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COMMENTS

PUNITIVE DAMAGES ON ORDINARY CONTRACTS

Punitive damages historically may not be recovered for breach of contract.¹ Montana by statute has not allowed punitive damages for breach of an obligation “arising from contract” since at least 1895.²

It would be wrong, however, to assume that the law of punitive damages on contract is settled.³ One recent change in Montana is the distinction now made for the purpose of punitive damages between insurance contracts and other ordinary contracts.⁴ Punitive damages may be recovered for breach of an insurance contract which also constitutes breach of a duty imposed upon the parties by statute.⁵ Punitive damages on insurance contracts are covered in the preceding article of this issue,⁶ and so will be discussed only briefly here.

The subject of this comment is punitive damages on ordinary contracts. Section I deals briefly with historical background of punitive damages in contract actions. Section II discusses the development of Montana case law. Section III suggests how to identify and establish a valid claim for punitive damages arising out of a contract. Also, section III traces the definition of fraud as it has developed through Montana punitive damages tort cases.

I. HISTORICAL BACKGROUND

Punitive damages, also called exemplary damages, are intended primarily to punish a party in a civil suit for a wrong done to society as well as to the plaintiff and to serve as an example for

1. 22 AM. JUR. 2d *Damages* § 245 (1965); RESTATEMENT OF CONTRACTS § 342 (1932); 11 S. WILLISTON, *CONTRACTS* § 1340 (1920); Sullivan, *Punitive Damages in the Law of Contract: The Reality and the Illusion of Legal Change*, 61 MINN. L. REV. 207 (1977) [hereinafter cited as Sullivan].

2. MONTANA CODE ANNOTATED [hereinafter cited as MCA] § 27-1-221 (1979) (formerly REVISED CODES OF MONTANA (1947) [hereinafter cited as R.C.M. 1947] § 17-208, enacted in 1895).

3. Sullivan, *supra* note 1, at 221.

4. *First Security Bank v. Goddard*, ___ Mont. ___, 593 P.2d 1040, 1047 (1979).

5. *Id.*

6. Harman, *An Insurer's Liability for the Tort of Bad Faith*, 42 MONT. L. REV. 67 (1981) [hereinafter cited as Harman].

the over-all good of society.⁷ Since parties to a contract create contractual obligations by an exercise of will, and failure to discharge these self-imposed obligations does not inevitably violate objective standards of societal conduct, the needs of society which justify an award of punitive damages generally are not present in a contract situation.⁸ It is also thought that since damages are more readily calculable when based on a contract, there is seldom a need or justification to extend the award to non-pecuniary losses in order to fully compensate the injured party.⁹ The general rule against punitive damages on contract originated in England, and was carried over to the United States possibly as a result of tradition more than definitive legal reasoning.¹⁰

Several exceptions to the general rule have developed. The two oldest exceptions, generally accepted, are breach of a contract to marry,¹¹ and breach of a contract by a public service company.¹² Some courts allow punitive damages on a contract if there is also a fiduciary duty between the parties to the contract.¹³ And in some

7. Sullivan, *supra* note 1, at 217, 219.

8. *Id.*; W. PROSSER, LAW OF TORTS 613 (4th ed. 1971); M.S.R. Assocs., Ltd. v. Consolidated Mut. Ins. Co., 58 A.D.2d 859, 396 N.Y.S.2d 685 (1977) (only a private wrong and not a public right involved); Halpert v. Rosenthal, 107 R.I. 406, 413, 267 A.2d 730, 735 (1970) (In case of breach of contract, damage resulting from an innocent misrepresentation of a material fact relied upon is equally injurious to that resulting from fraud.).

9. Sullivan, *supra* note 1, at 218; Peterson v. Culver Educ. Found., ___ Ind. ___, 402 N.E.2d 448, 453 (1980) (Well-defined parameters of damages which may be assessed for breach of contract lend a needed measure of stability and predictability to the free enterprise system.). Vallesjo v. Jamestown College, 244 N.W.2d 753 (N.D. 1976).

No damages can be recovered for a breach of contract if they are not clearly ascertainable in both their nature and origin The damages must be such as may fairly be supposed to have entered into the contemplation of the parties when they made the contract The injured person . . . is not to be put in a better position by a recovery of damages than he would have been if there had been performance.

Id. at 758-59.

10. Sullivan, *supra* note 1, at 208-20.

11. 22 AM. JUR. 2d Damages § 245 (1965). See also Sullivan, *supra* note 1, at 223: The justification for permitting these awards rests mainly upon the peculiar nature of the interests invaded by breach of contract to marry. Because the damage suffered by the plaintiff is often uniquely personal, the character of the interest abused frequently has much more in common with a typical tort action than with the standard contract action.

12. See Sullivan, *supra* note 1, at 223-24:

English law early recognized that those engaged in public or common callings had an obligation to serve all applicants for their services Legal rules governing the common callings were shaped by the need to protect the public against exploitation or oppression by the providers of important public services [which] . . . [i]n modern society [are] . . . the common carrier or public utility that enjoys monopoly or quasi-monopoly power.

13. In order for the exception to lie, apparently, there must be a true fiduciary relationship, e.g., broker-principal, but retail dealer-distributor held not a fiduciary relationship.

jurisdictions, breach of contract involving fraudulent conduct justifies an exception.

