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Legal Reasoning and Wrongful Discharge Tort Law in California

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INTRODUCTION

Millions of workers serve under contracts which express nothing about the right of either employee or employer to leave the employment relationship. For many years, the doctrine of "employment-at-will" permitted an employer to discharge any employee at his pleasure. In 1980, in *Tameny v. Atlantic Richfield Co.*, the California Supreme Court held that a discharge in violation of public policy is a tort.[1] Since then, an explosion in wrongful discharge tort litigation has occurred.

Several courts of appeal subsequently recognized a second wrongful discharge tort. These courts held that a termination is tortious where the employer has breached the covenant of good faith and fair dealing which inheres in every contract.[2] On December 29, 1988, in a landmark decision, *Foley v. Interactive Data Corp.*,[3] the California Supreme Court held that a tort action is not available when the employer discharges an employee in bad faith.

This article places wrongful discharge tort law within a larger context. Many distinguished legal commentators have criticized what they call the "formal" style of legal reasoning. These commentators have recognized an alternative style of legal reasoning: instrumentalism. This article examines the influence of formal and instrumental thinking on wrongful discharge tort cases in California.

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1. Tameny v. Atlantic Richfield Co., 27 Cal. 3d 167, 164 Cal. Rptr. 839 (1980).

2. In this article, the covenant of good faith and fair dealing is referred to as "the covenant." A breach of the covenant is referred to as "bad faith."

3. Foley v. Interactive Data Corp., 47 Cal. 3d 654, 254 Cal. Rptr. 211 (1988). In Newman v. Emerson Radio Corp., 89 Daily Journal D.A.R. 6755 (May 25, 1989), the court held that the *Foley* decision applied retroactively to all cases pending on January 30, 1989.

I. THE EMPLOYMENT-AT-WILL DOCTRINE

The doctrine of employment-at-will holds that where the parties do not expressly agree to the contrary, either the employer or the employee may terminate the contract at any time.[4] California enacted an at-will statute in 1872, and the rule remained firmly entrenched for almost a century.[5] The only significant judicially-created exception to the rule came in 1959, when an appellate court held that an employee's discharge may not violate considerations of public policy.[6]

In 1980 and 1981, a trilogy of decisions transformed wrongful discharge law in California.[7] First, the California Supreme Court held that a cause of action sounding in tort lies whenever an employee is terminated in violation of public policy.[8] Justice Tobriner, writing for the majority in *Tameny v. Atlantic Richfield Co.*, also suggested that, in certain instances, a dismissal might be a tortious breach of the covenant of good faith and fair dealing.[9] Several months later in *Cleary v. American Airlines*, a court of appeal followed Tobriner's suggestion and allowed a discharged employee to state a bad faith cause of action for breach of the covenant.[10] Finally, in *Pugh v. See's Candies*, another court of appeal held that the presumption of employment-at-will may be overcome to prove a breach of contract.[11] Under *Pugh*, an implied contractual promise to dismiss only for good cause may be proven by the plaintiff. The implied promise is identified by examining the totality of the relationship between the parties.[12]

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4. Blades, *Employment At Will vs. Industrial Freedom: On Limiting the Abusive Exercise of Employer Power*, 67 COLUM. L. REV. 1404, 1416-19 (1967); Feinman, *The Development of the Employment At Will Rule*, 20 AM. J. LEGAL HIST. 118 (1976); Note, *Protecting At Will Employees Against Wrongful Discharge: The Duty to Terminate Only in Good Faith*, 96 HARV. L. REV. 1816, 1824-28 (1980).

5. CAL. CIV. CODE § 51999.9 (1872). The statute provided: "An employment having no specified term may be terminated at the will of either party, on notice to the other, except where otherwise provided by this title." The statute now appears at CAL LAB. CODE § 2922 (West 1971). Swaffield v. Universal Esco Corp., 271 Cal. App. 2d 147, 76 Cal. Rptr. 680 (1969); Wilson v. Red Bluff Daily News, 237 Cal. App. 2d 87, 46 Cal. Rptr. 591 (1965); Lynch v. Gagnon, 96 Cal. App. 512, 274 P. 584 (1929).

6. Petermann v. International Bhd. of Teamsters, 174 Cal. App. 2d 184, 344 P.2d 25 (1959). For a discussion of this case, *see infra* notes 61-63 and accompanying text.

7. Miller & Estes, *Recent Judicial Limitations On The Right To Discharge: A California Trilogy*, 16 U.C.D. L. REV. 65 (1982).

8. Tameny v. Atlantic Richfield Co., 27 Cal. 3d 167, 164 Cal. Rptr. 211 (1980).

9. *Id.* at 179, n.12, 164 Cal. Rptr. at 846.

10. Cleary v. American Airlines, 111 Cal. App. 3d 443, 168 Cal. Rptr. 722 (1980).

11. Pugh v. See's Candies, Inc., 116 Cal. App. 3d 311, 171 Cal. Rptr. 917 (1980) ("Pugh I"). In *Pugh*, the employer summarily discharged an at-will employee after he criticized the company's new collective bargaining agreement as a "sweetheart contract." During his 32 years with the company, the employee had risen from dishwasher to vice president in charge of production. There had been no written criticism of his work.

12. *Id.* at 326-27, 329-30, 171 Cal. Rptr. 925-28. On retrial, the jury returned a

Since 1980, wrongful discharge lawsuits have proliferated in California.[13] Preventive measures by legal counsel to minimize employers' liability has led to the emergence of what one frustrated judge has termed "the disemployment industry."[14] Many terminated employees have won substantial damage awards from sympathetic juries.[15] Numerous appellate decisions have sought to clarify the tort duties imposed on employers.[16] Most recently, in *Foley v. Interactive Data Corp.*, the California Supreme Court declared that an employer's breach of the implied covenant is not a

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general verdict for the employer. Pugh v. See's Candies, Inc., 203 Cal. App. 3d 743, 250 Cal. Rptr. 195 (1988).

13. Sacramento Daily Recorder, July 19, 1988, at 1, col. 2 (reporting estimate by Stanford labor law professor William B. Gould IV, that one wrongful termination is filed in the California courts each day). Other commentators have estimated that, throughout the nation, several hundred thousand American employees are wrongfully terminated each year. Peck, *Book Review*, 8 IND. REL. L.J. 263, 264 (1986).

14. Cox v. Resilient Flooring Div., 638 F. Supp. 726, 735 (C.C.D. Cal. 1986).

15. A survey of California trials during the period 1979-87 illustrates the economic impact of the new tort. For public policy cases, the median award to employees has been $265,000, while the average award was $512,000. When cases won by employers are included, the average award to employees was still $280,000. For bad faith cases, the median award to ,employees was $142,000 and the average award was $540,000. When bad faith cases won by employers are included, the average award to employees was $314,000. The awards for contract cases were much lower: $60,000 (median), $127,000 (average), $78,000 (including cases won by employers). Jung & Harkness, *The Facts of Wrongful Discharge, Los Angeles Daily Journal Report*, Nov. 20, 1987, at 1, col. 1. This article summarizes a study by the Rand Corporation.

16. The California Supreme Court has granted petitions for review in 11 pending wrongful discharge cases. The cases are: Welch v. Metro Goldwyn-Mayer Film Co. (S.008779, hg. granted March 2, 1989) 207 Cal. App. 3d 164, 254 Cal. Rptr. 645 (appropriate measure of damages in a wrongful discharge action based on breach of an employment contract; allegation that employer is liable in tort for conspiring to induce breach of employment contract); Chapman v. Research Industries, Inc. (S.003669, hg. granted Feb. 25, 1988) (allegation that employer breached implied covenant of good faith and fair dealing); Movie Company Enterprises v. V.S.C. Enterprises, Inc. (SO03414, hg. granted Feb. 25, 1988) (allegation that federal labor law preempts common law action for breach of the covenant); LaGoe v. Duber Industrial Security, Inc. (9000735, hg. granted Nov. 2, 1987), 194 Cal. App. 3d 349, 239 Cal. Rptr. 445 (allegation that wrongful discharge claim is defeated when employer has good faith belief that there is good cause to terminate); Conover v. Oracle Corporation (S001064, hg. granted July 16, 1987) (allegation that employer negligently misrepresented job opportunity to job applicant who was later terminated); Koire v. City of Los Angeles (S000735, hg. granted June 25, 1987) (allegation that denial of a promotion breaches the covenant of good faith and fair dealing); Litwack v. Fedmart Corporation (S000241, hg. granted May 14, 1987) (allegation that there is no breach of the covenant when the employer acts in good faith, based on probable cause); Ketchu v. Sears Roebuck and Company (S.F.25119, hg. granted Feb. 5, 1987) (allegation that wrongful discharge claim is defeated when employer has good faith, albeit mistaken, belief that there is cause to terminate); Newman v. Guardian Title Company (L.A.32263, hg. granted Oct. 30, 1986) (appropriate measure of damages in a wrongful discharge action); Miller v. Indasco, Inc. (L.A.32204, hg. granted June 20, 1986) 178 Cal. App. 3d 296, 223 Cal. Rptr. 551 (allegation that wrongful discharge action is barred by statute of limitations); Santa Maria Hospital v. Superior Court (L.A.32143, hg. granted Jan. 16, 1989) 172 Cal. App. 3d 698, 218 Cal. Rptr. 543 (allegation of intentional infliction of emotional distress).

tort.[17]

The *Foley* decision, while seminal, nonetheless left many important issues unresolved. The definition of public policy must be decided in future cases.[18] The full range of possible contractual damages for a wrongful discharge has yet to be fully explored.[19] The court must also determine the appropriate statute of limitations to apply to wrongful discharge contract actions,[20] and has yet to consider other, collateral tort actions arising out of employment termination.[21] Finally, in response to language in *Foley* emphasizing that the future of employment-at-will is a matter best left to the Legislature, several bills have been introduced in that body. These legislative proposals would significantly alter the law of employment termination in California.[22]

II. STYLES OF LEGAL REASONING

Legal historians and theorists have identified two influential, and contradictory, styles of legal reasoning. One style is universally known as formalism. The other style has been variously identified as sociological jurisprudence, realism, the Grand Style, purposive reasoning, or instrumentalism. In this article, the second style is referred to as instrumentalism. Both styles of reasoning are represented in the debate in the courts over the public policy exception to the doctrine of employment-at-will.

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17. Foley v. Interactive Data Corp., 47 Cal. 3d 654, 254 Cal. Rptr. 211 (1988).

18. *Id.* at 669, 254 Cal. Rptr. at 217 ("We do not decide in this case whether a tort action alleging a breach of public policy under *Tameny* may be based only on policies derived from a statute or constitutional provision or whether nonlegislative sources may provide the basis for the claim").

19. For a discussion of the damages issues in breach of contract cases, *see* Traynor, *Bad Faith Breach of a Commercial Contract: A Comment on the Seaman's Case*, 8 BUS. L. NEWS 1, 12-13 (1984) (advocating contract-based compensatory damages as an alternative to tort damages); Mandelbaum, *Wrongful Discharge Cases After 'Foley': More Sophisticated Approach to Contract Damages Expected*, Los Angeles Daily Journal Report, May 19, 1989, at 8, 9.

20. There is a two-year statute of limitations for breaches of oral contracts. CAL. CIV. PROC. CODE § 339 (West 1982).

21. Other tort actions might include defamation, interference with contractual relations, and infliction of emotional distress (both negligent and intentional).

22. *Capitol Reacts to Foley With Flurry of Bills*, Los Angeles Daily Journal, Jan. 20, 1989, at 1, col. 6. The bills which have been introduced by legislators are: Sen. Bill No. 282 (1989-1990 Reg. Sess.) (employee may be discharged only for "just cause"; employee may contest his dismissal in mandatory binding arbitration); Sen. Bill. No. 222 (1989-1990 Reg. Sess.) (employer cannot terminate, absent a legitimate business reason, if employee has served specified period and earns specified minimum salary); Sen. Bill No. 181 (1989-1990 Reg. Sess.) (employee may bring tort action if employer breaches the implied covenant; legislatively overrules the Foley decision); Sen. Bill No. 115 (1989-1990 Reg. Sess.) (prohibits employer from requiring employee to sign express at-will termination clause).

