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CONTRACT LAW — CONSEQUENTIAL DAMAGES — NEW YORK COURT OF APPEALS HOLDS THAT INSURERS MAY BE LIABLE FOR CONSEQUENTIAL DAMAGES. — *Bi-Economy Market, Inc. v. Harleystville Insurance Co.*, 886 N.E.2d 127 (N.Y. 2008).

Tales of insurance carrier delay and underpayment can be found in the pages of academic journals,<sup>1</sup> in the reports of consumer groups<sup>2</sup> and policy analysts,<sup>3</sup> and in popular culture<sup>4</sup> and public sentiment.<sup>5</sup> It is not surprising, therefore, that courts have sought out new legal mechanisms in order to hold insurers accountable. Recently, the New York Court of Appeals joined the fray in *Bi-Economy Market, Inc. v. Harleystville Insurance Co.*,<sup>6</sup> holding an insurance company potentially liable for consequential damages after it failed to pay out a policy in good faith.<sup>7</sup> Although it is tempting to read the decision as limited to cases of bad faith by insurers, such an interpretation does not square with the compensatory and contract law emphasis of the decision. *Bi-Economy* may therefore represent a broader shift in New York contract law toward more liberal rules for consequential damages than the specific context of insurer bad faith might suggest.

*Bi-Economy Market* was a meat market in Rochester, New York.<sup>8</sup> In 2002, a fire destroyed the company's inventory and caused heavy damage to its building and equipment.<sup>9</sup> At the time, *Bi-Economy* had a "Deluxe Business Owners" insurance policy with Harleystville Insurance Co.<sup>10</sup> The policy included coverage for the building, for business

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<sup>1</sup> See, e.g., Keith J. Crocker & Sharon Tennyson, *Insurance Fraud and Optimal Claims Settlement Strategies*, 45 J.L. & ECON. 469, 504 (2002) (finding that underpayment is an optimal strategy for insurance companies under certain circumstances).

<sup>2</sup> Cf. J. ROBERT HUNTER, CONSUMER FED'N OF AM., PROPERTY/CASUALTY INSURANCE IN 2008: OVERPRICED INSURANCE AND UNDERPAID CLAIMS RESULT IN UNJUSTIFIED PROFITS, PADDED RESERVES, AND EXCESSIVE CAPITALIZATION 1 (2008), [http://www.consumerfed.org/pdfs/2008Insurance\\_White\\_Paper.pdf](http://www.consumerfed.org/pdfs/2008Insurance_White_Paper.pdf) (finding that, compared to twenty years ago, benefits have decreased by fifteen percent per premium dollar spent despite record insurer profits).

<sup>3</sup> See, e.g., STEPHEN WOODBURY & WAYNE VROMAN, DENIED CLAIMS ACCURACY PILOT PROJECT: FOLLOW-UP REPORT 64, 80 (2000), available at <http://workforcesecurity.doleta.gov/unemploy/pdf/dcafollo.pdf> (finding that erroneous denials of unemployment insurance benefits cost consumers about \$565 million in fiscal year 1998).

<sup>4</sup> See, e.g., JOHN GRISHAM, *THE RAINMAKER* (1995) (bestselling fictional depiction of an insurance company that deliberately refused to pay claims).

<sup>5</sup> See Press Release, Ipsos Pub. Affairs, Individual Insurance Company Reputations Better Than Overall Industry (Oct. 4, 2006), available at [http://www.ipsos-na.com/news/client/act\\_dsp\\_pdf.cfm?name=mro61003-1rev.pdf&id=3206](http://www.ipsos-na.com/news/client/act_dsp_pdf.cfm?name=mro61003-1rev.pdf&id=3206) (finding that 21% of Americans hold a "favorable" opinion of the insurance industry, compared to 44% who hold an "unfavorable" opinion).

<sup>6</sup> 886 N.E.2d 127 (N.Y. 2008).

<sup>7</sup> *Id.* at 132.

<sup>8</sup> *Id.* at 128.

<sup>9</sup> *Id.* at 128–29.

