element which is most disturbing to manufacturers is not the potential judgment of legal liability but the injury which is done to the reputation of the product and its producers." Note that modern "event studies" establish that the decline in the value of the shares of a publicly traded company after a major product incident is greater than the anticipated amount of the liability. For evidence of the impact of these studies, see David Prince & Paul H. Rubin, The Effects of Product Liability Litigation on the Value of Firms, 45 Am. L. & Econ. Rev. 44 (2002):

> [F]irms facing lawsuits for their products suffer capital market losses approximately equal to a worst-case scenario associated with the litigation. Thus, it appears that individual firms may suffer reputation costs as a consequence of product liability lawsuits but that these reputation losses are smaller than losses from government actions such as recall.

See also David Dranove, Delivering Bad News: Market Responses to Negligence, 55 J.L. & Econ. 1, 2 (2012), which notes some "anecdotal evidence" that points to some reputational effect:

> For example, sales of Johnson & Johnson's Tylenol plummeted in 1982 after the product was tainted by tampering, and ValuJet lost customers and even changed its name after the 1996 crash of flight 592. More recently, the spate of vehicle recalls faced by Toyota over allegedly defective acceleration put the automaker under intense public scrutiny and caused its U.S. market share to plummet. . . .

To what extent should the negative effect depend on the perceived fault of the defendant in bringing about the incident? The promptness of its corrective actions? The willingness to remove product from the market? Is the perception of fault likely to be greater for airline crashes and brake failures than for contaminations known to be caused downstream by malicious third parties?

**3. *Implied Warranty: Elimination of Privity in Contract Law.*** The early privity limitation in Chysky v. Drake, *supra* at 53, was overruled 38 years later in Greenberg v. Lorenz, 173 N.E.2d 773 (N.Y. 1961). There the plaintiff was injured when she ate canned salmon that contained sharp metal slivers, sold by the defendant retail food dealer to her father. The court below dismissed the plaintiff's complaint because the plaintiff had not purchased the salmon herself. The Court of Appeals reversed. Just about that time, the warranty provisions of the law of sales were reworked under a new Uniform Commercial Code, which offers three possible approaches to the scope of the warranty.

## UNIFORM COMMERCIAL CODE

### §2-318. Third Party Beneficiaries of Warranties Express or Implied

**Alternative A**

A seller's warranty whether express or implied extends to any natural person who is in the family or household of his buyer or who is a guest in his home if it is reasonable

> to expect that such person may use, consume or be affected by the goods and who is injured in person by breach of the warranty. A seller may not exclude or limit the operation of this section.
>
> **Alternative B**
>
> A seller's warranty whether express or implied extends to any natural person who may reasonably be expected to use, consume or be affected by the goods and who is injured in person by breach of the warranty. A seller may not exclude or limit the operation of this section.
>
> **Alternative C**
>
> A seller's warranty whether express or implied extends to any person who may reasonably be expected to use, consume or be affected by the goods and who is injured by breach of the warranty. A seller may not exclude or limit the operation of this section with respect to injury to the person of an individual to whom the warranty extends.

New York originally adopted alternative A. In 1975, however, it adopted alternative B (N.Y. U.C.C. Law §2-318 (2024)). If *X* steals a roll from *Y*, who had purchased it from *Z*, should *X* recover from *Z* under the variations of section 2-318 when injured by a piece of sharp metal baked into the roll? Why should the parties, unlike the dealer in *Baxter*, *supra*, be unable to contract out of this provision?

4. ***Henningsen: Implied Warranty with a Vengeance.*** In Henningsen v. Bloomfield Motors, Inc., 161 A.2d 69 (N.J. 1960), Henningsen purchased a new Plymouth automobile, manufactured by the defendant Chrysler Corporation, from the defendant Bloomfield Motors, Inc. Henningsen gave the car to his wife, after indicating to the dealer his intention to make it a gift. The contract of sale between Mr. Henningsen and the two defendants expressly disclaimed all warranties by the dealer or manufacturer, except one that limited the liability of the defendants to the original purchaser and only then for replacement of defective parts within ninety days or 4,000 miles, whichever occurred first. Shortly after the car was purchased, the plaintiff, Mrs. Henningsen, was driving along a clear road when the steering mechanism suddenly went awry. The car went out of control and veered off the road and into a wall, injuring her. She sued on theories of negligence and warranty. After the trial court dismissed the negligence claim, the jury found for the plaintiff against both defendants on the warranty claim, and the defendants appealed. In a very lengthy opinion, Francis, J., examined how the courts had extended the implied warranty of merchantability to individuals who were not party to the original sales agreement, a development he found absolutely necessary as manufacturers increasingly distanced themselves from sales act liability to consumers by a complex web of contracts. He insisted that the limited protection to the plaintiff under this express warranty was a "sad commentary" on the marketing practices of automobile manufacturers.

Although he thought the ordinary warranty of merchantability might technically survive this disclaimer clause, Francis, J., did not rely on any interpretative techniques. Instead he voided the disclaimer clause on the ground that it "was not fairly obtained." It followed that the benefit of the implied warranty ran to the plaintiff, even in the absence of privity, so long as the defendant "puts a new automobile in the stream of trade and promotes its purchase by the public."

A breakthrough for its time, *Henningsen*'s importance appears to have waned somewhat, not because courts have rejected its outcome, but because, ironically, its implied warranty theory tied products liability actions too closely to the law of sales. Modern cases, however, still

occasionally allow a jury to find liability under a warranty theory while denying recovery under a tort theory. In Denny v. Ford Motor Co., 662 N.E.2d 730, 736 (N.Y. 1995), the plaintiff was injured when her Ford Bronco, owing to its high center of gravity, rolled over after she slammed on the brakes. The jury found that the vehicle was not "defective" but awarded her $1,200,000 in damages ($2,460,945 in 2024 dollars) on an implied warranty theory. The court rejected Ford's contention that tort had "completely subsumed" warranty theory, noting that the "negligence-like risk/benefit component of the defect element differentiates strict products liability claims from U.C.C.-based breach of implied warranty claims in cases involving design defects."

Can a product without a defect flunk the merchantability test? In Castro v. QVC Network, 139 F.3d 114, 118 (2d Cir. 1998), the plaintiff was badly burned when a twenty-five-pound Thanksgiving turkey fell on her legs and ankles. It caused second- and third-degree burns after it slipped out of a roaster manufactured by defendant U.S.A. T-Fal Corp. and sold by defendant QVC over its home-shopping network. The trial judge refused to offer separate instructions on both strict liability and warranty counts, but after the jury found for the defendants, Calabresi, J., relied on *Denny* to grant a new trial: "The imposition of strict liability for an alleged design 'defect' is determined by a risk-utility standard. The notion of 'defect' in a U.C.C.-based breach of warranty claim focuses, instead, on consumer expectations." Here, according to Calabresi, J., the purpose for which the product was marketed (cooking a large turkey) was different from its designed-for use (cooking low-volume baked goods). Will all "dual-purpose" goods henceforth require separate jury instructions?

What if a product component is unfit for its ordinary purpose? In Nemes v. Dick's Sporting Goods, Inc., 521 F. Supp. 3d 328, 343–44 (S.D.N.Y. 2021), a case about a crossbow with an allegedly defective finger guard, Roman, J., distinguished *Castro*:

> That holding does not reflect that a product's component parts, e.g., the handle of the pan, define the ordinary purpose of that product. . . . [T]he ordinary purpose of a good is not usually defined by the individual function of an ancillary component. . . . Instead, the implied warranty is breached where the product in question is not fit for the ordinary purpose for which it is to be used.

Is the court's holding sound given that consumers expect product components to serve the functions for which they are designed?

**5.** ***Strict Liability in Torts: The* Greenman *Reformulation.*** Shortly after *Henningsen*, the tort side of products liability also gravitated toward strict liability. In Greenman v. Yuba Power Products, Inc., 377 P.2d 897, 900–01 (Cal. 1963), the plaintiff's wife gave him a Shopsmith combination power tool, manufactured by the defendant, that could be used as a saw, a drill, and a wood lathe. The plaintiff read the manufacturer's brochure, which contained the following statements: "(1) WHEN SHOPSMITH IS IN HORIZONTAL POSITION—Rugged construction of frame provides rigid support from end to end. Heavy centerless-ground steel tubing insures perfect alignment of components. (2) SHOPSMITH maintains its accuracy because every component has positive locks that hold adjustments through rough or precision work." In the course of working the lathe, a piece of wood "suddenly flew out of the machine and struck him on the forehead, inflicting serious injury." There was substantial evidence that the plaintiff's injuries were caused by the defective construction of the Shopsmith, whose set screws were of insufficient strength to hold the wood in place while the lathe was being operated. The plaintiff recovered damages from the manufacturer for negligence and breach of both express and implied warranties.

One of the defendant's contentions on appeal was that the plaintiff's cause of action was barred because he failed to give notice of his injury within a "reasonable time" as required

by section 1769 of the California Civil Code. Traynor, J., speaking for the entire court, sidestepped the "intricacies" of the warranty provisions by opting for strict liability in tort:

> A manufacturer is strictly liable in tort when an article he places on the market, knowing that it is to be used without inspection for defects, proves to have a defect that causes injury to a human being. Recognized first in the case of unwholesome food products, such liability has now been extended to a variety of other products that create as great or greater hazards if defective.
>
> Although in these cases strict liability has usually been based on the theory of an express or implied warranty running from the manufacturer to the plaintiff, the abandonment of the requirement of a contract between them, the recognition that the liability is not assumed by agreement but imposed by law, and the refusal to permit the manufacturer to define the scope of its own responsibility for defective products make clear that the liability is not one governed by the law of contract warranties but by the law of strict liability in tort. Accordingly, rules defining and governing warranties that were developed to meet the needs of commercial transactions cannot properly be invoked to govern the manufacturer's liability to those injured by their defective products unless those rules also serve the purposes for which such liability is imposed.
>
> We need not recanvass the reasons for imposing strict liability on the manufacturer. The purpose of such liability is to insure that the costs of injuries resulting from defective products are borne by the manufacturers that put such products on the market rather than by the injured persons who are powerless to protect themselves. Sales warranties serve this purpose fitfully at best. In the present case, for example, plaintiff was able to plead and prove an express warranty only because he read and relied on the representations of the Shopsmith's ruggedness contained in the manufacturer's brochure. Implicit in the machine's presence on the market, however, was a representation that it would safely do the jobs for which it was built. Under these circumstances, it should not be controlling whether plaintiff selected the machine because of the statements in the brochure, or because of the machine's own appearance of excellence that belied the defect lurking beneath the surface, or because he merely assumed that it would safely do the jobs it was built to do. It should not be controlling whether the details of the sales from manufacturer to retailer and from retailer to plaintiff's wife were such that one or more of the implied warranties of the sales act arose. (Civ. Code, §1735.) "The remedies of injured consumers ought not to be made to depend upon the intricacies of the law of sales." To establish the manufacturer's liability it was sufficient that plaintiff proved that he was injured while using the Shopsmith in a way it was intended to be used as a result of a defect in design and manufacture of which plaintiff was not aware that made the Shopsmith unsafe for its intended use.

## SECTION C. THE RESTATEMENTS: A TALE OF TWO TEXTS

### RESTATEMENT (SECOND) OF TORTS

**§402a. Special Liability of Seller of Product for Physical Harm to User or Consumer**

(1) One who sells any product in a defective condition unreasonably dangerous to the user or consumer or to his property is subject to liability for physical harm thereby caused to the ultimate user or consumer, or to his property, if

(a) the seller is engaged in the business of selling such a product, and

(b) it is expected to and does reach the user or consumer without substantial change in the condition in which it is sold.

(2) The rule stated in Subsection (1) applies although

(a) the seller has exercised all possible care in the preparation and sale of his product, and

(b) the user or consumer has not bought the product from or entered into any contractual relation with the seller.

***Caveat:*** The Institute expresses no opinion as to whether the rules stated in this Section may not apply

(1) to harm to persons other than users or consumers

(2) to the seller of a product expected to be processed or otherwise substantially changed before it reaches the user or consumer or

(3) to the seller of a component part of a product to be assembled.

***Comment f. Business of Selling:*** The rule stated in this Section applies to any person engaged in the business of selling products for use or consumption. It therefore applies to any manufacturer of such a product, to any wholesale or retail dealer or distributor, and to the operator of a restaurant. . . .

The rule does not, however, apply to the occasional seller of food or other such products who is not engaged in that activity as a part of his business. Thus it does not apply to the housewife who, on one occasion, sells to her neighbor a jar of jam or a pound of sugar. Nor does it apply to the owner of an automobile who, on one occasion, sells it to his neighbor, or even sells it to a dealer in used cars, and this even though he is fully aware that the dealer plans to resell it. The basis for the rule is the ancient one of the special responsibility for the safety of the public undertaken by one who enters into the business of supplying human beings with products which may endanger the safety of their persons and property, and the forced reliance upon that undertaking on the part of those who purchase such goods. This basis is lacking in the case of the ordinary individual who makes the isolated sale, and he is not liable to a third person, or even to his buyer, in the absence of his negligence. . . .

***Comment g. Defective Condition:*** The rule stated in this Section applies only where the product is, at the time it leaves the seller's hands, in a condition not contemplated by the ultimate consumer, which will be unreasonably dangerous to him. The seller is not liable when he delivers the product in a safe condition, and subsequent mishandling or other causes make it harmful by the time it is consumed. The burden of proof that the product was in a defective condition at the time that it left the hands of the particular seller is upon the injured plaintiff; and unless evidence can be produced which will support the conclusion that it was then defective, the burden is not sustained.

Safe condition at the time of delivery by the seller will, however, include proper packaging, necessary sterilization, and other precautions required to permit the product to remain safe for a normal length of time when handled in a normal manner.

***Comment h.*** A product is not in defective condition when it is safe for normal handling and consumption. If the injury results from abnormal handling, as where a bottled beverage is knocked against a radiator to remove the cap, or from abnormal preparation for use, as where too much salt is added to food, or from abnormal consumption, as where a child eats too much candy and is made ill, the seller is not liable. . . .

The defective condition may arise not only from harmful ingredients, not characteristic of the product itself either as to presence or quantity, but also from foreign objects contained in the product, from decay or deterioration before sale, or from the way in which the product is prepared or packed. No reason is apparent for distinguishing between the product itself and the container in which it is supplied; and the two are purchased by the user or consumer as an integrated whole. Where the container is itself dangerous, the product is sold in a defective condition. Thus a carbonated beverage in a bottle which is so weak, or cracked, or jagged at the edges, or bottled under such excessive pressure that it may explode or otherwise cause harm to the person who handles it, is in a defective and dangerous condition. . . .

***Comment i. Unreasonably Dangerous:*** The rule stated in this Section applies only where the defective condition of the product makes it unreasonably dangerous to the

user or consumer. Many products cannot possibly be made entirely safe for all consumption, and any food or drug necessarily involves some risk of harm, if only from over-consumption. Ordinary sugar is a deadly poison to diabetics, and castor oil found use under Mussolini as an instrument of torture. That is not what is meant by "unreasonably dangerous" in this Section. The article sold must be dangerous to an extent beyond that which would be contemplated by the ordinary consumer who purchases it, with the ordinary knowledge common to the community as to its characteristics. Good whiskey is not unreasonably dangerous merely because it will make some people drunk, and is especially dangerous to alcoholics; but bad whiskey, containing a dangerous amount of fusel oil, is unreasonably dangerous. Good tobacco is not unreasonably dangerous merely because the effects of smoking may be harmful; but tobacco containing something like marijuana may be unreasonably dangerous. Good butter is not unreasonably dangerous merely because, if such be the case, it deposits cholesterol in the arteries and leads to heart attacks; but bad butter, contaminated with poisonous fish oil, is unreasonably dangerous.

***Comment j. Directions or Warning:*** In order to prevent the product from being unreasonably dangerous, the seller may be required to give directions or warning, on the container, as to its use. The seller may reasonably assume that those with common allergies, as for example to eggs or strawberries, will be aware of them, and he is not required to warn against them. Where, however, the product contains an ingredient to which a substantial number of the population are allergic, and the ingredient is one whose danger is not generally known, or if known is one which the consumer would reasonably not expect to find in the product, the seller is required to give warning against it, if he has knowledge, or by the application of reasonable, developed human skill and foresight should have knowledge, of the presence of the ingredient and the danger. Likewise in the case of poisonous drugs, or those unduly dangerous for other reasons, warning as to use may be required.

But a seller is not required to warn with respect to products, or ingredients in them, which are only dangerous or potentially so, when consumed in excessive quantity, or over a long period of time, when the danger, or potentiality of danger, is generally known and recognized. Again the dangers of alcoholic beverages are an example, as are also those of foods containing such substances as saturated fats, which may over a period of time have a deleterious effect upon the human heart.

Where warning is given, the seller may reasonably assume that it will be read and heeded; and a product bearing such a warning, which is safe for use if it is followed, is not in defective condition, nor is it unreasonably dangerous.

***Comment k. Unavoidably Unsafe Products:*** There are some products which, in the present state of human knowledge, are quite incapable of being made safe for their intended and ordinary use. These are especially common in the field of drugs. An outstanding example is the vaccine for the Pasteur treatment of rabies, which not uncommonly leads to very serious and damaging consequences when it is injected. Since the disease itself invariably leads to a dreadful death, both the marketing and the use of the vaccine are fully justified, notwithstanding the unavoidable high degree of risk which they involve. Such a product, properly prepared, and accompanied by proper directions and warning, is not defective, nor is it *unreasonably* dangerous. The same is true of many other drugs, vaccines, and the like, many of which for this very reason cannot legally be sold except to physicians, or under the prescription of a physician. It is also true in particular of many new or experimental drugs as to which, because of lack of time and opportunity for sufficient medical experience, there can be no assurance of safety, or perhaps even of purity of ingredients, but such experience as there is justifies the marketing and use of the drug notwithstanding a medically recognizable risk. The seller of such products, again with the qualification that they are properly prepared and marketed, and proper warning is

given, where the situation calls for it, is not to be held to strict liability for unfortunate consequences attending their use, merely because he has undertaken to supply the public with an apparently useful and desirable product, attended with a known but apparently reasonable risk.

***Comment m. "Warranty":*** The rule stated in this Section does not require any reliance on the part of the consumer upon the reputation, skill, or judgment of the seller who is to be held liable, nor any representation or undertaking on the part of that seller. The seller is strictly liable although, as is frequently the case, the consumer does not even know who he is at the time of consumption. The rule stated in this Section is not governed by the provisions of the Uniform Sales Act, or those of the Uniform Commercial Code, as to warranties; and it is not affected by limitations on the scope and content of warranties, or by limitation to "buyer" and "seller" in those statutes. Nor is the consumer required to give notice to the seller of his injury within a reasonable time after it occurs, as is provided by the Uniform Act. . . .

***Comment n. Contributory Negligence:*** Since the liability with which this Section deals is not based upon negligence of the seller, but is strict liability, the rule applied to strict liability cases (see §524) applies. Contributory negligence of the plaintiff is not a defense when such negligence consists merely in a failure to discover the defect in the product, or to guard against the possibility of its existence. On the other hand the form of contributory negligence which consists in voluntarily and unreasonably proceeding to encounter a known danger, and commonly passes under the name of assumption of risk, is a defense under this Section as in other cases of strict liability. If the user or consumer discovers the defect and is aware of the danger, and nevertheless proceeds unreasonably to make use of the product and is injured by it, he is barred from recovery.

## NOTES

**1.** ***Second Restatement §402A.*** Until the adoption of the Restatement (Third) of Torts: Products Liability, section 402A and its comments formed the basic text of modern products liability law. At its inception, section 402A was noted for its adoption of a broad strict liability rule for product defects. Its early drafts were originally confined to foodstuffs and products intended for intimate bodily use, but by 1965 the strict liability rule was extended to all products. This broad application made it more difficult to devise a single rule to cover an endless diversity of products—for example, the unique issues raised by pharmaceuticals. Accordingly, Prosser and other drafters of the Second Restatement addressed many difficult questions in the comments to the basic text, which, over time, have become as important as the basic provision itself. Even today, the Third Restatement has not displaced the Second across the board, so it is critical to gain mastery over both. On the adoption of section 402A, see Richard A. Epstein, Modern Products Liability Law Ch. 6 (1980); George L. Priest, The Invention of Enterprise Liability: A Critical History of the Intellectual Foundations of Modern Tort Law, 14 J. Legal Stud. 461, 505–19 (1985).

The Second Restatement also contains section 402B, "Misrepresentation by Seller of Chattels to Consumer," which adopts a strict liability standard for a product seller, proclaiming that one "who, by advertising, labels, or otherwise, makes to the public a misrepresentation of a material fact concerning the character or quality of a chattel sold by him is subject to liability for physical harm to a consumer of the chattel caused by justifiable reliance upon the misrepresentation." Section 402B has been swallowed up in litigation by section 402A. Does it provide a superior basis for liability in *Henningsen*? In *Greenman*?

**2. *Bystander's Recovery.*** Current case law has gone beyond the Second Restatement by allowing injured bystanders to sue the original manufacturer. The initial hesitation regarding bystander cases rested in part on the uncertainty of whether any implied warranty or misrepresentation theory could hold the defendant accountable to anyone outside the chain of contracts. The bystander is not lured into using the product by the defendant's representations. Neither is she an immediate or ultimate beneficiary of any seller or manufacturer warranty. The bystander's case for strict liability in tort is far stronger: As with abnormally dangerous activities, the bystander has been hurt by a process that was in no sense her making because she never used the product at all. Although in practice bystander injuries are relatively infrequent compared to the numerous injuries to product consumers or users, today the liability of the manufacturer or seller to the bystander is universally allowed. See, e.g., Elmore v. Am. Motors Corp., 451 P.2d 84 (Cal. 1969); Codling v. Paglia, 298 N.E.2d 622 (N.Y. 1973); Dix W. Noel, Defective Products: Extension of Strict Liability to Bystanders, 38 Tenn. L. Rev. 1 (1970).

**RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY**

**§1. Liability of Commercial Seller or Distributor for Harm Caused by Defective Products**

One engaged in the business of selling or otherwise distributing products who sells or distributes a defective product is subject to liability for harm to persons or property caused by the defect.

**§2. Categories of Product Defects**

[For purposes of determining liability under section 1:]
A product is defective when, at the time of sale or distribution, it contains a manufacturing defect, is defective in design, or is defective because of inadequate instructions or warnings. A product:

(a) contains a manufacturing defect when the product departs from its intended design even though all possible care was exercised in the preparation and marketing of the product;

(b) is defective in design when the foreseeable risks of harm posed by the product could have been reduced or avoided by the adoption of a reasonable alternative design by the seller or other distributor, or a predecessor in the commercial chain of distribution, and the omission of the alternative design renders the product not reasonably safe;

(c) is defective because of inadequate instructions or warnings when the foreseeable risks of harm posed by the product could have been reduced or avoided by the provision of reasonable instructions or warnings by the seller or other distributor, or a predecessor in the commercial chain of distribution, and the omission of the instructions or warnings renders the product not reasonably safe.

## NOTES

**1. *Into the Next Generation.*** The Third Restatement reflects the transformation of products liability law after 1965. Most significantly, it adopts the now dominant tripartite classification of manufacturing, design, and warning defects, and establishes a distinct liability rule for each class. It keeps the original strict liability rule for products with manufacturing defects but imposes only the more limited obligation to make product designs, warnings, and instructions "reasonably safe." Although the Third Restatement rejects RST §402A's caveat

on bystander liability, many of the old rules still carry over, such as the exclusion of "casual sellers." See RTT: PL §1, cmt. *c.* Subsequent provisions of the Third Restatement examine each class of defects, and contain additional provisions to deal with prescription drugs, issues of causation, and affirmative defenses. For an early discussion of the revisions of the Second Restatement, by the joint reporters for the Third Restatement, see James A. Henderson, Jr. & Aaron Twerski, A Proposed Revision of Section 402A of the Restatement (Second) of Torts, 77 Cornell L. Rev. 1512 (1992). For an acceptance of the Third Restatement over the Second, see Evans v. Lorillard Tobacco Co., 990 N.E.2d 997, 1013–14 (Mass. 2013); for a continued preference for the Second Restatement over the Third, see Tincher v. Omega Flex, Inc., 104 A.3d 328, 335 (Pa. 2014), discussed *infra* Note 2.

**2.** ***Who Chooses to Adopt the Third Restatement?*** The Pennsylvania Supreme Court in *Tincher, supra* Note 1, wrestled with whether the courts, rather than the legislature, should play an active role in deciding whether to adopt the Third Restatement. While the court in *Tincher* believed this decision should be left to the democratically elected General Assembly, is it ever justified to leave this decision to the courts?

## SECTION D. PRODUCT DEFECTS

### 1. Manufacturing Defects

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: PRODUCTS LIABILITY**

**§3. Circumstantial Evidence Supporting Inference of Product Defect**

It may be inferred that the harm sustained by the plaintiff was caused by a product defect existing at the time of sale or distribution, without proof of a specific defect, when the incident that harmed the plaintiff:

(a) was of a kind that ordinarily occurs as a result of product defect; and

(b) was not, in the particular case, solely the result of causes other than product defect existing at the time of sale or distribution.

### *Speller v. Sears, Roebuck and Co.*

790 N.E.2d 252 (N.Y. 2003)

Graffeo, J. In this products liability case, defendants — a product manufacturer and retailer — were granted summary judgment dismissing plaintiffs' complaint. Because we conclude that plaintiffs raised a triable issue of fact concerning whether a defective refrigerator caused the fire that resulted in plaintiffs' injuries, we reverse and reinstate the complaint against these defendants.

Plaintiffs' decedent Sandra Speller died in a house fire that also injured her seven-year-old son. It is undisputed that the fire originated in the kitchen. Plaintiffs commenced this action against Sears, Roebuck & Co., Whirlpool Corporation and the property owner alleging negligence, strict products liability and breach of warranty. Relevant to this appeal, plaintiffs asserted that the fire was caused by defective wiring in the refrigerator, a product manufactured by Whirlpool and sold by Sears.

A party injured as a result of a defective product may seek relief against the product manufacturer or others in the distribution chain if the defect was a substantial factor in causing the injury. . . .

In this case, plaintiffs' theory was that the wiring in the upper right quadrant of the refrigerator was faulty, causing an electrical fire which then spread to other areas of the kitchen and residence. Because that part of the refrigerator had been consumed in the fire, plaintiffs noted that it was impossible to examine or test the wiring to determine the precise nature of the defect. Thus, plaintiffs sought to prove their claim circumstantially by establishing that the refrigerator caused the house fire and therefore did not perform as intended. [The defendant's experts claimed that the fire started on the stove, but they conceded "that a fire would not occur in a refrigerator unless the product was defective."]

Of course, if a plaintiff's proof is insufficient with respect to either prong of this circumstantial inquiry, a jury may not infer that the harm was caused by a defective product unless plaintiff offers competent evidence identifying a specific flaw.

Here, in their motion for summary judgment, defendants focused on the second prong of the circumstantial inquiry, offering evidence that the injuries were not caused by their product but by an entirely different instrumentality—a grease fire that began on top of the stove. This was the conclusion of the Fire Marshal who stated during deposition testimony that his opinion was based on his interpretation of the burn patterns in the kitchen, his observation that one of the burner knobs on the stove was in the "on" position, and his conversation with a resident of the home who apparently advised him that the oven was on when the resident placed some food on the stovetop a few hours before the fire.

In order to withstand summary judgment, plaintiffs were required to come forward with competent evidence excluding the stove as the origin of the fire. To meet that burden, plaintiffs offered three expert opinions: the depositions of an electrical engineer and a fire investigator, and the affidavit of a former Deputy Chief of the New York City Fire Department. Each concluded that the fire originated in the refrigerator and not on the stove.

In his extensive deposition testimony, the electrical engineer opined that the fire started in the top-right-rear corner of the refrigerator, an area that housed the air balancing unit, thermostat, moisture control and light control. He stated that the wiring in this part of the appliance had been destroyed in the fire, making it impossible to identify the precise mechanical failure and, thus, he could only speculate as to the specific nature of the defect. He testified that the "most logical probability" was that a bad connection or bad splice to one of the components in that portion of the unit caused the wire to become "red hot" and to ignite the adjacent plastic. He tested the combustibility of the plastic and confirmed that the "plastic lights up very easily, with a single match" and continues to burn like candle wax. The engineer observed that the doors of the refrigerator were "slightly bellied out," indicating they were blown out from the expanding hot gases inside the refrigerator. The wall behind the refrigerator was significantly damaged and the upper right quadrant was burned to such a degree that it was not likely to have been caused by an external fire. Interpreting the burn patterns differently from the Fire Marshal, the electrical engineer found that the cabinets above the stove, although damaged, were not destroyed to the extent he expected to find if there had been a stovetop grease fire.

Plaintiffs' fire investigator similarly opined that the fire originated in the refrigerator's upper right corner, in part basing his conclusion on his observations of the scene three days after the fire and his examination of the appliances. He also interviewed a witness to the fire. He testified that he eliminated the stove as the source of the fire after his examination of that appliance and the cabinets above it. Contrary to the testimony of the Fire Marshal, he observed that all of the burner knobs on the stove were in the same position, either all "off" or all "on." He further examined the burn patterns, noting that if the blaze had been caused by

a grease fire on the stove, the cabinets directly above would have been consumed in the fire. Instead, they were merely damaged. He acknowledged that he did not know exactly how the fire started inside the refrigerator but indicated he suspected there had been a poor connection in the wiring that caused the wire to smolder until it ignited the highly combustible foam insulation inside the unit.

The former Deputy Chief of the New York City Fire Department asserted in his affidavit that the "fire damage to the area around the refrigerator when compared to that of the stove clearly shows the longer and heavier burn at the refrigerator," indicating the fire originated there. He also stated that he had ruled out all other possible origins of the fire.

Upon review of these expert depositions and affidavit, we conclude that plaintiffs raised a triable question of fact by offering competent evidence which, if credited by the jury, was sufficient to rebut defendants' alternative cause evidence. In other words, based on plaintiffs' proof, a reasonable jury could conclude that plaintiffs excluded all other causes of the fire.

We therefore disagree with the Appellate Division's characterization of plaintiffs' submissions as equivocal. Plaintiffs' experts consistently asserted that the fire originated in the upper right quadrant of the refrigerator and each contended the stove was not the source of the blaze. Both parties supported their positions with detailed, non-conclusory expert depositions and other submissions which explained the bases for the opinions.

Defendants contend that after they came forward with evidence suggesting an alternative cause of the fire, plaintiffs were foreclosed from establishing a product defect circumstantially but were then required to produce evidence of a specific defect to survive summary judgment. We reject this approach for two reasons. First, such an analysis would allow a defendant who offered minimally sufficient alternative cause evidence in a products liability case to foreclose a plaintiff from proceeding circumstantially without a jury having determined whether defendant's evidence should be credited. Second, it misinterprets the court's role in adjudicating a motion for summary judgment, which is issue identification, not issue resolution. . . . [P]laintiffs directly rebutted defendants' submissions with competent proof specifically ruling out the stove as the source of the blaze. Because a reasonable jury could credit this proof and find that plaintiff excluded all other causes of the fire not attributable to defendants, this case presents material issues of fact requiring a trial.

[Reversed.]

## NOTES

**1.** ***Proof of Manufacturing Defect.*** What role, if any, did the decedent or her son play in bringing about the fire? Even if the fire started in the refrigerator, did the plaintiffs introduce any evidence of an original defect in the equipment? If so, was it a manufacturing (construction) defect or a design defect? As should be evident, the switch from negligence to strict liability in manufacturing defect cases does not eliminate difficult causal questions that arise when the plaintiff's conduct occupies an uncertain place in the chain of causation, a problem exemplified by long-lived products subject to intensive and protracted use. Indeed many states have adopted statutes of repose that limit the availability of products liability suits to a certain number of years after purchase.

In Jagmin v. Simonds Abrasive Co., 211 N.W.2d 810 (Wis. 1973), the plaintiff was struck in the face by a grinding wheel that broke into pieces while he was operating it. The plaintiff established that the wheel was manufactured by the defendant. He further testified that he had used the wheel in the proper manner, that he had not placed undue stress on it, that

he had no evidence suggesting that any other person had used the wheel while he was away from his job, and that the wheel had several hours of useful life left at the time the accident took place. The wheel itself was destroyed after it broke. The trial court refused to allow the case to go to the jury, ruling that there was insufficient evidence on the question of "defect." The Wisconsin Supreme Court reversed, allowing an "exceedingly close" case to reach the jury on a modified version of res ipsa loquitur. The plaintiff's evidence tended to exclude the possibility of any responsible cause of the injury apart from an original product defect, even if that defect could not be identified. Does the plaintiff's evidence negate the possibility that the wheel was damaged in shipment or in installation? Does the plaintiff's evidence explain why the wheel worked as long as it did? Does Henderson's account of the *MacPherson* facts, *supra* at 52, argue in favor of requiring a specific identification of a product defect in manufacturing cases? Do modern discovery rules mitigate any information disparities between the consumer and the product manufacturer?

In a modern twist on *Speller*, the plaintiff in Red Hed Oil, Inc. v. H.T. Hackney Co., 292 F. Supp. 3d 764, 775, 778 (E.D. Ky. 2017), sued the distributor and manufacturers of e-cigarettes that allegedly caught fire and caused extensive damage to the plaintiff's convenience store. The plaintiff's manufacturing and design defect claims failed on similar causation issues as those originally raised in *Speller*. According to Hood, J.:

> Plaintiffs fail to provide factual allegations that these e-cigarettes did, in fact, cause this fire. Plaintiffs blame it on a defect, but they do not specify what defect, which product was defective, or how the defect sparked the fire. . . .
>
> The plaintiffs do not allege an alternative design, how the products deviated from the intended design, how the e-cigarettes were assembled wrong, or how the e-cigarettes fail the risk-utility test. Plaintiffs cannot rely on general assertions that the e-cigarettes were dangerous; they must make at least some factual allegations as to *how*.

**2. *Manufacturing Defects in Food Cases.*** In *Escola*, food cases were one of the original battlegrounds for a theory of strict liability. In particular, the early common law held manufacturers strictly liable for any "foreign object" that was found within the food, be it a sliver of tin or some waste impurities from animals. By the same token, the earlier cases refused to hold manufacturers liable under any theory for substances "natural" to the product served. Thus the leading case of Mix v. Ingersoll Candy Co., 59 P.2d 144, 148 (Cal. 1936), held that "[b]ones which are natural to the type of meat served cannot legitimately be called a foreign substance, and a consumer who eats meat dishes ought to anticipate and be on his guard against the presence of such bones."

Modern cases have uniformly rejected this approach in favor of a reasonable expectations test. In Schafer v. JLC Food Systems, 695 N.W.2d 570, 575 (Minn. 2005), the plaintiff took a bite from a pumpkin muffin served at the defendant's restaurant only to experience a sharp pain in her throat, which later turned into a serious infection. Page, J., wrote:

> Under the [Third] Restatement approach, consumer expectations are based on culturally defined, widely shared standards allowing a seller's liability to be resolved by judges and triers of fact based on their assessment of what consumers have a right to expect from preparation of the food in question. §7 cmt. b. . . .
>
> Instead of drawing arbitrary distinctions between foreign and natural substances that caused harm, relying on consumers' reasonable expectations is likely to yield a more equitable result. After all, an unexpected natural object or substance contained in a food product, such as a chicken bone in chicken soup, can cause as much harm as a foreign object or substance, such as a piece of glass in the same soup.

Page, J., next allowed the plaintiff to get to the jury even though she could not "present evidence identifying the object that caused the alleged harm," relying again on the strict

liability analog to res ipsa loquitur, whereby, as in *Jagmin*, the plaintiff's task is to exclude all other causes of harm. Should this test be adopted in cases of food poisoning that manifest themselves a day after eating in the restaurant?

Berkheimer v. REKM, LLC, 206 N.E.3d 90, 94 (Ohio Ct. App. 2023), aff'd __ N.E.3d __, 2024 WL 352817 (Ohio July 25, 2024), denied recovery to a plaintiff who could have reasonably expected to find a bone in a "boneless chicken wing." Hendrickson, J., reasoned that "reasonable expectations" depend on whether a part is a natural to the food at issue. Is this a return to the foreign-natural test by another name?

## 2. Design Defects

### *Campo v. Scofield*

95 N.E.2d 802 (N.Y. 1950)

Fuld, J. Plaintiff, working on his son's farm, was engaged in feeding onions into an "onion topping" machine, when his hands became caught in its revolving steel rollers and were badly injured. . . .

If a manufacturer does everything necessary to make the machine function properly for the purpose for which it is designed, if the machine is without any latent defect, and if its functioning creates no danger or peril that is not known to the user, then the manufacturer has satisfied the law's demands. We have not yet reached the state where a manufacturer is under the duty of making a machine accident proof or foolproof. Just as the manufacturer is under no obligation, in order to guard against injury resulting from deterioration, to furnish a machine that will not wear out, so he is under no duty to guard against injury from a patent peril or from a source manifestly dangerous.

To illustrate, the manufacturer who makes, properly and free of defects, an axe or a buzz saw or an airplane with an exposed propeller, is not to be held liable if one using the axe or the buzz saw is cut by it, or if some one working around the airplane comes in contact with the propeller. In such cases, the manufacturer has the right to expect that such persons will do everything necessary to avoid such contact, for the very nature of the article gives notice and warning of the consequences to be expected, of the injuries to be suffered.

### *2 Harper and James, Torts §28.5*

(1956)

The bottom does not logically drop out of a negligence case against the maker when it is shown that the purchaser knew of the dangerous condition. Thus if the product is a carrot-topping machine with exposed moving parts, or an electric clothes wringer dangerous to the limbs of the operator, and if it would be feasible for the maker of the product to install a guard or safety release, it should be a question for the jury whether reasonable care demanded such a precaution, though its absence is obvious. Surely reasonable men might find here a great danger, even to one who knew the condition and since it was so readily avoidable they might find the maker negligent.

**John W. Wade**

## *On the Nature of Strict Tort Liability for Products*

44 Miss. L.J. 825, 836–37 (1973)

If there is agreement that the determination of whether a product is unreasonably dangerous, or is not duly safe, involves the necessary application of a standard, it will, like the determination of negligence or of strict liability for an abnormally dangerous activity, require the consideration and weighing of a number of factors. I offer here a revised list of factors which seem to me to be of significance in applying the standard.

(1) The usefulness and desirability of the product — its utility to the user and to the public as a whole.
(2) The safety aspects of the product — the likelihood that it will cause injury, and the probable seriousness of the injury.
(3) The availability of a substitute product which would meet the same need and not be as unsafe.
(4) The manufacturer's ability to eliminate the unsafe character of the product without impairing its usefulness or making it too expensive to maintain its utility.
(5) The user's ability to avoid danger by the exercise of care in the use of the product.
(6) The user's anticipated awareness of the dangers inherent in the product and their availability, because of general public knowledge of the obvious condition of the product, or of the existence of suitable warnings or instructions.
(7) The feasibility, on the part of the manufacturer, of spreading the loss by setting the price of the product or carrying liability insurance.

## NOTE

***Two (or Is It Three?) Views of Design Defect.*** The passages quoted above set up the possible approaches to design defect litigation. The open and obvious test of *Campo* dominated the law until the adoption of the Second Restatement, in which a design defect was determined by the consumer expectations test. RST §402A, cmts. *g* & *i*. Contrary to *Campo*, Professors Harper and James insisted that a negligence cause of action was not necessarily defeated by the obvious nature of the defect. Professor Wade's influential formulation of the risk-utility standard offers a strict liability version of the relevant cost-benefit analysis. The Third Restatement requires a modified risk-utility test, in which the plaintiff is charged with showing that a "reasonable alternative design" exists that would make the product less dangerous. Judicial embrace of these different versions of design defect liability have ebbed and flowed over the past sixty years. The next case deals with the rise of the negligence standard in design defect cases dealing with the crashworthiness of automobiles.

### *a. Development of the Negligence Test*

## *Volkswagen of America, Inc. v. Young*

321 A.2d 737 (Md. 1974)

[The decedent had stopped his 1968 Volkswagen Beetle at a red light when he was hit from behind by a 1967 Ford, negligently driven by William Benson. As a result, the decedent's

car was pushed forward. The seat bracketing pieces and seat adjustment mechanisms broke away from the body of the car. In the ensuing "second collision" the decedent was hurled into the rear of the car and was killed by head and torso injuries sustained on impact. The plaintiff sued Volkswagen in federal district court. She alleged that the Beetle was "defectively designed, manufactured, and marketed with defects which rendered it structurally hazardous, not merchantable, and not fit for the purpose intended" in that its entire seat assembly was "unreasonably vulnerable to separation from the floor upon collision." The district court certified this question to the Maryland Court of Appeals, the highest state court:

> Whether or not, under Maryland law, the definition of the "intended use" of a motor vehicle includes the vehicle's involvement in a collision; and thus in turn, whether a cause of action is stated against the manufacturer or importer of said vehicle in breach of warranty or negligence or absolute liability or misrepresentation by allegations that the design and manufacture of the vehicle unreasonably increased the risk of injury to occupants following a collision not caused by any defect of the vehicle.

The Maryland court answers the question in the affirmative, holding that the "intended use" of an automobile was not only to provide transportation but also reasonably safe transportation, and that the plaintiff's complaint stated a cause of action in negligence under Maryland law.]

Eldridge, J. . . . This is the first case to reach this Court concerning the extent of an automobile manufacturer's liability for a design defect resulting in enhanced injuries in a motor vehicle accident, where the defect did not cause the initial impact or movement of the injured person. Such cases are often called "second collision" cases or "automobile crashworthiness" cases. They differ from other products liability cases involving defective automobiles by the combination of two factors. First, the alleged defect is in the design of the automobile rather than a negligent deviation during the construction or assembly process from the manner in which the vehicle was supposed to be made. The latter is usually called a "construction defect." Second, the defect is not the cause of the initial impact. Typically, the actions of the driver of the car in which the plaintiff is riding, or the actions of the driver of another vehicle, or the actions of some third person, cause an initial disruption or impact which in turn results in the plaintiff's colliding with the interior (or occasionally the exterior) of the car. The plaintiff's collision with the car is the so-called "second collision." The issue of whether the automobile manufacturer has a duty to take reasonable steps to design its vehicles so as to minimize the injuries caused by "second collisions" has engendered much controversy and comment throughout the nation.

**A 1968 Volkswagen Beetle Type 1, the model of the decedent's car in *Young***

*Source: Phil Talbot / Alamy*

The principal case holding that an automobile manufacturer has no duty to design its cars so as to minimize the injuries suffered in automobile accidents is Evans v. General Motors Corporation, 359 F.2d 822 (7th Cir. 1966). The plaintiff in *Evans* was killed when his 1961 Chevrolet station wagon was struck broadside by

another car. He claimed that General Motors was negligent in designing the frame of his car, inasmuch as an "X" type frame rather than a box or perimeter type frame was used, contrary to the construction of some other cars. The claim was that an "X" type frame without side rails would not adequately protect occupants during a side impact collision, and that the defendant manufacturer had created an unreasonable risk of serious injury. The trial court, applying Indiana law, dismissed the complaint for failure to state a claim on which relief could be granted, and the dismissal was affirmed by the United States Court of Appeals for the Seventh Circuit. The Court of Appeals held that the critical question was the nature of the manufacturer's duty. It went on to conclude that a manufacturer has a duty only to design a car reasonably fit for its intended purpose, and that "[t]he intended purpose of an automobile does not include its participation in collisions with other objects, despite the manufacturer's ability to foresee the possibility that such collisions may occur. As defendant argues, the defendant also knows that its automobiles may be driven into bodies of water, but it is not suggested that defendant has a duty to equip them with pontoons." (*Id*. at 825.)

The Court of Appeals for the Seventh Circuit also stated as grounds for its decision that a "manufacturer is not under a duty to make his automobile accident-proof or fool-proof" and that requiring "manufacturers to construct automobiles in which it would be safe to collide . . . [is] a legislative function. . . ."

The seminal case on the other side of the issue is Larsen v. General Motors Corporation, 391 F.2d 495 (8th Cir. 1968). The plaintiff in *Larsen* suffered severe bodily injuries while driving a 1963 Corvair which collided head-on with another car. The impact caused the steering mechanism to thrust forward into the plaintiff's head. The suit against General Motors charged negligence in the design of the steering assembly and the placement of the component parts of the steering assembly into the structure of the car. It was alleged that General Motors was also negligent in not warning the user of this latent condition. The specific defect relied upon by the plaintiff was that the solid steering shaft was so designed as to extend "without interruption from a point 2.7 inches in front of the leading surface of the front tires to a position directly in front of the driver," exposing him "to an unreasonable risk of injury from the rearward displacement of that shaft in the event of a left-of-center head-on collision. So positioned it receives the initial impact of forces generated by a left-of-center head-on collision. The unabsorbed forces of the collision in this area are transmitted directly toward the driver's head, the shaft acting as a spear aimed at a vital part of the driver's anatomy." *Id.* at 497, n.2. The plaintiff also pointed out that other cars were designed so as to protect against such rearward displacement, in that the steering column did not protrude beyond the forward surface of the front tires. The lower court in *Larsen* granted General Motors' motion for summary judgment on the theory that the manufacturer had no duty to design a vehicle which would protect the plaintiff from injury in a collision. On appeal, the United States Court of Appeals for the Eighth Circuit reversed, holding that the plaintiff had made out a sufficient case for consideration by the jury.

[The court in *Larsen* gave a broad interpretation to "intended use," stating:]

> Automobiles are made for use on the roads and highways in transporting persons and cargo to and from various points. This intended use cannot be carried out without encountering in varying degrees the statistically proved hazard of injury-producing impacts of various types. The manufacturer should not be heard to say that it does not intend its product to be involved in any accident when it can easily foresee and when it knows that the probability over the life of its product is high, that it will be involved in some type of injury-producing accident. . . .

The Court of Appeals concluded that an automobile manufacturer "is under a duty to use reasonable care in the design of its vehicle to avoid subjecting the user to an unreasonable risk of injury in the event of a collision." (*Id.* at 502.)

The *Larsen* court then emphasized the limitations of its holding that it was not making automobile manufacturers "insurers"; that it was merely applying common law principles of negligence; that the standard for manufacturers was "reasonable care"; and that an automobile did not have to be absolutely crash-proof but only designed to provide "a reasonably safe vehicle in which to travel." (*Id.* at 503.)*

In our view, Larsen v. General Motors Corporation, *supra*, and the cases following it, are more in accord with traditional negligence principles than Evans v. General Motors Corporation, *supra*. . . .

That the design defect does not cause the initial collision should make no difference if it is a cause of the ultimate injury. Where the injuries to an occupant of a motor vehicle resulted from both the negligence of a driver as well as a negligent condition created by some other entity, this Court has held that both negligent actors may be liable. . . .

In sum, "traditional rules of negligence" lead to the conclusion that an automobile manufacturer is liable for a defect in design which the manufacturer could have reasonably foreseen would cause or enhance injuries on impact, which is not patent or obvious to the user, and which in fact leads to or enhances the injuries in an automobile collision. . . .

While the intended purpose of an automobile may not be to participate in collisions, the intended purpose includes providing a reasonable measure of safety when, inevitably, collisions do occur. For many years automobiles have been equipped with safety glass, bumpers, windshield wipers, etc. More recently, and largely as a result of governmental action, automobiles are equipped with additional safety devices such as seat belts, shoulder harnesses, padded dashboards, padded visors, non-protruding knobs, etc. Frequent collisions are foreseeable, and the intended purpose of all of these parts of the vehicle is to afford reasonable safety when those collisions occur.

The arguments that there is no duty to design "accident-proof" or "injury-proof" vehicles, and that automobile manufacturers are not insurers, are "straw men." No case has ever held that an automobile manufacturer must design an "accident-proof" or "injury-proof" vehicle or that the manufacturer is an insurer. Concerning two of the examples most often used by the advocates of non-liability for design defects, no one has suggested that an automobile must be designed to withstand a high speed head-on collision with a truck or to float if it leaves the road and goes into a body of water. . . .

The standard to be applied is the traditional one of reasonableness.

The contention that the design of automobiles involves a legislative function and not a judicial function, similarly furnishes no sound reason for exempting automobile "second collision" cases from the normal principles of tort liability. Legislative or administrative requirements that persons or businesses conduct their operations in a particular manner, and adhere to specified standards, have never been viewed as supplanting tort liability. On the contrary, such statutory or regulatory requirements are deemed to furnish standards by which courts or juries determine, along with other circumstances, whether or not conduct is negligent. Failure to adhere to those standards is evidence of negligence for the court or jury to consider. Moreover, the most significant legislation dealing with motor vehicle safety standards makes it clear that Congress did not view the question of safe motor vehicle design as solely a legislative problem. The National Traffic and Motor Vehicle Safety Act of 1966 specifically provided that "Compliance with any Federal motor vehicle safety standard issued under this subchapter does not exempt any person from any liability under common law." 15 U.S.C. 1397(c). . . .

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* [The defendant in *Larsen* received a unanimous verdict after a three-week trial, having introduced scientific evidence that the plaintiff had not been hit by the steering column. For a discussion of the expert evidence introduced at trial, see Bowman, Defense of an Auto Design Negligence Case, 10 For the Defense, No. 5, May 1969.—Eds.]

In addition, there can be no recovery if the danger inherent in the particular design was obvious or patent to the user of the vehicle. . . .

[The court then refuses to apply the strict liability theory of section 402A to design defect cases.] Consequently, the tort liability under Maryland law of a manufacturer or supplier of a motor vehicle, for a defective design which enhances injuries in a collision, depends upon traditional principles of negligence.

## NOTES

**1.** ***Determining Standards for Design Defects.*** As *Young* indicates, design defect liability grew up under the aegis of negligence. As such, can the court accept the negligence doctrine and allow a complete defense for any dangers that were "obvious or patent" to the user of the vehicle? Could a jury regard a Volkswagen van, with its engine in the rear, as defective? A convertible? A cigarette lighter? For a negative answer on the first query, see Dreisonstok v. Volkswagenwerk A.G., 489 F.2d 1066 (4th Cir. 1974); for a negative answer on the second, see Delvaux v. Ford Motor Co., 764 F.2d 469 (7th Cir. 1985); and for a negative answer on the third, see Todd v. Societe Bic, S.A., 21 F.3d 1402, 1407 (7th Cir. 1994). When the defects are obvious, how should the cost-benefit analysis be conducted?

Conversely, how would *Young* play out under section 402A of the Second Restatement? Note that traditional strict liability works well to protect strangers against a defendant's use of force, as with abnormally dangerous activities, but it seems inappropriate to require any defendant to protect the plaintiff against any use (or misuse) of force initiated by either the plaintiff, a third party, or an act of God. A motorcycle gasoline tank might be made "totally" safe against impact, but its weight and unwieldiness would make the motorcycle unmovable. Once absolute protection is rejected as unworkable, reasonableness standards take over. In some instances, standards are set by legislation. See, e.g., The National Traffic and Motor Vehicle Safety Act, 49 U.S.C. §§30101–30170, wherein, for example, 49 C.F.R. §571.216 (2024) ("Roof Crush Resistance") provides that a force equal to 1.5 times a car's unloaded weight, or 22,240 newtons (5,000 pounds), whichever is less, should not move the roof more than 127 millimeters (five inches) when applied to either of its front corners. Because statutory compliance does not provide an absolute defense in a design defect case, courts typically turn to cost-benefit tests to determine the applicable design standard. But how? For an early skeptical response, see James A. Henderson, Jr., Judicial Review of Manufacturers' Conscious Design Choices: The Limits of Adjudication, 73 Colum. L. Rev. 1531, 1540 (1973), stressing the "polycentric nature" of design decisions, which requires a design engineer to find the proper balance of "such factors as market price, functional utility, and aesthetics, as well as safety." Henderson insisted these matters could not be adequately reexamined in litigation because courts are not "institutionally suited to establishing safety standards." For the early impetus on liability for design defects, see Ralph Nader & Joseph A. Page, Automobile Design and Judicial Process, 55 Calif. L. Rev. 645 (1967).

**2.** ***Enhancement of Injury.*** The defendant in a crashworthiness case is not responsible for the unavoidable injuries associated with the original impact, but only for those harms that were "enhanced or aggravated" by the defective design. In light of the implicit division on causation, who bears the burden of proof on the issue of enhancement? One view is that the plaintiff must prove that "it is more probable than not that the alleged defect aggravated or enhanced the injuries resulting from the initial collision." See Caiazzo v. Volkswagenwerk

A.G., 647 F.2d 241, 251 (2d Cir. 1981). *Caiazzo* was promptly rejected in Mitchell v. Volkswagenwerk A.G., 669 F.2d 1199, 1204–05 (8th Cir. 1982):

> The primary difficulty we have with this analysis is that it forces not only the parties but the jury as well to try a hypothetical case. Liability and damage questions are difficult enough within orthodox principles of tort law without extending consideration to a case of a hypothetical victim. More realistically, the parties and juries should direct their attentions to what actually happened rather than what might have happened.
>
> By placing the burden of proof on a plaintiff to prove that the designer was the sole cause of not only an enhanced indivisible injury, but, in addition, that he would not otherwise have received injuries absent a defect, the injured victim is relegated to an almost hopeless state of never being able to succeed against a defective designer. The public interest is little served. We write to reaffirm that *Larsen* was not intended to create a rule which requires the plaintiff to assume an impossible burden of proving a negative fact.

Is the defendant ever the sole responsible party in any crashworthiness case? How can a jury avoid trying a "hypothetical case" once the defendant introduces evidence that the alleged defect did not cause all or some of the harms? Does the burden of production ever switch back to the plaintiff? Whatever the force of these objections, the Third Restatement takes the same view. Even though the theory of proximate causation holds the defendant liable only for the "increased harm," the full loss falls on the defendant "[i]f proof does not support a determination . . . of the harm that would have resulted in the absence of the product defect." RTT: PL §16(c).

Egbert v. Nissan Motor Co., Ltd., 228 P.3d 737, 746 (Utah 2010), rejected the Restatement view and both *Mitchell* and *Caiazzo* by taking its cue from Utah Code Ann. §78B-5-818(3) (West 2024), which provides: "No defendant is liable to any person seeking recovery for any amount in excess of the proportion of fault attributed to that defendant. . . ." Durham, C.J., concluded that fault, broadly defined under the statute, should always be apportioned between two parties when the jury has "sufficient" evidence of the culpability of each.

> [B]ecause all injuries, as a matter of Utah law, can and must be apportioned, there is no shifting of burden — informal or formal — to a defendant product seller to prove apportionment. The plaintiff bears the burden of proof in an enhanced-injury case. Finally, because of the nature of an enhanced-injury claim and the abolition of joint and several liability, a defendant product seller cannot become liable for the entire injury merely by virtue of being a codefendant.

**3.** ***Crashworthiness Cases: Acceptance, Disquiet, and Reform?*** The crashworthiness doctrine of *Larsen* and *Young* is today the law in every state and explicitly embraced in the Third Restatement. See RTT: PL §16, cmt. *a*. But some courts have expressed misgivings about its potential scope. In Dawson v. Chrysler Corp., 630 F.2d 950, 962–63 (3d Cir. 1980), the plaintiff, a police officer, was hurrying to answer a burglar alarm when his Dodge Monaco patrol car slipped off a rain-soaked highway into an "unyielding" steel pole some fifteen inches in diameter. The pole ripped through the side of the car, crushed the plaintiff, and left him a quadriplegic. The plaintiff argued the car was defective because it did not have "a full continuous steel frame extending through the door panels," which would have kept the pole from penetrating the passenger space. The defendant's expert testified that the plaintiff's proposed changes would have added between 200 and 250 pounds of weight to the car and cost some $300 ($1,213 in 2024 dollars). He also noted that "deformation" of a car in a crash is in general desirable because it absorbs the impact that would otherwise be transmitted to the occupant. Adams, J., uneasily affirmed the plaintiff's jury verdict under New Jersey law:

> The result of such arrangement is that while the jury found Chrysler liable for not producing a rigid enough vehicular frame, a factfinder in another case might well hold the manufacturer

liable for producing a frame that is too rigid. Yet, as pointed out at trial, in certain types of accidents — head-on collisions — it is desirable to have a car designed to collapse upon impact because the deformation would absorb much of the shock of the collision, and divert the force of deceleration away from the vehicle's passengers. In effect, this permits individual juries applying varying laws in different jurisdictions to set nationwide automobile safety standards and to impose on automobile manufacturers conflicting requirements. It would be difficult for members of the industry to alter their design and production behavior in response to jury verdicts in such cases, because their response might well be at variance with what some other jury decides is a defective design. Under these circumstances, the law imposes on the industry the responsibility of insuring vast numbers of persons involved in automobile accidents.

The level of cynicism about this "damned-if-you-do-damned-if-you-don't" problem surfaced in Blankenship v. General Motors Corp., 406 S.E.2d 781, 783–84 (W. Va. 1991). Neely, J., joined the crashworthiness parade for reasons that had little to do with the intrinsic merits of the doctrine:

West Virginia is a small rural state with .66 percent of the population of the United States. Although some members of this court have reservations about the wisdom of many aspects of the tort law, as a court we are utterly powerless to make the *overall* tort system for cases arising in interstate commerce more rational: Nothing that we do will have any impact whatsoever on the set of economic trade-offs that occur in the *national* economy. And, ironically, trying unilaterally to make the American tort system more rational through being uniquely responsible in West Virginia will only punish our residents severely without, in any regard, improving the system for anyone else.

So long as West Virginians have to pay premiums on General Motors cars sold around the world, it would be "foolish and irresponsible," according to Neely, J., not to allow West Virginians to collect on their implicit insurance policies for accidents to them.

**4. *The Decline of Open and Obvious.*** Automobiles were not the only product for which liability expanded dramatically in the 1970s. The design liability for machine tools and other equipment exploded as well. *Campo* was explicitly overruled in Micallef v. Miehle Co., 348 N.E.2d 571, 577–78 (N.Y. 1976). There the plaintiff sought to "chase a hickie" (that is, remove a foreign object) that had made its way onto a high-speed printing press manufactured by the defendant. Without shutting down the press (which would have cost valuable production time), he tried to remove the hickie with an eight-inch piece of plastic, and his finger got caught in the nip-point of the machine. The plaintiff tried to turn off the press, but the shut-off button was beyond his reach. Cooke, J., rejected the open and obvious rule in *Campo*:

Apace with advanced technology, a relaxation of the *Campo* stringency is advisable. A casting of increased responsibility upon the manufacturer, who stands in a superior position to recognize and cure defects, for improper conduct in the placement of finished products into the channels of commerce furthers the public interest. To this end, we hold that a manufacturer is obligated to exercise that degree of care in his plan or design so as to avoid any unreasonable risk of harm to anyone who is likely to be exposed to the danger when the product is used in the manner for which the product was intended as well as an unintended yet reasonably foreseeable use.

What constitutes "reasonable care" will, of course, vary with the surrounding circumstances and will involve "a balancing of the likelihood of harm, and the gravity of harm if it happens, against the burden of the precaution which would be effective to avoid the harm." Under this approach, "the plaintiff endeavors to show the jury such facts as that competitors used the safety device which was missing here, or that a 'cotter pin costing a penny' could have prevented the accident. The defendant points to such matters as cost, function, and competition as narrowing the design choices. He stresses 'trade-offs.' If the product would be unworkable when the alleged missing feature was added, or would be so expensive as to be priced out of the market, that would be relevant defensive matter." (Rheingold, Expanding Liability of the Product Supplier: A Primer, 2 Hofstra L. Rev. 521, 537.)

The Third Restatement endorses *Micallef*. See RTT: PL §2, illus. 3. This now dominant position is articulated in section 2, comment *d*: "The fact that a danger is open and obvious is relevant to the issue of defectiveness, but does not necessarily preclude a plaintiff from establishing that a reasonable alternative design should have been adopted that would have reduced or prevented injury to the plaintiff." States have generally followed suit in adopting "open and obvious" as a factor in determining defectiveness under a risk-utility or reasonable alternative design standard, rather than as a standalone defense. Thus in Genie Indus., Inc. v. Matak, 462 S.W.3d 1, 17 (Tex. 2015), Boyd, J., explained:

> We have rejected such absolute rules [of open and obvious] in favor of the more fluid risk-utility analysis because that analysis provides a more effective way to encourage manufacturers to reach an optimum level of safety in designing their products. A design that eliminates a risk is safer than a design that retains the risk, even if the risk is open and obvious or warned against.

But there are nevertheless some limits to liability. In Linegar v. Armour of America, Inc., 909 F.2d 1150, 1154 (8th Cir. 1990), the decedent, a highway trooper, wore a standard-issue Armour bulletproof vest that, as he knew, did not wrap around his torso. He was killed in a routine traffic stop. His vest stopped all bullets that hit it but did not prevent a bullet from entering his body near his armpit and penetrating his heart. More extensive vests were available, but these were both uncomfortable to wear and somewhat less maneuverable. After citing RST §402A, comment *i*, Bowman, J., held that "[a]n otherwise completely effective protective vest cannot be regarded as dangerous, much less unreasonably so, simply because it leaves some parts of the body obviously exposed." The Third Restatement endorses *Linegar*. See RTT: PL §2, illus. 10.

### *b. Consumer Expectations versus Risk-Utility Tests*

## *Barker v. Lull Engineering Co.*

573 P.2d 443 (Cal. 1978)

Tobriner, C.J. In August 1970, plaintiff Ray Barker was injured at a construction site at the University of California at Santa Cruz while operating a high-lift loader manufactured by defendant Lull Engineering Co. and leased to plaintiff's employer by defendant George M. Philpott Co., Inc. Claiming that his injuries were proximately caused, inter alia, by the alleged defective design of the loader, Barker instituted the present tort action seeking to recover damages for his injuries. The jury returned a verdict in favor of defendants, and plaintiff appeals from the judgment entered upon that verdict, contending primarily that in view of this court's decision in Cronin v. J. B. E. Olson Corp. 501 P.2d 1153 (Cal. 1972), the trial court erred in instructing the jury "that strict liability for a defect in design of a product is based on a finding that the product was unreasonably dangerous for its intended use. . . ."

As we explain, we agree with plaintiff's objection to the challenged instruction and conclude that the judgment must be reversed. . . .

[W]e have concluded from this review that a product is defective in design either (1) if the product has failed to perform as safely as an ordinary consumer would expect when used in an intended or reasonably foreseeable manner, or (2) if, in light of the relevant factors discussed below, the benefits of the challenged design do not outweigh the risk of danger inherent in such design. In addition, we explain how the burden of proof with respect to the latter "risk-benefit" standard should be allocated.

This dual standard for design defect assures an injured plaintiff protection from products that either fall below ordinary consumer expectations as to safety, or that, on balance, are not

as safely designed as they should be. At the same time, the standard permits a manufacturer who has marketed a product which satisfies ordinary consumer expectations to demonstrate the relative complexity of design decisions and the tradeoffs that are frequently required in the adoption of alternative designs. Finally, this test reflects our continued adherence to the principle that, in a product liability action, the trier of fact must focus on the *product*, not on the *manufacturer's conduct*, and that the plaintiff need not prove that the manufacturer acted unreasonably or negligently in order to prevail in such an action. . . .

### 1. The Facts of the Present Case

[Barker, a substitute driver, was injured while using a Lull High-Lift Loader, which was designed to be kept level on a sloping terrain. He had received only limited instruction in the use of the loader. While attempting to lift a load of lumber about 18 feet on uneven ground, he tried to maneuver the forks on the base of the load to compensate for sloping ground. As he lost control of the loader, he attempted to jump away from it and was struck and seriously injured by some falling timber.

Barker claimed that the loader was defective in several respects: first, that it was not equipped with seat belts or a roll-bar; second, that it was not equipped with "outriggers" that might have given it greater lateral stability; third, that it was not equipped with an automatic locking device on its leveling mechanism; and, fourth, that it was not equipped with a separate park gear. In response to this assignment of defects, the defendant argued as follows: first, that seat belts or roll-bars were in fact dangerous because they prevented any quick escape from the loader; second, that the outriggers were not needed if the loader was operated on level terrain as was intended, that none of the defendant's competitors had such outriggers, and that a regular crane should have been called in if work on uneven terrain was required; third, that the leveling device used was the most convenient and safe for the operator; and, fourth, that none of the transmissions manufactured for loaders incorporated a park position. The defendant also argued that the plaintiff's inexperience and panic were the sole source of his injury.

The jury returned a verdict for the defendant by a vote of ten to two.] . . .

### 3. A Trial Court May Properly Formulate Instructions to Elucidate the "Defect" Concept in Varying Circumstances. In Particular, in Design Defect Cases, a Court May Properly Instruct a Jury That a Product Is Defective in Design if (1) the Plaintiff Proves That the Product Failed to Perform as Safely as an Ordinary Consumer Would Expect When Used in an Intended or Reasonably Foreseeable Manner, or (2) the Plaintiff Proves That the Product's Design Proximately Caused Injury and the Defendant Fails to Prove, in Light of the Relevant Factors, That on Balance the Benefits of the Challenged Design Outweigh the Risk of Danger Inherent in Such Design. . . .

As this court has recognized on numerous occasions, the term defect as utilized in the strict liability context is neither self-defining nor susceptible to a single definition applicable in all contexts.[8] . . . [T]he concept of defect raises considerably more difficulties in the design defect context than it does in the manufacturing or production defect context.

8. One commentator has observed that, in addition to the deficiencies in the "unreasonably dangerous" terminology noted in *Cronin*, the Restatement's language is potentially misleading because "[i]t may suggest an idea like ultrahazardous, or abnormally dangerous, and thus give rise to the impression that the plaintiff must prove that the product was unusually or extremely dangerous." (Wade, On the Nature of Strict Tort Liability for Products, 44 Miss. L.J. 825, 832 (1973).) We agree with this criticism and believe it constitutes a further reason for refraining from utilizing the "unreasonably dangerous" terminology in defining a defective product.

In general, a manufacturing or production defect is readily identifiable because a defective product is one that differs from the manufacturer's intended result or from other ostensibly identical units of the same product line. For example, when a product comes off the assembly line in a substandard condition it has incurred a manufacturing defect. . . . A design defect, by contrast, cannot be identified simply by comparing the injury-producing product with the manufacturer's plans or with other units of the same product line, since by definition the plans and all such units will reflect the same design. Rather than applying any sort of deviation-from-the-norm test in determining whether a product is defective in design for strict liability purposes, our cases have employed two alternative criteria in ascertaining, in Justice Traynor's words, whether there is something "wrong, if not in the manufacturer's manner of production, at least in his product." (Traynor, The Ways and Meanings of Defective Products and Strict Liability, 32 Tenn. L. Rev. 363, 366 [1965].)

First, our cases establish that a product may be found defective in design if the plaintiff demonstrates that the product failed to perform as safely as an ordinary consumer would expect when used in an intended or reasonably foreseeable manner. This initial standard, somewhat analogous to the Uniform Commercial Code's warranty of fitness and merchantability (Cal. U. Com. Code, §2314), reflects the warranty heritage upon which California product liability doctrine in part rests. As we noted in *Greenman*, "implicit in [a product's] presence on the market . . . [is] a representation that it [will] safely do the jobs for which it was built." When a product fails to satisfy such ordinary consumer expectations as to safety in its intended or reasonably foreseeable operation, a manufacturer is strictly liable for resulting injuries. . . .

As Professor Wade has pointed out, however, the expectations of the ordinary consumer cannot be viewed as the exclusive yardstick for evaluating design defectiveness because "[i]n many situations . . . the consumer would not know what to expect, because he would have no idea how safe the product could be made." . . . Numerous California decisions have implicitly recognized this fact and have made clear, through varying linguistic formulations, that a product may be found defective in design, even if it satisfies ordinary consumer expectations, if through hindsight the jury determines that the product's design embodies "excessive preventable danger," or, in other words, if the jury finds that the risk of danger inherent in the challenged design outweighs the benefits of such design. . . .

A review of past cases indicates that in evaluating the adequacy of a product's design pursuant to this latter standard, a jury may consider, among other relevant factors, the gravity of the danger posed by the challenged design, the likelihood that such danger would occur, the mechanical feasibility of a safer alternative design, the financial cost of an improved design, and the adverse consequences to the product and to the consumer that would result from an alternative design. . . .

Although our cases have thus recognized a variety of considerations that may be relevant to the determination of the adequacy of a product's design, past authorities have generally not devoted much attention to the appropriate allocation of the burden of proof with respect to these matters. . . . The allocation of such burden is particularly significant in this context in as much as this court's product liability decisions, from *Greenman* to *Cronin*, have repeatedly emphasized that one of the principal purposes behind the strict product liability doctrine is to relieve an injured plaintiff of many of the onerous evidentiary burdens inherent in a negligence cause of action. Because most of the evidentiary matters which may be relevant to the determination of the adequacy of a product's design under the "risk-benefit" standard—e.g., the feasibility and cost of alternative designs—are similar to issues typically presented in a negligent design case and involve technical matters peculiarly within the knowledge of the manufacturer, we conclude that once the plaintiff makes a prima facie showing that the injury was proximately caused by the product's design, the burden should appropriately shift to the

defendant to prove, in light of the relevant factors, that the product is not defective. Moreover, inasmuch as this conclusion flows from our determination that the fundamental public policies embraced in *Greenman* dictate that a manufacturer who seeks to escape liability for an injury proximately caused by its product's design on a risk-benefit theory should bear the burden of persuading the trier of fact that its product should not be judged defective, the defendant's burden is one affecting the burden of proof, rather than simply the burden of producing evidence. . . .

Because the jury may have interpreted the erroneous instruction given in the instant case as requiring plaintiff to prove that the high-lift loader was ultrahazardous or more dangerous than the average consumer contemplated, and because the instruction additionally misinformed the jury that the defectiveness of the product must be evaluated in light of the product's "intended use" rather than its "reasonably foreseeable use" . . . , we cannot find that the error was harmless on the facts of this case. In light of this conclusion, we need not address plaintiff's additional claims of error, for such issues may not arise on retrial.

The judgment in favor of defendants is reversed.

## NOTES

**1.** ***What Is a Design Defect?*** Some jurisdictions today follow *Barker* and allow either the consumer expectations test or the risk-utility test to prove a design defect. Other jurisdictions adopt just one of the two tests. In Aubin v. Union Carbide Corp., 177 So. 3d 489, 510 (Fla. 2015), the plaintiff alleged he developed mesothelioma from exposure to asbestos contained in defendant's construction products. The jury found in favor of the plaintiff, but the intermediate appellate court reversed on the ground that the trial court failed to instruct the jury using the Third Restatement's reasonable alternative design test for design defect claims. Pariente, J., in turn reversed the intermediate court. In so doing he rejected the Third Restatement's view on alternative design while extolling the virtues of the consumer expectations test:

> The important aspect of strict products liability that led to our adoption [of the consumer expectations test] remains true today: the burden of compensating victims of unreasonably dangerous products is placed on the manufacturers, who are most able to protect against the risk of harm, and not on the consumer injured by the product. Increasing the burden for injured consumers to prove their strict liability claims for unreasonably dangerous products that were placed into the stream of commerce is contrary to the policy reasons behind the adoption of strict liability. . . .

Other design defect tests were propounded during the late 1970s, but have receded in recent years as most courts have adopted the *Barker* test. For example, Azzarello v. Black Brothers Co., Inc., 391 A.2d 1020, 1027 (Pa. 1978), held that even though the supplier was not "an insurer of all injuries caused by the product," it nonetheless was cast "in the role of a guarantor of his product's safety," under which the words "unreasonably dangerous" had no part. Instead "the jury may find a defect where the product left the supplier's control lacking any element necessary to make it safe for its intended use or possessing any feature that renders it unsafe for the intended use." Pennsylvania retreated from the *Azzarello* test in Tincher v. Omega Flex, Inc., 104 A.3d 328, 335 (Pa. 2014), but refused to adopt the Third Restatement reasonable alternative design test. In *Tincher*, the plaintiff sought to show that corrugated stainless-steel tubing used to transport natural gas to the Tinchers' first floor fireplace

was defective because it was punctured by a lightning strike. Castille, C.J., reversed a jury verdict and announced this test for product defect:

> [W]e conclude that a plaintiff pursuing a cause upon a theory of strict liability in tort must prove that the product is in a "defective condition." The plaintiff may prove defective condition by showing either that (1) the danger is unknowable and unacceptable to the average or ordinary consumer, or that (2) a reasonable person would conclude that the probability and seriousness of harm caused by the product outweigh the burden or costs of taking precautions. The burden of production and persuasion is by a preponderance of the evidence.

An approach to design defects more restrictive than *Barker*'s was taken in Wilson v. Piper Aircraft Corp., 577 P.2d 1322, 1327–28 (Or. 1978), a wrongful death action brought by the representatives of two passengers who died in the crash of a Piper Cherokee airplane manufactured by the defendants. The plaintiffs claimed that the defective design was the engine's susceptibility to icing, in part because the aircraft was not equipped with a state-of-the-art injection-type fuel system. Holman, J., parted with *Barker* by imposing stringent requirements that the plaintiff present evidence "from which the jury could find the suggested alternatives are not only technically feasible but also practicable in terms of cost and the over-all design and operation of the product." Further the Federal Aviation Administration (FAA) had awarded the defendant a certificate of airworthiness, which in its own terms set only minimum design standards. The court concluded that

> in a field as closely regulated as aircraft design and manufacture, it is proper to take into consideration, in determining whether plaintiffs have produced sufficient evidence of defect to go to the jury, the fact that the regulatory agency has approved the very design of which they complain after considering the dangers involved.

**2.** ***State of the Art: Time of Sale or Time of Trial?*** In setting the appropriate design standard for product safety, many judicial decisions look in part to the state of the art in the product supplier's trade or business. The state of the art refers to something more stringent than the "common practice" in the industry and embraces the scientific, technological, and safety standards that are reasonably feasible at the time of product design. Thus in Kim v. Toyota Motor Corp., 424 P.3d 290, 296 (Cal. 2018), Kruger, J., distinguished industry custom — "the use of the challenged design within the relevant industry," i.e., "what is done" — from state-of-the-art evidence — "what can be done under present technological capacity." See also RTT: PL §2, cmt. *d*.

Most courts today do not allow compliance with the state of the art to resolve the design defect question in the defendant's favor but nonetheless treat it as a factor to consider, which "is both necessary and probative on the issue of 'unreasonably dangerous.'" Reed v. Tiffin Motor Homes, Inc., 697 F.2d 1192, 1197 (4th Cir. 1982). In Bruce v. Martin-Marietta Corp., 544 F.2d 442, 447 (10th Cir. 1976), the court measured the state of the art at the time the defendant's airplane seats entered the stream of commerce in 1952, not at the time of the crash in 1970. The record showed that the seats met all FAA standards as well as the applicable state of the art for 1952. In the court's view, the crucial test was the "expectation of the ordinary consumer," who "would not expect a Model T to have safety features which are incorporated in automobiles today." Contrast with City of Pomona v. SQM North America Corp., 801 Fed. App'x 488, 489–90, 492 (9th Cir. 2020), which involved "Pomona's strict product liability claim that fertilizer manufactured by SQM contaminated the city's water supply with a toxic chemical called perchlorate." Under *Barker* "the jury must determine 'through hindsight' whether 'the risk of danger inherent in the challenged design outweighs the benefits of such design.'" Accordingly, in an action for current harm, the court allowed

"jurors to consider risks that were not, and could not have been, known to the manufacturer at the time of manufacture." This prompted a vigorous dissent from Lee, J.:

> Notably, the City conceded at oral argument that it has not located a single California state court ruling—in the forty years since *Barker*'s issuance—that applied *Barker* to hold a party liable based on scientific knowledge that was unknowable at the time of the incident but known at the time of trial.

**3. *Subsequent Improvements.*** The substantive disputes in state of the art cases frequently raise evidentiary inquiries: can evidence of subsequent design changes be introduced to show the defectiveness of the defendant's basic design? In Ault v. International Harvester Co., 528 P.2d 1148, 1152 (Cal. 1974), the California Supreme Court allowed such evidence, saying:

> The contemporary corporate mass producer of goods, the normal products liability defendant, manufactures tens of thousands of units of goods; it is manifestly unrealistic to suggest that such a producer will forego making improvements in its product, and risk innumerable additional lawsuits and the attendant adverse effect upon its public image, simply because evidence of adoption of such improvement may be admitted in an action founded on strict liability for recovery on an injury that preceded the improvement.

Nonetheless, a strong majority of courts have refused to admit the evidence in both negligence and strict liability cases. See Cann v. Ford Motor Co., 658 F.2d 54, 60 (2d Cir. 1981). Federal Rule of Evidence 407 provides:

> When measures are taken that would have made an earlier injury or harm less likely to occur, evidence of the subsequent measures is not admissible to prove:
>
> - negligence;
> - culpable conduct;
> - a defect in a product or its design; or
> - a need for a warning or instruction.

Or, as Baron Bramwell put it, the rule rejects the notion that "because the world gets wiser as it gets older, therefore it was foolish before." Hart v. Lancashire & Yorkshire Ry. Co. (1869) 21 LT 261, 263 (quoted in Note of Advisory Committee on Proposed Rule 407).

**4. *Product Modification.*** Much litigation has focused on the question whether a product alteration made after a manufacturer has shipped goods constitutes a superseding cause sufficient to relieve the original manufacturer of liability for design defects. Young v. Aeroil Prods. Co., 248 F.2d 185 (9th Cir. 1957), represents the traditional view of protecting manufacturers from liability based on subsequent alterations. There the decedent had been crushed to death when the portable elevator he had been operating toppled. The decedent's employer had previously added additional equipment to the elevator, causing its imbalance. Even though the defendant had sold the elevator with the express warranty that it was balanced, the court held that the warranty was unavailing because "[t]he thing being used was not the thing sold."

In Hoover v. New Holland North America, Inc., 11 N.E.3d 693 (N.Y. 2014), the plaintiff, a sixteen-year-old girl, was badly injured when "she was caught and dragged into the rotating driveline of a tractor-driven post hole digger distributed by defendant-appellant CNH America LLC (CNH) and sold by defendant-appellant Niagara Frontier Equipment Sales, Inc. (Niagara) (collectively, defendants)." The manufacturer of the device, Alamo/SMC Corporation (SMC), was not joined as a defendant in the suit. "The jury returned a verdict in favor of plaintiff in the amount of $8,811,587.29 and apportioned liability as follows: 35

percent to CNH, 30 percent to SMC, 30 percent to Smith [the owner of the digger], 3 percent to Gary Hoover [the plaintiff's stepfather], and 2 percent to Niagara."

The defendant's product had been distributed with extensive warnings, including: "DANGER! SHIELD MISSING DO NOT OPERATE!" and "KEEP ALL SHIELDS IN PLACE AND IN GOOD CONDITION." Smith was aware of these warnings but nonetheless decided not to replace the key shields on the device after they incurred damage over several years from installing between 1,000 and 2,000 posts per year. Smith testified that he removed the guard and continued to use the machine without replacing the guard "because it was only going to break again."

Abdus-Salaam, J., rejected the defendant's motion for summary judgment on the ground that

> Smith did not modify the digger in order to "circumvent[]" the utility of the shield or to "adapt" the digger to suit his own needs. Rather, Smith removed the shield because its "functional utility" had already been destroyed, and his testimony raised a question of fact whether removal of the broken shield was to blame for plaintiff's injuries. Plaintiff also proffered Berry's expert affidavit, in which the engineer averred that the shield was "not reasonably safe" because it was not "designed to last the life" of the digger, and that defendants' failure to incorporate a safer yet feasible alternative design, such as an integral guard or metal shield, was "a substantial factor" in causing plaintiff's injuries.

Smith, J., dissented, arguing that the full liability should rest on Smith because "[h]e chose not to get a replacement shield—which would have cost $40 and taken no more than half an hour to install—because 'it's only going to get bent up and broke again.'" How does the case come out under the open and obvious defense?

In Singh v. Gemini Auto Lifts, Inc., 27 N.Y.S.3d 637, 638–39 (App. Div. 2016), the court extended *Hoover* to reach a situation where the plaintiff caught his hand in a hole on an automotive lift, from which the plastic cover had been removed. The court held that the plaintiff had raised triable issues of fact "as to whether the lift was intended to be used without the cover in place." Does it make sense for courts to resolve liability in the face of post-sale modifications in terms of design defects? What about liability for failure to warn? See *infra*, Note 1.

The Third Restatement recognizes that product alteration and modification may defeat or diminish defendant's responsibility, but develops no specialized rules to deal with them, treating them (along with product misuse) as parts of the broader questions of product defect, causation, and plaintiff's conduct. RTT: PL §2, cmt. *p*.

### *c. The Third Restatement Reasonable Alternative Design Test*

The Third Restatement rejected the consumer expectations test as part of its attempt to rein in what was perceived to be excessive liability arising out of the *Barker* dual-pronged standard.

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: PRODUCTS LIABILITY**

**§2. Categories of Product Defect**

A product: . . .

(b) is defective in design when the foreseeable risks of harm posed by the product could have been reduced or avoided by the adoption of a reasonable alternative design by the seller or other distributor, or a predecessor in the commercial chain of distribution, and the omission of the alternative design renders the product not reasonably safe. . . .

*Comment a. Rationale:* . . . The emphasis is on creating incentives for manufacturers to achieve optimal levels of safety in designing and marketing products. Society does not benefit from products that are excessively safe — for example, automobiles designed with maximum speeds of 20 miles per hour — any more than it benefits from products that are too risky. Society benefits most when the right, or optimal, amount of product safety is achieved. . . .

*Illustration 5:* ABC Co. manufactures novelty items. One item, an exploding cigar, is made to explode with a loud bang and the emission of smoke. Robert purchased the exploding cigar and presented it to his boss, Jack, at a birthday party arranged for him at the office. Jack lit the cigar. When it exploded, the heat from the explosion lit Jack's beard on fire causing serious burns to his face. . . . [T]he finder of fact might find ABC liable for the defective design of the exploding cigar even if no reasonable alternative design was available that would provide similar prank characteristics. The utility of the exploding cigar is so low and the risk of injury is so high as to warrant a conclusion that the cigar is defective and should not have been marketed at all.

Does an alternative design test ensure optimal product-design safety?

## NOTES

**1.** ***Alternative Designs.*** The reasonable alternative design test in the Third Restatement was developed largely in response to the New Jersey case of O'Brien v. Muskin Corp., 463 A.2d 298, 302–03, 305–06 (N.J. 1983). Muskin sold a pool to Arthur Henry, which, when assembled, had an embossed vinyl bottom and a depth of about three feet. The plaintiff, twenty-three years old, dove into the pool from either a nearby platform or from the eight-foot-high roof of the Henrys' garage. "As his outstretched hands hit the vinyl-lined pool bottom, they slid apart, and O'Brien struck his head on the bottom of the pool, thereby sustaining injuries." The plaintiff's expert claimed that the pool design was dangerous because wet vinyl was more than twice as slippery as the rubber latex used to line in-ground pools. The trial court excluded that testimony when the expert admitted that he knew of no above-ground pool lined with a material other than vinyl. On appeal the court allowed the design defect count to go to the jury on Professor Wade's risk-utility test, noting that for the plaintiff to reach the jury under such a test, "it was not necessary for plaintiff to prove the existence of alternative, safer designs."

In New Jersey, *Muskin* was altered by statute, which provided, among other things, that "the manufacturer or seller shall not be liable if: (1) At the time the product left the control of the manufacturer, there was not a practical and technically feasible alternative design that would have prevented the harm without substantially impairing the reasonably anticipated or intended function of the product. . . ." N.J. Stat. Ann. §2A:58C-3(a) (West 2024). The Third Restatement takes much the same line by requiring "that the plaintiff show a reasonable alternative design . . . even though the plaintiff alleges that the category of product sold by the defendant is so dangerous that it should not have been marketed at all." RTT: PL §2, cmt. *d*. It explicitly disapproved of *Muskin* because "the vinyl pool liner that [the manufacturer] utilized was the best and safest liner available and that no alternative, less slippery liner was feasible." RTT: PL §2, illus. 4. Is it appropriate for a jury to decide that, absent a reasonably feasible alternative design, above-ground pools should not be marketed at all? In dealing with its alternative design conception, section 2, comment *f* of the Third Restatement observes:

> A broad range of factors may be considered in determining whether an alternative design is reasonable and whether its omission renders a product not reasonably safe. The factors include,

> among others, the magnitude and probability of the foreseeable risks of harm, the instructions and warnings accompanying the product, and the nature and strength of consumer expectations regarding the product, including expectations arising from product portrayal and marketing. The relative advantages and disadvantages of the product as designed and as it alternatively could have been designed may also be considered. Thus, the likely effects of the alternative design on production costs; the effect of alternative design on product longevity, maintenance, repair, and esthetics; and the range of consumer choice among products are factors that may be taken into account.

**2. *Judicial Reception of the Third Restatement.*** The reasonable alternative design requirement has received a mixed reception. In Potter v. Chicago Pneumatic Tool Co., 694 A.2d 1319, 1332, 1334–35 (Conn. 1997), Katz, J., noted that a majority of states did not impose the Third Restatement's alternative design requirement, and refused to do so, lest the law place an "undue burden" on plaintiffs by requiring them to use expert evidence in every design defect case. In *Tincher*, 104 A.3d at 395, *supra* Note 2, at 68, Castille, J., likewise resisted the move to the Third Restatement's "evidence-bound standard of proof," on the ground that "[t]he approach suggests *a priori* categorical exemptions for some products — such as novel products with no alternative design — but not others." He elaborated this rationale:

> Neither courts, nor the American Law Institute for that matter, are in the business of articulating general principles tailored to anoint special "winners" and "losers" among those who engage in the same type of conduct. In our view, the question of "special tort-insulated status" for certain suppliers — for example, manufacturers of innovative products with no comparable alternative design — optimally "requires an assessment and balancing of policies best left to the General Assembly."

The necessity for a reasonable alternative design was, however, embraced in Casey v. Toyota Motor Engineering & Manufacturing North America Inc., 770 F.3d 322, 332–34 (5th Cir. 2014), in which the plaintiff claimed that the defective design of Toyota's side curtain airbag resulted in his wife's death in a one-car accident in which she had been driving at excessive speed. The plaintiff's expert witness testified that a different material (elastomer) mentioned in an unrelated patent application was safer than the nylon material then used by Toyota. Higginson, J., first noted that the plaintiff's "reliance on the patent application's tests was not evidence of the alternative design's superior safety because the testing did not involve similar forces and factors as involved in Mrs. Casey's rollover accident." He continued:

> In addition, there is no evidence in the record that the baseline material to which the patent applicants compared their invention was the same as the airbag used in the airbag installed in Mrs. Casey's vehicle. While both used nylon, there is no evidence that the weave, coating, or other construction of the Toyota airbag was the same as the baseline used in the patent's tests. In sum, because the patent application did not test the alternative material under similar accident conditions, Casey has failed to show that using that material would have prevented or reduced the risk of injury in Mrs. Casey's accident.

Higginson, J., then noted that the plaintiff had not shown that the new design would not "inject any new risks into the vehicle or diminish its usefulness or safety in any way," or "that the alternative design could have been implemented in the 2010 Toyota Highlander, has been implemented in any vehicle, or could possibly be implemented." Finally, he noted that the "economic feasibility" of the alternative design had not been proven.

Aaron D. Twerski, An Essay on the Quieting of Products Liability Law, 105 Cornell L. Rev. 1211, 1211 (2020), argues that the reasonable alternative design test has become the de facto norm:

> In fifteen of the seventeen states that allow recovery based on consumer expectations the author could not find a single case in which the plaintiff did not introduce a reasonable alternative

> design. And in all jurisdictions but one, a defendant is free to introduce risk-utility evidence as relevant to the issue of whether the product disappoints consumer expectations. Thus, whether a reasonable alternative design is required de jure, it is de facto a staple in almost all design defect cases.

Should the plaintiff ever be able to invoke a design that has never been put to commercial use as the appropriate alternative design?

**3. *"Unavoidably Unsafe" Products.*** The "comment *k*" defense, derived from RST §402A, *supra* at 63, precludes certain "unavoidably unsafe products," notably prescription drugs and medical devices, from being classified as defective merely because they are, at the time of distribution, incapable of being made safe. States differ in terms of whether they apply a "blanket" or "case-by-case" (i.e., product-by-product) approach to comment *k*. The "blanket" approach exempts from strict liability design defect certain categories of products deemed "unavoidably unsafe." For example, the California Supreme Court deemed all prescription drugs categorically exempt from strict liability for design defect in Brown v. Superior Court, 751 P.2d 470, 477 (Cal. 1988):

> (1) a drug manufacturer's liability for a defectively designed drug should not be measured by the standards of strict liability; (2) because of the public interest in the development, availability, and reasonable price of drugs, the appropriate test for determining responsibility is the test stated in comment k; and (3) for these same reasons of policy, we disapprove the holding . . . that only those prescription drugs found to be "unavoidably dangerous" should be measured by the comment k standard and that strict liability should apply to drugs that do not meet that description.

A large majority of states, however, reject the blanket approach in favor of a "case-by-case" approach that requires the defendant to establish that the product is "unavoidably unsafe." For example, the New Jersey Supreme Court held in Feldman v. Lederle Laboratories, 479 A.2d 374, 382–83 (N.J. 1984), that only certain drugs—namely those proven to be "unavoidably unsafe" on a case-by-case basis—qualify for comment *k*'s protection:

> [W]e see no reason to hold as a matter of law and policy that all prescription drugs that are unsafe are unavoidably so. Drugs, like any other products, may contain defects that could have been avoided by better manufacturing or design. Whether a drug is unavoidably unsafe should be decided on a case-by-case basis. . . .

To meet this burden, the defendant must show that no feasible alternative design exists that would accomplish the same purpose with a lesser risk and that the drug's overall benefits outweigh the risks it presents to individual safety.

**4. *Modern Defective Drug Design Litigation.*** In Benefield v. Pfizer Inc., 103 F. Supp. 3d 449, 462 (S.D.N.Y. 2015), the plaintiff brought a design defect claim over conditions allegedly developed from taking Tygacil, a brand-name antibacterial drug that she was prescribed for an abdominal infection. Pfizer argued that the design defect claims should be dismissed because the plaintiff failed to allege "better alternatives." Oetken, J., rejected Pfizer's contention:

> Several factors figure in the risk-utility test, but the "heart" of the analysis is about "whether the design chosen was a reasonable one from among the feasible choices of which the manufacturer was aware or should have been aware." . . . At this stage, Plaintiffs must merely "set forth sufficient facts from which the Court can reasonably infer that the design was defective." . . . Plaintiffs have done so. They have plausibly alleged that Tygacil brought about [plaintiff's] injuries.

How does the plaintiff's assertion of injury demonstrate that risk outweighs utility?

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: PRODUCTS LIABILITY**

**§6. Liability of Commercial Product Seller or Distributor for Harm Caused by Defective Prescription Drugs and Medical Devices**

(c) A prescription drug or medical device is not reasonably safe due to defective design if the foreseeable risks of harm posed by the drug or medical device are sufficiently great in relation to its foreseeable therapeutic benefits that reasonable health-care providers, knowing of such foreseeable risks and therapeutic benefits, would not prescribe the drug or medical device for any class of patients. . . .

***Comment b. Rationale:*** . . . The traditional refusal by courts to impose tort liability for defective designs of prescription drugs and medical devices is based on the fact that a prescription drug or medical device entails a unique set of risks and benefits. What may be harmful to one patient may be beneficial to another. Under Subsection (c) a drug is defectively designed only when it provides no net benefit to any class of patients. . . .

Criticism of the Third Restatement's design defect test was voiced in Bryant v. Hoffman-LaRoche, 585 S.E.2d 723, 727–28 (Ga. Ct. App. 2003), in which the plaintiff sued the defendant on the ground that his wife died as a result of the heart medication Posicor, which he alleged was defectively designed and thus interacted poorly with other drugs she had taken. The defendant manufacturer urged that the case be governed by RTT: PL §6(c). The court rejected this view in favor of comment *k* to the Second Restatement, noting:

> [Section] 6(c) has been criticized for its failure to reflect existing case law, its lack of flexibility with regard to drugs involving differing benefits and risks, its unprecedented application of a reasonable physician standard, and the fact that a consumer's claim could easily be defeated by expert opinion that the drug had some use for someone, despite potentially harmful effects on a large class of individuals. [Freeman v. Hoffman-LaRoche, 618 N.W.2d 827 (Neb. 2000).] To date, no court has adopted the Third Restatement's strict liability test for prescription drugs, and one court [*Freeman*] has explicitly refused to adopt the test. . . .
>
> Moreover, we agree with the majority of courts that Comment *k* serves as an affirmative defense and that the defense has no application to claims of manufacturing defect or failure to warn.

Does section 6(c) functionally grant absolute immunity to all FDA-approved drugs?

For further criticism of the "complete overhaul" of the design defect provisions in the Third Restatement, see George W. Conk, Is There a Design Defect in the Restatement (Third) of Torts: Products Liability?, 109 Yale L.J. 1087 (2000). But Professors Henderson and Twerski insist:

> A claim that seeks to find a given drug design defective because the manufacturer should have developed a safer alternative drug is inappropriate because courts are incapable of sensibly deciding whether the alternative proposed by the plaintiff would have met with FDA approval. Since any drug marketed in the United States must be approved by the FDA, a court must be able to determine that the FDA would have approved the drug. Given the many-year duration of the FDA approval process, which involves testing of thousands of patients, no court could rationally determine that an alternative drug would have been approved.

Aaron D. Twerski & James A. Henderson, Jr., Drug Design Liability: Farewell to Comment k, 67 Baylor L. Rev. 521, 577 (2015). Does this argument preclude the claim in *Bryant*? A malpractice action against the treating physician? Require federal preemption of state law? Catherine M. Sharkey, Field Preemption: Opening the "Gates of Escape" from Tort Law, 50 J.

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Legal Stud. S27, S47–50 (2021), argues that federal preemption, see Section H, *infra*, stunted the development of 6(c).

## 3. The Duty to Warn

Implicit in many design defect decisions is the view that it is better to design out certain dangerous conditions than it is to warn consumers and users of their dangers. Although that rule works well for many forms of equipment, it poses significant challenges for pharmaceutical and chemical products for which small changes in molecular composition can negate the effectiveness of the product for its intended purpose, or require a new round of approvals from, for example, the Food and Drug Administration or the Environmental Protection Agency. In these cases, the use of product warnings instead of design alterations could offer a sensible compromise, especially when the potential harms are not apparent to a product user from the appearance of the product or from common knowledge about its lurking dangers. What legal standards should apply in these warning cases?

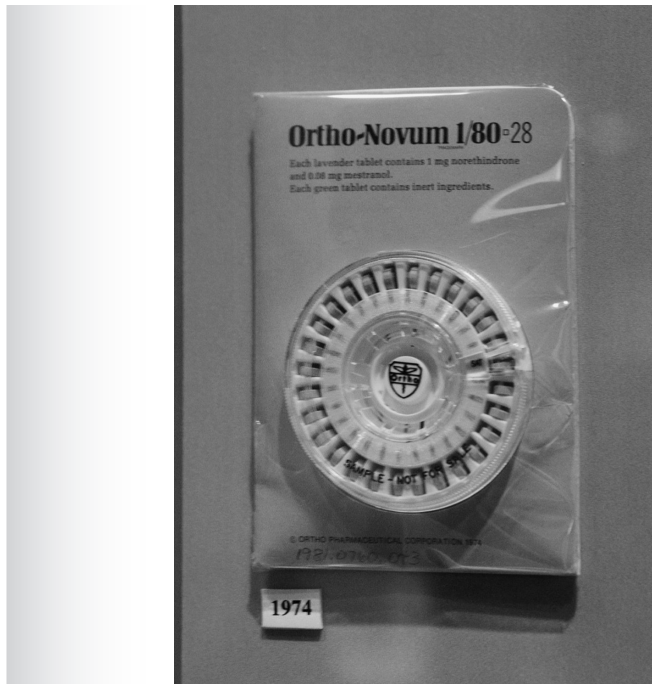
### *MacDonald v. Ortho Pharmaceutical Corp.*

475 N.E.2d 65 (Mass. 1985)

Abrams, J. This products liability action raises the question of the extent of a drug manufacturer's duty to warn consumers of dangers inherent in the use of oral contraceptives. The plaintiffs brought suit against the defendant, Ortho Pharmaceutical Corporation (Ortho), for injuries allegedly caused by Ortho's birth control pills, and obtained a jury verdict in their favor. The defendant moved for a judgment notwithstanding the verdict. The judge concluded that the defendant did not owe a duty to warn the plaintiffs, and entered judgment for Ortho. The plaintiffs appealed. We transferred the case to this court on our own motion and reinstate the jury verdict.

We summarize the facts. In September, 1973, the plaintiff Carole D. MacDonald (MacDonald), who was twenty-six years old at the time, obtained from her gynecologist a prescription for Ortho-Novum contraceptive pills, manufactured by Ortho. As required by the then effective regulations promulgated by the United States Food and Drug Administration (FDA), the pill dispenser she received was labeled with a warning that "oral contraceptives are powerful and effective drugs which can cause side effects in some users and should not be used at all by some women," and that "[t]he most serious known side effect is abnormal blood clotting which can be fatal." The warning also referred MacDonald to a booklet which she obtained from her gynecologist, and which was distributed by Ortho pursuant to FDA requirements. The booklet contained detailed information about the contraceptive pill, including the increased risk to pill users that vital organs such as the brain may be damaged by abnormal blood clotting. [The warning supplied listed the death and injury rates to women of various ages from taking the pill and noted "that women who have had blood clots in the legs, lungs, or brain [should] not use oral contraceptives."] The word "stroke" did not appear on the dispenser warning or in the booklet.

MacDonald's prescription for Ortho-Novum pills was renewed at subsequent annual visits to her gynecologist. The prescription was filled annually. On July 24, 1976, after approximately three years of using the pills, MacDonald suffered an occlusion of a cerebral artery by a blood clot, an injury commonly referred to as a stroke [or a "cerebral vascular accident"]. The injury caused the death of approximately twenty per cent of MacDonald's brain tissue, and left her permanently disabled. She and her husband initiated an action in the Superior Court against Ortho, seeking recovery for her personal injuries and his consequential damages and loss of consortium.




**Ortho-Novum Dialpak dispenser**

*Source: B Christopher / Alamy*

MacDonald testified that, during the time she used the pills, she was unaware that the risk of abnormal blood clotting encompassed the risk of stroke, and that she would not have used the pills had she been warned that stroke is an associated risk. [The court notes that the amended FDA regulations listed "'the serious side effects of oral contraceptives, such as thrombophlebitis, pulmonary embolism, myocardial infarction, retinal artery thrombosis, *stroke*, benign hepatic adenomas, induction of fetal abnormalities, and gallbladder disease' (emphasis added). See 21 C.F.R. §310.501(a)(2)(iv) (1984)."] The case was submitted to a jury on the plaintiffs' theories that Ortho was negligent in failing to warn adequately of the dangers associated with the pills and that Ortho breached its warranty of merchantability. These two theories were treated, in effect, as a single claim of failure to warn. The jury returned a special verdict, finding no negligence or breach of warranty in the manufacture of the pills. The jury also found that Ortho adequately advised the gynecologist of the risks inherent in the pills;[7] the jury found, however, that Ortho was negligent and in breach of warranty because it failed to give MacDonald sufficient warning of such dangers. The jury further found that MacDonald's injury was caused by Ortho's pills, that the inadequacy of the warnings to MacDonald was the proximate cause of her injury, and that Ortho was liable to MacDonald and her husband.

After the jury verdict, the judge granted Ortho's motion for judgment notwithstanding the verdict, concluding that, because oral contraceptives are prescription drugs, a manufacturer's duty to warn the consumer is satisfied if the manufacturer gives adequate warnings to the prescribing physician, and that the manufacturer has no duty to warn the consumer directly.

The narrow issue, on appeal, is whether, as the plaintiffs contend, a manufacturer of birth control pills owes a direct duty to the consumer to warn her of the dangers inherent in the use of the pill. We conclude that such a duty exists under the law of this Commonwealth.

### 1. Extent of Duty to Warn . . .

[The court first notes that the general rule was that the defendant must warn all "persons who it is foreseeable will come in contact with, and consequently be endangered by, that product." It then recognizes a "narrow" exception, as set out in Restatement (Second) of Torts §388, comment *n*, when warnings have been given to a responsible intermediary "so that the manufacturer has no duty directly to warn the consumer." It continues:]

7. MacDonald stated at trial that her gynecologist had informed her only that oral contraceptives might cause bloating, and had not advised her of the increased risk of stroke associated with consumption of birth control pills. The physician was not joined as a defendant in this action, and no questions relating to any potential liability on his part are before us. MacDonald further testified at trial that she had read both the warning on the Dialpak tablet dispenser as well as the booklet which she received from her gynecologist.

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The rule in jurisdictions that have addressed the question of the extent of a manufacturer's duty to warn in cases involving prescription drugs is that the prescribing physician acts as a "learned intermediary" between the manufacturer and the patient, and "the duty of the ethical drug manufacturer is to warn the doctor, rather than the patient, [although] the manufacturer is directly liable to the patient for a breach of such duty." McEwen v. Ortho Pharmaceutical Corp., 528 P.2d 522 (Or. 1974). Oral contraceptives, however, bear peculiar characteristics which warrant the imposition of a common law duty on the manufacturer to warn users directly of associated risks. Whereas a patient's involvement in decision-making concerning use of a prescription drug necessary to treat a malady is typically minimal or nonexistent, the healthy, young consumer of oral contraceptives is usually actively involved in the decision to use "the pill," as opposed to other available birth control products, and the prescribing physician is relegated to a relatively passive role.

Furthermore, the physician prescribing "the pill," as a matter of course, examines the patient once before prescribing an oral contraceptive and only annually thereafter. At her annual checkup, the patient receives a renewal prescription for a full year's supply of the pill. Thus, the patient may only seldom have the opportunity to explore her questions and concerns about the medication with the prescribing physician. Even if the physician, on those occasions, were scrupulously to remind the patient of the risks attendant on continuation of the oral contraceptive, "the patient cannot be expected to remember all of the details for a protracted period of time." 35 Fed. Reg. 9002 (1970).

Last, the birth control pill is specifically subject to extensive Federal regulation [which, inter alia, requires that "users of these drugs should, without exception, be furnished with written information telling them of the drug's benefits and risks"].

The oral contraceptive thus stands apart from other prescription drugs in light of the heightened participation of patients in decisions relating to use of "the pill"; the substantial risks affiliated with the product's use; the feasibility of direct warnings by the manufacturer to the user; the limited participation of the physician (annual prescriptions); and the possibility that oral communications between physicians and consumers may be insufficient or too scanty standing alone fully to apprise consumers of the product's dangers at the time the initial selection of a contraceptive method is made as well as at subsequent points when alternative methods may be considered. We conclude that the manufacturer of oral contraceptives is not justified in relying on warnings to the medical profession to satisfy its common law duty to warn, and that the manufacturer's obligation encompasses a duty to warn the ultimate user. Thus, the manufacturer's duty is to provide to the consumer written warnings conveying reasonable notice of the nature, gravity, and likelihood of known or knowable side effects, and advising the consumer to seek fuller explanation from the prescribing physician or other doctor of any such information of concern to the consumer.[13]

### 2. Adequacy of the Warning

Because we reject the judge's conclusion that Ortho had no duty to warn MacDonald, we turn to Ortho's separate argument, not reached by the judge, that the evidence was insufficient to warrant the jury's finding that Ortho's warnings to MacDonald were inadequate. Ortho contends initially that its warnings complied with FDA labeling requirements, and that those requirements preempt or define the bounds of the common law duty to warn. We disagree. The regulatory history of the FDA requirements belies any objective to cloak them

13. This opinion does not diminish the prescribing physician's duty to "disclose in a reasonable manner all significant medical information that the physician possesses or reasonably should possess that is material to an intelligent decision by the patient whether to" take "the pill." Harnish v. Children's Hosp. Medical Center, 439 N.E.2d 240 (Mass. 1982).

with preemptive effect. In response to concerns raised by drug manufacturers that warnings required and drafted by the FDA might be deemed inadequate by juries, the FDA commissioner specifically noted that the boundaries of civil tort liability for failure to warn are controlled by applicable State law. 43 Fed. Reg. 4214 (1978). Although the common law duty we today recognize is to a large degree coextensive with the regulatory duties imposed by the FDA, we are persuaded that, in instances where a trier of fact could reasonably conclude that a manufacturer's compliance with FDA labeling requirements or guidelines did not adequately apprise oral contraceptive users of inherent risks, the manufacturer should not be shielded from liability by such compliance. Thus, compliance with FDA requirements, though admissible to demonstrate lack of negligence, is not conclusive on this issue, just as violation of FDA requirements is evidence, but not conclusive evidence, of negligence. We therefore concur with the plaintiffs' argument that even if the conclusion that Ortho complied with FDA requirements were inescapable, an issue we need not decide, the jury nonetheless could have found that the lack of a reference to "stroke" breached Ortho's common law duty to warn.

The common law duty to warn, like the analogous FDA "lay language" requirement, necessitates a warning "comprehensible to the average user and . . . convey[ing] a fair indication of the nature and extent of the danger to the mind of a reasonably prudent person."

Whether a particular warning measures up to this standard is almost always an issue to be resolved by a jury; few questions are "more appropriately left to a common sense lay judgment than that of whether a written warning gets its message across to an average person." Ferebee v. Chevron Chem. Co., 552 F. Supp. 1293, 1304 (D.D.C. 1982). A court may, as a matter of law, determine "whether the defendant has conformed to that standard, in any case in which the jury may not reasonably come to a different conclusion," Restatement (Second) of Torts §328B(d) and Comment *g* (1965), but judicial intrusion into jury decision-making in negligence cases is exceedingly rare. Further, we must view the evidence in the light most favorable to the plaintiffs. The test is whether "anywhere in the evidence, from whatever source derived, any combination of circumstances could be found from which a reasonable inference could be drawn in favor of the plaintiff."

Ortho argues that reasonable minds could not differ as to whether MacDonald was adequately informed of the risk of the injury she sustained by Ortho's warning that the oral contraceptives could cause "abnormal blood clotting which can be fatal" and further warning of the incremental likelihood of hospitalization or death due to blood clotting in "vital organs, such as the brain." We disagree. . . . We cannot say that this jury's decision that the warning was inadequate is so unreasonable as to require the opposite conclusion as a matter of law. The jury may well have concluded, in light of their common experience and MacDonald's testimony, that the absence of a reference to "stroke" in the warning unduly minimized the warning's impact or failed to make the nature of the risk reasonably comprehensible to the average consumer. Similarly, the jury may have concluded that there are fates worse than death, such as the permanent disablement suffered by MacDonald, and that the mention of the risk of death did not, therefore, suffice to apprise an average consumer of the material risks of oral contraceptive use.

We reverse the judgment, which the judge ordered notwithstanding the verdict, and remand the case to the Superior Court for the entry of judgment for the plaintiffs.

So ordered.

O'Connor, J., dissenting. . . . I would hold that, as a matter of law, by adequately informing physicians of the risks associated with its product and by complying with applicable FDA regulations, a contraceptive pill manufacturer fulfils the duty to warn that it owes consumers. . . .

I believe that the "prescription drug" rule, combined with the *Harnish* rule most fairly and efficiently allocates among drug manufacturers, physicians, and drug users, the risks and responsibilities involved with the use of prescription drugs. Furthermore, I believe that those rules best ensure that a prescription drug user will receive in the most effective manner the information that she needs to make an informed decision as to whether to use the drug. The rules place on drug manufacturers the duty to gather, compile, and provide to doctors data regarding the use of their drugs, tasks for which the manufacturers are best suited, and the rules place on doctors the burden of conveying those data to their patients in a useful and understandable manner, a task for which doctors are best suited. Doctors, unlike printed warnings, can tailor to the needs and abilities of an individual patient the information that that patient needs in order to make an informed decision whether to use a particular drug. Manufacturers are not in position to give adequate advice directly to those consumers whose medical histories and physical conditions, perhaps unknown to the consumers, make them peculiarly susceptible to risk. Prescription drugs — including oral contraceptives — differ from other products because their dangers vary widely depending on characteristics of individual consumers. Exposing a prescription drug manufacturer to liability based on a jury's determination that, despite adequately informing physicians of the drug's risks and complying with FDA regulations, the manufacturer failed reasonably to warn a particular plaintiff-consumer of individualized risks is not essential to reasonable consumer protection and places an unfair burden on prescription drug manufacturers.

## NOTES

**1.** ***Physicians as Learned Intermediaries.*** Why did the plaintiffs not join the treating physician? To what extent is the decision in *MacDonald* strengthened or weakened by the wide availability of all forms of product warnings on the Internet? The learned intermediary rule held firm in Harrison v. American Home Products Corp. (AHP), 165 F.3d 374, 379 (5th Cir. 1999), when the plaintiffs complained of adverse side effects from the contraceptive Norplant, a long-term birth control method. Jolly, J., stressed the "significant role" that physicians played "in prescribing Norplant and in educating their patients about the benefits and disadvantages to using it." He also rejected the view that AHP's aggressive direct-to-consumer marketing campaign undercut the physicians' duty to warn in the absence of any evidence that the plaintiffs "actually saw, let alone relied, on" any AHP marketing materials. What result if they had so relied?

Consider Perez v. Wyeth Laboratories, 734 A.2d 1245 (N.J. 1999), where the court imposed a direct duty to warn the plaintiff patient on Wyeth, the drug manufacturer, because of its "massive advertising campaign for Norplant in 1991, which it directed at women rather than at their doctors" through such women's magazines as *Glamour, Mademoiselle*, and *Cosmopolitan.* The *Perez* rule, however, has not caught on. In 2022, Owens, J., surveyed the landscape and noted that "only New Jersey has adopted a direct-to-consumer exception, but that decision has not been subsequently relied on." Dearinger v. Eli Lilly & Co., 510 P.3d 326, 331 (Wash. 2022) (en banc). Recently, Hunte v. Abbott Laboratories, Inc., 569 F. Supp. 3d 115 (D. Conn. 2021), certified to the Connecticut Supreme Court the question whether a direct-to-consumer marketing exception applies to infant formula for premature babies.

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: PRODUCTS LIABILITY**

**§6. Liability of Commercial Seller or Distributor for Harm Caused by Defective Prescription Drugs and Medical Devices**

(d) A prescription drug or medical device is not reasonably safe due to inadequate instructions or warnings if reasonable instructions or warnings regarding foreseeable risks of harm are not provided to:

(1) prescribing and other health-care providers who are in a position to reduce the risks of harm in accordance with the instructions or warnings; or

(2) the patient when the manufacturer knows or has reason to know that health-care providers will not be in a position to reduce the risks of harm in accordance with the instructions or warnings.

On the status of the learned intermediary defense in birth control and mass vaccination cases, the Third Restatement takes a studious pass: "The Institute leaves to developing case law whether exceptions to the learned intermediary rule in these or other situations should be recognized." RTT: PL §6, cmt. *e*.

How does *MacDonald* come out under the Third Restatement test? In 2021, the U.S. Court of Appeals for the Eighth Circuit determined Nebraska "would follow what has become an 'overwhelming majority' rule" in adopting the Third Restatement's version of the learned intermediary doctrine, finding that Massachusetts in *MacDonald* "stands alone in unequivocally adopting" a prescription-contraceptives exception. Ideus v. Teva Pharms. U.S., Inc., 986 F.3d 1098, 1102 (8th Cir. 2021).

Should drug manufacturers' direct promotional activities for other drugs be factored into the mix under section 6(d)(2)? For a sharp criticism of drug marketing practices, see Katherine Traverse Vukadin, Failure-to-Warn: Facing Up to the Real Impact of Pharmaceutical Marketing on the Physician's Decision to Prescribe, 50 Tulsa L. Rev. 75, 75, 104 (2014), insisting that "[f]ailure-to-warn jurisprudence should stop relying on empty paper compliance and recognize present-day pharmaceutical marketing as a compelling and driving force in the decision to prescribe." Nonetheless, successful overpromotion cases are difficult to win, given the requirement that "such overpromotion caused the physician to initiate or maintain the prescription at issue. General claims of overpromotion are not sufficient." *In re* Zyprexa Prods. Liab. Litig., 649 F. Supp. 2d 18, 33 (E.D.N.Y. 2009); see also DiBartolo v. Abbott Lab'ys., 914 F. Supp. 2d 601 (S.D.N.Y. 2012).

**2.** ***Pharmacists' Duty to Warn.*** A pharmacist's education and training justify the imposition of a set of standard duties: (1) a duty to fill a prescription correctly, (2) a duty to remedy inadequacies on the face of the prescription, (3) and a duty to take reasonable care in preparing or dispensing the medicine.

The vast majority of states retain the general common law rule that pharmacists do not have a duty to warn patients of the risks of medication. Under the learned intermediary doctrine, a court "could not place a greater burden on pharmacists" than on drug manufacturers because it is within the discretion of the physician, as the party who prescribes the drug, to warn the patient. Fakhouri v. Taylor, 618 N.E.2d 518, 519 (Ill. App. Ct. 1993). The Third Restatement §6(e) also restricts the liability of retail sellers of drugs and medical devices to cases of manufacturing defects (why?) or for failing "to exercise reasonable care and such failure causes harm to persons." Nonetheless some courts have required pharmacists

to (1) inform a doctor of a contraindication or of an abnormally high dosage; (2) provide a detailed warning where, through advertising, the pharmacy claims to have an enhanced warning or safety system in place; and (3) provide a warning where the pharmacist knows or has reason to know a customer's allergies. Thus in Happel v. Wal-Mart Stores, Inc., 766 N.E.2d 1118, 1124 (Ill. 2002), the defendant maintained a registry that warned of possible adverse drug interactions or allergic reactions for all of its customers. A duty to warn was imposed because "[t]he burden on defendant of imposing this duty is minimal. All that is required is that the pharmacist telephone the physician and inform him or her of the contraindication. Alternatively, the pharmacist could provide the same information to the patient."

**Dr. Albert Sabin**
*Source: Bettmann / Corbis*

**3. *Mass Vaccination Cases.*** The dissemination and adequacy of warnings has proved critically important to mass immunization programs. Davis v. Wyeth Laboratories, Inc., 399 F.2d 121, 129–31 (9th Cir. 1968), and Reyes v. Wyeth Laboratories, Inc., 498 F.2d 1264 (5th Cir. 1974), are the watershed cases involving liability for the Sabin live-virus polio vaccine. In *Davis*, the plaintiff contracted polio after being vaccinated as part of a mass immunization program administered by the local pharmacist when no physician was available to do the job. The program for immunization was promoted by one of the defendant's representatives whose expenses were reimbursed by the local medical organization. The court held that the defendant did not meet its duty to warn when it failed to inform the plaintiff of the one-in-a-million chance that the vaccine could cause polio, even when properly prepared and administered.

> Ordinarily in the case of prescription drugs warning to the prescribing physician is sufficient. . . .
>
> Here, however, although the drug was denominated a prescription drug it was not dispensed as such. It was dispensed to all comers at mass clinics without an individualized balancing by a physician of the risks involved. In such cases (as in the case of over-the-counter sales of nonprescription drugs) warning by the manufacturer to its immediate purchaser will not suffice. . . . In such cases, then, it is the responsibility of the manufacturer to see that warnings reach the consumer, either by giving warning itself or by obligating the purchaser to give warning. . . .
>
> This duty does not impose an unreasonable burden on the manufacturer. When drugs are sold over the counter to all comers warnings normally can be given by proper labeling. Such method of giving warning was not available here, since the vaccine came in bottles never seen by the consumer. But other means of communication such as advertisements, posters, releases to be read and signed by recipients of the vaccine, or oral warnings were clearly available and could easily have been undertaken or prescribed by appellee.

In *Reyes*, the court then let the jury decide whether the vaccine was the physical cause of the injury and whether an adequate warning would have led the plaintiff to change his behavior. Is this a higher or lower standard than in *MacDonald*? Note that the standard used is akin

to the informed consent test. Is that an appropriate duty for the manufacturer? Does that duty change if a learned intermediary is involved?

The *Reyes* court continued: "In the absence of evidence rebutting the presumption, a jury finding that the defendant's product was the producing cause of the plaintiff's injury would be sufficient to hold him liable." Does this presumption make sense if the background rate of infection from the "wild strain" is known on average to be 10 or 100 times as great as that from vaccines?

*Reyes* and *Davis* were first-generation cases in which no warnings had been provided. Subsequent litigation focused on the adequacy of the warnings. In Givens v. Lederle, 556 F.2d 1341, 1343 (5th Cir. 1977), another Sabin vaccine case, the defendant Lederle's warning to physicians stated in full:

> Paralytic disease following the ingestion of live polio virus vaccines has been reported in individuals receiving the vaccine, and in some instances, in persons who were in close contact with subjects who had been given live oral polio virus vaccine. Fortunately, such occurrences are rare, and it could not be definitely established that any such case was due to the vaccine strain and was not coincidental with infection due to naturally occurring poliomyelitis, or other enteroviruses.

The package insert also noted that the risk, if any, was one in three million. The physician who had inoculated the plaintiff's daughter gave the plaintiff no warning of the risk because he thought that the insert was too "nebulous" to require it. On appeal, the court held that his testimony, together with evidence showing that such infections had occurred, supported the jury's verdict that the warning was inadequate, especially because the warning denied any definite connection between the vaccine and the disease. Dr. Sabin had testified for the defendant that his vaccine could not possibly cause polio.

The number of large damage awards in the late 1970s and 1980s substantially increased the costs of vaccines. See Richard L. Manning, Changing Rules of Tort Law and the Market for Childhood Vaccines, 37 J.L. & Econ. 247, 248 (1994), whose econometric analysis shows that the price of the DPT vaccine between 1975 and 1990 increased by over 2,000 percent, and of that increase over 96 percent went to litigation costs.

In response to the crisis, Congress passed the National Childhood Vaccine Injury Act of 1986 (NCVIA), which provides for a complex system of no-fault compensation of up to $250,000 for persons who suffer particular side effects from certain vaccine programs within specified time limits. 42 U.S.C. §300aa (2024). The statute raises many of the hard issues of proof of causation found in other products liability settings.

**4.** ***Federal Liability for Bad Vaccines Under the Federal Tort Claims Act (FTCA).*** The U.S. Food and Drug Administration (FDA) has extensive regulatory authority over new vaccines and the power to approve or withhold the release of particular vaccines to the marketplace. At the same time, like other federal agencies, it receives the protection of the discretionary function exception to the FTCA, which insulates the government from liability if the action challenged in the case involves the permissible exercise of policy judgment. In Berkovitz v. United States, 486 U.S. 531, 542, 546 (1988), the infant plaintiff suffered a severe case of polio after ingesting a dose of Orimune manufactured by Lederle Laboratories, which settled with the plaintiff. The case involved a two-step process. First the Division of Biologic Standards (DBS) gave general licensing approval for production of the vaccine, after which the Bureau of Biologics (BoB) had responsibility for releasing particular lots of the vaccine. Marshall, J., first rejected the government's position that the discretionary function exception precludes liability for any and all acts arising out of the regulatory programs of federal agencies. He then concluded that the DBS was not protected by that exception when "the DBS issued a product license without first receiving data that the manufacturer must

submit showing how the product, at the various stages of the manufacturing process, matched up against regulatory safety standards" because the DBS has "no discretion to issue a license without first receiving the required test data." But with respect to the release of a particular lot, Marshall, J., held that "the discretionary function exception bars any claims that challenge the Bureau's formulation of policy as to the appropriate way in which to regulate the release of vaccine lots." Does that make sense if there are standard protocols that the BoB should use to decide whether or not to release vaccines? Or should the FDA receive a broader protection to encourage it to reduce erroneous releases by remaining in the inspection business, given the strict liability of the drug manufacturers?

**5. *Standardized Warnings.*** The decisions in both *MacDonald* and *Givens* that allow juries to treat FDA warnings as statutory minimums have prompted some legislative reform. Consider the Michigan Revised Judicature Act of 1961, Mich. Comp. Laws §600.2946(5) (2024), which allows for FDA warnings to be an absolute defense in duty to warn cases for drugs lawfully on the market unless the drug manufacturer during the drug approval process "intentionally withholds from or misrepresents" to the FDA information about the drug that results in it obtaining an approval that would have been denied if accurate information had been supplied. When the Michigan statute applies, a defendant can typically obtain summary judgment in a duty to warn case. Defenders of the statute point to the excessive risk aversion that the FDA has on the question of new drug approval. Opponents of the statute point to the serious gaps in the FDA approval process. For a review of the huge literature on this topic, see Catherine T. Struve, The FDA and the Tort System: Postmarketing Surveillance, Compensation, and the Role of Litigation, 5 Yale J. Health Pol'y L. & Ethics 587 (2005) (critical of the statute); and Lars Noah, Rewarding Regulatory Compliance: The Pursuit of Symmetry in Products Liability, 88 Geo. L.J. 2147 (2000) (supportive of the statute).

## *Vassallo v. Baxter Healthcare Corp.*

696 N.E.2d 909 (Mass. 1998)

Greaney, J. In this products liability case, the plaintiff Florence Vassallo claimed that the defendants, Baxter Healthcare Corporation and Baxter International, Inc., were liable to her for damages because silicone breast implants, manufactured by a predecessor company to the defendants (Heyer-Schulte Corporation), that had been implanted in her were negligently designed, accompanied by negligent product warnings, and breached the implied warranty of merchantability, with the consequence that she was injured. [The plaintiff underwent breast implant surgery in 1977, and her implants ruptured in 1992, and were replaced with saline implants in 1993. In 1976, the defendant's Dear Doctor letter did not address all possible adverse consequences that leakage could have on an implant user, including "risks of chronic inflammation, permanent tissue scarring, or possible effects on the immune system." The court reviews the plaintiff's expert evidence on the harm caused by the slow release of silicone gel. It also examines extensive testimony that Heyer-Schulte knew of the risk of rupture and of its adverse consequences. The plaintiff alleged that had she known of the true state of affairs, she would never have consented to the implants.] Plaintiff Vincent Vassallo claimed a loss of consortium. The plaintiffs also asserted a claim for violation of G.L. c. 93A, §§2(a) and 9. [The court affirms the judgment for the plaintiffs below on the negligence and statutory claims.]

We conclude, however, that we should change our products liability law to conform to the clear majority rule regarding what has to be shown to recover in a breach of warranty claim for failure to warn of risks associated with a product. . . .

We take this opportunity . . . to consider the defendants' argument that we should change our products liability law concerning the implied warranty of merchantability from what is stated in Hayes v. Ariens Co., 462 N.E.2d 273 (Mass. 1984), and that the law should be reformulated to adopt a "state of the art" standard that conditions a manufacturer's liability on actual or constructive knowledge of the risks.

Our current law, regarding the duty to warn under the implied warranty of merchantability, presumes that a manufacturer was fully informed of all risks associated with the product at issue, regardless of the state of the art at the time of the sale, and amounts to strict liability for failure to warn of these risks. This rule has been justified by the public policy that a defective product, "unreasonably dangerous due to lack of adequate warning[s], [is] not fit for the ordinary purposes for which [it is] used regardless of the absence of fault on [a defendant's] part."

At trial, [the judge followed *Hayes* by refusing to issue a "jury instruction that a manufacturer need only warn of risks 'known or reasonably knowable in light of the generally accepted scientific knowledge available at the time of the manufacture and distribution of the device.'"] While the judge's instruction was a correct statement of our law, we recognize that we are among a distinct minority of States that applies a hindsight analysis to the duty to warn.[17] . . .

The thin judicial support for a hindsight approach to the duty to warn is easily explained. The goal of the law is to induce conduct that is capable of being performed. This goal is not advanced by imposing liability for failure to warn of risks that were not capable of being known.

The Restatement (Third) of Torts: Products Liability §2(c) (1998), approved by the American Law Institute, reaffirms the principle expressed in Restatement (Second) of Torts, *supra* at §402A comment *j*, by stating that a product "is defective because of inadequate instructions or warnings when the foreseeable risks of harm posed by the product could have been reduced or avoided by the provision of reasonable instructions or warnings . . . and the omission of the instructions or warnings renders the product not reasonably safe." The rationale behind the principle is explained by stating that "[u]nforeseeable risks arising from foreseeable product use . . . by definition cannot specifically be warned against." Restatement (Third) of Torts: Products Liability, *supra* at §2 comment *m*, at 34. However, comment *m* also clarifies the manufacturer's duty "to perform reasonable testing prior to marketing a product and to discover risks and risk-avoidance measures that such testing would reveal. A seller is charged with knowledge of what reasonable testing would reveal." *Id*. . . .

In recognition of the clear judicial trend regarding the duty to warn in products liability cases, and the principles stated in Restatement (Third) of Torts: Products Liability, *supra* at §2 and comment *m*, we hereby revise our law to state that a defendant will not be held liable under an implied warranty of merchantability for failure to warn or provide instructions about risks that were not reasonably foreseeable at the time of sale or could not have been discovered by way of reasonable testing prior to marketing the product. A manufacturer will be held to the standard of knowledge of an expert in the appropriate field, and will remain subject to a continuing duty to warn (at least purchasers) of risks discovered following the sale of the product at issue. In accordance with the usual rule governing retroactivity in this type of action, the standard just expressed will apply to all claims on which a final judgment has not been entered, or as to which an appeal is pending or the appeal period has not expired, and to all claims on which an action is commenced after the release of this opinion. [The court notes that the defendant could not take advantage of this change in law because of the adverse jury

17. The Reporters' Note to the Restatement (Third) of Torts: Products Liability §2(c) comment *m*, at 106 (1998), lists four States taking the position that a manufacturer is charged with a duty to warn of risks without regard to whether the manufacturer knew or reasonably should have known of the risks, including Massachusetts; Hawaii; Pennsylvania; Washington.

verdict on the negligence count, and the jury's apparent conclusion that defendant did have actual or constructive notice of the risks associated with their silicone implants.]

[Affirmed.]

## NOTES

**1. *Post-Sale Duty to Warn.*** *Vassallo* recognizes a continuing duty to warn, even as it rejects a hindsight duty to warn. Assuming a company learns of a latent risk that had gone undiscovered despite reasonable pre-market testing, should it now have a duty to notify past buyers of the product of the newly discovered risk? See RTT: PL §10.

### RESTATEMENT OF THE LAW (THIRD) OF TORTS: PRODUCTS LIABILITY

#### §10. Liability of Commercial Product Seller or Distributor for Harm Caused by Post-Sale Failure to Warn

(a) One engaged in the business of selling or otherwise distributing products is subject to liability for harm to persons or property caused by the seller's failure to provide a warning after the time of sale or distribution of a product if a reasonable person in the seller's position would provide such a warning.

(b) A reasonable person in the seller's position would provide a warning after the time of sale if:

(1) the seller knows or reasonably should know that the product poses a substantial risk of harm to persons or property; and

(2) those to whom a warning might be provided can be identified and can reasonably be assumed to be unaware of the risk of harm; and

(3) a warning can be effectively communicated to and acted on by those to whom a warning might be provided; and

(4) the risk of harm is sufficiently great to justify the burden of providing a warning.

***Comment j. Distinguishing post-sale failures to warn from defects existing at the time of sale:*** When a product is defective at the time of sale, liability can be established without reference to a post-sale duty to warn. A seller who discovers after sale that its product was defective at the time of sale within the meaning of this Restatement cannot generally absolve itself of liability by issuing a post-sale warning.

RTT: PL §11 details the circumstances under which a manufacturer can be liable for a failure to recall. The Reporters delimited these sections as additional duties — not as a way for manufacturers to immunize themselves against liability for time-of-sale defects by issuing post-sale warnings. RTT: PL §10, cmt. *j*.

**2. *Unavoidably Dangerous Products.*** Closely related to RST §402A, comment *j*, is comment *k*, which deals with products known to be unavoidably dangerous, typically drugs. See *supra* at 65. In these cases, it is impractical to remove the product from the market or to alter its design or composition because mitigating the adverse side effects would undermine the effectiveness of the product. Consequently, a warning that allows informed consumer choice is the only workable alternative. Thus, in Nolen v. C.R. Bard Inc., 533 F. Supp. 3d 584, 592 (M.D. Tenn. 2021), Trauger, J., opined that, while defendant "may ultimately

be entitled to the protection of Comment k," the "availability of that protection" depends on whether defendant "adequately warned physicians regarding the heightened risks" of the product.

Similarly, in the case of blood transfusions, jurisdictions have rejected the strict liability position for contaminated blood so long as adequate warning is provided. In Brody v. Overlook Hospital, 317 A.2d 392, 395 (N.J. Super. Ct. App. Div. 1974), the court reasoned that donor blood is a medical necessity, and without the capacity to cheaply test it for diseases, it is unavoidably unsafe. More than forty states have enacted legislation adopting the negligence standard in blood transfusion cases, including Illinois. 745 Ill. Comp. Stat. 40/3 (2024).

## *Hood v. Ryobi America Corp.*

181 F.3d 608 (4th Cir. 1999)

Wilkinson, C.J. Wilson M. Hood lost part of his thumb and lacerated his leg when he removed the blade guards from his new Ryobi miter saw and then used the unguarded saw for home carpentry. Hood sued Ryobi, alleging that the company failed adequately to warn of the saw's dangers and that the saw was defective. Applying Maryland products liability law, the district court granted summary judgment to Ryobi on all claims.

The saw and owner's manual bore at least seven clear, simple warnings not to operate the tool with the blade guards removed. The warnings were not required to spell out all the consequences of improper use. Nor was the saw defective — Hood altered and used the tool in violation of Ryobi's clear warnings. Thus we affirm the judgment.

### I

Hood purchased a Ryobi TS-254 miter saw in Westminster, Maryland on February 25, 1995, for the purpose of performing home repairs. The saw was fully assembled at the time of purchase. It had a ten-inch diameter blade mounted on a rotating spindle controlled by a finger trigger on a handle near the top of the blade. To operate the saw, the consumer would use that handle to lower the blade through the material being cut.

Two blade guards shielded nearly the entire saw blade. A large metal guard, fixed to the frame of the saw, surrounded the upper half of the blade. A transparent plastic lower guard covered the rest of the blade and retracted into the upper guard as the saw came into contact with the work piece.

A number of warnings in the operator's manual and affixed to the saw itself stated that the user should operate the saw only with the blade guards in place. For example, the owner's manual declared that the user should "KEEP GUARDS IN PLACE" and warned: "ALWAYS USE THE SAW BLADE GUARD. Never operate the machine with the guard removed"; "NEVER operate this saw without all guards in place and in good operating condition"; and "WARNING: TO PREVENT POSSIBLE SERIOUS PERSONAL INJURY, NEVER PERFORM ANY CUTTING OPERATION WITH THE UPPER OR LOWER BLADE GUARD REMOVED." The saw itself carried several decals stating "DANGER: DO NOT REMOVE ANY GUARD. USE OF SAW WITHOUT THIS GUARD WILL RESULT IN SERIOUS INJURY"; "OPERATE ONLY WITH GUARDS IN PLACE"; and "WARNING . . . DO NOT operate saw without the upper and lower guards in place."

The day after his purchase, Hood began working with the saw in his driveway. While attempting to cut a piece of wood approximately four inches in height Hood found that the blade guards prevented the saw blade from passing completely through the piece. Disregarding the manufacturer's warnings, Hood decided to remove the blade guards from the saw.

Hood first detached the saw blade from its spindle. He then unscrewed the four screws that held the blade guard assembly to the frame of the saw. Finally, he replaced the blade onto the bare spindle and completed his cut.

Rather than replacing the blade guards, Hood continued to work with the saw blade exposed. He worked in this fashion for about twenty minutes longer when, in the middle of another cut, the spinning saw blade flew off the saw and back toward Hood. The blade partially amputated his left thumb and lacerated his right leg.

Hood admits that he read the owner's manual and most of the warning labels on the saw before he began his work. He claims, however, that he believed the blade guards were intended solely to prevent a user's clothing or fingers from coming into contact with the saw blade. He contends that he was unaware that removing the blade guards would permit the spinning blade to detach from the saw. But Ryobi, he claims, was aware of that possibility. In fact, another customer had sued Ryobi after suffering a similar accident in the mid-1980s. . . .

## II

A manufacturer may be liable for placing a product on the market that bears inadequate instructions and warnings or that is defective in design. Hood asserts that Ryobi failed adequately to warn of the dangers of using the saw without the blade guards in place. Hood also contends that the design of the saw was defective. We disagree on both counts.

### A

Hood first complains that the warnings he received were insufficiently specific. Hood admits that Ryobi provided several clear and conspicuous warnings not to operate the saw without the blade guards. He contends, however, that the warnings affixed to the product and displayed in the operator's manual were inadequate to alert him to the dangers of doing so. In addition to Ryobi's directive "never" to operate a guardless saw, Hood would require the company to inform of the actual consequences of such conduct. Specifically, Hood contends that an adequate warning would have explained that removing the guards would lead to blade detachment.

We disagree. Maryland does not require an encyclopedic warning. Instead, "a warning need only be one that is reasonable under the circumstances." Levin v. Walter Kidde & Co., 248 A.2d 151, 153 (Md. 1968). A clear and specific warning will normally be sufficient—"the manufacturer need not warn of every mishap or source of injury that the mind can imagine flowing from the product." Liesener v. Weslo, Inc., 775 F. Supp. 857, 861 (D. Md. 1991); see *Levin*, 248 A.2d at 154 (declining to require warning of the danger that a cracked syphon bottle might explode and holding "never use cracked bottle" to be adequate as a matter of law). In deciding whether a warning is adequate, Maryland law asks whether the benefits of a more detailed warning outweigh the costs of requiring the change.

Hood assumes that the cost of a more detailed warning label is minimal in this case, and he claims that such a warning would have prevented his injury. But the price of more detailed warnings is greater than their additional printing fees alone. Some commentators have observed that the proliferation of label detail threatens to undermine the effectiveness of warnings altogether. As manufacturers append line after line onto product labels in the quest for the best possible warning, it is easy to lose sight of the label's communicative value as a whole. Well-meaning attempts to warn of every possible accident lead over time to voluminous yet impenetrable labels—too prolix to read and too technical to understand.

By contrast, Ryobi's warnings are clear and unequivocal. Three labels on the saw itself and at least four warnings in the owner's manual direct the user not to operate the saw with the blade guards removed. Two declare that "serious injury" could result from doing so. This is not

a case where the manufacturer has failed to include any warnings at all with its product. Ryobi provided warnings sufficient to apprise the ordinary consumer that it is unsafe to operate a guardless saw—warnings which, if followed, would have prevented the injury in this case.

It is apparent, moreover, that the vast majority of consumers do not detach this critical safety feature before using this type of saw. Indeed, although Ryobi claims to have sold thousands of these saws, Hood has identified only one fifteen-year-old incident similar to his. Hood has thus not shown that these clear, unmistakable, and prominent warnings are insufficient to accomplish their purpose. Nor can he prove that increased label clutter would bring any net societal benefit. We hold that the warnings Ryobi provided are adequate as a matter of law.

**B**

Hood's defective design claim is likewise unpersuasive [on the ground that the product alterations defeat liability].

Affirmed.

## NOTES

**1.** ***Warnings, Design Modification, and the Heeding Presumption.*** In Liriano v. Hobart Corp., 700 N.E.2d 303, 308 (N.Y. 1998), the seventeen-year-old plaintiff caught his right hand and lower arm in a commercial meat grinding machine from which the employer had removed the safety guard. Unlike in *Hood*, no warnings stated that it was dangerous to remove the guard. On an advisory opinion of a certified question from the Second Circuit, Ciparick, J., held that a duty to warn cause of action could survive even in cases where a product modification blocked liability under a design defect theory. The court noted that if the injured person is

> fully aware of the hazard through general knowledge, observation or common sense, or participated in the removal of the safety device whose purpose is obvious, lack of a warning about that danger may well obviate the failure to warn as a legal cause of an injury resulting from that danger. . . . Similarly, a limited class of hazards need not be warned of as a matter of law because they are patently dangerous or pose open and obvious risks.

Nonetheless the court then returned the failure to warn cause of action for a "fact-specific" inquiry in the Second Circuit.

Next, in Liriano v. Hobart Corp., 170 F.3d 264 (2d Cir. 1999), Calabresi, J., upheld a jury verdict for the plaintiff (subject to a one-third reduction for comparative negligence) because the youthful plaintiff had only recently immigrated to the United States; had worked for his employer—Super Grocery Store—for only a week, and had never been given instructions on how to operate the grinder, which he had used only two or three times. In light of the variation in product users, some users might not discover dangers that others find obvious. Accordingly, Calabresi, J., held that the

> jury could reasonably find that there exist people who are employed as meat grinders and who do not know (a) that it is feasible to reduce the risk with safety guards, (b) that such guards are made available with grinders, and (c) that the grinders should be used only with the guards.

Calabresi, J., further held that, on the question of causation, the burden of proof shifted to the defendant:

> When a defendant's negligent act is deemed wrongful precisely because it has a strong propensity to cause the type of injury that ensued, that very causal tendency is evidence enough to

> establish a *prima facie* case of cause-in-fact. The burden then shifts to the *defendant* to come forward with evidence that its negligence was *not* such a but-for cause.

The heeding presumption received an extensive analysis in Foster v. Ethicon, Inc., 529 F. Supp. 3d 992, 1002 (D.S.D. 2021), where the plaintiff brought claims for complications resulting from the installation of Ethicon's pelvic mesh, a medical device that aims to repair defective tissue in the pelvis. In this case, the plaintiffs argued that the warnings given to the physicians were insufficient to convey the seriousness of the risk. Lange, C.J., regarded that as beside the point, for, as the defendant argued, "Ms. Foster cannot show causation because Dr. Ferrell [the treating physician] did not rely on the TVT's [implanted device] warnings and would have prescribed the TVT for Ms. Foster even if he had received an adequate warning." Lange, C.J., continued, "Ms. Foster is entitled to a rebuttable presumption that Dr. Ferrell would have read and heeded an adequate warning. As explained below, however, Ethicon has rebutted the presumption and Ms. Foster has failed to show a material question of fact on causation."

**2.** ***When Must a Warning Be Given? Latent Defects.*** In Ayers v. Johnson & Johnson Co., 818 P.2d 1337, 1341 (Wash. 1991) (en banc), David Ayers, then aged fifteen months, had taken an unmarked bottle of Johnson's baby oil out of the purse of his thirteen-year-old sister. Just as he began to drink the oil, his mother yelled at him, causing him to gasp and inhale the oil in his lungs. Once there, the baby oil coated his air sacs and quickly led to oxygen deprivation that resulted in serious injuries: His leg motions became spastic; he had limited control over his head movements; and he suffered brain impairment, seizures, and loss of the ability to speak.

Both sides agreed that once David inhaled the baby oil, no medical attention could have prevented these injuries. The plaintiff contended that a warning on the bottle was needed to alert users of this risk to keep baby oil out of the reach of infants in the first place. The plaintiff's mother testified that she read warnings, kept dangerous products away from her young children, and instructed her teenage daughters to do the same. Both mother and daughters testified that they thought baby oil could cause diarrhea or stomach upset, but not more serious injuries. Johnson & Johnson argued that it was rank speculation to claim that the additional knowledge would have led to different conduct because all members of the Ayers family knew that the baby oil was only for external use and was dangerous if taken internally. The jury found for the plaintiff, and its verdict was sustained on appeal:

> On the basis of this evidence, the jury was entitled to infer that if the Ayerses had known of the dangers of aspiration, they would have treated the baby oil with greater care; that they would have treated it with the caution they used in relation to items they recognized as highly dangerous, like cleaning products; and that had they done so, the accident would have never occurred. We conclude that the evidence of causation presented to the jury was sufficient to sustain the jury's verdict.

Should Johnson & Johnson change the warnings on its bottles? On its package inserts? If a warning should be included, what should it say?

**3.** ***Duty to Warn: Patent Defects.*** The risks in *Ayers* were both latent and remote. What ought to be done with respect to generic properties of common substances known to cause harm, such as alcohol? In Garrison v. Heublein, Inc., 673 F.2d 189, 189 (7th Cir. 1982), the court rejected the plaintiff's claim for "physical and mental injuries as a result of consuming the defendant's product [Smirnoff vodka] over a twenty-year period," holding that the defendant had no duty to warn of risks that were common knowledge.

Common knowledge, however, did not allow the defendant to obtain a summary judgment in Hon v. Stroh Brewery Co., 835 F.2d 510, 511 (3d Cir. 1987). The plaintiff's husband had died of pancreatitis that the plaintiff alleged had resulted mainly from his consumption of about eight to twelve cans of the defendant's beer each week over a period of several years.

*"Screens out harmful ultraviolet rays, conditions skin, repels insects, won't wash off while swimming, will not stain most fabrics. Warning: Contact with eyes, ears, nose, or mouth may be fatal."*

*Source: Edward Frascino / The New Yorker Collection / The Cartoon Bank*

The court accepted the plaintiff's claim that a warning was required because it was not common knowledge that "*either* excessive *or* prolonged, even though moderate, use of alcohol may result in diseases of many kinds, including pancreatic disease." The court rejected the defendant's comment *j* defense in part because the jury could find that Stroh's advertising campaign linked the consumption of large quantities of beer to the "good life." It found that "comment *j* does not say that whenever alcohol is consumed over a long period of time the dangers are necessarily generally known. Rather it says that *when* the danger is generally known, no warning is required." Note that federal regulations, 27 C.F.R. §16.21 (2024), now require the following warning label to be attached conspicuously to containers of alcoholic beverages sold:

> GOVERNMENT WARNING: (1) According to the Surgeon General, women should not drink alcoholic beverages during pregnancy because of the risk of birth defects. (2) Consumption of alcoholic beverages impairs your ability to drive a car or operate machinery, and may cause health problems.

## *Air & Liquid Systems Corp. v. DeVries*

586 U.S. 446 (2019)

Kavanaugh, J.

In maritime tort cases, we act as a common-law court, subject to any controlling statutes enacted by Congress. This maritime tort case raises a question about the scope of a manufacturer's duty to warn. The manufacturers here produced equipment such as pumps, blowers, and turbines for three Navy ships. The equipment required asbestos insulation or asbestos parts in order to function as intended. When used on the ships, the equipment released asbestos fibers into the air. Two Navy veterans who were exposed to asbestos on the ships developed cancer and later died. The veterans' families sued the equipment manufacturers, claiming that the manufacturers were negligent in failing to warn of the dangers of asbestos.

### II

. . . Maritime law has likewise recognized common-law principles of products liability for decades. See East River S. S. Corp., 476 U.S. at 865[, *supra* Chapter 1, Note, at 6].

In this negligence case, we must decide whether a manufacturer has a duty to warn when the manufacturer's product requires later incorporation of a dangerous part — here, asbestos — in order for the integrated product to function as intended.

We start with basic tort-law principles. Tort law imposes "a duty to exercise reasonable care" on those whose conduct presents a risk of harm to others. Restatement (Third) of Torts: Liability for Physical and Emotional Harm §7, p. 77 (2005). For the manufacturer of a product, the general duty of care includes a duty to warn when the manufacturer "knows or has reason to know" that its product "is or is likely to be dangerous for the use for which it is supplied" and the manufacturer "has no reason to believe" that the product's users will realize that danger. Restatement (Second) of Torts §388, p. 301 (1963–1964).

In tort cases, the federal and state courts have not reached consensus on how to apply that general tort-law "duty to warn" principle when the manufacturer's product requires later incorporation of a dangerous part in order for the integrated product to function as intended. Three approaches have emerged.

The first approach is the more plaintiff-friendly foreseeability rule that the Third Circuit adopted in this case: A manufacturer may be liable when it was foreseeable that the manufacturer's product would be used with another product or part, even if the manufacturer's product did not require use or incorporation of that other product or part.

The second approach is the more defendant-friendly bare-metal defense that the manufacturers urge here: If a manufacturer did not itself make, sell, or distribute the part or incorporate the part into the product, the manufacturer is not liable for harm caused by the integrated product — even if the product required incorporation of the part and the manufacturer knew that the integrated product was likely to be dangerous for its intended uses.

The third approach falls between those two approaches. Under the third approach, foreseeability that the product may be used with another product or part that is likely to be dangerous is not enough to trigger a duty to warn. But a manufacturer does have a duty to warn when its product requires incorporation of a part and the manufacturer knows or has reason to know that the integrated product is likely to be dangerous for its intended uses. Under that approach, the manufacturer may be liable even when the manufacturer does not itself incorporate the required part into the product.

We conclude that the third approach is the most appropriate for this maritime tort context.

To begin, we agree with the manufacturers that a rule of mere foreseeability would sweep too broadly. See generally Restatement (Third) of Torts: Liability for Physical and Emotional Harm §7, Comment j, at 82; Restatement (Second) of Torts §395, Comment j, at 330. Many products can foreseeably be used in numerous ways with numerous other products and parts. Requiring a product manufacturer to imagine and warn about all of those possible uses — with massive liability looming for failure to correctly predict how its product might be used with other products or parts — would impose a difficult and costly burden on manufacturers, while simultaneously overwarning users. In light of that uncertainty and unfairness, we reject the foreseeability approach for this maritime context.

That said, we agree with the plaintiffs that the bare-metal defense ultimately goes too far in the other direction. In urging the bare-metal defense, the manufacturers contend that a business generally has "no duty" to "control the conduct of a third person as to prevent him from causing physical harm to another." *Id.*, §315, at 122. That is true, but it is also beside the point here. After all, when a manufacturer's product is dangerous in and of itself, the manufacturer "knows or has reason to know" that the product "is or is likely to be dangerous for the use for which it is supplied." *Id.*, §388, at 301. The same holds true, we conclude, when the manufacturer's product requires incorporation of a part that the manufacturer knows or has reason to know is likely to make the integrated product dangerous for its intended uses.

As a matter of maritime tort law, we find no persuasive reason to distinguish those two similar situations for purposes of a manufacturer's duty to warn. See Restatement (Third) of Torts: Products Liability §2, Comment i, p. 30 (1997) ("[W]arnings also may be needed to inform users and consumers of nonobvious and not generally known risks that unavoidably inhere in using or consuming the product").

Importantly, the product manufacturer will often be in a better position than the parts manufacturer to warn of the danger from the integrated product. See generally G. Calabresi, The Costs of Accidents 311–318 (1970). The product manufacturer knows the nature of the ultimate integrated product and is typically more aware of the risks associated with that integrated product. By contrast, a parts manufacturer may be aware only that its part could conceivably be used in any number of ways in any number of products. A parts manufacturer may not always be aware that its part will be used in a way that poses a risk of danger.

To be sure, as the manufacturers correctly point out, issuing a warning costs time and money. But the burden usually is not significant. Manufacturers already have a duty to warn of the dangers of their own products. That duty typically imposes a light burden on manufacturers. Requiring a manufacturer to also warn when the manufacturer knows or has reason to know that a required later-added part is likely to make the integrated product dangerous for its intended uses should not meaningfully add to that burden. . . .

The manufacturers further assert that requiring a warning in these circumstances will lead to excessive warning of consumers. Again, however, we are not aware of substantial overwarning problems in those jurisdictions that have adopted this approach. And because the rule we adopt here applies only in certain narrow circumstances, it will not require a plethora of new warnings. . . .

In the maritime tort context, we hold that a product manufacturer has a duty to warn when (i) its product requires incorporation of a part, (ii) the manufacturer knows or has reason to know that the integrated product is likely to be dangerous for its intended uses, and (iii) the manufacturer has no reason to believe that the product's users will realize that danger.

[Affirmed.]

Gorsuch, J., dissenting:

. . . [T]he traditional common law rule still makes the most sense today. The manufacturer of a product is in the best position to understand and warn users about its risks; in the language of law and economics, those who make products are generally the least-cost avoiders of their risks. By placing the duty to warn on a product's manufacturer, we force it to internalize the full cost of any injuries caused by inadequate warnings—and in that way ensure it is fully incentivized to provide adequate warnings. By contrast, we dilute the incentive of a manufacturer to warn about the dangers of its products when we require other people to share the duty to warn and its corresponding costs.

## NOTES

**1. *"Third Wave" of Asbestos Litigation?*** Asbestos fits within the category of "unavoidably dangerous products," *supra*, because it is both highly useful as an insulation product and because it undeniably causes many fatal conditions—chief among them asbestosis, mesothelioma, and bronchogenic carcinoma. Manufacturers have a duty to warn, even though they may be shielded from design defect liability. The watershed case is Borel v. Fibreboard Paper Products Corp., 493 F.2d 1076 (5th Cir. 1973), which affirmed a jury verdict against asbestos

manufacturers on behalf of an insulation worker who had extensive contact with asbestos for more than 30 years. Wisdom, J., in an exhaustive opinion, found sufficient evidence of the dangers of asbestos in the medical literature to impose on manufacturers—here held to the standard of "experts" in the field—a duty to warn all workers coming in contact with the product to allow them to make an informed choice of whether to expose themselves to asbestos.

Prior to *Borel*, no plaintiff had ever recovered from an asbestos manufacturer. The decision unleashed an avalanche of suits against asbestos suppliers. The first generation of asbestos cases was brought against the manufacturers of asbestos products, virtually all of whom were driven into bankruptcy. One early case suggested that manufacturers could have been held responsible for unknowable defects. See Beshada v. Johns-Manville Prods. Corp., 447 A.2d 539 (N.J. 1982). But this push for strict liability for asbestos was rejected, just as it was for medical products in *Vassallo*. See, e.g., Anderson v. Owens-Corning Fiberglass Corp., 810 P.2d 549, 558–59 (Cal. 1991). In both cases, however, plaintiffs consistently won on negligence theories and often obtained hefty punitive damages.

The second wave of litigation, which began in the late 1990s, pushed further with suits against second-tier defendants, such as firms that operated premises on which asbestos products were used or which incorporated asbestos into their own products (e.g., brake linings). Typically, these cases did not involve asbestosis, but rather evidence of pleural plaque. "Pleural plaques have been described as 'discrete, elevated, opaque, shiny, rounded lesions, . . . diffuse or nodular,' of the parietal pleura or diaphragm. They strongly indicate asbestos exposure." Peter H. Schuck, The Worst Should Go First: Deferral Registries in Asbestos Litigation, 15 Harv. J.L. & Pub. Pol'y 541, 545 (1992). Although these plaques indicate exposure, they do not increase the risk of deadly asbestosis or any other deadly disease. See William Weiss, Asbestos-Related Pleural Plaques and Lung Cancer, 103 Chest. 1854 (1993).

An effort to forge a class action settlement of these cases was rejected in Amchem Products, Inc. v. Windsor, 521 U.S. 591 (1997), partly on the ground that it did not provide adequate safeguards for future injured persons. See also Ortiz v. Fibreboard Corp., 527 U.S. 815 (1999). The matter has now spilled over into the political arena, but Congress thus far has been unable to fashion any solution that satisfies the plaintiffs, the various asbestos defendants, and their insurers.

**2. *Warnings and Consumer Behavior.*** Troy A. Paredes, Blinded by the Light: Information Overload and Its Consequences for Securities Regulation, 81 Wash. U. L.Q. 417, 440–43 (2003), argues that consumers tend to make poorer choices as the amount of available information increases: "[A]s more information becomes available, a person might use less information, on net, as the information search and processing costs increase. Making matters worse, studies show that people do not always focus on the most relevant information but might become distracted by less relevant information." Posner, J., took Paredes's message to heart in Robinson v. McNeil Consumer Healthcare, 615 F.3d 861, 869 (7th Cir. 2010), which rejected the plaintiff's claim against the manufacturer of an ibuprofen drug for failing to warn against SJS/TEN, a very rare but serious skin disease that caused blindness in one eye and the loss of 60 percent of the plaintiff's skin:

> [T]he label would have had to describe as well every other serious disease that might, however infrequently, be caused, or even just arguably caused (for it is unclear whether ibuprofen can cause SJS/TEN), by ibuprofen. And it would have to recite the symptoms of the disease if it was rare. The resulting information overload would make label warnings worthless to consumers.

The impatience with warnings received a very different spin in Howard A. Latin, Good Warnings, Bad Products, and Cognitive Limitations, 41 UCLA L. Rev. 1193 (1994). Latin rejects the "Rational Risk Calculator Model" of human behavior, often championed by

economists, in favor of the rival "Mistake and Momentary Inattention" model. This model draws more heavily on psychological and sociological literature to support the view that even cautious actors are subject to momentary lapses in judgment or attention. Latin strongly supports this second perspective, which clearly implies that even "good" warnings should not be respected when cheap design alternatives are available to protect the users of products from the disastrous consequences of not heeding a warning. Latin's object of attack is Restatement §402A, comment *j*: "Where warning is given, the seller may reasonably assume that it will be read and heeded." If the Mistake and Momentary Inattention model is correct, Latin argues the law should require design changes no matter how strong or "good" the warnings are.

Latin's prescriptions were followed in Uniroyal Goodrich Tire Co. v. Martinez, 977 S.W.2d 328, 337 (Tex. 1998), in which the plaintiff mechanic was injured when a 16-inch tire exploded while he sought to mount it on a 16.5-inch wheel in the face of stern "NEVERS," beginning with "NEVER MOUNT A 16" SIZE DIAMETER TIRE ON A 16.5" RIM. Mounting a 16" tire on a 16.5" rim can cause severe injury or death." Phillips, C.J., rejected the test of section 402A, comment *j*, and, citing Latin, adopted the position of the Third Restatement §2, comment *l*, "that warnings and safer alternative designs are factors, among others, for the jury to consider in determining whether the product as designed is reasonably safe." Who is right? Does Latin's approach work for dangerous drugs, or only consumer products? As a variation on the warnings question, what should be done with Q-Tips or other cotton swabs whose standard warnings instruct people never to insert them into the ear? Is the correct remedy to redesign the Q-Tip, strengthen the warning, take the product off the market, or keep the status quo?

## SECTION E. WHO IS A PRODUCT SELLER?

Second Restatement §402A only applies to sellers who are "engaged in the business of selling . . . a product."

### *Loomis v. Amazon.com LLC*

277 Cal. Rptr. 3d 769 (Ct. App. 2021)

Ohta, J. Kisha Loomis brought suit against Amazon.com LLC (Amazon) for injuries she suffered from an allegedly defective hoverboard. The hoverboard was sold by a third party seller named TurnUpUp through the Amazon website. The trial court granted summary judgment in favor of Amazon. The primary issue on appeal is whether Amazon may be held strictly liable for Loomis's injuries from the defective product. . . . We reverse and remand with directions.

#### Facts

Loomis ordered a hoverboard on Amazon's website on November 28, 2015. The listing identified the seller to be TurnUpUp, a name used by SMILETO to sell its products on Amazon's marketplace. SMILETO is allegedly a company based in China. . . . Loomis gifted the hoverboard to her son. On New Year's Eve, he plugged it into an outlet in Loomis's bedroom to charge. Loomis's boyfriend later discovered a fire burning in her bedroom. Her bed and the hoverboard were on fire. Loomis suffered burns to her hand and foot as a result of fighting the fire. . . .

Amazon.com is an online marketplace where Amazon and third party sellers list their products for sale. Amazon describes its marketplace as "an online mall" which provides an "online storefront" to third party sellers. Where Amazon is the seller of a product, it is

identified as the seller on the product detail page, and it sources the product, sets the price, and holds title to it. This case does not involve an Amazon-listed product. Where a third party is the seller, it is identified as such on the product detail page and again on the order confirmation page before the user places the order. The third party sources the product, sets the price, and holds title to it.

All third party sellers operate under the Amazon services business solutions agreement (BSA). . . .

## Analysis

### Vertical Chain of Distribution

As technology advances, innovation is paving the way to new business practices. Amazon is on the leading edge of e-commerce. Based on our review of Amazon's third party business model under the BSA, we are persuaded that Amazon's own business practices make it a direct link in the vertical chain of distribution under California's strict liability doctrine.

Contrary to Amazon's assertion that it merely provided an online storefront for TurnUpUp and others to sell their wares, it is undisputed Amazon placed itself squarely between TurnUpUp, the seller, and Loomis, the buyer, in the transaction at issue. When Loomis wanted to buy a hoverboard for her son, she perused product listings on Amazon's website. Amazon took Loomis's order and processed her payment. It then transmitted the order to TurnUpUp, who packaged and shipped the product to Loomis. . . . TurnUpUp was not allowed to communicate with Loomis directly. If Loomis had wanted to return the hoverboard, the return would have been routed through Amazon.

Amazon remitted Loomis's payment to TurnUpUp after deducting its fees, including a 15 percent referral fee based on the total sale price. These facts undermine Amazon's characterization of its marketplace as an online mall providing online storefronts for sellers. Owners of malls typically do not serve as conduits for payment and communication in each transaction between a buyer and a seller. Moreover, they do not typically charge a per-item fee rather than a fixed amount to rent their storefronts. Instead, these actions — (1) interacting with the customer, (2) taking the order, (3) processing the order to the third party seller, (4) collecting the money, and (5) being paid a percentage of the sale — are consistent with a retailer or a distributor of consumer goods.

### Stream of Commerce Approach

Although we conclude Amazon is a link in the vertical chain of distribution, we nevertheless recognize e-commerce may not neatly fit into a traditional sales structure. The stream of commerce approach or market enterprise theory offers an alternative basis for strict liability. . . . [A] defendant may be strictly liable under the stream of commerce approach if:

(1) the defendant received a direct financial benefit from its activities and from the sale of the product;
(2) the defendant's role was integral to the business enterprise such that the defendant's conduct was a necessary factor in bringing the product to the initial consumer market; and
(3) the defendant had control over, or a substantial ability to influence, the manufacturing or distribution process.

[The court then holds that the 15 percent referral fee satisfied the first condition; it holds that the second issue was triable because "it has presented no evidence of its role in bringing TurnUpUp's hoverboards to market." It then holds that the third factor was satisfied because Amazon could exert influence over the process thanks to its "ability to require safety certification, indemnification, and insurance before it agrees to list any product."]

**Policy Considerations Underlying the Doctrine Are Furthered by Imposing Strict Products Liability in This Case**

In analyzing whether strict liability is appropriate in new circumstances, courts assess whether relevant public policy goals are furthered by its application. . . . [T]he relevant public policy considerations are:

(1) Whether Amazon may play a substantial part in insuring that the product is safe or may be in a position to exert pressure on the manufacturer to that end;
(2) Whether Amazon may be the only member in the distribution chain reasonably available to the injured plaintiff; and
(3) Whether Amazon is in a position to adjust the costs of compensating the injured plaintiff amongst various members in the distribution chain.

We address each in turn.

[Ohta, J., holds that the limited steps that Amazon could take satisfied the first test, and predicts that a strict liability rule will encourage Amazon to "expand its safety compliance requirement, and to use its "gatekeeper" rule to pressure upstream suppliers to take additional precautions.]

As to consumer compensation, Amazon may be the only member of the distribution chain reasonably available for an injured consumer to recover damages. Amazon contends there is no evidence to show how frequently an injured plaintiff is truly left without recourse. The record shows, however, that Forrinx, the only other defendant in this matter, failed to appear and a default was taken against it. . . .

As to loss spreading, Amazon can adjust the costs of consumer protection between it and third party sellers through its fees, indemnity requirements, and insurance. . . .

Accordingly, we hold the application of strict liability to Amazon's third party seller business model is supported by the relevant public policy considerations[.]

Wiley, J., concurring. [W]e have an easy case that beautifully illustrates the deep structure of modern tort law: a judicial quest to minimize the social costs of accidents — that is, the sum of the cost of accidents and the cost of avoiding accidents. Judges have been applying this social cost-benefit analysis as a felt instinct for a long time. . . . That deep structure makes this case simple to decide. When efforts to minimize accident costs are relatively inexpensive and apt to be effective, courts impose tort duties. Amazon has cost-effective options for minimizing accident costs. Amazon therefore has a duty in strict liability to the buyers from its site, including Kisha Loomis. . . .

Amazon's options are practical and cost-effective; indeed, Amazon says it is *already* taking these actions. Amazon thus must face strict liability for Loomis's fiery encounter with the hoverboard she bought from Amazon's site. Imposing this duty on Amazon creates financial incentives that back up Amazon's good words about its concern for customer safety.