A. Formalism and Instrumentalism

A concise statement of the distinction between formalism and instrumentalism[23] has been offered by Roberto Mangabeira Unger.[24] Unger stated that "[l]egal reasoning is formalistic when the mere invocation of rules and the deduction of conclusions from them is believed sufficient for every legal choice."[25] Unger also identified an alternative style, purposive reasoning, which can be equated with instrumentalism. Legal reasoning is instrumental "when the decision about how to apply a rule depends on a judgment of how most effectively to achieve the purposes ascribed to the rule."[26]

In the United States, formalism has often been associated with doctrines invoking a dichotomy between public and private activity.[27] The two activities were perceived as radically distinct. In the private sphere, governmental regulation was illegitimate. In the other sphere—the public sphere—governmental intrusion was appropriate. Courts were charged with the task of identifying the boundaries between the public and private spheres of activity. The fusion of formalism with the concept of the public-private dichotomy has been identified by some theorists as the "classical" style

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23. Influential discussions of the formal-instrumental dichotomy include: M. HORWITZ, THE TRANSFORMATION OF AMERICAN LAW, 1780-1860 (1977); K. LLEWELLYN, THE COMMON LAW TRADITION: DECIDING APPEALS (1960); Kennedy, *Form and Substance in Private Law Adjudication*, 89 HARV. L. REV. 1685 (1976) [hereinafter Kennedy, *Form and Substance*]; Nelson, *The Impact of the Antislavery Movement Upon Styles of Judicial Reasoning in Nineteenth Century America*, 87 HARV. L. REV. 513 (1974).

24. R. UNGER, LAW IN MODERN SOCIETY: TOWARD A CRITICISM OF SOCIAL THEORY 194-216 (1976).

25. *Id.* at 194. *See also* P. ATIYAH, THE RISE AND FALL OF FREEDOM OF CONTRACT 388 (1979). Atiyah states:

> Formalism really represents an attitude of mind rather than anything else; the attitude is that of the judge who believes that all law is based on legal doctrine and principles which can be deducted from precedents; that there is only one 'correct' way of deciding a case; that it is not the function of the judge to invoke policy considerations, or even arguments about the relative justice of the parties' claims; that the reasons behind principles and rules are irrelevant; that the role of the judge is purely passive and interpretive; that law is a science of principles, and so on.

Id. A classic illustration of the formalist mentality appears in Justice Owen Roberts' opinion in U.S. v. Butler, 297 U.S. 1, 62, 56 S. Ct. 312, 318 (1936). Roberts stated that the judge has "only one duty—to lay the article of the Constitution which is invoked beside the statute which is challenged and to determine whether the latter squares with the former." One historian has called this the "slot machine theory of constitutional interpretation." A. SCHLESINGER, THE POLITICS OF UPHEAVAL 458 (1960).

26. R. UNGER, *supra* note 24, at 194, n.24.

27. E. Mensch, *The History of Mainstream Legal Thought*, in THE POLITICS OF LAW: A PROGRESSIVE CRITIQUE 23-29 (D. Kairys ed. 1982); Kennedy, *Form and Substance*, *supra* note 23, at 1728-40; Kennedy, *Toward an Historical Understanding of Legal Consciousness: The Case of Classical Legal Thought in America, 1850-1940*, in 3 RESEARCH IN LAW AND SOCIETY 3 (1980).

of legal thought.[28] In this article, references to formalism also refer to the classical style.

A key element in academic legal thought during the past century has been a "revolt against formalism."[29] It is often said that formalism dominated judicial opinion writing during the late nineteenth century.[30] As successive waves of critics attacked formalism, the other style of legal reasoning, instrumentalism, emerged as the anti-formal alternative.[31]

Two of the earliest participants in the revolt against formalism were Oliver Wendell Holmes, Jr. and Roscoe Pound. By 1905, in a celebrated series of articles and opinions, Holmes had staked out his position: "General propositions do not decide concrete cases."[32] He urged that judges should take into account such considerations as history, social context, and the functional purposes of legal rules.[33] Pound, the long-time dean of the Harvard Law School, adopted a similar approach, which he called "sociological jurisprudence."[34] By 1908, Pound had attacked "mechanical jurisprudence" and had stated that legal principles should be studied to evaluate "their social operation and the effects which they produce."[35]

The full-scale assault on formalism came with the advent of realism, in the 1920s and 1930s.[36] The realists were (primarily) a

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28. Kennedy, *Form and Substance, supra* note 23, at 1724-40; E. MENSCH, *supra* note 27, at 23-29.

29. The phrase was coined by the intellectual historian Morton White. M. WHITE, THE REVOLT AGAINST FORMALISM (1949). White referred to general developments in the history of American ideas. *See also* E. PURCELL, THE CRISIS OF DEMOCRATIC THEORY: SCIENTIFIC NATURALISM AND THE PROBLEM OF VALUE (1975); W. TWINING, KARL LLEWELLYN AND THE REALIST MOVEMENT 3-83 (1973); Mensch, *supra* note 23, 26-29; White, *From Sociological Jurisprudence to Legal Realism: Jurisprudence and Social Change in Early Twentieth Century America*, 58 VA. L. REV. 999 (1972); Note, *'Round and 'Round the Bramble Bush: From Legal Realism to Critical Legal Scholarship*, 95 HARV. L. REV. 1669 (1982).

30. M. HORWITZ, *supra* note 23; Nelson, *supra* note 23; *Contra*, Scheiber, *Instrumentalism and Property Rights: A Reconsideration of American "Styles of Judicial Reasoning" in the 19th Century*, WIS. L. REV. 1, 8 (1975) ("If the picture was thus a mixed one in the 1820-50 period—with 'instrumentalist' judges often invoking formalistic doctrine, and doctrinaire critics adducing instrumental arguments—it was also so in the late nineteenth century").

31. W. TWINING, *supra* note 29, at 3-83.

32. Lochner v. New York, 193 U.S. 45, 76, 25 S. Ct. 349 (1905) (Holmes, J., dissenting).

33. Holmes, *Privilege, Malice, and Intent*, 8 HARV L. REV. 1 (1984); Holmes, *The Path of the Law*, 10 HARV. L. REV. 457 (1897).

34. Pound, *The Scope and Purpose of Sociological Jurisprudence*, 25 HARV. L. REV. 389, 514 (1912).

35. *Id. See also* Pound, *Mechanical Jurisprudence*, 8 COLUM. L. REV. 605, 609 (1908) ("The sociological movement in jurisprudence is a movement for pragmatism as a philosophy of law.")

36. W. TWINING, *supra* note 29, at 375-87; Kennedy, *Form and Substance, supra*

group of eastern law professors. The realists disagreed on many things, but were united in their opposition to formalism. They denied that abstract general principles could invariably be invoked "logically" to decide specific cases. The realists emphasized the importance of social context and the functional purposes served by law. They vigorously disputed the classical belief that a meaningful boundary can be drawn between public and private activity. The realists also argued that judges, like legislators, make public policy.

In 1960, two decades after the heyday of realism, a prominent realist, Karl Llewellyn, published *The Common Law Tradition*, a study of appellate judicial work.[37] Llewellyn discussed the phenomenon of judicial style:

> It is the general and pervasive manner over the country at large, at any given time, of going about the job, the general outlook, the ways of professional knowhow, the kind of thing the men of law are sensitive to and strive for, the tone and flavor of the working and of the results. It is well described as a 'period-style'; it corresponds to what we have long known as period-style in architecture or the graphic arts or furniture or music or drama. Its slowish movement but striking presence remind me also of shifting 'types' of economy ('agricultural', 'industrial', e.g.) and of the cycles or spirals many sociologists and historians discover in the history of political aggregations or of whole cultures.[38]

Llewellyn distinguished what he called the Formal Style from the Grand Style. According to Llewellyn, the hallmarks of the Grand Style are that:

> '[P]recedent' is carefully regarded, but if it does not make sense it is ordinarily re-explored; 'policy' is explicitly inquired into; alleged 'principle' must make for wisdom as well as for order if it is to qualify as such, but when so qualified it acquires peculiar status. On the side both of case-law and of statutes, where the reason stops there stops the rule; and in working with statutes it is the normal business of the court not only to read the statute but also to implement that statute in accordance with purpose and reason.[39]

The Formal Style is quite different:

> The rules of law are to decide the cases; policy is for the legislature, not for the courts, and so is change even in pure common

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note 23, at 1731-33; Note, *'Round and 'Round the Bramble Bush: From Legal Realism to Critical Legal Scholarship*, *supra* note 29, at 1670-76.

37. K. LLEWELLYN, *supra* note 23. For analysis of this book, *see* W. TWINING, *supra* note 29, at 203-69.

38. K. LLEWELLYN, *supra* note 23, at 36.

39. K. LLEWELLYN, JURISPRUDENCE: REALISM IN THEORY AND PRACTICE 217 (1962), quoted in W. TWINING, *supra* note 29, at 210-11.

> law. Opinions run in deductive form with an air or expression of single-line inevitability. 'Principle' is a generalization producing order which can and should be used to prune away those 'anomalous' cases or rules which do not fit, such cases or rules having no function except, in places where the supposed 'principle' does not work well, to accomplish sense—but sense is no official concern of a formal-style court.[40]

In the 1970s, several historians examined the influence of instrumentalism and formalism.[41] Instrumentalism was defined as a "self-conscious attempt to view law as a means toward the attainment of some end."[42] Formalism was depicted as "the notion that social controversies could be resolved by deductions drawn from first principles on which all men agreed. . . ."[43] Some commentators argued that in the nineteenth century the predominant style shifted from instrumentalism to formalism.[44] In this century, in the post-realist era, modern legal thought has been portrayed as a continuing (and unsuccessful) effort to reconcile both formalism and instrumentalism.[45]

B. Stereotyped Arguments

Duncan Kennedy, in an influential article published in 1976, analyzed the tensions between formal and substantive visions of justice.[46] Kennedy suggested that competing ideological visions generate countervailing, stereotypical sets of policy arguments. He argued that "the arguments are symmetrical, few in number, and repeated endlessly in different legal contexts."[47] Legal reasoning,

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40. K. LLEWELLYN, *supra* note 23, at 38.

41. M. HORWITZ, *supra* note 23; Klare, *Judicial Deradicalization of the Wagner Act and the Origins of Modern Legal Consciousness, 1937-1941*, 62 MINN. L. REV. 265 (1978); Nelson, *supra* note 23.

42. Nelson, *supra* note 23, at 515.

43. Nelson, *supra* note 23, at 566.

44. M. HORWITZ, *supra* note 23; Nelson, *supra* note 23; *Contra*, Scheiber, *supra* note 30.

45. Klare, *supra* note 41, at 335 ("The formalist and realist traditions are continued sub silentio in judicial decisions, but in a manner consistent with legal vision.")

46. Kennedy, *Form and Substance*, *supra* note 23. Kennedy identified two diametrically opposed visions of substantive justice: altruism and individualism. Kennedy also distinguished between rules and standards. He concluded that there is a connection between rules and individualism; that there is a similar linkage between standards and altruism; and that "the individualist/formalist and the altruist/informalist operate from flatly contradictory visions of the universe." *Id.* at 1776.

These insights, while extremely important, do not support the political arguments which Professor Kennedy advanced in subsequent writings. Professor Kennedy is a co-founder of the Critical Legal Studies movement. This movement is associated with a radical critique of the legal system as an instrument of social oppression. The author of this article is not associated with the Critical Legal Studies movement and does not share their ideological views on the alleged desirability of redistributing wealth and power in American society.

