NOTES

Farm Crop Energy v. Old National Bank: A Meaningful Test For Damages Under Promissory Estoppel?

I. INTRODUCTION

A 1984 Washington Appellate Court decision, *Farm Crop Energy v. Old National Bank*,[1] provided the court with an opportunity to resolve the confusion in promissory estoppel law[2] by announcing a workable standard for computing damages. The unique facts of the case, and the "appropriate circumstances"[3] test announced by the court increased, rather than ended this confusion.

Old National Bank (ONB) and Farm Crop Energy had entered a conditional loan agreement for the construction of a fuel alcohol plant. Farm Crop subsequently advanced money to the plant contractor, relying on the assurance of an ONB officer that the loan would be made.[4] ONB then refused to make the loan, and Farm Crop brought suit on a number of theories including promissory estoppel. The trial court granted Farm Crop both their reliance costs and lost profits.[5] On

1. Farm Crop Energy v. Old National Bank, 38 Wash. App. 50, 685 P.2d 1097, *cert. granted*, 103 Wash. 2d 1004 (1984).

2. Promissory estoppel is used as a basis of recovery in numerous situations and as application of the doctrine expands into the commercial area, the issue of whether lost profits should be awarded under the doctrine has proven to be very bothersome to courts and commentators alike. *See infra* notes 16-25 and accompanying text. For a review of commercial cases involving promissory estoppel, *see* Metzger and Phillips, *The Emergence of Promissory Estoppel as an Independent Theory of Recovery*, 35 RUTGERS L. REV. 472, 513-28 (1983) (discussing promises by employers and franchisors, sub-contractor bid cases, credit-related promises, and various other "problems," "promises," and "situations"). *Farm Crop* is only the second reported opinion in Washington to squarely address the issue of lost profits under promissory estoppel. The first opinion was Silverdale Hotels v. Lomas & Nettleton, 36 Wash. App. 762, 677 P.2d 773, *cert. denied*, 101 Wash. 2d 1021 (1984) (denying an award of lost profits under promissory estoppel). *See also infra* notes 24 and 52.

3. *Farm Crop*, 38 Wash. App. at 57, 685 P.2d at 1102.

4. *Id.* at 52, 685 P.2d at 1100. *See infra* notes 27-30 and accompanying text.

5. *Farm Crop*, 38 Wash. App. at 52, 685 P.2d at 1102.

appeal, the issue was whether lost profits were recoverable under promissory estoppel.[6] The appellate court held that they were in "appropriate circumstances."[7]

The purpose of this Note is to analyze the issues surrounding an award of lost profits under promissory estoppel and to propose a method for determining when such an award is appropriate. The *Farm Crop* court took a step in the right direction by advocating a flexible approach to the damages question in promissory estoppel cases. However, because of the inherent ambiguity in the test and the failure of the court to articulate any meaningful criteria on which to base a decision, the "appropriate circumstances" standard provides neither guidance nor justification for determining the appropriate measure of damages.[8]

This Note proposes that an award of lost profits under promissory estoppel should be made only when the circumstances surrounding the making of the promise justify enforcing it as if it were a contract.[9] Operating on the assumption that a promise is found to be a reasonable basis for reliance, this Note will propose some criteria by which a court can determine when a promise justifies a damage award in excess of the costs of reliance.[10] These criteria will then be applied to the *Farm Crop* facts to demonstrate that remedies can be administered under a standard that is rational and flexible, yet provides reasonable certainty.[11]

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6. *Id.* at 56, 685 P.2d at 1102.

7. *Id.* at 57, 685 P.2d at 1102.

8. *See infra* notes 71-95 and accompanying text.

9. *See infra* notes 98-114 and accompanying text.