Two methods have developed to find the exception for fraudulent conduct. The first method requires that the contract itself be breached by fraudulent conduct.¹⁴ The second method awards the punitive damages on a tort existing independent of the contract between parties whose relationship was created by the contract.¹⁵

With the first method, technically, all that is required to bring the exception into play is a satisfactory showing that the conduct breaching the contract was fraudulent, or was accompanied by fraud.¹⁶ Application of this method in a pure sense can significantly increase the incidence of punitive damages awards in that jurisdiction because the possibility of fraudulent conduct cuts across the whole range of contract relations and because fraud is often defined liberally.¹⁷

With the second method, the punitive damages are not recovered on the actual breach of contract, but rather are found on a tort independent of the contract. This method, therefore, is not a true exception to the general rule although it is usually called an exception by courts which use it.¹⁸ If it is applied correctly, no amount of fraud in the contract transaction will warrant punitive damages if there is no tort present arising from breach of a duty separate from the ordinary contractual duty. Such a separate duty can be present between parties although their relationship is originally created by the contract.

The second method is difficult to apply because the line of distinction between contract and tort often cannot be precisely drawn.¹⁹ The distinction is based on whether the duty breached is the contractual duty itself or a duty separate from the contract. Some courts attempt to identify the duty, while others do not distinguish between the duties but base the distinction between con-

See Sullivan, *supra* note 1, at 228-29. See also 22 AM. JUR. 2d *Damages* § 245 (1965).

14. Sullivan, *supra* note 1, at 229-30.

15. *Id.* at 236-37.

16. *Id.* at 231. See also *Peterson v. Culver Educ. Found.*, ___ Ind. ___, 402 N.E.2d 448, 454-56 (1980) (Tortious activity is often "mingled" with the breach of contract. Therefore an independent tort is not a prerequisite to recovery of punitive damages. Defendant's malicious state of mind is stressed in the court's findings.).

17. Sullivan, *supra* note 1, at 229-30.

18. *Id.* at 236-37; 22 AM. JUR. 2d *Damages* § 245 (1965). *Peterson v. Culver Educ. Found.*, ___ Ind. ___, 402 N.E.2d 448, 453 (1980) refers to this method as an exception to the general rule.

19. Sullivan, *supra* note 1, at 237-38; *Peterson v. Culver Educ. Found.*, ___ Ind. ___, 402 N.E.2d 448, 454 (1980).

tract and tort on a finding of misfeasance versus nonfeasance.²⁰ Misfeasance is defective performance of the contract or an active and intentional type of conduct, while nonfeasance is simply failure to perform. Courts using the misfeasance-nonfeasance distinction find the essential tort present in misfeasance.

Differences between these two methods may seem obvious here but sometimes the cases are not clear. Some courts have confused the two rationales by combining them or by adopting one while also using language from the other. For example, a court might adopt the first method but then attempt to justify it by stating that a tort must be shown in addition to the fraudulent breach of contract.²¹ Or, a court might rely on the second method and base the award of punitive damages on an independent tort but then also talk about malicious or oppressive breach of the contract.²² When a jurisdiction becomes caught in the grey area between the two methods there is a characteristic inability to predict the outcome of an individual case.²³

Overall, if a jurisdiction has retained the general rule against punitive damages on contract, then the second method requiring an independent tort is the most direct means to get punitive damages on contract since it can be accepted alongside the general rule. Montana has employed this method for insurance contracts, as is discussed in the preceding article of this issue.²⁴ Neither method, however, has been used in Montana for ordinary contracts. Instead, Montana has gone to a common law doctrine of election of the form of action by the plaintiff.

II. MONTANA LAW

In Montana if there is breach of a duty other than the contractual duty, the plaintiff, to recover punitive damages, can elect to affirm the contract and sue on the tort.²⁵ The independent tort must always involve conduct proscribed in the punitive damages statute, which states:

When exemplary damages allowed. In any action for a breach of

20. Sullivan, *supra* note 1, at 239.

21. *Id.* at 235.

22. *Id.* at 237; Peterson v. Culver Educ. Found., ___ Ind. ___, 402 N.E.2d 448, 454 (1980).

23. Sullivan, *supra* note 1, at 235.

24. First Security Bank v. Goddard, ___ Mont. ___, 593 P.2d 1040 (1979), *discussed in* Harman, *supra* note 6, at 67.

25. Dimler v. District Court, 170 Mont. 77, 81, 550 P.2d 917, 920 (1976), *citing*, 37 AM. JUR. 2d *Fraud and Deceit* § 332 (1968).

an obligation *not arising from contract*, where the defendant has been guilty of oppression, fraud, or malice, actual or presumed, the jury, in addition to the actual damages, may give damages for the sake of example, and by way of punishing the defendant.²⁶

Westfall v. Motors Insurance Corporation,²⁷ decided in 1962, was the Montana Supreme Court's first opportunity to construe the statute as it applies to contracts.²⁸ There plaintiff purchased an accident insurance policy from defendant on a used automobile.²⁹ The maximum coverage of the policy was based on the actual cash value of the car rather than the amount financed. When plaintiff submitted a claim to defendant, the adjuster reported as the actual cash value the amount financed. He also secured from the plaintiff a release which discharged defendant from further obligation on the policy by promising that plaintiff would receive "something [extra] out of it or have a car."³⁰ The defendant then paid off the debt on the car and paid plaintiff only the unearned portion of the insurance premium.³¹ Plaintiff sued for compensatory and punitive damages on fraudulent misrepresentation of the true actual cash value and also on fraudulent misrepresentation of the terms of the release.³² The jury returned a verdict for plaintiff of actual and punitive damages.³³

On appeal the court reversed, stating that the action was on contract and not within the punitive damages statute. Each of the fraudulent acts, the court concluded, was breach of an obligation arising directly from contract, and there was no other basis available upon which to award punitive damages. The court considered the release first since rescission of the release was necessary to reinstate the original insurance contract.³⁴ By statute a release is a type of contract,³⁵ and as such is voidable and subject to rescission for fraud or mistake of fact.³⁶ The required finding of fraud, to make a release voidable, can be satisfied by fraudulent procure-

26. MCA § 17-1-221 (1979) (emphasis added).

27. 140 Mont. 564, 374 P.2d 96 (1962).