Some suggest considerations of moral justice can compete with tort law's calculus of social benefit. . . . If they ever do, moral justice and cost-benefit analyses do not conflict in this case.

## *Amazon, Inc. v. McMillan*

625 S.W.3d 101 (Tex. 2021)

Busby, J. Texas law imposes strict liability on manufacturers and some sellers of defective products. . . . The Fifth Circuit asks whether Amazon.com is a "seller" under Texas law when

it does not hold title to third-party products sold on its website but controls the process of the transaction and delivery.

We answer no. The Legislature's definition of "seller" in Chapter 82 of the Civil Practice and Remedies Code is consistent with and does not expand the common-law definition. Under that definition, when the ultimate consumer obtains a defective product through an ordinary sale, the potentially liable sellers are limited to those who relinquished title to the product at some point in the distribution chain. Therefore, Amazon is not a "seller" of third-party products under Texas law.

## Background

. . . Amazon's online retail marketplace offers Amazon-branded products, third party-branded products owned by Amazon and listed on the website as "sold by" Amazon, and products owned and "sold by" third parties. According to the website's "Conditions of Use," to which all customers must agree when making a purchase, Amazon makes no warranties for products "sold by" third-party merchants and disclaims responsibility for third-party product descriptions. Other than a short line of text under the "buy" button identifying the seller, the experience of purchasing products "sold by" third-party merchants is no different from buying products "sold by" Amazon. When a customer purchases a third-party product listed on Amazon.com, Amazon processes payment, retains a portion of the purchase price, and remits the remainder to the third-party merchant.

A third-party merchant who sells a product through Amazon.com may store and ship that product itself or use the Fulfillment by Amazon (FBA) logistics service. Under FBA, the merchant uses Amazon warehouses to store product inventory, and Amazon packages a product when it is sold and delivers it to a carrier for shipment to the purchaser. The merchant retains title to its products prior to the ultimate customer purchase. But Amazon maintains significant control over products sold through FBA. Amazon has the ability to refuse products and controls all aspects of customer service. Amazon also processes returns and delivers customer refunds for FBA products, and merchants must reimburse Amazon for these costs.

This suit concerns a product "sold by" a third-party merchant that used the FBA service. According to the allegations of the complaint filed in federal court, Morgan McMillan's husband purchased a remote control on Amazon.com that was "sold by" "USA Shopping 7693." Almost a year later, McMillan's nineteen-month-old daughter opened the remote's battery compartment and swallowed the included button battery. Though the battery was surgically removed, battery fluid caused permanent damage to the child's esophagus. When McMillan sought information from Amazon about "USA Shopping 7693," Amazon identified the account as belonging to Hu Xi Jie, an FBA user with an address in China. Amazon subsequently suspended Hu Xi Jie's account and removed the remote from its website.

McMillan sued both Amazon and Hu Xi Jie in the U.S. District Court for the Southern District of Texas, alleging, among other causes of action, strict liability for design and marketing defects. McMillan attempted to serve Hu Xi Jie through the Texas Secretary of State, *see* Tex. Civ. Prac. & Rem. Code § 17.044(b), but Hu Xi Jie did not answer or make an appearance. At the close of discovery, Amazon moved for summary judgment on the ground that it was not a seller of the remote and therefore could not be held strictly liable. . . .

The district court denied Amazon's motion for summary judgment.

. . . [T]he Fifth Circuit certified the following question to this Court, which we accepted:

Under Texas products-liability law, is Amazon a "seller" of third-party products sold on Amazon's website when Amazon does not hold title to the product but controls the process of the transaction and delivery through Amazon's Fulfillment by Amazon program?

### Analysis

#### II. The Statutory Meaning of "Seller" in Chapter 82 is Consistent with Our Cases and the Restatements

Before the Legislature adopted the Texas Products Liability Act, sellers of defective products could be held strictly liable under the common law. See Restatement (Second) of Torts § 402A. Under the Act, codified as Chapter 82 of the Civil Practice and Remedies Code, the general rule is the opposite: a non-manufacturing seller "is not liable for harm caused . . . by [a] product unless the claimant proves" that one of the enumerated exceptions applies. Tex. Civ. Prac. & Rem. Code § 82.003.

Although the extent of seller liability is different under the common law and Chapter 82, the definition of who constitutes a seller is similar. The statute defines a seller as "a person who is engaged in the business of distributing or otherwise placing, for any commercial purpose, in the stream of commerce for use or consumption a product or any component part thereof." Id. § 82.001(3). To decide whether Amazon is a seller under Chapter 82, we must determine whether Amazon's role in the distribution chain amounts to "distributing or otherwise placing" a product in the stream of commerce. . . .

#### III. Chapter 82 Does Not Expand Liability for Those Not Considered Sellers Under the Common Law

McMillan argues that our common-law cases require "only possession at the time of sale, not title," to be considered a seller. . . . She likewise contends that "Chapter 82 does not require [a seller] to have title or ownership interest in the products sold."

McMillan's arguments are incorrect because they attempt to commingle principles that our sale and non-sale cases have kept separate. In cases where an ordinary sale takes place, we have never held that a seller can be anyone other than the person or entity who relinquishes title. And nothing in Chapter 82 signals that the Legislature intended to expand seller liability beyond that available under the common law.

Chapter 82 is a liability-restricting statute. As noted above, it provides that non-manufacturing sellers are not liable for product defects unless one of the enumerated exceptions applies. Thus, Chapter 82 does not expand the pool of potentially liable non-manufacturing sellers beyond those recognized at common law; it reduces that pool.

Given that Chapter 82 is more restrictive than the common law, we see no indication that the Legislature intended for "distributing or otherwise placing" to include commercial behavior beyond ordinary sales and previously qualifying non-sale commercial transactions. Accordingly, the necessary qualities of those transactions provide the limits of "seller" status under Chapter 82. Our cases show that both sales and non-sale commercial transactions, at a minimum, involve sellers that hold or relinquish title in a product's distribution chain.

When the facts involve a sale in the ordinary sense, none of our cases have suggested that anyone other than a person or entity who has *relinquished* title in the chain can be a "seller." . . .

Likewise, when a non-sale commercial transaction occurs, none of our cases have suggested that anyone other than those who have at least *held* title in the chain can be a seller. . . . Our cases and Chapter 82's language indicate that ordinary sales and non-sale commercial transactions are distinct from one another; there is no indication that the Legislature intended for non-sale concepts to apply when a sale occurs. . . .

Considering title to determine seller status is also consistent with the approach taken by other jurisdictions that follow the Restatement's framework for strict products liability. Using this approach, many courts have concluded that Amazon is not a seller when it does not hold or relinquish title to the product. See, e.g., State Farm Fire & Cas. Co. v. Amazon.com,

Inc., 835 F. App'x 213, 216 (9th Cir. 2020) (holding that Amazon was not a "seller" under Arizona's common-law Restatement-based multi-factor test, under which holding title is a factor); Erie Ins. Co. v. Amazon.com, Inc., 925 F.3d 135, 144 (4th Cir. 2019) (concluding that Amazon did not hold title and thus was not a "seller" under Maryland law, which is based on Restatement section 402A); Eberhart v. Amazon.com, Inc., 325 F. Supp. 3d 393, 397–98 (S.D.N.Y. 2018) (concluding that "regardless of what attributes are necessary to place an entity within the chain of distribution, the failure to take title to a product places that entity on the outside," and such a requirement is reinforced by the Restatement (Third) of Torts: Products Liability); but see State Farm Fire & Cas. Co. v. Amazon.com Servs., Inc., 70 Misc.3d 697, 137 N.Y.S.3d 884, 889 (Sup. Ct. 2020) (disagreeing with *Eberhart* that title is dispositive under New York law).

In sum, we conclude that when a product-related injury arises from a transaction involving a sale, sellers are those who have relinquished title to the allegedly defective product at some point in the chain of distribution. The rule that a person need not transfer title to be held strictly liable is limited to non-sale commercial transactions.

### IV. Amazon Is Not a "Seller" Under Texas Law When It Does Not Hold or Relinquish Title to an Allegedly Defective Product

Having explained the relevant legal principles, we next apply those principles to answer the Fifth Circuit's question. Here, the summary-judgment evidence shows that the distribution chain concluded with a sale to the consumer: McMillan obtained title to the remote for a price. She did not engage in a non-sale commercial transaction, such as receiving the remote through a lease or as a promotional sample. Therefore, Amazon is a "seller" if it either made the ultimate sale to McMillan or relinquished title at some point upstream in the distribution chain. Amazon did neither.

First, Amazon did not make the ultimate consumer sale because Amazon did not hold title to the remote and relinquish it to McMillan; Hu Xi Jie held title at the time of transfer. McMillan argues that Amazon's Conditions of Use—which provide for transfer of title upon Amazon's delivery of a product to the shipping company—establish that Amazon transferred title to her. But Amazon's ability to transfer title from Hu Xi Jie to a purchaser does not confer title on Amazon. Amazon's possession and transfer of Hu Xi Jie's products could be considered an entrustment, but entrustments do not make an entrustee a "seller" for strict-liability purposes. . . .

Second, there is no evidence that Amazon held or relinquished title to the remote at any point upstream from the sale to McMillan. As an FBA user, Hu Xi Jie maintained title to the inventory even while Amazon had possession. Possession followed by a transfer of title between third parties does not constitute a sale. In fact, none of Amazon's upstream actions—such as web hosting, advertising, marketing, warehousing, payment processing, and shipping—constituted a sale under Texas law. . . . Nor does considering these actions together change the result. By offering a suite of marketing, financing, and logistics services to third-party sellers, Amazon has developed a business model that is not title dependent. And though Amazon's business model gives the company a significant amount of control over the process of the transaction and the delivery of the product, this control does not transform an otherwise non-title-holding sales facilitator into a "seller." . . .

Because McMillan obtained the remote through a transfer of title for a price, and Amazon did not hold or relinquish title at any point in the remote's distribution chain, Amazon was not "engaged in the business of distributing or otherwise placing" the remote into the stream of commerce. On this record, therefore, Amazon is not a chapter 82 seller under Texas law. . . .

## NOTES

**1. *Online Platforms: The Fifth Stage of Products Liability?*** Catherine M. Sharkey, Products Liability in the Digital Age: Online Platforms as "Cheapest Cost Avoiders," 73 Hastings L.J. 1327 (2022), heralds the arrival of a new stage of products liability in the digital age. *Loomis* fits the pattern that, at each new juncture,

> judges have relied explicitly on deterrence, or prevention of harm, rationales to address new forms of risks and prevent them from materializing into harms. This is no less true as we enter a new stage of digital e-commerce risks faced by society in the 21st century.

Catherine M. Sharkey, The Irresistible Simplicity of Preventing Harm, 16 J. Tort L. 143, 151 (2023). Aaron D. Twerski & Edward J. Janger, The Heavy Hand of Amazon: A Seller Not a Neutral Platform, 14 Brook. J. Corp. Fin. & Com. L. 259, 267 (2020), likewise prods courts to recognize how "Amazon itself controls access to the site, the manner in which the items are displayed, and receives compensation at every stage. In fact, except for the formality of title, the level of integration in Amazon's supply chain is comparable to that of a standard brick-and-mortar seller."

Whereas *Loomis* relied on the common law evolution of products liability in California, *McMillan* declined to find liability under Texas's product liability statute. See also Stiner v. Amazon.com, Inc., 164 N.E.3d 394 (Ohio 2020). On a certified question of law, the Supreme Court of Louisiana held that under the Louisiana Products Liability Act, "the operator of an online marketplace is a 'seller' of third-party products sold in its marketplace when the operator did not hold title to the product but: (i) had physical custody of the product in its distribution warehouse; and (ii) controlled the process of the transaction and delivery through its product fulfillment program." *Pickard v. Amazon.com, Inc.*, 387 So.3d 515 (La. June 28, 2024).

Given the volume and diversity of merchant offerings, is Amazon in the best position to eliminate the unsafe character of products in the first instance? Would adding a vetting process for merchants hinder the business prospects of new or small merchants? What about requiring foreign sellers to designate domestic parties who could then bear liability?

**2. *Liability of Retailers and Distributors.*** Products liability law has long applied uniformly to all ordinary product retailers and distributors in the initial chain of distribution. Traynor, J., made this case in Vandermark v. Ford Motor Co., 391 P.2d 168, 171–72 (Cal. 1964), holding an automobile dealer strictly liable for product defects:

> Retailers like manufacturers are engaged in the business of distributing goods to the public. They are an integral part of the overall producing and marketing enterprise that should bear the cost of injuries resulting from defective products. In some cases the retailer may be the only member of that enterprise reasonably available to the injured plaintiff. In other cases the retailer himself may play a substantial part in insuring that the product is safe or may be in a position to exert pressure on the manufacturer to that end; the retailer's strict liability thus serves as an added incentive to safety. Strict liability on the manufacturer and retailer alike affords maximum protection to the injured plaintiff and works no injustice to the defendants, for they can adjust the costs of such protection between them in the course of their continuing business relationship.

Does *Vandermark* require liability in *Loomis*?

The Consumer Product Safety Commission concluded that Amazon is a distributor under the CPSA with respect to products "sold through its Fulfilled by Amazon program," writing that "[t]he substantial record before us establishes Amazon's extensive control over these products, beginning with receipt of a Fulfilled by Amazon participant's products at an Amazon distribution center, and storage of this inventory until it is purchased by and

shipped to a consumer." Amazon.com, Inc., CPSC Docket No. 21-2, at 1, 3–6, 26–27, 44 (July 30, 2024). As a distributor, sections 15(c) and 15(d) of the CPSA authorize the CPSC to require Amazon to make various notifications and take remedial actions in the public interest, potentially concerning an untold number of products. To what extent does this statutory designation as a "distributor" establish Amazon's status as an upstream distributor for products liability claims?

The Third Restatement follows the Second, as product sellers include "nonmanufacturing sellers and distributors such as wholesalers and retailers," RTT: PL §1, comment *e*, even when they act as mere conduits that do nothing to make the products dangerous. In addition, section 20, comment *f*, treats commercial lessors and bailors as product sellers, such that a dealer will be held to the same rules when he allows a test drive as when he sells a car. Section 2, comment *o*, acknowledges that nonmanufacturing sellers "often are not in a good position feasibly to adopt safer product designs or better instructions or warnings." But it reiterates that nonmanufacturing sellers are nonetheless subject to the same standards applicable to manufacturers: "As long as the plaintiff establishes that the product was defective when it left the hands of a given seller in the distributive chain, liability will attach to that seller." §2, cmt. *c.* Should a retailer be liable if it has no control over the manufacture, design, or warnings associated with a given product? What might the safety implications be?

In Defries v. Yamaha Motor Corp., 300 Cal. Rptr. 3d 670, 678 (Ct. App. 2022), Raphael, J., over a strong dissent, extended *Vandermark* and section 2, comment *c*, to hold that an upstream distributor "had a nondelegable duty to deliver a dirt bike to [the plaintiff] free from dangerous defects, regardless of whether those defects were caused by . . . one of [its] dealers in the final assembly." How is a distributor of partially unassembled products to monitor the quality of a downstream dealer's assembly? Is there an indemnity over?

Some cases have imposed liability on parties involved in only a fraction of the production cycle. In Sprung v. MTR Ravensburg, Inc., 788 N.E.2d 620, 623 (N.Y. 2003), Kaye, J., applied a strict liability regime to a custom fabricator for General Motors, arguing:

> Like other manufacturers, custom fabricators engaged in the regular course of their business hold themselves out as having expertise in manufacturing their custom products, have the opportunity and incentive to ensure safety in the process of making those products, and are better able to shoulder the costs of injuries caused by defective products than injured consumers or users.

Feinman, J., followed suit in Matter of Eighth Judicial District Asbestos Litigation, 129 N.E.3d 891 (N.Y. 2019), holding that the manufacturer of a coke oven that was custom fabricated for a steel plant had a duty to warn. Who was in the better position to warn end users about asbestos dangers? Does it matter that tort claims against employers are often precluded by workers' compensation schemes?

**3.** ***Used and Reconditioned Products.*** How does products liability law apply to the sale of used or reconditioned products? In Tillman v. Vance Equipment Co., 596 P.2d 1299, 1303–04 (Or. 1979), the court refused to apply the strict liability rule of section 402A to a defendant who sold a good on an "as is" basis, noting that "it would work a significant change in the very nature of used goods markets"; parties who want warranties typically bargain for them.

Roughly speaking, the Third Restatement (see RTT: PL §8) follows cases like *Tillman* by limiting liability of the seller of used products to those defects that it created, or those created by predecessors in the same commercial chain of distribution. The Third Restatement also requires the reseller of used products to comply with all applicable regulations in force at the time of resale. *Id.* §8(d). In some states, legislation addresses the issue. See, e.g., Kan. Stat. Ann. §60-3306(b)(3) (2024), which explicitly offers sellers of used products protection

against liability in a products liability claim when "the product was sold in substantially the same condition as it was when it was acquired for resale" and judgment against the manufacturer is "reasonably certain of being satisfied."

**4.** ***Successor Liability.*** Can a corporation that acquires either the assets or shares of an original product seller be sued for its predecessor's torts after the original corporation liquidates? The leading case in support of successor liability is Ray v. Alad Corp., 560 P.2d 3, 9 (Cal. 1977), where the new defendant corporation acquired the prior corporation's name and customer lists while continuing to produce the same product line with the same equipment and personnel. The court rested its case for successor liability on three separate grounds:

> (1) the virtual destruction of the plaintiff's remedies against the original manufacturer caused by the successor's acquisition of the business, (2) the successor's ability to assume the original manufacturer's risk-spreading role, and (3) the fairness of requiring the successor to assume a responsibility for defective products that was a burden necessarily attached to the original manufacturer's good will being enjoyed by the successor in the continued operation of the business.

A majority of courts, however, decline to recognize the product line exception. In Semenetz v. Sherling & Walden, Inc., 851 N.E.2d 1170, 1174 (N.Y. 2006), the New York Court of Appeals expressed a common concern that small businesses with limited assets face "economic annihilation" if burdened with the liabilities of their predecessors in ways that could deter the resale of existing assets, even though the liquidation of that corporation also cuts off tort liability for the user of its products. Accordingly, RTT: PL §12 allows successor liability only when the acquisition

> (a) is accompanied by an agreement for the successor to assume such liability; or (b) results from a fraudulent conveyance to escape liability for the debts or liabilities of the predecessor; or (c) constitutes a consolidation or merger with the predecessor; or (d) results in the successor becoming a continuation of the predecessor.

For a proposal that all corporations wishing to go out of business by either sale or liquidation be required to get asset insurance, see Michael D. Green, Successor Liability: The Superiority of Statutory Reform to Protect Products Liability Claimants, 72 Cornell L. Rev. 17 (1986). For a defense of using successor liability to induce corporate purchasers to exact greater diligence in their asset acquisitions, see Richard L. Cupp, Redesigning Successor Liability, 1999 Ill. L. Rev. 845.

## SECTION F. WHAT IS A PRODUCT?

### In re: *Social Media Adolescent Addiction/Personal Injury Products Liability Litigation*

702 F. Supp. 3d 809 (N.D. Cal. 2023)

Rogers, J. This Order addresses the first wave of legal arguments stemming from the filing, on behalf of children and adolescents, of hundreds of individual cases across the United States against five companies operating some of the world's most used social media platforms: Meta's Facebook and Instagram, Google's YouTube, ByteDance's TikTok, and Snapchat. Notably, this multi-district litigation ("MDL") encompasses, in addition to individual suits, over 140 actions brought on behalf of school districts and actions filed jointly by over thirty state Attorneys General. . . .

. . . [T]he Court has conducted an analysis of the actual functionality defects alleged in the complaint, and in that context, has determined whether (and to what extent) the claims against the platforms can proceed.

## I. Background

### B. Relevant Facts Alleged

. . . Defendants are companies that own and operate "social media" platforms. Each platform allows users to create profiles and to share content including messages, videos, and photos. Significantly, these platforms are more than mere message boards or search engines. In addition to enabling users to look for content, or to send content to other specific users, in many instances, the platforms determine when and to whom certain content is shown. As noted, the platforms here at issue are Facebook and Instagram, both operated by Meta; Snapchat; TikTok; and YouTube.

Use of these platforms is generally free. Defendants make money primarily by selling advertising space. Marketers covet such space because defendants possess vast data about users. This enables them to target advertisements to specific audiences. Given this business model, profits from these platforms are highly dependent on the number of users, the amount of time each user spends on the platform, and the amount of information a user provides, directly or indirectly, to the platform about themselves.

#### i. Defect Allegations

As pled, defendants target children as a core market and designed their platforms to appeal to and addict them. Because children still developing impulse control are uniquely susceptible to harms arising out of compulsive use of social media platforms, defendants have "created a youth mental health crisis" through the defective design of their platforms. Further, these platforms facilitate and contribute to the sexual exploitation and sextortion of children, as well as the ongoing production and spread of child sex abuse materials ("CSAM") online.

To that end, defendants know that children use their products, both from public and internal data. Indeed, the ability to estimate a user's age and other characteristics increases the value of defendants' platforms to advertisers. Further, defendants specifically try to cultivate children as users. They believe that early adoption of their platforms will increase the likelihood a child will continue to use the platform as they age. Given the susceptibility of the addictive elements of the platforms, adolescents are more likely to use them for long periods of time, allowing defendants to sell more space to advertisers. Millions of children use defendants' platforms "compulsively." Many report that they feel they are addicted to the platforms, wish they used them less, and feel harmed by them. Defendants are also aware that their platforms harm child users. Beginning in at least 2014, researchers began demonstrating that addictive and compulsive use of defendants' platforms leads to negative mental and physical outcomes for children. At least some defendants also knew about these harms from internal data and studies. [The court summarized, in some detail, the myriad ways in which the design of defendants' platforms cause the harms described above. These aspects, or functions, include "endless feeds" of content shown to users; lack of screen-time limitations; "intermittent variable rewards"; ephemeral content; limitations on content length; notifications; algorithmic prioritization of content; filters; barriers to deletion; connection of child and adult users; private chats; geolocation; age verification; and lack of parental controls.]. . .

## V. Products Liability: Whether the Defects Alleged Concern "Products"

. . . Plaintiffs state both design defect and failure to warn claims relative to defendants' platforms. As discussed at length at the hearing, the claims are predicated upon the existence of a "product." Thus, the Court begins there.

### A. Background

#### i. Overview of Parties' Arguments

. . . Defendants seek dismissal on the basis that (i) their platforms are services, not products; and (ii) even if they are not services, plaintiffs' allegations primarily concern access to and distribution of content posted on the platforms, which cannot form the basis of a cognizable products liability claim. Plaintiffs emphasize that they do *not* claim that content caused them harm; instead, they purport to challenge design choices by defendants regarding various features of their respective platforms' user interfaces.

These approaches are overly simplistic and misguided. . . . The cases generally concern a specific product defect and the determination of whether a specific technology is a product hinges on the specifics of that defect. The same applies here. The Court determines it is necessary to analyze each defect pled by plaintiffs to determine whether they have adequately alleged the existence of a product (or products). . . .

### C. Analysis

#### ii. The Court's Defect-Specific Approach

. . . [T]he Court analyzes whether the various *functionalities* of defendants' platforms challenged by plaintiffs are products. . . .

##### *a. Defective Parental Controls and Age Verification (Defects i, ii, and iii)*

The first three design defects relate to defendants' allegedly defective parental controls and age verification systems, namely: (i) a failure to implement robust age verification processes to determine users' ages . . . ; (ii) a failure to implement effective parental controls . . . ; and (iii) a failure to implement effective parental notifications . . . .

The Court begins by asking whether these alleged defects are analogous to tangible personal property in the context of their use and distribution. *See* Third Restatement § 19(a). The answer is yes. Myriad tangible products contain parental locks or controls to protect young children. . . .

The Court also considers whether these defects concern design elements of defendants' platforms and are content-agnostic, as plaintiffs argue, or are more akin to ideas, content, and free expression upon which products liability claims cannot be based. Again, these identified defects primarily relate to the manner in which young users are able to access defendants' apps, including whether their age is accurately assessed during the sign-up process and whether, subsequent to signing up, their activity and settings can be accessed and controlled by their parents. . . .

##### *b. Failure to Assist Users in Limiting In-App Screen Time (Defects iv and v)*

The next two design defects pertain to app session duration: (i) a failure to implement opt-in restrictions to the length and frequency of use sessions . . . ; and (ii) a failure to implement default protective limits to the length and frequency of use sessions . . . .

Again, the Court begins with an analogy to tangible personal property. The most obvious analog to these identified defects is physical timers and alarms, which have long been in use. Modern examples are also available. For instance, many of us carry in our pockets smart

phones which are tangible products. These phones contain features that enable users to receive auto-notifications should they exceed pre-set "screen time" limits. These examples are sufficiently analogous to tangible personal property in terms of their use and distribution.

Importantly, these alleged defects are also content-agnostic. Plaintiffs' theory concerns the manner in which users access the apps (*i.e.*, for uninterrupted, long periods of time), not the content they view there. For this reason, these alleged defects are not excluded on the grounds that they pertain to "ideas, thoughts, and expressive content" . . .

Accordingly, the Court finds the two above-referenced design defects are product components and therefore appropriately fall within a product liability claim.

#### *c. Creating Barriers to Account Deactivation and/or Deletion (Defect vii)*

Plaintiffs allege that each defendant's account deactivation/deletion process is needlessly complicated and serves to disincentivize users from leaving their respective social media platforms. . . .

Here, defendants' global arguments casting all of plaintiffs' allegations as essentially content-related are particularly lacking. . . .

Further, the Court is not inclined to view this alleged defect as akin to a service. . . . [A]ccount deletion and deactivation, as pled, is a user-directed process. . . .

Given the procedural posture of the action, the Court therefore finds a sufficient plausible basis to classify the defect as a product.

#### *d. Failure to Label Edited Content (Defect vi)*

Next, plaintiffs allege defendants fail to label images and videos that have been edited through in-app "filters" as edited content.

This alleged defect concerns the *design* of defendants' social media platforms rather than the content made available through such platforms. . . . That said, the Court recognizes that the labeling, or failing to label, content, in any way, is tied to the nature of the content itself. . . . However, that connection relates to the output of the labeling, not the labeling tool itself.

. . . [T]he Court finds that this design defect may proceed as a product to the extent that plaintiffs' allegations center on the design of the filter. For instance, labeling a photo as "edited" does not alter the underlying photo as much as it guides the user in better understanding how to interpret that photo. The Court finds this distinction meaningful. Accordingly, while a closer question, plaintiffs have plausibly stated the existence of a product relative to this defect.

#### *e. Making Filters Available to Users to Manipulate Content (Defect viii)*

The next alleged defect concerns defendants' filters, which enable users to manipulate content prior to posting it on defendants' platforms or otherwise sharing it with others. . . .

Plaintiffs challenge two main categories of filters. One, they target filters that permit users to "blur imperfections" and otherwise enhance their appearance in order to "create the perfect selfie." . . . Plaintiffs assert the widespread use of such filters promotes unattainable beauty standards and facilitates social comparison, which combine to cause negative mental health outcomes for users, particularly young girls. Two, they target filters like Snapchat's Speed Filter, which enable users to overlay content on top of existing content. Specifically, the Speed Filter is a functionality that enables users to overlay the speed they are traveling in real life onto a photo or video before sharing that content with others via the Snapchat app. . . .

With respect to the filters that permit appearance alteration, the Court notes that defendants, admittedly in the First Amendment context, have referred to such filters as "*tools* that allow users to speak to one another," such as by "creating or modifying their own expression (including with visual effects that change the look of images)." Defendants' use of the word

"tools" here is notable because defendants implicitly concede that a distinction exists between a "tool," or functionality, that permits users to manipulate content and the content itself. Here, the concession inures to plaintiffs' benefit as it bolsters their contention that this alleged defect is really about design, not content. Given the procedural posture, plaintiffs' products liability claims may proceed with respect to defendants' appearance-altering filters.

[Turning to Snapchat's Speed Filter, the court relied on Lemmon v. Snap, Inc., 995 F.3d 1085 (9th Cir. 2021), where plaintiffs challenged the design of Snapchat's platform insofar as it provides users with the Speed Filter as a tool for overlaying their speed onto photos and videos. "As plaintiffs challenge essentially the same functionality as was at issue in that case and plead their allegations in similar ways, the Court determines *Lemmon* applies here."]

Accordingly, the Court determines plaintiffs have plausibly alleged that both categories of filters are products and permits their claims to proceed on that basis.

#### *f. Failure to Enable Processes to Report CSAM (Defect ix)*

Finally, the Court analyzes plaintiffs' allegations that defendants failed to design their platforms to include "reporting protocols [that] allow users or visitors" "to report CSAM and adult predator accounts *specifically without the need to create or log in to the products prior to reporting.*"

The Court determines this allegation specifically concerns the *design* of defendants' platforms. Plaintiffs seek to hold defendants accountable for requiring users to have logged into a registered account in order to report certain obscene content or profiles. This is quintessentially a matter of design, user interface, and system architecture rather than content. . . .

Accordingly, the Court determines that plaintiffs have adequately alleged that the design of defendants' CSAM and adult predator account reporting mechanisms are products.

### D. Conclusion

For the foregoing reasons, the Court determines that plaintiffs adequately plead the existence of product components as to each alleged defect analyzed herein. [The court then discussed the remaining elements of plaintiffs' products liability claims: duty and causation. The court held "defendants owe plaintiff users of their social media platforms duties owing to their status as product makers, which are limited in scope to the defects previously determined by this Court to be product components. Defendants do not, however, owe plaintiffs a duty to protect them from harm from third party users of defendants' platforms." The court then held that plaintiffs had adequately pled causation.]

### RESTATEMENT (THIRD) OF TORTS: PRODUCTS LIABILITY §19(A)

(a) A product is tangible personal property distributed commercially for use or consumption. Other items, such as real property and electricity, are products when the context of their distribution and use is sufficiently analogous to the distribution and use of tangible personal property that it is appropriate to apply the rules stated in th[e] Restatement.

(b) Services, even when provided commercially, are not products.

(c) Human blood and human tissue, even when provided commercially, are not subject to [the] Restatement.

## NOTES

**1. *"Intangibles" as Products?*** The Third Restatement defines products as "tangible personal property distributed commercially for use or consumption." RTT: PL §19. It recognizes, though, that intangibles can be products when analogized to "tangible personal property" based on "the context of their distribution and use." Courts have attached products liability to "maps and navigational charts" containing "false information." Id. & cmt. *d.* They have also done so with respect to certain intangible forces, such as electricity. Specifically, "a majority of courts have held that electricity becomes a product when it passes through the customer's meter and enters the customer's premises." *Id.*

The *In re Social Media* plaintiffs argue that the "distribution" of defendants' platforms is akin to platforms made by "product designers," overseen by "product managers," and then packaged and shipped to the public via stores. How convincing is such an analogy? Does it matter that defendants' platforms are not exclusively accessed by downloading an app from an online "store" but can also be accessed via their webpages and can even come preloaded on certain connected devices?

**2. *Information as a Product.*** Does products liability law apply to information? The Restatement generally excludes intangible property like information contained in books or media due to free speech concerns: "Most courts, expressing concern that imposing strict liability for the dissemination of false and defective information would significantly impinge on free speech have, appropriately, refused to impose strict products liability in these cases." The seminal case of Winter v. G.P. Putnam's Sons, 938 F.2d 1033, 1033, 1034, 1035–38 (9th Cir. 1991) illustrates the point. There, plaintiffs were mushroom enthusiasts who become severely ill after eating wild mushrooms they identified as nondangerous based on a reference book. They subsequently sued the book's publisher under a strict products liability theory, alleging the book was defectively designed in that it contained erroneous and misleading information about the identification of deadly mushrooms. The district court granted summary judgment to the book publisher finding that the content of the book (*i.e.*, whether a specific mushroom was safe to eat) was not a product. The Ninth Circuit affirmed.

The Ninth Circuit's opinion in *Winter* is routinely cited for the proposition that ideas, thoughts, and free expression cannot form a product on which a products liability case can be based. The Ninth Circuit allowed that the mushroom reference book *itself* could be a product, although its contents, as "pure thought and expression," were not. The logic of *Winter* has been repeatedly reaffirmed in the case law. In James v. Meow Media, Inc., 300 F.3d 683, 701 (6th Cir. 2002), a fourteen-year-old student shot, wounded, and killed his high school classmates. Parents brought suit against entities that developed and distributed violent online content that the assailant consumed through video games and movies. They alleged that the "inherent dangerousness" of the content rendered it a "product" for which its developers should be held strictly liable. The trial court disagreed, dismissing plaintiffs' products liability claims on the grounds that "intangible thoughts, ideas, and expressive content are not 'products' within the realm of the strict liability doctrine." The Sixth Circuit ultimately affirmed, concluding "[t]he video game cartridges, movie cassette, and internet transmissions are not sufficiently 'tangible' to constitute products in the sense of their communicative content." See also Estate of B.H. v. Netflix, Inc., 2022 WL 551701, at *1 (N.D. Cal. Jan. 12, 2022), relying on *Winter* to dismiss products liability claims against Netflix in connection with Netflix's production, dissemination, and recommendation of a television show involving suicide to a young girl who went on to herself commit suicide, likening the plaintiffs' claims to those against "books, movies, or other forms of media."

This reluctance to extend liability to intangible products presents new complications in our increasingly digital world. Consumers engage with intangible products like computer

software and smartphone apps constantly, raising questions as to whether the owners of these platforms can be held liable for the information disseminated through them.

Section 230(c)(1) of the Communications Decency Act of 1996 (CDA) has been broadly construed to immunize online companies from liability arising from third-party information content. Its text reads: "No provider or user of an interactive computer service shall be treated as the publisher or speaker of any information provided by another information content provider." 47 U.S.C. §230(c)(1). If these providers cannot be held liable for the content on their platforms, can they be held liable under a products liability theory for the algorithms that bring content to consumers' attention?

In Twitter v. Taamneh, 598 U.S. 471 (2023), plaintiffs sued Twitter for damages under the Antiterrorism Act, 18 U.S.C. §2333, alleging, inter alia, that its recommendation algorithms helped ISIS recruit members, which contributed to a terrorist attack that harmed plaintiffs. A unanimous Supreme Court held that plaintiffs failed to state a claim for aiding and abetting as required under the statute. In Gonzalez v. Google, 598 U.S. 617 (2023), a parallel case, the Court heard arguments challenging the Ninth Circuit's determination that CDA §230 barred similar claims against Google, regardless of whether liability could be found under the Antiterrorism Act. The Court punted on this question, remanding the case in light of *Taamneh* given that, without liability under the Antiterrorism Act, plaintiff stated no independent claim for relief. *Gonzalez* thus left for a further day resolution of the scope of CDA §230 immunity in the context of algorithms. What result if plaintiffs cast their claim as a product liability theory?

Several courts have distinguished between products liability claims that are focused primarily on content (and thus, were not cognizable) and those focused primarily on design (which are cognizable). Brookes v. Lyft, Inc., 2022 WL 19799628, at *3 (Fla. Cir. Ct. Sept. 30, 2022), held that the ridesharing company Lyft's mobile app was a product that was "defective because of the way it habituat[ed] and distract[ed] Lyft drivers to constantly monitor the application," including while driving.

Snapchat has also been a target of successful products liability claims. The *In re Social Media* court relied on Lemmon v. Snap, Inc., 995 F.3d 1085 (9th Cir. 2021), where the Ninth Circuit declined to grant CDA §230 immunity on the grounds that plaintiffs' negligent design claim did not seek to hold Snap liable as a publisher of third-party information but rather relied on Snap's own architecture and reward system. In Maynard v. Snapchat, Inc., 870 S.E.2d 739, 743 (Ga. 2022), the plaintiff sued Snapchat after being rear-ended by a car going 107 miles per hour, driven by a Snapchat user who told her passengers prior to the accident that she was "'just trying to get the car to 100 m.p.h. to post it on Snapchat' using Snapchat's Speed Filter." Colvin, J., held:

> [T]he Maynards asserted a conventional design-defect claim based on the ordinary design duty recognized under our decisional law. . . . [They] alleged that . . . Snap knew that other drivers were using the Speed Filter while speeding at 100 miles per hour or more as part of "a game," purposefully designed its products to encourage such behavior, [and] knew of at least one other instance in which a driver who was using Snapchat while speeding caused a car crash. . . .

What result in *Lemmon* and *Maynard* if the Speed Filter had been designed by another user?

**3. *Products Versus Services.*** The *In re Social Media* defendants argued that their platforms are "interactive communication services," not products. The plaintiffs argued that whether or not defendants also provide services to consumers, their platforms are nonetheless products. Inevitably questions arise about whether a particular seller is providing a product or a service. One concern is that the broad definition of a seller in products liability cases could allow its strict liability rules to spill over into areas that have traditionally been governed under negligence law. In Cafazzo v. Central Medical Health Services, Inc., 668 A.2d 521, 525, 526,

527 (Pa. 1995), that concern led Montemuro, J., to reject an attempt to hold a hospital and physician strictly liable for the defects in a mandibular prosthesis used during an operation. Montemuro, J., held that supplying the product was "ancillary" to the provision of medical services, even if there happened to be a surcharge on the medical product:

> [I]t must be noted that the "seller" need not be engaged solely in the business of selling products such as the defective one to be held strictly liable. An example supporting this proposition appears in comment *f* of the Restatement (Second) of Torts, §402A and concerns the owner of a motion picture theater who offers edibles such as popcorn and candy for sale to movie patrons. The analogue to the instant case is valid in one respect only: both the candy and the . . . implant are ancillary to the primary activity, viewing a film or undergoing surgery respectively. However, beyond that any comparison is specious. A movie audience is free to purchase or not any food items on offer, and regardless of which option is exercised the primary activity is unaffected. On the other hand, while the implant was incidental to the surgical procedure here, it was a necessary adjunct to the treatment administered, as were the scalpel used to make the incision, and any other material objects involved in performing the operation, all of which fulfill a particular role in provision of medical service, the primary activity.

Montemuro, J., reasoned that strict liability would not provide an incentive for hospitals and doctors to choose different services, as they rely on the FDA's stamp of approval. He warned against allowing the "selection of the wrong product [to] become[] a matter of professional negligence for which recovery is available." Nor did he think strict liability was needed to compensate the injured party, finding that the "net effect of this cost spreading would further endanger the already beleaguered health care system."

The Third Restatement follows the Second by holding that "[s]ervices, even when provided commercially, are not products," RTT: PL §19(b), including those services to inspect, repair, and maintain machinery of the original product seller. A replacement part therefore is subject to products liability, but its installation is not.

**4. *Is Software a Product or Service?*** The Third Restatement anticipated that courts might, at some future date, be asked to determine whether software is a product. It did not express a view on the matter and instead simply made two notes. First, academics have long urged such an extension of tort doctrine. Second, courts could turn to the Uniform Commercial Code ("UCC")'s treatment of mass-marketed software as "goods" for persuasive authority. See generally Third Restatement §19(a) & cmt. *d*.

Would this extend the limits of products liability too far? What if the software is custom software that operates as a service? Or deals primarily with ideas, content, and free expression that cannot typically form the basis of a products liability claim? What if products liability were limited to mass-marketed software?

## SECTION G. PLAINTIFF'S CONDUCT

### *Daly v. General Motors Corp.*

575 P.2d 1162 (Cal. 1978)

Richardson, J. The most important of several problems which we consider is whether the principles of comparative negligence expressed by us in Li v. Yellow Cab Co., apply to actions founded on strict products liability. We will conclude that they do. . . .

[The decedent was driving his Opel southbound on the Harbor Freeway between 50 and 70 miles per hour when it struck the metal divider. The car spun around and the decedent was forcibly thrown from the car, sustaining fatal head injuries. The plaintiffs alleged that the door

lock was defectively designed because of its exposed push button, which, it was claimed, was forced open during the original collision.]

Over plaintiffs' objections, defendants were permitted to introduce evidence indicating that: (1) the Opel was equipped with a seat belt-shoulder harness system, and a door lock, either of which if used, it was contended, would have prevented Daly's ejection from the vehicle; (2) Daly used neither the harness system nor the lock; (3) the 1970 Opel owner's manual contained warnings that seat belts should be worn and doors locked when the car was in motion for "accident security"; and (4) Daly was intoxicated at the time of collision, which evidence the jury was advised was admitted for the limited purpose of determining whether decedent had used the vehicle's safety equipment. After relatively brief deliberations the jury returned a verdict favoring all defendants, and plaintiffs appeal from the ensuing adverse judgment.

### Strict Products Liability and Comparative Fault . . .

Those counseling against the recognition of comparative fault principles in strict products liability cases vigorously stress, perhaps equally, not only the conceptual, but also the semantic difficulties incident to such a course. The task of merging the two concepts is said to be impossible, that "apples and oranges" cannot be compared, that "oil and water" do not mix, and that strict liability, which is not founded on negligence or fault, is inhospitable to comparative principles. The syllogism runs, contributory negligence was only a defense to negligence, comparative negligence only affects contributory negligence, therefore comparative negligence cannot be a defense to strict liability. . . . While fully recognizing the theoretical and semantic distinctions between the twin principles of strict products liability and traditional negligence, we think they can be blended or accommodated.

The inherent difficulty in the "apples and oranges" argument is its insistence on fixed and precise definitional treatment of legal concepts. In the evolving areas of both products liability and tort defenses, however, there has developed much conceptual overlapping and interweaving in order to attain substantial justice. The concept of strict liability itself, as we have noted, arose from dissatisfaction with the wooden formalisms of traditional tort and contract principles in order to protect the consumer of manufactured goods. Similarly, increasing social awareness of its harsh "all or nothing" consequences led us in *Li* to moderate the impact of traditional contributory negligence in order to accomplish a fairer and more balanced result. We acknowledged an intermixing of defenses of contributory negligence and assumption of risk and formally effected a type of merger. . . .

Furthermore, the "apples and oranges" argument may be conceptually suspect. It has been suggested that the term "contributory negligence," one of the vital building blocks upon which much of the argument is based, may indeed itself be a misnomer since it lacks the first element of the classical negligence formula, namely, a duty of care owing to another. . . .

Given all of the foregoing, we are, in the wake of *Li*, disinclined to resolve the important issue before us by the simple expedient of matching linguistic labels which have evolved either for convenience or by custom. Rather, we consider it more useful to examine the foundational reasons underlying the creation of strict products liability in California to ascertain whether the purposes of the doctrine would be defeated or diluted by adoption of comparative principles. We imposed strict liability against the manufacturer and in favor of the user or consumer in order to relieve injured consumers "from *problems of proof* inherent in pursuing negligence . . . and warranty . . . remedies. . . ." As we have noted, we sought to place the burden of loss on manufacturers rather than ". . . injured persons *who are powerless to protect themselves . . ."* (["*protection of otherwise defenseless victims* of manufacturing defects and the spreading throughout society of the cost of compensating them"] italics added).

The foregoing goals, we think, will not be frustrated by the adoption of comparative principles. Plaintiffs will continue to be relieved of proving that the manufacturer or distributor was negligent in the production, design, or dissemination of the article in question. Defendant's liability for injuries caused by a defective product remains strict. The principle of protecting the defenseless is likewise preserved, for plaintiff's recovery will be reduced *only* to the extent that his own lack of reasonable care contributed to his injury. The cost of compensating the victim of a defective product, albeit proportionately reduced, remains on defendant manufacturer, and will, through him, be "spread among society." However, we do not permit plaintiff's own conduct relative to the product to escape unexamined, and as to that share of plaintiff's damages which flows from his own fault we discern no reason of policy why it should, following *Li*, be borne by others. Such a result would directly contravene the principle announced in *Li*, that loss should be assessed equitably in proportion to fault.

We conclude, accordingly, that the expressed purposes which persuaded us in the first instance to adopt strict liability in California would not be thwarted were we to apply comparative principles. What would be forfeit is a degree of semantic symmetry. However, in this evolving area of tort law in which new remedies are judicially created, and old defenses judicially merged, impelled by strong considerations of equity and fairness we seek a larger synthesis. If a more just result follows from the expansion of comparative principles, we have no hesitancy in seeking it, mindful always that the fundamental and underlying purpose of *Li* was to promote the equitable allocation of loss among all parties legally responsible in proportion to their fault.

A second objection to the application of comparative principles in strict products liability cases is that a manufacturer's incentive to produce safe products will thereby be reduced or removed. While we fully recognize this concern we think, for several reasons, that the problem is more shadow than substance. First, of course, the manufacturer cannot avoid its continuing liability for a defective product even when the plaintiff's own conduct has contributed to his injury. The manufacturer's liability, and therefore its incentive to avoid and correct product defects, remains; its exposure will be lessened only to the extent that the trier finds that the victim's conduct contributed to his injury. Second, as a practical matter a manufacturer, in a particular case, cannot assume that the user of a defective product upon whom an injury is visited will be blameworthy. Doubtless, many users are free of fault, and a defect is at least as likely as not to be exposed by an entirely innocent plaintiff who will obtain full recovery. In such cases the manufacturer's incentive toward safety both in design and production is wholly unaffected. Finally, we must observe that under the present law, which recognizes assumption of risk as a complete defense to products liability, the curious and cynical message is that it profits the manufacturer to make his product so defective that in the event of injury he can argue that the user had to be aware of its patent defects. To that extent the incentives are inverted. We conclude, accordingly, that no substantial or significant impairment of the safety incentives of defendants will occur by the adoption of comparative principles.

In passing, we note one important and felicitous result if we apply comparative principles to strict products liability. This arises from the fact that under present law when plaintiff sues in negligence his own contributory negligence, however denominated, may diminish but cannot wholly defeat his recovery. When he sues in strict products liability, however, his "assumption of risk" *completely bars* his recovery. Under *Li*, as we have noted, "assumption of risk" is merged into comparative principles. . . . The consequence is that after *Li* in a negligence action, plaintiff's conduct which amounts to "negligent" assumption of risk no longer defeats plaintiff's recovery. Identical conduct, however, in a strict liability case acts as a complete bar under rules heretofore applicable. Thus, strict products liability, which was developed to free injured consumers from the constraints imposed by traditional negligence and warranty theories, places a consumer plaintiff in a worse position than would be the case were his claim

founded on simple negligence. This, in turn, rewards adroit pleading and selection of theories. The application of comparative principles to strict liability obviates this bizarre anomaly by treating alike the defenses to both negligence and strict products liability actions. In each instance the defense, if established, will reduce but not bar plaintiff's claim.

A third objection to the merger of strict liability and comparative fault focuses on the claim that, as a practical matter, triers of fact, particularly jurors, cannot assess, measure, or compare plaintiff's negligence with defendant's strict liability. We are unpersuaded by the argument and are convinced that jurors are able to undertake a fair apportionment of liability. . . . [The court then notes that comparative principles have functioned smoothly in the unseaworthiness cases tried in admiralty, even though unseaworthiness is a strict liability concept.]

We find equally unpersuasive a final objection that the merger of the two principles somehow will abolish or adversely affect the liability of such intermediate entities in the chain of distribution as retailers . . . and bailors. . . . We foresee no such consequence. Regardless of the identity of a particular defendant or of his position in the commercial chain the basis for his liability remains that he has marketed or distributed a defective product. If, as we believe, jurors are capable of assessing fully and fairly the legal responsibility of a manufacturer on a strict liability basis, no reason appears why they cannot do likewise with respect to subsequent distributors and vendors of the product.

We note that the majority of our sister states which have addressed the problem, either by statute or judicial decree, have extended comparative principles to strict products liability.

Our research discloses that of the more than 30 states which have adopted some form of comparative negligence, three (including California) have done so judicially. . . . [The court notes that its position enjoys considerable academic support, and that the proposed Uniform Comparative Fault Act embraces a comparative fault principle in strict liability actions. It concludes that it also covers assumption of risk, to the extent that it is a form of contributory negligence.]

Jefferson, J., concurring and dissenting. . . . What the majority envisions as a fair apportionment of liability to be undertaken by the jury will constitute nothing more than an *unfair reduction* in the plaintiff's total damages suffered, resulting from a jury process that necessarily is predicated on speculation, conjecture and guesswork. . . .

Mosk, J., dissenting. I dissent.

This will be remembered as the dark day when this court, which heroically took the lead in originating the doctrine of products liability [in *Greenman*] and steadfastly resisted efforts to inject concepts of negligence into the newly designed tort (Cronin v. J. B. E. Olson Corp.), inexplicably turned 180 degrees and beat a hasty retreat almost back to square one. The pure concept of products liability so pridefully fashioned and nurtured by this court for the past decade and a half is reduced to a shambles.

The majority inject a foreign object — the tort of negligence — into the tort of products liability by the simple expedient of calling negligence something else: on some pages their opinion speaks of "comparative fault," on others reference is to "comparative principles," and elsewhere the term "equitable apportionment" is employed, although this is clearly not a proceeding in equity. But a rose is a rose and negligence is negligence; thus the majority find that despite semantic camouflage they must rely on Li v. Yellow Cab Co., even though *Li* is purely and simply a negligence case which merely rejects contributory negligence and substitutes therefor comparative negligence.

. . . [I]n *Cronin* we stressed that "the very purpose of our pioneering efforts in this field was to relieve the plaintiff from problems of proof inherent in pursuing negligence." And in

Luque v. McLean, 501 P.2d 1163 (Cal. 1972), this court unanimously declared that "contributory negligence does not bar recovery in a strict liability action." . . .

The bench and bar have abided by this elementary rule. They have learned to avoid injecting negligence — whether of the defendant or the plaintiff — into a products liability case. And they have understood the reason behind the distinction between negligence of any party and products liability. It was expressed over three decades ago by Justice Traynor in his concurring opinion in Escola v. Coca Cola Bottling Co.[, *supra* at 55]. . . .

Transferring the liability, or part of the liability, from the party responsible for putting the article in the stream of commerce to the consumer is precisely what the majority propose to do. They do this by employing a euphemism: the victim's recovery is to be "proportionately reduced." The result, however delicately described, is to dilute the defect of the article by elevating the conduct of the wounded consumer to an issue of equal significance. We can be as certain as tomorrow's daylight that every defendant charged with marketing a defective product will hereafter assert that the injured plaintiff did something, anything, that conceivably could be deemed contributorily negligent: he drove the vehicle with a defective steering mechanism 56 miles an hour instead of 54; or he should have discovered a latent defect hidden in the machinery; or perhaps he should not have succumbed to the salesman's persuasion and purchased the defective object in the first instance. I need no crystal ball to foresee that the pleading of affirmative defenses alleging contributory negligence — or the currently approved substitute terminology — will now become boilerplate. . . .

The defective product is comparable to a time bomb ready to explode; it maims its victims indiscriminately, the righteous and the evil, the careful and the careless. Thus when a faulty design or otherwise defective product is involved, the litigation should not be diverted to consideration of the negligence of the plaintiff. The liability issues are simple: was the product or its design faulty, did the defendant inject the defective product into the stream of commerce, and did the defect cause the injury? The conduct of the ultimate consumer-victim who used the product in the contemplated or foreseeable manner is wholly irrelevant to those issues. . . .

The majority note one "felicitous result" of adopting comparative negligence to products liability: the merger of assumption of risk — which they term a "bizarre anomaly" — into their innovative defense. I find that result neither felicitous nor tenable. In Barker v. Lull Engineering Co., we defined a defective product as one which failed to perform safely when used in an intended or foreseeable manner. If a consumer elects to use a product patently defective when other alternatives are available, or to use a product in a manner clearly not intended or foreseeable, he assumes the risks inherent in his improper utilization and should not be heard to complain about the condition of the object. One who employs a power saw to trim his fingernails — and thereafter finds the number of his fingers reduced — should not prevail to any extent whatever against the manufacturer even if the saw had a defective blade. I would retain assumption of risk as a total defense to products liability, as it always has been.

I would affirm the judgment.

## NOTES

**1.** ***Foreseeable Misuse.*** In most crashworthiness cases, the plaintiff's misconduct goes far beyond the "normal and proper use" contemplated in *Escola*. In LeBouef v. Goodyear Tire & Rubber Co., 623 F.2d 985, 989 (5th Cir. 1980), the decedent purchased "a new, 1976 Mercury Cougar equipped with a 460 cubic-inch, 425-horsepower engine, and with Goodyear HER78-15 Custom Polysteel Radial Tires." The car was capable of going 100 miles per hour, but Goodyear had tested the tires for safety only for speeds of eighty-five miles per hour.

Ford's only warning was "a statement in the Cougar owner's manual that '[c]ontinuous driving over ninety mph requires using high-speed-capability tires'; the manual did not state whether the tires in question were or were not of high-speed-caliber." The decedent was driving while intoxicated at speeds of 100 to 105 miles per hour and was killed when the car veered off the road. The trial court, sitting without a jury, found that the tire, although properly manufactured, was defective because of its insufficient warnings about the risk of tread separation at high speeds. It also found that "while [the decedent's] excessive speed was a contributory cause of the accident, his intoxication was not." It also rejected the contributory negligence and assumption of risk defenses. On appeal, the decision was affirmed, and the court had this to say about the misuse defense:

> Certainly the operation of the Cougar in excess of 100 miles per hour was not "normal" in the sense of being a routine or intended use. "Normal use," however, is a term of art in the parlance of Louisiana products liability law, delineating the scope of a manufacturer's duty and consequent liability; it encompasses all *reasonably foreseeable* uses of a product. . . . The sports car involved here was marketed with an intended and recognized appeal to youthful drivers. The 425 horsepower engine with which Ford had equipped it provided a capability of speeds over 100 miles per hour, and the car's allure, no doubt exploited in its marketing, lay in no small measure in this power and potential speed. It was not simply foreseeable, but was to be readily expected, that the Cougar would, on occasion, be driven in excess of the 85 miles per hour proven maximum safe operating speed of its Goodyear tires. Consequently, Ford cannot, on the basis of abnormal use, escape its duty either to provide an adequate warning of the specific danger of tread separation at such high speeds or to ameliorate the danger in some other way.

The foreseeable misuse standard has been criticized as creating a "moral hazard" problem by sanctioning reckless behavior and increasing the probability of accidents. In addition, foreseeable misuse creates an implicit transfer of wealth from careful to careless drivers because the manufacturer cannot differentiate in price charged between a retiree and a traveling salesman, or between the careful driver who has never had a ticket and the teenage hot-rodder. Richard A. Epstein, Products Liability as an Insurance Market, 14 J. Legal Stud. 645 (1985), notes that first-party insurers routinely make these risk classifications in selling automobile insurance.

**2. *The Restatement Position.*** The Third Restatement follows *Daly* in what has become the majority position. See RTT: PL §17. In essence, the Third Restatement declines to treat product misuse, alteration, or assumption of risk as independent defenses. Rather, to the extent that these are traced to the plaintiff's conduct, they are governed by the comparative fault system in effect within the jurisdiction, usually pure comparative negligence or the 50 percent cut-off rule. Prior to the Third Restatement, many states followed a rule that provided that the plaintiff was under no duty to discover latent defects contained in the defendant's product. Under the influence of comparative negligence, this defense may be allowed, at least in some cases: "[W]hen the defendant claims that the plaintiff failed to discover a defect, there must be evidence that the plaintiff's conduct in failing to discover a defect did, in fact, fail to meet a standard of reasonable care." RTT: PL §17, cmt. *d*.

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: PRODUCTS LIABILITY**

**§17. Apportionment of Responsibility Between or Among Plaintiff, Sellers and Distributors of Defective Products, and Others**

(a) A plaintiff's recovery of damages for harm caused by a product defect may be reduced if the conduct of the plaintiff combines with the product defect to cause the

harm and the plaintiff's conduct fails to conform to generally applicable rules establishing appropriate standards of care.

(b) The manner and extent of the reduction under Subsection (a) and the apportionment of plaintiff's recovery among multiple defendants are governed by generally applicable rules apportioning responsibility.

**3. *Contractual Defenses to Products Liability Actions.*** The Waiver Society Project, https://www.waiversociety.org/, is an ongoing project that tracks "the ubiquity of waivers in our world." Such express assumption of risk by contract is a complete defense to a tort action in some settings. One vital question is whether product sellers should be able, directly or through intermediaries, to contract out of their liability with potential product users and consumers. The contractual regime could redefine product defect, cap damages, or eliminate liability altogether. Since *Henningsen*, courts have uniformly rejected that approach, which also receives a chilly reception in the Third Restatement. See RTT: PL §18. The rule does not apply to cases of purely economic loss usually covered under the U.C.C., nor does it necessarily apply whenever product users and consumers are "represented by informed and economically powerful consumer groups or intermediaries." RTT: PL §18, cmt. *d.* Does a reduction in price or increase in product or service access count as the necessary quid pro quo? How would the law of products liability have to be rewritten if the contractual waivers were freely accepted in all cases of physical injury or property damage?

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: PRODUCTS LIABILITY**

**§18. Disclaimers, Limitations, Waivers, and Other Contractual Exculpations as Defenses to Products Liability Claims for Harm to Persons**

Disclaimers and limitations of remedies by product sellers or other distributors, waivers by product purchasers, and other similar contractual exculpations, oral or written, do not bar or reduce otherwise valid products-liability claims against sellers or other distributors of new products for harm to persons.

***Comment a. Effects of contract defenses on products liability tort claims for harm to persons:*** . . . It is presumed that the ordinary product user or consumer lacks sufficient information and bargaining power to execute a fair contractual limitation of rights to recover. . . .

***Comment d. Waiver of rights in contractual settings in which product purchasers possess both adequate knowledge and sufficient economic power:*** . . . This Section does not address whether consumers, especially when represented by informed and economically powerful consumer groups or intermediaries, with full information and sufficient bargaining power, may contract with product sellers to accept curtailment of liability in exchange for concomitant benefits, or whether such consumers might be allowed to agree to substitute alternative dispute resolution mechanisms in place of traditional adjudication. When such contracts are accompanied by alternative nontort remedies that serve as an adequate quid pro quo for reducing or eliminating rights to recover in tort, arguments may support giving effect to such agreements. Such contractual arrangements raise policy questions different from those raised by this Section and require careful consideration by the courts.

> ***§21. Comment f. Harm to other property: disclaimers and limitations of remedies:*** . . . When a defective product causes harm to property owned by third persons, the contractual arrangements between the contracting parties should not shield the seller from liability to the third party. However, contractual limitations on tort liability for harm to property, when fairly bargained for, may provide an effective way for the contracting parties efficiently to allocate risks of such harm between themselves.

## SECTION H. FEDERAL PREEMPTION

A major fraction of tort litigation addresses the interaction between direct forms of federal regulation and the state-based common law of products liability. The debate over federal preemption implicates the policy debate over the relative desirability of ex ante regulation by federal agencies versus ex post litigation by injured parties in ensuring optimal health and safety standards. Robert L. Rabin, Reassessing Regulatory Compliance, 88 Geo. L.J. 2049, 2068–70 (2000), argues that even with the presence of federal regulators, tort litigation is beneficial because the process involves the collection of information about post-market use and defects that might not otherwise come to light, particularly in the case of fraud on the part of the manufacturer. Tort liability, in Rabin's account, effectively complements regulation, by providing independent incentives for product safety. In contrast, Epstein has argued that the imposition of tort liability will only make matters worse if the regulatory system already embodies safety standards that are too strict. "Where the FDA incorrectly blocks a drug from entering the market, litigation can do nothing to correct that error. Where the regulatory process lets drugs correctly on the market, litigation remains costly even if it vindicates the defendant." Richard A. Epstein, The Case for Field Preemption of State Laws in Drug Cases, 103 Nw. U.L. Rev. 463, 470 (2009).

At its core, federal preemption is not just a question of public policy, but also a question of statutory interpretation with constitutional overtones. The Supremacy Clause, Article VI, §2, of the U.S. Constitution, provides that any federal statute or regulation trumps any inconsistent state law:

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land: and the Judges in every State shall be bound thereby, any Thing in the Constitution or Law of any State to the contrary not with standing.

In some instances, the federal statute explicitly displaces state law. Express preemption by Congress is often the exception, not the rule. More often real or apparent conflicts between federal and state laws give rise to complex matters of statutory construction. Early on, in Rice v. Santa Fe Elevator Corp., 331 U.S. 218, 230–31 (1947), the Supreme Court set out the basic presumption against federal preemption when it wrote:

> [W]e start with the assumption that the historic police powers of the States [to regulate safety and health] were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress. Such a purpose may be evidenced in several ways. The scheme of federal regulation may be so pervasive as to make reasonable the inference that Congress left no room for the States to supplement it. Or the Act of Congress may touch a field in which the federal interest is so dominant that the federal system will be assumed to preclude enforcement of state laws on the same subject. Likewise, the object sought to be obtained by the federal law and the character of obligations imposed by it may reveal the same purpose. Or the state policy may produce a result inconsistent with the objective of the federal statute.

After *Rice*, implied preemption takes on three different guises. So-called field preemption arises when the federal statute is sufficiently comprehensive to "occupy the field," thereby precluding any state standards in that substantive area. Field preemption is virtually nonexistent in products liability. Most products cases involve "conflict preemption," which comes in two varieties: (1) the state law is flatly inconsistent with the federal statute ("impossibility preemption"), and (2) the enforcement of the state law frustrates or presents an obstacle to the federal scheme ("obstacle preemption"). Working out the implications of this basic system is challenging given the modern proliferation of design, warning, and liability theories at the state law level.

## *Geier v. American Honda Motor Co.*

529 U.S. 861 (2000)

Breyer, J. This case focuses on the 1984 version of a Federal Motor Vehicle Safety Standard promulgated by the Department of Transportation under the authority of the National Traffic and Motor Vehicle Safety Act of 1966, 80 Stat. 718, 15 U.S.C. §1381 et seq. (1988 ed.). The standard, FMVSS 208, required auto manufacturers to equip some but not all of their 1987 vehicles with passive restraints. We ask whether the Act pre-empts a state common-law tort action [for a design defect] in which the plaintiff claims that the defendant auto manufacturer, who was in compliance with the standard, should nonetheless have equipped a 1987 automobile with airbags. We conclude that the Act, taken together with FMVSS 208, pre-empts the lawsuit.

### I

In 1992, petitioner Alexis Geier, driving a 1987 Honda Accord, collided with a tree and was seriously injured. The car was equipped with manual shoulder and lap belts which Geier had buckled up at the time. The car was not equipped with airbags or other passive restraint devices.

[Breyer, J., outlines the procedural history of the case and notes the sharp split of opinion in the lower federal and state courts.]

We granted certiorari to resolve these differences. We now hold that this kind of "no airbag" lawsuit conflicts with the objectives of FMVSS 208, a standard authorized by the Act, and is therefore pre-empted by the Act.

In reaching our conclusion, we consider three subsidiary questions. First, does the Act's express pre-emption provision pre-empt this lawsuit? We think not. Second, do ordinary pre-emption principles nonetheless apply? We hold that they do. Third, does this lawsuit actually conflict with FMVSS 208, hence with the Act itself? We hold that it does.

**1987 Honda Accord**

*Source: Wikimedia Commons*

## II

We first ask whether the Safety Act's express pre-emption provision pre-empts this tort action. The provision reads as follows:

> "Whenever a Federal motor vehicle safety standard established under this subchapter is in effect, no State or political subdivision of a State shall have any authority either to establish, or to continue in effect, with respect to any motor vehicle or item of motor vehicle equipment[,] any safety standard applicable to the same aspect of performance of such vehicle or item of equipment which is not identical to the Federal standard." 215 U.S.C. §1392(d) (1988 ed.).

American Honda points out that a majority of this Court has said that a somewhat similar statutory provision in a different federal statute — a provision that uses the word "requirements" — may well expressly pre-empt similar tort actions. Petitioners reply that this statute speaks of pre-empting a state-law "safety *standard*," not a "requirement," and that a tort action does not involve a safety *standard*. Hence, they conclude, the express pre-emption provision does not apply.

We need not determine the precise significance of the use of the word "standard," rather than "requirement," however, for the Act contains another provision, which resolves the disagreement. That provision, a broad "savings" clause, says that "[c]ompliance with" a federal safety standard "does not exempt any person from any liability under common law." 15 U.S.C. §1397(k) (1988 ed.). The saving clause assumes that there are some significant number of common-law liability cases to save. And a reading of the express pre-emption provision that excludes common-law tort actions gives actual meaning to the saving clause's literal language, while leaving adequate room for state tort law to operate — for example, where federal law creates only a floor, *i.e.*, a minimum safety standard. See, *e.g.*, Brief for United States as Amicus Curiae 21 (explaining that common-law claim that a vehicle is defectively designed because it lacks antilock brakes would not be pre-empted by 49 CFR §571.105 (1999), a safety standard establishing minimum requirements for brake performance). Without the saving clause, a broad reading of the express pre-emption provision arguably might pre-empt those actions, for, as we have just mentioned, it is possible to read the pre-emption provision, standing alone, as applying to standards imposed in common-law tort actions, as well as standards contained in state legislation or regulations. And if so, it would pre-empt all nonidentical state standards established in tort actions covering the same aspect of performance as an applicable federal standard, even if the federal standard merely established a minimum standard. On that broad reading of the pre-emption clause little, if any, potential "liability at common law" would remain. And few, if any, state tort actions would remain for the saving clause to save. We have found no convincing indication that Congress wanted to pre-empt, not only state statutes and regulations, but also common-law tort actions, in such circumstances. Hence the broad reading cannot be correct. The language of the pre-emption provision permits a narrow reading that excludes common-law actions. Given the presence of the saving clause, we conclude that the pre-emption clause must be so read.

## III

We have just said that the saving clause at least removes tort actions from the scope of the express pre-emption clause. Does it do more? In particular, does it foreclose or limit the operation of ordinary pre-emption principles insofar as those principles instruct us to read statutes as pre-empting state laws (including common-law rules) that "actually conflict" with the statute or federal standards promulgated thereunder? . . .

Nothing in the language of the saving clause suggests an intent to save state-law tort actions that conflict with federal regulations. The words "[c]ompliance" and "does not

exempt," sound as if they simply bar a special kind of defense, namely, a defense that compliance with a federal standard automatically exempts a defendant from state law, whether the Federal Government meant that standard to be an absolute requirement or only a minimum one. See Restatement (Third) of Torts: Products Liability §4(b), Comment *e* (1997) (distinguishing between state-law compliance defense and a federal claim of pre-emption). It is difficult to understand why Congress would have insisted on a compliance-with-federal-regulation precondition to the provision's applicability had it wished the Act to "save" all state-law tort actions, regardless of their potential threat to the objectives of federal safety standards promulgated under that Act. . . .

Why, in any event, would Congress not have wanted ordinary pre-emption principles to apply where an actual conflict with a federal objective is at stake? Some such principle is needed. In its absence, state law could impose legal duties that would conflict directly with federal regulatory mandates, say, by premising liability upon the presence of the very windshield retention requirements that federal law requires. . . .

## IV

The basic question, then, is whether a common-law "no airbag" action like the one before us actually conflicts with FMVSS 208. We hold that it does.

In petitioners' and the dissent's view, FMVSS 208 sets a minimum airbag standard. As far as FMVSS 208 is concerned, the more airbags, and the sooner, the better. But that was not the Secretary's view. The Department of Transportation's (DOT's) comments, which accompanied the promulgation of FMVSS 208, make clear that the standard deliberately provided the manufacturer with a range of choices among different passive restraint devices. Those choices would bring about a mix of different devices introduced gradually over time; and FMVSS 208 would thereby lower costs, overcome technical safety problems, encourage technological development, and win widespread consumer acceptance—all of which would promote FMVSS 208's safety objectives.

### A

[A review of the history of the regulation is omitted.]

### B

Read in light of this history, DOT's own contemporaneous explanation of FMVSS 208 makes clear that the 1984 version of FMVSS 208 reflected the following significant considerations. First, buckled up seatbelts are a vital ingredient of automobile safety. . . . Second, despite the enormous and unnecessary risks that a passenger runs by not buckling up manual lap and shoulder belts, more than 80% of front seat passengers would leave their manual seatbelts unbuckled. Third, airbags could make up for the dangers caused by unbuckled manual belts, but they could not make up for them entirely.

Fourth, passive restraint systems had their own disadvantages, for example, the dangers associated with, intrusiveness of, and corresponding public dislike for, nondetachable automatic belts. Fifth, airbags brought with them their own special risks to safety, such as the risk of danger to out-of-position occupants (usually children) in small cars. . . .

Sixth, airbags were expected to be significantly more expensive than other passive restraint devices, raising the average cost of a vehicle price $320 for full frontal airbags over the cost of a car with manual lap and shoulder seatbelts (and potentially much more if production volumes were low). And the agency worried that the high replacement cost—estimated to be $800—could lead car owners to refuse to replace them after deployment. . . .

FMVSS 208 reflected these considerations in several ways. Most importantly, that standard deliberately sought variety — a mix of several different passive restraint systems. It did so by setting a performance requirement for passive restraint devices and allowing manufacturers to choose among different passive restraint mechanisms, such as airbags, automatic belts, or other passive restraint technologies to satisfy that requirement. And DOT explained why FMVSS 208 sought the mix of devices that it expected its performance standard to produce. DOT wrote that it had *rejected* a proposed FMVSS 208 "all airbag" standard because of safety concerns (perceived or real) associated with airbags, which concerns threatened a "backlash" more easily overcome "if airbags" were "not the only way of complying." It added that a mix of devices would help develop data on comparative effectiveness, would allow the industry time to overcome the safety problems and the high production costs associated with airbags, and would facilitate the development of alternative, cheaper, and safer passive restraint systems. And it would thereby build public confidence, necessary to avoid another interlock-type fiasco.

The 1984 FMVSS 208 standard also deliberately sought a *gradual* phase-in of passive restraints. . . .

In effect, petitioners' tort action depends upon its claim that manufacturers had a duty to install an airbag when they manufactured the 1987 Honda Accord. Such a state law — *i.e.*, a rule of state tort law imposing such a duty — by its terms would have required manufacturers of all similar cars to install airbags rather than other passive restraint systems, such as automatic belts or passive interiors. It thereby would have presented an obstacle to the variety and mix of devices that the federal regulation sought.

[Affirmed.]

Stevens, J., dissenting.

Airbag technology has been available to automobile manufacturers for over 30 years. There is now general agreement on the proposition "that, to be safe, a car must have an airbag." Indeed, current federal law imposes that requirement on all automobile manufacturers. The question raised by petitioners' common-law tort action is whether that proposition was sufficiently obvious when Honda's 1987 Accord was manufactured to make the failure to install such a safety feature actionable under theories of negligence or defective design. The Court holds that an interim regulation motivated by the Secretary of Transportation's desire to foster gradual development of a variety of passive restraint devices deprives state courts of jurisdiction to answer that question. I respectfully dissent from that holding, and especially from the Court's unprecedented extension of the doctrine of pre-emption. . . .

## NOTES

**1.** ***State Law "Requirements" and Common Law Duties.*** *Geier* was one of many cases that struggled to set the boundaries of the preemption doctrine. Nine years earlier, in Cipollone v. Liggett Group, Inc., 505 U.S. 504, 521, 524 (1992), the Supreme Court set the stage for the modern developments when, for the first time, it interpreted federal statutory preemptive "requirements" to include common law tort actions. More specifically, the Court held that plaintiff's duty to warn claims against cigarette manufacturers were preempted under the Public Health Cigarette Smoking Act, 15 U.S.C. §§1331–1340, which in section 5(b) provided:

> No requirement or prohibition based on smoking and health shall be imposed under State law with respect to the advertising or promotion of any cigarettes the packages of which are labeled in conformity with the provisions of this Act.

The Court rejected plaintiff's claim that this provision only preempted claims based on state statutes and administrative rules, holding that "those words easily encompass obligations that take the form of common law rules." Thereafter, the Court concluded that plaintiff's failure to warn claims insofar as they "require a showing that respondents' post-1969 advertising or promotions should have included additional, or more clearly stated, warnings . . . are preempted." But this ruling did not preempt, for example, design defect, express warranty, or fraud claims.

The Court turned its back on both *Cipollone* and *Geier* by giving a narrow reading to federal preemption in Bates v. Dow Agrosciences LLC, 544 U.S. 431, 442, 445, 454 (2005). There the petitioners, Texas peanut farmers, sued Dow claiming that their crops were damaged during the 2000 growing season when treated with Dow's Strongarm pesticide, which they claimed stunted their crops and did not kill weeds. Strongarm was marketed with a warning that said: "Use of Strongarm is recommended in all areas where peanuts are grown." The plaintiffs alleged that Strongarm was only appropriate in soils with a pH below 7.0, and not in Texas where the soil had a pH of 7.2. After the initiation of the plaintiffs' suit, Dow changed its warning to read: "Do not apply Strongarm to soils with a pH of 7.2 or greater." Stevens, J., held that the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA), 7 U.S.C. §136 (2024), did not preempt the plaintiff's claim. Its preemption provision provided in section 136v(b): "Such State shall not impose or continue in effect any requirements for labeling or packaging in addition to or different from those required under this subchapter."

Stevens, J., first held that the states have "ample authority" to impose additional sanctions "for violating state rules that merely duplicate federal requirements." He then denied that petitioners' claims for defective design, defective manufacture, negligent testing, and breach of express warranty were preempted, but he remanded the case to see if the plaintiff's duty to warn claims were preempted.

Would any of these claims have survived if Strongarm had been originally marketed with a warning that said the product was not to be used in soil with a pH over 7.2? If not, then why doesn't the comprehensive federal control over warnings trigger the application of conflict preemption?

**2.** ***Deference to the Regulating Federal Agency.*** In Sprietsma v. Mercury Marine, 537 U.S. 51, 54, 60 (2002), a unanimous Supreme Court held that the Federal Boat Safety Act of 1971, 46 U.S.C. §§4301–4311 (2024), and the regulations promulgated under it, did not preempt a state tort action brought on behalf of a decedent who was killed when she fell overboard from "an 18-foot ski boat equipped with a 115-horsepower outboard motor manufactured by [defendant]." As in *Geier*, the FBSA contained a preemption clause that forbade the state imposition of requirements that were not "identical" to those contained in the federal regulation. That clause was coupled with a savings clause for common law actions. As in *Geier*, the Secretary of Transportation conducted an exhaustive safety study, but refused to issue any regulations that mandated propeller guards because the data were insufficient to resolve the key tradeoff: "[G]iven current technology, feasible propeller guards might prevent penetrating injuries but increase the potential for blunt trauma caused by collision with the guard, which enlarges the boat's underwater profile." Stevens, J., allowed the action to go forward out of deference to the agency's explanation of its decision not to regulate:

> The agency is likely to have a thorough understanding of its own regulation and its objectives and is "uniquely qualified" to comprehend the likely impact of state requirements. In the case before us today, the Solicitor General, joined by counsel for the Coast Guard, has informed us that the agency does not view the 1990 refusal to regulate or any subsequent regulatory actions by the Coast Guard as having any pre-emptive effect.

Should it matter that the Coast Guard waited until after the Supreme Court granted certiorari in *Sprietsma* to elaborate its view? Catherine M. Sharkey, Products Liability Preemption: An

Institutional Approach, *supra*, highlights the influence of the underlying federal regulator in preemption disputes.

**3. Geier *Revisited.*** The continued vitality of *Geier* was tested in Williamson v. Mazda Motor of America, Inc., 562 U.S. 323, 332 (2011). Thanh Williamson was a passenger in the rear aisle seat of a Mazda minivan. While wearing a lap belt, she was killed when the minivan was struck head-on by another car. FMVSS 208 requires auto manufacturers to install lap-and-shoulder belts on those seats located next to the doors or frames of any vehicle. But with respect to the inside rear seats, including Williamson's aisle seat, the regulation gave the manufacturers the choice of installing either lap belts or lap-and-shoulder belts. Willamson's estate claimed that Mazda should have installed lap-and-shoulder belts, not lap belts, on all rear inner seats. The trial court dismissed the tort claim; the California appellate court affirmed, concluding that, as in *Geier*, the choice explicitly reserved to the manufacturer under federal regulation preempted the state tort suit. The Supreme Court unanimously allowed the state tort claim to proceed. Breyer, J., explained: "Like the regulation in *Geier*, the regulation here leaves the manufacturer with a choice. And, like the tort suit in *Geier*, the tort suit here would restrict that choice. But unlike *Geier*, we do not believe here that choice is a significant regulatory objective," as the agency's choice did not involve the timing of the introduction of a new technology, such as airbags, into the market. Continuing the Court's trend of agency deference, Breyer, J., was swayed by "the promulgating agency's contemporaneous explanation of its objectives, and the agency's current views of the regulation's pre-emptive effect." Should an agency be required to state in advance whether it attaches preemptive weight to its regulation?

Following cues from *Sprietsma* and *Williamson*, the Supreme Court of Arizona recently held that the National Highway Traffic Safety Administration had not established clear policy objectives sufficient to preempt state tort claims alleging failure to install automatic emergency braking technologies. Varela v. FCA US LLC, 505 P.3d 244 (Ariz. 2022). Is it ever safe for a manufacturer to take advantage of any low-cost option left to it under federal regulation?

## *Wyeth v. Levine*

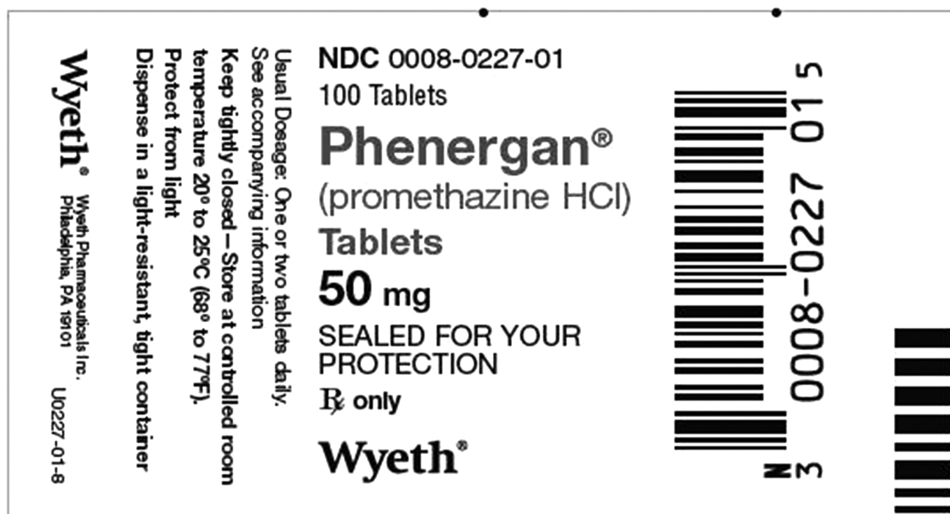
555 U.S. 555 (2009)

Stevens, J. Directly injecting the drug Phenergan into a patient's vein creates a significant risk of catastrophic consequences. A Vermont jury found that petitioner Wyeth, the manufacturer of the drug, had failed to provide an adequate warning of that risk and awarded damages to respondent Diana Levine to compensate her for the amputation of her arm. The warnings on Phenergan's label had been deemed sufficient by the federal Food and Drug Administration (FDA) when it approved Wyeth's new drug application in 1955 and when it later approved changes in the drug's labeling. The question we must decide is whether the FDA's approvals provide Wyeth with a complete defense to Levine's tort claims. We conclude that they do not.

### I

Phenergan is Wyeth's brand name for promethazine hydrochloride, an antihistamine used to treat nausea. The injectable form of Phenergan can be administered intramuscularly or intravenously, and it can be administered intravenously through either the "IV-push" method, whereby the drug is injected directly into a patient's vein, or the "IV-drip" method, whereby the drug is introduced into a saline solution in a hanging intravenous bag and slowly descends through a catheter inserted in a patient's vein. The drug is corrosive and causes irreversible gangrene if it enters a patient's artery.

Levine's injury resulted from an IV-push injection of Phenergan. On April 7, 2000, as on previous visits to her local clinic for treatment of a migraine headache, she received an




**Phenergan label**

*Source: National Institutes of Health*

intramuscular injection of Demerol for her headache and Phenergan for her nausea. Because the combination did not provide relief, she returned later that day and received a second injection of both drugs. This time, the physician assistant administered the drugs by the IV-push method, and Phenergan entered Levine's artery, either because the needle penetrated an artery directly or because the drug escaped from the vein into surrounding tissue (a phenomenon called "perivascular extravasation") where it came in contact with arterial blood. As a result, Levine developed gangrene, and doctors amputated first her right hand and then her entire forearm. In addition to her pain and suffering, Levine incurred substantial medical expenses and the loss of her livelihood as a professional musician.

[In part the warning provided:

> Due to the close proximity of arteries and veins in the areas most commonly used for intravenous injection, extreme care should be exercised to avoid perivascular extravasation or inadvertent intra-arterial injection. Reports compatible with inadvertent intra-arterial injection of Phenergan Injection, usually in conjunction with other drugs intended for intravenous use, suggest that pain, severe chemical irritation, severe spasm of distal vessels, and resultant gangrene requiring amputation are likely under such circumstances. . . . Phenergan Injection should be given in a concentration no greater than 25 mg per mL and at a rate not to exceed 25 mg per minute. When administering any irritant drug intravenously, it is usually preferable to inject it through the tubing of an intravenous infusion set that is known to be functioning satisfactorily. In the event that a patient complains of pain during intended intravenous injection of Phenergan Injection, the injection should be stopped immediately to provide for evaluation of possible arterial placement or perivascular extravasation.

The physician's assistant injected the Phenergan into an artery at a rate of 100 mg per minute. She did not use any tubing and did not stop when the patient complained of pain.]

After settling claims against the health center and clinician, Levine brought an action for damages against Wyeth, relying on common-law negligence and strict-liability theories. Although Phenergan's labeling warned of the danger of gangrene and amputation following inadvertent intra-arterial injection, Levine alleged that the labeling was defective because it failed to instruct clinicians to use the IV-drip method of intravenous administration instead of

the higher risk IV-push method. More broadly, she alleged that Phenergan is not reasonably safe for intravenous administration because the foreseeable risks of gangrene and loss of limb are great in relation to the drug's therapeutic benefits. . . .

[The jury awarded the plaintiff $7,400,000, which was reduced by the $700,000 the plaintiff had obtained in settlement from the health clinic.]

## II

. . . Our [analysis] must be guided by two cornerstones of our pre-emption jurisprudence. First, "the purpose of Congress is the ultimate touchstone in every pre-emption case." Second, "[i]n all pre-emption cases, and particularly in those in which Congress has 'legislated . . . in a field which the States have traditionally occupied,' . . . we 'start with the assumption that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress.'"

[A review of the history of federal regulation of drugs and drug labeling is omitted.]

## III

Wyeth first argues that Levine's state-law claims are pre-empted because it is impossible for it to comply with both the state-law duties underlying those claims and its federal labeling duties. The FDA's premarket approval of a new drug application includes the approval of the exact text in the proposed label. Generally speaking, a manufacturer may only change a drug label after the FDA approves a supplemental application. There is, however, an FDA regulation that permits a manufacturer to make certain changes to its label before receiving the agency's approval. Among other things, this "changes being effected" (CBE) regulation provides that if a manufacturer is changing a label to "add or strengthen a contraindication, warning, precaution, or adverse reaction" or to "add or strengthen an instruction about dosage and administration that is intended to increase the safe use of the drug product," it may make the labeling change upon filing its supplemental application with the FDA; it need not wait for FDA approval.

. . . Levine . . . present[ed] evidence of at least 20 incidents prior to her injury in which a Phenergan injection resulted in gangrene and an amputation. After the first such incident came to Wyeth's attention in 1967, it notified the FDA and worked with the agency to change Phenergan's label. In later years, as amputations continued to occur, Wyeth could have analyzed the accumulating data and added a stronger warning about IV-push administration of the drug.

. . . Wyeth suggests that the FDA, rather than the manufacturer, bears primary responsibility for drug labeling. Yet through many amendments to the FDCA and to FDA regulations, it has remained a central premise of federal drug regulation that the manufacturer bears responsibility for the content of its label at all times. It is charged both with crafting an adequate label and with ensuring that its warnings remain adequate as long as the drug is on the market. . . .

Of course, the FDA retains authority to reject labeling changes made pursuant to the CBE regulation in its review of the manufacturer's supplemental application, just as it retains such authority in reviewing all supplemental applications. But absent clear evidence that the FDA would not have approved a change to Phenergan's label, we will not conclude that it was impossible for Wyeth to comply with both federal and state requirements. . . .

Impossibility pre-emption is a demanding defense. On the record before us, Wyeth has failed to demonstrate that it was impossible for it to comply with both federal and state requirements. The CBE regulation permitted Wyeth to unilaterally strengthen its warning, and the mere fact that the FDA approved Phenergan's label does not establish that it would have prohibited such a change.

## IV

Wyeth also argues that requiring it to comply with a state-law duty to provide a stronger warning about IV-push administration would obstruct the purposes and objectives of federal drug labeling regulation. Levine's tort claims, it maintains, are pre-empted because they interfere with "Congress's purpose to entrust an expert agency to make drug labeling decisions that strike a balance between competing objectives." We find no merit in this argument, which relies on an untenable interpretation of congressional intent and an overbroad view of an agency's power to pre-empt state law.

Wyeth contends that the FDCA establishes both a floor and a ceiling for drug regulation: Once the FDA has approved a drug's label, a state-law verdict may not deem the label inadequate, regardless of whether there is any evidence that the FDA has considered the stronger warning at issue. The most glaring problem with this argument is that all evidence of Congress' purposes is to the contrary. Building on its 1906 Act, Congress enacted the FDCA to bolster consumer protection against harmful products. Congress did not provide a federal remedy for consumers harmed by unsafe or ineffective drugs in the 1938 statute or in any subsequent amendment. Evidently, it determined that widely available state rights of action provided appropriate relief for injured consumers. It may also have recognized that state-law remedies further consumer protection by motivating manufacturers to produce safe and effective drugs and to give adequate warnings.

If Congress thought state-law suits posed an obstacle to its objectives, it surely would have enacted an express pre-emption provision at some point during the FDCA's 70-year history. . . . Its silence on the issue, coupled with its certain awareness of the prevalence of state tort litigation, is powerful evidence that Congress did not intend FDA oversight to be the exclusive means of ensuring drug safety and effectiveness. . . .

[Justice Stevens then rejects the argument that a 2006 preamble to an FDA regulation is sufficient to interpret the FDCA as setting "both a 'floor' and a 'ceiling,'" so that "FDA approval of labeling . . . preempts conflicting or contrary State law." He then held that the preamble is "at odds with what evidence we have of Congress' purposes, and . . . reverses the FDA's own longstanding position without providing a reasoned explanation, including any discussion of how state law has interfered with the FDA's regulation of drug labeling during decades of coexistence."]

In short, Wyeth has not persuaded us that failure-to-warn claims like Levine's obstruct the federal regulation of drug labeling. Congress has repeatedly declined to pre-empt state law, and the FDA's recently adopted position that state tort suits interfere with its statutory mandate is entitled to no weight. Although we recognize that some state-law claims might well frustrate the achievement of congressional objectives, this is not such a case.

[Affirmed.]

Alito, J., dissenting.

## I

The court frames the question presented as a "narro[w]" one — namely, whether Wyeth has a duty to provide "an adequate warning about using the IV-push method" to administer Phenergan. But that ignores the antecedent question of who — the FDA or a jury in Vermont — has the authority and responsibility for determining the "adequacy" of Phenergan's warnings. Moreover, it is unclear how a "stronger" warning could have helped respondent; after all, the physician's assistant who treated her disregarded at least six separate warnings that are already on Phenergan's labeling, so respondent would be hard pressed to prove that a seventh would have made a difference.

More to the point, the question presented by this case is not a "narrow" one, and it does not concern whether Phenergan's label should bear a "stronger" warning. Rather, the real issue is whether a state tort jury can countermand the FDA's considered judgment that Phenergan's FDA-mandated warning label renders its intravenous (IV) use "safe." Indeed, respondent's amended complaint alleged that Phenergan is "not reasonably safe for intravenous administration," respondent's attorney told the jury that Phenergan's label should say, "'Do not use this drug intravenously,'"; respondent's expert told the jury, "I think the drug should be labeled 'Not for IV use,'" and during his closing argument, respondent's attorney told the jury, "Thank God we don't rely on the FDA to . . . make the safe[ty] decision. You will make the decision. . . . The FDA doesn't make the decision, you do."

Federal law, however, *does* rely on the FDA to make safety determinations like the one it made here. The FDA has long known about the risks associated with IV push in general and its use to administer Phenergan in particular. Whether wisely or not, the FDA has concluded — over the course of extensive, 54-year-long regulatory proceedings — that the drug is "safe" and "effective" when used in accordance with its FDA-mandated labeling. The unfortunate fact that respondent's healthcare providers ignored Phenergan's labeling may make this an ideal medical malpractice case. But turning a common-law tort suit into a "frontal assault" on the FDA's regulatory regime for drug labeling upsets the well-settled meaning of the Supremacy Clause and our conflict pre-emption jurisprudence.

## II

### A

To the extent that the purpose of Congress is the ultimate touchstone in every preemption case, Congress made its "purpose" plain in authorizing the FDA — not state tort juries — to determine when and under what circumstances a drug is "safe." "[T]he process for approving new drugs is at least as rigorous as the premarket approval process for medical devices," Riegel v. Medtronic, Inc., 552 U.S. 312, 343 (2008) (Ginsburg, J., dissenting), and we held that the latter pre-empted a state-law tort suit that conflicted with the FDA's determination that a medical device was "safe." [Alito, J., sets forth the lengthy FDCA approval process.]

## III

[Part A provides a detailed account of the FDA's regulatory oversight of the Phenergan warning. Alito, J., argues that the FDA did in fact consider the costs and benefits associated with IV push.]

### B

Given the "balance" that the FDA struck between the costs and benefits of administering Phenergan via IV push, *Geier* compels the pre-emption of tort suits (like this one) that would upset that balance. The contrary conclusion requires turning yesterday's dissent into today's majority opinion. . . .

*Geier* does not countenance the use of state tort suits to second-guess the FDA's labeling decisions. And the Court's contrary conclusion has potentially far-reaching consequences.

### C

By their very nature, juries are ill-equipped to perform the FDA's cost-benefit-balancing function. . . . [J]uries tend to focus on the risk of a particular product's design or warning label that arguably contributed to a particular plaintiff's injury, not on the overall benefits of that design or label; "the patients who reaped those benefits are not represented in court." Indeed,

patients like respondent are the only ones whom tort juries ever see, and for a patient like respondent — who has already suffered a tragic accident — Phenergan's risks are no longer a matter of probabilities and potentialities.

In contrast, the FDA has the benefit of the long view. Its drug-approval determinations consider the interests of all potential users of a drug, including "those who would suffer without new medical [products]" if juries in all 50 States were free to contradict the FDA's expert determinations. And the FDA conveys its warnings with one voice, rather than whipsawing the medical community with 50 (or more) potentially conflicting ones. After today's ruling, however, parochialism may prevail. . . .

To be sure, state tort suits can peacefully coexist with the FDA's labeling regime, and they have done so for decades. But this case is far from peaceful coexistence. The FDA told Wyeth that Phenergan's label renders its use "safe." But the State of Vermont, through its tort law, said: "Not so."

The state-law rule at issue here is squarely pre-empted. Therefore, I would reverse the judgment of the Supreme Court of Vermont.

## NOTES

**1.** ***Drug and Medical Device Preemption.*** *Levine* forms a key part in a succession of high-stakes litigation over the extensive federal regulatory scheme for new drugs and medical devices. The saga starts with Medtronic, Inc. v. Lohr, 518 U.S. 470, 489 (1996), in which the plaintiff sued on a variety of failure to warn and design defect theories when her pacemaker failed, requiring emergency surgery. The Medical Device Amendment Act (MDA), 21 U.S.C. §360k(a), reads:

> [N]o State or political subdivision of a State may establish or continue in effect with respect to a device intended for human use any requirement (1) which is different from, or in addition to, any requirement applicable under [the MDA] to the device, and (2) which relates to the safety or effectiveness of the device or to any other matter included in a requirement applicable to the device under [the MDA].

The pre-market notification process is an abbreviated review of the product lasting an average of twenty hours, under which the FDA undertakes no tests or systematic review of product safety but allows for the marketing of the product as long as it is "substantially equivalent" to a pre-1976 product already on the market, at least until the earlier product is required to undergo a pre-market approval (PMA) process. Stevens, J., relied on *Rice*'s presumption against preemption to hold that the pre-market notification process did not preempt either the duty to warn or manufacturing defect claims, but only prohibited those design defect actions that specifically targeted medical devices for special treatment. "Given the ambiguities in the statute and the scope of the preclusion that would occur otherwise, we cannot accept Medtronic's argument that by using the term 'requirement,' Congress clearly signaled its intent to deprive States of any role in protecting consumers from the dangers inherent in many medical devices."

The preemptive effect of the MDA was back before the Supreme Court in Riegel v. Medtronic, Inc., 552 U.S. 312 (2008). There the plaintiff was injured when a cardiologist used Medtronic's FDA-approved Evergreen Balloon Catheter to perform an angioplasty — designed to clear clogged arteries — at a pressure of ten atmospheres when it was only rated for use at eight atmospheres. The overinflated balloon ruptured inside the plaintiff, causing serious injuries. The question before the Supreme Court was not the state law tort question

whether the overinflation counted as a product misuse that severed causal connection. Rather it was whether, in light of *Lohr*, the Medical Device Act "preempts state-law claims seeking damages for injuries caused by medical devices that received premarket approval from the Food and Drug Administration." Unlike pre-market notification, the PMA process involves an exhaustive review of product design and data, because the balloon catheter was classified as a potentially dangerous, or Class III, device that required intensive scrutiny because of the serious risk its use posed to human life and health. As in *Lohr*, the Court assumed that the "requirements" under state law included private law actions. Scalia, J., in an eight-to-one decision (with Ginsburg, J., dissenting) found that the "rigorous process" of FDA review, which required an average of 1,200 hours per submission, dictated preemption. He noted that a jury should not be allowed to second guess the explicit decision of the agency, which included extensive post-market surveillance and regulated product advertisement.

To what extent does preemption protection for medical device manufacturers increase pressure on physicians subject to malpractice claims? Elissa P. Gentry & Benjamin J. McMichael, Responses to Liability Immunization: Evidence from Medical Devices, 17 J. Empirical Legal Stud. 789 (2020), provides some evidence that "physicians in high-malpractice-pressure states change their treatment plans to reduce the use of medical devices, relative to physicians in low-malpractice-pressure states."

To avoid express preemption under the MDA, plaintiffs have brought forward novel claims based on the manufacturer's failure to warn the FDA of risks that emerge postapproval. In Glover v. Bausch & Lomb, Inc., 6 F.4th 229, 239 (2d Cir. 2021), the plaintiff, who suffered pain and loss of vision after she was implanted with Trulign Toric intraocular lenses in both of her eyes to correct her vision following cataract surgery, alleged that the defendant Bausch & Lomb failed to warn the FDA of known safety risks and failed to comply with the FDA's postapproval safety requirements. Thus framed, the plaintiff contended that her negligence and failure-to-warn claims should "proceed under traditional tort law and are not a veiled attempt to enforce federal requirements that Congress has not provided a private right of action to enforce." Lynch, J., certified to the Connecticut Supreme Court the question whether Connecticut recognized such a state law claim. The Connecticut Supreme Court responded in the affirmative, holding that "defendants had a duty under the [Connecticut Product Liability Act] to comply with federal statutes and regulations requiring them to report adverse events . . . to the FDA and to comply with the FDA's postapproval requirements in a timely manner." Glover v. Bausch & Lomb, Inc., 275 A.3d 168, 172 (Conn. 2022).

Academic writing has taken varying positions on FDA preemption. Richard A. Nagareda, FDA Preemption: When Tort Law Meets the Administrative State, J. Tort L. (Dec. 4, 2006), at 1, proposes that FDA preemption be conditioned on the willingness of drug companies to supply further information about their products to the public at large. In response, see Richard A. Epstein, Why the FDA Must Preempt Tort Litigation: A Critique of *Chevron* Deference and a Response to Richard Nagareda, J. Tort L. (Dec. 4, 2006), at 1, urging a return to the field preemption doctrine. Catherine M. Sharkey, Products Liability Preemption: An Institutional Approach, *supra* at 44, suggests that the court should scrutinize the agency record and give deference to the agency only to the extent that the agency considered the precise risk at issue in the suit.

**2. *Levine's "Clear Evidence" Rule Revisited.*** In Merck Sharp & Dohme Corp. v. Albrecht, 587 U.S. 299, 303, 316 (2019), the Supreme Court clarified the "clear evidence" standard articulated in *Levine*, explaining:

> "Clear evidence" . . . is evidence that shows the court that the drug manufacturer fully informed the FDA of the justifications for the warning required by state law and that the FDA, in turn, informed the drug manufacturer that the FDA would not approve a change to the drug's label to include that warning.

The Court also held that judges, rather than juries, should determine what constitutes "clear evidence." Breyer, J., explained:

> The complexity of the . . . law helps to illustrate why we answer this question by concluding that the question is a legal one for the judge, not a jury. The question often involves the use of legal skills to determine whether agency disapproval fits facts that are not in dispute. Moreover, judges, rather than lay juries, are better equipped to evaluate the nature and scope of an agency's determination. Judges are experienced in [t]he construction of written instruments, such as those normally produced by a federal agency to memorialize its considered judgments. And judges are better suited than are juries to understand and to interpret agency decisions in light of the governing statutory and regulatory context. To understand the question as a legal question for judges makes sense given the fact that judges are normally familiar with principles of administrative law. Doing so should produce greater uniformity among courts; and greater uniformity is normally a virtue when a question requires a determination concerning the scope and effect of federal agency action.

**3.** ***Vaccines and Preemption.*** The case for preemption of tort law claims is stronger for vaccines than for other pharmaceutical drugs. First, the National Childhood Vaccine Injury Act of 1986 includes an express preemption provision:

> No vaccine manufacturer shall be liable in a civil action for damages arising from a vaccine-related injury or death associated with the administration of a vaccine . . . if the injury or death resulted from side effects that were unavoidable even though the vaccine was properly prepared and was accompanied by proper directions and warnings.

42 U.S.C. §300aa-22(b)(1) (2024).

Second, Congress established a no-fault vaccine injury compensation fund to provide substitute remedies.

In Bruesewitz v. Wyeth LLC, 562 U.S. 223, 239, 251 (2011), Hannah, a seemingly healthy infant, suffered violent seizures following her injection with Tri-Immunol, a "whole cell" diphtheria, tetanus, and pertussis (DTP) vaccine manufactured by Wyeth. The Bruesewitzes claimed that Tri-Immunol was defective and that Wyeth had, at the relevant time, an approved license for Tri-Solgen, an alternative, safer "fractionated" DTP vaccine.

Scalia, J., writing for a five-member majority, engaged in a close textualist reading of the "concessive subordinate clause," to conclude that the statute categorically preempts liability for design defects, while leaving intact liability for manufacturing defects and failure to warn claims. According to Scalia, J., Congress intended to impose this "quid pro quo": "The vaccine manufacturers fund from their own sales an informal, efficient compensation program for vaccine injuries; in exchange they avoid costly tort litigation and the occasional disproportionate jury verdict." And (sounding a theme similar to that of Alito, J., in his *Levine* dissent) Congress expressed a preference, "a sensible choice to leave complex epidemiological judgments about vaccine design to the FDA and the National Vaccine Program rather than juries." Sotomayor, J., dissented on the ground that "Congress must . . . have intended a vaccine manufacturer to demonstrate in each civil action that the particular side effects of a vaccine's design were 'unavoidable[,]'" and the majority's alternative reading "leaves a regulatory vacuum in which no one ensures that vaccine manufacturers adequately take account of scientific and technological advancements when designing or distributing their products." How should this preemption provision apply to "avoidable" side effects? Does the provision do any work if the FDA warnings are not deemed proper in all cases?

**4.** ***Generic Drugs and Preemption.*** Should the fact that generic drugs are subject to a different regulatory framework from brand-name drugs affect the preemption analysis? Instead of a lengthy pre-market approval process used for brand-name drugs, generics go through an abbreviated review process that tests the product only for bioequivalence with its

branded counterpart. The packaging for the generic must also be sent to the FDA, 21 U.S.C. §355(j)(2)(A)(v), and the label for the generic must match the label for the branded drug. 21 C.F.R. §314.127(a)(7).

In PLIVA, Inc. v. Mensing, 564 U.S. 604, 623–24 (2011), Gladys Mensing and Julie Demahy sued the generic drug manufacturers of metoclopramide for failing to adequately warn of the danger that long-term use of the drug could result in tardive dyskinesia, a severe neurological disorder. The manufacturers raised preemption as a defense, arguing that, because the federal statutes and FDA regulations required them to use the same labeling as their brand-name counterparts, it was impossible for them to comply with both federal law and any state tort law duty that required them to use a different label. In a sharply divided five-to-four decision, Thomas, J., upheld the impossibility preemption defense. Thomas, J., recognized that immunizing generic but not brand-name drug manufacturers from state tort liability "makes little sense" insofar as afflicted individuals who took generic drugs are denied the remedies available to persons who receive brand-name drugs. But he insisted that it was not the Court's role to correct or reinterpret statutory schemes established by Congress that clearly preempted claims against the generic manufacturers. Sotomayor, J., again wrote in dissent, claiming that the majority opinion had cut back on the burden to receive the otherwise narrow impossibility defense of *Levine*, given that "generic manufacturers of metoclopramide (Manufacturers) have shown only that they *might* have been unable to comply with both federal law and their state-law duties to warn respondents Gladys Mensing and Julie Demahy."

Thereafter, in Mutual Pharmaceutical Co., Inc. v. Bartlett, 570 U.S. 472 (2013), Alito, J., held (in another sharply divided five-to-four decision) "that [the New Hampshire] state-law design-defect claims that turn on the adequacy of a drug's warnings are pre-empted by federal law under *PLIVA*." In so doing, he noted that impossibility preemption was appropriate because it precluded actions that required the generic drug manufacturer either to redesign the drug or to strengthen its warning. Breyer, J., dissented on the ground that the state law litigation could properly "supplement" the FDA's regulatory activities.

Should it make a difference that generic manufacturers may market their drugs if they meet a statutory requirement that they be "the same" as the branded drug? Is uniformity in warnings important? Can it be preserved if each of ten or more generic manufacturers has an independent duty to update warnings?

In the wake of *PLIVA* and *Bartlett*, plaintiffs have sought to hold manufacturers of brand-name drugs liable for failing to warn of harms suffered by using generics, whose labels copied that of the brand-name drugs. In T.H. v. Novartis Pharmaceuticals Corp., 407 P.3d 18, 31 (Cal. 2017), Cuéllar, J., imposed such "innovator liability" on the brand-name manufacturer:

> Time and again we have recognized how "[t]he overall policy of preventing future harm is ordinarily served, in tort law, by imposing the costs of negligent conduct upon those responsible." A brand-name drug manufacturer is not only in the best position to warn of a drug's harmful effects: It is also the only manufacturer with the unilateral authority under federal law to issue such a warning for the brand-name drug or its generic bioequivalent.

The Third Restatement has recently embraced such claims under the somewhat forgotten theory of negligent misrepresentation. RTT: Miscellaneous Provisions Ch. 3. §18A, cmt. *q* (Tentative Draft 2023).

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: MISCELLANEOUS PROVISIONS (TENTATIVE DRAFT 2023)**

**§18a. Negligent Misrepresentation Causing Physical Harm**

(a) An actor who negligently furnishes false information is subject to liability for any physical harm factually caused by another's reliance on the information that is within the actor's scope of liability.

What should be done if the brand pharmaceutical company has stopped making the drug once the generic has entered the market? Does it make sense to hold a firm with 10 percent of the market liable for all misstatements in the labels issued by generic manufacturers? For exhaustive commentary, see Lars Noah, "Market Shift Liability": Market Share Theory's Still More Radical Claim, 92(3) Tenn. L. Rev. (forthcoming 2025).

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# CHAPTER 3

# MISREPRESENTATION

## SECTION A. INTRODUCTION

All civil societies prohibit at least two forms of harmful conduct—aggression and deceit. Sometimes the two are very much intertwined: The assailant who feints before he throws a blow combines both wrongs in a single act. Even with accidental harms, force and misrepresentation often work in tandem. Thus a misrepresentation forms one link in the chain of causation when physical injuries are attributable to latent defects in the defendant's premises or products, when both appear to be safe but are not. Similarly, informed consent suits against physicians and duty to warn cases against product manufacturers arise from, if not express misrepresentations, then either implied representations from product appearance or from inadequate disclosures where there is a duty to speak. Finally, misrepresentations can play a critical role in the law of defamation, when a defendant's false statement leads a third party to avoid interacting in either business or social contexts with the plaintiff.

Oddly enough, though, none of these scenarios are addressed by the traditional tort of misrepresentation, which limits itself to cases where a plaintiff claims *economic*, namely *pecuniary or commercial*, loss because she acted, to her detriment, in reliance on the defendant's misrepresentation. See RTT: LEH §9. Typical situations covered by the tort of misrepresentation include entering into a losing contract or making cash advances in reliance on the defendant's false statements. Usually the plaintiff is required to show not only that she was misled by the defendant's misstatements, but also that the defendant knew that his statements were false, or at least was indifferent to their truth or falsity. See RTT: LEH §10.

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§9. Fraud**

One who fraudulently makes a material misrepresentation of fact, opinion, intention, or law, for the purpose of inducing another to act or refrain from acting, is subject to liability for economic loss caused by the other's justifiable reliance on the misrepresentation.

**§10. Scienter**

A misrepresentation is fraudulent if the maker of it

(a) knows or believes that the matter is not as he represents it to be,

(b) knows that he does not have the confidence in the accuracy of his representation that he states or implies, or

(c) knows that he does not have the basis for the representation that he states or implies.

The first section of the following materials is devoted to the law of fraud, and the second to the law of negligent misrepresentation.



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## SECTION B. FRAUD

### 1. Misrepresentation and Scienter

### *Pasley v. Freeman*

100 Eng. Rep. 450 (K.B. 1789)

[The plaintiffs were merchants who asked the defendant about the financial condition of John Christopher Falch before selling Falch a large amount of goods on credit. Plaintiffs alleged that the defendant "did wrongfully and deceitfully encourage and persuade the said John Pasley and Edward, to sell and deliver to the said John Christopher Falch divers other goods, wares and merchandizes, to wit, 16 other bags of cochineal of great value, to wit, of the value of [about £2,634] upon trust and credit; and did for that purpose then and there falsely, deceitfully, and fraudulently, assert and affirm to the said John Pasley and Edward, that the said John Christopher then and there was a person safely to be trusted and given credit in that respect." The plaintiffs further alleged that they sold the goods on credit, but that Falch, as the defendant had known all along, was a bad credit risk, wholly unable to pay for the goods; in fact he paid for no part of them. The plaintiffs sued the defendant to recover from him the value of the goods sold and delivered to Falch. Verdict for the plaintiffs.]

The Court took time to consider of this matter, and now delivered their opinions seriatim.

Grose, J. [finding for the defendant] Upon the face of this count in the declaration, no privity of contract is stated between the parties. No consideration arises to the defendant; and he is in no situation in which the law considers him in any trust, or in which it demands from him any account of the credit of Falch. He appears not to be interested in any transaction between the plaintiffs and Falch, nor to have colluded with them; but he knowingly asserted a falsehood, by saying that Falch might be safely entrusted with the goods, and given credit to, for the purpose of inducing the plaintiffs to trust him with them, by which the plaintiffs lost the value of the goods. . . . It is admitted, that the action is new in point of precedent: but it is insisted that the law recognises principles on which it may be supported. The principle on which it is contended to lie is, that wherever deceit or falsehood is practised to the detriment of another, the law will give redress. . . . When this was first argued at the Bar, on the motion for a new trial, I confess I thought it reasonable that the action should lie: but, on looking into the old books for cases in which the old action of deceit has been maintained upon the false affirmation of the defendant, I have changed my opinion. . . . I have not met with any case of an action upon a false affirmation, except against a party to a contract, and where there is a promise, either express or implied, that the fact is true, which is misrepresented: and no other case has been cited at the Bar. Then if no such case has ever existed, it furnishes a strong objection against the action, which is brought for the first time for a supposed injury, which has been daily committed for centuries past: . . . A variety of cases may be put: suppose a man recommends an estate to another, as knowing it to be of greater value than it is; when the purchaser has bought it, he discovers the defect, and sells the estate for less than he gave; why may not an action be brought for the loss upon any principle that will support this action? And yet such an action has never been attempted. Or, suppose a person present at the sale of an horse asserts that he was his horse, and that he knows him to be sound and sure-footed, when in fact the horse is neither the one nor the other; according to the principle contended for by the plaintiffs, an action lies against the person present as well as the seller; and the purchaser has two securities. And even in this

very case, if the action lies, the plaintiffs will stand in a peculiarly fortunate predicament, for then they will have the responsibility both of Falch and the defendant. And they will be in a better situation than they would have been if, in the conversation that passed between them and the defendant, instead of asserting that Falch might safely be trusted, the defendant had said, "If he do not pay for the goods, I will": for then undoubtedly an action would not have lain against the defendant. . . . The misrepresentation stated in the declaration is respecting the credit of Falch; the defendant asserted that the plaintiffs might safely give him credit: but credit to which a man is entitled is matter of judgment and opinion, on which different men might form different opinions, and upon which the plaintiffs might form their own; to mislead which no fact to prove the good credit of Falch is falsely asserted. It seems to me therefore that any assertion relative to credit, especially where the party making it has no interest, nor is in any collusion with the person respecting whose credit the assertion is made, is . . . not an assertion of a fact peculiarly in the knowledge of the defendant. Whether Falch deserved credit depended on the opinion of many; for credit exists on the good opinion of many. Respecting this, the plaintiffs might have inquired of others, who knew as much as the defendant; it was their fault that they did not, and they have suffered damage by their own laches. It was owing to their own gross negligence that they gave credence to the assertion of the defendant, without taking pains to satisfy themselves that that assertion was founded in fact, as in the case of Bayly v. Merrel. I am therefore of opinion, that this action is as novel in principle as it is in precedent, that it is against the principles to be collected from analogous cases, and consequently that it cannot be maintained.

Buller, J. [finding for the plaintiff] The foundation of this action is fraud and deceit in the defendant, and damage to the plaintiffs. And the question is, whether an action thus founded can be sustained in a Court of Law? Fraud without damage, or damage without fraud, gives no cause of action; but where these two concur, an action lies. But it is contended, that this was a bare naked lie; that, as no collusion with Falch is charged, it does not amount to a fraud: and, if there were any fraud, the nature of it is not stated. And it was supposed by the counsel who originally made the motion, that no action could be maintained, unless the defendant, who made this false assertion, had an interest in so doing. I agree that an action cannot be supported for telling a bare naked lie; but that I define to be, saying a thing which is false, knowing or not knowing it to be so, and without any design to injure, cheat, or deceive, another person. Every deceit comprehends a lie; but a deceit is more than a lie on account of the view with which it is practised, it's being coupled with some dealing, and the injury which it is calculated to occasion, and does occasion, to another person. Deceit is a very extensive head in the law; and it will be proper to take a short view of some of the cases which have existed on the subject, to see how far the Courts have gone, and what are the principles upon which they have decided. [Buller, J., reviewed the precedents and concluded that proof of collusion or conspiracy was not necessary to make out an action for deceit.] Some general arguments were urged at the Bar, to shew that mischiefs and inconveniences would arise if this action were sustained; for if a man, who is asked a question respecting another's responsibility, hesitate, or is silent, he blasts the character of the tradesman: and if he say that he is insolvent, he may not be able to prove it. But let us see what is contended for: it is nothing less than that a man may assert that which he knows to be false, and thereby do an everlasting injury to his neighbour, and yet not be answerable for it. This is as repugnant to law as it is to morality. Then it is said, that the plaintiffs had no right to ask the question of the defendant. But I do not agree in that; for the plaintiffs had an interest in knowing what the credit of Falch was. It was not the inquiry of idle curiosity, but it was to govern a very extensive concern. The defendant undoubtedly had his option to give an answer to the question, or not: but if he gave none, or said he did not know, it is impossible for any Court of Justice to adopt the possible inferences

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of a suspicious mind as a ground for grave judgment. All that is required of a person in the defendant's situation is, that he shall give no answer, or that if he do, he shall answer according to the truth as far as he knows. . . . If the answer import insolvency, it is not necessary that the defendant should be able to prove that insolvency to a jury; for the law protects a man [from a suit for defamation] in giving that answer, if he does it in confidence and without malice. No action can be maintained against him for giving such an answer unless express malice can be proved. From the circumstance of the law giving that protection, it seems to follow, as a necessary consequence, that the law not only gives sanction to the question, but requires that, if it be answered at all, it shall be answered honestly. . . .

Ashhurst, J. [finding for the plaintiff] . . . For the gist of the action is the injury done to the plaintiff, and not whether the defendant meant to be a gainer by it: what is it to the plaintiff whether the defendant was or was not to gain by it; the injury to him is the same. And it should seem that it ought more emphatically to lie against him, as the malice is more diabolical, if he had not the temptation of gain. For the same reason, it cannot be necessary that the defendant should collude with one who has an interest. But if collusion were necessary, there seems all the reason in the world to suppose both interest and collusion from the nature of the act; for it is to be hoped that there is not to be found a disposition so diabolical as to prompt any man to injure another without benefiting himself. . . . Another argument which has been made use of is, that this is a new case, and that there is no precedent of such an action. Where cases are new in their principle, there I admit that it is necessary to have recourse to legislative interposition in order to remedy the grievance: but where the case is only new in the instance, and the only question is upon the application of a principle recognized in the law to such new case, it will be just as competent to Courts of Justice to apply the principle to any case which may arise two centuries hence as it was two centuries ago; if it were not, we ought to blot out of our law books one fourth part of the cases that are to be found in them. . . .

Lord Kenyon, C.J. [finding for the plaintiff] . . . There are many situations in life, and particularly in the commercial world, where a man cannot by any diligence inform himself of the degree of credit which ought to be given to the persons with whom he deals; in which cases he must apply to those whose sources of intelligence enable them to give that information. The law of prudence leads him to apply to them, and the law of morality ought to induce them to give the information required. In the case of Bulstrode the carrier might have weighed the goods himself: but in this case the plaintiffs had no means of knowing the state of Falch's credit but by an application to his neighbours. . . . Then it was contended here that the action cannot be maintained for telling a naked lie: but that proposition is to be taken sub modo. If, indeed, no injury is occasioned by the lie, it is not actionable: but if it be attended with a damage, it then becomes the subject of an action. . . . But in this case the two grounds of the action concur: here are both the damnum et injuria. The plaintiffs applied to the defendant telling him that they were going to deal with Falch, and desiring to be informed of his credit, when the defendant fraudulently, and knowing it to be otherwise, and with a design to deceive the plaintiffs, made the false affirmation which is stated on the record, by which they sustained a considerable damage. Then can a doubt be entertained for a moment but that this is injurious to the plaintiffs? If this be not an injury, I do not know how to define the word. . . . It is admitted that the defendant's conduct was highly immoral, and detrimental to society. I am of the opinion that the action is maintainable on the grounds of deceit in the defendant, and injury and loss to the plaintiffs.

[Judgment for the plaintiff affirmed.]

## NOTES

**1. *The Birth of an Action.*** What impact on commercial life if Pasley v. Freeman had been decided the other way? Would Grose, J., the lone dissenter, have allowed the action if the plaintiff had paid the defendant for the information? Note that the early reception to *Pasley* was not always favorable. In Evans v. Bicknell, 31 Eng. Rep. 998, 1003 (Ch. 1801), Lord Eldon, stressing the difficulty of proof when the plaintiff's "stout assertion" is met with the defendant's "positive denial," thought that the protection of the Statute of Frauds was needed. Should the action be allowed if there is testimony of a third-party witness who heard the exchange?

**2. *An Action for Deceit.*** Under *Pasley*, the action for deceit requires, as its name suggests, proof of deliberate lying. During the nineteenth century, courts from time to time sought to expand deceit to reach a defendant guilty only of "legal fraud" or "fraud in law"—i.e., a false statement of fact made without having any reasonable grounds for believing his statement to be true—in practice a form of negligence liability. The debate over whether deceit covered negligent misrepresentations came to a head in the famous case of Derry v. Peek, 14 App. Cas. 337, 374–76 (H.L.E. 1889). The defendants were directors of a corporation who issued a prospectus in which they claimed a special act of Parliament gave them "the right to use steam or mechanical motive power, instead of horses" to run their trams along public ways, which would give the corporation substantial financial advantage. The plaintiff invested in shares of the company on the faith of the representations, which proved false, as the corporation was entitled to use mechanical power only on a limited portion of its tracks. After the company liquidated, the plaintiff sued the directors for deceit to recover the value of his original investment. The trial judge dismissed the plaintiff's cause of action, which was subsequently allowed by the Court of Appeal. Cotton, L.J., equated speaking "recklessly, or without care whether it is true or false" with speaking "without any reasonable ground for believing it to be true." Peek v. Derry, [1887] 37 Ch. 541, 566. That decision, in turn, was reversed in the House of Lords. Lord Herschell assailed Cotton's suggestion that negligence and recklessness are "convertible expressions": "To make a statement careless whether it be true or false, and therefore without any real belief in its truth, appears to me to be an essentially different thing from making, through want of care, a false statement, which is nevertheless honestly believed to be true." Lord Herschell summarized the law:

> I think the authorities establish the following propositions: First, in order to sustain an action of deceit, there must be proof of fraud, and nothing short of that will suffice. Secondly, fraud is proved when it is shewn that a false representation has been made (1) knowingly, or (2) without belief in its truth, or (3) recklessly, careless whether it be true or false. Although I have treated the second and third as distinct cases, I think the third is but an instance of the second, for one who makes a statement under such circumstances can have no real belief in the truth of what he states. To prevent a false statement [from] being fraudulent, there must, I think, always be an honest belief in its truth. And this probably covers the whole ground, for one who knowingly alleges that which is false, has obviously no such honest belief. Thirdly, if fraud be proved, the motive of the person guilty of it is immaterial. It matters not that there was no intention to cheat or injure the person to whom the statement was made.

He added that "if I thought that a person making a false statement had shut his eyes to the facts, or purposely abstained from inquiring into them, I should hold that honest belief was absent and that he was just as fraudulent as if he had knowingly stated that which was false." Nonetheless, on the evidence he concluded that charges of fraud could not be sustained, only to express his misgivings about letting the defendant off scot-free on the ground that "those who put before the public a prospectus to induce them to embark their money in a commercial enterprise ought to be vigilant to see that it contains such representations only as are in

strict accordance with fact. . . .” Parliament responded to this invitation with the Director’s Liability Act, 1890, 53 & 54 Vict. ch. 64, which provides in part that a director or promoter of a corporation will be held liable for damages to purchasers of stocks and bonds unless the director or promoter can show that “he had reasonable ground to believe,” and at all material times did believe, his statements to be true. The statute also contained special rules governing the liability of directors for statements in the prospectus that reflected the opinion of experts in the venture or the state of the public record. What is the appropriate standard of liability in these cases? How could the defendants in *Derry* not have known of the limitations in their charter?

**3. *Fraud and Recklessness Generally.*** *Derry* remains extremely influential in U.S. courts in defining the appropriate scope of fraud. In Neurosurgery & Spine Surgery, S.C. v. Goldman, 790 N.E.2d 925, 933 (Ill. App. 2003), the court relied heavily on *Derry* when it “decline[d] to extend the tort of fraudulent misrepresentation to encompass noncommercial and nonfinancial dealings between parties.” In other cases, courts have been careful not to blur the line between fraud and negligence. Thus in *In re* Acosta, 406 F.3d 367, 372 (5th Cir. 2005), the question was whether a creditor’s claim was nondischargeable in bankruptcy on the ground that the debtor had fraudulently failed to disclose two prior liens on the debtor’s property. Vance, J., held that the fraud was not established.

> An intent to deceive may be inferred from “reckless disregard for the truth or falsity of a statement combined with the sheer magnitude of the resultant misrepresentation.” Nevertheless, an honest belief, even if unreasonable, that a representation is true and that the speaker has information to justify it does not amount to an intent to deceive. Thus, a “dumb but honest” defendant does not have scienter.

*Id.*; accord *In re* Fautz, 636 B.R. 553, 566–67 (Bankr. D. Mass. 2022).

Nonetheless, recklessness can be found in those cases in which a defendant holds himself out as possessing a level of expertise that he in fact lacks. Thus in Skowronski v. Sachs, 818 N.E.2d 635 (Mass. App. Ct. 2004), a jeweler certified an inferior diamond as a stone of a higher grade when he had no knowledge of the proper procedures required of an expert in that area. The court found that the misrepresentations were reckless, and hence fraudulent, when the defendant did not disclose his want of expertise.

**4. *Securities Fraud Today.*** The problem of fraud continues to be an active source of litigation in a wide variety of transactions in established securities markets. See The Securities and Exchange Act of 1934, 15 U.S.C. §§78a-78mm (2012). Section 10(b), 15 U.S.C. §78j(b), provides that it shall be unlawful “[t]o use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.” Pursuant to the statute, the Securities and Exchange Commission (SEC) published Rule 10b-5, 17 C.F.R. §240.10b-5 (2016):

> **EMPLOYMENT OF MANIPULATIVE AND DECEPTIVE DEVICES**
>
> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

In Ernst & Ernst v. Hochfelder, 425 U.S. 185, 199 (1976), a reprise of *Derry*, the Supreme Court was asked to hold that negligent misrepresentations were actionable under Rule 10b-5, because the effects were the same "regardless of whether the conduct is negligent or intentional." The Court rejected the invitation, noting that as a matter of ordinary English the SEC's argument

> simply ignores the use of the words "manipulative," "device," and "contrivance" — terms that make unmistakable a Congressional intent to proscribe a type of conduct quite different from negligence. Use of the word "manipulative" is especially significant. It is and was virtually a term of art when used in connection with securities markets. It connotes intentional or willful conduct designed to deceive or defraud investors by controlling or artificially affecting the price of securities.

*Ernst & Ernst* left open the question, decided in the affirmative in *Derry*, whether recklessness should be equated with fraud in the context of securities transactions. Every circuit court to consider the matter has held that reckless conduct meets the scienter requirement under the Securities Act, although they differ in the level of recklessness required. For one recent illustration, see Public Employees' Retirement Association v. Deloitte & Touche LLP, 551 F.3d 305, 314 (4th Cir. 2009). In that case, Wilkinson, J., applied a stringent standard of recklessness in a suit against Deloitte & Touche (D&T) as outside auditor for the Dutch firm Royal Ahold and its subsidiary, U.S. Foodservice (USF), arising from Deloitte & Touche's alleged failure to account for certain business agreements and complex side agreements in evaluating Ahold's consolidated return.

> In order to establish a strong inference of scienter, plaintiffs must do more than merely demonstrate that defendants should or could have done more. They must demonstrate that the Deloittes were either knowingly complicit in the fraud, or so reckless in their duties as to be oblivious to malfeasance that was readily apparent. The inference we find most compelling based on the evidence in the record is not that the defendants were knowingly complicit or reckless, but that they were deceived by their client's repeated lies and artifices. Perhaps their failure to demand more evidence of consolidation was improper under accounting guidelines, but that is not the standard, which "requires more than a misapplication of accounting principles."

The Supreme Court has yet to rule on whether recklessness constitutes a species of fraud. See Tellabs, Inc. v. Makor Issues & Rights, Ltd., 551 U.S. 308 (2007), cited in *D&T*, a securities fraud case brought against Tellabs and its chief executive officer that failed to reach the question. See also Matrixx Initiatives, Inc. v. Siracusano, 563 U.S. 27, 48 (2011), where the Court skirted the issue "[b]ecause Matrixx does not challenge the Court of Appeals' holding that the scienter requirement may be satisfied by a showing of 'deliberate recklessness.'" It seems highly unlikely, however, that the Court will deviate from the overwhelming consensus in the circuit courts that recklessness does suffice.

**5. *The Private Securities Litigation Reform Act of 1995.*** *Tellabs* resolved a hotly disputed pleading issue under the PSLRA that, in an effort to curb what were regarded as abusive class actions, requires the plaintiff to "specify each statement alleged to have been misleading, [and] the reason or reasons why the statement is misleading." Further, in dealing with the defendant's state of mind, the PSLRA imposes two related requirements: First, "if an allegation regarding the statement or omission is made on information and belief, the complaint shall state with particularity all facts on which that belief is formed," and, second, the complaint must "state with particularity facts giving rise to a strong inference that the defendant acted with the required state of mind." §78u-4(b).

Ginsburg, J., held that "the inference of scienter must be more than merely 'plausible' or 'reasonable' — it must be cogent and at least as compelling as any opposing inference of nonfraudulent intent." 551 U.S. at 314. She added that the proper inquiry "is whether *all* of the

facts alleged, taken collectively, give rise to a strong inference of scienter, not whether any individual allegation, scrutinized in isolation, meets that standard." *Id.* at 310.

Sotomayor, J., offered some additional guidance on *Tellabs*'s "holistic" approach in *Matrixx Initiatives*, 563 U.S. at 49, *supra* Note 4. Investors brought a 10(b)-5 class action against a pharmaceutical company based on the company's alleged failure to disclose reports of a possible link between one of its products, a cold remedy, and loss of smell, rendering statements made by Matrixx misleading. The complaint alleged that Matrixx "was sufficiently concerned about the information it received . . . that it hired a consultant to review the product" and

> [m]ost significantly, Matrixx issued a press release that suggested that studies had confirmed that [its cold remedy product] does not cause anosmia [loss of smell] when, in fact, it had not conducted any studies relating to anosmia and the scientific evidence at that time, according to the panel of scientists, was insufficient to determine whether [the product] did or did not cause anosmia.

The Court, affirming the Ninth Circuit, held that the scienter allegations, when "'taken collectively,' give rise to a 'cogent and compelling' inference that Matrixx elected not to disclose the reports of adverse events not because it believed they were meaningless but because it understood their likely effect on the market." Does *Matrixx* relax the *Tellabs* standard, such that more plaintiffs should be able to withstand a motion to dismiss? What effect, if any, will it have on settlement negotiations in securities fraud cases?

## *Vulcan Metals Co. v. Simmons Manufacturing Co.*

248 F. 853 (2d Cir. 1918)

[The defendant, Simmons Manufacturing, sold to the plaintiff, Vulcan Manufacturing Co., all of its patents, tools, dies, and equipment for the manufacture of vacuum cleaners, together with all machines and parts then on hand. During the sales negotiations, Simmons' agents made two categories of representations to Albert Freeman, a promoter of the Vulcan Corporation. The first group included "commendations of the cleanliness, economy, and efficiency of the machine"; that it was superior to rival methods of cleaning, such as "beating and brushing"; that it was so simple that a child of six could use it; that it was durable and long lasting; and that it promised its users perfect satisfaction, if properly adjusted. The second class of representations stated that the defendant "[c]ompany had not sold the machine, or made any attempt to sell it; that they had not shown it to any one; that it had never been on the market, and that no one outside the company officials and the men in the factory knew anything about it." To explain why defendant had been keeping these superior machines under wraps, its agent stated that, although 15,000 units were on hand, "it would be a mistake for them to attempt to sell these along with their ordinary line, which was furniture."

The plaintiff's action for deceit alleged that the purchase was made in reliance on these representations, but that "the machines and patents were totally inefficient and unmarketable." Simmons counterclaimed on the notes that Vulcan signed for part of the purchase price; Freeman had signed as a guarantor on the notes. The district court directed a verdict for Simmons on both the original action and the counterclaim, finding that Vulcan had not proved any actionable fraud. The record showed that the machines, when exploited by Vulcan, were of little value and that "their manufacture was discontinued by that company not very long after they had undertaken it." There was also evidence that defendant's agents had made several efforts to sell the machines, which had proved unsuccessful because the machines could not create the vacuum necessary for their operation.]

L. Hand, J. [after stating the facts as above]. The first question is of the misrepresentations touching the quality and powers of the patented machine. These were general commendations, or, in so far as they included any specific facts, were not disproved; e.g., that the cleaner would produce 18 inches of vacuum with 25 pounds water pressure. They raise, therefore, the question of law how far general "puffing" or "dealers' talk" can be the basis of an action for deceit.

The conceded exception in such cases has generally rested upon the distinction between "opinion" and "fact"; but that distinction has not escaped the criticism it deserves. An opinion is a fact, and it may be a very relevant fact; the expression of an opinion is the assertion of a belief, and any rule which condones the expression of a consciously false opinion condones a consciously false statement of fact. When the parties are so situated that the buyer may reasonably rely upon the expression of the seller's opinion, it is no excuse to give a false one. And so it makes much difference whether the parties stand "on an equality." For example, we should treat very differently the expressed opinion of a chemist to a layman about the properties of a composition from the same opinion between chemist and chemist, when the buyer had full opportunity to examine. The reason of the rule lies, we think, in this: There are some kinds of talk which no sensible man takes seriously, and if he does he suffers from his credulity. If we were all scrupulously honest, it would not be so; but, as it is, neither party usually believes what the seller says about his own opinions, and each knows it. Such statements, like the claims of campaign managers before election, are rather designed to allay the suspicion which would attend their absence than to be understood as having any relation to objective truth. It is quite true that they induce a compliant temper in the buyer, but it is by a much more subtle process than through the acceptance of his claims for his wares.

So far as concerns statements of value, the rule is pretty well fixed against the buyer. . . .

In the case at bar, since the buyer was allowed full opportunity to examine the cleaner and to test it out, we put the parties upon an equality. It seems to us that general statements as to what the cleaner would do, even though consciously false, were not of a kind to be taken literally by the buyer. As between manufacturer and customer, it may not be so; but this was the case of taking over a business, after ample chance to investigate. Such a buyer, who the seller rightly expects will undertake an independent and adequate inquiry into the actual merits of what he gets, has no right to treat as material in his determination statements like these. The standard of honesty permitted by the rule may not be the best; but, as Holmes, J., says in Deming v. Darling, 20 N.E. 107 (Mass. 1889), the chance that the higgling preparatory to a bargain may be afterwards translated into assurances of quality may perhaps be a set-off to the actual wrong allowed by the rule as it stands. We therefore think that the District Court was right in disregarding all these misrepresentations.

As respects the representation that the cleaners had never been put upon the market or offered for sale, the rule does not apply; nor can we agree that such representations could not have been material to Freeman's decision to accept the contract. The actual test of experience in their sale might well be of critical consequence in his decision to buy the business, and the jury would certainly have the right to accept his statement that his reliance upon these representations was determinative of his final decision. We believe that the facts as disclosed by the depositions of the Western witnesses were sufficient to carry to the jury the question whether those statements were false. It is quite true, as the District Judge said, that the number of sales was small, perhaps not 60 in all; but they were scattered in various parts of the Mountain and Pacific States, and the jury might conclude that they were enough to contradict the detailed statements of Simmons that the machines had been kept off the market altogether. . . .

The next question is as to whether any such misrepresentations were conclusively cured by the recital in the contract of purchase as follows:

> The party of the first part [the Simmons Company] has been engaged in the manufacture of a certain type of vacuum cleaning machines, and the parties of the first and second part [the National Suction Cleaner Company] have been engaged in the sale thereof.

We all agree that an adequate retraction of the false statement before Freeman executed the contract would be a defense. Whether this be regarded as terminating the consequences of the original wrong, or as a correction of it, is of little importance. Further, we agree that, even if Freeman had in fact never learned of the retraction, it would serve, if given under such circumstances as justified the utterer in supposing that he would. For example, a letter actually delivered into his hands containing nothing but a retraction would be a defense, though it abundantly appeared that he had never read it. His loss might still be the consequence, and the reasonable consequence, but for the letter, of the original fraud; but the writer would have gone as far as necessary to correct that fraud, and we should not be disposed to hold it as an insurer that its correction should be effective. Judge Ward and I, however, do not think that such a recital in such a place was certain to catch the eye of the reader, and that therefore neither was the defendant's duty of retraction inevitably discharged, nor, what is nearly the same thing, did the defendant show beyond question that Freeman actually saw it. . . .

It results from the foregoing that the judgment [for the defendant] in the action for deceit must be reversed. In the action [by Simmons] upon the notes the judgment upon the notes will be affirmed, because the Vulcan Metals Company, Incorporated, did not make any offer to return the machines, tools, and patents, which were not shown to be without any value, and consequently it was in no position to rescind.

[The dissent argued that the plaintiff should be "presumed to know what [the contract] means and says," and thus barred from suit.]

## NOTES

**1. *Puffing.*** Why don't the provisions of the express purchase contract allocate all risk associated with the overall sale to the buyer? If Simmons had offered to return all the materials that it had received, could the buyer have recovered the purchase price in full even if the value of the invention had declined in the interim? As noted in *Vulcan Metals*, Holmes, J., gave wide latitude for puffing in Deming v. Darling, 20 N.E. 107, 108–09 (Mass. 1889). The plaintiff purchased a railroad bond from the defendant's agent, who claimed that a railroad mortgage served as good security for the bond such that "the bond was of the very best and safest, and was an A No. 1 Bond, which we understand to mean simply that it was a first rate bond, or that the railroad was good security for the bonds, we are constrained to hold that he is not liable, under the circumstances of this case, even if he made the statement in bad faith." The jury was instructed to find for the defendant if the statement was made in good faith, but not if otherwise. On appeal from the plaintiff's verdict, Justice Holmes refused to treat as false the defendant's "vague commendations of his wares" that did not contain false statements of facts. In his view, "[t]he rule of law is hardly to be regretted, when it is considered how easily and insensibly words of hope or expectation are converted by an interested memory into statements of quality and value when the expectation has been disappointed." Is this risk identified by Holmes present in the case at hand?

Nonetheless, there are clear limits to the puffing doctrine. In Smith v. Land and House Property Corp., 28 Ch. D. 7 (C.A. 1884), the plaintiffs offered a hotel for sale, stating that it

was let to "Mr. Frederick Fleck (a most desirable tenant)." Before the contract of sale could be signed, Fleck went into bankruptcy after he made several late partial payments on the lease. The defendant refused to complete the transaction on the ground that the statement about Fleck was a misrepresentation. The plaintiffs sought specific performance, claiming that their remark was "a mere expression of opinion." Bowen, L.J., sided with the defendants and held they were excused from consummating the transaction:

> If the facts are not equally known to both sides, then a statement of opinion by the one who knows the facts best involves very often a statement of a material fact, for he impliedly states that he knows facts which justify his opinion. Now a landlord knows the relations between himself and his tenant; other persons either do not know them at all or do not know them equally well, and if the landlord says that he considers that the relations between himself and his tenant are satisfactory, he really avers that the facts peculiarly within his knowledge are such to render that opinion reasonable. Now are the statements here statements which involve such a representation of material fact? They are statements on a subject as to which prima facie the vendors know everything and the purchasers nothing. The vendors state that the property is let to a most desirable tenant, what does that mean? I agree that it is not a guarantee that the tenant will go on paying his rent, but it is to my mind a guarantee of a different sort, and amounts at least to an assertion that nothing has occurred in the relations between the landlords and the tenant which can be considered to make the tenant an unsatisfactory one. That is an assertion of a specific fact. . . . In my opinion a tenant who had paid his last quarter's rent by driblets under pressure must be regarded as an undesirable tenant.

*Smith* was relied on in connection with securities fraud in *Omnicare, infra* Note 4. Is there any reason why the context of securities fraud should render general fraud principles inapplicable?

**2. *Misrepresentations of Law.*** At common law, the dominant rule once provided that the action for deceit did not lie for misrepresentations of law. One reason was that legal rules were generally matters of public record to which the plaintiff and defendant had equal access. Alternatively, the plaintiff could confirm those representations from an independent source if she desired. That rule has not, in general, been applied when a lawyer misrepresents the law to a lay adversary on the ground that it would be "unconscionable."

The older rule has also been relaxed so as to allow fraud actions for "mixed" statements of fact and law. In National Conversion Corp. v. Cedar Building Corp., 246 N.E.2d 351, 355 (N.Y. 1969), the plaintiff tenant entered into a five-year lease with the defendant landlord after the landlord had represented in the lease that the zoning allowed the plaintiff to conduct the business of converting restaurant garbage into fertilizer. The representations were false, and the plaintiff was allowed to recover both the rentals paid prior to the rescission and the costs of the installation and removal of its equipment. Breitel, J., specifically rejected the defendant's claim that its misrepresentations were not actionable:

> The statements in this case, both before the execution of the lease, and in the body of the lease, exemplify ideally an instance in which the statements are not intended or understood merely as an expression of opinion. Landlords said they knew the premises were in an unrestricted district. This meant that they knew as a fact, that the zoning resolution did not restrict the use of the particular premises, and tenant so understood it. When coupled with the further fact that tenant's lawyer was persuaded not to verify the status of the premises on the landlords' representation, it is equally clear that tenant understood the statement to be one of fact, namely, what the zoning resolution provided by description, map, and requirements as to the area in question. The misrepresented fact, if it is at all necessary to find misrepresented facts, was what the zoning resolution contained by way of description, map, and requirements, hardly opinions as to the law albeit matters to be found in a law.

*National Conversion* continues to dominate in this area. In AIU Insurance Company v. Deajess Medical Imaging, P.C., 882 N.Y.S.2d 812, 820 (N.Y. Sup. Ct. 2009), the defendant

had submitted no-fault reimbursement claims through professional corporations he managed to the plaintiff insurance companies, thereby falsely representing that these professional corporations were wholly owned by licensed physicians and therefore eligible for no-fault reimbursement. *National Conversion* was relied on for the proposition that it is an "over-simple dichotomy" to distinguish between law and fact for the purposes of an action in deceit. "'A statement as to law, like a statement as to anything else, may be intended and understood either as one of fact or one of opinion only, according to the circumstances of the case.' . . . Since a misrepresentation as to the law may give rise to an action for fraud, so may a misrepresentation as to a mixed question of fact and law, such as eligibility for no fault reimbursement." Should the same rule apply if the defendant represents to a third party that the plaintiffs are employees (thus entitled to certain benefits) when they are independent contractors? If there is some dispute over the issue and the underlying facts are fully disclosed? See Van Vechten Veeder et al., *infra* Chapter 6, for the parallel distinction in the law of defamation when the defendant calls the plaintiff a thief or a murderer.

**3.** ***Materiality in Fraud Cases.***

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§9. Fraud**

***Comment d. Materiality:*** Liability for fraud attaches only to misrepresentations that are material. A misrepresentation is material if a reasonable person would give weight to it in deciding whether to enter into the relevant transaction, or if the defendant knew that the plaintiff would give it weight (whether reasonably or not). The question, in effect, is whether the defendant knew or should have known that the misrepresentation would matter to the plaintiff. . . . This element of the tort is most likely to be important when one party to a negotiation makes false statements to the other about a matter collateral to the immediate subject of the bargain. . . . The materiality requirement also excludes liability for statements amounting to "puffery"—that is, a seller's broad and predictably exaggerated statements about the quality of an item, as distinct from particular claims of fact. (Claims based on such statements may be dismissed, in the alternative, for want of justifiable reliance.)

**4.** ***Materiality in Securities Cases.*** Under the securities law, the plaintiff must prove material falsehood but not fraud. In TSC Industries, Inc. v. Northway, Inc., 512 F.2d 324, 330 (7th Cir. 1975), plaintiff challenged a complex joint proxy statement under a so-called "roll-up" transaction that combined the operation of the two entities under 15 U.S.C. §78(n). The alleged omissions all involved allegedly incomplete statements about the respective responsibilities of the CEOs of the target corporation. The Seventh Circuit found that various statements and omissions were material as a matter of law if they touched on "all facts which a reasonable stockholder might consider important." The Supreme Court, concerned that this lax standard might lead to endless disclosures of trivial facts, stated the applicable standard more narrowly: "An omitted fact is material if there is a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote." TSC Indus., Inc. v. Northway, Inc., 426 U.S. 438, 449 (1976). Justice Marshall rebuffed that claim:

> The proxy statement prominently displayed the facts that National owned 34% of the outstanding shares in TSC, and that no other person owned more than 10%. It also prominently

> revealed that 5 out of 10 TSC directors were National nominees, and it recited the positions of those National nominees with National—indicating, among other things, that Stanley Yarmuth was president and a director of National, and that Charles Simonelli was executive vice president and a director of National. These disclosures clearly revealed the nature of National's relationship with TSC and alerted the reasonable shareholder to the fact that National exercised a degree of influence over TSC. In view of these disclosures, we certainly cannot say that the additional facts that Yarmuth was chairman of the TSC board of directors and Simonelli chairman of its executive committee were, on this record, so obviously important that reasonable minds could not differ on their materiality.

*Id.* at 452–53.

The key takeaway here hearkens back to both *Vulcan* and *Deming*. There is no need to disclose facts that the plaintiff can infer from the facts that were in fact disclosed.

In Basic Inc. v. Levinson, 485 U.S. 224, 238–39 (1988), the Supreme Court held that the definition of materiality in *TSC Industries* also applied to actions brought under Rule 10b-5, governing actions for fraud with respect to the purchase or sale of securities. Basic's president publicly announced that "management was unaware" of any reason for extensive trading in its stock, after it had been approached by a larger company seeking to acquire it. The Court rejected Basic's argument that its statements were proper as long as the parties had not entered into an "agreement-in-principle" for the acquisition. It wrote: "No particular event or factor short of closing the transaction need be either necessary or sufficient by itself to render merger discussions material." Rather, "materiality 'will depend at any given time upon a balancing of both the indicated probability that the event will occur and the anticipated magnitude of the event in the light of the totality of the company activities,'" which could include "board resolutions, instructions to investment bankers, and actual negotiations between principals or their intermediaries." The Court remanded the case for further consideration under its standard.

The Supreme Court revisited this issue of materiality in its lengthy opinion in Omnicare, Inc. v. Laborers District Council Construction Industry Pension Fund, 575 U.S. 175 (2015), which deals with registration statements filed with the Securities and Exchange Commission. Section 11, 15 U.S.C. §77k(a), states:

> In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security . . . [may] sue.

In connection with a new public offering of common stock, Omnicare stated generally that:

> We believe our contract arrangements with other healthcare providers, our pharmaceutical suppliers and our pharmacy practices are in compliance with applicable federal and state laws. . . .
>
> We believe that our contracts with pharmaceutical manufacturers are legally and economically valid arrangements that bring value to the healthcare system and the patients that we serve.

Both statements were accompanied by caveats. On the first, Omnicare "mentioned several state-initiated 'enforcement actions against pharmaceutical manufacturers for offering payments to pharmacies that dispensed their products'"; it then cautioned that the laws relating to that practice might "be interpreted in the future in a manner inconsistent with our interpretation and application." *Id.* On the second, "Omnicare noted that the Federal Government had expressed 'significant concerns' about some manufacturers' rebates to pharmacies and warned that business might suffer 'if these price concessions were no longer provided.'"

The plaintiffs sued for violation of section 11, claiming that defendant's representations were "materially false" because the federal government later conducted an investigation against Omnicare for violation of its anti-kickback laws. In a lengthy opinion, Kagan, J., asked two questions — "one focusing on what the statement says and the other on what it leaves out." The first issue examined the relationship between statement of fact and opinion. The second dealt with the relevance of any omission.

On the first question, she concluded that the defendants were entitled to some protection to the extent of their good-faith belief in their own statements, so that liability could not be established solely by showing that a statement of opinion turned out to be false. By "the same token every such statement explicitly affirms one fact: that the speaker actually holds the stated belief." Kagan, J., then held that the two quoted sentences "are pure statements of opinion." On the second issue, she thought the question was closer because a bald statement of opinion becomes actionable "if a registration statement omits material facts about the issuer's inquiry into or knowledge concerning a statement of opinion, and if those facts conflict with what a reasonable investor would take from the statement itself, then §11's omissions clause creates liability." She stressed that the test here raised the same principles found in the Restatement of Torts §539, which in turn relied on Bowen's, L.J., opinion in Smith v. Land and House Property Corp., [1884] 28 Ch. 7, 15. There, Bowen states that when "the facts are not equally known to both sides, then a statement of opinion by the one who knows the facts best . . . impliedly states that [the speaker] knows facts which justify his opinion." Is a sophisticated party able to infer that if state investigations have happened, federal examinations could happen as well?

The puffing defense received greater support in Carvelli v. Ocwen Financial Corp., 934 F.3d 1307, 1319–20 (9th Cir. 2019), where the plaintiffs, including the University of Puerto Rico Retirement System, sued the defendants who were a mortgage servicing company that had repeated difficulties keeping accurate account records. The complaint alleged that the company failed to disclose that it used "a dysfunctional system incapable of servicing mortgages." It then turned to the puffing issue:

> While this Court has accepted the puffery defense in the common-law context, we've yet to apply it in a reported securities-fraud case. We see no basis for not doing so, however, and in fact the defense seems a particularly good fit in the securities context.
>
> So, what of Ocwen's statements promising, among other things, that it continued "to devote substantial resources to . . . regulatory compliance and risk management efforts," that its investments in those areas were "now mature and delivering improved results," that it felt "good about the progress" it had made towards its "national mortgage settlement compliance," and that it had "taken a leading role in helping to stabilize communities most affected by the financial crisis"? The district court reasoned that these statements — and others like them — weren't the sort that a reasonable investor could possibly regard as significant because "Ocwen never said it was in compliance with regulations but rather made vague statements about its efforts towards compliance." In short, Ocwen's statements were puffery.
>
> The Retirement System raises two objections. First, it contends that Ocwen's statements can't be nonactionable puffery because Ocwen did not "genuinely or reasonably believe them." This argument fails. Whether a statement was made in bad faith or without a reasonable basis is irrelevant to the question whether the statement is nonetheless so airy as to be insignificant. Certainly, such considerations could (and very well may be) relevant to whether the statements were made with the requisite level of scienter or whether the statements are entitled to safe-harbor protection (more on that later) — but what matters for *materiality* purposes is whether a statement is of a type that a reasonable investor would find relevant to investment decision-making. Put another way, "[t]he anti-fraud provisions of the securities laws are plainly disinterested with immaterial statements, no matter the state of mind of the speaker."

Is this case consistent with the statement of Bowen, L.J., in *Smith*?

**5.** ***Material Omissions.*** How do the principles announced in *Omnicare* apply to actionable omissions? In Affiliated Ute Citizens of the State of Utah v. United States, 406 U.S. 128, 153–54 (1972), the Ute Distribution Corporation issued shares in its corporate assets to "mixed-blood" descendants of the Ute Tribes. The articles of incorporation required that any mixed-blood shareholder wanting to sell shares to outsiders had to first offer these shares to tribal members but could sell to outsiders if no tribe member was prepared to accept the offer. Employees of the First Security Bank purchased shares from mixed-blood shareholders without disclosing to them that the price they offered was below that which they could receive by selling the shares in outside markets. Blackmun, J., refused to deny liability on the ground that the tribe members could not establish causation.

> Under the circumstances of this case, involving primarily a failure to disclose, positive proof of reliance is not a prerequisite to recovery. All that is necessary is that the facts withheld be material in the sense that a reasonable investor might have considered them important in making this decision. This obligation to disclose and this withholding of a material fact establish the requisite element of causation in fact.

Compare the factual circumstances of *Omnicare* with those in *Affiliated Ute*. In the latter, the information at issue was clearly material because defendants had perfect knowledge of the legal rules governing the sales of the shares in question. In contrast, knowledge of background information was irrelevant in finding the defendants liable for material omissions in *Omnicare*.

**6.** ***Insider Trading.*** The use of undisclosed information plays a central role whenever corporate insiders, typically directors, key officers, or major shareholders, purchase common stock from outsiders. In Goodwin v. Agassiz, 186 N.E. 659, 661 (Mass. 1933), the defendants were directors of a corporation that purchased shares over the Boston Exchange from the plaintiff, himself an experienced trader who had kept records of his own transactions in the company's stock. The plaintiff sought to rescind the sale or obtain other appropriate relief on the ground that the defendants did not disclose that they had received reports from a geologist that indicated that certain properties owned by the corporation might contain valuable mineral deposits. The court barred the plaintiff's legal claim because he "made no inquiries of the defendant or of other officers of the company."

> Fiduciary obligations of directors ought not to be made so onerous that men of experience and ability will be deterred from accepting such office. Law in its sanctions is not coextensive with morality. It cannot take to put all parties to every contract on an equality as to knowledge, experience, skill and shrewdness. It cannot undertake to relieve against hard bargains made between competent parties without fraud. On the other hand, directors cannot rightly be allowed to indulge with impunity in practices which do violence to prevailing standards of upright business men. Therefore, where a director personally seeks a stockholder for the purpose of buying his shares without making disclosure of material facts within his peculiar knowledge and not within reach of the stockholder, the transaction will be closely scrutinized and relief may be granted in appropriate instances.

What might these instances be? Should the share purchase in *Goodwin* be judged by the same rules applicable to latent defects in real estate?

Today, the federal regulation of insider trading under Rule 10b-5 of the Securities and Exchange Acts, *supra* Note 4, at 154, has been read to require directors to make public disclosures before they trade on inside information. See, e.g., SEC v. Texas Gulf Sulfur Co., 401 F.2d 833 (2d Cir. 1968), another famous case involving mineral deposits. Under *Goodwin*, should it make a difference if other transactions between unrelated parties took place on the day that the plaintiff sold to the defendants? Should the rule be different if insiders sell their shares, or sell short, because they have undisclosed information about the firm's negative prospects? In

principle, should the corporate charter be allowed to stipulate that insiders may trade without disclosure on the organized exchange? There is a huge amount of literature on insider trading; see, e.g., Dennis W. Carlton & Daniel R. Fischel, The Regulation of Insider Trading, 35 Stan. L. Rev. 857 (1983), who argue that the corporate charter should be allowed to determine whether, and if so, how much, insider trading should be allowed so long as its terms are fully disclosed. Would most new companies think it desirable to place restrictions on insider trading to maximize the sale price of stock at the initial offering?

Aggressive criminal prosecutions for insider trading against "tippees" — persons who directly or indirectly obtain undisclosed information from insiders — were rebuffed in United States v. Newman, 773 F.3d 438, 442 (2d Cir. 2014), by the Second Circuit, which oversees financial activity in New York City, on two grounds. First, the government did not allege a sufficient direct personal benefit to the insider who released the information to analysts. Second, the information in question was commingled with other information and passed through three or four different parties before it was used by traders, so that it was unclear that the defendants "knew that they were trading on information obtained from insiders in violation of those insiders' fiduciary duties."

In Salman v. United States, 580 U.S. 39 (2016), the Supreme Court abrogated the *Newman* decision's direct personal benefit requirement. Salman, the defendant tipper, provided his brother with material nonpublic information. Despite the lack of a clear pecuniary benefit to the tipper in exchange for the information, the Court found the defendant liable for insider trading. However, it remains unclear whether the *Salman* decision only applies in cases where the tipper and tippee are relatives, and the transaction provides no indirect benefits for the firm, which was arguably the case in *Newman*, where the material information was released by the company's own representatives in order to increase overall share value. In SEC v. Watson, 659 F. Supp. 3d 409, 416 (S.D.N.Y. 2023), the court specified some examples of personal benefits that needed to find tipper liability in insider trading: "a 'pecuniary gain,' a 'reputational benefit that will translate into future earning,' a 'relationship between the insider and the recipient that suggests a *quid pro quo* from the latter,' the tipper's 'intention to benefit the particular recipient,' and a 'gift of confidential information to a trading relative or friend' where '[t]he tip and trad resemble trading by the insider himself followed by a gift of the profits to the recipient.'" Why is there any need to show a personal benefit to the tipper if the tippee, as a donee, made improper use of the information? For discussion, see Richard A. Epstein, Returning to the Common-Law Principles of Insider Trading After *Newman v. United States*, 125 Yale L.J. 1482 (2016).

Richard A. Epstein, Rethinking Disclosure Obligations in Securities Regulations: Why Less Is (Much) More, 2023 Mich. St. L. Rev. 1, 33, takes an even grimmer view of these cases:

> There is a sobering lesson to be learned from this progression from nineteenth-century common law cases to the modern onslaught of executive overregulation. The early cases on securities liability addressed a deadbeat lessee as if he were reputable, or stating that you had licenses to run steam power that you did not have. Real statements that matter. And if the law were confined to these instances, its great achievement would not lie in the litigated cases, but in the deterrent effect that reduces these frauds before they start. But as the ambitions of the securities laws expand, they face diminishing marginal returns, so in the post-1964 era, all of the great cases are better decided with a no-liability verdict.

**7.** ***Climate Disclosures.*** In 2023 the SEC proposed an extensive set of obligations for major corporations to require disclosures of various climate-related activities to "reflect the Commission's efforts to respond to investors' demand for more consistent, comparable, and reliable information about the financial effects of climate-related risks on a registrant's operations and how it manages those risks while balancing concerns about mitigating the associated

costs of the rules." The Enhancement and Standardization of Climate-Related Disclosures for Investors, 17 C.F.R. §§210, 229, 230, 232, 239, 249. In the initial version of the regulations, the SEC sought to require disclosure of three kinds of emissions: Scope 1 emissions, which come from the company itself; Scope 2 emissions, which come from firms from which the firm makes purchases; and Scope 3 emissions, which include a broad class of what are termed "indirect emissions." In its final rules, issued on March 6, 2024, the SEC by a 3-2 vote eliminated the third class, but not the first two.

The objections to the proposal noted the huge cost of collecting this information about the international activities of many firms and insisted that direct disclosures mandated by the SEC on actual emissions, when combined with extensive private efforts to control supply chain emissions, were a far better alternative. The adoption of the rules prompted an immediate judicial challenge in the Eighth Circuit, such that on April 4, 2024, the SEC "determined to exercise its discretion to stay the Final Rules pending the completion of judicial review of the consolidated Eighth Circuit petitions," while continuing to "vigorously" defend the legality of the rule. SEC Act of 1933, Release No. 11280/April 4, 2024; SEC Act of 1934 Release No. 99908/April 4, 2024.

## *Swinton v. Whitinsville Savings Bank*

42 N.E.2d 808 (Mass. 1942)

Qua, J. The declaration alleges that on or about September 12, 1938, the defendant sold the plaintiff a house in Newton to be occupied by the plaintiff and his family as a dwelling; that at the time of the sale the house "was infested with termites, an insect that is most dangerous and destructive to buildings"; that the defendant knew the house was so infested; that the plaintiff could not readily observe this condition upon inspection; that, "knowing the internal destruction that these insects were creating in said house," the defendant falsely and fraudulently concealed from the plaintiff its true condition; that the plaintiff at the time of his purchase had no knowledge of the termites, exercised due care thereafter, and learned of them about August 30, 1940; and that, because of the destruction that was being done and the dangerous condition that was being created by the termites, the plaintiff was put to great expense for repairs and for the installation of termite control in order to prevent the loss and destruction of said house.

There is no allegation of any false statement or representation, or of the uttering of a half truth which may be tantamount to a falsehood. There is no intimation that the defendant by any means prevented the plaintiff from acquiring information as to the condition of the house. There is nothing to show any fiduciary relation between the parties, or that the plaintiff stood in a position of confidence toward or dependence upon the defendant. So far as appears the parties made a business deal at arm's length. The charge is concealment and nothing more; and it is concealment in the simple sense of mere failure to reveal, with nothing to show any peculiar duty to speak. The characterization of the concealment as false and fraudulent of course adds nothing in the absence of further allegations of fact.

If this defendant is liable on this declaration every seller is liable who fails to disclose any nonapparent defect known to him in the subject of the sale which materially reduces its value and which the buyer fails to discover. Similarly it would seem that every buyer would be liable who fails to disclose any nonapparent virtue known to him in the subject of the purchase which materially enhances its value and of which the seller is ignorant. See Goodwin v. Agassiz, 186 N.E. 659 (Mass. 1933). The law has not yet, we believe, reached the point of imposing upon the frailties of human nature a standard so idealistic as this. That the particular

case here stated by the plaintiff possesses a certain appeal to the moral sense is scarcely to be denied. Probably the reason is to be found in the facts that the infestation of buildings by termites has not been common in Massachusetts and constitutes a concealed risk against which buyers are off their guard. But the law cannot provide special rules for termites and can hardly attempt to determine liability according to the varying probabilities of the existence and discovery of different possible defects in the subjects of trade.

[Affirmed.]

## NOTES

**1.** ***Latent Defects: Liability for Nondisclosure by a Seller?*** In *Swinton*, the approach to the topic of termites was treated as one of pure silence, but add the representation "you're sure to love the house" and the case is instantly closer to a misrepresentation.

What if the defendant had plastered over the parts of the woodwork where termites were present? Could the action for concealment properly lie, even for Qua, J.? Other cases have held that actions by the defendant to cover up some defect count as fraud, even in the absence of words to that effect. Thus in Croyle v. Moses, 90 Pa. 250 (1879), the defendant committed fraud when he hitched up his horse short in order to conceal the fact that the animal was "a cribber and a windsucker." Likewise, Osborn v. Gene Teague Chevrolet Co., 459 P.2d 988 (Or. 1969), sustained the plaintiff's verdict in a fraud case in which the defendant used car dealer had set back the odometer from 100,000 to 62,000 miles, without making any verbal misrepresentations.

The no-duty rule in *Swinton* has eroded over time. Obde v. Schlemeyer, 353 P.2d 672, 674–75 (Wash. 1960), another termite case, rejected *Swinton*, reasoning:

> Where there are concealed defects in demised premises, dangerous to the property, health, or life of the tenant, which defects are known to the landlord when the lease is made, but unknown to the tenant, and which a careful examination on his part would not disclose, it is the landlord's duty to disclose them.

In addition, RTT: LEH §13 qualifies its general rule of nondisclosure with duties to disclose "material information" where "the actor knows that the other party to a transaction is mistaken about a basic assumption behind it, and that the other party, because of the relationship between them, the customs of the trade, or other circumstances, would reasonably expect disclosure of what the actor knows." Do these qualifications on the general rule of nondisclosure reflect a hidden pro-defendant bias in RTT: LEH §13?

### RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM

**§13. Duties to Disclose; Tacit Misrepresentation**

A failure to disclose material information may result in liability if the actor has a duty to speak. Such a duty exists where:

(a) the actor has made a prior statement and knows that it will likely mislead another if not amended, even if it was not misleading when made; or

(b) the actor is in a fiduciary or confidential relationship with another that obliges the actor to make disclosures; or

(c) the actor knows that the other party to a transaction is mistaken about a basic assumption behind it, and that the other party, because of the relationship between

them, the customs of the trade, or other circumstances, would reasonably expect disclosure of what the actor knows. . . .

***Illustration 8***. Buyer purchases a house from Seller. Buyer then discovers serious defects in the foundation that Seller did not disclose. The court finds that Seller knew of the defects before the sale, knew they would be of great importance to Buyer, and knew they were not discoverable by the use of reasonable care; Buyer had obtained a customary and competent inspection, and the defects were not found. Seller is subject to liability to Buyer for fraud. . . .

***Illustration 11***. Buyer purchases house from Seller, then discovers that its driveway encroaches on a neighbor's property. The court finds that Seller knew of the encroachment and did not disclose it to Buyer. The court also finds, however, that the encroachment could have been discovered by a survey or by inspection of public records, neither of which Buyer performed. Seller had no obligation to disclose the encroachment to Buyer and is not liable for fraud. Other rights and remedies may be available to Buyer by statute.

***Comment d. Superior Knowledge:*** . . . In Illustration 8, denying recovery would give future buyers an incentive to invest in more expensive inspections that would rarely be worth the cost. It is more efficient to require the seller to reveal what he knows in the sales contract. In Illustration 11, by contrast, requiring each side to inform itself of the facts — or even just requiring the buyer to put direct questions to the seller — is not unduly burdensome, and is consistent with the commercial customs that govern real-estate transactions.

What evidence of community norms might be relevant to whether disclosure is required? If the standard contract for a home purchase contains an explicit warranty by the seller that a house is free of termites or other latent defects, is disclosure required when that contract is not used? What other devices might be used to address this recurrent risk? Note that it is common practice today for buyers to hire inspectors to do a comprehensive home inspection after signing the contract but before closing the deal. In general, the contract sales price is modified to take into account the costs of repairing the defects the inspection disclosed.