47. Kennedy, *Distributive and Paternalist Motives in Contract and Tort Law, With*

because of the fundamental contradictions between underlying philosophies, often deteriorates into "the mechanical manipulation of balanced, pro/con policy arguments that come in matched pairs."[48] In the context of formalism and instrumentalism, the tension between the styles generates three standard sets of balanced pro/con policy arguments. The arguments arise when: (1) a court must choose between rules and standards; (2) a court decides whether it should be concerned with the social consequences of a legal rule; and (3) a court considers the institutional competence of the judiciary to make public policy. These arguments—rules vs. standards, social consequences, and institutional competence—recur in many different doctrinal disputes cutting across numerous branches of private law, including wrongful discharge cases.

The issue of rules and standards turns on the specificity and abstraction of the law.[49] All legal requirements can be placed on a continuum ranked according to the degrees of generality. Formalists prefer rules, while instrumentalists prefer standards. A law granting suffrage to any person over the age of 18 is an example of a rule. A law granting suffrage to "mature" persons only is an example of a standard. The virtue of a rule is that it promotes certainty and restrains arbitrariness. The vice of a rule is that it may be over- or under-inclusive and thereby incapable of achieving the purpose of the law (e.g., some persons over the age of 18 may not be mature voters). The advantages (and defects) of a standard are asymmetrical to those of a rule. A standard may be applied with a measure of discretion, so as to achieve the purpose underlying the standard; the danger with standards, of course, is that decision makers may enjoy too much latitude.

The issue of social consequences involves the court in an assessment of its willingness to consider the functional purpose of legal rules and the role of litigants as stand-ins for large social groups. Formalism de-personalizes the parties, divorces them from social context, and ignores social consequences. As Grant Gilmore explained in his critique of formalism in nineteenth century contract law:

> The status of the contracting parties and the subject matter of their deal were no longer to be taken into account. The law, under the new dispensation, no longer recognized factors or brokers, farmers or workers, merchants or manufacturers, shipown-

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Special Reference to Compulsory Terms and Unequal Bargaining Power, 41 MD. L. REV. 563, 581 (1982).

48. Kennedy, *The Stages of the Decline of the Public/Private Distinction*, 130 U. PA. L. REV. 1349, 1353 (1982).

49. Kennedy, *Form and Substance*, *supra* note 23, at 1687-1701.

> ers or railroads, husbands or wives, parents or children--only faceless characters named A and B, whoever they might be and whatever it might be they were trying to accomplish.[50]

Instrumentally-minded judges, on the other hand, are acutely aware of social context and self-consciously shape the common law to achieve various social purposes.[51]

Finally, the tension between formalism and instrumentalism generates matching sets of balanced arguments in a constantly recurring debate over institutional competence.[52] Formalists tirelessly argue that public policy is a matter best left to the Legislature. Judges should be confined to the limited, passive role of interpreting and applying statutes. The great evil is "judicial legislation." Instrumentalism, on the other hand, holds that judges can, should, and do, make public policy.[53]

Two caveats are in order. First, formalism and instrumentalism are styles of reasoning, and not rigorous methodologies.[54] Most judges are rarely, if ever, explicitly formal or instrumental. Second, the long, sustained attack on formalism has persuaded formally-minded courts to inject limited elements of instrumentalism into their opinions. It is not uncommon for an opinion to offer both instrumental and formal arguments in support of a legal conclusion.[55]

III. THE PUBLIC POLICY EXCEPTION

The public policy exception to the at-will rule holds that where a discharge violates public policy, the employee may sue in tort.[56] The courts have disagreed as to the correct definition of "public policy." The debate over the sources of public policy illustrates the continuing tension between formalism and instrumentalism.

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50. G. GILMORE, THE AGES OF AMERICAN LAW 46 (1977).

51. *See infra* notes 183-85 and accompanying text.

52. Kennedy, *Form and Substance*, *supra* note 23, at 1751-60.

53. *E.g.*, Cardozo, *supra* note 51, at 114 ("If you ask how he [the judge] is to know when one interest outweighs another, T can only answer that he must get his knowledge just as the legislator gets it, from experience and study and reflection; in brief, from life itself. . . . Each is indeed legislating within the limits of his competence.")

54. *E.g.*, Goetsch, *The Future of Legal Formalism*, 24 AM. J. LEG. HISTORY 221, 255 (1980). ("So legal formalism must be approached more as a loosely bound structure of legal thought rather than as a rigidly detailed system operated in mechanical fashion.")

55. *E.g.*, Nelson, *supra* note 23, at 515, n.12. ("Almost any result can be justified in almost any case by use of either style."); Klare, *supra* note 41.

56. For a survey of the public policy cases, *see* Note, *Defining Public Policy Torts in At Will Dismissals*, 34 STAN. L. REV. 153 (1981).

A. Formal and Instrumental Analysis

The formal analysis of the public policy exception can be easily sketched. The analysis suggests that a tort action lies only where the discharge violates a statute explicitly prohibiting the dismissal. To support this conclusion, a formally-minded judge would advance several stereotyped arguments: employer misconduct should be defined by fixed, predictable rules, not elastic, open-ended standards; only a statute explicitly prohibiting a dismissal attains the necessary degree of certainty and specificity; the firing of a single employee has no general social ramifications, unless the Legislature has indicated otherwise. The first principle—the appropriate definition of public policy—is a matter best left to the Legislature. If courts attempt to define "public policy," they usurp the power of the legislative branch.

The instrumental analysis is the mirror opposite of formalism. It is well illustrated by observations in a student note in the Harvard Law Review.[57] The author asserts that no "bright line" rule can be drawn, because of the incoherence of the public-private dichotomy:

> [A]ny particular line between 'private' and 'public interests' is vulnerable to the argument that it should have been drawn elsewhere. . . . The realms of public and private interest in employment overlap substantially. . . . All dismissals without 'just cause,' no matter how 'private' their motivation, undermine the community's interest in economic productivity, stable employment and fairness in the workplace.[58]

The student author argued that lower- and lower-middle-class workers are underrepresented by attorneys, and that there should be a universal "just cause" standard governing termination.[59]

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57. Note, *Protecting Employees At Will Against Wrongful Discharge: The Public Policy Exception*, 86 HARV. L. REV. 1931 (1983).

58. *Id.* at 1948 (*Cf.* Mallor, *Punitive Damages for Wrongful Discharge*, 26 WM. & MARY L. REV. 448, 459-60 (1985) ("The 'Achilles heel' of the public policy exception is the imprecision inherent in the term 'public policy' "). Professor Mallor, after surveying many jurisdictions, concluded: "The public policy cases can be viewed along a continuum. Plaintiffs are likely to prevail when two factors are present: the public policy is clear, that is, both specific and based on written law, and the discharge presents a clear threat of frustrating that policy." *Id.* at 462. The analysis in Part II of this Article suggests that formally-minded judges will identify a public policy only where it is "clear"; i.e., expressly prohibited by statute.

For a brief but suggestive comment on "continuumization" as an attempt to reconcile contradictory conceptions of justice, see Kennedy, *The Stages of the Decline of the Public/Private Distinction*, *supra* note 48, at 1352-53. ("People who believe in continuua tend to explain how they go about deciding what legal response is appropriate . . . by listing 'factors' that 'cut' one way or the other and must be balanced.")

59. *Id.* at 1933 ("The courts should recognize the public's interest in eliminating the power of employers to discharge their employees without just cause").

B. *The California Cases*

The courts in California initially recognized a public policy exception where the employer violated a statute expressly prohibiting a dismissal.[60] In *Petermann v. International Brotherhood of Teamsters*, the court expanded the potential scope of "public policy."[61] In *Petermann*, the employer gave the employee an impossible choice—commit the crime of perjury before a legislative investigative committee, or be fired. No statute expressly specified that an employer could not fire a worker who refused to perjure himself. The *Petermann* court nonetheless recognized the employee's cause of action and declared: "The right to discharge an employee under an [at-will] contract may be limited by statute [citation] or *by considerations of public policy*" [emphasis supplied].[62] The court then stated that the employee's discharge violated the state's declared policy against perjury.[63] After *Petermann*, the courts of appeal held that there must be a statutory basis for an action based on public policy. Three courts recognized actions based on Labor Code Section 923, which permits employees to engage in concerted activities.[64] Other actions were disallowed where the employee could not identify a statute.[65]

In *Tameny v. Atlantic Richfield Co.*, the California Supreme Court recognized the public policy exception and adopted the expansive *Petermann* formulation of the employer's duty.[66] Justice Tobriner's majority opinion in *Tameny* was an exercise in the instrumental style. Tobriner adopted a standard, not a rule.[67] He

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60. Lockheed Aircraft Corp. v. Superior Court, 28 Cal. 2d 481, 171 P.2d 21 (1946) (statute prohibiting dismissal of employees for engaging in political activities); Kouff v. Bethlehem-Alameda Shipyard, Inc., 90 Cal. App. 2d 322, 202 P.2d 1059 (1949) (statute prohibiting dismissal of employee for serving as election officer on election day).

61. Petermann v. International Bhd. of Teamsters, 174 Cal. App. at 18, 344 P.2d at 25.

62. *Id.* at 188, 344 P.2d at 27.

63. *Id.* at 188-89, 344 P.2d at 27.

64. CAL. LAB. CODE 5923 (West 1971); Montalvo v. Zamora, 7 Cal. App. 3d 69, 86 Cal. Rptr. 401 (1970); Wetherton v. Growers' Farm Labor Assoc., 275 Cal. App. 2d 168, 79 Cal. Rptr. 543 (1969); Glenn v. Clearman's Golden Cock Inn, Inc., 192 Cal. App. 2d 793, 13 Cal. Rptr. 769 (1961).

65. Becket v. Welton Becket & Assoc., 39 Cal. App. 3d 815, 114 Cal. Rptr. 531 (1974); Mallard v. Boring, 182 Cal. App. 2d 390, 6 Cal. Rptr. 171 (1960).

66. Tameny v. Atlantic Richfield Co., 27 Cal. 3d at 177-78, 164 Cal. Rptr. at 845-46. The employee alleged that he had been discharged because he refused to participate in an illegal price-fixing scheme. The scheme would have violated federal and state antitrust laws.

67. *Id.* at 174, 164 Cal. Rptr. at 842-43. ("*Petermann* held that even in the absence of an explicit statutory provision prohibiting the discharge of a worker . . . fundamental principles of public policy and adherence to the objectives underlying the state's penal statutes" requires that an employee may not be dismissed for violating a law.") *Id.*

emphasized the social importance of protecting employees.[68] He also stated that the sources of public policy are not limited to legislative enactments.[69]

The dissenting opinions, by contrast, resonated with the formal style. Justice Manuel argued that the cause of action must arise out of "a clear statutory source."[70] He expressed a preference for rules over standards when he stated: "I see no reason to search further for [the source of public policy] among the vague and ill-defined dictates of 'fundamental policy.' "[71] Justice Clark, in a separate dissent, also followed the formal style. He complained that "we again substitute our policy judgment for that of the legislature."[72] Clark did not discuss the social consequences of the at-will rule.[73]

After *Tameny*, the courts of appeal continued to disagree as to the sources of public policy. Some courts limited the sources to statutes.[74] This judicial reluctance followed from the formal emphasis on institutional competence. Some courts might "mistake their own predilections for public policy which deserves recognition at law."[75] Other courts endorsed the instrumental view.[76] As Justice Kaufman stated for the court of appeals in *Koehrer v. Superior Court*: ". . . it is immaterial whether the public policy is proclaimed by statute or delineated in a judicial decision."[77]

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68. *Id.* at 178, 164 Cal. Rptr. at 845.

69. *Id.* ("The rights of employees have not only been proclaimed by a mass of legislation . . . but the courts have likewise evolved certain additional protections at common law.")