28. *Westfall* was discussed in Pitch, *Punitive Damages for Fraudulent Procurement of a Release are Prohibited by Statute*, 24 MONT. L. REV. 71 (1962).

29. *Westfall*, 140 Mont. at 565, 374 P.2d at 97.

30. *Id.* at 566, 374 P.2d at 97-98.

31. *Id.*, 374 P.2d at 98.

32. *Id.* at 567, 374 P.2d at 98.

33. *Id.*

34. *Id.* at 568, 374 P.2d at 99.

35. MCA § 28-1-601 (1979), cited in *Westfall* as R.C.M. 1947 § 58-509, provides that "[a]n obligation is extinguished by a release therefrom given to the debtor by the creditor, upon a new consideration, or in writing, with or without new consideration."

36. *Westfall*, 140 Mont. at 568, 374 P.2d at 98-99.

ment of the release because, in Montana, activity during procurement of a contract is part of the whole contract transaction.³⁷ Thus, in *Westfall*, fraud in the procurement of the release was fraud in the contract itself. The court then relied on a California case, *Crogan v. Metz*,³⁸ which held that an award of punitive damages may not be granted in an action based on breach of contract even though the breach is willful or fraudulent.³⁹ Under application of *Crogan*, the misrepresentation of the terms of the release did not warrant punitive damages no matter how fraudulent.⁴⁰ Also, the court stated, fraudulent procurement of the release was breach of an obligation arising out of contract, upon which punitive damages are precluded by Montana Code Annotated [hereinafter cited as MCA] § 27-1-221 (1979).

The court's use of *Crogan* and the punitive damages statute applied as well to consideration of the original insurance contract. Misrepresentation of the actual cash value of the car, however willful or fraudulent it may have been, was simply a breach of performance of the terms of the insurance contract.⁴¹ *Westfall* was confirmed in Montana federal court by *Wade v. Great American Insurance Co.*,⁴² in which defendant refused to pay a claim on a theft insurance policy.

In 1965, *Westfall* controlled in *Ryan v. Ald, Inc.*,⁴³ which involved an agreement for purchase of laundromat machines. Defendant was the seller but plaintiff installed the machines himself. When he had problems, defendant sent parts and instructions and an agent, but the machines never did work.⁴⁴ Plaintiff sued on fraud and breach of contract. The jury was allowed to hear evidence that oral promises were made by defendant before the purchase that he would install the machines and show plaintiff how they worked.⁴⁵ Plaintiff recovered actual and punitive dam-

37. *Id.* at 569, 374 P.2d at 99 (procurement of contract is part of contract transaction). *Cf.*, *Walker v. Signal Companies, Inc.*, 84 Cal. App. 3d 982, 149 Cal. Rptr. 119, 126 (1978) (Punitive damages may be awarded where a defendant fraudulently induces the plaintiff to enter a contract because California distinguishes fraudulent inducement from a breach of the contract itself.).

38. 47 Cal. 2d 398, 303 P.2d 1029, 1033 (1956).

39. *Id.* See also *American Int'l Land Corp. v. Hanna*, 323 So.2d 567, 569 (Fla. 1976) (flagrant breach does not constitute tortious fraud and deceit); *Deming v. Buckley's Art Gallery*, 196 F. Supp. 246, 253 (W.D. Ark. 1961) (in consideration of alleged misrepresentations for purpose of rescission of contract, willfulness and maliciousness are unimportant).

40. *Westfall*, 140 Mont. at 570, 374 P.2d at 99-100.

41. *Id.* at 570, 374 P.2d at 100.

42. 255 F. Supp. 735, 736 (D.Mont. 1966).

43. 146 Mont. 299, 406 P.2d 373 (1965).

44. *Id.* at 301, 406 P.2d at 374.

45. *Id.*

ages. On appeal, the court stated that, besides violating the parol evidence rule, oral promises could not be used to prove fraud for the purpose of punitive damages.⁴⁶ Oral promises made both prior to and subsequent to the written contract would all arise out of the same contract transaction, the later promises being a "continuation" of the initial ones. These promises, if fraudulent, would constitute fraudulent inducement of the contract. In this case, as in *Westfall*, fraudulent inducement of contract was breach of the contract. Thus, punitive damages were not recoverable and evidence pertaining to them was not admissible.⁴⁷

Plaintiff's right to elect whether the form of action is contract or tort was recognized in 1953, in *Garden City Floral Co. v. Hunt*.⁴⁸ Citing cases from several other jurisdictions, the Montana court stated that to find a tort there must be a duty, other than the duty arising from the contract, which is breached by active misfeasance rather than passive negligence.⁴⁹ Although *Garden City Floral* did not involve fraud or punitive damages, the theory of election is the same as that employed to allow punitive damages on contract in *State ex rel. Dimler v. District Court*.⁵⁰