A tricky permutation involves conditions external to the property sold, to which neither the general rules of the Restatement nor home inspections apply, but where it is still necessary to decide whether the seller must inform the buyer or whether the buyer must make independent inquiries or inspections. Statutory interventions are common. Thus the New Jersey legislature enacted the New Residential Construction Off-Site Conditions Disclosure Act, which mandates the disclosure of the availability of information regarding off-site conditions that might affect the value of residential real estate and provides immunity from tort actions where such disclosure is made. In New Jersey, sellers act at their peril if they deviate from the language of the statutorily mandated disclosures. In Cohen v. W.B. Associates, Inc., 882 A.2d 456 (N.J. Super. Ct. Law Div. 2005), after giving notice of the availability of lists disclosing off-site conditions (as mandated by statute), the sellers added a paragraph describing one of the lists as referring to "property . . . formally used as, or . . . currently used as, . . . Campo De Marlboro" while neglecting to mention that "Campo De Marlboro" was "a minimum security prison operated by the New Jersey Department of Corrections." The purchasers were allowed to pursue common law fraud and misrepresentation claims against the sellers, who relinquished statutory immunity by making representations beyond those required by statute. Perri, J.S.C., explained that otherwise the statute's purpose — "to eliminate any ambiguity in the seller's obligation and to insure that buyers are unequivocally aware of their obligation of due diligence" — would be undermined.

2. ***Partial Disclosures.*** Even when there is no general duty to speak, partial disclosures are not allowed: "[O]ne who voluntarily elects to make a partial disclosure is deemed to have assumed a duty to tell the whole truth, i.e., to make full disclosure, even though the speaker was under no duty to make the partial disclosure in the first place." Union Pac. Res. Grp., Inc. v. Rhone-Poulenc, Inc., 247 F.3d 574, 584 (5th Cir. 2001); see also RST §551(2)(b); RTT: LEH §9(c), illus. 4.

The same principle was applied at the summary judgment stage in Bledsoe v. FCA US LLC, 663 F. Supp. 3d 753 (E.D. Mich. 2023). The plaintiffs brought a class action on behalf "of all persons or entities in the United States who, as of November 1, 2016, owned or leased a 2007 to 2012 Dodge Ram 2500 or Dodge Ram 3500 pickup truck equipped with a Cummins 6.7-Liter diesel engine." The complaint alleged that these vehicles were marketed as "clean diesel" even though the defendants had installed certain "defeat devices" which by design reduced the reported levels of emissions during testing to permissible levels even for vehicles that emitted far higher levels of emissions on the road. Berg, J., held as a matter of law that "where the plaintiffs can demonstrate that defendants told 'half-truths' about a product . . . there is a duty to disclose additional information to ensure that a partial disclosure is not misleading." He then further concluded that the plaintiffs had conducted exhaustive testing of these emissions systems from which a jury could find evidence of a forbidden defeat device. What is the harm to the consumer (as opposed to the environment) from buying a car with a device that reduced its cost of operation?

What result if the information that is supplied by one party at one time becomes obsolete with the passage of time? Generally any defendant who has led the plaintiff to believe in the truth of a certain state of affairs is under a duty to update that information to correct any earlier misimpressions, even if he makes no additional representations. See RST §551(2)(c); RTT: LEH §13(a). But there are clear limits on any such duty. In Hord v. Environmental Research Institute of Michigan, 617 N.W.2d 543 (Mich. 2000), the court held that an accurate 1991 operating summary of a firm's prospects did not generate an implicit duty to update the information when conditions changed thereafter. The court denied that "plaintiff had a right to rely on the 1991 summary as an accurate picture of the company's performance in fiscal year 1992, without some additional inquiry or affirmative representation by defendant."

*Hord* was relied on by the Sixth Circuit in MacDonald v. Thomas M. Cooley Law School, 724 F.3d 654, 663–64 (6th Cir. 2013), to grant the law school's motion to dismiss a fraud claim filed by graduates claiming that the school misrepresented its graduate employment statistics. According to Martin, J., "the graduates' reliance on the 'percentage of graduates employed' statistic to mean 'percentage of graduates employed in full-time legal positions' was not reasonable." He thus held that "a plaintiff's subjective misunderstanding of information that is not objectively false or misleading cannot mean that a defendant has committed the tort of fraudulent misrepresentation." Is there any presentation by law schools of such employment statistics that would be out of bounds?

More recently in securities fraud, Naglich v. Applied Optoelectronics, 436 F. Supp. 3d 954, 969–70 (S.D. Tex. 2020), held that the defendant company was not under a duty to update earlier sales predictions, which became outdated when the company temporarily stopped shipping their product to one of its large customers. "Defendants are correct that '[t]he authorities cited by Plaintiff found a "duty to update" only where a defendant is representing that its statements continue to remain current, not where (as here) Defendants disclosed historical information and repeatedly disclaimed any inference that this information would remain current after the date it was created or would be updated.'" Is it justifiable to rely on an earlier statement when instructed to make further inquiries? Should such a duty for defendants to update be presumed in the case of silence?

## *Laidlaw v. Organ*

15 U.S. 178 (1817)

[The plaintiff Organ was a New Orleans tobacco merchant. He had learned from a friend that peace had been concluded between the British and American forces fighting in the War of 1812. Before the information was made public, Organ contracted to purchase a large order of tobacco from defendant Laidlaw. Before the sale was completed, Laidlaw had asked the plaintiff whether he knew of any information that would affect the price of the tobacco; from the record, it is unclear whether the plaintiff had made any reply, or if so, what he had said. When the peace was announced, the price of tobacco rose between 30 and 50 percent, owing to the end of the British blockade, which allowed for shipment to points outside the United States. Laidlaw, who had delivered the tobacco to Organ, repossessed it by force. Organ brought suit for damages for the loss of the tobacco. The key question in the case was whether their prior agreement, pursuant to which the tobacco was transferred, was vitiated by fraud or nondisclosure. The jury found that Organ was entitled to receive the tobacco, whereupon Laidlaw appealed. After extensive argument Marshall, C.J., issued a brief opinion.]

Marshall, C.J. The question in this case is, whether the intelligence of extrinsic circumstances, which might influence the price of the commodity, and which was exclusively within the knowledge of the vendee, ought to have been communicated by him to the vendor? The court is of opinion that he was not bound to communicate it. It would be difficult to circumscribe the contrary doctrine within proper limits, where the means of intelligence are equally accessible to both parties. But at the same time, each party must take care not to say or do any thing tending to impose upon the other. The court thinks that the absolute instruction of the judge [to find for the plaintiff Organ] was erroneous, and that the question, whether any imposition was practised by the vendee upon the vendor ought to have been submitted to the jury. For these reasons the judgment must be reversed, and the cause remanded to the district court of Louisiana, with directions to award a venire facias de novo [new trial].

## NOTES

**1. *Latent Virtue: Liability for Nondisclosure by a Buyer?*** Unlike the latent defect cases, a *buyer* who acquires superior information about the subject matter of the contract may refrain from disclosing a material fact relating to its value to the seller. The situation can occur in contexts far removed from the stock market. Thus the proprietor of a secondhand music store may sell a Stradivarius violin for a trifling price to a violin expert who happens to wander into the premises. Generally the buyer is under no duty to disclose, even though the price would surely be higher if the seller knew the violin's pedigree. See RST §551, cmt. *k*, illus. 6. As RTT: LEH §13, comment *d* elaborates: "Better information is a legitimate advantage at the bargaining table, and the law encourages its acquisition," with a caveat in the limited circumstances where a party has "a legitimate reason to rely on an adversary to supply the information."

An analogous problem often arises with land purchases. Generally the purchaser of farmland need not disclose that he is buying it because he believes that it contains oil. Similarly the land developer who takes an option on farmland in trying to assemble a large parcel of land from several buyers for a major real estate development is normally under no duty to disclose the purpose of his venture, and may even act, or hire others to act for him, in a manner calculated to persuade his seller that he is in fact only interested in the farmland for its own sake.

In Guaranty Safe Deposit & Trust Co. v. Liebold, 56 A. 951, 953 (Pa. 1904), the option in question had been procured by the trust company to provide a site for a steel mill. The court held that the trust company had no duty to disclose.

> In this commercial age options are daily procured by those in possession of information from which they expect to profit, simply because those from whom the options are sought are ignorant of it. When the prospective seller knows as much as the prospective buyer, options can rarely, if ever, be procured, and the rule that counsel for appellant would have us apply would practically abolish them. The prospective buyer seeks an option instead of at once entering into a contract for the purchase of land, because, no matter what information he may possess exclusively, he is unwilling to act upon it until it becomes a certainty. In the meantime, on the contingency of its becoming so, he makes his contingent bargain to purchase. This is fair in law and in morals. If the appellee concealed anything it was his duty to disclose, or said anything to mislead or deceive the appellant, this rule, of course, would not apply; but they dealt at arm's length, as men always do under such circumstances, each trying to make what was supposed to be the best bargain for himself at the time.

The court then noted that its conclusion was especially apt because Liebold had increased his asking price for the land in response to a "rumor" that a large manufacturing company was contemplating setting up business in town.

In Nussbaum v. Weeks, 263 Cal. Rptr. 360, 367 (Ct. App. 1989), the defendant, a district water manager, purchased land from the plaintiff-seller knowing that the water district would soon allow them to be irrigated, increasing the land's value. The court found there was no duty for the defendant to disclose this to the seller: "The buyer . . . has a duty to disclose material facts only under certain limited circumstances not present here. . . . They include situations in which a fiduciary or confidential relationship exists, situations in which a partial or misleading disclosure is made, and situations in which the buyer knows that the seller would reasonably expect a disclosure to be made." Further, "[i]f the buyer's duty [to disclose] were extended as broadly as the seller's duty, the rule would result in the ridiculous conclusion that a buyer must disclose to the seller factors that have or will indicate the seller is selling the property below its true value. . . . [S]uch a rule would eliminate the freedom to negotiate in the market place." Because there was no duty to disclose, the court found no fraud as a matter of law and reversed a jury verdict for the plaintiffs.

**2.** ***An Economic Account of Nondisclosure.*** The legal consequences of nondisclosure between the parties often can be clarified by an agreement between them. A purchaser can always ask a seller point blank if the premises are infested with termites; a seller can always ask a buyer if he believes oil lies under the seller's farmland or whether the land is slated for industrial development. If the party so asked responds with a falsehood, the ordinary rules of fraud apply; and if he refuses to answer the direct question, the other party is on notice and can act accordingly. Within this environment, the law helps devise a set of default rules to govern in the absence of any explicit agreement. One notable effort to find a coherent set of principles to govern nondisclosure cases is found in Anthony T. Kronman, Mistake, Disclosure, Information, and the Law of Contracts, 7 J. Legal Stud. 1, 9 (1978):

> Where nondisclosure is permitted (or put differently, where the knowledgeable party's contract rights are enforced despite his failure to disclose a known mistake), the knowledge involved is typically the product of a costly search. A rule permitting nondisclosure is the only effective way of providing an incentive to invest in the production of such knowledge. By contrast, in the cases requiring disclosure, and in those excusing a unilaterally mistaken promisor because the other party knew or had reason to know of his error, the knowledgeable party's special information is typically not the fruit of a deliberate search. Although information of this sort is socially useful as well, a disclosure requirement will not cause a sharp reduction in the amount of such information which is actually produced. If one takes into account the investment costs

incurred in the deliberate production of information, the two apparently divergent lines of cases described above may both be seen as conforming (roughly) to the principle of efficiency, which requires that the risk of a unilateral mistake be placed on the most effective risk-preventer.

Kronman applies his analysis to most of the cases set out above. How good is the fit?

## 2. Reliance and Causation

### *Edgington v. Fitzmaurice*

29 Ch. 459 (1885)

[The plaintiff advanced £1,500 for debentures — long-term, fixed-rate financial instruments secured against a company's assets — of a company of which the defendants were directors and officers. In the circular distributed to raise the funds, the defendants announced that they had acquired a valuable property that was "subject to the half yearly payment of £500 in redemption of a mortgage of which £21,500 is outstanding." Elsewhere in the prospectus the defendants stated they would use the moneys raised "to complete . . . alterations and additions to the buildings, and to purchase their own horses and vans," and "to further develop the arrangements at present existing for the direct supply of cheap fish from the coast."

The statements in the prospectus were alleged to be misrepresentations on the following grounds:

1. That the prospectus was so framed as to lead to the belief that the debentures would be a charge on the property of the company.
2. That the prospectus omitted to refer to a second mortgage for £5,000 to Messrs. Hores and Pattisson, which had been made on the 10th of August, 1880.
3. That the prospectus stated that the property was subject to the half-yearly payment of £500 in redemption of the mortgage for £21,500, but omitted to state that on the 5th of April 1884, the whole balance of the mortgage that would then be due, namely, £18,000, might be at once called in.
4. That the real object of the issue of debentures was to pay off pressing liabilities of the company and not to complete the buildings or to purchase horses and vans or to develop the business of the company.

At trial, Denman, J., found for the plaintiffs. The defendants appealed.]

Bowen, L.J. This is an action for deceit, in which the Plaintiff complains that he was induced to take certain debentures by the misrepresentations of the Defendants, and that he sustained damage thereby. The loss which the Plaintiff sustained is not disputed. In order to sustain his action he must first prove that there was a statement as to facts which was false; and secondly, that it was false to the knowledge of the Defendants, or that they made it not caring whether it was true or false. For it is immaterial whether they made the statement knowing it to be untrue, or recklessly, without caring whether it was true or not, because to make a statement recklessly for the purpose of influencing another person is dishonest. It is also clear that it is wholly immaterial with what object the lie is told. That is laid down in Lord Blackburn's judgment in Smith v. Chadwick[, 9 App. Cas. 187 (H.L.E. 1884)], but it is material that the defendant should intend that it should be relied on by the person to whom he makes it. But, lastly, when you have proved that the statement was false, you must further shew that the plaintiff has acted upon it and has sustained damage by so doing: you must shew that the statement was either the sole cause of the plaintiff's act, or materially contributed to his so acting. . . .

The alleged misrepresentations were three. [Bowen, L.J., then concludes that there is insufficient evidence of fraudulent misrepresentation for the first two allegations, dealing with whether the lender could call in the mortgage payments at once, and further that the property in question did not serve as security of another loan. Bowen thought these were material representations but did not think that they were made dishonestly.]

[W]hen we come to the third alleged misstatement I feel that the Plaintiff's case is made out. I mean the statement of the objects for which the money was to be raised. These were stated to be to complete the alterations and additions to the buildings, to purchase horses and vans, and to develop the supply of fish. A mere suggestion of possible purposes to which a portion of the money might be applied would not have formed a basis for an action of deceit. There must be a misstatement of an existing fact: but the state of a man's mind is as much a fact as the state of his digestion. It is true that it is very difficult to prove what the state of a man's mind at a particular time is, but if it can be ascertained it is as much a fact as anything else. A misrepresentation as to the state of a man's mind is, therefore, a misstatement of fact. Having applied as careful consideration to the evidence as I could, I have reluctantly come to the conclusion that the true objects of the Defendants in raising the money were not those stated in the circular. . . .

Then the question remains — Did this misstatement contribute to induce the Plaintiff to advance his money. Mr. Davey's argument has not convinced me that they did not. He contended that the Plaintiff admits that he would not have taken the debentures unless he had thought they would give him a charge on the property, and therefore he was induced to take them by his own mistake, and the misstatement in the circular was not material. But such misstatement was material if it was actively present to his mind when he decided to advance his money. The real question is, what was the state of the Plaintiff's mind, and if his mind was disturbed by the misstatement of the Defendants, and such disturbance was in part the cause of what he did, the mere fact of his also making a mistake himself could make no difference. It resolves itself into a mere question of fact. I have felt some difficulty about the pleadings, because in the statement of claim this point is not clearly put forward, and I had some doubt whether this contention as to the third misstatement was not an afterthought. But the balance of my judgment is weighed down by the probability of the case. What is the first question which a man asks when he advances money? It is, what is it wanted for? Therefore I think that the statement is material, and that the Plaintiff would be unlike the rest of his race if he was not influenced by the statement of the objects for which the loan was required. The learned Judge in the Court below came to the conclusion that the misstatement did influence him, and I think he came to a right conclusion.

## NOTE

***Causation in Fraud Cases.*** Will a defendant in a fraud case have a good causal defense if the plaintiff knew of the falsity at the time the statement was made? If the plaintiff had the means to learn of the falsity of the defendant's statements? In litigating fraud cases, the best defense is often a good offense. One tactic is for the defendant to insist that the plaintiff, far from being deceived, is only a disgruntled investor trying to recoup an unfortunate business investment out of the defendant's hide. Alternatively the defendant might portray the plaintiff as fraudulent in his relations with third parties, say, persons for whom the plaintiff received a finder's fee for persuading them to invest with the defendant. Complex webs of human interactions lead to protracted battles over causation in an effort to understand the interaction of various oral and written statements, sometimes formal and sometimes not, the meaning of which becomes ambiguous with the passage of time.

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§11. Factual Causation; Justifiable Reliance**

The person to whom a fraudulent misrepresentation is made can recover against its maker for economic loss only if:

(a) that person relies on the misrepresentation in acting or refraining from action;
(b) the reliance is justifiable; and
(c) the misrepresentation causes the loss.

***Comment a. Reliance and Causation:*** A successful claim for fraud requires proof that the plaintiff relied on the defendant's misrepresentation. The element of reliance overlaps with (and may be considered a form of) the usual requirement in tort that a defendant's wrong be a factual or "but for" cause of the harm that the plaintiff suffered. The plaintiff may have been influenced by several sources, or by multiple statements—some true, some false—made by the same party. Liability is nevertheless intact if the defendant's fraud made a necessary contribution to the plaintiff's loss, typically by inducing the plaintiff to enter a damaging transaction. If the plaintiff was subject to multiple influences, each of which would have been sufficient to cause the resulting loss, the defendant whose fraud was among those influences may be held liable even though it may appear that the fraud was not a "but for" cause of the harm. . . .

On the other hand,. . . . [a] claim likewise fails if the plaintiff suffered harm as a result of the defendant's fraud but without relying on it. In that case, the plaintiff's loss may have been caused by the defendant's conduct, but the plaintiff's interest in receiving truthful information—the interest protected by the tort of fraud—was not invaded. . . .

## *BV Nederlandse Industrie Van Eiprodukten v. Rembrandt Enterprises, Inc.*

[2019] EWCA Civ 596

Longmore, L.J.

. . .

[This dispute arose out of a contract entered into between Rembrandt Enterprises, Inc. ("Rembrandt") and Netherlands, BV Nederlandse Industrie van Eiprodukten ("NIVE") for the supply and delivery of certain egg products that Rembrandt needed to replace over 50 percent of its own birds that had been infected in the avian flu epidemic, which struck the United States in April 2015. Without new supplies, Rembrandt could not meet its own contract commitments. Rembrandt then entered into a contract with NIVE "to buy 4200 metric tons of dry whole egg, dry yolk and dry white over a two year period for prices of €6.15, €4.15 and €14.90 per kilogram respectively, provided that its procedures in the Netherlands satisfied the US regulatory authorities for supervision of the egg business. The authorities gave the required approval on 1st June 2015."

Prior to that date NIVE emailed Rembrandt on May 21, 2015, stating that it faced "unanticipated extra regulatory costs and that the prices would have to be increased and on 12th June 2015 NIVE proposed a €2.50 per kilogram increase in the price 'after thorough calculation.'" After some negotiation, Rembrandt requested a breakdown of the extra costs. On June 22, 2015, NIVE sent Rembrandt a cost calculation of €2.59 per kilogram. Two days

later Rembrandt agreed the price increase; on June 25, a new contract was made in materially the same terms as the original contract, save that all the prices had been increased by €2.50 per kilogram.

As the avian flu crisis abated, the price for these egg products fell, and Rembrandt then wrote to NIVE that it was suspending the deal for two years. NIVE then instituted litigation to recover its lost profits from the sales. In response, Rembrandt sought contractual rescission on two grounds. The first was that NIVE products did not meet the requisite U.S. standards. The second, the subject of this case, was that NIVE had padded the price increases in the second contract by adding in a hidden element of profit, so that the transaction was found by the trial judge to have been infected by fraud. The question arose whether Mr. Rettig, the head of Rembrandt, would have entered into that second contract if he had known the full facts, to which he answered that he did not know for sure, given the novel nature of the circumstances.]

### The Judgment

[Given that finding of fraud, the trial judge further] held that in law there was a presumption that Rembrandt relied on the representations and that it was for NIVE to prove that the second contract would have been made even if there had been no fraudulent misrepresentation. That NIVE could not do. The fact that Mr David Rettig, the chief executive officer of Rembrandt could not answer the question "what would Rembrandt have done" if it had known that the increased figure included an element of profit was nothing to the point. This gives rise to the first main ground of appeal. . . .

Before considering the law, it is necessary to set out the primary facts found by the judge relevant to the question whether NIVE's misrepresentation induced the second contract. These are set out by the judge as follows:

> By 24th June 2015 Rembrandt had accepted the requested price increase of EUR 2.50 per kg. It appears that the decision was taken by Mr. Rettig. He gave evidence, which was not challenged, that he took the decision. He said his reasons for doing so were threefold. First, given the shortage of eggs in the US market he wished to secure product quickly to secure an advantage over competitors. Second, despite the requested increase in price, the pricing remained "viable." In particular the dried egg white price remained lower than the Urner Barry market price. Third, he had no reason to believe that the costs put forward by NIVE were not genuine and although they appeared higher than Rembrandt's own costs he thought they would be much the same for all Netherlands producers. Mr. Rettig also said in his witness statement that had he known that the stated costs were not NIVE's real costs of complying with US regulations but contained a very significant element of profit he would have viewed the situation very differently.

It was suggested to Mr. Rettig in cross-examination that he was very anxious to get dried egg product from NIVE and that he "didn't really have anywhere else to go." He said that was not true; what was imported from NIVE "was less than 15% of our overall imports." He said "if we didn't end up with NIVE, we could find other suppliers, whether with Spain, Italy, Latvia, the other countries that produced." . . . He was asked what he would have done had he been told that 2.50 was not a real number, that the additional costs could be between 1.50 and 2.50 but that NIVE were insistent on getting an extra 2.50 per kg. He replied: "I don't know. It's hypothetical. I can't answer." It was suggested to him that Rembrandt was sufficiently desperate for the eggs that he would have agreed to the demand. Mr. Rettig replied: "Oh my gosh. After this testimony, I mean, we had 30 other countries we were working with. We were interested in an early solution. I'll stand by my previous testimony."

It is tolerably clear from this that the incidence of burden of proof may be important. If the onus of proving that the fraudulent misrepresentation induced Rembrandt to make the second contract is on Rembrandt (as it would be for non-fraudulent misrepresentations),

Rembrandt's claim to rescission may fail. If on the other hand, the onus is on NIVE to prove that Rembrandt would have made the second contract even if they had known that NIVE was fraudulently representing that the increased price was solely due to increases in cost and contained no element of profit, Rembrandt's claim to rescission should "probably" succeed. I say "probably" because Mr Guy Morpuss QC for NIVE had a secondary argument that the only onus on NIVE had been discharged by virtue of the fact that Mr Rettig could not say what Rembrandt would have done if it had known the true facts.

It is also important to know what has to be proved by the party who has the onus of proof. Is it that the representee would/would not have acted differently but for the misrepresentation? Or is it that the representation played a part (or influenced) the decision of the representee? Or is it sufficient that the representee might/might not have acted differently?

It is surprising that these are still controversial questions in English law especially since the test for inducement in cases of innocent or negligent representation appears to be settled in the form that the representee has the burden of showing inducement in the sense that he has to show he would not have entered into the relevant contract had the representation not been made.

Although, as far as fraud (and particularly rescission for fraud) is concerned, the test for inducement appears to be controversial, both Mr Gavin Kealey QC for Rembrandt and Mr Morpuss for NIVE submitted that the test was settled in Victorian times and that, if subsequent cases were inconsistent with the Victorian ones, the law had taken a wrong turn.

The judge decided the case on the basis that the burden of proof was on NIVE to show that, if the representation had not been made, Rembrandt would still have made the second contract. He said:

> . . . "The conclusion I have reached is that, whilst Mr Rettig might have agreed to the requested price increase, NIVE cannot show that he would have agreed to the requested price increase. The fraudulent misrepresentation as to the additional costs of complying with the US regulations was made for the very purpose of persuading Rembrandt to agree the requested price increase. That end was achieved. Very strong evidence is required to rebut the presumption or inference of inducement in such a case. Whilst there is evidence that Mr Rettig, on behalf of Rembrandt, might have agreed to the requested price increase had the misrepresentation not been made I do not consider that that evidence has the clarity and cogency necessary to enable to enable NIVE to persuade the court that Mr Rettig would in fact have agreed to the requested price increase even if the misrepresentation had not been made."

[Longmore, L.J., then provides an extensive analysis of the Victorian cases—including Derry v. Peek, Pasley v. Freeman, and Edgington v. Fitzmaurice—on inducement in cases of fraudulent misrepresentation.]

In the light of these authorities it seems to me that the law at the end of the nineteenth century had assimilated the requirement of inducement in the tort of deceit and in actions for rescission for fraudulent misrepresentation and could be stated as being that the representee had to prove he had been materially "influenced" by the representations in the sense that it was "actively present to his mind" to use Bowen LJ's phrase [in Edgington v Fitzmaurice]; that, whereas there is a presumption that a statement, likely to induce a representee to enter into a contract, did so induce him, that is merely a presumption of fact which is to be taken into account along with all the evidence. There was no requirement as a matter of law, that the representee should state in terms that he would not have made the contract but for the misrepresentation but the absence of such a statement was part of the overall evidential picture from which the judge had to ascertain whether there was inducement or not. The fact that there were other reasons (besides the representation) for the claimant to have made the contract did not mean that he was not induced by the representation made. . . .

[The court then reviewed other cases of duress and deceit and held that under] the principle set out in Edgington v Fitzmaurice that the representee only has to show that the representation was "a cause" of his entering the relevant contract. . . .

It seems to me, therefore, that overall the modern authorities do not add much to the conclusions that I drew from the Victorian authorities . . . above. . . .

There remains the question whether, if it be the case that the burden of proof is on the representee to show that he was induced (albeit with the help of the presumption which is very difficult to rebut), it is sufficient for him to show that he might have acted differently. . . .

I have already pointed out the ambiguity in the word "might". . . . If it means no more than being actively present in the mind of the representee to repeat the phrase of Bowen LJ, it is perhaps a convenient shorthand. But if it means that the court cannot make up its mind on inducement and therefore decides as a matter of law to give the representee the benefit of the doubt, it is not a helpful concept because that would be contrary to the law as I conceive it to be, . . . which requires the representee to prove inducement albeit with the assistance of a presumption that "will be very difficult to rebut." To some extent this is a matter of terminology but terminology can be important in some cases. . . .

I turn then to consider whether that presumption was rebutted on the facts of the present case. The judge held that it was not and this court must necessarily be reluctant to differ from the judge on what is essentially a question of fact. . . . [The court then held that evidence was unclear whether Mr. Rettig would have acceded to the price increase even without the misrepresentation. Accordingly, like the appellate court in *Edgington*, he declined to set aside the decision of Teare, J., below and thus rejected this appeal.]

## NOTES

**1.** ***A Presumption of Reliance Under English Law?*** How should the burden of proof issue be resolved? Does that issue matter if the correct substantive standard allows NIVE to recover its actual cost increases, but not the padded amounts? Does that solution make fraudulent statements a no-risk proposition for the defendant?

For a parallel problem, in City of Sterling Heights Policy & Fire Retirement System v. Reckitt Benckiser Group PLC, 587 F. Supp. 3d 56 (S.D.N.Y. 2022), the City of Pontiac General Employees' Retirement System (Pontiac) asserted that it acquired shares in Reckitt on the London Stock Exchange at artificially inflated prices and was injured when the market learned the truth about the defendants' tactics to boost the sales of its pharmaceutical drug that was used to combat opioid addiction. Granting defendants' motion to dismiss for Pontiac's failure to allege reliance on any claimed misstatement or omission, Castel, J., rebuffed Pontiac's invocation of a "broad presumption of reliance under English law" and limited such a presumption to circumstances where "a plaintiff who had direct dealings with a defendant pursued a course of action after hearing the alleged misrepresentation" (citing BV Nederlandse Industrie Van Eiprodukten v. Rembrandt Enterprises, Inc. (misrepresentation during negotiation about shipment of egg products)). Castel, J., elaborated:

> Pontiac states, without elaboration, that it reasonably relied on defendants' purported misstatements and omissions when it acquired the shares, but the allegations are conclusory and do not, for instance, assert that it examined the contents of Reckitt's public filings or was aware of statements made in investor-relations calls. Because Pontiac does not allege that it had knowledge of any purported misrepresentation, it cannot plausibly allege that it relied on that misrepresentation.

Castel, J., also rejected Pontiac's assertion that reliance could be inferred "from all the facts and matters . . . that the aforesaid misrepresentations and omissions (a) were made by Defendants with the intention that Pontiac . . . rely upon them, and (b) induced Pontiac . . . to acquire and/or retain Reckitt ordinary shares." Castel, J., emphasized that "Pontiac, as the plaintiff, is in the best position to know whether it had knowledge of and relied upon a misrepresentation at the time it purchased Reckitt shares."

**2. *Direct Evidence of Actual Reliance.*** In modern fraud cases, the plaintiff is in the "best position" to provide direct evidence on the element of actual reliance, which focuses on the *plaintiff's* state of mind and actions. Such was not the case in early historical cases, where the plaintiffs were not allowed to testify as witnesses, and thus had to rely on a presumption of reliance for lack of direct evidence. With proof, however, of the *defendant's* knowledge or state of mind, the plaintiff typically must rely on inferences drawn from circumstantial evidence. See Notes 4 and 5 following *Pasley*, *supra* at 150, discussing securities fraud; Pub. Emps'. Retirement Ass'n of Colo. v. Deloitte & Touche LLP, 551 F.3d 305, 314 (4th Cir. 2009) (discussing "[t]he inference [of scienter] we find most compelling based on the evidence in the record"); Tellabs, Inc. v. Makro Issues & Rights, Ltd., 551 U.S. 308 (2007) (discussing inferences of scienter that satisfy the Private Securities Litigation Reform Act's pleading requirements); Matrixx Initiatives, Inc. v. Siracusano, 563 U.S. 27, 48 (2011), *supra* (finding that the scienter allegations, when "'taken collectively' give rise to a 'cogent and compelling' inference" of fraud) (citations omitted).

**3. *Justifiable Reliance.*** The reliance interest tends to dominate fraud cases. Proving the reliance interest forces courts to choose either an objective or subjective standard of evaluation to decide whether the plaintiff's reliance was in fact "justifiable."

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§11. Factual Causation; Justifiable Reliance**

***Comment d. Justifiable Reliance:*** Principles of comparative negligence do not apply to a claim of fraud, but liability does require a showing that the plaintiff's reliance on what the defendant said was "justifiable." Justifiable reliance is an element of the plaintiff's cause of action; its absence is not an affirmative defense that the defendant must assert.

Justifiable reliance amounts to freedom from recklessness: plaintiffs who close their eyes to a known or obvious danger that a statement is fraudulent cannot recover losses they suffer from reliance on it. . . . Justifiable reliance has a personalized character. It is measured by reference to the plaintiff's capabilities and knowledge; a plaintiff's sophistication may affect a court's judgments about what dangers were fairly considered obvious. . . . Finally, the justifiable reliance required by this Section does not call for a comparison of the fault attributable to the plaintiff and defendant. It is a threshold requirement; if it is satisfied, incremental doubts about the plaintiff's degree of care will not reduce the resulting recovery from the intentional tortfeasor. . . .

Courts disagree over what level of awareness is necessary for actual reliance to no longer be justifiable. For example, in Illinois Central Railroad Co. v. Harried, 681 F. Supp. 2d 773, 775–77 (S.D. Miss. 2009), the Southern District of Mississippi compared the law of various jurisdictions and made an *Erie* guess that Mississippi would consider "justifiable reliance" to be less stringent than "reasonable reliance," i.e., that a plaintiff's reliance could still be "justifiable," even if less than that of a reasonably prudent person. Iowa has come to a similar

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conclusion, that "reliance does not necessarily need to conform to the standard of a reasonably prudent person," because "[t]his standard reflects that fraudulent misrepresentation is an intentional tort, and like other intentional torts, recovery is not necessarily barred by the fault of the plaintiff that contributed to the damage." Spreitzer v. Hawkeye State Bank, 779 N.W.2d 726, 737 (Iowa 2009).

Florida courts, on the other hand, adhere to "reasonable reliance," meaning that "a misrepresentation is not actionable where its truth might have been discovered by the exercise of ordinary diligence." Addison v. Carballosa, 48 So. 3d 951, 955 (Fla. Dist. Ct. App. 2010). In such jurisdictions there is a baseline assumption of reasonable prudence for plaintiffs asserting fraud claims.

As RTT: LEH §11, comment *d* acknowledges, still other jurisdictions use a standard akin to recklessness, employing both an objective reasonableness standard and a subjective assessment of the plaintiff's knowledge to determine whether her reliance is justified. See, e.g., Cocchiara v. Lithia Motors, Inc., 297 P.3d 1277, 1286 (Or. 2013).

**4.** ***Contributory Negligence in Fraud Cases.*** RTT: LEH §11, comment *d* acknowledges: "Requiring justifiable reliance creates arguable tension with the usual rule that contributory negligence is no defense to an intentional-tort claim. The requirement here does not impose a duty of active investigation on a plaintiff, however, and does not entitle a defendant to exploit a plaintiff's foolishness with impunity."

In Seeger v. Odell, 115 P.2d 977, 980 (Cal. 1941), Traynor, J., noted: "Negligence on the part of the plaintiff in failing to discover the falsity of a statement is no defense when the misrepresentation was intentional rather than negligent." In Teamsters Local 282 Pension Trust Fund v. Angelos, 762 F.2d 522, 528 (7th Cir. 1985), Easterbrook, J., explained the rule in holding that the failure of a pension trustee to investigate did not relieve the defendant of liability for securities fraud.

> Securities law seeks to impose on issuers duties to disclose, the better to obviate the need for buyers to investigate. The buyer's investigation of things already known to the seller is a wasteful duplication of effort. If the securities laws worked perfectly there would be little need for investigation; sellers would disclose to the buyers and the market the information necessary for informed trading. Because some frauds will not be caught, and because people cannot interpret information flawlessly, this mechanism cannot work perfectly. This failure makes investigations by investors necessary and creates incentives for sellers to hire certifiers (such as auditors and investment bankers) to verify sellers' statements. But such investigations and other devices are distinctly second-best solutions to legal and practical problems, and we will not establish a legal rule under which investors must resort to the costly self-help approach of investigation on pain of losing the protection of the principal legal safeguard, the rule against fraud.

This is just another way to state the common law rule that contributory negligence is not a defense to an intentional or reckless tort.

**5.** ***Contracting Out of Fraud Liability.*** In IBM v. Lufkin Industries, LLC, 573 S.W.3d 224, 229 (Tex. 2019), the Texas Supreme Court clarified that parties can disclaim the reliance element of fraud by an explicit contractual agreement. There are five factors relevant to this determination: (1) the terms of the contract were negotiated, rather than boilerplate, and during negotiations the parties specifically discussed the issue that has become the topic of the subsequent dispute; (2) the complaining party was represented by counsel; (3) the parties dealt with each other at arm's length; (4) the parties were knowledgeable in business matters; and (5) the release language was clear. Compare these factors to RTT: LEH §11, comment *e*, illustrations 9–10 ("The effect of a 'no-reliance' clause on a tort claim for fraud thus depends on two considerations: the specificity of its wording and the sophistication of the parties.").

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§11. Factual Causation; Justifiable Reliance**

***Comment e. No-Reliance Clauses:*** . . . [Disclaimers of reliance] may undermine a plaintiff's claim to have relied on fraudulent statements made before the contract was signed. Disclaimers of either sort can serve a useful commercial purpose, not by shielding parties who lie but by protecting both parties from costly litigation about whether they lied. Disclaimers also may allow parties to usefully allocate responsibility for determining the truth about the subject of a transaction. But disclaimers also can serve as traps for parties who are content to treat a written contract as final but do not mean to assume the risk that the other side has committed fraud. The effect of a "no-reliance" clause on a tort claim for fraud thus depends on two considerations: the specificity of its wording and the sophistication of the parties. . . .

Compare also the "contracting parties" paradigm of the economic loss rule from Chapter 1. Is the ability to contract out of fraud liability consistent with the policy rationales for the economic loss rule? Or is it a countervailing example of tort drowning in a sea of contract?

## 3. Proximate Cause

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§12. Scope of Liability**

An actor who makes a fraudulent misrepresentation is subject to liability for harm only if the risk of the harm was foreseeably increased by the fraud.

***Comment a. Scope of Liability Generally:*** This Section addresses the issue sometimes known as "proximate" causation: the scope of a defendant's liability for injuries of which a misrepresentation is a factual or "but for" cause. Briefly stated, a plaintiff can recover only for the types of losses that might reasonably have been expected to result from the defendant's fraud. . . . Thus no liability results when a defendant's lie causes the plaintiff to make an investment that fails for reasons entirely unrelated to what the defendant said. . . . On the other hand, a lie that caused a small increase in the likelihood of the loss that the plaintiff suffered is sufficient to support liability. . . . The requirement of a causal connection between the subject of the misrepresentation and the source of plaintiff's loss is a notable difference between the remedies that tort law provides for fraud and the remedies supplied by the law of restitution or contract. . . .

## *Laborers Local 17 Health and Benefit Fund v. Philip Morris, Inc.*

191 F.3d 229 (2d Cir. 1999)

Cardamone, J. [Plaintiffs' funds were organized under the Employee Retirement Income Security Act of 1974 (ERISA) to provide health care to their union members. These funds claimed that they were the victims of tobacco industry fraud on its patients, which induced

those patients to overconsume cigarettes and therefore to increase plaintiffs' costs of providing health care under its plans to participants that suffered from illnesses related to cigarette smoking.

Among the causes of action pleaded were those alleging Racketeer Influenced and Corrupt Organizations Act (RICO) violations and common law fraud, both of which were held to present the same requirement for proof of proximate causation. Later in its opinion, the court said: "These [RICO] principles also apply in general terms to the fraud and special duty causes of action asserted by plaintiffs under New York common law."]

The complaint seeks past and future damages to recover for "money expended . . . to provide medical treatment to [plaintiffs'] participants and beneficiaries who have suffered and are suffering from tobacco-related illnesses." As interpreted by the district court, the complaint also seeks damages inflicted on the Funds' infrastructure independent of the harm suffered by plan participants. These latter damages, alleged to be separate and wholly distinct from participants' medical costs, consist of losses suffered due to the Funds' inability to control costs, to promote the use of safer alternative products, and to establish programs to educate their participants not to use tobacco products.

Ordinarily, plaintiffs' right to sue for damages would be subrogated to the rights of those individual smokers for whom they provided health care benefits. In other words, plaintiffs would stand in the shoes of the injured participants and recoup damages from defendants, as tortfeasors, only to the extent defendants were liable to the participants themselves. But the Funds have not asserted such a subrogation action in this complaint. Instead, they have sued in their own right for the money spent for plan participants and [for infrastructure losses].

## Discussion

### Proximate Cause

The first certified question we are called upon to answer [on interlocutory appeal] raises a question of proximate cause, namely, whether the chain of causation linking defendants' alleged wrongdoing to plaintiffs' alleged injuries is too remote to permit recovery as a matter of law. We begin by analyzing this subject in the context of plaintiffs' RICO claims.

#### I. Proximate Cause as an Element of Standing Under RICO

The RICO provision for civil actions states

> Any person injured in his business or property by reason of a violation of section 1962 of this chapter may sue therefor in any appropriate United States district court and shall recover threefold the damages he sustains and the cost of the suit, including a reasonable attorney's fee.

18 U.S.C. §1964(c) (2012). In *Holmes* [v. Securities Investor Protection Corp., 503 U.S. 258, 268 (1992)], the Supreme Court stated that a plaintiff's standing to sue under RICO requires "a showing that the defendant's violation not only was a 'but for' cause of his injury, but was the proximate cause as well." To determine in a given case whether proximate cause is present, common law principles are applied.

**A. The Concept in General.** In everyday terms, the concept [of proximate cause] might be explained as follows: Because the consequences of an act go endlessly forward in time and its causes stretch back to the dawn of human history, proximate cause is used essentially as a legal tool for limiting a wrongdoer's liability only to those harms that have a reasonable connection to his actions. The law has wisely determined that it is futile to trace the consequences of a wrongdoer's actions to their ultimate end, if end there is.

**B. Direct Injury as a Requirement of Proximate Cause.** Over the passage of time, however, courts have somewhat clarified the definition of proximate cause by identifying several traditional common law principles limiting liability whose application, in aggregate, formulates the proximate cause analysis. As noted in *Holmes*, "'proximate cause' [is used] to label generically the judicial tools used to limit a person's responsibility for the consequences of that person's own acts." . . .

Among these "judicial tools," one notion traditionally included in the concept of proximate causation is the requirement that there be "some direct relation between the injury asserted and the injurious conduct alleged." For this reason, "a plaintiff who complain[s] of harm flowing merely from the misfortunes visited upon a third person by the defendant's acts [is] generally said to stand at too remote a distance to recover."

**C. Applying the Direct Injury Test to Instant Case.** Ultimately, however, whether plaintiffs' injuries are labeled as "infrastructure harm" or "harm to financial stability," their damages are entirely derivative of the harm suffered by plan participants as a result of using tobacco products. Without injury to the individual smokers, the Funds would not have incurred any increased costs in the form of the payment of benefits, nor would they have experienced the difficulties of cost prediction and control that constituted the crux of their infrastructure harms. Being purely contingent on harm to third parties, these injuries are indirect. Consequently, because defendants' alleged misconduct did not proximately cause the injuries alleged, plaintiffs lack standing to bring RICO claims against defendants. . . .

### II. Policy Considerations

Further, this conclusion is consistent with the three policy factors addressed by *Holmes*, which buttress the principle that plaintiffs with indirect injuries lack standing to sue under RICO. "First, the less direct an injury is, the more difficult it becomes to ascertain the amount of a plaintiff's damages attributable to the violation, as distinct from other, independent, factors." . . . It will be virtually impossible for plaintiffs to prove with any certainty: (1) the effect any smoking cessation programs or incentives would have had on the number of smokers among the plan beneficiaries; (2) the countereffect that the tobacco companies' direct fraud would have had on the smokers, despite the best efforts of the Funds; and (3) other reasons why individual smokers would continue smoking, even after having been informed of the dangers of smoking and having been offered smoking cessation programs. On a fundamental level, these difficulties of proving damages stem from the agency of the individual smokers in deciding whether, and how frequently, to smoke. In this light, the direct injury test can be seen as wisely limiting standing to sue to those situations where the chain of causation leading to damages is not complicated by the intervening agency of third parties (here, the smokers) from whom the plaintiffs' injuries derive.

These concerns become particularly pointed in a case, like the present one, where the injuries are alleged to derive not simply from defendants' affirmative misconduct but also from plaintiffs' fraudulently induced inaction. That is, it is often easier to ascertain the damages that flow from actual, affirmative conduct, than to speculate what damages arose from a party's failure to act. In the latter situation, as in the case at hand, it becomes difficult to distinguish among the multitude of factors that might have affected the damages. Here, for example, plaintiffs' alleged damages might have derived from inefficiencies in the Funds' own management, as well as from non-smoking related health problems suffered by the smokers, and it would be the sheerest sort of speculation to determine how these damages might have been lessened had the Funds adopted the measures defendants allegedly induced them not to adopt.

The complexity of these calculations makes the ultimate question of damages suffered by the Funds virtually impossible to determine. Indeed, this case seems to present precisely the type of large, complicated damages claims that *Holmes* . . . sought to avoid. Moreover, for us to rule otherwise could lead to a potential explosion in the scope of tort liability, which, while perhaps well-intentioned, is a subject best left to the legislature.

The second policy factor addressed in *Holmes* focuses on the possibility that "recognizing claims of the indirectly injured would force courts to adopt complicated rules apportioning damages among plaintiffs removed at different levels of injury from the violative acts, to obviate the risk of multiple recoveries." [The court then finds that the New York rules on collateral benefits do not eliminate the need to coordinate multiple payments.]

In the third policy factor discussed by *Holmes*, the Supreme Court concluded that the need to grapple with the problems of calculating and apportioning damages was unjustified where "directly injured victims can generally be counted on to vindicate the law as private attorneys general, without any of the problems attendant upon suits by plaintiffs injured more remotely." The Funds correctly note that these RICO causes of action could not be asserted by the smokers or by the Funds in a subrogation action because the RICO statute requires an injury to "business or property," whereas the smokers' injuries are personal in nature. Hence, the Funds conclude there are no more directly injured "private attorneys general" who could vindicate the law for these alleged RICO violations. The district court also found that because individual smokers would not be able to bring a RICO action, the harms alleged in plaintiffs' complaint would go unremedied were the Funds' action not allowed to continue.

Yet, to the contrary, our holding that plaintiffs lack standing under RICO need not bring about the result plaintiffs fear. The Funds may still bring a subrogation action to recover the medical costs paid out for the individual smokers, and the smokers themselves have sufficient independent incentive to pursue their own causes of action for such additional types of injuries as pain and suffering.

**III. Is a Defendant's Specific Intent to Harm a Plaintiff an Exception to the Direct-Injury Rule?**

Plaintiffs aver that even if their claims fail the direct injury test, they should still have standing to sue because an exception to this rule exists where the defendants specifically intend to harm plaintiffs.

[The court then reviews the relevant cases.] As such, these decisions regarding specific intent do not support the proposition that an indirect injury is actionable where the injury was specifically intended by the defendant. In other words, an allegation of specific intent does not overcome the requirement that there must be a direct injury to maintain this action.

**IV. Common Law Fraud and Special Duty Claims**

[After an examination of the New York cases, the court concludes that] analogous principles to those that doomed plaintiffs' RICO causes of action also bar plaintiffs' common law fraud and special duty actions. . . .

Accordingly, we hereby reverse the district court's March 25, 1998 order with respect to causes of action I and II (the RICO claims), V (the fraud claim), and VI (the special duty claim). The case is remanded to the district court with directions to dismiss plaintiffs' complaint.

## NOTES

1. ***Causation and Privity in Fraud Cases.*** *Laborers Local 17* shows vividly how common law fraud actions often surface in modern contexts, namely, as virtual duplicates of federal RICO claims. The need to limit a defendant's liability for its words is generally greater than it is for deeds because, in our modern era, the number of persons who can claim to have relied on a defendant's public statements is potentially infinite. That said, how clear is the line between direct and indirect causation in fraud cases? If that dichotomy is no longer tenable, what is an appropriate doctrinal substitute? Should the analysis be affected by the fact that individual smokers have largely failed in their common law actions to recover damages from tobacco companies? Whatever its merits, *Laborers Local 17* has been followed in at least seven other circuits that have considered the issue. See, e.g., Serv. Emps. Int'l Union Health & Welfare Fund v. Philip Morris, Inc., 249 F.3d 1068, 1072 n.2 (D.C. Cir. 2001).

In *Holmes*, relied on in *Laborers Local 17*, the defendants were alleged to have engaged in stock manipulation whereby, from 1964 to 1981, they made unduly optimistic statements about the performance of six companies in order to drive up those companies' values. From time to time, the defendants traded in the stock of these companies to create the appearance of a liquid market. Several brokers and dealers purchased substantial quantities of the manipulated stocks with their own funds, only to lose the value of their investment when the fraud was uncovered. The Securities Investor Protection Corporation (SIPC) then had to pay $13 million to cover the losses suffered by clients when these brokerage houses failed. The Supreme Court held that the action by SIPC was barred on the ground that the damages were too remote. Should the customers of the failed houses be allowed to sue for their losses? If not, where is the break in the causal chain? Is there sufficient protection here because the brokerage houses could have sued for their own losses in the fraud? Do the brokerage houses have an incentive to sue after the failure of SIPC's case?

The issue of proximate cause arose again in Lexmark International, Inc. v. Static Control Components, 572 U.S. 118 (2014), which involved liability under the Lanham Act, which provides that any person who makes a "false or misleading representation . . . in a commercial advertisement or promotion . . . shall be liable in a civil action by any person who believes that he or she is or is likely to be damaged by such act." 15 U.S.C. §1125(a). Lexmark manufactured refillable toner cartridges. To secure the return of these cartridges, it offered its customers a "Prebate," "which enabled customers to purchase new toner cartridges at a 20-percent discount if they would agree to return the cartridge to Lexmark once it was empty." To secure that return, it inserted a computer chip in the cartridge that would disable it once the ink ran out. Static Control devised its own microchip that mimicked the behavior of Lexmark's chip and thus allowed Lexmark customers to come to Static Control for refilling. Lexmark brought suit for copyright infringement. Static Control counterclaimed for a violation of the misrepresentation provision of the Lanham Act. It first claimed that Lexmark had purposely misled end users by claiming that they were "legally bound" by the prebate terms to return the cartridges to Lexmark, and second, that they had purposely misled other companies in the cartridge business by claiming that "it was illegal to use Static Control's products to refurbish those cartridges." Scalia, J., relying on *Holmes*, held that these allegations stated a cause of action under the Lanham Act, even though Lexmark was not a direct competitor of Static Control.

> First, Static Control alleged that Lexmark disparaged its business and products by asserting that Static Control's business was illegal. . . . When a defendant harms a plaintiff's reputation by casting aspersions on its business, the plaintiff's injury flows directly from the audience's belief in the disparaging statements. Courts have therefore afforded relief under §1125(a) not only

where a defendant denigrates a plaintiff's product by name, but also where the defendant damages the product's reputation by, for example, equating it with an inferior product. . . .

The District Court emphasized that Lexmark and Static Control are not direct competitors. But when a party claims reputational injury from disparagement, competition is not required for proximate cause; and that is true even if the defendant's aim was to harm its immediate competitors, and the plaintiff merely suffered collateral damage. Consider two rival carmakers who purchase airbags for their cars from different third-party manufacturers. If the first carmaker, hoping to divert sales from the second, falsely proclaims that the airbags used by the second carmaker are defective, both the second carmaker and its airbag supplier may suffer reputational injury, and their sales may decline as a result. In those circumstances, there is no reason to regard either party's injury as derivative of the other's; each is directly and independently harmed by the attack on its merchandise.

The Lanham Act also deals with cases in which the defendant seeks to "confuse" its products with those of the plaintiff, discussed further *infra* Chapter 4, at 268.

**2. *Causation and Damages in Fraud Cases.*** In *Edgington* and most fraud cases, the plaintiff seeks to recover for the lost value of the investment or purchase made, to the extent that this is attributable to the defendant's fraud, which in turn must be distinguished from declines in the value attributable to other sources, such as changes in general economic conditions or area-specific government regulations. See RST §549. Note that section 549(2) is rarely invoked. In loan cases like *Pasley* and *Edgington*, the expectation and reliance interests are often the same, as the creditor wants to recover the amount owed with interest. The expectation measure gives the plaintiff the benefit of her deal, which is repayment with interest. The reliance measure puts the plaintiff back in the position she held before the transaction, which in financial cases also involves repayment with interest. In sales contexts, however, the two measures can diverge, as the profit from the deal can exceed the amount invested plus interest.

In *In re* Detweiller, No. 09-63377, 2017 WL 650062 (Bankr. N.D. Ohio, Feb. 16, 2017), the debtor, who owned a real estate development, misrepresented to the plaintiff-purchasers (1) the timeframe in which utilities and amenities would be built out onto their property, and (2) that there were bonds securing the construction of roads onto their property. Applying Tennessee law, the court noted that "Tennessee recognizes the benefit of the bargain rule as the appropriate measure of damages in fraudulent misrepresentation cases. The benefit of the bargain measures the difference between the actual value of the property that the purchaser received and the value of [sic] the property would have had but for the misrepresentation." Finding the benefit of the bargain remedy to be appropriate in the case at bar, the court awarded the difference of the purchase price, as a marker for the value of the property had it been developed as promised, and what the debtor had paid for the undeveloped property (which remained undeveloped), as a marker for the value of the property in its current condition.

Indeed in *Laborers Local 17*, *supra* at 179, the court hesitates to find proximate cause given both the impracticability and the potential unjust enrichment of allowing recovery for damages where "it becomes difficult to distinguish among the multitude of factors that might have affected the damages. . . . The complexity of these calculations makes the ultimate question of damages suffered by the Funds virtually impossible to determine." See also Koch v. Royal Wine Merchs., Ltd., 907 F. Supp. 2d 1332, 1341 (S.D. Fla. 2012) (discussing the same *Holmes* factors of the "difficulty apportioning responsibility for a plaintiff's damages between a defendant's conduct and other, independent factors," and "the risk of multiple recoveries" arising from uncertain causal chains).

**RESTATEMENT OF THE LAW (SECOND) OF TORTS**

**§549. Measure of Damages for Fraudulent Misrepresentation**

(1) The recipient of a fraudulent misrepresentation is entitled to recover as damages in an action of deceit against the maker the pecuniary loss to him of which the misrepresentation is a legal cause, including

(a) the difference between the value of what he has received in the transaction and its purchase price or other value given for it; and

(b) pecuniary loss suffered otherwise as a consequence of the recipient's reliance upon the misrepresentation.

(2) The recipient of a fraudulent misrepresentation in a business transaction is also entitled to recover additional damages sufficient to give him the benefit of his contract with the maker, if these damages are proved with reasonable certainty.

## *Ernst & Young, L.L.P. v. Pac. Mut. Life Ins. Co.*

51 S.W.3d 573 (Tex. 2001)

O'Neill, J. In this case, we must decide the scope of an accounting firm's liability for making fraudulent misrepresentations in an audit report. Specifically, we consider whether the intent-to-induce-reliance element of a fraud claim requires a direct relationship between the alleged fraudfeasor and a specific known person—commonly referred to in this context as "privity." . . .

### I. Background

At the center of this litigation is a series of notes that InterFirst Corporation issued in 1982 and Pacific Mutual Life Insurance Company purchased in 1987 after InterFirst merged with RepublicBank Corporation. Pacific claims that in purchasing the InterFirst notes it relied on an Ernst & Young audit report that confirmed RepublicBank's financial strength. When RepublicBank filed for bankruptcy shortly after the merger and the InterFirst notes became virtually worthless, Pacific sued Ernst & Young for fraudulent misrepresentation. . . .

The trial court granted Ernst & Young's summary judgment motion and denied Pacific's cross-motion as moot. Pacific appealed, and the court of appeals reversed the summary judgment. It held that there were fact issues on each element of Pacific's common-law fraud claim. . . . In concluding that a fact issue existed on Ernst & Young's intent, the court of appeals applied section 531 of the *Restatement*, which provides:

> One who makes a fraudulent misrepresentation is subject to liability to the persons or class of persons whom he intends or *has reason to expect* to act or to refrain from action in reliance upon the misrepresentation, for pecuniary loss suffered by them through their justifiable reliance in the type of transaction in which he intends or has reason to expect their conduct to be influenced.

Restatement (Second) of Torts §531 (1977) (emphasis added). The court held that Pacific's three affidavits created a fact issue on whether Ernst & Young had "reason to expect" that an institutional investor like Pacific would rely on its representations about RepublicBank's financial strength in purchasing securities issued by InterFirst before the banks merged. We granted Ernst & Young's petition for review to examine the intent element of Pacific's fraud claim.

## II. Fraud

. . . To prevail on its fraud claim, Pacific must prove that: (1) Ernst & Young made a material representation that was false; (2) it knew the representation was false or made it recklessly as a positive assertion without any knowledge of its truth; (3) it intended to induce Pacific to act upon the representation; and (4) Pacific actually and justifiably relied upon the representation and thereby suffered injury. . . . Ernst & Young contends that it did not intend to induce Pacific's reliance on its audit report and, in any event, Pacific's reliance was not justifiable.

The court of appeals applied the *Restatement's* "reason-to-expect" standard; that is, Pacific could establish fraud's intent element by showing that Ernst & Young had "reason to expect" that institutional investors like Pacific would rely on Ernst & Young's audit opinion when evaluating securities that the audited entity backs. Ernst & Young claims the court of appeals erred because Texas law requires Pacific to demonstrate a direct intent to specifically induce Pacific's reliance in order to maintain its fraud claim. In other words, Ernst & Young asserted that Pacific must show that Ernst & Young, in auditing RepublicBank's 1986 financial statements, specifically intended to induce Pacific to buy the InterFirst notes. Ernst & Young likens the direct-intent requirement to the doctrine of "privity," which requires a direct relationship between the alleged fraudfeasor and a specific known person. Ernst & Young contends that the *Restatement's* reason-to-expect standard is incompatible with Texas law in this regard. We disagree.

### A. Intent

Our fraud jurisprudence has traditionally focused not on whether a misrepresentation is directly transmitted to a known person alleged to be in privity with the fraudfeasor, but on whether the misrepresentation was intended to reach a third person and induce reliance. . . . Thus, we have held that a misrepresentation made through an intermediary is actionable if it is intended to influence a third person's conduct. . . .

Under *Restatement* section 531, a person who makes a misrepresentation is liable to the person or class of persons the maker intends or "has reason to expect" will act in reliance upon the misrepresentation. Restatement (Second) of Torts §531 (1977). Our jurisprudence, which focuses on the defendant's knowledge and intent to induce reliance, is consistent with the *Restatement* and with the law in other jurisdictions that have considered the issue. . . .

The *Restatement's* comments further illustrate the narrow scope of the reason-to-expect standard and foreclose the potential for "unlimited liability" that Ernst & Young decries. Even an obvious risk that a misrepresentation might be repeated to a third party is not enough to satisfy the reason-to-expect standard; rather, the alleged fraudfeasor must "have information that would lead a reasonable man to conclude that there is *an especial likelihood* that it will reach those persons *and will influence their conduct.*" Restatement (Second) of Torts §531 cmt. d (1977) (emphasis added). . . . In sum, the reason-to-expect standard requires more than mere foreseeability; the claimant's reliance must be "especially likely" and justifiable, and the transaction sued upon must be the type the defendant contemplated. . . .

We conclude that section 531's reason-to-expect standard comports with our jurisprudence and does not expand the parameters of common-law fraud in Texas as Ernst & Young claims. . . . But we agree with Ernst & Young that the court of appeals incorrectly applied the reason-to-expect standard to the summary-judgment proof.

### B. Reason to Expect

Pacific offered affidavits from an employee and two experts to show that Ernst & Young had reason to expect that Pacific would rely on the RepublicBank audit opinion when deciding to purchase the InterFirst notes. Victor Moore, a certified public accountant, testified that

Ernst & Young "knew" that investors in all securities backed by First Republic, the merged entity, would rely upon the information in the audit report. Larry Card, a Pacific executive vice-president, testified that it was "known and expected" by public accounting firms like Ernst & Young that documents like the prospectuses and proxy materials at issue here are widely disseminated throughout the investment community and investors rely upon information from these materials when evaluating investments in securities the subject entity backs. Finally, Alan Coleman, former dean of Southern Methodist University's Edwin L. Cox School of Business, testified that investors like Pacific commonly rely on representations made in SEC-filed documents in evaluating securities backed by an entity. He also testified that Ernst & Young's contention that it did not intend Pacific to rely on the audit report in buying the InterFirst notes was contrary to commonly accepted and firmly established practices in the investment community. The court of appeals concluded that this evidence raised a fact issue on whether Ernst & Young had "reason to expect" Pacific's reliance on the audit report in deciding to buy the InterFirst notes. We disagree.

Pacific's affidavits speak in terms of what is commonly "known" or "expected" in the investment community. But even an obvious risk that a third person will rely on a representation is not enough to impose liability. *See* Restatement (Second) of Torts §531 cmt. d (1977). General industry practice or knowledge may establish a basis for foreseeability to show negligence, but it is not probative of fraudulent intent. To prove that an alleged fraudfeasor had reason to expect reliance,

> [t]he maker of the misrepresentation *must have information* that would lead a reasonable man to conclude that there is *an especial likelihood* that it will reach those persons and will influence their conduct. There must be something in the situation *known to the maker* that would lead a reasonable man to govern his conduct on the assumption that this will occur. *If he has the information*, the maker is subject to liability under the rule stated here.

*Id.* (emphasis added). The generalized industry practice or understanding the affidavits describe is insufficient to show that Ernst & Young possessed information of an especial likelihood that investors like Pacific would rely on Ernst & Young's statements in the merger-related prospectuses in purchasing securities InterFirst had issued years earlier.

Pacific argues that, even without the affidavits, the SEC documents were filed under statutes designed to protect investors like Pacific; accordingly, *Restatement* section 536 affords a presumption that Ernst & Young had reason to expect Pacific's reliance on the filed documents. Restatement (Second) of Torts §536 (1977). Section 536 provides:

> If a statute requires information to be . . . filed . . . for the protection of a particular class of persons, one who makes a fraudulent misrepresentation in so doing is subject to liability to the persons for pecuniary loss suffered through their justifiable reliance upon the misrepresentation in a transaction of the kind in which the statute is intended to protect them.

*Id.* Under this section, one who complies with a statutory filing requirement is presumed to have reason to expect that the information will reach and influence the class of persons the statute is designed to protect. *Id.* cmt. c. In determining the protected class, the focus is on the statute's purpose rather than the person furnishing the information. *Id.* cmt. d.

. . . [U]nlike section 531, which is compatible with Texas fraud jurisprudence, section 536 has no counterpart in Texas common law and other courts have rarely applied it. . . . Because section 536 effectively alleviates a claimant's burden to show intent to induce reliance in fraud actions, it should be applied narrowly if at all. Investors already have remedies for securities violations under Rule 10b-5 and other federal and state securities laws. Indeed, this case was originally filed in federal court as a Rule 10b-5 action, but was dismissed because the statute of limitations had run. Because these and other remedies are available to protect investors, we

are reluctant to apply section 536's presumption and subject market participants to liability for fraud damages to an almost limitless class of potential plaintiffs.

In sum, we hold that, because Ernst & Young negated the intent-to-induce-reliance element of Pacific's fraud claim, the trial court properly granted summary judgment in Ernst & Young's favor. And because summary judgment was proper on this basis, we need not consider Ernst & Young's alternative argument that Pacific's reliance was not justifiable. . . .

### IV. Conclusion

We conclude that Ernst & Young is entitled to summary judgment on Pacific's fraud claim because it negated the intent element of the claim as a matter of law by establishing that it did not have reason to expect Pacific would rely on the audit report when it bought the InterFirst notes. . . .

## NOTE

***"Acting with the Purpose of Inducing Reliance."*** Proximate cause concerns the intended reach, or scope, of the misrepresentation. Part of this inquiry is whether the defendant acted with the purpose of inducing reliance.

### RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM

#### §12. Scope of Liability

***Comment b. The Purpose of the Representation:*** Liability for fraud requires a showing that the defendant spoke for the purpose of influencing the plaintiff or a class of parties in which the plaintiff was included. The liability, in turn, extends to damage suffered by those whose reliance the defendant intended to induce. It also includes damage suffered by others whom the defendant had reason to expect would rely on a statement. The plaintiff need not have dealt directly with the defendant. It is enough if the defendant had reason to expect that the plaintiff would receive the statement and rely on it. . . .

The principles just stated require more than just foreseeability of a risk that the plaintiff might someday rely on what the defendant says. They require, rather, that the defendant have reason to consider that reliance likely, even if the plaintiff's identity is indistinct. It might seem peculiar to place such limits on the liability of a defendant who, by hypothesis, has acted with a culpable state of mind. But the limits reflect a reasonable solicitude for the potential defendant who commits no fraud but speaks often, or who employs others who speak often. Even when speaking truthfully, such a party may wish to prepare for (and insure against) the risk of litigation, with its attendant expenses, risk of error, and other hardships. The limits explained here help such defendants measure their potential exposure in advance and act accordingly.

Moreover—whether this proximate cause element is termed "intent to mislead," "acting with the purpose of inducing reliance," or "indirect reliance"—actual and justifiable reliance by the plaintiff remains a separate necessary element of fraud, just like factual causation is a necessary element of negligence. Even if "a misrepresentation may arrive indirectly through an intermediary . . . reliance [by the plaintiff] directly upon that misrepresentation is required." Admiral Ins. Co. v. Heath Holdings USA, Inc., No. 3:03-CV-1634-G, 2004 WL 1144062, at *5 n.5 (N.D. Tex. May 21, 2004).

## 4. Relaxing Reliance: Securities Fraud, Class Actions, and Statutory Fraud Schemes

### *Kaufman v. i-Stat Corp.*

754 A.2d 1188 (N.J. 2000)

LaVecchia, J. This appeal presents the question whether a class of plaintiffs in a common-law action for fraud can prove the element of reliance through the presumption of a fraud on the market. The theory of fraud on the market, as described by the United States Supreme Court in Basic Inc. v. Levinson, 485 U.S. 224 (1988), allows plaintiffs to bring class actions under federal securities-fraud law by excusing those plaintiffs from the burden of proving individual reliance. Instead, plaintiffs may establish the reliance element of their claims by showing that they purchased securities in the secondary markets at attractive prices that had been artificially affected by an issuer's misrepresentations and omissions.

Plaintiff Susan Kaufman held shares of defendant i-Stat Corporation ("i-Stat") over a period during which i-Stat allegedly misrepresented certain financial matters and the misrepresentations were discovered and publicized. The misrepresentations were never made to Kaufman by i-Stat or any intermediary. Kaufman relied on the price of the stock in her decisions, and now contends that, because i-Stat's misrepresentations were reflected in the share price, she can make out claims for common-law fraud and negligent misrepresentation on the basis of the share price alone.

Even though the theory of fraud on the market has a place in the securities law of this nation, it is a stranger to New Jersey's securities laws. It is also not consistent with the current requirements for a common-law action for fraud in New Jersey. Use of the fraud-on-the-market theory is not the equivalent of proof of indirect reliance that is required minimally in a common-law fraud action. Because we discern no compelling reason to deviate from our current standard of proof for the reliance element in a common-law fraud action, and because we, like many commentators, cast a jaundiced eye on the worth of the fraud-on-the-market theory, we decline to expand our common law to permit its use. Accordingly, we reverse the judgment of the Appellate Division and reinstate the trial court's dismissal of plaintiff's fraud claim.

#### I.

. . . i-Stat is a public New Jersey corporation that manufactures and markets diagnostic blood-analysis equipment designed to assist medical professionals at the point of patient care. Specifically, the company makes a hand-held blood analyzer and cartridges to test individual patients. The corporation's stock is traded on the NASDAQ National Market System. On October 31, 1995, during the events at issue in this action, i-Stat had 11,083,421 shares of common stock issued and outstanding.

On May 9, 1995, i-Stat announced its financial results for the first fiscal quarter of 1995, ending March 31. The company reported net sales of $3,359,000, as compared to reported net sales of $1,651,000 for the same period in the previous year. The company reported a net loss of $6,531,000 ($0.59 per share) for the first quarter as compared with a net loss of $6,056,000 ($0.55 per share) for the same period in the prior year. Kaufman alleges that, to produce the improved sales figures, i-Stat misrepresented acceptance of the company's products to the public by "report[ing] sales that were not, in fact, true sales, but were, instead, loans on a trial basis." For example, i-Stat allegedly reported "sales" to certain hospitals without disclosing that the "sales" were induced by "charitable donations" from interested third

parties to the purchasing hospitals. These sales practices resulted in an exaggerated representation of the company's sales and degree of market acceptance of its products.

On May 22, 1995, Susan Kaufman purchased one hundred shares of i-Stat common stock at 21 ¾, a total investment of $2175. Meanwhile, on that date, *Forbes* magazine reported that a medical investment newsletter believed i-Stat was experiencing difficulties and that its products were not economical. On June 21, 1995, an article in *The Financial Post*, a Canadian financial publication, reported "the expected profitability and growth of the Company," citing an interview with defendant Imants Lauks. On September 21, 1995, i-Stat reached its all-time high, trading at 43 ¾.

The bubble began to burst on January 28, 1996. On that date, *The New York Times* reported that Daniel R. Frank, manager of the Fidelity Advisor Strategic Opportunities Fund, whose successor is still the largest institutional holder of i-Stat, had made charitable contributions to hospitals to enable them to obtain i-Stat's diagnostic equipment.

Then, on March 19, 1996, *The Wall Street Journal* reported that the Securities and Exchange Commission ("SEC") was investigating i-Stat's business. The article revealed that some of i-Stat's "sales" had been loans of the products to hospitals on a trial basis rather than actual sales. i-Stat responded with a press release confirming the SEC's investigation and inquiry into its sales procedures. On that same day, i-Stat's shares, which had been declining, tumbled 2 ½ to 28 ¾. Two million shares of i-Stat, nearly one sixth of the shares outstanding on that date, traded on March 19.

On May 20, 1996, Kaufman sold 50 shares at 20 ¼. On June 19, she filed suit as putative class representative on behalf of all purchasers of i-Stat common stock between May 9, 1995, and March 19, 1996. . . . Kaufman alleged common-law fraud and negligent misrepresentation, contending that i-Stat's deliberately false and misleading statements regarding its financial status and deceptive sales practices inflated the stock price during the class period. . . .

i-Stat filed an answer alleging various affirmative defenses. Both parties stipulated to the following: (1) Kaufman did not "actually or directly receive or rely on any communication containing any misrepresentation . . . nor . . . actually receive or rely on any communication which omitted material facts[;]" (2) Kaufman purchased her stock through a brokerage firm and did not directly receive or rely on any communication from the brokerage firm concerning the i-Stat purchase; and (3) Kaufman "relied exclusively on the integrity of the market price of i-Stat stock at the time of her purchase." Therefore, Kaufman's satisfaction of the reliance element of the common-law fraud and negligent misrepresentation claims depends entirely on the fraud-on-the-market theory.

i-Stat moved for summary judgment on the ground that Kaufman failed to state a cause of action in fraud or in negligent misrepresentation because she could not satisfy the actual reliance requirement in each. The trial court granted the motion, dismissing Kaufman's claims with prejudice. . . .

On appeal, the Appellate Division reversed the dismissal of plaintiff's complaint on the common-law-fraud claim but affirmed the dismissal of the negligent-misrepresentation claim. The court concluded that plaintiff's reliance on the integrity of the market price of the security was sufficient to satisfy the reliance requirement of a common-law-fraud claim when the security was inflated artificially by the corporation's deliberate false statements, but declined to extend this form of proof of reliance to a negligent-misrepresentation claim, citing public policy considerations in favor of a more limited scope of liability for negligent communication of fraudulent misrepresentations. . . .

## II.

Assuming the allegations made by plaintiff Susan Kaufman on behalf of a putative class are correct, and because this is an appeal of a grant of summary judgment we give her the benefit

of every inference that they are, then the misrepresentations and omissions made by the management of i-Stat corporation caused her to lose money. . . .

The misdeeds that plaintiff alleges i-Stat to have committed, if proven, clearly fall within the ambit of [a Rule 10b-5 securities fraud action]. . . .

[Heightened procedural requirements in the Private Securities Litigation Reform Act] have led plaintiffs to attempt to "avoid some of the new provisions of the [PSLRA] by seeking procedural advantages available in state courts." . . .

Most of those cases newly brought in state court have been, as this one is, substitutes for Rule 10b-5 actions. To maintain those actions' viability, the plaintiffs bringing them have sought to have the courts hearing them incorporate the doctrine of fraud on the market into the common law of their respective states. Plaintiff, however, has cited no case in which a state court ruling on its common law has accepted the invitation. Defendants, by contrast, have found several cases declining to allow the fraud-on-the-market theory to establish reliance at common law. . . . Our research reveals that one court has accepted the theory in dictum, but no claim based directly on the theory appears to have been adjudicated in the jurisdiction. . . .

The federal courts with jurisdiction in New Jersey have rejected the idea that fraud on the market can create a common-law action for fraud. Thus, the Third Circuit, in one of the landmark decisions on fraud on the market, Peil v. Speiser, 806 F.2d 1154 (3d Cir. 1986), on which the Supreme Court relied extensively in *Basic*, declined to allow a state-law claim to proceed because "no state courts have adopted the theory, and thus direct reliance remains a requirement of a common law securities fraud claim." . . .

The question in this matter is whether the public interest in the development of our common law of fraud is served by plaintiff's contention that the fraud-on-the-market theory should be permitted to be used in New Jersey despite a contrary conclusion in the many other jurisdictions that have considered the same question.

## III.

### A.

Plaintiff characterizes the fraud-on-the-market theory as no more than a reasonable application of indirect reliance principles. Indirect reliance allows a plaintiff to prove a fraud action when he or she heard a statement not from the party that defrauded him or her but from that party's agent or from someone to whom the party communicated the false statement with the intention that the victim hear it, rely on it, and act to his or her detriment. . . . The Appellate Division accepted plaintiff's argument, noting that the fraud-on-the-market theory of federal securities fraud law was "[b]ased on a similar analysis," and holding "that indirect reliance in the form of reliance on the integrity of the market price for a corporate security which has been artificially inflated by the corporation's deliberate false statements concerning its financial condition may satisfy the reliance element of a common law fraud action." . . .

Defendants note this shift from a chain of communicated false statements, however indirectly passed along from one to another, and argue that this Court's standard for reliance, even indirect reliance, requires that the plaintiff have actually relied on the misstatement, i.e., that the plaintiff actually received and considered the misstatement or omission, however indirectly uttered, before he or she completed the transaction. Defendant argues that until the decision below, "no New Jersey state court [had] stretched the limits of common law liability to encompass a situation [in which] plaintiff never actually received or relied on any of the alleged misstatements."

We agree with defendants. The actual receipt and consideration of any misstatement remains central to the case of any plaintiff seeking to prove that he or she was deceived by the misstatement or omission. . . .

C.

Indirect reliance remains today what we held it to be. . . . If proven, it is an element of a claim of fraud. If a party to a transaction makes a false statement to another party, intending or knowing that the other party in the transaction will hear it and rely on it, and the second party to the transaction actually hears the substance of the misrepresentation, by means however attenuated, and considers the actual content of that misrepresentation when making the decision to complete the transaction, then that person has established indirect reliance to support a fraud claim.

In this case, plaintiff has explicitly stated that she did not consider i-Stat's financial statements, either by herself or in consultation with an investment professional, but acted only on the market price. By that statement she denies that she ever considered i-Stat's sales volume in her buying decision. Thus, she has failed to establish that she relied, however indirectly, on the misstatements of i-Stat and its management. Therefore, under our traditional standard for proof of reliance, even indirect reliance, plaintiff fails to show reliance and, therefore, fails to make out a claim for fraud. . . .

V.

. . . Accepting fraud on the market as proof of reliance in a New Jersey common-law fraud action would undercut the public interest in preventing forum-shopping, weaken our law of indirect reliance, and run contrary to the policy direction of the Legislature and Congress. We decline to expand our law regarding satisfaction of the reliance element of a fraud action on the basis of a complex economic theory that has not been satisfactorily proven. In so holding, we note that plaintiff had available to her an adequate federal remedy perfectly suited to her complaint. She chose not to pursue it.

VI.

Accordingly, the decision of the Appellate Division allowing the reliance element of a fraud claim to be proven by the fraud-on-the-market theory is reversed, and the judgment of the Superior Court, Law Division is reinstated, dismissing plaintiff's action.

Stein, J., dissenting. In this appeal, the issue before the Court is whether reliance on the integrity of the market price for a corporate security satisfies the reliance element of a cause of action for common law fraud. . . .

I.

The narrow issue before the Court is whether the fraud-on-the-market theory of reliance, articulated and adopted by the United States Supreme Court in Basic Inc. v. Levinson, 485 U.S. 224, 241–48, 108 S. Ct. 978, 989–92, 99 L.Ed.2d 194, 214–19 (1988), adequately may satisfy the reliance element of a state law claim for common law fraud.

A.

A common-law fraud action has five elements. They are "(1) a material misrepresentation of a presently existing or past fact; (2) knowledge or belief by the defendant of its falsity; (3) an intention that the other person rely on it; (4) reasonable reliance thereon by the other person; and (5) resulting damages." . . .

Since 1957 New Jersey has recognized that indirect reliance may satisfy the reliance element of a common law fraud action. . . .

Thus, proof that a party deliberately made false representations with the intent that they be communicated to others for the purpose of inducing others to rely upon them may satisfy the reliance element of common law fraud.

In this appeal, i-Stat issued materially misleading public statements about its financial condition and prospects, subsequent to which the price of its stock rose. The stock market "act[ed] as the unpaid agent of the investor [and] inform[ed plaintiff] that given all the information available to it, the value of the stock is worth the market price." . . . Under the principle of indirect reliance . . . i-Stat's intentional misrepresentation may be actionable as a common law fraud even though the authors of the false information did not communicate directly to plaintiff.

The question thus is whether the principle of indirect reliance applies in the context of purchasers of publicly traded securities where the fraud was perpetrated generally on the public with the intention that *all* purchasers of the securities would be defrauded. The answer to that question is found in the United States Supreme Court's analysis of the fraud-of-the-market theory in Section 10b-5 cases.

**B.**

. . . Prior to the United States Supreme Court's 1988 *Basic* decision, to satisfy the reliance element of a fraud claim brought under Rule 10b-5 victims of fraudulent misrepresentations were required to show that they actually relied on the misrepresentations made by defendants. . . .

In *Basic, supra*, the Supreme Court first concluded that the reliance element in a claim based on fraudulent misrepresentations under Rule 10b-5 may be satisfied by proof that the plaintiff relied on the integrity of the market price. . . . The Supreme Court stated that the fraud-on-the-market theory of reliance is "based on the hypothesis that, in an open and developed securities market, the price of a company's stock is determined by the available material information regarding the company and its business. . . . Misleading statements will therefore defraud purchasers of stock even if the purchasers do not directly rely on the misstatements." . . . As such, "[t]he causal connection between the defendants' fraud and the plaintiffs' purchase of stock in such a case is no less significant than in a case of direct reliance on misrepresentations." . . .

The fraud-on-the-market theory of reliance is but a rebuttable presumption of reliance. . . . The Supreme Court found that it was fair to allow reliance to be presumed in Rule 10b-5 cases because requiring "a plaintiff to show a speculative state of facts, *i.e.*, how he would have acted if omitted material information had been disclosed or if the misrepresentation had not been made would place an unnecessarily unrealistic evidentiary burden on the Rule 10b-5 plaintiff who has traded on an impersonal market." . . .

Defendants may "rebut proof of the elements giving rise to the presumption, or show that the misrepresentation in fact did not lead to a distortion of price or that an individual plaintiff traded or would have traded despite his knowing the statement was false." . . . Similarly, the presumption may be rebutted by "[a]ny showing that severs the link between the alleged misrepresentation and either the price received (or paid) by the plaintiff, or his decision to trade at a fair market price" or if credible information "entered the market and dissipated the effects of the misstatements." . . .

For an action to be maintained as a class action, "questions of law or fact common to the members of the class [must] predominate over any questions affecting only individual members." *Rule* 4:32-1(b)(3). Without the fraud-on-the-market theory of reliance in securities fraud cases, each individual plaintiff would be required to prove his or her own actual reliance on the fraudulent misrepresentation or omission of the defendant. In that context, individual issues of reliance would predominate over common issues and class action certification generally would be denied. . . .

### III.

Recognizing fraud on the market as a means of proving reliance in common law fraud actions requires "merely an application of existing common law principles expressed in the indirect reliance cases from . . . other jurisdictions, and in the Restatement Second of Torts." . . . It requires only that we recognize that "[t]he genius of the common law is its flexibility and capacity for growth and adaptation." . . . "It has always been recognized that the common law is not a rigid, inflexible, static thing, but is a living organism, ever growing and expanding to meet the problems and needs of changing social and economic conditions." . . . Merely because an asserted right is somewhat novel is "not [a] valid reason [ ] for denying its existence. . . . The common law is not a primer of rigid and absolute rules, but rather a body of broad and comprehensive principles created by judicial decisions and based on justice, reason, and common sense." . . .

I would affirm the judgment of the Appellate Division. Justice O'Hern and Justice Long join in the opinion.

## NOTES

**1.** ***Loss Causation in Securities Fraud on the Market Cases.*** In all misrepresentations, the plaintiff must show "loss causation," or some causal link between the alleged falsehoods and the plaintiff's economic loss. Requiring strict proof of the traditional reliance element in deceit cases would normally block the action. Should plaintiffs be able to overcome that barrier by showing that the defendant's false statements led to systematic market movements adverse to the interest of the plaintiffs? In *Basic*, cited in *Kaufman*, the Supreme Court approved using the "fraud on the market" theory in federal securities cases:

> The fraud on the market theory is based on the hypothesis that, in an open and developed securities market, the price of a company's stock is determined by the available material information regarding the company and its business. . . . Misleading statements will therefore defraud purchasers of stock even if the purchasers do not directly rely on the misstatements. . . . The causal connection between the defendants' fraud and the plaintiffs' purchase of stock in such a case is no less significant than in a case of direct reliance on misrepresentations.

*Basic* then held that the fraud on the market theory created a "rebuttable presumption of reliance." "Requiring proof of individualized reliance from each member of the proposed plaintiff class effectively would have prevented respondents from proceeding with a class action, since the individual issues then would have overwhelmed the common ones." The Court therefore concluded that although individual proof of reliance might be appropriate in the "face-to-face transactions contemplated by early fraud cases," it was inappropriate for transactions in mass markets.

White, J., wrote a skeptical dissent: "But with no staff economists, no experts schooled in the 'efficient-capital-market hypothesis,' no ability to test the validity of empirical market studies, we are not well equipped to embrace novel constructions of a statute based on contemporary microeconomic theory." See generally Daniel R. Fischel, Use of Modern Finance Theory in Securities Fraud Cases, 38 Bus. Law. 1 (1982). On efficient markets generally, see Ronald J. Gilson & Reinier H. Kraakman, The Mechanisms of Market Efficiency, 70 Va. L. Rev. 549 (1984).

Proof of loss causation in securities actions is now regulated by the PSLRA, 15 U.S.C. §78u-4(b)(4), as follows:

> (4) Loss causation. In any private action arising under this title, the plaintiff shall have the burden of proving that the act or omission of the defendant alleged to violate this title caused the loss for which the plaintiff seeks to recover damages.

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This provision was instrumental in the Supreme Court's decision in Dura Pharmaceuticals, Inc. v. Broudo, 544 U.S. 336, 343–44 (2005), which refused the plaintiff's invitation to allege a securities claim simply by alleging in the complaint and subsequently establishing that "the price" of the security "on the date of purchase was inflated because of the misrepresentation," without accounting for any circumstances between purchase and sale.

> [I]f, say, the purchaser sells the shares quickly before the relevant truth begins to leak out, the misrepresentation will not have led to any loss. If the purchaser sells later after the truth makes its way into the marketplace, an initially inflated purchase price might mean a later loss. But that is far from inevitably so. When the purchaser subsequently resells such shares, even at a lower price, that lower price may reflect, not the earlier misrepresentation, but changed economic circumstances, changed investor expectations, new industry-specific or firm-specific facts, conditions, or other events, which taken separately or together account for some or all of that lower price.

The fraud on the market theory received a boost from the Supreme Court in Erica P. John Fund, Inc. v. Halliburton Co., 563 U.S. 804, 813 (2011). In overturning the decisions below, a unanimous Court held that the fraud on the market theory of *Basic* and *Dura* did not require representative plaintiffs to prove loss causation in order to obtain class certification in a private securities fraud case. The plaintiffs' complaint alleged that in order to inflate its stock price, the defendant had deliberately underestimated its liability for potential asbestos claims and overstated its anticipated benefits from a construction contract and potential merger. Roberts, C.J., explained that the lower court's insistence on proof of loss causation

> contravenes *Basic*'s fundamental premise—that an investor presumptively relies on a misrepresentation so long as it was reflected in the market price at the time of his transaction. The fact that a subsequent loss may have been caused by factors other than the revelation of a misrepresentation has nothing to do with whether an investor relied on the misrepresentation in the first place, either directly or presumptively through the fraud-on-the-market theory. Loss causation has no logical connection to the facts necessary to establish the efficient market predicate to the fraud-on-the-market theory.

Subsequently in Amgen, Inc. v. Connecticut Retirement Plans and Trust Funds, 568 U.S. 455, 463 (2013), a divided Supreme Court extended *Halliburton* by holding that certification of the plaintiff class could take place even before any proof by the plaintiff of the materiality or any statements or omissions about Amgen's statements on the safety or efficacy of its two "flagship drugs."

**2.** ***Damages Under the Fraud on the Market Theory.*** Under the fraud on the market theory, how should damages be computed? Take a simple case in which a company places false statements in its prospectus in order to increase the price it can obtain for a new offering of its publicly traded stock. If a person both buys and sells shares in the firm before the fraud is unmasked, ordinarily he should not recover damages. The extra money paid to purchase the shares is roughly offset by the extra money obtained on sale. But if an open-market purchase is made before the fraud is discovered, and the sale is made after the market breaks, then the downward adjustment in the share price (measurable, with difficulty, by statistical techniques) sets the level of the damages suffered by these share purchasers.

Using the fraud on the market approach makes it appear that all other market participants have suffered at the hands of the defendant. In many cases, however, many ignorant buyers or sellers profit incidentally from the defendant's fraud. Consider a person who already owns stock in a company that launches a new issue of stock with fraudulent statements that inflate the value of both its new shares and the existing shares. The owner might dispose of the shares before the fraud is revealed, thereby obtaining a higher price than if the fraud had never been committed. The buyer of those shares will in turn suffer losses once the fraud has been revealed. The gains and losses of buyer and seller will roughly net out. The fraud on the market theory, however, charges the buyer's losses to the issuer while ignoring the seller's gains. The theory, therefore, in

principle, overdeters fraud by overstating the social losses that it causes. One possible escape is to set damages equal to the gains that the fraudulent defendant obtained from the fraud. Yet even these gains may be hard to measure, and, in some cases like *Basic*, appear to be nonexistent. On these damages problems, see Fischel, *supra* Note 1, at 194, 38 Bus. Law. at 16–17.

**3. *Class Actions and Relaxing Reliance.*** In the context of consumer fraud, two opinions from Chief Judge Diane Wood of the Seventh Circuit established that the individualized reliance inquiry may be relaxed during class certification. Suchanek v. Sturm Foods, Inc., 764 F.3d 750, 759–60 (7th Cir. 2014) (Wood, C.J.); Beaton v. SpeedyPC Software, 907 F.3d 1018, 1029–30 (7th Cir. 2018) (Wood, C.J.). For state law analogues, see Marler v. E.M. Johansing, LLC, 199 Cal. App. 4th 1450 (2011) (holding that an inference of reliance may be made on a class-wide basis); Strawn v. Farmers Ins. Co., 256 P.3d 100 (Or. 2011) (holding that class-wide reliance need not be individualized); Rikos v. P&G, 799 F.3d 497, 517–18 (6th Cir. 2015) (same, summarizing North Carolina state cases). See also Sarah Roshanne Anchors, Mass Market Fraud Theory: Dispensing with Individual Reliance in Class Actions Where Plaintiffs Allege Pervasive Misrepresentations to the Public, 43 Tort Trial & Ins. Prac. L.J. 221 (2008).

Other courts find that individualized reliance inquiries may be necessary in class actions. Compare Castano v. Am. Tobacco Co., 84 F.3d 734, 745 (5th Cir. 1996) ("[A] fraud class action cannot be certified when individual reliance will be an issue."), with White v. Symetra Assigned Benefits Serv. Co., No. 20-1866 MJP, 2022 WL 3092849, at *19–25 (W.D. Wash. Aug. 3, 2022) (summarizing circuit split as to "common sense" inferences of reliance in consumer fraud class actions, and ultimately allowing such an inference).

**4. *Statutory Fraud and Consumer Protection Schemes.*** Public law statutes need not be bound by common law elements. Statutory fraud often does away with reliance altogether. This legislative choice may be thought of as a decision to punish and deter misconduct, irrespective of a direct causal link to the plaintiff. For an example of relaxing, but not eliminating, the reliance element in state-level consumer protection statutes, see Daniel v. Ford Motor Co., 806 F.3d 1217, 1225–26 (9th Cir. 2015) (holding that two California consumer protection statutes allow reliance to "be presumed, or at least inferred," when a seller makes a material omission to a buyer). In this context, "[m]ateriality is judged from the perspective of a 'reasonable consumer.'" Mendoza v. Midea Microwave & Elec. Appliances Mfg. Co. Ltd., No 1:20-cv-01133, 2023 WL 8358208, at *4 (E.D. Cal. Dec. 1, 2023).

## *People of New York v. Trump*

No. 452564/2022, 2024 WL 733991 (N.Y. Sup. Ct. Feb. 16, 2024)

Engoron, J. After presiding over a non-jury trial that began on October 2, 2023, and ended on December 13, 2023, with closing arguments on January 11, 2024, this Court makes the following findings of fact and conclusions of law and issues this Decision and Order:

### Summary

Donald Trump and entities he controls own many valuable properties, including office buildings, hotels, and golf courses. Acquiring and developing such properties required huge amounts of cash. Accordingly, the entities borrowed from banks and other lenders. The lenders required personal guarantees from Donald Trump, which were based on statements of financial condition compiled by accountants that Donald Trump engaged. The accountants created these "compilations" based on data submitted by the Trump entities. In order to borrow more and at lower rates, defendants submitted blatantly false financial data to the accountants, resulting in fraudulent financial statements. When confronted at trial with the statements, defendants' fact and expert witnesses simply denied reality, and defendants failed to accept responsibility or to impose internal controls to prevent future recurrences.

As detailed herein, this Court now finds defendants liable, continues the appointment of an Independent Monitor, orders the installation of an Independent Director of Compliance, and limits defendants' right to conduct business in New York for a few years.

### Introduction

In this civil action, plaintiff, the People of the State of New York, by Letitia James, Attorney General of the State of New York, seeks monetary penalties and injunctive relief against Donald John Trump ("Donald Trump") (the former president of the United States) [and his affiliates and family members]. Plaintiff essentially alleges (1) that the individual defendants violated New York Executive Law §63(12) by submitting false financial statements to banks and insurance companies to obtain better rates on loans and insurance coverage; and (2) that the holding entities are liable for the individual defendants' misdeeds. Defendants (1) allege that the statements were completely or substantially correct; and (2) crow that the borrowers paid back all loans fully and on time.

#### Common Law Fraud

The instant action is not a garden-variety common law fraud case. Common law fraud (also known as "misrepresentation") has five elements: (1) A material statement; (2) falsity; (3) knowledge of the falsity ("scienter"); (4) justifiable reliance; and (5) damages. Alleging the elements is easy; proving them is difficult. Is the statement one of fact or opinion? Material according to what standard? Knowledge demonstrated how? Justifiable subjectively or objectively? In mid-twentieth century New York, to judge by contemporary press reports and judicial opinions, fraudsters were having a field day.

#### Executive Law Section 63(12)

Along came Executive Law §63(12), which began life as Laws of 1956, Chapter 592, "An act to amend the executive law, in relation to cancellation of registration of doing business under an assumed name or as partners for repeated fraudulent or illegal acts."

In the subsequent six decades, the State has toughened the statute. In Laws of 1965, Chapter 666, the definitions of the words "fraud" and "fraudulent" were expanded to include "any device, scheme or artifice to defraud and any deception, misrepresentation, concealment, false pretence [sic], false promise or unconscionable contractual provisions." The statute casts a wide net. . . .

Executive Law §63(12) now reads as follows:

> Whenever any person shall engage in repeated fraudulent or illegal acts or otherwise demonstrate persistent fraud or illegality in the carrying on, conducting or transaction of business, the attorney general may apply . . . for an order enjoining the continuance of such business activity or of any fraudulent or illegal acts, directing restitution and damages and, in an appropriate case, cancelling any certificate filed under and by virtue of the provisions of section four hundred forty of the former penal law or section one hundred thirty of the general business law, and the court may award the relief applied for or so much thereof as it may deem proper subject to subdivision eleven of section four of the state finance law.

#### The Financial Marketplace

This Court takes judicial notice that New York State, particularly New York City, is the financial capital of the country and one of the financial capitals of the world. The City's fabled Wall Street is synonymous with capital formation, investing, trading, lending, and borrowing. In a summary judgment Decision and Order dated September 26, 2023, NYSCEF Doc. 1531, the Court addressed the State's judicially recognized interest in an honest marketplace: "In varying

contexts, courts have held that a state has a quasi-sovereign interest in protecting the integrity of the marketplace." People v. Grasso, 11 NY3d 64, 69 at n.4 (2008); People v Coventry First LLC, 52 AD3d 345, 346 (1st Dept 2008) ("the claim pursuant to Executive Law §63(12) constituted proper exercises of the State's regulation of businesses within its borders in the interest of securing an honest marketplace"); People v. Amazon.com, Inc., 550 F Supp 3d 122, 130–31 (SDNY 2021) ("[T]he State's statutory interest under §63(12) encompasses the prevention of either 'fraudulent or illegal' business activities.

Timely and total repayment of loans does not extinguish the harm that false statements inflict on the marketplace. Indeed, the common excuse that "everybody does it" is all the more reason to strive for honesty and transparency and to be vigilant in enforcing the rules. Here, despite the false financial statements, it is undisputed that defendants have made all required payments on time; the next group of lenders to receive bogus statements might not be so lucky. New York means business in combating business fraud.

**Procedural Background**

Office of the Attorney General of the State of New York ("OAG") filed the instant complaint on September 21, 2022. On November 3, 2022, in response to a motion by OAG, this Court found preliminarily that defendants had a propensity to engage in persistent fraud by submitting false and misleading Statements of Financial Condition ("SFCs") on behalf of Donald Trump. Accordingly, the Court granted a preliminary injunction against any further fraud and appointed the Hon. Barbara S. Jones (ret.) as an independent monitor to oversee defendants' financial statements and significant asset transfers. To date, Judge Jones has delivered six reports to this Court. . . .

**The Complaint**

The Complaint asserts seven causes of action. The first cause of action is of a type known as a "stand-alone §63(12) claim." Consistent with the wording of the statute, plaintiff need only prove that defendants used false statements in business. . . .

**Summary Judgment**

On September 26, 2023, this Court granted plaintiff summary judgment only on liability and only on the first cause of action. Simply put, the Court found that plaintiff had capacity and standing to sue; that non-party disclaimers and party "worthless clauses" do not insulate defendants' material misrepresentations; that intent, scienter, and reliance are not elements of a stand-alone §63(12) claim; that disgorgement of profits is an available remedy; and that the subject financial statements materially misrepresented the value of the Trump Tower Triplex, The Seven Springs Estate, certain apartments in Trump Park Avenue, 40 Wall Street, Mar-a-Lago, and a golf course in Aberdeen, Scotland.

**The Trial**

The eleven-week trial of this action addressed whether defendants are liable pursuant to the second through seventh causes of action and what monetary penalties and/or injunctive relief this Court should impose. Plaintiff is seeking "disgorgement" of "ill-gotten gains," and to limit defendants' abilities to conduct business in New York. Constitutional provisions guaranteeing a jury trial, such as the Seventh Amendment to the United States Constitution, apply only to cases "at common law," so-called "legal" cases. The phrase "at common law" is used in contradistinction to cases that are "equitable" in nature. Whether a case is "legal" or "equitable" depends on the relief that plaintiff sought. Here, plaintiff seeks disgorgement and injunctions, each of which are forms of equitable relief. Thus, there was no right to a jury, and the case was "tried to the Court;" the Court being the sole factfinder and the sole "judge of credibility." This Court listened carefully to every witness, every question, every answer. Witnesses testified from the

witness stand, approximately a yard from the Court, who was thus able to observe expressions, demeanor, and body language. The Court has also considered the simple touchstones of self-interest and other motives, common sense, and overall veracity.

## Findings of Fact

This Court heard testimony from 40 witnesses over 43 days and makes the following findings of fact:

### The Non-Party Witnesses

[The Court then reviewed the lengthy list of fact witnesses and experts.]

## Conclusions of Law

### Burden of Proof

An action brought by the Attorney General seeking equitable relief for repeated or ongoing fraud in conducting business is subject to a "preponderance of the evidence" standard, as is customary in civil litigation. Moreover, defendants have provided no legal authority for their contention that the higher "clear and convincing" standard does, or should, apply.

### Defenses Asserted

#### Reliance

Defendants have argued vociferously throughout the trial that there can be no fraud as, they assert, that none of the banks or insurance companies relied on any of the alleged misrepresentations. The proponents of this theory posit that lenders demand complex statements of financial condition but then ignore them.

Defendants' argument is to no avail, as none of plaintiff's causes of action requires that it demonstrate reliance. Instead, plaintiff must merely show that defendants *intended* to commit the fraud. Reliance is not a requisite element of either Executive Law §63(12) or of any of the alleged Penal Law violations.

However, the Court notes that, although not required, there is ample documentary and testimonial evidence that the banks, insurance companies, and the City of New York did, in fact, rely on defendants to be truthful and accurate in their financial submissions. The testimony in this case makes abundantly clear that most, if not all, loans began life based on numbers on an SFC, which the lenders interpreted in their own unique way. The testimony confirmed, rather than refuted, the overriding importance of SFCs in lending decisions.

#### Blame the Accountants

The crux of the defense at trial was that defendants relied on their accountants, mainly Mazars, but sometimes Whitley Penn, to make sure that the SFCs were accurate, and that responsibility for any misrepresentations lies with the accountants, not defendants. Donald Trump, Jr. and Eric Trump testified several times that they would have relied on their accountants to find any errors in the SFCs' supporting data.

This defense is wholly undercut by the overwhelming evidence adduced at trial demonstrating that Mazars and Whitley Penn relied on the Trump Organization, not vice versa, to be truthful and accurate, and they had a right to do so.

#### Materiality

In its summary judgment decision, this Court already found that the SFCs from 2014-2021 were false by material amounts as a matter of law.

Indeed, materiality under this statute is judged not by reference to reliance by or materiality to a particular victim, but rather on whether the financial statement "properly reflected the financial condition" of the person to which the statement pertains. People v. Essner, 124 Misc 2d 830, 835 (Sup Ct, NY County 1984) ("there need be no 'victim,' ergo, reliance is neither an element of the crime nor a valid yardstick with which to test the materiality of a false statement").

Materiality has been one of the great red herrings of this case all along. Faced with clear evidence of a misstatement, a person can always shout that "it's immaterial." Absolute perfection, including with numbers, exists only in heaven. If fraud is insignificant, then, like most things in life, it just does not matter. As an ancient maxim has it, *de minimis non curat lex*, the law is not concerned with trifles. Neither is this Court.

But that is not what we have here. Whether viewed in relative (percentage) or absolute (numerical) terms, objectively (the governing standard) or subjectively (how the lenders viewed them), defendants' misstatements were material. . . . The frauds found here leap off the page and shock the conscience.

#### Different Appraisers, Different Appraisals

Yet another great red herring in this case has been that different appraisers can legitimately and in good faith appraise the same property at different amounts. True enough, as appraising is an art as well as a science. However, the science part cannot be fraudulent. When two appraisals rely on starkly different assumptions, that is not evidence of a difference of opinion, that is evidence of deceit.

Donald Trump was aware of many of the key facts underpinning various material fraudulent misstatements in the SFCs: he was aware of having deeded away the right to use Mar-a-Lago as anything other than a social club, and notwithstanding, continued to value it as if it could be used as a single family residence; he was aware that the Triplex apartment in which he, a real estate mogul and self-identified expert, resided for decades was not 30,000 square feet, but actually 10,996 square feet; he was aware that he did not control the Vornado partnership interest even though he represented it as "cash"; he was aware that he had permission to build only 500 private residences in Aberdeen, notwithstanding that he represented that he had permission for 2500; and he was aware that 40 Wall Street was operating at a deficit despite proclaiming that it was running a net operating income of $64 million. . . .

### Disgorgement of Ill-Gotten Gains

> [W]here, as here, there is a claim based on fraudulent activity, disgorgement may be available as an equitable remedy, notwithstanding the absence of loss to individuals or independent claims for restitution. Disgorgement is distinct from the remedy of restitution because it focuses on the gain to the wrongdoer as opposed to the loss to the victim. Thus, disgorgement aims to deter wrongdoing by preventing the wrongdoer from retaining ill-gotten gains from fraudulent conduct. Accordingly, the remedy of disgorgement does not require a showing or allegation of direct losses to consumers or the public; the source of the ill-gotten gains is "immaterial."

People v. Ernst & Young, LLP, 114 AD3d 569 (1st Dept 2014) (disgorgement is not impermissible penalty "since the wrongdoer who is deprived of an illicit gain is ideally left in the position he would have been had there been no misconduct") (internal citations omitted); *see also* People v Amazon.com, Inc., 550 F Supp 3d 122, 130 (SDNY 2021) ("Executive Law §63(12) authorizes the Attorney General to seek injunctive and other relief," and finding "the Attorney General can seek disgorgement of profits on the State's behalf"). Indeed, the last sentence of Executive Law §63(12) clearly contemplates disgorgement ("all monies recovered or obtained under this subdivision").

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### The Personal Guarantee Interest Rate Differential

Plaintiff's expert, Michiel McCarty, testified reliably and convincingly that defendants profited by paying lower interest rates on loans from Deutsche Bank's Private Wealth Management Division, based on fraudulent SFCs, than the interest rates they would have paid under non-recourse loans simultaneously offered to them.

In total, defendants' fraud saved them approximately $168,040,168 in interest, which shall be imposed, jointly and severally, among Donald Trump and the defendant entities that he owns and controls, as the misconduct at issue was committed by the Trump Organization's top management.

### Pre-Judgment Interest

Public policy favors awarding interest in equity actions.

Weighing these public policy considerations, the Court directs that pre-judgment interest, per CPLR 5004(a), shall run from the following dates, [the date the Attorney General commenced its investigation, for all disgorgement of ill-gotten interest from all projects] . . .

## Injunctive Relief

An Attorney General who has demonstrated "repeated illegal or fraudulent acts" may obtain injunctive relief pursuant to Executive Law §63(12). State v. Princess Prestige Co., 42 NY2d 104, 106 (1977); People v. Gen. Elec. Co., 302 AD2d 314, 315 (1st Dept 2003).

When determining whether injunctive relief is appropriate, courts are instructed to consider the following facts:

> [T]he fact that the defendant has been found liable for illegal conduct; the degree of scienter involved; whether the infraction is an "isolated occurrence"; whether defendant continues to maintain that his past conduct was blameless; and whether, because of his professional occupation, the defendant might be in a position where future violations could be anticipated.

S.E.C. v Cavanagh, 155 F3d 129, 135 (2d Cir 1998). Consideration of each of these factors weighs heavily towards granting injunctive relief.

### Necessity of Ongoing Oversight

### Refusal to Admit Error

The English poet Alexander Pope (1688-1744) first declared, "To err is human, to forgive is divine." Defendants apparently are of a different mind. After some four years of investigation and litigation, the only error ("inadvertent," of course) that they acknowledge is the tripling of the size of the Trump Tower Penthouse, which cannot be gainsaid. Their complete lack of contrition and remorse borders on pathological.

This Court is not constituted to judge morality; it is constituted to find facts and apply the law. In this particular case, in applying the law to the facts, the Court intends to protect the integrity of the financial marketplace and, thus, the public as a whole. Defendants' refusal to admit error — indeed, to continue it, according to the Independent Monitor — constrains this Court to conclude that they will engage in it going forward unless judicially restrained.

### Trump Organization's History of Corporate Malfeasance

[Detailing prior legal actions against the Trump Organization and related individuals and appointing an independent monitor.]

**Prior Cancellation of Business Licenses**

In its September 26, 2023, Decision and Order granting partial summary judgment to OAG, this Court ordered the cancellation of defendants' business licenses. The Appellate Division, First Department has stayed this relief pending the final disposition on appeal.

However, as going forward there will be two-tiered oversight, an Independent Monitor and an Independent Director of Compliance, of the major activities that could lead to fraud, cancellation of the business licenses is no longer necessary. Accordingly, this Court hereby modifies its September 26, 2023, Decision and Order solely to the extent of removing the language ordering the LLCs cancellation en masse.

**Industry Bans**

The Attorney General asks, and the Court has the authority, temporarily or permanently, to enjoin certain defendants from participating in certain business activities as a result of their persistent fraud.

The Court hereby enjoins Donald Trump . . . from serving as an officer or director of any New York corporation or other legal entity in New York for a period of three years.

The Court hereby enjoins Donald Trump and the Trump Organization and its affiliates from applying for loans from any financial institution chartered by or registered with the New York State Department of Financial Services for a period of three years.

## NOTE

***Reliance and Inaction.*** Executive Law §63(12) is only one of several statutes that removes the need of the New York State Attorney General to prove reliance on fraud in order to sue for damages or disgorgement from individuals or businesses that engage in fraud. In 1921, New York State adopted the Martin Act, N.Y. Gen. Bus. §§352-c, 353 to counteract the widespread fraud. In New York v. Federated Radio Corp., 154 NE 655, 657 (N.Y. 1926), the defendant had made wrongful representations to the public at large, when it was not possible to track down the people to whom the false statements were made. To stop this petty abuse, Pound, J., held:

> The words "fraud" and "fraudulent practice," in this connection, should therefore be given a wide meaning, so as to include all acts, although not originating in any actual evil design or contrivance to perpetrate fraud or injury upon others, which do by their tendency to deceive or mislead the purchasing public come within the purpose of the law.

Under this view, proof of reliance by any individual was regarded as an obstacle to deal with street fraud, with little reason to think that legitimate brokers and sellers would be caught by the Act. For a general history of the Martin Act, see Richard A. Epstein, Regulatory Enforcement Under New York's Martin Act: From Financial Fraud to Global Warming, 14 N.Y.U. J.L. & Bus. 805 (2018).

Note the contrast with the Trump case. Engoron, J., ordered Trump to pay $364 million in damages and interest in compensating for fraud he committed by inflating his net worth to obtain favorable treatment from banks and insurers, for which he ordered disgorgement. Typical of the case on which he relied was New York v. Interstate Traffic, 321 N.Y.S. 147 (1971), where then-Attorney General Louis Lefkowitz sued Interstate for its false representations to prospective students, stating that by passing an examination exam they could immediately get jobs in an expanding construction industry paying $6.60 per hour. He attached affidavits from some fifty-three graduates who recounted their failures and proved that only fourteen graduates of a class of 179 got jobs, and only for lower wages. In this case individual actions are costly and ineffective, and the element of reliance stands out from the evidence.

In contrast, as Engoron noted, Deutsche Bank made millions from these transactions with no default. Should the presumption that the bank relied on Trump's reputation follow when the bank did its own due diligence?

## SECTION C. NEGLIGENT MISREPRESENTATION

### *Ultramares Corp. v. Touche*

174 N.E. 441 (N.Y. 1931)

Cardozo, C.J. The action is in tort for damages suffered through the misrepresentations of accountants, the first cause of action being for misrepresentations that were merely negligent and the second for misrepresentations charged to have been fraudulent.

In January, 1924, the defendants, a firm of public accountants, were employed by Fred Stern & Co., Inc., to prepare and certify a balance sheet exhibiting the condition of its business as of December 31, 1923. They had been employed at the end of each of the three years preceding to render a like service. Fred Stern & Co., Inc., which was in substance Stern himself, was engaged in the importation and sale of rubber. To finance its operations, it required extensive credit and borrowed large sums of money from banks and other lenders. All this was known to the defendants. The defendants knew also that in the usual course of business the balance sheet when certified would be exhibited by the Stern Company to banks, creditors, stockholders, purchasers, or sellers, according to the needs of the occasion, as the basis of financial dealings. Accordingly, when the balance sheet was made up, the defendants supplied the Stern company with thirty-two copies certified with serial numbers as counterpart originals. Nothing was said as to the persons to whom these counterparts would be shown or the extent or number of the transactions in which they would be used. In particular there was no mention of the plaintiff, a corporation doing business chiefly as a factor, which till then had never made advances to the Stern Company, though it had sold it merchandise in small amounts. The range of the transactions in which a certificate of audit might be expected to play a part was as indefinite and wide as the possibilities of the business that was mirrored in the summary.

By February 26, 1924, the audit was finished and the balance sheet made up. It stated assets in the sum of $2,550,671.88 and liabilities other than capital and surplus in the sum of $1,479,956.62, thus showing a net worth of $1,070,715.26. Attached to the balance sheet was a certificate as follows:

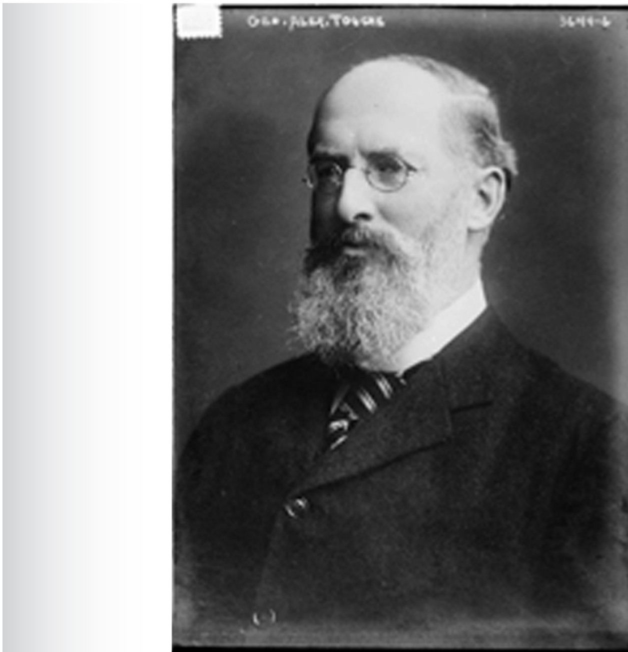
TOUCHE, NIVEN & CO.
Public Accountants
Eighty Maiden Lane
New York

February 26, 1924

Certificate of Auditors

We have examined the accounts of Fred Stern & Co., Inc., for the year ending December 31, 1923, and hereby certify that the annexed balance sheet is in accordance therewith and with the information and explanations given us. We further certify that, subject to provision for federal taxes on income, the said statement, in our opinion, presents a true and correct view of the financial condition of Fred Stern & Co., Inc., as at December 31, 1923.

*Touche, Niven & Co.*
Public Accountants



**Sir George Alexander Touche, one of the founders of Touche, Niven & Co., which is now a major consulting firm known as Deloitte.**

*Source: Wikimedia Commons*

[Cardozo, C.J., noted that the accountant's statement was wrong in all material respects. Stern & Co. was in fact insolvent at the time the balance sheet was prepared, and the defendant auditors had been taken in by false statements of income and expenses prepared by Stern's officers. After an extensive review of the evidence, Cardozo, C.J., concluded that a skilled auditor would have followed up on various leads and detected the fraud perpetrated by Stern & Co.'s chief officers. On the faith of the balance sheet certified by the defendant, the plaintiff, as part of its factoring business, advanced various sums to Stern & Co. throughout most of 1924. Stern & Co. collapsed in January 1925, leaving the plaintiff with a host of unpaid loans, both unsecured and inadequately secured. In November 1926, the plaintiffs sued the defendants for both negligence and fraud. The trial judge refused to allow the fraud count to go to the jury. The jury, however, found the defendant negligent and awarded the plaintiff some $187,500. The trial judge, who had reserved judgment on the sufficiency of the negligence claim, entered a judgment for the defendant on the ground that the plaintiff's claim for negligent misrepresentation did not state a cause of action. That decision was reversed by the appellate division. Cardozo, C.J., noted that the finding of negligence was supported by the evidence. "The reckoning was not wrong upon the evidence before us, if duty be assumed."]

We are brought to the question of duty, its origin and measure.

The defendants owed to their employer a duty imposed by law to make their certificate without fraud, and a duty growing out of contract to make it with the care and caution proper to their calling. Fraud includes the pretense of knowledge when knowledge there is none. To creditors and investors to whom the employer exhibited the certificate, the defendants owed a like duty to make it without fraud, since there was notice in the circumstances of its making that the employer did not intend to keep it to himself. A different question develops when we ask whether they owed a duty to these to make it without negligence. If liability for negligence exists, a thoughtless slip or blunder, the failure to detect a theft or forgery beneath the cover of deceptive entries, may expose accountants to a liability in an indeterminate amount for an indeterminate time to an indeterminate class. The hazards of a business conducted on these terms are so extreme as to enkindle doubt whether a flaw may not exist in the implication of a duty that exposes to these consequences. We put aside for the moment any statement in the certificate which involves the representation of a fact as true to the knowledge of the auditors. If such a statement was made, whether believed to be true or not, the defendants are liable for deceit in the event that it was false. The plaintiff does not need the invention of novel doctrine to help it out in such conditions. The case was submitted to the jury and the verdict was returned upon the theory that even in the absence of a misstatement of a fact there is a liability also for erroneous opinion. The expression of an opinion is to be subject to a warranty

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implied by law. What, then, is the warranty, as yet unformulated, to be? Is it merely that the opinion is honestly conceived and that the preliminary inquiry has been honestly pursued, that a halt has not been made without a genuine belief that the search has been reasonably adequate to bring disclosure of the truth? Or does it go farther and involve the assumption of a liability for any blunder or inattention that could fairly be spoken of as negligence if the controversy were one between accountant and employer for breach of a contract to render services for pay?

The assault upon the citadel of privity is proceeding in these days apace. How far the inroads shall extend is now a favorite subject of juridical discussion. . . . In the field of the law of contract there has been a gradual widening of the doctrine of Lawrence v. Fox (20 N.Y. 268 (1859)), until today the beneficiary of a promise, clearly designated as such, is seldom left without a remedy (Seaver v. Ransom[, 120 N.E. 639 (N.Y. 1918)]). Even in that field, however, the remedy is narrower where the beneficiaries of the promise are indeterminate or general. Something more must then appear than an intention that the promise shall redound to the benefit of the public or to that of a class of indefinite extension. The promise must be such as to "bespeak the assumption of a duty to make reparation directly to the individual members of the public if the benefit is lost" (Moch Co. v. Rensselaer Water Co [159 N.E. 896 (N.Y. 1928)]). In the field of the law of torts a manufacturer who is negligent in the manufacture of a chattel in circumstances pointing to an unreasonable risk of serious bodily harm to those using it thereafter may be liable for negligence though privity is lacking between manufacturer and user (MacPherson v. Buick Motor Co., 217 N.Y. 382 (1916); American Law Institute, Restatement of the Law of Torts, §262). A force or instrument of harm having been launched with potentialities of danger manifest to the eye of prudence, the one who launches it is under a duty to keep it within bounds (*Moch*). Even so, the question is still open whether the potentialities of danger that will charge with liability are confined to harm to the person, or include injury to property. In either view, however, what is released or set in motion is a physical force. We are now asked to say that a like liability attaches to the circulation of a thought or a release of the explosive power resident in words.

Three cases in this court are said by the plaintiff to have committed us to the doctrine that words, written or oral, if negligently published with the expectation that the reader or listener will transmit them to another, will lay a basis for liability though privity be lacking. These are Glanzer v. Shepard (233 N.Y. 236 (1922)); International Products Co. v. Erie R.R. Co.[, 155 N.E. 662 (N.Y. 1927)], and Doyle v. Chatham & Phenix Nat. Bank[, 171 N.E. 574 (N.Y. 1930)].

In Glanzer v. Shepard the seller of beans requested the defendants, public weighers, to make return of the weight and furnish the buyer with a copy. This the defendants did. Their return, which was made out in duplicate, one copy to the seller and the other to the buyer, recites that it was made by order of the former for the use of the latter. The buyer paid the seller on the faith of the certificate which turned out to be erroneous. We held that the weighers were liable at the suit of the buyer for the moneys overpaid. Here was something more than the rendition of a service in the expectation that the one who ordered the certificate would use it thereafter in the operations of his business as occasion might require. Here was a case where the transmission of the certificate to another was not merely one possibility among many, but the "end and aim of the transaction," as certain and immediate and deliberately willed as if a husband were to order a gown to be delivered to his wife, or a telegraph company, contracting with the sender of a message, were to telegraph it wrongly to the damage of the person expected to receive it. The intimacy of the resulting nexus is attested by the fact that after stating the case in terms of legal duty, we went on to point out that viewing it as a phase or extension of Lawrence v. Fox, or Seaver v. Ransom, we could reach the same result by stating it in terms of contract. The bond was so close as to approach that of privity, if not

completely one with it. Not so in the case at hand. No one would be likely to urge that there was a contractual relation, or even one approaching it, at the root of any duty that was owing from the defendants now before us to the indeterminate class of persons who, presently or in the future, might deal with the Stern company in reliance on the audit. In a word, the service rendered by the defendant in Glanzer v. Shepard was primarily for the information of a third person, in effect, if not in name, a party to the contract, and only incidentally for that of the formal promisee. In the case at hand, the service was primarily for the benefit of the Stern company, a convenient instrumentality for use in the development of the business, and only incidentally or collaterally for the use of those to whom Stern and his associates might exhibit it thereafter. Foresight of these possibilities may charge with liability for fraud. The conclusion does not follow that it will charge with liability for negligence.

[A discussion of International Products Co. v. Erie Railroad Co. and Doyle v. Chatham & Phenix National Bank is omitted.]

From the foregoing analysis the conclusion is, we think, inevitable that nothing in our previous decisions commits us to a holding of liability for negligence in the circumstances of the case at hand, and that such liability, if recognized, will be an extension of the principle of those decisions to different conditions, even if more or less analogous. The question then is whether such an extension shall be made.

The extension, if made, will so expand the field of liability for negligent speech as to make it nearly, if not quite, coterminous with that of liability for fraud. Again and again, in decisions of this court, the bounds of this latter liability have been set up, with futility the fate of every endeavor to dislodge them. Scienter has been declared to be an indispensable element except where the representation has been put forward as true of one's own knowledge, or in circumstances where the expression of opinion was a dishonorable pretense. . . . Even an opinion, especially an opinion by an expert, may be found to be fraudulent if the grounds supporting it are so flimsy as to lead to the conclusion that there was no genuine belief back of it. Further than that this court has never gone. Directors of corporations have been acquitted of liability for deceit though they have been lax in investigation and negligent in speech. This has not meant, to be sure, that negligence may not be evidence from which a trier of the facts may draw an inference of fraud (Derry v. Peek, [L.R.] 14 A.C. 337[, *supra* Note 2, at 153]) but merely that if that inference is rejected, or, in the light of all the circumstances, is found to be unreasonable, negligence alone is not a substitute for fraud. . . . A change [from fraud to negligence] so revolutionary, if expedient, must be wrought by legislation. . . .

Liability for negligence if adjudged in this case will extend to many callings other than an auditor's. Lawyers who certify their opinion as to the validity of municipal or corporate bonds with knowledge that the opinion will be brought to the notice of the public, will become liable to the investors, if they have overlooked a statute or a decision, to the same extent as if the controversy were one between client and adviser. Title companies insuring titles to a tract of land, with knowledge that at an approaching auction the fact that they have insured will be stated to the bidders, will become liable to purchasers who may wish the benefit of a policy without payment of a premium. These illustrations may seem to be extreme, but they go little, if any, farther than we are invited to go now. Negligence, moreover, will have one standard when viewed in relation to the employer, and another and at times a stricter standard when viewed in relation to the public. Explanations that might seem plausible, omissions that might be reasonable, if the duty is confined to the employer, conducting a business that presumably at least is not a fraud upon his creditors, might wear another aspect if an independent duty to be suspicious even of one's principal is owing to investors. "Every one making a promise having the quality of a contract will be under a duty to the promisee by virtue of the promise, but under another duty, apart from contract, to an indefinite number of potential beneficiaries when performance has begun. The assumption of one relation will mean the involuntary

assumption of a series of new relations, inescapably hooked together." (*Moch*.) "The law does not spread its protection so far." (Robins Dry Dock & Repair Co. v. Flint, 275 U.S. 303 (1927)[, *supra* Chapter 1, at 21]).

Our holding does not emancipate accountants from the consequences of fraud. It does not relieve them if their audit has been so negligent as to justify a finding that they had no genuine belief in its adequacy, for this again is fraud. It does no more than say that if less than this is proved, if there has been neither reckless misstatement nor insincere profession of an opinion, but only honest blunder, the ensuing liability for negligence is one that is bounded by the contract, and is to be enforced between the parties by whom the contract has been made. We doubt whether the average business man receiving a certificate without paying for it and receiving it merely as one among a multitude of possible investors, would look for anything more.

(2) The second cause of action is yet to be considered.

The defendants certified as a fact, true to their own knowledge, that the balance sheet was in accordance with the books of account. If their statement was false, they are not to be exonerated because they believed it to be true. We think the triers of the facts might hold it to be false.

[The court reviewed the evidence on the second cause of action and noted that accountants are to be judged by a strict standard of construction "when certifying to an agreement between the audit and the entries" as the defendants did here. The court also concluded that the defendants could not protect themselves against a charge that they did not detect the fictitious invoices "by invoking a practice known as that of testing and sampling," on the ground that it was "plainly insufficient" to determine whether there were in fact any accounts at all. The court concluded that the defendants could not escape liability because they had "delegated the performance of this work to agents of their own selection."

Plaintiff's first cause of action was dismissed; a new trial was granted on plaintiff's second cause of action.]

## NOTES

**1. *Liability for Negligent Misrepresentation.*** *Ultramares* is still the leading U.S. common law decision on liability for negligent misrepresentation. Does its invocation of the privity limitation make more sense here than it does in the products liability cases? The waterworks cases? If the defendants had been told to mail a copy of their certified statement directly to the plaintiff for use in its lending operations, could the plaintiff have recovered in negligence? Does *Ultramares* imply that only third parties who pay for the preparation of the report can sue for its negligent preparation? Could the plaintiff recover under a third-party beneficiary theory? Could the accountant limit liability for negligence by contract? For fraud?

In New York, *Ultramares* was extensively reexamined in White v. Guarente, 372 N.E.2d 315, 318–19 (N.Y. 1977). There the court held that the plaintiff, a limited partnership specializing in trading and hedging marketable securities, stated a negligent misrepresentation cause of action against the defendant Arthur Andersen & Co. The partnership had retained the accounting firm to audit the activities of its general partners who had improperly withdrawn their own funds from the firm. Andersen negligently missed these withdrawals. Unlike the situation in *Ultramares*, the suit did not expose Andersen to liability to "the extensive and indeterminable investing public-at-large," but "rather to a known group possessed of vested rights, marked by a definable limit and made up of certain components." Andersen "must have been aware that a limited partner would necessarily rely on or make use of the audit and tax returns

of the partnership, or at least constituents of them, in order to properly prepare his or her own tax returns." Were the limited partners in privity with the defendants, because the partnership hired the defendants to do the audit? In Credit Alliance Corp. v. Arthur Andersen & Co., 483 N.E.2d 110 (N.Y. 1985), Jasen, J., reiterated that liability for negligent misrepresentation under *Ultramares* depended on whether the defendants supplied the report for a particular purpose to "a known party or parties" of whom the defendants were aware, but relaxed the strict *Ultramares* privity requirement to extend to relationships "sufficiently approaching privity." Accord Frio Energy Partners, LLC v. Fin. Tech. Leverage, LLC, 680 F. Supp. 3d 322, 348–49 (S.D.N.Y. 2023).

The Second Restatement of Torts §552 limits liability for negligent misrepresentation to, at most, individuals who are members "of a limited group of persons for whose benefit and guidance" the information is supplied, provided that there is reliance on that information in that transaction, or "in a substantially similar transaction." RTT: LEH §5 adopts this position with small changes. The Second Restatement position has been adopted in numerous recent cases, including Ellis v. Grant Thornton LLP, 530 F.3d 280, 285, 292 (4th Cir. 2008), in which the plaintiff, the president of a bank, sued an accounting firm retained by the bank for negligent misrepresentations (both oral and made in the audit report) concerning the financial condition of the bank. The plaintiff alleged that he relied on defendant's representations of the bank's solid financial condition in deciding to accept employment as bank president. The audit report plainly stated: "This report is intended for the information and use of the [bank] and its regulatory agencies and should not be used by third parties for any other purpose." Reversing the district court's award of nearly $2.5 million in damages following a bench trial on the negligent misrepresentation claim, Hamilton, J., held that plaintiff had not satisfied the elements of RST §552 given that the accounting firm "was not aware . . . that its audit was being performed for the benefit of potential employees of [the bank]." And further: "A person as sophisticated and experienced in the banking business as [plaintiff] is, he knew he could not justifiably rely on [the accountant's] statements when the report itself stated otherwise."

**2. *From Privity to Foreseeability and Back.*** The narrow liability rule in *Ultramares* received a chillier reception in H. Rosenblum, Inc. v. Adler, 461 A.2d 138, 145, 149, 153 (N.J. 1983). There the defendant accounting firm, Touche Ross & Co., was sued for negligent misrepresentation for failing to ferret out the fraud that Giant Stores Corporation had perpetrated against the plaintiffs, who, under a merger agreement, accepted worthless Giant stock in exchange for shares of their own private corporations. The trial judge dismissed the negligent misrepresentation claim against Touche Ross & Co., but the New Jersey Supreme Court remanded the case for trial. Schreiber, J., first noted the tension between Cardozo's opinions in *MacPherson* and *Ultramares*, and then insisted that privity should not be a barrier to misrepresentation claims any more than claims arising from physical injury. Relying on RST §552, Schreiber, J., concluded: "Generally, within the outer limits fixed by the court as a matter of law, the reasonably foreseeable consequences of the negligent act define the duty and should be actionable."

Reasoning that the "auditor's function has expanded from that of a watchdog for management to an independent evaluator of the adequacy and fairness of financial statements issued by management to stockholders, creditors, and others," Schreiber, J., continued:

> When the independent auditor furnishes an opinion with no limitation in the certificate as to whom the company may disseminate the financial statements, he has a duty to all those whom that auditor should reasonably foresee as recipients from the company of the statements for its proper business purposes, provided that the recipients rely on the statements pursuant to those business purposes. The principle that we have adopted applies by its terms only to those foreseeable users who receive the audited statements from the business entity for a proper business

> purpose to influence a business decision of the user, the audit having been made for that business entity. Thus, for example, an institutional investor or portfolio manager who does not obtain audited statements from the company would not come within the stated principle. Nor would stockholders who purchased the stock after a negligent audit be covered in the absence of demonstrating the necessary conditions precedent. Those and similar cases beyond the stated rule are not before us and we express no opinion with respect to such situations.

These expansionist tendencies of accountants' liability were in turn checked, at least in part, in Bily v. Arthur Young & Co., 834 P.2d 745, 767 (Cal. 1992), which rejected the "foreseeability" test of *Rosenblum* on the ground that it could impose "a potential liability far out of proportion to its fault," and held that sophisticated investors could have purchased, if they chose, protection from the auditor by contract. Fearing the contraction of necessary auditing services, the court followed RST §552 and restricted potential liability to a narrow class of persons, who, although not clients, "are specifically intended beneficiaries of the audit report who are known to the auditor and for whose benefit it renders the audit report."

A convenient summary of the various lines of authority is found in *Ellis*, *supra* Note 1. Hamilton, J., noted that four lines of authority had developed to resolve an accountant's liability to third parties for negligent misrepresentation:

> The first of these approaches was announced in [*Ultramares*], which held that negligence actions were only permitted by parties in privity of contract or in a situation so close as to approach that of privity. The second approach was also developed by the New York Court of Appeals, which slightly modified the *Ultramares Corp.* approach in 1985 [in *Credit Alliance*]. The third approach is set forth in §552 of the Restatement (Second) of Torts. Under this approach, a person or limited class of persons who the auditor can foresee as parties who will (and do) rely upon financial statements are allowed to recover. The fourth approach is the reasonably foreseeable approach, which permits all parties who are reasonably foreseeable recipients of financial statements for business purposes to recover as long as they reply on the statements for these business purposes [citing *Rosenblum*].

In the absence of direct dealings—what *Credit Alliance* called "linking conduct" between the auditor and non-client—plaintiffs have had little luck in their suits against accountants. In CRT Investments Ltd. v. BDO Seidman, LLP, 925 N.Y.S.2d 439, 441 (App. Div. 2011), the plaintiffs were investors in a Cayman Island hedge fund who sued their accountants in negligence when their investment turned sour. A short per curiam decision held:

> The complaint fails to plead a factual basis for inferring that BDO Seidman did anything more than perform the routine business of auditing. Where, as here, direct contact between the accountant and the plaintiff is minimal or nonexistent, the plaintiff cannot recover for the accountant's alleged negligence. The fact that plaintiffs were entitled to and received a copy of the audited financial statements, or that BDO Seidman knew that the investors would rely upon the information contained in the financial statements, does not establish the requisite linking conduct. BDO Seidman's work in the course of the audit was performed pursuant to professional standards applicable in the context of any audit, and was not undertaken pursuant to any specific duty owed to plaintiffs. Therefore, plaintiffs cannot establish the direct nexus necessary to give them a claim against BDO Seidman for negligent misrepresentation.

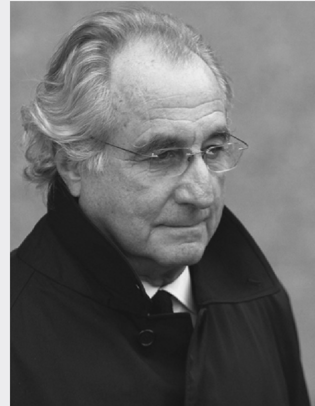
**3.** ***Reliance and Causation in Negligent Misrepresentation Cases.*** *Kaufman, supra* at 189, makes clear that the element of reliance is just as critical for negligent misrepresentation as for fraud cases. See also Cadlo v. Owens-Ill., Inc., 125 Cal. App. 4th 513 (2004) (the reliance element in negligent misrepresentation is the same as in fraud). Likewise, the causation inquiry is equally vexing. In Oregon Steel Mills, Inc. v. Coopers & Lybrand, LLP, 83 P.3d 322, 330 (Or. 2004), the defendant accountants negligently and incorrectly prepared consolidated

financial statements, which delayed the public offering of the plaintiff's shares by two months, from April to June 1996, when the shares sold for $2.50 less per share than they would have on the earlier date. Balmer, J., granted summary judgment to the defendant on the issue of causation. He noted first that these losses in market value were in principle distinguishable from the reputational losses that might have impaired the plaintiff to raise additional funds in capital markets. Instead, he held that interventions by unrelated market forces did not count as "a reasonably foreseeable result of defendant's wrongful conduct." His analysis parallels that for cases of delay in the delivery of nonperishable goods or the receipt of a building permit because of a negligent application. In all of these cases, it is in some sense foreseeable that the value of the plaintiff's project could either go up or down with equal probability. But in the absence of special circumstances (such as the sale of perishable goods), the only systematic loss is the *interest* on the amount receivable attributable to the delay. Stated otherwise, in some cases the delay will work to the *advantage* of the plaintiff by allowing for a later sale in a rising market. So long as securities markets are efficiently priced, the defendant is overpenalized if forced to pay for the downturns in value, so long as the plaintiff is entitled to pocket any (foreseeable) gains from any interim upturn in value. The interest payment leaves the plaintiff indifferent with respect to time, assuming that the additional costs of completing the new issue are borne by the negligent defendant.

**Exhibit 3.1 The Biggest Ponzi Scheme in History**

The judgment in *CRT Investments* was part of the tremendous fallout following the collapse of a $65 billion fraud perpetrated by disgraced financier Bernard L. Madoff. After pleading guilty to orchestrating, as the *New York Times* put it, the "largest, longest, and most widespread Ponzi scheme in history," Chin, J., of the Federal District Court for the Southern District of New York sentenced Madoff to 150 years' imprisonment, the maximum allowable sentence for the crimes to which he pled guilty.

Madoff's victims ranged from modest investors — many of whom lost their life savings — to major financial and cultural institutions. The generous returns they believed they were getting from investing with Madoff evaporated almost overnight once the scheme was exposed.



*Source: Brendan McDermid/Reuters*

**4. *Modern Securities Law and the Indeterminate Class.*** The specter of *Ultramares* haunts modern securities law in which vast potential liability for material nondisclosures, as well as misstatements, is a daily fact of life. Who should be entitled to sue under the securities laws for their financial losses? Section 10(b) of the Securities Exchange Act, *supra* Note 4, at 154, proscribes fraud "in connection with the purchase or sale of securities." In Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723, 747–48 (1975), the plaintiffs alleged that they did not purchase shares of the defendant's stock because the defendants had made false and misleading negative statements about its value. The Supreme Court held that only actual purchasers and sellers of stocks could sue under section 10(b). The Court feared that the plaintiffs' proposed rule would admit an enormous class of potential plaintiffs into court, place heavy

strains on the system of discovery, and require defendants to litigate against plaintiffs whose claims were wholly hypothetical. In explicit reliance on *Ultramares*, the Court concluded:

> [W]hile much of the development of the law of deceit has been the elimination of artificial barriers to recovery on just claims, we are not the first court to express concern that the inexorable broadening of the class of plaintiff who may sue in this area of the law will ultimately result in more harm than good.

*Blue Chip* was followed by the Texas Supreme Court in Grant Thornton LLP v. Prospect High Income Fund, 314 S.W.3d 913, 915, 930 (Tex. 2010), which rejected the view that there is "an obligation on the auditor to provide an accurate accounting not to the corporation or known investor, but to anyone who reads and relies on it," concluding baldly that the only such suits allowed in Texas "must involve a direct communication between the plaintiff and the defendant."

Does this approach in both securities and common law actions answer Lord Devlin's concern that there is no sensible distinction between financial loss and physical injury cases? If both *Ultramares* and Goodwin v. Agassiz are sound law, is there any reason for a special regime of securities fraud law?

**5. *Contracting Out of Liability for Negligent Misrepresentation.*** Should negligent misrepresentation cases even be treated as tort cases? In Hedley, Byrne & Co. Ltd. v. Heller & Partners Ltd., [1964] App. Cas. 465, 526 [H.L. 1963], Hedley, Byrne was a firm of advertising agents that extended over £15,000 of credit to a firm called Easipower. It made this loan only after obtaining a credit report on Easipower from Heller, who allegedly negligently overstated Easipower's creditworthiness. Lord Devlin concluded that in principle it made no difference "whether financial loss is caused through physical injury or whether it is caused directly."

> If irrespective of contract, a doctor negligently advises a patient that he can safely pursue his occupation and he cannot and the patient's health suffers and he loses his livelihood, the patient has a remedy. But if the doctor negligently advises him that he cannot safely pursue his occupation when in fact he can and he loses his livelihood, there is said to be no remedy. Unless, of course, the patient was a private patient and the doctor accepted half a guinea for his trouble: then the patient can recover all. I am bound to say, my Lords, that I think this to be nonsense. . . . It arises, if it is the law, simply out of a refusal to make sense. The line is not drawn on any intelligible principle. It just happens to be the line which those who have been driven from the extreme assertion that negligent statements in the absence of contractual or fiduciary duty give no cause of action have in the course of their retreat so far reached.

Lord Devlin nonetheless ruled for the defendant on the strength of its disclaimer. "A man cannot be said voluntarily to be undertaking a responsibility if at the very moment when he is said to be accepting it he declares that in fact he is not."

Once disclaimers are regarded as effective, what presumption should govern negligence liability in their absence? Victor P. Goldberg, Accountable Accountants: Is Third-Party Liability Necessary?, 17 J. Legal Stud. 295, 300–01 (1988), defended *Ultramares* on the ground that the default rule should be one of no liability:

> If it turned out that it was appropriate that accountants should compensate third parties for their negligence, it would not be very difficult to have them assume the liability by contract rather than by having it imposed by tort. Third parties could receive explicit assurance in the form of a warranty, guarantee, bond, or a similar device. Even without explicit liability, the negligent accounting firm would suffer the consequences of poor performance in the form of a decline in the value of its "brand name." Since it is probably true that accountants are not very good guarantors, I would guess that accountants would rarely agree to compensate third parties. But it is crucial to recognize that it is unnecessary for courts or legislatures to guess. It is sufficient for them to allow the parties to resolve the problem by contract.

For a defense of the expanded liability of accountants, see Howard B. Weiner, Common Law Liability of the Certified Public Accountant for Negligent Misrepresentation, 20 San Diego L. Rev. 233 (1983). See also William Bishop, Negligent Misrepresentation Through Economists' Eyes, 96 Law Q. Rev. 360 (1980).

Some states allow no-reliance clauses only for negligent misrepresentation, but not for intentional fraud. Recall Note 5 following *NIVE*, *supra* at 173. See *In re* Cendant Corp. Secs. Litig., 72 F. Supp. 2d 498, 501–03 (D.N.J. 1999) (contrasting Connecticut common law, which made this distinction, with New York, which did not); Rajarman v. GEICO Indem. Co., No. 23-CV-425-JPS, 2023 U.S. Dist. LEXIS 199081, *28–32 (E.D. Wis. Oct. 31, 2023) (Wisconsin makes this distinction).

**6.** ***The Economic Loss Rule.*** Does the economic loss rule between contracting parties bar claims for negligent misrepresentation? In Van Sickle Construction Co. v. Wachovia Commercial Mortgage, Inc., 783 N.W.2d 684 (Iowa 2010), the Iowa Supreme Court held that that the economic loss rule does not bar claims for negligent misrepresentation, despite (or rather because of) its nature as an inherently economic injury:

> A review of the purposes of the economic loss doctrine and the situations in which it has been applied convinces us that it provides no bar to the recovery of economic losses caused by a negligent misrepresentation. . . .
>
> The economic loss doctrine was conceived to prevent litigants with contract claims from litigating them inappropriately as tort claims. We see no reason to apply the rule to bar a recovery of economic losses for the tort of negligent misrepresentation that is, and always has been, an economic tort allowing for recovery of purely economic damages. Restatement (Second) of Torts §552B, at 140. Application of the economic loss doctrine in negligent misrepresentation cases would essentially eliminate the tort.

But the Restatement stakes out a contrary position:

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§5. Negligent Misrepresentation**

(5) This Section does not recognize liability for negligent misrepresentations made in the course of negotiating or performing a contract between the parties.

# CHAPTER 4

# ECONOMIC HARMS

## SECTION A. INTRODUCTION

This chapter continues to explore when and how tort law protects economic interests from interference by third parties. Chapter 1 began by drawing a distinction between recovery for economic losses in the wake of property damage or bodily injury and pure financial loss. The former is ordinarily available in tort, whether the underlying claim involves negligence, strict liability, or an intentional wrong. In contrast, recovery for purely financial injury is more limited. Chapter 3 demonstrated that economic interests receive explicit protection when the plaintiff seeks a remedy for the pecuniary losses attributable to misrepresentation, so long as various obstacles — what mental state, what kind of causation, and what damages — are overcome.

This chapter extends that analysis by considering three separate instances of economic harms to strangers. Section B examines the extent to which the law protects contractual relationships by supplying a contracting party not only contract remedies against a promisor in breach, but also tort remedies against a third party who has induced, or threatens to induce, that contractual breach. Section C next considers the protection afforded, not to existing contracts, but to potential business relationships with third parties that the defendant has disrupted not only by words but also by the use of force. Plaintiffs in such cases can recover only in tort, if at all, against that third party if the proposed contract was never consummated. Section D offers a glimpse at the common law protection of intellectual property, including a discussion of the overlap between the common law rules and today's statutory regimes that regulate patents, copyrights, trade secrets, trade names, and trademarks. The common law principles concerning protection of this valuable information are key to understanding the ever-growing and changing statutory regimes.

Courts tread carefully before imposing liability for purely economic harms. Their reluctance stems from two sources: First, as with negligent misrepresentation, courts fear that generalized protection of economic interests against any diminution in value will spawn endless lawsuits and administrative nightmares. The second fear is that the principle of "unfair competition," if incautiously expanded, will destroy ordinary business competition and the social prosperity and innovation it provides. Accordingly, composers, inventors, and authors will expend the energy to create only if they are confident that their creations will be protected from potential infringers, copiers, and outright pirates. With tangible property, a clear prohibition against trespass can do much to protect the fruits of individual labor. But with intellectual property, that simple device of physical exclusion is not available, so a more complex legal regime is required. Courts must balance these conflicting goals. Their task is made all the more challenging by the inherent complexities of the creative processes and the expanded possibilities for infringement in our technology-driven age. In this arena, common law remedies often fall short, and labor, antitrust, patent, copyright, trade name, and trademark statutes assume ever-greater importance.



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## SECTION B. INDUCEMENT OF BREACH OF CONTRACT

**Exhibit 4.1 Edward III and the Pestilence**

The Statute of Labourers was enacted in the wake of the Black Plague of 1348-1349. Most likely caused by a potent bubonic plague carried by infected fleas traveling on rats via Asian trade routes, the Black Plague devastated England. It is estimated that the initial spread of infection, plus periodic outbreaks over the next 30 years, decreased the population of England by 30 to 50 percent. Given the minimal contemporaneous understanding of contagion and pathology, many sincerely believed the world was coming to an end. The desolation created an urgent need to replace deceased workers, particularly crop harvesters. Early orders of Edward III mandating work at pre-plague wages made way for Parliament to pass the Statute of Labourers, an unprecedented foray by the government into the realm of labor and employment.

*Information source: Ormrod, Edward III 357–62 (2011)*
*Image source: The British Library*

### THE STATUTE OF LABOURERS (1351)

**3 Ed. III 1351**

. . . Because a great part of the people and especially of the, workmen and servants has now died in that pestilence [the Black Plague], some, seeing the straights of the masters and the scarcity of servants, are not willing to serve unless they receive excessive wages, and others, rather than through labour to gain their living, prefer to beg in idleness: We . . . have seen fit to ordain: that every man and woman of our kingdom of England, of whatever condition, whether bond or free, who is able bodied and below the age of sixty years, not living from trade nor carrying on a fixed craft, nor having of his own the means of living, or land of his own with regard to the cultivation of which he might occupy himself, and not serving another, if he, considering his station, be sought after to serve in a suitable service, he shall be bound to serve him who has seen fit so to seek after him; and he shall take only the wages liveries, meed or salary which, in the places where he sought to serve, were accustomed to be paid in the twentieth year of our reign of England, or the five or six common years next preceding. Provided, that in thus retaining their service, the lords are preferred before others of their bondsmen or their land tenants. . . .

And if a reaper or mower, or other workman or servant, of whatever standing or condition he be, who is retained in the service of any one, do depart from the said service before the end of the term agreed, without permission or reasonable cause, he shall undergo the penalty of imprisonment, and let no one, under the same penalty, presume to receive or retain such a one in his service.

## *Lumley v. Gye*

118 Eng. Rep. 749 (K.B. 1853)

The 1st count of the declaration stated that plaintiff was lessee and manager of the Queen's Theatre, for performing operas for gain to him; and that he had contracted and agreed with Johanna Wagner to perform in the theatre for a certain time, with a condition, amongst others, that she should not sing nor use her talents elsewhere during the term without plaintiff's consent in writing: Yet defendant, knowing the premises, and maliciously intending to injure plaintiff as lessee and manager of the theatre, whilst the agreement with Wagner was in force, and before the expiration of the term, enticed and procured Wagner to refuse to perform: by means of which enticement and procurement of defendant, Wagner wrongfully refused to perform, and did not perform during the term.

**Exhibit 4.2 Johanna Wagner**
Johanna Wagner (1828-1894) was a great mezzo-soprano and a niece of the composer Richard Wagner. The dispute in Lumley v. Gye arose at the height of her fame. In the companion case of Lumley v. Wagner, Ms. Wagner (Notes 1, 6) was enjoined from singing for the defendant but not ordered to sing for the plaintiff. In the aftermath of the dispute, Ms. Wagner returned home without singing for either company. But in 1856 she returned to England to sing for Lumley, and was regarded so highly that Queen Victoria, departing from her usual rule, went to the opera house to hear her sing. After her singing career ended, she became a noted voice instructor.

*Source: The Print Collector/Getty Images*

Count 2, for enticing and procuring Johanna Wagner to continue to refuse to perform during the term, after the order of Vice Chancellor Parker, affirmed by Lord St. Leonards, restraining her from performing at a theatre of defendants.

Count 3. That Johanna Wagner had been and was hired by plaintiff to sing and perform at his theatre for a certain time, as the dramatic artiste of plaintiff, for reward to her, and had become and was such dramatic artiste of plaintiff at his theatre: Yet defendant, well knowing &c., maliciously enticed and procured her, then being such dramatic artiste, to depart from the said employment.

In each count special damage was alleged. . . .

Crompton, J. . . . It was said, in support of the demurrer, that it did not appear in the declaration that the relation of master and servant ever subsisted between the plaintiff and Miss Wagner; that Miss Wagner was not averred, especially in the two first counts, to have entered upon the service of the plaintiff; and that the engagement of a theatrical performer, even if the performer has entered upon the duties, is not of such a nature as to make the performer a servant, within the rule of law which gives an action to the master for the wrongful enticing away of his servant. And it was laid down broadly, as a general proposition of law, that no action will lie for procuring a person to break a contract, although such procuring is with a malicious intention and causes great and immediate injury. And the law as to enticing servants was said to be contrary to the general rule and principle of law, and to be anomalous, and probably to

have had its origin from the state of society when serfdom existed, and to be founded upon, or upon the equity of, the Statute of Labourers[, 25 Ed. 3 (1349)]. It was said that it would be dangerous to hold that an action was maintainable for persuading a third party to break a contract, unless some boundary or limits could be pointed out; and that the remedy for enticing away servants was confined to cases where the relation of master and servant, in a strict sense, subsisted between the parties; and that, in all other cases of contract, the only remedy was against the party breaking the contract.

Whatever may have been the origin or foundation of the law as to enticing of servants, and whether it be, as contended by the plaintiff, an instance and branch of a wider rule, or whether it be, as contended by the defendant, an anomaly and an exception from the general rule of law on such subjects, it must now be considered clear law that a person who wrongfully and maliciously, or, which is the same thing, with notice, interrupts the relation subsisting between master and servant by procuring the servant to depart from the master's service, or by harbouring and keeping him as servant after he has quitted it and during the time stipulated for as the period of service, whereby the master is injured, commits a wrongful act for which he is responsible at law. I think that the rule applies wherever the wrongful interruption operates to prevent the service during the time for which the parties have contracted that the service shall continue: and I think that the relation of master and servant subsists, sufficiently for the purpose of such action, during the time for which there is in existence a binding contract of hiring and service between the parties; and I think that it is a fanciful and technical and unjust distinction to say that the not having actually entered into the service, or that the service not actually continuing, can make any difference. The wrong and injury are surely the same, whether the wrong doer entices away the gardener, who has hired himself for a year, the night before he is to go to his work, or after he has planted the first cabbage on the first morning of his service; and I should be sorry to support a distinction so unjust, and so repugnant to common sense, unless bound to do so by some rule or authority of law plainly shewing that such distinction exists. The proposition of the defendant, that there must be a service actually subsisting, seems to be inconsistent with the authorities that shew these actions to be maintainable for receiving or harbouring servants after they have left the actual service of the master. . . .

[Crompton, J., then reviewed earlier cases.]

. . . It appears to me that Miss Wagner had contracted to do work for the plaintiff within the meaning of this rule; and I think that, where a party has contracted to give his personal services for a certain time to another, the parties are in the relation of employer and employed, or master and servant, within the meaning of this rule. And I see no reason for narrowing such a rule; but I should rather, if necessary, apply such a remedy to a case "new in its instance, but" "not new in the reason and principle of it," that is, to a case where the wrong and damage are strictly analogous to the wrong and damage in a well recognised class of cases. In deciding this case on the narrower ground, I wish by no means to be considered as deciding that the larger ground taken by Mr. Cowling is not tenable, or as saying that in no case except that of master and servant is an action maintainable for *maliciously* inducing another to break a contract to the injury of the person with whom such contract has been made. It does not appear to me to be a sound answer, to say that the act in such cases is the act of the party who breaks the contract; for that reason would apply in the acknowledged case of master and servant. Nor is it an answer, to say that there is a remedy against the contractor, and that the party relies on the contract; for, besides that reason also applying to the case of master and servant, the action on the contract and the action against the malicious wrong-doer may be for a different matter; and the damages occasioned by such malicious injury might be calculated on a very different principle from the amount of the debt which might be the only sum recoverable on the contract. Suppose a trader, *with a malicious intent to ruin a rival trader*, goes to a banker or

other party who owes money to his rival, and begs him not to pay the money which he owes him, and by that means ruins or greatly prejudices the party: I am by no means prepared to say that an action could not be maintained, and that damages, beyond the amount of the debt if the injury were great, or much less than such amount if the injury were less serious, might not be recovered. . . . In this class of cases it must be assumed that it is the malicious act of the defendant, and that malicious act only, which causes the servant or contractor not to perform the work or contract which he would otherwise have done. The servant or contractor may be utterly unable to pay anything like the amount of the damage sustained entirely from the wrongful act of the defendant: and it would seem unjust, and contrary to the general principles of law, if such wrongdoer were not responsible for the damage caused by his wrongful and malicious act. . . .

Without however deciding any such more general question, I think that we are justified in applying the principle of action for enticing away servants to a case where the defendant *maliciously procures* a party, who is under a valid contract to give her exclusive personal services to the plaintiff for a specified period, to refuse to give such services *during the period for which she had so contracted*, whereby the plaintiff was injured.

I think, therefore, that our judgment should be for the plaintiff.

[The concurring opinions of Erle and Wightman, JJ., are omitted.]

Coleridge, J. [dissenting]. . . . In order to maintain this action, one of two propositions must be maintained; either that an action will lie against any one by whose persuasions one party to a contract is induced to break it to the damage of the other party, or that the action, for seducing a servant from the master or persuading one who has contracted for service from entering into the employ, is of so wide application as to embrace the case of one in the position and profession of Johanna Wagner. After much consideration and enquiry I am of [the] opinion that neither of these propositions is true; and they are both of them so important, and, if established by judicial decision, will lead to consequences so general, that, though I regret the necessity, I must not abstain from entering into remarks of some length in support of my view of the law.

It may simplify what I have to say, if I first state what are the conclusions which I seek to establish. They are these: that in respect of breach of contract the general rule of our law is to confine its remedies by action to the contracting parties, and to damages directly and proximately consequential on the act of him who is sued; that, as between master and servant, there is an admitted exception, that this exception dates from the Statute of Labourers, 23 Edw. III, and both on principle and according to authority is limited by it. If I am right in these positions, the conclusion will be for the defendant, because enough appears on this record to show, as to the first, that he, and, as to the second, that Johanna Wagner, is not within the limits so drawn.

First then, that the remedy for breach of contract is by the general rule of our law confined to the contracting parties. . . . There would be such a manifest absurdity in attempting to trace up the act of a free agent breaking a contract to all the advisers who may have influenced his mind, more or less honestly, more or less powerfully, and to make them responsible civilly for the consequences of what after all is his own act, and for the whole of the hurtful consequences of which the law makes him directly and fully responsible, that I believe it will never be contended for seriously. . . . [W]hen you apply the term of effectual persuasion to the breach of a contract, it has obviously a different meaning [from cases where a master orders a trespass by a servant]; the persuader has not broken and could not break the contract, for he had never entered into any; he cannot be sued upon the contract; and yet it is the breach of the contract only that is the cause of damage. Neither can it be said that in breaking the

contract the contractor is the agent of him who procures him to do so; it is still his own act; he is principal in so doing, and is the only principal. This answer may seem technical; but it really goes to the root of the matter. It shows that the procurer has not done the hurtful act; what he has done is too remote from the damage to make him answerable for it. [After discussing certain precedents, Judge Coleridge continued:] None of this reasoning applies to the case of a breach of contract: if it does, I should be glad to know how any treatise on the law of contract could be complete without a chapter on this head, or how it happens that we have no decisions upon it. Certainly no subject could well be more fruitful or important; important contracts are more commonly broken with than without persuaders or procurers, and these often responsible persons when the principals may not be so. I am aware that with respect to an action on the case the argument primae impressionis is sometimes of no weight. If the circumstances under which the action would be brought have not before arisen, or are of rare occurrence, it will be of none, or only of inconsiderable weight; but, if the circumstances have been common, if there has been frequently occasion for the action, I apprehend it is important to find that the action has yet never been tried. Now we find a plentiful supply both of text and decision in the case of seduction of servants: and what inference does this lead to, contrasted with the silence of the books and the absence of decisions on the case of breach of ordinary contracts? . . . To draw a line between advice, persuasion, enticement and procurement is practically impossible in a court of justice; who shall say how much of a free agent's resolution flows from the interference of other minds, or the independent resolution of his own? This is a matter for the casuist rather than the jurist; still less is it for the juryman. Again, why draw the line between bad and good faith? If advice given mala fide, and loss sustained, entitle me to damages, why, though the advice be given honestly, but under wrong information, with a loss sustained, am I not entitled to them. According to all legal analogies, the bona fides of him who, by a conscious wilful act, directly injures me will not relieve him from the obligation to compensate me in damages for my loss. Again, where several persons happen to persuade to the same effect, and in the result the party persuaded acts upon the advice, how is it to be determined against whom the action may be brought, whether they are to be sued jointly or severally, in what proportions damages are to be recovered? . . .

I conclude then that this action cannot be maintained because: 1st. Merely to induce or procure a free contracting party to break his covenant, whether done maliciously or not, to the damage of another, for the reasons I have stated, is not actionable; 2d. That the law with regard to seduction of servants from their master's employ, in breach of their contract, is an exception, the origin of which is known, and that that exception does not reach the case of a theatrical performer. . . .

## NOTES

**1.** ***Protection of Contractual Interests Under Lumley v. Gye.*** The original Statute of Labourers was passed shortly after the height of the Black Plague, which started in 1346 in central Asia and moved through virtually all of Europe, resulting in an estimated death toll of between 75 million and 200 million people by its end in 1353. The law sought to protect government-mandated contracts from interference with third parties. Could it also be construed to protect voluntary arrangements, and, if so, which? Note that Lumley v. Gye involved a personal services contract with a party of unique operatic skills, a far cry from the reapers and mowers listed in the statute. Typically there is little reason to protect ordinary contracts at competitive wages from third-party interference, because of the ease of hiring a replacement for the lost worker, whom few will have an incentive to lure away in any event.

The situation was quite the opposite with the uniquely talented Ms. Wagner, who was sued directly for breach of contract in Lumley v. Wagner, 42 Eng. Rep. 687, 693 (Ch. 1852), the companion case to Lumley v. Gye, in which Lumley enjoined Wagner from singing elsewhere in a manner inconsistent with the efficient breach theory:

> Wherever this Court has not proper jurisdiction to enforce specific performance, it operates to bind men's consciences, as far as they can be bound, to a true and literal performance of their agreements; and it will not suffer them to depart from their contracts at their pleasure, leaving the party with whom they have contracted to the mere chance of any damages which a jury may give. . . . The effect, too, of the injunction in restraining J. Wagner from singing elsewhere may, in the event of an action being brought against her by the Plaintiff, prevent any such amount of vindictive damages being given against her as a jury might probably be inclined to give if she carried her talents and exercised them at the rival theatre: the injunction may also, as I have said, tend to the fulfilment of her engagement; though, in continuing the injunction, I disclaim doing indirectly what I cannot do directly.

Why no decree ordering Wagner to sing?

**2. *Inducement of Breach of Contract in Labor Disputes.*** The protection afforded in *Lumley* is also critical to certain contractual arrangements where an employee does possess distinctive attributes or information. In Bowen v. Hall, 6 Q.B.D. 333 (1881), Lumley v. Gye was applied to the contract of an employee brickmaker who had knowledge of a secret glazing process and who was induced to breach a definite five-year contract of employment with the plaintiff. The court held that malice was the gist of the tort and noted that although "mere persuasion" was not actionable, "if the persuasion be used for the indirect purpose of injuring the plaintiff, or of benefiting the defendant at the expense of the plaintiff, it is a malicious act." How does this definition of malice differ from the "notice" referred to by Crompton, J., in *Lumley*? Shortly thereafter, in Temperton v. Russell, [1893] 1 Q.B. 715, inducement of breach of contract was held to reach interference with an ordinary contract for the sale of goods, here in the context of a labor dispute. On the early history and expansion of the action, see John Nockleby, Tortious Interference with Contractual Relations in the Nineteenth Century: The Transformation of Property, Contract, and Tort, 93 Harv. L. Rev. 1510 (1980).

Perhaps the most controversial application of the tort of inducement of breach of contract stemmed from its use as a weapon of business in labor disputes. In the leading American case, Hitchman Coal & Coke Co. v. Mitchell, 245 U.S. 229 (1917), the defendants were employees of the Mineworkers Union, who had induced the miners at the plaintiff's mine to stay on the job after they had agreed to join the union on some future request. The miners were held in breach of their "yellow-dog" contract between the employer and the workers, whereby the miners, working under a contract at will, agreed not to join a union while remaining in the plaintiff's employ. In this context, injunctive relief could be valuable when one party, the union, may induce many parties, the employees, to act in breach of contract. In *Lumley*, the only reason given for the second tort action was that its tortious basis could result in greater damages against Gye than he could have gotten from Wagner. But in *Hitchman Coal*, the injunction against the union was sought because the plaintiff could not easily maintain multiple damage actions against dozens of employees who could have quit in unison. The injunctive relief was able to stop in its tracks the union efforts to close mines.

It is for just this reason that *Hitchman* was repudiated in the labor context, first in 1932 by the Norris-LaGuardia Act, 29 U.S.C. §§101-115 (2024), which prohibited the enforcement of yellow-dog contracts in federal courts, *id*. §103, and thereafter in 1935 by the National Labor Relations Act, 29 U.S.C. §§151-169 (2024), which made it an "unfair labor practice" to discriminate against employees because of their participation in union activities, 29 U.S.C. §158(a)(3). For an early defense of the statute, see Calvert Magruder, A Half Century of Legal Influence upon the Development of Collective Bargaining, 50 Harv. L. Rev. 1071 (1937);

for a defense of the common law regime, see Richard A. Epstein, A Common Law for Labor Relations: A Critique of the New Deal Labor Legislation, 92 Yale L.J. 1357, 1370–75 (1983). See also Richard A. Epstein, Labor Unions: Saviors or Scourges?, 41 Cap. U. L. Rev. 1 (2013); Craig Becker, Labor Law—The Law of a Balanced Society: A Reply to Professor Epstein, 41 Cap. U. L. Rev. 35 (2013). Becker was a member of the National Labor Relations Board and is now Senior Counsel to the AFL-CIO after serving as its General Counsel.

**3. *Contracts Covered by the Tort.*** In *Lumley*, the plaintiff's contract afforded him an undeniable cause of action against Wagner. Should the defendant's inducement be actionable when there is some infirmity in the underlying contract? For example, the action in general will not lie for gambling contracts that violate public policy. Yet the tort action is available for inducing nonperformance of contracts with lesser infirmities. Thus ample authority allows the inducement action even if the contract between the plaintiff and the third party is voidable (say, because a child is underage) or unenforceable (say, because of the statute of limitations or the Statute of Frauds). See RST §766. "[S]ince men usually honor their promises no matter what flaws a lawyer can find, the offender should not be heard to say that the contract he meddled with could not have been enforced." Harris v. Perl, 197 A.2d 359, 363 (N.J. 1964).

In some contexts, the defendant's conduct is actionable even if the contract between the plaintiff and the defendant is terminable at the will of either party. See, e.g., Walker v. Cronin, 107 Mass. 555 (1871). That general statement is clearly true to the extent that one of the parties is induced to breach some other covenant contained in the underlying contract: In *Walker*, the employee refused to return tools and materials to the employer upon leaving employment terminable at will. But it is highly unlikely that the doctrine applies when the employee's conduct is not in breach of contract, as when he simply leaves the plaintiff for higher wages offered elsewhere. Nor can at-will employees sue for interference with contract when displaced by new workers who sign on for lower wages. Indeed today "the general rule in the District of Columbia [and elsewhere] is that an at-will employment agreement cannot form the basis of a claim of tortious interference with contractual relations." Metz v. BAE Sys. Tech. Sols. & Servs. Inc., 774 F.3d 18, 23–24 (D.C. Cir. 2014).