10. This position is taken for the purposes of simplicity. There is authority for granting other remedies, such as specific performance or injunctive relief. *See, e.g.*, Mazer v. Jackson Ins. Agency, 340 So.2d 770, 772-75 (Ala. 1976) (enjoining violation of restrictive covenant); McClatchy Newspapers v. Superior Court, 163 Cal. App. 3d 214, 235-40, 209 Cal. Rptr. 598, 612-15 (1984) (limiting estoppel to carrying out the exact promise of confidentiality made by a grand jury, i.e., sealing records pertaining to one witness); Larabee v. Booth, 463 N.E.2d 487 (Ind. Ct. App. 1984) (granting specific performance of promise to convey land); Christy v. Hoke, 127 Ariz. 169, 171, 618 P.2d 1095, 1096 (1980) (granting specific performance of an oral agreement to grant an easement). However, it is generally required that there be an inadequate remedy at law before equitable relief is granted. *Accord* Tyler Pipe Indus. v. Dep't of Revenue, 96 Wash. 2d 785, 638 P.2d 1213 (1982); Streater v. White, 26 Wash. App. 430, 613 P.2d 187 (1980). Thus, the majority of cases result in an award of monetary damages because that is traditionally seen as adequately fulfilling the need for a remedy in contract actions. The next logical step after determining that money damages are an appropriate remedy is to determine what type of damages to award. *See also infra* note 112-115 and accompanying text.

11. *See infra* notes 119-131 and accompanying text.

II. A BRIEF HISTORY OF THE PROMISSORY ESTOPPEL DAMAGE DISPUTE

Promissory estoppel was originally created to address the problem of enforcing gratuitous promises,[12] which under traditional contract principles were unenforceable because of a lack of consideration.[13] This situation frequently resulted in an injustice because if the promisee undertook action in reliance on a gratuitous promise there was no remedy available if the promisor refused to perform.[14] Promissory estoppel was created to enforce these promises on the basis of the promisee's

12. *See generally* RESTATEMENT (SECOND) OF CONTRACTS § 90 (1981); Henderson, *Promissory Estoppel and Traditional Contract Doctrine*, 78 YALE L.J. 343 (1969) [hereinafter Henderson, *Promissory Estoppel*]; Comment, *Once More Into the Breach: Promissory Estoppel and Traditional Damage Doctrine*, 37 U. CHI. L. REV. 559 (1970) [hereinafter *Into the Breach*].

13. Consideration, in the form of a promise or performance being exchanged for the promise, is the traditional cornerstone of contracts and is seen as the basis for enforcing the contract: without it, a contract is generally unenforceable. "[I]t is the essence of consideration, that, by the terms of the agreement, it is given and accepted as the motive or inducement of the promise. Conversely, the promise must be made and accepted as the conventional motive or inducement for furnishing the consideration." O. W. HOLMES, THE COMMON LAW 293 (1891); Wisconsin & Mich. Ry. v. Powers, 191 U.S. 379, 386 (1983) (Holmes, J.); *Accord* Henderson, *Promissory Estoppel, supra* note 12, at 345 (the classifications of responsibility that we have come to regard as conventional, and which have been accorded black-letter status in the RESTATEMENT OF CONTRACTS, evidence a preoccupation with the belief that only promises for which some agreed price has been paid are deserving of enforcement. Thus, according to the catechism of consideration, action in reliance upon a promise is sufficient reason for enforcement only when the action is bargained for by the promisor and given in return by the promisee.). *See also, Into the Breach, supra* note 12, at 561; RESTATEMENT (SECOND) OF CONTRACTS § 71 (1981).

14. This was because the promise was not bargained for as defined by RESTATEMENT (SECOND) OF CONTRACTS § 71(2) (1981) (a performance or return promise is bargained for if it is sought by the promisor in exchange for his promise and is given by the promisee in exchange for that promise). The classic example of the promisee being left without a remedy is Kirksey v. Kirksey, 8 Ala. 31 (1845) (plaintiff abandoned possession of her land and moved onto her brother-in-law's farm in reliance on his promise that he would provide her with a place to live. After two years plaintiff was asked to leave the farm and was subsequently unsuccessful at recovering damages in a suit based on reliance).