70. *Id.* at 179, 164 Cal. Rptr. at 846, CAL. LAB. CODE 52856 (West 1971) provides, in pertinent part, that "[a]n employee shall substantially comply with all directions of his employer concerning the service on which he is engaged, except where such obedience is impossible or unlawful."

71. Tameny v. Atlantic Richfield Co., 27 Cal. 3d at 179, 164 Cal. Rptr. at 846.

72. *Id.*

73. *Id.* at 179-83, 164 Cal. Rptr. at 846-48.

74. Hejmadi v. AMFAC, Inc., 209 Cal. App. 3d 525, 538-40, 249 Cal. Rptr. 5, 11-12 (1988); Tyco Indus. v. Superior Court, 164 Cal. App. 3d 148, 157-59 (1985); Shapiro v. Wells Fargo, 152 Cal. App. 3d 467, 476-78, 199 Cal. Rptr. 613, 617-18 (1984); Hentzel v. Singer Co., 138 Cal. App. 3d 290, 295-304, 188 Cal. Rptr. 159, 161-68 (1982).

75. Hentzel v. Singer Co., 138 Cal. 3d at 297, 188 Cal. Rptr. at 163-64 (1982).

76. Dabbs v. Cardiopulmonary Management Services, 188 Cal. App. 3d 1437, 1437-45, 234 Cal. Rptr. 130-34 (1987) ("Fundamental policy may be expressed either by the Legislature in a statute or by the courts in decisional law"); Koehrer v. Superior Court, 181 Cal. App. 3d 1155, 1163-67, 276 Cal. Rptr. 820, 825 (1986).

77. Koehrer v. Superior Court, 180 Cal. App. 3d at 1165, 226 Cal. Rptr. at 825 (1986) (Kaufman, J.). Justice Kaufman was subsequently elevated to the California Supreme Court. His dissenting opinion in the *Foley* case is discussed in Part VII, *infra*.

IV. THE SEAMAN'S CASE

In the *Tameny* decision, Justice Tobriner hinted in a footnote that a wrongful discharge might be a bad faith tort.[78] In a later decision, *Seaman's Direct Buying Service, Inc. v. Standard Oil*, the Supreme Court also suggested that there might be a wrongful discharge tort.[79] The *Seaman's* case strongly influenced the subsequent evolution of wrongful discharge tort law.[80]

A. The Covenant

The *Seaman's* decision was a landmark in a series of good faith cases dating back to 1942. In *Universal Sales v. California Press Mfg.*, the supreme court held that, by operation of law, the covenant is implied into every contract; it is nondisclaimable.[81] The nondisclaimable duty has been defined in broad, general terms. The most commonly cited judicial definition of good faith is that "[i]n every contract there is an implied covenant of good faith and fair dealing that neither party will do anything which injures the right of the other to receive the benefits of the agreement."[82] There are other, equally general formulations of the duty.[83] The duty to act in good faith was applied to many different types of contractual relationships.[84]

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78. Tameny v. Atlantic Richfield Co., 27 Cal. 3d at 179, fn.12, 164 Cal. Rptr. at 846.

79. Seaman's Direct Buying Serv., Inc. v. Standard Oil Co., 36 Cal. 3d 752, 768-70, 686 P.2d 1158, 206 Cal. Rptr. 359 (1984).

80. The *Seaman's* case arose out of the breach of a commercial contract. The Standard Oil Company agreed to supply oil to a marine fuel dealer. When market conditions changed shortly thereafter, Standard refused to honor the agreement and claimed the contract was not legally binding. At trial, the jury awarded punitive damages of $11,058,810 for breach of the implied covenant.

81. Universal Sales v. California Press Mfg., 20 Cal. 2d 751, 128 P.2d 665, 677 (1942).

82. Brown v. Superior Court, 34 Cal. 2d 559, 564, 212 P.2d 878, 881 (1949).

83. Nelson v. Abraham, 29 Cal. 2d 745, 751, 177 P.2d 931, 934 (1947) ("There is an implied covenant that neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract"); Colwell Co. v. Hubert, 248 Cal. App. 2d 567, 575, 56 Cal. Rptr. 753, 759 (1967) ("This covenant not only imposes upon each contracting party the duty to refrain from doing anything which would render performance of the contract impossible by an act of his own, but also the duty to do everything that the contract presupposes that he will do to accomplish its purpose"). The Uniform Commercial Code defines "good faith" as "honesty in fact in the conduct or transaction concerned." U.C.C. §§ 1-201 (19). For merchants, the Code defines good faith as "honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade." U.C.C. §§ 2-103 (1)(b).

"Good faith performance or enforcement of a contract emphasizes faithfulness to an agreed common purpose and consistency with the justified expectations of the other party . . . The appropriate remedy for a breach of the duty of good faith also varies with the circumstances." RESTATEMENT (SECOND) OF CONTRACTS Sec. 205, comment a.

84. The cases are collected at Louderback and Jurike, *Standards for Limiting the*

For many years, the victim of a breach of the covenant was confined to contractual remedies. In 1967, in a landmark case, the California Supreme Court recognized that an insurer's breach of the covenant is a tort.[85] This rule was confirmed in a series of insurance cases, which typically arose when the insurer denied coverage or otherwise ignored the interests of the insured.[86] Various forms of insurer misconduct were identified as torts.[87]

Subsequently, several courts suggested that misconduct by a non-insurer might also be a tortious breach of the covenant. In 1978, in *Sawyer v. Bank of America*, a court of appeal stated: "The tort of breaching an implied covenant of good faith and fair dealing consists in bad faith action, extraneous to the contract, with the motive intentionally to frustrate the obligee's enjoyment of contract rights."[88] In 1980, in *Wagner v. Benson*, the court suggested that bad faith tort actions might not be limited to insurance transactions.[89] Also in 1980, Justice Tobriner, in his *Tameny* opinion, suggested in dictum that an unreasonable dismissal of an employee might violate the covenant.[90]

In 1984, the California Supreme Court, in the *Seaman's* case, expressly stated that not all breaches of the covenant are torts.[91]

Tort of Bad Faith Breach of Contract, 16 U.S.F. L. REV. 187, 194-96, nn.31-40 (1982).

85. Crisci v. Security Ins. Co., 66 Cal. 2d 425, 426 P.2d 173, 58 Cal. Rptr. 13 (1967). In this opinion, the court emphasized the vulnerability of the insured: "Plaintiff did not seek by the contract involved here to obtain a commercial advantage but to protect herself against the risks of accidental losses, including the mental distress which might follow from the losses." In Communale v. Traders & Gen. Ins. Co., 50 Cal. 2d 654, 663, 328 P.2d 198, 203 (1958), the court had stated that "wrongful refusal to settle has generally been treated as a tort."

86. The cases are collected in Miller & Estes, *A California Trilogy*, *supra* note 7, at 87-91.

87. *E.g.*, Egan v. Mutual of Omaha Ins. Co., 24 Cal. 3d 809, 157 Cal. Rptr. 482 (1979) (failure to properly investigate the insured's claim); Neal v. Farmers' Ins. Exchange, 21 Cal. 3d 910, 148 Cal. Rptr. 389 (1978) (failure to act on a timely basis after the insured requested a prompt settlement); Gruenberg v. Aetna Ins. Co., 9 Cal. 3d 566, 510 P.2d 1032, 108 Cal. Rptr. 480 (1973) (denial of benefits after wrongfully inducing the injured to violate the terms of the policy); Fletcher v. Western National Life Ins. Co., 10 Cal. App. 3d 376, 89 Cal. Rptr. 78 (1970) (insurer withheld disability benefits to save money for the company); Crisci v. Security Ins. Co., 66 Cal. 2d 425, 426 P.2d 173, 158 Cal. Rptr. 13 (1967) (refusal to accept settlement offer within amount of policy).

88. Sawyer v. Bank of America NT&SA, 83 Cal. App. 3d 135, 139, 145 Cal. Rptr. 623, 625 (1978). In *Sawyer*, a bank inadvertently failed to pay an insurance premium on a vehicle owned by the plaintiff. The bank then denied that it was liable. Given these facts, the court of appeal refused to sustain an award of general and special damages, although it did note the theoretical existence of the tortious breach of the covenant.

89. Wagner v. Benson, 101 Cal. App. 3d 27, 33, 161 Cal. Rptr. 516, 520 (1980). The court stated, "A bad faith cause of action sounding in tort has never been extended to contractual relationships other than in the insurance field (citation). This does not mean such claims are limited only to insurance transactions." *Id.* at 33, 161 Cal. Rptr. at 520.

90. Tameny v. Atlantic Richfield Co., at 179, n.12, 164 Cal. Rptr. at 846.

91. Seaman's Direct Buying Serv., Inc., v. Standard Oil Co., 36 Cal. 3d 752, 769, 686 P.2d 1158, 206 Cal. Rptr. 359, 362 (1984).

It also refused to state the opposite rule, that all breaches of the covenant can never be tortious.[92] Instead, the court invented a new tort and offered an extremely provocative dictum describing employment as a special relationship.[93]

B. The New Tort

The *Seaman's* opinion holds that an independent tort action is available "when, in addition to breaching the contract, [the defendant] seeks to shield itself from liability by denying, in bad faith, and without probable cause, that the contract exists."[94] There is no tort unless a breach of contract precedes the defendant's deliberate disavowal of the very existence of the agreement.[95] The *Seaman's* tort is not a bad faith tort. Indeed, the supreme court, in a per curiam opinion, expressly noted that it did not rely on the covenant to decide the case.[96]

The new tort was more or less invented out of thin air. The *Seaman's* court cited just two out-of-state cases.[97] In *Adams v. Crater Welling Drilling, Inc.*, punitive damages were imposed to punish a defendant who had threatened to file a frivolous lawsuit.[98] The *Adams* case essentially involved the familiar tort of abuse of process. In *Jones v. Abriani*, the court stated that punitive damages may be available where the defendant fraudulently induces an innocent party to enter into a consumer contract to purchase a mobile home.[99] *Jones* was, essentially, a fraud case.

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92. *Id.*

93. *Id.* at 769, 206 Cal. Rptr. at 363. The court noted: "It is not even necessary to predicate liability on a breach of the implied covenant." *Id.* A court of appeal subsequently characterized the *Seaman's* decision as recognizing "a new intentional tort." Quigley v. Pet, Inc., 162 Cal. App. 3d 877, 890, 208 Cal. Rptr. 394, 401 (1984).

94. Seaman's Direct Buying Service, Inc. v. Standard Oil Co., *supra* note 91, at 769, 706 Cal. Rptr. at 363.

95. *Id.*

96. *Id.*

97. *Id.* In a concurring opinion in a case involving a claim under California law, Judge Kozinski offered a harsh criticism of the *Seaman's* decision. Oki America, Inc. v. Microtech International, Inc., 872 F.2d 312, 314-17 (9th Cir. 1989). Kozinski's critique essentially rests on two formal arguments. First, he stated that the test for the Seaman's tort is an unduly amorphous standard: "[i]t is impossible to draw a principled distinction between a tortious denial of a contract's existence and a permissible denial of liability. . ." *Id.* at 315. Second, Judge Kozinski stated that the judicial branch is institutionally incompetent to make these determinations: "Courts are slow, clumsy, heavy-handed institutions, ill-suited to oversee the negotiations between institutions." *Id.* at 316.

98. Adams v. Crater Well Drilling, Inc., 276 Or. 789, 556 P.2d 679 (1976).

99. Jones v. Abriani, 169 Ind. 556, 350 N.E. 2d 645 (1976). The supreme court's reference to this case was inappropriate. The court, in *Seaman's*, emphasized that the new tort existed entirely apart from any special relationship which might exist between the parties. Yet the Indiana court, in *Abriani*, was heavily influenced by the special relationship concept: "It is hard to imagine where the public interest to be served is more important than in consumer matters, especially when the consumer is in an inferior bargaining

Neither of the cases involved "stonewalling" or a denial of the existence of the contract.