<sup>10</sup> *Id.* at 129.

property, and, importantly, for up to one year of business interruption losses.<sup>11</sup>

Following the fire, Bi-Economy submitted a claim to Harleystville, which disputed the claim and advanced only \$163,161.92.<sup>12</sup> After more than a year of disputes, Bi-Economy was awarded an additional \$244,019.88.<sup>13</sup> Bi-Economy also claimed twelve months of lost business income, but Harleystville offered to pay only part of that claim.<sup>14</sup> Without insurance payments, Bi-Economy struggled to pay its debts.<sup>15</sup> After nine months, the creditors called in their loans on the business.<sup>16</sup> Bi-Economy never reopened.<sup>17</sup>

In October 2004, Bi-Economy brought suit for breach of contract.<sup>18</sup> The suit alleged that “Bi-Economy [had] suffered consequential damages arising from the complete demise of its business operation,” and moreover that this demise “was a direct and foreseeable consequence of Harleystville’s . . . wrongful conduct.”<sup>19</sup> Harleystville moved for summary judgment on the breach of contract claim.<sup>20</sup> Citing provisions of the policy that excluded “consequential losses,” Harleystville argued that these terms precluded consequential *damages*.<sup>21</sup>

The Supreme Court granted Harleystville’s motion for partial summary judgment,<sup>22</sup> and the Appellate Division affirmed.<sup>23</sup> The Appellate Division’s decision relied on *Kenford Co. v. County of Erie*,<sup>24</sup> which held that consequential damages are available only when they “have been brought within the contemplation of the parties as the

<sup>11</sup> *Id.* Business interruption losses include the total net profit or loss that would have been earned plus “[c]ontinuing normal operating expenses incurred, including payroll,” *id.* (internal quotation mark omitted), from the time of the damage to the date when the property “should be repaired, rebuilt or replaced with reasonable speed and similar quality,” *id.* (internal quotation mark omitted).

<sup>12</sup> *Id.*

<sup>13</sup> *Id.* This award was the result of binding alternative dispute resolution. *Id.*

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

<sup>15</sup> Brief for Plaintiff-Appellant at 17–18, *Bi-Econ.*, 886 N.E.2d 127 (N.Y. 2008) (No. 06-00847), 2007 WL 4938078.

<sup>16</sup> *Id.* at 30–31.

<sup>17</sup> *Bi-Econ.*, 886 N.E.2d at 129.

<sup>18</sup> See Second Amended Complaint at 21–23, *Bi-Econ. Market, Inc. v. Harleystville Ins. Co.*, No. 04-11840, 2006 WL 4758833 (N.Y. Sup. Ct. Jan. 18, 2006) (No. 04-11840), 2005 WL 5713283. Bi-Economy also sought relief via estoppel and New York insurance law. *Id.* at 21, 23–27.

<sup>19</sup> *Id.* at 22.

<sup>20</sup> *Bi-Econ.*, 886 N.E.2d at 129.

<sup>21</sup> Defendants’ Amended Answer to First Amended Complaint at 4–5, *Bi-Econ.*, No. 04-11840, 2006 WL 4758833 (N.Y. Sup. Ct. Jan. 18, 2006) (No. 04-11840), 2005 WL 5713284.

<sup>22</sup> *Bi-Econ.*, 2006 WL 4758833 (order).

<sup>23</sup> *Bi-Econ. Market, Inc. v. Harleystville Ins. Co.*, 829 N.Y.S.2d 795, 797 (App. Div. 2007) (mem.).

<sup>24</sup> 537 N.E.2d 176 (N.Y. 1989). *Kenford* essentially applied the rule from *Hadley v. Baxendale*, 94 EX. 341, 156 Eng. Rep. 145 (1854), to New York. See *Kenford*, 537 N.E.2d at 180.

probable result of a breach at the time of or prior to contracting.”<sup>25</sup> The policy terms excluding “consequential losses” were taken to show that the parties had not contemplated consequential damages.<sup>26</sup>

The Court of Appeals reversed and reinstated Bi-Economy’s cause of action.<sup>27</sup> In a decision by Judge Pigott,<sup>28</sup> the court held that consequential damages were appropriate. In accord with *Kenford*, the court stated that consequential damages would be available if they had been contemplated by the parties at the time of the contract.<sup>29</sup> The court emphasized that such damages are compensatory, not punitive.<sup>30</sup>