Prior to the creation of promissory estoppel, the courts often struggled with this problem, frequently solving it by finding the promisee's reliance to be consideration for the promise. *See* Depauw University v. Ankeny, 97 Wash. 451, 454, 166 P. 1148, 1149 (1917) (a subscription agreement to pay money to a charitable, benevolent, or education institution is supported by consideration and is therefore enforceable if, in reliance upon such agreement, an act has been done, money expended, or obligations incurred). *Cf.* Young Men's Christian Ass'n v. Olds Co., 84 Wash. 630, 632, 147 P. 406, 407 (1915) (if work has been done or expenditure has been made upon the faith of and in reliance upon a subscription, a consideration is thus furnished to support the promise).

reliance.[15] One of the major issues concerning recovery under promissory estoppel is whether the promisee is entitled to recover expectation damages, or whether the promisee is limited to recovering the costs of reliance.[16] The increasing use of promissory estoppel in commercial cases has sharpened the debate over how recovery under the doctrine should be limited.[17]

Courts and commentators have generally taken three approaches to measuring damages in promissory estoppel cases: the reliance measure,[18] the expectancy measure,[19] and an ad-hoc approach.[20] Advocates of the reliance measure generally

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15. RESTATEMENT (SECOND) OF CONTRACTS § 90, comment a (1981) (allowing recovery of damages based on reliance as an alternative to meeting the consideration requirements of § 71(1) of the RESTATEMENT, which requires that performance or a return promise be bargained for).

16. Interestingly, the first debate over the proper measure of damages occurred at the Reporter's meeting for the RESTATEMENT OF CONTRACTS, with Professor Williston advocating the expectancy measure and Professor Coudert advocating the reliance measure. Their debate also provides an interesting example of when the reliance and expectancy measures would not be equivalent in a gratuitous promise situation. Suppose Johnny's uncle promises him $1000 to buy a car and Johnny relies by purchasing a $500 car. Under the reliance measure Johnny would only be entitled to $500, but under the expectancy measure, as Williston said himself, Johnny would be entitled to the full $1000. 4 ALI Proceedings App. 97-106 (1926).

17. *See generally* Faber & Matheson, *Beyond Promissory Estoppel: Contract Law And the "Invisible Handshake"*, 52 U. CHI. L. REV. 903 (1985) [hereinafter Faber, *Invisible Handshake*]; Henderson, *Promissory Estoppel*, *supra* note 12; Note, *Promissory Estoppel in Washington*, 55 WASH. L.REV. 795 (1980) [hereinafter *Estoppel in Washington*]; *Into the Breach*, *supra* note 12, at 561-65.

18. This measure of damages attempts to put the promisee in as good a position as he was before the promise was made by reimbursing him for his costs incurred in reliance on the promise. Fuller & Perdue, *The Reliance Interest in Contract Damages*, 46 YALE L.J. 2, 54 (1936) [hereinafter Fuller, *The Reliance Interest*]. *See* Goodman v. Dicker, 169 F.2d 684 (D.C. Cir. 1948) (the true measure of damages is the loss sustained by expenditures made in reliance upon the assurance of a dealer franchise); Wheeler v. White, 398 S.W.2d 93, 97 (Tex. 1965) (the promisee is allowed to recover no more than reliance damages measured by the detriment sustained).

19. This measure of damages attempts to put the promisee in as good a position as he would have been had the promise been performed by giving him the value of the expectation the promise created. Fuller, *The Reliance Interest*, *supra* note 18 at 54. *See* Walters v. Marathon Oil Co., 642 F.2d 1098, 1100-01 (7th Cir. 1981); Signal Hill Aviation Co. v. Stroppe, 96 Cal. App. 3d 627, 158 Cal. Rptr. 178 (1979); Chrysler Corp. v. Quimby, 51 Del. 264, 144 A.2d 123, *reh'g denied*, 144 A.2d 885 (1958). *See generally* Faber, *Invisible Handshake*, *supra* note 17; Note, *What Should Be The Extent Of Damages In Pennsylvania In An Action Of Assumpsit Based On The Doctrine Of Promissory Estoppel?*, 59 DICK. L. REV. 163 (1955) [hereinafter Note, *Pennsylvania Damages*]; Note, *Promissory Estoppel-Measure of Damages*, 13 VAND. L. REV. 705 (1960) [hereinafter *Measure of Damages*].