In *Dimler*, plaintiffs elected to affirm the terms of the contract and sue for damages on the independent tort of fraud.⁵¹ Plaintiffs were buyers in a real estate contract for deed. Defendants, as sellers, had advertised that the house had two bathrooms and had made the upstairs bathroom appear to be in use when in fact there was no plumbing to the second floor of the house. Plaintiffs discovered the fraud the day after they moved in.⁵² They wanted to keep the house, so rather than rescind the sale, plaintiffs affirmed the contract and sued for damages in fraud.⁵³ The district court granted a motion to strike the prayer for punitive damages. Upon writ of supervisory control, the Montana Supreme Court reinstated the punitive damages claim. They distinguished *Westfall* and *Ryan* as actions for breach of contract, and allowed *Dimler* to proceed in tort.⁵⁴ *Westfall* and *Ryan*, the court stated, both involved rescission as a necessary part of the relief granted to the plaintiff

46. *Id.* at 303, 406 P.2d at 375.

47. *Id.*

48. 126 Mont. 537, 543, 255 P.2d 352, 355-56 (1953). See also *Fraser v. Clark*, 137 Mont. 362, 376, 352 P.2d 681, 688 (1960), and citations therein.

49. 126 Mont. at 543, 255 P.2d at 358 (in a doubtful question between contract and tort the doubt must be resolved in favor of contract).

50. 170 Mont. 77, 550 P.2d 917 (1976).

51. *Id.* at 79, 550 P.2d at 918.

52. *Id.*

53. *Id.*

54. *Id.* at 81, 550 P.2d at 919-20.

and if rescission is part of the relief the action is on contract. But if the contract is affirmed, the court went on, the claim for injuries received from fraudulent actions incident to the contract is in tort. The plaintiff cannot do both.⁵⁵ Since the action in *Dimler* was in tort, it therefore involved the type of obligation upon which punitive damages are allowed by MCA § 27-1-221 (1979).

Dimler did not change the general rule in Montana against punitive damages on contract, and three years later, the general rule was affirmed as to ordinary contracts between businessmen in *First State Bank v. Goddard*.⁵⁶ *Goddard* involved an insurance contract governed by the insurance laws of Montana.⁵⁷ It is discussed at length in the preceding article of this issue.⁵⁸ In *Goddard* the court distinguished insurance contracts from other contracts because the peculiar relationship between parties to the consumer-held insurance contract warrants special duties on insurers. They reasoned the insured is usually at an economic disadvantage to the insurer, the insurer almost always prepares the forms used, and the insured, often in financial straits, is especially vulnerable to oppressive tactics by the insurer.⁵⁹ This rationale came from *Battista v. Lebanon Trotting Association*,⁶⁰ a 1976 Ohio federal court case. Quoting *Battista* in *Goddard*, the Montana court was careful to include the following statement: "The special considerations existent in a consumer-held insurance contract do not apply to an or-

55. *Id.* See also 37 AM. JUR. 2d *Fraud and Deceit* §§ 332-33 (1968); *Falls Sand & Gravel Co. v. Western Concrete, Inc.*, 270 F. Supp. 495 (D.Mont. 1967) ("It is clear that in Montana and generally, a party may not pursue both an action for rescission and damages for deceit or misrepresentation." *Id.* at 500); *Fraser v. Clark*, 137 Mont. 362, 376, 352 P.2d 681, 688 (1960).

56. — Mont. —, 593 P.2d 1040 (1979).

57. The court in *Goddard* stated:

In Montana, insurance companies insuring credit disability risks have a statutory duty that exists beyond the insurance contract itself. Their statutory duty under section 40-4213, R.C.M. 1947, now section 33-21-105 MCA, is that all claims shall be settled as soon as possible and in accordance with the terms of the insurance contract It is the breach of that statutory requirement, a duty independent of the insurance contract, that gives rise to tort liability in the case at bar.

Thus, the insurer's duty of good faith and fair dealing with its insureds in the payment of claims has statutory blessing and authority

This Court recognized that a breach of contract might also give rise to an action in tort in *State ex rel. Larson v. District Court* (1967), 149 Mont. 131, 136, 423 P.2d 598, 600, when it said: "Thus, in the insurance contract we have a unique situation; that is, some acts may be both breaches of contract and violations of the laws of Montana."

— Mont. —, 593 P.2d at 1047.

58. Harman, *supra* note 6, at 67.

59. *Goddard*, — Mont. —, 593 P.2d at 1047, citing *Battista v. Lebanon Trotting Assoc.*, 538 F.2d 111 (6th Cir. 1976).

60. 538 F.2d 111, 117-18 (6th Cir. 1976).

inary contract between businessmen"⁶¹ *Battista* followed the Ohio general rule that breach of an ordinary contract does not create a tort claim, regardless of motive, and that punitive damages are not available for breach of contract.⁶² The dangers inherent in the insurance contract created by disparity between the parties' positions are not present in an ordinary contract between businessmen. Thus, Montana, pursuant to *Goddard*, clearly endorses the traditional rule against punitive damages on contracts in the case of an ordinary contract.

III. IDENTIFYING AND ESTABLISHING A VALID CLAIM FOR PUNITIVE DAMAGES ON CONTRACT

There are five parts to this section. The first deals with the importance of pleading with particularity. The second, third, and fourth parts discuss a progressive analysis which can be made of a contract case to determine whether a claim for punitive damages will lie. The questions involved in this analysis are, whether recission is a necessary part of the relief, whether there is a tort independent of the contract, and whether to affirm the contract and sue on the tort. The fifth part briefly discusses the requirement of oppression, fraud, or malice in the punitive damages statute which plaintiff must always satisfy once an independent tort is established.