The court then determined that consequential damages were within the contemplation of the parties because of the nature of the obligation. Two aspects of the contract were focal points. First, the court looked at the type of policy — business interruption insurance — as relevant to whether the collapse of the business was within the contemplation of the parties. “[T]he very purpose of business interruption coverage would have made Harleysville aware that if it breached its obligations[,] . . . it would have to respond in damages to Bi-Economy for the loss of its business as a result of the breach.”<sup>31</sup> Second, the court emphasized that the contract implicitly included an obligation to investigate and pay covered claims in good faith.<sup>32</sup> The court used this good faith obligation to show that the contract was not merely a contract to pay money, but also a contract for peace of mind.<sup>33</sup> Given this characterization, the court stated that failing to award consequential damages would insufficiently compensate the non-breaching party. The damages would be needed to make Bi-Economy whole and to give it the benefit of its bargain.<sup>34</sup>

In dissent, Judge Smith<sup>35</sup> began by noting that the court had previously held that punitive damages are not ordinarily available for breach of an insurance contract.<sup>36</sup> He suggested that the majority

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<sup>25</sup> *Bi-Econ.*, 829 N.Y.S.2d at 796 (quoting *Kenford*, 537 N.E.2d at 178) (internal quotation mark omitted).

<sup>26</sup> *Id.*

<sup>27</sup> *Bi-Econ.*, 886 N.E.2d at 130.

<sup>28</sup> Judge Pigott was joined by Chief Judge Kaye and Judges Ciparick, Graffeo, and Jones.

<sup>29</sup> *Bi-Econ.*, 886 N.E.2d at 130.

<sup>30</sup> *Id.* at 131.

<sup>31</sup> *Id.* at 132.

<sup>32</sup> *Id.* at 131 (“As in all contracts, implicit in contracts of insurance is a covenant of good faith and fair dealing, such that ‘a reasonable insured would understand that the insurer promises to investigate in good faith and pay covered claims.’” (quoting *N.Y. Univ. v. Cont’l Ins. Co.*, 662 N.E.2d 763, 769 (N.Y. 1995))).

<sup>33</sup> *Id.* at 131.

<sup>34</sup> *Id.* at 131–32. Finally, the court dismissed the suggestion that the policy’s “consequential loss” provisions were related to consequential damages.

<sup>35</sup> Judge Read joined the dissent.

<sup>36</sup> *Bi-Econ.*, 886 N.E.2d at 133 (Smith, J., dissenting) (citing *N.Y. Univ.*, 662 N.E.2d 763; *Rocanova v. Equitable Life Assurance Soc’y of U.S.*, 634 N.E.2d 940 (N.Y. 1994)).

opinion tacitly overturned these holdings: “The ‘consequential’ damages authorized by the majority, though remedial in form, are obviously punitive in fact.”<sup>37</sup> Judge Smith also rejected the court’s appeal to the covenant of good faith and fair dealing. In his view, a covenant of good faith is applicable when “a party has complied with the literal terms of the contract, but has done so in a way that undermines the purpose of the contract and deprives the other party of the benefit of the bargain.”<sup>38</sup> Here the literal terms of the contract were breached, so there was “no need” to resort to the covenant of good faith.<sup>39</sup> As a result, the appeal to good faith served only to “obscur[e] the fact that the predicate for ‘consequential’ damages here is exactly the same conduct, bad faith failure to pay claims, that [the court had previously] refused to make a predicate for punitive damages.”<sup>40</sup>

On its face, the *Bi-Economy* decision purports to be a straightforward application of the contract law rule for consequential damages. Any expanded liability for insurers is, however, a major shift in New York, a state with generally insurer-friendly liability laws.<sup>41</sup> The temptation, therefore, is to read the decision narrowly. There are two potential narrow readings. First, one might suggest that the decision rests on the unique role of business interruption insurance.<sup>42</sup> This possibility, however, is substantially undermined by the Court of Appeals’s decision on the same day allowing consequential damages in a companion case that did not involve business interruption insurance.<sup>43</sup>

The more natural way to narrow the *Bi-Economy* decision is by viewing it as restricted to cases of bad faith. A number of courts<sup>44</sup> and

<sup>37</sup> *Id.*

<sup>38</sup> *Id.* at 134.

<sup>39</sup> *Id.*

<sup>40</sup> *Id.* Judge Smith also noted his opposition to punitive damages. *Id.* at 133.