Although the *per curiam* opinion in *Seaman's* was innovative, it was not nearly so bold as the concurring and dissenting opinion filed by then-Chief Justice Bird.[100] Bird wrote that the nature of the non-disclaimable duties imposed by the covenant depends on "the expectations of the party and the purposes of the contract."[101] In some circumstances, Bird added, "the voluntary breach of an acknowledged contract is itself a violation of the duty to deal fairly and in good faith."[102]

C. *Employment As a Special Relationship*

Although it was unwilling to extend the tort remedy to all bad faith cases, the supreme court also refused to eliminate the bad faith tort. Earlier, in 1979, the court had ruled that insurance is a special relationship.[103] In 1984, in the *Seaman's* case, the court signaled its willingness to recognize at least one other special relationship, that of employment.[104]

The special relationship model is important for two reasons. First, as a matter of black letter law, breaches of the covenant, when there is a special relationship, are torts. Second, at a deeper, more philosophical level, when a court recognizes a relationship as "special," it reasons instrumentally.[105]

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position and forced to sign an adhesive contract or do without the item desired." 350 N.E.2d at 650.

100. Seaman's Direct Buying Services v. Standard Oil Co., 36 Cal. 3d at 774-82, 206 Cal. Rptr. 366-71. Bird dissented from that part of the per curiam opinion which stated that it was not necessary to predicate liability on a breach of the covenant.

101. *Id.* at 777, 206 Cal. Rptr. at 368.

102. *Id.* at 781, 206 Cal. Rptr. at 371. The broad scope of the "reasonable expectations" test is suggested by a law review commentary: "Breach of the implied covenant must take into account the employee's reasonable expectations. Such expectations not only include not being fired on the basis of false charges, but also being afforded rights established by company policies, not being terminated in violation of statutory protections and being treated in a manner consistent with the treatment of other similarly situated individuals. Reasonable expectations may also be based on past employer practices or predominating industry standards. A complete listing of employer conduct which would violate the reasonable expectation of the employee is unnecessary. It is sufficient to note that in the future the courts should analyze all the circumstances surrounding an employment relationship in addressing the issue of bad faith discharge." Hagerty, *Breach of the Implied Covenant of Good Faith and Fair Dealing in Employment Contracts: From Here to Longevity and Beyond*, 14 W. STATE U. L. REV. 445, 463 (1987).

103. Egan v. Mutual of Omaha Ins. Co., 24 Cal. 3d 809, 157 Cal. Rptr. 482 (1979).

104. Seaman's Direct Buying Service, Inc. v. Standard Oil Co., 36 Cal. 3d 752, 206 Cal. Rptr. 359 (1984).

105. Egan v. Mutual of Omaha Ins. Co., *supra* note 87, 24 Cal. 3d 820, 157 Cal. Rptr. 487 (quoting Goodman & Seaton, *Foreword: Ripe For Decision, Internal Workings and Current Concerns of the California Supreme Court*, 62 CAL. L. REV. 309, 346-47 (1974).

In *Egan v. Mutual of Omaha Insurance Co.*, the court stated that the special relationship between the insurer and its insured warranted the tort action and explained:

> The insurers' obligations are . . . rooted in their status as purveyors of a vital service labeled quasi-public in nature. Suppliers of services affected with a public interest must take the public's interest seriously, where necessary placing it before their interest in maximizing gains and limiting disbursements. . . . [A]s a supplier of public service rather than a manufactured product, the obligations of insurers go beyond meeting reasonable expectations of coverage. The obligations of good faith and fair dealing encompass qualities of decency and humanity inherent in the responsibilities of a fiduciary. Insurers hold themselves out as fiduciaries, and with the public's trust must go private responsibility consonant with that trust.
>
> Furthermore, the relationship of insurer and insured is inherently unbalanced; the adhesive nature of insurance contracts places the insurer in a superior bargaining position. The availability of punitive damages is thus compatible with recognition of insurers' underlying public obligations and reflects an attempt to restore balance in the contractual relationship.[106]

This language establishes that the special relationship model is essentially instrumental. The model considers the functional, social consequences of a legal rule. Not surprisingly, formally-minded academic commentators have criticized the model on the ground that it is a standard, not a rule.[107]

In 1984, in the *Seaman's* case, the California Supreme Court declined to characterize an "ordinary commercial contract" as a special relationship.[108] The court stated:

> In holding that a tort action is available for breach of the covenant in an insurance contract, we have emphasized the 'special relationship' between insurer and insured. . . . When we move from such special relationships to consideration of the tort remedy in the context of the ordinary commercial contract, we move into largely uncharted and potentially dangerous waters. Here, parties of roughly equal bargaining power are free to shape the contours of their agreement. . . . In such contracts, it may be

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106. Egan v. Mutual of Omaha Ins. Co., 24 Cal. 3d 820, 157 Cal. Rptr. 487-88.

107. In an important student note, Michael Cohen criticized the model on essentially formal grounds. Cohen, *Reconstructing Breach of the Implied Covenant of Good Faith and Fair Dealing As a Tort*, 73 CAL. L. REV. 1291, 1298-1301 (1986) (the special relationship model is "inadequate to define the scope and applicability of a tort duty of good faith and fair dealing"). C. Delos Putz and Nona Klippen, in another formally-minded analysis, argued that the special relationship is "illusory"; that it is not a "principled basis of decision"; and that "the qualifying contracts cannot be identified until the issue has been litigated, which is too late." Putz & Klippen, *Commercial Bad Faith: Attorney Fees—Not Tort Liability—Is the Remedy for "Stonewalling,"* 21 U.S.F. L. REV. 419, 478-79 (1987).

108. Seaman's Direct Buying Service, Inc. v. Standard Oil, Cal. 3d 768, 206 Cal. Rptr. 362-63.

> difficult to distinguish between breach of the covenant and breach of contract, and there is the risk that interjecting tort remedies will intrude upon the expectations of the parties. This is not to say that tort remedies have no place in such a commercial context, but that it is wise to proceed with caution in determining their scope and application.[109]

What types of relationships, then, are special? Insurance (under *Egan*) is one. Before the recent decision in *Foley*, it appeared that employment might be another. In footnote 6 of its *Seaman's* opinion, the court stated:

> In *Tameny* . . . this court intimated that breach of the covenant of good faith and fair dealing in the employment relationship might give rise to tort remedies. That relationship has some of the same characteristics as the relationship between insurer and insured.[110]

D. The "Special Relationship" After The Seaman's Case

Several weeks after the filing of the *Seaman's* decision, one court of appeal followed the suggestion in footnote 6 and identified employment as a special relationship (but not in the context of an involuntary termination).[111] In *Wallis v. Superior Court*, a former employee entered into an agreement with his ex-employer. The parties agreed that the employer would provide the employee with a pension in exchange for a promise not to compete. The employer then breached the agreement.[112] The Court in *Wallis* held that:

> For purposes of serving as a predicate to tort liability, we find that the following 'similar characteristics' must be present in a contract: (1) the contract must be such that the parties are in inherently unequal bargaining positions; (2) the motivation for entering the contract must be a non-profit motivation, i.e., to secure peace of mind, security, future protection; (3) ordinary contract damages are not adequate because (a) they do not require the party in the superior position to account for its actions, and (b) they do not make the inferior party 'whole'; (4) one party is especially vulnerable because of the type of harm it may suffer and of necessity places trust in the other party to perform;

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109. *Id.*

110. *Id.*, 36 Cal. 3d 769, n.6, 206 Cal. Rptr. 362 ("In *Tameny* . . . this court intimated that breach of the covenant of good faith and fair dealing in the employment relationship might give rise to tort remedies. That relationship has some of the characteristics as the relationship between insurer and insured. [*See* Louderback & Jurike, *Standards for Limiting the Tort of Bad Faith Breach of Contract* 16 U.S.F. L. REV. 187, 220-26) (1981).]" The Louderback & Jurike article does not identify employment as a relationship that "might give rise to tort remedies.")

111. Wallis v. Superior Court (Kroehler Mfg. Co.), 160 Cal. App. 3d 1109, 207 Cal. Rptr. 123 (1984)

112. *Id.* at 1113, 207 Cal. Rptr. at 125.

and (5) the other party is aware of this vulnerability.[113]

Various courts of appeal have recognized the *Wallis* factors as legitimate criteria for identifying a special relationship in a context other than either insurance or employment. One court held that there is a special relationship between a bank and its depositors.[114] The general approach, however, has been for the court to acknowledge the special relationship model, but then to hold that the model does not apply to the particular contractual dispute the court has been asked to decide.[115]

The *Seaman's* case encouraged wrongful discharge tort claims. After the *Seaman's* decision, it was possible for an employer to commit a *Seaman's* tort. More importantly, if a special relationship triggered a bad faith tort action, and if employment was a special relationship, a court could conclude that a wrongful discharge was a bad faith tort.

V. The Bad Faith Tort in the Courts of Appeal

In the post-*Tameny*, pre-*Foley* era, numerous courts of appeal considered the bad faith wrongful discharge tort. The original decision recognizing the tort (*Cleary v. American Airlines*) was confusing and raised more questions than it answered.[116] After 1984, the courts relied on the language in the *Seaman's* case to identify the new bad faith tort duties of employers.

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113. *Id.* at 1118, 207 Cal. Rptr. at 129. The court cited no authority for the existence of this five-prong test. The analysis is similar to the four-prong test advocated in the law review article by Louderback and Jurike, *supra* note 84.

114. Commercial Cotton Company, Inc. v. United California Bank, 163 Cal. App. 3d 511, 209 Cal. Rptr. 551 (1985) (refusal of bank to reimburse depositor for loss caused by bank's negligent error.)

115. Martin v. U-Haul Company of Fresno, 204 Cal. App. 3d 396, 251 Cal. Rptr. 17 (1988) (termination of contract with independent rental equipment dealer); Okun v. Martin, 203 Cal. App. 3d 805, 250 Cal. Rptr. 220 (1988); (exclusion of investor from business opportunities); Rogoff v. Grabowski, 200 Cal. App. 3d 624, 246 Cal. Rptr. 185 (1988) (breach of contract to provide limousine service for an evening); Multiplex Ins. Agency, Inc. v. California Life Ins. Co., 189 Cal. App. 3d 925, 235 Cal. Rptr. 12 (1987) (wrongful refusal by insurance company to pay commission allegedly due to insurance agent). In a decision which did not refer to the *Wallis* criteria, another court of appeal held that there was no special relationship between two commercial enterprises, notwithstanding the fact that the contract involved a major portion of the plaintiff's business, Quigley v. Pet Incorporated, 162 Cal. App. 3d 877, 208 Cal. Rptr. 394 (1984). *See also* Premier Wine & Spirits v. E. & J. Gallo Winery, 846 F.2d 547, 540 (1988) (termination of nonexclusive wholesale distributorship agreement; the federal court stated that it did not "detect elements of public interest or fiduciary relations that would make the distributorship close to one of employment or insurance.")

116. Cleary v. American Airlines, 111 Cal. App. 3d 443, 168 Cal. Rptr. 722 (1980).

A. The Cleary Decision

In 1981, in the *Cleary* case, the court of appeal stated that a wrongful discharge in violation of the covenant gave rise to a tort action.[117] The court held: "The longevity of the employee's service, together with the expressed policy of the employer, operates as a form of estoppel, precluding any discharge of such an employee by the employer without good cause."[118] There are, however, numerous problems with the *Cleary* opinion. The employee's common law cause of action was probably preempted by federal labor law.[119] The court misinterpreted an earlier decision.[120] Most importantly, the court did not explain why it singled out the two particular criteria of longevity and adherence to internal company rules as the controlling factors.[121]

After 1981, only one court of appeal—the court of appeal in the *Foley* case—adhered strictly to the two-prong test in *Cleary*.[122] One other court implied that *Cleary* should be interpreted narrowly.[123] The majority of the appeals courts, however, followed the proposition that "the theory of recovery articulated in *Cleary*

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117. *Id.*

118. *Id.* at 456, 168 Cal. Rptr. at 722.