A. Pleading

Pleading with great particularity is crucial to a valid claim for punitive damages arising out of contract. Since many and varied types of contracts and circumstances can be involved in election of action, proper notice may often require additional information and clarity in the complaint. Rule 9(b) of the Montana Rules of Civil Procedure requires that all averments of fraud shall be stated with particularity. It makes sense that plaintiff's intent to affirm the underlying contract should also be pleaded particularly since it certainly forms a part or basis of the claim of fraud. To affirm, plaintiff should plead all contract terms as written and performed by

61. *Goddard*, ___ Mont. ___, 593 P.2d at 1047; *Battista*, 538 F.2d at 118.

62. In *Battista*, 538 F.2d at 118, the court, citing *Ketcham v. Miller*, 104 Ohio St. 372, Syl. 1, 136 N.E. 145 (1922), stated:

To hold otherwise would be to abandon the venerable rule that the motive of a breaching party to a contract is irrelevant to the merit of the promisee's claim, and would allow parties to convert contract actions into actions in tort by attacking the motive of the breaching party, a course of action precluded by the rule of *Ketcham*.

the parties. A further reason to plead with particularity is that, as used in *Dimler*, the method of election is new in Montana,⁶³ and it can only be to plaintiff's benefit to give defendant and the court clear notice as to the form of action he is bringing.

B. Rescission

The first determination which must be made in anticipating a claim for punitive damages on a contract is whether or not rescission of the contract is part of the plaintiff's relief. As stated in *Dimler*,⁶⁴ if rescission is part of the relief sought, then the action is on contract, and punitive damages are not recoverable. Rescission in a particular case may be required for some reason or may be at plaintiff's option. When plaintiff has the option, he then can affirm the contract and sue on a tort. When he cannot avoid rescission, however, he cannot affirm, and the action must be on contract. This discussion, although by no means exhaustive, brings out some general principles about rescission as a remedy and suggests an analysis which can be used for each particular case to determine rescission versus affirmation.

Rescission is appropriate to many different types of contracts.⁶⁵ The basis of rescission as a remedy for breach of contract is to restore the parties to the status quo.⁶⁶ For the injured party

63. *Dimler* has been cited only once in *Van Ettinger v. Pappin*, — Mont. —, 588 P.2d 988, 995 (1978) (Plaintiff elected to affirm the contract, as in *Dimler*, but election was not allowed because he had notice of the fraud while the contract was executory).

64. *Dimler*, 170 Mont. at 81, 550 P.2d at 919.

65. Examples of types of contracts are: *General Dynamics Corp. v. Selb Mfg. Co.*, 481 F.2d 1204 (8th Cir. 1973) (parts manufacturing contracts); *Associated Hardware Supply Co. v. Big Wheel Distrib. Co.*, 355 F.2d 114 (3d Cir. 1966) (purchase of goods); *Bankers Trust Co. v. Pacific Employers Ins. Co.*, 282 F.2d 106 (9th Cir. 1960) (fire insurance contract); *Mooney v. State Farm Ins. Co.*, 344 F. Supp. 697 (D.N.H. 1972) (employment contract); *Falls Sand & Gravel Co. v. Western Concrete, Inc.*, 270 F. Supp. 495 (D.Mont. 1967) (sub-contract for concrete); *Deming v. Buckley's Art Gallery*, 196 F. Supp. 246 (W.D. Ark. 1961) (implied contract to return money obtained by fraud); *Walker v. Signal Companies, Inc.*, 84 Cal. App. 3d 982, 149 Cal. Rptr. 119 (1978) (house construction); *Cole v. Associated Constr. Co.*, 141 Conn. 49, 103 A.2d 529 (1954) (house construction); *Greer v. Williams*, 375 So.2d 333 (Fla. App. 1979) (oral contract to buy a racehorse); *Doerr v. Villate*, 74 Ill. App. 2d 332, 220 N.E.2d 767 (1966) (oral contract in medical malpractice); *Peterson v. Culver Educ. Found.*, — Ind. —, 402 N.E.2d 448 (1980) (teacher employment contract); *Chavez v. Saums*, 1 Kan. App. 2d 564, 571 P.2d 62 (1977) (express contract between lawyer and client); *Letzig v. Rupert*, 209 Kan. 143, 495 P.2d 955 (1972) (option contracts); *Fraser v. Clark*, 137 Mont. 362, 352 P.2d 681 (1960) (real estate contract); *J. Dunn & Sons, Inc. v. Paragon Homes of New England, Inc.*, 110 N.H. 215, 265 A.2d 5 (1970) (sale contracts—pre-fab homes, equipment and supplies); *Hall Jones Oil Corp. v. Claro*, 459 P.2d 858 (Okla. 1969) (oil and gas leases); *Crutcher-Rolfs-Cummings, Inc. v. Ballard*, 540 S.W.2d 380 (Tex. 1976) (royalties on a patent); *Horner v. Ahern*, 206 Va. 860, 153 S.E.2d 216 (1967) (real estate contract).