In some specialized situations, inducing the termination of even an at-will business arrangement can create liability. In Albert v. Loksen, 239 F.3d 256, 276 (2d Cir. 2001), the defendant supervisor made false and defamatory statements about Albert (a hospital physicist) to the chief administrator of the hospital's radiology department in order to procure Albert's termination. The court held that it was a triable issue of fact whether the supervisor employee acted with "common-law or actual malice" that was "motivated by a desire to undermine Albert's threats to report safety violations and other misconduct." Sack, J., allowed the plaintiff's action notwithstanding his at-will employment arrangement:

> An at-will employee may maintain a tortious interference claim, however, in "certain limited situations." To do so, he or she must establish that a "third party used wrongful means to effect the termination such as fraud, misrepresentation, or threats, that the means used violated a duty owed by the defendant to the plaintiff, or that the defendant acted with malice.

In Ixchel Pharma, LLC v. Biogen, Inc., 470 P.3d 571, 581 (Cal. 2020), Ixchel had entered into a development contract with Forward with respect to a promising new drug, dimethyl fumarate (DMF). The contract was terminable at will by either side on sixty days' notice. Biogen and Forward then settled a patent dispute for $1.25 billion that would allow Forward to license another DMF drug. That settlement required Forward to give Ixchel the sixty days' notice needed for termination. Ixchel then sued Biogen for both tortious interference with contract and for interference with prospective advantage. Lui, J., first held that the tort is only actionable if the defendant engaged in an independently wrongful act, which is one that "is proscribed by some constitutional, statutory, regulatory, common law, or other determinable

legal standard." That rule meant that contracts at will and prospective advantages both received less legal protection than a contract binding on both parties.

Having decided that there was insufficient proof of unlawful interference in either of these cases, Lui, J., then held that the question was whether Biogen's conduct constituted a violation of the Business and Professions Code section 16600, which resolved into the question whether the applicable standard was a rule of reason test that required the court to ask "whether an agreement harms competition more than it helps" by considering "the facts peculiar to the business," or whether reasonableness was irrelevant because such interference was a per se wrong on the antitrust law. Lui, J., concluded that the per se test cut too deeply into ordinary economic arrangements and remanded the case under the rule of reason standard. How does a trial court answer the net benefit question if both deals promised economic gain?

**4.** ***Basis of Liability for Inducement of Breach of Contract.*** The Second Restatement of Torts §766 provides that "[o]ne who intentionally and improperly interferes with the performance of a contract" is subject to tortious liability, provided that "the actor must have knowledge of the contract with which he is interfering." RST §766, cmt. *i*.

**RESTATEMENT OF THE LAW (SECOND) OF TORTS**

**§766. Intentional Interference with Performance of Contract by Third Person**

One who intentionally and improperly interferes with the performance of a contract (except a contract to marry) between another and a third person by inducing or otherwise causing the third person not to perform the contract, is subject to liability to the other for the pecuniary loss resulting to the other from the failure of the third person to perform the contract.

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§17. Interference with Contract**

(1) A defendant is subject to liability for interference with contract if:
(a) a valid contract existed between the plaintiff and a third party;
(b) the defendant knew of the contract;
(c) the defendant engaged in wrongful conduct as defined in Subsection (2);
(d) the defendant intended to cause a breach of the contract or disruption of its performance;
(e) the defendant's wrongful conduct caused a breach of the contract or disruption of performance; and
(f) the plaintiff suffered economic loss as a result.

(2) Conduct is wrongful for purposes of this Section if:
(a) the defendant acted for the purpose of appropriating the benefits of the plaintiff's contract;
(b) the defendant's conduct constituted an independent and intentional legal wrong; or
(c) the defendant engaged in the conduct for the sole purpose of causing harm to the plaintiff.

Even then, notice of the existing relationship, while necessary, may not be sufficient to constitute the tort, given that the interference with the relationship must also be "improper" or "wrongful" in some way. How does the Third Restatement's framework differ from that of the Second Restatement?

On any view, liability for inducement thus stands on a different footing from liability for ordinary physical damage to person and property. One explanation for the difference is offered in Richard A. Epstein, Inducement of Breach of Contract as a Problem of Ostensible Ownership, 16 J. Legal Stud. 1, 24 (1987), which argues that the notice system tracks the rules used when a bailee sells the bailed goods to a third party without the permission of the owner. The buyer with knowledge of the bailor's interest is treated as a purchaser in bad faith from whom the true owner can recover the goods. However, the claim of the true owner is often denied when the bailee looks like the "ostensible owner" to the rest of the world because the third party is now a purchaser in good faith. "The tort of inducement of breach of contract is designed to protect contracts for the sale of labor by preventing others from subsequently acquiring that labor for themselves, once they know it has been committed to another. It is a restriction against double-dealing." Accordingly, the plaintiff may only maintain the action for inducement of breach of contract against one who *knows* of the existence of the contract, as the words "with notice" in Lumley v. Gye imply. With personal service contracts, moreover, actual notice is typically required because the recordation systems in use for land and certain valuable chattels (airplanes, cars) are not available. When celebrities are involved, therefore, the best protection may be to publicly announce the signing of a contract in order to place the world on notice of the existence of the contract, without, however, revealing any confidential terms.

An alternative view holds that *inducement* of breach of contract requires "the conjunction of notice, persuasion by the offer of better terms, and receipt of benefits by Inducer." Lillian R. BeVier, Reconsidering Inducement, 76 Va. L. Rev. 877, 885 n.25 (1990). How often will breaches take place if the inducer does not offer better terms, or at least better long-term prospects? What if the defendant induces breach for the benefit of a third party?

**5. *Privileged Inducements.*** As with other torts, the party that induces a breach of contract may well have some privilege, analogous to those in necessity and defamation cases, for committing a prima facie wrong. The Second Restatement gets at this notion by restricting liability for those actions that are done "improperly" based on a balance of motives and interests of the two parties. RST §767, cmt. *b*. Thus interference has been held privileged when done to further public morals. For example, in Brimelow v. Casson [1924] 1 Ch. 302, the privilege was upheld when the plaintiff was alleged to have employed chorus girls on such unfavorable terms that they had to resort to prostitution to earn enough money to live. The Third Restatement, however, articulates clearer rules for what is privileged: "(a) lawful disclosure of truthful facts to another; (b) lawful and good-faith efforts to protect a legal interest; or (c) lawful and good-faith efforts to protect an economic interest in the contractual relationship at issue." RTT: LEH §20.

One privilege of great practical importance generally allows the officer or lawyer of a firm to advise the firm to breach an existing contract. The officer or lawyer is not treated as an independent third party acting for economic advantage, but as acting pursuant to a "confidential arrangement" between the parties. See, e.g., Imperial Ice Co. v. Rossier, 112 P.2d 631 (Cal. 1941). The privilege, however, is not absolute, as Andreasen, J., observed in Jones v. Lake Park Care Center, Inc., 569 N.W.2d 369, 377 (Iowa 1997):

> When acting as an agent within the scope of the qualified privilege, there can be no tortious interference because only two parties exist; the corporation and the contracting party. However, when an officer or director acts beyond the scope of their qualified privilege, they are no longer acting as agents of the corporation and can be personally liable for their acts.

*Jones* applied this principle in a terminated employee's suit for intentionally interfering with an employment contract against the husband and wife, who were the sole shareholders of a small day care center. Andreasen, J., agreed with the lower court's finding that the dismissal was for "improper reasons." Does any dismissal after bad blood fall within this exception?

**6. *The Theory of Efficient Breach.*** One notable attack on the doctrine of Lumley v. Gye rests on the principle that the tort of inducement of breach of contract may be misplaced because breach of contract itself may create social wealth by increasing overall consumer satisfaction. See Harvey S. Perlman, Interference with Contract and Other Economic Expectancies: A Clash of Tort and Contract Doctrine, 49 U. Chi. L. Rev. 61 (1982).

Perlman's argument hearkens back to Holmes's famous aphorism: "The only universal consequence of a legally binding promise is that the law makes the promisor pay damages if the promised event does not come to pass." Oliver Wendell Holmes, Jr., The Common Law 301 (1881). In modern terms, the breach of contract is said to be "efficient" whenever it allows the promisor to shift his resources to a higher valued use. The logic runs as follows: The innocent party is left as well off by an award of damages equal to the benefits provided under the contract; the promisor is left better off, having purchased his freedom; therefore, the net social welfare is increased. The theory of "efficient breach" thus holds that a promisor should always be allowed to extricate himself unilaterally from a bargain if he is prepared to pay the proper social price, which equals only expectation damages. Accordingly, inducement of breach of contract should not be made tortious, lest it undermine the incentives of contractual parties not to breach contracts when it is efficient to do so. Perlman concludes, therefore, that the action should be allowed only when the defendant has used unlawful and independently tortious means, chiefly force or fraud, to induce the breach.

The soundness of the efficient breach argument depends at least in part on the ability of the expectation damages to leave a promisee indifferent between performance and breach. But if the contract damages do not reflect the full range of objective and subjective losses, the plaintiff's recovery, net of litigation costs, could well leave the innocent promisee worse off. See Richard A. Epstein, Inducement of Breach of Contract as a Problem of Ostensible Ownership, *supra* Note 4; Daniel Friedmann, The Efficient Breach Fallacy, 18 J. Legal Stud. 1 (1989), which argues that the costs of untangling expectation damages may well exceed the costs needed to negotiate a release from the original contract.

Expectation damages, moreover, are not universally regarded as the gold standard of contract remedies. Specific performance is generally allowed in real estate transactions (and other cases involving "unique" goods) and, even with personal service contracts, a promisee may enjoin the promisor from undertaking employment inconsistent with previous contractual obligations. See Fred S. McChesney, Tortious Interference with Contract Versus "Efficient" Breach: Theory and Empirical Evidence, 28 J. Legal Stud. 131, 185 (1999), for an exhaustive examination of the case law, concluding that "most of the legal rules relevant to inducement are consistent with the property-based model of interference," and not with the efficient breach theory, including of course the injunction issued in Lumley v. Wagner. In contemporary litigation, the tort has far broader implications in modern technological industries.

## *Asahi Kasei Pharma Corp. v. Actelion Ltd.*

222 Cal. App. 4th 945 (2014)

Bruiniers, J.

Asahi Kasei Pharma Corporation (Asahi) is a Japanese corporation which develops and markets pharmaceutical products and medical devices. One of its products is Fasudil, a drug which Asahi sought to market in the United States (U.S.) for treatment of pulmonary arterial

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**Headquarters of Actelion, near Basel, Switzerland**

*Source: Fabrice Coffrini/AFP/Getty Images*

hypertension (PAH). In order to obtain regulatory approvals for Fasudil, and to develop and commercialize it in North America and Europe, Asahi entered into a licensing and development agreement (the License Agreement) with CoTherix, Inc. (CoTherix), a California-based biopharmaceutical company focused on developing and commercializing products for the treatment of cardiovascular disease. Appellant Actelion Ltd. is a Swiss pharmaceutical company that markets a PAH treatment drug, bosentan (under the trade name Tracleer), and holds the dominant share of the relevant market. Actelion Ltd., through a subsidiary, acquired all of the stock of CoTherix, and concurrently notified Asahi that CoTherix would discontinue development of Fasudil for "business and commercial reasons."

[Asahi sued Actelion and three Actelion executives in California state court, alleging, inter alia, intentional interference with contract and interference with Asahi's prospective economic advantage. The jury found that all defendants acted "with malice, oppression or fraud," and awarded nearly $550 million in compensatory damages and $30 million in punitive damages.]

[W]e address the scope of liability for tortious interference with a contract by a nonparty to the contract, and we affirm the judgment in favor of Asahi. . . .

## I. Background and Procedural History

. . . Studies indicated that Fasudil had the potential to promote healing of blood vessel lesions and limit the scarring associated with PAH.

Development of Fasudil for new medical uses was commercially attractive to Asahi if it could be done expeditiously. To recoup investment, a drug must be developed sufficiently early in its patent life to ensure an adequate period of market exclusivity after receipt of regulatory approval and before generic competition arrives. . . .

In order to gain regulatory approvals necessary for new medical uses of Fasudil, Asahi entered into the License Agreement with CoTherix on June 23, 2006. . . . Under the terms of the License Agreement, CoTherix agreed to obtain U.S. and European regulatory approvals for Fasudil to treat certain diseases, and to develop and commercialize it in those markets. . . . Asahi considered CoTherix's ability to move quickly in clinical development of Fasudil to be particularly important to preservation of Fasudil's market exclusivity before facing generic competition.

Actelion Ltd. has, since December 2001, marketed Tracleer, an endothelin receptor antagonist and oral PAH drug that has been approved by the Food and Drug Administration (FDA) for use in the U.S. Tracleer is what is known in the pharmaceutical industry as a "blockbuster" drug, generating over $1 billion in revenue annually, and Actelion has held the dominant share of the relevant market. In 2006, 98 percent of Actelion's U.S. revenues were dependent upon Tracleer sales.

At trial, Asahi presented evidence that Actelion acquired CoTherix specifically because it saw Fasudil as a significant threat to its market dominance with Tracleer and that Defendants

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used unlawful means to stop the development of Fasudil, thereby interfering with the License Agreement. Specifically, Asahi argued that Defendants used extortion and fraud to "painstakingly kill[ ]" Fasudil as a competitive product.

. . . In July 2006, a director of business development for Actelion Pharmaceuticals Ltd., Carina Spaans, referenced CoTherix, Fasudil and another company in her notes, with the following comment: "Buying both companies will leave the market for Tracleer free for Actelion." Negotiation of an acquisition of CoTherix began in August. . . . On November 19, 2006, Actelion U.S. Holding Company and CoTherix signed an agreement and plan of merger, which was publicly announced the following day.

Beginning November 20, 2006, Asahi repeatedly sought assurances from CoTherix and Actelion that Fasudil development would continue after the proposed merger. . . . Despite Actelion's knowledge that failure to provide assurances might constitute material breach of the License Agreement, no assurances were provided. In mid-December, Asahi requested a videoconference with Actelion . . . [during which Asahi was assured]: "Actelion does not have an intention to make any delay of [F]asudil development." On January 3, 2007, CoTherix, after conferring with Actelion, told Asahi: "[W]e continue to honor our agreement to move [F]asudil forward. Please note that I have no power to compel Actelion to provide you with the response you desire."

. . . On January 9, Actelion acquired all of the stock of CoTherix and concurrently notified Asahi that it was discontinuing development of Fasudil for "business and commercial reasons." . . .

### The Litigation Below

Asahi first initiated the ICC Arbitration proceeding, against CoTherix only, claiming breach of contract. Among other damages, Asahi claimed the value of development work CoTherix failed to perform through June 2009 and development-based milestone payments. On December 15, 2009, the arbitrators awarded Asahi over $91 million.

[Asahi then sued Actelion and its executives in California state court, alleging, inter alia, "intentional interference with the license agreement" and "wrongful interference with Asahi's prospective economic advantage in the 'continued development of Fasudil.'"]

### The Trial

In January 2011, the matter proceeded to jury trial against the Defendants. On April 29, the jury returned a unanimous liability verdict against the Defendants, awarding $358.95 million for [lost profits]; $187.4 million for lost development costs; $450,000 for regulatory maintenance costs; and $75,000 for the cost of an investigator-sponsored study. . . . The jury also unanimously found the Defendants acted with "malice, oppression or fraud."

In the punitive damage phase of trial, the jury awarded damages against the Individual Defendants only [totaling $30 million]. . . .

## II. Discussion

### A. Tortious Interference with the License Agreement

"To recover in tort for intentional interference with the performance of a contract, a plaintiff must prove: (1) a valid contract between plaintiff and another party; (2) defendant's knowledge of the contract; (3) defendant's intentional acts designed to induce a breach or disruption of the contractual relationship; (4) actual breach or disruption of the contractual relationship; and (5) resulting damage. In this way, the 'expectation that the parties will honor the terms of the contract is protected against officious intermeddlers.'"

. . . Actelion contends that it cannot be liable for tortious interference with the License Agreement because "[t]he tort duty not to interfere with [a] contract falls only on strangers — interlopers who have no legitimate interest in the scope or course of the contract's performance." Specifically, they argue: "As a matter of law, [the underlying policy of the tort of intentional interference with contract — preventing outsiders who have no legitimate social or economic interest in the contract from interfering with the expectations of contracting parties — ] precludes imposition of liability against Actelion for terminating development of [F]asudil, because that act took place after consummation of the [a]cquisition [of CoTherix], at which time Actelion was not a stranger to CoTheri[x]'s agreement with Asahi." The Individual Defendants join in this argument and maintain: "By the same token, the [I]ndividual [D]efendants — as high-level executives of Actelion — were not strangers to the [License] Agreement, but instead were responsible for determining how Actelion, standing in the shoes of CoTherix, would deal with that agreement."

Asahi counters that California law nevertheless recognizes that corporate owners, officers and directors may be liable for interfering with corporate contracts, and that claims of privilege or justification are defenses that must be pleaded and proved. And to prevail on such defenses, Defendants must show that they did not "use improper means."

**1. Jury Instructions on Wrongful Interference with the License Agreement**

The jury was instructed on the elements of a cause of action for wrongful interference with contract. The court declined to give a special jury instruction, proposed by Actelion, that would have directed that the jury could not hold Actelion liable for inducing CoTherix to breach the License Agreement after the acquisition on January 9, 2007, because at that time Actelion had a direct interest in the contractual relationship between CoTherix and Asahi.

. . . [T]he jury was instructed: "A person cannot be liable for interference with that person's own contract, if that person was a party to the contract at the time of the interference." And the trial court instructed the jury on the justification defense: [A] defendant [is] not liable for intentional interference with contract if that defendant's conduct was justified, but that "[t]he affirmative defense of justification does not apply if the particular Defendant used unlawful means to interfere with the [License Agreement]. . . . 'Unlawful means' includes intentional misrepresentation, concealment, and extortion." Having been so instructed, the jury nonetheless found that all Defendants intentionally interfered with the License Agreement. . . .

**3. Analysis**

Defendants contend that, after January 9, 2007, they could not be liable for interfering with the License Agreement because "Actelion had a 'legitimate . . . economic interest in the contractual relationship.'" [The court then discusses Applied Equipment Corp. v. Litton Saudi Arabia Ltd., 869 P.2d 454 (Cal. 1994), where the California Supreme Court held that "*a contracting party* cannot be held liable in tort for conspiracy to interfere with its own contract" in order to uphold "vital and established distinctions between contract and tort theories of liability." "The tort duty not to interfere with the contract falls only on strangers — interlopers who have no legitimate interest in the scope or course of the contract's performance."]

Defendants do not contend that they were parties to the License Agreement after January 9, 2007. . . . Instead, Actelion contends that *Applied Equipment* should be read broadly so as to limit liability for intentional interference to complete "strangers" to the contract, not simply nonparties to the contract. . . .

Defendants urge this court to take the *Applied Equipment* court's language . . . to mean a noncontracting party who also has no interest in the contract. But the California courts have not recognized a corporate owner's absolute privilege to interfere with its subsidiary's contract. [Discussion of California cases omitted.]

. . . "A stranger," as used in *Applied Equipment*, means one who is not a party to the contract or an agent of a party to the contract. . . . Actelion, by virtue of its ownership interest, is not automatically immune from liability for tortious interference with the License Agreement.

Defendants misplace their reliance on *Mintz* [v. Blue Cross of California, 172 Cal. App. 4th 1594, 1604 (2009).] . . . *Mintz* is distinguishable from this case in that the party charged with interference was specifically authorized to act as agent of a party to the contract. Defendants point to no evidence in the record establishing that Actelion was authorized to act as CoTherix's agent with respect to the License Agreement.

Nor are we persuaded by Defendants' reliance on Kasparian v. County of Los Angeles, 38 Cal. App. 4th 242 (1995). . . . The *Kasparian* court followed *Applied Equipment* and extended its holding to the tort of interference with prospective economic relations. The court concluded that the partnership could not be held liable, as a matter of law, for such a tort because "[i]t can only be asserted against a stranger to the relationship." However, without any discussion, the court also included the individual partner defendants within that holding. To the extent *Kasparian* implicitly holds that the owners of a business entity are automatically deemed to be exempt from interference liability because their economic interest means they are not "strangers," we disagree. . . .

We hold that the jury was properly instructed on the elements of wrongful interference with contract and properly charged with considering whether Defendants "used unlawful means to interfere with the [License Agreement]." So instructed, the jury found that each of the Defendants intentionally interfered with the License Agreement. . . .

#### 4. Liability of the Individual Defendants

[Bruiniers, J., held that the individual defendants, as "officers" or "directors" of Actelion, had "actively participated in the tortious conduct" and thus could be held personally liable for an intentional economic tort. He also rejected the Actelion executives' claim of "manager's privilege" — namely their right to protect their principal's interests by counseling breach of a contract with a third party on the ground that "[t]he manager's privilege does not exempt a manager from liability when he or she tortiously interferes with a contract or relationship between third parties."]

[Affirmed.]

## NOTES

**1. *Sins of Subsidiary Visited Upon Parent Company.*** *Asahi* holds that a parent company that acquires a subsidiary party to a contract qualifies under California law as a "stranger" or "interloper" to the agreement, subject to liability for tortious interference with a contract. Does Actelion have a legitimate economic interest in the licensing agreement? Why does the court insist nonetheless that it remains a "stranger" as a nonparty to the contract?

**2. *"Tortifying" Ordinary Contract Actions?*** Actelion argued to the California Supreme Court (which denied review in March 2014) that "[b]y 'tortifying' ordinary contract actions, the decision below threatens to discourage businesses from investing in California, for it places corporations and their executives at risk of crippling tort damages — magnified by the prospect of punitive damages — whenever a subsidiary incurs contract liability." Recall that Asahi won $91 million against Actelion in arbitration. By subsequently suing in tort, Asahi opened the door to punitive damages and won one of the largest damages verdicts in California's history. "Tech giants and other corporations that have grown by serial acquisition fear the Actelion precedent could expose them — at least in California — to open-ended liability over licensing

disputes involving the smaller new-technology companies they are wont to gobble up like so many cocktail nuts." Paul M. Barrett, An Obscure Pharma Lawsuit Puts California's Tech Titans on Edge, Bloomberg (Mar. 13, 2014, 10:46 AM), http://www.bloomberg.com/bw/articles/2014-03-12/an-obscure-pharma-lawsuit-puts-californias-tech-titans-on-edge. While the intentional interference tort protects contractual stability, does it do so at the expense of other significant economic concerns? What are the likely ramifications of imposing tort liability for competitive business practices and commercial dealings? Should courts limit liability for tortious interference in order to preserve the distinction between contract and tort?

**3.** ***Calculating Prospective Lost Profits.*** Recovery for lost profits generally requires "reasonable certainty" but "not absolute certainty." The *Asahi* court distinguished "established" businesses whose lost profits "may be ascertained with reasonable certainty from the past volume of business and other provable data relevant to the probable future sales" from "unestablished" ones whose profits are too "uncertain, contingent and speculative." The court conceded that "this case does not fit neatly into the established business versus new business paradigm." As an added wrinkle, regulatory approval by the FDA and EMEA (European Medicines Agency) was a prerequisite to selling the to-be-developed Fasudil drug. In fact, according to *Nature*, the probability of success for a drug at Fasudil's stage (entering Phase II clinical trials) is roughly 15 percent. What result if Actelion only stopped its work on the project when it thought it would not get FDA approval? Should Asahi be required to find another development partner after Actelion cancelled the deal?

**4.** ***A Victory for Drug Development?*** As part of its recitation of the "background and procedural history," the *Asahi* court refers to Actelion's market dominance and its efforts to eliminate a competitor drug. Asahi had brought an antitrust claim, which the court previously dismissed. Did the court look to tort as an alternative remedy to guard against anticompetitive actions? See Asahi Kasei Pharma Corp. v. CoTherix, Inc., 204 Cal. App. 4th 1, 18–19 (2012) ("Asahi [argues] at least one of Actelion's purposes . . . was to eliminate Fasudil. . . . CoTherix was aware of Actelion's purpose; as part of an agreed 'strategy' Actelion directed CoTherix and its principals to give false assurances to Asahi. . . . [But] Asahi failed to produce evidence of any premerger meeting of the minds. . . .").

**5.** ***Was "Tortifying" a False Alarm?*** In the first decade since *Asahi*, no major decision has challenged its holding. See Caliber Paving Co., Inc. v. Rexford Indus. Realty & Mgmt., Inc., 54 Cal. App. 5th 175, 183–86 (2020) (holding that *Asahi* is the majority position in California and collecting cases in agreement). Less controversial aspects of *Asahi*'s holding have garnered further agreement without much comment. See Workplace Techs. Rsch., Inc. v. Project Mgmt. Inst., Inc., 664 F. Supp. 3d 1142, 1166–67 (S.D. Cal. 2023) (holding that when an intentional interference case "concerns a hybrid of an established and unestablished business[,] any reliable proof of lost profits will therefore suffice"). Either the alarm over "tortifying" contract law was a false alarm, or perhaps *Asahi* has thus far flown under the radar.

## SECTION C. COVENANTS NOT TO COMPETE

### *Mitchel v. Reynolds*

24 Eng. Rep. 347 (1711)

A bond or promise to restrain oneself from trading in a particular place, if made upon a reasonable consideration, is good. *Secus* if it be on no reasonable consideration, or to restrain a man from trading at all.

Debt upon a bond. The defendant prayed . . . whereas the defendant had assigned to the plaintiff a lease of a messuage and bakehouse in *Liquorpond Street*, in the parish of *St. Andrew's Holborn*, for the term of five years: now if the defendant should not exercise the trade of a baker within that parish during the said term, or, in case he did, should within three days after proof thereof made, pay to the plaintiff the sum of fifty pounds, then the said obligation to be void. Defendant pleaded, that he was a baker by trade, that he had served an apprenticeship to it, [and that] said bond was void in law. . . . Whereupon the plaintiff demurred in law.

Parker, C.J., delivered the resolution of the court.

The general question upon this record is, whether this bond, being made in restraint of trade, be good?

And we are all of opinion, that a special consideration being set forth in the condition, which shews it was reasonable for the parties to enter into it, the same is good; and that the true distinction of this case is, not between promises and bonds, but between contracts *with* and *without* consideration; and that wherever a sufficient consideration appears to make it a proper and an useful contract, and such as cannot be set aside without injury to a fair contractor, it ought to be maintained; but with this constant diversity, *viz*. where the restraint is general not to exercise a trade throughout the kingdom, and where it is limited to a particular place; for the former of these must be void, being of no benefit to either party, and only oppressive, as shall be shewn by and by.

The entering upon the trade, and not whether the right of action accrued by bond, promise or covenant, was the consideration in that case.

*1st*, That to obtain the sole exercise of any known trade throughout *England*, is a complete monopoly, and against the policy of the law.

*2dly*, That when restrained to particular places or persons (if lawfully and fairly obtained), the same is not a monopoly.

*3dly*, That since these restraints may be by custom, and custom must have a good foundation, therefore the thing is not absolutely, and in itself, unlawful.

*4thly*, That it is lawful upon good consideration, for a man to part with his trade.

*5thly*, That since actions upon the case are actions *injuriarum*, it has been always held, that such actions will lie for a man's using a trade contrary to custom, or his own agreement; for there he uses it *injuriously*.

*6thly*, That where the law allows a restraint of trade, it is not unlawful to enforce it with a penalty.

*7thly*, That no man can contract not to use his trade at all.

*8thly*, That a particular restraint is not good without just reason and consideration.

. . .

*4thly*, The fourth reason is in favour of these contracts, and is, that there may happen instances wherein they may be useful and beneficial, as to prevent a town from being overstocked with any particular trade; or in case of an old man, who finding himself under such circumstances either of body or mind, as that he is likely to be a loser by continuing his trade, in this case it will be better for him to part with it for a consideration, that by selling his custom, he may procure to himself a livelihood, which he might probably have lost, by trading longer.

*5thly*, The law is not so unreasonable, as to set aside a man's own agreement for fear of an uncertain injury to him, and fix a certain damage upon another; as it must do, if contracts with a consideration were made void.

There is a sort of presumption, that it is not of any benefit to the obligee himself, because, it being a general mischief to the publick, every body is affected thereby; for it is to be observed, that tho' it be not shewn to be the party's trade or livelihood, or that he had no

estate to subsist on, yet all the books condemn those bonds, on that reason, *viz*. as taking away the obligor's livelihood, which proves that the law presumes it; and this presumption answers all the difficulties that are to be found in the books.

As *1st*, That all contracts, where there is a bare restraint of trade and no more, must be void; but this taking place only where the consideration is not shewn can be no reason why, in cases where the special matter appears so as to make it a reasonable and useful contract, it should not be good; for there the presumption is excluded, and therefore the courts of justice will inforce these latter contracts, but not the former.

*2dly*, It answers the objection, that a bond does not want a consideration, but is a perfect contract without it; for the law allows no action on a *nudum pactum*, but every contract must have a consideration, either· expressed, as in *assumpsits*, or implied, as in *bonds* and *covenants*, but these latter, tho' they are perfect as to the form, yet may be void as to the matter; as in a covenant to stand seised, which is void without a consideration, tho' it be a compleat and perfect deed.

*3dly*, It shews why a contract not to trade in any part of *England*, tho' with consideration, is void; for there is something more than a presumption against it, because it can never be useful to any man to restrain another from trading in all places, tho' it may be, to restrain him from trading in some, unless he intends a monopoly, which is a crime.

As to the general indefinite distinction made between bonds. and promises in this case, it is in plain words this, that the agreement itself is good, but when it is reduced into the form of a bond, it immediately becomes void; but for what reason, see 3 Lev. 241. Now a bond may be considered two ways, either as a security, or as a compensation. . . .

*1st*, Why should it be void as a security? Can a man be bound too fast from doing an injury? which I have proved the using of a trade contrary to custom or promise, to be.

*2dly*, Why should it be void as a compensation? Is there any reason why parties of full age, and capable of contracting, may not settle the *quantum* of damages for such an injury? . . .

*4thly*, Restraints by custom may (as I have proved) be inforced with penalties which are imposed without the party's consent, nay by the injured party without the concurrence of the other; and if so, then *a fortiori* he may bind himself by a penalty.

The plaintiff took a baker's house, and the question is, whether he or the defendant shall have the trade in this neighbourhood; the concern of the public is equal on both sides.

What makes this the more reasonable is, that the restraint is exactly proportioned to the consideration, *viz*. the term of five years.

To conclude: In all restraints of trade, where nothing more appears, the law presumes them bad; but if the circumstances are set forth, that presumption is excluded, and the Court is to judge of those circumstances, and determine accordingly; and if upon them it appears to be a just and honest contract, it ought to be maintained. For these reasons we are of opinion, that the plaintiff ought to have judgment.

## NOTES

**1.** ***The Birth of a Doctrine.*** *Mitchel* is widely credited with establishing the modern law of contracts in restraint of trade. It was not the first of such cases. Dyer's Case, 2 Hen. V, fol. 5, pl. 26 (1414) (Eng.) had held that an employer could not impose on his apprentice a contractual restriction that prevented him from plying his trade in the same locale for a six-month period. The case was decided on particularistic grounds. The employer did not show up in court to enforce the agreement, which was not enforced, perhaps because the court feared

that his restriction was an indirect attempt to extend the apprenticeship. But so little is known about the case on such key issues about the geographical options available to the apprentice.

*Mitchel* offers a much more complete account. The issue of restraint arose as a defense by the defendant, who claimed that the covenant that restricted his ability to ply his trade was not enforceable because it was in restraint of trade. The analysis in that case did in so many terms describe itself as a rule of reason case, but it has always been read to deploy the analysis that asked the court to evaluate the gains to the parties from the enforcement of the agreement as against the harm imposed. Its analysis did not track in all respects the modern law. It may well be that a restraint that covers the entire kingdom is in restraint of trade, and that most local restraints are lawful. And there is in these cases a constant tension that asks whether the attack on these covenants is intended to protect the individual worker or the right of public at large to gain access to his work. In this area does it matter how many bakers ply work within the community, or is the removal of a single competitor sufficient to trigger the inquiry?

**2.** ***Employment Covenants Not to Compete: General Considerations.*** As is evident from *Mitchel*, the debate over these covenants remains active to this day. On the one hand, a covenant not to compete imposes an obvious restraint on trade that necessarily interferes with the emergence of a new competitor. In many instances it might be in the interest of the employee to accept that restriction in exchange for a large sum of cash, so that the contract can make both sides better off. But the loser then is the public that now has, as in *Mitchel*, one fewer baker in the market that could (especially in small towns) lead to less competition and thus higher prices and lower quantities for sale, which is the usual consequence of any contract in restraint of trade.

On the other side, especially in modern contexts, the covenant in these cases may be justified on the ground that it allows the employer to share greater amounts of information with the worker in order to better do the job. That information could include know-how for certain processes, future plans for expanding the product line, plans for opening outlets in new markets, customer lists, the use of secret processes, and more. An employer has a well-nigh absolute right to protection of this valuable information while the employee still remains in his employ. But that protection is generally insufficient to deal with the case where that same employee quits or is fired and then wants to use that information in starting up his rival firm or in a new job for a different employer. In essence, the claim for protection is that the employee is not entitled to a free gift of information that was costly for the employer to develop, so that it becomes imperative to encourage the sharing of information today to prevent its use by a rival tomorrow. It is equally clear that the short-term threat is always greater than the long-term one because all information depreciates in value over time, and in proportion to the distance from its current uses.

Antitrust law generally has developed three distinct categories to deal with this problem. The first are per se rules that ban certain levels of cooperation that have little efficiency gain and large social losses. Most notably are the per se rules that ban territorial divisions among rival sellers or that require each of them to limit the quantities sold or the prices below which they cannot be sold. There is at the other extreme a set of practices that are generally regarded as per se legal in that there is no duty not to engage in certain practices, of which the most famous is the general rule that no firm is under an obligation to do business in order to improve the position of its rivals. Verizon v. Offices of Curtis V. Trinko, 540 U.S. 398 (2004): "Thus, as a general matter, the Sherman Act does not restrict the long recognized right of [a] trader or manufacturer engaged in an entirely private business, freely to exercise his own independent discretion as to parties with whom he will deal," subject to limited exceptions. Similarly, it is virtually per se legal to engage in so-called predatory pricing, in which goods are sold at below-market costs in the short run, with the hopes of recouping the gains in the long run. See *infra* Note 1, at 250. In the middle lie cases that are decided in accordance with the

"rule of reason," which seeks to balance off the legitimate interests found in connection with covenants not to compete with well-defined features.

**3.** ***Rule of Reason Decisions.*** The relevant tradeoffs in these rule of reason cases is well described in ABC v. Wolf, 420 N.E.2d 363 (N.Y. 1981), a case in which Wolf, a well-known sportscaster, breached his covenant with ABC to negotiate in good faith a renewal of his current contract, only to take a position with its rival CBS. The court refused to stop Wolf from working in his new business.

> After a personal service contract terminates, the availability of equitable relief against the former employee diminishes appreciably. Since the period of service has expired, it is impossible to decree affirmative or negative specific performance. Only if the employee has expressly agreed not to compete with the employer following the term of the contract, or is threatening to disclose trade secrets or commit another tortious act, is injunctive relief generally available at the behest of the employer. Even where there is an express anticompetitive covenant, however, it will be rigorously examined and specifically enforced only if it satisfies certain established requirements. Indeed, a court normally will not decree specific enforcement of an employee's anticompetitive covenant unless necessary to protect the trade secrets, customer lists or good will of the employer's business, or perhaps when the employer is exposed to special harm because of the unique nature of the employee's services. And, an otherwise valid covenant will not be enforced if it is unreasonable in time, space or scope or would operate in a harsh or oppressive manner There is, in short, general judicial disfavor of anticompetitive covenants contained in employment contracts.
>
> Underlying the strict approach to enforcement of these covenants is the notion that, once the term of an employment agreement has expired, the general public policy favoring robust and uninhibited competition should not give way merely because a particular employer wishes to insulate himself from competition. Important, too, are the "powerful considerations of public policy which militate against sanctioning the loss of a man's livelihood." At the same time, the employer is entitled to protection from unfair or illegal conduct that causes economic injury. The rules governing enforcement of anticompetitive covenants and the availability of equitable relief after termination of employment are designed to foster these interests of the employer without impairing the employee's ability to earn a living or the general competitive mold of society.

Should Wolf be subject to liability for damages for taking the rival job? If so, how should they be measured?

The time, space, and scope restrictions referred to in ABC v. Wolf are usually treated as follows. The common response as to the temporal restraint in these cases is to allow these restraints to last for one year, but not longer. The second dimension deals with the scope of the product line, and in this instance the standard rule is that the employer can restrict the employee during that period from using product lines already in existence, but cannot bar the entry into new products that the defendant hopes to produce and sell. The third dimension deals with geographical scope. Here the employer can only enjoin activity in those areas where he has a particular establishment, but not into any area in which the employer hopes to expand its business. In general the protection of the employer is the strongest when the covenant is sought to protect trade secrets. But there are limits:

> [A] new employer need not actively induce an employee to quit her job. Nor must a new employer even have knowledge of the covenant in the employee's previous contract, when it hires her, in order to incur liability for tortious interference with that covenant. Rather, the central question is whether, upon learning of the restrictive covenant that binds its new employee, the new employer nevertheless "engages the employee to work for him in an activity that would mean violation of the contract not to compete."

Fowler v. Printers II, Inc., 598 A.2d 794, 804 (Md. App. 1991) (quoting RST §768, cmt. *i*).

Note that the inducement of breach of contract case does not require that the defendant

use illegal means to disrupt the plaintiff's contractual relationships with its employees. See CRST Van Expedited, Inc. v. Werner Enters., Inc., 479 F.3d 1099 (9th Cir. 2007); Redfearn v. Trader Joe's Co., 20 Cal. App. 5th 989 (Ct. App. 2018). In industries like computer software development, in which labor turnover is high, does it work to the long-term advantage of all firms to allow workers to switch jobs freely save in exceptional circumstances?

**4. *Covenants Not to Compete in the Sale of Businesses.*** Although less common than in employment contexts, covenants not to compete play a critical role in the sale of a business. The fear of the buyer is that the seller will reenter the old business with a new firm and rely on its reputation and contacts to take back much of the business that has just been sold, so that the business could not be sold without some extensive protection against reentry that goes far beyond that allowed in employment cases. Thus in Nordenfelt v. Maxim Nordenfelt Guns and Ammunition [1894] AC 535, Nordenfelt, the seller, agreed that his firm "would not make guns or ammunition anywhere in the world, and would not compete with Maxim in any way for a period of 25 years." He received £200,000 as fair compensation for the sale. Lord Macnaghten upheld that restraint in these words:

> Now, in the present case it was hardly disputed that the restraint was reasonable, having regard to the interests of the parties at the time when the transaction was entered into. It enabled Mr. Nordenfelt to obtain the full value of what he had to sell; without it the purchasers could not have been protected in the possession of what they wished to buy. Was it reasonable in the interests of the public? It can hardly be injurious to the public, that is, the British public, to prevent a person from carrying on a trade in weapons of war abroad. But apart from that special feature in the present case, how can the public be injured by the transfer of a business from one hand to another? If a business is profitable there will be no lack of persons ready to carry it on. In this particular case the purchasers brought in fresh capital, and had at least the opportunity of retaining Mr. Nordenfelt's services. But then it was said there is another way in which the public may be injured. Mr. Nordenfelt has "committed industrial suicide," and as he can no longer earn his living at the trade which he has made peculiarly his own, he may be brought to want and become a burden to the public. My Lords, this seems to me to be very far-fetched. Mr. Nordenfelt received over £200,000 for what he sold. He may have got rid of the money. I do not know how that is. But even so, I would answer the argument in the words of Tindal C.J.: "If the contract is a reasonable one at the time it is entered into we are not bound to look out for improbable and extravagant contingencies in order to make it void."

**5. *The Blue Pencil Doctrine.*** Most noncompete agreements contain multiple covenants that relate to the scope and enforcement of these agreements. In some cases, the courts will find one clause of the agreement unacceptable but the remainder of the contract appropriate. For example, it may be illegal for an agreement not to compete to oust the jurisdiction of the courts. See Rose & Frank Co. v. JR Crompton & Sons, [1924] UKHL 2. Similar issues can arise with choice of law provisions. See Cynosure LLC v. Reveal Lasers LLC, No. CV 22-11176-PBS, 2022 WL 18033055 (D. Mass. Nov. 9, 2022), upholding the use of the Delaware forum for dealing with covenants not to compete in Massachusetts.

But it is possible to excise that clause and then enforce the rest of the agreement if it meets the applicable standard. There are always questions whether the clause struck down renders the agreement unintelligible, at which point it should not be enforced. But even on the substantive provisions, it is often possible to cut down a substantive provision that says "the employer agrees not to compete with the employer in its home town, and throughout the rest of the county." The second clause can be struck and the first clause enforced.

In recent years, there has been a strong challenge against noncompetes, which is marked by the effort of the FTC to replace the rule of reason approach with a rule of per se illegality.

## *FTC Announces Rule Banning Noncompetes*

Press Release, FTC (Apr. 23, 2024)

Today, the Federal Trade Commission issued a final rule to promote competition by banning noncompetes nationwide, protecting the fundamental freedom of workers to change jobs, increasing innovation, and fostering new business formation.

"Noncompete clauses keep wages low, suppress new ideas, and rob the American economy of dynamism, including from the more than 8,500 new startups that would be created a year once noncompetes are banned," said FTC Chair Lina M. Khan. "The FTC's final rule to ban noncompetes will ensure Americans have the freedom to pursue a new job, start a new business, or bring a new idea to market."

The FTC estimates that the final rule banning noncompetes will lead to new business formation growing by 2.7% per year, resulting in more than 8,500 additional new businesses created each year. The final rule is expected to result in higher earnings for workers, with estimated earnings increasing for the average worker by an additional $524 per year, and it is expected to lower health care costs by up to $194 billion over the next decade. In addition, the final rule is expected to help drive innovation, leading to an estimated average increase of 17,000 to 29,000 more patents each year for the next 10 years under the final rule.

Noncompetes are a widespread and often exploitative practice imposing contractual conditions that prevent workers from taking a new job or starting a new business. Noncompetes often force workers to either stay in a job they want to leave or bear other significant harms and costs, such as being forced to switch to a lower-paying field, being forced to relocate, being forced to leave the workforce altogether, or being forced to defend against expensive litigation. An estimated 30 million workers — nearly one in five Americans — are subject to a noncompete.

Under the FTC's new rule, existing noncompetes for the vast majority of workers will no longer be enforceable after the rule's effective date. Existing noncompetes for senior executives — who represent less than 0.75% of workers — can remain in force under the FTC's final rule, but employers are banned from entering into or attempting to enforce any new noncompetes, even if they involve senior executives. Employers will be required to provide notice to workers other than senior executives who are bound by an existing noncompete that they will not be enforcing any noncompetes against them. . . .

In the final rule, the Commission has determined that it is an unfair method of competition, and therefore a violation of Section 5 of the FTC Act, for employers to enter into noncompetes with workers and to enforce certain noncompetes.

The Commission found that noncompetes tend to negatively affect competitive conditions in labor markets by inhibiting efficient matching between workers and employers. The Commission also found that noncompetes tend to negatively affect competitive conditions in product and service markets, inhibiting new business formation and innovation. There is also evidence that noncompetes lead to increased market concentration and higher prices for consumers.

### Alternatives to Noncompetes

The Commission found that employers have several alternatives to noncompetes that still enable firms to protect their investments without having to enforce a noncompete.

Trade secret laws and non-disclosure agreements (NDAs) both provide employers with well-established means to protect proprietary and other sensitive information. Researchers estimate that over 95% of workers with a noncompete already have an NDA.

The Commission also finds that instead of using noncompetes to lock in workers, employers that wish to retain employees can compete on the merits for the worker's labor services by improving wages and working conditions.

## NOTES

**1.** ***The FTC Takes Action.*** Behind this press release lies a comprehensive report, "The Non-Compete Rule," of some 570 pages, https://www.ftc.gov/system/files/ftc_gov/pdf/noncompete-rule.pdf. It seeks to lay out the rationale for the new development. That report was signed by Lina Khan and the two other Democrats on the Committee, with dissents by two Republican members, whose brief comments stressed their concern that the Federal Trade Commission did not have the requisite power under Sections 5 and 6(g) of the FTC Act. The former prohibits unfair methods of competition, and the latter allows the FTC to promulgate rules and regulations to carry out the provisions of the FTC. The new approach replaces an earlier 2015 FTC approach that followed the rule of reason approach under Section 1 of the Sherman Act, whereas the current approach asks whether the methods involved go beyond competition on the merits. This issue is still a matter of much contention but is more a matter of administrative law than of tort law. See Complaint, Ryan, LLC v. FTC, No. 3:24-CV-986 (N.D. Tex, filed Apr. 4, 2024), https://files.lbr.cloud/public/2024-04/Ryan.pdf?VersionId=0yu9qPkQFUOJ5XXAaZvtgXK4EzWprx7N (characterizing the rule as "retroactively invalidat[ing] 30 million employment contracts and preempt[ing] the regulatory regimes of at least 46 states").

**2.** ***Empirical Research.*** The FTC points to a large number of empirical studies that validate its contentions. There is strong evidence that the relaxation of these covenants not to compete may make sense in certain industries, such as the tech industry, where all firms face the same prisoner's dilemma. If they cannot coordinate their efforts, then each firm will be better off keeping its employees under a noncompete when other firms do the same. But if the state bans or limits these noncompetes, the empirical claim is that all tech firms benefit more from a market in which there is the free movement of labor than one more tightly bound under the rule. See Ronald J. Gilson, The Legal Infrastructure of High Technology Industrial Districts: Silicon Valley, Route 128, and Covenants Not to Compete, 74 N.Y.U. L. Rev. 575, 585–86 (1999):

> Voluntary spillovers occur through such mechanisms as joint ventures and cooperative supply relationships in which a mutual exchange of technology between a customer and a supplier takes place. The benefits of such knowledge spillovers then accrue to the suppliers' other customers. Involuntary spillovers occur through the movement of workers to new employers. Tacit information associated with an employers' technology is embedded in the human capital of its employees. When an employee changes jobs, that tacit information is available to the new employer. These knowledge spillovers supercharge the innovative capacity of the district with renewed agglomeration economies, facilitating the development of new technologies that create a new industrial life cycle.

Yet, especially with trade secrets, it appears that many employers in different industries do not rate tacit knowledge spillovers as highly as Gilson, for the loss of a customer list could result in the immediate loss of customers, and in this regard the tech industry does not appear to have any distinct features to set it apart from other trades. Hence the desirability of these noncompetes may well be industry and clause dependent. The arguments thus range broadly. For a sample, see Eric Posner, Antitrust and Labor Markets: Reply to Richard Epstein, 15 N.Y.U. J.L. & Liberty 389 (2022); for a two-part response, see Richard A. Epstein,

The Application of Antitrust Law to Labor Markets — Then and Now, 15 N.Y.U. J.L. & Liberty 327 (2022); Richard A. Epstein, Antitrust Overreach in Labor Markets: A Response to Eric Posner, 15 N.Y.U. J.L. & Liberty 407 (2022). The Posner critique is part of a larger concern with the unappreciated antitrust difficulties in labor markets. See Eric Posner, How Antitrust Law Fails Workers (2021), which reports major wage differentials across broad swaths of industry. For a comprehensive study that cuts generally in the opposite direction, see Elena Prager & Matt Schmitt, Employer Consolidation and Wages, 111 Am. Econ. Rev. 397 (2021), which finds some negative effects on wages in high-wage workers, e.g., nurses and professionals in the hospital market, but not with general workers, e.g., clerks and custodial, whose skills can easily move across different industrial classifications for product markets.

These general disputes over employer monopoly power spill over into disputes over the power noncompetes. One question is whether the very narrow exception for senior employees is broad enough to cover the full range of desirable uses of these covenants. This proved a powerful sticking point when Governor Kathy Hochul vetoed similar legislation in New York State, Bill No. AO1278B, https://nyassembly.gov/leg/?default_fld=&leg_video=&bn=A01278&term=&Summary=Y&Actions=Y&Text=Y, chiefly because it did not respect the standard use of these covenants with the departures of senior officials.

One of the key challenges to the FTC rules is whether the substitutes offered are sufficient to protect key trade secrets. Can NDAs be as effective as noncompete clauses that stop the contact in order to reduce the slippage when workers join new firms, where it may be impossible to tell whether the new firm's new development was the result of its independent discovery, or was obtained from the employee?

**3. *Middle- and Lower Income Class Workers.*** There are also issues with the application of the new and old rules on lower- and middle-class workers. As a first approximation, these workers rarely possess distinctive services that justify the costs of running a system of restrictions. So even before the modern attack on the covenants, courts under the standard rule of reason test invalidated those that seemed unduly restrictive. The most notable example was McDonald's, who was held to task by President Biden in his push for the more vigorous enforcement of the antitrust laws against businesses generally. McDonald's claimed it had only used them to deal with movements from one franchisee to another before 2017, and never against going elsewhere.

There are, of course, reasons for this distinction. Moving to some different franchise system makes it less likely that the information acquired in the first position will be of use in the second. But the movement of outlets within the same system does pose a risk that one franchisee will invest in the training of a worker who can then be hired by a second outlet, such that the first employer subsidizes the second on a misappropriation theory similar to that in INS v. AP, *infra* at 257. The case law on this topic treats these movements as per se legal, see Continental Television, Inc. v. GTE Sylvania, Inc., 433 U.S. 36 (1977). But even before the recent developments in New York and in the FTC, "[s]even fast food chains — including Arby's, Cinnabon and McDonald's — have pledged to end so-called 'no-poaching' rules that have prevented employees from moving from one franchise to another within the same restaurant chain" in a nationwide agreement entered into by Washington State Attorney General Bob Ferguson. Jackie Wattles, 7 Fast Food Chains Agree to End "No-Poach" Rules (CNN Bus. July 12, 2018), https://money.cnn.com/2018/07/12/news/companies/no-poach-fast-food-industry-wages-attorneys-general/index.html.

# SECTION D. INTENTIONAL INTERFERENCE WITH PROSPECTIVE ADVANTAGE

## *Tarleton v. M'Gawley*

170 Eng. Rep. 153 (K.B. 1793)

This was a special action on the case. The declaration stated that the plaintiffs were possessed and owners of a certain ship called the *Tarleton*, which at the time of committing the grievance was lying at Calabar on the coast of Africa, under the command of Fairweather. That the ship had been fitted out at Liverpool with goods proper for trading with the natives of that coast for slaves and other goods. That also before the [sic] committing the grievance Fairweather had sent a smaller vessel called the *Bannister* with a crew on board, under the command of one Thomas Smith, and loaded with goods proper for trading with the natives, to another part of the said coast called Cameroon, to trade with the natives there. That while the last-mentioned ship was lying off Cameroon, a canoe with some natives on board came to the same for the purpose of establishing a trade, and went back to the shore, of which defendant had notice. And that he well knowing the premises, but contriving and maliciously intending to hinder and deter the natives from trading with the said Thomas Smith, for the benefit of the plaintiffs, with force and arms, fired from a certain ship called the *Othello*, of which he was master and commander, a certain cannon loaded with gunpowder and shot at the said canoe, and killed one of the natives on board the same. Whereby the natives of the said coast were deterred and hindered from trading with the said T. Smith for the benefit, &c. and plaintiffs lost their trade.

The plaintiffs called Thomas Smith, who proved the facts stated in the declaration; and further, that the defendant had declared the natives owed him a debt, and that he would not suffer any ship to trade with them until that was paid; in pursuance of which declaration he committed the act complained of by the plaintiffs. On his cross-examination he admitted that by the custom of that coast no Europeans can trade until a certain duty has been paid to the king of the country for his licence, and that no such duty had been paid, or licence obtained by the captain of the plaintiff's vessel.

Law, for the defendant, contended that the plaintiffs being engaged in a trade which by the law of that country was illicit, could not support an action for an interruption of such illicit commerce, and compared this case to an action brought for interrupting a plaintiff in his endeavours to smuggle goods into this country, or alarming the owner of a house which the plaintiff was about to break into. He also objected that this act of the defendant amounted to a felony, and therefore could not be made the ground of a civil action, but he did not lay much stress on this objection.

Lord Kenyon. This action is brought by the plaintiffs to recover a satisfaction for a civil injury which they have sustained. The injury complained of is, that by the improper conduct of the defendant the natives were prevented from trading with the plaintiffs. The whole of the case is stated on the record, and if the parties desire it, the opinion of the Court may hereafter be taken whether it will support an action. I am of opinion it will. This case has been likened to cases which it does not at all resemble. It has been said that a person engaged in a trade violating the law of the country cannot support an action against another for hindering him in that illegal traffick. That I entirely accede to, but it does not apply to this case. This is a foreign law; the act of trading is not itself immoral, and a jus positivum is not binding on foreigners. The king of the country and not the defendant should have executed that law. Had this been an

accidental thing, no action could have been maintained, but it is proved that the defendant had expressed an intention not to permit any to trade, until a debt due from the natives to himself was satisfied. If there was any Court in that country to which he could have applied for justice he might have done so, but he had no right to take the law into his own hands.

The plaintiffs had a verdict, and the parties agreed to refer the damages to arbitration.

*Note* [in original Report].—In the beginning of the cause the plaintiffs' counsel proposed asking the witnesses whether some of the negroes did not assign their fear of the defendant as a reason for not trading with the plaintiffs, but Lord Kenyon said that no declaration of the negroes could be received in evidence.

## RESTATEMENT OF THE LAW (SECOND) OF TORTS

### §766B. Intentional Interference with Prospective Contractual Relation

One who intentionally and improperly interferes with another's prospective contractual relation (except a contract to marry) is subject to liability to the other for the pecuniary harm resulting from loss of the benefits of the relation, whether the interference consists of

(a) inducing or otherwise causing a third person not to enter into or continue the prospective relation or

(b) preventing the other from acquiring or continuing the prospective relation.

***i. Actor's Knowledge of Other's Contract***. . . . The interference with the other's prospective contractual relation is intentional if the actor desires to bring it about or if he knows that the interference is certain or substantially certain to occur as a result of his action. . . .

The interference, however, must also be improper. The factors to be considered in determining whether an interference is improper are stated in §767. One of them is the actor's motive and another is the interest sought to be advanced by him. Together these factors mean that the actor's purpose is of substantial significance. . . . If the means used is innately wrongful, predatory in character, a purpose to produce the interference may not be necessary. . . .

## RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM

### §18. Interference with Economic Expectation

A defendant is subject to liability for interference with economic expectation if:

(a) the plaintiff had a reasonable expectation of economic benefit from a relationship with a third party;

(b) the defendant committed an independent and intentional legal wrong;

(c) the defendant intended to interfere with the plaintiff's expectation;

(d) the defendant's wrongful conduct caused the expectation to fail; and

(e) the plaintiff suffered economic loss as a result.

***b. Independently Wrongful Acts.*** To support liability under this Section, the defendant's conduct must have been wrongful in some way recognized elsewhere by the law. . . .

The requirement of wrongfulness is supported by two general considerations. First, it helps confine liability under this Section to cases in which liability is best justified. . . .

Second, the requirement of wrongfulness provides potential defendants with clear guidance about where their exposure to liability starts and stops. . . .

## *Korea Supply Co. v. Lockheed Martin Corp.*

9 Cal. 4th 1134 (2003)

Moreno, J. This case addresses what claims and remedies may be pursued by a plaintiff who alleges a lost business opportunity due to the unfair practices of a competitor.

. . . [W]e address whether, to state a claim for interference with prospective economic advantage, a plaintiff must allege that the defendant specifically intended to interfere with the plaintiff's prospective economic advantage. We conclude that a plaintiff need not plead that the defendant acted with the specific intent to interfere with the plaintiff's business expectancy in order to state a claim for this tort. We affirm the judgment of the Court of Appeal on this issue.

### I.

. . . Plaintiff KSC is a corporation engaged in the business of representing manufacturers of military equipment in transactions with the Republic of Korea. In the mid–1990's, the Republic of Korea solicited bids for a SAR [synthetic aperture radar] system for use by its military. KSC represented MacDonald Dettwiler, a Canadian company, in its bid to obtain the contract award. KSC expected a commission of 15 percent of the contract price, or over $30 million, if MacDonald Dettwiler were awarded the contract.

In June 1996, the Korean Ministry of Defense announced that Loral, an American competitor of the Canadian company MacDonald Dettwiler, was awarded the contract, despite the fact that MacDonald Dettwiler's bid was about $50 million lower and that the project management office of the Korean Defense Intelligence Command had determined that MacDonald Dettwiler's equipment was far superior to Loral's system. The Ministry of Defense explained that the decision to award Loral the contract was based on a suggestion that the United States government would not be favorably disposed to share intelligence information with the Republic of Korea if the latter selected a Canadian supplier.

Beginning in October 1998, major news publications in the Republic of Korea revealed that an internal investigation had established that the SAR contract was awarded to Loral as a result of bribes and sexual favors, rather than pressure from the United States government. Loral's agent for the procurement of the SAR contract, defendant Linda Kim, had bribed two Korean military officers. In addition, Ms. Kim had extended bribes and sexual favors to the Minister of National Defense, the ultimate decision maker with respect to the award of the SAR contract. Ms. Kim reportedly received approximately $10 million in commission from Loral, an amount that exceeded the maximum established by the Foreign Corrupt Practices Act (15 U.S.C. §78dd–2) and foreign military sales policies and regulations. As a result of the internal investigation by the Republic of Korea, several persons were imprisoned, including high-ranking Korean military officers. Ms. Kim herself was indicted in absentia; she avoided imprisonment because she resides in the United States and refuses to travel to the Republic of Korea.

Upon learning of these alleged reasons for the award of the SAR contract to Loral, KSC commenced the present action on May 5, 1999. . . . KSC alleged that defendants "conspired, knowingly and intentionally to induce and did knowingly and intentionally induce the Republic of Korea, through its authorized agencies, to award the SAR contract to Loral instead of MacDonald Dettwiler by employing wrongful means including bribes and sexual favors." . . . "In securing the contract by wrongful means, Loral acted with full knowledge of the commission relationship between plaintiff and MacDonald Dettwiler and knowing that its interference with the award of the contract . . . would cause plaintiff severe loss."

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"Defendant Lockheed Martin has been the beneficiary of the illegal Loral–Kim conduct and to that extent has been unjustly enriched."

The . . . complaint asserts three causes of action: (1) conspiracy to interfere with prospective economic advantage, (2) intentional interference with prospective economic advantage, and (3) unfair competition pursuant to Business and Professions Code section 17200. For its unfair competition claim, KSC sought disgorgement to it of the profits realized by Lockheed Martin on the sale of the SAR to Korea. For the tort claims, KSC sought damages for the loss of its expected compensation from MacDonald Dettwiler.

Lockheed Martin, joined by Ms. Kim, generally demurred to all counts. The trial court sustained the demurrer without leave to amend,. . . . The Court of Appeal reversed the trial court's judgment in full, finding that plaintiff had sufficiently stated causes of action for unfair competition and for intentional interference with prospective economic advantage.

Lockheed Martin sought review [of the Court of Appeal's] holding that the tort of intentional interference with prospective economic advantage does not require plaintiff to plead that defendant acted with the specific intent to interfere with plaintiff's business expectancy. We granted review. . . .

### III.

Lockheed Martin argues that KSC fails to state a claim for intentional interference with prospective economic advantage because it has not shown that Lockheed Martin acted with the specific intent to disrupt KSC's business relationship. KSC counters that a plaintiff need only show that the defendant acted with the knowledge that its wrongful acts were substantially certain to disrupt plaintiff's business expectancy. We conclude that the tort of intentional interference with prospective economic advantage does not require a plaintiff to plead that the defendant acted with the specific intent, or purpose, of disrupting the plaintiff's prospective economic advantage. Instead, to satisfy the intent requirement for this tort, it is sufficient to plead that the defendant knew that the interference was certain or substantially certain to occur as a result of its action.

### A.

We first articulated the elements of the tort of intentional interference with prospective economic advantage in *Buckaloo v. Johnson* (1975) 14 Cal.3d 815, 827, 122 Cal. Rptr. 745, 537 P.2d 865 (*Buckaloo*). These elements are usually stated as follows: "'(1) an economic relationship between the plaintiff and some third party, with the probability of future economic benefit to the plaintiff; (2) the defendant's knowledge of the relationship; (3) intentional acts on the part of the defendant designed to disrupt the relationship; (4) actual disruption of the relationship; and (5) economic harm to the plaintiff proximately caused by the acts of the defendant.'" . . .

. . . [A] plaintiff seeking to recover damages for interference with prospective economic advantage must plead and prove as part of its case-in-chief that the defendant's conduct was "wrongful by some legal measure other than the fact of interference itself." . . .

### B.

Having clarified the required elements, we now consider the intent requirement of this tort. The question is whether a plaintiff must plead and prove that the defendant engaged in wrongful acts *with the specific intent* of interfering with the plaintiff's business expectancy. We conclude that specific intent is not a required element of the tort of interference with prospective economic advantage. While a plaintiff may satisfy the intent requirement by pleading specific intent, i.e., that the defendant desired to interfere with the plaintiff's prospective

economic advantage, a plaintiff may alternately plead that the defendant knew that the interference was certain or substantially certain to occur as a result of its action.

Lockheed Martin argues that specific intent is an established element of this tort. It contends that to satisfy the tort's third element—intentional wrongful acts designed to disrupt the plaintiff's relationship with its benefactor—a plaintiff must allege that the defendant purposely sought the disruption. It asserts that the inclusion of the word "designed" in the typical formulation of the third element is evidence that a plaintiff is required to plead specific intent. We disagree. . . .

Contrary to Lockheed Martin's assertion, the inclusion of the word "designed" in the third element of the tort does not necessarily mean that this tort contains a specific intent requirement. Our analysis of the intent requirement for the tort of intentional interference with contract in *Quelimane Company, Inc. v. Stewart Title Guaranty Company* (1998) 19 Cal.4th 26, 77 Cal. Rptr.2d 709, 960 P.2d 513 (*Quelimane*) is instructive. In *Quelimane*, we articulated the elements of this tort, stating that the third element requires a plaintiff to plead the "'defendant's intentional acts designed to induce a breach or disruption of the contractual relationship.'" . . . Notwithstanding the presence of the word "designed," we found that this tort did not require a plaintiff to plead that the defendant acted with the specific intent to interfere. . . .

[Discussion of RST §766 ("Intentional Interference with Performance of Contract by Third Person"), *supra*, and RST §766B ("Intentional Interference with Prospective Contractual Relation"), *supra*, and commentary for each that includes "know[ledge] that the interference is certain or substantially certain to occur as a result of his action."]

Based on our reading of the Restatement and our discussion in *Quelimane* of the intent requirement, we reject Lockheed Martin's argument that the tort of intentional interference with prospective economic advantage contains a requirement that a plaintiff plead and prove that the defendant acted with the specific intent, purpose, or design to interfere with the plaintiff's prospective advantage. Instead, we agree with the Restatement that it is sufficient for the plaintiff to plead that the defendant "[knew] that the interference is certain or substantially certain to occur as a result of his action." (Rest.2d Torts, §766B, com. d, p. 22.)

### C.

We caution that although we find the intent requirement to be the same for the torts of intentional interference with contract and intentional interference with prospective economic advantage, these torts remain distinct. . . .

We note initially that even though these two torts are distinct, some plaintiffs may be able to state causes of action for both torts. As we stated in *Buckaloo*, "the tort of interference with contract is merely a species of the broader tort of interference with prospective economic advantage." . . . In the present case, KSC's claim was appropriately stated as one for interference with prospective economic advantage. KSC did not allege in its complaint that it had a contractual agreement with MacDonald Dettwiler. KSC merely alleged that it had an economic expectancy in that it was acting as MacDonald Dettwiler's broker and it expected a commission if the contract was awarded to MacDonald Dettwiler. KSC nowhere pleads that this expectancy amounted to an enforceable contract.

Moreover, the existence of a contract does not mean that a plaintiff's claim must be brought exclusively as one for interference with contract. In *Buckaloo*, we concluded that the tort of interference with prospective economic advantage "is considerably more inclusive than actions based on contract or interference with contract, and thus is not dependent on the existence of a valid contract." Thus, a plaintiff who believes that he or she has a contract but who recognizes that the trier of fact might conclude otherwise might bring claims for both torts so that in the event of a finding of no contract, the plaintiff might prevail on a claim for

interference with prospective economic advantage. In the present case, even if KSC could have alleged a contractual relationship with MacDonald Dettwiler, its claim was properly brought as one for interference with prospective economic advantage. As we explain below, however, a plaintiff that chooses to bring a claim for interference with prospective economic advantage has a more rigorous pleading burden since it must show that the defendant's conduct was independently wrongful.

. . . [T]he distinction between these two torts is found in the independent wrongfulness requirement of the tort of interference with prospective economic advantage. We stated in *Quelimane:* "Because interference with an existing contract receives greater solicitude than does interference with prospective economic advantage, it is not necessary that the defendant's conduct be wrongful apart from the interference with the contract itself. . . . Intentionally inducing or causing a breach of an existing contract is . . . a wrong in and of itself. Because this formal economic relationship does not exist and damages are speculative when remedies are sought for interference in what is only prospective economic advantage, [we have previously] concluded that some wrongfulness apart from the impact of the defendant's conduct on that prospect should be required." . . .

. . . . An act is not independently wrongful merely because defendant acted with an improper motive. . . . The tort of intentional interference with prospective economic advantage is not intended to punish individuals or commercial entities for their choice of commercial relationships or their pursuit of commercial objectives, unless their interference amounts to independently actionable conduct. . . . We conclude, therefore, that an act is independently wrongful if it is unlawful, that is, if it is proscribed by some constitutional, statutory, regulatory, common law, or other determinable legal standard. . . .

Here, KSC has clearly satisfied the independent wrongfulness requirement. In its complaint, KSC alleged that defendant Kim, as an agent for Loral, engaged in bribery and offered sexual favors to key Korean officials in order to obtain the contract from the Republic of Korea. Under the Foreign Corrupt Practices Act, it is unlawful to pay or offer money or anything of value to a foreign official for the purposes of influencing any act or decision of the foreign official, or to induce the foreign official to use his or her influence with a foreign government to affect or influence any act or decision of the government. In addition, the complaint alleges that the commissions paid by Loral to Kim exceeded the maximum allowable amounts established by the Foreign Corrupt Practices Act. The complaint thus clearly alleges that defendants engaged in unlawful behavior in order to secure the SAR contract. KSC has, therefore, sufficiently alleged that defendants' acts, in addition to interfering with KSC's business expectancy, were wrongful in and of themselves.

**D.**

It is this independent wrongfulness requirement that makes defendants' interference with plaintiff's business expectancy a tortious act. Because we have determined that the act of interference with prospective economic advantage is not tortious in and of itself, the requirement of pleading that a defendant has engaged in an act that was independently wrongful distinguishes lawful competitive behavior from tortious interference. Such a requirement "sensibly redresses the balance between providing a remedy for predatory economic behavior and keeping legitimate business competition outside litigative bounds." . . .

The independent wrongfulness requirement also differentiates California law from that of other states and the Restatement Second of Torts . . . [which] require a plaintiff only to plead that the defendant's interference was improper, and not that the interference was independently unlawful. . . .

. . .

F.

An actor engaging in unlawful conduct with the knowledge that its actions are certain or substantially certain to interfere with a party's business expectancy should be held accountable. Liability for such actions, which are independently wrongful, should not turn on the subjective intent of the defendant.

We conclude that the Court of Appeal correctly determined that to state a claim for intentional interference with prospective economic advantage, a plaintiff need not plead that the defendant acted with the specific intent to interfere with the plaintiff's business expectancy. Further, we agree that plaintiff in this case has sufficiently pled that defendants acted with the required intent, that is, the knowledge that its actions were certain or substantially certain to interfere with plaintiff's business expectancy.

IV.

. . . [W]e affirm the judgment of the Court of Appeal with respect to its determination that plaintiff has stated a cause of action for the tort of interference with prospective economic advantage. The present case is remanded to the Court of Appeal for proceedings consistent with this opinion.

## NOTES

**1.** ***Interference with Prospective Advantage Versus Inducement of Breach of Contract.*** The protection afforded the plaintiffs in *Tarleton* and *Korea Supply Co*. is both narrower and broader than that granted in Lumley v. Gye. It is narrower in that prospective advantage is protected only against interference by means that are unlawful in themselves, in this case the use of force against the natives. But it is broader in that it protects not only the promisee who may have claims against the promisor under an existing contract, but also the promisee who might not have a viable contract-based claim (for instance, because the contract is terminable at will). The cause of action also protects a party who was never able to form a contract in the first place. Why allow this separate cause of action when the plaintiff's potential customers are protected by a wide array of other tort claims? In evaluating the plaintiff's case in *Tarleton*, should it make a difference whether the customers suffer physical injury or only the loss of a bargain? One frequent justification for the result in *Tarleton* is that the trader's suit helps vindicate the economic interests of potential customers who might be reluctant to incur heavy litigation costs to recover for small economic losses, especially if their interests are numerous and diffuse.

**2.** ***Unlawful Means and Prospective Advantage.*** While the facts in *Tarleton* are both novel and dramatic, its underlying principle has a long common law lineage. In Keeble v. Hickeringill, 103 Eng. Rep. 1127, 1128 (Q.B. 1706) (reported K.B. 1809), the plaintiff used decoy ducks to attract wild fowl to his meadow for the purpose of capturing and selling them. The defendant, who operated a rival duck decoy of his own in the neighborhood, repeatedly discharged guns nearby, driving away the ducks that landed in the plaintiff's meadow. In affirming a verdict for plaintiff, Holt, C.J., said:

> [I]f Mr. Hickeringill had set up another decoy on his own ground near the plaintiff, no action would lie because he had as much liberty to make and use a decoy as the plaintiff. . . . One schoolmaster sets up a new school to the damage of an antient school, and thereby the scholars are allured from the old school to come to his new. (The action was held there not to lie.) But

suppose Mr. Hickeringill should lie in the way with his guns, and fright the boys from going to school, and their parents would not let them go thither; sure the schoolmaster might have an action for the loss of his scholars.

Holt's brief remarks about the "antient school" contain this bellwether principle of the law: The maxim "prior in time is higher in right" used to establish title to land and chattels has no application to competitive injury. The incumbent may enjoy a "first mover" advantage but gets no legal protection against the subsequent entrant so long as the second player does not resort to illegal means. Indeed, one reason why interference with trade proved crucial in *Keeble* was that the plaintiff did not gain possession of the ducks solely because they alighted on his pond but instead because the plaintiff had set up decoys to trap them. The theory of trade interference worked, moreover, solely because the defendant was the plaintiff's "direct competitor." What result if the defendant shot his guns to kill and capture the ducks, knowing he might frighten them away? Or if defendant is a modern animal rights activist determined to protect all wildlife from needless slaughter? What other means unlawful in themselves are sufficient to support the plaintiff's action? In Evenson v. Spaulding, 150 F. 517, 522 (9th Cir. 1907), the plaintiffs were Iowa manufacturers of high-class buggies and wagons who sold their product in the state of Washington through salesmen and agents. The defendants were employees of an association of Washington buggy manufacturers; they dogged the plaintiffs' salesmen whenever they tried to sell their wagons and buggies to local customers, usually on a public highway. The court recognized that the defendants had the right to compete with the plaintiffs for sales to local customers, but held that the defendants' conduct, and their "policy of molestation," exceeded the permissible limits of competition, "by breaking in on conversations, making false representations as to the nature of the appellees' goods . . . and other offensive acts."

In Reeves v. Hanlon, 95 P.3d 513, 515–16 (Cal. 2004), Hanlon and Greene left Reeves's immigration firm "without notice or warning," after which it was alleged that they "improperly persuaded plaintiffs' employees to join H&G, personally solicited plaintiffs' clients to discharge plaintiffs and to instead obtain services from H&G, misappropriated plaintiffs' trade secrets, destroyed computer files and data, and withheld plaintiffs' property, including a corporate car." Baxter, J., held that

> inducing the termination of an at-will employment relation may be actionable under the standard applicable to claims for intentional interference with prospective economic advantage. Accordingly, to recover for a defendant's interference with an at-will employment relation, a plaintiff must plead and prove that the defendant engaged in an independently wrongful act — i.e., an act "proscribed by some constitutional, statutory, regulatory, common law, or other determinable legal standard."

**3.** ***"Independent Wrongfulness" Requirement and the Restatements.*** *Korea Supply Co.* makes a point of exposing the daylight between California's independent wrongfulness requirement and that in RST §766B, *supra* at 238. See *Korea Supply Co.*, 29 Cal. 4th at 1160–61:

> Unlike California, the Restatement Second of Torts does not require a plaintiff to plead that a defendant engaged in an independently wrongful act in order to show "improper" interference. Instead, a general intent plus an actor's motive or purpose to interfere is enough to subject a defendant to liability under the Restatement. In the absence of an independent wrongfulness requirement, a purpose to interfere with the plaintiff's business expectancy suffices to distinguish actionable conduct from behavior that is merely competitive, and therefore privileged. . . .
>
> Thus, while California does follow the Restatement's general intent requirement, California law adheres to a narrower interpretation of what conduct is improper under this tort. . . .

> California has required plaintiffs to show that a defendant has engaged in an independently, or inherently, wrongful act. Under this requirement, a defendant's motive or purpose is relevant only to the extent that it renders the defendant's conduct unlawful. . . .

The Third Restatement embraces this position. See RTT: LEH §18, comment *b*, *supra* at 238 ("to support liability under this section, the defendant's conduct must have been wrongful in some way recognized elsewhere by the law."). It does so to limit liability. Was requiring the act to be illegal unto itself necessary to, in the words of the Third Restatement, "confine liability" and "provide potential defendants with clear guidance"? *Id*. Recall Note 1, *supra* at 243, noting how *Tarleton* already created a narrow standard.

Finally, when paired with the wrongfulness requirement, does the intent requirement's broad scope still allow for arguably "indirect" victims like *Korea Supply Co*.? The Restatement seems to think so. See RTT: LEH §18, comment *e* ("The defendant need not know the identity of the party whose expectation will be disrupted. It is enough if the defendant anticipates disruption to the expectations of a definite party, known by name or not.").

## SECTION E. UNFAIR COMPETITION

### *Mogul Steamship Co. v. McGregor, Gow & Co.*

23 Q.B.D. 598 (1889), affirmed [1892] A.C. 25

Bowen, L.J. We are presented in this case with an apparent conflict or antinomy between two rights that are equally regarded by the law—the right of the plaintiffs to be protected in the legitimate exercise of their trade, and the right of the defendants to carry on their business as seems best to them, provided they commit no wrong to others. The plaintiffs complain that the defendants have crossed the line which the common law permits; and inasmuch as, for the purposes of the present case, we are to assume some possible damage to the plaintiffs, the real question to be decided is whether, on such an assumption, the defendants in the conduct of their commercial affairs have done anything that is unjustifiable in law. The defendants are a number of shipowners who formed themselves into a league or conference for the purpose of ultimately keeping in their own hands the control of the tea carriage from certain Chinese ports, and for the purpose of driving the plaintiffs and other competitors from the field. In order to succeed in this object, and to discourage the plaintiffs' vessels from resorting to those ports, the defendants during the "tea harvest" of 1885 combined to offer to the local shippers very low freights, with a view of generally reducing or "smashing" rates, and thus rendering it unprofitable for the plaintiffs to send their ships thither. They offered, moreover, a rebate of 5 per cent. to all local shippers and agents who would deal exclusively with vessels belonging to the Conference, and any agent who broke the condition was to forfeit the entire rebate on all shipments made on behalf of any and every one of his principals during the whole year—a forfeiture of rebate or allowance which was denominated as "penal" by the plaintiffs' counsel. It must, however, be taken as established that the rebate was one which the defendants need never have allowed at all to their customers. It must also be taken that the defendants had no personal ill-will to the plaintiffs, nor any desire to harm them except such as is involved in the wish and intention to discourage by such measures the plaintiffs from sending rival vessels to such ports. . . . It is to be observed with regard to all these acts of which complaint is made that they were acts that in themselves could not be said to be illegal unless made so by the object with which, or the combination in the course of which, they were done; and that in reality what is complained of is the pursuing of trade competition to a length

"Judical Politeness"

**Charles Synge Christopher Bowen, Baron Bowen (1835-1894), as caricatured in *Vanity Fair* in 1892. Bowen was a graduate of Balliol College, where he excelled in the classics. He was called to the bar at Lincoln's Inn in 1861. After early disappointments he became a distinguished barrister who was called to the bench in 1879 but made his mark on the Court of Appeal in 1882, where many of his judgments, including Edgington v. Fitzmaurice, *supra* Chapter 3, at 171, The Moorcock, and Carlill v. Carbolic Smoke Ball Co., are still regarded as classics of the legal literature. He was appointed to the House of Lords, but died before in 1894 just as his service began.**

*Source: Wikimedia Commons*

which the plaintiffs consider oppressive and prejudicial to themselves. We were invited by the plaintiffs' counsel to accept the position from which their argument started — that an action will lie if a man maliciously and wrongfully conducts himself so as to injure another in that other's trade. Obscurity resides in the language used to state this proposition. The terms "maliciously," "wrongfully," and "injure" are words all of which have accurate meanings, well known to the law, but which also have a popular and less precise signification, into which it is necessary to see that the argument does not imperceptibly slide. An intent to "injure" in strictness means more than an intent to harm. It connotes an intent to do wrongful harm. "Maliciously," in like manner, means and implies an intention to do an act which is wrongful, to the detriment of another. The term "wrongful" imports in its turn the infringement of some right. The ambiguous proposition to which we were invited by the plaintiffs' counsel still, therefore, leaves unsolved the question of what, as between the plaintiffs and defendants, are the rights of trade. For the purpose of clearness, I desire, as far as possible, to avoid terms in their popular use so slippery, and to translate them into less fallacious language wherever possible.

. . . Now, intentionally to do that which is calculated in the ordinary course of events to damage, and which does, in fact, damage another in that other person's property or trade, is actionable if done without just cause or excuse. Such intentional action when done without just cause or excuse is what the law calls a malicious wrong. . . .

. . . The acts of the defendants which are complained of here were intentional and were also calculated, no doubt, to do the plaintiffs damage in their trade. But in order to see whether they were wrongful we have still to discuss the question whether they were done without any just cause or excuse. Such just cause or excuse the defendants on their side assert to be found in their own positive right (subject to certain limitations) to carry on their own trade freely in the mode and manner that best suits them, and which they think best calculated to secure their own advantage.

What, then, are the limitations which the law imposes on a trader in the conduct of his business as between himself and other traders? There seem to be no burdens or restrictions in law upon a trader which arise merely from the fact that he is a trader, and which are not

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equally laid on all other subjects of the Crown. His right to trade freely is a right which the law recognises and encourages, but it is one which places him at no special disadvantage as compared with others. No man, whether trader or not, can, however, justify damaging another in his commercial business by fraud or misrepresentation. Intimidation, obstruction, and molestation are forbidden; so is the intentional procurement of a violation of individual rights, contractual or other, assuming always that there is no just cause for it. The intentional driving away of customers by shew of violence: Tarleton v. M'Gawley; the obstruction of actors on stage by preconcerted hissing: Clifford v. Brandon[, 170 Eng. Rep. 1183 (N.P. 1809)]; the disturbance of wild fowl in decoys by the firing of guns: Keeble v. Hickeringill[, 103 Eng. Rep. 1127 (Q.B. 1706)]; the impeding or threatening servants or workmen: Garret v. Taylor[, 79 Eng. Rep. 485 (K.B. 1620)]; the inducing persons under personal contracts to break their contracts: Bowen v. Hall; Lumley v. Gye; all are instances of such forbidden acts. But the defendants have been guilty of none of these acts. They have done nothing more against the plaintiffs than pursue to the bitter end a war of competition waged in the interest of their own trade. To the argument that a competition so pursued ceases to have a just cause or excuse when there is ill-will or a personal intention to harm, it is sufficient to reply (as I have already pointed out) that there was here no personal intention to do any other or greater harm to the plaintiffs than such as was necessarily involved in the desire to attract to the defendants' ships the entire tea freights of the ports, a portion of which would otherwise have fallen to the plaintiffs' share. I can find no authority for the doctrine that such a commercial motive deprives of "just cause or excuse" acts done in the course of trade which would but for such a motive be justifiable. So to hold would be to convert into an illegal motive the instinct of self-advancement and self-protection, which is the very incentive to all trade. To say that a man is to trade freely, but that he is to stop short at any act which is calculated to harm other tradesmen, and which is designed to attract business to his own shop, would be a strange and impossible counsel of perfection. But we were told that competition ceases to be the lawful exercise of trade, and so to be a lawful excuse for what will harm another, if carried to a length which is not fair or reasonable. The offering of reduced rates by the defendants in the present case is said to have been "unfair." This seems to assume that, apart from fraud, intimidation, molestation, or obstruction, of some other personal right in rem or in personam, there is some natural standard of "fairness" or "reasonableness" (to be determined by the internal consciousness of judges and juries) beyond which competition ought not in law to go. There seems to be no authority, and I think, with submission, that there is no sufficient reason for such a proposition. It would impose a novel fetter upon trade. The defendants, we are told by the plaintiffs' counsel, might lawfully lower rates provided they did not lower them beyond a "fair freight," whatever that may mean. But where is it established that there is any such restriction upon commerce? And what is to be the definition of a "fair freight"? It is said that it ought to be a normal rate of freight, such as is reasonably remunerative to the shipowner. But over what period of time is the average of this reasonable remunerativeness to be calculated? All commercial men with capital are acquainted with the ordinary expedient of sowing one year a crop of apparently unfruitful prices, in order by driving competition away to reap a fuller harvest of profit in the future; and until the present argument at the bar it may be doubted whether shipowners or merchants were ever deemed to be bound by law to conform to some imaginary "normal" standard of freights or prices, or that Law Courts had a right to say to them in respect of their competitive tariffs, "Thus far shalt thou go and no further." To attempt to limit English competition in this way would probably be as hopeless an endeavour as the experiment of King Canute [to turn back the tides]. . . .

**Exhibit 4.3 Is King Canute Misunderstood?**

[W]as the legendary Viking leader and 11th Century King of England so deluded to really assume he had the powers to turn back the tide? . . .

The first written account of the Canute episode appeared in Historia Anglorum (The History of the English People) by chronicler Henry of Huntingdon, who lived within 60 years of the death of Canute (1035 A.D.).

According to the story, the king had his chair carried down to the shore and ordered the waves not to break upon his land.

When his orders were ignored, he pronounced: “Let all the world know that the power of kings is empty and worthless and there is no King worthy of the name save Him by whose will heaven and earth and sea obey eternal laws,” (Historia Anglorum, ed D E Greenway). . . .

But most modern-day analogies of Canute turn Henry of Huntingdon’s account on its head. . . .

“It is often used about politicians who consider themselves so powerful they can stop the tide of something, such as rising wages—as arrogant as King Canute,” says Prof [Simon] Keynes [of the department of Anglo-Saxon, Norse and Celtic at the University of Cambridge]. . . .

*Information source: Westcott, Is King Canute Misunderstood?, BBC News, May 26, 2011*
*Image source: Hulton Archive/Getty Images*

It is urged, however, on the part of the plaintiffs, that even if the acts complained of would not be wrongful had they been committed by a single individual, they become actionable when they are the result of concerted action among several. In other words, the plaintiffs, it is contended, have been injured by an illegal conspiracy. Of the general proposition, that certain kinds of conduct not criminal in any one individual may become criminal if done by combination among several, there can be no doubt. The distinction is based on sound reason, for a combination may make oppressive or dangerous that which if it proceeded only from a single person would be otherwise, and the very fact of the combination may shew that the object is simply to do harm, and not to exercise one’s own just rights. In the application of this undoubted principle it is necessary to be very careful not to press the doctrine of illegal conspiracy beyond that which is necessary for the protection of individuals or of the public; and it may be observed in passing that as a rule it is the damage wrongfully done, and not the conspiracy, that is the gist of actions on the case for conspiracy. But what is the definition of an illegal combination? It is an agreement by one or more to do an unlawful act, or to do a lawful act by unlawful means; and the question to be solved is whether there has been any such agreement here. Have the defendants combined to do an unlawful act? Have they combined to do a lawful act by unlawful means? A moment’s consideration will be sufficient to shew that this new inquiry only drives us back to the circle of definitions and legal propositions which I have already traversed in the previous part of this judgment. The unlawful act agreed to, if any, between the defendants must have been the intentional doing of some act to

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the detriment of the plaintiffs' business without just cause or excuse. Whether there was any such justification or excuse for the defendants is the old question over again, which, so far as regards an individual trader, has been already solved. The only differential that can exist must arise, if at all, out of the fact that the acts done are the joint acts of several capitalists, and not of one capitalist only. The next point is whether the means adopted were unlawful. The means adopted were competition carried to a bitter end. Whether such means were unlawful is in like manner nothing but the old discussion which I have gone through, and which is now revived under a second head of inquiry, except so far as a combination of capitalists differentiates the case of acts jointly done by them from similar acts done by a single man of capital. But I find it impossible myself to acquiesce in the view that the English law places any such restriction on the combination of capital as would be involved in the recognition of such a distinction. If so, one rich capitalist may innocently carry competition to a length which would become unlawful in the case of a syndicate with a joint capital no larger than his own, and one individual merchant may lawfully do that which a firm or a partnership may not. What limits, on such a theory, would be imposed by law on the competitive action of a joint-stock company limited, is a problem which might well puzzle a casuist. The truth is, that the combination of capital for purposes of trade and competition is a very different thing from such a combination of several persons against one, with a view to harm him, as falls under the head of an indictable conspiracy. There is no just cause or excuse in the latter class of cases. There is such a just cause or excuse in the former. . . . Would it be an indictable conspiracy to agree to drink up all the water from a common spring in a time of drought; to buy up by preconcerted action all the provisions in a market or district in times of scarcity; to combine to purchase all the shares of a company against a coming settling-day; or to agree to give away articles of trade gratis in order to withdraw custom from a trader? May two itinerant match-vendors combine to sell matches below their value in order by competition to drive a third match-vendor from the street? . . .

In the result, I agree with Lord Coleridge, C.J., and differ, with regret, from the Master of the Rolls. The substance of my view is this, that competition, however severe and egotistical, if unattended by circumstances of dishonesty, intimidation, molestation, or such illegalities as I have above referred to, gives rise to no cause of action at common law. I myself should deem it to be a misfortune if we were to attempt to prescribe to the business world how honest and peaceable trade was to be carried on in a case where no such illegal elements as I have mentioned exist, or were to adopt some standard of judicial "reasonableness," or of "normal" prices, or "fair freights," to which commercial adventurers, otherwise innocent, were bound to conform.

In my opinion, accordingly, this appeal ought to be dismissed with costs.

[Fry, L.J., issued an opinion concurring in the judgment of Bowen, L.J.

Lord Esher, M.R., dissenting:]

It follows that the act of the defendants in lowering their freights far beyond a lowering for any purpose of trade — that is to say, so low that if they continued it they themselves could not carry on trade — was not an act done in the exercise of their own free right of trade, but was an act done evidently for the purpose of interfering with, i.e. with intent to interfere with, the plaintiffs' right to a free course of trade, and was therefore a wrongful act as against the plaintiffs' right; and as injury ensued to the plaintiffs, they had also in respect of such act a right of action against the defendants. The plaintiffs, in respect of that act, would have had a right of action if it had been done by one defendant only; they have it still more clearly when that act was done by several defendants combined for that purpose. For these reasons I come to the conclusion that the plaintiffs were entitled to judgment. The damages, if that be the correct conclusion as to the right of action, are to be ascertained. They are, in my opinion,

the difference between the freight of 25*s*., which the plaintiffs were forced to accept, and the freight they would have obtained without other interference than a legal fair competition in 1885, and damages at large for being prevented from endeavouring to earn freight from Hankow to England in subsequent years, after taking into account the probability of using their ships in some other trade. I am of opinion that the appeal should be allowed.

## NOTES

**1. *Predatory Pricing.*** *Mogul* is one of the first cases in which the defendants were sued for entering into a scheme of what is now called predatory pricing (i.e., a practice of selling below cost in the short run in the hope of obtaining monopoly gains later, after driving the competition from the market). In dealing with the legality of the practice, Bowen, L.J., did not concentrate on the social losses that predation might generate, or on the market power, if any, commanded by the defendants, which increased with the size of the group membership. Instead, he was content to show that the defendant's practices did not involve the use of forbidden means: fraud, misrepresentation, intimidation, obstruction, and molestation headed his list. For discussion, see Richard A. Epstein, Intentional Harms, 4 J. Legal Stud. 391, 431 (1975).

The modern economic understanding of predation does not dispute the illegality of force and fraud. But it asks the further question of whether predation constitutes an activity that is likely to cause social losses, even when restricted to downward price movements; and, if so, whether a court is capable of distinguishing between such predation and ordinary competition. The modern law and economics literature has generally defended the no-liability outcome in *Mogul* on the ground that predation does not offer any firm or group a secure route to gain market power. The classic article on the subject is John S. McGee, Predatory Price Cutting: The Standard Oil (N.J.) Case, 1 J.L. & Econ. 137 (1958), which concluded that mergers and acquisitions, but not predation, vaulted Standard Oil to its dominant market position. Thereafter McGee expressed doubt that predation could ever lead to monopoly. Historically the defendants' combination in *Mogul* broke up even before the legal issues were resolved on appeal, and no successful effort of wide-scale predation has yet been uncovered.

Notwithstanding the paucity of empirical evidence on the point, some writers have advocated, roughly speaking, a definition of predation that renders it illegal to sell a product below its marginal cost of production, a test adumbrated in Esher's, M.R., dissent, when he defines the unfair price as one at which the defendants could not "continue" to sell their wares. See Phillip Areeda & Donald F. Turner, Predatory Pricing and Related Practices Under Section 2 of the Sherman Act, 88 Harv. L. Rev. 697 (1975). The major response to this position is that no firm can hope to recoup in the long run the losses that it must incur in the short run to flood the market with low-cost products, so that consistent with *Mogul*, "[t]he antitrust offense of predation should be forgotten." See Frank H. Easterbrook, Predatory Strategies and Counterstrategies, 48 U. Chi. L. Rev. 263 (1981).

In the antitrust universe, that position carried the day in Matsushita Electric Industrial Co., Ltd. v. Zenith Radio Corp., 475 U.S. 574 (1986), when the Supreme Court upheld summary judgment for defendants, Japanese television manufacturers charged with a conspiracy to drive their American competitors out of business. The Court imposed a very high burden of proof on the plaintiffs given the inherent implausibility of their predation claim. The Court extended its views on predatory pricing to the converse situation of predatory bidding in Weyerhaeuser v. Ross-Simmons Hardwood Lumber Co., 549 U.S. 312, 316, 322 (2007). The Court unanimously rejected Ross-Simmons's antitrust claim that Weyerhaeuser

had engaged in unfair trade practices by using "its dominant position in the alder sawlog market to drive up the prices for alder sawlogs to levels that severely reduced or eliminated the profit margins of Weyerhaeuser's alder sawmill competition." Taking the same skeptical approach toward predatory pricing as in *Matsushita*, the Court reasoned that excessive intervention could easily deter beneficial competition, given the many procompetitive reasons for high bids, including the desire to build up future inventories. In addition, Thomas, J., noted that "[a] predatory-bidding scheme requires a buyer of inputs to suffer losses today on the chance that it will reap supracompetitive profits in the future." Accordingly the Court limited these claims to those few cases in which the buyer could show both that the defendant's high bids "led to below-cost pricing of the predator's outputs" and that "the defendant has a dangerous probability of recouping the losses incurred in bidding up input prices through the exercise of monopsony [i.e., buyer-side monopoly] power." The plaintiffs also failed to meet the high standards for a predation claim under *Weyerhaeuser* in Anesthesia Associates of Ann Arbor, PLLC v. Blue Cross Blue Shield of Michigan, No. 2:20-cv-12916, 2021 WL 4169711 (E.D. Mich 2021). The plaintiff's atypical predation case claimed that the low Blue Cross reimbursement rates caused doctors to resign from their plans. The complaint's "fundamental flaw is that Plaintiff does not plausibly plead that low reimbursement rates incur short-term losses for Defendant." *Id*. at *10.

For exhaustive discussion of these issues, see Steven C. Salop, Anticompetitive Overbuying by Power Buyers, *in* Symposium: Buyer Power and Antitrust, 72 Antitrust L.J., no. 2, 2005.

**2.** ***The English Trilogy.*** *Mogul* was the first of three major cases decided around 1900 that attempted to define the limits of fair competition at common law. The other two cases were Allen v. Flood, [1898] A.C. 1, and Quinn v. Leathem, [1901] A.C. 495, both of which involved labor, not trade, disputes. In Allen v. Flood, the defendant Allen represented the ironworkers' union; the plaintiff Flood and his coworkers were members of the shipwrights union. Both members of both unions worked for the Glengall Iron Co. under contracts at will. Allen told Glengall that the ironworkers would walk off the job unless the shipwrights were dismissed. To keep the service of the ironworkers, Glengall dismissed the plaintiff shipwrights, who promptly sued. The holding in the House of Lords took a highly abstract form: "An act lawful in itself is not converted by a malicious or a bad motive into an unlawful act so as to make the doer of the act liable to a civil action." The House of Lords dismissed the plaintiff's claim. An excerpt from Lord Herschell's lengthy opinion charts the move from this abstract proposition to the law of trade disputes:

> In Temperton v. Russell [[1893] 1 Q.B. 715, *supra* at 219], the further step was taken by the majority of the Court . . . of asserting that it was immaterial that the act induced was not the breach of a contract, but only the not entering into a contract, provided that the motive of desiring to injure the plaintiff, or to benefit the defendant at the expense of the plaintiff, was present. It seems to have been regarded as only a small step from the one decision to the other, and it was said that there seemed to be no good reason why, if an action lay for maliciously inducing a breach of contract, it should not equally lie for maliciously inducing a person not to enter into a contract. So far from thinking it a small step from the one decision to the other, I think there is a chasm between them. The reason for a distinction between the two cases appears to me to be this: that in the one case the act procured was the violation of a legal right, for which the person doing the act which injured the plaintiff could be sued as well as the person who procured it; whilst in the other case no legal right was violated by the person who did the act from which the plaintiff suffered: he would not be liable to be sued in respect of the act done, whilst the person who induced him to do the act would be liable to an action. . . .

In Quinn v. Leathem, [1901] A.C. 495, the last case in the trilogy, the plaintiff Leathem was a wholesale meat slaughterer. The defendant union demanded that he replace his current workers with union members paid at union wages. The union refused to accept the plaintiff's

offer to pay his own workers union scale; it was, however, prepared to admit the fired workers as union members, but without any seniority. When the plaintiff refused to comply with the union's demands, the union (in what today is called a secondary boycott) warned the plaintiff's best customer, his brother-in-law Munce, that his own workers would be called off the job unless Munce stopped buying his meat from the plaintiff. Munce yielded, and the plaintiff sued the union. The House of Lords upheld his claim. As stated in the headnote: "A combination of two or more, without justification or excuse, to injure a man in his trade by inducing his customers or servants to break their contracts with him or not to deal with him or continue in his employment is, if it results in damage to him, actionable." Lord Shand distinguished *Quinn* from *Allen* in a single sentence:

> In Allen v. Flood the purpose of the defendant was by the acts complained of to promote his own trade interest, which it was held he was entitled to do, although injurious to his competitors, whereas in the present case, while it was clear there was a combination, the purpose of the defendants was to injure the plaintiff in his trade as distinguished from the intention of legitimately advancing their own interests.

Is a union's interest to secure work for its own members a permissible justification under *Mogul*? For criticism of *Quinn*, see Charles O. Gregory, Labor and the Law Ch. 2 (2d rev. ed. 1958). For a defense of *Quinn* and an attack on *Allen*, see Sylvester Petro, Unions and the Southern Courts: Part III—The Conspiracy and Tort Foundations of the Labor Injunction, 60 N.C. L. Rev. 544, 558–67 (1982). Does the union in either *Allen* or *Flynn* stand a good chance to recoup its losses if forced to go out on strike to make good on its respective threats?

In any case, labor law has largely supplanted the common law rules in this area in both England and the United States. In particular, the Trade Disputes Act, Ed. VII ch. 47, deviated from common law principles on three particulars. It did not allow the enforcement of labor contracts; it forbade actions for the collective refusal to deal—a per se antitrust offense—in the absence of the threat or force; and it barred actions for the inducement of contract in labor disputes. In the United States, the National Labor Relations Act, as amended, 29 U.S.C. §§151–69, articulated a system of union elections buttressed by a statutory requirement that an employer designate an exclusive bargaining representative after a union won that right through election. What are the relative merits of the different approaches?

**3. *Malice in the Trade Cases.*** The leading American authority on the place of malice in unfair competition cases is Tuttle v. Buck, 119 N.W. 946, 948 (Minn. 1909). The plaintiff was a barber by trade and the defendant a banker. The plaintiff claimed that the defendant, acting out of sheer malice, sought to drive him out of the barbering business. The defendant hired two barbers, gave them rent-free use of a barbershop, and by "threats of his personal displeasure sought to persuade members of the general public not to frequent the plaintiff's business." The trial judge upheld the complaint on demurrer and the decision was affirmed on appeal. Elliott, J., writing for the court, held that the wholly malicious conduct of the defendant, if proved, overstepped the proper bounds of fair competition—only to express thereafter his personal doubts about the sufficiency of the plaintiff's factual allegations:

> There is no allegation that the defendant was intentionally running the business at a financial loss to himself, or that after driving the plaintiff out of business the defendant closed up or intended to close up his shop. From all that appears from the complaint he may have opened the barber shop, energetically sought business from his acquaintances and the customers of the plaintiff, and as a result of his enterprise and command of capital obtained it, with the result that the plaintiff, from want of capital, acquaintance, or enterprise, was unable to stand the competition and was thus driven out of business.

How long will any economic entity survive or prosper if motivated solely by malice instead of self-interest? See generally J.B. Ames, How Far an Act May Be a Tort Because of the Wrongful Motive of the Actor, 18 Harv. L. Rev. 411 (1905).

## *International News Service v. Associated Press*
248 U.S. 215 (1918)

Pitney, J. [The plaintiff Associated Press served some 900 newspapers throughout the United States in the gathering and distributing of news, which its member papers then sold to the public. Its annual budget was about $3,500,000. The defendant International News Service performed the same service for some 400 newspapers for about $2,000,000 per annum.]

**Justice Mahlon Pitney (1858-1924), who served as Associate Justice of the Supreme Court from 1912-1922. He also served as a Congressman, New Jersey State Senator, and Justice of the New Jersey Supreme Court.**
*Source: Wikimedia Commons*

The parties are in the keenest competition between themselves in the distribution of news throughout the United States; and so, as a rule, are the newspapers that they serve, in their several districts. . . .

The bill was filed to restrain the pirating of complainant's news by defendant in three ways: First, by bribing employees of newspapers published by complainant's members to furnish Associated Press news to defendant before publication, for transmission by telegraph and telephone to defendant's clients for publication by them; Second, by inducing Associated Press members to violate its by-laws and permit defendant to obtain news before publication; and Third, by copying news from bulletin boards and from early editions of complainant's newspapers and selling this, either bodily or after rewriting it, to defendant's customers. . . .

The only matter that has been argued before us is whether defendant may lawfully be restrained from appropriating news taken from bulletins issued by complainant or any of its members, or from newspapers published by them, for the purpose of selling it to defendant's clients. Complainant asserts that defendant's admitted course of conduct in this regard both violates complainant's property right in the news and constitutes unfair competition in business. And notwithstanding the case has proceeded only to the stage of preliminary injunction, we have deemed it proper to consider the underlying questions, since they go to the very merits of the action and are presented upon facts that are not in dispute. As presented in argument, these questions are: 1. Whether there is any property in news; 2. Whether, if there be property in news collected for the purpose of being published, it survives the instant of its publication in the first newspaper to which it is communicated by the news-gatherer; and 3. Whether defendant's admitted course of conduct in appropriating for commercial use matter taken from bulletins or early editions of Associated Press publications constitutes unfair competition in trade.

The federal jurisdiction was invoked because of diversity of citizenship, not upon the ground that the suit arose under the copyright or other laws of the United States. Complainant's news matter is not copyrighted. . . .

[T]he news element — the information respecting current events contained in the literary production — is not the creation of the writer, but is a report of matters that ordinarily are *publici juris*; it is the history of the day. It is not to be supposed that the framers of the Constitution, when they empowered Congress "to promote the progress of science and useful arts, by securing for limited times to authors and inventors the exclusive right to their respective writings and discoveries" (Const., Art. I, §8, par. 8), intended to confer upon one who might happen to be the first to report a historic event the exclusive right for any period to spread the knowledge of it.

We need spend no time, however, upon the general question of property in news matter at common law, or the application of the copyright act, since it seems to us the case must turn upon the question of unfair competition in business. And, in our opinion, this does not depend upon any general right of property analogous to the common-law right of the proprietor of an unpublished work to prevent its publication without his consent; nor is it foreclosed by showing that the benefits of the copyright act have been waived. We are dealing here not with restrictions upon publication but with the very facilities and processes of publication. The peculiar value of news is in the spreading of it while it is fresh; and it is evident that a valuable property interest in the news, as news, cannot be maintained by keeping it secret. Besides, except for matters improperly disclosed, or published in breach of trust or confidence, or in violation of law, none of which is involved in this branch of the case, the news of current events may be regarded as common property. What we are concerned with is the business of making it known to the world, in which both parties to the present suit are engaged. That business consists in maintaining a prompt, sure, steady, and reliable service designed to place the daily events of the world at the breakfast table of the millions at a price that, while of trifling moment to each reader, is sufficient in the aggregate to afford compensation for the cost of gathering and distributing it, with the added profit so necessary as an incentive to effective action in the commercial world. The service thus performed for newspaper readers is not only innocent but extremely useful in itself, and indubitably constitutes a legitimate business. The parties are competitors in this field; and, on fundamental principles, applicable here as elsewhere, when the rights or privileges of the one are liable to conflict with those of the other, each party is under a duty so to conduct its own business as not unnecessarily or unfairly to injure that of the other.

Obviously, the question of what is unfair competition in business must be determined with particular reference to the character and circumstances of the business. The question here is not so much the rights of either party as against the public but their rights as between themselves. And although we may and do assume that neither party has any remaining property interest as against the public in uncopyrighted news matter after the moment of its first publication, it by no means follows that there is no remaining property interest in it as between themselves. For, to both of them alike, news matter, however little susceptible of ownership or dominion in the absolute sense, is stock in trade, to be gathered at the cost of enterprise, organization, skill, labor, and money, and to be distributed and sold to those who will pay money for it, as for any other merchandise. Regarding the news, therefore, as but the material out of which both parties are seeking to make profits at the same time and in the same field, we hardly can fail to recognize that for this purpose, and as between them, it must be regarded as quasi property, irrespective of the rights of either as against the public. . . .

The peculiar features of the case arise from the fact that, while novelty and freshness form so important an element in the success of the business, the very processes of distribution and publication necessarily occupy a good deal of time. Complainant's service, as well as

defendant's, is a daily service to daily newspapers; most of the foreign news reaches this country at the Atlantic seaboard, principally at the City of New York, and because of this, and of time differentials due to the earth's rotation, the distribution of news matter throughout the country is principally from east to west; and, since in speed the telegraph and telephone easily outstrip the rotation of the earth, it is a simple matter for defendant to take complainant's news from bulletins or early editions of complainant's members in the eastern cities and at the mere cost of telegraphic transmission cause it to be published in western papers issued at least as early as those served by complainant. Besides this, and irrespective of time differentials, irregularities in telegraphic transmission on different lines, and the normal consumption of time in printing and distributing the newspaper, result in permitting pirated news to be placed in the hands of defendant's readers sometimes simultaneously with the service of competing Associated Press papers, occasionally even earlier.

Defendant insists that when, with the sanction and approval of complainant, and as the result of the use of its news for the very purpose for which it is distributed, a portion of complainant's members communicate it to the general public by posting it upon bulletin boards so that all may read, or by issuing it to newspapers and distributing it indiscriminately, complainant no longer has the right to control the use to be made of it; that when it thus reaches the light of day it becomes the common possession of all to whom it is accessible; and that any purchaser of a newspaper has the right to communicate the intelligence which it contains to anybody and for any purpose, even for the purpose of selling it for profit to newspapers published for profit in competition with complainant's members.

The fault in the reasoning lies in applying as a test the right of the complainant as against the public, instead of considering the rights of complainant and defendant, competitors in business, as between themselves. The right of the purchaser of a single newspaper to spread knowledge of its contents gratuitously, for any legitimate purpose not unreasonably interfering with complainant's right to make merchandise of it, may be admitted; but to transmit that news for commercial use, in competition with complainant—which is what defendant has done and seeks to justify—is a very different matter[, . . . whereby the defendant] is endeavoring to reap where it has not sown[,] . . . with special advantage to defendant in the competition because of the fact that it is not burdened with any part of the expense of gathering the news. The transaction speaks for itself, and a court of equity ought not to hesitate long in characterizing it as unfair competition in business.

. . . It is no answer to say that complainant spends its money for that which is too fugitive or evanescent to be the subject of property. That might, and for the purposes of the discussion we are assuming that it would, furnish an answer in a common-law controversy. But in a court of equity, where the question is one of unfair competition, if that which complainant has acquired fairly at substantial cost may be sold fairly at substantial profit, a competitor who is misappropriating it for the purpose of disposing of it to his own profit and to the disadvantage of complainant cannot be heard to say that it is too fugitive or evanescent to be regarded as property. It has all the attributes of property necessary for determining that a misappropriation of it by a competitor is unfair competition because contrary to good conscience.

The contention that the news is abandoned to the public for all purposes when published in the first newspaper is untenable. Abandonment is a question of intent, and the entire organization of the Associated Press negatives such a purpose. The cost of the service would be prohibitive if the reward were to be so limited. No single newspaper, no small group of newspapers, could sustain the expenditure. . . .

It is to be observed that the view we adopt does not result in giving to complainant the right to monopolize either the gathering or the distribution of the news, or, without complying with the copyright act, to prevent the reproduction of its news articles; but only postpones participation by complainant's competitor in the processes of distribution and reproduction

of news that it has not gathered, and only to the extent necessary to prevent that competitor from reaping the fruits of complainant's efforts and expenditure, to the partial exclusion of complainant, and in violation of the principle that underlies the maxim sic utere tuo, etc.

It is said that the elements of unfair competition are lacking because there is no attempt by defendant to palm off its goods as those of the complainant, characteristic of the most familiar, if not the most typical, cases of unfair competition. But we cannot concede that the right to equitable relief is confined to that class of cases. In the present case the fraud upon complainant's rights is more direct and obvious. Regarding news matter as the mere material from which these two competing parties are endeavoring to make money, and treating it, therefore, as *quasi* property for the purposes of their business because they are both selling it as such, defendant's conduct differs from the ordinary case of unfair competition in trade principally in this — that, instead of selling its own goods as those of complainant, it substitutes misappropriation in the place of misrepresentation, and sells complainant's goods as its own.

[The Court then brought its opinion to a close by considering (1) whether plaintiff is barred in equity because it has "unclean hands," since it utilizes "tips" obtained from defendant's service, and concluded that this practice "is not shown to be such as to constitute an unconscientious or inequitable attitude . . . so as to fix upon complainant the taint of unclean hands"; (2) whether the injunction was too broad, and decided that although it may be subject to some criticism it should be left to the trial court to modify it if necessary at a later stage in the case.]

The decree of the Circuit Court of Appeals will be affirmed.

[Justice Holmes, in an opinion in which Justice McKenna concurred, would have limited relief to requiring defendant to give express credit to plaintiff for the news it took.]

Brandeis, J., dissenting. . . . News is a report of recent occurrences. . . . The general rule of law is, that the noblest of human productions — knowledge, truths ascertained, conceptions, and ideas — become, after voluntary communication to others, free as the air to common use. Upon these incorporeal productions the attribute of property is continued after such communication only in certain classes of cases where public policy has seemed to demand it. These exceptions are confined to productions which, in some degree, involve creation, invention, or discovery. But by no means all such are endowed with this attribute of property. The creations which are recognized as property by the common law are literary, dramatic, musical, and other artistic creations; and these have also protection under the copyright statutes. The inventions and discoveries upon which this attribute of property is conferred only by statute, are the few comprised within the patent law. . . .

Plaintiff further contended that defendant's practice constitutes unfair competition, because there is "appropriation without cost to itself of values created by" the plaintiff; and it is upon this ground that the decision of this court appears to be based. To appropriate and use for profit, knowledge and ideas produced by other men, without making compensation or even acknowledgment, may be inconsistent with a finer sense of propriety; but, with the exceptions indicated above, the law has heretofore sanctioned the practice. . . .

. . . The unfairness in competition which hitherto has been recognized by the law as a basis for relief, lay in the manner or means of conducting the business; and the manner or means held legally unfair, involves either fraud or force or the doing of acts otherwise prohibited by law. In the "passing off" cases (the typical and most common case of unfair competition), the wrong consists in fraudulently representing by word or act that defendant's goods are those of plaintiff. In the other cases, the diversion of trade was effected through physical or moral coercion, or by inducing breaches of contract or of trust or by enticing away employees. In some others, called cases of simulated competition, relief was granted because defendant's purpose was unlawful; namely, not competition but deliberate and wanton destruction of plaintiff's business. . . .

Nor is the use made by the International News Service of the information taken from papers or bulletins of Associated Press members legally objectionable by reason of the purpose for which it was employed. The acts here complained of were not done for the purpose of injuring the business of the Associated Press. Their purpose was not even to divert its trade, or to put it at a disadvantage by lessening defendant's necessary expenses. The purpose was merely to supply subscribers of the International News Service promptly with all available news. . . .

[Justice Brandeis then argued that the complexity of the problem called for legislative and administrative solutions because courts are "powerless" to create, regulate, or enforce new forms of property rights, even "to redress a newly-disclosed wrong, although the propriety of some remedy appears to be clear." He also noted that the public interest might be affected because the British and French governments refused to give INS access to the war news from the front because of the pro-German sympathies of its Hearst papers. The INS lifted stories only where it was excluded from direct access to the news.]

## NOTE

***The Limits of* INS.** Justice Pitney's decision in INS v. AP is generally regarded as the foundation of the modern tort of misappropriation. As Justice Brandeis's dissent makes clear, the opinion goes beyond the libertarian conception of passing or palming off in that it does not involve any use of fraud that comes when one party falsely announces that its goods are the goods of another. The difficult question is how far this new tort will go. Does Pitney explain why it is needed given the protections otherwise afforded? Will the catalogue of tort actions ever be closed if judicial decisions can create novel property interests whenever one person tries to take advantage of the labor of another? Would the Court have allowed the action if the INS had only serviced papers that were not in direct competition with papers serviced by the Associated Press? Would Brandeis, J., have remained in dissent if INS's Hearst papers had been allowed access to the front by the British authorities?

The lower courts have often given *INS* a chilly reception. Judge Learned Hand, in particular, sought to limit its reach in Cheney Bros. v. Doris Silk Corp., 35 F.2d 279, 280 (2d Cir. 1929). The plaintiff was a silk manufacturer "which puts out each season many new patterns, designed to attract purchasers by their novelty and beauty." The expected life of any new pattern was generally about eight or nine months, and about 80 percent of the patterns marketed typically had no consumer appeal. Design patents were costly to obtain, and copyright protection was then generally unavailable as a matter of law. The plaintiff sought to enjoin the defendant, who copied one of the plaintiff's popular patterns and undersold the plaintiff. Hand, J., appealed to legislative deference in denying the plaintiff any relief under the supposed "general doctrine" of *INS*, noting that any creation of new rights would "flagrantly conflict" with long-established congressional schemes regulating copyrights and patents:

> Qua patent, we should at least have to decide, as tabula rasa, whether the design or machine was new and required invention; further, we must ignore the Patent Office whose action has always been a condition upon the creation of this kind of property. Qua copyright, although it would be simpler to decide upon the merits, we should equally be obliged to dispense with the conditions imposed upon the creation of the right. Nor, if we went so far, should we know whether the property so recognized should be limited to the periods prescribed in the statutes, or should extend as long as the author's grievance. It appears to us incredible that the Supreme Court should have had in mind any such consequences. To exclude others from the enjoyment of a chattel is one thing; to prevent any imitation of it, to set up a monopoly in the plan of its

> structure, gives the author a power over his fellows vastly greater, a power which the Constitution allows only Congress to create.

In effect, Hand's argument was that congressional coverage of related areas preempted the judicial creation of new rights. How did Pitney, J., sidestep that challenge? Should there have been a preemption issue on the table when the Chicago Board of Trade copied the Dow Jones Averages for its new financial futures indexes, which the Illinois Supreme Court enjoined in Board of Trade of City of Chicago v. Dow Jones & Co., Inc., 456 N.E.2d 84, 90 (Ill. 1983), on the ground that "there are an infinite number of stock market indexes which could be devised" such that no one gains monopoly power through the control over one specific index?

On the relationship between *INS* and the *Dow Jones* case, see Douglas G. Baird, Common Law Intellectual Property and the Legacy of *International News Service v. Associated Press*, 50 U. Chi. L. Rev. 411 (1983). For a qualified defense of *INS*, see Richard A. Epstein, *International News Service v. Associated Press*: Custom and Law as Sources of Property Rights in News, 78 Va. L. Rev. 87 (1992); Douglas G. Baird, The Story of *INS v. AP*, *in* Intellectual Property Stories (Ginsburg & Dreyfuss eds., 2006). Michael E. Kenneally, Misappropriation and the Morality of Free-Riding, 18 Stan. Tech. L. Rev. 289, 291 (2015), observes that *INS* taps into the widespread "notion that free-riding is unethical . . . But despite the influence that anti-free-riding sentiments have had, no one has offered much of a justification for them. Much criticism of free-riding is nothing more than name-calling." For the contrary position, see Richard A. Epstein, The Irrelevance of the First Amendment to the Modern Regulation of the Internet, 23 Competition: J. Antitrust & Unfair Competition L. Sec. St. B. Cal. 100, 106 (2014):

> [T]he remedy afforded in Justice Mahlon Pitney's opinion was shaped so as not to prevent anyone else from obtaining and disseminating the underlying public facts by independent effort. Rather, it only prevented the freeloading in *information gathering* that would make it less desirable for AP to generate the information in the first place.

How ought *INS* be read today?

## *The National Basketball Association v. Motorola, Inc.*

105 F.3d 841 (2d Cir. 1997)

Winter, J.

Motorola, Inc. and Sports Team Analysis and Tracking Systems ("STATS") appeal from a permanent injunction entered by Judge Preska. The injunction concerns a handheld pager sold by Motorola and marketed under the name "SportsTrax," which displays updated information of professional basketball games in progress. The injunction prohibits appellants, absent authorization from the National Basketball Association and NBA Properties, Inc. (collectively the "NBA"), from transmitting scores or other data about NBA games in progress via the pagers, STATS's site on America On-Line's computer dial-up service, or "any equivalent means."

The crux of the dispute concerns the extent to which a state law "hot-news" misappropriation claim based on International News Service v. Associated Press, 248 U.S. 215 (1918) ("*INS*"), survives preemption by the federal Copyright Act and whether the NBA's claim fits within the surviving *INS*-type claims. We hold that a narrow "hot-news" exception does survive preemption. However, we also hold that appellants' transmission of "real-time" NBA game scores and information tabulated from television and radio broadcasts of games in progress does not constitute a misappropriation of "hot news" that is the property of the NBA.

## I. Background

The facts are largely undisputed. Motorola manufactures and markets the SportsTrax paging device while STATS [through reporters who listen to or watch the games] supplies the game information that is transmitted to the pagers. The product became available to the public in January 1996, at a retail price of about $200. SportsTrax's pager has an inch-and-a-half by inch-and-a-half screen and operates in four basic modes: "current," "statistics," "final scores" and "demonstration." It is the "current" mode that gives rise to the present dispute. In that mode, SportsTrax displays the following information on NBA games in progress: (i) the teams playing; (ii) score changes; (iii) the team in possession of the ball; (iv) whether the team is in the free-throw bonus; (v) the quarter of the game; and (vi) time remaining in the quarter. The information is updated every two to three minutes, with more frequent updates near the end of the first half and the end of the game. There is a lag of approximately two or three minutes between events in the game itself and when the information appears on the pager screen. . . .

**Baseball version of SportsTrax**
*Source: Eric E. Johnson/Konomark*

## II. The State Law Misappropriation Claim

### A. Summary of Ruling

[Winter, J., first traces the early evolution of the broadcast of baseball and other events, and notes that before 1976 the "general understanding" was that live broadcasts were not copyrightable and that much doubt remained "whether a recorded broadcast or videotype of such an event was copyrightable."]

. . . In 1976, however, Congress passed legislation expressly affording copyright protection to simultaneously-recorded broadcasts of live performances such as sports events. See 17 U.S.C. §101. Such protection was not extended to the underlying events.

The 1976 amendments also contained provisions preempting state law claims that enforced rights "equivalent" to exclusive copyright protections when the work to which the state claim was being applied fell within the area of copyright protection. Based on legislative history of the 1976 amendments, it is generally agreed that a "hot-news" *INS*-like claim survives preemption. However, much of New York misappropriation law after *INS* goes well beyond "hot-news" claims and is preempted.

We hold that the surviving "hot-news" *INS*-like claim is limited to cases where: (i) a plaintiff generates or gathers information at a cost; (ii) the information is time-sensitive; (iii) a defendant's use of the information constitutes free-riding on the plaintiff's efforts; (iv) the defendant is in direct competition with a product or service offered by the plaintiffs; and (v) the ability of other parties to free-ride on the efforts of the plaintiff or others would so reduce

the incentive to produce the product or service that its existence or quality would be substantially threatened.[8] We conclude that SportsTrax does not meet that test.

### C. The State-Law Misappropriation Claim

The theory of the New York misappropriation cases relied upon by the district court is considerably broader than that of *INS*. However, we believe that [any] broad misappropriation doctrine based on amorphous concepts such as "commercial immorality" or society's "ethics" is preempted. Such concepts are virtually synonymous for wrongful copying and are in no meaningful fashion distinguishable from infringement of a copyright. . . .

In light of [more recent] cases . . . that emphasize the narrowness of state misappropriation claims that survive preemption, most of the broadcast cases relied upon by the NBA are simply not good law. Those cases were decided at a time when simultaneously-recorded broadcasts were not protected under the Copyright Act and when the state law claims they fashioned were not subject to federal preemption. . . .

Our conclusion, therefore, is that only a narrow "hot-news" misappropriation claim survives preemption for actions concerning material within the realm of copyright.

[The court then restates the five elements set out above.]

*INS* is not about ethics; it is about the protection of property rights in time-sensitive information so that the information will be made available to the public by profit-seeking entrepreneurs. If services like AP were not assured of property rights in the news they pay to collect, they would cease to collect it. The ability of their competitors to appropriate their product at only nominal cost and thereby to disseminate a competing product at a lower price would destroy the incentive to collect news in the first place. The newspaper-reading public would suffer because no one would have an incentive to collect "hot news."

We therefore find the extra elements — those in addition to the elements of copyright infringement — that allow a "hot-news" claim to survive preemption are: (i) the time-sensitive value of factual information, (ii) the free-riding by a defendant, and (iii) the threat to the very existence of the product or service provided by the plaintiff.

### 2. The Legality of SportsTrax

We conclude that Motorola and STATS have not engaged in unlawful misappropriation under the "hot-news" test set out above. To be sure, some of the elements of a "hot-news" *INS* claim are met. The information transmitted to SportsTrax is not precisely contemporaneous, but it is nevertheless time-sensitive. Also, the NBA does provide, or will shortly do so, information like that available through SportsTrax. It now offers a service called "Gamestats" that provides official play-by-play game sheets and half-time and final box scores within each arena. It also provides such information to the media in each arena. In the future, the NBA plans to enhance Gamestats so that it will be networked between the various arenas and will support a pager product analogous to SportsTrax. SportsTrax will of course directly compete with an enhanced Gamestats.

However, there are critical elements missing in the NBA's attempt to assert a "hot-news" *INS*-type claim. As framed by the NBA, their claim compresses and confuses three different informational products. The first product is generating the information by playing the games; the second product is transmitting live, full descriptions of those games; and the third product is collecting and retransmitting strictly factual information about the games. The first and second products are the NBA's primary business: producing basketball games for live attendance and licensing copyrighted broadcasts of those games. The collection and retransmission of strictly factual material about the games is a different product: e.g., box-scores in newspapers,

8. Some authorities have labeled this element as requiring direct competition between the defendant and the plaintiff in a primary market. . . . [See] Restatement (Third) of Unfair Competition, §38 cmt. *c*, at 412–13. . . .

summaries of statistics on television sports news, and real-time facts to be transmitted to pagers. In our view, the NBA has failed to show any competitive effect whatsoever from SportsTrax on the first and second products and a lack [of] any free-riding by SportsTrax on the third.

With regard to the NBA's primary products—producing basketball games with live attendance and licensing copyrighted broadcasts of those games—there is no evidence that anyone regards SportsTrax or the AOL site as a substitute for attending NBA games or watching them on television. In fact, Motorola markets SportsTrax as being designed "for those times when you cannot be at the arena, watch the game on TV, or listen to the radio. . . ."

The NBA argues that the pager market is also relevant to a "hot-news" *INS*-type claim and that SportsTrax's future competition with Gamestats satisfies any missing element. We agree that there is a separate market for the real-time transmission of factual information to pagers or similar devices, such as STATS's AOL site. However, we disagree that SportsTrax is in any sense free-riding off Gamestats.

An indispensable element of an INS "hot-news" claim is free-riding by a defendant on a plaintiff's product, enabling the defendant to produce a directly competitive product for less money because it has lower costs. SportsTrax is not such a product. The use of pagers to transmit real-time information about NBA games requires: (i) the collecting of facts about the games; (ii) the transmission of these facts on a network; (iii) the assembling of them by the particular service; and (iv) the transmission of them to pagers or an on-line computer site. Appellants are in no way free-riding on Gamestats. Motorola and STATS expend their own resources to collect purely factual information generated in NBA games to transmit to SportsTrax pagers. They have their own network and assemble and transmit data themselves.

. . . SportsTrax and Gamestats are each bearing their own costs of collecting factual information on NBA games, and, if one produces a product that is cheaper or otherwise superior to the other, that producer will prevail in the marketplace. This is obviously not the situation against which *INS* was intended to prevent: the potential lack of any such product or service because of the anticipation of free-riding.

[Injunction denied.]

## NOTE

***Pyrrhic Victory for Motorola?*** Some four months after Motorola beat back an injunction by the NBA, it stopped promoting its SportsTrax pager and substituted in its place a new product called "ESPN to go" that it developed in connection with ESPN, the Walt Disney sports subsidiary, which reported NBA scores with at least a five-minute delay. The device did not let its user follow a single game, but instead used a single broadcast point to send multiple scores in different sports. Motorola announced: "We are simply voluntarily abiding by the N.B.A.'s guidelines." Motorola Sidelines Device Providing Live N.B.A. Scores, N.Y. Times, June 2, 1997, http://www.nytimes.com/1997/06/02/business/motorola-sidelines-device-providing-live-nba-scores.html. Why the voluntary retreat?

## *Barclays Capital Inc. v. Theflyonthewall.com*

650 F.3d 876 (2d Cir. 2011)

[Barclays, Merrill Lynch, and Morgan Stanley are firms that invested heavily (and separately) in market research targeting specific firms and industries. Each firm first released its buy/hold/sell recommendations to its paid customers prior to the start of each trading day in New

York, in time for these customers to incorporate that information into their morning trading strategies. Only after the start of trade on the New York Stock Exchange (NYSE) did the firms release the information to the general public. Their two-part strategy was intended to give the preferred customers a leg up on the market, followed by an additional boost for the early purchases once the general public received that same information. The defendant, Theflyonthewall.com ("Fly"), removed the informational advantages from the firm's customers by collecting that information from a variety of sources, which it then released to the general public prior to the start of trading on the NYSE, noting carefully which recommendations were made by which firms. Some firms would send reports to Fly directly. For firms that did not consent to this sharing, Fly relied on unauthorized communications with firm employees. After 2005, Fly abandoned this latter practice and instead relied on "other news outlets, chat rooms, 'blast IMs,'" and other informal channels.

The district court, Cote, J., enjoined Fly from its distribution scheme until 30 minutes before the start of trade. Barclays Capital, Inc. v. Theflyonthewall.com, 700 F. Supp. 2d 310 (S.D.N.Y. 2010). The Second Circuit reversed that decision in a lengthy opinion that was much preoccupied with *NBA v. Motorola*. Sack, J., set the stage by noting that *INS*, which used federal common law in a diversity case, was "no longer good law" after federal common law was largely abolished by Erie R.R. v. Tompkins, 304 U.S. 64 (1938), even though the hot-news exception—the modern reformulation of *INS*'s misappropriation—survived in limited form after the passage of the 1976 Copyright Act. He then offered this generalization:]

The adoption of new technology that injures or destroys present business models is commonplace. Whether fair or not, that cannot, without more, be prevented by application of the misappropriation tort. Indeed, because the Copyright Act itself provides a remedy for wrongful copying, such unfairness may be seen as supporting a finding that the Act preempts the tort. . . .

The NBA panel repeatedly emphasized the "narrowness" of the "hot news" tort exception from preemption. . . . In Krause v. Titleserv, Inc., 402 F.3d 119, 123 (2d Cir. 2005), we declined to limit protection for copyrights held by "owners" of computer programs to those with formal title to such programs. The first reason we gave was that title may depend on state law that differs from one state to another. . . .

Indeed, central to the principle of preemption generally is the value of providing for legal uniformity where Congress has acted nationally. . . .

This is a pressing concern when considering the "narrow" "hot news" misappropriation exemption from preemption. The broader the exemption, the greater the likelihood that protection of works within the "general scope" of the copyright and of the type of works protected by the Act will receive disparate treatment depending on where the alleged tort occurs and which state's law is found to be applicable. . . .

[Sack, J., then noted that the claim for preemption was not defeated simply because the firms' "[r]ecommendations themselves are not copyrightable." He then concluded that the hot-news exception had no relevance at all:]

[F]inally, the Firms' claim is not a so-called *INS*-type non-preempted claim because Fly is not, under NBA's analysis, "free-riding." It is collecting, collating and disseminating factual information—the facts that Firms and others in the securities business have made recommendations with respect to the value of and the wisdom of purchasing or selling securities—and attributing the information to its source. The Firms are making the news; Fly, despite the Firms' understandable desire to protect their business model, is breaking it.

Moreover, Fly, having obtained news of a Recommendation, is hardly selling the Recommendation "as its own," *INS*, 248 U.S., at 239. It is selling the information with specific attribution to the issuing Firm. Indeed, for Fly to sell, for example, a Morgan Stanley Recommendation "as its own," as INS sold the news it cribbed from AP to INS subscribers, would be

of little value to either Fly or its customers. . . . It is not the identity of Fly and its reputation as a financial analyst that carries the authority and weight sufficient to affect the market. It is Fly's accurate attribution of the Recommendation to the creator that gives this news its value. . . .

In this case, as the district court found, approximately half of Fly's twenty-eight employees are involved on the collection of the Firms' Recommendations and production of the newsfeed on which summaries of the Recommendations are posted. Fly is reporting financial news — factual information on Firm Recommendations — through a substantial organizational effort. Therefore, Fly's service — which collects, summarizes, and disseminates the news of the Firms' Recommendations — is not the "*INS*-like" product that could support a non-preempted cause of action for misappropriation. . . .

By way of comparison, we might, as the *NBA* Court did, speculate about a product a Firm might produce which might indeed give rise to a non-preempted "hot-news" misappropriation claim. If a Firm were to collect and disseminate to some portion of the public facts about securities recommendations in the brokerage industry (including, perhaps, such facts it generated itself — its own Recommendations), and were Fly to copy the facts contained in the Firm's hypothetical service, it might be liable to the Firm on a "hot-news" misappropriation theory. That would appear to be an *INS*-type claim and might survive preemption.

[A concurrence by Raggi, J., was more sympathetic to *INS* and the firms, but ultimately she concluded as follows:]

I am not prepared to foreclose the possibility of a "hot news" claim by a party who disseminates news it happens to create. I conclude simply that the facts emphasized by the majority preclude the Firms from stating a non-preempted "hot news" claim for a different reason derived from *NBA*: the Firms' product and Fly's newsfeed do not directly compete.

## NOTES

**1. INS *in Relation to the Creation and Dissemination of Information.*** No judge dissented in *Fly*, but any dissent would presumably use the opinion of Cote, J., in the district court as its starting point. The point of departure is that the defendants in this case know that the information that they intercepted was intended for other individuals, and that its value derived from its exclusive use for a short period of time. Removing the differential advantage in effect puts the entire service out of business, such that the overall market in information will be less efficient afterward than before. The effort to secure broader dissemination early on thus leads to a reduction in the total quantity of the information generated, as all incentives to produce the information are stripped away. That result is avoided if this information is treated as a kind of a trade secret, given in confidence to a select audience, which keeps its value only until it is revealed. To limit, therefore, the hot-news exception only to news of public events gets matters exactly backward, for the private generation of new information merits greater protection than reports of the general events of the day, which are in the public domain. It should therefore not matter that the defendants are not in direct competition with the plaintiff if, unlike the situation in *NBA*, the use of this information is lifted directly from the plaintiffs and undermines their business.

In their amicus brief, Google and Twitter argued that "[h]ot news becomes cold in a nanosecond in the modern world." Does that point explain why legal protection should be denied, or why it is needed? One court has drawn a line based on the purpose of the reproduction. See Fox News Network, LLC v. TVEyes, Inc., 43 F. Supp. 3d 379, 399 (S.D.N.Y. 2014) ("TVEyes is not a valuable service because its subscribers credit it as a reliable news outlet, it is

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valuable because it reports what the news outlets and commentators are saying and therefore does not 'scoop' or free-ride on the news services. Thus, the hot news misappropriation claim is preempted by the Copyright Act. . . .").

**2. *Hot News as a "Collective Action Problem."*** Prior to the publication of the Second Circuit decision, the hot-news doctrine received a detailed examination in Shyamkrishna Balganesh, "Hot News": The Enduring Myth of Property in News, 111 Colum. L. Rev. 419, 425 (2011). Citing Cote's, J., decision, Balganesh lamented the fact that recent proposals, including one from the Federal Trade Commission, to protect hot news in order to alleviate the revenue problems of newspapers, are "developments [that] effectively resuscitated the hot news doctrine." Balganesh insists that the hot-news doctrine was designed not to create property rights in news, but to address the serious "collective action problem that was and is unique to the newspaper industry, related to the practice of cooperative newsgathering." For a response, see Richard A. Epstein, The Protection of "Hot News": Putting Balganesh's "Enduring Myth" About *International News Service v. Associated Press* in Perspective, 111 Colum. L. Rev. *Sidebar* 79, 89–90, 88 (2011), who rejects the collective action argument:

> A collective action problem arises when a group of individuals acting alone are unable to achieve a result that they collectively desire. . . . The need for many newspapers to gather information is obvious enough, and Balganesh is surely right to say that "forcing each newspaper to collect the news individually on its own was recognized to be wasteful, duplicative, and prohibitively expensive, for all but the largest incumbents." But that is beside the point in this context. Any association with 950 or even 400 members faces an evident collective action problem. . . . Indeed, the very fact that this lawsuit takes place between two such associations means that they have already solved their collective action problems, such that the ultimate litigation operates on the same principles that would govern a dispute between two natural persons.
>
> [Instead the] key difference between these two cases and misappropriation is that the latter depends on a notion of mutually beneficial forced exchanges: Each side is told to give up its right to pick things off the other's bulletin boards for the mutual advantage of both. No hard line libertarian theory can tolerate these forced Pareto efficient exchanges, which is why the decision in *International News* represents a quantum leap beyond the earlier cases that did fit into the force and fraud paradigm. Justice Pitney got the point intuitively. Neither Justices Holmes nor Brandeis grasped the point.

For a critical evaluation of *Theflyonthewall.com*, see Nicole Marimon, Shutting Down the Turbine: How the News Industry and News Aggregators Can Coexist in a Post-*Barclays v. Theflyonthewall.com* World, 23 Fordham Intell. Prop. Media & Ent. L.J. 1441, 1445 (2013), which argues that "the best solution is to keep a common law doctrine, but one with changes that include a new conception of what timeliness means and that stipulate what kinds of remedies apply."

**3. *The Meme Stock Saga.*** The permutations around *INS* continued apace during the year 2021 in connection with the so-called "meme stock" crisis. "Meme stocks" include such companies as GameStop, AMC Theaters, and Blackberry that have been sold short by major investment houses who thought that they were overvalued in the marketplace, and thus hoped to cover their shorts when the price of the stocks went down. But a loose, highly determined group of online investors struck back at these short sellers by bidding up the price of these shares to inflict massive losses on the short sellers. The motivations of these informal groups were as much social as they were economic. The persistence of these high prices inflicted large losses on the short sellers, driving at least one firm into bankruptcy, in part for the sheer pleasure of seeing the mighty fall.

The episode here represents an odd form of self-help because there was no imminent threat of danger to any property held by the investors who drove the prices upward. Is there any antitrust remedy against the concerted action? In dealing with these cases, is there any way

that the hot news concept articulated above from *INS* gives voice to the claim that either side had created hot news that was capable of misappropriation by others? For a detailed account, see Tori N. Chiu & Moin A. Yahya, Meme Stock Vigilantism: A Property Rights Approach, 17 Ohio St. Bus. L.J. 1, 45–48 (2023). The authors do not mention notions of "malice" or antitrust. Should they have done so?

## *Ely-Norris Safe Co. v. Mosler Safe Co.*

7 F.2d 603 (2d Cir. 1925)

Suit in equity by the Ely-Norris Safe Company against the Mosler Safe Company. From decree of dismissal, plaintiff appeals. Reversed.

The jurisdiction of the District Court depended upon diverse citizenship, and the suit was for unfair competition. The bill alleged that the plaintiff manufactured and sold safes under certain letters patent, which had as their distinctive feature an explosion chamber, designed for protection against burglars. Before the acts complained of, no one but the plaintiff had ever made or sold safes with such chambers, and, except for the defendant's infringement, the plaintiff has remained the only manufacturer and seller of such safes. By reason of the plaintiff's efforts the public has come to recognize the value of the explosion chamber and to wish to purchase safes containing them. Besides infringing the patent, the defendant has manufactured and sold safes without a chamber, but with a metal band around the door, in the same place where the plaintiff put the chamber, and has falsely told its customers that this band was employed to cover and close an explosion chamber. Customers have been thus led to buy safes upon the faith of the representation, who in fact wished to buy safes with explosion chambers, and would have done so, but for the deceit.

The bill prayed an injunction against selling safes with such metal bands, and against representing that any of its safes contained an explosion chamber. From the plaintiff's answers to interrogatories it appeared that all the defendant's safes bore the defendant's name and address, and were sold as its own. Furthermore, that the defendant never gave a customer reason to suppose that any safe sold by it was made by the plaintiff. . . .

Hand, J. (after stating the facts as above.) American Washboard Co. v. Saginaw Mfg. Co., 103 F. 281 (6th Cir. [1900]), was . . . a case in substance like that at bar, because there the plaintiff alleged that it had acquired the entire output of sheet aluminum suitable for washboards. It necessarily followed that the plaintiff had a practical monopoly of this metal for the articles in question, and from this it was a fair inference that any customer of the defendant, who was deceived into buying as an aluminum washboard one which was not such, was a presumptive customer of the plaintiff, who had therefore lost a bargain. This was held, however, not to constitute a private wrong, and so the bill was dismissed. . . .

We must concede, therefore, that on the cases as they stand the law is with the defendant, and the especially high authority of the court which decided American Washboard Co. v. Saginaw Mfg. Co., *supra*, makes us hesitate to differ from their conclusion. Yet there is no part of the law which is more plastic than unfair competition, and what was not reckoned an actionable wrong 25 years ago may have become such today. We find it impossible to deny the strength of the plaintiff's case on the allegations of its bill. As we view it, the question is, as it always is in such cases, one of fact. While a competitor may, generally speaking, take away all the customers of another that he can, there are means which he must not use. One of these is deceit. The false use of another's name as maker or source of his own goods is deceit, of which the false use of geographical or descriptive terms is only one example. But we conceive that in the end the questions which arise are always two: Has the plaintiff in fact lost customers? And

has he lost them by means which the law forbids? The false use of the plaintiff's name is only an instance in which each element is clearly shown.

In the case at bar the means are as plainly unlawful as in the usual case of palming off. It is as unlawful to lie about the quality of one's wares as about their maker; it equally subjects the seller to action by the buyer. . . . The reason, as we think, why such deceits have not been regarded as actionable by a competitor, depends only upon his inability to show any injury for which there is a known remedy. In an open market it is generally impossible to prove that a customer, whom the defendant has secured by falsely describing his goods, would have bought of the plaintiff, if the defendant had been truthful. Without that, the plaintiff, though aggrieved in company with other honest traders, cannot show any ascertainable loss. He may not recover at law, and the equitable remedy is concurrent. The law does not allow him to sue as a vicarious avenger of the defendant's customers.

But, if it be true that the plaintiff has a monopoly of the kind of wares concerned, and if to secure a customer the defendant must represent his own as of that kind, it is a fair inference that the customer wants those and those only. Had he not supposed that the defendant could supply him, presumably he would have gone to the plaintiff, who alone could. At least, if the plaintiff can prove that in fact he would, he shows a direct loss, measured by his profits on the putative sale. If a tradesman falsely foists on a customer a substitute for what the plaintiff alone can supply, it can scarcely be that the plaintiff is without remedy, if he can show that the customer would certainly have come to him, had the truth been told.

Yet that is in substance the situation which this bill presents. It says that the plaintiff alone could lawfully make such safes, and that the defendant has sold others to customers who asked for the patented kind. It can make no difference that the defendant sold them as its own. The sale by hypothesis depended upon the structure of the safes, not on their maker. To be satisfied, the customer must in fact have gone to the plaintiff, or the defendant must have infringed. Had he infringed, the plaintiff could have recovered his profit on the sale; had the customer gone to him, he would have made that profit. Any possibilities that the customers might not have gone to the plaintiff, had they been told the truth, are foreclosed by the allegation that the plaintiff in fact lost the sales. . . .

Decree reversed.

## *Mosler Safe Co. v. Ely-Norris Safe Co.*

273 U.S. 132 (1926)

Holmes, J. [After summarizing the facts set out in the decision below.] At the hearing below all attention seems to have been concentrated on the question passed upon and the forcibly stated reasons that induced this Court of Appeals to differ from that for the Sixth Circuit. But, upon a closer scrutiny of the bill than seems to have been invited before, it does not present that broad and interesting issue. [Justice Holmes then restates the key allegations of the unfair competition claim: (1) The plaintiff has a patent on the explosion chamber, and (2) the defendant has designed and sold safes that have no such chamber but appear to the public that they did.] The plaintiff relies upon its patent suit for relief in respect of the sales of safes alleged to infringe its rights. It complains here only of false representations as to safes that do not infringe but that are sold as having explosion chambers although in fact they do not.

It is consistent with every allegation in the bill and the defendant in argument asserted it to be a fact, that there are other safes with explosion chambers beside that for which the plaintiff has a patent. The defendant is charged only with representing that its safes had an

explosion chamber, which, so far as appears, it had a perfect right to do if the representation was true. If on the other hand the representation was false as it is alleged sometimes to have been, there is nothing to show that customers had they known the facts would have gone to the plaintiff rather than to other competitors in the market, or to lay a foundation for the claim for a loss of sales. The bill is so framed as to seem to invite the decision that was obtained from the Circuit Court of Appeals, but when scrutinized is seen to have so limited its statements as to exclude the right to complain.

Decree reversed.

## NOTES

**1.** ***Passing Off.*** Would establishing the plaintiff's monopoly on all explosion chambers justify its demand for an injunction? Damages? Both? How might damages be calculated if allowed? What result if all plaintiffs who made safes with explosion chambers joined together in a class action suit?

In one sense, the plaintiff's case for passing off builds on the elements of ordinary misrepresentation already developed in Chapter 3 and recognized in the context of unfair competition as early as *Mogul*. Initially the passing off action builds from the admitted proposition that a disappointed buyer has an action against the seller who has passed off its own goods as the superior product of a rival. Yet in practice no individual purchaser is likely to bear the cost of recovering its trifling losses attributable to the defendant's misrepresentation. Nor would that suit, even if successful, vindicate the interests of the rival in its own product's reputation and good will. In passing off cases, therefore, the *competitor* replaces the purchaser as the plaintiff. The claim is that the defendant has falsely represented that its own product is better than it really is by pretending that his product is the plaintiff's or by claiming that his product has desirable attributes associated with the plaintiff's product that it, in fact, lacks. The substantive underpinnings of passing off are clear enough: The defendant's misrepresentation induces third parties to desert the plaintiff. The measure of damages is the profits from lost sales, which depend critically on the fraction of defendant's buyers (often less than 100 percent) that would have migrated to the plaintiff's wares if the passing off had not happened.

**2.** ***Product Disparagement.*** Clearly distinct from passing off are claims for product disparagement. With disparagement the defendant asserts that the plaintiff's product is worse than it really is, so as to induce consumers to purchase other products, including the defendant's. See Tex Smith, The Harmonica Man v. Godfrey, *infra* Chapter 6, Note 1, at 355. Disparagement is really a form of product defamation, although many courts treat it as a distinct tort not governed by the myriad of defamation rules such as those concerning innuendo or special damages. As the court noted in Dairy Stores, Inc. v. Sentinel Publishing Co., 516 A.2d 220, 224 (N.J. 1986):

"Well, gentlemen, I must say this *is* a coincidence."

*Source: I. Klein/The New Yorker Collection/The Cartoon Bank.*

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> Although the two causes sometimes overlap, actions for defamation and product disparagement stem from different branches of tort law. A defamation action, which encompasses libel and slander, affords a remedy for damage to one's reputation. By comparison an action for product disparagement is an offshoot of the cause of action for interference with contractual relations, such as sales to a prospective buyer. The two causes may merge when a disparaging statement about a product reflects on the reputation of the business that made, distributed or sold it. If, for example, a statement about the poor quality of a product implies that the seller is fraudulent, then the statement may be actionable under both theories.

For more on product disparagement, see Restatement (Third) Unfair Competition §2.

**3.** ***The Lanham Act.*** There is a close kinship between actions for unfair competition and those for violation of the Lanham Act, 15 U.S.C. §§1051–1141 (2024), the trademark statute. Its general intention is expressed in section 1127: "The intent of this [Act] is to regulate commerce within the control of Congress by making actionable the deceptive and misleading use of marks in such commerce . . . [and] to protect persons engaged in such commerce against unfair competition. . . ." The statute provides protection for both common law and statutory trademarks. The section also protects a diverse collection of marks, symbols, design elements, and characters that the public, or some relevant portion thereof, directly associates with the plaintiff or its product. The Restatement (Third) Unfair Competition, §2, comment *b*, notes how the Act undid the restrictive rule in *Ely-Norris*:

> As originally enacted, §43(a) of the Act, 15 U.S.C. §1125(a), recognized a right of action against "a false designation of origin, or any false description or representation" used in connection with any goods or services in favor of "any person who believes that he is or is likely to be damaged." Some early interpretations confined §43(a) to misrepresentations relating to source; other interpretations viewed it as a codification of existing common law liability under the "single source" doctrine. Subsequent decisions, however, established the section's general applicability to deceptive advertising and rejected the attempt to engraft the common law limitations onto the statutory tort. The 1988 revision of §43(a) confirmed its application to both misrepresentations of source and other deceptive representations made in connection with the marketing of goods and services.

**4.** ***Trademark and Trade Name Litigation: Direct Competitors.*** A veritable explosion of cases constantly tests the outer limits of trademark and trade name protection. The classic suits seek to enjoin direct competitors. In Warner Bros., Inc. v. Gay Toys, Inc., 658 F.2d 76 (2d Cir. 1981), the court allowed Warner Bros. to enjoin Gay Toys from the marketing of its "Dixie Racer," a 1969 Dodge Charger complete with a bright orange color, Confederate flag decal, numbers on the door, and the various symbols of the "General Lee," all based on the then-popular television series *The Dukes of Hazzard*. As commonly happens, the defendant had sought unsuccessfully to obtain a license from the plaintiff to market *Dukes of Hazzard* cars. Thereafter, it had modified the features of an existing car to bear greater resemblance to the *Dukes of Hazzard* car, from which it still differed in certain respects. Notwithstanding those residual differences, the plaintiff obtained a preliminary injunction against the defendant by marshaling a wide array of evidence to show that ordinary customers confused the defendant's car with the original *Dukes of Hazzard* line: The defendant's Dixie Racer had sales far in excess of its other cars in the same line; dealers sold the defendant's car as "The *Dukes of Hazzard* Car"; and, as consumer surveys had determined, 80 percent of the children asked thought the Dixie Racer was the *Dukes of Hazzard* car. What evidence might be introduced to rebut the charge of trademark violation? Could the case have been treated as one of unfair competition at common law?

**5.** ***Trademark and Trade Name Litigation: Other Applications.*** Although most trademark litigation takes place between direct competitors, trademark protection need not be so limited. In MGM-Pathé Communications v. Pink Panther Patrol, 774 F. Supp. 869,

875 (S.D.N.Y. 1991), the plaintiff owned the registered trademark "THE PINK PANTHER," which applies to the popular series of films about its bumbling detective hero. It also lent its trademark to producers of a wide range of consumer and children's goods. The defendant was a gay rights defense organization that used the PINK PANTHER name in connection with an upside-down pink triangle (used by the Nazis to mark homosexuals) as its symbol. Even though the defendant group sold no goods in competition with the plaintiffs, the court enjoined its use of the PINK PANTHER trademark on the ground that ordinary individuals could mistakenly assume that the owners of the trademark sponsored or otherwise supported the activities of the Patrol.

**Peter Sellers in *The Return of the Pink Panther* (1975).**
*Source: AF Archive/Alamy*

> [It] is indeed entirely likely that a large percentage of the population of the United States might see and hear both plaintiff's and defendants' names during a single evening of nationwide television broadcasting, if a telecast of an MGM film should be followed by a newscast including reference to the Patrol's activities.

But trade name protection (and common law misappropriation) claims were both denied in New Kids on the Block v. New America Publishing, Inc., 971 F.2d 302, 308 (9th Cir. 1992). Two newspapers, *USA Today* and *The Star*, ran popularity polls on 900-number phone lines, asking callers to say which of the (five) New Kids was the hottest (or coolest). Kozinski, C.J., held that the defendant's use of their trade name was a privileged *nominative* use because there was no other conceivable way in which any newspaper could otherwise refer to the group to get their readers' opinions about it. "It is no more reasonably possible, however, to refer to the New Kids as an entity than it is to refer to the Chicago Bulls, Volkswagens or the Boston Marathon without using the trademark." The use of the name was therefore adjudged fair because

> [b]oth *The Star* and *USA Today* reference the New Kids only to the extent necessary to identify them as the subject of the polls; they do not use the New Kids' distinctive logo or anything else that isn't needed to make the announcements intelligible to readers. Finally, nothing in the announcement suggests joint sponsorship or endorsement by the New Kids.

Should it make a difference that the New Kids have their own 900 numbers for their fans to use?

The nominative use argument also prevailed in Toyota Motor Sales, U.S.A., Inc. v. Tabari, 610 F.3d 1171, 1175, 1179 (9th Cir. 2010), in which Toyota sought to enjoin the defendants from using the Lexus name in its promotional materials. Kozinski, C.J., sharply rebuffed the claim:

> The Tabaris are using the term Lexus to describe their business of brokering Lexus automobiles; when they say Lexus, they mean Lexus. We've long held that such use of the trademark is a fair use, namely nominative fair use. And fair use is, by definition, not infringement. The Tabaris did in fact present a nominative fair use defense to the district court.

The case was then remanded to the District Court, with the instruction that "a domain name containing a mark cannot be nominative fair use if it suggests sponsorship or

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endorsement by the trademark holder." See generally Paul J. Heald, Federal Intellectual Property Law and the Economics of Preemption, 76 Iowa L. Rev. 959 (1991).

**6. *Patents.*** Inventions have long received explicit statutory protection, which defines patentable subject matter as "any new and useful process, machine, manufacture, or composition of matter, or any new and useful improvement thereof." Other requirements are originality, novelty, and nonobviousness. See generally 35 U.S.C. §§100–05 (2024). Procedurally a patent application must be filed within one year of its public use or publication, and it must contain "a written description of the invention, and of the manner and process of making and using it, in such full, clear, concise, and exact terms as to enable any person skilled in the art to which it pertains . . . to make and use the same," concluding "with one or more claims particularly pointing out and distinctly claiming the subject matter which the inventor or a joint inventor regards as the invention." 35 U.S.C. §112 (2024). Why are the procedural elements for the perfection of a patent so critical to the operation of the system?

On the economic function of the patent system, see Edmund W. Kitch, The Nature and Function of the Patent System, 20 J.L. & Econ. 265 (1977), who claims that the system has two functions: prospect and reward. The reward function spurs invention by conferring an exclusive monopoly. The prospect function (an analogy to the rule in mining law that allows the party who discovers a vein of ore to have the first crack at its exploitation) helps ensure that certain "prospects"—here, new inventions—will be efficiently and sensibly developed by giving exclusive rights in the period between the time an invention is first patented and the time it is first commercially exploited. The prospect function is of special importance with drugs that cannot be marketed until they receive regulatory approval. The prospect theory has been criticized for downplaying the risk that the holder of a broad patent will seek to exploit it not through development, but by blocking the use of the invention by other parties. A broad patent therefore has the undesirable effect of forcing people to "invent around" patented devices. What is the relationship between a law of patents and a law of trade secrets? Why are both needed? For criticism of the prospect theory, see Mark A. Lemley, Ex Ante Versus Ex Post Justifications for Intellectual Property, 71 U. Chi. L. Rev. 129 (2004).

**7. *Federal Preemption of State Unfair Competition Laws: Unpatentable Designs.*** Both *INS* and *Mosler Safe* were decided as a matter of general federal common law under the then-applicable doctrine of Swift v. Tyson, 41 U.S. 1 (1842). Now that Erie Railroad v. Tompkins, 304 U.S. 64 (1938), blocks the creation of new federal common law, the federal preemption issue raised in both *NBA* and *Barclays* traces back to Article I, §8, Clause 8 of the U.S. Constitution, which gives Congress the power "[t]o promote the Progress of Science and useful Arts, by securing for limited times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries."

In Sears, Roebuck & Co. v. Stiffel Co., 376 U.S. 225, 231–32 (1964), Sears, Roebuck marketed pole lamps that were substantially identical to those sold by Stiffel. Stiffel's design patent claim for injunctive relief was rejected by the trial judge "for want of invention." The trial judge, however, accepted Stiffel's unfair competition claim when Sears sold lamps identical to Stiffel's, even though there was no "palming off" or confusion as to source. The Supreme Court reversed, noting that patents, as a form of monopoly, only issue when the stringent conditions set out in the federal statute are satisfied.

> To allow a State by use of its law of unfair competition to prevent the copying of an article which represents too slight an advance to be patented would be to permit the State to block off from the public something which federal law has said belongs to the public. The result would be that while federal law grants only 14 or 17 years' protection [now 20 years from the application date—Eds.] to genuine inventions, States could allow perpetual protection to articles too lacking in novelty to merit any patent at all under federal constitutional standards.

*Sears* was applied in Bonito Boats, Inc. v. Thunder Craft Boats, Inc., 489 U.S. 141, 159–60 (1989), to strike down a state statute, Fla. Stat. §559.94 (1987), outlawing the use of the "plug molding" process. This process allowed one competitor to use the hull of a rival producer as the "plug" to create a mold that it then used to make identical hulls for its own use. No passing off or confusion was involved, but the plug mold technique allowed a later competitor to produce a hull at lower cost than the initial entrant. The Supreme Court limited protection for the hull design to that available under the federal patent statutes.

> The Florida scheme offers [its] protection for an unlimited number of years to all boat hulls and their component parts, without regard to their ornamental or technological merit. Protection is available for subject matter for which patent protection has been denied or has expired, as well as for designs which have been freely revealed to the consuming public by their creators.
>
> . . . We think it clear that such protection conflicts with the federal policy "that all ideas in general circulation be dedicated to the common good unless they are protected by a valid patent."

**8. *Trade Secrets.*** Current law also gives extensive protection to trade secrets, defined in the First Restatement §757, comment *b* as

> any formula, pattern, device or compilation of information which is used in one's business, and which gives him an opportunity to obtain an advantage over competitors who do not know or use it. It may be a formula for a chemical compound, a process of manufacturing, treating or preserving materials, a pattern for a machine or other device, or a list of customers.

The Restatement (Third) Unfair Competition §39 (1995) now provides:

> A trade secret is any information that can be used in the operation of a business or other enterprise and that is sufficiently valuable and secret to afford an actual or potential economic advantage over others.

Trade secrets often protect certain types of unpatentable materials (e.g., industrial "know-how"). Sometimes firms treat as trade secrets materials of doubtful patentability, or even matters that are clearly patentable, if they believe, as is often the case with "process" patents, that the disclosure of information through patenting will allow others to make undetectable but unauthorized use of their process.

After *Sears*, it was an open question whether patent law preempted state trade secret law. The Court resolved that question against preemption and in favor of extended trade secret protection in Kewanee Oil Co. v. Bicron Corp., 416 U.S. 470, 483–84 (1974), both for non-patentable and patentable trade secrets. On the former, Burger, C.J., wrote:

> Abolition of trade secret protection would, therefore, not result in increased disclosure to the public of discoveries in the area of nonpatentable subject matter. Also, it is hard to see how the public would be benefited by disclosure of customer lists or advertising campaigns; in fact, keeping such items secret encourages businesses to initiate new and individualized plans of operation, and constructive competition results.

The Court approved of trade secret protection for arguably patentable material:

> Certainly the patent policy of encouraging invention is not disturbed by the existence of another form of incentive to invention. In this respect the two systems are not and never would be in conflict. Similarly, the policy that matter once in the public domain must remain in the public domain is not incompatible with the existence of trade secret protection. By definition a trade secret has not been placed in the public domain.

Finally the Court extended trade secret protection to cases of clear patentability, because its denial might encourage private parties to adopt complex and costly security devices that could hamper innovation or, in the alternative, be driven to apply for a patent that they otherwise would not seek.

On the general question of preemption, see Paul Goldstein, *Kewanee Oil Co. v. Bicron Corp.*: Notes on a Closing Circle, 1974 Sup. Ct. Rev. 81.

**9. *Copyrights.*** For the current legal position on preemption under the copyright laws, see Copyright Act of 1976, 17 U.S.C. §301 (2024), governing works created as of January 1, 1978. It first preempts state law with respect to "works of authorship that are fixed in a tangible medium of expression" only to later provide that

> [n]othing in this title annuls or limits any rights or remedies under the common law or statutes of any State with respect to (1) subject matter that does not come within the subject matter of copyright . . . including works of authorship not fixed in any tangible medium of expression, or . . . (3) activities violating legal or equitable rights that are not equivalent to any of the exclusive rights within the general scope of copyright.

In ProCD, Inc. v Zeidenberg, 86 F.3d 1447, 1454 (7th Cir. 1996), the defendant Zeidenberg used a database supplied by ProCD for commercial purposes in violation of his agreement with the plaintiff ProCD. Easterbrook, J., denied that Zeidenberg's otherwise valid contract action was preempted by the Copyright Act.

> Rights "equivalent to any of the exclusive rights within the general scope of copyright" are rights established by law — rights that restrict the options of persons who are strangers to the author. Copyright law forbids duplication, public performance, and so on, unless the person wishing to copy or perform the work gets permission; silence means a ban on copying. A copyright is a right against the world. Contracts, by contrast, generally affect only their parties; strangers may do as they please, so contracts do not create "exclusive rights."

Chicago Board Options Exchange, Inc. v. International Securities Exchange, L.L.C., 973 N.E.2d 390, 398 (Ill. 2012), likewise distinguishes wrongful *copying* from wrongful *use*, declining to apply Copyright Act preemption to the mere use of stock index information that is already in the public domain. But see Adina's Jewels, Inc. v. Shashi, Inc., 442 F. Supp. 3d 766, 772 (S.D.N.Y. 2020) (declining to consider a claim for copying jewelry design as a trademark claim, which would not be preempted by the Act, and instead holding that the alleged "copying and knocking off [of] highly stylized jewelry products" is preempted because it "neatly falls within the bounds of the infringement protection").

For different views on this preemption argument, compare Mark A. Lemley, Intellectual Property and Shrinkwrap Licenses, 68 S. Cal. L. Rev. 1239, 1255–59 (1995), with Richard A. Epstein, *ProCD v. Zeidenberg*: Do Doctrine and Function Mix?, *in* Contract Stories 94, 113–21 (Baird ed., 2006). On the copyright law generally, see William M. Landes & Richard A. Posner, An Economic Analysis of Copyright Law, 18 J. Legal Stud. 325 (1989).

Proof of infringement can often be difficult when copying involves both protected and unprotected works. In Compulife Software Inc. v. Newman, 959 F.3d 1288, 1306 (11th Cir. 2020):

> [C]opyright-infringement analysis should proceed as follows: Once the plaintiff has proven that he has a valid copyright and that the defendant engaged in factual copying, the defendant may seek to prove that some or all of the copied material is unprotectable. If the defendant carries this burden as to any portion of the copied material, that material should be filtered out of the analysis before comparing the two works. After filtration is complete, the burden shifts back to the plaintiff to prove substantial similarity between any remaining (*i.e.*, unfiltered) protectable material and the allegedly infringing work. If the defendant demonstrates — at the filtration stage — that it copied only unprotectable material, such that no substantial similarities remain after filtration, the defendant is entitled to summary judgment.

**10. *Artificial Intelligence and Unfair Competition.*** Companies deploying artificial intelligence are the latest targets of unfair competition suits. In Leovy v. Google LLC, No.

3:23-cv-03440 (N.D. Cal.), the plaintiffs allege all manner of business torts related to Google's use of information on the Internet to train its AI model, Bard. Google's motion to dismiss defends its large language models' massive aggregation of source information as a lawful business practice:

> Plaintiffs imagine they have a property or privacy right in information they shared publicly on the internet that entitles them to stop anyone from gathering and using such information in ways they don't like, such as for generative AI. But outside copyright law (including its protection for fair use), there is no general right to control publicly-available information. . . . Gathering and using public information is not, as Plaintiffs claim on behalf of all U.S. internet users, "stealing." Nor is it an invasion of privacy, trespass, hacking, negligence, unfair competition, or any of the other wrongs Plaintiffs charge. Accordingly, Plaintiffs' state law claims should be dismissed.

Motion to Dismiss (ECF No. 35), at 1–2. Further, as discussed *supra* Note 9, at 272, Copyright Act preemption will likely be a live issue in this potential wave of litigation:

> Plaintiffs aver that Google copied written text, photographs, videos, and audio that Plaintiffs posted online. . . .
>
> . . . The Copyright Act affords exclusive rights to "reproduce the copyrighted work in copies," "prepare derivative works," and "distribute" and "display" copies publicly. 17 U.S.C. §§106(1)-(3), (5). These theories underlie Plaintiffs' [consumer fraud], larceny/conversion/trespass, unjust enrichment, negligence, and intentional interference claims, which all allege that Google copied Plaintiffs' information from the internet, used it to create an AI model, and/or further displayed it to the public, all without Plaintiffs' consent. In other words, Plaintiffs assert rights to control the reproduction and public distribution of their creative content posted on the internet, and its use to create another work. Those are copyright claims masquerading as state-law property claims, and they are preempted. . . . Plaintiffs' unfair competition claim is likewise preempted to the extent predicated on these state law claims or alleged copyright infringement.

*Id*. at 28–29.

In New York Times Co. v. Microsoft Corp., No. 1:23-cv-11195 (S.D.N.Y.), The New York Times makes a more targeted allegation that Microsoft, through OpenAI, illegally appropriated, without consent, huge amounts of stored data culled from New York Times sources to train ChatGPT, which then operates in direct competition with the Times's online services. Microsoft's motion to dismiss invokes *INS* (*supra* at 253) and *NBA* (*supra* at 258), asserting that AI "large-language models" are not "spitting out today's news," such that a "hot news" exception applies to copyright preemption. Motion to Dismiss (ECF No. 65), at 22. Microsoft seeks to cast doubt that "the GPT-based tools 'would so reduce the incentive to produce' [*New York Times*] content 'that its existence or quality would be substantially threatened.'" *Id*. at 23 (quoting NBA v. Motorola, Inc., 105 F.3d 841, 845 (2d Cir. 1997)). Does the Times have an action if the defendants attribute to the Times stories that it did not run? Does it matter the use of the material did not result in verbatim copying as in *INS*?