20. *See Farm Crop*, 38 Wash. App. 50, 685 P.2d 1097; Hoffman v. Red Owl Stores, 26 Wis. 2d 683, 133 N.W. 2d 267 (1965); *Into the Breach*, *supra* note 12, at 559; and 1A A. CORBIN, CONTRACTS § 205, at 240 (1963). This, of course, assumes that the court finds

argue that because a contract has not been formed and the purpose of enforcing the promise is to prevent an injustice, the promisee should not be permitted to recover more than the cost of reliance.[21] Advocates of the expectancy measure argue that if the transaction is worthy of legal enforcement, then it is economically desirable to enforce the expectation interest and thereby encourage similar transactions.[22] Finally, those who advocate an ad-hoc approach argue that promissory estoppel is an equitable remedy intended to prevent injustice and that damages should be awarded based on the merits of the case.[23] Washington has adopted an ad-hoc approach under the rubric of "appropriate circumstances."[24] As will be seen, the *Farm Crop* decision does not clearly explain what constitutes an appropriate circumstance for an award of lost profits.[25]

III. THE FARM CROP FACTS

Farm Crop Energy, a Washington corporation, was formed

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the promise to be binding. The court always has the option of doing nothing by finding the promise to be non-binding.

21. This argument focuses on the intended purpose of promissory estoppel to prevent injustice in situations in which a contract has not been properly formed. Since there is not a full contractual agreement, the argument is that full contract damages should not be available. Allowing such a recovery, it is argued, will be unjust to the promisor and will discourage valuable negotiations and transactions. It is also argued that, in many cases, expectation damages would be highly disproportionate to the costs of reliance. *See* Boyer, *Promissory Estoppel and Limitations of the Doctrine*, 98 U. PA. L.REV. 459 (1950) [hereinafter Boyer, *Limitations*]; *see generally Estoppel in Washington*, *supra* note 12.

22. Other arguments include the difficulty of measuring reliance, the fact that § 90 of RESTATEMENT (SECOND) OF CONTRACTS is located in the chapter on formation of contracts, and that promissory estoppel is an emerging basis of contract independent of consideration. This was Professor Williston's position in the debates over the forebearer to § 90. 4 ALI Proceedings App. 97-106 (1926). *See also* Faber, *Invisible Handshake*, *supra* note 17; *Into the Breach*, *supra* note 12; *Pennsylvania Damages*, *supra* note 19; *Measure of Damages*, *supra* note 19.

23. This is the position of the RESTATEMENT. Comment d provides that "the same factors which bear on whether any relief should be granted also bear on the character and extent of the remedy." RESTATEMENT (SECOND) OF CONTRACTS § 90, comment d (1981). *See also* 1A A. CORBIN, CONTRACTS § 205 (1964) (there is no reason why the courts of the present day should not "make the remedy fit the crime" and make the amount of a judgment for damages depend upon the special circumstances and the merits of the claims of all existing claimants).

24. This was the result in *Farm Crop* and it could be argued that the Washington Supreme Court implicitly recognized this when they denied certiorari in the case of Silverdale Hotels v. Lomas & Nettleton, 36 Wash. App. 762, 677 P.2d 773, *cert. denied*, 101 W.2d 1021 (1984). In that case, the Court of Appeals based its denial of lost profits not on any rule of law but rather on the fact that the promisor had not promised the promisee any profits. *Id.* at 772, 677 P.2d at 790. *See infra* note 52.

25. *See infra* notes 48-60 and accompanying text.

in 1980 for the purpose of constructing and operating a fuel alcohol plant in Washington. The investors in Farm Crop approached ONB in February of 1981 intending to obtain a loan for the construction of the plant.[26] ONB issued a loan commitment letter with a number of conditions attached.[27] In May of 1981, some of Farm Crop's officers met with Mr. Danelo, an ONB officer, to discuss these conditions.[28] At this meeting, Farm Crop informed Mr. Danelo that substantial savings on the plant's construction could be had if $175,000 were immediately advanced to Matrix Energy, the plant contractor.[29] Farm Crop's Officers contended that Mr. Danelo told Farm Crop to go ahead and advance the money, because the loan would be made.[30] After Farm Crop advanced the money to Matrix Energy, ONB announced that because Farm Crop had not met the conditions, the bank would not make the promised loan.[31]

Farm Crop brought suit against ONB alleging promissory estoppel as one basis of recovery.[32] At trial, the jury returned a verdict for Farm Crop and awarded $175,000 in reliance damages and $120,000 in lost profits.[33] ONB appealed, contending, among other things, that lost profits could not be recovered in an action based on promissory estoppel.[34] The Court of

26. *Farm Crop*, 38 Wash. App. at 52, 685 P.2d at 1099.