66. *Deming v. Buckley's Art Gallery*, 196 F. Supp. 246, 251 (W.D. Ark. 1961).

to be made whole again is considered a sufficient remedy for even a fraudulent breach of a contract into which that person entered of his own free will. Therefore, if rescission is a part of the relief granted, there theoretically is no need of further compensation or punishment of the defendant. Certainly, plaintiff should never plead rescission and an action on an independent tort for the same contract because of inconsistency between the two.⁶⁷

Whether rescission is required may be determined in various ways, several of which are mentioned here. Each individual case may produce other factors and circumstances which likewise require rescission. The following are examples from the Montana cases used in this comment. Some additional points which should be helpful are briefly mentioned.

Plaintiff should always anticipate that even with careful pleading the court will look beyond the face of the complaint to find rescission, as occurred in both *Westfall* and *Ryan*.⁶⁸ Ambiguities between the court's opinions and their actions complicate this analysis. The *Dimler* majority seems to say that rescission was specifically pleaded in *Westfall* and *Ryan*.⁶⁹ But, as pointed out by the *Dimler* dissent, there is no indication in the *Westfall* opinion or the *Ryan* opinion that rescission was actually in the prayer for relief.⁷⁰

In *Westfall*, the court looked to applicable statutory law and to the form of the relief requested by plaintiff. In plaintiff's allegations, as summarized,⁷¹ he did plead fraudulent representations of the terms of the release from liability and of the actual cash value of his car. The court analyzed the statutory law of a release contract which provided that rescission was the relief available for fraud on a release.⁷² Rescission of the release was also necessary to reach the issue of fraud on the insurance contract. The court did not say that rescission of the insurance contract was necessary, but the relief granted to plaintiff was based on the actual cash value which was a term of the contract. Since the relief granted was based on the contract, punitive damages could not be recovered.

The court may also consider conduct of the parties as a way to find rescission of which *Ryan* and *Dimler* are both examples. The

67. *Id.*

68. In a question of contract versus tort, if the question is regarded as a doubtful one, the doubt must be resolved in favor of contract. *Garden City Floral*, 126 Mont. at 543, 255 P.2d at 355-56.

69. *Dimler*, 170 Mont. at 81, 550 P.2d at 919-20.

70. *Id.* at 84, 550 P.2d at 921.

71. *Westfall*, 140 Mont. at 567, 374 P.2d at 98.

72. *Id.* at 568, 374 P.2d at 98-99.

Ryan opinion is unclear as to plaintiff's position on rescission of the contract to purchase laundromat machines. However, the same case was before the court two years later—on a different theory.⁷³ There the court stated that before plaintiff filed the first case on the original theory he tried to get his money back and to rescind the contract, and defendant refused.⁷⁴ The attempt to rescind probably was in the record of the first case even though the court did not specifically report it. Although it is impossible to be certain, the two *Ryan* cases indicate that plaintiff may be held to any attempt to rescind made before initiating legal action which attempt appears later in the court record. In *Dimler*,⁷⁵ although again it is not clear from the language of the opinion whether plaintiffs pleaded the election to affirm, the court stated that they "chose" to affirm.⁷⁶ Plaintiffs remained in the house and continued making payments, which demonstrated their choice to affirm. The point is that conduct can be conclusive. It can ruin plaintiff's election to affirm the contract unless the basis of his form of action is set out unmistakably in the complaint.⁷⁷

Another question, different from the above discussion, may arise in the case of a written contract which contains an express rescission clause. Can the contract even though it contains the clause be affirmed for the purpose of punitive damages? Some indication of Montana's attitude in regard to a rescission clause comes from *Dimler*⁷⁸ in which the court cited *Horner v. Ahern*,⁷⁹ a Virginia case, as an instance of correct use of the doctrine of election. In *Horner*, a real estate contract contained a clause which allowed plaintiffs to rescind the contract if the house were found to have termite damages. The contract was executed and termite damage was later discovered by the plaintiffs. They affirmed the contract and sued for damages in tort. Defendants contended that to affirm the contract, plaintiffs must affirm the rescission clause, and so would be bound to rescission as the only remedy for termite

73. *Ryan v. Ald, Inc.*, 149 Mont. 367, 427 P.2d 53 (1967).

74. *Id.* at 369, 427 P.2d at 55.

75. *Dimler*, 170 Mont. at 79, 550 P.2d at 918.

76. *Id.*

77. *Cf. Deming v. Buckley's Art Gallery*, 196 F. Supp. 246 (W.D. Ark. 1960).

The court is *of the opinion* that the complaint *sets up all the essentials* necessary to support an action for rescission of the contract on the ground of fraud, and that plaintiff, having elected to repudiate or rescind the contract, cannot recover punitive damages in addition to the purchase price. (emphasis added.)

Id. at 253. The court found rescission even though the parties had not specifically requested it.

78. *Dimler*, 170 Mont. at 83, 550 P.2d at 920.

79. 206 Va. 860, 153 S.E.2d 216 (1967).

damage. The Virginia court, however, allowed plaintiffs to use the rescission clause as proof of defendant's duty to make full disclosure of termite damage and did not require the operation of the clause to be affirmed since the clause was meant to become operative only if the damage was discovered before final execution of the contract.⁸⁰ If Montana, therefore, relies on *Horner* in a case involving a contract with a rescission clause, the clause should not necessarily mandate the plaintiff's form of action. The court should be willing to look at the purpose of the clause and the time it was intended to be operative. A plaintiff in such a case who leaves the court to its own devices cannot rely on the result, so he should determine exactly how to use the clause and plead that intent carefully.