## CHAPTER 5

# PUBLIC NUISANCE

## SECTION A. INTRODUCTION

**RESTATEMENT OF THE LAW (SECOND) OF TORTS**

**§821B. Public Nuisance**

(1) A public nuisance is an unreasonable interference with a right common to the general public.

(2) Circumstances that may sustain a holding that an interference with a public right is unreasonable include the following:

(a) Whether the conduct involves a significant interference with the public health, the public safety, the public peace, the public comfort or the public convenience, or

(b) whether the conduct is proscribed by a statute, ordinance or administrative regulation, or

(c) whether the conduct is of a continuing nature or has produced a permanent or long-lasting effect, and, as the actor knows or has reason to know, has a significant effect upon the public right.

***Comment i. Action for Damages Distinguished from One for Injunction:*** In determining whether to award damages, the court's task is to decide whether it is unreasonable to engage in the conduct without paying for the harm done. Although a general activity may have great utility it may still be unreasonable to inflict the harm without compensating for it. In an action for injunction the question is whether the activity itself is so unreasonable that it must be stopped. It may be reasonable to continue an important activity if payment is made for the harm it is causing, but unreasonable to continue it without paying.

**§821C. Who Can Recover for Public Nuisance**

(1) In order to recover damages in an individual action for a public nuisance, one must have suffered harm of a kind different from that suffered by other members of the public exercising the right common to the general public that was the subject of interference.

(2) In order to maintain a proceeding to enjoin to abate a public nuisance, one must

(a) have the right to recover damages, as indicated in Subsection (1), or

(b) have authority as a public official or public agency to represent the state or a political subdivision in the matter, or

(c) have standing to sue as a representative of the general public, as a citizen in a citizen's action or as a member of a class in a class action.



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## SECTION B. PRIVATE PUBLIC NUISANCE

### 1. Traditional

#### *Anonymous*

Y.B. Mich. 27 Hen. 8, f. 27, pl. 10 (1536)

One brought a Writ sur son cas [on his case] against another. He alleged that, whereas the plaintiff had used to have a way from his house to a close over the King's highway for carriage and re-carriage, etc., the defendant had stopped the King's highway, so that the plaintiff could not go to his aforesaid close, to his tort and damage.

Baldwin, C.J. It seems to me that this action does not lie to the plaintiff for the stopping of the highway; for the King has the punishment of that, and he has his plaint in the Leet and there he has his redress, because it is a common nuisance to all the King's lieges, and so there is no reason for a private particular person to have an accion sur son cas; for if one person shall have an action for this, by the same reason every person shall have an action, and so he will be punished a hundred times on the same case.

Fitzherbert, J., to the contrary. I agree well that each nuisance done in the King's highway is punishable in the Leet and not by an action, unless it be where one man has suffered greater hurt or inconvenience than the generality have; but he who has suffered such greater displeasure or hurt can have an action to recover the damage which he has by reason of this special hurt. So if one makes a ditch across the highway, and I come riding along the way in the night and I and my horse are thrown into the ditch so that I have great damage and displeasure thereby, I shall have an action here against him who made this ditch across the highway, because I have suffered more damage than any other person. So here the plaintiff had more convenience by this highway than any other person had, and so when he is stopped he suffers more damage because he has no way to go to his close. Wherefore it seems to me that he shall have this action pour ce special matiere [for his special harm]: but if he had not suffered greater damage than all others suffered, then he would not have the action. Quod Nota. [Which was noted.]

## NOTE

***Private Public Nuisances.*** S.C. Code Ann. §49-1-10 (2024) treats all navigable streams as common highways, and defines their obstruction as a public nuisance. But that section says nothing about what private actions could be maintained in the event of breach. In Overcash v. South Carolina Electric & Gas Co., 614 S.E.2d 619, 621 (S.C. 2005), the plaintiff was seriously injured in a boating accident involving a dock obstruction in public waters. Burnett, J., denied the cause of action:

> The dissent by Justice Fitzherbert in a 1536 King's Bench decision [*supra*] derailed the course of nuisance law as a branch of the common law, which once dealt only with harm to real property.* Justice Fitzherbert argued against the contemporaneous understanding of the law in advocating an individual's action for special or particular damage, including personal injury, should be recognized under a cause of action for public nuisance. Although Justice Fitzherbert's view

*[Fitzherbert's decision was in fact the majority decision, even though the Chief Justice spoke first.—Eds.]

> has been widely followed by other courts, we decline to recognize a common law cause of action under the doctrine of public nuisance for purely personal injuries.

Why not an ordinary negligence action? Even if the cause of action were not dismissed in that case, were the injuries suffered sufficiently "different in kind" so as to permit recovery under the Second Restatement's approach?

## *Burgess v. M/V Tamano*

370 F. Supp. 247 (D. Me. 1973)

Gignoux, J. Plaintiffs in these class actions seek to recover damages incurred as a result of the discharge into the waters of Casco Bay of approximately 100,000 gallons of Bunker C oil from the tanker M/V TAMANO early on the morning of July 22, 1972, when she struck an outcropping of "Soldier Ledge" while passing through Hussey Sound en route to the port of Portland. Variously named as defendants or third-party defendants are the TAMANO, her owners, her captain, her pilot and the local pilots' association, her charterer, Texaco, Inc., the State of Maine, and the United States of America. Liability is asserted on theories of negligence, unseaworthiness, trespass and nuisance. . . .

Presently before the Court are defendants' motions to dismiss the claims of three of the plaintiff classes: the commercial fishermen . . . ; the commercial clam diggers . . . ; and . . . the owners of motels, trailer parks, camp grounds, restaurants, grocery stores, and similar establishments in Old Orchard Beach, whose businesses are dependent on tourist trade. . . . [D]efendants contend that the economic interests (loss of profits and impairment of earning capacity) which these classes of plaintiffs assert to have been damaged by the oil spill are not legally cognizable because none of the classes had any property interest in the coastal waters and marine life or shores claimed to have been injured by the spill. For reasons to be briefly stated, the Court holds that the motions to dismiss the claims of the commercial fishermen and clam diggers must be denied, but that the motions to dismiss the claims of the Old Orchard Beach businessmen, other than those who owned shore property physically injured by the spill, must be granted. . . .

First, as to the claims of the commercial fishermen and clam diggers, it is not disputed that title to its coastal waters and marine life, including the seabeds and the beds of all tidal waters, is vested in the State of Maine and that individual citizens have no separate property interest therein. It is also uncontroverted that the right to fish or to harvest clams in Maine's coastal waters is not the private right of any individual, but is a public right held by the State "in trust for the common benefit of the people." Moulton v. Libbey, 37 Me. 472, 488 (1854). Since the fishermen and clam diggers have no individual property rights with respect to the waters and marine life allegedly harmed by the oil spill, their right to recover in the present action depends upon whether they may maintain private actions for damages based upon the alleged tortious invasion of public rights which are held by the State of Maine in trust for the common benefit of all the people. As to this issue, the long standing rule of law is that a private individual can recover in tort for invasion of a public right only if he has suffered damage particular to him — that is, damage different in kind, rather than simply in degree, from that sustained by the public generally. Prosser, Law of Torts, §88 at 586–87 (4th ed. 1971); Restatement (Second) of Torts §821C(1) (Tent. Draft No. 17, 1971). Concededly, the line between damages different in kind and those different only in degree from those suffered by the public at large has been difficult to draw. But the Court is persuaded that the commercial fishermen and clam diggers have sufficiently alleged "particular" damage to support their private actions.

The commercial fishermen and clam diggers in the present cases clearly have a special interest, quite apart from that of the public generally, to take fish and harvest clams from the coastal waters of the State of Maine. The injury of which they complain has resulted from defendants' alleged interference with their direct exercise of the public right to fish and to dig clams. It would be an incongruous result for the Court to say that a man engaged in commercial fishing or clamming, and dependent thereon for his livelihood, who may have had his business destroyed by the tortious act of another, should be denied any right to recover for his pecuniary loss on the ground that his injury is no different in kind from that sustained by the general public. Indeed, in substantially all of those cases in which commercial fishermen using public waters have sought damages for the pollution or other tortious invasion of those waters, they have been permitted to recover [citing myriad cases]. These cases are no more than applications of the more general principle that pecuniary loss to the plaintiff will be regarded as different in kind "where the plaintiff has an established business making a commercial use of the public right with which the defendant interferes. . . ." Prosser, Law of Torts. In the view of this Court, to the extent their pecuniary losses can be established, the commercial fishermen and clam diggers should be entitled to recover for the same.

Unlike the commercial fishermen and clam diggers, the Old Orchard Beach businessmen do not assert any interference with their direct exercise of a public right. They complain only of loss of customers indirectly resulting from alleged pollution of the coastal waters and beaches in which they do not have a property interest. Although in some instances their damage may be greater in degree, the injury of which they complain, which is derivative from that of the public at large, is common to all businesses and residents of the Old Orchard Beach area.

In such circumstances, the line is drawn and the courts have consistently denied recovery. In the view of this Court, the Old Orchard Beach businessmen can show no such distinct harm from the oil spill as to support their present action.

[Defendants' motions to dismiss the claims of the commercial fisherman and clam diggers denied. Motions to dismiss the claims of the businessmen are granted.]

## *532 Madison Ave. Gourmet Foods, Inc. v. Finlandia Center, Inc.*

750 N.E.2d 1097 (N.Y. 2001)

Kaye, C.J. Two of the three appeals involve the same event. On December 7, 1997, a section of the south wall of 540 Madison Avenue, a 39-story office tower, partially collapsed and bricks, mortar and other material fell onto Madison Avenue at 55th Street, a prime commercial location crammed with stores and skyscrapers. The collapse occurred after a construction project, which included putting 94 holes for windows into the building's south wall, aggravated existing structural defects. New York City officials directed the closure of 15 heavily trafficked blocks on Madison Avenue—from 42nd to 57th Street—as well as adjacent side streets between Fifth and Park Avenues. The closure lasted for approximately two weeks, but some businesses nearest to 540 Madison remained closed for a longer period. . . .

Plaintiffs contend that they stated valid causes of action for public nuisance, alleging that the collapses forced closure of their establishments, causing special damages beyond those suffered by the public.

A public nuisance exists for conduct that amounts to a substantial interference with the exercise of a common right of the public, thereby offending public morals, interfering with the use by the public of a public place or endangering or injuring the property, health, safety

or comfort of a considerable number of persons. A public nuisance is a violation against the State and is subject to abatement or prosecution by the proper governmental authority.

A public nuisance is actionable by a private person only if it is shown that the person suffered special injury beyond that suffered by the community at large. This principle recognizes the necessity of guarding against the multiplicity of lawsuits that would follow if everyone were permitted to seek redress for a wrong common to the public. . . .

The question here is whether plaintiffs have suffered a special injury beyond that of the community so as to support their damages claims for public nuisance.

In *Burns Jackson Miller Summit & Spitzer v. Lindner*, 59 N.Y.2d 314 (N.Y. 1983) we refused to permit a public nuisance cause of action by two law firms seeking damages for increased expenses and lost profits resulting from the closure of the New York City transit system during a labor strike. We concluded that, because the strike was so widespread, every person, firm and corporation conducting a business or profession in the City suffered similar damage and thus the plaintiffs could not establish an injury different from that of the public at large.

While not as widespread as the transit strike, the Madison Avenue and Times Square closures caused the same sort of injury to the communities that live and work in those extraordinarily populous areas. . . . When business interference and ensuing pecuniary damage is "so general and widespread as to affect a whole community, or a very wide area within it, the line is drawn[.]" Prosser, Private Action for Public Nuisance, 52 Va. L. Rev. 997, 1015 (1966). While the degree of harm to the named plaintiffs may have been greater than to the window washer, per diem employee or neighborhood resident unable to reach the premises, in kind the harm was the same.

*Leo v. General Elec. Co.*, 145 A.D.2d 291, 538 N.Y.S.2d 844, is inapposite. In *Leo*, the Appellate Division recognized a private right of action by plaintiff commercial fishermen who contended that defendant's pollution of the Hudson River with toxic polychlorinated biphenyls (commonly known as PCBs), created a public nuisance that had a devastating effect on their ability to earn a living. Plaintiffs were able to establish that their injuries were special and different in kind, not merely in degree: a loss of livelihood was not suffered by every person who fished the Hudson. By contrast, every person who maintained a business, profession or residence in the heavily populated areas of Times Square and Madison Avenue was exposed to similar economic loss during the closure periods. Thus, in that the economic loss was "common to an entire community and the plaintiff[s] suffer[ed] it only in a greater degree than others, it is not a different kind of harm and the plaintiff[s] cannot recover for the invasion of the public right." RST §821C comment *h*. . . .

[T]he order of the Appellate Division should be reversed, with costs, the defendants' motion to dismiss the complaint granted and the certified question answered in the negative.

## NOTES

**1.** ***"Special" Injury Requirement.*** General damages from public nuisances are controlled exclusively by direct public action, usually administrative regulation or criminal prosecution. The private action is maintainable only for "special," "peculiar," or "disproportionate" harm to the individual plaintiff. The reasons for this division lie less in matters of justice and more in matters of administration. The traditional requirement of special damages for public nuisance was intended to exclude large numbers of small claims by achieving the appropriate deterrence through direct administrative actions. General damages are of low intensity and

are widely diffused across an extended population. Private actions for admitted grievances are therefore simply too costly to maintain. The enforcement function is centralized to preserve the deterrent and control objectives of the tort law, even though direct compensation to aggrieved parties is necessarily abandoned.

When, however, the harms are "special," private actions may again be maintained, as in all ordinary tort situations, for now the administrative burdens are far smaller relative to the size of the stakes. See generally Richard A. Epstein, Nuisance Law: Corrective Justice and Its Utilitarian Constraints, 8 J. Legal Stud. 49, 98–102 (1979). What is the relationship between public nuisances and the live and let live doctrine in the law of private nuisances?

Catherine M. Sharkey, Public Nuisance as Modern Business Tort: A New Unified Framework for Liability for Economic Harms, 70 DePaul L. Rev. 431, 448–50 (2020), elaborates upon the enforcement rationale, whereby the special injury rule deputizes a subclass of impacted individuals or entities to sue to force the tortfeasor to internalize the social costs of its activities. Sharkey contends that this "channeling" rationale explains why the "'special injury' requirement has emerged as the core doctrinal distinction" between cognizable public nuisance claims and barred negligent interference with economic relations claims.

The Third Restatement sets forth a limitation of liability rationale, noting that absent the special injury requirement, "[d]efendants would be subject to potentially massive and unpredictable liabilities, and courts would be faced with a large and unwieldy number of lawsuits." RTT: LEH §8, cmt. *c*. Does the special injury requirement exist solely to limit defendants' public nuisance liability for pure economic harms? Who has the better argument? Is the special injury requirement a means to achieve optimal deterrence by identifying the "right" victims? Or is it animated by the same limitation-of-liability concerns driving the stranger economic loss rule, as in the *Southern California Gas* court's treatment of plaintiffs' negligence claims? See *supra* Chapter 1, Section D, at 27.

Courts have struggled to articulate what amounts to private harms that are "different in kind" from those of the general public. Consider Mills v. Hall & Richards, 9 Wend. 315–16 (N.Y. Sup. Ct. 1832), where defendant had built a dam that created a pool of water that attracted malarial mosquitoes, and "after the rebuilding of the dam, the fever and ague was more common in that section of the country than it had been before." Plaintiff and his family suffered health effects. Sutherland, J., wrote: "a man may overflow his own land; but if such overflow spread disease and death through the neighborhood, it may be abated, and he must respond in damages for the special injury which any individual may have sustained from it."

Contrast *Mills* with Palmer v. Amazon.com, Inc., 51 F.4th 491, 519–21 (2d Cir. 2022), where workers at an 840,000-square-foot Amazon fulfillment center warehouse on Staten Island claimed that Amazon's workplace policies prevented workers from engaging in COVID-19 preventative social distancing or basic hygiene and sanitation practices. Nardini, J., concluded that "although Plaintiffs may plead a harm that is different *in degree* from the community at large, they fail to plead a harm that is different *in kind*, thereby failing to allege the special injury required to state a claim for public nuisance under New York law." Chin, J., dissented:

> Plaintiffs faced heightened COVID-19 risks due to the conditions of their employment. The harms here . . . are different in kind because they resulted from Amazon's affirmative decisions not to implement any sufficient measures to mitigate the high risk of COVID-19 transmission inherent in warehouse work.

What is the violation of the public right alleged by the workers in *Palmer*? Which position aligns with *Mills*?

**2.** ***Commercial Fishermen's Exception?*** One complication involves ownership of the fish. "The plaintiffs who do not own the fish cannot complain if the Union Oil company

captures them. As they cannot complain of capture, they cannot complain of destruction after capture. As they cannot complain of destruction after capture, they cannot complain of destruction before capture." Richard A. Epstein, Nuisance Law: Corrective Justice and Its Utilitarian Constraints, 8 J. Legal Stud. 49, 52 (1979). This position overlooks, however, the problem of the common pool — that is, that resources not subject to private ownership will be destroyed or consumed too rapidly. Because the fish are unowned, any individual actor motivated by self-interest will not take into account the social losses that premature capture and destruction work on the common pool. See generally Richard James Sweeney, Robert D. Tollison & Thomas D. Willett, Market Failure, the Common-Pool Problem, and Ocean Resource Exploitation, 17 J.L. & Econ. 179 (1974). *Oppen* fills the gap by providing the tort action to the nonowners who suffer disproportionate impact. In Pruitt v. Allied Chemical Corp., 523 F. Supp. 975 (E.D. Va. 1981), the district court allowed the suits of the commercial fishermen and the marina, boat, tackle, and bait shop owners who were damaged by the spillage of kepone into the James River and the Chesapeake Bay. However, it denied the actions of the various seafood wholesalers, retailers, and distributors who purchased and marketed the seafood of the commercial fishermen whose harm was deemed "insufficiently direct." It also refused to allow actions by employees of the various groups named. Is this consistent with *Darnell-Taenzer* and *Illinois Brick*?

Similarly, in *In re* Exxon Valdez, 104 F.3d 1196, 1198 (9th Cir. 1997), stemming from the massive oil spill from the *Exxon Valdez* oil tanker, the court allowed the plaintiff class of Alaska natives to recover economic damage from loss of fishing resources, but refused to permit their claim for "cultural damage" to their "subsistence way of life." The *Exxon Valdez* oil spill prompted Congress to address the legal barriers to recovery for anyone other than commercial fishermen by enacting a comprehensive scheme for economic recovery in the wake of an oil spill. The Oil Pollution Act of 1990, 33 U.S.C. §2702 et seq. (2024), altered the common law landscape by allowing any claimant who suffered economic losses to pursue a claim against a "responsible party." It was against the backdrop of the Oil Pollution Act that BP plc funded the Court Supervised Settlement Program as part of a class action settlement of the consolidated multidistrict litigation (MDL) arising from the Deepwater Horizon oil spill in the Gulf of Mexico, and then later reached a class-wide punitive damages settlement with Halliburton, one of BP's codefendants. See Catherine M. Sharkey, The BP Oil Spill Settlements, Classwide Punitive Damages, and Societal Deterrence, 64 DePaul L. Rev. 681 (2015).

**3. *Intentional and Unreasonable?*** For a claim to sound in public nuisance, a defendant's "wrongful act" must cause harm to a right held in common — a *public* right. RTT: LEH §8, cmt. *b*. In jurisdictions with public nuisance statutes, a defendant's conduct may be wrongful per se. In jurisdictions without public nuisance statutes, plaintiffs may have to show that "the conduct was intentional and unprivileged, that it was unreasonable, or that it was subject to strict liability." Note that reasonableness may itself be determined by reference to *other* statutes. See City and County of San Francisco v. Purdue Pharma L.P., *infra* at 284 ("Conduct is unreasonable if it violates a statute, ordinance, or administrative regulation.").

**4. *A Land- (and Water-) Based Tort?*** Professor Epstein maintains that "the interests in lands, air, or water protected by the law of nuisance are identical for both private and public nuisance," and that neither private nor public nuisance "has ever covered financial losses. . . ." *Amicus Curiae* Brief of Competitive Enterprise Institute at 8, Oklahoma *ex rel.* Hunter v. Johnson & Johnson, Appeal No. 118,474 (Okla. Oct. 22, 2020). Epstein contends, moreover, that the public nuisance tort "alters the doctrine of causation to take into account the creation of rights of way, as on a public highway" and recognizes "indirect forms of harm, such as pouring water into a reservoir, which then escapes when its weight is sufficient to burst through its foundation." On this view, these limited expansions of causation theory provide a sort of institutional accommodation — they allow for scalable litigation to address blockages

of public ways. But causation is never expanded "to the point where the chain of indirect causes is allowed to stretch to infinity. If the water is stable in a reservoir, the defendant will not be responsible if a third person wrecks its foundations so that the water can escape." Richard A. Epstein, Beware of Prods and Pleas: A Defense of the Conventional Views on Tort and Administrative Law in the Context of Global Warming, 121 Yale L.J. 317, 321–22 (2011).

How would Epstein's classical understanding apply to *532 Madison Ave.*? There was, after all, a blockage of a public way. Is the court's liability-limitation understanding of the special injury requirement reconcilable with Epstein's theory? For example, would it be feasible to limit liability by conferring special injury standing only on plaintiffs who can no longer access their workplace due to the blockage, as opposed to vendors (capable of relocation) who can still access their wares but face reduced foot traffic due to the effects of the collapse on surrounding streets?

## 2. A New Business Tort?

**RESTATEMENT OF THE LAW (THIRD) OF TORTS: LIABILITY FOR ECONOMIC HARM**

**§8. Public Nuisance Resulting in Economic Loss**

An actor whose wrongful conduct harms or obstructs a public resource or public property is subject to liability for resulting economic loss if the claimant's losses are distinct in kind from those suffered by members of the affected community in general.

## NOTES

**1. *Public Nuisance and Economic Losses.*** The Third Restatement distinguishes between public nuisances that cause physical harm to persons or property and those that cause purely economic harm. RTT: LEH §8 excludes public nuisance claims that arise from "physical harm, as when a defendant negligently leaves an obstruction in a road and the plaintiff collides with it, or as when a defendant's pollution causes damage to property that the plaintiff owns." RTT: LEH §8, cmt. *a*. Is this a principled or stable distinction? Recall that interference with the use and enjoyment of property is the hallmark of nuisance law. Does an unabated public nuisance that reduces foot traffic to a business, but does not physically damage a business owner's property, fall within the ambit of §8? What if a public nuisance causes incidental, trifling physical damage to a property (such as a cloud of soot mildly damaging paint), but most of a plaintiff's loss can be characterized as pure economic harm?

**2. *A New Theory of Liability?*** In *Southern California Gas, supra* Chapter 1, at 27, a massive leak in a Los Angeles suburb caused massive dislocation of both businesses and residences, but no physical injuries. These businesses sued for economic recovery nonetheless. Professors Mark Gergen, Stephen Sugarman, and Gregory Keating filed an amicus brief supporting recovery, noting that the business plaintiffs' claims are covered by the public nuisance rule of RTT: LEH §8. Application for Leave to File Amicus Curiae Brief and Amicus Curiae Brief of California Tort Law Scholars in Support of Affirmance at 17, *In re* S. Cal. Gas Leak Cases, 441 P.3d 881 (Cal. 2019) (No. S246669). The scholars argued that RTT: LEH §8 applies to the claims for damages resulting from economic loss. They found limitations of liability in the "special injury" requirement of comment *c*. And they explained that comment *c* weighs the plaintiffs' need for appropriate compensation and deterrence against the defendants' need to

reduce redundant litigation, which may lead to overdeterrence. The scholars also pointed to the special injury requirement's role in separating plaintiffs who may sue from those who may not—ideally in a "principled fashion." Weighing these competing considerations, the scholars concluded that the business plaintiffs seeking lost profits due to the gas leak suffered no "actionable injury" under RTT: LEH §8.

Note that in *Southern California Gas Co.*, the California Supreme Court rejected the plaintiffs' claims by applying RTT: LEH §7's general no duty rule, *not* §8's special injury requirement. Public nuisance received only a fleeting mention:

> In justifying that position, the Restatement echoes widespread judicial concern that purely economic losses "proliferate more easily than losses of other kinds" and "are not self-limiting" in the same way. Those characteristics, the Restatement explains, threaten "liabilities that are indeterminate and out of proportion to [a defendant's] culpability," and with them "exaggerated pressure to avoid an activity altogether." For centuries, in fact, similar concerns have justified strict limits on private recovery for a public nuisance. See 4 Blackstone, Commentaries 167 (noting that a public nuisance is usually not privately actionable because "it would be unreasonable to multiply suits by giving every man a separate right of action").

S. Cal. Gas Co. v. Superior Court of L.A. Cnty., 441 P.3d 881, 892 (Cal. 2019) (No. S246669).

But the amici scholars also contended that §7 is inappropriate to resolve the case, even though they arrive at the same conclusion as the Court on plaintiffs' recovery for pure economic loss. Why? Does it matter that §7's limited but general no-duty rule is grounded in considerations pertaining to judicial economy, as opposed to a subject-specific no duty rule for negligent interference with contract or prospective economic advantage? If §7 is about judicial economy, then why do amici insist on applying §8's special injury requirement?

**3. *Historical Roots of "Channeling" in Unfair Competition Torts.*** Catherine M. Sharkey, Public Nuisance as Modern Business Tort, *supra* Note 1, at 280, traces the channeling rationale in modern public nuisance actions back to historical unfair competition cases stretching back to the eighteenth century. In Ely-Norris Safe Co. v. Mosler Safe Co., *supra* Chapter 4, at 265, Judge Learned Hand held that at common law, a business competitor may not assert the rights of consumers. 7 F.2d 603, 604 (2d Cir. 1925), *rev'd on other grounds*, 273 U.S. 132 (1927). Judge Hand employed language that implied both an awareness of and a rejection of the channeling rationale. He noted that "[t]he law does not allow [a competitor] to sue as a vicarious avenger of the defendant's customers." The Lanham Act dispenses with *Mosler Safe*'s restriction on competitor standing and recognizes competitor rights against a false designator of origin or a false description or representation. See 15 U.S.C. §1125 (2018). As in the public nuisance context, the "channeling" rationale explains conferring standing on the party most invested in asserting their own interest, and therefore best able to overcome the coordination problem faced by potential plaintiffs with lesser injuries. Tarleton v. M'Gawley, 170 Eng. Rep. 153 (K.B. 1793), *supra* Chapter 4, at 237, provides another vivid illustration. There, the plaintiff sought recovery for tortious interference with prospective economic advantage from a defendant who fired shots to prevent indigenous people from trading with his competitor. Note that, as in *Mosler Safe*, there is only one party with both a sufficiently weighty injury and the resources and desire to sue. But by filing suit, the plaintiff in *Tarleton* also vindicates the economic interests of the indigenous traders and prevents the social loss that might result if trading were to be interrupted.

Do you see any analogy to public nuisance? Is it fair to say that in public nuisance cases, "special injury" plaintiffs always vindicate the interests of the general public? Are "special injury" plaintiffs best positioned to mitigate social loss? Or is this inquiry specific to particular plaintiffs and particular injuries?

In Laborers 17 Health and Benefit Fund v. Philip Morris, Inc., 191 F.3d 229, 236 (2d Cir. 1999), *supra* Chapter 3, at 179, the Second Circuit reiterated the "direct injury" test for RICO standing. The court rejected the plaintiffs' efforts to substitute for that test a "zone of interests test," which asks whether plaintiffs are "within the class of persons sought to be benefited by the provision at issue." (quoting Holmes v. Sec. Inv'r Prot. Corp., 503 U.S. 258, 287 (1992) (Scalia, J., concurring)). Does *Laborers 17* suggest that the direct injury test reflects something more than a "channeling" rationale? After all, if a plaintiff can allege a concrete injury *and* show that Congress has singled them out as a class for standing, why should courts not defer to Congress's judgment on the "channeling" question?

## SECTION C. PUBLIC PUBLIC NUISANCE

### 1. Opioids

### *City and County of San Francisco v. Purdue Pharma L.P.*

620 F. Supp. 3d 936 (N.D. Cal. 2022)

Breyer, J. The opioid epidemic has plagued San Francisco for over twenty years. The number of individuals who die annually from opioid overdoses continues to climb. Thousands of city residents, from all walks of life, struggle with addiction. Widespread opioid use has strained the city's hospitals. It has forced streets, parks, and public spaces to close. It has exacerbated crime and homelessness. Every year, San Francisco devotes significant resources to a multi-prong fight against the opioid epidemic. That fight includes this case.

This case is part of a nationwide multidistrict litigation stemming from the ongoing opioid epidemic. Cities, counties, and states across the country have filed claims against manufacturers, distributors, and dispensers of prescription opioids. While the facts of each case vary, the claims center on the contention that each defendant has contributed to the opioid epidemic that has engulfed the country . . .

At trial, Plaintiff brought a single public nuisance claim against Walgreens. The question for the Court is whether Plaintiff proffered sufficient evidence at trial to prove this claim. To carry its burden of proof, Plaintiff had to establish that it is more likely than not that Walgreens knowingly engaged in unreasonable conduct that was a substantial factor in contributing to the opioid epidemic in San Francisco. After careful consideration of the evidence, the Court finds that Plaintiff carried its burden. . . .

#### I. Findings of Fact

. . . For over two decades, San Francisco has been battling an opioid epidemic, defined by high rates of opioid abuse and addiction throughout the city. . . .

San Franciscans grapple with the effects of the opioid epidemic every day. City workers, including park rangers, street cleaners, fire fighters, paramedics, doctors, and librarians, respond to overdoses, clean up opioid debris, and work to help those suffering from opioid addiction. Neighborhoods across the city have been devastated. Residents' use of public areas — like parks, sidewalks, and libraries — has been significantly impaired and, in some cases, ruined. Even right outside this courthouse, people suffering from severe opioid addiction buy, sell, and use opioids in plain sight. The impact on the city has been "worse than catastrophic." . . .

[Breyer, J., discussed at length trial evidence to support its findings of fact:

"Walgreens is the largest retail pharmacy chain in San Francisco. Between 2006 and 2020, Walgreens distributed and dispensed over one hundred million prescription opioid pills in the city. The Controlled Substances Act ("CSA") and its implementing regulations impose duties on distributors and dispensers of prescription opioids. In exchange for the privilege of distributing and dispensing prescription opioids, Walgreens has regulatory obligations to take reasonable steps to prevent the drugs from being diverted and harming the public. The evidence at trial established that Walgreens breached these obligations.

The evidence at trial established that from 2006 to 2020, Walgreens pharmacies in San Francisco dispensed hundreds of thousands of red flag opioid prescriptions without performing adequate due diligence. Tens of thousands of these prescriptions were written by doctors with suspect prescribing patterns. The evidence showed that Walgreens did not provide its pharmacists with sufficient time, staffing, or resources to perform due diligence on these prescriptions. Pharmacists experienced constant pressure to fill prescriptions as quickly as possible, and a shortage of resources to review them before dispensing. As a result of Walgreens' fifteen-year failure to perform adequate due diligence, Plaintiff proved that it is more likely than not that Walgreens pharmacies dispensed large volumes of medically illegitimate opioid prescriptions that were diverted for illicit use and that substantially contributed to the opioid epidemic in San Francisco."]

## II. Conclusions of Law

Plaintiff proved that Walgreens is liable for substantially contributing to the public nuisance—the ongoing opioid epidemic—in San Francisco. . . .

Plaintiff is authorized to bring this action for abatement of a public nuisance existing within San Francisco. To succeed on its public nuisance claim at trial, Plaintiff had the burden of proving by a preponderance of the evidence that Walgreens had knowledge that its unreasonable conduct caused a substantial interference with a right common to the public. Plaintiff carried its burden.

### A. Unreasonable Conduct with Knowledge

#### 1. Unreasonable Conduct

Conduct encompasses any action that "assist[s] in creating a system that causes" an interference with a public right. [Citing cases and Restatement (Second) of Torts §821B.] Conduct is unreasonable if it violates a statute, ordinance, or administrative regulation. Conduct is also unreasonable if "the gravity of the harm outweighs the social utility of the defendant's conduct.". . . .

At trial, Plaintiff proved that Walgreens pharmacies violated 21 C.F.R. §1306.04(a) for fifteen years. [Section 1306.04(a) states that "[t]he responsibility for the proper prescribing and dispensing of controlled substances is upon the prescribing practitioner, but a corresponding responsibility rests with the pharmacist who fills the prescription." That responsibility in turn "requires pharmacists and pharmacies to identify and resolve objective signs 'arising during the presentation of a prescription' that create 'a reasonable suspicion that the prescription is not, on its face, legitimate.'"]

This is unreasonable conduct sufficient to support a public nuisance claim. The CSA and its implementing regulations strike a bargain with registrants. In exchange for the privilege of dispensing powerful controlled substances, pharmacies are required to take reasonable steps to prevent those substances from being diverted and harming the public. [Breyer J. then addressed the evidence set out above on Walgreens' systematic neglect of its duties.]

### 2. Knowledge

California's public nuisance claim has a knowledge requirement. But the California Supreme Court has not squarely addressed the extent to which a plaintiff must prove that a defendant has knowledge of the harm resulting from its unreasonable conduct. The California Court of Appeal articulated the knowledge requirement clearly in People v. ConAgra Grocery Prod. Co., 17 Cal. App. 5th 51, 83–86 (2017) . . . .

In ConAgra, the court held that the plaintiff presented sufficient evidence to establish that the defendants acted with the requisite level of knowledge because the record "indicated that the defendants had learned about the harms and hazards of lead exposure by the 1920s, yet still promoted its lead products." ConAgra, 17 Cal. App. 5th at 85. . .

Applying ConAgra here, Plaintiff proved that Walgreens "must have known" of the harms that would result from violating its regulatory duties for over a decade. The CSA and its implementing regulations reflect the dangers posed by the controlled substances that Walgreens dispenses. The regulations that apply to Walgreens were put in place precisely because of the harms that result when opioids are diverted. Based on the regulatory scheme alone, it is reasonable to infer that Walgreens "must have known" that failing to prevent diversion of opioids would result in harm in San Francisco. . . .

### B. Factual and Legal Causation

[The court held that the elements of factual causation ("defendant's conduct was a 'substantial factor in bringing about' the nuisance") and legal causation ("the defendant's wrongful conduct was not 'too remote from the current hazard to be its "legal cause,"' i.e., proximate causation") were satisfied. With regard to factual causation, the court credited "circumstantial evidence of sufficient substantiality" to permit reasonable inferences that "support a finding of causation in fact."]

The substantial factor test subsumes "but for" causation. It also addresses situations "involving independent or concurrent causes in fact." Conduct may substantially contribute to a nuisance even where there are "independent or concurrent causes in fact." See id. If a defendant's conduct operated concurrently with other forces to produce the harm, it is a substantial factor, so long as "the injury, or its full extent, would not have occurred but for that conduct." . . .

California courts have repeatedly held that causation may be reasonably inferred from circumstantial evidence in the context of mass torts. In ConAgra, plaintiff filed a public nuisance claim against manufacturers of lead paint, alleging that the manufacturers promoted the use of lead paint for the interior of homes and buildings, despite knowing of the health hazards that it posed, thereby contributing to a public nuisance in California. People v. ConAgra Grocery Prods. Co., 17 Cal. App. 5th 51, 66 (2017). On appeal, defendants argued that plaintiffs failed to prove causation because there was no direct evidence of any customer using lead paint because they believed it was safe based on defendants' marketing. Id. at 102–03. The Court of Appeal rejected the argument. It held that "there was plenty of evidence that defendants' affirmative promotions of lead paint for interior residential use played at least a 'minor' role in creating the nuisance that now exists." Id. The evidence established that defendants engaged in multi-year marketing campaigns, aimed at window and door manufacturers as well as consumers, and promoted the use of lead paint for residential interiors. Id. Based on the length of the marketing campaigns and the volume of marketing materials, the Court of Appeal held that "the trial court could reasonably infer that at least some of those who were targets of these recommendations heeded them. That is all that the substantial factor test requires." Id. at 103.

Proximate cause involves "various considerations of policy that limit an actor's responsibility for the consequences of his conduct." "Because the purported causes of an event may be

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traced back to the dawn of humanity, the law has imposed additional limitation on liability other than simple causality." See ConAgra, 17 Cal. App. 5th at 104, 227. There "is no bright line demarcating a legally sufficient proximate cause from one that is too remote," but courts place great emphasis on "foreseeability of harm" in determining whether a proximate cause has been established.

At trial, Plaintiff proved that the numerous forms of harm resulting from Walgreens' unlawful dispensing of illegitimate opioid prescriptions were foreseeable. The risks posed by opioids have been known to medical practitioners for decades and have been codified in the Controlled Substances Act since 1970. The regulatory duties that the CSA imposes on pharmacies to prevent diversion of opioids reflect the danger that opioids pose. "A lack of reasonable care in the handling, distribution, and administration of controlled substances can foreseeably harm the individuals who take them. That's why they're controlled in the first place—overuse or misuse can lead to addictions and long-term health problems." . . .

Unlike nuisance law in other states, "California law has never imposed such a requirement that there be some form of injury to land or property[.]" See Ileto v. Glock Inc., 349 F.3d 1191, 1213 (9th Cir. 2003) ("[T]he district court's determination that a nuisance must be associated with property is contrary to clearly established California law."). Indeed, "California common law consistently has defined nuisance in broad terms that encompass injuries to health, or acts that are 'indecent or offensive to the senses' or obstructions to the free use of property in any manner that might interference with the 'comfortable enjoyment of life or property.'" Id. Further, this case does not raise concern that "floodgates" of litigation will open against a company that sells any product with a known risk of harm. Plaintiff's case against Walgreens is not based on dispensing controlled substances with known risks of harm—it is based on Walgreens' fifteen-year violation of federal regulations that were put in place to prevent the controlled substances that Walgreens dispenses from causing harm. See Ileto, 349 F.3d at 1214–15. Walgreens' conduct in dispensing opioids—not the opioids themselves—is the fundamental cause of the harm here.

### C. Substantial Interference with Public Rights

Public nuisance law "protect[s] the quality of organized social life." "A public nuisance is one which affects at the same time an entire community or neighborhood, or any considerable number of persons, although the extent of the annoyance or damage inflicted up individuals may be unequal." Cal. Civ. Code §3480. "[P]ublic nuisances are offenses against, or interferences with, the exercise of rights common to the public." The California Supreme Court has recognized five categories of public rights that can give rise to a claim for a public nuisance—"the public health, the public safety, the public peace, the public comfort or the public convenience."

Throughout this case, Walgreens has argued that a public nuisance claim requires Plaintiff to identify discrete conduct or conditions that are abatable. Walgreens contends that "every California public nuisance decision" involves "well-defined conduct" like "emitting noxious odors" or "a well-defined hazardous condition" like water pollution or lead paint in home. Walgreens argues that to be actionable, a nuisance claim must involve discrete conduct or conditions that can be remedied through abatement.

California courts have repeatedly rejected Walgreens' "ability to abate" argument. "[L]iability for nuisance does not hinge on whether the defendant owns, possesses or controls the property, nor on whether he is in a position to abate the nuisance; the critical question is whether the defendant created or assisted in the creation of the nuisance." . . .

At trial, Plaintiff proved that the opioid epidemic, defined by high rates of opioid abuse, addiction, and overdoses, constitutes a public nuisance. Plaintiff further proved that the

opioid epidemic interferes with all five categories of public rights recognized by the California Supreme Court—"the public health, the public safety, the public peace, the public comfort or the public convenience." And Plaintiff proved that Walgreens substantially contributed to the opioid epidemic in San Francisco, which has caused widespread harm across the city and interfered with public peace, comfort and convenience.

### III. Conclusion

For the foregoing reasons, Plaintiff has proven by a preponderance of the evidence that Walgreens substantially contributed to the public nuisance in San Francisco. A subsequent trial will be held to determine the extent to which Walgreens must abate the public nuisance that it helped to create.

## NOTES

**1. Purdue Pharma *Aftermath.*** After the court determined that the sole remaining defendant, Walgreens, substantially contributed to the public nuisance of an opioid epidemic, preparations for a November damages trial began. San Francisco submitted a brief detailing its proposed plan to remediate the public nuisance, which included measures such as increasing health care provider education, establishing recovery centers, distributing anti-overdose drugs throughout the city, and improving drug storage measures. See People's Trial Brief for Remedial Phase (Phase 2), City and Cnty. of S.F. v. Purdue Pharma LP, 620 F. Supp. 3d 936 (N.D. Cal. 2022) (No. 3:18-cv-07591-CRB). The city estimated that this plan would cost approximately $8.1 billion over fifteen years to implement, but acknowledged that "such an award may not provide justice to the parties and to the public interest" since "an award too large for Walgreens to pay . . . will rather delay and reduce the City's receipt of much needed funds" to help abate the nuisance. Before the proceedings in the damages trial could begin, Walgreens announced a $5 billion tentative settlement in another nationwide opioid-related litigation. Although San Francisco was not covered by the nationwide lawsuit, Breyer, J., vacated trial-related deadlines on the heels of this announcement so that the parties could engage in settlement talks. Ultimately, Walgreens settled with San Francisco for $230 million. See Dorothy Atkins, Walgreens to Pay SF $230M After Landmark Opioid Trial Loss, Law360 (May 17, 2023, 2:10 PM), https://www.law360.com/articles/1678694/walgreens-to-pay-sf-230m-after-landmark-opioid-trial-loss.

**2. *"Traditional" Public Nuisance Claims.*** *City & County of San Francisco* is one of the bellwether trials in a larger MDL, which is consolidated before Judge Polster in Ohio and likely constitutes the largest civil action in U.S. history. The bulk of the actions have settled, often for billions of dollars. To what extent is Walgreens responsible for opioid addiction in persons who acquired their opioids elsewhere or illegally? If various social policies of the city exacerbated the problem, should its conduct give rise to a contributory negligence defense?

Note that California's public nuisance statute broadly defines a nuisance as:

> Anything which is injurious to health, including, but not limited to, the illegal sale of controlled substances, or is indecent or offensive to the senses, or an obstruction to the free use of property, so as to interfere with the comfortable enjoyment of life or property, or unlawfully obstructs the free passage or use, in the customary manner, of any navigable lake, or river, bay, stream, canal, or basin, or any public park, square, street, or highway, is a nuisance.

Cal. Civ. Code §3479 (West 2024). Courts in several jurisdictions have expressed grave concerns about extending public nuisance to the sale or distribution of opioids. One concern

raised is that nuisance law traditionally applies only "in the context of conduct that interferes with public property or resources." See City of Huntington v. AmerisourceBergen Drug Corp., 609 F. Supp. 3d 408, 472 (S.D.W. Va. 2022); State *ex rel.* Hunter v. Johnson & Johnson, 499 P.3d 719, 727 (Okla. 2021) (overturning a $465 million trial verdict).

Richard A. Epstein, The Private Law Connections to Public Nuisance Law: Some Realism About Today's Intellectual Nominalism, 17 J.L. Econ. & Pol'y 282, 285 (2022), calls for a return to a land-based view of public nuisance, grounded in private nuisance. Thomas W. Merrill, Public Nuisance as Risk Regulation, 17 J.L. Econ. & Pol'y 347 (2022), disagrees, as a historical matter, that public nuisance must be land-based, but argues, more radically, that public nuisance is not a tort but rather a public action to regulate prospective harms. Now that legislative and regulatory bodies can define proscribed conduct in advance, Merrill argues the use of public nuisance for tort should be curtailed.

**3. *The* ConAgra *Prelude.*** In *City & County of San Francisco*, Breyer, J., relied on People v. ConAgra Grocery Products Co., 17 Cal. App. 5th 51 (2017). Although both cases involved causes of action for public nuisance, the *ConAgra* cases, focusing on the use of lead paint, had a very different factual background. In these cases, it was established that high concentrations of lead paint could result in major neurological damage to children, and that knowledge of this effect was found in readily available medical sources. Lead paint manufactured before 1950 was found in many homes in which small children were exposed to it, and the plaintiffs knew of its deadly properties. They developed a program to create a fund "to pay $1.15 billion into a fund to be used to abate the public nuisance created by interior residential lead paint in the 10 California jurisdictions represented by plaintiff," but only for units constructed before 1950. Should the liabilities here be imposed on the current owners of those units? See *In re* Lead Paint Litig., 924 A.2d 484 (2007). Lead paint was banned in residential projects in 1971 and for all uses in the United States in 1978. Its use was both legal and widespread before 1950. Should large companies be liable for paint sold by smaller firms whom they acquired after the initial sales?

**4. *Products as Public Nuisances.*** One concern with applying "the law of public nuisance to the sale, marketing and distribution of products would invite litigation against any product with a known risk of harm." *City of Huntington*, 609 F.Supp.3d at 474. See, e.g., Complaint, City of N.Y. v. Hyundai Motor Am. (S.D.N.Y. 2023) (No. 1:23-cv-4772) (alleging that car company defendants' failure to install industry-standard antitheft immobilization devices in its automobiles leading to a vehicle theft epidemic created a public nuisance); Complaint at 5, People v. PepsiCo Inc. (N.Y. Sup. Ct. 2023) (alleging that a beverage company "has significantly contributed to, and continues to contribute to, the existence of a public nuisance" by continuing to manufacture, distribute, and sell large quantities of single-use plastic packaging); Complaint, People v. 3M Co. (Cal. Super. Ct. 2023) (No. 24STCV09939) (alleging that the manufacturers and distributors of "forever" chemicals created or assisted in creating a public nuisance due to the pollution caused by third-party use of its chemicals).

In *Johnson & Johnson*, the Supreme Court of Oklahoma explains that "[p]ublic nuisance is fundamentally ill-suited to resolving claims against product manufacturers" because "(1) the manufacture and distribution of products rarely cause a violation of a public right, (2) a manufacturer does not generally have control of its product once it is sold, and (3) a manufacturer could be held perpetually liable for its products under a nuisance theory." 499 P.3d at 719, 726.

Epstein contends that the *Johnson & Johnson* plaintiffs proceeded on a public nuisance theory because in the products context, "[l]iability is imposed when parties respond to representations by purchasing or using the product, but only when consumers or users of the information change their position for the worse in reliance on that information, for otherwise there is no causal connection between what has been said or implied on the one hand, and

the injury on the other." *Amicus Curiae* Brief of Competitive Enterprise Institute at 12, Oklahoma *ex rel.* Hunter v. Johnson & Johnson, Appeal No. 118,474 (Okla. Oct. 22, 2020). Do you agree with Professor Epstein that the *Johnson & Johnson* plaintiffs sought to recover on a public nuisance theory to avoid having to show material reliance on manufacturers' representations? Would plaintiffs who could hypothetically show material reliance in the products context qualify to recover special damages on a public nuisance theory? Or does the problem lie not just in proving special damages, but in showing a public injury altogether? See *id.* at 11 ("There is no intimation of a public injury (as opposed to a series of private injuries) anywhere in the district court's discussion, which extensively turns on its flawed accounts of misrepresentation and product liability.").

Note that neither the Second nor Third Restatements have addressed whether the sale of products can constitute a nuisance. According to Holliday, Am. L. Prod. Liab. 3d §27:8:

> It is generally recognized that a product which has caused injury cannot be classified as a nuisance to hold liable the manufacturer or seller for the product's injurious effects, and that a product manufacturer who builds and sells the product and does not control the enterprise in which the product is used is not in the situation of one who creates a nuisance and is not liable in a products liability case under a nuisance theory for harm caused by a defect in the product. . . .
>
> On the other hand, it has been held that manufacturers can be liable for nuisance long after they relinquish ownership or control over their polluting products. Additionally, there is authority that liability for nuisance does not hinge on whether the defendant owns, possesses or controls the property, nor on whether the defendant is in a position to abate the nuisance, and that the critical question is whether the defendant created or assisted in the creation of the nuisance. However, this authority also recognizes that the law of nuisance is not intended to serve as a surrogate for ordinary products liability. . . .

Does this approach regarding the sale of products and private nuisance address whether the sale of products can lead to liability for public nuisance? How should courts determine whether a defendant created or assisted in creating a nuisance? Should the ability to abate or control of the product in question inform that determination?

**5.** ***Public Health and Safety Nuisances.*** To what extent does *City & County of San Francisco* sketch out a more limited conception of the violation of a public right? Recall that liability in *City & County of San Francisco* is premised on repeated regulatory violations. Is this akin to negligence per se? Does it obviate the need for an extended discussion of public rights? For elaboration, see Catherine M. Sharkey, Public Health & Safety Nuisances, 74 DePaul L. Rev. (forthcoming 2025).

**6.** ***Private Public Nuisance and the Opioids Crisis.*** West Boca Medical Center survived a motion to dismiss on its private public nuisance claim. See W. Boca Med. Ctr., Inc. v. AmerisourceBergen Drug Corp. (In re Nat'l Prescription Opiate Litig.), 452 F. Supp. 3d 745, 774–75 (N.D. Ohio 2020). On the question of public right, the court referred to earlier orders in the MDL, which cited the Restatement (Second) of Torts §821B in determining that public health qualifies as a public right. The court noted that West Boca's injuries were not "merely derivative" of the "public" injury because, as a hospital, West Boca incurred increased costs stemming from the purchase of excess opioid pills—an injury sufficiently distinct in kind to survive the pleading stage. One obstacle in *West Boca* was that, per the defendants, Florida nuisance law requires an interference with the use and enjoyment of property. But the district court relied on a Florida Supreme Court decision that held that the unlicensed practice of medicine is a nuisance per se, and downplayed a Florida circuit court decision determining that public nuisance does not apply to products liability, to conclude that Florida nuisance law is not limited to interferences with property interests. Given the sheer size of the opiate MDL, will courts need to parse the public nuisance case law of nearly every state?

**7. *Public Nuisance Remedies.*** Thomas W. Merrill, Is Public Nuisance a Tort?, 4 J. Tort L. ii, 18 (2011), argues:

> If public nuisance is a single cause of action — as the [*Second*] *Restatement* implicitly insists — and private parties can in some circumstances obtain damages under this cause of action, what possible argument supports the conclusion that public officials cannot obtain damages? At the same time, if public nuisance is a single cause of action, and public officials cannot obtain damages, what possible argument supports awarding damages to private parties for the same violation?

Does it make sense for there to be different enforcement regimes and remedies for private public nuisance and public public nuisance?

Abatement is typically the only remedy available to public entities in a traditional public nuisance suit. See, e.g., Cal. Civ. Proc. Code §731 (West 2024). The abatement remedy sought in *City & County of San Francisco*, however, includes monetary sums awarded to the plaintiff to reduce not the defendant's continuing actions, but rather the ongoing effect of its past ones, in this case the ongoing impact of the opioid crisis on the city. Thomas W. Merrill, The New Public Nuisance: Illegitimate and Dysfunctional, 132 Yale L. J. F. 985 (2023), sharply criticizes the practice of granting monetary remedies in public nuisance actions, arguing that it incentivizes municipal plaintiffs to partner with private firms on contingency fee to pursue defendants with deep pockets, as opposed to those most responsible for the harm. Leslie Kendrick, The Perils and Promise of Public Nuisance, 132 Yale L.J. 702 (2023), sets forth a defense of contemporary public nuisance suits, including those seeking monetary damages.

Should public entities seeking damages be required to show special injury? Is there any functional difference between damages and an abatement fund?

**8. *Guns and Public Nuisances.*** The contemporary advent of public nuisance suits to address large-scale societal ills began with the tobacco litigation in the 1990s. Soon thereafter local governments sought to bring public nuisance suits for the public costs needed to combat local criminal use of handguns. In Cincinnati v. Berretta USA Corp., 768 N.E.2d 1136 (Ohio 2002), the city alleged that the gun manufacturers created a nuisance "through their ongoing conduct of marketing, distributing, and selling firearms in a manner that facilitated their flow into the illegal market." Although the manufacturers did not control the actual use of firearms that cause injury, Sweeney, J., held: "Just as the individuals who fire the guns are held accountable for the injuries sustained, appellees can be held liable for creating the alleged nuisance."

By contrast, in Camden County Board of Chosen Freeholders v. Berretta, U.S.A. Corp., 273 F.3d 536 (3d Cir. 2001), the court rejected the claim that selling guns was a public nuisance simply because some fraction of them ended up in the hands of criminals. The court noted that gun distribution takes place through several channels, from manufacture, to sale to distributors, and to the diversion of guns into the hands of potential criminals, and concluded that "[t]his causal chain is simply too attenuated to attribute sufficient control to the manufacturers to make out a public nuisance claim." In City of Philadelphia v. Beretta U.S.A. Corp., 277 F.3d 415, 424 (3d Cir. 2002), the plaintiffs tried to shorten the causal chain by arguing that the "thriving illegal market . . . injures [them], even before any guns acquired in the illegal market are actually used in the commission of a crime." But Greenberg, J., held that even an efficient resale market acquired guns through the same pattern of distribution as in *Camden County Board.*

Washington State recently passed a statute deeming it a public nuisance to market firearms products without "reasonable controls" to prevent the risk of downstream illegal sale or inventory theft. 2023 Wash. Sess. Laws ch. 163. The statute is substantially similar to statutes passed in Hawaii (see Act 28, 2023 Haw. Ses. Laws), California (see 2022 Cal. Stat. ch. 98), New York (see 2021 N.Y. Sess. ch. 237), New Jersey (see 2022 N.J. Laws ch. 56),

and Delaware (see 83 Del. Laws ch. 332 (2022)). The National Shooting Sports Foundation (NSSF) has challenged these statutes as preempted by the Protection of Lawful Commerce in Arms Act, 15 U.S.C. §§7901–03. A federal district court in New York rejected the NSSF's challenge and granted the defendants' motion to dismiss. Nat'l Shooting Sports Found., Inc. v. James, 604 F. Supp. 3d 48, 55 (N.D.N.Y. 2022). The NSSF appealed the denial of the case to the Second Circuit, which heard oral arguments on November 3, 2023 (but has yet to announce its decision). By contrast, a federal district court in New Jersey granted a preliminary injunction preventing implementation of the New Jersey law. Nat'l Shooting Sports Found. v. Platkin, No. 22-6646, 2023 WL 1380388 (D.N.J. Jan. 31, 2023). On appeal, the Third Circuit dismissed plaintiff's pre-enforcement challenge as premature. Nat'l Shooting Sports Found. v. Attorney Gen'l of N.J., 80 F.4th 215 (3d Cir. Aug. 17, 2023). For a broad overview of the litigation, see Tobi Raji, The Brewing Gun-Control Fight That Could Be Headed to the Supreme Court, Wash. Post (Feb. 21, 2023), https://www.washingtonpost.com/politics/2023/02/21/gun-manufacturer-shooting-lawsuits-supreme-court/.

Academic views on treating gun sales as a public nuisance are divided. In Keith N. Hylton, The Economics of Public Nuisance Law and the New Enforcement Actions, 18 Sup. Ct. Econ. Rev. 43, 73–76 (2010), Professor Hylton supports treating initial gun sales as public nuisance, given their inherent dangers. In sharp contrast, Professor Merrill claims that the public nuisance doctrine has "gone off the rails," and that these issues are better dealt with by the criminal law. See Thomas W. Merrill, Is Public Nuisance a Tort?, J. Tort L., September 1, 2011 at 5.

## 2. Climate Change

### *City of New York v. Chevron Corp.*

993 F.3d 81 (2d Cir. 2021)

Sullivan, J. The question before us is whether municipalities may utilize state tort law to hold multinational oil companies liable for the damages caused by global greenhouse gas emissions. Given the nature of the harm and the existence of a complex web of federal and international environmental law regulating such emissions, we hold that the answer is "no."

Global warming presents a uniquely international problem of national concern. It is therefore not well-suited to the application of state law. Consistent with that fact, greenhouse gas emissions are the subject of numerous federal statutory regimes and international treaties. These laws provide interlocking frameworks for regulating greenhouse gas emissions, as well as enforcement mechanisms to ensure that those regulations are followed.

The City of New York has sidestepped those procedures and instead instituted a state-law tort suit against five oil companies to recover damages caused by those companies' admittedly legal commercial conduct in producing and selling fossil fuels around the world. In so doing, the City effectively seeks to replace these carefully crafted frameworks—which are the product of the political process—with a patchwork of claims under state nuisance law. [W]e cannot condone such an action and we AFFIRM the dismissal of the City's complaint.

#### I. Background

Global warming is one of the greatest challenges facing humanity today. Among the scientific community, there is near universal consensus that global warming is primarily caused, or at least accelerated, by the burning of fossil fuels, which emits greenhouse gases like carbon

dioxide and methane into the atmosphere. Once released, those gases can remain in the atmosphere for hundreds of years, where they trap heat that would otherwise radiate into space.

According to the complaint, New York City "is exceptionally vulnerable" to the effects of global warming, such as rising sea levels, because of its "520-mile coastline." So, in the aftermath of Hurricane Sandy, the City "launched a $20 billion-plus multilayered investment program in climate resiliency across all five boroughs." These preparations have included constructing seawalls and other coastal armaments, enlarging and augmenting the City's storm and wastewater infrastructure, and implementing public-health programs designed to tackle the effects of heatwaves, among other measures meant to protect the public and City property.

Even though every single person who uses gas and electricity—whether in travelling by bus, cab, Uber, or jitney, or in receiving home deliveries via FedEx, Amazon, or UPS—contributes to global warming, the City asserts that its taxpayers should not have to shoulder the burden of financing the City's preparations to mitigate the effects of global warming. Rather, the City suggests that a group of large fossil fuel producers are primarily responsible for global warming and should bear the brunt of these costs. Included among that group are Defendants Chevron Corporation, ConocoPhillips, Exxon Mobil Corporation (together, the "Domestic Producers"), BP p.l.c., and Royal Dutch Shell plc (together with BP, the "Foreign Producers" and, collectively with the Domestic Producers, the "Producers"). The Producers "are, respectively, the first (Chevron), second (Exxon), fourth (BP), sixth (Shell), and ninth (ConocoPhillips) largest cumulative producers of fossil fuels worldwide" since the mid-nineteenth century.

As the City sees it, the Producers have known for decades that their fossil fuel products pose a severe risk to the planet's climate. The City alleges that, despite that knowledge, the Producers downplayed the risks and continued to sell massive quantities of fossil fuels, which has caused and will continue to cause significant changes to the City's climate and landscape.

The City freely admits that it is not able to halt the Producers' conduct under any federal statute or international agreement. Indeed, it acknowledges that the Producers' conduct is "lawful . . . commercial activit[y]." Nonetheless, the City believes that it is appropriate to "shift the costs of protecting the City from climate change impacts back onto the companies that have done nearly all they could to create this existential threat."

Understanding the context of this dispute requires some background knowledge about our nation's regulatory framework concerning environmental issues. The Clean Air Act . . . "is an intricate regulatory regime intended to 'protect and enhance the quality of the [n]ation's air resources so as to promote the public health and welfare and the productive capacity of its population.'"

Consistent with that mandate, the Environmental Protection Agency (EPA) was established in 1970 to implement programs to regulate pollution from both mobile and stationary sources under the Clean Air Act and other related statutes, a role which was later interpreted to include the regulation of carbon dioxide and other greenhouse gases. . . .

## III. Discussion

### A. The City's State-Law Tort Claims Are Displaced by Federal Common Law

#### 1. What Is Federal Common Law?

In the aftermath of Erie Railroad Co. v. Tompkins, 304 U.S. 64 (1938), "[f]ederal courts, unlike state courts, . . . do not possess a general power to develop and apply their own rules of decision." But *Erie* was not a death knell to all federal common law. . . .

In a nutshell, federal common law exists in only the "few and restricted" enclaves, where a federal court is "compelled to consider federal questions [that] cannot be answered from federal statutes alone." And once Congress speaks directly to those questions, "the need for such an unusual exercise of lawmaking by federal courts disappears." In that sense, federal

common law functions much like legal duct tape—it is a "necessary expedient" that permits federal courts to address issues of national concern until Congress provides a more permanent solution.

Despite its utility, however, courts have been quick to declare that our constitutional architecture restricts federal common law to a "modest role." And for good reason. Where federal common law exists, it "pre-empt[s] and replace[s]" state law. It thus threatens a potent mix of judicial lawmaking and encroachment on our federalist structure. . . .

**2. Does Federal Common Law Apply Here?**

. . . Stripped to its essence, then, the question before us is whether a nuisance suit seeking to recover damages for the harms caused by global greenhouse gas emissions may proceed under New York law. Our answer is simple: no.

For over a century, a mostly unbroken string of cases has applied federal law to disputes involving interstate air or water pollution. This is because such quarrels often implicate two federal interests that are incompatible with the application of state law: (i) the "overriding . . . need for a uniform rule of decision" on matters influencing national energy and environmental policy, and (ii) "basic interests of federalism." The City's lawsuit is no different.

To state the obvious, the City does not seek to hold the Producers liable for the effects of emissions released in New York, or even in New York's neighboring states. Instead, the City intends to hold the Producers liable, under New York law, for the effects of emissions made around the globe over the past several hundred years. In other words, the City requests damages for the cumulative impact of conduct occurring simultaneously across just about every jurisdiction on the planet.

Such a sprawling case is simply beyond the limits of state law. To start, a substantial damages award like the one requested by the City would effectively regulate the Producers' behavior far beyond New York's borders. Since "[g]reenhouse gases once emitted 'become well mixed in the atmosphere,'" "emissions in [New York or] New Jersey may contribute no more to flooding in New York than emissions in China." Any actions the Producers take to mitigate their liability, then, must undoubtedly take effect across every state (and country). And all without asking what the laws of those other states (or countries) require. Because it therefore "implicat[es] the conflicting rights of [s]tates [and] our relations with foreign nations," this case poses the quintessential example of when federal common law is most needed. . . .

The City disagrees, positing that because it seeks damages—not abatement or the imposition of pollution standards—its claims do not threaten to regulate emissions at all, let alone beyond New York's borders. But this ignores economic reality. As the Supreme Court has long recognized, "'regulation can be effectively exerted through an award of damages,' and 'the obligation to pay compensation can be, indeed is designed to be, a potent method of governing conduct and controlling policy.'"

Thus, while the City is not expressly seeking to impose a standard of care or emission restrictions on the Producers, the goal of its lawsuit is perhaps even more ambitious: to effectively impose strict liability for the damages caused by fossil fuel emissions no matter where in the world those emissions were released (or who released them). If the Producers want to avoid all liability, then their only solution would be to cease global production altogether. And even if some level of ongoing liability were deemed palatable, a significant damages award would no doubt "compel[]" the Producers to develop new "means of pollution control." [Citing Boomer v. Atl. Cement Co., 257 N.E.2d 870 (N.Y. 1970) (acknowledging that nuisance damages "effective[ly] spur" a change in behavior).] . . . Consequently, though the City's lawsuit would regulate cross-border emissions in an indirect and roundabout manner, it would regulate them nonetheless.

### B. The Clean Air Act, in Turn, Displaces the City's Federal Common Law Claims Where Domestic Emissions Are Involved

Having concluded that the City's claims must be brought under federal common law, we see that those federal claims immediately run headlong into a problem of their own. For many of the same reasons that federal common law preempts state law, the Clean Air Act displaces federal common law claims concerned with domestic greenhouse gas emissions. . . .

That Congress chose to preempt the federal common law of nuisance with a well-defined and robust statutory and regulatory scheme of environmental law is by no means surprising. Numerous courts have bemoaned the "often . . . 'vague' and 'indeterminate'" standards attached to nuisance law. . . . Such an elastic standard is especially ill-suited to address "the technically complex area of environmental law," particularly since it would be administered by federal judges who "lack the scientific, economic, and technological resources" to "cop[e] with issues of this order." By contrast, it makes far more sense to "entrust[ ] [the] complex balancing" of interests that climate change demands to an "expert agency" such as the EPA.

At bottom, it is enough to say that the issues raised in this dispute concerning domestic emissions are squarely addressed by the Clean Air Act. As a result, we affirm the district court's conclusion that the City's federal common law claims concerning domestic greenhouse gas emissions are displaced by statute.

### C. The Clean Air Act's Displacement of Federal Common Law Does Not Resuscitate the City's State-Law Claims

As its final volley on this issue, the City argues that if the Clean Air Act displaced federal common law, then the City's state law nuisance claims may snap back into action unless specifically preempted by statute. In other words, the City sees the Clean Air Act as having vaporized any preemptive effect that federal common law had on state law, thereby requiring us to engage in a traditional statutory preemption analysis. But while the caselaw on this point is admittedly not a model of clarity, the City's position is difficult to square with the fact that federal common law governed this issue in the first place.

## IV. Conclusion

For the reasons stated above, we AFFIRM the judgment of the district court.

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## *City and County of Honolulu v. Sunoco LP*

537 P.3d 1173 (Haw. 2023)

Recktenwald, C.J. The City and County of Honolulu and the Honolulu Board of Water Supply (collectively, Plaintiffs) brought suit against a number of oil and gas producers (collectively, Defendants) alleging five counts: public nuisance, private nuisance, strict liability failure to warn, negligent failure to warn, and trespass. Defendants appeal the circuit court's denial of their motions to dismiss for both lack of jurisdiction and failure to state a claim. We conclude that the circuit court properly denied both motions, and accordingly, this lawsuit can proceed.

Plaintiffs argue this is a traditional tort case alleging that Defendants engaged in a deceptive promotion campaign and misled the public about the dangers of using their oil and gas products. Plaintiffs claim their theory of liability is simple: Defendants knew of the dangers of using their fossil fuel products, "knowingly concealed and misrepresented the climate impacts

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of their fossil fuel products," and engaged in "sophisticated disinformation campaigns to cast doubt on the science, causes, and effects of global warming," causing increased fossil fuel consumption and greenhouse gas emissions, which then caused property and infrastructure damage in Honolulu. Simply put, Plaintiffs say the issue is whether Defendants misled the public about fossil fuels' dangers and environmental impact.

Defendants disagree. They say this is another in a long line of lawsuits seeking to regulate interstate and international greenhouse gas emissions, all of which have been rejected. Greenhouse gas emissions and global warming are caused by "billions of daily choices, over more than a century, by governments, companies, and individuals," and Plaintiffs "seek to recover from a handful of Defendants for the cumulative effect of worldwide emissions leading to global climate change and Plaintiffs' alleged injuries." They argue: (1) the circuit court lacked specific jurisdiction over the Defendants; (2) Plaintiffs' claims are preempted by federal common law, which in turn, was displaced by the Clean Air Act (CAA); and (3) alternatively, Plaintiffs' claims are preempted by the CAA.

We agree with Plaintiffs. This suit does not seek to regulate emissions and does not seek damages for interstate emissions. Rather, Plaintiffs' complaint "clearly seeks to challenge the promotion and sale of fossil-fuel products without warning and abetted by a sophisticated disinformation campaign." Mayor & City Council of Baltimore v. BP P.L.C., 31 F.4th 178, 233 (4th Cir. 2022), cert. denied, __ U.S. __, 143 S. Ct. 1795, 215 L.Ed.2d 678 (2023) (characterizing a complaint brought against many of the same Defendants in this case alleging broadly the same counts, theory of liability, and injuries). This case concerns torts committed in Hawai'i that caused alleged injuries in Hawai'i. . . .

. . . Defendants acknowledge that the federal common law that once governed interstate pollution damages and abatement suits was displaced by the CAA. Nonetheless, Defendants argue that despite displacement, federal common law still lives. Defendants say that federal common law still lives but only with enough power to preempt state common law claims "involving interstate air pollution." According to Defendants, federal common law is both dead and alive—it is dead in that the CAA has displaced it, but alive in that it still operates with enough force to preempt Plaintiffs' state law claims.

Under Defendants' preemption theory, this court should first look to whether the federal common law governing interstate pollution damages and abatement claims preempts Plaintiffs' state common law claims. After determining that federal common law does in fact preempt Plaintiffs' state common law claims, Defendants say this court should then look to whether the CAA displaced federal common law claims (and Defendants say it did). Indeed, were this court to adopt Defendants' two-step approach, Plaintiffs would have no viable cause of action under state or federal law. Federal common law would preempt state common law, and in turn, the CAA would displace federal common law. No common law cause of action would be available. Further, no federal statutory cause of action would be available because the CAA does not contain one available to Plaintiffs, see 42 U.S.C. §7401 et seq., and any state statutory cause of action would be preempted by federal common law, which, in turn, would be displaced by the CAA.

We decline to follow Defendants' two-step approach because it engages in backwards reasoning. This court would first need to determine whether the federal common law governing interstate pollution suits is still good law before determining whether it can preempt state law claims. . . .

. . . Defendants primarily rely on *City of New York* to argue that their two-step preemption analysis is the correct one. In that case, New York City filed a state-law tort suit in federal court "against five oil companies to recover damages caused by those companies' admittedly legal commercial conduct in producing and selling fossil fuels around the world." 993 F.3d at 86. At issue was whether New York City's claims were preempted by either federal common

law or the CAA. *Id.* at 89. The Second Circuit first looked to whether federal common law governing interstate pollution damages and abatement suits preempted New York City's state law claims, holding that it did. *Id.* at 95 (determining that New York City's "claims must be brought under federal common law"). Next, the court examined whether the federal common law was displaced by the CAA, holding again that it was. *Id.* at 98 (determining that "federal common law claims concerning domestic greenhouse gas emissions are displaced by statute."). Thus, the Second Circuit held that displaced federal common law preempted New York City's state law claims. *Id.* at 95–98.

We agree with the Fourth Circuit's analysis in [Mayor & City Council of Baltimore v. BP P.L.C, 31 F.4th 178 (4th Cir. 2022)], which explained why *City of New York* is not persuasive in that respect: "[A]fter recognizing federalism and the need for a uniform rule of decision as federal interests, *City of New York* confusingly concludes that federal common law is 'most needed in this area' because New York's state-law claims touch upon the federal government's relations with foreign nations. [993 F.3d] at 91–92. But it never details what those foreign relations are and how they conflict with New York's state-law claims. *See id.* at 92. The same is true when *City of New York* declares that state law would 'upset[ ] the careful balance' between global warming's prevention and energy production, economic growth, foreign policy, and national security. *Id.* at 93." . . .

. . . The source of Plaintiffs' alleged injury is Defendants' alleged failure to warn and deceptive promotion. *See* [City and County of Honolulu v. Sunoco LP, 39 F.4th 1101 1113 (9th Cir. 2022)] ("[t]his case is about whether oil and gas companies misled the public about dangers from fossil fuels."). Even were this court to determine that federal common law retains preemptive effect after displacement, the federal common law cited to by Defendants would not preempt Plaintiffs' claims in this case. The source of Plaintiffs' injury is not pollution, nor emissions. Instead, the source of Plaintiffs' alleged injury is Defendants' alleged failure to warn and deceptive promotion. Therefore, even if federal common law had not been displaced, Plaintiffs' claims would not be preempted by it.

[The court then determined that the Clean Air Act also does not preempt plaintiffs' claims. The court found no "express," "field," or "conflict" preemption.]

## NOTES

**1. Sunoco *Aftermath.*** Following the *Sunoco* court's ruling that federal law did not preempt the plaintiff's public nuisance claims, the energy company defendants filed a writ of certiorari to have the U.S. Supreme Court review the decision. The petitioners claim that the court's decision creates a conflict with the "materially identical state-law claims" raised in the *City of New York* case and that Supreme Court precedent has long supported the notion that "interstate pollution is one of the few inherently federal areas necessarily governed by federal law." Petition for Writ of Certiorari at 14, 22, City and Cnty. of Honolulu v. Sunoco LP, 537 P.3d 1173 (Haw. 2023) (No. 23-947). In response, Honolulu distinguished the case at hand from *City of New York*, characterizing the New York case as one where the defendants would be forced to cease production of fossil fuels entirely to avoid liability while the current lawsuit seeks to hold the defendants liable solely for the "effects of climate change allegedly caused by [their] breach of Hawai'i law regarding failures to disclose, failures to warn, and deceptive promotion. Brief for Respondents at 12, City and Cnty. of Honolulu v. Sunoco LP, 537 P.3d 1173, 1207 (Haw. 2023) (No. 23-947). Honolulu also argues that the CAA does not preempt a cause of action for public nuisance because the statute does not prohibit the defendants "from warning consumers about the dangers of using their fossil fuel products" and that, at

most, this case will incentivize the defendants to be more truthful in the promotion of their products. In June 2024, the Court called for the view of the Solicitor General's opinion as to whether the petition should be granted. As of this writing, the matter is still unresolved.

**2. *Evaluating the Torts Claims.*** There are two classes of potential defendants — the actual emitters and the more remote suppliers of fossil fuels, including crude oil, which has a wide range of alternative uses. Which is the better class of defendants? Which are the cheapest cost avoiders? If it is downstream producers, just how much of the harm can be attributed to five oil companies? Aisha I. Saad, Attribution for Climate Torts, 64 B.C. L. Rev. 867, 903–07 (2023), situates the causation problems in climate suits within the framework of scientific and legal techniques developed in the toxic torts context, which similarly involved the problems of latency periods, additive effects, fungible products, and noise induced by concurrent natural contributions and contributory behavior.

In addition to the causal inquiry, how does one measure the losses attributable to global warming, including potential sea rise? The background rate of sea-level rise has been about five inches per century for about 10,000 years. How can one predict its levels in 2050? Should one take those potentials into account now? Note, too, that the City of New York makes extensive use of fossil fuels in its own activities. Does that count as a form of comparative negligence that reduces recovery?

In this vein, consider Smith v. Fonterra Co-Operative Group Ltd., [2024] NZSC 5 (N.Z.), a climate change case in which the Supreme Court of New Zealand analogized to "historic waterway cases." In those cases, defendants' harmful particulates worked their way down waterways before ultimately interfering with plaintiffs' rights. The New Zealand Supreme Court used the waterway cases to explain that "the 'but for' causation reasoning that dominates the tort of negligence" does not "serve the same function in the tort of public nuisance." Should courts look solely to historical public nuisance cases to address causation in the climate change litigation context? Do the sheer magnitude of the harm and complexity of the causation inquiry counsel in favor of a different approach?

**3. *Federal Displacement of Federal Common Law Public Nuisance Claims.*** To date, the use of public nuisance suits has been frustrated by Supreme Court determinations that federal common law public nuisance claims are displaced by the comprehensive systems of direct federal regulation. Thus, in City of Milwaukee v. Illinois, 451 U.S. 304, 317 (1981), the Court held that public nuisance suits brought by Illinois were blocked by the explicit effluent limitations set out in the 1972 amendments to the Federal Water Pollution Control Act. Justice Rehnquist wrote: "Congress has not left the formulation of appropriate federal standards to the courts through application of often vague and indeterminate nuisance concepts and maxims of equity jurisprudence, but rather has occupied the field through the establishment of a comprehensive regulatory program supervised by an expert administrative agency."

Subsequently, in American Electric Power Co. v. Connecticut, 564 U.S. 410 (2011), the Court was asked "whether the plaintiffs (several States, the city of New York, and three private land trusts) can maintain federal common law public nuisance claims against carbon-dioxide emitters (four private power companies and the federal Tennessee Valley Authority)," with an eye to setting emissions levels for each outfit. A unanimous Court, speaking through Justice Ginsburg, held that to the extent that these claims rested on federal common law they were blocked. Citing *Milwaukee*, Ginsburg, J., held that "the Clean Air Act and the EPA actions it authorizes displace any federal common law right to seek abatement of carbon-dioxide emissions from fossil-fuel fired power plants."

For criticism of *AEP*, see Benjamin Ewing & Douglas A. Kysar, Prods and Pleas: Limited Government in an Era of Unlimited Harm, 121 Yale L.J. 350 (2011). For a response, see Richard A. Epstein, Beware of Prods and Pleas: A Defense of the Conventional Views on Tort and Administrative Law in the Context of Global Warming, 121 Yale L.J. Online 317 (2011).

**4. *State Law Public Nuisance Claims?*** *City of New York* read the city's state law claims as necessarily arising under federal common law (on what basis?) and then found those claims displaced under *AEP*. *City and County of Honolulu* recognized a variety of state law claims as part of "a traditional tort case alleging that Defendants engaged in a deceptive promotion campaign and misled the public about the dangers of using their oil and gas products," and then held they were not preempted by the Clean Air Act.

Compare with County of San Mateo v. Chevron Corp., 32 F.4th 733, 747 (9th Cir. 2022), where the court affirmed the remand of plaintiff's state law tort theories, including public nuisance, failure to warn, design defect, private nuisance, negligence, and trespass, to state court. Ikuta, J., rebuffed defendants' argument that plaintiff's global-warming claims arise under federal law and, as such, are removable to federal court.

> [E]ven if we assume that the Counties' complaints "could give rise to a cognizable claim" under federal common law, the global-warming-related tort claims do not "require resolution of a substantial question of federal law" because they do not require any interpretation of a federal statutory or constitutional issue, and are "displaced by the Clean Air Act."

Is there any meaningful difference between the state and federal public nuisance claims? Richard A. Epstein, The Private Law Connections to Public Nuisance Law: Some Realism About Today's Intellectual Nominalism, 17 J.L. Econ. & Pol'y 282, 297 (2022), sees no role for such state tort actions. "[T]he power of a state in a federal system is only to tax and regulate those activities solely within its borders. It cannot be allowed, and should not be allowed, to do so with respect to activities that take place elsewhere with local consequences."

To what extent does a heightened "special injury" requirement guard against the proliferation of private suits on state law public nuisance theories—and avoid the cross-border regulation problem raised by Judge Sullivan and by Professor Epstein? Richard A. Epstein, Federal Preemption, and Federal Common Law, in Nuisance Cases, 102 Nw. U. L. Rev. 551, 558 (2008), argues that "private rights of action are generally inappropriate" in public nuisance suits. Judge Sullivan, by contrast, cites the technical complexities of environmental law to justify displacement/preemption. 993 F.3d at 98. What are the implications of Judge Sullivan's view for state tort claims *outside* the public nuisance context?

Jonathan H. Adler, Displacement and Preemption of Climate Nuisance Claims, 17 J.L. Econ. & Pol'y 217 (2022), argues that preemption of state tort claims is unwarranted. Catherine M. Sharkey, Common Law Tort as a Transitional Regulatory Regime: A New Perspective on Climate Change Litigation, in Climate Liberalism: Perspectives on Liberty, Property and Pollution 103 (Jonathan H. Adler, ed., Palgrave Macmillan, 2023), posits that tort claims can serve a valuable information-production role, especially in areas that pose emerging and incompletely understood health and safety risks. Is litigation the cheapest way to produce such information in the climate context?

**5. *Climate-Related Public Nuisance Suits and Extraterritorial Actors.*** How should courts rule on state-law-based public nuisance claims that affect parties that operate solely out of state? In State *ex rel.* Jennings v. BP America Inc., C.A. No. N20C-09-097, at 6, 14, 20, 65 (Del. Super. Ct. Jan. 9, 2024), Delaware sued several extractors, producers, refiners, distributors, promoters, marketers, and sellers of fossil fuel products for contributing to a public nuisance resulting from the pollution caused by their greenhouse-gas-based products. Delaware also alleged that the defendants "exacerbated the costs of adapting to and mitigating the adverse impacts of" climate change by employing strategies to delay regulatory measures, and that they "could have taken other practical, cost-effective steps to reduce the use of their fossil fuel products" and resulting pollution. When the defendants attempted to remove the case to a federal court, the District of Delaware remanded the case back to the Delaware Superior Court, partly because "Plaintiff's claims are not completely preempted" by federal common law and the complaint "only asserts state-law causes of action."

In answering the question whether federal law preempted Delaware's cause of action for public nuisance, the Delaware Superior Court charted a middle position between the *City of New York* and *Sunoco* courts. The court found that the CAA preempted Delaware's claims for damages for the harm caused by out-of-state greenhouse emissions, but that the claims related to injuries from "air pollution originating from sources in Delaware" were not similarly preempted. Does it make sense to limit the ability of states to sue only in-state actors for public nuisance when out-of-state actors may have a greater adverse impact on the cleanliness of that state's air and water? How should courts go about apportioning liability for such pollution-based harms?

Intervening in the *Sunoco* case, Brief of Richard A. Epstein and John Yoo as Amici Curiae in Support of Petitions for Writ of Certiorari, City and Cnty. of Honolulu v. Sunoco LP, 537 P.3d 1173 (Haw. 2023), argues that finding that the CAA preempts state law public nuisance claims in *Sunoco* would "prevent the extraterritorial application of state law" and would preserve "a balanced system that prevents a single state from regulating a nationwide industry by the back door." Do these criticisms of the *Sunoco* decision also apply to the *BP America* decision? In what ways does *BP America* differ from *Sunoco*? From *City of New York*? How should courts go about applying state law to extraterritorial actors in public nuisance cases?

**6.** ***(Yet Another) View of the Cathedral: Cheapest Cost Avoiders in the Climate Change Litigation Context.*** Are there other benefits to state tort claims beyond the production of information? Assume, for example, that the health and safety risks of climate change are well understood. Would allowing the *City of New York* plaintiffs to proceed on a state law public nuisance theory have forced the defendants to internalize certain externalities relating to the production and use of fossil fuels? Recall that one justification for tort liability is the notion of economic deterrence. On this view, the tort system both forces defendants to internalize the costs of their future expected activities *and* seeks to identify the "cheapest cost avoider" — the "party or parties in the best position to avoid the harms at the lowest cost." *See* Brief of Professor Catherine M. Sharkey as Amicus Curiae in Support of Plaintiff-Appellant, City of New York v. Chevron Corp., 993 F.3d 81 (2d Cir. 2021) (No. 18-2188). Sharkey contends that fossil fuel defendants are the cheapest cost avoiders, insofar as they "have the relevant expertise and resources to conduct cost-benefit analyses comparing increased consumption with increased costs produced by that consumption," and that they can spread costs to relevant stakeholders — such as their shareholders, or the consumers of their products. By contrast, Sharkey notes, "victims" of climate change cannot reasonably take care to avoid the risks posed by fossil fuel emitters because of information asymmetries and the high transaction costs of organized resistance. Note that multinational corporations are almost invariably more "organized" litigants than municipalities — they benefit from trade associations and the like. Is it fair to consider costs to collective action in ascertaining cheapest cost avoiders, when doing so would likely place a thumb on the scale in favor of plaintiffs?

One of the most effective ways for cheapest cost avoider defendants to mitigate their liability is through liability insurance policies. This is especially true in the context of climate-change-related public nuisance suits, an area of the law where nearly two-thirds of the 2,341 total cases have been filed since 2015 and almost 200 were filed from June 2022 to May 2023. *See* Joana Setzer & Catherine Higham, Global Trends in Climate Change Litigation: 2023 Snapshot 16 (2023). As a result of this large increase in climate change litigation, with many cases featuring large multinational energy companies, many insurers are reconsidering their approach to dealing with such defendants and their policies. In Aloha Petroleum, Ltd. v. National Union Fire Insurance Co. of Pittsburgh, PA, Civ. 22-00372 JAO-WRP, at *3, *8 (D. Haw. Sep. 5, 2023), one of the defendants from the *Sunoco* case sued its insurance provider for denying its claims for defense and indemnity coverage under its existing insurance policies. In that case, the insurance company defendants raised twenty-two affirmative

defenses to its obligation to provide coverage, including an argument that climate change litigation fees are not covered under the policy because the plaintiff acted recklessly with respect to is polluting activities. Other scholars have suggested that insurance companies should take other measures to proactively ensure that the scope of their policies does not cover such litigation fees through the use of exclusions, sublimits, and endorsements. See Jason Reeves & Deepa Sutherland, Climate Change Litigation: What Can Liability Insurers Expect in 2024?, Zelle LLP (Feb. 2, 2024). Will the reluctance of insurers to cover defense costs for climate change litigation help mitigate the moral hazard associated with liability insurance? What are the best ways for these insurers to go about avoiding coverage for such lawsuits?

**7.** ***Regulatory Solutions.*** If private lawsuits fail, what system of regulation should be put in their place? Should there be a tax on carbon dioxide emissions, tied to the level of anticipated harm? How would such a tax work for goods that are made outside the United States with carbon dioxide intensive processes? How should the tax be adjusted with changes, up or down, in the perception of the relationship of carbon dioxide levels to global warming? Alternatively, should there be emissions quotas for carbon dioxide? If so, should they be transferrable between parties? For discussions of these questions, compare Alex Muresianu, Carbon Taxes in Theory and Practice, May 2023, https://taxfoundation.org/research/all/eu/carbon-taxes-in-practice/, which argues that existing carbon taxes around the world "reduc[e] emissions at a relatively low economic cost, with a substantial portion of revenue being returned to taxpayers or replacing other tax increases," with Benjamin Zycher, Against a Carbon Tax, Am. Enter. Inst. (June 16, 2022), https://www.aei.org/articles/against-a-carbon-tax/, which argues: "a greenhouse gases tax, like almost all seemingly plausible climate policies, would be all costs and no benefits." Moreover, consider Roger H. Gordon, Carbon Taxes: Many Strengths But Key Weaknesses, Oct. 2023, http://www.nber.org/papers/w31754, which addresses the free-rider problem: "A country would clearly prefer to avoid the costs of abating its own emissions, while continuing to enjoy the benefits from the abatements undertaken in other countries. Reaching a cooperative agreement in such a prisoner-dilemma setting is exceedingly hard."

Separately, note that forcing fossil fuel companies to internalize externalities in tort does not require a regulator to conduct a separate cost-benefit analysis. This is one advantage of damages remedies over regulatory caps. *See* Brief of Professor Catherine M. Sharkey as Amicus Curiae in Support of Plaintiff-Appellant, City of New York v. Chevron Corp., 993 F.3d 81 (2d Cir. 2021) (No. 18-2188).

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# CHAPTER 6

# DEFAMATION

## SECTION A. INTRODUCTION

Iago:

Good name in man and woman, dear my lord,
Is the immediate jewel of their souls:
Who steals my purse steals trash; 'tis something, nothing;
'Twas mine, 'tis his, and has been slave to thousands;

But he that filches from me my good name
Robs me of that which not enriches him,
And makes me poor indeed.

*Othello*, Act III, scene iii

Of all the areas of tort law, defamation is perhaps the most difficult to organize and to understand. At one time defamation was, with only the occasional statutory intervention, a common law subject. Starting from the premise that an individual's reputation should be protected against false words, the common law judges developed an elaborate set of rules to determine what statements were defamatory, when they were actionable or privileged, and what damages could be recovered for them.

The common law of defamation is still important today, but its uncontested supremacy was undermined sixty years ago by the epochal (no lesser word will do) Supreme Court decision in New York Times v. Sullivan, 376 U.S. 254 (1964), which, for the first time, invoked the First Amendment guarantee of freedom of speech to limit the common law of defamation. More specifically, *Sullivan* held that public officials could maintain actions in defamation only upon proof that the defendant's statement was made with "actual malice," defined by the Supreme Court as "knowledge that [the statement] was false or with reckless disregard of whether it was false or not." *Sullivan* was quickly extended to public figures in Curtis Publishing Co. v. Butts, 388 U.S. 130 (1967). Finally, the third of the great constitutional trilogy, Gertz v. Robert Welch, Inc., 418 U.S. 323 (1974), constitutionalized the law of defamation governing suits by private plaintiffs against media defendants. Thereafter the 1980s witnessed many complex and contentious First Amendment cases in which, by and large, the media defendants came out on top by mounting fierce defenses. Since then, there have been relatively few high-profile defamation suits against media defendants, so the basic constitutional ground rules have remained unchanged for the past generation.

Constitutionalizing large portions of the law of defamation did not mark, however, the end of traditional common law issues. Even when public officials sue media defendants, it is still necessary to determine whether the statements made were defamatory, whether they were true, and whether they caused damage to the plaintiff. A complex network of common law issues weaves its way through the modern constitutional fabric so that the skilled defamation



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lawyer must be a master of two intersecting approaches. In addition, as suits by public officials and public figures have dwindled, recent years have witnessed an uptick in defamation actions against businesses, colleges and universities, and charitable organizations, for example, in various personnel matters.

Suits against Internet service providers (ISPs) for messages posted by others began to emerge in the late 1990s. Congress and the courts, fearing the possible adverse effect of tort liability on new digital means of communications, cut back on the scope of liability for Internet providers. Congress enacted §230 of the Communications Decency Act of 1996 (CDA), further explored in this chapter, which states, "No provider or user of an interactive computer service shall be treated as the publisher or speaker of any information provided by another information content provider." 47 U.S.C. §230(c)(1). As a result of §230, there has been little to no application of defamation law as it pertains to new technologies in the United States. Congress's policy choice to virtually freeze the development of defamation law in this regard is an outlier compared to many other countries, which instead have applied a notice and take-down scheme to ISPs. Nonetheless, should Congress ever repeal or amend §230, large and important questions will arise about the application of defamation and related torts to modern social media platforms.

In recent years, high-profile defamation litigation is reemerging as an important area of the law due to concerns about the proliferation of misinformation (or disinformation). Specifically, antidisinformation defamation suits target traditional media companies because of the ways in which they are able to profit from the spread of such false information. Thus, in U.S. Dominion, Inc. v. Fox News Network, the plaintiff sued Fox News for repeatedly airing false broadcasts claiming that its voting machines influenced the outcome of the 2020 Presidential election in favor of Joe Biden. No. N21C-03-257; No. N21C-11-082 (Del. Super. Ct. Mar. 31, 2023), at 16–17. Dominion sought damages in the staggering amount of $1.6 billion. The parties settled for $787.5 million on the eve of trial. See David Bauder, Randall Chase, and Geoff Mulvihill, Dominion Reach $787M Settlement Over Election Claims, Associated Press (Apr. 18, 2023). Defamation suits have also proved effective in protecting individuals who have been the victims of long-lived conspiratorial threats, including death. See Nicki Brown, Alex Jones Ordered to Pay $473 Million in Punitive Damages in Sandy Hook Defamation Case, Reuters (Nov. 10, 2022). These awards are often difficult to collect, but the suits have nonetheless done much to discredit these defendants. See Oliver Darcy, Alex Jones' Company Files for Bankruptcy Amid Texas Trial to Award Damages to Sandy Hook Families, CNN Business (July 30, 2022). For further discussion on the recent upsurge in defamation cases, see Lili Levi, Disinformation and the Defamation Renaissance: A Misleading Promise of "Truth," 57 U. Rich. L. Rev. 1235 (2023).

The shifting patterns of litigation should not be allowed to conceal the still significant differences between the constitutional and common law orientations. Everyone agrees that the central task of the modern law of defamation is to reconcile the interest in reputation with that in freedom of speech. No one thinks that the appropriate balance permits the complete protection of one interest to the exclusion of the other. The disagreement is over the proper balance. Roughly speaking, the common law set its initial presumption in favor of reputation, whereas the Supreme Court has tilted the constitutional balance in favor of freedom of speech. As a result, defamation (and for similar reasons, privacy) stands virtually alone in modern tort law. As the plaintiff's right to recover has been vigorously expanded in other areas, in defamation cases the balance has shifted, often quite dramatically, in favor of the defendant.

The rapid changes in the law of defamation suggest two possible approaches to the subject. The first begins with New York Times v. Sullivan and the constitutional materials and works backward to the common law doctrines as the need arises. Although that approach highlights dramatic and memorable disputes, on balance it suffers from the greater disadvantage of requiring us to jump midstream into a most troubled area of the law, without the

benefit of a (more or less) systematic presentation of its historical development, and without a sense of its special character and language. This chapter, for the sake of historical continuity and analytical clarity, examines the common law tort before turning to the constitutional overlay. These traditional inquiries include: What is publication? What is defamation? What is the distinction between libel and slander, and why is it important? What is the basis of liability in defamation — strict liability, negligence, or intention to harm? What are general and special damages? What privileges are available for defamatory statements in both the private and the public spheres? Are these privileges "absolute" or "qualified"? Only thereafter is the constitutional material taken up in its historical sequence.

**Robert C. Post**

## *The Social Foundations of Defamation Law: Reputation and the Constitution*

74 Calif. L. Rev. 691 (1986)

. . . The common law, as a rule, has "not attempted to define reputation." The dictionary describes it as the "common or general estimate of a person with respect to characteristics or other qualities." Reputation thus inheres in the social apprehension that we have of each other. In one sense, of course, virtually all of our social relationships consist of such apprehension, and it is not clear what it would mean for them all to be "protected" by defamation law. But by looking carefully at the nature of the "injuries affecting a man's *reputation* or good name" defamation is actually designed to redress, one can uncover a more focused image of the exact kinds of social apprehension that defamation law considers "normal," or "desirable," or deserving of the law's protection.

### A. Reputation as Property

. . . The concept of reputation that is most easily available to contemporary observers is that of reputation in the marketplace. This concept of reputation can be understood as a form of intangible property akin to goodwill. It is this concept of reputation that underlies our image of the merchant who works hard to become known as creditworthy or of the carpenter who strives to achieve a name for quality workmanship. Such a reputation is capable of being earned, in the sense that it can be acquired as a result of an individual's efforts and labor. . . . The concept of reputation as property explains why defamation law proscribes aspersions on an individual's character even in contexts that are not narrowly oriented toward business relationships. This is because character can be viewed . . . as "the fruit of personal *exertion*." On this account character "is not inherited from parents; it is not created by external advantages; it is no necessary appendage of birth, or wealth, or talents, or station; but the result of one's own endeavors. . . ."

### B. Reputation as Honor

. . . [Reputation as honor] differs from the concept of reputation as property in [several] characteristics. Whereas reputation as property presupposes the equality of all individuals before the marketplace, honor presupposes that individuals are unequal. An individual's honor is but the personal reflection of the status which society ascribes to his social position. . . . Whereas reputation as property assumes that the value of reputation fluctuates according to individual effort and market conditions, reputation as honor is fixed. Different social positions will be more or less honorific, and within each social position either one will have the honor which

is due that position, or one will not and be accordingly dishonored. Honor cannot be converted into a continuous medium of exchange. It cannot be bought and sold like goodwill, but is instead attached to specific social roles. . . . Whereas reputation as property presupposes that individual identity is distinct from reputation, in the sense that an individual can always construct a new reputation, honor is a matter that swallows "the whole man." . . . The concept of reputation as honor is inconsonant with aspects of defamation law that are difficult to understand from the perspective of reputation as property. For example, the common law distinction between defamatory and nondefamatory communications, which in a market society would leave some actual injuries inexplicably uncompensated, can be conceptualized as a method of distinguishing between those communications that are relevant to the question of honor, and those that are not. Similarly, the common law presumption of damages, which in a market society is simply an undeserved windfall to the plaintiff, can be conceived as empowering juries to pursue the "noncompensatory" end of vindicating the plaintiff's honor in the community.

### C. Reputation as Dignity

. . . The gulf that appears to separate reputation from dignity can be spanned only if defamation law contains an implicit theory of the relationship between the private and public aspects of the self. . . . Dignity . . . is a ritual and ceremonial aspect of the self that we associate with the self's integrity, which is to say with its completeness. Dignity can only be confirmed by the respect that is its due. . . . A preliminary objection to this concept of reputation as dignity is that defamation will not impose liability for breach of a civility rule unless there has been a "publication to a third party". . . . If the function of defamation law is to protect individual dignity, and if individual dignity can be compromised by the violation of civility rules in face-to-face interactions, it is not clear why defamation law refuses to impose liability in such situations. . . . The response to this objection requires us to probe somewhat more deeply into the relationship between civility and dignity. . . . In a purely dyadic exchange, the breach of a rule of civility will have equivocal significance because it is not clear whether the dignity of the recipient or the social competence of the actor has been impaired. When the breach occurs in the presence of third parties, however, the audience is in effect invited to choose between these two interpretations. . . . The dignity that defamation law protects is thus the respect (and self-respect) that arises from full membership in society.

## SECTION B. PUBLICATION

### *Mims v. Metropolitan Life Insurance Co.*

200 F.2d 800 (5th Cir. 1952)

Strum, J. This is an action for libel brought by appellant against appellee, a corporation. The trial court entered summary judgment for defendant below on the ground, amongst others, that there was no publication of the alleged libel, from which judgment plaintiff appeals.

After about 32 years in the employ of defendant company as a branch manager and in other capacities, plaintiff was discharged. He suspected that the reason for this discharge was his refusal to contribute $1.00 to the campaign fund of Senator Taft of Ohio, as suggested in a chain letter sent by defendant's supervisor of agencies in New York to a group of local agency managers, one of whom in turn forwarded a copy to plaintiff. In February, 1950, plaintiff

replied to the agent from whom he received the copy that he was not in sympathy with Senator Taft's policies, and declined to contribute.

When plaintiff's services were discontinued early in 1951, he wrote to his friend Senator Sparkman of Alabama, asking the latter to investigate the cause thereof. Pursuant to this request, and with plaintiff's knowledge and approval, Senator Sparkman directed a letter of inquiry to the defendant's president in New York, summarizing Senator Sparkman's understanding of the situation, and concluding: "I shall appreciate your attention to this matter and your giving me such information as you may care to give."

Defendant's president replied at length by letter, denying that plaintiff's discharge was in any way due to his refusal to contribute to the campaign fund, and stating in effect that it was due to inefficiency and to unsatisfactory production in the branch agencies of which plaintiff was manager from 1934 to 1951, so that it finally became necessary to discontinue plaintiff's services. The letter concludes that the only mistake made by defendant was in giving plaintiff so long an opportunity to make good, in the hope that he might improve. That letter is the basis of this suit. Plaintiff asserts that the statements therein are false, made with malice, and are therefore libelous and unprivileged.

The letter in question was dictated by the president of the defendant company to a company-employed stenographer, who wrote it. It was then mailed to Senator Sparkman in reply to his inquiry, and was received and read by him in Washington, D.C. Plaintiff relies on these circumstances as a sufficient publication to support an action for libel against the corporate defendant. It is not charged that the letter was seen by any other person.

Publication is essential to libel, and the publication must be made to one or more third parties. It is held in New York that dictation of a libelous letter by an individual to his own employee constitutes a sufficient publication in an action against the individual who dictated the letter, as in such circumstances the stenographer is a third party. *Ostrowe v. Lee*, 256 N.Y. 36, 175 N.E. 505. . . .

But this is not such a case. Here, the letter was written by, and the action is against, a corporate defendant which can act only through its agents. Both the person who dictated the letter, and the stenographer who transcribed it, were employed by and acting for the corporation in the performance of a single corporate function, each supplying a component part thereof. When the letter was thus dictated and transcribed, it was not the act of two individuals acting separately. It was one corporate entity acting through two instrumentalities, neither of whom is a third party as respects the corporation, because each is acting as a part of the corporate entity in the performance of a single corporate act, the production of the letter, in the regular course of their duties.

This court has held that where the language complained of was communicated only by one corporate officer to another in the regular course of the corporation's business, such communication did not amount to a publication which would support an action for libel. Although there is one case to the contrary, the weight of authority in New York, where the letter in question was dictated and transcribed, is that mere dictation of libelous matter by a corporate officer or employee to a stenographer also employed by the corporation, in the regular course of the corporation's business, is not such a publication as will support an action for libel against the corporation itself, as in such circumstances the stenographer is not a third party. . . . This is not such a case as Kennedy v. James Butler, 245 N.Y. 204, 156 N.E. 666, in which a corporate defendant communicated libelous matter to employees who had no part in producing the writing, thus exceeding the normal necessities of preparing the writing. If the language of this letter had been communicated to an employee of the corporation whose duties were unconnected with the process by which the letter was produced, such communication might be regarded as an actionable publication. But such is not the case here. Upon the authorities above cited, we hold that there was no sufficient publication of the letter in New York.

We have been directed to no decision squarely in point in the District of Columbia, as to whether writing the letter to Senator Sparkman, in the circumstances here involved, would constitute publication, although that jurisdiction follows the established general rule that it is essential to liability for either libel or slander that the defamatory language be communicated to some one other than the person defamed. It is the law of Alabama, however, which is the state of the forum in which this action was brought, and the state of which the plaintiff is a citizen, that if the language complained of was uttered only to the complaining party or to his agent representing him in the matter discussed in the communication, it is not such a publication as will support an action for slander. Particularly is this true where the communication was solicited by the plaintiff or his agent. This rule prevails in many other jurisdictions, though there is authority to the contrary. See note, 172 A.L.R. 208.

In making the inquiry above mentioned, Senator Sparkman was acting at the express request of plaintiff and with his approval,—virtually as plaintiff's alter ego. Defendant's president replied to the person through whom the inquiry was thus made. The letter complained of having been solicited by plaintiff, through his representative Senator Sparkman, plaintiff thereby impliedly consented that defendant reply through the same representative. In contemplation of law it was a reply to the plaintiff himself. Without plaintiff's solicitation, the letter would not have been written. Upon the authorities about cited, we hold that there was no sufficient publication in the District of Columbia. The statements in the letter sued on do not exceed the scope of the inquiry so as to render the publication actionable because excessive, within the doctrine of Massee v. Williams, 6 Cir., 207 F. 222.

Plaintiff asserts that the language of the letter was uttered with malice, thus destroying the qualified privilege which would otherwise attend it. But we do not reach the matter of privilege or malice until publication has been established, which here has not been done.

Affirmed.

Rives, J., dissenting. There was publication I think, in New York; and the evidence made a strong, if not compelling, case for the jury that there was also publication in Washington.

The fact that a corporation is an artificial entity, and therefore can act only through its agents, does not give it any added immunity for its torts. Corporate agents are just as much individual human beings as are the agents of natural persons. The same rules should apply to both. . . .

The controlling case in New York, it seems to me, should be Ostrowe v. Lee, 256 N.Y. 36, 175 N.E. 505, where Judge Cardozo's opinion settled beyond dispute that publication results from dictation, where the stenographic notes have been transcribed. That case involved a stenographer employed by an individual, but there is nothing in Judge Cardozo's opinion to indicate that the rule would be different if the stenographer were employed by a corporation. . . .

It seems clear to me, however, that the matter did not concern merely the plaintiff but was of great public interest and that Senator Sparkman was properly acting not as a representative of the plaintiff, but in his capacity as a Senator of the United States. He was giving the defendant an opportunity to offer an explanation before referring the matter to the Senate Elections Subcommittee. Certainly the jury could have found that Senator Sparkman was not the plaintiff's alter ego. I therefore respectfully dissent.

## NOTES

**1.** ***Publication, Privilege, and the Defamation Triangle.*** The publication requirement has important structural significance for the law of defamation. Without this requirement,

defamation would be indistinguishable from the insult or deceit that arises when the defendant utters an abusive or false statement to the plaintiff directly. The publication requirement shows that the tort of defamation protects only the interest in reputation, not self-esteem. The publication requirement also accounts for much of the complexity of defamation law, for it ensures that every defamation case must involve at least three people: the plaintiff, the defendant, and the third party to whom the statement was made. Indeed defamation often expands this simple triangle. For example, one defendant can defame a plaintiff to many third parties, each of whom interacts with the plaintiff in different ways.

The publication requirement likewise sets the defamation tort apart from other torts related to economic harms, such as inducement of breach of contract or intentional interference with prospective advantage. For those torts, the key focus is on the loss that the plaintiff suffered as a result of the defendant's actions; therefore causation and loss are the elements of those torts that receive primary focus in litigation. Conversely the defamation tort focuses on protecting the plaintiff's reputational interest, thus placing the primary focus on whether the allegedly defamatory matters were communicated to third parties such that the plaintiff's reputation may be diminished in the eyes of those third parties.

**2. *Prima Facie Publication vs. the Intra-Corporate Privilege.*** The corporate context in *Mims* helps explain the court's unwillingness to find publication. The alternative view is that communications such as those at issue in *Mims* are publications, albeit protected by a qualified intra-corporate privilege. See Newell v. JDS Holdings, L.L.C., 834 N.W.2d 463, 471–72 (Iowa Ct. App. 2013); see also Waugh v. Genesis Healthcare LLC, 222 A.3d 1063, 1067 (Me. 2019), where the court held that the plaintiff failed to prove that the defendant's statements were not protected by a conditional intra-corporate privilege. Some courts have held that this privilege is defeasible upon showing that the publisher of the allegedly defamatory materials is abusing their privilege. See McBride v. Sch. Dist. of Greenville Cnty., 698 S.E.2d 845, 853 (S.C. Ct. App. 2010) ("[A]n employee's statement to another employee is a 'publication' when the privilege of the employees' common interest is abused"). The Second Restatement embraces this position, too. See §577, cmt. *i* (Am. L. Inst. 1977). In Toler v. Süd-Chemie, Inc., 458 S.W.3d 276, 282 n.8 (Ky. 2014), where the parties did not strongly question publication, the court punted: "Whether we should chart a new course and adopt the concept of intracorporate nonpublication can wait for another day."

Conversely, other courts view corporate agents as mere extensions of their principals and, thus, adhere to the minority view that intra-corporate communications do not constitute publications. See, e.g., Bell v. Rogers, 698 So. 2d 749, 756 (La. Ct. App. 1997) ("[S]tatements between employees, made within the course and scope of their employment, are not statements communicated or publicized to third persons so as to constitute publication."). Nevertheless, some of those courts limit the minority view by excepting from publication only communications between managerial employees. See, e.g., RCO Legal, P.S., Inc. v. Johnson, 347 Ga. App. 661, 674 (2018) ("[N]ot all intracorporate statements come within the exception, only those statements received by one who because of his duty or authority has reason to receive the information."). The Restatement of the Law (Third) of Torts: Defamation and Privacy (Preliminary Draft No. 4) explicitly rejects this minority view on the theory that it allows corporate employers to defame their employees without recourse. See Ch. 1 §2, cmts. *j* & *k* (Am. L. Inst. 2024).

**3. *Litigation Strategy and the Intersection of Privileges and Publication.*** One interesting way in which the element of publication and intra-corporate privileges intersect is in the context of litigation strategy. In many cases, such as in *Mims*, courts must decide whether to rule that there is no publication or whether there is an actionable publication and the defendant must later prove that it is privileged as an affirmative defense. If a court were to adopt the former approach, it would likely rule that the plaintiff failed to prove its prima facie defamation case and, thus, may dismiss the claim at the summary judgment stage. Conversely

if a court were to adopt the latter approach, the defendant would have the burden of proving that the communication was privileged at a later stage in the proceedings. This route would involve the factfinder responding to a series of fact-intensive inquiries that could only be handled after a full trial and would lead to drastic changes in the parties' respective litigation strategies. If the *Mims* court decided to treat the letter in question as a publication sufficient for defamation, would that change the outcome of the case? If so, how? Furthermore the Restatement (Second) of Torts specifies that "[t]he fact that a defamatory matter is communicated to an agent of the defamer does not prevent it from being a publication sufficient to constitute actionable defamation." §577, cmt. *e* (Am. L. Inst. 1977). How do you reconcile this position with the decision in *Mims?*

This issue regarding litigation strategy is clearly important in the context of defamation lawsuits, but it also rears its head in the context of other economic torts. For example, recall the case of Asahi Kasei Pharma. Corp. v. Actelion Ltd., *supra* Chapter 4, at 223. The court determined that Actelion was liable for inducement of breach of contract partially based on the fact that California does not afford a company's owner an absolute privilege to interfere with its subsidiary's contracts. Although the *Asahi* case did not involve a defamation claim, it poses a similar issue in regard to privilege and litigation strategy as *Mims*. If the court had found that Actelion was not a stranger to contract due to its ownership of CoTherix, then it likely would have dismissed the inducement of breach claim from the outset (as a party cannot tortiously interfere with its own contract). However, because the court determined that Actelion was a stranger to CoTherix's contract, this determination enabled the cause of action to proceed while prompting Actelion to raise the issue of privilege later in the proceedings. In what ways is the intersection between prima facie elements of the torts and privileges in *Mims* and *Asahi* similar? In what ways is it different?

For further discussion regarding the various privileges related to defamation law, see the discussion of nonconstitutional defenses in Section G.

**RESTATEMENT OF THE LAW (SECOND) OF TORTS**

**§577. What Constitutes Publication**

(1) Publication of defamatory matter is its communication intentionally or by a negligent act to one other than the person defamed.

(2) One who intentionally and unreasonably fails to remove defamatory matter that he knows to be exhibited on land or chattels in his possession or under his control is subject to liability for its continued publication.

***Comment e. Publication to Agent:*** The fact that the defamatory matter is communicated to an agent of the defamer does not prevent it from being a publication sufficient to constitute actionable defamation. The publication may be privileged, however. . . . So too, the communication to a servant or agent of the person defamed is a publication although if the communication is in answer to a letter or a request from the other or his agent, the publication may not be actionable in defamation.

## NOTES

**1.** ***The Prima Facie Elements.*** Publication requires communication to at least one third party. See, e.g., Delta Health Grp., Inc. v. Stafford, 887 So. 2d 887, 896 (Ala. 2004) ("A plaintiff usually satisfies the publication element by proof of communication of the defamatory matter to someone other than himself."). Some states define publication by statute. See, e.g.,

Ga. Code §51-5-3 (2024) ("A libel is published as soon as it is communicated to any person other than the party libeled."). The Second Restatement includes a state of mind requirement for publication — intent *or* negligence. The Restatement of the Law (Third) Torts: Defamation and Privacy (Preliminary Draft No. 4) takes the view that defendants must also have either actual or constructive knowledge of a communication's meaning. Does this additional mental state requirement avoid chilling effects in the information age? Is it required by *Sullivan*, which demands only a form of heightened recklessness as to *falsity*?

**2.** ***Publication by Default.*** Section 577(2) is vividly illustrated by Hellar v. Bianco, 244 P.2d 757, 758 (Cal. App. 1952), in which the

> [r]espondents were the proprietors of a public tavern and for the convenience of patrons maintained a toilet room for men on the wall of which there appeared on May 4, 1950, libelous matter indicating that appellant was an unchaste woman who indulged in illicit amatory ventures. The writer recommended that anyone interested should call a stated telephone number, which was the number of the telephone in appellant's home, and "ask for Isabelle," that being appellant's given name.

The plaintiff was told of the writing by a telephone call from a stranger requesting a date. The defendant did not promptly remove the material when requested to do so by the plaintiff's husband. The trial court dismissed the plaintiff's claim, and the appellate court reversed, holding that knowingly permitting such matter to remain after a reasonable opportunity to remove it made the owner of the tavern liable for a republication. Could a patron of the bar be charged with defamation if he saw the statement and did not remove it?

Since *Hellar*, courts have struggled with the question whether to impose an affirmative duty to remove defamatory matter from one's property. The Restatement (Second) of Torts relied on *Hellar* by imposing liability on those who "intentionally and unreasonably fail to remove defamatory matter that he knows to be exhibited on land or chattels in his possession or under his control." §577(2). The Restatement of the Law (Third) Torts: Defamation and Privacy (Preliminary Draft No. 4) replaces and updates §577(2), however, imposing liability on those who have actual or constructive knowledge of the defamatory matter and fail to remove the matter in a way that leads to a reasonable inference that they endorse or ratify the defamatory content therein. See Ch. 1 §3. How do these approaches differ? Furthermore, although Preliminary Draft No. 4 claims to replace and update §577(2), the lack of fresh case law has effectively led to Draft No. 4 adopting the same position advocated for in *Hellar*. See Ch. 1 §4, cmt. *c*, Reporter's notes. How does the stagnation of the development of this area of defamation law relate to the stagnation of the development of common law after CDA §230?

Although *Hellar* has found support in the various Restatements, the decision is not without its critics. In Tacket v. General Motors Corp., 836 F.2d 1042, 1046–47 (7th Cir. 1987), Easterbrook, J., took a dim view of *Hellar*, stating that "the common law of washrooms is otherwise" and distinguishing places where an observer might infer ratification by the possessor of the property — such as "the interior walls of a manufacturing plant, over which supervisory personnel exercise greater supervision and control" — from places like public washrooms or subway cars, where an observer would not infer ratification. Easterbrook, J., added that the "burden of constant vigilance greatly exceeds the benefits" from imposing liability on property owners who fail to remove allegedly defamatory materials. Does Easterbrook, J., strike the right balance between protecting the reputational interests of those harmed by defamatory statements and placing the burden of avoidance on the parties that can prevent such harms most effectively?

**3.** ***Republication by the Plaintiff.*** A particularly troublesome question arises when the plaintiff herself shows defamatory material to others. Normally this is held to be a publication by the plaintiff. The problem is acute in the area of employment recommendations.

See, e.g., Colonial Stores, Inc. v. Barrett, 38 S.E.2d 306, 308–09 (Ga. Ct. App. 1946) (doctrine appropriate where statute compelled plaintiff to repeat, in "certificate of availability" required by War Manpower Commission, "improper conduct toward fellow employees" as reason for termination). In Kiblitsky v. Lutheran Medical Center, 32 Misc. 3d 575, 580, 582 (N.Y. Sup. Ct. 2011), Demarest, J., discussed the merits of a cause of action for "compelled self-publication" or permitting

> a discharged employee to sue for defamation even if an employer made the defamatory statement to no one other than the employee if the employer knows, or should know, of circumstances where the employee is later put in a position in which he or she has no reasonable means of avoiding publication of the statement and must repeat such statement; usually when seeking new employment.

On the one hand,

> the adoption of the doctrine of self-publication would encourage every employee who feels he or she was discharged for an unflattering reason to bring suit thus unduly burdening the courts as well as creating a huge potential for liability for employers who could do very little to prevent such suits.

On the other hand, self-defamation claims seem warranted where "a plaintiff has no realistic alternative but to submit the defamatory material," in situations where "the defendant knew or could have foreseen that the plaintiff would be compelled to repeat the defamatory statement."

In the case at hand, the plaintiff psychiatrist was terminated "for cause" and then compelled to report this not only to future employers but also to the New York State Board of Education in the process of renewing her license. Her claim, however, did not succeed for two reasons: first, because the New York's Appellate Division "has upheld the general rule that no defamation exists where the plaintiff himself was the only disseminator of the information that he had been fired," and second, because the plaintiff failed to provide the identities of potential employers to whom she was allegedly compelled to repeat the defamatory statements.

By contrast, in McKinney v. County of Santa Clara, 168 Cal. Rptr. 89, 94 (Cal. Ct. App. 1980), the court allowed the compelled self-publication cause of action to proceed because of the strong causal link "where the foreseeable republication is made by the person defamed operating under a strong compulsion to republish the defamatory statement and the circumstances which create the strong compulsion are known to the originator of the defamatory statement at the time he communicates it to the person defamed." See also Van-Go Transp. Co. v. N.Y.C. Bd. of Educ., 971 F. Supp. 90, 104 (E.D.N.Y. 1997).

This doctrine has already been in retreat. Of the seven states that adopted the doctrine of compelled self-publication, four have limited it in later decisions or through statutes. See, e.g., Gore v. Health-Tex, Inc., 567 So. 2d 1307, 1308–09 (Ala. 1990) ("We are not prepared to hold that a plaintiff's own repetition of allegedly defamatory statements can supply the element of publication essential in a slander action."); Churchey v. Adolph Coors Co., 759 P.2d 1336, 1344–45 (Colo. 1988) (en banc), superseded by Colo. Rev. Stat. §13-25-125.5 (2024) ("Self-publication . . . of the defamatory statement to a third person by the person making such allegation shall not give rise to claim for libel or slander against the person who originally communicated the defamatory statement"); Lewis v. Equitable Life Assurance Soc'y, 389 N.W.2d 876 (Minn. 1986), substantially limited by Minn. Stat. §181.993 (2024) (ruling that an employee is barred from bringing a defamation action against the employer upon receiving a written reason for the employee's termination that the employee requested).

Additionally, the courts of eleven states have outright rejected the doctrine, and eight federal courts have either rejected the doctrine or have refused to apply it without clear signals

from state judiciaries. Restatement of the Law (Third) Torts: Defamation and Privacy (Preliminary Draft No. 4) embraces the majority position of the states by rejecting the doctrine of compelled self-publication. See Ch. 1 §2 cmt. *q* (Am. L. Inst. Mar. 2024).

## *Firth v. State of New York*

775 N.E.2d 463 (N.Y. 2002)

Levine, J. This appeal presents the first occasion for us to determine how our defamation jurisprudence, developed in connection with traditional mass media communications, applies to communications in a new medium — cyberspace — in the modern Information Age. Specifically, we must resolve the question whether, for statute of limitations purposes, the single publication rule is applicable to allegedly defamatory statements that are posted on an Internet site and, if so, whether an unrelated modification to a different portion of the Web site constitutes a republication.

Claimant George Firth was formerly employed by the Department of Environmental Conservation as Director of the Division of Law Enforcement. His responsibilities included weapons acquisition. At a press conference held on December 16, 1996, the Office of the State Inspector General issued a report entitled "The Best Bang for Their Buck," which was critical of claimant's managerial style and procurement of weapons. On the same day, the State Education Department posted an executive summary with links to the full text of the report on its Government Information Locator Service Internet site.

On March 18, 1998, more than one year after the report was first released and posted on the Internet, claimant filed a claim against the State alleging that the report defamed him. The State moved to dismiss on the ground that the claim was time-barred under the one-year statute of limitations for defamation. In opposition, claimant argued the merits of his defamation claim, failing to address the statute of limitations issue. . . .

The Court of Claims granted summary judgment to the State, rejecting claimant's argument that the ongoing availability of the report via the Internet constituted a continuing wrong or new publication. The court concluded that the statute of limitations began to run on December 16, 1996, when the report was first made available on the Internet. The court did not address whether the modification of the State's Web site by the addition of the report on the DMV constituted a republication of the report concerning claimant.

The Appellate Division affirmed. . . . Claimant now appeals as of right to this Court (see CPLR 5601[a]).

In Gregoire v. Putnam's Sons, we adopted the single publication rule, namely that

> the publication of a defamatory statement in a single issue of a newspaper, or a single issue of a magazine, although such publication consists of thousands of copies widely distributed, is, in legal effect, one publication which gives rise to one cause of action and that the applicable statute of limitation[s] runs from the date of that publication (81 N.E.2d 45, 47 [N.Y. 1948]; see RST §577A[3]).

Claimant argues that the single publication rule should not be applied verbatim to defamatory publications posted on the Internet in light of significant differences between Internet publications and traditional mass media. Instead, claimant maintains that because a Web site may be altered at any time by its publisher or owner and because publications on the Internet are available only to those who seek them, each "hit" or viewing of the report should be considered a new publication that retriggers the statute of limitations. We disagree.

Under the early common law of defamation, which claimant seeks to have applied in this case, each communication of a defamatory statement to a third person constituted a separate

publication giving rise to a new cause of action. In *Gregoire*, we held that a publisher's sale from stock of a copy of a book containing libelous language did not constitute a new publication. We explained that if the multiple publication rule were applied to such a sale, "the [s]tatute of [l]imitation[s] would never expire so long as a copy of such book remained in stock and is made by the publisher the subject of a sale or inspection by the public. Such a rule would thwart the purpose of the Legislature . . . to bar completely and forever all actions which, as to the time of their commencement, overpass the limitation there prescribed upon litigation."

In addition to increasing the exposure of publishers to stale claims, applying the multiple publication rule to a communication distributed via mass media would permit a multiplicity of actions, leading to potential harassment and excessive liability, and draining of judicial resources. Further, the single publication rule actually reduces the possibility of hardship to plaintiffs by allowing the collection of all damages in one case commenced in a single jurisdiction. . . .

The policies impelling the original adoption of the single publication rule support its application to the posting of the Inspector General's report regarding claimant on the State's Web site. Communications accessible over a public Web site resemble those contained in traditional mass media, only on a far grander scale. . . . Communications posted on Web sites may be viewed by thousands, if not millions, over an expansive geographic area for an indefinite period of time.

Thus, a multiple publication rule would implicate an even greater potential for endless retriggering of the statute of limitations, multiplicity of suits and harassment of defendants. Inevitably, there would be a serious inhibitory effect on the open, pervasive dissemination of information and ideas over the Internet, which is, of course, its greatest beneficial promise. Thus, we hold that the single publication rule applies in this case.

Claimant alternatively argues that if the single publication rule governs, the State should be deemed to have republished the report within one year of the filing of the claim when it added an unrelated report of the Inspector General on the DMV to the Education Department's Web site in May 1997. We conclude as a matter of law that this modification of the State's Web site did not constitute a republication of the allegedly defamatory report at issue here.

Republication, retriggering the period of limitations, occurs upon a separate aggregate publication from the original, on a different occasion, which is not merely "a delayed circulation of the original edition." The justification for this exception to the single publication rule is that the subsequent publication is intended to and actually reaches a new audience. Thus, for example, repetition of a defamatory statement in a later edition of a book, magazine or newspaper may give rise to a new cause of action.

The mere addition of unrelated information to a Web site cannot be equated with the repetition of defamatory matter in a separately published edition of a book or newspaper. . . . The justification for the republication exception has no application at all to the addition of unrelated material on a Web site, for it is not reasonably inferable that the addition was made either with the intent or the result of communicating the earlier and separate defamatory information to a new audience.

We observe that many Web sites are in a constant state of change, with information posted sequentially on a frequent basis. For example, this Court has a Web site which includes its decisions, to which it continually adds its slip opinions as they are handed down. Similarly, Web sites are used by news organizations to provide readily accessible records of newsworthy events as they occur and are reported. Those unrelated additions are indistinguishable from the asserted DMV report modification of the State's Web site here. A rule applying the republication exception under the circumstances here would either discourage the placement of information on the Internet or slow the exchange of such information, reducing the Internet's

unique advantages. In order not to retrigger the statute of limitations, a publisher would be forced either to avoid posting on a Web site or use a separate site for each new piece of information. These policy concerns militate against a holding that any modification to a Web site constitutes a republication of the defamatory communication itself.

[Affirmed.]

## NOTES

**1. *Mass Publication.*** *Firth* follows the Restatement (Second) of Torts §577A, which provides that "[a]ny one edition of a book or newspaper, or any one radio or television broadcast, exhibition of a motion picture or similar aggregate communication is a single publication" for which only one action in defamation may be maintained. Courts have uniformly followed *Firth* in applying the single publication rule to Internet publication. As Easterbrook, J., explains in Pippen v. NBC Universal Media, LLC, 734 F.3d 610 (7th Cir. 2013):

> [N]o court has been persuaded that the even greater control that Internet publishers have over their content [as compared to book publishers] — and the much lower cost of editing or deleting that content — is a reason to exclude them from the [single publication rule]. Indeed, courts have drawn the opposite conclusion: the Internet's greater reach comes with an "even greater potential for endless retriggering of the statute of limitations, multiplicity of suits and harassment of defendants."

A contrary ruling, as Griffin, J., notes in Clark v. Viacom International Inc., 617 F. App'x 495, 503 (6th Cir. 2015), would "as a functional matter . . . make the statute of limitations irrelevant in the online defamation context," given that "[t]he possibility of defamation liability would hover over any publicly available online statement regardless of its age as long as a plaintiff could find a third party who had not previously seen it."

**2. *Republication Exception.*** In *Firth*, posting of an unrelated report to a website housing the allegedly defamatory statement did not constitute republication. Nor have courts found the following to constitute republication: a third party reposting the statement elsewhere on the Internet (see Jankovic v. Int'l Crisis Grp., 494 F.3d 1080 (D.C. Cir. 2007)); creating hypertext links to the previously published statement (see Salyer v. S. Poverty L. Ctr., Inc., 701 F. Supp. 2d 912 (W.D. Ky. 2009)); changing the URL where the story was posted (see Canatalla v. Van De Kamp, 486 F.3d 1128 (9th Cir. 2007)); or new "top comments" by third parties on an article written by the defendant (see Biro v. Conde Nast, 963 F. Supp.2d 255, 268 (S.D.N.Y. 2013)).

By contrast, in Larue v. Brown, 333 P.3d 767, 773 (Ariz. Ct. App. 2014), Gould, J., held that updates or modifications that affect the substance of the allegedly defamatory material constituted "republication" of the defamatory statements. Thus a husband and wife's defamation action against the wife's ex-husband and his wife based on Internet articles alleging that the husband had molested the wife's four-year-old daughter was not barred by the statute of limitations where defendants had replied to comments made in response to their original defamatory articles when "[t]he comments were displayed directly beneath the original articles, thereby implying they were supplements to the original articles."

Not all changes to alleged defamatory material constitute republication. In many defamation cases, there is a delicate question of whether minor modifications constitute the publication of a new article or a modest modification of an old one. The question assumes a good deal of urgency when the statute of limitations has run on the original publication but not on the revision. In Petro-Lubricant Test v. Adelman, 184 A.3d 457, 462–63 (N.J. 2018),

the defendant Adelman operated a website that published a list of "America's Worst Bosses," on which the individual plaintiff, John Wintermute, ranked 39th. After Wintermute complained, the article was modified, but not to Wintermute's liking. Albin, J., split the baby:

> We now hold that the single publication rule applies to an internet article. However, if a material and substantive change is made to the article's defamatory content, then the modified article will constitute a republication, restarting the statute of limitations. In the record before us, there are genuine issues of disputed fact concerning whether Adelman made a material and substantive change to the original article. . . .
>
> The most significant change for purposes of this appeal is the replacement of, "[Wintermute] also allegedly forced workers to listen to and read white supremacist materials," with "John Wintermute also allegedly regularly subjected his employees to 'anti-religion, anti-minority, anti-Jewish, anti-[C]atholic, anti-gay rants,'" quoting from Laforgia's complaint.
>
> Adelman continued to rank Wintermute as number thirty-nine on eBossWatch.com's worst-bosses list.

Should the statute of limitations ever start anew if the revised version of the article is less defamatory than the original?

**3.** ***Republication by Third Parties.*** Even before the advent of the Internet, the common law held the defendant liable for defamation only when he had both knowledge of what was published and discretion over whether to make or withhold publication. Neither of those requirements was met, for example, by a public library that rarely knew the contents of its many holdings and could not refuse to check out a book that might contain some defamatory material.

> Those who merely deliver or transmit defamatory material previously published by another will be considered to have published the material only if they knew, or had reason to know, that the material was false and defamatory. It is this rule that protects libraries and vendors of books, magazines, and newspapers.

Church of Scientology of Minn. v. Minn. State Med. Ass'n Found., 264 N.W.2d 152, 156 (Minn. 1978).

This rule has particular relevance to active Internet sites. In February 1996, Congress enacted the Communications Decency Act of 1996 (CDA), 47 U.S.C. §230(c)(1), which effectively immunizes ISPs from liability for distributing or publishing defamatory material created by others. But what if the ISP takes an active role in promoting defamatory material created by another?

## *Zeran v. America Online, Inc.*

129 F.3d 327 (4th Cir. 1997)

Wilkinson, C.J. Kenneth Zeran brought this action against America Online, Inc. ("AOL"), arguing that AOL unreasonably delayed in removing defamatory messages posted by an unidentified third party, refused to post retractions of those messages, and failed to screen for similar postings thereafter. The district court granted judgment for AOL on the grounds that the CDA — 47 U.S.C. §230 — bars Zeran's claims. Zeran appeals, arguing that §230 leaves intact liability for interactive computer service providers who possess notice of defamatory material posted through their services. He also contends that §230 does not apply here because his claims arise from AOL's alleged negligence prior to the CDA's enactment. Section 230, however, plainly immunizes computer service providers like AOL from liability for information that originates with third parties. Furthermore, Congress clearly expressed its intent that §230 apply to lawsuits, like Zeran's, instituted after the CDA's enactment. Accordingly, we affirm the judgment of the district court. . . .

. . . On April 25, 1995, an unidentified person posted a message on an AOL bulletin board advertising "Naughty Oklahoma T-Shirts." The posting described the sale of shirts featuring offensive and tasteless slogans related to the April 19, 1995, bombing of the Alfred P. Murrah Federal Building in Oklahoma City. Those interested in purchasing the shirts were instructed to call "Ken" at Zeran's home phone number in Seattle, Washington. As a result of this anonymously perpetrated prank, Zeran received a high volume of calls, comprised primarily of angry and derogatory messages, but also including death threats. . . .

. . . Meanwhile, an announcer for Oklahoma City radio station KRXO received a copy of the first AOL posting. On May 1, the announcer related the message's contents on the air, attributed them to "Ken" at Zeran's phone number, and urged the listening audience to call the number. After this radio broadcast, Zeran was inundated with death threats and other violent calls from Oklahoma City residents. Over the next few days, Zeran talked to both KRXO and AOL representatives. He also spoke to his local police, who subsequently surveilled his home to protect his safety. By May 14, after an Oklahoma City newspaper published a story exposing the shirt advertisements as a hoax and after KRXO made an on-air apology, the number of calls to Zeran's residence finally subsided to fifteen per day.

Zeran first filed suit on January 4, 1996, against radio station KRXO in the United States District Court for the Western District of Oklahoma. On April 23, 1996, he filed this separate suit against AOL in the same court. Zeran did not bring any action against the party who posted the offensive messages. . . . AOL answered Zeran's complaint and interposed [CDA] §230 as an affirmative defense. AOL then moved for judgment on the pleadings pursuant to Fed. R. Civ. P. 12(c). The district court granted AOL's motion, and Zeran filed this appeal.

The relevant portion of §230 states: "No provider or user of an interactive computer service shall be treated as the publisher or speaker of any information provided by another information content provider." 47 U.S.C. §230(c)(1). By its plain language, §230 creates a federal immunity to any cause of action that would make service providers liable for information originating with a third-party user of the service. Specifically, §230 precludes courts from entertaining claims that would place a computer service provider in a publisher's role. Thus, lawsuits seeking to hold a service provider liable for its exercise of a publisher's traditional editorial functions—such as deciding whether to publish, withdraw, postpone or alter content—are barred. . . .

. . . Zeran argues, however, that the §230 immunity eliminates only publisher liability, leaving distributor liability intact. Publishers can be held liable for defamatory statements contained in their works even absent proof that they had specific knowledge of the statement's inclusion. . . .

. . . Because of the difference between these two forms of liability, Zeran contends that the term "distributor" carries a legally distinct meaning from the term "publisher." Accordingly, he asserts that Congress' use of only the term "publisher" in §230 indicates a purpose to immunize service providers only from publisher liability. He argues that distributors are left unprotected by §230 and, therefore, his suit should be permitted to proceed against AOL. We disagree. Assuming *arguendo* that Zeran has satisfied the requirements for imposition of distributor liability, this theory of liability is merely a subset, or a species, of publisher liability, and is therefore also foreclosed by §230.

The terms "publisher" and "distributor" derive their legal significance from the context of defamation law. Although Zeran attempts to artfully plead his claims as ones of negligence, they are indistinguishable from a garden variety defamation action. Because the publication of a statement is a necessary element in a defamation action, only one who publishes can be subject to this form of tort liability. Restatement (Second) of Torts §558(b) (1977). Publication does not only describe the choice by an author to include certain information. In addition, both the negligent communication of a defamatory statement and the failure to remove such

a statement when first communicated by another party — each alleged by Zeran here under a negligence label — constitute publication. . . .

. . . Those who are in the business of making their facilities available to disseminate the writings composed, the speeches made, and the information gathered by others may also be regarded as participating to such an extent in making the books, newspapers, magazines, and information available to others as to be regarded as publishers. They are intentionally making the contents available to others, sometimes without knowing all of the contents — including the defamatory content — and sometimes without any opportunity to ascertain, in advance, that any defamatory matter was to be included in the matter published. AOL falls squarely within this traditional definition of a publisher and, therefore, is clearly protected by §230's immunity.

. . . Zeran . . . contends that interpreting §230 to impose liability on service providers with knowledge of defamatory content on their services is consistent with the statutory purposes [of CDA §230]. Zeran fails, however, to understand the practical implications of notice liability in the interactive computer service context. . . .

If computer service providers were subject to distributor liability, they would face potential liability each time they receive notice of a potentially defamatory statement — from any party, concerning any message. Each notification would require a careful yet rapid investigation of the circumstances surrounding the posted information, a legal judgment concerning the information's defamatory character, and an on-the-spot editorial decision whether to risk liability by allowing the continued publication of that information. . . . Because service providers would be subject to liability only for the publication of information, and not for its removal, they would have a natural incentive simply to remove messages upon notification, whether the contents were defamatory or not. . . . Thus, like strict liability, liability upon notice has a chilling effect on the freedom of Internet speech.

More generally, notice-based liability for interactive computer service providers would provide third parties with a no-cost means to create the basis for future lawsuits. Whenever one was displeased with the speech of another party conducted over an interactive computer service, the offended party could simply "notify" the relevant service provider, claiming the information to be legally defamatory. In light of the vast amount of speech communicated through interactive computer services, these notices could produce an impossible burden for service providers, who would be faced with ceaseless choices of suppressing controversial speech or sustaining prohibitive liability. Because the probable effects of distributor liability on the vigor of Internet speech and on service provider self-regulation are directly contrary to §230's statutory purposes, we will not assume that Congress intended to leave liability upon notice intact. . . .

. . . For the foregoing reasons, we affirm the judgment of the district court.

## *Blumenthal v. Drudge*

992 F. Supp. 44 (D.D.C. 1998)

[In early 1995, Matt Drudge created an electronic publication called the Drudge Report, a gossip column focusing on gossip from Hollywood and Washington, DC. In addition to posting content on a free Internet website, Drudge had developed a list of regular subscribers to whom he emailed the Drudge Report. In 1997, Drudge entered into an agreement with America Online (AOL), an ISP, to make the Drudge Report available to all members of AOL's service for a period of one year. Drudge agreed to create, edit, update, and "otherwise manage"

the content of the Drudge Report, and AOL retained the right to "remove content that AOL reasonably determine[s] to violate AOL's then standard terms of service." Under the licensing agreement, Drudge transmitted new editions of the Drudge Report by emailing them to AOL and AOL then posted the new editions on its service. In exchange, Drudge received a flat monthly "royalty payment" of $3,000 from AOL. Drudge had no other source of income.

On August 10, 1997, the Drudge Report posted a story claiming that Sidney Blumenthal, who was about to begin employment as an assistant to President Clinton, had physically abused his wife, Jacqueline Jordan Blumenthal, who also worked in the White House as Director of the President's Commission on White House Fellowships. The Blumenthals sued AOL and Drudge, contending that the statement was defamatory. Drudge later retracted the story and publicly apologized. AOL filed a motion for summary judgment, arguing that it was immune from suit under section 230 of the CDA.]

**Matt Drudge (left) and Sidney Blumenthal (right)**

*Sources: Drudge: Evan Agostini/Getty Images; Blumenthal: MediaPunch Inc / Alamy Stock Photo*

Friedman, J. . . .

[Under the Communications Decency Act of 1996], whether wisely or not, [Congress] made the legislative judgment to effectively immunize providers of interactive computer services from civil liability in tort with respect to material disseminated by them but created by others. In recognition of the speed with which information may be disseminated and the near impossibility of regulating information content, Congress decided not to treat providers of interactive computer services like other information providers such as newspapers, magazines or television and radio stations, all of which may be held liable for publishing or distributing obscene or defamatory material written or prepared by others. While Congress could have made a different policy choice, it opted not to hold interactive computer services liable for their failure to edit, withhold or restrict access to offensive material disseminated through their medium. . . .

AOL acknowledges both that section 230(c)(1) would not immunize AOL with respect to any information AOL developed or created entirely by itself and that there are situations in which there may be two or more information content providers responsible for material

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disseminated on the Internet-joint authors, a lyricist and a composer, for example. While section 230 does not preclude joint liability for the joint development of content, AOL maintains that there simply is no evidence here that AOL had any role in creating or developing any of the information in the Drudge Report. The Court agrees. It is undisputed that the Blumenthal story was written by Drudge without any substantive or editorial involvement by AOL. AOL was nothing more than a provider of an interactive computer service on which the Drudge Report was carried, and Congress has said quite clearly that such a provider shall not be treated as a "publisher or speaker" and therefore may not be held liable in tort. 47 U.S.C. §230(c)(1).

[The court analyzed Wilkinson's, C.J., reasoning in *Zeran* and concluded: "The court in *Zeran* has provided a complete answer to plaintiffs' primary argument, an answer grounded in the statutory language and intent of Section 230."]

Plaintiffs make the additional argument, however, that Section 230 of the Communications Decency Act does not provide immunity to AOL in this case because Drudge was not just an anonymous person who sent a message over the Internet through AOL. He is a person with whom AOL contracted, whom AOL paid $3,000 a month—$36,000 a year, Drudge's sole, consistent source of income—and whom AOL promoted to its subscribers and potential subscribers as a reason to subscribe to AOL. Furthermore, the license agreement between AOL and Drudge by its terms contemplates more than a passive role for AOL; in it, AOL reserves the "right to remove, or direct [Drudge] to remove, any content which, as reasonably determined by AOL . . . violates AOL's then-standard Terms of Service. . . ." By the terms of the agreement, AOL also is "entitled to require reasonable changes to . . . content, to the extent such content will, in AOL's good faith judgment, adversely affect operations of the AOL network."

In addition, shortly after it entered into the licensing agreement with Drudge, AOL issued a press release making clear the kind of material Drudge would provide to AOL subscribers—gossip and rumor—and urged potential subscribers to sign onto AOL in order to get the benefit of the Drudge Report. The press release was captioned: "AOL Hires Runaway Gossip Success Matt Drudge." It noted that "[m]averick gossip columnist Matt Drudge has teamed up with America Online," and stated: "Giving the Drudge Report a home on America Online (keyword: Drudge) opens up the floodgates to an audience ripe for Drudge's brand of reporting. . . . AOL has made Matt Drudge instantly accessible to members who crave instant gossip and news breaks." Why is this different, the Blumenthals suggest, from AOL advertising and promoting a new purveyor of child pornography or other offensive material? Why should AOL be permitted to tout someone as a gossip columnist or rumor monger who will make such rumors and gossip "instantly accessible" to AOL subscribers, and then claim immunity when that person, as might be anticipated, defames another?

If it were writing on a clean slate, this Court would agree with plaintiffs, [given that AOL is not a "passive conduit like the telephone company," but instead exercises "editorial control" over Drudge's work]. But Congress has made a different policy choice by providing immunity even where the interactive service provider has an active, even aggressive role in making available content prepared by others. In some sort of tacit quid pro quo arrangement with the service provider community, Congress has conferred immunity from tort liability as an incentive to Internet service providers to self-police the Internet for obscenity and other offensive material, even where the self-policing is unsuccessful or not even attempted. . . .

Any attempt to distinguish between "publisher" liability and notice-based "distributor" liability and to argue that Section 230 was only intended to immunize the former would be unavailing. Congress made no distinction between publishers and distributors in providing immunity from liability. [Here, the court embraces the reasoning from *Zeran*.] While it appears to this Court that AOL in this case has taken advantage of all the benefits conferred

by Congress in the Communications Decency Act, and then some, without accepting any of the burdens that Congress intended, the statutory language is clear: AOL is immune from suit, and the Court therefore must grant its motion for summary judgment.

## NOTES

**1. *Internet Service Providers as Publishers.*** Before the passage of the Communications Decency Act of 1996, courts struggled to decide whether ISPs should be considered distributors or publishers. In Cubby, Inc. v. CompuServ, Inc., 776 F. Supp. 135, 141 (S.D.N.Y. 1991), the court held that a computer service company that provided its subscribers with access to an electronic library of news publications put together by an independent third party and loaded onto a server was a mere "distributor" of information. Accordingly it could not be held liable for defamatory statements made in news publications absent a showing that it knew or had reason to know of specific defamatory material. In contrast, the court in Stratton Oakmont, Inc. v. Prodigy Services Co., 23 Media L. Rep. 1794 (N.Y. Sup. Ct. 1995), distinguished *Cubby* and held that Prodigy, a company that used an automatic software screening program to control content on its bulletin boards, was a publisher rather than a distributor. Section 230 of the CDA was passed a year later to remove the liability created by the *Stratton Oakmont* decision. Did Congress find the appropriate balance between incentivizing self-regulation and the promotion of Internet communications?

**2. *Scope of CDA §230 Immunity.*** In *Zeran*, AOL did not remove the material from its site for some time despite promising to do so, exposing the plaintiff to death threats and other abusive communications. Why grant the immunity after the defendant has been informed of the defamatory material? Note that the plaintiff in *Zeran* argued that *Stratton Oakmont* recognized a legal distinction between publishers and distributors. But the *Zeran* court explained that decisions like *Stratton Oakmont* distinguish between "publishers" and "distributors" only insofar as those two terms describe two different standards of liability — distributors must have knowledge of the existence of a defamatory statement — even though both fall within the larger "publisher" category for purposes of §230 immunity.

**3. *Distributor Liability and Defamation.*** In the age of the Internet, the distinction between publisher liability and distributor liability has become a critical issue. If publisher and distributor liability are distinct concepts, why does the dicta in the *Zeran* case above discuss distributor liability as a subset of publisher liability? What does this tell us about the relationship between the two types of liability?

One of the primary reasons that courts tend to apply different rules to these two different groups is the different roles they play in acquiring and disseminating information. Primary publishers such as newspapers, broadcasters, authors, and book publishers tend to play a more active role in gathering and distributing information. Distributors, such as bookstores, news vendors, libraries, and others who merely transmit information provided to them by third parties play a far more passive role. Because distributors are not presumed by U.S. courts to have knowledge of the content they disseminate to the public, they are typically subject to liability only when the distributor's failure to stop distributing the information leads to a reasonable inference that the distributor endorses or ratifies its content. See Restatement of the Law (Third) Torts: Defamation and Privacy (Preliminary Draft No. 4), Ch. 1 §4, cmt. *c* (Am. L. Inst. Mar. 2024). The Third Restatement takes the position that ISPs should legally qualify as distributors. Are these positions reconcilable?

Although the Third Restatement has adopted a toned-down version of the "notice-and-take-down" scheme, it does not go as far as other common law defamation regimes have. For

example, the European E-Commerce Directive enacted in 2000 enables European countries to hold ISPs liable for third-party content posted or stored on their platforms if they fail to remove the content after being notified of its illegality.

As the development of U.S. defamation law has become increasingly stagnant due to CDA §230, the imposition of a notice-and-take-down scheme has garnered more and more support from U.S. legal scholars. Cass R. Sunstein, Your Good Name, *in* Liars: Falsehoods and Free Speech in an Age of Deception 89, 103 (2021), advocates an approach similar to the Digital Millennium Copyright Act that would require Internet companies to take down defamatory materials after receiving notice of their defamatory nature. See also Jack Balkin, How to Regulate (and Not Regulate) Social Media, Knight Institute Occasional Paper Series, No. 1 (Mar. 25, 2020). In what ways does a notice-and-take-down scheme differ from the Second Restatement's approach? Does the Third Restatement's approach make a notice-and-take-down scheme unworkable in the United States? What changes need to be made to U.S. defamation law for a notice-and-take-down scheme to be enacted?

## *Jones v. Dirty World Ent. Recordings LLC*

755 F.3d 398 (6th Cir. 2014)

Gibbons, J. This case presents the issue of whether the Communications Decency Act of 1996 (CDA), 47 U.S.C. §230, bars the state-law defamation claims of plaintiff-appellee Sarah Jones. Jones was the unwelcome subject of several posts anonymously uploaded to www.TheDirty.com, a popular website operated by defendants-appellants Nik Lamas-Richie and DIRTY WORLD, LLC ("Dirty World"), and of remarks Richie posted on the site. The website enables users to anonymously upload comments, photographs, and video, which Richie then selects and publishes along with his own distinct, editorial comments. In short, the website is a user-generated tabloid primarily targeting nonpublic figures.

In response to the posts appearing on www.TheDirty.com, Jones brought an action in federal district court alleging state tort claims of defamation, libel *per se*, false light, and intentional inflection of emotional distress. Richie and Dirty World claimed that §230(c)(1) barred these claims. The district court rejected this argument and denied defendants-appellants' motion to dismiss, motion for summary judgment, motion to revise judgment, and motion for judgment as a matter of law. The district court also denied Richie's and Dirty World's motion for leave to file an interlocutory appeal. The case was submitted to a jury, twice. The first trial ended in a mistrial upon a joint motion. The second trial resulted in a verdict in favor of Jones for $38,000 in compensatory damages and $300,000 in punitive damages. On appeal, Richie and Dirty World maintain that §230(c)(1) barred Jones's claims. . . .

. . . Richie is currently employed as the manager of DIRTY WORLD, LLC ("Dirty World"), which owns and operates the website www.TheDirty.com. . . . Richie's website garnered attention from national media, and, as the site increased in popularity, it branched out to cover more than seventy different cities in the United States and Canada. . . . For the past several years and currently, users of the site, who colloquially refer to themselves as "The Dirty Army," may submit "dirt" — *i.e.*, content that may include text, photographs, or video about any subject. Users may also post comments about the content submitted by others. The vast majority of the content appearing on www.TheDirty.com is comprised of submissions uploaded directly by third-party users. . . . Submissions appear on the website as though they were authored by a single, anonymous author — "THE DIRTY ARMY." This eponymous introduction is automatically added to every post that Richie receives from a third-party user. Many, but not all, of the submissions and commentaries appearing on the website relate to stories, news, and gossip about local individuals who are not public figures.

Sarah Jones is a resident of northern Kentucky. Jones was a teacher at Dixie Heights High School in Edgewood, Kentucky, and a member of the Cincinnati Bengals, the cheerleading squad for the Cincinnati Bengals professional football team. From October 2009 to January 2010, Jones was the subject of several submissions posted by anonymous users on www.TheDirty.com and of editorial remarks posted by Richie. [The court recounted the posts, which pertained to, *inter alia*, Jones's purported sexual proclivities, her partners' infidelities, and the possibility that Jones's partners infected her with sexually transmitted diseases. Ritchie commented on several posts, noting that Jones—and the Cincinnati Bengals cheerleaders as a whole—are not physically attractive. Ritchie also lamented that he was no longer "jealous of those high school kids for having a cheerleader teacher" in response to a post pertaining to sexually transmitted diseases.]

Jones sent Richie over twenty-seven emails, pleading for Richie to remove these posts from the website, to no avail. Jones's father similarly wrote to Richie, also to no avail. She then sought legal help, and her attorney informed Richie that if the posts were not removed by December 14, 2009, Jones would file suit. . . . After the litigation commenced, Richie posted a public letter to Jones: "If you know the truth then why do you care? . . . All you had to do is read the FAQ section like every other normal person to get stuff removed. You dug your own grave here Sarah." . . . [Ritchie] also removed the first three posts regarding Jones.

The sole issue on appeal is whether the district court erred in denying Dirty World's and Richie's motion for judgment as a matter of law by holding that the CDA does not bar Jones's state tort claims. . . .

[The court reviewed the purposes of §230 immunity: (1) It "maintain[s] the robust nature of Internet communication and, accordingly, . . . keep[s] government interference in the medium to a minimum." (2) It "protects against the 'heckler's veto' that would chill free speech." (3) It "encourages interactive computer service providers to self-regulate."]

. . . Section 230(c)(1)'s grant of immunity is not without limits, however. It applies only to the extent that an interactive computer service provider is not also the information content provider of the content at issue. An "information content provider" is defined as "any person or entity that is responsible, in whole or in part, for the creation or development of information provided through the Internet or any other interactive computer service." 47 U.S.C. §230(f)(3). A website operator can simultaneously act as both a service provider and a content provider. If a website displays content that is created entirely by third parties, then it is only a service provider with respect to that content—and thus is immune from claims predicated on that content. But if a website operator is in part responsible for the creation or development of content, then it is an information content provider as to that content—and is not immune from claims predicated on it. . . .

. . . This case turns on how narrowly or capaciously the statutory term "development" in §230(f)(3) is read. The district court held, and Jones maintains on appeal, that Dirty World and Richie are not immune under the CDA because Dirty World and Richie are information content providers with respect to the information underlying Jones's defamation claims because they developed that information. . . . According to the district court, "a website owner who intentionally encourages illegal or actionable third-party postings to which he adds his own comments ratifying or adopting the posts becomes a 'creator' or 'developer' of that content and is not entitled to immunity." Dirty World and Richie argue that the district court's test of development is erroneous, swallowing the protection provided by §230(c)(1) and undermining the purposes served by the CDA. They maintain that, properly understood, they did not develop the statements forming the basis of Jones's defamation claims. . . .

. . . An overly inclusive interpretation of "development" in §230(f)(3) would posit that a website operator is responsible for the development of content created by a third party merely by displaying or allowing access to it. But to read the term so broadly would defeat

the purposes of the CDA and swallow the core immunity that §230(c) provides for the "exercise of a publisher's traditional editorial functions" [citing *Zeran*, *supra*]. Our recognition that the CDA affords immunity forecloses this overbroad reading of "development." By contrast, an overly exclusive interpretation of "development" would exclude all the publishing, editorial, and screening functions of a website operator from the set of actions that the term denotes. . . .

. . . Consistent with our sister circuits, we adopt the material contribution test to determine whether a website operator is "responsible, in whole or in part, for the creation or development of [allegedly tortious] information." 47 U.S.C. §230(f)(3). . . .

We now apply the material contribution measure of "development" to the facts of this case. . . . Dirty World and Richie did not author the statements at issue; however, they did select the statements for publication. But Richie and Dirty World cannot be found to have materially contributed to the defamatory content of the statements posted on October 27 and December 7, 2009, simply because those posts were selected for publication. . . . Nor can they be found to have materially contributed to the defamatory content through the decision not to remove the posts. [Citing *Zeran*, *supra* at 316]. . . .

. . . Because (1) the defendants are interactive service providers, (2) the statements at issue were provided by another information content provider, and (3) Jones's claim seeks to treat the defendants as a publisher or speaker of those statements, the CDA bars Jones's claims. . . .

. . . For the foregoing reasons, we vacate the judgment in favor of Jones and reverse the district court's denial of Dirty World's and Richie's motion for judgment as a matter of law with instructions to enter judgment as a matter of law in their favor.

## NOTES

**1.** ***Rejection of the "Encouragement Test."*** The district court found that Dirty World and Richie's conduct exceeded the bounds of §230 immunity. Specifically, it held that a "website owner who intentionally encourages illegal or actionable third-party postings to which he adds his own comments ratifying or adopting the posts becomes a 'creator' or 'developer' of that content and is not entitled to immunity." The Sixth Circuit rejected this encouragement test of CDA immunity:

> Many websites not only allow but also actively invite and encourage users to post particular types of content. Some of this content will be unwelcome to others—*e.g.*, unfavorable reviews of consumer products and services, allegations of price gouging, complaints of fraud on consumers, reports of bed bugs, collections of cease-and-desist notices relating to online speech. And much of this content is commented upon by the website operators who make the forum available. Indeed, much of it is "adopted" by website operators, gathered into reports, and republished online.

Jones v. Dirty World, 755 F.3d at 414. Would the encouragement test subject websites to hecklers' suits? How would courts decide what constitutes "encouragement" to determine immunity under the CDA?

**2.** ***Rejection of "Ratification Test."*** The district court also decided that when an ISP adds commentary to third-party content that "ratifies or adopts" that content, then the provider becomes a "creator" or "developer" of that content and is not entitled to the CDA's protection. To what extent should a website operator be responsible for what makes another party's statement actionable by commenting on that statement? Does the ratification test unduly stretch the concept of responsibility? Does the broad immunity furnished by the CDA

leave persons who are the objects of anonymously posted, online, defamatory content without remedy? Are there any limits to §230 immunity? What about if a website requires users to post illegal or actionable conduct as a condition of use?

## *Fair Housing Council of San Fernando Valley v. Roommates.Com, LLC*

521 F.3d 1157 (9th Cir. 2008)

Kozinski, C.J. Defendant Roommate.com, LLC ("Roommate") operates a website designed to match people renting out spare rooms with people looking for a place to live. At the time of the district court's disposition, Roommate's website featured approximately 150,000 active listings and received around a million page views a day. Roommate seeks to profit by collecting revenue from advertisers and subscribers.

Before subscribers can search listings or post housing opportunities on Roommate's website, they must create profiles, a process that requires them to answer a series of questions. In addition to requesting basic information—such as name, location and email address—Roommate requires each subscriber to disclose his sex, sexual orientation and whether he would bring children to a household. . . .

. . . The Fair Housing Councils of the San Fernando Valley and San Diego ("Councils") sued Roommate in federal court, alleging that Roommate's business violates the federal Fair Housing Act ("FHA"), 42 U.S.C. §3601 *et seq*., and California housing discrimination laws. Councils claim that Roommate is effectively a housing broker doing online what it may not lawfully do off-line. The district court held that Roommate is immune under section 230 of the CDA, 47 U.S.C. §230(c), and dismissed the federal claims without considering whether Roommate's actions violated the FHA. . . . Councils appeal the dismissal of the FHA claim and Roommate cross-appeals the denial of attorneys' fees.

Section 230 of the CDA immunizes providers of interactive computer services against liability arising from content created by third parties. . . . This grant of immunity applies only if the interactive computer service provider is not also an "information content provider," which is defined as someone who is "responsible, in whole or in part, for the creation or development of" the offending content. *Id*. §230(f)(3).

A website operator can be both a service provider and a content provider: If it passively displays content that is created entirely by third parties, then it is only a service provider with respect to that content. But as to content that it creates itself, or is "responsible, in whole or in part" for creating or developing, the website is also a content provider. Thus, a website may be immune from liability for some of the content it displays to the public but be subject to liability for other content. . . .

. . . Councils allege that requiring subscribers to disclose their sex, family status and sexual orientation "indicates" an intent to discriminate against them, and thus runs afoul of both the FHA and state law. . . . [W]e examine the scope of plaintiffs' substantive claims only insofar as necessary to determine whether section 230 immunity applies. However, we note that asking questions certainly *can* violate the Fair Housing Act and analogous laws in the physical world. For example, a real estate broker may not inquire as to the race of a prospective buyer, and an employer may not inquire as to the religion of a prospective employee. If such questions are unlawful when posed face-to-face or by telephone, they don't magically become lawful when asked electronically online. The Communications Decency Act was not meant to create a lawless no-man's-land on the Internet. . . .

. . . Councils also charge that Roommate's development and display of subscribers' discriminatory preferences is unlawful. Roommate publishes a "profile page" for each subscriber on its website. The page describes the client's personal information—such as his sex, sexual

orientation and whether he has children — as well as the attributes of the housing situation he seeks. . . . Roommate then displays these answers, along with other information, on the subscriber's profile page. This information is obviously included to help subscribers decide which housing opportunities to pursue and which to bypass. In addition, Roommate itself uses this information to channel subscribers away from listings where the individual offering housing has expressed preferences that aren't compatible with the subscriber's answers. . . . By requiring subscribers to provide the information as a condition of accessing its service, and by providing a limited set of pre-populated answers, Roommate becomes much more than a passive transmitter of information provided by others; it becomes the developer, at least in part, of that information. . . .

. . . Similarly, Roommate is not entitled to CDA immunity for the operation of its search system, which filters listings, or of its email notification system, which directs emails to subscribers according to discriminatory criteria. Roommate designed its search system so it would steer users based on the preferences and personal characteristics that Roommate itself forces subscribers to disclose. If Roommate has no immunity for asking the discriminatory questions, as we concluded above, it can certainly have no immunity for using the answers to the unlawful questions to limit who has access to housing. . . .

. . . Roommate's search function is similarly designed to steer users based on discriminatory criteria. Roommate's search engine thus differs materially from generic search engines such as Google, Yahoo! and MSN Live Search, in that Roommate designed its system to use allegedly unlawful criteria so as to limit the results of each search, and to force users to participate in its discriminatory process. In other words, Councils allege that Roommate's search is designed to make it more difficult or impossible for individuals with certain protected characteristics to find housing — something the law prohibits. By contrast, ordinary search engines do not use unlawful criteria to limit the scope of searches conducted on them, nor are they designed to achieve illegal ends — as Roommate's search function is alleged to do here. Therefore, such search engines play no part in the "development" of any unlawful searches. . . .

. . . Councils finally argue that Roommate should be held liable for the discriminatory statements displayed in the "Additional Comments" section of profile pages. . . . Roommate publishes these comments as written. It does not provide any specific guidance as to what the essay should contain, nor does it urge subscribers to input discriminatory preferences. Roommate is not responsible, in whole or in part, for the development of this content, which comes entirely from subscribers and is passively displayed by Roommate. . . . Councils argue that — given the context of the discriminatory questions presented earlier in the registration process — the "Additional Comments" prompt impliedly suggests that subscribers should make statements expressing a desire to discriminate on the basis of protected classifications; in other words, Councils allege that, by encouraging *some* discriminatory preferences, Roommate encourages other discriminatory preferences when it gives subscribers a chance to describe themselves. But the encouragement that bleeds over from one part of the registration process to another is extremely weak, if it exists at all. Such weak encouragement cannot strip a website of its section 230 immunity, lest that immunity be rendered meaningless as a practical matter. . . .

. . . We believe that this distinction is consistent with the intent of Congress to preserve the free-flowing nature of Internet speech and commerce without unduly prejudicing the enforcement of other important state and federal laws. When Congress passed section 230 it didn't intend to prevent the enforcement of all laws online; rather, it sought to encourage interactive computer services that provide users *neutral* tools to post content online to police that content without fear that through their "good Samaritan . . . screening of offensive material," 47 U.S.C. §230(c), they would become liable for every single message posted by third parties on their website.

In light of our determination that the CDA does not provide immunity to Roommate for all of the content of its website and email newsletters, we remand for the district court to determine in the first instance whether the alleged actions for which Roommate is not immune violate the Fair Housing Act, 42 U.S.C. §3604(c). . . .

## NOTES

**1.** ***Material Contribution to Illegality Test.*** In *Roommates*, the boundaries of section 230 immunity are tested in the brave new world where online service providers replace traditional housing services, subject to the strictures of law prohibiting discrimination. On remand, the district court found Roommate liable for violating the FHA and granted in part plaintiffs' motion for partial summary judgment. 2008 WL 14410024, at *8 (C.D. Cal. 2008). The Ninth Circuit overturned the ruling on the ground that the FHA does not apply to shared living units. 666 F.3d 1216, 1222 (9th Cir. 2012). This saga illustrates the practical difficulties in ascertaining material contributions to illegality. Does the complexity of the underlying statutory scheme in *Roommates* suggest that the material contribution standard is unworkable?

Compare *Roommates* with Chicago Lawyers' Committee for Civil Rights Under Law, Inc. v. Craigslist, Inc., 519 F.3d 666 (7th Cir. 2008), where an online service provider offered an electronic meeting place for buyers, sellers, or renters to post notices advertising housing that stated preference, limitation, or discrimination based on race, religion, sex, or family status. The court held it was not a "publisher" or "speaker," under the CDA, of posted notices with information provided by someone else. Should the distinction between a publisher and distributor rest upon whether or not a website prepares survey questions or only offers an open entry field?

**2.** ***Hyperlinking and Publication.*** A hot topic in defamation with the rise of the Internet is whether including a hyperlink to a defamatory statement constitutes a republication. Generally courts have held that a hyperlink alone is not a republication that establishes a separate, actionable cause of action for defamation. See *In re* Phila. Newspapers, LLC, 690 F.3d 161, 175 (3d Cir. 2012) ("[A]s long as it does not restate the defamatory material, [mere reference to an article] does not republish the material"); Lokhova v. Halper, 995 F.3d 134, 143 (4th Cir. 2021) ("The public policy supporting the single publication rule and the traditional principles of republication dictate that a mere hyperlink, without more, cannot constitute republication"). Additionally certain jurisdictions have extended this doctrine of immunizing hyperlinks from liability to situations where the plaintiff includes minor additional commentary along with the hyperlink. See, e.g., Lindberg v. Dow Jones & Co., 2021 WL 3605621, at *2 (S.D.N.Y. Aug. 11, 2021) (finding that in-text comments included with a hyperlink to "a *Journal* investigation in February" was not a publication of the underlying content). However, courts have been less forgiving when comments included with the hyperlinks indicate support of the linked defamatory content. See, e.g., Brimelow v. N.Y. Times Co., 2020 WL 7405261, at *7 (S.D.N.Y. Dec. 16, 2020) (distinguishing defendant's behavior on the basis that they "adopted" the characterization of the plaintiff made by the hyperlinked source material and "shared [it] with a new audience"). How does this hyperlink doctrine connect to the "material contribution to illegality" test employed by the courts in the *Roommates* and *Dirty World* cases?