119. Cleary alleged that the stated reason for his dismissal was a pretext and that he was actually dismissed for union organizing activities. The union activity of airline employees is governed by the Federal Railway Labor Act, administered by the National Mediation Board. 45 U.S.C. § 181 (1982). The federal statute preempts a state cause of action for wrongful termination. Graf v. Elgin, Joliet & E. Ry Co., 790 F.2d 1341, 1348 (7th Cir. 1986) (Posner, J.). This observation concerning the preemption of Mr. Cleary's claim was originally made in Brody, *Wrongful Termination as Labor Law*, 34 SW. U. L. REV. 434, 460, n.131 (1988).

120. Cleary v. American Airlines, *supra* note 10, 111 Cal. App. 3d 453, 168 Cal. Rptr. 729, citing the following observation in Coats v. General Motors, 3 Cal. App. 2d 340, 348, 39 P.2d 838, 841: ". . . where there is evidence tending to show the discharge was due to reasons other than dissatisfaction with the services, the question is one for the jury." The Coats decision did not impose an independent duty on the employer. In *Coats*, the contract provided that the employee would receive a stock bonus, unless he was dismissed because of unsatisfactory service (of which the executive committee shall be the sole judge). Coats v. General Motors, 3 Cal. App. 3d 340, 343, 39 P.2d 838, 840. The question was whether the employee had performed his contractually-obliged services to the satisfaction of the other party.

121. The court cited a student law review note, *Implied Contracts to Job Security*, 26 STAN. L. REV. 335 (1974), "for analysis and criticism of the common law rule." This article identified several criteria which tend to support implied contractual rights to job security: special benefits to the employer, detrimental reliance by the employee, the policy of the firm, the nature of the job, the common law of the industry, and longevity of service. *Id.* at 350-65.

122. Foley v. Interactive Data Corp., 193 Cal. App. 3d 28, 219 Cal. Rptr. 866 (1986) (Roth, J.).

123. Newfield v. Ins. Co. of the West, 156 Cal. App. 2d 440, 445-46, 203 Cal. Rptr. 9, 12 (1984) (cause of action for bad faith discharge "always predicated upon other public policy grounds, statutory violations, an express [or clearly implied] contract ground, or upon a combination of elements" such as "company policies, faithful service, and lack of criticism").

is not dependent on the particular factors considered in that case."[124]

B. *The Post-Seaman's Cases*

What, then, was the predominant theory of recovery? In the pre-*Foley* era, there were two leading cases. In *Khanna v. Microdata*, the court defined the employer's duties by adopting the *Sawyer* test: in employment contracts, the covenant is breached whenever the employer "engages in 'bad faith action' extraneous to the contract, combined with the obligor's intent to frustrate the [employee's] enjoyment of contract rights."[125] In the other leading case, *Koehrer v. Superior Court*, the court built upon the concepts developed in the *Seaman's* opinion.[126] The court held there is no tort if the employer believed in good faith that he had good reason to terminate the employee.[127]

Justice Kaufman, writing for the *Koehrer* court, interpreted the *Seaman's* tort as a bad faith tort.[128] He stated:

> While the court in Seaman's stated that it was not necessary to base its decision on the implied covenant of good faith and fair dealing [citation], it is difficult otherwise to understand its repeated reference to 'good faith' and 'bad faith'. . . . In any event, its language is instructive.[129]

This observation was mistaken. The Supreme Court in the *Seaman's* case specifically emphasized that the *Seaman's* tort is entirely independent of the bad faith tort.[130]

There was another difficulty with the *Koehrer* opinion.[131] The

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124. Khanna v. Microdata Corp., 170 Cal. App. 3d 250, 262, 215 Cal. Rptr. 860, 867 (1986). The other employment cases rejecting the narrow approach include: Koehrer v. Superior Court, 181 Cal. App. 3d 1155, 226 Cal. Rptr. 820 (1986); Rulon-Miller International Business Machines Corp., 162 Cal. App. 3d 241, 208 Cal. Rptr. 524 (1984); Shapiro v. Wells Fargo Realty Advisors, 152 Cal. App. 3d 467, 199 Cal. Rptr. 613 (1984); Crosier v. United Parcel Service, Inc., 150 Cal. App. 3d 1132, 198 Cal. Rptr. 361 (1983).

125. Khanna v. Microdata Corp., 170 Cal. App. 3d at 262, 215 Cal. Rptr. at 867, quoting Sawyer v. Bank of America, 83 Cal. App. 3d at 139, 145 Cal. Rptr. at 623. In *Khanna*, the employee alleged that he had been discharged in an effort to deprive him of previously-earned sales commissions.

126. Koehrer v. Superior Court, 181 Cal. App. 3d 1155, 226 Cal. Rptr. 820 (Kaufman, J.).

127. *Id.* at 1172, 226 Cal. Rptr. at 829. ("If the employer merely disputes his liability under the contract by asserting in good faith and with probable cause that good cause existed for discharge, the implied covenant is riot violated and the employer is not liable in tort.") In evaluating the employer's conduct under this test, there is a subjective element ("good faith") and an objective element ("probable cause").

128. *Id.* at 1172, 226 Cal. Rptr. at 829.

129. *Id.*

130. Seaman's Direct Buying Service v. Standard Oil Co., *supra* note 79, 36 Cal. 3d at 769, 206 Cal. Rptr. 363. ("For the purposes of this case . . . it is not even necessary to predicate liability on a breach of the implied covenant").

131. For a somewhat similar discussion of the point developed in this paragraph, *see*

two-prong test in *Seaman's* is different from the two-prong test in *Koehrer*. In a *Seaman's* tort, the defendant must first breach the contract (the first prong) and then unreasonably deny that the contract exists.[132] In the *Koehrer* bad faith tort, the employer asserts in good faith that there is good cause to terminate (the first, subjective prong), and must also make this assertion with probable cause (the second, objective prong).[133] The tests in the two cases are quite different.

The distinction is important and can be illustrated by reference to the facts in the *Koehrer* case. In *Koehrer*, it was unclear whether the employer had breached the contract (the first prong under *Seaman's*). The contract provided that the plaintiffs would manage three apartment buildings for one year. The employees were then discharged less than four months after they had begun to render services. The employer alleged they had failed to perform their contractual duties. In any event, the employer never denied that there was a contract, and so there was no violation of the second part of the *Seaman's* test.[134] Under the *Seaman's* test, properly applied, the employee's action would not have survived a motion for summary judgment. The *Koehrer* court ruled, however, that there was a triable issue of fact, and the case presumably went before a jury.

Why did Justice Kaufman transmute the special relationship test (arising out of the covenant) into a *Seaman's*-type tort? One can only speculate. It would seem that the formal approach to deciding the case was not a viable alternative. The standard definition of the covenant was much too general to determine whether an employee had been discharged wrongfully. At the same time, the special relationship test was not desirable because it required the court to engage in instrumental analysis. The court would have been required to formulate an open-ended standard; to investigate complex employment markets; and to make an overt decision about a difficult question of policy. It was much easier to bor-

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Bacon & Gomez, *Huber Is A Ruling At Odds With Prior Decisions*, Los Angeles Daily Journal, March 18, 1988, at 4, cols. 3-6. Bacon & Gomez criticize a federal decision which followed *Khanna* and *Koehrer*. Huber v. Standard Ins. Co., 841 F.2d 980 (9th Cir. 1988).

132. Seaman's Direct Buying Service v. Standard Oil Co., *supra* note 79, 36 Cal. 3d at 769, 206 Cal. Rptr. 363. ("a party to contract may incur remedies when, in addition to breaching the contract, it seeks to shield itself from liability by denying, in bad faith and without probable cause, that the contract exists").

133. Koehrer v. Superior Court, 181 Cal. App. 3d 1155, 226 Cal. Rptr. 829. The text is quoted in full at note 127, *supra*.

134. Koehrer v. Superior Court, 181 Cal. App. 3d 1160-61, 226 Cal. Rptr. 822. The contract provided that the plaintiffs would manage three apartment buildings for two years. They were discharged less than four months after they began their employment. The employer provided them with a letter reciting their alleged deficiencies.

row the *Seaman's* test.

How would the *Seaman's* test, properly applied, have affected an employee, who, unlike the plaintiffs in *Koehrer*, served at-will, without a fixed term of service? In an at-will contract, the employee, by definition, has no expectation of continuing in employment. Therefore, a termination cannot breach the contract.[135] The second prong of the contract is never reached; there is no analysis of the reasonableness of the employer's conduct; and there is no tort.

The distinction between a breach of contract and a breach of covenant was noted by the court in *Hejmadi v. AMFAC, Inc.*[136] The *Hejmadi* court emphasized that a termination does not breach an at-will contract.[137] There is a potential tort only in limited circumstances: "Where the employment is strictly at-will, there may exist in certain employment relationships an expectation of a contractual benefit which is independent of continuing employment."[138]

The *Hejmadi* case is the converse of the earlier *Cleary* opinion. The *Cleary* decision is instrumental. The new tort was justified with the rationale that, because of modern economic conditions, the at-will rule should be changed to protect employees (i.e., because of the social consequences argument).[139] Also, courts are institutionally capable of making policy.[140] *Hejmadi* is also an instrumental opinion, but with a completely different twist. Because of the complexity of the employment markets, the consequences of changing the at-will rule are unknown and unpredictable, and the rule should not be changed (i.e., because of the social conse-

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135. Several courts have held that there can be no breach of the covenant where there is an express at-will term in the contract. Malmstrom v. Kaiser Aluminum and Chemical Corp., 187 Cal. App. 3d 299, 231 Cal. Rptr. 820 (1986); Gerdlund v. Electronic Dispensers International, 190 Cal. App. 3d 266, 235 Cal. Rptr. 279 (1985). For a more recent, and contrary view, *see* Rodie v. Max Factor Co., _ Cal. App. 3d_ , 256 Cal. Rptr. 1 (1989). The *Rodie* court held that a subsequent oral promise may modify a written at-will clause in a contract of employment.

136. Hejmadi v. AMFAC, Inc., 202 Cal. App. 3d 525, 249 Cal. Rptr. 5 (1988).

137. *Id.* at 546-52, 249 Cal. Rptr. at 14-20.

138. *Id.* 202 Cal. App. 3d 549, 249 Cal. Rptr. 19. In the at-will contract, there can be no expectation of "continuing employment." The *Hejmadi* court gave an example of "a contractual benefit which is independent of continuing employment": previously-earned sales commissions. If an at-will employee is dismissed to deprive him of commissions, there would be a cause of action under the *Hejmadi* analysis.

139. Cleary v. American Airlines, 111 Cal. App. 3d 449, 168 Cal. Rptr. 725 ("When viewed in the context of present-day economic reality and the joint, reasonable expectations of employers and their employees, the 'freedom' bestowed by the rule of law on the employee may indeed be fictional").

140. *Id.* at 450, 168 Cal. Rptr. at 726 (although the legislature has not amended the at-will statute, "some exceptions have been made to its application in particular cases where, for reasons of public policy—*as perceived by the judiciary or the Legislature*—such exceptions have been deemed warranted") (emphasis supplied).

quences argument).[141] The *Hejmadi* court also stated that the courts are not institutionally competent to make policy.[142]

C. *The Need For a Supreme Court Decision*

In general, however, the decisions in the courts of appeal during the period 1981-1988 were neither instrumental nor formal. The courts were primarily concerned with adapting the decisions of the supreme court to the particular problem of the employer's duty to act in good faith. The courts did not indicate that they were engaged in social engineering (i.e., an instrumental approach). Nor did the courts invoke the covenant and then blandly conclude that the employer had (or had not) breached the duty (i.e., a formal approach).