27. Included in the conditions were individual guarantees from each of the investors, some limited and some unlimited, and a $500,000 loan guaranty from the Small Business Administration (SBA). The SBA required unlimited guarantees from all investors, contracts for raw materials, and contracts for the alcohol and spent grain. *Id.*

28. *Id.*

29. *Id.* at 52, 685 P.2d at 1100.

30. There was some dispute at trial as to whether Mr. Danelo said the loan would go through unconditionally or whether he indicated that the conditions still attached. *Id.* It might be asked at this point whether Farm Crop could reasonably believe that the conditions did not attach after four months of negotiations and being fully aware that the conditions had not been met. These factors could have some bearing on what the parties reasonable expectations might have been when the assurances were made.

31. *Id.*

32. Farm Crop pleaded breach of contract, waiver, equitable estoppel and promissory estoppel. *Id.*

33. *Id.* at 52, 685 P.2d at 1099.

34. *Id.* at 56, 685 P.2d at 1102. ONB was correct on this point because although Washington courts had explicitly recognized promissory estoppel in Luther v. National Bank of Commerce, 2 Wash. 2d 470, 484, 98 P.2d 667, 673 (1940) and also recognized that it could serve as a basis for an action for damages, Klinke v. Famous Recipe Fried Chicken, Inc., 94 Wash. 2d 255, 259, 616 P.2d 644, 646 (1980), no previous Washington decision had allowed an award of lost profits under a clear case of promissory estoppel. *See* Central Heat, Inc. v. Daily Olympian, Inc., 74 Wash. 2d 126, 443 P.2d 544 (1968) (expectancy recovery, but not a true promissory estoppel decision as there was

Appeals rejected this contention and held that lost profits could be recovered under promissory estoppel in "appropriate circumstances."[35] The court reasoned that an award of lost profits was appropriate because Farm Crop had lost its opportunity.[36]

IV. THE COURT'S REASONING IN FARM CROP

The Court of Appeals recognized that two lines of analysis could be applied to the Farm Crop case.[37] The first begins with the premise that the commitment letter from ONB created a binding contractual agreement.[38] The court reasoned that the jury could find Farm Crop had not met the conditions of the letter.[39] Thus, unless there had been a waiver of the conditions or an equitable estoppel, Farm Crop would not be entitled to performance.[40] The court stated that ONB's May assurance could be treated under either of these doctrines,[41] but the

consideration for the defendant's promise). *See also Luther*, 2 Wash. 2d at 471, 98 P.2d at 668 (expectancy recovery but as a contract had been formed, Luther is questionable authority for promissory estoppel). *See generally* Estes v. Hammerstead, Inc., 8 Wash. App. 22, 503 P.2d 1149 (1972) (reliance recovery); Hellbaum v. Burwell & Morford, 1 Wash. App. 694, 463 P.2d 225 (1969) (reliance relief). *Cf. Estoppel in Washington*, *supra* note 17, at 814 n.103 (concluding that the few Washington decisions reaching the issue of appropriate relief have split between the reliance and the expectancy measure).

35. *Farm Crop*, 38 Wash. App. at 57, 685 P.2d at 1102.

36. *Id.* There may have been other factors influencing the court's decision. *See infra* notes 57-60 and accompanying text.

37. "Although it might have been preferable to treat this latter [May] assurance under the doctrines of waiver and equitable estoppel, it is possible to treat it as a separate promise. Thus, it was not error to instruct on the doctrine of promissory estoppel." *Id.* at 53, 685 P.2d at 1100. The two lines of analysis lead to entirely different bases and theories of recovery. Under the waiver or equitable estoppel analysis, recovery would be based on the commitment letter with Farm Crop being excused from performance of the letter's conditions because of the May assurance. Recovery on that basis would be on a contract theory. Under the promissory estoppel analysis, recovery would be based on the May assurance alone. As the court correctly noted, recovery under promissory estoppel could not be based on the commitment letter because promissory estoppel is used to avoid injury when parties have failed to properly form a contract. *Id.* at 57, 685 P.2d at 1102. Promissory estoppel is an equitable theory. *See also* notes 40-42 *infra* and accompanying text.