**3.** ***Rise of Algorithmic and Machine Learning.*** With the rise of artificial intelligence and machine learning, how should the "material contribution" test apply to websites that generate news feed content based on users' past browsing data? In Gonzalez v. Google, Inc., 598 U.S. 617 (2023), the plaintiffs sued Google on a theory that the company was directly and

secondarily liable for the death caused by ISIS's terrorist attacks in Paris. The plaintiffs argued that Google forfeited CDA immunity by materially contributing to videos uploaded by ISIS by spreading the video through YouTube video-sharing channels' subscribers. The court rejected the plaintiffs' argument that Google's algorithms constituted "development," because "development" required "not merely . . . augmenting the content generally, but [rather] materially contributing to its alleged unlawfulness." Because Google's targeted algorithms were content neutral, Google did not satisfy the "material contribution test" and therefore did not lose CDA immunity for the upload of ISIS videos.

When the case reached the Supreme Court in Google v. Gonzalez, 598 U.S. 617 (2023), the Court dismissed the claims in a per curiam opinion without addressing the question of §230 immunity. In a companion case, Twitter Inc. v. Taamneh, 598 U.S. 471 (2023), where the plaintiffs sued Facebook, Twitter, and Google for knowingly allowing ISIS and its members to use their platforms to aid their recruitment, fundraising, and propaganda efforts, the Court dismissed the claims: "The mere creation of those platforms . . . is not culpable." In its ruling, the Court impliedly supported the underlying reasoning of §230 by specifying that "we generally do not think that internet or cell service providers incur culpability merely for providing their services to the public writ large." But the Court left for another day the question whether the defendants were immunized by §230.

As machine-learning algorithms based on user-generated data become increasingly sophisticated, at what point should they qualify as "development" sufficient to strip away CDA immunity? Websites like Facebook take increasingly active roles by providing catered news feeds and suggested contacts based on its algorithms. Should Facebook qualify as a co-developer of content, where the suggested news feeds and groups are generated by its machine-learning algorithms, instead of humans? With the increasing sophistication of machine-learning algorithms and aggregation of user-generated data, how should CDA respond? If the original purposes of granting ISPs immunity were to protect the development of the Internet and promote self-regulation, what new purposes does CDA immunity serve in the age of artificial intelligence?

**4. *CDA §230 Immunity and Online Censorship.*** With the strong populist resentment against Internet services like Facebook and Google, pressure continues to mount to either repeal or limit section 230. For a cautionary response, see Jeff Kosseff, Section 230 Created the Internet as We Know It. Don't Mess with It, Los Angeles Times, Mar. 29, 2019, https://www.latimes.com/opinion/op-ed/la-oe-kosseff-section-230-internet-20190329-story.html. An August 2019 draft executive order entitled "Protecting Americans from Online Censorship" proposed significant limitations on the autonomy that ISPs enjoy under CDA §230. The White House proposal contemplated having the Federal Communications Commission (FCC) police alleged social media censorship. The draft order "calls for the FCC to develop new regulations clarifying how and when the law protects social media websites when they decide to remove or suppress content on their platforms." Should the FCC step in to regulate social media platforms? If so, would government intervention create more or less online censorship?

Although the provisions of this White House proposal were substantially incorporated into President Trump's Executive Order on Preventing Online Censorship, President Biden revoked that order after entering office. See Exec. Order No. 13,925, 85 Fed. Reg. 34079 (May 28, 2020); Exec. Order No. 14,029, 86 Fed. Reg. 27025 (May 14, 2021).

The Supreme Court has not clarified the protection afforded to social media companies when removing or editing content posted on their platforms. In Moody v. NetChoice LLC, 603 U.S. 707, 144 S. Ct. 2383 (2024), trade associations with social media company

members sued the Attorney General of Florida over the enactment of a law that restricted the ability of social media companies to control whether and how content posted on their platforms is displayed for other users. The Supreme Court consolidated this case with NetChoice, LLC v. Paxton, Docket No. 22–555, which involved the passage of a similar law enacted by Texas. Instead of responding to the First Amendment claims raised in these cases, the Supreme Court vacated the lower courts' decisions and remanded the cases because "Neither the Eleventh Circuit nor the Fifth Circuit performed the facial analysis" required by the issues at hand. The Court also refrained from clarifying the extent to which regulating content moderation on social media platforms comports with First Amendment protections for free speech. Justice Jackson commented that "not every hypothesized regulation of such a company's operations will necessarily be able to withstand the force" of the First Amendment, but beyond that "it is difficult to say much more at this time." *Id*. at 1 (Jackson, J., concurring). In this case does it matter whether the court finds that these sites are run autonomously or whether they coordinate their activities with the government or with each other?

In the early case of Associated Press v. United States, 326 U.S. 1, 6–7, 20 (1945) where a system of by-laws "which prohibited all AP members from selling news to non-members, and which granted each member powers to block its non-member competitors from membership," Black, J. held that the First Amendment offered no protection of these activities:

> Member publishers of AP are engaged in business for profit exactly as are other business men who sell food, steel, aluminum, or anything else people need or want. All are alike covered by the Sherman Act. The fact that the publisher handles news while others handle food does not, as we shall later point out, afford the publisher a peculiar constitutional sanctuary in which he can with impunity violate laws regulating his business practices. . . .
>
> The First Amendment, far from providing an argument against application of the Sherman Act, here provides powerful reasons to the contrary.

That position was explicitly and strongly endorsed in Miami Herald v. Tornillo, 418 U.S. 241, 252 (1974), *infra* at 357.

Does it apply to coordinated actions by the plaintiff if they remove the conservative site Parler from their servers on the grounds that they supplied unbalanced coverage in favor of the January 6, 2021 events? One early commentor wrote: "The most crucial part of today's case is that the platforms are no different from newspapers, the archetypal bearers of free press and free speech rights." Noah Feldman, Supreme Court Social Media Ruling Is a Free-Speech Landmark, Bloomberg (July 1, 2024, 12:20 PM), https://www.eastbaytimes.com/2024/07/03/feldman-supreme-court-social-media-ruling-is-a-free-speech-landmark/. Given the connectedness of media sites, is that correct?

## SECTION C. FALSE OR DEFAMATORY STATEMENTS

**RESTATEMENT OF THE LAW (SECOND) OF TORTS**

**§559. Defamatory Communication Defined**

A communication is defamatory if it tends so to harm the reputation of another as to lower him in the estimation of the community or to deter third persons from associating or dealing with him.

## *Parmiter v. Coupland*

151 Eng. Rep. 340, 342 (Ex. 1840)

Parke, B. A publication, without justification or lawful excuse, which is calculated to injure the reputation of another, by exposing him to hatred, contempt, or ridicule, is a libel.

## *Muzikowski v. Paramount Pictures Corp.*

322 F.3d 918 (7th Cir. 2003)

Wood, J. [In 2000, defendant Paramount Pictures released a movie, *Hardball*, with the actor Keanu Reeves, which was based on a book written by Daniel Coyle, *Hardball: A Season in the Projects*. The book recorded Coyle's experiences as a Little League coach on the North Side of Chicago. The book was described as a work of nonfiction and contained throughout it various references to plaintiff Robert Muzikowski by name. In contrast to the book, the movie credits stated: "While this motion picture is in part inspired by actual events, persons and organizations, this is a fictitious story and no actual persons, events or organizations have been portrayed." The movie then chronicles the activities of other coaches in the league, including one fictitious coach named Conor O'Neill. Neither Robert Muzikowski's first or last name is used in the film. O'Neill's character was based in part on the plaintiff Muzikowski, but the movie attributed to O'Neill certain derogatory features that Muzikowski did not have. The accurate biographical information was that the O'Neill character had dropped out of college after the death of his father, had used illegal drugs and alcohol, had been arrested for participating in a bar brawl that left a scar on his left hand, had driven a blue station wagon, had from time to time "lost it," and had spoken at the funeral of one of his players who had been killed in a gang incident. After Paramount began promoting the movie in 2000, Muzikowski began getting telephone calls from all over the country from friends and acquaintances telling him that Paramount was about to make a movie about him. The defamation suit arose because of the negative features that *Hardball* had added to the historical record. It stated that O'Neill had not been able to break his drinking habit when, in reality, Muzikowski had not had a drink in 17 years. The movie depicted O'Neill as having committed various crimes such as "battery, theft, criminal destruction of property, disorderly conduct, and drinking on the public way," and depicted him as falsely representing himself as a broker when he did not hold a license. In the movie, O'Neill is a ticket scalper and gambler, and gets involved with Little League to pay off a gambling debt when in fact Muzikowski had done so "solely out of a genuine concern for children."

The plaintiff's efforts to enjoin distribution of the film came to naught, and the district court dismissed his claim for damages on summary judgment. After disposing of some preliminary procedural matters, Wood, J., continued:]

### III

The parties agree that Illinois law applies to the substance of Muzikowski's claim, and so (to the extent it is pertinent) we will confine our discussion accordingly. A defamatory statement is one that "tends to cause such harm to the reputation of another that it lowers that person in the eyes of the community or deters third persons from associating with him." Kolegas v. Heftel Broad. Corp., 607 N.E.2d 201, 206 (Ill. 1992). An Illinois defamation action may state a claim either for defamation *per se* (statements so harmful to reputation

that damages are presumed) or defamation *per quod* (statements requiring extrinsic facts to show their defamatory meaning). Bryson v. News Am. Publ'ns, Inc., 672 N.E.2d 1207, 1214 (Ill. 1996). The district court found that Muzikowski had not stated a claim for defamation *per se* because the statements Paramount made were reasonably capable of an "innocent construction" or of referring to somebody other than Muzikowski. It dismissed the *per quod* claim because, under Fed. R. Civ. P. 9(g) (which applies to a state law defamation case in federal court), Muzikowski had not met the heightened pleading standard for special damages and pecuniary loss.

### A

We begin with the defamation *per se* claim. In a *per se* action, Muzikowski may recover only if Paramount's statements fit into one of the limited categories of statements or imputations that Illinois considers actionable *per se*: (1) commission of a criminal offense; (2) infection with a venereal disease; (3) inability to perform or want of integrity in the discharge of duties of public office; (4) fornication or adultery; or (5) words that prejudice a party in her trade, profession, or business.

Even if a statement falls into a recognized category, it will not be actionable per se if the statement "may reasonably be innocently interpreted or reasonably be interpreted as referring to someone other than the plaintiff." Chapski v. Copley Press, 442 N.E.2d 195, 199 (Ill. 1982). In Illinois courts, this determination is made by the judge and it is regarded as a question of law. Allocation of functions between judge and jury in federal court, however, are a matter of federal law. Moreover, facts beyond those that appear in a federal complaint may be relevant to the reasonableness inquiry, which requires that statements be read in their natural sense, not in the light most favorable to the defendant. However, if a statement is capable of two reasonable constructions, one defamatory and one innocent, the innocent one will prevail.

Paramount provides two reasons why it is reasonable to construe the statements in question as referring to someone other than Muzikowski (namely O'Neill, an entirely fictional character). First, it points to material differences between Muzikowski and O'Neill, which Muzikowski himself identifies in his complaint. Second, it contends that because Hardball is a work of fiction, it cannot reasonably be interpreted to refer to Muzikowski.

The second contention is more easily dispensed with and so we turn to it first. "[S]imply because the story is labeled 'fiction' and, therefore, does not purport to describe any real person" does not mean that it may not be defamatory *per se*. In *Bryson*, the plaintiff sued a magazine publisher over an article appearing in its fiction section. The article featured a character who also had the last name of Bryson (but not the plaintiff's first name), and who was described as a "slut." The article was set in southern Illinois, where both the plaintiff and the author of the article resided, and the plaintiff alleged 25 other physical attributes and life experiences she shared with the character. Under these circumstances, the Illinois Supreme Court held that the plaintiff should have the opportunity to prove that the character bore "such a close resemblance to the plaintiff that reasonable persons would understand that the character was actually intended to portray the plaintiff." In light of *Bryson*, the mere fact that Paramount labeled its movie "fictitious" is not enough to shield it from an Illinois defamation action.

Paramount responds that its case is different from *Bryson* because Robert Muzikowski is never referenced by name in *Hardball*, and thus his pleading cannot be construed to support a claim for defamation *per se*. . . . [*Bryson* and other cases suggest] that there is no automatic ban on recovery if the plaintiff is not named, . . . but that instead that Illinois imposes a heightened pleading standard for complaints basing claims on publications that do not literally name the plaintiff.

That may be the Illinois pleading rule, but it of course does not apply in a federal court. . . . Even if Muzikowski's complaint would not have met Illinois's heightened pleading standard, we are satisfied that it was sufficient to put Paramount on notice of his claim. In his complaint, he lists in great detail many similarities between himself and O'Neill that could cause a reasonable person in the community to believe that O'Neill was intended to depict him and that Paramount intended *Hardball*'s mischaracterizations to refer to him.

Notwithstanding those details, Paramount argues that Muzikowski has failed to plead a category of speech that is defamatory *per se*. Muzikowski in response asserts that he fits within two of the five possible categories. First, Muzikowski claims Paramount's portrayal of O'Neill has injured him in his profession or business. In *Hardball*, O'Neill is lying when he tells people that he is a licensed securities broker. As a matter of substantive Illinois law, alleging or implying that a person is not a legitimate member of her profession is defamatory *per se*. Paramount is correct that some of Muzikowski's other allegations, such as his claim that he will be damaged because the movie asserts that his motives for coaching were pecuniary and not philanthropic, are statements of opinion which do not amount to defamation *per se*. But the narrow accusation that O'Neill/Muzikowski is an unlicensed broker fits squarely within the *per se* category.

Furthermore, Muzikowski has adequately alleged that Paramount has imputed to him the commission of a crime of moral turpitude. Such a crime cannot be a mere misdemeanor but must be punishable by imprisonment. Muzikowski describes numerous crimes that the O'Neill character commits, some of which (such as ticket scalping and drinking on the public way) are not punishable by imprisonment. Some of them, however, are more serious, such as the crime of theft, which has been held to be defamatory *per se*.

In the end, the most serious hurdle Muzikowski faces is the question whether he has in essence pleaded himself out of court, by showing that the federal trier of fact (whether judge or jury) would be compelled to find an innocent construction of the movie. Paramount argues that this is the case, and in support of its position it points to a number of differences between the real and the fictional man that are apparent on the face of the complaint. *Hardball* focuses on how O'Neill, a down-and-out gambler, finds redemption by coaching an inner-city baseball league. Muzikowski, in contrast, found redemption long before he became involved in Little League. O'Neill drinks alcohol, while Muzikowski no longer does. O'Neill gambles while Muzikowski does not, and O'Neill begins coaching only to pay for his gambling addiction while Muzikowski co-founded multiple inner-city leagues out of a genuine concern for children.

In our view, Muzikowski might be able to produce evidence showing that there is in fact no *reasonable* interpretation of the movie that would support an innocent construction. He may be able to show that no one could think that anyone but him was meant, and the changes to "his" character, far from supporting an innocent construction that O'Neill is a fictional or different person, only serve to defame him in the ways already discussed. We conclude that Muzikowski's allegations, read in the light most favorable to him, entitle him to the chance to prove his claim under a defamation *per se* theory. As the case develops further, of course, it is entirely possible that Paramount will be able to produce enough facts to support its "innocent construction" argument. At this stage, however, we believe it was premature to reject Muzikowski's case.

**B**

[The court then dismissed Muzikowski's per quod claim because he "concedes in his reply brief that he did not itemize his losses or plead specific damages of actual financial injury."]

[Reversed and remanded.]

## NOTES

**1. *Mitior Sensus.*** As *Muzikowski* indicates, defamation law must set rules of construction for ambiguous statements. In the early common actions for slander, the maxim was: "Sensus verborum est duplex, mitis et asper, et verba semper sunt accipienda in mitiore sensu." (Loosely translated: "When words have two meanings, lenient and severe, they will always be construed in the more lenient sense.") An early work, George Spencer Bower, Actionable Defamation 332, 333 (1908), recounted the extremes to which this rule had been taken:

> To take a few illustrations, it was solemnly held in one case that a "coiner" *might* mean an officer in the Mint; in another, the expression "forger" *might* conceivably import no more than the honourable industry of the metal-worker. . . .
>
> This curious doctrine originated at a period in the history of the English law of defamation when the devices employed by the courts of common law to recover their lost jurisdiction over actions of slander had achieved an embarrassing success, and similarly artificial methods had to be resorted to in order to keep within manageable bounds the ever rising flood of this species of litigation. The fact that the doctrine was never applied to libel, the courts not being burdened overmuch with actions of this description, betrays the opportunism of its origin, and so also does the fact that, as soon as the practical necessity for its application ceased to exist, the rule, like all other expedients "ad hoc," disappeared utterly.

For a modern account of this and other early developments in the law of defamation, see Richard H. Helmholz, Select Cases on Defamation to 1600 (1985).

**2. *Ordinary Meaning Versus Innocent Construction.*** The question of innocent construction often turns on time and circumstances. In *Bryson*, discussed in *Muzikowski*, the defendant described the plaintiff using the term "slut," which Roby v. Murphy, 27 Ill. App. 394 (1888), had held to be not defamatory in 1888.

> At the time *Roby* was decided, Webster's dictionary defined the term "slut" as "an untidy woman," "a slattern" or "a female dog," and stated that the term was "the same as 'bitch.'" Apparently, when *Roby* was decided, none of the dictionary definitions of "slut" implied sexual promiscuity. Moreover, the *Roby* court found that, even in its "common acceptance," the term "slut" did not amount to a charge of unchastity.
>
> We cannot simply assume that the term "slut" means the same thing today as it did a century ago. Many modern dictionaries include the definitions of the term "slut" cited in *Roby*, but add new definitions that imply sexual promiscuity. See, e.g., Webster's New World Dictionary (2d Coll. ed. 1975) ("a sexually immoral woman"); American Heritage Dictionary 1153 (2d Coll. ed. 1985) ("[a] woman of loose morals" "prostitute"). Moreover, in the present age, the term "slut" is commonly used and understood to refer to sexual promiscuity.

McMorrow, J., weighed in with this dissent:

> As a general rule, it is not actionable to call a woman a "slut" unless the word is used in such a manner as to impute whoredom. This rule recognizes that the word itself does not always impute a breach of chastity, but carries with it such nonactionable connotations as brazen or shameless. Indeed, as defendants point out, and the majority concedes, the American Heritage Dictionary contains several definitions of the word "slut," such as a "slovenly, dirty woman," "a woman of loose morals," a "prostitute," "a bold, brazen girl," or "a female dog." Consequently, because the word has many different meanings, most of which are not defamatory *per se*, context is crucial; for as noted above, if a word "may reasonably be innocently interpreted," it is not actionable *per se*.

The Supreme Court refused to apply any rule of innocent construction in Milkovich v. Lorain Journal Co., 497 U.S. 1, 21 (1990), as follows: "It is simply this: if you get in a jam, lie your way out," and "[i]f you're successful enough, and powerful enough, and can sound sincere enough, you stand an excellent chance of making the lie stand up, regardless

of what really happened." The Court rebuffed defendant's efforts to dismiss these statements as "loose, figurative or hyperbolic language" to which the opinion privilege would attach. "Simply couching such statements in terms of opinion does not dispel these implications; and the statement, 'In my opinion Jones is a liar,' can cause as much damage to reputation as the statement, 'Jones is a liar.'"

Similarly, in Masson v. New Yorker Magazine, Inc., 501 U.S. 496, 513 (1991), the Supreme Court refused to afford the opinion privilege to allegedly fabricated quotations in which the plaintiff was said to have described himself as an "intellectual gigolo" — "you get pleasure from him, but don't take him out in public" — during an interview with Janet Malcolm, the writer of the *New Yorker* story. Kennedy, J., noted that in a serious account published in a magazine that "seemed to enjoy a reputation for scrupulous factual accuracy," a reader could be expected to take these words at "face value."

> A defendant may be able to argue to the jury that quotations should be viewed by the reader as nonliteral or reconstructions, but we conclude that a trier of fact in this case could find that the reasonable reader would understand the quotations to be nearly verbatim reports of statements made by the subject.

*Masson* further explained the common law principle that inaccuracies alone do not render a statement false if there remains "substantial truth" to what was said. "Minor inaccuracies do not amount to falsity so long as 'the substance, the gist, the sting, of the libelous charge be justified.'" *Masson* thus rejected the notion that any alteration of the plaintiff's words beyond corrections of grammar and syntax alone would prove falsity for the purpose of establishing actual malice.

*Masson* finally came to closure eleven years after the publication of the original *New Yorker* story, when the jury found that two of Malcolm's statements were false, one of which was defamatory, but that none had been published with the actual malice necessary for awarding damages. For an account of the subdued ending to an epic struggle, see David Margolick, Psychoanalyst Loses Libel Suit Against New Yorker Reporter, N.Y. Times, Nov. 3, 1994, at A1.

In Lott v. Levitt, 556 F.3d 564, 569–70 (7th Cir. 2009), defendant Steven Levitt (and his unnamed coauthor Steven Dubner) published in their best-selling book *Freakonomics*, which embarked on a "treasure-hunt" of freakish curiosities, the following passage about the economist John Lott, who was the author of the book *More Guns, Less Crime*:

**John Lott**
*Source: Wikimedia Commons*

> Then there was the troubling allegation that Lott actually invented some of the survey data that support his more-guns/less-crime theory. Regardless of whether the data were faked, Lott's admittedly intriguing hypothesis doesn't seem to be true. When other scholars have tried to replicate his results, they found that right-to-carry laws simply don't bring down crime.

In response to Lott's claim that this passage "amounted to an accusation that he falsified his results," Evans, J., invoked the doctrine of innocent construction to deflect Lott's claim that the statement was defamatory per se:

> Using an academic definition of "replicate," Lott maintains that the passage means that others repeated, to a tee, his technical analysis but were unable to duplicate his results, suggesting that he either faked his data or performed his analysis incompetently.

> But this technical reading is not the only reasonable interpretation of the passage. After all, *Freakonomics* didn't become a bestseller by targeting just academics. . . . In this context, it is reasonable to read "replicate" in more generic terms. That is, the sentence could mean that scholars tried to reach the same conclusion as Lott, using different models, data, and assumptions, but could not do so. This reading does not imply that Lott falsified his results or was incompetent; instead, it suggests only that scholars have disagreed with Lott's findings about the controversial relationship between guns and crime. By concluding that this more generic definition of "replicate" is reasonable, we are not assuming that the reader is a simpleton. After all, econometrics is far from conventional wisdom. We are, however, taking into account the context of the statement and acknowledging that the natural and obvious meaning of "replicate" can lie outside the realm of academia for this broadly appealing book.
>
> A closer look at the paragraph where the contested sentence is found supports this innocent reading. The paragraph describes and critiques Lott's "idea," "theory," and "hypothesis," but makes no mention of his methodology or what data set he used. In this context, it is natural to read Levitt's statement as a critique on his theory, rather than an accusation of falsifying data. In fact, instead of weighing in on the rumor that Lott faked some of his results, Levitt distanced himself from it. Levitt mentioned the "troubling allegation," but noted that "[r]egardless of whether the data were faked, Lott's admittedly intriguing hypothesis doesn't seem to be true." Far from assailing Lott's competence, he acknowledged that Lott's theory is "sensible" and "intriguing."

Does Lott's claim survive if it applies only to the professional economists who read the book?

**3. *Newspaper Headlines.*** Unlike reviews and opinion pieces, context plays a diminished role with newspaper headlines, which are thereafter corrected by qualifications buried in the body of the text. A headline may be libelous even though the full story sufficiently explains it. The rule was justified in Sprouse v. Clay Communication, Inc., 211 S.E.2d 674, 686 (W. Va. 1975):

> Generally, where the headline is of normal size and does not lead to a conclusion totally unsupported by the body of the story, both story and headline are to be considered together for their total impression. However, where oversized headlines are published which reasonably lead the average reader to an entirely different conclusion [from] the facts recited in the body of the story, and where the plaintiff can demonstrate that it was the intent of the publisher to use such misleading headlines to create a false impression on the normal reader, the headlines may be considered separately with regard to whether a known falsehood was published.

See also Restatement (Second) of Torts §563, comment *d*, which notes that the "context" of a defamatory newspaper headline does not "ordinarily" include the text of the article itself. These principles were applied in Kaelin v. Globe Communications Corp., 162 F.3d 1036 (9th Cir. 1998), in which the defendant published in the *National Examiner* a headline—COPS THINK KATO DID IT—one week after O.J. Simpson was acquitted of the murders of Nicole Brown Simpson and Ronald Goldman. The court held that the headline standing alone was capable of meaning that Kato Kaelin, who was staying in a guest house on the Simpson property, had committed the murders. It rejected the argument that a sub-headline—"he fears that they want him for perjury, say pals"—and the story, buried seventeen pages in the interior of the *National Examiner*, were sufficient to escape liability.

> Since the publication occurred just one week after O.J. Simpson's highly publicized acquittal for murder, we believe that a reasonable person, at that time, might well have concluded that the "it" in the first sentence of the cover and the internal headlines referred to the murders. Such a reading of the first sentence is not negated by or inconsistent with the second sentence as a matter of logic, grammar, or otherwise. In our view, an ordinary reader reasonably could have read the headline to mean that the cops think that Kato committed the murders *and* that Kato thinks that he is wanted for perjury.

**4. *Of and Concerning the Plaintiff.*** H. Walker Royall was involved in controversial development activities in Freeport, Texas. His efforts, along with those of others, were chronicled in a book, *Bulldozed*, written by Carla Main, portions of which sought to "tell the story of the City's plan to use eminent domain to condemn waterfront property along the Old Brazos River to build a private yacht marina." Royall sued Main, her publisher Encounter Books, and Professor Richard Epstein for defamation. Epstein had written this blurb on the back of the book:

> Like a Greek tragedy unfolding, Carla Main's book chronicles the eminent domain struggles in Freeport, Texas, which pitted the Gore family, with its longtime shrimp business, against the machinations of an unholy alliance between city politicians and avaricious developers. If you have ever shared the Supreme Court's unquestioned deference to the public planning process that shaped its ill-fated *Kelo* decision, you'll surely change your mind as you follow this sordid saga to its bitter end. You'll never look at eminent domain in the same way again.

Even though Royall was not named in the blurb, could he prevail on a defamation claim based on the blurb, by seeking to link it to specific statements about him in the book? If so, is the statement defamatory?

Such issues are even trickier with regard to charges of libel in fictional writings. Thus in Greene v. Paramount Pictures Corp., 138 F. Supp. 3d 226, 236 (E.D.N.Y. 2015), Greene alleged that he had been defamed in the portrayal of Nicky "Rugrat" Koskoff in the movie *The Wolf of Wall Street*. Seybert, J., noted that libel in fiction plaintiffs walk a fine line of "simultaneously assert[ing] that the character is 'of and concerning' him and her because of their similarities, but also must deny significant aspects of the fictional character, i.e. the defamatory aspects of the character." She held that, given the similarities between plaintiff and Koskoff and the public nature of the fraud, the plaintiff's claims survived a motion to dismiss.

On the constitutional status of the "of and concerning" requirement, see New York Times v. Sullivan, *infra* at 383.

## *Wilkow v. Forbes, Inc.*

241 F.3d 552 (7th Cir. 2001)

Easterbrook, J.

[This case pertains to a *Forbes* magazine column on the case of Bank of America National Trust & Savings Ass'n v. 203 North LaSalle Street Partnership, 526 U.S. 434 (1999), which involved the interaction of two bankruptcy rules. The first, the absolute-priority rule, requires that secured creditors be paid off in the order of their loan, such that a senior mortgagee has to be paid off in full before a junior mortgagee receives any payment. The second, the new-value rule, allows a subsequent contributor of equity to the business to vault over preexisting lenders to the extent that they contribute new value to the enterprise.] . . . [I]n *203 North LaSalle* we [the Seventh Circuit] held that the equity investors could retain ownership of a commercial office building, in exchange for about $6 million in new capital over a five-year period, even though the principal lender would fall about $38 million short of full repayment. This was the decision on which *Forbes* published a short column, seven months before the Supreme Court held the plan "doomed, . . . without necessarily exhausting its flaws, by its provision for vesting equity in the reorganized business in the Debtor's partners without extending an opportunity for anyone else either to compete for that equity or to propose a competing reorganization plan." 526 U.S. at 454.

The majority opinion in the Supreme Court required about 8,000 words to resolve the case — and without reaching a final decision on the vitality of the new-value exception

(though the majority's analysis hog-tied the doctrine). The majority opinion in this court ran about 9,500 words, with 5,200 more in a dissent. A 670-word article such as the one *Forbes* published could not present either the facts of the case or the subtleties of the law. What the article lacked in analysis, however, it made up for with colorful verbs and adjectives. Taking lenders' side, *Forbes* complained that "many judges, ever more sympathetic to debtors, are allowing unscrupulous business owners to rob creditors." According to the article, a partnership led by Marc Wilkow "stiffed" the bank, paying only $55 million on a $93 million loan while retaining ownership of the building. . . . Its core paragraph reads:

> By the mid-1990s, rents were not keeping up with costs. When the principal came due in January 1995, Wilkow and his partners pleaded poverty. To keep the bank from foreclosing, LaSalle Partnership filed for bankruptcy. Appraisals of the property came in at less than $60 million. In theory the bank was entitled to the entire amount. It suggested selling the property to the highest bidder. Determined to keep the building, LaSalle partners asked the bankruptcy court instead to accept a plan under which the bank would likely receive a fraction of what it was owed while the partners would keep the building. The bank, not the equity holder, would take the hit.

Wilkow replied with this libel suit under the diversity jurisdiction, contending that *Forbes* and Brigid McMenamin, the article's author, defamed him by asserting that he was in poverty (or, worse, "pleaded poverty" when he was solvent) and had filched the bank's money. According to Wilkow, *Forbes* should at least have informed its readers that the bank had lent the money without recourse against the partners, so that a downturn in the real estate market, rather than legal machinations, was the principal source of the bank's loss. . . .

[Easterbrook, J., addressed some procedural, choice of law, and constitutional issues, and continued:]

We don't think it necessary to consider either constitutional limits on liability for defamation or privileges under New York law, because this article is not defamatory under Illinois law in the first place. In Illinois, a "statement of fact is not shielded from an action for defamation by being prefaced with the words 'in my opinion,' but if it is plain that the speaker is expressing a subjective view, an interpretation, a theory, conjecture, or surmise, rather than claiming to be in possession of objectively verifiable facts, the statement is not actionable." Haynes v. Alfred A. Knopf, Inc., 8 F.3d 1222, 1227 (7th Cir. 1993).

Characterizations such as "stiffing" and "rob" convey McMenamin's objection to the new-value exception. She expostulates against judicial willingness to allow debtors to retain interests in exchange for new value, not particularly against debtors' seizing whatever opportunities the law allows. Nothing in the article implies that Wilkow did (or even proposed) anything illegal; *Forbes* informed the reader that the district court and this court *approved* Wilkow's proposed plan of reorganization. Every detail in the article (other than the quotation in the final paragraph) comes from public documents; the article does not suggest that McMenamin knows extra information implying that Wilkow pulled the wool over judges' eyes or engaged in other misconduct. Colloquialisms such as "pleaded poverty" do not imply that Wilkow was destitute and failing to pay his personal creditors, an allegation that would have been defamatory. Read in context, the phrase conveys the idea that the partnership could not repay the loan out of rents received from the building's tenants. After all, inability to pay one's debts as they come due is an ordinary reason for bankruptcy, and 203 North LaSalle Street Partnership *did* file a petition in bankruptcy. Filing a bankruptcy petition is one way of "pleading poverty."

Although the article drips with disapproval of Wilkow's (and the judges') conduct, an author's opinion about business ethics isn't defamatory under Illinois law, as *Haynes* and *Bryson* explain. Informing the reader about the nonrecourse nature of the loan might have made Wilkow look better, but it would not have drawn the article's sting: that the partners got to keep the property even though the bank lost $38 million. The original deal's fundamental

structure was that the partnership would repay the loan from rental income, and that if revenue was insufficient the bank could choose to foreclose (cutting its loss and reinvesting at the market rate elsewhere), to renegotiate a new interest rate with the partners, or to forebear in the hope that the market would improve and the full debt could yet be paid. These options collectively would be worth more than the market value of the building on the date of default. Yet the partners refused to honor these promises to the bank. They persuaded judges to eliminate the bank's rights to foreclose, to renegotiate, or to forebear and retain the full security interest. The plan of reorganization stripped down the security interest, prevented the bank from foreclosing, and required it to finance the partnership's operations for the next decade, at a rate of interest below what the bank would have charged in light of the newly revealed riskiness of the loan. If the real estate market fell further during that time, so that the partnership could not repay even the reduced debt, then the bank was going to lose still more money. The present value of the promises made to the bank in the plan of reorganization therefore was less than the appraised value of the building. But the partners stood to make a great deal of money if the market turned up again (as it did), for they had shucked $38 million in secured debt while retaining most appreciation in the property's value. Whether that was a sound use of bankruptcy reorganization, independent of the plan's new-value aspects, is open to question.

A reporter is entitled to state her view that an ethical entrepreneur should have offered the lender a better bargain, such as allowing the bank to foreclose and take its $55 million with certainty, avoiding the additional risk that this plan fastened on the lender. Foreclosure would have had serious consequences for the partners, who would have lost about $20 million in recaptured tax benefits. These potential losses created room for negotiation. Armed with the new-value exception, however, the partners were able to retain the tax benefits, sharing none with the bank in exchange for its approval of a restructuring, while depriving the bank of a security interest that would have been valuable when the market recovered. Although a reader might arch an eyebrow at Wilkow's strategy, an allegation of greed is not defamatory; sedulous pursuit of self-interest is the engine that propels a market economy. Capitalism certainly does not depend on sharp practices, but neither is an allegation of sharp dealing anything more than an uncharitable opinion. Illinois does not attach damages to name-calling. See Stevens v. Tillman, 855 F.2d 394, 400–02 (7th Cir. 1988) (collecting cases, including examples such as "sleazy" and "rip-off"). Wilkow's current and potential partners would have read this article as an endorsement of Wilkow's strategy; they want to invest with a general partner who drives the hardest possible bargain with lenders. By observing that Wilkow used every opening the courts allowed, *Forbes* may well have improved his standing with investors looking for real estate tax shelters (though surely it did not help his standing with lenders). No matter the net effect of the article, however, it was not defamatory under Illinois law, so the judgment of the district court is Affirmed.

## NOTES

**1.** ***Reputation in the Eyes of Which Beholder?*** The last paragraph of Easterbrook's opinion observes that potential investors could find the *Forbes* story favorable about the plaintiffs. How should the law of defamation apply if a story is read positively by some readers and negatively by others? Does the general community response matter if only specialized individuals are likely to do business with Wilkow in the future?

According to the Restatement (Second) of Torts, "reputation is the estimation in which one's character is held by his neighbors or associates." §557, cmt. *b*. In practice, this has meant that the question whether a communication harms the plaintiff's reputation is determined

using a reasonable person standard. See Chau v. Lewis, 771 F.3d 118 (2d Cir. 2014) (ruling that mere disparagement of the plaintiff is not actionable "if it fails to rise to the necessary level of derogation . . . measured not by the sensitivities of the maligned, but the critique of reasonable minds that would think the speech attributes odious or despicable characterizations to its subject").

**RESTATEMENT OF THE LAW (SECOND) OF TORTS**

**§559. Defamatory Communication Defined**

***Comment e. Standard by Which Defamation Is Determined:*** A communication to be defamatory need not tend to prejudice the other in the eyes of everyone in the community or of all of his associates, nor even in the eyes of a majority of them. It is enough that the communication would tend to prejudice him in the eyes of a substantial and respectable minority of them, and that it is made to one or more of them or in a manner that makes it proper to assume that it will reach them. . . . Although defamation is not a question of majority opinion, neither is it a question of the existence of some individual or individuals with views sufficiently peculiar to regard as derogatory what the vast majority of persons regard as innocent. . . .

***Illustration 3:*** *A*, a member of a gang of hoodlums, writes to *B*, a fellow bandit, that *C*, a member of the gang, has reformed and is no longer to be trusted with the loot of the gang. *A* has not defamed *C*.

American law traditionally allows the plaintiff to prevail if she can point to any subgroup of the population that would find the statement defamatory. In Peck v. Tribune Co., 214 U.S. 185, 189–90 (1909), an advertisement printed in the defendant's newspaper used the picture of the plaintiff, a nurse in real life, over the name of some other woman who had extolled the virtues of the malt whiskey promoted in the ad. Holmes, J., held, first, that the ad referred to the plaintiff, notwithstanding the incorrect name below the picture. He continued:

> It was pointed out that there was no general consensus of opinion that to drink whiskey is wrong or that to be a nurse is discreditable. It might have been added that very possibly giving a certificate and the use of one's portrait in aid of an advertisement would be regarded with irony, or a stronger feeling, only by a few. But it appears to us that such inquiries are beside the point. It may be that the action for libel is of little use, but while it is maintained it should be governed by the general principles of tort. If the advertisement obviously would hurt the plaintiff in the estimation of an important and respectable part of the community, liability is not a question of a majority vote.
>
> We know of no decision in which this matter is discussed upon principle. But obviously an unprivileged falsehood need not entail universal hatred to constitute a cause of action. No falsehood is thought about or even known by all the world. No conduct is hated by all. That it will be known by a large number and will lead an appreciable fraction of that number to regard the plaintiff with contempt is enough to do her practical harm.

Accordingly Holmes held that the question of defamation should have been left to the jury. Should an offset to damages be allowed if the statement *improves* the reputation of the plaintiff in the eyes of another respectable segment of the community?

**2.** ***The Role of the Jury.*** The majority of states bifurcate the question whether a statement is defamatory into two separate questions: whether the statement is *capable* of having a defamatory meaning and whether the statement *actually* is defamatory in context. The former question is for the judge; the latter for the jury. See, e.g., Johnson v. Purpera, 320 So. 3d 374,

388 (La. 2021) ("Whether a communication is capable of a particular meaning and whether that meaning is defamatory is a question for the court; whether a communication, which is capable of a defamatory meaning, was so understood by its recipient is a question for the trier of fact or the jury.").

**3. *Defining the Community.*** The background of both the plaintiff and her local community matter in determining whether a statement is defamatory. In Nguyen-Lam v. Cao, 171 Cal. App. 4th 858, 867 (Ct. App. 2009), the court emphasized that labeling the school superintendent a "Communist" in a heavily Vietnamese-American district was slander per se. Similarly in Parsi v. Daioleslam, 595 F. Supp. 2d 99, 109 (D.D.C. 2009), the court concluded that allegations that plaintiffs were agents of the Iranian government were capable of conveying a defamatory meaning if those statements lowered plaintiffs in the estimation of a substantial, respectable group of their fellow Iranian residents.

Not all courts are keen on the Second Restatement's "substantial and respectable minority" standard. In Virginia Citizens Defense League v. Couric, 910 F.3d 780, 784 n.1 (4th Cir. 2018), the Fourth Circuit (applying Virginia law) opted instead to define defamatory communications via a generic "reasonable person" standard. Why might the court have been skeptical of the substantial and respectable minority standard? That standard is *exclusive* of non-"respectable" thinkers. Has carving out wrong-thinking individuals become an untenable task for courts? See Michtavi v. N.Y. Daily News, 587 F.3d 551, 552 (2d Cir. 2009) ("It has become increasingly hard to ascertain as a matter of law what a right-thinking person would think. . . .").

**4. *The "Libel-Proof" Plaintiff?*** What result if the defendant defames a plaintiff who already has a horrible reputation in the relevant community for unrelated acts? Cooper v. Greeley, 1 Denio 347, 348, 352, 365 (N.Y. 1845), involved a celebrity literary dispute between the writer James Fenimore Cooper and Horace Greeley, the editor of *New York Tribune*. When threatened with the action Greeley famously replied: "Mr. Cooper will have to bring his action to trial somewhere. He will not like to bring it in New York, for we are known here, nor in Otsego for he is known there." The court construed the newspaper remark to mean that plaintiff had such a poor reputation in Otsego that he would not risk filing suit there. The defendants pleaded in justification that plaintiff had acquired in Otsego "the reputation of a proud, captious, censorious, arbitrary, dogmatical, malicious, illiberal, revengeful and litigious man, wherefore the said plaintiff was in bad repute in the said county of Otsego." The court allowed defendant's plea, noting: "Reputation is the estimate in which an individual is held by public fame in the place where he is known. And the existence of a good or bad reputation is, I think, a fact which may be directly put in issue." But why should this issue be pleaded as a justification, instead of as a denial of harm flowing from the false statement?

While the Restatement of the Law (Third) Torts: Defamation and Privacy (Preliminary Draft No. 4) neither explicitly adopts nor rejects the libel-proof plaintiff doctrine, some courts continue to apply it in limited cases. For example, in Dykstra v. St. Martin's Press LLC, No. 31813, slip op. at *2, *4, *13 (N.Y. Sup. Ct. May 29, 2020), former professional baseball player Lenny Dykstra sued an ex-teammate for claiming in his autobiography that Dykstra directed racial slurs at other players and accusing Dykstra of having a criminal record. When the defendants moved to dismiss the case partially on the theory that Dykstra was the "classic libel-proof plaintiff," the court acknowledged that "the case at hand is one of those rare circumstances" in which such a theory can succeed. The court dismissed the case because it was undisputed that Dykstra had previously acquired a reputation of being a "racist, misogynist, and anti-gay, as well as a sexual predator, drug-abuser, a thief, and an embezzler" and, thus, the passage in the defendant's book "has not exposed Dykstra to *any further* 'public contempt, ridicule, aversion or disgrace.'"

**5. *Group Libel.*** Yet another variation on this basic theme involves defamatory statements made about a group of which the plaintiff is a member. Whether or not a plaintiff succeeds in demonstrating defamation "of and concerning" herself depends on the size of the group and on whether the defamatory comment speaks of all members of the group or merely of some. In general, recovery applies only to all individuals in small groups. In Neiman-Marcus v. Lait, 13 F.R.D. 311 (S.D.N.Y. 1952), the defendants, in their book *U.S.A. Confidential*, charged that some models and saleswomen of the Neiman-Marcus store in Texas frequently served as "call girls" and that most of the male salesmen were gay. Suit was brought by nine models (constituting the entire staff of models at the time of publication), by fifteen salesmen (out of a group of twenty-five at the time of publication), and by thirty saleswomen (out of a group of 382 at the time of publication). The defendants probably did not contest the claims of the nine models but moved to dismiss those of the salesmen and saleswomen. The court denied the motion as to the salesmen, emphasizing that the group was small and that the characterization was of "most" of them. It granted the motion to dismiss as to the saleswomen because of the size of the group, saying that "no reasonable man would take the writer seriously and conclude from the publication a reference to any individual sales woman."

The theory of small group defamation was established in Elias v. Rolling Stone LLC, 872 F.3d 97, 101, 107 (2d Cir. 2017), where a *Rolling Stone* article implied that seven members of the Phi Kappa Psi fraternity of the University of Virginia had participated in or had turned a blind eye to an alleged gang rape. That story, written by Sabrina Rubin Erdely, turned out to be fabricated, after which *Rolling Stone* issued an apology and retracted the story. The alleged rapists were not individually named. The district court dismissed the complaint on the ground that as a matter of law the references were not specific enough to be "of and concerning" the plaintiffs. On appeal, Forrest, J., reversed the decision below:

> [W]e conclude that the complaint plausibly alleged that the statements in the Article were "of and concerning" them individually. We further conclude that the complaint plausibly alleged that all Plaintiffs were defamed as members of Phi Kappa Psi under a theory of small group defamation. . . .
>
> Because a reader of the Article could plausibly conclude that each member of Phi Kappa Psi was implicated either directly or indirectly in the alleged rapes, Plaintiffs can proceed under a theory of small group defamation.

Small group defamation was especially justified in this case given that there were only fifty-three members of the fraternity.

For much of this century there has been considerable concern over the calculated defamation of large groups such as Jews, Catholics, and African Americans. Yet in these cases defamation claims consistently fail. Thus in Khalid Abdullah Tarig Al Mansour Faissal Fahd Al Talal v. Fanning, 506 F. Supp. 186, 187 (N.D. Cal. 1980), the plaintiff brought a class action on behalf of some 600 million Muslims, alleging that the film *Death of a Princess* was defamatory to all Muslims because "it depicts the public execution of a Saudi Arabian princess for adultery." The court denied the claim, noting that "to permit an action to lie for the defamation of such a multitudinous group . . . would render meaningless the rights guaranteed by the First Amendment to explore issues of public import." For an argument that group libel rules should be automatically dismissed for groups over twenty-five, see Joseph H. King, Jr., Reference to the Plaintiff Requirement in Defamatory Statements Directed at Groups, 35 Wake Forest L. Rev. 343 (2000). May other sanctions be used against campus students who make slurs about members of other religious groups that do not single out anyone for specific identification?

**6. *Injurious Falsehood.*** Should a plaintiff be allowed to recover special damages for harm caused by false but *nondefamatory* statements? In Decker v. Princeton Packet, Inc., 561 A.2d 1122, 1127 (N.J. 1989), publication of the obituary of a living plaintiff was not

defamatory because it "did not impute to the plaintiff, any wrong and did not hold her up to ridicule." Had there been proof of special damages, however, should the plaintiff have been allowed to recover, if not for defamation, for a separate tort of injurious falsehood? As the large number of defamation suits in commercial settings shows, defamation can be most devastating when it induces third parties not to do business with a plaintiff. The plaintiff's injury is, of course, every bit as serious when the diversion of business is induced by injurious but nondefamatory falsehoods. For example, in Radcliffe v. Evans, 2 Q.B. 524 [Q.B. 1892], the defendant newspaper reported that the plaintiff had ceased to carry on his business as an engineer and boilermaker. The jury specially found that the words did not reflect on the plaintiff's character and were not libelous. Judgment for the plaintiff was affirmed, however, with Bowen, L.J., saying:

> That an action will lie for written or oral falsehoods, not actionable per se nor even defamatory, where they are maliciously published, where they are calculated in the ordinary course of things to produce, and where they do produce, actual damage, is established law. Such an action is not one of libel or of slander, but an action on the case for damage willfully and intentionally done without just occasion or excuse, analogous to an action for slander of title.

If defamation is actionable without proof of malice, why require proof of malice in injurious falsehood cases? Should damages for emotional distress be allowed in injurious falsehood cases? See William L. Prosser, Injurious Falsehood: The Basis of Liability, 59 Colum. L. Rev. 425 (1959).

## SECTION D. LIBEL AND SLANDER

### *Varian Medical Systems, Inc. v. Delfino*

113 Cal. App. 4th 273 (Ct. App. 2003)

Premo, Acting P.J. . . . Defendants Michelangelo Delfino and Mary Day used Internet bulletin boards to post numerous derogatory messages about their former employer, Varian Associates, Inc. (Varian) and two Varian executives. Varian and the two executives sued. Defendants treated the lawsuit as a challenge to their constitutional right to free speech and responded with a flood of spiteful messages posted on hundreds of Internet bulletin boards. By the time of trial defendants had posted over 13,000 messages and vowed to continue posting until they died.

Defendants' position at trial was that their postings contained only truth, opinion, or hyperbole. They stressed their belief that they were constitutionally entitled to publish the offending messages and that large corporate plaintiffs ought not be permitted to stifle free speech by filing suit against them. The jury was not persuaded. Defendants were found liable for defamation, invasion of privacy, breach of contract, and conspiracy. The trial court determined that in view of defendants' promise to post until they died an injunction was necessary to prevent future injury. The judgment gives plaintiffs $775,000 in damages and a broad injunction.

On appeal we are asked to consider whether the fact that defendants' messages appeared on Internet bulletin boards affects the character of the offending messages for purposes of defamation law. Specifically, defendants argue that typical Internet hyperbole cannot be considered defamatory. Defendants also argue that to the extent speech on the Internet may be defamatory it must be designated as slander, which requires proof of special damages, rather than libel, for which damages are presumed. . . .

### A. Is There Sufficient Evidence to Support a Finding That Plaintiffs Were Defamed?

[The court first determined that there was sufficient evidence to support the jury's finding that defendants had defamed the plaintiffs. The statements included accusations of lies, hallucinations, mental illness, incompetence, harassment, discrimination, and stalking. Some of the derogatory messages stated that one of the plaintiffs rose in the ranks to her position through sexual favors and included other terms with sexual implications. The court also decided that even though Internet message boards were typically "freewheeling and irreverent," they were not exempt from established legal and social norms.]

### B. Are Internet Postings Libel or Slander?

Defendants next argue that to the extent their Internet messages could be considered defamatory, they must be characterized as slander. Defendants point out that the distinction is crucial because slander requires proof of special damages and libel does not and since plaintiffs did not prove any special damages they cannot recover for defamation. . . . The issue presented here involves a question that has arisen only with the advent of Internet communications. Application of the common law to matters involving the Internet is of considerable public interest. Moreover, the distinction between libel and slander involves a practical difference in the requirements for pleading and proof so that the question is one that is likely to recur. . . .

A defamatory communication may be characterized either as libel or slander. (Civ. Code, §44.) The traditional distinction between libel and slander is that libel is written and slander is spoken. Defendants ignore this distinction and focus instead upon the practical difference, which involves the necessity to prove damages. Both distinctions are of ancient origin. Slander was considered a sin in Medieval England. When the action migrated to the civil courts the courts required proof of "temporal" or actual damages to avoid interfering with the church's authority over spiritual matters.

Libel arose with the advent of the printing press. Libel was at first a crime and was used to suppress political writings. It was later applied to non-political defamatory writings. Libel has been considered the greater wrong, either because of its criminal origins or because the permanence of its form endowed it with a greater propensity to breach the peace. In any event, by the early 19th Century libel was actionable per se, that is, damage was presumed.

Libel today is defined as a defamatory publication communicated "by *writing, printing, picture, effigy, or other fixed representation to the eye*. . . ." (Civ. Code, §45, italics added.) Slander is "*orally uttered, and also communications by radio or any mechanical or other means*. . . ." (Civ. Code, §46, italics added.) Television broadcasts are also treated as slander in this state. (See White v. Valenta, 234 Cal. App. 2d 243, 254 (1965).)

Defendants argue that Internet messages fall into the statutory classification of slander because they are communications by "any mechanical or other means" as specified in the slander statute. (§46.) Logic tells us that "mechanical or other means" cannot apply to all mechanical methods for producing a communication. After all, the cause of action for libel arose with the invention of mechanical means for reproducing the printed word. But the slander statute itself contains no clue to what the Legislature intended by the phrase. Accordingly, we may resort to the legislative history. Prior to 1945 Civil Code section 46 defined slander as a "false and unprivileged publication other than libel." (Stats. 1945, ch. 1489, §2.) At the time there was some dispute about whether radio broadcasts should be characterized as slander or libel since even though communications delivered by radio were spoken, in most cases the messages were read from a written script. Some jurisdictions reasoned that because radio broadcasts had such a great potential for injury they should be treated as the supposedly greater wrong of libel. The California Legislature either rejected or ignored that reasoning and

simply designated radio broadcasts as slander, amending the section to read as it does today. (Stats. 1945, ch. 1489, §2.) Thus, by categorizing radio broadcasts as slander, our Legislature adhered to the traditional distinction between libel and slander, i.e., that libel is written and slander is spoken.

[The court further reviewed the legislative history and rejected defendants' contention that "communications by radio or any mechanical or other means" was intended to include anything like a computer or other device used to produce written communications.]

Defendants also urge us to categorize communications over the Internet as the supposed lesser wrong of slander because, since Internet communication is the modern-day equivalent of a speech on the "village green," it deserves the greater protection traditionally accorded slander. The argument confuses the analyses. In defamation cases we are always mindful of the balance between the defendant's constitutional right to free speech and the plaintiff's interest in protecting his or her good name. However, that balance is struck by weighing factors such as the plaintiff's status (as a public or private figure) and the subject of speech itself against the defendant's constitutional interests. Whether the speech is classified as libel or slander is an arbitrary and, some would say, archaic distinction. At any rate, in California the distinction has little if anything to do with the constitutional analysis.

We find the plain language of the defamation statutes is dispositive. That is, defendants' messages were publications *by writing*. The messages were composed and transmitted in the form of written words just like newspapers, handbills, or notes tacked to a conventional bulletin board. They are representations "to the eye." True, when sent out over the Internet the messages may be deleted or modified and to that extent they are not "fixed." But in contrast with the spoken word, they are certainly "fixed." Furthermore, the messages are just as easily preserved (as by printing them) as they are deleted or modified. In short, the only difference between the publications defendants made in this case and traditionally libelous publications is defendants' choice to disseminate the writings electronically.

It has been noted that many forms of publication available to us today "cannot realistically be analyzed by reference to the traditional libel-slander dichotomy, which modern technology has rendered increasingly obsolete." (Polygram Records, Inc. v. Superior Court, 170 Cal. App. 3d 543, 552, fn. 9 (1985).) In this case, however, the publications are readily analyzed by reference to the existing statutes. We hold that written defamatory communications published by means of the Internet are properly characterized as libel.

[The court upheld the $775,000 damage award, but overturned the original injunction placed upon defendants' future Internet posts. The court held that the portion of the injunction prohibiting future speech was an impermissible prior restraint under both the state and federal constitutions.]

## NOTES

**1.** ***The Common Law Distinction.*** Historically the common law drew a distinction between libel and slander. Libel was the proper theory when the defendant's statement was embodied in some permanent form, such as a book or a picture, or even a wax sculpture. Even public shadowing to prevent an individual from testifying against the defendant was treated as libelous because "[a]ctual pursuit and public surveillance of person and home are suggestive of criminality fatal to public esteem and productive of public contempt and ridicule." Schultz v. Frankfort Marine Accident & Plate Glass Ins. Co., 139 N.W. 386, 390 (Wis. 1913).

Slander, for its part, consists primarily of false spoken words. In addition, "the use of a mere transitory gesture commonly understood as a substitute for spoken words, such as a

nod of the head, a wave of the hand, or a sign of the fingers, is slander rather than libel." RST §568, cmt. *d*. More generally, Restatement (Second) of Torts §568(3) provides: "The area of dissemination, the deliberate and premeditated character of its publication and the persistence of defamation are factors to be considered in determining whether a publication is a libel rather than a slander."

The Restatement (Second) of Torts §568A states the modern position that "[b]roadcasting of defamatory matter by means of radio or television is libel, whether or not it is read from a manuscript." The English Defamation Act, 15 & 16 Geo. VI and Eliz. II. ch. 66, §§1, 16 (1952), adopts the same rule. Should social media websites, such as Facebook and X (formerly Twitter), be treated as libel or slander? Does it make a difference if the user is able to limit or not limit the visibility of his or her posts? How should courts handle these communications?

For the classic criticism of the distinction between libel and slander, see Van Vechten Veeder, The History and Theory of the Law of Defamation, 3 Colum. L. Rev. 546, 571–73 (1903).

**2. *Slander Per Se.*** Under traditional law, libels were ordinarily actionable per se without proof of special damages, while slander was generally actionable only upon proof of special damages (e.g., a lost business arrangement), except in four exceptional categories of cases:

a. *Loathsome diseases*. The presumption of damage has been confined to diseases that are not merely contagious but also "loathsome," such as plague, leprosy, and venereal disease, and therefore result in social ostracism. The development of medical science has tended to freeze this category to the above limited examples. In Chuy v. Philadelphia Eagles Football Club, 595 F.2d 1265, 1281–82 (3d Cir. 1979), the court held that cancer was not a loathsome disease, reasoning that "[t]he public's reaction today to a victim of cancer is usually one of sympathy rather than scorn, support and not rejection." By contrast, in Nolan v. State, 158 A.D.3d 186, 196, 69 N.Y.S.3d 277, 285 (App. Div. 2018), the court ruled that statements that impute HIV-positive status to a person were defamatory per se under the traditional "loathsome disease" category, because "a significant segment of society has been too slow in understanding that those who have the disease are entitled to equal treatment under the law and the full embrace of society." Does it make sense that cancer is no longer considered a loathsome disease when HIV/AIDS is? How relevant is the risk of infection via bodily contact or contagion through the air?

b. *Criminal conduct*. Also slanderous per se at common law was the imputation of criminal activities, the law apparently concerned that such a statement might expose plaintiff to criminal prosecution. However, all charges of criminal misconduct are not slanderous per se. Most jurisdictions now insist that the crime involve "moral turpitude." See, e.g., Wooten v. Martin, 131 S.W. 783 (Ky. 1910). Other jurisdictions follow the English rule and require that the words charge an offense punishable by death or imprisonment.

   If plaintiff is accused of conduct that is criminal under the law in the state where the allegations are made, but not criminal where the conduct was performed, are the statements slanderous per se? Klumph v. Dunn, 66 Pa. 141 (1870), opted for the "law of the country where the words are spoken," because it is by those laws that the reputation of the plaintiff is judged.

c. *Imputation of unchastity*. The older common law did not treat as slanderous per se words that imputed unchastity to a woman. That result was reversed by statute in England in 1891 and in several states in the United States. States without such statutes sometimes granted recovery on the ground that the charge of fornication

was criminal under local laws. Other states allowed the action regardless of whether there were imputations of criminal conduct. The first Restatement of Torts treated allegations of unchastity as slanderous per se. RT §574. See also 740 Ill. Comp. Stat. 145/1 (2024), which makes it actionable slander to publish or utter words that charge any person of being guilty of "fornication or adultery." The Second Restatement §574 now makes slanderous per se allegations of "serious sexual misconduct," which, as comment *c* now makes clear, applies to both men and women. Does that include premarital sexual relations?

How should false allegations of being gay be treated? In Albright v. Morton, 321 F. Supp. 2d 130 (D. Mass. 2004), the court held that a statement identifying someone as a homosexual is not defamatory per se under Massachusetts law because such a statement no longer imputes criminal conduct. The court also said that if it were to agree that calling someone a homosexual is defamatory per se, it would, in effect, validate anti-homosexual sentiment and legitimize relegating homosexuals to second-class status. But attitudes shifted sharply in Laguerre v. Maurice, 138 N.Y.S.3d 123, 126, 130 (2020), when the pastor at the Gethsemane Seventh Day Adventist Church in Brooklyn stated the plaintiff, a former church elder, "was a homosexual" in front of 300 church members in order to have the plaintiff removed from the church. In overruling earlier cases, Roman, J., asserted that "earlier cases . . . which held that the false imputation of homosexuality constitutes a category of defamation per se, are inconsistent with current public policy." Does that insulate specific efforts to drive, maliciously, the plaintiff out of the church?

What about false allegations of transgender status? In Simmons v. American Media, Inc., No. BC660633, 2017 WL 5325381, at *1 (Cal. Sup. Sept. 1, 2017), the court, citing *Albright*, rejected plaintiff's defamation claim based on a statement that he had withdrawn from public life "due to him transitioning from male to female." The court reasoned that "even if there is a sizeable portion of the population who would view being transgender as negative, the court should not . . . 'directly or indirectly, give effect to these prejudices.'" *Id*. at *5; see generally Clay Calvert et al., Defamation Per Se and Transgender Status: When Macro-Level Value Judgments About Equality Trump Micro-Level Reputational Injury, 85 Tenn. L. Rev. 1029, 1030 (2018).

d. *Slander of a person's trade or profession*. This critical category includes such charges that a surgeon is a butcher, or a cashier has his hands in the till. More problematic are statements reflecting adversely on the plaintiff's character by charging dishonesty, sloth, immorality, or drunkenness. Also slanderous per se are unprivileged charges of dishonesty or corruption against public officials.

In Ravnikar v. Bogojavlensky, 782 N.E.2d 508, 512 (Mass. 2003), both plaintiff and defendant were physicians working at a common facility. The defendant commented to a prospective new patient of the plaintiff that the plaintiff was dying of cancer when in fact she had been cured. Because the individual patient retained the plaintiff's service anyway, no special damages could be proved. Nonetheless, the court allowed her claim for general damages to proceed, because "a statement that a physician is terminally ill can discourage potential patients by creating the natural inference that death is not far off and that the physician will be distracted by her medical condition and its treatment." Why is this not a case of injurious falsehood?

In contrast, in Gahafer v. Ford Motor Co., 328 F.3d 859, 862–63 (6th Cir. 2003), an obscenity-laced tirade accusing the plaintiff, a middle-manager employee, of fraud and castigating him for diverting time from his responsibilities

as a "dimensional control engineer" was not treated as slander per se because these statements only hinted at frustration with Gahafer's time commitment to his job responsibilities.

**3.** ***Libel Per Quod and Libel Per Se.*** The elaborate common law distinction between libel per quod and libel per se, referred to in *Muzikowski, supra* at 330, depends on whether the reference to the plaintiff can be derived from the statement itself, in which case it can be libel per se (in itself) or whether it requires some reference to extrinsic evidence, in which case it is libel per quod (through which). When the defendant mentions the plaintiff by name, the statement may be libel per se. But when the defendant says, "The person who stole my money lives in the house next door," extrinsic evidence is needed to establish that the statement refers to the plaintiff.

Even if the identity of the plaintiff is undisputed, extraneous facts may still be needed to establish the defamatory meaning. In Braun v. Armour & Co., 173 N.E. 845 (N.Y. 1930), the defendant had issued an advertisement setting forth a list of dealers in its meat products, including plaintiff, stating: "These progressive dealers listed here sell Armour's Star Bacon in the new window-top carton." In the complaint, the plaintiff added that he was a dealer in kosher meat and that bacon was a non-Kosher product. Again the court held that the complaint stated a cause of action.

## SECTION E. BASIS OF LIABILITY: INTENTION, NEGLIGENCE, AND STRICT LIABILITY IN DEFAMATION

### *E. Hulton & Co. v. Jones*

[1910] A.C. 20

[The defendant newspaper ran an article written by its Paris correspondent that in part read as follows: "'Whist! There is Artemus Jones with a woman who is not his wife, who must be, you know—the other thing!' whispers a fair neighbor of mine excitedly to her bosom friend's ear. Really, is it not surprising how certain of our fellow-countrymen behave when they come abroad? Who would suppose by his goings on, that he is a church warden at Peckham?" Plaintiff was a lawyer named Thomas Artemus Jones of North Wales; he was not a church warden, nor did he reside at Peckham, but he had, up to 1901, contributed signed articles to defendant's newspaper. Defendant's contention that it had never heard of plaintiff and had used the name Artemus Jones as a fictitious name was accepted as true by plaintiff at the trial. Plaintiff produced witnesses who said they had read the article and thought that it referred to plaintiff. The trial judge charged the jury that the issue was not what the writer had intended but how the statement would be understood. At the trial plaintiff recovered a jury verdict of £1,750. The Court of Appeal affirmed by a two-to-one vote and, on appeal, the House of Lords affirmed.

The issue was perhaps most succinctly put during argument in the House of Lords when defendant's counsel said: "The question is who was meant," and Lord Loreburn asked: "Is it not rather who was hit?" Counsel replied: "No. A man cannot be held responsible for remote and improbable results of his actions."]

Loreburn, L.C. My Lords, I think this appeal must be dismissed. A question in regard to the law of libel has been raised which does not seem to me to be entitled to the support of your Lordships. Libel is a tortious act. What does the tort consist in? It consists in using language which others knowing the circumstances would reasonably think to be defamatory

of the person complaining of and injured by it. A person charged with libel cannot defend himself by shewing that he intended in his own breast not to defame, or that he intended not to defame the plaintiff, if in fact he did both. He has none the less imputed something disgraceful and has none the less injured the plaintiff. A man in good faith may publish a libel believing it to be true, and it may be found by the jury that he acted in good faith believing it to be true, and reasonably believing it to be true, but that in fact the statement was false. Under those circumstances he has no defence to the action, however excellent his intention. If the intention of the writer be immaterial in considering whether the matter written is defamatory, I do not see why it need be relevant in considering whether it is defamatory of the plaintiff. The writing, according to the old form, must be malicious, and it must be of and concerning the plaintiff. Just as the defendant could not excuse himself from malice by proving that he wrote it in the most benevolent spirit, so he cannot shew that the libel was not of and concerning the plaintiff by proving that he never heard of the plaintiff. His intention in both respects equally is inferred from what he did. His remedy is to abstain from defamatory words. . . .

The damages are certainly heavy, but I think your Lordships ought to remember two things. The first is that the jury were entitled to think, in the absence of proof satisfactory to them (and they were the judges of it), that some ingredient of recklessness, or more than recklessness, entered into the writing and the publication of this article, especially as Mr. Jones, the plaintiff, had been employed on this very newspaper, and his name was well known in the paper and also well known in the district in which the paper circulated. In the second place the jury was entitled to say this kind of article is to be condemned. There is no tribunal more fitted to decide in regard to publications, especially publications in the newspaper Press, whether they bear a stamp and character which ought to enlist sympathy and to secure protection. If they think that the licence is not fairly used and that the tone and style of the libel is reprehensible and ought to be checked, it is for the jury to say so; and for my part, although I think the damages are certainly high, I am not prepared to advise your Lordships to interfere, especially as the Court of Appeal have not thought it right to interfere, with the verdict.

## NOTES

**1.** ***Strict Liability and Malicious Intent.*** Would Lord Loreborn have reduced the plaintiff's damages if he had been convinced that the reference to plaintiff was strictly accidental? If the plaintiff's name had been Tom Jones? *Hulton* is followed today in the United States in defamation cases governed by common law rules. See, e.g., Tate v. Bradley, 837 F.2d 206, 208 (5th Cir. 1988) ("Actual malice, in the sense of spite or ill will, is presumed and need not be proved if the words are defamatory on their face.").

**2.** ***Basis of Liability for Publication.*** Even after *Hulton*, it seems widely agreed that the defendant will be liable only if the publication was intentional or at least negligent. Thus the Restatement (Second) of Torts §577, comment *n*, excuses the defendant for "accidental" publications. That rule applies when *A* writes defamatory statements about *B*, which are then stolen from a locked desk by a thief who reads or publishes them. Similarly, if *A* sends a defamatory letter about *B* to *B* through the mail, the publication is regarded as accidental if a robber reads or publishes the stolen letter. Finally, if *A* sends a defamatory letter to *B* marked "personal" that is opened and read by *B*'s secretary, there is no publication, unless *A* knew of the secretary's practice. Note that if defendant is strictly liable for publication, he could escape responsibility so long as the publication was made by some independent third person.

## SECTION F. DAMAGES

### 1. Special Damages

"By 'actual damage' is meant what in the books is usually called 'special damage.' This latter expression is either meaningless or misleading." Bower, Actionable Defamation, Article 13, at 33 (1908).

## *Terwilliger v. Wands*

17 N.Y. 54 (1858)

[Action for slander. Plaintiff proved that defendant told La Fayette Wands that plaintiff was having continued sexual intercourse with one Mrs. Fuller and that he—plaintiff—would do all he could to keep Mr. Fuller in the penitentiary so that he could continue to enjoy Mrs. Fuller's favors. Plaintiff proved that defendant had said much the same thing to one Neiper, a good friend of plaintiff's, who had told plaintiff about this statement. Also he proved that Neiper had told him that this information about plaintiff was spreading all over the county. As a result of learning this information, plaintiff became very ill, both mentally and physically, had to have medical treatment, and could not do any work; subsequently his crops and business were neglected, and he had to hire more help. The judgment for the defendant below was affirmed.]

Strong, J. The words spoken by the defendant not being actionable of themselves, it was necessary in order to maintain the action to prove that they occasioned special damages to the plaintiff. The special damages must have been the natural, immediate and legal consequence of the words. . . . [The court first concluded that defendant was not responsible for a repetition of the words to plaintiff, and continued:]

But there is another ground upon which the judgment must be affirmed. The special damages relied upon are not of such a nature as will support the action. The action for slander is given by the law as a remedy for "injuries affecting a man's reputation or good name by malicious, scandalous and slanderous words, tending to his damage and derogation." (3 Bl. Com., 123.) It is injuries affecting the reputation only which are the subject of the action. In the case of slanderous words actionable per se, the law, from their natural and immediate tendency to produce injury, adjudges them to be injurious, though no special loss or damage can be proved. "But with regard to words that do not apparently and upon the face of them import such defamation as will of course be injurious, it is necessary that the plaintiff should aver some particular damage to have happened." (3 Bl. Com., 124.) As to what constitutes special damages, Starkie mentions the loss of a marriage, loss of hospitable gratuitous entertainment, preventing a servant or bailiff from getting a place, the loss of customers by a tradesman; and says that in general whenever a person is prevented by the slander from receiving that which would otherwise be conferred upon him, though gratuitously, it is sufficient. (1 Stark. on Sland., 195, 202.) . . . These instances are sufficient to illustrate the kind of special damage that must result from defamatory words not otherwise actionable to make them so; they are damages produced by, or through, impairing the reputation.

It would be highly impolitic to hold all language, wounding the feelings and affecting unfavorably the health and ability to labor, of another, a ground of action; for that would be to make the right of action depend often upon whether the sensibilities of a person spoken of are easily excited or otherwise; his strength of mind to disregard abusive, insulting remarks concerning him; and his physical strength and ability to bear them. Words which would make hardly an impression on most persons, and would be thought by them, and should be by all,

undeserving of notice, might be exceedingly painful to some, occasioning sickness and an interruption of ability to attend to their ordinary avocations. . . . In this view of the law words which do not degrade the character do not injure it, and cannot occasion loss. . . . The slander may not have been credited by or had the slightest influence upon any one unfavorable to the plaintiff; and it does not appear that anybody believed it or treated the plaintiff any different from what they would otherwise have done on account of it. The cause was not adapted to produce the result which is claimed to be special damages. Such an effect may and sometimes does follow from such a cause but not ordinarily; and the rule of law was framed in reference to common and usual effects and not those which are accidental and occasional. . . .

## NOTE

***Special Damages Today.*** Is there any reason to exclude recovery for mental anguish of the sort that would be suffered by a reasonable person in plaintiff's position? The modern case law still shows a certain resistance toward emotional distress as special damages. Zeran v. Diamond Broadcasting, Inc., 203 F.3d 714 (10th Cir. 2000), grew out of the same unfortunate incident as Zeran v. America Online, *supra* at 316. Only this time, the plaintiff sued the radio station that had broadcast the show urging listeners to tell "Ken" Zeran what they thought of his tactics. Kimball, J., first held that the defamatory statements did not fall into any of the categories of slander per se, and thus required proof of special damages for two reasons:

> Emotional distress is not a form of special damages, and Plaintiff's *de minimis* medical expenses, consisting of one visit to his physician and one prescription drug purchase, are insufficient to support the cause of action. Under . . . the *de minimis* doctrine, the law does not care for, or take notice of, very small or trifling matters. . . .
>
> Plaintiff's defamation claim [also] fails because Plaintiff has not shown that any person thinks less of him, Kenneth Zeran, as a result of the broadcast. As the district court found, there was no evidence that anyone who called his number in response to the posting or the broadcast even knew his last name. In other words, under the facts of this case, there was an insufficient link between Plaintiff's business telephone number and Plaintiff himself for Plaintiff to have sustained damage to his reputation.

If Zeran had sustained more medical expenses, would these have been recoverable even if his reputation in the community had not suffered? In Wood v. Wood, 693 A.2d 673, 674 (Vt. 1997), the court stated that "evidence of sleeping problems, loss of appetite, development of a temporary drinking problem, and deteriorating family relationships demonstrated actual harm. We have also recognized that proof of 'embarrassment and temporary injury to reputation' would be sufficient to support an award of general damages."

## *Ellsworth v. Martindale-Hubbell Law Directory, Inc.*

280 N.W. 879 (N.D. 1938)

[In this action for libel, plaintiff alleged that defendant misstated his professional and financial rating in the code form that it used in its directory. The directory itself was widely relied on by lawyers in many states and countries who needed to forward legal business. Plaintiff claimed that his rating in defendant's private key symbols was defamatory and that as a result his reputation was injured. In his pleadings, he elaborately set forth the translation of this private key system, with which all members of his profession were presumably familiar. From 1907 through 1926, plaintiff received the rating "a v 5 g," of which "a" meant legal ability

very high, "v," recommendations very high, "5," financial worth $10,000 to $20,000, and "g," promptness in paying bills very good. The defamation itself consisted of the ratings in the 1928 edition: "b w 5 f," of which "b" meant legal ability second class, "w," recommendations second class, "5," financial worth $10,000 to $20,000, and "f," promptness in paying bills fair. The defendant's 1929 edition left the rating of plaintiff blank, which plaintiff alleged meant that his rating was so low that it did not merit mention in the directory. It appeared that defendant had written a strong letter of protest after the 1928 edition.

Previously, in Ellsworth v. Martindale-Hubbell Law Directory, Inc., 268 N.W. 400 (N.D. 1936), the court held that the alleged defamation was not actionable per se and therefore required that the plaintiff allege and prove special damages to maintain his action. The plaintiff's amended complaint offered allegations as to his professional income in 1928, the year prior to the alleged misstatements, and for the succeeding three years. During these years his earnings were substantially lower, allegedly because of defendant's publication, with damages over $2,500. Defendant appealed from an order overruling its demurrer to the amended complaint.]

Nuessle, J. . . . The sole question on this appeal is as to whether this amended paragraph sufficiently sets forth the special damages claimed to have been suffered. The defendant contends that it does not. That it fails to set out the names of the clients lost by the plaintiff because of the publication of the alleged defamatory matter, and that it does not specify particularly the origin, character, and amount of the business the plaintiff has been deprived of because of its publication.

In substance, the amended complaint alleges that the plaintiff has been engaged in the practice of law for many years; that he has always borne a good reputation as a man and as a lawyer; that he has had a substantial law business that came to him largely from forwarders through a widely spread foreign territory; that he was personally unacquainted with such forwarders; that the defendant's publication in which the alleged defamatory matter was published, was circulated generally throughout such territory and among those who forwarded business to the plaintiff; that, as a consequence of the circulation of such matter and immediately following such publication and circulation, his practice decreased in the manner and to the extent as set out in that portion of the complaint quoted. . . .

. . . From the nature of the circumstances as disclosed by the pleading the plaintiff cannot describe the particular items of business which he has lost or give the names of particular individuals who would have become his clients had it not been for the publication. But he does show a diminution of his business and of the income therefrom by pleading what that business amounted to prior to the publication and what it was after the publication, and as a result thereof. As to whether he can make proof in support of the allegations contained in his pleading is another matter with which we are not now concerned. . . .

[In] Odgers, Libel & Slander, 5th ed. at page 382, it is stated:

> But it is not always necessary for the plaintiff to call as his witnesses those who have ceased to deal with him. He may be able to show by his account-books or otherwise, a general diminution of business as distinct from the loss of particular known customers or promised orders. He has still to connect that diminution of business with the defendant's words. Such a connection may sometimes be established by the nature of the words themselves. Where the defendant has published a statement about the plaintiff's business, which is intended or reasonably calculated to produce, and in the ordinary course of things does produce, a general loss of business, evidence of such loss of business is admissible, and sufficient special damage to support the action, although the words are not actionable per se, and although no specific evidence is given at the trial of the loss of any particular customer or order by reason of such publication.

[Affirmed.]

**RESTATEMENT OF THE LAW (SECOND) OF TORTS**

**§575. Slander Creating Liability Because of Special Harm**

One who publishes a slander that, although not actionable per se, is the legal cause of special harm to the person defamed, is subject to liability to him.

***Comment b. Special Harm***: . . . Thus, while a slander that has been so widely disseminated as to cause persons previously friendly to the plaintiff to refuse social intercourse with him is not of itself special harm, the loss of the material advantages of their hospitality is sufficient. Special harm may be a loss of presently existing advantage, as a discharge from employment. It may also be a failure to realize a reasonable expectation of gain, as the denial of employment which, but for the currency of the slander, the plaintiff would have received. It is not necessary that he be legally entitled to receive the benefits that are denied to him because of the slander. It is enough that the slander has disappointed his reasonable expectation of receiving a gratuity.

## NOTE

***Proof of Special Damages.*** Plaintiff's attempt to establish special damages can raise sharp questions of fact if defendant claims that plaintiff's loss was caused not by defendant's defamatory statement but by some independent event. In Touma v. St. Mary's Bank, 712 A.2d 619, 622 (N.H. 1998), the defendant's foreclosure notice made it appear that plaintiff's restaurant would be closed down because of the bank's takeover of the plaintiff's landlord who had defaulted on his loan to the bank. Horton, J., conceded that the notice was defamatory, but held, in affirming the denial of special damages below, that the plaintiff had not established that any lost profits were attributable to the defective foreclosure notice:

> Although the plaintiff contends that the foreclosure notice is the only explanation for the restaurant's decline in March 1993, the record establishes that gross revenues actually began to decline several months earlier. Moreover, the trial court could reasonably have concluded that the plaintiff's rebuttal advertisements and continued operation of the restaurant should have halted any decline caused by the foreclosure notice; in fact, sales continued to decline thereafter.

In Pippen v. NBC Universal Media LLC, 734 F.3d 610, 614 (7th Cir. 2013), various media outlets reported that the former Chicago Bulls great Scottie Pippen had filed for bankruptcy when he had not, even though he had suffered from several well-publicized financial reversals. Easterbrook, J., wrote:

> Pippen's complaint alleges that his endorsement and personal-appearance opportunities dwindled as a result of the defendants' false reports. In a proposed amended complaint, Pippen itemized losses that in his view flowed from defendants' statements; he identified specific business opportunities that had been available to him earlier but that, following the defendants' statements, were available no more. This is more than a general allegation of economic loss; it is an allegation that third parties have ceased to do business with him because of the defendants' actions. This contention may be substantively inadequate. It appears to be an example of the *post hoc ergo propter hoc* fallacy: since Pippen's opportunities diminished after the statements were made, he believes they must have diminished *because* the statements were made. This theory of causation is weak for professional athletes, whose earnings related to past stardom drop as time passes since their playing days. But, as a matter of pleading, Pippen did enough.

Pippen's pleading victory was short-lived, as his complaint was dismissed on the ground that as a public figure he could not recover for damages unless he showed that the defendants

had acted with actual malice, which was not established by showing either their failure to check public records of bankruptcy filings or to ask Pippen directly about his financial position.

## 2. General Damages

**McCormick**

### *Damages*

§116, p. 422 (1935)

When "special" damage need not be shown, "general" damage may be recovered. That such damage has been suffered need not be proved by the plaintiff, for it is presumed; however, it is customary to make proof of some of the items. The elements of "general" damage are: (1) injury to reputation; (2) loss of business; (3) wounded feelings and bodily suffering resulting therefrom.

### *Faulk v. Aware, Inc.*

231 N.Y.S.2d 270 (Sup. Ct. 1962)

[Aware, Inc., is a "membership corporation whose purpose is to combat communism in the entertainment and communication industries." John Henry Faulk, a popular radio and TV performer, brought a libel action against Aware, Inc., and Vincent Hartnett, its founder and president, for statements made by them and widely distributed charging him with communist sympathies and affiliations.]

Geller, J. In this libel action the jury rendered a verdict awarding compensatory damages of $1,000,000 against the three defendants and punitive damages of $1,250,000 each against defendants Aware, Inc., and Vincent Hartnett. . . .

The fact that the amounts awarded are very large does not necessarily render the verdict excessive as a matter of law. The question is whether there is a rational basis for the jury's awards in the evidence adduced and in the circumstances of this case. The court should not substitute its judgment for that of the jury, unless the amounts awarded are insupportable under any fair-minded view of the facts. . . .

However, since an award of damages always rests in the "sound discretion" of a jury, it is subject to court review. That discretion must be exercised in accordance with the applicable rules of law and on the basis of the evidence in the case.

The damages recoverable for a libel consist of two items [compensatory and punitive].

We will consider each of these two types of awards separately, just as the jury was instructed to do in its deliberations and form of verdict.

#### I. Compensatory Damages

. . .

The principal item of damages was plaintiff's claim that he had been rendered unemployable in the television and radio industry as the direct result of the alleged libel and the concerted acts of the defendants, depriving him of the opportunity to realize his earning capacities in his profession. . . .

There was substantial testimony, which was uncontradicted, that prior to the alleged libel in February, 1956, plaintiff, in addition to his regular radio show, had appeared on a

large number of television programs and had shown particular talent for that medium, being especially suited for the game, fun and quiz shows which were extremely popular during the period here involved. There also was uncontradicted testimony of an upward trend during this period in the television industry and in the income earned by television performers.

Plaintiff offered proof of his earning capacity through experts in the industry familiar with his achievements and abilities, among whom were Mark Goodson, David Susskind and Garry Moore, well-known producers of television shows.

It is well settled that a person wrongfully injured is entitled to recover for deprivation of future earning capacity, without limitation to his actual earnings preceding the injury; and that opinion testimony with regard to his potential earnings in that field by experts familiar with his capacities, is admissible.

. . . [The plaintiff's expert witnesses] testified that he would have earned between $150,000 and $500,000 annually, giving the reasons for their opinion. Defendants offered no proof in contradiction of plaintiff's experts.

The minimal figure of plaintiff's experts would represent damages of $900,000 for the six years involved. Assuming that the jury accepted that figure, they could take into consideration the other elements of injury to plaintiff's reputation and his mental anguish and distress in public and private life arising from the nature of the charge made against him, and find basis for arriving at compensatory damages in the sum of $1,000,000. . . .

### II. Punitive Damages . . .

[The court upheld the award of punitive damages against the claim that they were excessive.]

## *Faulk v. Aware, Inc.*

244 N.Y.S.2d 259 (App. Div. 1963)

Rabin, J. . . . We are greatly concerned, however, with the size of the verdict — both as to compensatory and punitive damages. . . . We find the verdict to be grossly excessive and most unrealistic — even in the field of entertainment.

The plaintiff's prior earnings are an important factor in assessing the damage suffered when his earnings are cut off. His damage need not be limited to the level of his actual earnings at the time of the libel. His potential earnings may be taken into consideration when there is evidence to enable a jury to assess those potentialities. . . . In this case, the plaintiff's potential earnings were fixed by his witnesses in amounts ranging from $100,000.00 to $1,000,000.00 a year. The larger figure was arrived at by reference to the earnings of those who had reached the very top of the profession. We are mindful of the statement of our colleague, Mr. Justice Breitel, in the *Grayson* case where he said: "[I]n the case of persons of rare and special talents many are called but few are chosen." While the plaintiff's experts testified that the plaintiff would, without doubt, be among the "chosen," it seems that none of these experts, although in the entertainment field, was perceptive enough to contract for his services even though his earnings were never more than about $35,000.00 a year.

Those who testified to potential earnings of between $100,000.00 and $250,000.00 arrived at that estimate based upon what comparable performers were receiving. Yet they gave no explanation as to why the plaintiff's earnings were so comparatively low. In short, the testimony of the experts left plenty of room for speculation.

Upon that testimony, the jury was justified in its obvious conclusion that the plaintiff's prospects for advancement in his profession were extremely good and that his income would

rise correspondingly. Despite that however, there is hardly enough justification for the finding of compensatory damages in the amount of $1,000,000.00, even making allowance for his mental pain and suffering. It is interesting to note that at current savings bank interest rates, his yearly income for life would exceed the best of his past earnings. We believe that the compensatory damages should be fixed at a figure no higher than $400,000.00.

[The court reduced the punitive damage award against Aware to $50,000 and against Hartnett to $100,000.]

## NOTES

**1. *Justification for General Damages.*** Courts use general damages in defamation cases to avoid the administrative and evidentiary problems that arise in seeking to prove special damages. The key premise is that a rough estimate is a better first approximation of the true state of affairs than the alternative approach, which denies recovery altogether. In Tex Smith, The Harmonica Man, Inc. v. Godfrey, 102 N.Y.S.2d 251, 253 (Sup. Ct. 1951), the defendant, a famous media figure, had made disparaging remarks about the plaintiff's ukuleles on both television and radio. The court noted that Godfrey's words could be taken as reflecting ill upon the plaintiff or its products. If the former, damages could be recovered for slander per se. The court continued:

> If the words are regarded purely as a reflection on the instruments, the same result would be reached. Here the words only become actionable if it is shown that damage followed upon their utterance. There was a time when such damage had to be specifically shown — the loss of a contract, a position, or the like. It is practically impossible for one selling to the general public at retail or by mail order to show loss of particular sales. Under such circumstances those people were without remedy from the most groundless calumny. It is, however, now recognized that allegations and proof of a general loss of sales is sufficient, leaving it to the trier of the facts to determine whether the loss is properly to be attributed to the slander or not. The allegations of the complaint on this subject are sufficient by this standard.

**2. *Proof of General Damages.*** In defamation cases proof of general damages does not in principle preclude proof of special damages in addition. For example, in Bishop v. New York Times, 135 N.E. 845, 848 (N.Y. 1922), the court stated:

> We are inclined to the view that a plaintiff is not compelled to rely upon a favorable presumption with which the law endows his cause of action, but that he may prove, if he can, that he has been avoided and shunned by former friends and acquaintances as the direct and well-connected result of the libel.

In Macy v. New York World-Telegram Corp., 141 N.E.2d 566, 570 (N.Y. 1957), the defendant newspaper falsely charged the plaintiff, a prominent civic figure and a congressman running for reelection, with threatening to make public a certain letter if plaintiff were not chosen as his party's senatorial nominee. On appeal the court vacated the plaintiff's jury award of $50,000 for general damages and granted the newspaper a new trial because the plaintiff's own testimony was that he had been subject to personal attacks, expelled from his country club, and denied his seat in the House of Representatives. The court said that in some cases the plaintiff could rely on his own hearsay testimony to show the loss that followed from the libel, but it concluded that the "better practice would be to call as witnesses for plaintiff, subject to cross-examination, the persons who were supposed to have spoken or acted adversely to plaintiff and to demonstrate, if such demonstration be possible, a connection to the libel."

**3.** ***Constitutional Response.*** The traditional common law views on general and punitive damages have been analyzed in a constitutional context in Gertz v. Robert Welch, Inc., 418 U.S. 323 (1974), *infra* at 397, and Dun & Bradstreet, Inc. v. Greenmoss Builders, Inc., 472 U.S. 749 (1985), *infra* at 402.

## 3. Other Remedies

### *a. Injunctions*

Courts have long refused to enjoin either slander or libel. Historically that equitable remedy was said to deprive defendants of the right to a jury trial when an "adequate" remedy at law was available. More recently the rule rests squarely on the constitutional ground that injunctive relief would necessarily infringe on the freedom of speech protected by the First Amendment by denying the speaker the option of getting his message to the public at large. See Near v. Minn., 283 U.S. 697 (1931); see also Rodney A. Smolla, 1 Law of Defamation §§9:86–90 (2d ed. 2015).

Does defamation over the Internet present a stronger case for injunctive relief? Recall that in *Delfino*, *supra* at 342, the trial court granted an injunction in light of defendants' vow to continue their defamatory Internet postings until they died. The injunction was overturned on appeal, however, as an unconstitutional prior restraint on speech. Are plaintiffs powerless to prevent ongoing, irreparable harm caused by Internet postings?

Would CDA §230 immunity nonetheless provide a shield against any injunctive relief? A plurality of the California Supreme Court thought so in Hassell v. Bird, 420 P.3d 776 (Cal. 2018), holding that section 230 immunity protected Yelp from a lower court order requiring Yelp to remove defamatory comments. Cuéllar, J., vehemently dissented:

> The Internet has the potential not only to enlighten but to spread lies, amplifying defamatory communications to an extent unmatched in our history. The resulting injuries to individuals' reputational interests from defamation, revenge porn, and similar content can be grave and long-lasting, and negative effects on businesses can be equally or more severe.

See also Joseph G. Marano, Caught in the Web: Enjoining Defamatory Speech That Appears on the Internet, 69 Hastings L.J. 1311 (2018).

### *b. Retraction*

Alternatively the law could require the defendant to retract the defamatory utterance, usually by publishing a withdrawal of the libel in the same newspaper or broadcast that originally published it. At common law retraction was not considered a complete defense, but only mitigated damages. See, e.g., Webb v. Call Publishing Co., 180 N.W. 263 (Wis. 1920), holding that a retraction does not fully restore the plaintiff to the position enjoyed before the initial libel was published. Even if the retraction receives broad publicity, many people who read the original defamatory statement are likely to miss it. Further, the retraction itself might not erase lingering doubts that the original statement contained at least some grain of truth.

Recently many states have enacted retraction statutes that apply to print defendants, broadcast defendants, or both. For example, Minn. Stat. §548.06 (2024) limits the plaintiff to special damages unless the defendant refuses to supply a retraction "on the same page and in the same point type and the statement headed in 18-point type or larger 'RETRACTION,' as were the statements complained of, in a regular issue thereof published within one week after such service. . . ." This statute represents an elegant compromise of conflicting interests in an effort to stop litigation before it begins. The statute first gives the plaintiff an incentive to seek the retraction: Unless that is done, she can only recover special damages. The statute does not set any specific time to request the retraction. Even so, the plaintiff has a strong incentive to do so quickly to correct the record while the issue is current. The statute next uses both carrots

and sticks to get the defendant to respond quickly to the retraction demand. If the demand is not met, the defendant exposes himself to suit for both special and general damages. If it is honored, the plaintiff gets at most special damages, but even those are denied if the defendant can show that he made an honest mistake in publishing the facts. Publishing the retraction also blocks suits for punitive damages. Any retraction must be full and complete because evasive apologies could confirm in the minds of readers that the defendant still stands behind the original charges. These statutory procedures are routinely invoked today, making the corrections columns a common feature of the modern newspaper. For an exhaustive tabulation of retraction statutes, see Robert D. Sack, Sack on Defamation: Libel, Slander and Related Problems §11.2 (5th ed. 2024); for a general account, see Rodney A. Smolla, 1 Law of Defamation §§9:70–84 (2d ed. 2015).

But once again, does CDA §230 relieve ISPs of any retraction obligations? In Bennett v. Google, LLC, 882 F.3d 1163, 1168 (D.C. Cir. 2018), the court reasoned that Google's decision not to retract content published by a user was fundamentally a publishing decision protected by section 230.

### *c. Reply Statutes*

In Miami Herald Publishing Co. v. Tornillo, 418 U.S. 241, 244, 257–58 (1974), a unanimous Supreme Court struck down a Florida "right of reply" statute that

> provides that if a candidate for nomination or election is assailed regarding his personal character or official record by any newspaper, the candidate has the right to demand that the newspaper print, free of cost to the candidate, any reply the candidate may make to the newspaper's charges. The reply must appear in as conspicuous a place and in the same kind of type as the charges which prompted the reply, provided it does not take up more space than the charges. Failure to comply with the statute constitutes a first-degree misdemeanor.

As drafted, the statute was not limited to defamatory statements. The Court held it unconstitutional in part because it increased the costs of printing and distributing a newspaper. Its decision rested, however, on more than purely economic considerations:

> Faced with the penalties that would accrue to any newspaper that published news or commentary arguably within the reach of the right-of-access statute, editors might well conclude that the safe course is to avoid controversy. Therefore, under the operation of the Florida statute, political and electoral coverage would be blunted or reduced. Government-enforced right of access inescapably "dampens the vigor and limits the variety of public debate," New York Times Co. v. Sullivan. . . .
>
> Even if a newspaper would face no additional costs to comply with a compulsory access law and would not be forced to forgo publication of news or opinion by the inclusion of a reply, the Florida statute fails to clear the barriers of the First Amendment because of its intrusion into the function of editors. A newspaper is more than a passive receptacle or conduit for news, comment, and advertising. The choice of material to go into a newspaper, and the decisions made as to limitations on the size and content of the paper, and treatment of public issues and public officials — whether fair or unfair — constitute the exercise of editorial control and judgment. It has yet to be demonstrated how governmental regulation of this crucial process can be exercised consistent with First Amendment guarantees of a free press as they have evolved to this time.

Should a right to reply be granted in the context of political broadcasts? Has *Tornillo* received a second life in connection with social media platforms? See *supra* Note 4, at 328.

### *d. Declaratory Relief and "Libel Tourism"*

Libel tourism refers to the practice of obtaining libel judgments from jurisdictions with claimant-friendly libel laws, even when the author or alleged libelous material has little

connection to that jurisdiction, solely to chill the author's activities in his home country. For an eye-opening overview, see Writ Large: Are English Courts Stifling Free Speech Around the World?, The Economist, Jan. 8, 2009. For a case that prompted much legislative reform, see Ehrenfeld v. Mahfouz, 518 F.3d 102 (2d Cir. 2008), in which the court refused to protect an American author against a Saudi Arabian plaintiff who had won a judgment against her in an English court for selling her book *Funding Evil*, which accused him of supporting Islamic terrorism. The book sold 23 copies in the United Kingdom, but she was ordered to pay £10,000 plus costs to Mahfouz. *Ehrenfeld* provoked a strong response in the United States with the prompt passage of the Securing the Protection of our Enduring and Established Constitutional Heritage (SPEECH) Act, Pub. L. No. 111-233, 124 Stat. 2480 (2024), which bars enforcement of foreign libel judgments that do not meet U.S. constitutional standards of due process and First Amendment protection.

The practice of libel tourism also led the United Kingdom to pass the Defamation Act of 2013 (ch. 26), which toughened the standards needed to prevail in defamation cases by adding in section 1 "a serious harm," in section 2 a defense for statements that were "substantially true," in section 3 a defense for honest opinions, in section 4 a defense for statements on "a matter of public interest," and in section 5 a general defense for operators of websites who did not post the offending statement. The net effect of these provisions is to move the UK law closer to the U.S. law. For the purposes of the SPEECH Act, is the quality of UK judgments in defamation cases measured by the terms of the UK statute, or by its application, as interpreted by UK courts?

For further discussion on this topic, see Jack Larkin, False Havens: Assessing New Developments in the Libel Tourism Debate, 11 J. of Media L. 82 (2019).

## NOTE

***Domestic Libel Tourism?*** The Depp v. Heard lawsuits ignited renewed attention on libel tourism. In 2018, Amber Heard published an opinion piece in the Washington Post claiming that her ex-husband Johnny Depp had subjected her to "sexual violence" and "domestic abuse." Elahe Izadi & Sarah Ellison, Why Johnny Depp Lost His Libel Case in the U.K. But Won in the U.S., Wash. Post, June 1, 2021. The Sun, a British tabloid, separately published an article labeling Depp a "wife beater." Depp sued The Sun for defamation in England and later sued Heard for defamation in Fairfax, Virginia. Ironically, although the United Kingdom's defamation law presents a lower bar to recovery than U.S. law (due to the latter's requirement of proof of actual malice), Depp lost his lawsuit against The Sun in England but was awarded $15 million in damages in his case against Heard in Virginia. Some pundits attributed the difference in outcomes to the factfinder in the cases; the UK case was decided by a judge, whereas the U.S. case was decided by a jury.

*Depp* is also interesting because it illuminates differences in defamation law across different states. Depp's decision to bring the case in Virginia as opposed to California, where both he and Heard reside, is an example of domestic libel tourism. States differ with regard to enacted anti-SLAPP (strategic lawsuits against public participation) statutes. Generally, anti-SLAPP statutes enable early dismissal of meritless defamation lawsuits. In the case at hand, Virginia's anti-SLAPP statute was much more relaxed than California's, thus making it more challenging for Virginia defendants to have meritless suits dismissed at the outset. Notably, Depp v. Heard influenced Virginia to tighten its anti-SLAPP statutes to make this sort of domestic libel tourism less likely in the future. Furthermore, by suing in Virginia as opposed to California, Depp took advantage of other aspects of Virginia defamation law, which has a narrower definition of claim preclusion (res judicata) that bars previous litigation only if

conducted between the same two parties. Therefore, because Depp had not named Heard as a defendant in the UK case, Heard could not use the UK court's judgment to avoid liability in the U.S. case.

## SECTION G. NONCONSTITUTIONAL DEFENSES

### 1. Truth

## *Auvil v. CBS 60 Minutes*

67 F.3d 816 (9th Cir. 1996)

Per Curiam: Grady and Lillie Auvil et al., suing on behalf of themselves and other similarly situated Washington State apple growers ("growers"), appeal from the district court's summary judgment in favor of CBS "60 Minutes" ("CBS"). The district court held that the growers failed to prove the falsity of the message conveyed by the "60 Minutes" broadcast of "'A' is for Apple," which concerned the use of Alar, a chemical sprayed on apples. We . . . affirm because we agree that the growers have failed to raise a genuine issue of material fact as to the falsity of the broadcast.

#### Background

On February 26, 1989, CBS's weekly news show "60 Minutes" aired a segment on daminozide, a chemical growth regulator sprayed on apples. The broadcast, entitled "'A' is for Apple," also addressed the slow pace of government efforts to recall the chemical. The broadcast was based largely on a Natural Resources Defense Council ("NRDC") report, entitled *Intolerable Risk: Pesticides in Our Children's Food* ("*Intolerable Risk*"), which outlined health risks associated with the use of a number of pesticides on fruit, especially the risks to children. "'A' is for Apple" focused on the NRDC report's findings concerning daminozide, as well as the EPA's knowledge of daminozide's carcinogenity. Scientific research had indicated that daminozide, more commonly known by its trade name, Alar, breaks down into unsymmetrical dimethylhydrazine (UDMH), a carcinogen.

The segment opened with the following capsule summary from Ed Bradley, a "60 Minutes" commentator:

> The most potent cancer-causing agent in our food supply is a substance sprayed on apples to keep them on the trees longer and make them look better. That's the conclusion of a number of scientific experts. And who is most at risk? Children, who may someday develop cancer from this one chemical called daminozide. Daminozide, which has been sprayed on apples for more than 20 years, breaks down into another chemical called UDMH.

During the broadcast, Bradley garnered a number of viewpoints on the Alar issue. Those interviewed included an Environmental Protection Agency ("EPA") administrator, an NRDC attorney, a U.S. congressman, a professor of pediatrics at Harvard Medical School, and a scientist from the Consumers Union, which publishes *Consumer Reports* magazine. After Bradley's opening synopsis, the broadcast segment began with the EPA administrator's admission that the EPA had known of cancer risks associated with daminozide for sixteen years, but that EPA regulations had hampered the removal of the chemical from the market. The U.S. Congressman rejected the EPA administrator's explanation that the laws were to blame for the EPA's hesitation. He thought that it was well within the EPA's power to remove daminozide

from the market, and that the EPA's reluctance stemmed from its fear that Uniroyal, the company that manufactured daminozide, would sue the EPA. The broadcast segment continued with testimonials from the NRDC attorney, who discussed the findings published in *Intolerable Risk*, focusing on the cancer risks to children from ingestion of apples treated with daminozide. The NRDC's findings were corroborated both by the EPA administrator and the Harvard pediatrician. The broadcast ended with the statements of a Consumers Union scientist, who revealed that most manufacturers of apple products said they no longer use apples treated with daminozide but that the manufacturers were unsuccessful in keeping daminozide completely out of their products.

Following the "60 Minutes" broadcast, consumer demand for apples and apple products decreased dramatically. The apple growers and others dependent upon apple production lost millions of dollars. Many of the growers lost their homes and livelihoods.

In November 1990, eleven Washington State apple growers, representing some 4,700 growers in the Washington area, filed a complaint in Washington State Superior Court against CBS, local CBS affiliates, the NRDC, and Fenton Communications, Inc., a public relations firm used by the NRDC in 1989. The growers asserted, among others, a claim for product disparagement. . . .

## Discussion

We review the district court's summary judgment ruling *de novo*. To survive CBS's motion for summary judgment, the growers must set forth specific facts showing that there is a genuine issue for trial. . . .

[The court first held that the plaintiffs] whose products are disparaged face a higher burden of proof than do defamation plaintiffs. . . . Accordingly, for a product disparagement claim to be actionable, the plaintiff must prove, *inter alia*, the falsity of the disparaging statements. . . .

The growers offered evidence showing that no studies have been conducted to test the relationship between ingestion of daminozide and incidence of cancer in *humans*. Such evidence, however, is insufficient to show a genuine issue for trial regarding the broadcast's assertions that daminozide is a potent carcinogen. Animal laboratory tests are a legitimate means for assessing cancer risks to humans. . . .

The growers provide no other challenge to the EPA's findings, nor do they directly attack the validity of the scientific studies. All of the statements referenced above are factual assertions made by the interviewees, based on the scientific findings of the NRDC. These findings were corroborated by the EPA administrator and a Harvard pediatrician. The EPA, which often relies on the results of animal studies, acknowledged that it knew of the cancer risks associated with ingestion of daminozide and, in August 1985, classified daminozide as a "probable human carcinogen." Indeed, the EPA estimated that the dietary risk to the general population from UDMH, a metabolite of daminozide, was fifty times an acceptable risk and ultimately concluded that daminozide posed an unreasonable risk to the general population. . . .

On the subject of cancer risks to children from the use of daminozide on apples, the growers point to the following factual assertions to support their falsity claim:

> What we're talking about is a cancer-causing agent used on food that EPA knows is going to cause cancer for thousands of children over their lifetime.
>
> [T]he Natural Resources Defense Council[] has completed the most careful study yet on the effect of daminozide and seven other cancer-causing pesticides on the food children eat.
>
> [O]ver a lifetime, one child out of every 4,000 or so of our preschoolers will develop cancer just from these eight pesticides. [The NRDC study] says children are being exposed to a pesticide risk several hundred times greater than what the agency says is acceptable.

The growers offered evidence showing that no scientific study has been conducted on cancer risks to children from the use of pesticides. However, CBS based its statements regarding cancer and children on the NRDC's findings that the daminozide found on apples is more harmful to children because they ingest more apple products per unit of body weight than do adults. The growers have provided no affirmative evidence that daminozide does not pose a risk to children. The fact that there have been no studies conducted specifically on the cancer risks to children from daminozide does nothing to disprove the conclusion that, if children consume more of a carcinogenic substance than do adults, they are at higher risk for contracting cancer. The growers' evidence, therefore, does not create a genuine issue as to the falsity of the broadcast's assertion that daminozide is more harmful to children.

Despite their inability to prove that *statements* made during the broadcast were false, the growers assert that summary judgment for CBS was improper because a jury could find that the broadcast contained a provably false *message*, viewing the broadcast segment in its entirety. They further argue that, if they can prove the falsity of this implied message, they have satisfied their burden of proving falsity.

The growers' contentions are . . . unprecedented and inconsistent with Washington law. No Washington court has held that the analysis of falsity proceeds from an implied, disparaging message. It is the statements themselves that are of primary concern in the analysis. . . .

The Washington courts' view finds support in the Restatement, which instructs that a product disparagement plaintiff has the burden of proving the "falsity of the *statement*." Restatement (Second) of Torts §651(1)(c) (emphasis added). This standard refers to individual statements and not to any overall message. Therefore, we must reject the growers' invitation to infer an overall message from the broadcast and determine whether that message is false.

We also note that, if we were to accept the growers' argument, plaintiffs bringing suit based on disparaging speech would escape summary judgment merely by arguing, as the growers have, that a jury should be allowed to determine both the overall message of a broadcast and whether that overall message is false. Because a broadcast could be interpreted in numerous, nuanced ways, a great deal of uncertainty would arise as to the message conveyed by the broadcast. Such uncertainty would make it difficult for broadcasters to predict whether their work would subject them to tort liability. Furthermore, such uncertainty raises the spectre of a chilling effect on speech.

### Conclusion

Because the growers have failed to raise a genuine issue of material fact regarding the falsity of statements made during the broadcast of "'A' is for Apple," the district court's decision granting CBS's motion for summary judgment is

Affirmed.

## NOTES

**1. *The Alar "Scare."*** Should the plaintiff or defendant bear the burden of proof on the truth issue? What if the plaintiffs in *Auvil* had introduced evidence showing no increased incidence of cancer among children who ate large numbers of apples? Airing the *60 Minutes* segment to 40 million people across the country was estimated to cause apple growers nationwide to suffer more than $100 million in lost sales. The story affected sales of all apples even though only about 15 percent of apples were treated with Alar. A few months after the original CBS story, Uniroyal Chemical Co. pulled Alar from the market and had its registration canceled

**Meryl Streep in the 1980s. In 1989, Streep testified before Congress and on TV talk shows about Alar's dangers.**

*Source: Hulton-Deutsch Collection/Corbis*

with the EPA. In 1991, C. Everett Koop, the former U.S. Surgeon General, concluded that, properly used, "Alar-treated apple products posed no hazard to the health of children or adults." A 1991 study of the National Cancer Institute concluded that the Alar flap was an "unfounded carcinogen scare." Ernst L. Wynder, Primary Prevention of Cancer: Planning and Policy Considerations, 83 J. Nat'l Cancer Inst. 475 (1991). For a retrospective on the controversy, see Ashton, After 10 Years, Debate Continues over Pesticide That Tainted Red Apples, Seattle Post-Intelligencer, Mar. 1, 1999, at B4.

**2.** ***Defamation and Truth.*** What is the proper relationship between defamation and truth? The conventional view holds that the prima facie case in defamation does not require a showing that the defendant published a false statement. Instead it is enough that the defendant published defamatory matter about ("of and concerning") the plaintiff that tends to lower the estimation of plaintiff in the eyes of third parties to whom it is directed. Truth is regarded as an absolute defense to the defamation so published, which is tantamount to an assertion that a statement is defamatory only if it is false; that is, a misrepresentation to third persons. See RST §581A. Should truthful statements of the defendant ever be regarded as libelous?

The allocation of truth as a defense suggests that the burden lies on the defendant to establish the defense. That orientation is consistent with the approach of the earlier common law, which was more hostile to the defense of truth than *Auvil*. In order to protect reputation, common law courts often read statements quite closely, rejecting the defense where there had been small and seemingly insignificant factual errors in the defendant's statement. The headnote in Sharpe v. Stevenson, 34 N.C. 348, 348 (1851), gives some hint of the required level of precision: "In an action of slander (under our statute) for charging that the plaintiff had criminal intercourse with one *A*. at a particular time and place, the defendant cannot justify by showing that she had such intercourse with *A*. at another time and place." That result was criticized in J.C. Courtney, Absurdities of the Law of Slander and Libel, 36 Am. L. Rev. 552, 563 (1902), in which the author observed: "A criminal abandon in the drawing-room as completely destroys all claim to a reputation for chastity as a lascivious embrace in the bushes." For a modern hint of the same point, see Haynes v. Alfred A. Knopf, Inc., 8 F.3d 1222, 1228 (7th Cir. 1993), in which Posner, C.J., observes: "The rule of substantial truth is based on a recognition that falsehoods which do no *incremental* damage to the plaintiff's reputation do not injure the only interest that the law of defamation protects."

**3.** ***Quotations.*** The defense of truth did not allow the defendant to obtain summary judgment in Price v. Stossel, 620 F.3d 992, 1003 (9th Cir. 2010). There the court overturned a lower court's dismissal of a televised preacher's defamation claim against John Stossel and ABC's show *20/20* based on excerpts from the plaintiff's sermon that were included in a segment of Stossel's show titled "Enough." Stossel introduced the segment: "They preach the gospel of giving to God. But how much of what you give do they keep for themselves? Is it time for someone to say 'enough'?" An audiovisual clip shows the plaintiff boasting: "I live in a 25-room mansion. I have my own $6 million yacht. I have my own private jet, and I have my own helicopter, and I have seven luxury automobiles." Yet context matters. Schroeder, J., held that because in evaluating the defense of truth

> the proper comparison is between the meaning of the quotation as published and the meaning of the words as uttered, we conclude that the video quotation of Price's statement materially

> changed the meaning of Price's words. Price did not make any representations about his own wealth when he delivered the sermon that was excerpted in the Clip. In the quote, as misrepresented by the Clip, Price is speaking about himself, whereas in the context of the actual sermon, Price is telling a story about someone entirely different.

Why not grant the plaintiff a summary judgment on the issue of truth?

**4. *Known to be False.*** In the usual defamation case, the false information leads people to shun the plaintiff because they revise their opinion of her. But what should be done in those cases where the false statement leads people to hold the plaintiff in hatred, ridicule, or contempt when they *know* the statement to be false but are titillated by it nonetheless? In Hustler Magazine v. Falwell, 485 U.S. 46 (1988), the Supreme Court held that the vicious nature of the defendant's parody rendered it intrinsically unbelievable and therefore undercut the plaintiff's libel claim. *Falwell* has been followed with enthusiasm by lower courts that have treated *deliberate* parody as outside the scope of defamation on the ground that no one could believe it to be true. In New Times, Inc. v. Isaacks, 146 S.W.3d 144 (Tex. 2004), the plaintiff, District Attorney Bruce Isaacks, was pilloried in a satirical article in the *Dallas Observer* lampooning officials involved in the arrest and detention of a thirteen-year-old for writing a Halloween story that was deemed to contain "terrorist threats."

> Entitled "Stop the madness," the fictitious article described the arrest and detention of "diminutive 6 year-old" Cindy Bradley, who was purportedly jailed for writing a book report about "cannibalism, fanaticism, and disorderly conduct" in Maurice Sendak's classic children's book, *Where the Wild Things Are*. Adjacent to the article was a picture of a smiling child holding a stuffed animal and bearing the caption, "Do they make handcuffs this small? Be afraid of this little girl."

Fabricated facts and false quotes attributed to Isaacks and others were strewn throughout the piece. Isaacks demanded an apology, requested a retraction, and then sued for libel. The court below affirmed the trial court's denial of the defendant publisher's summary judgment motion because the article "fails to provide any notice to a reasonable reader that it was a satire or parody and that a reasonable reader could conclude that the article made statements of fact." On appeal, Jefferson, J., disagreed, dismissing the libel claim:

> On balance, the obvious clues in the article itself, the *Observer*'s general and intentionally irreverent tone, its semi-regular publication of satire, as well as the satire's timing and commentary on a then-existing controversy, lead us to conclude that "Stop the madness" could not reasonably be understood as stating actual facts about Isaacks. . . .

In a similar vein, in Farah v. Esquire Magazine, 736 F.3d 528 (D.C. Cir. 2013), Rogers, J., affirmed the dismissal of a defamation action brought by the author of Where's the Birth Certificate? The Case That Barack Obama Is Not Eligible to Be President against Esquire Magazine for an article criticizing the book on its blog. The article claimed that the publisher had "suddenly and without any warning decided to recall and 'pulp' the . . . book the very day after it was released." It also attributed to the author an obviously fictitious book entitled "Capricorn One: NASA, JFK, and the Great 'Moon Landing' Cover-Up." Rogers, J., emphasized the significance of "context," which includes "the immediate context of the disputed statements," "the type of publication, the genre of writing, and the publication's history of similar works," as well as "[t]he broader social context." And she held: "Even if none of these elements standing alone — the story's substance, outlandish and humorous details, stylistic elements — would convince the reasonable reader that the blog post was satirical, taken in context and as a whole they could lead to no other conclusion."

For the constitutional dimension, see Philadelphia Newspapers, Inc. v. Hepps, 475 U.S. 767 (1986), *infra* Note 2, at 401.

## 2. Privileges in the Private Sphere

### *Watt v. Longsdon*

[1930] 1 K.B. 130

[Watt sued Longsdon for three separate defamatory publications. Plaintiff was the managing director in Casablanca, Morocco, of a British oil company of which the defendant was a director. At the time the various communications took place, the company was in the process of voluntary liquidation. In April 1928, Browne, who was the company's manager in Casablanca, wrote a letter to the defendant in England at about the time the plaintiff left Casablanca for Lisbon after the plaintiff's wife had returned to England. Browne's letter charged that plaintiff had left a liquor bill of £88, which Browne doubted would ever get paid, and related in detail how the plaintiff's maid had been plaintiff's mistress for several months. Browne expressed his surprise, "especially as she is an old woman, stone deaf, almost blind, with dyed hair!!!" but stated that the maid was able to give corroborating details. Browne's letter stated further that servants had told him that the plaintiff had had "orgies" with dancing girls, that he had designs on Browne's wife, and that plaintiff had shown himself to be "a blackguard, a thief, a liar and . . . lives exclusively to satisfy his own passions and lust." In a postscript, Browne suggested that it would probably be better not to show the plaintiff's wife the letter but that Mr. Singer, chairman of the board of directors of the company, should be told. In May 1928, defendant sent Browne's letter to Singer; and this is the first act of defamation complained of.

Defendant at the same time wrote Browne a letter in which he shared Browne's general view of the plaintiff and asked Browne to obtain sworn statements from his informants, offering to pay any bribes necessary to obtain such statements; the letter further said he thought it his duty to inform plaintiff's wife but that he would not do so until he had the sworn statements in his hand. This letter from the defendant to Browne was the second act of defamation complained of.

A few days later, without having received further confirmation of the statements in Browne's letter, the defendant showed it to plaintiff's wife, with the result that plaintiff and his wife separated, and she began suit for divorce. The showing of Browne's letter to plaintiff's wife was the third act of defamation complained of.

Defendant did not defend the truth of the libels contained in the letters. Nevertheless, Horridge, J., gave judgment for the defendant, ruling that all three publications were privileged. The Court of Appeal reversed for the reasons indicated below.]

Scrutton, L.J. This case raises, amongst other matters, the extremely difficult question, equally important in its legal and social aspect, as to the circumstances, if any, in which a person will be justified in giving to one partner to a marriage information which that person honestly believes to be correct, but which is in fact untrue, about the matrimonial delinquencies of the other party to the marriage. . . .

By the law of England there are occasions on which a person may make defamatory statements about another which are untrue without incurring any legal liability for his statements. These occasions are called privileged occasions. A reason frequently given for this privilege is that the allegation that the speaker has "unlawfully and maliciously published," is displaced by proof that the speaker had either a duty or an interest to publish, and that this duty or interest confers the privilege. But communications made on these occasions may lose their privilege: (1.) they may exceed the privilege of the occasion by going beyond the limits of the duty or interest, or (2.) they may be published with express malice, so that the occasion is not being legitimately used, but abused. . . . The classical definition of

"privileged occasions" is that of Parke B. in Toogood v. Spyring, a case where the tenant of a farm complained to the agent of the landlord, who had sent a workman to do repairs, that the workman had broken into the tenant's cellar, got drunk on the tenant's cider, and spoilt the work he was sent to do. The workman sued the tenant. Parke B. gave the explanation of privileged occasions in these words: "In general, an action lies for the malicious publication of statements which are false in fact, and injurious to the character of another (within the well-known limits as to verbal slander), and the law considers such publication as malicious, unless it is fairly made by a person in the discharge of some public or private duty, whether legal or moral, or in the conduct of his own affairs, in matters where his interest is concerned. In such cases, the occasion prevents the inference of malice, which the law draws from unauthorized communications, and affords a qualified defence depending upon the absence of actual malice. If fairly warranted by any reasonable occasion or exigency, and honestly made, such communications are protected for the common convenience and welfare of society; and the law has not restricted the right to make them within any narrow limits." It will be seen that the learned judge requires: (1.) a public or private duty to communicate, whether legal or moral; (2.) that the communication should be "fairly warranted by any reasonable occasion or exigency"; (3.) or a statement in the conduct of his own affairs where his interest is concerned. Parke B. had given several other definitions in slightly varying terms. [Later cases add] to the protection of his own interest spoken of in Toogood v. Spyring the protection of the interests of another where the situation of the writer requires him to protect those interests. This, I think, involves that his "situation" imposes on him a legal or moral duty. The question whether the occasion was privileged is for the judge, and so far as "duty" is concerned, the question is: Was there a duty, legal, moral, or social, to communicate? As to legal duty, the judge should have no difficulty; the judge should know the law; but as to moral or social duties of imperfect obligation, the task is far more troublesome. The judge has no evidence as to the view the community takes of moral or social duties. . . . Is the judge merely to give his own view of moral and social duty, though he thinks a considerable portion of the community hold a different opinion? Or is he to endeavour to ascertain what view "the great mass of right-minded men" would take? It is not surprising that with such a standard both judges and text-writers treat the matter as one of great difficulty in which no definite line can be drawn. . . .

[After considering various other English precedents, the court summarized the occasions giving rise to a privileged communication as follows:] [E]ither (1.) a duty to communicate information believed to be true to a person who has a material interest in receiving the information, or (2.) an interest in the speaker to be protected by communicating information, if true, relevant to that interest, to a person honestly believed to have a duty to protect that interest, or (3.) a common interest in and reciprocal duty in respect of the subject matter of the communication between speaker and recipient. . . .

In my opinion Horridge J. went too far in holding that there could be a privileged occasion on the ground of interest in the recipient without any duty to communicate on the part of the person making the communication. But that does not settle the question, for it is necessary to consider, in the present case, whether there was, as to each communication, a duty to communicate, and an interest in the recipient.

First as to the communication between Longsdon and Singer, I think the case must proceed on the admission that at all material times Watt, Longsdon and Browne were in the employment of the same company, and the evidence afforded by the answer to the interrogatory put in by the plaintiff that Longsdon believed the statements in Browne's letter. In my view on these facts there was a duty, both from a moral and material point of view, on Longsdon to communicate the letter to Singer, the chairman of his company, who, apart from questions of present employment, might be asked by Watt for a testimonial to a future

employer. Equally, I think Longsdon receiving the letter from Browne, might discuss the matter with him, and ask for further information, on the ground of a common interest in the affairs of the company, and to obtain further information for the chairman. I should therefore agree with the view of Horridge J. that these two occasions were privileged, though for different reasons. Horridge J. further held that there was no evidence of malice fit to be left to the jury, and, while I think some of Longsdon's action and language in this respect was unfortunate, as the plaintiff has put in the answer that Longsdon believed the truth of the statements in Browne's and his own letter, like Lord Dunedin in Adam v. Ward, I should not try excess with too nice scales, and I do not dissent from his view as to malice. As to the communications to Singer and Browne, in my opinion the appeal should fail, but as both my brethren take the view that there was evidence of malice which should be left to the jury, there must, of course, be a new trial as to the claim based on these two publications.

The communication to Mrs. Watt stands on a different footing. I have no intention of writing an exhaustive treatise on the circumstances when a stranger or a friend should communicate to husband or wife information he receives as to the conduct of the other party to the marriage. I am clear that it is impossible to say he is always under a moral or social duty to do so; it is equally impossible to say he is never under such a duty. It must depend on the circumstances of each case, the nature of the information, and the relation of speaker and recipient. It cannot, on the one hand, be the duty even of a friend to communicate all the gossip the friend hears at men's clubs or women's bridge parties to one of the spouses affected. On the other hand, most men would hold that it was the moral duty of a doctor who attended his sister in law, and believed her to be suffering from a miscarriage, for which an absent husband could not be responsible, to communicate that fact to his wife and the husband. . . . If this is so, the decision must turn on the circumstances of each case, the judge being much influenced by the consideration that as a general rule it is not desirable for any one, even a mother in law, to interfere in the affairs of man and wife. Using the best judgment I can in this difficult matter, I have come to the conclusion that there was not a moral or social duty in Longsdon to make this communication to Mrs. Watt such as to make the occasion privileged, and that there must be a new trial so far as it relates to the claim for publication of a libel to Mrs. Watt. The communications to Singer and Browne being made on a privileged occasion, there must be a new trial of the issue as to malice defeating the privilege. There must also be a new trial of the complaint as to publication to Mrs. Watt, the occasion being held not to be privileged. . . .

Greer, L.J. . . . In my judgment no right minded man in the position of the defendant, a friend of the plaintiff and his wife, would have thought it right to communicate the horrible accusations contained in Mr. Browne's letter to the plaintiff's wife. The information came to Mr. Browne from a very doubtful source, and in my judgment no reasonably right-minded person could think it his duty, without obtaining some corroboration of the story, and without first communicating with the plaintiff, to pass on these outrageous charges of marital infidelity of a gross kind, and drunkenness and dishonesty to the plaintiff's wife. As regards the publication to the plaintiff's wife, the occasion was not privileged, and it is unnecessary to consider whether there was evidence of express malice. As regards the publication to the chairman of the company, who owned nearly all the shares, and to Mr. Browne, I think on the facts as pleaded there was between the defendant and the recipients of the letters a common interest which would make the occasion privileged, but I also think there is intrinsic evidence in the letter to Browne, and evidence in the hasty and unjustifiable communication to the plaintiff's wife, which would be sufficient to entitle the plaintiff to ask for a verdict on these publications on the ground of express malice. . . .

I think the defendant's conduct in disseminating the gross charges that he did to the plaintiff's wife, and to Mr. Singer, and repeating and to some extent adding to them in his letter to Mr. Browne, and his offer to provide funds for procuring the evidence of the two women in Casablanca, affords some evidence of malice which ought to have been left to the jury. It is not for us to weigh the evidence. It will be for the jury to decide whether they are satisfied that in publishing the libels the defendant was in fact giving effect to his malicious or otherwise improper feelings towards the plaintiff, and was not merely using the occasion for the protection of the interests of himself and his two correspondents.

## NOTES

1. ***When Is a Communication Privileged?*** The common law has sought to identify those socially useful private communications that should be encouraged by relaxing the basic rule of liability, whether strict, or more recently, negligence. To achieve the proper balance most courts and commentators, both in England and the United States, have closely followed Baron Park's scheme outlined in Toogood v. Spyring, 149 Eng. Rep. 1044 (Ex. 1834), discussed in *Watt*. Under this scheme, the existence of privileged occasions depends on the interest of the speaker, the interest of his audience, or a common interest between the speaker and his audience. See RST §§594–96, following the basic rule.

### RESTATEMENT OF THE LAW (SECOND) OF TORTS

**§594. Protection of the Publisher's Interest**

An occasion makes a publication conditionally privileged if the circumstances induce a correct or reasonable belief that

(a) there is information that affects a sufficiently important interest of the publisher, and

(b) the recipient's knowledge of the defamatory matter will be of service in the lawful protection of the interest.

### RESTATEMENT OF THE LAW (SECOND) OF TORTS

**§595. Protection of Interest of Recipient of a Third Person**

(1) An occasion makes a publication conditionally privileged if the circumstances induce a correct or reasonable belief that

(a) there is information that affects a sufficiently important interest of the recipient or a third person, and

(b) the recipient is one to whom the publisher is under a legal duty to publish the defamatory matter or is a person to whom its publication is otherwise within the generally accepted standards of decent conduct.

(2) In determining whether a publication is within generally accepted standards of decent conduct it is an important factor that

(a) the publication is made in response to a request rather than volunteered by the publisher or

(b) a family or other relationship exists between the parties.

**RESTATEMENT OF THE LAW (SECOND) OF TORTS**

**§596. Common Interest**

An occasion makes a publication conditionally privileged if the circumstances lead any one of several persons having a common interest in a particular subject matter correctly or reasonably to believe that there is information that another sharing the common interest is entitled to know.

References (or "characters") concerning (or for) former servants can be privileged, where the defendant is replying to an inquiry. In Gardner v. Slade, 116 Eng. Rep. 1467, 1470 (Q.B. 1849), a case involving a domestic servant, Wightman, J., said:

> It is quite a mistake to treat questions of this kind as if the law allowed a privilege only for the benefit of the giver of the character. It is of importance to the public that characters should be readily given. The servant who applies for the character, and the person who is to take him, are equally benefited. Indeed, there is no class to whom it is of so much importance that characters should be freely given as honest servants.

The privilege has been extended to many intragroup situations such as churches, fraternal organizations, labor unions, shareholders of a corporation, and, more recently, faculty evaluation committees (Colson v. Stieg, 433 N.E.2d 246 (Ill. 1982)), student evaluation committees (Doe v. Gonzaga Univ., 24 P.3d 390 (Wash. 2001)), and physicians and their health plans with respect to the medical records of their patients (Kuwik v. Starmark Star Mktg. & Admin., Inc., 619 N.E.2d 129, 134, 135 (Ill. 1993)).

The potential dangers in this area, especially with references for former employees, has sparked an effort to regulate the matter by consent, which, when given, is generally understood to create only a qualified privilege. See RST §583: "[O]ne who agrees to submit his conduct to investigation, knowing that its results will be published, consents to the publication of honest findings of investigators." In many cases, the fear of defamation suits has led former employers to adopt a strict rule under which they only provide information as to dates of employment and last position held. Even salary information (which is hard to interpret with bonuses and the like) is often not disclosed.

**2. *Credit Reports.*** In Smith v. Thomas, 132 Eng. Rep. 146 (C.P. 1835), a case involving a credit reference, the court observed:

> The publication is alleged to have taken place in the course of a confidential communication between one tradesman and another, as to the solvency of a third person, whom the inquirer was about to trust. If such communications are not protected by law from the danger of vexatious litigation in cases where they turn out to be incorrect in fact, the stability of men engaged in trade and commerce would be exposed to the greatest hazard, for no man would answer an inquiry as to the solvency of another.

This privilege has also been extended to commercial credit agencies. In Shore v. Retailers Commercial Agency, 174 N.E.2d 376, 379 (Mass. 1961), Spaulding, J., wrote:

> We are of opinion that reports made by a mercantile agency to an interested subscriber should be conditionally privileged. Those about to engage in a commercial transaction like to know something about the persons with whom they are dealing. Often they are unable to get that information themselves and must obtain it through mercantile agencies. In furnishing such information the agencies are supplying a legitimate business need and ought to have the protection of the privilege. Without such protection few would undertake to furnish the information, and the cost would be high, if not prohibitive. . . . We are not to be understood as holding that there is a privilege where information is published by the agency generally to subscribers having no particular interest in the report. Restatement: Torts, §595, comment *g*.

*Shore* reflects the majority view in the United States, with only Georgia and Idaho denying that a conditional privilege attaches to credit reports. See Robert D. Sack, Sack on Defamation: Libel, Slander and Related Problems §9.2.2.C (5th ed. 2024). This area of privilege has generally not been affected by *New York Times*. See *Dun & Bradstreet*, *infra* at 402.

**3. *Volunteers.*** As *Watt* indicates, one troublesome problem arises when the defendant has volunteered communication to a third party without a request. Generally a party is not necessarily protected in answering an inquiry; nor is he necessarily exposed by volunteering information. Rather, Restatement (Second) of Torts §595(2)(a) notes that it is an "important factor" that "the publication is made in response to a request rather than volunteered by the publisher."

In Count Joannes v. Bennett, 87 Mass. 169, 172 (1862), the defendant, the family pastor and intimate friend, was persuaded by the father to write the daughter a letter urging her to call off her proposed marriage to plaintiff. The court held that the contents of the letter were not privileged, pointing out that the defendant, although he acted "from laudable motives in writing it," was no longer the daughter's pastor and was in no way related to her other than as a friend. The court said, in part:

> It is obvious that if such communications could be protected merely on the ground that the party making them held friendly relations with those to whom they were written or spoken, a wide door would be left open by which indiscriminate aspersion of private character could escape with impunity. Indeed, it would rarely be difficult for a party to shelter himself from the consequences of uttering or publishing a slander or libel under a privilege which could be readily made to embrace almost every species of communication. The law does not tolerate any such license of speech or pen.

Does the same result obtain under *Watt*?

**4. *Defamation in Self-Defense.*** A distinct form of conditional privilege also arises "when the person making the publication reasonably believes that his interest in his own reputation has been unlawfully invaded by another person and that the defamatory matter that he publishes about the other is reasonably necessary to defend himself"—"including the statement that his accuser is an unmitigated liar." RST §594, cmt. *k*. The boundaries of this privilege are not clearly established, which gives rise to questions reminiscent of those raised with self-defense against physical attack: How vigorous must the plaintiff's original aggression have been? Must the original attack have been defamatory? What if it was true or privileged? Must the statement made in self-defense concern the precise subject as the original accusation and, if not, how much leeway is there? Again, how much verbal force may the defendant use in reply? Does the privilege extend to the defense of third parties? Further, the doctrine has strong overtones of assumption of risk and contributory negligence because the plaintiff, having invited a reply, cannot complain when a vigorous one is given to a public already alert to controversy.

## 3. Privileges in the Public Sphere

### *a. Legal Proceedings and Reports Thereon*

## *Kennedy v. Cannon*

182 A.2d 54 (Md. 1962)

Sybert, J. This appeal questions whether the trial court erred in directing a verdict for the defendant, an attorney, in a suit for slander on the grounds that the allegedly slanderous statement was privileged as part of the defendant's duty as counsel to his client, and that no malice on the part of the defendant had been shown.

[The defendant-appellee, Robert Powell Cannon, was the lawyer for an African American man, Charles Humphreys, charged with raping the plaintiff-appellant, Jane Linton Kennedy a white, married woman. He admitted to having had intercourse with her but claimed that she had consented to the act. The defendant Cannon spoke to the editor of the local paper, giving his side of the story. The editor said it would be "impossible to print matter of that type and at such great length." The story in the afternoon paper recounted the plaintiff's charges against Humphreys, noted his admission of intercourse, and concluded with the defendant saying, "He [Humphreys] emphatically denies the charge. He says that the woman submitted to his advances willingly."]

As a result of the publication of the statement appellant Kennedy alleged she suffered humiliation and harassment by annoying phone calls from unknown persons and eventually was forced to move with her family out of the community and the State. She instituted a suit against appellee alleging that the words spoken by him to the newspaper charged her with the crime of adultery, were slanderous per se under Art. 88, §1, Code (1957), and were not privileged.

The appellee admitted on the witness stand that the newspaper article correctly quoted his statement to the editor. He sought to justify its publication on the ground that the physical safety of his client required it. He stated he feared the possibility of a lynching if only the material released by the State's Attorney were published. Recalling a lynching which had occurred in Salisbury under similar circumstances some 25 years previously, he said he felt that the account should include a denial of the charge based upon his client's claim of consent by the woman. At the conclusion of the testimony before a jury, the trial court granted appellee's motion for a directed verdict, expressing the opinion that when the State had undertaken to publish a statement about the case damaging to his client, the appellee was justified and privileged in replying as he did. Appellant appeals from the judgment for costs entered in favor of appellee. . . .

The privilege afforded an attorney in a judicial proceeding and its rationale are discussed in the leading case of Maulsby v. Reifsnider, 69 Md. 143 (1888), where this Court stated:

> . . . All agree, that counsel are privileged and protected to a certain extent, at least, for defamatory words spoken *in a judicial proceeding*, and words thus spoken are not actionable, which would in themselves be actionable, if spoken elsewhere. He is obliged, in the discharge of a professional duty, to prosecute and defend the most important rights and interests, the life it may be, or the liberty or the property of his client, and it is absolutely essential to the administration of justice that he should be allowed the widest latitude in commenting on the character, the conduct and motives of parties and witnesses and other persons directly or remotely connected with the subject-matter in litigation. And to subject him to actions of slander by every one who may consider himself aggrieved, and to the costs and expenses of a harassing litigation, would be to fetter and restrain him in that open and fearless discharge of duty which he owes to his client, and which the demands of justice require. Not that the law means to say, that one, because he is counsel in the trial of a cause, has the right, abstractly considered, deliberately and maliciously to slander another, but it is the fear that if the rule were otherwise, actions without number might be brought against counsel who had not spoken falsely and maliciously. It is better therefore to make the rule of law so large that counsel acting bona fide in the discharge of duty, shall never be troubled, although by making it so large, others who have acted mala fide and maliciously, are included. The question whether words spoken by counsel were spoken maliciously or in good faith, are, and always will be, open questions, upon which opinion may differ, and counsel, however innocent, would be liable if not to judgments, to a vexatious and expensive litigation. The privilege thus recognized by law is not the privilege merely of counsel, but the privilege of clients, and the evil, if any, resulting from it must be endured for the sake of the greater good which is thereby secured. But this privilege is not an absolute and unqualified privilege, and cannot be extended beyond the reason and principles on which it is founded. . . . (Emphasis added.)

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[The court went on to hold that the words, in order for an absolute privilege to attach, also had to be relevant to the judicial proceedings in which they were spoken.]

This absolute immunity extends to the judge as well as to witnesses and parties to the litigation, for defamatory statements uttered in the course of a trial or contained in pleadings, affidavits, depositions, and other documents directly related to the case. . . . An absolute privilege is distinguished from a qualified privilege in that the former provides immunity regardless of the purpose or motive of the defendant, or the reasonableness of his conduct, while the latter is conditioned upon the absence of malice and is forfeited if it is abused. . . .

Appellee in this case contends that under the *Maulsby* case, his statement was absolutely privileged. It is not disputed that the statement was relevant to the criminal proceeding. The essential question to be answered is whether it was published in — that is, as part of — a "judicial proceeding."

The term "judicial proceeding" is broad enough to cover all steps in a criminal action, so that when Humphreys was arrested and charged with rape it would be a valid conclusion that the judicial proceeding had commenced. . . . However, this does not necessarily mean that every statement made by an attorney after the inception of a judicial proceeding will be privileged.

Appellee cites the oft quoted rule from 3 Restatement, Torts, §586:

> An attorney at law is absolutely privileged to publish false and defamatory matter of another in communications preliminary to a proposed judicial proceeding, or in the institution of, or during the course and as a part of a judicial proceeding in which he participates as counsel, if it has some relation thereto.

However, the extension of this absolute privilege to statements not made in the judicial proceeding itself is limited both by the comments on the rule of the Restatement itself, and by the decisions. The scope of the privilege is restricted to communications such as those made between an attorney and his client, or in the examination of witnesses by counsel, or in statements made by counsel to the court or jury. . . . Appellee cites no authorities which would extend the privilege beyond a communication to one actually involved in the proceeding, either as judge, attorney, party or witness. On the other hand, it has been held that such absolute privilege will not attach to counsel's extrajudicial publications, related to the litigation, which are made outside the purview of the judicial proceeding. . . . Nor will the attorney be privileged for actionable words spoken before persons in no way connected with the proceeding. [The court discusses several cases.]

All of the above cited cases make it obvious that aside from any question of ethics, an attorney who wishes to litigate his case in the press will do so at his own risk. We hold that appellee had no absolute privilege in regard to the statement made by him to the newspaper.

However, the argument is made (and the language of the trial court's opinion shows that it was persuasive there) that the forum had been chosen by the State's Attorney, and not by appellee, and that he had a right, perhaps even a duty to his client, to publish the statement in question. This argument raises indirectly the contention that because of the attorney client relationship, at least a qualified privilege existed in the absence of a showing of malice or abuse of the privilege.

[The court then denied that the appellee had met the requirements for a qualified privilege defeasible on proof of malice.] . . . Other steps more consonant with Canon 20, Canons of Professional Ethics, were open to appellee. He could have requested the transfer of Humphreys to the jail of another jurisdiction for safekeeping until trial. He could have sought to have the objectionable matter, contained in the proposed article, kept out of publication. Even if this attempt were unsuccessful, other tactics were possible to the attorney who eventually defended the case, e.g., a request for change of venue, voir dire examination of prospective

jurors in regard to the article, and preservation of the question of the prejudicial effect of the article, for appellate review.

[The court concluded that even though it "disapproved" of the actions of the State's Attorney, the appellees' claims for absolute and qualified privilege had to be denied. Yet owing to the unsettled state of the law, it held that on retrial the jury could consider the defendant's good faith on the question of mitigation of damages.]

. . .

For the reasons stated, the granting of a directed verdict for appellee was erroneous and the case should have been submitted to the jury.

## NOTES

**1.** ***Litigating in the Press.*** The *Kennedy* adage — lawyers who try their cases in the media do so at their peril — retains its vitality. But distinctions are made. In Norman v. Borison, 17 A.3d 697 (Md. 2011), Harrell, J., extended the absolute privilege to the republication of incomplete judicial proceedings to the press and on the Internet in a putative class action case. Attorneys in the case provided to the press a copy of their complaint before it was filed, along with verbal "sound bites" for potential articles. Distinguishing *Kennedy*, Harrell, J., noted that the attorneys "were not attempting to set up a slanderous defense to the allegation of rape or some other crime in the press." Instead, "[b]y republishing or reporting on those erstwhile pleadings, the press could be seen as a tool assisting in the notification to potential class members of the contemplated proceedings." The justification was sweeping:

> We extend the absolute privilege to [extrinsic, out-of-court statements] for the traditional reason — to encourage the free divulgence of information in pursuit of justice. More specifically, we apply the privilege because "the evaluation and investigation of facts and opinions for the purpose of determining what, if anything, is to be raised or used in pending litigation is as integral a part of the search for truth . . . as is the presentation of such facts and opinions during the course of the trial."

But with a significant caveat: "[B]ut for the fact that the mortgage rescue scam suit was striving to become a class action, our conclusion might have been different." Can framing a suit as a class action provide cover for funneling defamatory statements to the press?

**2.** ***Scope of the Absolute Privilege.*** The common law courts have long recognized that the absolute privilege extends without doubt to judges in the course of official business, to lawyers for conduct both preliminary to and in the course of judicial proceedings, and to parties to judicial proceedings. RST §§585–87. But courts continue to grapple with the question of the privilege's scope. In Barker v. Huang, 610 A.2d 1341, 1345–46 (Del. 1992), the court rebuffed the plaintiff's invitation to create an exception for sham statements made in the course of litigation. Horsey, J., wrote:

> To allow claims of defamation in the context of judicial proceedings to proceed to costly discovery in an attempt to ferret out facts purporting to show a sham nature to the litigation would largely defeat the purpose of the privilege. Moreover, sufficient sanctions already exist to deter and punish frivolous litigation. We therefore hold that no "sham litigation" exception to the defense of absolute privilege exists under the law of Delaware.

In Lewis v. Crochet, 105 F.4th 272, 284 (5th Cir. 2024), the plaintiff worked as an assistant athletic director at Louisiana State University who hired and managed student workers in the team's administrative office. There she both saw and experienced various actions of sexual harassment committed by the head football coach, Les Miles, that were not examined by the

heads of athletic departments. In the course of its investigations, LSU hired the defendant's law firm to investigate the matter, and it retained various documents pertaining to the investigation. Lewis then invoked the crime-fraud exception to the attorney-client privilege to obtain those documents, but she was rebuffed by Stewart, J., who held that "Lewis presented no evidence that the Board sought to fraudulently conceal public records through the attorney-client relationship. Thus, we conclude that the district court clearly erred in determining that the Boards sought Appellants' counsel 'for advice that would assist it in carrying out a contemplated illegal or fraudulent scheme.'" Are there any cases where document retention could invoke the crime-fraud exception? Marc I. Steinberg & Logan J. Weissler, The Litigation Privilege as a Shelter for Miscreant Legal Counsel, 97 Or. L. Rev. 1, 49 (2018), thinks so.

**3. *Other Governmental Bodies.*** In what other settings are statements absolutely privileged? This basic question has been raised countless times in the modern administrative state about bodies that have complex internal procedures. Thus in Craig v. Stafford Construction Co., 856 A.2d 372, 382 (Conn. 2004), the plaintiff Craig was a police officer who claimed that the defendant company and its employee "had defamed him when they filed a citizen complaint with the [internal affairs division of the Hartford Police] department alleging that he had directed racial slurs toward them at a construction site." The plaintiff was charged with "conduct unbecoming of a police officer." The court found that "[d]uring the investigatory process, Ramistella [the employee] made a false statement" regarding the incident and thereafter withdrew his complaint. Several months later the plaintiff was found not guilty.

A unanimous court held that the extensive procedures — including taking sworn statements from witnesses and the accused and preparing an extensive report subject to internal review — created a quasi-judicial proceeding in which the charging witnesses were protected by an absolute privilege.

> [A]lthough we recognize the debilitating affect [sic] that a false allegation of racial discrimination can have on a police officer, we conclude that the policy of encouraging citizens' complaints against those people who wield extraordinary power within the community outweighs the need to protect the reputation of the police officer against whom the complaint is made.

Should the rule be relaxed when the defendant admits to a false statement? Similarly, all reports that private individuals make to police officers about possible criminal activity of other private parties are also treated as communications "made preliminary to a proposed judicial proceeding." RST §587, cmt. *b*. See, e.g., Correllas v. Viverios, 572 N.E.2d 7, 13 (Mass. 1991), defending this rule on the ground that any witness has a strong incentive to tell the truth, for "[b]y implicating the plaintiff, the defendant knew that she would have to repeat her accusations at the plaintiff's trial, and do so under oath, subjecting herself to possible perjury for any false testimony."

But the absolute privilege has not been extended to police officers' own investigatory reports. In Dear v. Devaney, 983 N.E.2d 240, 246–47 (Mass. App. Ct. 2013), Kafker, J., held that statements — including "speculation" and "recounting of unidentified hearsay" — made by police officers during the investigation, not prosecution, of license suspension proceedings were not protected by an absolute privilege. Kafker, J., relied heavily on the fact that "as he was neither a party nor a witness at the proceeding, Dear had no opportunity to test the validity of the statements at the proceeding."

States are divided on the type of privilege accorded to hospital peer review committees that evaluate — often in response to individual complaints — the performance of staff physicians. Franklin v. Blank, 525 P.2d 945, 946 (N.M. App. 1974), held that both a letter written to initiate peer review and the peer review process at common law were shielded by an absolute privilege. "The appropriate professional societies, by exercising peer review, can and do perform a great public service by exercising control over those persons placed in a position

of public trust but nevertheless unfit to bear that responsibility." But in DiMiceli v. Klieger, 206 N.W.2d 184 (Wis. 1973), the court recognized only a qualified privilege. Today, most states have specific statutes that supply some privilege for peer review proceedings. Thus Fla. Stat. Ann. §766.101 (West 2024) protects a peer review committee member, or health care provider who gives information to a peer review committee, when "the committee member or health care provider acts without intentional fraud." Further amendments limit the use that can be made in court of information presented to a peer review committee. In contrast, Cal. Civ. Code §47 (West 2024) extends the privilege to "any other official proceeding authorized by law," with unrelated exceptions.

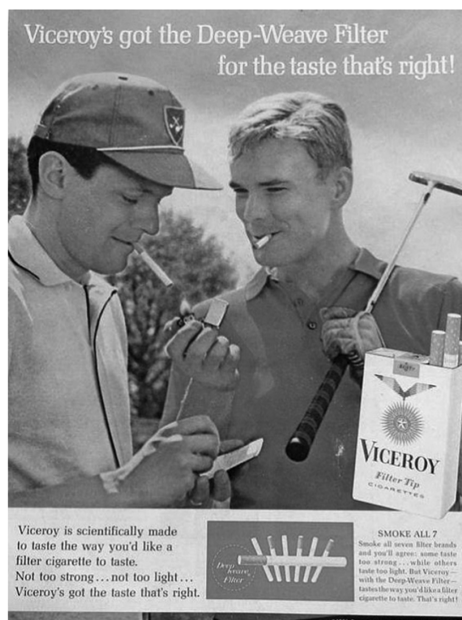
For bodies that look less like courts and more like political fora, a conditional privilege is the norm. In Park Knoll Associates v. Schmidt, 451 N.E.2d 182, 183 (N.Y. 1983), the court, with two judges dissenting, held that the president of a tenant's association did *not* enjoy absolute privilege from liability, as he was not an attorney, party, or witness in a judicial or quasi-judicial proceeding. Likewise a claim for absolute privilege was rebuffed in Ezekiel v. Jones Motor Co., Inc., 372 N.E.2d 1281, 1285 (Mass. 1978), when the defendant's employee, testifying before a joint management-union grievance board, falsely accused the plaintiff of stealing company property.

For a still classic discussion, see Van Vechten Veeder, Absolute Immunity in Defamation: Judicial Proceedings, 9 Colum. L. Rev. 463 (1909).

### *b. Reports of Public Proceedings or Meetings*

## *Brown & Williamson Tobacco Corp. v. Jacobson*

713 F.2d 262 (7th Cir. 1983)




**A Viceroy cigarette advertisement from 1964**

*Source: Viceroy*

Posner, J.

This diversity suit brought by Brown & Williamson, the manufacturer of Viceroy cigarettes, charges CBS and Walter Jacobson with libel and other violations of Illinois law. Jacobson is a news commentator for WBBM-TV, a Chicago television station owned by CBS. [In 1975, the Ted Bates advertising agency teamed up with the Kennan market-research firm to develop a strategy for selling Viceroys to young people by placing smoking in the same "illicit pleasure category" as "wine, beer, shaving, wearing a bra (or purposely not wearing one)." Brown & Williamson promptly rejected the entire approach and fired Ted Bates "primarily because of displeasure with the proposed strategy."] In 1981 the Federal Trade Commission published a report that discussed the Kennan report and announced that "B & W adopted many of the ideas contained in this report in the development of a Viceroy

advertising campaign," and quoted passages from a "Viceroy Strategy" Report of 1976 which states: "The marketing efforts must cope with consumers' attitudes about smoking and health, either providing them a *rationale* for smoking a full flavor VICEROY or providing a means of *repressing* their concerns about smoking a full flavor VICEROY." In November 1981 a CBS reporter spoke with a representative of Viceroy about the initial 1975 campaign and was told that the company had rejected the proposal and had fired the Ted Bates agency. Some ten days later, and again in March 1982, Walter Jacobson broadcast a show in which he accused the "killer business" of going to Madison Avenue for help in hooking young people to smoke. As part of that segment Jacobson said:

> Well, there is a confidential report on cigarette advertising in the files of the Federal Government right now, a Viceroy advertising, the Viceroy strategy for attracting young people, starters they are called, to smoking—"FOR THE YOUNG SMOKER. . . . A CIGARETTE FALLS INTO THE SAME CATEGORY WITH WINE, BEER, SHAVING OR WEARING A BRA. . . ." says the Viceroy strategy—"A DECLARATION OF INDEPENDENCE AND STRIVING FOR SELF-IDENTITY." Therefore, an attempt should be made, says Viceroy, to ". . . PRESENT THE CIGARETTE AS AN INITIATION INTO THE ADULT WORLD," to ". . . PRESENT THE CIGARETTE AS AN ILLICIT PLEASURE . . . A BASIC SYMBOL OF THE GROWING-UP, MATURING PROCESS." An attempt should be made, say the Viceroy slicksters, "TO RELATE THE CIGARETTE TO 'POT,' WINE, BEER, SEX. DO NOT COMMUNICATE HEALTH OR HEALTH-RELATED POINTS." That's the strategy of the cigarette slicksters, the cigarette business which is insisting in public, "We are not selling cigarettes to children."
>
> They're not slicksters, they're liars.

While Jacobson is speaking these lines the television screen is showing Viceroy ads published in print media in 1980. Each ad shows two packs of Viceroys alongside a golf club and ball. . . .

Under contemporary as under traditional Illinois law, Jacobson's broadcast is libelous per se. Accusing a cigarette company of what many people consider the immoral strategy of enticing children to smoke—enticing them by advertising that employs themes exploitive of adolescent vulnerability—is likely to harm the company. It may make it harder for the company to fend off hostile government regulation and may invite rejection of the company's product by angry parents who smoke but may not want their children to do so. These harms cannot easily be measured, but so long as some harm is highly likely the difficulty of measurement is an additional reason, under the modern functional approach of the Illinois courts, for finding libel per se rather than insisting on proof of special damage. . . .

The defendants also argue and the district court also found that the libel was privileged as a fair and accurate summary of the Federal Trade Commission staff's report on cigarette advertising. The parties agree as they must that Illinois recognizes a privilege for fair and accurate summaries of, or reports on, government proceedings and investigations. They agree that the privilege extends to a public FTC staff report on an investigation. But they disagree over whether Jacobson's summary of the FTC staff report was "fair," that is, whether the overall impression created by the summary was no more defamatory than that created by the original. See Restatement (Second) of Torts §611, comment *f* (1977). Since this is a question of fact, and the case was dismissed on the pleadings, all we need decide is whether the fairness of the Jacobson summary emerges so incontrovertibly from a comparison of the FTC staff report with the broadcast that no rational jury considering these documents with the aid of whatever additional evidence Brown & Williamson might introduce could consider the summary unfair. . . .

The fact that there are discrepancies between a libel and the government report on which it is based need not defeat the privilege of fair summary. Unless the report is published verbatim it is bound to convey a somewhat different impression from the original, no matter how

carefully the publisher attempts to summarize or paraphrase or excerpt it fairly and accurately. An unfair summary in the present context is one that amplifies the libelous effect that publication of the government report verbatim would have on a reader who read it carefully—that carries a "greater sting." The FTC staff report conveys the following message: six years ago a market-research firm submitted to Brown & Williamson a set of rather lurid proposals for enticing young people to smoke cigarettes and Brown & Williamson adopted many of its ideas (though not necessarily the specific proposals quoted in the report) in an advertising campaign aimed at young smokers which it conducted the following year. The Jacobson broadcast conveys the following message: Brown & Williamson currently is advertising cigarettes in a manner designed to entice children to smoke by associating smoking with drinking, sex, marijuana, and other illicit pleasures of youth. So at least a rational jury might interpret the source and the summary, and if it did it would be entitled to conclude that the summary carried a greater sting and was therefore unfair.

[Reversed and remanded.]

## NOTES

**1.** ***Brown & Williamson on Remand.*** At trial, Brown & Williamson recovered $3 million in actual damages and over $2 million in punitive damages of which $50,000 were against Jacobson personally and the rest against CBS. The trial judge found that there were no significant actual damages and thus awarded nominal damages of $1. On appeal this amount was increased to $1 million and the punitive damages award was preserved. Brown & Williamson Tobacco Corp. v. Jacobson, 827 F.2d 1119 (7th Cir. 1987).

**2.** ***English Origins of the Fair Reporting Privilege.*** In general the privilege of "record libel"—the traditional term for the fair report privilege—is accorded to persons who publish to the world statements that previously have been made on the public record. In one famous early case, Stockdale v. Hansard, 112 Eng. Rep. 1112 (Q.B. 1839), the court held that a parliamentary report, even though published by Hansard at the direct request of Parliament, was not privileged. That decision was immediately overturned by legislation. See Parliamentary Papers Act, 1840, s. 4. It was not, however, until Wason v. Walter, 4 Q.B. 73 (1868), that the privilege was extended to proceedings of Parliament voluntarily republished by the press. This decision smacked of judicial legislation as Parliament had twice previously refused to create a privilege for such reports. In his opinion, Cockburn, C.J., noted that the privilege was well-established for judicial proceedings, and that it was "of paramount public and national importance that the proceedings of the houses of parliament shall be communicated to the public" in order that "confidence" be maintained in the legislative process. Today in England the privilege extends not only to reports of parliamentary proceedings but to those of administrative bodies as well. See, e.g., Perera v. Peiris, [1949] A.C. 1 (P.C.).

**3.** ***Scope of the Privilege in the United States.*** In this country, the record libel (or "fair reporting") privilege always applied to reports of legislative, judicial, and administrative proceedings, and was quickly extended to various functions performed by "quasi-public" bodies.

Clark, J., confirmed the absolute nature of the privilege in Funk v. Scripps Media, Inc., 570 S.W.3d 205 (Tenn. 2019), reasoning that "when a statement is made in a judicial proceeding, the statement is worthy of public notice, not only as a result of the contents of the statement, but also because of the context in which the statement was made." Allowing the privilege to be defeated upon showing of actual malice would thus undermine the purpose of the privilege, including "lessen[ing] the public's opportunities to be 'apprised of what takes place in the proceedings without having been present'" and "assess[ing] the value of our government in action."

**RESTATEMENT OF THE LAW (SECOND) OF TORTS**

**§611. Report of Official Proceeding or Public Meeting**

The publication of defamatory matter concerning another in a report of an official action or proceeding or of a meeting open to the public that deals with a matter of public concern is privileged if the report is accurate and complete or a fair abridgement of the occurrence reported.

***Comment f. Accuracy and Fairness of Report:*** The rule stated in this Section requires the report to be accurate. It is not necessary that it be exact in every immaterial detail or that it conform to that precision demanded in technical or scientific reporting. It is enough that it conveys to the persons who read it a substantially correct account of the proceedings.

Not only must the report be accurate, but it must be fair. Even a report that is accurate so far as it goes may be so edited and deleted as to misrepresent the proceeding and thus be misleading. . . .

## *Medico v. Time, Inc.*

643 F.2d 134 (3d Cir. 1981)

Adams, J. This appeal from a summary judgment in favor of the defendant presents an important question concerning the law of defamation. We must review the district court's determination that a news magazine enjoys a privilege, under the common law of Pennsylvania, to publish a summary of FBI documents identifying the plaintiff as a member of an organized crime "family." We affirm.

In its March 6, 1978 issue, Time magazine published an article describing suspected criminal activities of then-Congressman Daniel J. Flood. [The court excerpted the article, which detailed how Congressman Flood purportedly directed government business toward the Medico family.]

. . . [A]fter an exhaustive analysis of Pennsylvania precedents, the [district] court concluded that Pennsylvania courts, if presented with the question, would find summaries of non-public government reports within the privilege. The district judge then ascertained that the Time article represented a fair and accurate account of the FBI documents. Accordingly he held that the publication was privileged, and awarded summary judgment in favor of Time. . . .

Unlike many states, Pennsylvania has never codified the fair report privilege. . . . We believe it appropriate to accept as the law of Pennsylvania the version of the fair report privilege embodied in [Restatement (Second) Section 611: Report of Official Proceeding or Public Meeting].

. . . To ameliorate the chilling effect on the reporting of newsworthy events occasioned by the combined effect of the republication rule and the truth defense, the law has long recognized a privilege for the press to publish accounts of official proceedings or reports even when these contain defamatory statements. So long as the account presents a fair and accurate summary of the proceedings, the law abandons the assumption that the reporter adopts the defamatory remarks as his own. . . . Medico contends before this Court that the FBI documents should not be deemed "official" because they express only tentative and preliminary conclusions that the FBI has never adopted as accurate. . . . FBI files seem at least as "official" as the pleadings in civil cases. Although civil complaints are instituted, for the most part, by private parties, the FBI documents concerning Medico were compiled by government agents acting in their official capacities. . . .

. . . Three policies underlie the fair report privilege, and an examination of them provides further guidance for our decision today. Initially, an agency theory was offered to rationalize a privilege of fair report: one who reports what happens in a public, official proceeding acts as an agent for persons who had a right to attend, and informs them of what they might have seen for themselves. The agency rationale, however, cannot explain application of the privilege to proceedings or reports not open to public inspection.

A theory of public supervision also informs the fair report privilege. . . . We believe the public supervision rationale applies to the present case. As public inspection of courtroom proceedings may further the just administration of the laws, public scrutiny of the proceedings and records of criminal investigatory agencies may often have the equally salutary effect of fostering among those who enforce the laws "the sense of public responsibility." . . . [We need not] decide, however, whether the supervisory rationale is relevant to every republication of documents found in FBI files. For any general supervisory concern with respect to the FBI is heightened in the present case by the public interest in examining the conduct of the individuals it elects to positions of public trust. . . .

A third rationale for the fair report privilege rests, somewhat tautologically, on the public's interest in learning of important matters. . . . The Time article discussed two topics of legitimate public interest. First, . . . examination of the affairs of elected officials is obviously a matter of legitimate public concern. In addition, . . . there is significant public importance to reports on investigations of organized criminal activities, whether or not these implicate government officials. . . . In light of the difficulty in obtaining independent corroboration of FBI information, the press may often have to rely on materials the government acquires if it is to report on organized crime at all. We believe Time's publication of FBI materials concerning Medico served a legitimate public interest in learning about organized crime. . . .

. . . Once the libel defendant establishes the existence of a "privileged occasion" for the publication of a defamatory article, the burden returns to the plaintiff to prove that the defendant abused its privilege. . . . Pennsylvania law recognizes two forms of "abuse": the account of an official report may fail to be fair and accurate, . . . or the defamatory material may be published for the sole purpose of causing harm to the person defamed. . . .

. . . We agree with the district court that nothing in the record suggests that the Time article unfairly or inaccurately reported on the FBI materials. . . . Time has accurately portrayed the FBI records as indicating that Medico has been identified as part of the Bufalino crime family.

## NOTES

**1.** ***Rationales for Fair Reporting Privilege.*** As *Medico* makes clear, three policy rationales support the privilege. The agency rationale protects the press when it reports on official actions and statements that members of the public could have witnessed for themselves. The public supervision rationale allows the news media to serve as a check on the power of government. The general public interest rationale applies to media reports of important but not official actions.

Does *Medico* raise concerns that the privilege may sweep too broadly? Note that the *Medico* court describes the rationale for the fair reporting privilege which rests on the public's interest in learning of important matters as tautological. To be sure, the law enforcement records in *Medico* were not easily accessible to the general public, and the press served an important conduit function. But it is hardly difficult to imagine a situation where the information serving as the basis for a press report is more readily accessible — something less tantalizing and secretive

than mafia investigations. Should the press be able to rely on the public's right to know even where information is more accessible to the general public and the press retreats from its conduit function? Should these considerations change in the digital age? Are matters of public importance the same as matters of "public concern" under *Gertz*, *Hepps*, and the like?

**2. *Fair and Accurate?*** Much litigation has also focused on the requirement that the defendant's statement be a fair and accurate statement or abridgment of the official proceedings. The record libel privilege at common law applies "even if the reporter of defamatory statements made in court believes or knows them to be false; the privilege is abused only if the report fails the test of fairness or accuracy." Rosenberg v. Helinski, 616 A.2d 866, 873 (Md. 1992).

The reporter (or indeed any other person who narrates the event) does not waive the privilege because he refuses to become a commentator as well. Nor does reliance on anonymous sources per se destroy the privilege. But in many respects the privilege is circumscribed. In Howell v. Enterprise Publishing Co., 920 N.E.2d 1 (Mass. 2010), the court applied the absolute privilege of RST §611 to reports from anonymous sources that described nonpublic, closed-door proceedings that led to the termination of a sewage commissioner for possession of lewd photographs and videos on his work computer, but warned that "a report based on [an unofficial or anonymous] source runs a risk that the underlying official action will not be accurately and fairly described by the source, and therefore will not be protected." In Moreno v. Crookston Times Printing Co., 610 N.W.2d 321 (Minn. 2000), the court applied the absolute privilege to a fair and accurate report of remarks made to the city council but refused to apply it insofar as the article "included material reporting on events other than those that occurred at the city council meeting."

### *c. Fair Comment: Artistic and Literary Criticism*

The common law privilege of fair comment extended to all matters in the public eye, thereby allowing the defendant to express defamatory opinions on matters of public interest. This privilege extended to statements about public officials and candidates for public office; about educational, charitable, and religious institutions; about quasi-public institutions such as bar and medical associations; about sporting games and contests; and about artistic, literary, and scientific matters generally. The cardinal distinction under the common law privilege is between fact and opinion; the defense of fair comment applied only to the latter. For the line between fact and opinion, see Veeder, *infra* at 380. To be sure, a substantial minority of states held that the privilege applied to false statements of fact as well as to statements of opinion. See Dix W. Noel, Defamation of Public Officers and Candidates, 49 Colum. L. Rev. 875, 877–80 (1949). For the best exposition of this position at common law, see Coleman v. MacLennan, 98 P. 281 (Kan. 1908). The leading decision in support of the majority view was written by William Howard Taft, later President of the United States and Chief Justice of the U.S. Supreme Court, when he was a judge on the Court of Appeals. See Post Publ'g Co. v. Hallam, 59 F. 530 (6th Cir. 1893).

The leading common law decision on fair comment was Carr v. Hood, 170 Eng. Rep. 981, 983 (K.B. 1808), a libel action that arose from savage criticism of Sir John Carr's book *The Stranger in Ireland*. Lord Ellenborough rebuffed the action as follows:

> Here the supposed libel has only attacked those works of which Sir John Carr is the avowed author; and one writer in exposing the follies and errors of another may make use of ridicule, however poignant. Ridicule is often the fittest weapon that can be employed for such a purpose. If the reputation or pecuniary interests of the person ridiculed suffer, it is damnum absque injuria. Where is the liberty of the press if an action can be maintained on such principles? Perhaps the plaintiff's *Tour through Scotland* is now unsaleable; but is he to be indemnified by

> receiving a compensation in damages from the person who may have opened the eyes of the public to the bad taste and inanity of his compositions? Who would have bought the works of Sir Robert Filmer after he had been refuted by Mr. Locke? But shall it be said that he might have sustained an action for defamation against that great philosopher, who was labouring to enlighten and ameliorate mankind? We really must not cramp observations upon authors and their works. They should be liable to criticism, to exposure, and even to ridicule, if their compositions be ridiculous; otherwise the first who writes a book on any subject will maintain a monopoly of sentiment and opinion respecting it. This would tend to the perpetuity of error.—Reflection on personal character is another thing. Shew me an attack on the moral character of this plaintiff, or any attack upon his character unconnected with his authorship, and I shall be as ready as any judge who ever sate here to protect him; but I cannot hear of malice on account of turning his works into ridicule.