<sup>41</sup> See, e.g., Jeffrey Stempel, *Stempel on N.Y. Embraces Consequential Damages in Bad Faith Claims*, 2008 EMERGING ISSUES 191, at \*1 (Mar. 27, 2008) (describing the New York Court of Appeals as “normally a court embraced by insurers” and noting that “New York law is frequently the choice of insurers in drafting dispute resolution and choice-of-law clauses in policies”).

<sup>42</sup> This was the interpretation offered by one attorney who had submitted an amicus brief on behalf of insurers. “We are disappointed that the Court has opened a narrow window for a claim of extra contractual damages against insurers . . . . However, that window is apparently limited to business-interruption coverage because of its unique purposes.” Joel Stashenko, *N.Y. High Court Approves Consequential Damages Claims Against Insurers*, N.Y. L.J., Feb. 20, 2008, available at <http://www.law.com/jsp/article.jsp?id=1203430083933> (quoting Evan H. Krinick).

<sup>43</sup> See *Panasia Estates, Inc. v. Hudson Ins. Co.*, 886 N.E.2d 135 (N.Y. 2008). *Panasia* involved builders’ risk insurance, which shares no obvious similarity with business interruption insurance. The dissent in *Bi-Economy* noted that *Panasia* shows that the potential liability is not limited to business interruption insurance. See *Bi-Econ.*, 886 N.E.2d at 134–35 (Smith, J., dissenting).

<sup>44</sup> See *Silverman v. State Farm Fire & Cas. Co.*, No. 7699/08, slip op. at 5 (N.Y. Sup. Ct. Oct. 8, 2008) (“[C]iting recent decisions of the Court of Appeals, [plaintiffs] contend that they may sue for consequential damages resulting from the failure to provide coverage. Such a failure may indeed support such a claim if it flows from a breach of the covenant of good faith and fair dealing, which the courts will read into all insurance contracts.”); see also *U.S. Fire Ins. Co. v. Bunge N.*

commentators<sup>45</sup> have adopted this interpretation. The dissent also clearly understood the holding to be limited to cases of bad faith breach.<sup>46</sup> Moreover, there is language in the opinion that suggests this interpretation.<sup>47</sup> Reading the decision as relying on bad faith, however, is inconsistent with both the compensatory and contract law emphases in the opinion. Because the decision cannot be limited to bad faith in a conceptually consistent way, *Bi-Economy* should be understood as more broadly chipping away at the traditional contract law limitation on consequential damages.

First, limiting consequential damages to bad faith breach is incompatible with the compensatory approach in *Bi-Economy*. According to the compensatory rationale, consequential damages are awarded insofar as they restore the victim to her pre-breach position. According to the bad faith reading, in contrast, consequential damages are awarded in response to the bad faith of the insurer. The tension between these two views mirrors a general divide among courts over how to treat insurer malfeasance — as extracontractual or as contractual.<sup>48</sup>

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Am., Inc., No. 05-2192-JWL, 2008 U.S. Dist. LEXIS 59737, at \*60 (D. Kan. Aug. 4, 2008) (deciding that under *Bi-Economy*, plaintiff was not precluded from “pursu[ing] a claim for consequential damages based on the allegation (litigated within the context of its primary breach-of-contract claim) that [the insurer] breached its implied duty of good faith and fair dealing”).

<sup>45</sup> See, e.g., William T. Barker, Justin N. Kattan & Rachel G. Balaban, *Sonnenschein Nath & Rosenthal LLP on Bad-Faith Claims in New York Following Bi-Economy Market, Inc. v. Harleysville Insurance Co. and Panasia Estates, Inc. v. Hudson Insurance Co.*, 2008 EMERGING ISSUES 266 (June 9, 2008) (“Based on these decisions, it appears that consequential damages will often, perhaps always, be recoverable if they result from failure to evaluate a claim in good faith . . . .”); Jeffrey L. Kingsley & Mark B. Seiger, *Panasia Estates v. Hudson Insurance Company and Bi-Economy Market v. Harleysville: New York’s New Standard with Respect to First-Party Bad Faith Claims*, LEXISNEXIS EXPERT COMMENTARY, Apr. 2008 (reading *Bi-Economy* as saying “consequential damages are allowable in a first-party bad faith claim”); Posting of Jim Reed to NYInjuryLawBlog.com, <http://www.zifflaw.com/NYInjuryLawBlog/insurance-companies-are-now-liable-for-bad-faith-in-ny> (Feb. 23, 2008, 06:36). But see Peter N. Flocos, *New York Court of Appeals Holds that Policyholders May Recover Consequential Damages Arising From Insurers’ Bad Faith Conduct*, K&L GATES NEWSSTAND, Feb. 28, 2008, <http://www.klgates.com/newsstand/Detail.aspx?publication=4354> (“It is not clear from the discussion in *Bi-Economy* and *Panasia* whether policyholder consequential damages claims are limited *exclusively* to cases of ‘bad faith’ insurer conduct . . . .”).