Three further points on rescission are worth mentioning. First, when a court finds the action to be on contract because of rescission based on conduct, the act involved upon which rescission is based can be either fraudulent or innocent.⁸¹ Second, in some cases plaintiff may be locked-in to an action on contract, because the contract is fully executed and the amount of plaintiff's injury due to defendant's breach is the exact amount of the promised performance.⁸² Lastly, full or partial performance of a contract may render rescission impossible. For example, if goods purchased on contract for resale are sold by the time the case is settled, the parties cannot be restored to their positions prior to the contract.⁸³

In summary, if final analysis of the contract shows that rescission is necessary or that the court will likely find rescission as part of plaintiff's relief, then the claim must be on contract, and punitive damages cannot be recovered. If rescission is at plaintiff's choice, however, the contract can be affirmed, the first step necessary in claiming punitive damages.

C. *The Independent Duty*

If the contract can be affirmed, and if the plaintiff desires to

80. *Id.* at 867-68, 153 S.E.2d at 221.

81. *Halpert v. Rosenthal*, 107 R.I. 406, 413, 267 A.2d 730, 733-34 (1970).

82. *Westfall*, 140 Mont. at 567, 374 P.2d at 98 (plaintiff was actually damaged \$115, the difference between the actual cash value of the car and the amount paid by defendant). *Cf. Dimler*, 170 Mont. at 79, 550 P.2d at 918 (Plaintiff and defendant had both performed the terms of the contract for deed. Plaintiff, in keeping the house, was damaged by loss of value to the house because of the plumbing.).

83. *Associated Hardware Supply Co. v. Big Wheel Distrib. Co.*, 355 F.2d 114 (3d Cir. 1966). Because the contract cannot be rescinded, "fraud, as alleged [in this case] is an independent action, the recovery for which may be set off against or may even exceed the amounts due and owing under the contract." *Id.* at 120-21.

affirm it, the second step is to identify some duty separate from the contractual duty which defendant has breached. The additional duty must arise out of the same relationship and same set of facts as the contractual duty.⁸⁴ The additional duty may be one allowed at common law, or one imposed by statute.⁸⁵ It is advisable to look over all statutory law which could apply, since a statutory duty recently enacted might support an action in tort. If an independent duty can be identified, then plead the relationship between the parties and the facts supporting breach of the independent duty by the defendant.

D. *Election of Tort*

If there is breach of a duty independent of the contractual duty, and plaintiff has decided to affirm the contract and sue on the tort, intent to elect the tort should be pleaded precisely. Ordinarily, at common law, plaintiff has broad freedom to elect which form of action to proceed on, and determination of whether the action is on contract or in tort is controlled not by technical form but by substance.⁸⁶ Defendant, to be safe, should force an election of remedies if plaintiff's intent is not clear from the complaint. The action of rescission on contract and the action of fraud in the inducement may not be so incompatible as to compel election if the defendant does not force the issue.⁸⁷ However, plaintiff may not have to make the election until the trial.⁸⁸

84. The court in *Bankers Trust Co. v. Pacific Employers Ins. Co.*, 282 F.2d 106 (9th Cir. 1960) (cited in *Dimler*), stated:

[T]his doctrine of election of remedies applies only to choosing between different remedies allowed by law on the same state of facts, where the party has but one cause of action, one right infringed, one wrong to be redressed. "The doctrine does not require election between distinct causes of action arising out of separate and distinct facts." (citation omitted.)

Id. at 110. See also 18 AM. JUR. *Election of Remedies* § 11 (1938).

Bankers Trust Co. also states that an action on a contract induced by fraud is not inconsistent with an action for damages for deceit, and that suit on a contract and a suit for fraud in inducing the contract are two different causes of action with separate and consistent remedies. This view is certainly more flexible than that of *Westfall* which held that fraud in the procurement of a contract is in fact a breach of the contract itself. The Montana court, in citing *Bankers Trust Co.* with approval, may be loosening somewhat on the question of punitive damages on ordinary contracts along the same vein as the *Goddard* treatment of insurance contracts.

85. See, e.g., *Chavez v. Saums*, 1 Kan. App. 2d 564, 571 P.2d 62 (1977) (statutory duty imposed on lawyer-client relationship).

86. *Towns of Madbury & Lee v. State*, 115 N.H. 196, 198, 340 A.2d 103, 105 (1975); *Doerr v. Villate*, 74 Ill. App. 2d 332, 335, 220 N.E.2d 767, 769 (1966).

87. *Fraser v. Clark*, 137 Mont. 362, 377, 352 P.2d 681, 688 (1960).

88. *Warner Bros. Pictures Distrib. Corp. v. Endicott Circuit*, 55 N.Y.S.2d 300, 303 (1945). "One who is guilty of fraud has no option to insist that the aggrieved party sue ex

An interesting question arises if a contract cannot be fully performed at the time fraud is discovered and the election must be made. Can plaintiff affirm the unperformed contract? The test to determine whether the contract can be affirmed before fully performed is whether plaintiff has in fact acquired an equitable interest in the property which is the subject of the contract.⁸⁹ If plaintiff has an equitable interest, he may continue with performance, treat the contract as affirmed, and elect to sue for damages. It would be unfair to require him to wait until the contract is fully performed because the claim might then be barred by the statute of limitation.⁹⁰ This general principle should apply to any contract involving installment payments. One example is an option contract in which an equitable interest is acquired by plaintiff because installments paid are applied to the eventual purchase.⁹¹ By comparison, no equitable interest is acquired in a "pure option" contract which is executed by only one payment made within a specific period of time.⁹² If fraud is discovered in the procurement of a pure option contract which is still wholly executory, the plaintiff cannot affirm and elect a tort for damages.⁹³

In conclusion, once plaintiff has affirmed the contract and the action is in tort, the case will proceed for recovery of punitive damages as would any ordinary tort action. The action is no longer on contract. The contract simply forms the basis for the relationship between parties.