Lord Ellenborough himself was taken to task for giving the privilege too narrow a scope in George Spencer Bower, A Code of the Law of Actionable Defamation 383 (1908):

> Nothing could be more misleading than the above [opinion], which assumes not that honest comment is justified, because it is comment, but that the author is to be punished for "the bad taste and inanity of his compositions," [for] the sole justification, of the protection is the freedom of *any* man, however worthless his observations may be, to criticize with the severity he pleases (provided that he does not stray beyond the assigned limits of comment into the region of personal imputation) the public conduct or the published work, however exalted or brilliant the rest of the world may deem it, of *any* other man. Sir Robert Filmer had the same right to criticize Locke, as Locke had to criticize him. The fact that one criticism may demolish the author, and another the critic himself, is utterly irrelevant to the question of the legal right.

The early decisions faithfully adhered to the distinction between criticisms of the book and the author. Thus, in Cherry v. Des Moines Leader, 86 N.W. 323, 323 (Iowa 1901), the court extended fair comment privilege to a vicious review of the plaintiff's three-sister vaudeville act, which described it as being performed by "strange creatures with painted faces and hideous mien." But in Triggs v. Sun Printing & Publishing Association, 71 N.E. 739 (N.Y. 1904), the court, consistent with *Carr*, let the jury decide whether ridicule about the private life of Professor Oscar Lovell Triggs of the English Department of the University of Chicago strayed into forbidden personal territory by stating, for example, "that he was unable to select a name for his baby until after a year of solemn deliberation." What happens to the public/private distinction after *New York Times*?

**Van Vechten Veeder**

## *Freedom of Public Discussion*

23 Harv. L. Rev. 413, 419–20 (1910)

The distinction is fundamental, then, between comment upon given facts and the direct assertion of facts. And the significance of the distinction is plain. If the facts are stated separately, and the comment appears as an inference drawn from those facts, any injustice that the imputation might occasion is practically negatived by reason of the fact that the reader has before him the grounds upon which the unfavorable inference is based. When the facts are truthfully stated, comment thereon, if unjust, will fall harmless, for the former furnish a ready antidote for the latter. The reader is then in a position to judge whether the critic has not by his unfairness or prejudice libelled himself rather than the object of his animadversion. But if a bare statement is made in terms of a fact, or if facts and comment are so intermingled that it is not clear what purports to be inference and what is claimed to be fact, the reader will

naturally assume that the injurious statements are based upon adequate grounds known to the writer. In one case, the insufficiency of the facts to support the inference will lead fair-minded men to reject it; in the other, there is little, if any, room for the supposition that the injurious statement is other than a direct change of the fact, based upon grounds known to the writer, although not disclosed by him.

## NOTES

**1.** ***The Fact/Opinion Distinction at Work.*** The elusive line between fact and opinion retains its importance today, for while a plaintiff may recover for false statements of fact upon proof of actual malice, statements of opinion are protected by an absolute privilege. In policing that line, courts continue to rely on Veeder's early formulation. By way of illustration, the Massachusetts Supreme Judicial Court wrote: "[I]f I write, without more, that a person is an alcoholic, I may well have committed a libel prima facie; but it is otherwise if I write that I saw the person take a martini at lunch and accordingly state that he is an alcoholic." Nat'l Ass'n of Gov't Emps., Inc. v. Cent. Broad. Co., 396 N.E.2d 996, 1001 (Mass. 1979). That analogy proved persuasive in Beattie v. Fleet National Bank, 746 A.2d 717 (R.I. 2000). The defendant had issued a derogatory letter criticizing a real estate appraisal that Beattie had submitted to the bank, which

> faulted the comparable sales data he had relied upon to arrive at his valuation of the subject property. The bank's appraiser concluded the letter by stating that "in the aggregate, the data in this [appraisal] report combines to present such a misleading indication of the value of this property as to be considered fraudulent." The writer's opinion, however, was based upon disclosed, non-defamatory facts, including a seven-page memorandum enclosed with the letter that detailed the appraisal's perceived deficiencies. As a result, we hold that it did not constitute an actionable-defamatory communication.

**2.** ***Political Disputation.*** The stakes are often raised for the fact/opinion line in disputes with political overtones. Ollman v. Evans, 750 F.2d 970, 986 (D.C. Cir. 1984), arose from an Evans and Novak column in November 1978, called "The Marxist Professor's Intentions," that protested the planned move of the plaintiff, a Marxist, to the Department of Government and Politics at the University of Maryland. The column first attacked Ollman for using the classroom as a forum to promote "revolution" and labeled him "an outspoken proponent of political Marxism." It recounted how he had finished last of 16 candidates in an election for the council to the American Political Science Association, running under the party name of the Caucus for a New Political Science. Further it described Ollman's principal book, *Alienation: Marx's Conception of Man in Capitalist Society*, as a "ponderous tome."

Drawing heavily on common law precedents, Starr, J., proposed the following four-part test to elucidate the distinction between fact and opinion, with its clear constitutional overtones.

> Four constituent elements point to a given statement being one of fact: first, the proposition contains a "core meaning" understood by its intended audience; second, the proposition is "verifiable" by objective tests; third, the context increases the willingness to infer that the statement has a factual context; and fourth, the broader context is one that stresses fact or narrative, as opposed to editorials and reviews, where the reader expects greater latitude from the author. . . .
>
> The reasonable reader who peruses an Evans and Novak column on the editorial or Op-Ed page is fully aware that the statements found there are not "hard" news like those printed on the front page or elsewhere in the news sections of the newspaper. Readers expect that columnists will make strong statements, sometimes phrased in a polemical manner that would hardly be considered balanced or fair elsewhere in the newspaper. That proposition is inherent in the very notion of an "Op-Ed" page.

Bork, J., concurred to voice his worry about the onslaught of new libel actions, but he also expressed his impatience with "such things as four-factor frameworks, three-pronged tests, and two-tiered analyses," and urged a return to "first principles." He concluded that the column should be protected because "a damage award would have a heavily inhibiting effect upon the journalism of opinion."

The *Ollman* four-part test has nonetheless withstood the test of time. In rebuffing a defamation claim brought by a political activist against a journalist in Fairbanks v. Roller, 314 F. Supp. 3d 85, 90 (D.D.C. 2018), McFadden, J., explained that the *Ollman* factors tipped against finding defamatory a caption ("just two people doing a white power hand gesture in the White House") in a retweeted photo of the activist in front of the White House press room making a gesture that could be interpreted alternately as an "okay" hand symbol or "white power" symbol.

**3. *Restaurant Reviews.*** *Ollman* proved influential in Mr. Chow of New York v. Ste. Jour Azur, S.A., 759 F.2d 219, 227–28 (2d Cir. 1985). The defendant restaurant guide published a review (in French) that castigated the plaintiff's restaurant because, inter alia, "[i]t is impossible to have the basic condiments . . . on the table," "the sweet and sour pork contained more dough . . . than meat," "the green peppers . . . remained still frozen on the plate," and the Peking duck "was made up of only one dish (instead of the three traditional ones)." The guide defended its review in part as containing statements of opinion and not of fact. A skeptical jury awarded the plaintiff $20,000 in actual damages and $5 million in punitive damages, which were sustained by the trial judge. On appeal Meskill, J., applied the analysis of fact and opinion adopted by Starr, J., in *Ollman* and held that the review constituted protected opinion:

> Restaurant reviews are also [like the Evans and Novak column] the well recognized home of opinion and comment. Indeed, "by its very nature, an article commenting upon the quality of a restaurant or its food, like a review of a play or movie, constitutes the opinion of the reviewer." . . . The natural function of the review is to convey the critic's opinion of the restaurant reviewed: the food, the service, the decor, the atmosphere, and so forth. Such matters are to a large extent controlled by personal tastes. The average reader approaches a review with the knowledge that it contains only one person's views of the establishment. And importantly, "[a]s is essential in aesthetic criticism . . . the object of the judgment is available to the critic's audience." Appellee does not cite a single case that has found a restaurant review libelous. Appellants and *amici* on the other hand cite numerous decisions that have refused to do so. Although the rationale of each of these decisions is different, they all recognize to some extent that reviews, although they may be unkind, are not normally a breeding ground for successful libel actions.

The court then held that the statement about the Peking duck was an assertion of fact. "The statement is not metaphorical or hyperbolic; it clearly is laden with factual content." The plaintiff's victory on the point was bittersweet, however, because the false statement about the Peking duck was found protected by the actual malice rule, applicable because the restaurant was considered a public figure.

What if the condiments were always on the table, the sweet and sour pork was encased in a thin, delicate dough, and the green peppers were cooked perfectly? Does it make a difference that customers are free to patronize the restaurant if none will spend $40 or more for a dinner after reading that review?

Consider Pegasus v. Reno Newspapers, Inc. 118 Nev. 706, 717 (Nev. 2003), where the restaurant owner plaintiffs sued over a restaurant review that falsely claimed that the restaurant was serving prepackaged dishes and canned beans instead of using fresh ingredients. Although the restaurant provided invoices proving that it had used fresh ingredients in the preparation of its food, the court nevertheless ruled that the review was a statement of opinion. With

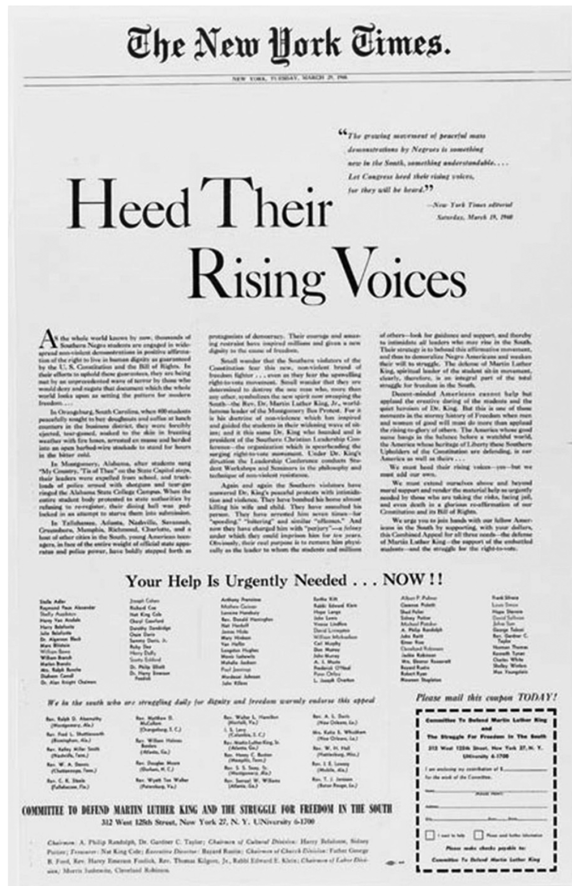
regard to the dishes, the court ruled that "the statement that the food came from a package, taken in context together with the tenor of the entire work, is an expression of opinion." Although the claim of canned beans presented a closer issue for the court, it similarly ruled that the statement was an expression of opinion because "in the context of the entire review, a reasonable person would understand the statement to be an expression of [the reviewer's] belief that canned beans had been used in the preparation of the food." Would the court reach the same conclusion if it had employed the *Ollman* four-part test in the case above? What weight should be given to the distinction between fact and opinion if the expression of a false fact, such as in this case, may be treated as a statement of opinion by courts?

## SECTION H. CONSTITUTIONAL PRIVILEGES

### 1. Public Officials and Public Figures

#### *New York Times Co. v. Sullivan*

376 U.S. 254 (1964)




**The advertisement at issue in New York Times v. Sullivan**

*Source: National Archives*

Brennan, J. We are required in this case to determine for the first time the extent to which the constitutional protections for speech and press limit a State's power to award damages in a libel action brought by a public official against critics of his official conduct.

[The plaintiff-respondent, L.B. Sullivan, was one of three elected Commissioners of Montgomery, Alabama, who claimed that he was defamed in a full-page ad, costing $4,800, taken out in the *New York Times* on March 29, 1960. The ad was entitled "Heed Their Rising Voices," and it charged in part that an "unprecedented wave of terror" had been directed against those who participated in the civil rights movement in the South. The letter was signed by 64 prominent members of the civil rights movement and contained statements in two key paragraphs that were said to be defamatory:

Third paragraph:

"In Montgomery, Alabama, after students sang 'My Country,' Tis of Thee' on the State Capitol

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steps, their leaders were expelled from school, and truckloads of police armed with shotguns and tear-gas ringed the Alabama State College Campus. When the entire student body protested to state authorities by refusing to re-register, their dining hall was padlocked in an attempt to starve them into submission."

Sixth paragraph:

"Again and again the Southern violators have answered Dr. King's peaceful protests with intimidation and violence. They have bombed his home almost killing his wife and child. They have assaulted his person. They have arrested him seven times—for 'speeding,' 'loitering' and similar 'offenses.' And now they have charged him with 'perjury'—a *felony* under which they could imprison him for *ten years*. . . ."

Although the ad did not mention Sullivan by name, he claimed that it referred to him by indirection because he had oversight responsibility of the police. Sullivan did not show that he suffered any special damages from the publication, but he claimed general damages for defamation. It was "uncontroverted" some of the particulars in the story were false: for example, the police had not ringed the campus, but were only deployed nearby; during the demonstration the students sang the National Anthem, not "My Country, 'Tis of Thee"; Dr. King had been arrested only four times, not seven; the nine students were expelled by the State Board of Education not for leading the demonstration, but "for demanding service at a lunch-counter at the Montgomery County Courthouse on another day." The jury awarded Sullivan $500,000 in damages and its decision was affirmed in the Alabama Supreme Court, 144 So. 2d 25 (1962).

Before publishing the ad, the Times had received a letter from A. Philip Randolph, chairman of the Committee, which certified that all the signatories had indeed signed the letter. Sullivan demanded a retraction of the letter from all parties, some of whom denied that they had authorized the use of their signatures. Those individual petitioners refused to retract the statements that they claimed they had never made; the *New York Times* wrote back, noting it was "puzzled" as to why Sullivan thought that the ad reflected adversely on him. This suit followed without further reply. The Times eventually published a retraction insofar as it applied to the Governor of Alabama, whom it believed could be seen as "the embodiment of the State of Alabama." At trial the jury found the advertisement libelous per se, and hence actionable without proof of malice or special damages. The $500,000 award followed, and the judgment was affirmed in all respects by the Alabama Supreme Court: "The First Amendment of the U.S. Constitution does not protect libelous publications" and "The Fourteenth Amendment is directed against State action and not private action." 144 So. 2d 25, 40 (1962).]

Because of the importance of the constitutional issues involved, we granted the separate petitions for certiorari of the individual petitioners and of the Times. We reverse the judgment. We hold that the rule of law applied by the Alabama courts is constitutionally deficient for failure to provide the safeguards for freedom of speech and of the press that are required by the First and Fourteenth Amendments in a libel action brought by a public official against critics of his official conduct. We further hold that under the proper safeguards the evidence presented in this case is constitutionally insufficient to support the judgment for respondent.

[The Court first discussed two preliminary issues: whether there was state action and whether the defendant's statement, as an advertisement, was beyond the protection of the First Amendment. It decided that the common law rule in Alabama constituted sufficient state action and that the statement was not a "commercial" advertisement but an "editorial" advertisement on an issue "of the highest public interest and concern." It then offered a summary of Alabama law, which followed the basic principles of defamation everywhere, and continued:]

The question before us is whether this rule of liability, as applied to an action brought by a public official against critics of his official conduct, abridges the freedom of speech and of the press that is guaranteed by the First and Fourteenth Amendments.

Respondent relies heavily, as did the Alabama courts, on statements of this Court to the effect that the Constitution does not protect libelous publications. Those statements do not foreclose our inquiry here. None of the cases sustained the use of libel laws to impose sanctions upon expression critical of the official conduct of public officials. . . . In deciding the question now, we are compelled by neither precedent nor policy to give any more weight to the epithet "libel" than we have to other "mere labels" of state law. Like insurrection, contempt, advocacy of unlawful acts, breach of the peace, obscenity, solicitation of legal business, and the various other formulae for the representation of expression that have been challenged in this Court, libel can claim no talismanic immunity from constitutional limitations. It must be measured by standards that satisfy the First Amendment. . . .

Thus we consider this case against the background of a profound national commitment to the principle that debate on public issues should be uninhibited, robust, and wide-open, and that it may well include vehement, caustic, and sometimes unpleasantly sharp attacks on government and public officials. The present advertisement, as an expression of grievance and protest on one of the major public issues of our time, would seem clearly to qualify for the constitutional protection. The question is whether it forfeits that protection by the falsity of some of its factual statements and by its alleged defamation of respondent.

Authoritative interpretations of the First Amendment guarantees have consistently refused to recognize an exception for any test of truth—whether administered by judges, juries, or administrative officials—and especially one that puts the burden of proving truth on the speaker. The constitutional protection does not turn upon "the truth, popularity, or social utility of the ideas and beliefs which are offered." N.A.A.C.P. v. Button, 371 U.S. 415, 445 (1963). As Madison said, "Some degree of abuse is inseparable from the proper use of everything; and in no instance is this more than in that of the press." 4 Elliot's Debates on the Federal Constitution (1876), p. 571. . . .

[E]rroneous statement is inevitable in free debate, and . . . it must be protected if the freedoms of expression are to have the "breathing space" that they "need . . . to survive." . . .

Injury to official reputation affords no more warrant for repressing speech that would otherwise be free than does factual error. Where judicial officers are involved, this Court has held that concern for the dignity and reputation of the courts does not justify the punishment as criminal contempt of criticism of the judge or his decision. Bridges v. California, 314 U.S. 252 (1941). This is true even though the utterance contains "half-truths" and "misinformation." Such repression can be justified, if at all, only by a clear and present danger of the obstruction of justice. If judges are to be treated as "men of fortitude, able to thrive in a hardy climate," surely the same must be true of other government officials, such as elected city commissioners. Criticism of their official conduct does not lose its constitutional protection merely because it is effective criticism and hence diminishes their official reputations.

If neither factual error nor defamatory content suffices to remove the constitutional shield from criticism of official conduct, the combination of the two elements is no less inadequate. This is the lesson to be drawn from the great controversy over the Sedition Act of 1798, 1 Stat. 596, which first crystallized a national awareness of the central meaning of the First Amendment. That statute made it a crime, punishable by a $5,000 fine and five years in prison, "if any person shall write, print, utter or publish . . . any false, scandalous and malicious writing or writings against the government of the United States, or either house of the Congress . . . , or the President . . . , with intent to defame . . . or to bring them, or either of them, into contempt or disrepute; or to excite against them, or either or any of them, the hatred of the good people of the United States." The Act allowed the defendant the defense of truth, and provided that the jury were to be judges both of the law and the facts. Despite these qualifications, the Act was vigorously condemned as unconstitutional in an attack joined in by Jefferson and Madison. . . .

Although the Sedition Act was never tested in this Court,[16] the attack upon its validity has carried the day in the court of history. Fines levied in its prosecution were repaid by Act of Congress on the ground that it was unconstitutional. See, e.g., Act of July 4, 1840, c. 45, 6 Stat. 802. . . .

There is no force in respondent's argument that the constitutional limitations implicit in the history of the Sedition Act apply only to Congress and not to the States. It is true that the First Amendment was originally addressed only to action by the Federal Government, and that Jefferson, for one, while denying the power of Congress "to control the freedom of the press," recognized such a power in the States. But this distinction was eliminated with the adoption of the Fourteenth Amendment and the application to the States of the First Amendment's restrictions. . . .

What a State may not constitutionally bring about by means of a criminal statute is likewise beyond the reach of its civil law of libel. The fear of damage awards under a rule such as that invoked by the Alabama courts here may be markedly more inhibiting than the fear of prosecution under a criminal statute. Alabama, for example, has a criminal libel law which subjects to prosecution "any person who speaks, writes, or prints of and concerning another any accusation falsely and maliciously importing the commission by such person of a felony, or any other indictable offense involving moral turpitude," and which allows as punishment upon conviction a fine not exceeding $500 and a prison sentence of six months. Alabama Code, Tit. 14, §350. Presumably a person charged with violation of this statute enjoys ordinary criminal-law safeguards such as the requirements of an indictment and of proof beyond a reasonable doubt. These safeguards are not available to the defendant in a civil action. The judgment awarded in this case — without the need for any proof of actual pecuniary loss — was one thousand times greater than the maximum fine provided by the Alabama criminal statute, and one hundred times greater than that provided by the Sedition Act. And since there is no double-jeopardy limitation applicable to civil lawsuits, this is not the only judgment that may be awarded against petitioners for the same publication.[18] Whether or not a newspaper can survive a succession of such judgments, the pall of fear and timidity imposed upon those who would give voice to public criticism is an atmosphere in which the First Amendment freedoms cannot survive. Plainly the Alabama law of civil libel is "a form of regulation that creates hazards to protected freedoms markedly greater than those that attend reliance upon the criminal law." Bantam Books, Inc. v. Sullivan, 372 U.S. 58, 70 (1963).

The state rule of law is not saved by its allowance of the defense of truth. . . . A rule compelling the critic of official conduct to guarantee the truth of all his factual assertions — and to do so on pain of libel judgments virtually unlimited in amount — leads to . . . "self-censorship." Allowance of the defense of truth, with the burden of proving it on the defendant, does not mean that only false speech will be deterred. Even courts accepting this defense as an adequate safeguard have recognized the difficulties of adducing legal proofs that the alleged libel was true in all its factual particulars. . . . Under such a rule, would-be critics of official conduct may be deterred from voicing their criticism, even though it is believed to be true and even though it is in fact true, because of doubt whether it can be proved in court or fear of the expense of having to do so. They tend to make only statements which "steer far wider of the unlawful zone." The rule thus dampens the vigor and limits the variety of public debate. It is inconsistent with the First and Fourteenth Amendments.

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16. The Act expired by its terms in 1801.

18. The Times states that four other libel suits based on the advertisement have been filed against it by others who have served as Montgomery City Commissioners and by the Governor of Alabama; that another $500,000 verdict has been awarded in the only one of these cases that has yet gone to trial; and that the damages sought in the other three total $2,000,000.

The constitutional guarantees require, we think, a federal rule that prohibits a public official from recovering damages for a defamatory falsehood relating to his official conduct unless he proves that the statement was made with "actual malice"—that is, with knowledge that it was false or with reckless disregard of whether it was false or not. [See] Coleman v. MacLennan, 98 P. 281 (Kan. 1908). . . .

We hold today that the Constitution delimits a State's power to award damages for libel in actions brought by public officials against critics of their official conduct. Since this is such an action, the rule requiring proof of actual malice is applicable. While Alabama law apparently requires proof of actual malice for an award of punitive damages, where general damages are concerned malice is "presumed." Such a presumption is inconsistent with the federal rule. "The power to create presumptions is not a means of escape from constitutional restrictions," Bailey v. Alabama, 219 U.S. 219, 239 (1911); "the showing of malice required for the forfeiture of the privilege is not presumed but is a matter for proof by the plaintiff. . . ." Lawrence v. Fox, 97 N.W.2d 719, 725 (Mich. 1959). Since the trial judge did not instruct the jury to differentiate between general and punitive damages, it may be that the verdict was wholly an award of one or the other. But it is impossible to know, in view of the general verdict returned. Because of this uncertainty, the judgment must be reversed and the case remanded. . . .

Since respondent may seek a new trial, we deem that considerations of effective judicial administration require us to review the evidence in the present record to determine whether it could constitutionally support a judgment for respondent. . . .

[We] consider that the proof presented to show actual malice lacks the convincing clarity which the constitutional standard demands, and hence that it would not constitutionally sustain the judgment for respondent under the proper rule of law. [The Court held that there was no evidence that the individual petitioners acted with reckless disregard, and that the evidence showed as a matter of law that the Times was at most negligent but not reckless with respect to the factual errors in the report and its handling of the retraction issue.]

We also think the evidence was constitutionally defective in another respect: it was incapable of supporting the jury's finding that the allegedly libelous statements were made "of and concerning" respondent. Respondent relies on the words of the advertisement and the testimony of six witnesses to establish a connection between it and himself. . . .

There was no reference to respondent in the advertisement, either by name or official position. A number of the allegedly libelous statements—the charges that the dining hall was padlocked and that Dr. King's home was bombed, his person assaulted, and a perjury prosecution instituted against him—did not even concern the police; despite the ingenuity of the arguments which would attach this significance to the word "They," it is plain that these statements could not reasonably be read as accusing respondent of personal involvement in the acts in question. The statements upon which respondent principally relies as referring to him are the two allegations that did concern the police or police functions: that "truckloads of police . . . ringed the Alabama State College Campus" after the demonstration on the State Capitol steps, and that Dr. King had been "arrested . . . seven times." . . . Although the statements may be taken as referring to the police, they did not on their face make even an oblique reference to respondent as an individual. . . .

The judgment of the Supreme Court of Alabama is reversed and the case is remanded to that court for further proceedings not inconsistent with this opinion.

Reversed and remanded.

Black, J., with whom Douglas, J., joins, concurring. I concur in reversing this half-million-dollar judgment against the New York Times Company and the four individual defendants. . . . I base my vote to reverse on the belief that the First and Fourteenth Amendments not merely "delimit" a State's power to award damages to "public officials against critics of

their official conduct" but completely prohibit a State from exercising such a power. The Court goes on to hold that a State can subject such critics to damages if "actual malice" can be proved against them. "Malice," even as defined by the Court, is an elusive, abstract concept, hard to prove and hard to disprove. The requirement that malice be proved provides at best an evanescent protection for the right critically to discuss public affairs and certainly does not measure up to the sturdy safeguard embodied in the First Amendment. Unlike the Court, therefore, I vote to reverse exclusively on the ground that the Times and the individual defendants had an absolute, unconditional right to publish in the Times advertisement their criticisms of the Montgomery agencies and officials. . . .

[The concurring opinion of Justice Goldberg has been omitted.]

## NOTES

**1.** ***Constitutionalizing Defamation Law.*** New York Times v. Sullivan ushered in a new constitutional jurisprudence for all defamation cases brought by public officials against media defendants. In choosing to override the common law, was the Court more swayed by the predicament of the *New York Times* or by the weaknesses of the common law of defamation? What are the narrowest grounds on which the plaintiff's verdict could be overturned? For an argument that Alabama misapplied the common law of defamation on all relevant issues, see Richard A. Epstein, Was *New York Times v. Sullivan* Wrong?, 53 U. Chi. L. Rev. 782 (1986). Consider whether any award greater than nominal damages could be supported in light of Justice Brennan's observations: "Approximately 394 copies of the edition of the Times containing the advertisement were circulated in Alabama. Of these, about 35 copies were distributed in Montgomery County. The total circulation of the Times for that day was approximately 650,000 copies." *New York Times*, 376 U.S. at 260.

**2.** ***The Private Conduct of Public Officials.*** In Monitor Patriot Co. v. Roy, 401 U.S. 265, 277 (1971), petitioner newspaper published a column characterizing senatorial candidate Roy as a "former small-time bootlegger." The jury found for respondent on the ground that the bootlegger charge was "in the private sector." Reversing that decision, the Court noted first that under *New York Times* "publications concerning candidates must be accorded at least as much protection under the First and Fourteenth Amendments as those concerning occupants of public office." It rejected respondent's contentions that *New York Times* applies only to a candidate's "official conduct," meaning "conduct relevant to fitness for office" and that the public-private issue is one for the jury. The Court held

> as a matter of constitutional law that a charge of criminal conduct, no matter how remote in time or place, can never be irrelevant to an official's or a candidate's fitness for office for purposes of the "knowing falsehood or reckless disregard" rule of New York Times Co. v. Sullivan.

For an enthusiastic interpretation of *New York Times* as an occasion "for dancing in the streets," see Harry Kalven, Jr., The *New York Times* Case: A Note on "The Central Meaning of the First Amendment," 1964 Sup. Ct. Rev. 191.

**3.** ***New York Times in the Internet Age.*** Has *New York Times* become anachronistic in the Internet age? Cass R. Sunstein, Falsehoods and the First Amendment, 33 Harv. J.L. & Tech. 387 (2020), notes that *New York Times* was decided in 1964, "which might as well be a century ago, or maybe a millennium, in light of the massive technological advances that followed it." Sunstein suggests that the actual malice standard be replaced by allowing an affected individual the right of "notice and take down." See *supra* Section B, Note 3, at 321. Should the challenged material be allowed to remain up until the defamation claim is investigated?

What legal remedies should be available for falsehoods created by "deepfake" videos? Deepfakes use algorithms to create human image synthesis; its most recent uses include fake celebrity pornography and revenge porn. Russell Spivak, "Deepfakes": The Newest Way to Commit One of the Oldest Crimes, 3 Geo. L. Tech. Rev. 339, 385 (2019), argues that the "actual malice" standard is automatically satisfied in all uses of deepfake technology given that "its creator must *know* the final result is fraudulent. . . ." Should the actual malice standard apply in response to deepfakes and other recent technologies? If so, will it inevitably be satisfied?

**4. *Rethinking* New York Times.** Justice Thomas called for a reconsideration of New York Times v. Sullivan in his concurrence opinion in the denial of certiorari of McKee v. Cosby, 586 U.S. __, 139 S. Ct. 675 (2019), a case in which the plaintiff had charged Bill Cosby, the famous TV actor, with forcible rape. In the court below the plaintiff was found to be a limited public figure because she had disclosed her allegations to a reporter. "We should not continue to reflexively apply this policy-driven approach to the Constitution. Instead, we should carefully examine the original meaning of the First and Fourteenth Amendments. If the Constitution does not require public figures to satisfy an actual-malice standard in state-law defamation suits, then neither should we." Justice Thomas pointed out that the constitutional libel rules were not aligned with the common law of libel, and it was not clear whether the First and Fourteenth Amendments displaced such common law. For example, the common law of libel did not require public officials to prove heightened liability to recover damages.

Fellow Supreme Court Justices have similarly raised questions regarding the continued vitality of the *New York Times* actual malice rule in the Internet age. In his dissenting opinion to the denial of certiorari of Berisha v. Lawson, 594 U.S. __, 141 S. Ct. 2424, 2428–29 (2021), Gorsuch, J., also called for the Court to abandon the actual malice standard. First, he criticized actual malice on the grounds that it "has evolved from a high bar to recovery into an effective immunity from liability." Additionally, he posited that "publishing without investigation, fact-checking, or editing has become the optimal legal strategy" because actual malice requires that the defendant have actual or constructive knowledge of the statement's falsity. Finally, he noted that applying the actual malice standard to all categories of public figures is no longer workable given that "private citizens can become 'public figures' on social media overnight."

Nor are such criticisms of *New York Times* and its actual malice standard limited to the domain of defamation. In Counterman v. Colorado, 600 U.S. 66, 112 (2023), a fractured Supreme Court, speaking through Kagan, J., ruled that for a true threat of violence to lose protection as free speech under the First Amendment, a plaintiff must prove that the speaker made such threats with a subjective *mens rea* of at least recklessness. In its decision, the majority decided that an objective standard was not sufficient here given the need to prove actual malice under *New York Times*. In her dissent, Barrett, J., criticized the majority's decision, arguing that:

> *Sullivan's* rationale does not justify a heightened *mens rea* for true threats. . . . Nor can public figures use counterspeech in the public square to protect themselves from serious threats of physical violence. And perversely, private individuals now have less protection from true threats than from defamation—even though they presumably value their lives more than their reputations. . . . The Court has therefore extended *Sullivan* in a way that makes no sense on *Sullivan*'s own terms.

Is it time to reconsider *New York Times*? On the grounds that it does not align with the common law of libel, or that it has become anachronistic in light of new technologies?

**5. *A World Without* New York Times.** Since defamation law was first constitutionalized in *Sullivan*, critics have wondered what a pure common law regime would look like in the United States.

The Australian case of Google LLC v. Defteros, [2022] HCA 27, sheds light on how a pure common law regime handles modern technology-based defamation issues. Defteros, a lawyer, sued Google for failing to remove an allegedly defamatory story hyperlinked on its search engine. Defteros brought the suit after Google denied his request to remove it. The trial court found that the hyperlinked article defamed Defteros and also ruled that Google's hyperlink to the article "was instrumental to the communication of the content of the Underworld article to the user." However, the High Court on appeal ruled that Google did not publish the defamatory article and rejected the trial court's finding that it had assisted the continued publication of the defamatory article. Would the outcome of this case change if it were brought under the U.S. constitutionalized defamation regime, as opposed to a common law regime with a notice-and-take-down regime? Does a pure common law regime in *Defteros* incentivize nonpublication? If so, is that incentive effect outweighed by institutional norms recognizing a free press and the moral hazard of setting up a robust system of libel insurance? If not, how would such a common law regime differ from the constitutionalized U.S. system absent the immunity given to ISPs?

Frederick Schauer, On the Relationship Between Press Law and Press Content, *in* Freeing the Press: The First Amendment in Action 51–57, 65 (2013), argues that "the existence of libel laws considerably stricter than post-*New York Times v. Sullivan* American libel law has done little to restrain or stifle press tendencies to be investigative, questioning, challenging, nasty, and often personal." Schauer specifically notes that Australia has adhered to a stringent defamation regime (strict liability, no proof of fault required, truth being an affirmative defense), which has not affected the robustness of Australia's press and investigative media. Schauer also argues that protecting journalists and other media from defamation liability could be better accomplished by establishing the set of privileges that Australia has created for political figures.

## *Curtis Publishing Co. v. Butts*

388 U.S. 130 (1967)

[No. 37, Curtis Publishing Co. v. Butts, involved charges in the *Saturday Evening Post* that Wally Butts, former coach of the University of Georgia football team and then director of athletics, had conspired to fix a 1962 Georgia-Alabama game by giving to Paul Bryant, coach of the University of Alabama team, crucial information about Georgia's offensive strategy. The article concluded: "The chances are that Wally Butts will never help any football team again. . . . The investigation by university and Southeastern Conference officials is continuing; motion pictures of other games are being scrutinized; where it will end no one so far can say. But careers will be ruined, that is sure." Butts sued for libel and a jury awarded him $60,000 in general damages and $3 million in punitive damages. After *New York Times*, the defendant requested a new trial, but the motion was denied on two grounds—first, that *New York Times* was inapplicable because the plaintiff was not a public official and, second, that the record contained ample evidence from which a jury could have concluded that the article was published with reckless disregard for truth. The judgment of the trial court was affirmed on appeal. 351 F.2d 702 (5th Cir. 1965).

No. 150, Associated Press v. Walker, arose out of the distribution of a news dispatch giving an eyewitness account of events on the campus of the University of Mississippi on the night of September 30, 1962, when a massive riot erupted because of federal efforts to enforce a court decree ordering the enrollment of a Negro, James Meredith, as a student in the University. The dispatch stated that respondent Edwin Walker, who was present on the campus, had taken command of the violent crowd and had personally led a charge against federal

marshals sent there to effectuate the court's decree and to assist in preserving order. Walker, a private citizen with a long and honorable military career, sued for libel claiming that he had "counseled restraint" to the students, had exercised no control over the crowd, and had not taken part in any charge against federal marshals. Some evidence showed that the Associated Press was negligent in assigning an inexperienced reporter to cover the story and had failed to catch minor discrepancies between an early oral dispatch and a later written dispatch. The jury awarded plaintiff $500,000 in compensatory and $300,000 in punitive damages. The trial court refused to enter the award of punitive damages, concluding that the record contained at most evidence of negligence but not malice. Both sides appealed. The decision was affirmed by the Texas Civil Court of Appeals, 393 S.W.2d 671 (1965). The U.S. Supreme Court granted certiorari after the Supreme Court of Texas denied writ of error.

Both plaintiffs were public figures but not public officials. Four separate Supreme Court opinions, much condensed here, addressed the question of how the standards of *New York Times* applied.]

Harlan, J. . . . We thus turn to a consideration, on the merits, of the constitutional claims raised by Curtis in *Butts* and by the Associated Press in *Walker*. Powerful arguments are brought to bear for the extension of the *New York Times* rule in both cases.

[Justice Harlan reviewed at length various leading precedents on free speech, and continued:]

In *New York Times* we were adjudicating in an area which lay close to seditious libel, and history dictated extreme caution in imposing liability. The plaintiff in that case was an official whose position in government was such "that the public [had] an independent interest in the qualifications and performance of the person who [held] it." Rosenblatt v. Baer, 383 U.S. 75, at 86 (1966). Such officials usually enjoy a privilege against libel actions for their utterances, see, e.g., Barr v. Matteo, 360 U.S. 564 (1960), and there were analogous considerations involved in *New York Times*. Thus we invoked "the hypothesis that speech can rebut speech, propaganda will answer propaganda, free debate of ideas will result in the wisest governmental policies," Dennis v. United States, 341 U.S. 494, 503 (1951), and limited recovery to those cases where "calculated falsehood" placed the publisher "at odds with the premises of democratic government and with the orderly manner in which economic, social, or political change is to be effected." Garrison v. Louisiana, 379 U.S. 64, 75 (1964). That is to say, such officials were permitted to recover in libel only when they could prove that the publication involved was deliberately falsified, or published recklessly despite the publisher's awareness of probable falsity. Investigatory failures alone were held insufficient to satisfy this standard.

In the cases we decide today none of the particular considerations involved in *New York Times* is present. These actions cannot be analogized to prosecutions for seditious libel. Neither plaintiff has any position in government which would permit a recovery by him to be viewed as a vindication of governmental policy. Neither was entitled to a special privilege protecting his utterances against accountability in libel. We are prompted, therefore, to seek guidance from the rules of liability which prevail in our society with respect to compensation of persons injured by the improper performance of a legitimate activity by another. Under these rules, a departure from the kind of care society may expect from a reasonable man performing such activity leaves the actor open to a judicial shifting of loss. In defining these rules, and especially in formulating the standards for determining the degree of care to be expected in the circumstances, courts have consistently given much attention to the importance of defendants' activities. The courts have also, especially in libel cases, investigated the plaintiff's position to determine whether he has a legitimate call upon the court for protection in light of his prior activities and means of self-defense. We note that the public interest in the circulation of the materials here involved, and the publisher's interest in circulating them, is not less than that involved in *New York Times*. And both Butts and Walker commanded a substantial

amount of independent public interest at the time of the publications; both, in our opinion, would have been labeled "public figures" under ordinary tort rules. Butts may have attained that status by position alone and Walker by his purposeful activity amounting to a thrusting of his personality into the "vortex" of an important public controversy, but both commanded sufficient continuing public interest and had sufficient access to the means of counterargument to be able to "expose through discussion the falsehood and fallacies" of the defamatory statements. Whitney v. California, 274 U.S. 357, 377 (1927) (Brandeis, J., dissenting).

These similarities and differences between libel actions involving persons who are public officials and libel actions involving those circumstanced as were Butts and Walker, viewed in light of the principles of liability which are of general applicability in our society, lead us to the conclusion that libel actions of the present kind cannot be left entirely to state libel laws, unlimited by any overriding constitutional safeguard, but that the rigorous federal requirements of *New York Times* are not the only appropriate accommodation of the conflicting interests at stake. We consider and would hold that a "public figure" who is not a public official may also recover damages for a defamatory falsehood whose substance makes substantial danger to reputation apparent, on a showing of highly unreasonable conduct constituting an extreme departure from the standards of investigation and reporting ordinarily adhered to by responsible publishers.

Nothing in this opinion is meant to affect the holdings in *New York Times* and its progeny, including our recent decision in Time, Inc. v. Hill [*infra* Chapter 7].

Having set forth the standard by which we believe the constitutionality of the damage awards in these cases must be judged, we turn now, as the Court did in *New York Times*, to the question whether the evidence and findings below meet that standard. We find the standard satisfied in No. 37, *Butts*, and not satisfied by either the evidence or the findings in No. 150, *Walker*.

[Justice Harlan reviewed the evidence in detail. He then examined defendants' challenge to the constitutionality of the punitive damages award and rejected it. His opinion concludes:]

The judgment of the Court of Appeals for the Fifth Circuit in No. 37 is affirmed. The judgment of the Texas Court of Civil Appeals in No. 150 is reversed and the case is remanded to that court for further proceedings not inconsistent with the opinions that have been filed herein by The Chief Justice, Justice Black, and Justice Brennan.

Warren, C.J., concurring in the result. . . . To me, differentiation between "public figures" and "public officials" and adoption of separate standards of proof for each have no basis in law, logic, or First Amendment policy. Increasingly in this country, the distinctions between governmental and private sectors are blurred. Since the depression of the 1930's and World War II there has been a rapid fusion of economic and political power, a merging of science, industry, and government, and a high degree of interaction between the intellectual, governmental, and business worlds. Depression, war, international tensions, national and international markets, and the surging growth of science and technology have precipitated national and international problems that demand national and international solutions. While these trends and events have occasioned a consolidation of governmental power, power has also become much more organized in what we have commonly considered to be the private sector. In many situations, policy determinations which traditionally were channeled through formal political institutions are now originated and implemented through a complex array of boards, committees, commissions, corporations, and associations, some only loosely connected with the Government. This blending of positions and power has also occurred in the case of individuals so that many who do not hold public office at the moment are nevertheless intimately involved in the resolution of important public questions or, by reason of their fame, shape events in areas of concern to society at large. . . .

I therefore adhere to the *New York Times* standard in the case of "public figures" as well as "public officials." It is a manageable standard, readily stated and understood, which also balances to a proper degree the legitimate interests traditionally protected by the law of defamation. . . .

I have no difficulty in concluding that No. 150, Associated Press v. Walker, must be reversed since it is in a clear conflict with *New York Times*. . . .

But No. 37, Curtis Publishing Co. v. Butts, presents an entirely different situation. . . .

[The Chief Justice discussed the failure of the defendants to raise at the trial any First Amendment defense and noted that the decision of the Post to "change its image" to boost sagging sales and revenue supported the damage award, especially because the Post refused to investigate the matter further after Butts and his daughter stated that the story was absolutely untrue.]

I am satisfied that the evidence here discloses that degree of reckless disregard for the truth of which we spoke in *New York Times* and *Garrison*. Freedom of the press under the First Amendment does not include absolute license to destroy lives or careers.

[Justice Black, with whom Justice Douglas joined, concurred in the reversal of *Walker* and dissented from the affirmance of *Butts*:]

I think it is time for this Court to abandon New York Times Co. v. Sullivan and adopt the rule to the effect that the First Amendment was intended to leave the press free from the harassment of libel judgments.

[Justice Brennan, with whom Justice White joined, concurred in the reversal of *Walker* and dissented from the affirmance of *Butts*. He agreed with the Chief Justice that the evidence in *Butts* supported a jury award for the plaintiff under the *New York Times* rule, but thought it proper "to remand for a new trial since the charge to the jury did not comport with that standard."]

## NOTES

**1. *An Embarrassment of Constitutional Standards?*** At the end of the day, *Butts* and *Walker* extended the actual malice test of *New York Times* from public officials to public figures. Five members of the Court (Black and Douglas adopting for this purpose the Warren position) rejected the arguments put forward by Harlan, which would have allowed a public figure to override the constitutional defense by showing, in essence, the gross negligence of the defendant. For a criticism of the Harlan position as lacking in "constitutional dimensions," see Harry Kalven, Jr., The Reasonable Man and the First Amendment, 1967 Sup. Ct. Rev. 267, 300.

> For centuries it has been the experience of Anglo-American law that the truth never catches up with the lie, and it is because it does not that there has been a law of defamation. I simply do not see how the constitutional protection in this area can be rested on the assurance that counterargument will take the sting out of the falsehoods the law is thereby permitting. And if this premise is not persuasive, the whole Harlan edifice tumbles.

Does Kalven's argument justify the extension of *New York Times* to public figures, or the return to the common law rules of fair comment for both public officials and public figures?

**2. *Actual Malice.*** The Supreme Court has strictly applied its actual malice standard to public officials and public figures alike. For example, in St. Amant v. Thompson, 390 U.S. 727, 732 (1968), the petitioner charged the respondent, a deputy sheriff, with criminal

conduct during a televised political speech. The Supreme Court assumed that the charges were defamatory and false and that respondent was a public official under *New York Times*, but held that the evidence failed to support respondent's contention that petitioner had acted with reckless disregard of the truth. The Court reaffirmed the view that "neither the defense of truth nor the standard of ordinary care would protect against self-censorship and thus adequately implement First Amendment policies" but then issued this warning about the actual malice standard:

> The defendant in a defamation action brought by a public official cannot, however, automatically insure a favorable verdict by testifying that he published with a belief that the statements were true. The finder of fact must determine whether the publication was indeed made in good faith. Professions of good faith will be unlikely to prove persuasive, for example, where a story is fabricated by the defendant, is the product of his imagination, or is based wholly on an unverified anonymous telephone call. Nor will they be likely to prevail when the publisher's allegations are so inherently improbable that only a reckless man would have put them in circulation. Likewise, recklessness may be found where there are obvious reasons to doubt the veracity of the informant or the accuracy of his reports.

**3. *Summary Judgments Under* New York Times.** Under *New York Times*, what amount of evidence must the plaintiff present to survive a motion for summary judgment on the actual malice question? In Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 254–55 (1986), columnist Jack Anderson published three articles about the Liberty Lobby and its key officials that "portrayed the [plaintiffs] as neo-Nazi, anti-Semitic, racist, and fascist." All were public figures. In response to respondents' defamation suit, the defendant moved for summary judgment on the strength of affidavits by Anderson's key researcher that he had spent "substantial time" researching the articles. The precise issue in the case was whether "the clear-and-convincing-evidence requirement [of *New York Times*] must be considered by a court ruling on a motion for summary judgment." The Court, speaking through Justice White, held that it did:

> Just as the "convincing clarity" requirement is relevant in ruling on a motion for directed verdict, it is relevant in ruling on a motion for summary judgment. When determining if a genuine factual issue as to actual malice exists in a libel suit brought by a public figure, a trial judge must bear in mind the actual quantum and quality of proof necessary to support liability under *New York Times*. For example, there is no genuine issue if the evidence presented in the opposing affidavits is of insufficient caliber or quantity to allow a rational finder of fact to find actual malice by clear and convincing evidence. . . .
>
> Our holding that the clear-and-convincing standard of proof should be taken into account on summary judgment motions does not denigrate the role of the jury. It by no means authorizes trial on affidavits. Credibility determinations, the weighing of the evidence, and the drawing of legitimate inferences from the facts are jury functions, not those of a judge, whether he is ruling on a motion for summary judgment or for a directed verdict. The evidence of the non-movant is to be believed, and all justifiable inferences are to be drawn in his favor.

The Court then remanded the case to the trial judge. In separate dissents, Justices Brennan and Rehnquist argued that the case should be left to the jury. In their view, using different standards for summary judgment would invade the province of the jury, induce trial judges to conduct exhaustive minitrials before making their decisions, and lead to confusion in the granting and denying of summary judgments.

**4. *Discovery on Mental State.*** The issue of actual malice necessarily injects the delicate question of the defendant's mental state into defamation cases against public officials and public figures. The modern rules of discovery, moreover, generally give the moving party broad latitude to "obtain discovery regarding any matter, not privileged, that is relevant to the claim or defense of any party" to the litigation. Fed. R. Civ. P. 26(b)(1). In Herbert v. Lando,

441 U.S. 153, 170 (1979), the defendant, an editor of the television show *60 Minutes*, urged the Court to hold (as did the Second Circuit below) that

> when a member of the press is alleged to have circulated damaging falsehoods and is sued for injury to the plaintiff's reputation, the plaintiff is barred from inquiring into the editorial process of those responsible for the publication, even though the inquiry would produce evidence material to the proof of a critical element of his cause of action.

The Court rejected the claim, in part for the following reasons:

> In the first place, it is plain enough that the suggested privilege for the editorial process would constitute a substantial interference with the ability of a defamation plaintiff to establish the ingredients of malice as required by *New York Times*. As respondents would have it, the defendant's reckless disregard of the truth, a critical element, could not be shown by direct evidence through inquiry into the thoughts, opinions and conclusions of the publisher but could be proved only by objective evidence from which the ultimate fact could be inferred. It may be that plaintiffs will rarely be successful in proving awareness of falsehood from the mouth of the defendant himself, but the relevance of answers to such inquiries, which the District Court recognized and the Court of Appeals did not deny, can hardly be doubted. To erect an impenetrable barrier to the plaintiff's use of such evidence on his side of the case is a matter of some substance, particularly when defendants themselves are prone to assert their good-faith belief in the truth of their publications, and libel plaintiffs are required to prove knowing or reckless falsehood with "convincing clarity."

Justice Brennan dissented in part:

> I would hold, however, that the First Amendment requires predecisional communication among editors to be protected by an editorial privilege, but that this privilege must yield if a public-figure plaintiff is able to demonstrate to the prima facie satisfaction of a trial judge that the publication in question constitutes defamatory falsehood.

Litigation in the case continued for seven more years, ending with a summary judgment for the defendant on the actual malice question. See Herbert v. Lando, 781 F.2d 298 (2d Cir. 1986). On the Supreme Court decision, see generally Marc A. Franklin, Reflections on *Herbert v. Lando*, 31 Stan. L. Rev. 1035 (1979); Jack H. Friedenthal, *Herbert v. Lando*: A Note on Discovery, 31 Stan. L. Rev. 1059 (1979).

**5.** ***Public Figures in the Supreme Court.*** The identification of public officials under the *New York Times* rule is, in general, a straightforward affair. The determination of who counts as a public figure presents, however, a trickier problem. To be sure, the list includes former public officials, professional athletes, entertainers, and celebrities (and here the ambiguity begins) most of the time and for most if not all purposes. Since *Butts*, the Supreme Court has frequently wrestled with this question. Thus in Time, Inc. v. Firestone, 424 U.S. 448 (1976), the Court held that the wife of "the scion of one of America's wealthier industrial families" was not a public figure even though she held a news conference during a sensational and messy divorce trial. The Court also held that a research scientist who was awarded William Proxmire's "Golden Fleece" award was not a public figure even though—as the award itself suggests—the plaintiff had been successful in getting federal grant support. See Hutchinson v. Proxmire, 443 U.S. 111 (1979). In the companion case of Wolston v. Reader's Digest Association, Inc., 443 U.S. 157 (1979), the plaintiff was listed in *Reader's Digest* as a Soviet agent along with (among others) Julius and Ethel Rosenberg and the plaintiff's uncle, Jack Soble. The plaintiff, who had refused to appear before a grand jury for questioning about his uncle, was not a public figure because he was neither a person of general prominence nor had he "thrust himself to the forefront" of a particular public controversy simply because he had fled when pursued by the government. See also the discussion in *Gertz, infra* at 397.

**6. *Public Figures in the Lower Courts.*** The lower courts have also joined the chase. Persons who had former connections with public events have generally been held to be public figures. Thus in Meeropol v. Nizer, 381 F. Supp. 29, 34 (S.D.N.Y. 1974), Tyler, J., held that the two sons of Julius and Ethel Rosenberg were public figures, notwithstanding the fact that they "later may have renounced the public spotlight by changing their name to Meeropol," because "as children they were the subject of considerable public attention."

In addition, a long list of persons, large insurance companies, professional football players, Navy officers during the Vietnam War, Johnny Carson, local mobsters, belly dancers, Nobel Prize winners, and debt collection agencies under public investigation have all been treated as public figures on a "limited basis" for those aspects of their conduct subjected to public scrutiny and review. In Reuber v. Food Chemical News, Inc., 925 F.2d 703, 706, 708 (4th Cir. 1991), the plaintiff was a research scientist at the National Cancer Institute who "disseminated his own research and took other actions which created the misleading impression that the NCI had reversed its official position that the pesticide malathion was a non-carcinogen." A letter from his supervisor rebuking his research and statements was published by the defendant. The Fourth Circuit held that the plaintiff was "a limited purpose" public figure because he had "injected" himself into the public arena by his previous publications on the problem. Additionally in Makaeff v. Trump University, LLC, 715 F.3d 254, 267–68 (9th Cir. 2013), Wardlaw, J., held that, while Donald Trump's public figure status could not be imputed *vel non* to Trump University, it was nonetheless a public figure for the limited purpose of a defamation claim over its educational practices on account of its "large scale, aggressive advertising." "Advertising," Wardlaw, J., continued, "can be a way of 'voluntarily expos[ing] [the company] to increased risk of injury from defamatory falsehood'"; moreover, a company that aggressively advertises "enjoy[s] significantly greater access to the channels of effective communication and hence ha[s] a more realistic opportunity to counteract false statements th[a]n private individuals normally enjoy."

**7. *Reform of Defamation Law.*** When handed down, *New York Times* was generally celebrated for its boost to the civil rights movement. Many commentators also thought that its actual malice rule could undo the litigation logjam in defamation cases. But starting in the 1970s and working through the 1980s, defamation suits were mammoth struggles avidly covered by the press. The expanded scope of civil litigation galvanized pressure for legislative reform. During the 1980s, the *New York Times* actual malice rule came under attack from both sides. For the plaintiffs, the chief grievance was that the actual malice rule allowed a defendant to escape liability even when admittedly false statements worked substantial damage to reputation, thereby denying official vindication for serious reputational harm. Media defendants in turn protested the enormous expense of defending a defamation action. Ironically the actual malice rule may well have been part of the problem. Although it reduces the number of potential cases, it also makes litigation outcomes more uncertain. In successful claims, moreover, the proof of actual malice might easily justify large and erratic claims for punitive damages.

The two titanic struggles of the 1980s were Sharon v. Time, Inc., 599 F. Supp. 538 (S.D.N.Y. 1984), and Westmoreland v. CBS, 10 Media L. Rep. 2417 (S.D.N.Y. 1984). In *Sharon*, the Israeli Minister of Defense filed a libel action against the publishers of *Time* magazine, for its published story "The Verdict Is Guilty: An Israeli Commission Apportions the Blame for the Beirut Massacre." Sharon claimed that portions of the article included false characterizations of classified information. General Westmoreland's suit alleged that a CBS broadcast claiming that he organized a conspiracy to downplay the intelligence that contradicted his own optimistic reports on the progress of the Vietnam War was libelous.

When the issue was hot, many suggestions received serious public attention. One idea was to abolish all defamation actions by public officials and public figures, at least against media

defendants. In this vein, see Anthony Lewis, *New York Times v. Sullivan* Reconsidered: Time to Return to "The Central Meaning of the First Amendment," 83 Colum. L. Rev. 603 (1983), advocating, among other changes, more frequent use of summary judgments, special verdicts, and a prohibition on recovery for mental anguish and punitive damages.

In the opposite direction, many scholars urged that the plaintiff be allowed to obtain a declaratory judgment on the question of truth or falsity without proof of actual malice, but only (under some versions of the proposal) by first waiving any right to damages. A declaratory judgment was achieved in a backhand manner in the *Sharon* case, in which, in response to specific questions propounded by special verdicts, the jury found both that *Time*'s statements were wrong and that the error was not actuated by actual malice. (Note that the trial in *Westmoreland* ended in February 1985, when the case was settled out of court right before it would have been sent to the jury.) What is the reputational effect of such a verdict on *Time*?

## 2. Private Parties

### *Gertz v. Robert Welch, Inc.*
418 U.S. 323 (1974)

[Elmer Gertz, a reputable attorney, was retained by the Nelson family to represent them in a civil action against Nuccio, a Chicago policeman who had previously been convicted of second-degree murder for the death of young Ronald Nelson. As counsel for the family, petitioner attended the coroner's inquest into Nelson's death and initiated actions for damages, but he neither discussed Officer Nuccio with the press nor played any part in the criminal proceeding.

Respondent published *American Opinion*, a periodical of the John Birch Society. As part of its campaign to warn America of a communist conspiracy to discredit local law enforcement agencies, respondent published an article entitled "Frame-Up: Richard Nuccio and the War on Police" that purported to show that Nuccio was innocent, that his prosecution was a communist "frame-up," and that petitioner was an "architect of the frame-up." The article also falsely charged that Gertz was a communist who had engaged in communist activities. The managing editor of *American Opinion* had not independently investigated the article's charges but had relied on its author's "extensive research." The article was accompanied by a photograph of petitioner over the caption "Elmer Gertz of Red Guild harasses Nuccio."

Gertz filed a libel action in federal district court and won a jury verdict for $50,000. The court refused to enter judgment on the verdict on the ground that the *New York Times* standard protects discussion of any public issue without regard to the status of the person defamed. The Court of Appeals affirmed, adding that petitioner had failed to show that respondent acted with actual malice as defined by *New York Times*, "mere proof of failure to investigate, without more" being insufficient to establish reckless disregard for the truth. 471 F.2d 801 (7th Cir. 1972). The Supreme Court reversed.]

Powell, J. . . . The principal issue in this case is whether a newspaper or broadcaster that publishes defamatory falsehoods about an individual who is neither a public official nor a public figure may claim a constitutional privilege against liability for the injury inflicted by those statements. The Court considered this question on the rather different set of facts presented in Rosenbloom v. Metromedia, Inc., 403 U.S. 29 (1971). . . .

The eight Justices who participated in *Rosenbloom* announced their views in five separate opinions, none of which commanded more than three votes. . . .

[The Court then reviewed *New York Times*, *Butts*, and *Walker*, and continued:]

In his opinion for the plurality in *Rosenbloom*, Mr. Justice Brennan took the *New York Times* privilege one step further. He concluded that its protection should extend to defamatory falsehoods relating to private persons if the statements concerned matters of general or public interest. He abjured the suggested distinction between public officials and public figures on the one hand and private individuals on the other. He focused instead on society's interest in learning about certain issues: "If a matter is a subject of public or general interest, it cannot suddenly become less so merely because a private individual is involved, or because in some sense the individual did not 'voluntarily' choose to become involved." *Id.*, at 43. Thus, under the plurality opinion, a private citizen involuntarily associated with a matter of general interest has no recourse for injury to his reputation unless he can satisfy the demanding requirements of the *New York Times* test.

[The Court then examined the other opinions in *Rosenbloom*.]

We begin with the common ground. Under the First Amendment there is no such thing as a false idea. However pernicious an opinion may seem, we depend for its correction not on the conscience of judges and juries but on the competition of other ideas. But there is no constitutional value in false statements of fact. Neither the intentional lie nor the careless error materially advances society's interest in "uninhibited, robust, and wide-open" debate on public issues. They belong to that category of utterances which "are no essential part of any exposition of ideas, and are of such slight social value as a step to truth that any benefit that may be derived from them is clearly outweighed by the social interest in order and morality." Chaplinsky v. New Hampshire, 315 U.S. 568, 572 (1942).

[Powell, J., reviewed the reasons why *New York Times* calls for "breathing room" and the avoidance of self-censorship to promote open debate.]

The need to avoid self-censorship by the news media is, however, not the only societal value at issue. If it were, this Court would have embraced long ago the view that publishers and broadcasters enjoy an unconditional and indefeasible immunity from liability for defamation. Such a rule would, indeed, obviate the fear that the prospect of civil liability for injurious falsehood might dissuade a timorous press from the effective exercise of First Amendment freedoms. Yet absolute protection for the communications media requires a total sacrifice of the competing value served by the law of defamation.

The legitimate state interest underlying the law of libel is the compensation of individuals for the harm inflicted on them by defamatory falsehood. We would not lightly require the State to abandon this purpose. . . .

Some tension necessarily exists between the need for a vigorous and uninhibited press and the legitimate interest in redressing wrongful injury. . . .

We think that [the decisions under *New York Times*] are correct, but we do not find their holdings justified solely by reference to the interest of the press and broadcast media in immunity from liability. Rather, we believe that the *New York Times* rule states an accommodation between this concern and the limited state interest present in the context of libel actions brought by public persons. For the reasons stated below, we conclude that the state interest in compensating injury to the reputation of private individuals requires that a different rule should obtain with respect to them.

Theoretically, of course, the balance between the needs of the press and the individual's claim to compensation for wrongful injury might be struck on a case-by-case basis. . . . But this approach would lead to unpredictable results and uncertain expectations, and it could render our duty to supervise the lower courts unmanageable. Because an ad hoc resolution of the competing interests at stake in each particular case is not feasible, we must lay down broad rules of general application. Such rules necessarily treat alike various cases involving differences as well as similarities. Thus it is often true that not all of the considerations which justify adoption of a given rule will obtain in each particular case decided under its authority.

With that caveat we have no difficulty in distinguishing among defamation plaintiffs. The first remedy of any victim of defamation is self-help—using available opportunities to contradict the lie or correct the error and thereby to minimize its adverse impact on reputation. Public officials and public figures usually enjoy significantly greater access to the channels of effective communication and hence have a more realistic opportunity to counteract false statements than private individuals normally enjoy. Private individuals are therefore more vulnerable to injury, and the state interest in protecting them is correspondingly greater.

More important than the likelihood that private individuals will lack effective opportunities for rebuttal, there is a compelling normative consideration underlying the distinction between public and private defamation plaintiffs. An individual who decides to seek governmental office must accept certain necessary consequences of that involvement in public affairs. He runs the risk of closer public scrutiny than might otherwise be the case. And society's interest in the officers of government is not strictly limited to the formal discharge of official duties. . . .

Those classed as public figures stand in a similar position. Hypothetically, it may be possible for someone to become a public figure through no purposeful action of his own, but the instances of truly involuntary public figures must be exceedingly rare. . . .

Even if the foregoing generalities do not obtain in every instance, the communications media are entitled to act on the assumption that public officials and public figures have voluntarily exposed themselves to increased risk of injury from defamatory falsehood concerning them. No such assumption is justified with respect to a private individual. He has not accepted public office or assumed an "influential role in ordering society." Curtis Publishing Co. v. Butts (Warren, C.J., concurring in result). He has relinquished no part of his interest in the protection of his own good name, and consequently he has a more compelling call on the courts for redress of injury inflicted by defamatory falsehood. Thus, private individuals are not only more vulnerable to injury than public officials and public figures; they are also more deserving of recovery. . . .

We hold that, so long as they do not impose liability without fault, the States may define for themselves the appropriate standard of liability for a publisher or broadcaster of defamatory falsehood injurious to a private individual. This approach provides a more equitable boundary between the competing concerns involved here. It recognizes the strength of the legitimate state interest in compensating private individuals for wrongful injury to reputation, yet shields the press and broadcast media from the rigors of strict liability for defamation. At least this conclusion obtains where, as here, the substance of the defamatory statement "makes substantial danger to reputation apparent." This phrase places in perspective the conclusion we announce today. Our inquiry would involve considerations somewhat different from those discussed above if a State purported to condition civil liability on a factual misstatement whose content did not warn a reasonably prudent editor or broadcaster of its defamatory potential. Such a case is not now before us, and we intimate no view as to its proper resolution.

[The Court then stated that the state interest in the protection of reputation "extends no further than compensation for actual injury."] For the reasons stated below, we hold that the States may not permit recovery of presumed or punitive damages, at least when liability is not based on a showing of knowledge of falsity or reckless disregard for the truth.

The common law of defamation is an oddity of tort law, for it allows recovery of purportedly compensatory damages without evidence of actual loss. Under the traditional rules pertaining to actions for libel, the existence of injury is presumed from the fact of publication. Juries may award substantial sums as compensation for supposed damage to reputation without any proof that such harm actually occurred. The largely uncontrolled discretion of juries to award damages where there is no loss unnecessarily compounds the potential of any system of liability for defamatory falsehood to inhibit the vigorous exercise of First Amendment

freedoms. Additionally, the doctrine of presumed damages invites juries to punish unpopular opinion rather than to compensate individuals for injury sustained by the publication of a false fact. More to the point, the States have no substantial interest in securing for plaintiffs such as this petitioner gratuitous awards of money damages far in excess of any actual injury.

We would not, of course, invalidate state law simply because we doubt its wisdom, but here we are attempting to reconcile state law with a competing interest grounded in the constitutional command of the First Amendment. It is therefore appropriate to require that state remedies for defamatory falsehood reach no farther than is necessary to protect the legitimate interest involved. It is necessary to restrict defamation plaintiffs who do not prove knowledge of falsity or reckless disregard for the truth to compensation for actual injury. We need not define "actual injury," as trial courts have wide experience in framing appropriate jury instructions in tort actions. Suffice it to say that actual injury is not limited to out-of-pocket loss. Indeed, the more customary types of actual harm inflicted by defamatory falsehood include impairment of reputation and standing in the community, personal humiliation, and mental anguish and suffering. Of course, juries must be limited by appropriate instructions, and all awards must be supported by competent evidence concerning the injury, although there need be no evidence which assigns an actual dollar value to the injury.

We also find no justification for allowing awards of punitive damages against publishers and broadcasters held liable under state-defined standards of liability for defamation. In most jurisdictions jury discretion over the amounts awarded is limited only by the gentle rule that they not be excessive. Consequently, juries assess punitive damages in wholly unpredictable amounts bearing no necessary relation to the actual harm caused. And they remain free to use their discretion selectively to punish expressions of unpopular views. Like the doctrine of presumed damages, jury discretion to award punitive damages unnecessarily exacerbates the danger of media self-censorship, but, unlike the former rule, punitive damages are wholly irrelevant to the state interest that justifies a negligence standard for private defamation actions. They are not compensation for injury. Instead, they are private fines levied by civil juries to punish reprehensible conduct and to deter its future occurrence. In short, the private defamation plaintiff who establishes liability under a less demanding standard than that stated by *New York Times* may recover only such damages as are sufficient to compensate him for actual injury.

[The Court rejected respondent's argument that plaintiff was a public official or public figure, even though he appeared at the inquest or had once served on a city housing committee. Nor was he a public official even though he was a lawyer and therefore an officer of the court. Likewise, his general activities in community and professional affairs did not give him any "general fame or notoriety in the community" sufficient to make him a public figure.

Justice Blackmun concurred for two reasons. First, he thought that the Court's position gave the press sufficient protection against punitive damages. And second, although he supported the *Rosenbloom* plurality, he voted with the Court to make a majority for the Court "to come to rest in the defamation area."

Chief Justice Burger dissented, voting to reinstate the jury's verdict in favor of Gertz.

Justice Douglas dissented, for the reasons stated by Justice Black in *New York Times*.

Justice Brennan dissented, for the reasons stated in his *Rosenbloom* opinion.]

White, J., dissenting. For some 200 years—from the very founding of the Nation—the law of defamation and right of the ordinary citizen to recover for false publication injurious to his reputation have been almost exclusively the business of state courts and legislatures. . . .

But now, using [the First] Amendment as the chosen instrument, the Court, in a few printed pages, has federalized major aspects of libel law by declaring unconstitutional in important respects the prevailing defamation law in all or most of the 50 States. That result is

accomplished by requiring the plaintiff in each and every defamation action to prove not only the defendant's culpability beyond his act of publishing defamatory material but also actual damage to reputation resulting from the publication. Moreover, punitive damages may not be recovered by showing malice in the traditional sense of ill will; knowing falsehood or reckless disregard of the truth will now be required.

[Justice White then reviewed the 1938 Restatement of Torts on defamation and rejected the Court's opinion for "totally ignoring history and settled First Amendment law."]

The Court evinces a deep-seated antipathy to "liability without fault." But this catch-phrase has no talismanic significance and is almost meaningless in this context where the Court appears to be addressing those libels and slanders that are defamatory on their face and where the publisher is no doubt aware from the nature of the material that it would be inherently damaging to reputation. He publishes notwithstanding, knowing that he will inflict injury. . . .

In these circumstances, the law has heretofore put the risk of falsehood on the publisher where the victim is a private citizen and no grounds of special privilege are invoked. The Court would now shift this risk to the victim, even though he has done nothing to invite the calumny, is wholly innocent of fault, and is helpless to avoid his injury. I doubt that jurisprudential resistance to liability without fault is sufficient ground for employing the First Amendment to revolutionize the law of libel, and in my view, that body of legal rules poses no realistic threat to the press and its service to the public. The press today is vigorous and robust. To me, it is quite incredible to suggest that threats of libel suits from private citizens are causing the press to refrain from publishing the truth. I know of no hard facts to support that proposition, and the Court furnishes none.

[Justice White concluded that a concentrated communications industry was well-equipped to cope with the common law rules of defamation and attacked the Court for its rejection of the common law rules on actual and punitive damages.]

## NOTES

**1.** ***The Negligence Principle Under* Gertz.** Some sense of the size of the negligence barrier can be gleaned from the subsequent history of *Gertz*. On retrial, the jury awarded the plaintiff $100,000 in compensatory damages and $300,000 in punitive damages, sums far in excess of those awarded in the original action. On appeal, in Gertz v. Robert Welch Inc., 680 F.2d 527 (7th Cir. 1982), both elements of the award were upheld over a number of objections regarding (1) the proof of actual malice, (2) the ability of the plaintiff to relitigate the malice question, and (3) the clarity of the instructions on both actual and punitive damages.

**2.** ***Falsity?*** In Philadelphia Newspapers v. Hepps, 475 U.S. 767 (1986), the Supreme Court added a falsity requirement to *Gertz*'s fault requirement: "[W]e hold that, at least where a newspaper publishes speech of public concern, a private-figure plaintiff cannot recover damages without also showing that the statements at issue are false." The defendants had published five stories between May 1975 and May 1976 about Hepps and the corporation of which he was the principal stockholder. The stories claimed that both had links to organized crime and had used those connections "to influence the State's governmental processes, both legislative and administrative." The trial judge held that the plaintiff bore the burden of proving falsity, as distinguished from fault, and the Pennsylvania Supreme Court affirmed. The Supreme Court recognized that "[t]here will always be instances when the factfinding process will be unable to resolve conclusively whether the speech is true or false; it is in those cases that the burden of proof is dispositive." But, "where the scales are in such an uncertain

balance, we believe that the Constitution requires us to tip them in favor of protecting true speech." The Court thus erred on the side of "ensur[ing] that true speech on matters of public concern is not deterred." *Hepps* rejected the uniform common law view requiring the defendant to demonstrate the truth of his statements. Wholly apart from the Constitution, are there good reasons to question the common law allocation of burden of proof?

A number of states have similarly treated falsity as an element of a prima facie case for defamation by analogy to ordinary misrepresentation cases. See, e.g., Solaia Tech., LLC v. Specialty Publ'g Co., 852 N.E.2d 825 (Ill. 2006) ("To state a defamation claim, a plaintiff must present facts showing that the defendant made a false statement about the plaintiff"); Lester v. Powers, 596 A.2d 65 (Me. 1991) ("[A defamatory] statement must be false"); Pegasus v. Reno Newspapers, Inc., 57 P.3d 82 (Nev. 2002) ("Defamation is a publication of a false statement of fact"). However, not all states adhere to this notion that a statement must be false to be actionable as defamatory. See, e.g., Shaefer v. Lynch, 406 So. 2d 185 (La. 1981) ("[T]ruthful statements which carry a defamatory implication can be actionable").

Other states have not insisted on falsity as an element of all defamation claims. Instead courts presume that the alleged defamatory matter is false and retain "substantial truth" as a defense to a defamation claim. These states effectively place the burden of proving that the alleged defamatory matter is true on the defendant rather than forcing the plaintiff to prove falsity as a threshold matter. What are the benefits of such a regime? What are the cons?

## *Dun & Bradstreet, Inc. v. Greenmoss Builders, Inc.*

472 U.S. 752 (1985)

Powell, J. In *Gertz*, we held that the First Amendment restricted the damages that a private individual could obtain from a publisher for a libel that involved a matter of public concern. More specifically, we held that in these circumstances the First Amendment prohibited awards of presumed and punitive damages for false and defamatory statements unless the plaintiff shows "actual malice," that is, knowledge of falsity or reckless disregard for the truth. The question presented in this case is whether this rule of *Gertz* applies when the false and defamatory statements do not involve matters of public concern.

Petitioner Dun & Bradstreet, a credit reporting agency, provides subscribers with financial and related information about businesses. All the information is confidential; under the terms of the subscription agreement the subscribers may not reveal it to anyone else. On July 26, 1976, petitioner sent a report to five subscribers indicating that respondent, a construction contractor, had filed a voluntary petition for bankruptcy. This report was false and grossly misrepresented respondent's assets and liabilities. That same day, while discussing the possibility of future financing with its bank, respondent's president was told that the bank had received the defamatory report. He immediately called petitioner's regional office, explained the error, and asked for a correction. In addition, he requested the names of the firms that had received the false report in order to assure them that the company was solvent. Petitioner promised to look into the matter but refused to divulge the names of those who had received the report.

After determining that its report was indeed false, petitioner issued a corrective notice on or about August 3, 1976, to the five subscribers who had received the initial report. The notice stated that one of respondent's former employees, not respondent itself, had filed for bankruptcy and that respondent "continued in business as usual." Respondent told petitioner that it was dissatisfied with the notice, and it again asked for a list of subscribers who had seen the initial report. Again petitioner refused to divulge their names.

Respondent then brought this defamation action in Vermont state court. It alleged that the false report had injured its reputation and sought both compensatory and punitive damages.

The trial established that the error in petitioner's report had been caused when one of its employees, a 17-year-old high school student paid to review Vermont bankruptcy pleadings, had inadvertently attributed to respondent a bankruptcy petition filed by one of respondent's former employees. Although petitioner's representative testified that it was routine practice to check the accuracy of such reports with the businesses themselves, it did not try to verify the information about respondent before reporting it.

After trial, the jury returned a verdict in favor of respondent and awarded $50,000 in compensatory or presumed damages and $300,000 in punitive damages. Petitioner moved for a new trial. It argued that in *Gertz*, this Court had ruled broadly that "the States may not permit recovery of presumed or punitive damages, at least when liability is not based on a showing of knowledge of falsity or reckless disregard for the truth," and it argued that the judge's instructions in this case permitted the jury to award such damages on a lesser showing. . . .

. . . In *Gertz*, we held that the fact that expression concerned a public issue did not by itself entitle the libel defendant to the constitutional protections of *New York Times*. These protections, we found, were not "justified solely by reference to the interest of the press and broadcast media in immunity from liability." *Id*. at 343. . . .

. . . We have never considered whether the *Gertz* balance obtains when the defamatory statements involve no issue of public concern. To make this determination, we must employ the approach approved in *Gertz* and balance the State's interest in compensating private individuals for injury to their reputation against the First Amendment interest in protecting this type of expression. The state interest is identical to the one weighted in *Gertz*. There we found that it was "strong and legitimate." *Id*. at 348. . . .

. . . The First Amendment interest, on the other hand, is less important than the one weighted in *Gertz*. We have long recognized that not all speech is of equal First Amendment importance. It is speech on "'matters of public concern'" that is "at the heart of the First Amendment's protection." . . .

. . . In *Gertz*, we found that the state interest in awarding presumed and punitive damages was not "substantial" in view of their effect on speech at the core of First Amendment concern. This interest, however, *is* "substantial" relative to the incidental effect these remedies may have on speech of significantly less constitutional interest . . .

. . . The only remaining issue is whether petitioner's credit report involved a matter of public concern. In a related context, we have held that "[w]hether . . . speech addresses a matter of public concern must be determined by [the expression's] content, form, and context . . . as revealed by the whole record." These factors indicate that petitioner's credit report contains no public issue. It was speech solely in the individual interest of the speaker and its specific business audience. This particular interest warrants no special protection when — as in this case — the speech is wholly false and clearly damaging to the victim's business reputation. . . .

. . . In addition, the speech here, like advertising, is hardy and unlikely to be deterred by incidental state regulation. . . .

. . . We conclude that permitting recovery of presumed and punitive damages in defamation cases absent a showing of "actual malice" does not violate the First Amendment when the defamatory statements do not involve matters of public concern.

## NOTES

**1.** ***Presumed Damages in Matters of Private Concern After* Dun & Bradstreet.** The Court's holding that the credit report was not directed to a public issue — "It was speech solely in the individual interest of the speaker and its specific business audience" — was badly fractured; only three Justices (Powell, Rehnquist, and O'Connor) adopted this middle course.

Two Justices (Burger and White) concurred in the result. Justice White concluded his long opinion by urging that *Gertz* be overruled, and further that "the defamatory publication in this case does not deal with a matter of public importance." The four dissenting Justices took exactly the opposite tack and urged that the speech involved in this case deserved explicit constitutional protection.

> The credit reporting at issue here surely involves a subject matter of sufficient public concern to require the comprehensive protections of *Gertz*. Were this speech appropriately characterized as a matter of only private concern, moreover, the elimination of the *Gertz* restrictions on presumed and punitive damages would still violate basic First Amendment requirements.

**2. *State Law Responses.***

(a) *Culpability standard. Gertz* treats negligence as the minimum threshold in defamation cases brought by private parties but allows states to impose more stringent requirements on plaintiffs. *Dun & Bradstreet* did not address *Gertz*'s culpability standard, and thus leaves open whether states could revert to a strict liability standard when private plaintiffs sue defendants on matters of no public concern.

More than forty states and the District of Columbia have at present chosen to adhere to *Gertz*'s negligence standard in suits by private figures against media defendants on matters of public concern. Only four states — Alaska, Colorado, Indiana, and New Jersey — require that the plaintiff prove actual malice. See Rodney A. Smolla, 1 Law of Defamation §§3.30-.31 (2d ed. 2015). Early on, New York adopted a gross negligence standard, requiring that "the publisher acted in a grossly irresponsible manner without due consideration for the standards of information gathering and dissemination ordinarily followed by responsible parties." Chapadeau v. Utica Observer-Dispatch, 341 N.E. 569 (N.Y. 1975). But New York has since moved away from this gross negligence standard, joining the majority of states in applying a simple negligence standard in such cases. See Gottwald v. Sebert, 220 N.E.3d 621 (N.Y. 2023) ("In New York, the accepted standard for [defamation cases brought by] private figures is negligence").

(b) *Presumed damages*. *Dun & Bradstreet* revisited *Gertz*'s second holding on presumed and punitive damages. Massachusetts, fearing "excessive and unbridled jury verdicts," abolished punitive damage actions after *Gertz* "in any defamation action, on any state of proof, whether based in negligence or reckless or wilful conduct." Stone v. Essex County Newspapers, Inc., 330 N.E.2d 161 (Mass. 1975). And in West v. J. Greg Allen Builder, Inc., 92 N.E.3d 634, 648 (Ind. Ct. App. 2017), the Court of Appeals of Indiana addressed presumed damages in the context of an alleged defamatory statement arising out of a homebuilding corporation's suit against its former president for breaches of fiduciary duties. Although the court did not address the plaintiff's private-figure status or whether the dispute was a matter of private concern, both conclusions seem apt, at least by way of analogy to the credit reporting dispute in *Dun & Bradstreet*. The court in *J. Greg Allen Builder* reversed a trial court's award of punitive damages based on insufficient evidence to sustain a jury finding of actual malice. But the court also characterized the allegations as libel per se and explained that "the law presumes damages in cases of defamation *per se*," which "would seem to relieve a plaintiff of the burden of proving malice." *Id*. at 647 n.2. Thus Indiana seems to split the baby. It adheres to the *Gertz* rule requiring actual malice for *punitive* damages, even where *Gertz* does not apply — in a situation involving a private-figure plaintiff and a matter of private concern — but it dispenses with *Gertz*'s actual malice requirement for *presumed* damages.

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Other jurisdictions have also continued to award presumed damages in cases where private plaintiffs sue for matters of private concern. In Bierman v. Weier, 826 N.W.2d 436, 454–55 (Iowa 2013), the defendant published a book in which he mentioned that his ex-wife had been molested by her father and suffered from severe mental illness. Both the defendant's ex-wife and her father sued for defamation. The court ruled in favor of retaining Iowa's longstanding rule of libel per se and the presumed damages that come with it. The court reasoned that the rule allowing presumed damages was "a useful rule in an area where it is often difficult . . . to prove actual damages," especially in cases brought by private plaintiffs regarding matters of private concern. The New Jersey Supreme Court similarly supported the award of presumed damages in W.J.A. v. D.A., 43 A.3d 1148, 1158–60 (N.J. 2012). In that case, the defendant created a website and posted accusing the plaintiff, his uncle, of sexually abusing him as a child while claiming that the plaintiff perjured himself and intimidated witnesses at a trial related to the abuse allegations. The court ruled that New Jersey should continue to award presumed damages based on the theory that "damage to reputation logically flows from defamation." Furthermore, the court argued that a rule abolishing presumed damages and requiring plaintiffs to prove actual damages would "force an average citizen to ferret out proof of loss of reputation from any of the world-wide potential viewers of the defamatory Internet transmission about that otherwise private person."

## *Obsidian Finance Group, LLC v. Cox*

740 F.3d 1284 (9th Cir. 2014)

Hurwitz, Circuit Judge:

This case requires us to address a question of first impression: What First Amendment protections are afforded a blogger sued for defamation? We hold that liability for a defamatory blog post involving a matter of public concern cannot be imposed without proof of fault and actual damages.

### I.

Kevin Padrick is a principal of Obsidian Finance Group, LLC (Obsidian), a firm that provides advice to financially distressed businesses. In December 2008, Summit Accommodators, Inc. (Summit), retained Obsidian in connection with a contemplated bankruptcy. After Summit filed for reorganization, the bankruptcy court appointed Padrick as the Chapter 11 trustee. Because Summit had misappropriated funds from clients, Padrick's principal task was to marshal the firm's assets for the benefit of those clients.

After Padrick's appointment, Crystal Cox published blog posts on several websites that she created, accusing Padrick and Obsidian of fraud, corruption, money-laundering, and other illegal activities in connection with the Summit bankruptcy. Cox apparently has a history of making similar allegations and seeking payoffs in exchange for retraction. Padrick and Obsidian sent Cox a cease-and-desist letter, but she continued posting allegations. This defamation suit ensued.

### A.

The district court held that all but one of Cox's blog posts were constitutionally protected opinions because they employed figurative and hyperbolic language and could not be proved true or false. The court held, however, that a December 25, 2010 blog post on

bankruptcycorruption.com made "fairly specific allegations [that] a reasonable reader could understand . . . to imply a provable fact assertion"—i.e., that Padrick, in his capacity as bankruptcy trustee, failed to pay $174,000 in taxes owed by Summit. The district judge therefore allowed that single defamation claim to proceed to a jury trial. The jury found in favor of Padrick and Obsidian, awarding the former $1.5 million and the latter $1 million in compensatory damages.

### B.

. . .

After closing arguments, the district court instructed the jury that under Oregon law, "Defendant's knowledge of whether the statements at issue were true or false and defendant's intent or purpose in publishing those statements are not elements of the claim and are not relevant to the determination of liability." The court further instructed that the "plaintiffs are entitled to receive reasonable compensation for harm to reputation, humiliation, or mental suffering even if plaintiff does not present evidence that proves actual damages . . . because the law presumes that the plaintiffs suffered these damages." The jury verdicts in favor of Padrick and Obsidian followed. . . .

## II.

Cox does not contest on appeal the district court's finding that the December 25 blog post contained an assertion of fact; nor does she contest the jury's conclusions that the post was false and defamatory. She challenges only the district court's rulings that (a) liability could be imposed without a showing of fault or actual damages and (b) Padrick and Obsidian were not public officials. . . .

This case involves the intersection between *Sullivan* and *Gertz* [on the choice between actual malice and ordinary negligence] in the context of a medium of publication—the Internet—entirely unknown at the time of those decisions.

### 1.

Padrick and Obsidian first argue that the *Gertz* negligence requirement applies only to suits against the institutional press. Padrick and Obsidian are correct in noting that *Gertz* involved an institutional media defendant and that the Court's opinion specifically cited the need to shield "the press and broadcast media from the rigors of strict liability for defamation." We conclude, however, that the holding in *Gertz* sweeps more broadly.

The *Gertz* court did not expressly limit its holding to the defamation of institutional media defendants. And, although the Supreme Court has never directly held that the *Gertz* rule applies beyond the institutional press, it has repeatedly refused in non-defamation contexts to accord greater First Amendment protection to the institutional media than to other speakers. [The opinion then discusses relevant Supreme Court precedent in trespass, copyright, and campaign finance contexts. Moreover "every other circuit to consider the issue has held that the First Amendment defamation rules in *Sullivan* and its progeny apply equally to the institutional press and individual speakers."]

. . . The protections of the First Amendment do not turn on whether the defendant was a trained journalist, formally affiliated with traditional news entities, engaged in conflict-of-interest disclosure, went beyond just assembling others' writings, or tried to get both sides of a story. As the Supreme Court has accurately warned, a First Amendment distinction between the institutional press and other speakers is unworkable: "With the advent of the Internet and the decline of print and broadcast media . . . the line between the media and others who wish to comment on political and social issues becomes far more blurred." [Citizens United v. Fed. Election Comm'n, 558 U.S. 310, 352 (2010).] In defamation cases, the

public-figure status of a plaintiff and the public importance of the statement at issue — not the identity of the speaker — provide the First Amendment touchstones.

We therefore hold that the *Gertz* negligence requirement for private defamation actions is not limited to cases with institutional media defendants. But this does not completely resolve the *Gertz* dispute. Padrick and Obsidian also argue that they were not required to prove Cox's negligence because *Gertz* involved a matter of public concern and this case does not.

2.

The Supreme Court has "never considered whether the *Gertz* balance obtains when the defamatory statements involve no issue of public concern." *Dun & Bradstreet*, [*supra*]. But even assuming that *Gertz* is limited to statements involving matters of public concern, Cox's blog post qualifies.

The December 25 post alleged that Padrick, a court-appointed trustee, committed tax fraud while administering the assets of a company in a Chapter 11 reorganization, and called for the "IRS and the Oregon Department of Revenue to look" into the matter. Public allegations that someone is involved in crime generally are speech on a matter of public concern. . . .

Cox's allegations in this case are similarly a matter of public concern. Padrick was appointed by a United States Bankruptcy Court as the Chapter 11 trustee of a company that had defrauded its investors through a Ponzi scheme. That company retained him and Obsidian to advise it shortly before it filed for bankruptcy. The allegations against Padrick and his company raised questions about whether they were failing to protect the defrauded investors because they were in league with their original clients.

Unlike the speech at issue in *Dun & Bradstreet* that the Court found to be a matter only of private concern, Cox's December 25 blog post was not "solely in the individual interest of the speaker and its specific business audience." The post was published to the public at large, not simply made "available to only five subscribers, who, under the terms of the subscription agreement, could not disseminate it further. . . ." And, Cox's speech was not "like advertising" and thus "hardy and unlikely to be deterred by incidental state regulation."

Because Cox's blog post addressed a matter of public concern, even assuming that *Gertz* is limited to such speech, the district court should have instructed the jury that it could not find Cox liable for defamation unless it found that she acted negligently. The court also should have instructed the jury that it could not award presumed damages unless it found that Cox acted with actual malice.

C.

Cox also argues that Padrick and Obsidian are "tantamount to public officials," because Padrick was a court-appointed bankruptcy trustee. She contends that the jury therefore should have been instructed that, under the *Sullivan* standard, it could impose liability for defamation only if she acted with actual malice. We disagree.

Although bankruptcy trustees are "an integral part of the judicial process," neither Padrick nor Obsidian became public officials simply by virtue of Padrick's appointment. Padrick was neither elected nor appointed to a government position, and he did not exercise "substantial . . . control over the conduct of governmental affairs.". . . No one would contend that a debtor-in-possession has become a public official simply by virtue of seeking Chapter 11 protection, and we can reach no different conclusion as to the trustee who substitutes for the debtor in administering a Chapter 11 estate. . . .

IV.

We reverse the district court's judgment against Cox concerning the December 25, 2010 blog post and remand for a new trial consistent with this opinion.

## NOTES

**1.** ***Media Versus Nonmedia Defendants.*** Many states apply *Gertz*—with its negligence threshold—to nonmedia as well as media defendants. See, e.g., Jacron Sales Co. v. Sindorf, 350 A.2d 688 (Md. 1976); Internet Sols. Corp. v. Marshall, 39 So. 3d 1201 (Fla. 2010); Toler v. Süd-Chemie, Inc., 458 S.W.3d 276 (Ky. 2014); Am. Future Sys. Inc. v. Better Bus. Bureau of E. Pa., 923, A.2d 389 (Pa. 2007); Skaskiw v. Vt. Agency of Agric., 112 A.3d 1277 (Vt. 2014). Oregon, in sharp contrast, reads *Gertz* more narrowly. Lowell v. Wright, 512 P.3d 403, 422 (Or. 2022), reaffirmed that "plaintiffs must prove that a defendant acted with actual malice to obtain presumed damages only if the defendant is a media defendant." Other states, such as Utah, have followed the Supreme Court in not ruling directly on the matter whether proof of actual malice is required in cases involving nonmedia defendants. See Ferguson v. Williams & Hunt, Inc., 221 P.3d 213–14 (Utah 2009) ("we leave open this question regarding strict liability in a purely private defamation action").

In determining "matters of public concern," should the identity of the defendant matter? In Maethner v. Someplace Safe, Inc., 929 N.W.2d 868, 877 (Minn. 2019), a husband alleged that his former wife defamed him by posting on a social-networking page pictures and statements that identified her as a survivor of domestic violence. He also alleged that Someplace Safe, a domestic violence advocacy organization, defamed him by presenting his former wife with a survivor award at a banquet, which it then publicized both in its press release and on its social-networking page. The Minnesota Court of Appeals allowed the case to go the jury. Gildea, C.J., reversed, holding that both defendants were entitled to summary judgment. She did not differentiate the two cases because Someplace Safe made its false statements as part of a highly publicized fundraising campaign.

> Taking *Gertz* and *Dun & Bradstreet* together, the proper focus regarding the availability of presumed damages is not on the status of the defendant as a media or nonmedia defendant. Rather, the dispositive inquiry is whether the matter at issue is one of public concern. The fact that the defendant is a member of the media may be relevant to determining whether a matter is one of public concern, but it is not, as the court of appeals suggested, the dispositive inquiry.

In whose favor should the defendant's media status cut?

**2.** ***Matters of Public Concern Revived?*** The "matter of public concern" test of Brennan, J. in *Rosenbloom* received an indirect boost in Snyder v. Phelps, 562 U.S. 443 (2011). *Snyder* involved a claim of intentional infliction of emotional distress on the family of a fallen Marine, which arose when the defendant members of the Westboro Baptist Church picketed near the funeral service of the plaintiff's son but stayed out of sight and hearing from the service. Even though the claim for defamation had been dropped below, Roberts, C.J., held that because the picketers addressed a matter of public concern, they were entitled to First Amendment protection.

> [E]ven if a few of the signs—such as "You're Going to Hell" and "God Hates You"—were viewed as containing messages related to [the private-figure plaintiffs] specifically, that would not change the fact that the overall thrust and dominant theme of [the church group's] demonstration spoke to broader public issues.

Controversy over "matters of public concern" is especially rich in the Internet age. Consider Johnson v. Freborg, 995 N.W.2d 374 (Minn. 2023), where the defendant accused three dance instructors of subjecting her to varying degrees of sexual assault in a post on her Facebook account. The Minnesota Supreme Court, reviewing only the question whether the post was a matter of public concern, deemed that the matter was of public concern because "the dominant theme of her posts speaks to the broader issue of sexual abuse in the context of the #MeToo movement." In reaching this determination, the Court acknowledged that "the context of the #MeToo movement is a key factor in our analysis," and relied on the fact that

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the defendant included the "#MeToo" hashtag in the post at issue in the case. To what extent has the Internet changed our understanding of matters of public concern? How has it eroded the public/private figure distinction?

**3.** ***What Remains a Matter of Private Concern?*** A recent high school graduate sued the operator of Gawker, an Internet news and gossip website. Gawker published a picture from her high school yearbook on the Internet in which she allegedly exposed her genitals during a graduation ceremony. In concluding that this was a private controversy (and thus Gawker was not protected by the First Amendment), Voorhees, J., reasoned:

> In balancing the curiosity of the public against the potential effect on the public [prior cases have] crafted a spectrum against which cases should be judged: on the one end are public policy issues affecting a genuine public controversy; on the other are lurid personal matters that capture only the voyeuristic attention of the people.

Araya v. Deep Dive Media, LLC, 966 F. Supp. 2d 582, 592 (W.D.N.C. 2013).

**4.** ***X (Formerly Twitter) and Instagram?*** How should courts apply traditional defamation standards to social media platforms such as X (formerly Twitter)? If the posted defamatory content is exhibited through merely reposting a defamatory article or a hyperlink to the defamatory article, the poster is generally held to be immune from liability. See, e.g., Mirage Ent., Inc. v. FEG Entretenimientos S.A., 326 F. Supp. 3d 26, 39 (S.D.N.Y. 2018) (holding that a defendant did not republish defamatory content within an online article by tweeting a hyperlink to it). Some courts, however, have held that posters may lose this immunity if the post includes language that furthers the defamatory nature of the underlying content. See Roca Labs, Inc. v. Consumer Op. Corp., 140 F. Supp. 3d 1311, 1321 (M.D. Fla. 2015) (holding that one who reposts loses CDA immunity by "substantively alter[ing] third-party content or becom[ing] directly involved in the alleged illegality"). Should retractions be required in cases of falsity, even without proof of actual damages?

With the rise of social media celebrities and bloggers, how should traditional defamation law respond to Internet defamation? DeSimone, Insta-Famous: Challenges and Obstacles Facing Bloggers and Social Media Personalities in Defamation Cases, 11 Mod. Am. 70, 71 (2018), probes how to classify "Insta-famous" celebrities for defamation purposes. Fashion bloggers such as Chiara Gerragni and Leandra Medine, who became financially successful by using social media accounts, are classified as limited purpose public figures because they "set themselves apart from recreational Internet users and make it clear that their intended use is to make money." But such fashion bloggers typically share their personal lives as "part of their overall business plan — they are creating an image and using their interests and likeability in order to create a sense of friendship with their followers." As limited purpose public figures, do such fashion bloggers operating over social media make attacks on their personal life fair game?

**5.** ***Fact vs. Opinion for Defamatory Statements on the Internet.*** Applying defamation law to statements made via social media platforms also raises anew questions about whether the statements made are ones of fact or opinion. Several courts have noted that the distinct conventions of communicating on social media platforms may influence that determination and, thus, may also influence whether such statements are actionable as defamation. See, e.g., Giduck v. Niblett, 408 P.3d 856 (Colo. App. 2014) ("the fact that these statements were placed in an online community where anonymous individuals can express highly biased opinions weighs in favor of finding these statements to be opinion"); Rochester City Lines, Co. v. City of Rochester, 846 N.W.2d 444 (Minn. Ct. App. 2014) ("[Defendant's] statements were made on his personal website and on a social media website. Therefore, the context of his statements was inherently informal"). Should the fora in which statements are made be determinative of their status as statements of fact or opinion? Determinative of whether they are actionable as defamatory?

**6. *Institutional Protections for Bloggers.*** Should bloggers and others who post materials on social media platforms be entitled to the same institutional protections afforded to traditional print and broadcast media throughout the twentieth century? Jack M. Balkin, How to Regulate (and Not Regulate) Social Media, 1 J. Free Speech L. 71 (2021), argues that they should be. Balkin argues that social media plays a similar role to print and broadcast media in the twentieth century by curating public opinion on matters related to art, politics, and culture. However, print and broadcast media curated public opinion through exercising editorial judgment. This differs dramatically from the role of social media in curating public opinion, as social media platforms do not post their own content and instead rely on the content posted by third parties on their platforms. Balkin therefore argues that the contemporary social media landscape lacks the knowledge institutions and knowledge professionals that helped traditional media produce and disseminate knowledge and opinion while also fostering a degree of trust in the institutions.

Balkin proposes three policy levers to incentivize such companies to professionalize and take greater responsibility for the information disseminated on the platforms: (1) using antitrust and competition law to encourage a large number of social media companies and to divorce advertising from moderation; (2) imposing a fiduciary model on social media companies that collect and use data so that social media companies owe their users duties of care, confidentiality, and loyalty in the use of their data; and (3) utilizing intermediary liability to hold social media companies responsible for unlawful content if they receive notice that content posted on their platforms is unlawful and yet fail to remove the content in question within a particular period of time (i.e., a notice-and-take-down scheme).

Would such regulatory measures and changes in policy incentivize social media companies to improve the social functions of their platforms? What problems might accompany the imposition of these regulatory and policy changes? How else might the incentives of social media companies change?

**7. *Defamation and Liability Insurance.*** To what extent is a robust liability insurance system a substitute for — or complement to — *Sullivan*'s remedy for chilling effects? Professor Kenneth Abraham argues that liability insurance, like *Sullivan* and its progeny, provides "breathing space" for speech tort defendants insofar as insurance precludes liability even for some unprotected speech. See Kenneth S. Abraham, Free Speech, Breathing Space, and Liability Insurance (May 7, 2024), Virginia Public Law and Legal Theory Research Paper No. 2024-38, https://ssrn.com/abstract=8420245, at 3, 19, 29–36.

Note how both the First Amendment cases and the existence of liability insurance invite a "consequentialist" conception of speech torts — as "breathing space for speech is the most consequentialist of concerns." But liability insurance adds a protective layer: It offsets the substantial legal fees that even *victorious* defendants face in the *Sullivan* regime. *See id.* at 14 (surveying cases and noting that a majority were resolved by potentially fee-intensive dispositive motions in favor of defendants). Moreover, such policies typically cover the costs of defending against plaintiffs who are unable to meet the actual malice standard.

Moreover, the "moral hazard" objection that deterrence theorists may raise against insurance — namely, that insured parties exercise less care than they otherwise would — works in *favor* of liability insurance for speech torts. That is because *Sullivan* and its progeny carve out a realm of *unprotected* speech for which defendants are nonetheless not liable by virtue of the actual malice standard. Liability insurance replicates this protection. One emerging question is whether nontraditional media defendants, such as blogs, can obtain coverage. Recall that *Obsidian*, *supra* at 405, clarified that *Gertz* is not limited to traditional media defendants. Does *Obsidian* counsel in favor of extending liability insurance coverage to blogs and the like? Should media defendants enjoy greater coverage than their nonmedia counterparts?

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# CHAPTER 7

# PRIVACY

## SECTION A. INTRODUCTION

By all accounts, the protection of the individual interest in privacy is one of the essential tasks of any civilized society. Before the late nineteenth century, tort law supplied no generalized remedy for the invasion of privacy as such but relied on other legal devices to maintain privacy protection. Thus the basic rules of private ownership, backed by the common law of trespass to land, allowed individuals to wall off their lands or buildings to preserve some measure of privacy. In addition, confidentiality arrangements, both by explicit agreement and common practice, allowed people to keep private sensitive information and records that they shared with physicians, employers, and insurers. But the great challenge in this area asks about the extent to which these traditional property, tort, and contract rules can cover the full range of privacy issues.

Historically, the creation of a separate and distinct tort of privacy was long in coming. Starting in the late nineteenth century, both commentators and judges began to move on this issue. The pattern of development was twofold from the outset. On one hand, the protection of the privacy interest was viewed defensively, enabling individuals to ward off the invasions of strangers. Elsewhere privacy protection served the opposite purpose, allowing individuals the exclusive right to the commercial use of their name and likeness, in what has come to be called the right of publicity.

This chapter explores the interrelationship among these themes. Section B traces the historical evolution of the privacy right from the classic article by Samuel Warren and Louis Brandeis through the early development of the doctrine. The next four sections take up the four standard heads of privacy analysis first articulated by Prosser in 1960: intrusion upon seclusion, public disclosure of embarrassing private facts, false light, and the right of publicity.

How well do these categories work in the age of social media and artificial intelligence (AI)? Since Prosser, the new technologies of the information age have spawned a new set of privacy issues, arising in our era of instant communications by mobile devices, the increased activity of social media sites, the rapid and extensive exchange of computerized information, and the development of data banks exploited by AI-enabled search engines. Large corporations like Meta (formerly Facebook) and Google base their business models on collecting, analyzing, and selling user data. The numbers speak volumes. As of 2024, many social media platforms have hundreds of millions if not billions of monthly active users: Facebook, 3.06 billion; YouTube, 2.5 billion; Instagram, 2 billion; WhatsApp, 1.58 billion; TikTok, 1.58 billion; Snapchat, 800 million; and X/Twitter, 611 million. See Simon Kemp, Digital 2024 April Global Statshot Report, DataReportal (Apr. 24, 2024), https://datareportal.com/reports/digital-2024-april-global-statshot.

Whereas some members of society ask for increased protection of privacy interests, others question the viability of privacy when individuals voluntarily disclose details of their private lives on blogs and social media websites on a regular basis. What privacy interests, if any, still



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warrant protection? U.S. courts, with a contractual orientation, have tended to respond by holding that individuals have a reasonable expectation of privacy wherever the Internet company voluntarily *creates* just that expectation by publishing a statement or policy indicating it will not collect or retain certain types of data. However, where a company clearly discloses the types of data it collects and how they will be used, courts tend to find that consumers have no reasonable expectation of privacy when the firms comply with their stated policies. In the European Union, statutory responses such as the General Data Privacy Regulation (GDPR) and the Digital Services Act (DSA) take a less contractual, more privacy-protective approach, requiring companies engaged in data collection or storage to publish and comply with data privacy policies. In the United States, state statutory responses such as California's Privacy Rights Act are beginning to expand protections for consumers in a way that resembles the protections granted by the GDPR and DSA. Moreover, other statutory responses in the United States, such as the Colorado Privacy Act, aim to establish a framework for handling new pressing issues in the privacy sphere like the use of AI in processing personal data for decision-making purposes.

## SECTION B. HISTORICAL BACKGROUND

**Samuel Warren & Louis B. Brandeis**

### *The Right to Privacy*

4 Harv. L. Rev. 193, 193–97 (1890)

That the individual shall have full protection in person and in property is a principle as old as the common law; but it has been found necessary from time to time to define anew the exact nature and extent of such protection. Political, social, and economic changes entail the recognition of new rights, and the common law, in its eternal youth, grows to meet the demands of society. Thus, in very early times, the law gave a remedy only for physical interference with life and property, for trespasses vi et armis. Then the "right to life" served only to protect the subject from battery in its various forms; liberty meant freedom from actual restraint; and the right to property secured to the individual his lands and his cattle. Later, there came a recognition of man's spiritual nature, of his feelings and his intellect. Gradually the scope of these legal rights broadened; and now the right to life has come to mean the right to enjoy life,—the right to be let alone; the right to liberty secures the exercise of extensive civil privileges; and the term "property" has grown to comprise every form of possession—intangible, as well as tangible.

Thus, with the recognition of the legal value of sensations, the protection against actual bodily injury was extended to prohibit mere attempts to do such injury; that is, the putting another in fear of such injury. From the action of battery grew that of assault. Much later there came a qualified protection of the individual against offensive noises and odors, against dust and smoke, and excessive vibration. The law of nuisance was developed. So regard for human emotions soon extended the scope of personal immunity beyond the body of the individual. His reputation, the standing among his fellow-men, was considered, and the law of slander and libel arose. Man's family relations became a part of the legal conception of his life, and the alienation of a wife's affections was held remediable. Occasionally the law halted,—as in its refusal to recognize the intrusion by seduction upon the honor of the family. But even here the demands of society were met. A mean fiction, the action per quod servitium amisit [through which the wife's services have been lost], was resorted to, and by allowing damages

for injury to the parents' feelings, an adequate remedy was ordinarily afforded. Similar to the expansion of the right to life was the growth of the legal conception of property. From corporeal property arose the incorporeal rights issuing out of it; and then there opened the wide realm of intangible property, in the products and processes of the mind, as works of literature and art, goodwill, trade secrets, and trademarks.

This development of the law was inevitable. The intense intellectual and emotional life, and the heightening of sensations which came with the advance of civilization, made it clear to men that only a part of the pain, pleasure, and profit of life lay in physical things. Thoughts, emotions, and sensations demanded legal recognition, and the beautiful capacity for growth which characterizes the common law enabled the judges to afford the requisite protection, without the interposition of the legislature.

Recent inventions and business methods call attention to the next step which must be taken for the protection of the person, and for securing to the individual what Judge Cooley calls the right "to be let alone." Instantaneous photographs and newspaper enterprise have invaded the sacred precincts of private and domestic life; and numerous mechanical devices threaten to make good the prediction that "what is whispered in the closet shall be proclaimed from the house-tops." For years there has been a feeling that the law must afford some remedy for the unauthorized circulation of portraits of private persons; and the evil of the invasion of privacy by the newspapers, long keenly felt, has been but recently discussed by an able writer. . . .

Of the desirability — indeed of the necessity — of some such protection, there can, it is believed, be no doubt. The press is overstepping in every direction the obvious bounds of propriety and decency. Gossip is no longer the resource of the idle and of the vicious, but has become a trade, which is pursued with industry as well as effrontery. To satisfy a prurient taste the details of sexual relations are spread broadcast in the columns of the daily papers. To occupy the indolent, column upon column is filled with idle gossip, which can only be procured by intrusion upon the domestic circle. The intensity and complexity of life, attendant upon advancing civilization, have rendered necessary some retreat from the world, and man, under the refining influence of culture, has become more sensitive to publicity, so that solitude and privacy have become more essential to the individual; but modern enterprise and invention have, through invasions upon his privacy, subjected him to mental pain and distress, far greater than could be inflicted by mere bodily injury. Nor is the harm wrought by such invasions confined to the suffering of those who may be made the subjects of journalistic or other enterprise. In this, as in other branches of commerce, the supply creates the demand. Each crop of unseemly gossip, thus harvested, becomes the seed of more, and, in direct proportion to its circulation, results in a lowering of social standards and of morality. Even gossip apparently harmless, when widely and persistently circulated, is potent for evil. It both belittles and perverts. It belittles by inverting the relative importance of things, thus dwarfing the thoughts and aspirations of a people. When personal gossip attains the dignity of print, and crowds the space available for matters of real interest to the community, what wonder that the ignorant and thoughtless mistake its relative importance. Easy of comprehension, appealing to that weak side of human nature which is never wholly cast down by the misfortunes and frailties of our neighbors, no one can be surprised that it usurps the place of interest in brains capable of other things. Triviality destroys at once robustness of thought and delicacy of feeling. No enthusiasm can flourish, no generous impulse can survive under its blighting influence.

It is our purpose to consider whether the existing law affords a principle which can properly be invoked to protect the privacy of the individual and, if it does, what the nature and extent of such protection is.

## NOTES

**1.** ***Inspiration for Seminal Privacy Article?*** William L. Prosser, Privacy, 48 Calif. L. Rev. 383, 383–84 (1960) recounts:

> In the year 1890 Mrs. Samuel D. Warren, a young matron of Boston, which is a large city in Massachusetts, held at her home a series of social entertainments on an elaborate scale. She was the daughter of Senator Bayard of Delaware, and her husband was a wealthy young paper manufacturer, who only the year before had given up the practice of law to devote himself to an inherited business. Socially Mrs. Warren was among the élite; and the newspapers of Boston, and in particular the *Saturday Evening Gazette*, which specialized in "blue blood" items, covered her parties in highly personal and embarrassing detail. It was the era of "yellow journalism," when the press had begun to resort to excesses in the way of prying that have become more or less commonplace today; and Boston was perhaps, of all of the cities in the country, the one in which a lady and a gentleman kept their names and their personal affairs out of the papers. The matter came to a head when the newspapers had a field day on the occasion of the wedding of a daughter, and Mr. Warren became annoyed. It was an annoyance for which the press, the advertisers and the entertainment industry of America were to pay dearly over the next seventy years.
>
> Mr. Warren turned to his recent law partner, Louis D. Brandeis, who was destined not to be unknown to history. The result was a noted article, The Right to Privacy, in the Harvard Law Review, upon which the two men collaborated. It has come to be regarded as the outstanding example of the influence of legal periodicals upon the American law. In the Harvard Law School class of 1877 the two authors had stood respectively second and first, and both of them were gifted with scholarship, imagination, and ability. Internal evidences of style, and the probabilities of the situation, suggest that the writing, and perhaps most of the research, was done by Brandeis; but it was undoubtedly a joint effort, to which both men contributed their ideas.

**2.** ***Historical Emergence of New Torts.*** Warren and Brandeis do not offer a strictly accurate account of the historical emergence of the new torts, as both the Roman and English law systems allowed actions for nuisance, mental distress, and defamation from very early times. But the prior existence of all these wrongs set the stage for Warren and Brandeis to isolate the common law principle for invasion of privacy. They reject analogies to libel and slander, insisting that privacy is not concerned with the plaintiff's reputation or "with the injury done to the individual in his external relations to the community." They also reject the view that the tort is designed to protect a person from "mere injury to feelings," by insisting that such harm is compensable only if the plaintiff is the victim of some "recognized" legal injury.

Warren and Brandeis then examine and reject the view that the plaintiff's right to privacy rests solely on a fiduciary or contract theory, given that these theories only protect parties from the misuse of information by others with whom they have previously formed some consensual relationship, as by posing for a picture or by lecturing to students in a private hall. Implicit in these special relationships is a firm understanding that the picture taken or the information acquired will be used only for limited purposes. These consensual theories do not explain how the right of privacy can be vindicated against a stranger who, for example, takes, as "the latest advances in photographic art" allow, the plaintiff's picture "surreptitiously," or who tape records a lecture from outside the hall.

**3.** ***The Analogy to Copyright.*** To Warren and Brandeis, the "in rem" nature of the tort means that the right must be good against the entire world. Accordingly, they find the key analogy to the privacy right in the common law of copyright, which gives the owner control over access to his *unpublished* materials. "In every such case the individual is entitled to decide whether that which is his shall be given to the public." *Id*. at 199. Because the better rule protects even writing of no literary value as long as it is unpublished, they conclude: "The principle which protects personal writings and all other personal productions, not against theft and

physical appropriation, but against publications in any form, is in reality not the principle of private property, but that of an inviolate personality." *Id.* at 205.

**4.** ***Limitations on the Right to Privacy.*** Having thus located the basic principle of protection, the authors identify six potential "limitations on this right to privacy": (1) privacy torts do not apply to oral communications in the absence of special damages; (2) privacy torts inherit all the privileges of defamation; (3) privacy torts are subject to a privilege for any matter "which is of public or general interest"; (4) truth is not a defense to invasion of privacy; (5) privacy torts do not require malice in the sense of ill will; and (6) privacy rights cease upon voluntary publication. *Id.* at 214–19.

**5.** ***Early Case Law.*** Twelve years after Warren and Brandeis published their article, the right to privacy was litigated in Roberson v. Rochester Folding Box Co., 64 N.E. 442, 443 (N.Y. 1902). The Franklin Mills Company purchased from its codefendant, the Rochester Folding Box Company, 25,000 lithographic prints, which it circulated widely in "stores, warehouses, saloons, and other public places." The defendants had, without her consent, reproduced on the prints a portrait of the plaintiff below the words "Flour of the Family," and above the words "Franklin Mills Flour," in large capital letters. The name of the defendant box company was printed in the lower right corner of the picture. The plaintiff claimed that by the publication of the picture she had

> been greatly humiliated by the scoffs and jeers of persons who have recognized her face and picture on this advertisement, and her good name has been attacked, causing her great distress and suffering, both in body and mind; that she was made sick, and suffered a severe nervous shock, was confined to her bed, and compelled to employ a physician, because of these facts.

The plaintiff's case reveals the two different sides to the privacy right. The first side rests on a theory of restitution under which the plaintiff demands that the defendant disgorge the profits it obtained from the unauthorized use of her picture. The analogy is to the general law of restitution that allows the recovery of gains from the defendant's unauthorized conversion of a physical asset. Additionally, the plaintiff challenges the defendant's invasion of her private space, seeking compensation for anguish and loss of society derived from the attack on her reputation and good name. In this regard, the privacy tort is far closer to defamation. Parker, J., had no patience with either claim:

> The so-called "right of privacy" is, as the phrase suggests, founded upon the claim that a man has the right to pass through this world, if he wills, without having his picture published, his business enterprises discussed, his successful experiments written up for the benefit of others, or his eccentricities commented upon either in handbills, circulars, catalogues, periodicals or newspapers; and, necessarily, that the things which may not be written and published of him must not be spoken of him by his neighbors, whether the comment be favorable or otherwise. While most persons would much prefer to have a good likeness of themselves appear in a responsible periodical or leading newspaper rather than upon an advertising card or sheet, the doctrine which the courts are asked to create for this case would apply as well to the one publication as to the other. . . .
>
> If such a principle be incorporated into the body of the law through the instrumentality of a court of equity, the attempts to logically apply the principle will necessarily result not only in a vast amount of litigation, but in litigation bordering upon the absurd, for the right of privacy, once established as a legal doctrine, cannot be confined to the restraint of the publication of a likeness, but must necessarily embrace as well the publication of a word picture, a comment upon one's looks, conduct, domestic relations or habits. And were the right of privacy once legally asserted it would necessarily be held to include the same things if spoken instead of printed, for one, as well as the other, invades the right to be absolutely let alone. . . .
>
> The legislative body could very well interfere and arbitrarily provide that no one should be permitted for his own selfish purpose to use the picture or the name of another for advertising

> purposes without his consent. In such event, no embarrassment would result to the general body of the law, for the rule would be applicable only to cases provided for by the statute. The courts, however, being without authority to legislate, are required to decide cases upon principle, and so are necessarily embarrassed by precedents created by an extreme, and therefore unjustifiable application of an old principle. . . .

The dissent of Gray, J., took sharp issue with the majority's reasoning:

> [I]f it is to be permitted that the portraiture may be put to commercial or other uses for gain by the publication of prints therefrom, then an act of invasion of the individual's privacy results, possibly more formidable and more painful in its consequences than an actual bodily assault might be. Security of person is as necessary as the security of property; and for that complete personal security which will result in the peaceful and wholesome enjoyment of one's privileges as a member of society there should be afforded protection, not only against the scandalous portraiture and display of one's features and person, but against the display and use thereof for another's commercial purposes or gain.

Gray's dissent was quickly adopted in other unauthorized advertisement cases, such as Pavesich v. New England Life Insurance Co., 50 S.E. 68 (Ga. 1905). The dissent received further attention two generations later in Hinish v. Meier & Frank Co., 113 P.2d 438, 447 (Or. 1941), when the defendant signed plaintiff's name to a telegram urging a veto of certain legislation that would put the defendant out of business. Plaintiff sued because he feared that the telegram might cost him his job and pension with the federal government in light of a statutory prohibition against federal employee participation in political affairs. In allowing the cause of action, the Oregon Supreme Court emphatically rejected *Roberson*:

> The opinion of the court in the *Roberson* case, after an exaggerated statement, as we view it, of what is claimed for the right of privacy, dwelt upon the absurd consequences which it was conceived would follow from acceptance of the doctrine. "The attempt to logically apply the principle," it was said, "will necessarily result not only in a vast amount of litigation, but in litigation bordering on the absurd." It was not stated that the litigation then before the court was absurd. It may be doubted whether any court today would render the decision that the New York court did in that case. . . . When a legal principle is pushed to an absurdity, the principle is not abandoned, but the absurdity avoided. The courts are competent, we think, to deal with difficulties of the sort suggested, and case by case, through the traditional process of inclusion and exclusion, gradually to develop the fullness of the principle and its limitations.

Why is *Hinish* not a case of defamation?

By 1960, many cases recognized some form of the right to privacy without articulating its basic structure. To fill that gap without doing too much violence to the case law, Prosser proposed his seminal fourfold classification of privacy interests.

**William L. Prosser**

## *Privacy*

48 Calif. L. Rev. 383, 389, 407 (1960)

[The] law of privacy comprises four distinct kinds of invasion of four different interests of the plaintiff, which are tied together by the common name, but otherwise have almost nothing in common except that each represents an interference with the right of the plaintiff, in the phrase coined by Judge Cooley, "to be let alone." Without any attempt to exact definition, these four torts may be described as follows:

1. Intrusion upon the plaintiff's seclusion or solitude, or into his private affairs.
2. Public disclosure of embarrassing private facts about the plaintiff.
3. Publicity which places the plaintiff in a false light in the public eye.
4. Appropriation, for the defendant's advantage, of the plaintiff's name or likeness.

It should be obvious at once that these four types of invasion may be subject, in some respects at least, to different rules; and that when what is said as to any one of them is carried over to another, it may not be at all applicable, and confusion may follow. . . .

Judge Biggs has described the present state of the law of privacy as "still that of a haystack in a hurricane." Disarray there certainly is; but almost all of the confusion is due to a failure to separate and distinguish these four forms of invasion, and to realize that they call for different things. . . .

Taking them in order—intrusion, disclosure, false light, and appropriation—the first and second require the invasion of something secret, secluded or private pertaining to the plaintiff; the third and fourth do not. The second and third depend upon publicity, while the first does not, nor does the fourth, although it usually involves it. The third requires falsity or fiction; the other three do not. The fourth involves a use for the defendant's advantage, which is not true of the rest. . . .

## NOTES

**1. *Prosser and Modern Privacy Torts.*** Prosser's classification has been adopted by many courts, and it forms the basis for the treatment of the subject in the Restatement (Second) of Torts §§652A-652L, of which Prosser was the original draftsman. For subsequent commentary, see Richard A. Posner, The Right of Privacy, 12 Ga. L. Rev. 393 (1978); Richard A. Epstein, Privacy, Property Rights, and Misrepresentations, 12 Ga. L. Rev. 455 (1978); Diane L. Zimmerman, Requiem for a Heavyweight: A Farewell to Warren and Brandeis's Privacy Tort, 68 Cornell L. Rev. 291 (1983); Ken Gormley, One Hundred Years of Privacy, 1992 Wis. L. Rev. 1335. For critiques of Prosser's framework, see Danielle K. Citron, Mainstreaming Privacy Torts, 98 Calif. L. Rev. 1805, 1810 (2010); Lior Strahilevitz, Reunifying Privacy Law, 98 Calif. L. Rev. 2007, 2032–33 (2010).

This chapter follows Prosser's classification in order. In the first three torts, the plaintiff seeks to ward off the defendant. In the fourth, the plaintiff seeks to enter the marketplace by treating the right of publicity as a species of intellectual property ripe for commercial development.

**2. *Criticisms of Early Privacy Torts.*** Although Prosser built on Warren and Brandeis's paper and theories in developing these classifications of privacy torts, not all legal scholars shared the same enthusiasm with recognizing this new area of tort law. Harry Kalven, Jr., Privacy in the Tort Law—Were Warren and Brandeis Wrong?, 31 Law & Contemporary Problems 326, 330–31 (1966), is one such scholar who did not so readily buy into the theories set forth by Warren and Brandeis. Kalven faulted their article for its failure to specify the prima facie elements of the privacy torts, its disregard of the measurement of damages and basis of liability for the torts, and the creation of a broad range of privileges that threaten to engulf the torts. Kalven also argued that, pursuant to these deficiencies in the Warren and Brandeis article, these problems were equally prevalent in the early development of the common law privacy torts. As you proceed to engage with each of the privacy torts throughout the chapter, consider whether Kalven's criticisms of the Warren and Brandeis article are valid. Are the issues Kalven notes persistent in the later development of the privacy torts, or are they simply issues stemming from the nascency of this area of the law?

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## SECTION C. INTRUSION UPON SECLUSION

**RESTATEMENT OF THE LAW (SECOND) OF TORTS**

**§652B. Intrusion Upon Seclusion**

One who intentionally intrudes, physically or otherwise, upon the solitude or seclusion of another or his private affairs or concerns, is subject to liability to the other for invasion of his privacy, if the intrusion would be highly offensive to a reasonable person.

Wyoming is the latest state to join the vast majority of states that accept the Second Restatement's intrusion tort. See Howard v. Aspen Way Enters., Inc., 406 P.3d 1271 (Wyo. 2017). Wyoming did so in a modern context in which the defendant had surreptitiously installed software on a computer leased to the plaintiff that allowed it to track the location of the computer, remotely activate its webcam, and capture screen shots and keystrokes. Hill, J., tied recognition of the intrusion tort to Wyoming's "well established" "commitment to individual privacy interests" dating back to the court's 1936 recognition that "'[t]he home is a favorite of the law. It is there that the citizen can claim the right of privacy, the right to be let alone, on clear grounds.'"

Other states have since indicated their support of the Second Restatement's intrusion tort without officially adopting the definition. For example, in Gantvoort v. Ranschau, 973 N.W.2d 225, 235 (S.D. 2022), a man sued his ex-wife for recording his conversations with an electronic device. He also sued her lawyer for his handling of the recordings. The court relied on the Second Restatement's intrusion tort in reaching the conclusion that the plaintiff failed to prove that the lawyer's "conduct involved an actual *invasion* of [the plaintiff's] privacy, which is a basic element of the tortious invasion of privacy claim." Additionally, other states have used the Second Restatement's intrusion tort to inform their handling of common law intrusion suits without officially adopting its definition. See, e.g., Guilbeau v. Durant H.M.A., LLC, 533 P.3d 764, 771 (Okla. 2023) (holding that intrusion upon seclusion "has two elements: (1) a nonconsensual intrusion (2) which would be highly offensive to a reasonable person" after referencing the Second Restatement's definition of the tort).

### *Nader v. General Motors Corp.*

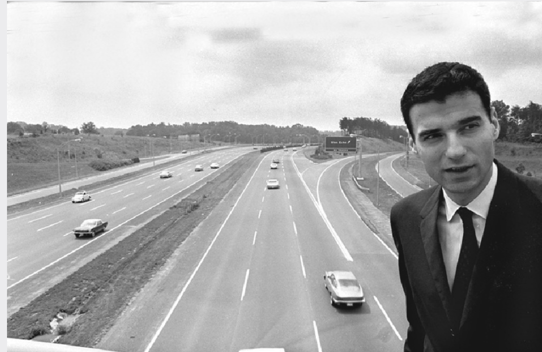
255 N.E.2d 765 (N.Y. 1970)

Fuld, C.J. On this appeal, we are called upon to determine the reach of the tort of invasion of privacy as it exists under the law of the District of Columbia.

The complaint, in this action by Ralph Nader, pleads four causes of action against the appellant, General Motors Corporation, and three other defendants allegedly acting as its agents. The first two causes of action charge an invasion of privacy, the third is predicated on the intentional infliction of severe emotional distress and the fourth on interference with the plaintiff's economic advantage. This appeal concerns only the legal sufficiency of the first two causes of action, which were upheld in the courts below as against the appellant's motion to dismiss.

The plaintiff, an author and lecturer on automotive safety, has, for some years, been an articulate and severe critic of General Motors' products from the standpoint of safety and design. According to the complaint—which, for present purposes, we must assume to be true—the appellant, having learned of the imminent publication of the plaintiff's book

**Exhibit 7.1 Ralph Nader**
In August 1970, Nader and G.M. settled their dispute, commenced approximately three years earlier, out of court for $425,000. "Nader said the money would be used to set up a 'continuous legal monitoring of General Motors' activities in the safety, pollution and consumer relations area.'" Nader's claims sought approximately $2 million in compensatory damages and "[a]n additional $7 million punitive damages suit was filed but later dropped." https://www.thecrimson.com/article/1970/8/14/gm-settles-out-of-court-to/.



*Source: AP Images*

"Unsafe at any Speed," decided to conduct a campaign of intimidation against him in order to "suppress plaintiff's criticism of and prevent his disclosure of information" about its products. To that end, the appellant authorized and directed the other defendants to engage in a series of activities which, the plaintiff claims in his first two causes of action, violated his right to privacy.

Specifically, the plaintiff alleges that the appellant's agents (1) conducted a series of interviews with acquaintances of the plaintiff, "questioning them about, and casting aspersions upon [his] political, social . . . racial and religious views . . . ; his integrity; his sexual proclivities and inclinations; and his personal habits"; (2) kept him under surveillance in public places for an unreasonable length of time; (3) caused him to be accosted by girls for the purpose of entrapping him into illicit relationships; (4) made threatening, harassing and obnoxious telephone calls to him; (5) tapped his telephone and eavesdropped, by means of mechanical and electronic equipment, on his private conversations with others; and (6) conducted a "continuing" and harassing investigation of him. . . .

[The court then held that the District of Columbia recognized Prosser's tort of intrusion upon seclusion.]

Quite obviously, some intrusions into one's private sphere are inevitable concomitants of life in an industrial and densely populated society, which the law does not seek to proscribe even if it were possible to do so. "The law does not provide a remedy for every annoyance that occurs in everyday life." However, the District of Columbia courts have held that the law should and does protect against certain types of intrusive conduct, and we must, therefore, determine whether the plaintiff's allegations are actionable as violations of the right to privacy under the law of that jurisdiction.

It should be emphasized that the mere gathering of information about a particular individual does not give rise to a cause of action under this theory. Privacy is invaded only if the information sought is of a confidential nature and the defendant's conduct was unreasonably intrusive. Just as a common-law copyright is lost when material is published, so, too, there can be no invasion of privacy where the information sought is open to public view or has been voluntarily revealed to others. In order to sustain a cause of action for invasion of privacy, therefore, the plaintiff must show that the appellant's conduct was truly "intrusive" and that it was designed to elicit information which would not be available through normal inquiry or observation.

The majority of the Appellate Division in the present case stated that *all of "[t]he activities complained of"* in the first two counts constituted actionable invasions of privacy under the law of the District of Columbia.[2] We do not agree with that sweeping determination. At most, only two of the activities charged to the appellant are, in our view, actionable as invasions of privacy under the law of the District of Columbia. . . .

Turning, then, to the particular acts charged in the complaint, we cannot find any basis for a claim of invasion of privacy, under District of Columbia law, in the allegations that the appellant, through its agents or employees, interviewed many persons who knew the plaintiff, asking questions about him and casting aspersions on his character. Although those inquiries may have uncovered information of a personal nature, it is difficult to see how they may be said to have invaded the plaintiff's privacy. Information about the plaintiff which was already known to others could hardly be regarded as private to the plaintiff. Presumably, the plaintiff had previously revealed the information to such other persons, and he would necessarily assume the risk that a friend or acquaintance in whom he had confided might breach the confidence. If, as alleged, the questions tended to disparage the plaintiff's character, his remedy would seem to be by way of an action for defamation, not for breach of his right to privacy.

Nor can we find any actionable invasion of privacy in the allegations that the appellant caused the plaintiff to be accosted by girls with illicit proposals, or that it was responsible for the making of a large number of threatening and harassing telephone calls to the plaintiff's home at odd hours. Neither of these activities, howsoever offensive and disturbing, involved intrusion for the purpose of gathering information of a private and confidential nature.

As already indicated, it is manifestly neither practical nor desirable for the law to provide a remedy against any and all activity which an individual might find annoying. On the other hand, where severe mental pain or anguish is inflicted through a deliberate and malicious campaign of harassment or intimidation, a remedy is available in the form of an action for the intentional infliction of emotional distress — the theory underlying the plaintiff's third cause of action. But the elements of such an action are decidedly different from those governing the tort of invasion of privacy, and just as we have carefully guarded against the use of the prima facie tort doctrine to circumvent the limitations relating to other established tort remedies we should be wary of any attempt to rely on the tort of invasion of privacy as a means of avoiding the more stringent pleading and proof requirements for an action for infliction of emotional distress.

Apart, however, from the foregoing allegations which we find inadequate to spell out a cause of action for invasion of privacy under District of Columbia law, the complaint contains allegations concerning other activities by the appellant or its agents which do satisfy the requirements for such a cause of action. The one which most clearly meets those requirements is the charge that the appellant and its codefendants engaged in unauthorized wiretapping and eavesdropping by mechanical and electronic means. The Court of Appeals in [Pearson v. Dodd, 410 F.2d 701 (D.C. 1969)] expressly recognized that such conduct constitutes a tortious intrusion and other jurisdictions have reached a similar conclusion. (See, e.g., Roach v. Harper, 105 S.E.2d 546 (W. Va. 1958).) In point of fact, the appellant does not dispute this, acknowledging that, to the extent the two challenged counts charge it with wiretapping and eavesdropping, an actionable invasion of privacy has been stated.

There are additional allegations that the appellant hired people to shadow the plaintiff and keep him under surveillance. In particular, he claims that, on one occasion, one of its agents followed him into a bank, getting sufficiently close to him to see the denomination of the bills he was withdrawing from his account. From what we have already said, it is manifest that the mere observation of the plaintiff in a public place does not amount to an invasion of his privacy. But, under certain circumstances, surveillance may be so "overzealous" as to render it actionable. Whether or not the surveillance in the present case falls into this latter

category will depend on the nature of the proof. A person does not automatically make public everything he does merely by being in a public place, and the mere fact that Nader was in a bank did not give anyone the right to try to discover the amount of money he was withdrawing. On the other hand, if the plaintiff acted in such a way as to reveal that fact to any casual observer, then, it may not be said that the appellant intruded into his private sphere. In any event, though, it is enough for present purposes to say that the surveillance allegation is not insufficient as a matter of law. . . .

[Affirmed.]

Breitel, J., concurring in result. [I]t is inappropriate to decide that several of the allegations as they now appear are referable only to the more restricted tort of intentional infliction of mental distress rather than to the common-law right of privacy upon which the first and second causes of action depend.

## NOTES

**1. *Invasions of Privacy Without Trespass.*** The invasion of privacy on public streets necessarily involves an element of balancing under yet another version of the live and let live test in the law of nuisance. Watching the comings and goings of other individuals is an inescapable part of public life from which all receive benefits that on average exceed their private burdens. It is only when extraordinary means are used in the public forum that a claim for invasion of privacy becomes viable. One conspicuous illustration of that imbalance is Galella v. Onassis, 487 F.2d 986, 992, 998–99 (2d Cir. 1973). There the plaintiff Ronald Galella was a freelance photographer or "paparazzo," who repeatedly hounded Jacqueline Kennedy Onassis and her children in an effort to secure photographs for publication. He often eluded the U.S. Secret Service agents assigned to guard her, bribed doormen, and romanced a family servant to gain access to the family.

**Galella's photograph of Jacqueline Kennedy Onassis walking on Madison Avenue in New York City, Oct. 7, 1971**

*Source: Ron Galella/Ron Galella Collection via Getty Images*

In *Galella*, the invasion of privacy was taken as a given, so that the entire dispute was over the choice of remedy. In the district court, Galella sued Onassis for false arrest, malicious prosecution, and interference with trade. Onassis, the defendant, then counterclaimed for invasion of privacy. The district court's initial temporary restraining order enjoined Galella from

> harassing, alarming, startling, tormenting, touching the person of the defendant . . . or her children . . . and from blocking their movements in the public places and thoroughfares, invading their immediate zone of privacy by means of physical movements, gestures or with photographic equipment and from performing any act reasonably calculated to place the lives and safety of the defendant . . . and her children in jeopardy.

After a full trial,

> Galella was enjoined from (1) keeping the defendant and her children under surveillance or following any of them; (2) approaching within 100 yards of the home of defendant or her children, or within 100 yards of either child's school or within 75 yards of either child or

> 50 yards of defendant; (3) using the name, portrait or picture of defendant or her children for advertising; (4) attempting to communicate with defendant or her children except through her attorney.

On appeal, Smith, J., accepted the need for injunctive relief to forestall the defendant's determined and intrusive coverage of the plaintiff and her family, but then limited its scope:

> The injunction, however, is broader than is required to protect the defendant. Relief must be tailored to protect Mrs. Onassis from the "paparazzo" attack which distinguishes Galella's behavior from that of other photographers; it should not unnecessarily infringe on reasonable efforts to "cover" defendant. Therefore, we modify the court's order to prohibit only (1) any approach within twenty-five (25) feet of defendant or any touching of the person of the defendant Jacqueline Onassis; (2) any blocking of her movement in public places and thoroughfares; (3) any act foreseeably or reasonably calculated to place the life and safety of defendant in jeopardy; and (4) any conduct which would reasonably be foreseen to harass, alarm or frighten the defendant.
>
> Any further restriction on Galella's taking and selling pictures of defendant for news coverage is, however, improper and unwarranted by the evidence.
>
> Likewise, we affirm the grant of injunctive relief to the government modified to prohibit any action interfering with Secret Service agents' protective duties. Galella thus may be enjoined from (a) entering the children's schools or play areas; (b) engaging in action calculated or reasonably foreseen to place the children's safety or well being in jeopardy, or which would threaten or create physical injury; (c) taking any action which could reasonably be foreseen to harass, alarm, or frighten the children; and (d) from approaching within thirty (30) feet of the children.

Timbers, J., dissented in part on the ground that deference should be accorded to the district court's determination of the sweep of injunctive relief. The dissent protested, for example, "a wholly unexplained and anomalous 84% reduction of the distance Galella is required to keep away from Mrs. Onassis (from 50 *yards* to 25 *feet*), and an equally implausible 87% reduction of the distance he is required to keep away from the children (from 75 *yards* to 30 *feet*)."

**2. *Theoretical Foundations for the Right to Privacy.*** Most social situations are not as extreme as those in either *Nader* or *Galella*, but they still may involve some imbalance that does not work to the advantage of all, as when people, while unobserved, seek to snoop or overhear conversations of others. These tactics can also be applied against individuals on private property, when there is no direct personal intrusion. Thus the tort of invasion of privacy does not require a physical trespass on plaintiff's property but may be accomplished by eavesdropping near an open window or by overhearing conversations by means of a parabolic microphone. The argument against recognizing this tort starts from the position "no physical invasion, no tort." On privacy, however, the cases have consistently gone the other way. Blackstone himself condemned "eaves-droppers, or such as listen under walls and windows," but he did so not only for what they did but also for "the slanderous and mischievous tales" they uttered. 4 Blackstone, Commentaries on the Laws of England 169 (1769). The more modern approach condemns the intrusion but downplays two elements in Blackstone's formulation: the physical entry and any subsequent defamatory publication. Rhodes v. Graham, 37 S.W.2d 46 (Ky. 1931), counts as a transitional case in which the action for invasion of privacy was allowed for phone conversations overheard by a technical trespass—the tapping of a telephone line. In Roach v. Harper, 105 S.E.2d 564 (W. Va. 1958), the court allowed an action for invasion of privacy when the defendant used a "hearing device" to overhear the plaintiff's private and confidential conversations in an apartment that he rented to her. In line with the case law trend, the modern dictionary definition excises all references to trespass in its definition of eavesdropping: "To listen, or try to listen, secretly, as to a private conversation."

Why the shift? Creating liability without trespass is best justified by asking whether the general security promoted by an expanded right works to the long-term advantage of all

individuals governed by the newer rule. That norm is reflected in settings where people voluntarily congregate in close quarters, as in the anti-snooping norm in crowded restaurants. By extension, the prohibition against snooping reduces the need for individuals to take elaborate precautions to fence themselves off from their neighbors, and thus allows for the more intensive use of land in crowded areas.

The soundness of the privacy right against intrusion has generated longstanding controversy in connection with the Fourth Amendment's guarantee against "unreasonable searches and seizures." Katz v. United States, 389 U.S. 347, 353 (1967), rejected the government's argument that its tap on a public telephone booth did not amount to a search or seizure because the electronic device did not commit a common law trespass because it "did not happen to penetrate the wall of the booth." Subsequent Fourth Amendment cases have retreated from *Katz*'s broad personal privacy holding. For example, in Smith v. Maryland, 442 U.S. 735 (1979), the Court refused to apply *Katz* when the police, without a warrant, used a device known as a "pen register" to record the numbers dialed from a particular phone and the times they were dialed, because no phone conversations were recorded. *Smith* was updated in United States v. Soybel, 13 F.4th 584, 594 (7th Cir. 2021), to cover IP pen registers, because they are "analogous in all material respects to a traditional telephone pen register."

Does the legitimate interest of privacy test allow a distinction between *Katz* and *Smith*?

**3. *Privacy in the Office.*** After *Katz*, what are employees' reasonable expectations of privacy in the workplace? In O'Connor v. Ortega, 480 U.S. 709, 717 (1987), the Supreme Court held, in a claim by a state hospital employee, that the search of his office by state hospital personnel without his knowledge or consent violated the Fourth Amendment. Although acknowledging that expectations of privacy in one's office, desk, and files "may be reduced by virtue of actual office practices and procedures, or by legitimate regulation," the Court held that, in this case, the employee had a reasonable expectation of privacy, given that he did not share his desk or file cabinets with others; nor did the hospital have any policy discouraging such personal use. Similarly, in *In re* Asia Global Crossing, Ltd., 322 B.R. 247, 257 (Bankr. S.D.N.Y. 2005), Bernstein, C.J., proposed this four-factor test to elaborate on this privacy standard in the context of an employee's use of the company email system to communicate with a third party about personal matters:

> (1) does the corporation maintain a policy banning personal or other objectionable use, (2) does the company monitor the use of the employee's computer or e-mail, (3) do third parties have a right of access to the computer or e-mails, and (4) did the corporation notify the employee, or was the employee aware, of the use and monitoring policies?

What about even newer communication and social networking technologies? In City of Ontario, California v. Quon, 560 U.S. 746 (2010), the Supreme Court declined to decide whether or not a government employee had an expectation of privacy with regard to personal text messages sent through a government-issued cell phone. Similar privacy disputes, particularly pertaining to an employee's use of a company computer to access personal files and Gmail, Twitter, Facebook, and eBay accounts, raise new issues for courts. In Biby v. Board of Regents, 419 F.3d 845 (8th Cir. 2005), the court held that an employee did not have an expectation of privacy with regard to personal files downloaded to a company computer. In *In re* CTLI, LLC, 528 B.R. 359, 377–78 (Bankr. S.D. Tex. 2015), the bankruptcy court held that a bankrupt business's social media accounts, including a Facebook "likes" page and Twitter account, were business rather than personal accounts and thus property of the company's bankruptcy estate. Hence the court rejected the employee's claim for privacy by treating the social media communications like employee messages on a work email account for which there is no individual privacy interest.

It should come as no surprise that many employers have employees sign contracts stating something like: "I have no expectation of privacy for any material on [the employer's] equipment, even if that material was generated for my personal use." That contractual stipulation proved unavailing in Bowers v. County of Taylor, 598 F. Supp. 3d 719 (W.D. Wis. 2022), where the County accessed files taken by Bowers, a county sergeant, and kept in a Dropbox account. Bowers had taken these files without permission and shared them with a television crew. Because the files taken by Bowers were stored in the cloud and not on the County's equipment, they were not covered by the clause. The County's IT policy also allowed the County to "access any electronic communications at any time," but Peterson, J., concluded that the disputed files were not electronic communications. Is this narrow interpretation of the exclusion consistent with the County's overall intention to make sure that sensitive files did not get distributed to the wrong people? Is there any objection, constitutional or otherwise, to amending the declarations to cover uses of all material, however acquired or stored?

## *Boring v. Google, Inc.*

362 Fed. Appx. 273 (3d Cir. 2010)

Jordan, J.

Aaron C. Boring and Christine Boring appeal from an order of the United States District Court for the Western District of Pennsylvania dismissing their complaint under Rule 12(b)(6) of the Federal Rules of Civil Procedure. For the reasons that follow, we affirm in part and reverse in part.

### I. Background

On April 2, 2008, the Borings commenced an action in the Court of Common Pleas of Allegheny County, Pennsylvania against Google, Inc., asserting claims for invasion of privacy, trespass, injunctive relief, negligence, and conversion. The Borings sought compensatory, incidental, and consequential damages in excess of $25,000 for each claim, plus punitive damages and attorney's fees.

The Borings' claims arise from Google's "Street View" program, a feature on Google Maps that offers free access on the Internet to panoramic, navigable views of streets in and around major cities across the United States. To create the Street View program, representatives of Google attach panoramic digital cameras to passenger cars and drive around cities photographing the areas along the street. According to Google, "[t]he scope of Street View is public roads." Google allows individuals to report and request the removal of inappropriate images that they find on Street View.

The Borings, who live on a private road in Pittsburgh, discovered that Google had taken "colored imagery of their residence, including the swimming pool, from a vehicle in their residence driveway months earlier without obtaining any privacy waiver or authorization." They allege that their road is clearly marked with a "Private Road, No Trespassing" sign, and they contend that, in driving up their road to take photographs for Street View and in making those photographs available to the public, Google "disregarded [their] privacy interest." . . .

[The district court granted Google's motion to dismiss all of the Borings' claims. With respect to the invasion of privacy claim, it held that "the Borings were unable to show that Google's conduct was highly offensive to a person of ordinary sensibilities." On trespass, the court held that "the Borings have not alleged facts sufficient to establish that they suffered any damages caused by the alleged trespass."]

## II. Discussion

. . .

### B. Invasion of Privacy

Pennsylvania law recognizes four torts under the umbrella of invasion of privacy: "[1] unreasonable intrusion upon the seclusion of another; [2] appropriation of another's name or likeness; [3] unreasonable publicity given to another's private life; and [4] publicity that unreasonably places the other in a false light before the public." . . .

#### i. Intrusion upon Seclusion

To state a claim for intrusion upon seclusion, plaintiffs must allege conduct demonstrating "an intentional intrusion upon the seclusion of their private concerns which was substantial and highly offensive to a reasonable person, and aver sufficient facts to establish that the information disclosed would have caused mental suffering, shame or humiliation to a person of ordinary sensibilities." Publication is not an element of the claim, and thus we must examine the harm caused by the intrusion itself.

No person of ordinary sensibilities would be shamed, humiliated, or have suffered mentally as a result of a vehicle entering into his or her ungated driveway and photographing the view from there. The Restatement cites knocking on the door of a private residence as an example of conduct that would not be highly offensive to a person of ordinary sensibilities. See Restatement (Second) of Torts, §652B cmt. *d*. The Borings' claim is pinned to an arguably less intrusive event than a door knock. Indeed, the privacy allegedly intruded upon was the external view of the Borings' house, garage, and pool — a view that would be seen by any person who entered onto their driveway, including a visitor or a delivery man. Thus, what really seems to be at the heart of the complaint is not Google's fleeting presence in the driveway, but the photographic image captured at that time. The existence of that image, though, does not in itself rise to the level of an intrusion that could reasonably be called highly offensive.

Significantly, the Borings do not allege that they themselves were viewed inside their home, which is a relevant factor in analyzing intrusion upon seclusion claims.

The Borings suggest that the District Court erred in determining what would be highly offensive to a person of ordinary sensibilities at the pleading stage, but they do not cite to any authority for this proposition. Courts do in fact, decide the "highly offensive" issue as a matter of law at the pleading stage when appropriate. . . .

In sum, accepting the Borings' allegations as true, their claim for intrusion upon seclusion fails as a matter of law, because the alleged conduct would not be highly offensive to a person of ordinary sensibilities.

[Based on the foregoing reasoning, the court also summarily dispatched the Borings' claim of invasion of privacy based upon "Publicity Given to Private Life," given that one element of that claim is that the publicity "would be highly offensive to a reasonable person."]

### C. Trespass

The District Court dismissed the Borings' trespass claim, holding that trespass was not the proximate cause of any compensatory damages sought in the complaint and that, while nominal damages are generally available in a trespass claim, the Borings did not seek nominal damages in their complaint. While the District Court's evident skepticism about the claim may be understandable, its decision to dismiss it under Rule 12(b)(6) was erroneous.

Trespass is a strict liability tort, "both exceptionally simple and exceptionally rigorous." Prosser on Torts at 63 (West, 4th ed. 1971). Under Pennsylvania law, it is defined as an "unprivileged, intentional intrusion upon land in possession of another." Though claiming not to have done so, it appears that the District Court effectively made damages an element of the claim, and that is problematic, since "[o]ne who intentionally enters land in the possession of another is subject to liability to the possessor for a trespass, although his presence on the land causes no harm to the land, its possessor, or to any thing or person in whose security the possessor has a legally protected interest." Restatement (Second) Torts §163.

Here, the Borings have alleged that Google entered upon their property without permission. If proven, that is a trespass, pure and simple. There is no requirement in Pennsylvania law that damages be pled, either nominal or consequential. It was thus improper for the District Court to dismiss the trespass claim for failure to state a claim. Of course, it may well be that, when it comes to proving damages from the alleged trespass, the Borings are left to collect one dollar and whatever sense of vindication that may bring, but that is for another day. For now, it is enough to note that they "bear the burden of proving that the trespass was the legal cause, i.e., a substantial factor in bringing about actual harm or damage," if they want more than a dollar. . . .

[Affirmed dismissal of claims for invasion of privacy (as well as unjust enrichment, injunctive relief, and punitive damages). Reversed and remanded dismissal of trespass claim.]

## NOTES

**1. *Privacy and the Era of Big Data.*** To what extent can one's daily activities be tracked, recorded, and shared with others today? Google's response to the Borings' complaint notably argued that "[t]oday's satellite-image technology means that . . . complete privacy does not exist." (Note that after several years of litigation on the trespass claim, Google agreed to pay the Borings a symbolic $1 consent judgment.)

What if one rents a car equipped with GPS (global positioning system)? In Turner v. American Car Rental, Inc., 884 A.2d 7, 12 (Conn. App. Ct. 2005), Dranginis, J., held that "it was a factual determination for the jury to make as to whether the global positioning system in the vehicle and the tracking of the plaintiff's operation of that vehicle constituted an invasion of privacy." Dranginis, J., nonetheless noted the absence of "any authority that equipping a motor vehicle with a global positioning system violates the privacy of the vehicle's operator" or "any legal authority that the operator of a motor vehicle has an expectation of privacy on the public highway."

What about when the invasion of privacy happens exclusively online? The social networking website Facebook enables sharing of its users' personal information as follows:

> Third-party websites can embed Facebook "like" buttons to let users share content on Facebook — for instance, CNN can embed "like" buttons on news articles that it publishes [online] to let users share content with their Facebook friends. To make the "like" button appear on the page, CNN embeds a small code snippet that Facebook provides. That code snippet causes the user's browser to send a background request to Facebook's servers. That request includes the URL of the page where the "like" button is embedded, as well as the contents of "cookies" — small text files — that Facebook has stored on that user's browser.

In *In re* Facebook Internet Tracking Litigation, 263 F. Supp. 3d 836, 840 (N.D. Cal. 2017), the plaintiffs alleged that Facebook violated their privacy by using its "like" buttons to track

and collect detailed records of their private web browsing activity. Davila, J., rebuffed plaintiffs' intrusion claim:

> [W]ebsites routinely embed content from third-party servers in the form of videos, images, and other media, as well as through their use of analytics tools, advertising networks, code libraries and other utilities. Each tool transmits to third parties the same data that Plaintiffs claim is highly sensitive. Since these requests are part of routine internet functionality . . . the Court finds that they are not a "highly offensive" invasion of Plaintiffs' privacy interests.

Davila, J., cited approvingly *In re* Google, Inc. Privacy Policy Litigation, 58 F. Supp. 3d 968, 988 (N.D. Cal. 2014), which held that Google's collection and disclosure of users' data, including their browsing histories, "do not plausibly rise to the level of intrusion necessary to establish an intrusion claim" given the "high bar" for an intrusion "highly offensive to a reasonable person."

Moreover, in rejecting any "reasonable expectation of privacy in the URLs of the pages they visit," Davila, J., relied on the fact that plaintiffs could have exercised self-help to safeguard their web browsing histories:

> [A]s Facebook explained in its privacy policy, "[y]ou can remove or block cookies using the settings in your browser." Similarly, users can "take simple steps to block data transmissions from their browsers to third parties," such as "using their browsers in 'incognito' mode" or "install[ing] plugin browser enhancements." Facebook's intrusion could have been easily blocked, but Plaintiffs chose not to do so.

In *In re* Google Location History Litigation, 514 F. Supp. 3d 1147, 1151 (N.D. Cal. 2021), the plaintiffs charged that Google had told its customers they had the ability to turn off Google's location tracking system at will. In fact, the system continued to track the plaintiffs even when turned off, allowing Google to obtain information that it could monetize by selling precise locations to potential advertisers. This deliberate "deceit" weighed in favor of determining that the data collection was done "in a manner highly offensive to a reasonable person," as Google's own communication to its customers had created a reasonable expectation of privacy. The court refused to hold that these intrusions were inoffensive as a matter of law and therefore held that the plaintiffs had stated a valid claim for intrusion on seclusion. It also noted that because the information was of value to Google, the plaintiffs had stated a valid claim for unjust enrichment. What are the measures of damages for these two kinds of claims? Note the similarities to the two kinds of claims fairly raised in *Roberson*, *supra* at 415.

In McCoy v. Alphabet, Inc., 2021 WL 405816 (N.D. Cal. Feb. 2, 2021), a similar invasion of privacy claim failed when the only data obtained concerned the "frequency and duration of use of certain apps," which did not cross the threshold of "highly offensive to a reasonable person."

**2.** ***Significance of Corporate Policy.*** Critical to the *In re Google Location History Litigation* court's finding a "reasonable expectation of privacy" was that Google told its users they could turn off location tracking. Other courts have similarly held that plaintiffs' reasonable expectations of privacy may be created by a company's statement or policy indicating that it would not collect or retain certain types of data. Speaking generally, though, where a company clearly discloses the types of data it collects and complies with its publicly stated policies (as in *In re Facebook Internet Tracking*, *supra* Note 1), courts have rejected the notion that plaintiffs have any reasonable expectation of privacy. Is compliance with published corporate policies the appropriate standard for determining whether an Internet company violates its consumers' privacy? Considering the ubiquity of online services such as email and Facebook, do the consumers who agree to those policies have reasonable alternatives?

**CALIFORNIA CONSUMER PRIVACY ACT OF 2018**

**§3. Purpose and Intent**

In enacting this Act, it is the purpose and intent of the people of the State of California to further the constitutional right of privacy by giving consumers an effective way to control their personal information, thereby affording better protection for their own privacy and autonomy, by:

(a) Giving California consumers the right to know what categories of personal information a business has collected about them and their children.

(b) Giving California consumers the right to know whether a business has sold this personal information, or disclosed it for a business purpose, and to whom.

(c) Requiring a business to disclose to a California consumer if it sells any of the consumer's personal information and allowing a consumer to tell the business to stop selling the consumer's personal information.

(d) Preventing a business from denying, changing, or charging more for a service if a California consumer requests information about the business's collection or sale of the consumer's personal information, or refuses to allow the business to sell the consumer's personal information.

(e) Requiring businesses to safeguard California consumers' personal information and holding them accountable if such information is compromised as a result of a security breach arising from the business's failure to take reasonable steps to protect the security of consumers' sensitive information.

A consumer can recover $1,000 (or actual damages, whichever is greater) for each violation of the Act.

## NOTES

**1.** ***The Rise of Statutory Protections.*** The California Consumer Privacy Act of 2018 (CCPA) provides enhanced statutory protections to "giv[e] consumers an effective way to control their personal information, thereby affording better protection for their own privacy and autonomy." Are such statutory protections necessary in an era of big data?

**2.** ***A European Approach?*** As initially enacted, the CCPA approached but was not as privacy protective as the European Union General Regulation on Data Privacy (GDPR), which seeks to return control over personal data to citizens of the EU. Not only does the GDPR require data processors to clearly disclose any data collection practices they engage in, the "lawful basis and purpose" for the data collection, how long they will maintain the data, and whether they plan to share the data with third parties; it also prohibits companies from processing personal data unless they have the informed consent of the individual whose data are being collected. Consumers have the right to revoke consent at any time.

To further bolster the data protections provided by the GDPR, the European Parliament adopted the Digital Services Act (DSA) in July 2022. Whereas the GDPR aimed to protect consumers by regulating the collection and use of consumer data, the DSA was designed to enhance data protections by imposing legal obligations on "very large online platforms" ("VLOPs") and "very large online search engines." Regulation (EU) 2022/2065 of the European Parliament and of the Council of 19 October 2022 on a Single Market for Digital Services and amending Directive 2000/31/EC (Digital Services Act) [2022] OJ L227/1, recital 41. The DSA requires that VLOPs publish annual transparency reports, implement notice-and-take-down procedures and redress mechanisms for its users, and suspend users who frequently post "manifestly illegal content." See *id.* at art. 15–16, 20, 23–24, 26. The DSA also imposes additional transparency obligations on these very large websites, such as supplying

users with information related to online advertisements and submitting reports to the European Commission on the number of disputes submitted and sanctions imposed.

To amend and expand the protections granted by the CCPA to more closely resemble those granted by the GDPR and the DSA, California citizens voted in favor of the California Privacy Rights Act (CPRA) in 2020. The CPRA created several new rights for California consumers, including the right to correct inaccuracies in their personal data held by other organizations and the right to limit the use and disclosure of their data. See Cal. Civ. Code §1798.106, .121 (2024). Additionally, the CPRA expanded protections for individuals by allowing them to opt out of the sharing and sale of their personal data as opposed to the right to restrict the sale of data under the CCPA. See *id*. at §1798.115(a) (2024). The CPRA also imposed greater burdens on businesses that collect data, such as a duty to inform consumers about how they use and collect data and restrictions on what type of data and circumstances under which such data may be collected, by including language from the GDPR. See *id*. at Sec. 3; Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation) [2016] OJ L119/1, recital 39. Finally, the CPRA bolstered privacy protections for its citizens by establishing the California Privacy Protection Agency to implement and enforce the provisions of the CPRA. See Cal. Civ. Code §1798.199.10.

**3.** ***A Flurry of State Activity?*** Besides California, only Colorado and Virginia have enacted comprehensive data privacy and protection laws. The Virginia Consumer Data Protection Act establishes many of the substantive rights that the CPRA granted to California citizens, but the Colorado Privacy Act (CPA) is notable for its treatment of automated decision-making ("profiling") using personal data. Specifically, the CPA grants consumers a universal right to opt out of the processing of personal data for purposes of targeted advertising, the sale of data, and profiling for decisions that result in legal or similarly significant effects for its customers. See Colo. Rev. Stat. §6-1-1306(1)(a)(I) (2024). The CPA also mandates that organizations collecting data for profiling purposes must provide clear notice to its users regarding the types of decisions subject to profiling, the types of data used for profiling, whether the accuracy and fairness of the profiling system have been evaluated, and information regarding how a consumer may opt out of profiling. See James X. Dempsey, Artificial Intelligence Regulation in the United States: A Patchwork of Laws, at 9. Additionally, the CPA allows consumers to obtain copies of the data used for profiling purposes and permits them to seek the correction or deletion of such data.

Although the CPA is landmark legislation in terms of the framework it sets forth for the governance of decision-making by AI, the CPA and its rules include significant limitations on the protection of consumer data. For example, the CPA excludes from its scope sixteen categories of data or entities and eleven types of data processing. See Colo. Rev. Stat. §6-1-1304(2)-(3) (2024). Furthermore, the CPA Rules enable data controllers not to take action regarding a consumer's opt-out request when a human meaningfully considers the data inputted into its profiling system and has the authority to change or influence the result of the profiling. See 4 C.C.R. 904-3, Rule 9.04(C). Finally, although the CPA permits consumers to opt out of automated profiling, it does not provide a mechanism for consumers to challenge the resulting decisions of such profiling. See Dempsey, Artificial Intelligence Regulation, *supra* at 9.

**4.** ***The Effectiveness of Statutory Protections.*** To what extent are websites and Internet companies complying with these newly enacted state standards for consumer protection? Lior Strahilevitz et al., Measuring Compliance with the California Privacy Act Over Space and Time, *in* Proceedings of the CHI Conference on Human Factors in Computing Systems (May 11, 2024), examined more than 1,000 websites and found that, although compliance was not perfect, the CCPA has been effective in enabling customers to opt out of the sale

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or sharing of their personal data. Strahilevitz et al. found that businesses increasingly implemented opt-out links on their websites and increasingly altered their existing opt-out links to comply with the heightened requirements of the CPRA, with around 70 percent of the websites viewed implementing such links by July 2023. The authors also discovered that more than half of the 581 websites that implement an opt-out link in at least one state tend to do so across all states, including states that have not yet enacted state-specific privacy laws, like Illinois.

Does this suggest a spillover effect of the CPRA on non-California consumers? Should California's formulation of data privacy law become the gold standard for data protection in the United States?

## *Desnick v. American Broadcasting Co., Inc.*

44 F.3d 1345 (7th Cir. 1995)

Posner, C.J. The plaintiffs—an ophthalmic clinic known as the "Desnick Eye Center" after its owner, Dr. Desnick, and two ophthalmic surgeons employed by the clinic, Glazer and Simon—appeal from the dismissal of their suit against the ABC television network, a producer of the ABC program *PrimeTime Live* named Entine, and the program's star reporter, Donaldson. The suit is for trespass, defamation, and other torts arising out of the production and broadcast of a program segment of *PrimeTime Live* that was highly critical of the Desnick Eye Center. . . .

In March of 1993 Entine telephoned Dr. Desnick and told him that *PrimeTime Live* wanted to do a broadcast segment on large cataract practices. The Desnick Eye Center has 25 offices in four midwestern states and performs more than 10,000 cataract operations a year, mostly on elderly persons whose cataract surgery is paid for by Medicare. The complaint alleges—and in the posture of the case we must take the allegations to be true, though of course they may not be—that Entine told Desnick that the segment would not be about just one cataract practice, that it would not involve "ambush" interviews or "undercover" surveillance, and that it would be "fair and balanced." Thus reassured, Desnick permitted an ABC crew to videotape the Desnick Eye Center's main premises in Chicago, to film a cataract operation "live," and to interview doctors, technicians, and patients. Desnick also gave Entine a videotape explaining the Desnick Eye Center's services.

Unbeknownst to Desnick, Entine had dispatched persons equipped with concealed cameras to offices of the Desnick Eye Center in Wisconsin and Indiana. Posing as patients, these persons—seven in all—requested eye examinations. Plaintiffs Glazer and Simon are among the employees of the Desnick Eye Center who were secretly videotaped examining these "test patients."

The program aired on June 10. Donaldson introduces the segment by saying, "We begin tonight with the story of a so-called 'big cutter,' Dr. James Desnick. . . . [I]n our undercover investigation of the big cutter you'll meet tonight, we turned up evidence that he may also be a big charger, doing unnecessary cataract surgery for the money." Brief interviews with four patients of the Desnick Eye Center follow. One of the patients is satisfied ("I was blessed"); the other three are not—one of them says, "If you got three eyes, he'll get three eyes." Donaldson then reports on the experiences of the seven test patients. The two who were under 65 and thus not eligible for Medicare reimbursement were told they didn't need cataract surgery. Four of the other five were told they did. Glazer and Simon are shown recommending cataract surgery to them. Donaldson tells the viewer that *PrimeTime Live* has hired a professor of ophthalmology to examine the test patients who had been told they needed cataract surgery,

and the professor tells the viewer that they didn't need it—with regard to one he says, "I think it would be near malpractice to do surgery on him." Later in the segment he denies that this could just be an honest difference of opinion between professionals.

[The show also broadcasted an interview with an ophthalmic surgeon who turned down a job with Desnick because of his inability to screen patients; a former marketing executive who noted that the firm took advantage of "people who had Alzheimer's, and people who did not know what planet they were on"; former patients who had unsatisfactory experiences at the clinic; and a former employee who said that Dr. Desnick altered vision tests to make it appear that people needed cataract operations. The show then detailed how Desnick "rigged" a glare machine to persuade people that they had cataracts.]

The plaintiffs' claims fall into two distinct classes. The first arises from the broadcast itself, the second from the means by which ABC and Entine obtained the information that they used in the broadcast. The first is a class of one. The broadcast is alleged to have defamed the three plaintiffs by charging that the glare machine is tampered with. [The court holds that the evidence, as presented, is sufficient to reach the jury on defamation.]

The second class of claims in this case concerns, as we said, the methods that the defendants used to create the broadcast segment. There are four such claims: that the defendants committed a trespass in insinuating the test patients into the Wisconsin and Indiana offices of the Desnick Eye Center, that they invaded the right of privacy of the Center and its doctors at those offices (specifically Glazer and Simon), that they violated federal and state statutes regulating electronic surveillance, and that they committed fraud by gaining access to the Chicago office by means of a false promise that they would present a "fair and balanced" picture of the Center's operations and would not use "ambush" interviews or undercover surveillance.

To enter upon another's land without consent is a trespass. The force of this rule has, it is true, been diluted somewhat by concepts of privilege and of implied consent. But there is no journalists' privilege to trespass. And there can be no implied consent in any nonfictitious sense of the term when express consent is procured by a misrepresentation or a misleading omission. The Desnick Eye Center would not have agreed to the entry of the test patients into its offices had it known they wanted eye examinations only in order to gather material for a television exposé of the Center and that they were going to make secret videotapes of the examinations. Yet some cases, illustrated by Martin v. Fidelity & Casualty Co., 421 So. 2d 109, 111 (Ala. 1982), deem consent effective even though it was procured by fraud. There must be *something* to this surprising result. Without it a restaurant critic could not conceal his identity when he ordered a meal, or a browser pretend to be interested in merchandise that he could not afford to buy. Dinner guests would be trespassers if they were false friends who never would have been invited had the host known their true character, and a consumer who in an effort to bargain down an automobile dealer falsely claimed to be able to buy the same car elsewhere at a lower price would be a trespasser in the dealer's showroom. Some of these might be classified as privileged trespasses, designed to promote competition. Others might be thought justified by some kind of implied consent—the restaurant critic for example might point by way of analogy to the use of the "fair use" defense by book reviewers charged with copyright infringement and argue that the restaurant industry as a whole would be injured if restaurants could exclude critics. But most such efforts at rationalization would be little better than evasions. The fact is that consent to an entry is often given legal effect even though the entrant has intentions that if known to the owner of the property would cause him for perfectly understandable and generally ethical or at least lawful reasons to revoke his consent.