<sup>46</sup> See *Bi-Econ.*, 886 N.E.2d at 133 (Smith, J., dissenting) (“The ‘consequential’ damages authorized by the majority, though remedial in form, are obviously punitive in fact. They are not triggered, as true consequential damages are, simply by a breach of contract, but only by a breach committed in bad faith.”).

<sup>47</sup> See *id.* at 132 (majority opinion) (“[I]f it breached its obligations under the contract to investigate in good faith and pay covered claims it would have to respond in damages to Bi-Economy for the loss of its business as a result of the breach.”); *id.* (“[I]n light of . . . Bi-Economy’s allegations that Harleysville breached its duty to act in good faith, we hold that Bi-Economy’s claim for consequential damages . . . cannot be dismissed on summary judgment.”).

<sup>48</sup> Courts have adopted both tort and contract approaches to bad faith insurance breach. First, many courts have determined that bad faith insurance breach itself constitutes a tort action. See, e.g., *Noble v. Nat’l Am. Life Ins. Co.*, 624 P.2d 866 (Ariz. 1981) (en banc); *Seaman’s Direct Buying Serv., Inc. v. Standard Oil Co.*, 686 P.2d 1158 (Cal. 1984) (per curiam); *Travelers Ins. Co.*

The incompatibility between the bad faith limitation and the compensatory approach arises because compensation is an independently sufficient justification for the damages, rendering the rationale of bad faith unnecessary. When focusing on compensation, there is no reason to believe that bad faith breach produces consequential injuries different from those produced by good faith breach. An insurer might make a good faith effort to fulfill its contractual obligations and yet still fail to do so — through negligence, incompetence, or bad luck. But the good faith of the insurer will be little consolation to the insured, who will not receive the coverage that she was owed,<sup>49</sup> and who might suffer the same repercussions as Bi-Economy. It is the breach of contract that causes the need for compensation, not the breach of good faith.

Second, interpreting *Bi-Economy* as relying on a contractual obligation of good faith is conceptually confused. On such a reading, the covenant of good faith imposes a duty to “pay covered claims.”<sup>50</sup> That is, the covenant is used to imply an additional duty to perform the contractual obligations.<sup>51</sup> It is not clear, however, how the covenant could add anything to the obligation already acquired through the contract. It is as though saying “and I promise to keep my promise” can add something to the original promise. Such an addition would be empty.<sup>52</sup> If Harleysville promised to pay Bi-Economy for twelve

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v. Savio, 706 P.2d 1258 (Colo. 1985); *Erie Ins. Co. v. Hickman*, 622 N.E.2d 515 (Ind. 1993); *Arnold v. Nat'l County Mut. Fire Ins. Co.*, 725 S.W.2d 165 (Tex. 1987). *But see, e.g.*, *Haagenson v. Nat'l Farmers Union Prop. & Cas. Co.*, 277 N.W.2d 648 (Minn. 1979) (en banc). Other decisions, in contrast, have confined bad faith breach to a contract action but have awarded consequential damages nonetheless. *See, e.g.*, *A & E Supply Co. v. Nationwide Mut. Fire Ins. Co.*, 798 F.2d 669 (4th Cir. 1986) (applying Virginia law); *Reichert v. Gen. Ins. Co. of Am.*, 428 P.2d 860 (Cal. 1967), *vacated on other grounds*, 442 P.2d 377 (Cal. 1968); *Olson v. Rugloski*, 277 N.W.2d 385 (Minn. 1979) (en banc); *Lawton v. Great Sw. Fire Ins. Co.*, 392 A.2d 576 (N.H. 1978).