Why were the judges of the courts of appeal reluctant to justify their decisions on either purely instrumental or purely formal terms? By definition, courts of appeal are intermediate courts. Instrumentalism was unavailable, because it would be inappropriate for a court of appeal to appear to formulate social policy or to perform legislative functions. Formalism was unavailable because of the supreme court's excessively general definition of the covenant. The definition of good faith was so broad that it was difficult to determine when a particular discharge breached the covenant.[143]

Therefore, the intermediate courts attempted to ascertain the nature of the employer's duty by referring to language in prior California Supreme Court opinions. The *Khanna* definition of the duty is quoted from *Sawyer*, which in turn interpreted an earlier supreme court decision.[144] The *Koehrer* definition drew upon the language in the *Seaman's* case.[145]

In the period between 1981 and 1988, almost all of the courts of appeal recognized the new wrongful discharge tort.[146] There

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141. Hejmadi v. AMFAC, Inc., *supra* note 136, 202 Cal. App. 3d 546, 249 Cal. Rptr. 17. The court stated: ". . . it is essential that the heterogenous nature of employment relationships be taken into account. The standards we create apply equally to the economically marginal employer of one or two employees as well as to the presumably profitable major corporate enterprise." ibid.

142. *Id.* at 544-45, 249 Cal. Rptr. at 16 (". . . it is not the prerogative of the judicial branch of government, absent some compelling reason based on fundamental public policy or statutory direction, to impose a limitation" on the right to discharge employees).

143. *See supra* text accompanying notes 81-84.

144. Khanna v. Microdata Corp., 170 Cal. App. 3d 250, 262, 215 Cal. Rptr. 867; Sawyer v. Bank of America, 83 Cal. App. 3d at 139, 145 Cal. Rptr. at 625; Brewer v. Simpson, 53 Cal. 2d 567, 584, 2 Cal. Rptr. 609, 620 (1960).

145. *See supra* text accompanying notes 126-30.

146. Foley v. Interactive Data Corp. 47 Cal. 3d 685-89, 254 Cal. Rptr. 228-31 (opinion of Lucas, C. J., reviewing cases), 47 Cal. 3d 703-05, 254 Cal. Rptr. 241-243 (opinion of Broussard, J., reviewing cases). Neither justice discussed Hejmadi v. AMFAC,

was a marked disagreement among the courts, however, with respect to the exact nature of the employer's duty under the covenant. By 1986 it was clear that the new tort would have to be reviewed by the supreme court.

VI. THE FOLEY CASE

On December 29, 1988, the California Supreme Court issued its long-awaited decision in *Foley v. Interactive Data Corporation.* The court had granted the petition for review on January 30, 1986. Oral argument was heard on June 11, 1986, and then reheard on April 6, 1987, after three new judges were named to the court following the confirmation elections of November 1986.[147]

A. The Facts

Although the legal issues arising out of the case were complex, the facts were relatively straightforward.[148] The Interactive Data Corporation (IDC) hired Daniel Foley on June 17, 1976. There was no written contract of employment and no express agreement as to whether Foley served at-will. Thereafter, Foley regularly received promotions and pay raises. On January 1, 1983, IDC transferred Richard Kuhne to fill a supervisory position over Foley. At that time, the Federal Bureau of Investigation (FBI) was investigating Kuhne for suspected embezzlement from his previous employer. IDC knew about the investigation. Foley did not know, however, that IDC was already aware of the FBI investigation.

On January 14, 1983, Foley confided to Kuhne's superior, Richard Earnest, that "he was worried about working for Kuhne, and concerned about Kuhne having a supervisory position at IDC." Earnest chastised Foley for raising the issue and warned him not to discuss the matter with anyone else. It is possible that Foley may have wanted Kuhne's job.

IDC and its supervisors then followed an inconsistent course of action. On March 3, 1983, Kuhne told Foley that Foley was to be demoted and transferred from California to Massachusetts. On March 15, 1983, Foley received a merit bonus of $6,726. On March 16, 1983, Kuhne told Foley he could continue in his cur-

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Inc., 202 Cal. App. 3d 525, 249 Cal. Rptr. 5, which was decided after the *Foley* case was re-argued.

147. The new justices were Kaufman, Arguelles, and Eagleson. Arguelles, who joined in the majority opinion, has since retired. His seat was filled by Justice Kennard. Justice Kennard joined the majority when it later held that Foley was fully retroactive.

148. The facts in the case are set forth at Foley v. Interactive Data Corp., 47 Cal. 3d at 663-64, 254 Cal. Rptr. 212-14.

rent position if he agreed to go on a "performance plan." On March 17, 1983, Kuhne gave Foley a choice: resignation or dismissal. Foley refused to resign and was dismissed by IDC. On September 26, 1983, Kuhne subsequently pleaded guilty to embezzlement from his previous employer. IDC retained Kuhne as an employee.

B. The Proceedings Below

Foley then sued IDC. In his second amended complaint, he asserted three separate theories: a tort cause of action alleging a discharge in violation of public policy; a contract cause of action alleging breach of an implied-in-fact promise to discharge for good cause only; and a tort cause of action alleging breach of the implied covenant of good faith.[149]

The trial court sustained a demurrer without leave to amend on all three causes, and entered judgments for the defendant. The court of appeal affirmed.[150] Justice Roth, writing for the court, strictly interpreted the rights of employees. The public policy exception is available only when there is an express statutory violation.[151] A claim for breach of an oral at-will contract is barred by the statute of frauds.[152] Finally, an employer tortiously breaches the implied covenant only where: (1) he violates express personnel procedures, and (2) the employee has served for a lengthy period of time.[153]

C. The Supreme Court Decision

Ultimately, the California Supreme Court held that "tort remedies are not available for breach of the implied covenant in an employment contract to employees who allege they have been discharged in violation of the covenant."[154] Chief Justice Lucas wrote the majority opinion and was joined by three other justices (Panelli, Arguelles, and Eagleson).[155] Justices Broussard, Kauf-

149. *Id.* at 662, 254 In the period between 1981 and 1988, almost all of the courts of appeal recognized the new wrongful discharge tort. There was a marked disagreement among the courts, however, with respect to the, exact nature of the employer's duty under the covenant. By 1986 it was clear that the new tort would have to he reviewed by the supreme court.

150. Foley v. Interactive Data Corp., 193 Cal. App. 3d 28, 219 Cal. Rptr. 866 (1986) (Roth, J.).

151. *Id.*, 193 Cal. App. 3d 35, 219 Cal. Rptr.

152. *Id.*, 193 Cal. App. 3d 35-37, 219 Cal. Rptr. 870-71.

153. *Id.*, 193 Cal. App. 3d 37, 219 Cal. Rptr. 871. The court noted there was a different approach, in the *Khanna* case, and simply disagreed, without further comment.

154. Foley v. Interactive Data, 47 Cal. 3d at 700; 254 Cal. Rptr. 239.

155. *Id.* at 662-700, 254 Cal. Rptr. 212-40.

man, and Mosk all filed dissenting opinions.[156]

In addition to the tort question, the Supreme Court decided two other issues relating to public policy and breach of contract. In Part I of his opinion, Justice Lucas held that the employee did not state a cause of action for violation of public policy.[157] The scope of the court's ruling on the public policy question was limited. The court expressly stated that it has not yet decided the question of whether the sources of public policy are limited to statutes or constitutional provisions.[158]

In Part II of the majority opinion, the court disposed of two issues arising out of the cause of action for breach of contract. First, the court held that a contract for employment does not fall within the Statute of Frauds: the statute did not bar Foley's lawsuit.[159] Second, the court held that in an at-will relationship, the employer's conduct may create an implied-in-fact contract limiting his right to discharge the employee arbitrarily. The court followed *Pugh* and stated that "the totality of the circumstances determines the nature of the contract"; if the plaintiff can plead and prove an implied promise not to discharge except for good cause, he is entitled to contractual damages.[160]

In Part III of his opinion, Justice Lucas addressed the bad faith discharge issue.[161] Part III can be divided into three sections. First, he reviewed and criticized the various appellate decisions recognizing the tort action.[162] Second, he discussed the special relationship model and concluded that "the underlying problem" was "the uncritical incorporation of the insurance model into the

156. *Id.* at 701-24, 254 Cal. Rptr. 240-56.

157. *Id.* at 665-71, 254 Cal. Rptr. 214-16.

158. *Id.* at 669, 254 Cal. Rptr. 217.

159. *Id.* at 671 675, 254 Cal. Rptr. 218-21. The Statute of Frauds provides that an oral contract is unenforceable if it is "[a]n agreement that by its terms is not to be performed within a year from the making thereof." CAL. CIV. CODE § 51624(a) (West 1985). The court held that because "the employee can quit or the employee can discharge for cause, even an agreement that strictly defines appropriate grounds for discharge can be completely performed within one year or within one day, for that matter." Foley v. Interactive Data Corp., 47 Cal. 3d at 673, 254 Cal. Rptr. at 220. *Cf.* White Lightning Co. v. Wolfson, 68 Cal. 2d 336, 438 P.2d 345, 66 Cal. Rptr. 697 (1968).

160. The evidentiary factors that may be used to prove an implied promise to discharge only for cause include "the personnel polices or practices of the employer, the employee's longevity of services, actions or communications by the employer reflecting assurances of continued employment, and the practices of the industry in which the employee is engaged." *Foley*, at 680, 254 Cal. Rptr. 225. The court also suggested that an express at-will contract can preclude proof of an implied promise: several decisions "can be interpreted to preclude enforcement of an implied in fact modification of an on-going employment agreement when some written provision insists on the employee's at-will status." *Id.* at 680, note 12, 254 Cal. Rptr. 225.

161. *Id.* at 682-700, 254 Cal. Rptr. 227-40.

162. *Id.* at 685-89, 254 Cal. Rptr. 228-31.

employment context."[163] Third, the Chief Justice noted that there are many different remedies which can be made available to compensate wrongfully discharged employees. Lucas declared that the selection of the appropriate remedy should be made by the Legislature, not the courts.[164]

Justice Broussard concurred with the majority on the public policy and breach of contract questions, but dissented from Part III of the opinion.[165] He emphasized that many appellate courts recognized the tort; stated that employment is similar to insurance; and rejected Lucas' call for deference to the Legislature. Justice Kaufman agreed with Broussard on these issues.[166] Justice Mosk dissented, not only on the tort issue, but also from Part I of the majority opinion. Mosk refused to narrowly define public policy. He stated that Foley's actions were "in the best interests of society as a whole, and therefore covered by the public policy rule."[167]

VII. Legal Reasoning in Foley

The formal-instrumental tension divided the court in the Foley case. Balanced pro and con arguments were used by the judges in their conflicting opinions.[168]

A. Formalism

The spirit of formalism permeated the majority opinion. Chief Justice Lucas stated a preference for rules, as opposed to standards, in common law. He offered a traditional justification for rules: predictability and certainty.[169] He believed, however, that "it would be difficult if not impossible to formulate a rule that would assure that only 'deserving' cases give rise to tort relief."[170]

The Lucas opinion is also formal in its argument that the judiciary should not make public policy. Law, the majority indicated, is separate from politics:

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163. *Id.* at 689, 689-93, 254 Cal. Rptr. 231-34.
164. *Id.* at 693-700, 254 Cal. Rptr. 240-50.
165. *Id.* at 701-15, 254 Cal. Rptr. 240-50.
166. *Id.* at 715-23, 254 Cal. Rptr. 250-56.
167. *Id.* at 723-24, 254 Cal. Rptr. 256.
168. *See supra* text accompanying notes 46-53.
169. Foley v. Interactive Data Corp, 47 Cal. 3d at 696, 254 Cal. Rptr. at 236. ("Predictability of the consequences of actions related to employment contracts is important to commercial stability.") In a footnote to this observation, the court stated that "the generally predictable and circumscribed damages available for breach of contract reflect the importance of this value in the commercial context." *Id.* at 696, n.33, 254 Cal. Rptr. at 236.
170. *Id.* at 697, 254 Cal. Rptr. at 237.