E. *Statutory Requirement*

If plaintiff elects to claim damages on a tort arising out of a contract relation, to recover punitive damages, he must prove that defendant was "guilty of oppression, fraud, or malice, actual or presumed, . . ." as required by MCA § 27-1-221 (1979). If the Montana court has been rather conservative in distinguishing contract from tort, it has been quite liberal in defining the conduct required to recover punitive damages on a tort. A definite broadening of fraud, oppression and malice is seen through tort cases in Montana involving punitive damages.⁹⁴

contractu and not ex delicto so as to eliminate the incriminating charge." *Id.*

89. *Letzig v. Rupert*, 209 Kan. 143, 147, 495 P.2d 955, 958 (1972).

90. *Id.* at 148, 495 P.2d at 958-59.

91. *Id.* at 147, 495 P.2d at 958.

92. *Id.*, 495 P.2d at 959.

93. *Id.* See also *Van Ettinger v. Pappin*, ___ Mont. ___, 588 P.2d 988, 995 (1978).

94. Montana tort cases involving punitive damages:

Oppression is not only unlawful, but is characterized by circumstances which are criminal, wanton, brutal, reckless or grossly fraudulent. *Luther v. Lee*, 62 Mont. 174, 179, 204 P.

An award of punitive damages is in any case extraordinary, and plaintiff is never entitled to it as a matter of right regardless of how bad the injury.⁹⁵ There must be something more alleged and proven than mere negligence.

In estimating the amount of exemplary damages the jury is to consider public good in the restraint of others from wrongdoing and punishment of the offender, and may consider the defendant's wealth and pecuniary ability.⁹⁶

IV. CONCLUSION

A claim for punitive damages arising out of contract should be placed before the court with careful attention to every element supporting the election of action in tort. The elements of the claim which, at a minimum, should appear in the complaint are:

1. An introductory statement of intent to elect an action for damages on a tort independent of the contract between the parties;
2. The relationship of the parties, as shown by,
 - a. terms of the contract involved,
 - b. performance of the contract by the parties,
 - c. decision not to rescind the contract; if applicable, reasons why contract cannot be rescinded,
 - d. decision to affirm the contract;
3. The election of action on the independent tort, by,
 - a. identification of the duty between the parties indepen-

365, 367 (1922). Oppression can be cruelty, severity, domination or excessive use of authority. *Ramsbacher v. Hohman*, 80 Mont. 480, 488, 261 P. 273, 276 (1927). Oppression in business tactics can be inferred, and where punitive damages are sought, motives of the defendant become the most material subject of inquiry. *Security Bank of Harlem v. Kittleson*, 149 Mont. 183, 187-88, 425 P.2d 72, 74 (1967). A sufficient motive is "ill will." *Ramsbacher*, 80 Mont. at 489, 261 P. at 276.

Malice may be proved directly or indirectly. Malice need not necessarily proceed from a spiteful, malignant or revengeful disposition, but may be conduct injurious to another proceeding from an ill-regulated mind, not sufficiently cautious before it occasions injury to another. *Ramsbacher*, 80 Mont. at 487, 261 P. at 276. Malice includes an act conceived in mischief, or of criminal indifference to civil obligations, or which is conscious of existing conditions from which injury or illness would likely result. *Cashin v. Northern Pac. Ry.*, 96 Mont. 92, 111, 28 P.2d 862, 869-70 (1934). An act of malice may consist of or be shown by the continuation of a course of conduct known by defendant to be unlawful and to cause injury. *Cashin*, 96 Mont. at 112, 28 P.2d at 869-70; *First Security Bank v. Goddard*, ___ Mont. ___, 593 P.2d 1040, 1048 (1979). Malice may be disregard of injury that might be inflicted to further economic gain of the defendant. *Cashin*, 96 Mont. at 113, 28 P.2d at 869-70; *Truzzolino Food Products Co. v. F. W. Woolworth Co.*, 108 Mont. 408, 420, 91 P.2d 415, 419 (1939). Malice-in-law may be implied from behavior which is unjustifiable. *Cherry-Burrell Co. v. Thatcher*, 107 F.2d 65, 69 (9th Cir. 1940); *Goddard*, ___ Mont. ___, 593 P.2d at 1049; *Cashin*, 96 Mont. at 111, 28 P.2d at 869-70.

95. *Gagnier v. Curran Constr. Co.*, 151 Mont. 468, 479-80, 443 P.2d 894, 900 (1968).

96. *Ramsbacher v. Hohman*, 80 Mont. 480, 489, 261 P. 273, 277 (1927).

- dent of the contractual duty,
 - b. statements alleging the tort of breach of the independent duty,
 - c. intent to elect an action for damages on the tort; and,
4. A claim for actual and punitive damages on the tort, including,
- a. allegations of injury for purpose of actual damages,
 - b. the punitive damages statute, MCA § 27-1-221 (1979),
 - c. allegations of conduct satisfying the requirement of the statute,
 - d. prayer for actual and punitive damages.

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