<sup>49</sup> Arguably, the victim of bad faith breach might suffer emotional damages not suffered by the victim of good faith breach. *Cf.* Ronnie Cohen & Shannon O'Byrne, *Cry Me a River: Recovery of Mental Distress Damages in a Breach of Contract Action — A North American Perspective*, 42 AM. BUS. L.J. 97, 101 (2005) (arguing that “recovery for mental distress damages [should] follow ordinary principles of contract law instead of being relegated to an exception-based approach”).

<sup>50</sup> *Bi-Econ.*, 886 N.E.2d at 132. The majority referred three times to good faith creating a duty to pay claims, suggesting that the court itself may be confusing matters. *See id.* at 131–32.

<sup>51</sup> This is in contrast to cases in which the covenant of good faith and fair dealing is used to imply obligations that are not strictly within the terms of the contract but are within the contract's spirit. *See* STEVEN J. BURTON & ERIC G. ANDERSEN, *CONTRACTUAL GOOD FAITH: FORMATION, PERFORMANCE, BREACH, ENFORCEMENT* 392 (1995) (noting that judges have departed from the “mainstream approach” when questions of good and bad faith are considered “in the area of insurance contracts”).

<sup>52</sup> *Cf.* Charles Fried, *The Convergence of Contract and Promise*, 120 HARV. L. REV. F. 1, 7 (2007). Professor Charles Fried admits that he is “in trouble” in attempting to explain why “a contract/promise that explicitly provides for specific performance in the event of breach” would still be given only expectation damages. *Id.* But he does not offer a satisfying explanation of the problem. The reason Professor Fried finds himself in trouble, it seems, is because saying “I promise” already creates the obligation to perform, so making additional promises to perform cannot add anything further.

months of business losses, one need not appeal to some other implied promise in order to explain Harleysville's obligations.<sup>53</sup> Moreover, this way of conceiving matters introduces an obvious regress. If good faith is simply an implied agreement, one can then ask what explains the obligation to perform this agreement to act in good faith. In essence, one cannot explain what is wrong with deliberately breaking a contract by appealing to a further contractual obligation.

Finally, the duty of good faith does not behave like a contractual term. If the duty of good faith were an implicit agreement between the parties, then it could be explicitly disavowed by a contractual provision.<sup>54</sup> But unlike other implied terms, the implied covenant of good faith is necessarily present in all contracts.<sup>55</sup> Good faith is not a particular term of an agreement, but rather it is a precondition to agreement itself. As such, to violate good faith is not to violate an agreement, but to violate an extracontractual obligation. The bad faith approach may thus be better conceived as tort liability imposed through a legal fiction.<sup>56</sup> It should be no surprise, therefore, that it is incompatible with the compensatory approach, which is contractual.

All this suggests giving up the idea that bad faith is necessary to the *Bi-Economy* holding. Instead, one should take seriously the court's compensatory rationale: consequential damages are available if they are necessary to restore a victim of breach of contract.<sup>57</sup> The difficulty with this interpretation is the rule from *Hadley v. Baxendale*,<sup>58</sup> according to which a non-breaching party may only recover losses that

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<sup>53</sup> The court stated that "this insurance contract included an additional performance-based component: the insurer agreed to evaluate a claim, and to do so honestly, adequately, and — most importantly — promptly." *Bi-Econ.*, 886 N.E.2d at 132. But these are not "additional" obligations — they are part of the basic contractual obligation. Any agreement to pay creates an obligation to pay honestly, adequately, and at the designated time.

<sup>54</sup> RESTATEMENT (SECOND) OF CONTRACTS § 204 (1981) (A term is "supplied by the court" when the parties "have not agreed with respect to a term.").

<sup>55</sup> *Id.* § 205 ("Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement.").