38. *Id.* at 53, 685 P.2d at 1100.

39. *Id.* It appears from the record that not all of the investors had signed the guarantees and no grain contract had been signed by Farm Crop. Not having met these requirements, the investors also had not obtained the required SBA loan guarantee.

40. *Farm Crop*, 38 Wash. App. at 53-54, 685 P.2d at 1100.

41. This is not to say that the outcome would have been favorable to Farm Crop if the May assurance was treated under either of these doctrines. Aside from the individual problems discussed below, recovery under either doctrine would depend on

Court held that promissory estoppel also was applicable.[42]

In its analysis, the court held that the May assurance met the elements of promissory estoppel:

> (1) A promise which (2) the promisor should reasonably expect to cause the promisee to change his position (3) which does cause the promisee to change his position (4) justifiably relying on the promise, in such a manner that (5) injustice can be avoided only by enforcement of the promise.[43]

Therefore, although the jury could find that ONB was not bound by the loan commitment,[44] Farm Crop's reliance on ONB's May assurance provided a proper basis for allowing Farm Crop to recover under the doctrine of promissory estop-

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a finding that the loan commitment letter constituted a binding contractual agreement.

Waiver is the intentional relinquishment of a known existing right. Wagner v. Wagner, 95 Wash. 2d 94, 621 P.2d 1279 (1980). Theoretically, under a waiver analysis the jury could have found that ONB had waived its right to demand performance of the commitment letter's conditions and therefore ONB was liable for breach of contract. However, as the Court of Appeals pointed out, if ONB was not yet entitled to performance of the conditions when it made the May assurance, then the assurance would not constitute a waiver of the conditions. *Farm Crop*, 38 Wash. App. at 54, 685 P.2d at 1100. Thus, although the parties agreed that waiver applied to the case, Farm Crop still might not recover under a waiver theory because either the right to demand performance had not yet matured and therefore, could not be waived in May or because the commitment letter did not create a contractual agreement.

Equitable estoppel requires three elements:

> (1) an admission, statement, or act inconsistent with the claim afterwards asserted; (2) an action by the other party on the faith of such admission, statement, or act; (3) an injury to such other party from permitting the first party to contradict or repudiate such admission, statement, or act.

Wilson v. Westinghouse Elec. Corp., 85 Wash. 2d 78, 81, 530 P.2d 298, 300 (1975). Under an equitable estoppel analysis, ONB could be estopped from demanding performance of the conditions because of the May assurance and therefore, be liable for breach of contract based on their subsequent revocation of the commitment letter. However, it must again be emphasized that this type of theory would provide Farm Crop with a recovery only if the commitment letter was found by the jury to be a contractual agreement.

The possibility of the jury finding that the commitment letter did not create a contractual agreement appears to be what necessitated an instruction on promissory estoppel. If the jury were to so find, neither equitable estoppel nor waiver would provide a remedy because they are defensive doctrines and do not in themselves provide an affirmative basis for relief. Promissory estoppel, on the other hand, could provide a grounds for recovery based on the May assurance alone.

42. *Farm Crop*, 38 Wash. App. at 53, 685 P.2d at 1100. This assumes that the contractual analysis of waiver or equitable estoppel would be inapplicable, for if it were, then recovery would be on the commitment letter (contract) and not on the May assurance. *See infra* note 41.

43. *Id.* at 52, 685 P.2d at 1100 (citing Corbit v. J. I. Case Co., 70 Wash. 2d 522, 539, 424 P.2d 290, 300-301 (1967)).