The law's willingness to give effect to consent procured by fraud is not limited to the tort of trespass. The Restatement gives the example of a man who obtains consent to sexual intercourse by promising a woman $100, yet (unbeknownst to her, of course) he pays her with a counterfeit bill and intended to do so from the start. The man is not guilty of battery, even

though unconsented-to sexual intercourse is a battery. Restatement (Second) of Torts §892B, illustration 9, pp. 373–74 (1979). Yet we know that to conceal the fact that one has a venereal disease transforms "consensual" intercourse into battery. Seduction, standardly effected by false promises of love, is not rape; intercourse under the pretense of rendering medical or psychiatric treatment is, at least in most states. Trespass presents close parallels. If a homeowner opens his door to a purported meter reader who is in fact nothing of the sort — just a busybody curious about the interior of the home — the homeowner's consent to his entry is not a defense to a suit for trespass. And likewise if a competitor gained entry to a business firm's premises posing as a customer but in fact hoping to steal the firm's trade secrets. Rockwell Graphic Systems, Inc. v. DEV Industries, Inc., 925 F.2d 174, 178 (7th Cir. 1991). . . .

How to distinguish the two classes of case — the seducer from the medical impersonator, the restaurant critic from the meter-reader impersonator? The answer can have nothing to do with fraud; there is fraud in all the cases. It has to do with the interest that the torts in question, battery and trespass, protect. The one protects the inviolability of the person, the other the inviolability of the person's property. The woman who is seduced wants to have sex with her seducer, and the restaurant owner wants to have customers. The woman who is victimized by the medical impersonator has no desire to have sex with her doctor; she wants medical treatment. And the homeowner victimized by the phony meter reader does not want strangers in his house unless they have authorized service functions. The dealer's objection to the customer who claims falsely to have a lower price from a competing dealer is not to the physical presence of the customer, but to the fraud that he is trying to perpetuate. The lines are not bright — they are not even inevitable. They are the traces of the old forms of action, which have resulted in a multitude of artificial distinctions in modern law. But that is nothing new.

There was no invasion in the present case of any of the specific interests that the tort of trespass seeks to protect. The test patients entered offices that were open to anyone expressing a desire for ophthalmic services and videotaped physicians engaged in professional, not personal, communications with strangers (the testers themselves). The activities of the offices were not disrupted. . . . Nor was there any "inva[sion of] a person's private space," as in our hypothetical meter reader case, as in the famous case of De May v. Roberts, 46 Mich. 160, 9 N.W. 146 (Mich. 1881), . . . and as in Dietemann v. Time, Inc., 449 F.2d 245 (9th Cir. 1971), on which the plaintiffs in our case rely. *Dietemann* involved a home. True, the portion invaded was an office, where the plaintiff performed quack healing of nonexistent ailments. The parallel to this case is plain enough, but there is a difference. Dietemann was not in business, and did not advertise his services or charge for them. His quackery was private.

No embarrassingly intimate details of anybody's life were publicized in the present case. There was no eavesdropping on a private conversation; the testers recorded their own conversations with the Desnick Eye Center's physicians. There was no violation of the doctor-patient privilege. There was no theft, or intent to steal, trade secrets; no disruption of decorum, of peace and quiet; no noisy or distracting demonstrations. Had the testers been undercover FBI agents, there would have been no violation of the Fourth Amendment, because there would have been no invasion of a legally protected interest in property or privacy. "Testers" who pose as prospective home buyers in order to gather evidence of housing discrimination are not trespassers even if they are private persons not acting under color of law. The situation of the defendants' "testers" is analogous. Like testers seeking evidence of violation of anti-discrimination laws, the defendants' test patients gained entry into the plaintiffs' premises by misrepresenting their purposes (more precisely by a misleading omission to disclose those purposes). But the entry was not invasive in the sense of infringing the kind of interest of the plaintiffs that the law of trespass protects; it was not an interference with the ownership or possession of land. We need not consider what if any difference it would make if the plaintiffs had festooned the premises with signs forbidding the entry of testers or other snoops. Perhaps none, but that is an issue for another day.

What we have said largely disposes of two other claims — infringement of the right of privacy, and illegal wiretapping. The right of privacy embraces several distinct interests, but the only ones conceivably involved here are the closely related interests in concealing intimate personal facts and in preventing intrusion into legitimately private activities, such as phone conversations. . . .

Affirmed in part, reversed in part, and remanded.

## NOTES

**1.** ***Trespass by Fraudulent Entry.*** In intrusion cases that involve an actual entry onto the plaintiff's land, the dispute sometimes boils down to whether the plaintiff's consent to entry has been vitiated by the defendant's fraud. In the early case of De May v. Roberts, 9 N.W. 146, 149 (Mich. 1881), the plaintiff was granted an action for invasion of privacy against an attending physician who brought a young unmarried man into the plaintiff's apartment to observe the physician delivering her baby.

> In obtaining admission at such a time and under such circumstances without fully disclosing his true character, both parties were guilty of deceit, and the wrong thus done entitles the injured party to recover the damages afterwards sustained, from shame and mortification upon discovering the true character of the defendants.

Is *Desnick* distinguishable? Does it matter that the restaurant critic sometimes publishes favorable reviews, whereas ABC will report nothing if they cannot uncover some scandal?

**2.** ***Publication and Fraudulent Entry.*** With *Desnick*, compare Dietemann v. Time, Inc., 449 F.2d 245, 249 (9th Cir. 1971), in which the plaintiff, "a disabled veteran with little education, was engaged in the practice of healing with clay, minerals, and herbs — as practiced, simply quackery." As part of an effort to expose the practices of the plaintiff and those like him, two of defendant's reporters for *Life* magazine, Mr. Ray and Mrs. Metcalf, hatched a scheme with the local district attorney's office that allowed the pair to gain entry into the plaintiff's home by falsely representing that they had been sent by a friend for treatment. By means of concealed equipment, Mrs. Metcalf transmitted the conversations between herself and the plaintiff to a parked car occupied by a *Life* employee and two government officials. Mr. Ray took secret pictures of the plaintiff, later used in the *Life* story, including one of the "plaintiff with his hand on the upper portion of Mrs. Metcalf's breast while he was looking at some gadgets and holding what appeared to be a wand in his right hand." Four weeks later, the plaintiff was arrested for practicing medicine without a license and, after the publication of the story, entered a plea of nolo contendere. Thereafter, he recovered $1,000 in a tort action for the invasion of privacy, and the verdict was affirmed on appeal. "The First Amendment has never been construed to accord newsmen immunity from torts or crimes committed during the course of newsgathering. The First Amendment is not a license to trespass, to steal, or to intrude by electronic means into the precincts of another's home or office." This quotation from *Dietemann* proved decisive in NAF v. Center for Medical Progress, 685 Fed. App'x 623, 625–26 (9th Cir. 2017), to hold liable defendants who falsely represented themselves as fetal tissue researchers to gain entry to a private meeting of abortion providers. The defendants videotaped the meetings despite signing nondisclosure agreements. Should it make any difference that *Desnick* took place in a public space, that *Dietemann* took place in a private home, and that *NAF* took place in a private meeting space? What result if the defendants had passed the information on to a third party for publication?

A similar damage suit for investigative reporting failed in Food Lion, Inc. v. Capital Cities/ABC, Inc., 194 F.3d 505 (4th Cir. 1999). The defendants, producers of the show *PrimeTime Live*, developed a scheme whereby two of their investigators, Susan Barnett and Lynne Litt, fraudulently obtained positions in the meat department of a Food Lion store. They used hidden cameras to take footage of its operations that was subsequently used in a hard-hitting broadcast about the grocery store's dangerous health practices in a November 1992 episode of *PrimeTime Live*. A jury awarded over $5.5 million in punitive damages against ABC, Inc., and the broadcast's executive and senior producers. The plaintiffs' claims for trespass and invasion of privacy were ultimately rebuffed on the ground that the "publication damages," namely, the substantial loss in business that followed the broadcast, could not be recovered given the First Amendment. As a matter of tort law, are these publication damages proximately caused by the initial trespass? For a criticism of *Desnick* and *Food Lion*, see Richard A. Epstein, Privacy, Publication, and the First Amendment: The Dangers of First Amendment Exceptionalism, 52 Stan. L. Rev. 1003, 1020–23 (2000).

Even plaintiffs who are not the targets of investigation have lost cases for intrusion upon seclusion based on the First Amendment protections granted to the press. In Howell v. New York Post Co., Inc., 612 N.E.2d 699, 700 (N.Y. 1993), the plaintiff was a patient at the Four Winds Hospital, a private psychiatric hospital. Her complaint (treated as true on appeal) alleged "that it was imperative to her recovery that the hospitalization remain a secret from all but her immediate family." A co-resident at the facility was Hedda Nussbaum, who had received massive publicity as the "adoptive" mother of six-year-old Lisa Steinberg, who had died of unrelenting child abuse. In September 1988, a *Post* photographer trespassed on the hospital grounds and used a telephoto lens to take pictures of a group of patients that included Nussbaum and the plaintiff. That evening the medical director of Four Winds pleaded with the *Post* not to run the picture. But the next day it appeared, showing a happy and recuperating Nussbaum in the company of friends, next to a picture of her bruised and disfigured face at the time of her arrest. The caption beneath the picture read:

> The battered face above belongs to the Hedda Nussbaum people remember — the former live-in lover of accused child-killer, Joel Steinberg. The serene woman in jeans at left is the same Hedda, strolling with a companion in the grounds of the upstate psychiatric center where her face and mind are healing from the terrible wounds Steinberg inflicted.

Although the plaintiff's name was not used in the picture, her identity was easily discernible.

Kaye, C.J., wrote for a unanimous court and rejected both the claim for intentional infliction of emotional distress and for an invasion of privacy. She held that a real relationship between the public story and the inclusion of the plaintiff in the picture blocked recognition of the privacy tort: "The visual impact would not have been the same had the *Post* cropped plaintiff out of the photograph, as she suggests was required." She then dispatched *Galella* (*supra* Note 1, at 421) by noting that the journalist's trespassory conduct here did not "remotely approach" the required minimum, given that the picture was taken outdoors and from a distance.

The fortunes of war shifted yet again in Sanders v. American Broadcasting Co., Inc., 978 P.2d 67, 77 (Cal. 1999), involving yet another *PrimeTime Live* broadcast. An ABC employee took a position as an employee of a telepsychic company and secretly videotaped her conversations with the plaintiff, another telepsychic. Even though these conversations were routinely witnessed by other employees, Werdegar, J., rejected the notion that privacy had "a binary, all-or-nothing characteristic," and concluded that "in the workplace, as elsewhere, the reasonableness of a person's expectation of visual and aural privacy depends not only on who might have been able to observe the subject interaction, but on the identity of the claimed intruder and the means of intrusion." Accordingly, "a person who lacks a reasonable expectation of

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complete privacy in a conversation, because it could be seen and overheard by coworkers (but not the general public), may nevertheless have a claim for invasion of privacy by intrusion based on a television reporter's covert videotaping of that conversation." *Desnick* was distinguished on the ground that *Sanders* is concerned "with interactions between coworkers rather than between a proprietor and a customer."

The California Supreme Court relied on *Sanders* in Taus v. Loftus, 151 P.3d 1185, 1216–17 (Cal. 2007), where the plaintiff had, as "Jane Doe," been the subject of previous stories indicating how she had suffered serious child abuse at the hands of her mother. The defendant, Elizabeth Loftus, a prominent cognitive psychologist and skeptic of "repressed memory" cases, published two articles that mentioned the plaintiff by name and disputed the accuracy of the original accounts. George, C.J., first held that the defendant had not invaded the plaintiff's privacy when she had discovered the plaintiff's identity by piecing together information from public sources. But he further held that the defendant did invade the plaintiff's privacy if, as alleged, she had secured an interview with the plaintiff's former foster mother by falsely pretending to be working with the physician who was currently treating the plaintiff, to obtain information that would not otherwise be divulged. Accordingly, a violation of a person's reasonable expectation of privacy could occur "when a third party—for example, a private investigator—obtains access to personal information about the person . . . by utilizing improper and unanticipated means, particularly when such information would not have been disclosed by the relative or friend absent the third party's use of such means." Should the action allow for damages for the publication of that information?

These partially real, partially fictionalized accounts were also the subject of dispute in Washington v. Netflix Productions, LLC, 2022 N.Y. Misc. Lexis 29302 (N.Y. Sup. Ct. Aug. 2, 2022). A Netflix special, *Surviving Death*, featured a boy who was held out to be the reincarnation of Jaylen, who had been murdered by his babysitter at five years old. Netflix sought to establish this connection by having the boy pick out family photos associated with his past life as Jaylen, but he falsely identified certain places Jaylen and his family supposedly visited. Jaylen's parents sued for violation of privacy. Even though the topic was newsworthy, the case was still allowed to go to a jury because the plaintiffs alleged that "the episode is not actually a documentary—but rather a fictional story with obvious liberties taken in order to fit a particular narrative—namely that reincarnation could be 'real' in order to keep its audience interested."

**3. *Receipt—and Publication—of Stolen Information.*** In Pearson v. Dodd, 410 F.2d 701, 705–06, 708 (D.C. Cir. 1969), the defendants, columnists Drew Pearson and Jack Anderson, received illegally made photocopies of numerous confidential documents from the offices of the plaintiff, Senator Thomas Dodd of Connecticut. The material concerned the plaintiff's relationship to certain lobbyists for foreign interests, and the defendants used it to portray the plaintiff in an unflattering fashion. Wright, J., first noted that the plaintiff had not proved his charge that the defendants had "aided and abetted in the removal of the documents." He then dismissed the action, drawing a distinction between the damages caused by obtaining and by publishing the information:

> Of course, appellants did more than receive and peruse the copies of the documents taken from appellee's files; they published excerpts from them in the national press. But in analyzing a claimed breach of privacy, injuries from intrusion and injuries from publication should be kept clearly separate. Where there is intrusion, the intruder should generally be liable whatever the content of what he learns. An eavesdropper to the marital bedroom may hear marital intimacies, or he may hear statements of fact or opinion of legitimate interest to the public; for purposes of liability that should make no difference. On the other hand, where the claim is that private information concerning plaintiff has been published, the question of whether that information is genuinely private or is of public interest should not turn on the manner in which it has been obtained. Of course, both forms of invasion may be combined in the same case.

In dismissing the action, Wright., J., noted that the material published was "of obvious public interest." Judge Tamm, concurring, observed:

> Some legal scholars will see in the majority opinion — as distinguished from its actual holding — an ironic aspect. Conduct for which a law enforcement officer would be soundly castigated is, by the phraseology of the majority opinion, found tolerable; conduct which, if engaged in by government agents would lead to the suppression of evidence obtained by these means, is approved when used for the profit of the press. There is an anomaly lurking in this situation: the news media regard themselves as quasi-public institutions yet they demand immunity from the restraints which they vigorously demand be placed on government. That which is regarded as a mortal taint on information secured by any illegal conduct of government would appear from the majority opinion to be permissible as a technique or modus operandi for the journalist.

Could Anderson and Pearson have been sued under *Dietemann* for the damages caused by the publication in their columns if they or their agents had personally obtained the material in question?

Shortly afterward, in New York Times Co. v. United States, 403 U.S. 713 (1971) (the "Pentagon Papers" case), the Supreme Court upheld the right of the press to publish classified information that had been stolen from the government by a third party so long as it related to matters of great public concern — in that case the motivations and justifications for the Vietnam War. *New York Times* left open the question of whether a party that had obtained the information lawfully could be held liable for disclosing information that he knew or had reason to know had been obtained illegally in the first instance. That question arose in Bartnicki v. Vopper, 532 U.S. 514, 530–31, 534 (2001). The plaintiffs Bartnicki and Kane were union leaders in the midst of contentious negotiations with the local school board. During a lengthy cell phone call, Kane told Bartnicki that "if they're [the Board] not gonna move for three percent, we're gonna have to go to their, their homes. . . . To blow off their front porches." An unknown person illegally intercepted the conversation, and then mailed a tape of the session to Yocum, the head of a local taxpayer's organization that had opposed the union demands. After the union won a favorable settlement, Yocum handed the tape over to Vopper, who broadcast it on his public affairs talk show. Federal and state law make it a crime for any person to "intentionally disclose" the contents of any phone communication that he knows or has reason to know was obtained in violation of federal law. However, the plaintiff's claim for invasion of privacy from the publication of the information failed because Vopper's publication was held protected under the First Amendment. Justice Stevens wrote:

> The normal method of deterring unlawful conduct is to impose an appropriate punishment on the person who engages in it. If the sanctions that presently attach to a violation of [the rule against illegal interceptions] do not provide sufficient deterrence, perhaps those sanctions should be made more severe. But it would be quite remarkable to hold that speech by a law-abiding possessor of information can be suppressed in order to deter conduct by a non-law-abiding third party. . . .
>
> In th[is] case[ ], privacy concerns give way when balanced against the interest in publishing matters of public importance. As Warren and Brandeis stated in their classic law review article: "The right of privacy does not prohibit any publication of matter which is of public or general interest." One of the costs associated with participation in public affairs is an attendant loss of privacy.

Chief Justice Rehnquist's dissent criticized the Court for speaking about "a matter of 'public concern,' an amorphous concept that the Court does not even attempt to define. But the Court's decision diminishes, rather than enhances, the purposes of the First Amendment, thereby chilling the speech of the millions of Americans who rely upon electronic technology to communicate each day." Why shouldn't Vopper be sued successfully in tort for receiving goods known to be stolen?

*Bartnicki* proved decisive in Yurish v. Sinclair Broadcast Group, Inc., 866 S.E.2d 156, 166 (W. Va. 2021), where the mother of a young girl placed a recording device in her daughter's hair to catch her teachers physically and verbally abusing students. The mother sent the tapes to various media companies, who published them. The court found that the teachers had no recourse against these media companies so long as they "did not participate in the unlawful interception of the communication."

## *Shulman v. Group W Productions, Inc.*

955 P.2d 469 (Cal. 1998)

Werdegar, J. More than 100 years ago, Louis Brandeis and Samuel Warren complained that the press, armed with the then recent invention of "instantaneous photographs" and under the influence of new "business methods," was "overstepping in every direction the obvious bounds of propriety and of decency." . . . The sense of an ever-increasing pressure on personal privacy notwithstanding, it has long been apparent that the desire for privacy must at many points give way before our right to know, and the news media's right to investigate and relate, facts about the events and individuals of our time. Brandeis and Warren were themselves aware that recognition of the right to privacy requires a line to be drawn between properly private events, words and actions and those of "public and general interest" with which the community has a "legitimate concern." . . .

. . . In the present case, we address the balance between privacy and press freedom in the commonplace context of an automobile accident. Plaintiffs, two members of a family whose activities and position did not otherwise make them public figures, were injured when their car went off the highway, overturning and trapping them inside. A medical transport and rescue helicopter crew came to plaintiffs' assistance, accompanied on this occasion by a video camera operator employed by a television producer. The cameraman filmed plaintiffs' extrication from the car, the flight nurse and medic's efforts to give them medical care during the extrication, and their transport to the hospital in the helicopter. The flight nurse wore a small microphone that picked up her conversations with other rescue workers and with one of the plaintiffs. This videotape and sound track were edited into a segment that was broadcast, months later, on a documentary television show, *On Scene: Emergency Response*. Plaintiffs, who consented neither to the filming and recording nor to the broadcasting, allege the television producers thereby intruded into a realm of personal privacy and gave unwanted publicity to private events of their lives. . . .

. . . Ruth and Wayne sued the producers of *On Scene: Emergency Response*, as well as others. The first amended complaint included two causes of action for invasion of privacy, one based on defendants' unlawful intrusion by videotaping the rescue in the first instance and the other based on the public disclosure of private facts, i.e., the broadcast. . . .

### II. Intrusion

Of the four privacy torts identified by Prosser, the tort of intrusion into private places, conversations or matter is perhaps the one that best captures the common understanding of an "invasion of privacy." It encompasses unconsented-to physical intrusion into the home, hospital room or other place the privacy of which is legally recognized, as well as unwarranted sensory intrusions such as eavesdropping, wiretapping, and visual or photographic spying. (See Rest. 2d Torts, § 652B, com. b., pp. 378–79 and illustrations.) . . .

. . . We ask first whether defendants "intentionally intrude[d], physically or otherwise, upon the solitude or seclusion of another," that is, into a place or conversation private to

Wayne or Ruth. . . . To prove actionable intrusion, the plaintiff must show the defendant penetrated some zone of physical or sensory privacy surrounding, or obtained unwanted access to data about, the plaintiff. The tort is proven only if the plaintiff had an objectively reasonable expectation of seclusion or solitude in the place, conversation or data source. . . . Cameraman Cooke's mere presence at the accident scene and filming of the events occurring there cannot be deemed either a physical or sensory intrusion on plaintiffs' seclusion. Plaintiffs had no right of ownership or possession of the property where the rescue took place, nor any actual control of the premises. Nor could they have had a reasonable expectation that members of the media would be excluded or prevented from photographing the scene; for journalists to attend and record the scenes of accidents and rescues is in no way unusual or unexpected. . . .

. . . Two aspects of defendants' conduct, however, raise triable issues of intrusion on seclusion. First, a triable issue exists as to whether both plaintiffs had an objectively reasonable expectation of privacy in the interior of the rescue helicopter, which served as an ambulance. Although the attendance of reporters and photographers at the scene of an accident is to be expected, we are aware of no law or custom permitting the press to ride in ambulances or enter hospital rooms during treatment without the patient's consent. . . . Second, Ruth was entitled to a degree of privacy in her conversations with Carnahan and other medical rescuers at the accident scene, and in Carnahan's conversations conveying medical information regarding Ruth to the hospital base. Cooke, perhaps, did not intrude into that zone of privacy merely by being present at a place where he could hear such conversations with unaided ears. But by placing a microphone on Carnahan's person, amplifying and recording what she said and heard, defendants may have listened in on conversations the parties could reasonably have expected to be private. . . . Whether Ruth expected her conversations with Nurse Carnahan or the other rescuers to remain private and whether any such expectation was reasonable are, on the state of the record before us, questions for the jury. We note, however, that several existing legal protections for communications could support the conclusion that Ruth possessed a reasonable expectation of privacy in her conversations with Nurse Carnahan and the other rescuers. [The court lists the physician-patient privilege and various California statutes that protect confidential information.] . . .

. . . We turn to the second element of the intrusion tort, offensiveness of the intrusion. . . . [T]he circumstances of an intrusion, including the motives or justification of the intruder, are pertinent to the offensiveness element. Motivation or justification becomes particularly important when the intrusion is by a member of the print or broadcast press in the pursuit of news material. . . . In deciding, therefore, whether a reporter's alleged intrusion into private matters (i.e., physical space, conversation or data) is "offensive" and hence actionable as an invasion of privacy, courts must consider the extent to which the intrusion was, under the circumstances, justified by the legitimate motive of gathering the news. Information collecting techniques that may be highly offensive when done for socially unprotected reasons — for purposes of harassment, blackmail or prurient curiosity, for example — may not be offensive to a reasonable person when employed by journalists in pursuit of a socially or politically important story. . . . The mere fact the intruder was in pursuit of a "story" does not, however, generally justify an otherwise offensive intrusion; offensiveness depends as well on the particular method of investigation used. At one extreme, "'routine . . . reporting techniques,'" such as asking questions of people with information ("including those with confidential or restricted information") could rarely, if ever, be deemed an actionable intrusion. . . . At the other extreme, violation of well-established legal areas of physical or sensory privacy — trespass into a home or tapping a personal telephone line, for example — could rarely, if ever, be justified by a reporter's need to get the story. . . . Between these extremes lie difficult cases, many involving the use of photographic and electronic recording equipment. Equipment such as hidden cameras and miniature cordless and directional microphones are powerful

investigative tools for newsgathering, but may also be used in ways that severely threaten personal privacy. California tort law provides no bright line on this question; each case must be taken on its facts. . . .

. . . On this summary judgment record, we believe a jury could find defendants' recording of Ruth's communications to Carnahan and other rescuers, and filming in the air ambulance, to be "'highly offensive to a reasonable person.'" . . . Defendants, it could reasonably be said, took calculated advantage of the patient's "vulnerability and confusion." . . . Arguably, the last thing an injured accident victim should have to worry about while being pried from her wrecked car is that a television producer may be recording everything she says to medical personnel for the possible edification and entertainment of casual television viewers. . . . Nor can we say as a matter of law that defendants' motive—to gather usable material for a potentially newsworthy story necessarily privileged their intrusive conduct as a matter of common law tort liability. A reasonable jury could conclude the producers' desire to get footage that would convey the "feel" of the event—the real sights and sounds of a difficult rescue—did not justify either placing a microphone on Nurse Carnahan or filming inside the rescue helicopter. Although defendants' purposes could scarcely be regarded as evil or malicious (in the colloquial sense), their behavior could, even in light of their motives, be thought to show a highly offensive lack of sensitivity and respect for plaintiffs' privacy. . . . Turning to the question of constitutional protection for newsgathering, one finds the decisional law reflects a general rule of nonprotection: the press in its newsgathering activities enjoys no immunity or exemption from generally applicable laws. . . . "It is clear that the First Amendment does not invalidate every incidental burdening of the press that may result from the enforcement of civil and criminal laws of general applicability. Under prior cases, otherwise valid laws serving substantial public interests may be enforced against the press as against others, despite the possible burden that may be imposed." . . . As to constitutional policy, we repeat that the threat of infringement on the liberties of the press from intrusion liability is minor compared with the threat from liability for publication of private facts. Indeed, the distinction led one influential commentator to assert flatly that "[i]ntrusion does not raise first amendment difficulties since its perpetration does not involve speech or other expression." . . . [N]o constitutional precedent or principle of which we are aware gives a reporter general license to intrude in an objectively offensive manner into private places, conversations or matters merely because the reporter thinks he or she may thereby find something that will warrant publication or broadcast.

The claim of these accident victims that their privacy was invaded by the production and broadcast of a documentary segment on their rescue raises questions about how the news media obtain their material (the intrusion claim), as well as about what they choose to publish or broadcast (the publication of private facts claim). Largely for constitutional reasons, the paths we have taken in analyzing these two privacy claims have diverged and led to different results.

The broadcast details of Ruth's rescue of which she complains were, as a matter of law, of legitimate public concern because they were substantially relevant to the newsworthy subject of the piece and their intrusiveness was not greatly disproportionate to their relevance. That analytical path is dictated by the danger of the contrary approach; to allow liability because this court, or a jury, believes certain details of the story as broadcast were not important or necessary to the purpose of the documentary, or were in poor taste or overly sensational in impact, would be to assert impermissible supervisory power over the press.

The intrusion claim calls for a much less deferential analysis. In contrast to the broad privilege the press enjoys for publishing truthful, newsworthy information in its possession, the press has no recognized constitutional privilege to violate generally applicable laws in pursuit of material. Nor, even absent an independent crime or tort, can a highly offensive intrusion into a private place, conversation, or source of information generally be justified by the plea

that the intruder hoped thereby to get good material for a news story. Such a justification may be available when enforcement of the tort or other law would place an impermissibly severe burden on the press, but that condition is not met in this case.

In short, the state may not intrude into the proper sphere of the news media to dictate what they should publish and broadcast, but neither may the media play tyrant to the people by unlawfully spying on them in the name of newsgathering. Summary judgment for the defense was proper as to plaintiffs' cause of action for publication of private facts (the second cause of action), but improper as to the cause of action for invasion of privacy by intrusion (the first cause of action).

The judgment of the Court of Appeal is affirmed except insofar as the Court of Appeal reversed and remanded for further proceedings on Ruth Shulman's cause of action for publication of private facts.

## NOTES

**1.** ***A Newsworthiness Privilege?*** Note that the *Shulman* court was not keen on establishing broad protection for journalists vis-à-vis the intrusion tort. Has the court's view that legitimate news gathering generally should not depend on clandestine or surreptitious means — such as recording devices — fallen out of favor, given that virtually everyone today has access to such recording devices in the form of smartphones? What about the Internet? Would a journalist who publishes leaked conversations online, thereby exposing significant corruption or bribery, fall under *Shulman*?

**2.** ***Tortious, Offensive, or Both?*** After *Shulman*, how should plaintiffs plead intrusion claims? The *Shulman* court proscribed "highly offensive intrusions" even absent "independent . . . tort[s]." But would pleading an independent tort help the plaintiffs? Imagine, for example, an offensive intrusion that is also cognizable as an "independent tort," such as an effort to record audio that requires a trespass to the plaintiff's person? To the treating physician? Does the trespass element render the effort more offensive? Or does the *Shulman* court suggest that offensiveness and the presence of an "independent tort" are separate analyses?

## SECTION D. PUBLIC DISCLOSURE OF EMBARRASSING PRIVATE FACTS

### RESTATEMENT OF THE LAW (SECOND) OF TORTS

#### §652D. Publicity Given to Private Life

One who gives publicity to a matter concerning the private life of another is subject to liability to the other for invasion of his privacy, if the matter publicized is of a kind that

(a) would be highly offensive to a reasonable person, and
(b) is not of legitimate concern to the public.

***Comment a. Publicity:*** The form of invasion of the right of privacy covered in this Section depends upon publicity given to the private life of the individual. "Publicity," as it is used in this Section, differs from "publication," as that term is used in §577 in connection with liability for defamation. "Publication," in that sense, is a word of art, which includes any communication by the defendant to a third person. "Publicity," on

the other hand, means that the matter is made public, by communicating it to the public at large, or to so many persons that the matter must be regarded as substantially certain to become one of public knowledge. The difference is not one of the means of communication, which may be oral, written, or by any other means. It is one of a communication which reaches, or is sure to reach, the public. . . .

***Comment b. Private Life:*** The rule stated in this Section applies only to publicity given to matters concerning the private, as distinguished from the public, life of the individual. There is no liability when the defendant merely gives further publicity to information about the plaintiff that is already public. Thus, there is no liability for giving publicity to facts about the plaintiff's life that are matters of public record, such as the date of his birth, the fact of his marriage, his military record, the fact that he is admitted to the practice of medicine or is licensed to drive a taxicab, or the pleadings that he has filed in a lawsuit. On the other hand, if the record is one not open to public inspection, as in the case of income tax returns, it is not public, and there is an invasion of privacy when it is made so. . . .

## *Sidis v. F-R Publishing Corp.*

113 F.2d 806 (2d Cir. 1940)

Clark, J. William James Sidis was the unwilling subject of a brief biographical sketch and cartoon printed in The New Yorker weekly magazine for August 14, 1937. Further references were made to him in the issue of December 25, 1937, and in a newspaper advertisement announcing the August 14 issue. He brought an action in the district court against the publisher, F-R Publishing Corporation. His complaint stated three "causes of action": The first alleged violation of his right of privacy as that right is recognized in California, Georgia, Kansas, Kentucky, and Missouri; the second charged infringement of the rights afforded him under §§50 and 51 of the N.Y. Civil Rights Law; the third claimed malicious libel under the laws of [nine states]. Defendant's motion to dismiss the first two "causes of action" was granted, and plaintiff has filed an appeal from the order of dismissal. . . .

William James Sidis was a famous child prodigy in 1910. His name and prowess were well known to newspaper readers of the period. At the age of eleven, he lectured to distinguished mathematicians on the subject of Four-Dimensional Bodies. When he was sixteen, he was graduated from Harvard College, amid considerable public attention. Since then, his name has appeared in the press only sporadically, and he has sought to live as unobtrusively as possible. Until the articles objected to appeared in The New Yorker, he had apparently succeeded in his endeavor to avoid the public gaze.

Among The New Yorker's features are brief biographical sketches of current and past personalities. In the latter department, which appears haphazardly under the title "Where Are They Now?" the article on Sidis was printed with a subtitle "April Fool." The author [James Thurber] describes his subject's early accomplishments in mathematics and the wide-spread attention he received, then recounts his general breakdown and the revulsion which Sidis thereafter felt for his former life of fame and study. The unfortunate prodigy is traced over the years that followed, through his attempts to conceal his identity, through his chosen career as an insignificant clerk who would not need to employ unusual mathematical talents, and through the bizarre ways in which his genius flowered, as in his enthusiasm for collecting streetcar transfers and in his proficiency with an adding machine. The article closes with an account of an interview with Sidis at his present lodgings, "a hall bedroom of Boston's shabby

south end." The untidiness of his room, his curious laugh, his manner of speech, and other personal habits are commented upon at length, as is his present interest in the lore of the Okamakammessett Indians. The subtitle is explained by the closing sentence, quoting Sidis as saying "with a grin" that it was strange, "but, you know, I was born on April Fool's Day." Accompanying the biography is a small cartoon showing the genius of eleven years lecturing to a group of astounded professors.

It is not contended that any of the matter printed is untrue. Nor is the manner of the author unfriendly; Sidis today is described as having "a certain childlike charm." But the article is merciless in its dissection of intimate details of its subject's personal life, and this in company with elaborate accounts of Sidis' passion for privacy and the pitiable lengths to which he has gone in order to avoid public scrutiny. The work possesses great reader interest, for it is both amusing and instructive; but it may be fairly described as a ruthless exposure of a once public character, who has since sought and has now been deprived of the seclusion of private life.

The article of December 25, 1937, was a biographical sketch of another former child prodigy, in the course of which William James Sidis and the recent account of him were mentioned. The advertisement published in the New York World-Telegram of August 13, 1937, read: "Out Today. Harvard Prodigy. Biography of the man who astonished Harvard at age 11. Where are they now? by J. L. Manley. Page 22. The New Yorker." . . .

All comment upon the right of privacy must stem from the famous article by Warren and Brandeis on The Right of [to] Privacy in 4 Harv. L. Rev. 193. [The court then quoted from those passages of the article, set out *supra*, where Warren and Brandeis realized that the interest of the individual in privacy must inevitably conflict with the interest of the public in news. Certain public figures, they conceded, such as holders of public office, must sacrifice their privacy and expose at least part of their lives to public scrutiny as the price of the powers they attain. But even public figures were not to be stripped bare. "In general, then, the matters of which the publication should be repressed may be described as those which concern the private life, habits, acts, and relations of an individual, and have no legitimate connection with his fitness for a public office. . . . Some things all men alike are entitled to keep from popular curiosity, whether in public life or not, while others are only private because the persons concerned have not assumed a position which makes their doings legitimate matters of public investigation."

It must be conceded that under the strict standards suggested by these authors plaintiff's right of privacy has been invaded. Sidis today is neither politician, public administrator, nor statesman. Even if he were, some of the personal details revealed were of the sort that Warren and Brandeis believed "all men alike are entitled to keep from popular curiosity."

But despite eminent opinion to the contrary, we are not yet disposed to afford to all of the intimate details of private life an absolute immunity from the prying of the press. Everyone will agree that at some point the public interest in obtaining information becomes dominant over the individual's desire for privacy. Warren and Brandeis were willing to lift the veil somewhat in the case of public officers. We would go further, though we are not yet prepared to say how far. At least we would permit limited scrutiny of the "private" life of any person who has achieved, or has had thrust upon him, the questionable and indefinable status of a "public figure." . . .

William James Sidis was once a public figure. As a child prodigy, he excited both admiration and curiosity. Of him great deeds were expected. In 1910, he was a person about whom the newspapers might display a legitimate intellectual interest, in the sense meant by Warren and Brandeis, as distinguished from a trivial and unseemly curiosity. But the precise motives of the press we regard as unimportant. And even if Sidis had loathed public attention at that time, we think his uncommon achievements and personality would have made the attention permissible. Since then Sidis has cloaked himself in obscurity, but his subsequent history,

containing as it did the answer to the question of whether or not he had fulfilled his early promise, was still a matter of public concern. The article in The New Yorker sketched the life of an unusual personality, and it possessed considerable popular news interest.

We express no comment on whether or not the news worthiness of the matter printed will always constitute a complete defense. Revelations may be so intimate and so unwarranted in view of the victim's position as to outrage the community's notions of decency. But when focused upon public characters, truthful comments upon dress, speech, habits, and the ordinary aspects of personality will usually not transgress this line. Regrettably or not, the misfortunes and frailties of neighbors and "public figures" are subjects of considerable interest and discussion to the rest of the population. And when such are the mores of the community, it would be unwise for a court to bar their expression in the newspapers, books, and magazines of the day.

Plaintiff in his first "cause of action" charged actual malice in the publication, and now claims that an order of dismissal was improper in the face of such an allegation. We cannot agree. If plaintiff's right of privacy was not invaded by the article, the existence of actual malice in its publication would not change that result. Unless made so by statute, a truthful and therefore non-libelous statement will not become libelous when uttered maliciously. A similar rule should prevail on invasions of the right of privacy. "Personal ill-will is not an ingredient of the offence, any more than in an ordinary case of trespass to person or to property." Warren and Brandeis. Nor does the malice give rise to an independent wrong based on an intentional invasion of the plaintiff's interest in mental and emotional tranquility. This interest, however real, is one not yet protected by law.

If the article appearing in the issue of August 14, 1937, does not furnish grounds for action, then it is clear that the brief and incidental reference to it contained in the article of December 25, 1937, is not actionable.

[The court then held that the plaintiff had no cause of action under §§50 and 51 of the N.Y. Civil Rights Law, *infra* at 455, because the story was not done for commercial purposes.]

Affirmed.

**William James Sidis in 1914**
*Source: Wikimedia Commons*

## NOTES

**1.** ***The Painful Past.*** The original, lengthy *New Yorker* piece, James Thurber, Where Are They Now? April Fool! New Yorker, Aug. 14, 1937, at 22–26, is available at https://www.sidis.net/newyorker3.htm. On *Sidis* generally, see Emile Karafiol, The Right to Privacy and

the *Sidis* Case, 12 Ga. L. Rev. 513 (1978). Evidently Sidis did secure a settlement from the *New Yorker* in 1944, the year he died at age 46 of a cerebral hemorrhage. His IQ had been estimated "easily" at between 250 and 300 and, as an adult, he could master a new language in a day. Earlier decisions were more receptive to allowing claims about truthful revelations of past actions. Melvin v. Reid, 297 P. 91, 91 (Cal. App. 1931), allowed a lawsuit by a former prostitute who had been tried for murder and acquitted against defendants who had published a film about her past that had ruined her marriage and exposed her to "obloquy, contempt, and ridicule, causing her grievous mental and physical suffering." A similar solicitude for privacy was shown in Briscoe v. Reader's Digest Association, Inc., 483 P.2d 34, 40 (Cal. 1971), when a rehabilitated criminal was allowed to sue for the publication of a similar story in *Reader's Digest*, on the ground that while the facts of the incident fell within the public domain, the identification of the actor did not. Peters, J., distinguished *Sidis* by noting that the plaintiff had no relevant past public name recognition. But *Briscoe* fell to the general newsworthiness privilege when it was overruled in Gates v. Discovery Communications, Inc., 101 P.3d 552 (Cal. 2004), as inconsistent with subsequent Supreme Court precedent, discussed *infra* Note 2.

**2.** ***The Painful Present.*** As might be expected, the newsworthiness privilege outlined in *Sidis* has undisputed clout in dealing with painful publication of present facts. In Sipple v. Chronicle Publishing Co., 201 Cal. Rptr. 665, 670 (Ct. App. 1984), the plaintiff "grabbed or struck" the arm of Sarah Jane Moore as she attempted to shoot President Gerald Ford in September 1975, possibly saving the President's life. Sipple received widespread publicity, including a column in the *San Francisco Chronicle* by Herb Caen disclosing that Sipple was gay—which was the first time that members of Sipple's immediate family learned that he was gay. As a result, his family abandoned him. Sipple suffered mental anguish, embarrassment, and humiliation. Caldecott, P.J., affirmed the trial court's grant of summary judgment to the defendant under the newsworthiness privilege, noting that so long as the information was widely known, its public release was justified because the

> record shows that the publications were not motivated by a morbid and sensational prying into [Sipple's] private life, but rather were prompted by legitimate political considerations, i.e., to dispel the false public opinion that gays were timid, weak and unheroic figures and to raise the equally important political question whether the President of the United States entertained a discriminatory attitude or bias against a minority group such as homosexuals.

In *Melvin*, *Briscoe*, and *Sipple*, should it make a difference if the plaintiffs had lied to their families?

*Sipple* relied on Virgil v. Time, Inc., 527 F.2d 1122, 1128–29 (9th Cir. 1975). *Virgil* stated:

> The privilege to publicize newsworthy matters is included in the definition of the tort set out in Restatement (Second) of Torts §652D. Liability may be imposed for an invasion of privacy only if "the matter publicized is of a kind which . . . is not of legitimate concern to the public." While the Restatement does not so emphasize, we are satisfied that this provision is one of constitutional dimension delimiting the scope of the tort and that the extent of the privilege thus is controlled by federal rather than state law.

***3. Public Disclosure in the Internet Age.*** A particularly vexing issue confronting courts is that of public disclosure torts arising from "revenge porn," or nonconsensual pornography shared on the Internet. In Patel v. Hussain, 485 S.W.3d 153, 182 (Tex. App. 2016), Patel, a jilted lover, uploaded to the Internet secretly recorded sexual videos of his former girlfriend Nadia, threatening her in text messages to "accept that this is never going to go away" and that she would "never live this down." As is typical in "revenge porn," Patel exploited the nature of Internet postings, which exist forever and circulate indefinitely: "The Internet is huge you will

never find out where it's posted," and, "Can't stop SOCIAL MEDIA!!" McCally, J., affirmed the jury's award of $500,000 in noneconomic damages for intrusion upon seclusion and public disclosure of private facts. She noted, moreover, that "the nature of the invasions of privacy here are particularly disturbing and shocking and should give rise to an inference of mental anguish resulting from the threats to Nadia's reputation."

Forty-six states, the District of Columbia, and one territory have recently enacted legislation making revenge porn a criminal or civil offense. Should plaintiffs also have a common law remedy against defendants who post explicit photos or videos without their consent?

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## *Haynes v. Alfred A. Knopf, Inc.*

8 F.3d 1222 (7th Cir. 1993)

Posner, C.J. Luther Haynes and his wife, Dorothy Haynes nee Johnson, appeal from the dismissal on the defendants' motion for summary judgment of their suit against Nicholas Lemann, the author of a highly praised, best-selling book of social and political history called *The Promised Land: The Great Black Migration and How It Changed America* (1991), and Alfred A. Knopf, Inc., the book's publisher. The plaintiffs claim that the book libels Luther Haynes and invades both plaintiffs' right of privacy. Federal jurisdiction is based on diversity, and the common law of Illinois is agreed to govern the substantive issues. The appeal presents difficult issues at the intersection of tort law and freedom of the press.

**Jacob Lawrence, "The Migration Series," Panel 1 ("During the World War there was a great migration North by Southern Negroes.")**

*Source: Jacob Lawrence,* The Migration Series*, Panel 1/The Jacob and Gwendolyn Knight Lawrence Foundation, Seattle/Artists Rights Society (ARS), New York*

Between 1940 and 1970, five million blacks moved from impoverished rural areas and, after sojourns of shorter or greater length in the poor black districts of the cities, moved to middle-class areas. Others, despite the ballyhooed efforts of the federal government, particularly between 1964 and 1972, to erase poverty and racial discrimination, remained mired in what has come to be called the "urban ghetto." *The Promised Land* is a history of the migration. It is not history as a professional historian, a demographer, or a social scientist would write it. Lemann is none of these. He is a journalist and has written a journalistic history, in which the focus is on individuals whether powerful or representative. In the former group are the politicians who invented, executed, or exploited the "Great Society" programs. In the latter are a handful of the actual migrants. Foremost among these is Ruby Lee Daniels. Her story is the spine of the book. We are introduced to her on page 7; we take leave of her on page 346, within a few pages of the end of the text of the book.

[Posner, C.J., details the history of Daniels's life, starting from her early days in the 1940s as a sharecropper in Mississippi, through her migration to Chicago, where she met and married Luther Haynes. The story describes his descent into drunkenness, adultery, bad temper, and financial irresponsibility throughout his marriage to Daniels. That marriage ended

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in divorce and thereafter Luther married another woman, Dorothy, with whom he lived a respectable life for 20 years. He now has a home, a steady job as a parking-lot attendant, and a position as deacon in his church.

Posner, C.J., first affirmed the dismissal of the defamation portions of the complaint on the ground that any deviations from the truth were too insubstantial to support an action for libel. He then addressed the privacy claims as follows.]

The branch of privacy law that the Hayneses invoke in their appeal is not concerned with, and is not a proper surrogate for legal doctrines that are concerned with, the accuracy of the private facts revealed. It is concerned with the propriety of stripping away the veil of privacy with which we cover the embarrassing, the shameful, the tabooed, truths about us. The revelations in the book are not about the intimate details of the Hayneses' life. They are about misconduct, in particular Luther's. (There is very little about Dorothy in the book, apart from the fact that she had had an affair with Luther while he was still married to Ruby and that they eventually became and have remained lawfully married.) The revelations are about his heavy drinking, his unstable employment, his adultery, his irresponsible and neglectful behavior toward his wife and children. So we must consider cases in which the right of privacy has been invoked as a shield against the revelation of previous misconduct.

[He then reviews *Melvin* and *Sidis* and notes that, like the protagonists in the earlier cases,] Luther Haynes did not aspire to be a representative figure in the great black migration from the South to the North. People who do not desire the limelight and do not deliberately choose a way of life or course of conduct calculated to thrust them into it nevertheless have no legal right to extinguish it if the experiences that have befallen them are newsworthy, even if they would prefer that those experiences be kept private. The possibility of an involuntary loss of privacy is recognized in the modern formulations of this branch of the privacy tort, which require not only that the private facts publicized be such as would make a reasonable person deeply offended by such publicity but also that they be facts in which the public has no legitimate interest.

The two criteria, offensiveness and newsworthiness, are related. An individual, and more pertinently perhaps the community, is most offended by the publication of intimate personal facts when the community has no interest in them beyond the voyeuristic thrill of penetrating the wall of privacy that surrounds a stranger. The reader of a book about the black migration to the North would have no legitimate interest in the details of Luther Haynes's sex life; but no such details are disclosed. Such a reader does have a legitimate interest in the aspects of Luther's conduct that the book reveals. For one of Lemann's major themes is the transposition virtually intact of a sharecropper morality characterized by a family structure "matriarchal and elastic" and by an "extremely unstable" marriage bond to the slums of the northern cities, and the interaction, largely random and sometimes perverse, of that morality with governmental programs to alleviate poverty. Public aid policies discouraged Ruby and Luther from living together; public housing policies precipitated a marriage doomed to fail. No detail in the book claimed to invade the Hayneses' privacy is not germane to the story that the author wanted to tell, a story not only of legitimate but of transcendent public interest.

The Hayneses question whether the linkage between the author's theme and their private life really is organic. They point out that many social histories do not mention individuals at all, let alone by name. That is true. Much of social science, including social history, proceeds by abstraction, aggregation, and quantification rather than by case studies; the economist Robert Fogel has won a Nobel prize for his statistical studies of economic history, including, not wholly unrelated to the subject of Lemann's book, the history of Negro slavery in the United States. But it would be absurd to suggest that cliometric or other aggregative, impersonal methods of doing social history are the only proper way to go about it and presumptuous to claim even that they are the best way. Lemann's book has been praised to the skies by

distinguished scholars, among them black scholars covering a large portion of the ideological spectrum — Henry Louis Gates Jr., William Julius Wilson, and Patricia Williams. Lemann's methodology places the individual case history at center stage. If he cannot tell the story of Ruby Daniels without waivers from every person who she thinks did her wrong, he cannot write this book.

Well, argue the Hayneses, at least Lemann could have changed their names. But the use of pseudonyms would not have gotten Lemann and Knopf off the legal hook. The details of the Hayneses' lives recounted in the book would identify them unmistakably to anyone who has known the Hayneses well for a long time (members of their families, for example), or who knew them before they got married; and no more is required for liability either in defamation law or in privacy law. Lemann would have had to change some, perhaps many, of the details. But then he would no longer have been writing history. He would have been writing fiction. The nonquantitative study of living persons would be abolished as a category of scholarship, to be replaced by the sociological novel. That is a genre with a distinguished history punctuated by famous names, such as Dickens, Zola, Stowe, Dreiser, Sinclair, Steinbeck, and Wolfe, but we do not think that the law of privacy makes it (or that the First Amendment would permit the law of privacy to make it) the exclusive format for a social history of living persons that tells their story rather than treating them as data points in a statistical study. . . .

*The Promised Land* does not afford the reader a titillating glimpse of tabooed activities. The tone is decorous and restrained. Painful though it is for the Hayneses to see a past they would rather forget brought into the public view, the public needs the information conveyed by the book, including the information about Luther and Dorothy Haynes, in order to evaluate the profound social and political questions that the book raises. Given the *Cox* decision, moreover, all the discreditable facts about the Hayneses that are contained in judicial records are beyond the power of tort law to conceal; and the disclosure of those facts alone would strip away the Hayneses' privacy as effectively as *The Promised Land* has done. (This case, it could be argued, has stripped them of their privacy, since their story is now part of a judicial record — the record of this case.) We do not think it is an answer that Lemann got his facts from Ruby Daniels rather than from judicial records. The courts got the facts from Ruby. We cannot see what difference it makes that Lemann went to the source.

[Summary judgment was proper under *Cox* because "on the basis of the evidence obtained in pretrial discovery no reasonable jury could render a verdict for the plaintiff. . . ."]

Affirmed.

## NOTES

**1. *The Prosaic Sources of Newsworthiness.*** Unlike *Sidis*, the history recounted in *Haynes* involves ordinary people whom the author chose to highlight, not those who are thrust into the public eye by their greatness or misfortunes. The newsworthiness privilege attaches to both kinds of involuntary public figures.

Similarly, in Chanko v. ABC, Inc., 2014 N.Y. Slip Op. 30116 at *2, *4 (Sup. Ct. N.Y. Co. Jan. 15, 2014), Chanko, a patient at New York Presbyterian Hospital, was involuntarily thrust into the spotlight when, as he was being transported into the emergency room, his voice was recorded by the staff of a television series, *NY Med*. More than a year after Chanko's death, his widow recognized her husband's voice and the doctors treating him while watching a recorded episode of the show. Having never consented to the taping of her husband's emergency room treatment, she sued ABC and two of the physicians. Mendez, J., dismissed the cause of action for common law invasion of privacy on the ground that "Mr. Chanko's

wife and family are not seen [in the segment], nor are they heard. . . ." In the wake of *Chanko*, "[t]he association that represents nearly all major New York city hospitals," the Greater New York Hospital Association, "has asked its members not to allow patients to be filmed for entertainment purposes without their consent," and "[b]ills are also moving through the New York State Legislature that would prohibit the broadcast of medical treatment without prior written consent." Benjamin Mueller, New York Hospitals Group Requests Ban on TV Filming, N.Y. Times, Aug. 13, 2015.

In Veilleux v. National Broadcasting Co., 206 F.3d 92 (1st Cir. 2000), *Dateline NBC* ran an hour-long show about the long-distance trucking industry that focused on the dangers of fatigue in driving and featured the plaintiffs Veilleux and Kennedy. *Dateline NBC* revealed on its show that Kennedy failed a drug test. Campbell, J., rebuffed the plaintiffs' claim for invasion of privacy noting that "Kennedy's drug test results reasonably tend to illustrate the report's newsworthy themes of interstate truck driving, highway safety and relevant government regulation." Citing *Haynes*, he concluded that "we follow other circuit courts that have permitted journalists to portray individuals' personal circumstances in ways that reveal their identities were sufficiently related to a matter of public concern." Has the newsworthiness privilege swallowed the tort, as Kalven claimed? Is all news now, by definition, fit to print (or air, or live stream)?

**2. *Limits to Newsworthiness?*** Information is *not* considered to be of legitimate public concern "when the publicity ceases to be the giving of information to which the public is entitled, and becomes a morbid and sensational prying into private lives for its own sake, with which a reasonable member of the public, with decent standards, would say that he had no concern." RST §652D, cmt. *h*. Drawing the protective line at "morbid and sensational prying" has proved to be difficult for courts.

In Jackson v. Mayweather, 217 Cal. Rprt. 3d 234 (Cal. Ct. App. 2017), the notorious boxer Floyd Mayweather was sued by his ex-fiancée Shantel Jackson for private disclosure of public facts for his social media postings about the termination of Jackson's pregnancy and its relationship to the couple's separation. Mayweather argued that Jackson "had surrendered her right to privacy when she made herself newsworthy by virtue of her relationship with Mayweather" and thus "the reason for the relationship's demise was equally newsworthy." Perluss, P.J., held that Mayweather's posts were covered by the broad newsworthiness privilege, reasoning that

> at a time when entertainment news and celebrity gossip often seem to matter more than serious policy discussions, given Jackson's high profile and voluntary disclosure on social media of many aspects of her personal life, the publication of those otherwise intimate facts must necessarily be considered newsworthy under the broad definition of that term.

He nonetheless drew the line at Mayweather's publication of sonogram photographs of the twins Jackson had been carrying before her pregnancy terminated, finding that these—unlike the social media posts—fell outside the newsworthiness protection, given that "publishing those images served no legitimate public purpose, even when one includes entertainment news within the zone of protection."

The particular sensitivity regarding photographic images was similarly at issue in Judge v. Saltz Plastic Surgery, P.C., 367 P.3d 1006, 1013 (Utah 2016), where Himonas, J., was called on to determine whether there was a legitimate public interest in nude pre- and post-operative photographs of a woman who underwent plastic surgery based on her participation in a news broadcast on the risks and benefits of plastic surgery or whether the inclusion of those photographs received from the doctor's office was "gratuitous or overly intrusive." He rejected summary judgment for the defendant, holding that "reasonable minds could differ on whether appearing on television to discuss cosmetic surgery gives rise to a legitimate public interest in viewing explicit photographic documentation of the results of the interviewee's surgery."

## *Shulman v. Group W Productions, Inc.*

955 P.2d 469 (Cal. 1998)

Werdegar, J. . . . [Facts recounted in main case excerpt, *supra* at 437. In summary, the plaintiffs were injured in a car accident and received emergency assistance from a medical transport and rescue helicopter. A cameraman for a television show filmed the plaintiffs as they were extricated from their car and transported to the hospital and recorded the plaintiffs' conversations with the rescue workers on the helicopter. The video and audio tracks were later broadcast in a segment on the documentary television show *On Scene: Emergency Response*. The plaintiffs sued the show's producers for invasion of privacy on two counts: (1) for unlawful intrusion by videotaping the rescue, and (2) for the public disclosure of private facts in the broadcast. The trial court, finding that the accident and rescue were matters of public interest and public affairs, granted the defendants' motion for summary judgment on the first cause of action.]

### I. Publication of Private Facts

. . . The element critical to this case is the presence or absence of legitimate public interest, i.e., newsworthiness, in the facts disclosed. After reviewing the decisional law regarding newsworthiness, we conclude, inter alia, that lack of newsworthiness is an element of the "private facts" tort, conclude that the analysis of newsworthiness inevitably involves accommodating conflicting interests in personal privacy and in press freedom as guaranteed by the First Amendment to the United States Constitution, and that in the circumstances of this case—where the facts disclosed about a private person involuntarily caught up in events of public interest bear a logical relationship to the newsworthy subject of the broadcast and are not intrusive in great disproportion to their relevance—the broadcast was of legitimate public concern, barring liability under the private facts tort. . . .

. . . Delineating the exact contours of the constitutional privilege of the press in publication of private facts is, however, particularly problematic, because this privilege has not received extensive attention from the United States Supreme Court. [The court discussed Cox Broadcasting Corp. v. Cohn, *infra* at 451, and The Florida Star v. B.J.F. (1989), *infra* at 454.]

. . . Newsworthiness—constitutional or common law—is . . . difficult to define because it may be used as either a descriptive or a normative term. "Is the term 'newsworthy' a descriptive predicate, intended to refer to the fact there is widespread public interest? Or is it a value predicate, intended to indicate that the publication is a meritorious contribution and that the public's interest is praiseworthy?" . . .

. . . An analysis measuring newsworthiness of facts about an otherwise private person involuntarily involved in an event of public interest by their relevance to a newsworthy subject matter incorporates considerable deference to reporters and editors, avoiding the likelihood of unconstitutional interference with the freedom of the press to report truthfully on matters of legitimate public interest. In general, it is not for a court or jury to say how a particular story is best covered. The constitutional privilege to publish truthful material "ceases to operate only when an editor abuses his broad discretion to publish matters that are of legitimate public interest." . . . Finally, an analysis focusing on relevance allows courts and juries to decide most cases involving persons involuntarily involved in events of public interest without "balanc[ing] interests in ad hoc fashion in each case[.]" . . .

. . . On the other hand, no mode of analyzing newsworthiness can be applied mechanically or without consideration of its proper boundaries. To observe that the newsworthiness of private facts about a person involuntarily thrust into the public eye depends, in the ordinary case, on the existence of a logical nexus between the newsworthy event or activity and the

facts revealed is not to deny that the balance of free press and privacy interests may require a different conclusion when the intrusiveness of the revelation is greatly disproportionate to its relevance. Intensely personal or intimate revelations might not, in a given case, be considered newsworthy, especially where they bear only slight relevance to a topic of legitimate public concern. . . .

. . . We agree with defendants that the publication of truthful, lawfully obtained material of legitimate public concern is constitutionally privileged and does not create liability under the private facts tort. As discussed above, however, a certain amount of interest-balancing does occur in deciding whether material is of legitimate public concern, or in formulating rules for that decision. . . .

. . . We agree at the outset with defendants that the subject matter of the broadcast as a whole was of legitimate public concern. Automobile accidents are by their nature of interest to that great portion of the public that travels frequently by automobile. The rescue and medical treatment of accident victims is also of legitimate concern to much of the public, involving as it does a critical service that any member of the public may someday need. The story of Ruth's difficult extrication from the crushed car, the medical attention given her at the scene, and her evacuation by helicopter was of particular interest because it highlighted some of the challenges facing emergency workers dealing with serious accidents.

The more difficult question is whether Ruth's appearance and words as she was extricated from the overturned car, placed in the helicopter and transported to the hospital were of legitimate public concern. Pursuant to the analysis outlined earlier, we conclude the disputed material was newsworthy as a matter of law. One of the dramatic and interesting aspects of the story as a whole is its focus on flight nurse Carnahan, who appears to be in charge of communications with other emergency workers, the hospital base and Ruth, and who leads the medical assistance to Ruth at the scene. Her work is portrayed as demanding and important and as involving a measure of personal risk (e.g., in crawling under the car to aid Ruth despite warnings that gasoline may be dripping from the car). The broadcast segment makes apparent that this type of emergency care requires not only medical knowledge, concentration and courage, but an ability to talk and listen to severely traumatized patients. One of the challenges Carnahan faces in assisting Ruth is the confusion, pain and fear that Ruth understandably feels in the aftermath of the accident. For that reason the broadcast video depicting Ruth's injured physical state (which was not luridly shown) and audio showing her disorientation and despair were substantially relevant to the segment's newsworthy subject matter.

Plaintiffs argue that showing Ruth's "intimate private, medical facts and her suffering was not necessary to enable the public to understand the significance of the accident or the rescue as a public event." The standard, however, is not necessity. That the broadcast could have been edited to exclude some of Ruth's words and images and still excite a minimum degree of viewer interest is not determinative. Nor is the possibility that the members of this or another court, or a jury, might find a differently edited broadcast more to their taste or even more interesting. The courts do not, and constitutionally could not, sit as superior editors of the press.

## NOTES

**1.** ***The Relationship Between Disclosure and Intrusion Torts.*** In *Shulman*, the court determined that there were triable issues of fact as to whether the plaintiffs had an actionable intrusion claim (see *supra* at 437) but affirmed the dismissal of the disclosure claim based on the newsworthiness of the accident. Does it make sense for the court to rule that the personal

information used in the broadcast was gathered in a way that is impermissibly intrusive, but that the disclosure of that same information is privileged because of its newsworthiness? Should the plaintiff's reasonable expectation of privacy in the context of their intrusion upon seclusion claim inform the court's decision with regard to the claim for public disclosure of private facts?

**2. *Newsworthiness and the First Amendment.*** The *Shulman* court ruled that the broadcast in question was not actionable as information disclosure to prevent courts from acting as "superior editors of the press." However, in discussing the newsworthy aspects of the rescue mission, the court only highlighted aspects of the mission unrelated to the plaintiff's physical appearance, such as "measure of personal risk" involved in climbing under the car and the "ability to talk and listen" to injured patients. Because the footage of the plaintiff's physical condition is so attenuated to the newsworthy aspects of the broadcast, could the court have ruled that use of the footage constituted actionable disclosure without infringing on First Amendment rights? At what point are the private facts being disclosed so attenuated to the newsworthy aspects of the work that they can be found actionable as disclosure of private facts? Should courts consider the necessity of the inclusion of private facts in such cases?

## *Cox Broadcasting Corp. v. Cohn*

420 U.S. 469 (1975)

White, J. . . . The issue before us in this case is whether consistently with the First and Fourteenth Amendments a State may extend a cause of action for damages for invasion of privacy caused by the publication of the name of a deceased rape victim which was publicly revealed in connection with the prosecution of the crime.

In August 1971, appellee's 17-year-old daughter was the victim of a rape and did not survive the incident. Six youths were soon indicted for murder and rape. Although there was substantial press coverage of the crime and of subsequent developments, the identity of the victim was not disclosed pending trial, perhaps because of Ga. Code Ann. §26-9901, which makes it a misdemeanor to publish or broadcast the name or identity of a rape victim. In April 1972, some eight months later, the six defendants appeared in court. Five pled guilty to rape or attempted rape, the charge of murder having been dropped. The guilty pleas were accepted by the court, and the trial of the defendant pleading not guilty was set for a later date.

In the course of the proceedings that day, appellant Wassell, a reporter covering the incident for his employer, learned the name of the victim from an examination of the indictments which were made available for his inspection in the courtroom. That the name of the victim appears in the indictments and that the indictments were public records available for inspection are not disputed. Later that day, Wassell broadcast over the facilities of station WSB-TV, a television station owned by appellant Cox Broadcasting Corporation, a news report concerning the court proceedings. The report named the victim of the crime and was repeated the following day.

In May 1972, appellee brought an action for money damages against appellants, relying on §26-9901 and claiming that his right to privacy had been invaded by the television broadcasts giving the name of his deceased daughter. [Relying in part on *Briscoe*, the Georgia courts rejected Cox's claim of constitutional privilege and held that the plaintiff had stated a claim for invasion of privacy in the form of a tort of public disclosure of private facts, and left it to the jury whether the public disclosure of his daughter's name invaded his "zone of privacy."]

Georgia stoutly defends both §26-9901 and the State's common law privacy action challenged here. Its claims are not without force, for powerful arguments can be made, and have been made, that however it may be ultimately defined, there *is* a zone of privacy surrounding

every individual, a zone within which the State may protect him from intrusion by the press, with all its attendant publicity. [The Court then referred to Warren and Brandeis; Prosser; Time, Inc. v. Hill, *infra* at 457; and Pavesich v. New England Life Insurance Co., *supra* at 416.]

These are impressive credentials for a right of privacy, but we should recognize that we do not have at issue here an action for the invasion of privacy involving the appropriation of one's name or photograph, a physical or other tangible intrusion into a private area, or a publication of otherwise private information that is also false although perhaps not defamatory. The version of the privacy tort now before us — termed in Georgia "the tort of public disclosure," is that in which the plaintiff claims the right to be free from unwanted publicity about his private affairs, which, although wholly true, would be offensive to a person of ordinary sensibilities. Because the gravamen of the claimed injury is the publication of information, whether true or not, the dissemination of which is embarrassing or otherwise painful to an individual, it is here that claims of privacy most directly confront the constitutional freedoms of speech and press. The face-off is apparent, and the appellants urge upon us the broad holding that the press may not be made criminally or civilly liable for publishing information that is neither false nor misleading but absolutely accurate, however damaging it may be to reputation or individual sensibilities.

[The Court notes that public officials and public figures must show actual malice to succeed in a defamation action under New York Times v. Sullivan, but it left unresolved] the question whether truthful publication of very private matters unrelated to public affairs could be constitutionally proscribed.

Those precedents, as well as other considerations, counsel similar caution here. In this sphere of collision between claims of privacy and those of the free press, the interests on both sides are plainly rooted in the traditions and significant concerns of our society. Rather than address the broader question whether truthful publications may ever be subjected to civil or criminal liability consistently with the First and Fourteenth Amendments, or to put it another way, whether the State may ever define and protect an area of privacy free from unwanted publicity in the press, it is appropriate to focus on the narrower interface between press and privacy that this case presents, namely, whether the State may impose sanctions on the accurate publication of the name of a rape victim obtained from public records — more specifically, from judicial records which are maintained in connection with a public prosecution and which themselves are open to public inspection. We are convinced that the State may not do so.

In the first place, in a society in which each individual has but limited time and resources with which to observe at first hand the operations of his government, he relies necessarily upon the press to bring him in convenient form the facts of those operations. Great responsibility is accordingly placed upon the news media to report fully and accurately the proceedings of government, and official records and documents open to the public are the basic data of governmental operations. Without the information provided by the press most of us and many of our representatives would be unable to vote intelligently or to register opinions on the administration of government generally. With respect to judicial proceedings in particular, the function of the press serves to guarantee the fairness of trials and to bring to bear the beneficial effects of public scrutiny upon the administration of justice.

Appellee has claimed in this litigation that the efforts of the press have infringed his right to privacy by broadcasting to the world the fact that his daughter was a rape victim. The commission of crime, prosecutions resulting from it, and judicial proceedings arising from the prosecutions, however, are without question events of legitimate concern to the public and consequently fall within the responsibility of the press to report the operations of government.

The special protected nature of accurate reports of judicial proceedings has repeatedly been recognized. . . .

[The Restatement provides that there is no liability when the information in dispute is contained in public records.] Thus even the prevailing law of invasion of privacy generally recognizes that the interests in privacy fade when the information involved already appears on the public record. The conclusion is compelling when viewed in terms of the First and Fourteenth Amendments and in light of the public interest in a vigorous press. The Georgia cause of action for invasion of privacy through public disclosure of the name of a rape victim imposes sanctions on pure expression — the content of a publication — and not conduct or a combination of speech and nonspeech elements that might otherwise be open to regulation or prohibition. The publication of truthful information available on the public record contains none of the indicia of those limited categories of expression, such as "fighting" words, which "are no essential part of any exposition of ideas, and are of such slight social value as a step to truth that any benefit that may be derived from them is clearly outweighed by the social interest in order and morality." Chaplinsky v. New Hampshire, 315 U.S. 568, 572 (1942).

By placing the information in the public domain on official court records, the State must be presumed to have concluded that the public interest was thereby being served. Public records by their very nature are of interest to those concerned with the administration of government, and a public benefit is performed by the reporting of the true contents of the records by the media. The freedom of the press to publish that information appears to us to be of critical importance to our type of government in which the citizenry is the final judge of the proper conduct of public business. In preserving that form of government the First and Fourteenth Amendments command nothing less than that the States may not impose sanctions for the publication of truthful information contained in official court records open to public inspection.

We are reluctant to embark on a course that would make public records generally available to the media but forbid their publication if offensive to the sensibilities of the supposed reasonable man. Such a rule would make it very difficult for the press to inform their readers about the public business and yet stay within the law. The rule would invite timidity and self-censorship and very likely lead to the suppression of many items that would otherwise be put into print and that should be made available to the public. At the very least, the First and Fourteenth Amendments will not allow exposing the press to liability for truthfully publishing information released to the public in official court records. If there are privacy interests to be protected in judicial proceedings, the States must respond by means which avoid public documentation or other exposure of private information. Their political institutions must weigh the interests in privacy with the interests of the public to know and of the press to publish.[26] Once true information is disclosed in public court documents open to public inspection, the press cannot be sanctioned for publishing it. In this instance as in others reliance must rest upon the judgment of those who decide what to publish or broadcast.

Appellant Wassell based his televised report upon notes taken during the court proceedings and obtained the name of the victim from the indictments handed to him at his request during a recess in the hearing. Appellee has not contended that the name was obtained in an improper fashion or that it was not on an official court document open to public inspection. Under these circumstances, the protection of freedom of the press provided by the First and Fourteenth Amendments bars the State of Georgia from making appellants' broadcast the basis of civil liability. . . .

Reversed.

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26. We mean to imply nothing about any constitutional questions which might arise from a state policy not allowing access by the public and press to various kinds of official records, such as records of juvenile-court proceedings.

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[Justice Powell concurred separately to state his views solely on the meaning of Gertz v. Robert Welch, Inc., which, he believed, constitutionally required that truth be an absolute defense in defamation actions brought by either public or private persons. Justice Rehnquist dissented on the ground that there had been no final judgment in the case from which an appeal could be taken to the Supreme Court.]

## NOTES

**1. *Privacy and the Public Record.*** What kinds of official records are not public? Social Security numbers? In Ostergren v. Cuccinelli, 615 F.3d 263 (4th Cir. 2010), a privacy advocate published on her website land records containing unredacted Social Security numbers to encourage state reform. The court held that the First Amendment protected the publication. How should the Supreme Court decide the questions left unanswered in *Cox* footnote 26? Does *Cox* accord constitutional status to section 652D of the Second Restatement? What of the confidentiality of public records of adoption proceedings? In Doe v. Sundquist, 106 F.3d 702 (6th Cir. 1997), the court held that no constitutional right of privacy prevented Tennessee from passing a law that allowed adopted children access to previously confidential adoption records for the purpose of identifying their birth parents.

The Supreme Court has addressed the clash between the First Amendment and privacy interests in a number of cases since *Cox*. In Oklahoma Publishing Co. v. District Court, 430 U.S. 308, 311 (1977), the state court entered a pretrial order enjoining the publication of the name and picture of an eleven-year-old boy charged with delinquency by second-degree murder for shooting a railroad switchman. The Court held under *Cox* that the ban violated the First Amendment.

> No objection was made to the presence of the press in the courtroom or to the photographing of the juvenile as he left the courthouse. There is no evidence that petitioner acquired the information unlawfully or even without the State's implicit approval. The name and picture of the juvenile here were "publicly revealed in connection with the prosecution of the crime," much as the name of the rape victim in *Cox Broadcasting* was placed in the public domain.

Could reporters have been excluded from the court? See Globe Newspaper Co. v. Super. Ct., 457 U.S. 596 (1982).

In The Florida Star v. B.J.F., 491 U.S. 524, 533 (1989), the plaintiff had filed a report with the local sheriff's department stating that she had been robbed and raped. The *Florida Star* obtained this report lawfully. Thereafter it published a short account of the rape using the plaintiff's name in its "Police Reports" section, in inadvertent violation of its own internal policy that barred the use of any rape victim's name. In a jury trial, the plaintiff recovered $75,000 in compensatory damages and $25,000 in punitive damages for the violation of Fla. Stat. §794.03 (1987), rendering it unlawful to "print, publish, or broadcast . . . in any instrument of mass communication the name, address, or other identifying fact or information of the victim of any sexual offense. . . ."

The Supreme Court threw out the jury awards for both compensatory and punitive damages. The Court refused to adopt any categorical rule making it constitutionally protected to publish the name of a rape victim, only to deny recovery on a more limited ground: "[I]f a newspaper lawfully obtains truthful information about a matter of public significance then state officials may not constitutionally punish publication of the information, absent a need to further a state interest of the highest order." The proper treatment for unlawfully obtained information was again left unsettled.

Justice White's dissent stressed that as a result of publication, "B.J.F. received harassing phone calls, required mental health counseling, was forced to move from her home, and was even threatened with being raped again." He distinguished his earlier opinion in *Cox* by noting that there the state did not undertake any effort to keep the information confidential, whereas in this instance the state did seek to keep the information quiet.

Note that one informal survey suggests that, in practice, over 90 percent of the newspapers in the country do not publish the names of rape victims. See Alex S. Jones, Rape Victim Is Still a Murky Issue for the Press, N.Y. Times, June 25, 1989, §1, at 18. Does the general practice help the majority or the dissent?

**2.** ***Statutory Response to* Cox.** *Cox* provoked two modifications of the New York privacy statute. In 1979, the legislature adopted, and has since modified, N.Y. Civ. Rights Law §50-b (Consol. 2024), which states:

> The identity of any victim of a sex offense, . . . or of an offense involving the alleged transmission of the human immunodeficiency virus, shall be confidential. No report, paper, picture, photograph, court file or other documents, in the custody or possession of any public officer or employee, which identifies such a victim shall be made available for public inspection. No such public officer or employee shall disclose any portion of any police report, court file, or other document, which tends to identify such a victim except as provided in subdivision two of this section.

Subdivision 2 in turn allows access to this information only by obtaining a court order that "good cause exists for disclosure to that person." Other interested parties may appear at the hearing. The statute indicates that any victim must give consent to any disclosure and makes it clear that the right does not operate for the benefit of the person charged with the sexual offense. A 1991 amendment to the statute, N.Y. Civ. Rights Law §50-c, creates a private right of action for damages suffered by "any person" injured by the disclosure. This section allows the court in its discretion to award reasonable attorney's fees to the prevailing plaintiff. The statute does not apply to disclosures made by private persons who have no access to public records.

## *Wolfe v. Schaefer*

619 F.3d 782 (7th Cir. 2010)

Posner, J. The plaintiff, Mervin Wolfe, is a lawyer who in 2008 ran for State's Attorney of Cumberland County, Illinois, and lost. He brought this suit in federal district court against his opponent, Barry Schaefer (the incumbent State's Attorney), and others, under 42 U.S.C. §1983. The suit charges that they violated the Fourth Amendment and the due process clause of the Fourteenth Amendment by publicly disclosing that Wolfe was under investigation by Illinois state agencies for possible violations of legal ethics, tax law, and unemployment insurance law. The judge dismissed the suit. The invocation of the Fourth Amendment is frivolous; of the due process clause, a little bit less so. . . .

. . . At argument his lawyer contended that state law is relevant to the com- plaint, but he seemed to equivocate between the view that any violation of state law is actionable under the due process clause of the Fourteenth Amendment, which is false, and the correct view, which is that state law can (within limits) create a property or liberty interest that is protected by the Constitution against a deprivation that involves a denial of due process [citations omitted]. . . .

. . . There is of course a common law tort of privacy, of a somewhat miscellaneous character: "it is generally recognized by a majority of jurisdictions that the [common law] right of

privacy may be invaded in four different ways: (1) unreasonable intrusion upon the seclusion of another; (2) appropriation of another's name or likeness; (3) unreasonable publicity given to another's private life; and (4) publicity that unreasonably places another in a false light before the public." [citations omitted] The interest protected by the third clause — informational privacy — is the one at issue in this case. . . . But as the plaintiff is not suing to enforce state common law rights, we must consider how much of that common law has become a part of federal constitutional law when the infringer is a state or federal entity and thus subject to the due process clause.

In *Whalen v. Roe*, 429 U.S. 589, 598–600, (1977), the Supreme Court had held that "liberty" includes "privacy." But except when dealing with searches and seizures, the Court in the decades since has confined the label "privacy" mainly to sexual and reproductive rights, such as the right to use contraceptives or have an abortion or engage in homosexual acts. . . . The Court has never held that the disclosure of private information denies due process. But in *Whalen* it did suggest that there might be a due process right to the non-disclosure of certain private information, 429 U.S. at 599–600, though it upheld the law challenged in that case: a law that required a copy of every prescription for certain drugs that have both lawful and unlawful uses (methadone, for example) to be filed with state health authorities. . . .

. . . The courts of appeals, including this court, have interpreted *Whalen* to recognize a constitutional right to the privacy of medical, sexual, financial, and perhaps other categories of highly personal information — information that most people are reluctant to disclose to strangers — and have held that the right is defeasible only upon proof of a strong public interest in access to or dissemination of the information.

. . . The Supreme Court, in contrast, has seemed more interested in limiting the right of informational privacy than in its recognition and enforcement. It has held that reputation is not part of the liberty that the due process clauses protect, Paul v. Davis, 424 U.S. 693, 711–13 (1976), even though concern with reputation is one of the principal reasons people don't want personal information about themselves broadcast to strangers. It has held that the First Amendment forbids a state to punish broadcasting the name of a murdered rape victim if her name is in judicial records open to public inspection. Cox Broadcasting Corp. v. Cohn, 420 U.S. 469, 494–96 (1975). . . . Even the publicizing of highly personal information that is not in a record open to public inspection is privileged if there is a public interest in access to the information. . . . Yet there is an air of paradox in giving constitutional protection in the name of privacy to conduct that stretches the ordinary understanding of the concept of privacy, yet denying it to intensely private information, which is at the concept's core.

. . . [But t]actically motivated concealment of embarrassing or discreditable personal information can — often it is intended to — hide things in which the public has a legitimate interest. That is illustrated by the present case, which involves a challenge to the disclosure of investigations of misconduct. . . . Conflicts between the interests in informational privacy and in public disclosure of information require accommodation. If Congress required airline passengers to fly nude in order to reduce the risk of a terrorist incident, one imagines that the law might well be held to infringe a constitutional right to privacy even though there is a substantial social interest in airline safety. This case is at the other end of the spectrum. Information that a public official or candidate for public office has been the subject of an investigation by an official body is likely to come out sooner or later and to have public value, often to the investigating agency itself. . . .

. . . Wolfe's suit was properly dismissed.

## NOTE

***The "Public Interest" and the Constitution.*** Is *Wolfe* really about the weighty public interest in uncovering wrongdoing, particularly when it concerns a candidate for office? If so, then why did the court bother analyzing the constitutional right to privacy cases? Does *Wolfe* suggest that the wide berth given to "public interest" stems from the relatively underdeveloped "core" privacy constitutional case law (as compared to, e.g., the more robust "right to privacy" articulated in *Whalen*, *Griswold*, *Roe*, and the like)? Is *Wolfe* an anti-*Sullivan*, insofar as the First Amendment seems to *broaden* a tort rather than narrow it?

## SECTION E. FALSE LIGHT

### RESTATEMENT OF THE LAW (SECOND) OF TORTS

**§652E. Publicity Placing Person in False Light**

One who gives publicity to a matter concerning another that places the other before the public in a false light is subject to liability to the other for invasion of his privacy, if

(a) the false light in which the other was placed would be highly offensive to a reasonable person, and

(b) the actor had knowledge of or acted in reckless disregard as to the falsity of the publicized matter and the false light in which the other would be placed.

***Caveat:*** The Institute takes no position on whether there are any circumstances under which recovery can be obtained under this Section if the actor did not know of or act with reckless disregard as to the falsity of the matter publicized and the false light in which the other would be placed but was negligent in regard to these matters.

***Comment b. Relation to Defamation:*** The interest protected by this Section is the interest of the individual in not being made to appear before the public in an objectionable false light or false position, or in other words, otherwise than as he is. In many cases to which the rule stated here applies, the publicity given to the plaintiff is defamatory, so that he would have an action for libel or slander under the rules stated in Chapter 24. In such a case the action for invasion of privacy will afford an alternative or additional remedy, and the plaintiff can proceed upon either theory, or both, although he can have but one recovery for a single instance of publicity. . . .

### *Time, Inc. v. Hill*

385 U.S. 374 (1967)

Brennan, J. . . . The question in this case is whether appellant, publisher of *Life* magazine, was denied constitutional protections of speech and press by the application by the New York courts of §§50-51 of the New York Civil Rights Law to award appellee damages on allegations that *Life* falsely reported that a new play portrayed an experience suffered by appellee and his family.

[In September 1952, James Hill, his wife, and five Hill children were held hostage for nineteen hours in their suburban Philadelphia home by three escaped convicts. The convicts released the Hill family untouched and unharmed, but the story made the front pages

of the newspapers when the police, in a widely publicized encounter, subsequently killed two of the convicts and captured the third. Shortly after the incident, the Hills moved to Connecticut.

In 1955 *Life* magazine, owned by defendant Time, Inc., published an article entitled "True Crime Inspires Tense Play" that told of a new Broadway thriller, *The Desperate Hours*. The article said that the experience of the Hill family, which had first been brought to attention in Joseph Hayes's novel *The Desperate Hours*, was now being "re-enacted" in a new play based on the original book. The article said the play showed that the family "rose to heroism" in its time of crisis. The article was accompanied by pictures of scenes from the play, reenacted in the Hills' suburban Philadelphia home. One showed a son being "roughed up" by a "brutish convict"; another, the "darling daughter" biting the hand of one of the convicts; and a third, of the father making a "brave try" to save his family.

Hill brought his action in the New York State Supreme Court under §§50 and 51 of the New York Civil Rights Law, alleging that the article was intended to, and in fact did, give the public the impression that the play was an accurate account of the experiences of the Hill family. Hill also alleged that the defendant knew that its article was "false and untrue." The defendant answered that the article was "a subject of legitimate news interest," that it was "a subject of general interest and of value and concern to the public" at the time it was published, and that it was "published in good faith without any malice whatsoever. . . ." The trial judge denied defendant's motion to dismiss and the jury awarded plaintiff $50,000 in actual and $25,000 in punitive damages.

The New York Court of Appeals affirmed on the ground that defendant's "fictionalized" account of plaintiff's personal life, used in this unauthorized biography, was not protected by the newsworthiness defense.]

We hold that the constitutional protections for speech and press preclude the application of the New York statute to redress false reports of matters of public interest in the absence of proof that the defendant published the report with knowledge of its falsity or in reckless disregard of the truth.

The guarantees for speech and press are not the preserve of political expression or comment upon public affairs, essential as those are to healthy government. One need only pick up any newspaper or magazine to comprehend the vast range of published matter which exposes persons to public view, both private citizens and public officials. Exposure of the self to others in varying degrees is a concomitant of life in a civilized community. The risk of this exposure is an essential incident of life in a society which places a primary value on freedom of speech and of press. . . . We create a grave risk of serious impairment of the indispensable service of a free press in a free society if we saddle the press with the impossible burden of verifying to a certainty the facts associated in news articles with a person's name, picture or portrait, particularly as related to nondefamatory matter. Even negligence would be a most elusive standard, especially when the content of the speech itself affords no warning of prospective harm to another through falsity. A negligence test would place on the press the intolerable burden of guessing how a jury might assess the reasonableness of steps taken by it to verify the accuracy of every reference to a name, picture or portrait.

In this context, sanctions against either innocent or negligent misstatement would present a grave hazard of discouraging the press from exercising the constitutional guarantees. Those guarantees are not for the benefit of the press so much as for the benefit of all of us. A broadly defined freedom of the press assures the maintenance of our political system and an open society. Fear of large verdicts in damage suits for innocent or merely negligent misstatement, even fear of the expense involved in their defense, must inevitably cause publishers to "steer . . . wider of the unlawful zone," and thus "create the danger that the legitimate utterance will be penalized."

But the constitutional guarantees can tolerate sanctions against *calculated* falsehood without significant impairment of their essential function. We held in *New York Times* that calculated falsehood enjoyed no immunity in the case of alleged defamation of a public official concerning his official conduct. Similarly, calculated falsehood should enjoy no immunity in the situation here presented us. . . .

Turning to the facts of the present case, the proofs reasonably would support either a jury finding of innocent or merely negligent misstatement by *Life*, or a finding that *Life* portrayed the play as re-enactment of the Hill family's experience reckless of the truth or with actual knowledge that the portrayal was false. [Justice Brennan then reviewed the evidence in great detail.]

The appellant argues that the statute should be declared unconstitutional on its face if construed by the New York courts to impose liability without proof of knowing or reckless falsity. Such a declaration would not be warranted even if it were entirely clear that this had previously been the view of the New York courts. The New York Court of Appeals . . . has been assiduous in construing the statute to avoid invasion of the constitutional protections of speech and press. We, therefore, confidently expect that the New York courts will apply the statute consistently with the constitutional command. Any possible difference with us as to the thrust of the constitutional command is narrowly limited in this case to the failure of the trial judge to instruct the jury that a verdict of liability could be predicated only on a finding of knowing or reckless falsity in the publication of the *Life* article.

The judgment of the Court of Appeals is set aside and the case is remanded for further proceedings not inconsistent with this opinion.

It is so ordered.

[Justice Black, with whom Justice Douglas joined, concurred, but reiterated his view in New York Times v. Sullivan that the First Amendment imposed a total bar on these suits.]

Douglas J., concurring. . . . The episode around which this book was written had been news of the day for some time. The most that can be said is that the novel, the play, and the magazine article revived that interest. A fictionalized treatment of the event is, in my view, as much in the public domain as would be a watercolor of the assassination of a public official. It seems to me irrelevant to talk of any right of privacy in this context. Here a private person is catapulted into the news by events over which he had no control. He and his activities are then in the public domain as fully as the matters at issue in New York Times Co. v. Sullivan. Such privacy as a person normally has ceases when his life has ceased to be private. . . .

[Harlan, J., concurring in part and dissenting in part, urged the adoption of a negligence standard, in part because of the inability of the Hills to use counterspeech to offset the errors found in the *Life* magazine account.]

Mr. Justice Fortas, with whom The Chief Justice and Mr. Justice Clark join, dissenting.

[The instructions given at the trial were] close enough to this Court's insistence upon "knowing or reckless falsity" as to render a reversal arbitrary and unjustified. If the defendant *altered* or *changed* the true facts so that the article as published was a *fictionalized* version, this, in my judgment, was a knowing or reckless falsity. "Alteration" or "change" denotes a positive act — not a negligent or inadvertent happening. "Fictionalization" and "fiction" to the ordinary mind mean so departing from fact and reality as to be *deliberately* divorced from the fact — not merely in detail but in general and pervasive impact.

## NOTES

**1. Time v. Hill *Today.*** Time v. Hill (where, in arguments before the Supreme Court, Hill was represented by Richard Nixon) was decided just before the Supreme Court held in *Butts*, *supra* Chapter 6, at 390, that the actual malice requirement applied to defamation suits brought by public figures against media defendants. Is there any reason to distinguish the false light from the defamation cases? The Court briefly reexamined Time v. Hill in Cantrell v. Forest City Publishing Co., 419 U.S. 245, 250–51 (1974), when it upheld a verdict for the plaintiff in a false-light case because the trial judge had properly instructed the jury that the plaintiff had the burden of showing that the defendant's story was written with knowledge of its falsity or with a reckless disregard of its truth. The plaintiff in *Cantrell* was a private person, but the Court chose not to reexamine Time v. Hill in light of Gertz v. Welch, *supra* Chapter 6, at 397, decided earlier in the same Term. Because the plaintiff had not objected to the jury instructions, the Court concluded that

> this case presents no occasion to consider whether a State may constitutionally apply a more relaxed standard of liability for a publisher or broadcaster of false statements injurious to a private individual under a false-light theory of invasion of privacy, or whether the constitutional standard announced in Time, Inc. v. Hill applies to all false-light cases.

**2. *"Publicity."*** Like the public disclosure tort, and unlike defamation, the false-light tort requires "publicity," as defined in RST §652D, comment *a*, *supra* at 440. "Publicity" is distinct from "publication" as used in defamation law; it does not suffice "to communicate a fact concerning the plaintiff's private life to a single person or even to a small group of persons," whereas "any publication in a newspaper or a magazine, even of small circulation, or in a handbill distributed to a large number of persons, or any broadcast over the radio, or statement made in an address to a large audience, is sufficient." Questions of fact may arise as to whether challenged statements were sufficiently publicized to support a false-light claim. For example, in Doe v. Hagar, 765 F.3d 855 (8th Cir. 2014), Sammy Hagar, the one-time lead singer of the band Van Halen, published his autobiography, entitled *Red: My Uncensored Life in Rock* (*Red*). In a passage in the book, he recounts a lurid story of a sexual rendezvous with "a former Playboy bunny from California" while on tour in Detroit and the aftermath when she claimed she was pregnant with Hagar's child and pursued him for child support. Hagar wrote: "I knew it was not my baby. It was extortion." More than 280,000 copies of Hagar's book sold worldwide. Plaintiff Jane Doe brought claims of libel per se and false-light invasion of privacy, contending that "Hagar's characterization of her as a schemer and criminal is false." According to Bright, J., "the widespread distribution of *Red* demonstrates that Hagar's statements are widely available within the community of individuals that could recognize Doe as the subject of the statements, including Hagar's associates, band members, and touring staff; those that Doe knew . . . while she was seeing Hagar; and Doe's friends and acquaintances." Bright, J., thus concluded that questions of fact remained with respect to the publicity element of the false-light claim and reversed the district court's grant of summary judgment in favor of Hagar.

**3. *False Light in State Courts.*** Nothing in *Time* requires any state to adopt the false light action in the first place, and many state courts have refused to recognize the tort. In Lake v. Wal-Mart Stores, Inc., 582 N.W.2d 231, 235–36 (Minn. 1998), the court accepted the privacy torts of intrusion on seclusion, commercial appropriation, and publication of private facts, but drew the line at false light: "False light is the most widely criticized of the four privacy torts and has been rejected by several jurisdictions." Other states remain committed to the distinction. In Godbehere v. Phoenix Newspapers, Inc., 783 P.2d 781, 786 (Ariz. 1989), the court held that the two torts redress different types of wrongful conduct, so that

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in some situations a jury could find the defendant's publication of false information or innuendo, although not outrageous, satisfies the elements of false light. In Welling v. Weinfeld, 866 N.E.2d 1051, 1057 (Ohio 2007), the court expressed the dominant view by holding that liability for a false light claim maintains the integrity of the right to privacy as a complement to the other right-to-privacy torts.

Compare Gary T. Schwartz, Explaining and Justifying a Limited Tort of False Light Invasion of Privacy, 41 Case W. Res. L. Rev. 885, 898 (1991), with Diane L. Zimmerman, False Light Invasion of Privacy: The Light That Failed, 64 N.Y.U. L. Rev. 364 (1989).

Should *Roberson, supra* at 415, be treated as a false-light case?

## *Cantrell v. Forest City Pub. Co.*

419 U.S. 245 (1974)

Stewart, J. Margaret Cantrell and four of her minor children brought this diversity action in a Federal District Court for invasion of privacy against the Forest City Publishing Co., publisher of a Cleveland newspaper, the Plain Dealer, and against Joseph Eszterhas, a reporter formerly employed by the Plain Dealer, and Richard Conway, a Plain Dealer photographer. The Cantrells alleged that an article published in the Plain Dealer Sunday Magazine unreasonably placed their family in a false light before the public through its many inaccuracies and untruths. The District Judge struck the claims relating to punitive damages as to all the plaintiffs and dismissed the actions of three of the Cantrell children in their entirety, but allowed the case to go to the jury as to Mrs. Cantrell and her oldest son, William. The jury returned a verdict against all three of the respondents for compensatory money damages in favor of these two plaintiffs. . . .

. . . In December 1967, Margaret Cantrell's husband Melvin was killed along with 43 other people when the Silver Bridge across the Ohio River at Point Pleasant, W. Va., collapsed. The respondent Eszterhas was assigned by the Plain Dealer to cover the story of the disaster. He wrote a "news feature" story focusing on the funeral of Melvin Cantrell and the impact of his death on the Cantrell family.

Five months later, after conferring with the Sunday Magazine editor of the Plain Dealer, Eszterhas and photographer Conway returned to the Point Pleasant area to write a follow-up feature. The two men went to the Cantrell residence, where Eszterhas talked with the children and Conway took 50 pictures. Mrs. Cantrell was not at home at any time during the 60 to 90 minutes that the men were at the Cantrell residence.

It is conceded that the story contained a number of inaccuracies and false statements. Most conspicuously, although Mrs. Cantrell was not present at any time during the reporter's visit to her home, Eszterhas wrote, "Margaret Cantrell will talk neither about what happened nor about how they are doing. She wears the same mask of non-expression she wore at the funeral. She is a proud woman. Her world has changed. She says that after it happened, the people in town offered to help them out with money and they refused to take it." Other significant misrepresentations were contained in details of Eszterhas' descriptions of the poverty in which the Cantrells were living and the dirty and dilapidated conditions of the Cantrell home.

The case went to the jury on a so-called "false light" theory of invasion of privacy. In essence, the theory of the case was that by publishing the false feature story about the Cantrells and thereby making them the objects of pity and ridicule, the respondents damaged Mrs. Cantrell and her son William by causing them to suffer outrage, mental distress, shame, and humiliation. . . .

At the close of the petitioners' case-in-chief, the District Judge struck the demand for punitive damages. He found that Mrs. Cantrell had failed to present any evidence to support the charges that the invasion of privacy "was done maliciously within the legal definition of that term." The Court of Appeals interpreted this finding to be a determination by the District Judge that there was no evidence of knowing falsity or reckless disregard of the truth introduced at the trial. Having made such a determination, the Court of Appeals held that the District Judge should have granted the motion for a directed verdict for respondents as to all the Cantrells' claims. 484 F.2d, at 155.

The Court of Appeals appears to have assumed that the District Judge's finding of no malice "within the legal definition of that term" was a finding based on the definition of "actual malice" established by this Court in New York Times Co. v. Sullivan, 376 U.S., at 280: "with knowledge that (a defamatory statement) was false or with reckless disregard of whether it was false or not." As so defined, of course, "actual malice" is a term of art, created to provide a convenient shorthand expression for the standard of liability that must be established before a State may constitutionally permit public officials to recover for libel in actions brought against publishers. As such, it is quite different from the common-law standard of "malice" generally required under state tort law to support an award of punitive damages. In a false-light case, common-law malice — frequently expressed in terms of either personal ill will toward the plaintiff or reckless or wanton disregard of the plaintiff's rights — would focus on the defendant's attitude toward the plaintiff's privacy, not toward the truth or falsity of the material published. See Time, Inc. v. Hill, 385 U.S., at 396 n.12. See generally W. Prosser, Law of Torts 9–10 (4th ed.).

Although the verbal record of the District Court proceedings is not entirely unambiguous, the conclusion is inescapable that the District Judge was referring to the common-law standard of malice rather than to the New York Times "actual malice" standard when he dismissed the punitive damages claims. For at the same time that he dismissed the demands for punitive damages, the District Judge refused to grant the respondents' motion for directed verdicts as to Mrs. Cantrell's and William's claims for compensatory damages. And, as his instructions to the jury made clear, the District Judge was fully aware that the Time, Inc. v. Hill meaning of the New York Times "actual malice" standard had to be satisfied for the Cantrells to recover actual damages. Thus, the only way to harmonize these two virtually simultaneous rulings by the District Judge is to conclude, contrary to the decision of the Court of Appeals, that in dismissing the punitive damages claims he was not determining that Mrs. Cantrell had failed to introduce any evidence of knowing falsity or reckless disregard of the truth. . . .

. . . For the foregoing reasons, the judgment of the Court of Appeals is reversed and the case is remanded to that court with directions to enter a judgment affirming the judgment of the District Court as to the respondents Forest City Publishing Co. and Joseph Eszterhas.

## NOTES

**1.** ***False Light and Defamation.*** In *Cantrell*, the plaintiffs were able to prevail on their false light claim based on the fact that defendants published an article knowingly containing falsehoods about the plaintiff. What result if the plaintiffs had sued for defamation as opposed to false light? Because the tort of false light requires proof of falsity, actual malice, and publicity (which exceeds the publication element of defamation), why would the plaintiffs sue under false light here? Would that decision be different if privileges such as fair reporting and newsworthiness were recognized as defenses to false light, as they are for defamation?

**2. *Criticisms of False Light.*** Due to the scope of the false light tort being seemingly coterminous with that of defamation, a number of jurisdictions have either not recognized the tort of false light or have explicitly refused to recognize such a cause of action. See, e.g., Jews for Jesus, Inc. v. Rapp, 997 So. 2d 1098 (Fla. 2008) (declining to recognize the tort of false light because "we simply cannot ignore the significant and substantial overlap between false light and defamation"); Brown v. Pearson, 483 S.E.2d 477, 484 (S.C. Ct. App. 1997) ("As to Appellants' claim of 'false light,' no South Carolina case has recognized this tort"). Another major criticism of false light stems from the fact that it permits recovery for largely the same conduct as defamation but without the procedural limitations that serve to protect defendants' constitutional rights. In Cain v. Hearst Corp., 878 S.W.2d 577, 584 (Tex. 1994), the Texas Supreme Court refused to recognize the tort of false light partly because the requirement that a statement be highly offensive to a reasonable person "fails to draw reasonably clear lines between lawful and unlawful conduct." As such, the *Cain* court acknowledged that "the uncertainty of not knowing what speech may subject the speaker or writer to liability would have an unacceptable chilling effect on free speech." Consider how this argument relates to Justice Douglas's dissent in the *Cantrell* case, where he expressed a desire to affirm the lower court's judgment reversing the damages awarded to the plaintiffs because "there must be freedom from damages lest the press be frightened into playing a more ignoble role than the Framers visualized." 419 U.S. at 255 (Douglas, J., dissenting). Is there a way to address these constitutional concerns surrounding false light while differentiating false light from defamation?

**3. *Support for False Light.*** John C.P. Goldberg & Benjamin C. Zipursky, A Tort for the Digital Age: False Light Invasion of Privacy Reconsidered, 73 DePaul L. Rev. 461, 474, 480–84 (2024), tries to justify the false light privacy tort by analogy to the tort of public disclosure, reasoning that "[i]f it wrongs someone to disseminate certain kinds of private information about them, then surely it wrongs them to purport to disclose the same information when it is actually *misinformation*." False light is thus the "pseudo-disclosure counterpart" to the tort of public disclosure of private facts and that, if we are to impose liability for disclosure then "[f]alsity should enhance the case for liability, not save the defendant from it." Does the relationship between the interests protected by the false light tort and other privacy torts warrant the existence of a separate tort of false light?

Goldberg and Zipursky also point out that the false light tort applies where courts are reluctant to characterize certain statements as defamatory, including the false attribution of disease or disability. Using that classification "carries the implication that a person should be deemed inferior or less deserving of respect or esteem" because of the false attribution. Is this justification still persuasive if a state legislature codifies false attribution of disease or disability and slander or libel per se? Why should courts recognize false light as a separate tort to handle this narrow set of cases when false light imposes a burden on plaintiffs to prove falsity and actual malice, where defamation only requires proof of actual malice?

## SECTION F. COMMERCIAL APPROPRIATION OF PLAINTIFF'S NAME OR LIKENESS, OR THE RIGHT OF PUBLICITY

### NEW YORK CIVIL RIGHTS LAW (2024)

**§50. Right of Privacy**

A person, firm or corporation that uses for advertising purposes, or for the purposes of trade, the name, portrait or picture of any living person without having first obtained

the written consent of such person, or if a minor of his or her parent or guardian, is guilty of a misdemeanor.

**§51. Action for Injunction and for Damages**

Any person whose name, portrait, picture, or voice is used within this state for advertising purposes or for the purposes of trade without the written consent first obtained as above provided may maintain an equitable action in the supreme court of this state against the person, firm or corporation so using his name, portrait, picture or voice, to prevent and restrain the use thereof; and may also sue and recover damages for any injuries sustained by reason of such use and if the defendant shall have knowingly used such person's name, portrait, picture or voice in such manner as is forbidden or declared to be unlawful by section fifty of this article, the jury, in its discretion, may award exemplary damages. . . .

**RESTATEMENT OF THE LAW (SECOND) OF TORTS**

**§652c. Appropriation of Name or Likeness**

One who appropriates to his own benefit the name or likeness of another is subject to liability to the other for invasion of his privacy.

***Comment b. How Invaded:*** The common form of invasion of privacy under the rule here stated is the appropriation and use of the plaintiff's name or likeness to advertise the defendant's business or product, or for some similar commercial purpose. Apart from statute, however, the rule stated is not limited to commercial appropriation. It applies also when the defendant makes use of the plaintiff's name or likeness for his own purposes and benefit, even though the use is not a commercial one, and even though the benefit sought to be obtained is not a pecuniary one. Statutes in some states have, however, limited the liability to commercial uses of the name or likeness.

**RESTATEMENT OF THE LAW (THIRD) OF UNFAIR COMPETITION**

**§46. Appropriation of the Commercial Value of Person's Identity: The Right of Publicity**

One who appropriates the commercial value of a person's identity by using without consent the person's name, likeness, or other indicia of identity for purposes of trade is subject to liability for the relief appropriate under the rules stated §§48 and 49 [governing injunctions and monetary relief, respectively].

## *Zacchini v. Scripps-Howard Broadcasting Co.*

433 U.S. 562 (1977)

White, J. Petitioner, Hugo Zacchini, is an entertainer. He performs a "human cannonball" act in which he is shot from a cannon into a net some 200 feet away. Each performance occupies some 15 seconds. In August and September 1972, petitioner was engaged to perform his act on a regular basis at the Geauga County Fair in Burton, Ohio. He performed in a fenced

area, surrounded by grandstands, at the fair grounds. Members of the public attending the fair were not charged a separate admission fee to observe his act.

On August 30, a freelance reporter for Scripps-Howard Broadcasting Co., the operator of a television broadcasting station and respondent in this case, attended the fair. He carried a small movie camera. Petitioner noticed the reporter and asked him not to film the performance. The reporter did not do so on that day; but on the instructions of the producer of respondent's daily newscast, he returned the following day and videotaped the entire act. This film clip approximately 15 seconds in length, was shown on the 11 o'clock news program that night, together with favorable commentary.

Petitioner then brought this action for damages, alleging that he is "engaged in the entertainment business," that the act he performs is one "invented by his father and . . . performed only by his family for the last fifty years," that respondent "showed and commercialized the film of his act without his consent," and that such conduct was an "unlawful appropriation of plaintiff's professional property." Respondent answered and moved for summary judgment, which was granted by the trial court.

The Court of Appeals of Ohio reversed. The majority held that petitioner's complaint stated a cause of action for conversion and for infringement of a common-law copyright, and one judge concurred in the judgment on the ground that the complaint stated a cause of action for appropriation of petitioner's "right of publicity" in the film of his act. All three judges agreed that the First Amendment did not privilege the press to show the entire performance on a news program without compensating petitioner for any financial injury he could prove at trial. . . .

. . . There is no doubt that petitioner's complaint was grounded in state law and that the right of publicity which petitioner was held to possess was a right arising under Ohio law. It is also clear that respondent's claim of constitutional privilege was sustained. . . .

. . . *Time, Inc. v. Hill*, which was hotly contested and decided by a divided Court, involved an entirely different tort from the "right of publicity" recognized by the Ohio Supreme Court. As the opinion reveals in *Time, Inc. v. Hill*, the Court was steeped in the literature of privacy law and was aware of the developing distinctions and nuances in this branch of the law. . . .

. . . The differences between these two torts are important. First, the State's interests in providing a cause of action in each instance are different. "The interest protected" in permitting recovery for placing the plaintiff in a false light "is clearly that of reputation, with the same overtones of mental distress as in defamation." [Citing Prosser, *supra* at 416]. By contrast, the State's interest in permitting a "right of publicity" is in protecting the proprietary interest of the individual in his act in part to encourage such entertainment. As we later note, the State's interest is closely analogous to the goals of patent and copyright law, focusing on the right of the individual to reap the reward of his endeavors and having little to do with protecting feelings or reputation. Second, the two torts differ in the degree to which they intrude on dissemination of information to the public. In "false light" cases the only way to protect the interests involved is to attempt to minimize publication of the damaging matter, while in "right of publicity" cases the only question is who gets to do the publishing. An entertainer such as petitioner usually has no objection to the widespread publication of his act as long as he gets the commercial benefit of such publication. Indeed, in the present case petitioner did not seek to enjoin the broadcast of his act; he simply sought compensation for the broadcast in the form of damages. . . .

. . . The broadcast of a film of petitioner's entire act poses a substantial threat to the economic value of that performance. As the Ohio court recognized, this act is the product of petitioner's own talents and energy, the end result of much time, effort, and expense. Much of its economic value lies in the "right of exclusive control over the publicity given to his performance"; if the public can see the act free on television, it will be less willing to pay to see it at the fair. . . .

. . . There is no doubt that entertainment, as well as news, enjoys First Amendment protection. It is also true that entertainment itself can be important news. Time, Inc. v. Hill. But it is important to note that neither the public nor respondent will be deprived of the benefit of petitioner's performance as long as his commercial stake in his act is appropriately recognized. Petitioner does not seek to enjoin the broadcast of his performance; he simply wants to be paid for it. Nor do we think that a state-law damages remedy against respondent would represent a species of liability without fault contrary to the letter or spirit of *Gertz v. Robert Welch, Inc.*, 418 U.S. 323 (1974). Respondent knew that petitioner objected to televising his act, but nevertheless displayed the entire film.

We conclude that although the State of Ohio may as a matter of its own law privilege the press in the circumstances of this case, the First and Fourteenth Amendments do not require it to do so.

Reversed.

## NOTES

**1. Zacchini *and the Reportage of Public Events.*** *Zacchini* was the first and only right of publicity case decided by the Supreme Court. Note that Zacchini could not have sued for copyright infringement for the broadcast, because he had not, as the federal copyright law requires, "fixed" his act in some tangible medium of expression, as by filming it himself. The copyright law, however, also contains a "fair use" exception, "for purposes such as criticism, comment, news reporting, teaching (including multiple copies for classroom use), scholarship, and research," which are not regarded as infringements of copyright. See Copyright Act, 17 U.S.C. §107 (2024). Should *Zacchini* have been decided on analogous "fair use" principles? If so, could the rebroadcast of the entire act be justified? For a discussion of the copyright analogies, see Douglas G. Baird, Note, Human Cannonballs and the First Amendment: *Zacchini v. Scripps-Howard Broadcasting Co.*, 30 Stan. L. Rev. 1185 (1978).

**2. *"Expressive" vs. "Commercial Uses."*** Right to publicity cases, both before and after *Zacchini*, focus on whether the use of a person's name and identity is "expressive"—in which case it is protected by the First Amendment—or "commercial"—in which case typically it is not. At the first pole, courts have uniformly held that the right of publicity does not prohibit newspapers, whether or not operated for profit, from using anyone's name or likeness in an ordinary news story. In Tropeano v. Atlantic Monthly Co., 400 N.E.2d 847, 851 (Mass. 1980), the defendant published a picture of the plaintiff in connection with its story "After the Sexual Revolution," without identifying her by name or discussing her. The court held that its publication did not amount to an appropriation of her likeness for advertisement and purposes of trade under Massachusetts law but was simply part of a "sociological commentary . . . The fact that the defendant is engaged in the business of publishing the Atlantic Monthly magazine for profit does not by itself transform the incidental publication of the plaintiff's picture into an appropriation for advertising or trade purposes." Indeed, if it did, all news stories would be fair game for the right of publicity.

Similarly, in Express One International, Inc. v. Steinbeck, 53 S.W.3d 895 (Tex. App. 2001), the court refused to apply the appropriation doctrine when the defendant posted critical comments about union supporters on Express One's Internet bulletin board. The defendant "Steinbeck intended to impugn Express One's reputation, rather than appropriate it," so that defamation was the proper remedy if any was available at all.

Closer to the line perhaps is Felsher v. University of Evansville, 755 N.E.2d 589 (Ind. 2001), where the court held that the tort of misappropriation did not protect corporate

entities because the various comments to the Restatement (such as the descendibility of the action at death) applied only to ordinary individuals. Thus in Doggett v. Travis Law Firm, P.C., 555 S.W.3d 127, 128 (Tex. App. 2018), the tort of invasion of privacy by misappropriation did not apply because a corporation has no right of privacy. Should matters change if the firm was organized as a partnership?

What about other kinds of groups? In Bi-Rite Enterprises, Inc. v. Button Master, 555 F. Supp. 1188, 1199 (S.D.N.Y. 1983), the court — exercising pendant jurisdiction over plaintiffs' right of publicity claim in what was ostensibly an unfair competition suit — explained that "the rationale for protecting [the publicity] interest extends to [musical] groups that have 'persona' sufficiently strong to meet the requirements applied to individuals." This rationale also prevailed in Hush Hush Sound, Inc. v. H&M Hennes, 2018 U.S. Dist. LEXIS 221973, where the plaintiff's DJ group, Classixx, defeated the defendant clothing chain's motion to dismiss. The court noted that "[g]roups of natural persons, including musical groups, do have a right of publicity," which they may transfer to third-party corporations like Hush Hush Sound. Is there any reason why commercial rights could not vest in corporations even if claims for invasion for seclusion do not?

Nor does the outcome change when historical events are fictionalized in public broadcasts. In Tyne v. Time Warner Entertainment Co., 901 So. 2d 802 (Fla. 2005), the plaintiffs were survivors among the crew members of the *Andrea Gail* who perished in the 1991 storm that formed the basis of Sebastian Junger's best-selling book, *The Perfect Storm*. The defendants in this case made and distributed a fictionalized version of the book, labeled as such, without asking for the permission of any of the survivors, or paying them for the use of the historical material. The survivors did not sue under a false light theory even though some of the scenes cast the decedents in a negative light, but they did sue for commercial misappropriation under Fla. Stat. §540.08 (2000). The Florida Supreme Court recognized that one of the defendants' purposes in this case was to make money, but rebuffed the claim holding that "the term 'commercial purpose' as used in section 540.08(1) does not apply to publications, including motion pictures, which do not directly promote a product or service." In its view, any broader application of the statute ran into serious difficulties under the First Amendment. Although not in these words, the broad newsworthiness privilege available in other branches of privacy law covers these misappropriation cases as well.

## *Finger v. Omni Publ'ns Int'l, Ltd.*

566 N.E.2d 141 (N.Y. 1990)

Alexander, J. Plaintiffs Joseph and Ida Finger commenced this action on behalf of themselves and their six children against defendant Omni Publications International, Ltd. seeking damages for the publication, without their consent, of a photograph of plaintiffs in conjunction with an article in Omni magazine discussing a research project relating to caffeine-aided fertilization. . . .

. . . The June 1988 issue of Omni magazine included in its "Continuum" segment an article entitled "Caffeine and Fast Sperm," in which it was indicated that based on research conducted at the University of Pennsylvania School of Medicine, in vitro fertilization rates may be enhanced by exposing sperm to high concentrations of caffeine.

A photograph of plaintiffs depicting two adults surrounded by six attractive and apparently healthy children accompanied the article. The caption beneath the photograph read "Want a big family? Maybe your sperm needs a cup of Java in the morning. Tests reveal that caffeine-spritzed sperm swim faster, which may increase the chances for in vitro fertilization." Neither the article nor the caption mentioned plaintiffs' names or indicated in any fashion

that the adult plaintiffs used caffeine or that the children were produced through in vitro fertilization.

Plaintiffs commenced this action alleging only violations of Civil Rights Law §§50 and 51. Defendant moved to dismiss the complaint, arguing that its use of the photograph in conjunction with the article did not violate Civil Rights Law §§50 and 51 because the picture was not used for trade or advertising but to illustrate a related news article on fertility. Defendant contended that because fertility is a topic of legitimate public interest, its use of the picture fit within the "newsworthiness exception" to the prohibitions of Civil Rights Law §50. . . .

. . . Plaintiffs contend that defendant violated Civil Rights Law §§50 and 51 by using their photograph without their consent "for advertising purposes or for the purposes of trade." . . .

. . . Although the statute does not define "purposes of trade" or "advertising," courts have consistently refused to construe these terms as encompassing publications concerning newsworthy events or matters of public interest. . . .

. . . Plaintiffs do not contest the existence of this "newsworthiness exception" and concede that the discussion of in vitro fertilization and the use of caffeine to enhance sperm velocity and motility are newsworthy topics. They contend, however, that their photograph bears "no real relationship" to the article, that none of plaintiffs' children were conceived by in vitro fertilization or any other artificial means, and that they never participated in the caffeine-enhanced reproductive research conducted at the University of Pennsylvania. . . .

. . . Plaintiffs misperceive the "newsworthy" theme of the article, which is fertility or increased fertility. Indeed, the article, in its opening sentences, observes that caffeine "can increase a man's fertility by boosting the performance of his sperm". . . .

As we have noted, the "newsworthiness exception" should be liberally applied. . . . [Q]uestions of "newsworthiness" are better left to reasonable editorial judgment and discretion; judicial intervention should occur only in those instances where there is "no real relationship" between a photograph and an article or where the article is an "advertisement in disguise." . . .

## *Carson v. Here's Johnny Portable Toilets, Inc.*

698 F.2d 831 (6th Cir. 1983)

Brown, J. . . .

Appellant, John W. Carson (Carson), is the host and star of "The Tonight Show," a well-known television program broadcast five nights a week by the National Broadcasting Company. Carson also appears as an entertainer in night clubs and theaters around the country. From the time he began hosting "The Tonight Show" in 1962, he has been introduced on the show each night with the phrase "Here's Johnny." . . .

. . . Appellee, Here's Johnny Portable Toilets, Inc., is a Michigan corporation engaged in the business of renting and selling "Here's Johnny" portable toilets. Appellee's founder was aware at the time he formed the corporation that "Here's Johnny" was the introductory slogan for Carson on "The Tonight Show." He indicated that he coupled the phrase with a second one, "The World's Foremost Commodian," to make "a good play on a phrase."

[Carson brought an action for, among other things, invasion of privacy and the right to publicity. He sought damages and an injunction prohibiting appellee's further use of the phrase "Here's Johnny" as a corporate name or in connection with the sale or rental of its portable toilets.] . . . After a bench trial, . . . the court ordered the dismissal of the appellants' complaint. . . . On the right of privacy and right of publicity theories, the court held that these rights extend only to a "name or likeness," and "Here's Johnny" did not qualify. . . .

. . . We do not believe that Carson's claim that his right of privacy has been invaded is supported by the law or the facts. Apparently, the gist of this claim is that Carson is embarrassed by and considers it odious to be associated with the appellee's product. Clearly, the association does not appeal to Carson's sense of humor. But the facts here presented do not, it appears to us, amount to an invasion of any of the interests protected by the right of privacy. In any event, our disposition of the claim of an invasion of the right of publicity makes it unnecessary for us to accept or reject the claim of an invasion of the right of privacy. . . .

. . . The right of publicity has developed to protect the commercial interest of celebrities in their identities. The theory of the right is that a celebrity's identity can be valuable in the promotion of products, and the celebrity has an interest that may be protected from the unauthorized commercial exploitation of that identity.

. . . We therefore conclude that, applying the correct legal standards, appellants are entitled to judgment. The proof showed without question that appellee had appropriated Carson's identity in connection with its corporate name and its product.

Although this opinion holds only that Carson's right of publicity was invaded because appellee intentionally appropriated his identity for commercial exploitation, the dissent, relying on its interpretation of the authorities and relying on policy and constitutional arguments, would hold that there was no invasion here. We do not believe that the dissent can withstand fair analysis. . . .

It should be obvious from the majority opinion and the dissent that a celebrity's identity may be appropriated in various ways. It is our view that, under the existing authorities, a celebrity's legal right of publicity is invaded whenever his identity is intentionally appropriated for commercial purposes. We simply disagree that the authorities limit the right of publicity as contended by the dissent. It is not fatal to appellant's claim that appellee did not use his "name." Indeed, there would have been no violation of his right of publicity even if appellee had used his name, such as "J. William Carson Portable Toilet" or the "John William Carson Portable Toilet" or the "J.W. Carson Portable Toilet." The reason is that, though literally using appellant's "name," the appellee would not have appropriated Carson's identity as a celebrity. Here there was an appropriation of Carson's identity without using his "name."

## NOTES

**1.** ***Pure Commercial Appropriation.*** Defendants receive no protection for acts of pure commercial appropriation. In Abdul-Jabbar v. General Motors Corp., 85 F.3d 407 (9th Cir. 1996), the court held that the publicity right protected Abdul-Jabbar's exclusive right to the use of his prior name, Lew Alcindor, under which he played while in college at UCLA. The court reasoned that the tort protected not only the plaintiff's name but also his identity. In White v. Samsung Electronics America, Inc., 971 F.2d 1395 (9th Cir. 1992), the plaintiff Vanna White, the popular hostess of the TV show *Wheel of Fortune*, sued Samsung when it used an image of a robot similar to White in an advertisement to promote its videocassette recorders. The ad depicted the robot, dressed in a wig, gown, and jewelry that Deutsch, Samsung's ad agency and codefendant, had consciously selected to resemble White's hair and dress. The robot was posed next to a game board that was instantly recognizable as the *Wheel of Fortune* game show set, in a stance for which White was famous. The caption of the ad read: "Longest-running game show. 2012 A.D." The court allowed the action even though the robot did not amount to an appropriation of her name or likeness under the California Civil Code, holding that the common law right of publicity "does not require that appropriations of identity be accomplished through particular means to be actionable." The court agreed with such

decisions as Midler v. Ford Motor Co., 849 F.2d 460 (9th Cir. 1988), in which a "sound-alike's" performance of a song that had made Bette Midler famous was found actionable. The decision in *White* provoked a sharp dissent from Kozinski, J.:

> Saddam Hussein wants to keep advertisers from using his picture in unflattering contexts. Clint Eastwood doesn't want tabloids to write about him. Rudolf Valentino's heirs want to control his film biography. The Girl Scouts don't want their image soiled by association with certain activities. George Lucas wants to keep Strategic Defense Initiative fans from calling it "Star Wars." Pepsico doesn't want singers to use the word "Pepsi" in their songs. Guy Lombardo wants an exclusive property right to ads that show big bands playing on New Year's Eve. Uri Geller thinks he should be paid for ads showing psychics bending metal through telekinesis. Paul Prudhomme, that household name, thinks the same about ads featuring corpulent bearded chefs. And scads of copyright holders see purple when their creations are made fun of.
>
> Something very dangerous is going on here. Private property, including intellectual property, is essential to our way of life. It provides an incentive for investment and innovation; it stimulates the flourishing of our culture; it protects the moral entitlements of people to the fruits of their labors. But reducing too much to private property can be bad medicine. Private land, for instance, is far more useful if separated from other private land by public streets, roads and highways. Public parks, utility rights-of-way and sewers reduce the amount of land in private hands, but vastly enhance the value of the property that remains.

In light of subsequent decisions like *In re NCAA*, excerpted below, is Kozinski, J., correct about the overexpansion of intellectual property rights in this area?

N.Y. Civ. Rights Law §§50, 51, *supra* at 455, further narrows the scope of the protectable interest in name or likeness. In Burck v. Mars, Inc., 571 F. Supp. 2d 446, 452 (S.D.N.Y. 2008), the court held that a candy manufacturer's creation and display of a cartoon character dressed in a street entertainer's signature costume, "the Naked Cowboy," did not amount to the use of the entertainer's "portrait or picture," as required to establish a violation of the New York law. The manufacturer used neither an actual photograph or picture nor a recognizable likeness or representation of the entertainer, but only evoked certain aspects of the fictional character he created.

Sections 50 and 51 of the New York law received further clarification in Lohan v. Take-Two Interactive Software, Inc., 97 N.E.3d 389, 391 (N.Y. 2018), which addressed the question "whether an avatar (that is, a graphical representation of a person, in a video game or like media) may constitute a 'portrait' within the meaning of Civil Rights Law §§50 and 51 and, if so, whether the images in question in the video game central to this matter are recognizable as plaintiff," in this instance the well-known actress Lindsay Lohan. Fahey, J., answered the first question in the affirmative and then held that the usual two-part test controlled whether the avatar was indeed a "portrait." First the court must determine whether "the person depicted is capable of being identified from the [avatar] alone," after which the jury must decide whether the attribution is in fact correct. Here, the plaintiff failed to pass the first part of the test as the avatar "merely [was] a generic artistic depiction of a 'twenty something' woman without any particular identifying physical characteristics." What result if the plaintiff introduced evidence showing that individuals in the target audience thought that the avatar was a knock-off of Lohan?

**2.** ***A Four-Headed Tort?*** Robert C. Post & Jennifer E. Rothman, The First Amendment and the Right(s) of Publicity, 130 Yale L.J. 86 (2020), identifies four variants of the publicity tort. The "right of performance" essentially restates *Zacchini*'s prohibition on unauthorized use of an entire act. The "right of commercial value" tracks the case law on celebrity likenesses, such as *Carson*. The "right of control" finds its roots in portraiture bans and proscribes the reproduction of one's likeness—such as through photographic imagery—without one's consent. *Finger* is most obviously on point. The "right of dignity" protects the integrity of

personality — an interest distinct from the "informational self-determination" furthered by the right to control. This dignitary right protects against the shame and embarrassment that results from having one's likeness displayed in unsavory settings. *Roberson*, *supra* at 415, is one early example. Does this framework accurately capture the interests, dignitary and otherwise, at the heart of the publicity tort? For example, can *Zacchini* be reduced to a purely commercial interest in a performance? What differentiates a "right of control" case from a "dignity" case? Surely the family in *Finger* had both an interest in "informational self-determination" and an interest in avoiding embarrassment by having their likeness featured in an article about reproductive health. Finally, does it make sense to carve out a "right of commercial value" — which applies to Johnny Carson and Vanna White, but not to ordinary individuals — when one leading criticism of the right of publicity tort is that it chiefly protects celebrities? See William M. Landes & Richard A. Posner, The Economic Structure of Intellectual Property Law, 222–28 (2003).

## *In re NCAA Student-Athlete Name & Likeness Licensing Litigation*

724 F.3d 1268 (9th Cir. 2013)

Bybee, J. Video games are entitled to the full protections of the First Amendment, because "[l]ike the protected books, plays, and movies that preceded them, video games communicate ideas — and even social messages — through many familiar literary devices (such as characters, dialogue, plot, and music) and through features distinctive to the medium (such as the player's interaction with the virtual world)." Such rights are not absolute, and states may recognize the right of publicity to a degree consistent with the First Amendment. Zacchini v. Scripps-Howard Broad. Co., 433 U.S. 562, 574–75 (1977). In this case, we must balance the right of publicity of a former college football player against the asserted First Amendment right of a video game developer to use his likeness in its expressive works.

The district court concluded that the game developer, Electronic Arts ("EA"), had no First Amendment defense against the right-of-publicity claims of the football player, Samuel Keller. We affirm. Under the "transformative use" test developed by the California Supreme Court, EA's use does not qualify for First Amendment protection as a matter of law because it literally recreates Keller in the very setting in which he has achieved renown. . . .

### I

Samuel Keller was the starting quarterback for Arizona State University in 2005 before he transferred to the University of Nebraska, where he played during the 2007 season. EA is the producer of the *NCAA Football* series of video games, which allow users to control avatars representing college football players as those avatars participate in simulated games. In *NCAA Football*, EA seeks to replicate each school's entire team as accurately as possible. Every real football player on each team included in the game has a corresponding avatar in the game with the player's actual jersey number and virtually identical height, weight, build, skin tone, hair color, and home state. EA attempts to match any unique, highly identifiable playing behaviors by sending detailed questionnaires to team equipment managers. Additionally, EA creates realistic virtual versions of actual stadiums; populates them with the virtual athletes, coaches, cheerleaders, and fans realistically rendered by EA's graphic artists; and incorporates realistic sounds such as the crunch of the players' pads and the roar of the crowd.

EA's game differs from reality in that EA omits the players' names on their jerseys and assigns each player a home town that is different from the actual player's home town. However, users of the video game may upload rosters of names obtained from third parties so that

the names do appear on the jerseys. In such cases, EA allows images from the game containing athletes' real names to be posted on its website by users. Users can further alter reality by entering "Dynasty" mode, where the user assumes a head coach's responsibilities for a college program for up to thirty seasons, including recruiting players from a randomly generated pool of high school athletes, or "Campus Legend" mode, where the user controls a virtual player from high school through college, making choices relating to practices, academics, and social life.

In the 2005 edition of the game, the virtual starting quarterback for Arizona State wears number 9, as did Keller, and has the same height, weight, skin tone, hair color, hair style, handedness, home state, play style (pocket passer), visor preference, facial features, and school year as Keller. In the 2008 edition, the virtual quarterback for Nebraska has these same characteristics, though the jersey number does not match, presumably because Keller changed his number right before the season started.

Objecting to this use of his likeness, Keller filed a putative class-action complaint in the Northern District of California asserting, as relevant on appeal, that EA violated his right of publicity. . . .

## II

. . .

### A

The California Supreme Court formulated the transformative use defense in Comedy III Productions, Inc. v. Gary Saderup, Inc., 21 P.3d 797 (Cal. 2001). The defense is "a balancing test between the First Amendment and the right of publicity based on whether the work in question adds significant creative elements so as to be transformed into something more than a mere celebrity likeness or imitation." The California Supreme Court explained that "when a work contains significant transformative elements, it is not only especially worthy of First Amendment protection, but it is also less likely to interfere with the economic interest protected by the right of publicity." . . .

*Comedy III* gives us at least five factors to consider in determining whether a work is sufficiently transformative to obtain First Amendment protection. First, if "the celebrity likeness is one of the 'raw materials' from which an original work is synthesized," it is more likely to be transformative than if "the depiction or imitation of the celebrity is the very sum and substance of the work in question." Second, the work is protected if it is "primarily the defendant's own expression"—as long as that expression is "something other than the likeness of the celebrity." This factor requires an examination of whether a likely purchaser's primary motivation is to buy a reproduction of the celebrity, or to buy the expressive work of that artist. Third, to avoid making judgments concerning "the quality of the artistic contribution," a court should conduct an inquiry "more quantitative than qualitative" and ask "whether the literal and imitative or the creative elements predominate in the work." Fourth, the California Supreme Court indicated that "a subsidiary inquiry" would be useful in close cases: whether "the marketability and economic value of the challenged work derive primarily from the fame of the celebrity depicted." Lastly, the court indicated that "when an artist's skill and talent is manifestly subordinated to the overall goal of creating a conventional portrait of a celebrity so as to commercially exploit his or her fame," the work is not transformative.

[A discussion of prior California Supreme Court cases, including *Comedy III* and Winter v. DC Comics, is omitted.]

[W]e conclude that EA's use of Keller's likeness does not contain significant transformative elements such that EA is entitled to the defense as a matter of law. . . . EA is alleged to have replicated Keller's physical characteristics in *NCAA Football*. . . . Here, . . . users

manipulate the characters in the performance of the same activity for which they are known in real life — playing football in this case. . . . The context in which the activity occurs is . . . realistic depictions of actual football stadiums in *NCAA Football*. As the district court found, Keller is represented as "what he was: the starting quarterback for Arizona State" and Nebraska, and "the game's setting is identical to where the public found [Keller] during his collegiate career: on the football field." . . .

Given that *NCAA Football* realistically portrays college football players in the context of college football games, the district court was correct in concluding that EA cannot prevail as a matter of law based on the transformative use defense. . . .

**B**

EA urges us to adopt for right-of-publicity claims the broader First Amendment defense that we have previously adopted in the context of false endorsement claims under the Lanham Act: the *Rogers* test.

Rogers v. Grimaldi[, 875 F.2d 994 (2d Cir. 1989),] is a landmark Second Circuit case balancing First Amendment rights against claims under the Lanham Act. The case involved a suit brought by the famous performer Ginger Rogers against the producers and distributors of *Ginger and Fred*, a movie about two fictional Italian cabaret performers who imitated Rogers and her frequent performing partner Fred Astaire. Rogers alleged both a violation of the Lanham Act for creating the false impression that she endorsed the film and infringement of her common law right of publicity.

The *Rogers* court recognized that "[m]ovies, plays, books, and songs are all indisputably works of artistic expression and deserve protection," but that "[t]he purchaser of a book, like the purchaser of a can of peas, has a right not to be misled as to the source of the product." "Consumers of artistic works thus have a dual interest: They have an interest in not being misled and they also have an interest in enjoying the results of the author's freedom of expression." The *Rogers* court determined that titles of artistic or literary works were less likely to be misleading than "the names of ordinary commercial products," and thus that Lanham Act protections applied with less rigor when considering titles of artistic or literary works than when considering ordinary products. The court concluded that "in general the Act should be construed to apply to artistic works only where the public interest in avoiding consumer confusion outweighs the public interest in free expression." The court therefore held:

> In the context of allegedly misleading titles using a celebrity's name, that balance will normally not support application of the [Lanham] Act unless the title has no artistic relevance to the underlying work whatsoever, or, if it has some artistic relevance, unless the title explicitly misleads as to the source or the content of the work. . . .

In this case, EA argues that we should extend this test, created to evaluate Lanham Act claims, to apply to right-of-publicity claims because it is "less prone to misinterpretation" and "more protective of free expression" than the transformative use defense. Although we acknowledge that there is some overlap between the transformative use test formulated by the California Supreme Court and the *Rogers* test, we disagree that the *Rogers* test should be imported wholesale for right-of-publicity claims. . . . As the history and development of the *Rogers* test makes clear, it was designed to protect consumers from the risk of consumer confusion — the hallmark element of a Lanham Act claim. The right of publicity, on the other hand, does not primarily seek to prevent consumer confusion. Rather, it primarily "protects a form of intellectual property [in one's person] that society deems to have some social utility." [*Comedy III*]. As the California Supreme Court has explained:

> Often considerable money, time and energy are needed to develop one's prominence in a particular field. Years of labor may be required before one's skill, reputation, notoriety or virtues

> are sufficiently developed to permit an economic return through some medium of commercial promotion. For some, the investment may eventually create considerable commercial value in one's identity.

The right of publicity protects the *celebrity*, not the *consumer*. Keller's publicity claim is not founded on an allegation that consumers are being illegally misled into believing that he is endorsing EA or its products. Indeed, he would be hard-pressed to support such an allegation absent evidence that EA explicitly misled consumers into holding such a belief. Instead, Keller's claim is that EA has appropriated, without permission and without providing compensation, his talent and years of hard work on the football field. The reasoning of *Rogers* and *Mattel* [Inc. v. MCA Records, Inc., 296 F.3d 894 (9th Cir. 2002) (following *Rogers*)]—that artistic and literary works should be protected unless they explicitly mislead consumers—is simply not responsive to Keller's asserted interests here.

We recognize that *Rogers* also dealt with a right-of-publicity claim—one under Oregon law—and applied a modified version of its Lanham Act test in order to adapt to that particular context:

> In light of the Oregon Court's concern for the protection of free expression, . . . the right of publicity [would not] bar the use of a celebrity's name in a movie title unless the title was "wholly unrelated" to the movie or was "simply a disguised commercial advertisement for the sale of goods or services."

However, the *Rogers* court was faced with a situation in which the "Oregon Courts . . . [had] not determined the scope of the common law right of publicity in that state." . . .

[W]e decline EA's invitation to extend the *Rogers* test to right-of-publicity claims. . . .

[Affirmed.]

Thomas, J., dissenting. . . . The majority confines its inquiry to how a single athlete's likeness is represented in the video game, rather than examining the transformative and creative elements in the video game as a whole. In my view, this approach contradicts the holistic analysis required by the transformative use test. The salient question is whether the entire work is transformative, and whether the transformative elements predominate, rather than whether an individual persona or image has been altered.

When EA's *NCAA Football* video game series is examined carefully, and put in proper context, I conclude that the creative and transformative elements of the games predominate over the commercial use of the likenesses of the athletes within the games.

### A

The first step in conducting a balancing is to examine the creative work at issue. At its essence, EA's *NCAA Football* is a work of interactive historical fiction. Although the game changes from year to year, its most popular features predominately involve role-playing by the gamer. For example, a player can create a virtual image of himself as a potential college football player. The virtual player decides which position he would like to play, then participates in a series of "tryouts" or competes in an entire high school season to gauge his skill. Based on his performance, the virtual player is ranked and available to play at select colleges. The player chooses among the colleges, then assumes the role of a college football player. He also selects a major, the amount of time he wishes to spend on social activities, and practice—all of which may affect the virtual player's performance. He then plays his position on the college team. In some versions of the game, in another mode, the virtual player can engage in a competition for the Heisman Trophy. In another popular mode, the gamer becomes a virtual coach. The coach scouts, recruits, and develops entirely fictional players for his team. The coach can then promote the team's evolution over decades of seasons.

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The college teams that are supplied in the game do replicate the actual college teams for that season, including virtual athletes who bear the statistical and physical dimensions of the actual college athletes. But, unlike their professional football counterparts in the *Madden NFL* series, the NCAA football players in these games are not identified.

The gamers can also change their abilities, appearances, and physical characteristics at will. Keller's impressive physical likeness can be morphed by the gamer into an overweight and slow virtual athlete, with anemic passing ability. And the gamer can create new virtual players out of whole cloth. Players can change teams. The gamer could pit Sam Keller against himself, or a stronger or weaker version of himself, on a different team. Or the gamer could play the game endlessly without ever encountering Keller's avatar. In the simulated games, the gamer controls not only the conduct of the game, but the weather, crowd noise, mascots, and other environmental factors. Of course, one may play the game leaving the players unaltered, pitting team against team. But, in this context as well, the work is one of historic fiction. The gamer controls the teams, players, and games.

Applying the *Comedy III* considerations to *NCAA Football* in proper holistic context, the considerations favor First Amendment protection. The athletic likenesses are but one of the raw materials from which the broader game is constructed. The work, considered as a whole, is primarily one of EA's own expression. The creative and transformative elements predominate over the commercial use of likenesses. The marketability and economic value of the game comes from the creative elements within, not from the pure commercial exploitation of a celebrity image. The game is not a conventional portrait of a celebrity, but a work consisting of many creative and transformative elements. . . .

**B**

Although one could leave the analysis with an examination of the transformative and creative aspects of the game, a true balancing requires an inquiry as to the other side of the scales: the publicity right at stake. Here, as well, the *NCAA Football* video game series can be distinguished from the traditional right of publicity cases, both from a quantitative and a qualitative perspective.

As a quantitative matter, *NCAA Football* is different from other right of publicity cases in the sheer number of virtual actors involved. Most right of publicity cases involve either one celebrity, or a finite and defined group of celebrities. . . .

In contrast, *NCAA Football* includes not just Sam Keller, but thousands of virtual actors. This consideration is of particular significance when we examine, as instructed by *Comedy III*, whether the source of the product marketability comes from creative elements or from pure exploitation of a celebrity image. There is not, at this stage of the litigation, any evidence as to the personal marketing power of Sam Keller, as distinguished from the appeal of the creative aspects of the product. Regardless, the sheer number of athletes involved inevitably diminish the significance of the publicity right at issue. *Comedy III* involved literal depictions of the Three Stooges on lithographs and T-shirts. . . . The commercial image of the celebrities in [that] case was central to the production, and its contact with the consumer was immediate and unavoidable. In contrast, one could play *NCAA Football* thousands of times without ever encountering a particular avatar. In context of the collective, an individual's publicity right is relatively insignificant. Put another way, if an anonymous virtual player is tackled in an imaginary video game and no one notices, is there any right of publicity infringed at all? . . .

## II

Given the proper application of the transformative use test, Keller is unlikely to prevail. The balance of interests falls squarely on the side of the First Amendment. The stakes are not

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small. The logical consequence of the majority view is that all realistic depictions of actual persons, no matter how incidental, are protected by a state law right of publicity regardless of the creative context. This logic jeopardizes the creative use of historic figures in motion pictures, books, and sound recordings. Absent the use of actual footage, the motion picture *Forrest Gump* might as well be just a box of chocolates. Without its historical characters, *Midnight in Paris* would be reduced to a pedestrian domestic squabble. The majority's holding that creative use of realistic images and personas does not satisfy the transformative use test cannot be reconciled with the many cases affording such works First Amendment protection. I respectfully disagree with this potentially dangerous and out-of-context interpretation of the transformative use test.

## NOTES

**1. *NCAA Aftermath.*** EA ultimately settled the right to publicity claims for $40 million, and the NCAA settled with its players for $20 million. At the time, NCAA student-athletes were contractually barred from receiving any compensation other than scholarships for their participation in athletics. NCAA bylaws even required student-athletes to contractually relinquish their right of publicity to the member schools and to the NCAA as a condition to participation in sports. Jennifer Hinds, Comment, The One-Sided Games of the NCAA: How *In Re NCAA Student-Athlete* Levels the Playing Field, 35 Loy. L.A. Ent. L. Rev. 95, 116 (2015), thus concludes that the Ninth Circuit "correctly rejected the First Amendment defenses that would have given EA a blanket license to continue to profit off of the backs of the athletes."

The movement toward greater protection of student-athletes has only accelerated since the *EA* decision. In 2019, California enacted the Fair Pay to Play Act, which allows student-athletes to make endorsement deals. See Alan Blinder, N.C.A.A. Athletes Could Be Paid Under New California Law, N.Y. Times, Oct. 1, 2019. Shortly thereafter, the NCAA voted to change their bylaws to allow student-athletes to profit from their names and likenesses. See Ganesh Setty & Jabari Young, The NCAA Will Allow Athletes to Profit from Their Name, Image and Likeness in a Major Shift for the Organization, CNBC, Oct. 29, 2019.

The next major change was yet to come. In NCAA v. Alston, 594 U.S. 69 (2021), the Supreme Court held that the NCAA had acted in restraint of trade in violation of Section 1 of the Sherman Act when it imposed the standard prohibitions on student-athletes seeking to maximize their own welfare, given the NCAA's undisputed monopsony (or buyer's monopoly) position. After much discussion, Justice Neil Gorsuch held that under a rule of reason approach (see *supra* Chapter 4, Note 3, at 232, on covenants not to compete), the District Court was correct when it "enjoined only restraints on education-related benefits — such as those limiting scholarships for graduate school, payments for tutoring, and the like," without altering any of the collective practices used to make the NCAA's "consumer facing" activities, like scheduling and promoting events, less competitive than they currently are. After *Alston*, matters dealing with name and likeness are free from any direct restraints by the NCAA. In May 2024, the so-called Power 5 conferences agreed to an extensive, backward-looking settlement that will set aside some $2.8 billion to pay back damages to former athletes who were denied these opportunities for self-promotion while they were players. The deal also has a forward-looking component that sets aside about $22 million for 2025 (with annual increases thereafter) of the $100 million in revenues that the typical major team raises from TV contracts, ticket sales, and sponsorships. The ownership rights have changed, but the earlier privacy rules on these changes have not.

**2. *Transformative and Expressive Uses.*** Returning to the merits of the misappropriation claim, the California Supreme Court adopted the "transformative use" test in Comedy III

Productions, Inc. v. Gary Saderup, Inc., 21 P.3d 797, 808 (Cal. 2001) (cited in *In re NCAA Licensing*). There, the court enjoined the defendant from selling T-shirts that featured a precise rendition of the well-known comedy act The Three Stooges. Invoking an explicit balancing of interests, the court reasoned:

> When artistic expression takes the form of a literal depiction or imitation of a celebrity for commercial gain, directly trespassing on the right of publicity without adding significant expression beyond that trespass, the state law interest in protecting the fruits of artistic labor outweighs the expressive interests of the imitative artist. . . . On the other hand, when a work contains significant transformative elements, it is not only especially worthy of First Amendment protection, but it is also less likely to interfere with the economic interest protected by the right of publicity. . . . [W]orks of parody or other distortions of the celebrity figure are not, from the celebrity fan's viewpoint, good substitutes for conventional depictions of the celebrity and therefore do not generally threaten markets for celebrity memorabilia that the right of publicity is designed to protect.

Should it make any difference that *Comedy III*, like most right-of-publicity cases, involved only a small number (three) of celebrities, whereas *In re NCAA Licensing* involves "thousands of virtual actors"? Does the "transformative-work" test merely vindicate commercial interests? Merely duplicate copyright law's fair use doctrine? See generally Post & Rothman, The First Amendment and the Right(s) of Publicity, *supra* Note 2, at 470.

*In re NCAA Licensing* is in line with the core right of publicity cases that prohibit firms from marketing pictures of professional athletes without their permission, even when the images are not being used to sell any separate product.

But what if the athletes' images are made subject to parody by the imposition of some additional creative element? In Cardtoons, L.C. v. Major League Baseball Players Association, 95 F.3d 959, 971 (10th Cir. 1996), the defendant produced "parody trading cards featuring caricatures of major league baseball players," which contained some humorous commentary on the players as well as information about such matters as salary and playing careers on the back. (Having San Francisco Giants star Barry Bonds "on your team is like having money in the bank.") Tacha, J., rejected the request of the Major League Baseball Players Association (MLBPA) to enjoin their sale, holding that the First Amendment protected their publication. After distinguishing White v. Samsung, 971 F.2d 1395 (9th Cir. 1992), Tacha, J., wrote:

> MLBPA maintains that there are many ways that Cardtoons could parody the institution of baseball that would not require use of player names and likenesses. Cardtoons could, for example, use generic images of baseball players to poke fun at the game. Second, MLBPA contends that Cardtoons could use recognizable players in a format other than trading cards, such as a newspaper or magazine, without infringing on its right of publicity. MLBPA argues that these alternative means of communication are adequate and, therefore, that we may uphold its property rights without seriously infringing upon Cardtoons' right to free expression. . . .
>
> In this case, Cardtoons' expression requires use of player identities because, in addition to parodying the institution of baseball, the cards also lampoon individual players. Further, Cardtoons' use of the trading card format is an essential component of the parody because baseball cards have traditionally been used to celebrate baseball players and their accomplishments.

By contrast, in Doe a/k/a Twist v. TCI Cablevision, 110 S.W.3d 363, 374 (Mo. 2003), Limbaugh, J., rejected the "transformative use" test in favor of the "predominant use" test where speech is both expressive and commercial. Anthony Twist, a.k.a. Tony Twist, a former professional hockey player in the National Hockey League, brought a misappropriation claim against the creators, publishers, and marketers of *Spawn*, a comic book that contained a villainous character sharing his name. Twist presented evidence that "in marketing *Spawn* products, [defendants] directly targeted hockey fans—Twist's primary fan base—by producing and licensing *Spawn* logo hockey pucks, hockey jerseys and toy zambonis." Limbaugh, J.,

held that "the use and identity of Twist's name has become predominantly a ploy to sell comic books and related products rather than an artistic or literary expression." Thus "free speech must give way to the right of publicity." Twist was awarded $15 million in damages, which was affirmed on remand. Doe v. McFarlane, 207 S.W.3d 52, 75–76 (Mo. Ct. App. 2006).

**3.** ***Other Tests for Commercial Appropriation.*** Some states follow neither the transformative use test or the predominant use test in determining whether the use of another's name, image, or likeness constitutes actionable appropriation. For example, the test used in Hilton v. Hallmark Cards, 599 F.3d 894, 910–11 (9th Cir. 2009) focuses on whether a plaintiff's identity has been "distort[ed]" or "transmogrif[ied]." Often this hurdle is hard for a plaintiff to clear: in Hamilton v. Speight, 827 F. App'x 238, 240 (3d Cir. 2020), the court affirmed a summary judgment for the defendant even though the plaintiff, a professional football player turned wrestler, could show some similarities between himself and the defendant's video game character. The court found no reasonable jury could conclude that plaintiff's persona was the "sum and substance" of the defendant's character. If this plaintiff could make out a claim of likeness, how many other athletes could make the same claim?

Additionally, in Parks v. LaFace Records, 329 F.3d 437, 463 (6th Cir. 2003), the court held that the plaintiff, Rosa Parks, whose act of defiance precipitated the Montgomery Bus Boycott of 1956, raised at least a jury question on whether the defendant record company had misappropriated her name by making it the title of a hit single, "Rosa Parks." There, the court asked whether the title of the song was "wholly unrelated" to the content of the song so that it could be regarded as a "disguised advertisement for the sale of" goods or services, or whether it was chosen "solely to attract attention" to the work. This test tracks the "relatedness" test of Rogers v. Grimaldi, *supra* at 473, and is arguably the most speech-protective analysis. See Post & Rothman, The First Amendment and the Right(s) of Publicity, *supra* at 470. Can this test be defended on a dignitary theory? Doesn't it allow for the use of one's name even in potentially embarrassing or compromising contexts? How would this case come out under *In re NCAA*'s transformative use test? Is Thomas, J., right to worry that *In re NCAA Licensing* "jeopardizes the creative use of historic figures in motion pictures, books, and sound recordings"?

**4.** ***The First Sale Doctrine.*** The close affinity between the common law right of publicity and traditional forms of intellectual property, such as copyrights and patents, is revealed in the first sale doctrine. In Allison v. Vintage Sports Plaques, 136 F.3d 1443, 1448–49 (11th Cir. 1998), the plaintiff's late husband, a well-known race car driver, had assigned to Maxx Race Cards the right to "manufacture and market trading cards bearing his likeness in exchange for a royalty of 18% of sales receipts." The defendant purchased trading cards bearing the image of plaintiff's husband from manufacturers and distributors, which it mounted in a plaque bearing the name of the featured player or team. The defendant did not copy or alter the cards in any way. The so-called first sale doctrine in the law of patents and copyrights provides that the holder of an intellectual property right has no further right to control its subsequent resale or further disposition once it is placed in the market. Kravitch, J., held that this doctrine barred plaintiff's claim for violation of the right of publicity:

> [A]ccepting appellants' argument would have profoundly negative effects on numerous industries and would grant a monopoly to celebrities over their identities that would upset the delicate "balance between the interests of the celebrity and those of the public." [*White*, 989 F.2d at 1515 (Kozinski, J., dissenting).] Indeed, a decision by this court not to apply the first-sale doctrine to right of publicity actions would render tortious the resale of sports trading cards and memorabilia and thus would have a profound effect on the market for trading cards, which now supports a multi-billion dollar industry. Such a holding presumably also would prevent, for example, framing a magazine advertisement that bears the image of a celebrity and reselling it as a collector's item, reselling an empty cereal box that bears a celebrity's endorsement, or even reselling a used poster promoting a professional sports team. Refusing to apply the first-sale

doctrine to the right of publicity also presumably would prevent a child from selling to his friend a baseball card that he had purchased, a consequence that undoubtedly would be contrary to the policies supporting that right.

A holding that the first-sale doctrine does limit the right of publicity, on the other hand, would not eliminate completely a celebrity's control over the use of her name or image; the right of publicity protects against unauthorized use of an image, and a celebrity would continue to enjoy the right to license the use of her image *in the first instance*—and thus enjoy the power to determine when, or if, her image will be distributed.

Note that the first sale doctrine need not necessarily reduce the plaintiff's total receipts. The royalty charge for the initial use could reflect both present and future users of the object sold. The single lump sum thus displaces a series of smaller payments that would be, to say the least, difficult to collect.

The first-sale doctrine also applies to protect a purchaser when "a mark is used to refer to a component incorporated into a new end product." See Bluetooth SIG Inc. v. FAC US LLC, 30 F.4th 870 (9th Cir. 2020), where the court held that SIG, the owner of the word mark "Bluetooth" had no right to enjoin the use of that name by the defendant automobile manufacturer (Fiat, Chrysler, Dodge, Jeep, and Ram) that incorporated Bluetooth devices in its cars purchased from third-party suppliers without obtaining a license from SIG.

## *Factors Etc., Inc. v. Pro Arts, Inc.*

579 F.2d 215 (2d Cir. 1978)

[The plaintiff in this action had received from Boxcars, Inc.—a corporation controlled by the late Elvis Presley and his business partner, Colonel Tom Parker—an exclusive license to commercially exploit the name and likeness of Elvis Presley. Factors Etc. had paid Boxcars $100,000 for the license against a guarantee of $150,000. Immediately upon learning of Presley's death, Pro Arts purchased the copyright of a Presley photograph from a staff reporter of the *Atlanta (Georgia) Journal*, which it published on a poster three days later. Above the picture were the words "IN MEMORY" and below it were the dates "1935-1977." Among the many purchasers of the posters was the New York codefendant, Stop and Shop Companies. Factors Etc. demanded in writing that Pro Arts cease marketing the poster and threatened suit if it did not. Pro Arts responded by filing a declaratory judgment action in the Northern District of Ohio. Factors Etc. brought suit in the Southern District of New York. The issue on appeal was whether the New York district court had properly issued a preliminary injunction against Pro Arts.]

Ingraham, J. . . . The injunction restrained Pro Arts during the pendency of the action from manufacturing, selling or distributing (1) any more copies of the poster labeled "IN MEMORY . . . 1935-1977," (2) any other posters, reproductions or copies containing any likeness of Elvis Presley, and (3) utilizing for commercial profit in any manner or form the name or likeness of Elvis Presley. The order also denied Pro Arts' motion to dismiss, stay or transfer. Pro Arts has duly perfected this interlocutory appeal from the order. . . .

On appeal, Pro Arts alleges two errors of law on the part of the trial court. According to Pro Arts, the trial court erred first in concluding that the right of publicity could survive the death of the celebrity. Second, Pro Arts argues that even if the right did so survive, Pro Arts was privileged, as a matter of law, in printing and distributing its "memorial poster" of Presley, because the poster celebrated a newsworthy event.

The first issue, the duration of the so-called "right of publicity," is one of state law, more specifically the law of the State of New York. Because of the dearth of New York case law in

this area, however, we have sought assistance from federal court decisions interpreting and applying New York law, as well as decisions from courts of other states.

[The court then relied on *Zacchini* and the excerpt from the Kalven article quoted therein to establish that the right of publicity is designed to protect the plaintiff's right of commercial exploitation and thus is sharply distinguishable from the other forms of privacy, which, in contrast, are designed "to minimize the intrusion or publication" of damaging information. It also noted that Haelan Laboratories, Inc. v. Topps Chewing Gum, Inc., 202 F.2d 866 (2d Cir. 1953), recognized that the right of publicity was transferable by its owner.]

There can be no doubt that Elvis Presley assigned to Boxcar a valid property right, the exclusive authority to print, publish and distribute his name and likeness. In so doing, he carved out a separate intangible property right for himself, the right to a certain percentage of the royalties which would be realized by Boxcar upon exploitation of Presley's likeness and name. The identification of this exclusive right belonging to Boxcar as a transferable property right compels the conclusion that the right survives Presley's death. The death of Presley, who was merely the beneficiary of an income interest in Boxcar's exclusive right, should not in itself extinguish Boxcar's property right. Instead, the income interest, continually produced from Boxcar's exclusive right of commercial exploitation, should inure to Presley's estate at death like any other intangible property right. To hold that the right did not survive Presley's death, would be to grant competitors of Factors, such as Pro Arts, a windfall in the form of profits from the use of Presley's name and likeness. At the same time, the exclusive right purchased by Factors and the financial benefits accruing to the celebrity's heirs would be rendered virtually worthless. . . .

Pro Arts' final argument is that even if Factors possesses the exclusive right to distribute Presley memorabilia, this right does not prevent Pro Arts from publishing what it terms a "memorial poster" commemorating a newsworthy event. In support of this argument, Pro Arts cites Paulsen v. Personality Posters, Inc., 299 N.Y.S.2d 501 (Sup. Ct. 1968), a case arising out of the bogus presidential candidacy of the television comedian Pat Paulsen. Paulsen sued defendant for publishing and distributing a poster of Paulsen with the legend "FOR PRESIDENT." The court refused to enjoin sale of the poster because Paulsen's choice of the political arena for satire made him "newsworthy" in the First Amendment sense. We cannot accept Pro Arts' contention that the legend "IN MEMORY . . ." placed its poster in the same category as one picturing a presidential candidate, albeit a mock candidate. We hold, therefore, that Pro Arts' poster of Presley was not privileged as celebrating a newsworthy event. . . .

Affirmed.

## NOTES

**1. *Commercial Life After Death?*** With *Pro Arts*, compare Memphis Development Foundation v. Factors Etc., Inc., 616 F.2d 956, 958–60 (6th Cir. 1980). The Development Foundation offered an eight-inch statuette of Elvis Presley to persons who contributed $25.00 to the Foundation. The Foundation instituted a declaratory judgment action to establish that Factors's license did not preclude its distribution of the statue. Factors counterclaimed for damages and injunctive relief. In holding that the right of publicity did not survive the death of the actor, the court took issue with *Pro Arts* by examining some of the fundamental principles underlying private property and a market economy:

> Recognition of a post-mortem right of publicity would vindicate two possible interests: the encouragement of effort and creativity, and the hopes and expectations of the decedent and those with whom he contracts that they are creating a valuable capital asset. Although fame

and stardom may be ends in themselves, they are normally by-products of one's activities and personal attributes, as well as luck and promotion. The basic motivations are the desire to achieve success or excellence in a chosen field, the desire to contribute to the happiness or improvement of one's fellows and the desire to receive the psychic and financial rewards of achievement. . . .

On the other hand, there are strong reasons for declining to recognize the inheritability of the right. A whole set of practical problems of judicial line-drawing would arise should the courts recognize such an inheritable right. How long would the "property" interest last? In perpetuity? For a term of years? Is the right of publicity taxable? At what point does the right collide with the right of free expression guaranteed by the First Amendment? Does the right apply to elected officials and military heroes whose fame was gained on the public payroll, as well as to movie stars, singers and athletes? Does the right cover posters or engraved likenesses of, for example, Farrah Fawcett Majors or Mahatma Gandhi, kitchen utensils ("Revere Ware"), insurance ("John Hancock"), electric utilities ("Edison"), a football stadium ("RFK"), a pastry ("Napoleon"), or the innumerable urban subdivisions and apartment complexes named after famous people? Our legal system normally does not pass on to heirs other similar personal attributes even though the attributes may be shared during life by others or have some commercial value. Titles, offices and reputation are not inheritable. Neither are trust or distrust and friendship or enmity descendible. An employment contract during life does not create the right for heirs to take over the job. Fame falls in the same category as reputation; it is an attribute from which others may benefit but may not own.

The law of defamation, designed to protect against the destruction of reputation including the loss of earning capacity associated with it, provides an analogy. There is no right of action for defamation after death. . . .

There is no indication that changing the traditional common law rule against allowing heirs the exclusive control of the commercial use of their ancestor's name will increase the efficiency or productivity of our economic system. It does not seem reasonable to expect that such a change would enlarge the stock or quality of the goods, services, artistic creativity, information, invention or entertainment available. Nor will it enhance the fairness of our political and economic system. It seems fairer and more efficient for the commercial, aesthetic, and political use of the name, memory and image of the famous to be open to all rather than to be monopolized by a few. An equal distribution of the opportunity to use the name of the dead seems preferable. The memory, name and pictures of famous individuals should be regarded as a common asset to be shared, an economic opportunity available in the free market system.

After *Memphis Development* decided that the right was not inheritable, the Second Circuit abandoned its earlier decision by giving "conclusive" effect "to a ruling by a court of appeals [the Sixth Circuit] deciding the law of a state within its circuit." Factors Etc., Inc. v. Pro Arts, Inc., 652 F.2d 278, 279 (2d Cir. 1981). Why aren't the descendible interests just those that are protected during life by the right of publicity? Should statutory compromises be allowed? See Indiana Code §32-36-1-8(a) (2024): "A person may not use an aspect of a personality's right of publicity for a commercial purpose during the personality's lifetime or for one hundred (100) years after the date of the personality's death without having obtained previous written consent from a [designated] person." On the descendibility question, see generally Peter Felcher & Edward Rubin, Privacy, Publicity, and Portrayal of Real People by the Media, 88 Yale L.J. 1577 (1979).

**The statuettes at issue in MDF v. Factors Etc., Inc. were eight-inch pewter replicas of this bronze statue of Elvis, for which MDF was trying to raise funds at the time. The statue, originally outdoors in downtown Memphis, has since been moved to the Memphis Welcome Center.**

*Source: Kevin Fleming/Corbis*

**2. *Privacy Rights After Death?*** In *Pro Arts*, the court determined that Elvis Presley's right to publicity was a transferable property right that survived beyond his death. However, with modern technology such as AI enabling the reanimation of dead celebrities and allowing people to share with the world the intimate details of another's life after that person's death, the question remains open as to whether privacy rights other than publicity survive beyond death.

Anita L. Allen & Jennifer E. Rothman, in Postmortem Privacy, 123 Mich. L. Rev. (forthcoming), advocate the extension of privacy rights to all decedents and not just those whose identity has "commercial value" at the time of their death. What sort of postmortem harms would be construed as wrongful invasions of privacy? Is there a significant risk that postmortem privacy rights will be asserted primarily by relatives of celebrities, similar to how recovery for misappropriation is effectively limited to the rich and famous?

**3. *Exploitation Only After Death?*** Should the right of publicity descend if it had not been used during the lifetime of the original creator? The California Supreme Court answered that question in the negative in Lugosi v. Universal Pictures, 603 P.2d 425 (Cal. 1979). The decedent had not taken any steps while alive to exploit his famous Dracula image, developed in his movie roles for the defendant. The defendant thereafter licensed a number of other businesses to make an impressive assortment of clothes, trinkets, and memorabilia that used the Dracula image. The California court refused to allow Lugosi's heirs to enjoin the sales. The legislature responded to *Lugosi* by adoption of Cal. Civ. Code §3344.1(b) (West 2024), which provides: "The rights recognized under this section are property rights, freely transferable or descendible, in whole or in part, by contract or by means of any trust or any other testamentary documents. . . ." This same view was taken in Estate of Bisignano v. Exile Brewing Co., LLC, 694 F. Supp. 3d 1088, 1117 (S.D. Iowa 2023), which concluded that these rights were descendible even if the decedent was not exploiting them at the time of her death.

**Bela Lugosi's on-screen debut as Count Dracula (image still from *Dracula*, 1931)**

*Source: World History Archive/Alamy*

In Cairns v. Franklin Mint Co., 24 F. Supp. 2d 1013 (C.D. Cal. 1998), the court refused to apply that statute for the benefit of the plaintiffs, trustees of the Princess Diana Memorial Fund, who brought suit to prevent the use of her name or likeness in conjunction with the sale of Princess Diana memorabilia because Great Britain, whose law applied in the case, does not recognize a descendible right of publicity.

**4. *Corporations and the Right of Publicity.*** Should corporations be able to assert the right of publicity? Melville B. Nimmer, The Right of Publicity, 19 Law and Contemporary Problems 203, 214–16 (Spring 1954), advocated granting business entities such a right. According to Nimmer, the theory of unfair competition and contractual remedies are both inadequate in such cases because the former establishes an excessively high bar for recovery and the latter requires privity of contract. He further posited that publicity "must be recognized as a property" right instead of a personal right and, as such, that "animals, inanimate objects, and business and other institutions all may be endowed with publicity values" allowing them to sue for misappropriation.

The majority position in the United States, though, is that publicity rights only extend to natural persons. The Restatement (Second) of Torts is resolute: "A corporation as such has no right of privacy." §652I, cmt. *c*. Courts have largely fallen in line. See, e.g., Jalin Realty Cap.

Advisors, LLC v. A Better Wireless, NISP, LLC, 917 F. Supp. 2d 927, 941 (D. Minn. 2013) ("No Minnesota court has previously allowed a commercial entity . . . to bring an appropriation claim and allowing Jalin to bring an appropriation claim would make Minnesota a major outlier"); Bear Foot, Inc. v. Chandler, 965 S.W.2d 386, (Mo. Ct. App. E.D. 1998); The Eagle's Eye, Inc. v. Ambler Fashion Shop, Inc., 627 F. Supp. 856, (E.D. Pa. 1985) ("it is clear that the right of publicity inures to an *individual* who seeks to protect and control the commercial value of his name or likeness"). In DeSilva v. Allergan USA, Inc., 2020 WL 5947827 (C.D. Cal. 2020), the court put a twist on the majority position, holding that while corporations do have "a lesser right to privacy than human beings and are not entitled to claim a right to privacy in terms of a fundamental right . . . some right to privacy still exists." Which rights and why?

In Doggett v. Travis Law Firm, P.C., 555 S.W.3d 127 (Tex. App. 2018), the Travis Law Firm sued a former contract attorney who continued to use the firm's name and letterhead in his practice after he left the firm for invasion of privacy by appropriation of name or likeness. Lloyd, J., reversed the jury's award of $24,279 in damages on the ground that "[n]o Texas authority has recognized a corporation's right to privacy." While squarely rejecting the appropriation claim as a species of invasion of privacy, however, Lloyd, J., left open the possibility that such a claim could be brought within the scope of unfair competition law. See *supra* Chapter 4, at 257 (discussion of INS v. AP). What does this suggest about the underlying interest protected by the privacy torts? Does it make sense?

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