<sup>56</sup> See Michael H. Cohen, Comment, *Reconstructing Breach of the Implied Covenant of Good Faith and Fair Dealing as a Tort*, 73 CAL. L. REV. 1291 (1985). There is some suggestion that punishing bad faith breach through punitive damages in tort is less efficient than using compensatory measures. See Linda Curtis, Note, *Damage Measurements for Bad Faith Breach of Contract: An Economic Analysis*, 39 STAN. L. REV. 161, 163 (1986); see also Roger C. Henderson, *The Tort of Bad Faith in First-Party Insurance Transactions After Two Decades*, 37 ARIZ. L. REV. 1153, 1182 (1995) ("In practically every lawsuit that is filed against an insurer providing first-party benefits there is a count seeking consequential and punitive damages . . ."); Alan O. Sykes, "Bad Faith" Breach of Contract by First-Party Insurers, 25 J. LEGAL STUD. 405, 431-43 (1996) (suggesting that "courts can carry the doctrine too far"). This comment makes no attempt to evaluate the policy choice between punitive damages in tort and expanded compensatory damages in contract.

<sup>57</sup> *Bi-Econ.*, 886 N.E.2d at 131-32.

<sup>58</sup> 94 EX. 341, 156 Eng. Rep. 145 (1854).

were within the contemplation of the parties at the time of contract.<sup>59</sup> As a faithful application of the traditional *Hadley* rule, the *Bi-Economy* decision is unconvincing.<sup>60</sup> But the decision aligns with our moral sense that Harleysville is accountable for the results of its breach.<sup>61</sup> In a sense, the court is simply stating that Harleysville is liable for the consequential damages because they were caused by its breach. The *Hadley* rule merely limits damages to those that were caused by the breach and not by some other twist of fate.<sup>62</sup> If this is right, then *Bi-Economy* is a shift away from rigid *Hadley* restrictions, and toward more compensatory contractual remedies.

Understandably, courts increasingly seek to offer remedies for the innocent losses that result from insurers' bad faith delays and refusals to pay. The *Bi-Economy* decision is undoubtedly an expansion of New York law. The compensatory and contractual emphases of the decision, however, suggest that the opinion is more an expansion of general contract remedies than an expansion limited to insurer bad faith.

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<sup>59</sup> *Id.* at 354, 156 Eng. Rep. at 151 (“[Contract damages] should be such as may fairly and reasonably be considered either arising . . . according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it.”).

<sup>60</sup> The dissent made this point somewhat sarcastically: “Can anyone seriously believe that the parties in these cases would, if they had ‘considered the subject,’ have contracted for the results reached here?” *Bi-Econ.*, 886 N.E.2d at 134 (Smith, J., dissenting). If the test is truly what liability the parties contemplated at the time, then Judge Smith’s criticism is quite reasonable.

<sup>61</sup> *Cf.* Seana Valentine Shiffrin, *The Divergence of Contract and Promise*, 120 HARV. L. REV. 708, 724 (2007) (noting that the *Hadley* rule is a departure from our moral perspective). Although Shiffrin is defending the divergence of contract and morality, the temptation to shift away from the *Hadley* rule is a temptation to bring contract law back into convergence with morality.

<sup>62</sup> Reading the *Hadley* rule as a causal limitation is not outlandish. First, *Hadley* itself is ambiguous. *See, e.g.*, Roy Ryden Anderson, *Incidental and Consequential Damages*, 7 J.L. & COM. 327, 353 (1987) (“What is so often overlooked about the *Hadley v. Baxendale* standard is that we were never meant to understand its precise meaning.”). Second, *Hadley* used a number of causal terms in describing consequential damages: they are a “probable result” of breach, they “ordinarily follow” from breach, and they occur in the “great multitude of cases.” *Hadley*, 94 Ex. at 354–55, 156 Eng. Rep. at 151. Third, some courts already interpret *Hadley*’s standard as concerning not what was in fact contemplated, but rather what would have been foreseeable. *See, e.g.*, Caspe v. Aacon Auto Transp., Inc., 658 F.2d 613, 617 (8th Cir. 1981) (“[Plaintiff] need only demonstrate that his harm was not so remote as to make it unforeseeable to a reasonable man at the time of contracting.” (quoting *Hector Martinez & Co. v. S. Pac. Transp. Co.*, 606 F.2d 106, 110 (5th Cir. 1979))); *see also* *Sun Maid Raisin Growers v. Victor Packing Co.*, 194 Cal. Rptr. 612, 616 (Cal. Ct. App. 1983). Finally, some authors have suggested the need to revise the *Hadley* rule. *See, e.g.*, Thomas A. Diamond & Howard Foss, *Consequential Damages for Commercial Loss: An Alternative to Hadley v. Baxendale*, 63 FORDHAM L. REV. 665, 692–93 (1994).