44. *See supra* notes 38-41 and accompanying text.

pel.[45] Holding ONB liable on the basis of the May assurance rather than on the loan commitment significantly altered the measure of damages. Under the first line of analysis, recovery would be based on the parties' original contract,[46] whereas recovery under the second line of analysis is based solely on the May assurance.[47]

The court then analyzed the proper measure of damages under promissory estoppel.[48] The court cited a number of judicial and scholarly authorities and determined that the general rule was to fashion an equitable remedy.[49] Having decided to fashion an equitable remedy, the court determined that equity called for an award to Farm Crop of not only their reliance expenditures but also their lost profits.[50] The reason proffered was that, "[p]resumably, Farm Crop and ONB anticipated a profitable venture. In relying on the loan commitment from ONB, Farm Crop did not seek alternative financing for its venture. Not only did it lose its money advanced, it lost its opportunity."[51] The court concluded by holding that these were "appropriate circumstances"[52] for an award of lost profits,

45. *Farm Crop*, 38 Wash. App. at 53, 685 P.2d at 1100.

46. *Id.* at 53-54, 685 P.2d at 1100. If recovery were on a contractual basis, Farm Crop would be entitled to all the normal contract damages including expectation damages. There would be no need for a debate as to whether they were entitled to lost profits as a matter of substantive law.

47. *Id.* This takes the case out of a contractual analysis and raises the issue as to whether Farm Crop is entitled to recover the same damages under promissory estoppel they would have if recovery had been on the contract.

48. *Id.* at 56, 685 P.2d at 1102.

49. *Id.* The court noted that the cases differed as to an award of lost profits. *Compare* Goodman v. Dicker, 169 F.2d 684 (D.C. Cir. 1948) (denying lost profits); Fretz Const. Co. v. Southern Nat'l Bank, 626 S.W.2d 478 (Tex. 1981) (denying lost profits); Hoffman v. Red Owl Stores, 26 Wis. 2d 683, 133 N.W.2d 267 (1965) (denying lost profits); with Chrysler Corp. v. Quimby 51 Del. 264, 144 A.2d 123, *reh'g denied*, 144 A.2d 885 (1958) (awarding lost profits); Kramer v. Alpine Vly. Resort, Inc., 108 Wis. 2d 417, 321 N.W. 2d 293 (1982) (awarding lost profits). The court cited the following authorities as specifically supporting a flexible approach: Hoffman v. Red Owl Stores, 26 Wis. 2d at 695, 133 N.W.2d at 276; 1A A. CORBIN, CONTRACTS § 205, at 240 (1963); J. CALAMARI & J. PERILLO, CONTRACTS § § 6-12 (1977); RESTATEMENT (SECOND) OF CONTRACTS § 90 and comment d (1981) (The remedy granted for breach may be limited as justice requires).

50. *Farm Crop*, 38 Wash. App. at 57, 685 P.2d at 1102.

51. *Id.*

52. The appropriate circumstances language derives from the court's attempt to distinguish the situation in *Farm Crop* from that in a recent Division Two opinion. Silverdale Hotels v. Lomas & Nettleton, 36 Wash. App. 762, 677 P.2d 773 (1984). In *Silverdale*, a construction lender had promised to cover a contractor's construction draws. When the lender refused to pay the draws unless the borrower deposited $1,200,000 with the lender, the contractor sued for the draws and lost profits based on

there was adequate proof of the lost profits,[53] and that the trial court did not err in submitting the issue to the jury.[54]

The court's reasoning that Farm Crop had lost its opportunity is worthy of further inquiry because it is unclear what the court meant by lost opportunity.[55] While it is clear that Farm Crop had lost the opportunity to get a loan from ONB, it is not so clear that this prevented them from entering the fuel alcohol business.[56] That the court did not question Farm Crop's

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promissory estoppel. The court held that the contractor was not entitled to lost profits because the lender had only promised to pay the contractor's draws and had not promised to pay any profits. *Id.* at 772, 677 P.2d at 780. The court held in *Farm Crop* that *Silverdale* was not to be read as prohibiting an award of lost profits under promissory estoppel in appropriate circumstances. *Farm Crop*, 38 Wash. App. at 57, 685 P.2d at 1102.