> Significant policy judgments affecting social policies and commercial relationships are implicated in the resolution of this question in the employment termination context. Such a determination . . . arguably is better suited to legislative decisionmaking.[171]

Lucas, however, did not write a purely formal opinion, because he could not ignore the exception that had been carved out for insurers. Insurance is a special relationship, because of the imbalance in bargaining power between the insurer and the insured.[172] Bad faith misconduct by insurers is tortious. Therefore, Lucas was compelled to address the question of whether employment could be analogized to insurance. This question, in turn, invited an instrumental analysis of the functional purposes which would be served by modifying the legal rule.

Lucas' treatment of this issue is an intriguing variation on formalism. A purely formal opinion would simply cite precedent, limit the exception to insurance on grounds of *stare decisis*, and avoid any consideration of the social effects of the at-will rule. Instead of resting on precedent, however, Lucas essentially relied on a theoretical model drawn from neoclassical economics. An economically rational employer will fire an employee only if that employee's marginal contributions exceed his marginal costs. If an employee is dismissed, he can go into the market and find another position. Lucas stated:

> [A]s a general rule, it is to the employer's benefit to retain good employees. The interests of employer and employee are most frequently in alignment . . . in terms of abstract relationships, as contrasted with abstract insurance relationships, there is less inherent relevant tension between the interests of employers and employees than exists between that of insurers and insureds.[173]

Instead of an abstract, general legal rule, the court invoked an abstract, general economic model. The court then assumed, as any strict formalist would, that the general model inevitably generated a particular conclusion. Profit-maximizing employers will not fire employees for irrational (unfair) motives; therefore, tort remedies are not required to protect workers.

There are, of course, several criticisms that can be offered

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171. *Id.* at 694, 254 Cal. Rptr. at 235. In a footnote, the court added that legislatures "have the ability to gather empirical evidence, solicit the advice of experts, and hold hearings at which all interested parties may present evidence and express their views *Id.* at 694, n.31, 254 Cal. Rptr. at 235.

172. "[W]hen an insurer in bad faith refuses to pay a claim or to accept a policy offer within settlement limits . . . the insured cannot turn to the marketplace to find another insurance company willing to pay for the loss already incurred." *Id.* at 692, 254 Cal. Rptr. at 234.

173. *Id.* at 693, 254 Cal. Rptr. at 234.

against this argument: not all employers act rationally and not all employees can readily find jobs elsewhere. This is not to suggest that Lucas' opinion, on this point, is "wrong." What the opinion does suggest is that, on this issue, the court essentially relied on a typically formal method of reasoning. The general rule (or model) was the significant consideration, not the social outcome.

B. Instrumentalism

By contrast, the arguments in the dissenting opinions illustrate the spirit of instrumentalism. Justice Broussard's opinion indicates that he is comfortable with standards. He noted that a "suitable test" is that "an employer acts in bad faith in discharging an employee if and only if he does not believe he has a legal right to discharge an employee."[174] In a footnote, Broussard intimated that "reasonableness" is also an appropriate standard: "The concept of reasonableness, like that of bad faith, is one familiar to tort law, and not generally considered so unpredictable or subjective as to justify denial of relief."[175]

Justices Broussard and Kaufman were also instrumental in that they refused to treat employees as faceless, impersonal abstractions. They both emphasized the social importance of protecting vulnerable workers.[176] Broussard stated: "Employment is even more important to the community than insurance; most people value their jobs more than insurance policies."[177] Kaufman made the point even more forcefully.[178]

It is not self-evident, however, that the new tort, if recognized, would have protected economically vulnerable employees. The effect of an economic intervention is difficult to calculate in advance.[179] The poor are left unprotected because wrongful dis-

174. *Id.* at 711, 254 Cal. Rptr. at 247.
175. *Id.* at 711, n.10, 254 Cal. Rptr. at 247.
176. *Id.* at 707-10, 718-19, 254 Cal. Rptr. at 244-46, 252-53.
177. *Id.* at 708, 254 Cal. Rptr. at 245.
178. *Id.* at 718-19, 254 Cal. Rptr. at 253.
179. Note, *Protecting At Will Employees Against Wrongful Discharge: The Duty to Terminate Only in Good Faith*, 93 HARV. L. REV. 1816, 1829 (1980). The author observes:

> The liberal rationale for judicial intervention—that inequalities of bargaining power must be recognized and corrected—is problematic. First, this theory fails to explain why an employee in a strong bargaining position, such as a highly skilled person recruited by a marginal firm in need of her skills, may not bargain for job security. Second, even when the parties are clearly not equal bargainers, judicial intervention at best only partially redresses the imbalance. Increased liability for wrongful discharge will generally raise the costs of hiring and firing. By altering only one term—termination rights—among a range of possible terms, which include wage rates, working conditions, and fringe benefits, the court leaves the employer free to shift the cost of the new protection. In most cases employees will eventually wind up 'paying' at least part of the new term's cost.

charge actions are normally filed only by middle and upper class managers.[180] Finally, the recognition of the tort might have had the paradoxical effect of partially defeating its stated purpose. Some commentators have argued that the wrongful discharge tort undermines labor unions.[181] Unions protect economically vulnerable employees, but the remedies for unjustly terminated union members are limited to reinstatement and back pay. The availability of the tort affords unorganized employees greater relief than their unionized counterparts. Therefore, it can be argued, the tort hurts rather than helps employees. In summary, it is not clear that a change in the legal rule would achieve the optimal economic outcome.

Justice Kaufman also stated that the courts possess the institutional competence to choose among competing social and economic policies. This, of course, is a key tenet of instrumentalism. He criticized "judicial abstention" and wrote:

> The imposition of a tort duty is not contingent upon a consensus of so-called experts. The courts are the custodians of the common law—not the economists, or the legislators, or even the law professors. We abdicate that duty when we abjure decision of common law questions under the guise of 'deference' to the political branches.[182]

Significantly, Kaufman quoted with approval the work of two great judicial critics of formalism: Benjamin Cardozo and Roger Traynor.[183] The legal historian Lawrence Friedman has written of these judges:

> The realists had no great reverence for legal tradition as such. Realist judges and writers were openly instrumental; they asked: what use is this doctrine or rule? A string of citations was definitely not a sufficient answer; it was no answer to invoke noble judges from the past, or to appeal to so-and-so's treatise, or to deduce a result logically from principles expressed in prior cases. There was less and less tolerance of artifice, fictions, real and apparent irrationalities. Law had to be a working social tool.[184]

Friedman believes that instrumentalism is now the dominant

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180. Note, *Protecting At Will Employees Against Wrongful Discharge; The Public Policy Exception*, *supra* note 57, at 1937-47 (1983); Feinman, *The Development of the Employment at Will Rule*, *supra* note 3, 130-35.

181. Brody, *Wrongful Termination As Labor Law*, 17 SW. U. L. REV. 434, 465-71 (1988). Brody asserts: "More effectively than any goon squad, it could bust unions." *Id.* at 471.

182. Foley v. Interactive Data Corp., 47 Cal. 3d at 721, 254 Cal. Rptr. at 255.

183. *Id.* at 719-22, 254 Cal. Rptr. at 253-56, quoting, inter alia, B. CARDOZO, THE NATURE OF THE JUDICIAL PROCESS (1921); People v. Pierce, 61 Cal. 2d 879, 395 P.2d 893, 40 Cal. Rptr. 845 (1964) (Traynor, J.); Muskoph v. Corning Hosp. Dist., 55 Cal. 2d 211, 359 P.2d 457, 11 Cal. Rptr. 89 (1961) (Traynor, J.).

184. L. FRIEDMAN, A HISTORY OF AMERICAN LAW (2d. Ed. 1985).

model of reasoning, at least among "an important elite" of judges and lawyers.[185] But formalism, as *Foley* demonstrates, is by no means dead.

C. *Was Foley Correctly Decided?*

It is true that formalism and instrumentalism generate matched sets of stereotyped, recurring arguments. In some instances, however, one argument or the other will be more appropriate to the particular issues presented by a case. In *Foley*, the controlling, and best, argument was the institutional competence argument advanced by Chief Justice Lucas. If the tort had been recognized, the court would have rewritten the law of employment in California.

In *Foley,* the California Supreme Court faced a difficult social and economic problem. Thousands of middle-aged, middle-level managers have been laid off by their employers as a consequence of the restructuring of corporate America in the 1980s.[186] The interests of employers must be balanced against the interests of these displaced executives.

The social problem is enormous and complex. It does not, however, involve the constitutionally protected rights of the interested parties. Since the constitutional revolution of the late 1930's, and the celebrated Footnote Four in the *Carolene Products* decision, courts have been willing to protect fundamental constitutional rights, just as they have been reluctant to overturn social and economic legislation.[187]

Legal rules determine economic outcomes. The new bad faith tort would have triggered a revolution in the employment market if it had been recognized by the supreme court. Every termination would have been a potential tort case. The creation of a new cause of action would have been an exercise in judicial legislation. It would not have been an incremental expansion within the settled principles of the common law. Such policy making, as Chief Jus-

185. *Id.* at 688-89.

186. Cox v. Resilient Flooring Div., 638 F. Supp. 726, 735 (C.C.D. Cal. 1986) ("A major social problem of this decade is what to do about the large numbers of executives and high-level employees, now in their fifties and older, who 'paid their dues, by working their way up corporate ladders which can no longer support their collective weight . . . the cases are arising at a time when whole generations of corporate learning are being rendered irrelevant by foreign competition and changes in technology . . . .")

187. *E.g.*, Kovacs v. Cooper, 336 U.S. 77, 95, 69 S. Ct. 448, 458 (1949) (Frankfurter, Jr., concurring) (". . . those liberties of the individual which history has attested as the indispensable conditions of an open as against a closed society come to this Court with a momentum for respect lacking when appeal is made to liberties which derive merely from shifting economic arrangements"); United States v. Carolene Products Co., 304 U.S. 144, 152, n.4, 58 S. Ct. 778, 783.

tice Lucas rightly emphasized, is a matter best left to the legislature.

Lucas' opinion cannot be seen as a reactionary victory for employers and the status quo. The legislature can repeal *Foley* and allow tort actions, if it so chooses. If it does not act, the people themselves can bypass the normal channels of government and enact legislation through the initiative process.[188] For now, remedies are available within the framework of the long-established rules of contract law. The *Foley* decision made it clear that a discharged employee is free to plead breach of an implied oral contract. One appellate decision filed since the *Foley* decision has even recognized an implied oral promise as superseding at-will clauses in written contracts.[189] Compensatory damages are still available where an employer has breached an implied contract.[190]

CONCLUSION

In this decade, the California Supreme Court has twice considered the availability of tort actions to protect employees. In *Tameny*, the court, by a 5-2 vote, recognized a wrongful discharge tort in an instrumental opinion which provoked formal dissents. During the succeeding eight years, there was an almost complete turnover of the personnel on the court. In *Foley*, the court, by a 4-3 vote, declined to recognize a second wrongful discharge tort in a formal opinion which triggered instrumental dissents.

There are now eleven other wrongful discharge tort cases pending before the court.[191] It can be expected that the arguments associated with formalism and instrumentalism will reappear when the court decides those cases.

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188. CAL. CONST. art. IV (power of the electors to propose statutes and amendments to the constitution, and to adopt or reject them).

189. Rodie v. Max Factor & Co., _ Cal. App. 3d_, 256 Cal. Rptr. 1 (1989).

190. Traynor, *Bad Faith Breach of a Commercial Contract: A Comment on the Seaman's Case*, 8 BUS. L. NEWS, 1, 14 (1984) ("contract damages can be "amplified" because juries can be encouraged as well as guided in bad faith cases to award a higher rather than a lower compensatory award with the leeways and the range of uncertainty that presently exist in the law of contract damages").

191. See cases cited at *supra* note 16, and accompanying text.