53. *Id.* at 57-58, 685 P.2d at 1102-1103. The court cites Larsen v. Walton Plywood Co., 65 Wash. 2d 1, 15, 390 P.2d 677, 686 *modified on reh'g*, 65 Wash. 2d 21, 396 P.2d 879 (1964), as providing the test for lost profits. Under *Larsen*, lost profits are recoverable when they are (1) within the contemplation of the parties at the time the contract was made, (2) the proximate result of the defendant's breach, and (3) proven with reasonable certainty. At this point, it may be asked whether lost profits were proven with the requisite certainty, an issue not otherwise dealt with in this Note. Farm Crop was a new business and the ordinary rule is that a new business may not recover prospective profits because they are inherently speculative. *Larsen*, 65 Wash. 2d at 16, 390 P.2d at 687. However, in Washington an expert may testify as to the market conditions and profitability of similar businesses and thereby provide a basis for calculating prospective profits of a new business. *Id.* Oddly enough, Farm Crop's own expert, the owner of Matrix Energy and future co-operator of Farm Crop's plant, testified that his own plant had been losing money. In addition, other fuel alcohol plants had been financial disasters. Despite this evidence, the court concluded that lost profits had been proven with the requisite certainty. *Farm Crop*, 38 Wash. App. at 57, 685 P.2d at 1102.

54. *Farm Crop*, 38 Wash. App. at 53, 685 P.2d at 1101.

55. If the court means simply that Farm Crop lost the opportunity to enter the fuel alcohol business then it is supporting an award of lost profits on a very superficial analysis. Aside from the problems of causation discussed in the text accompanying this footnote, the court's rationale would support an award of lost profits in almost any action brought by a promisor. By nature, any refusal to perform results is the loss of an opportunity. However, the loss of an opportunity has never been considered a sufficient basis alone to support an award of lost profits. *See infra* notes 84-88 and accompanying text.

If the court means that Farm Crop suffered an opportunity cost by entering the transaction with ONB, the court is undoubtedly correct. However, by moving from that point straight to an award of lost profits, the court overlooks many of the reasons for awarding lost profits in cases where a party has incurred an opportunity cost. Such reasons may call for different results under promissory estoppel than they do under contract. *See infra* notes 84-88 and accompanying text.

56. Specifically, it is not clear that Farm Crop could not have obtained a loan elsewhere and continued its endeavor to enter the fuel alcohol business. Assuming arguendo that it was proper for the court to award damages beyond the costs of reliance, it is not clear why the court did not address the issue of mitigation of damages, a normal requirement in a contract action for damages. *See* 5 A. CORBIN, CONTRACTS § 1039 (1964) (since the purpose of the rule governing damages is to put

failure to obtain another loan indicates that the ONB loan was Farm Crop's only opportunity. This could be one explanation of why the court believed the lost opportunity argument alone justified an award of lost profits.[57]

A second possible explanation is that the court felt ONB should be held to the consequences of its bargaining tactics. Although the loan agreement was an arm's length transaction, it is clear from the facts that ONB controlled the terms. During the four months prior to the May assurance, Farm Crop expended considerable time and effort in meeting ONB's demands.[58] By relying on ONB's May assurance, the Farm Crop investors committed themselves both to construction of the plant and to ONB as a lender. The court may have felt ONB was at fault for assuring that the loan would go through in light of the parties' prior conduct and the reliance induced by the assurance.[59] Thus, the court may have perceived the award of lost profits as a way to punish the bank and deter them from inducing reliance on behalf of borrowers. If this was the purpose the court had in mind, then the award of lost profits was clearly inappropriate. Punishment has never been regarded as a desirable or proper remedial goal of contract law.[60]

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the injured party in as good a position as he would have been put by full performance of the contract, the plaintiff is unable to recover for losses that he could have avoided by reasonable effort.). RESTATEMENT (SECOND) OF CONTRACTS § 350 (1981) (damages are not recoverable for loss that the injured party could have reasonably avoided without undue risk, burden or humiliation). This rule is applied in Washington. *See* Westland Const. Co. v. Chris Berg, Inc., 35 Wash. 2d 824, 837, 215 P.2d 683, 691 (1953) (one who has suffered because of the breach of a contract by another has a duty to make a reasonable effort to mitigate his damages). In a lending case, this would require the borrower to seek out a substitute loan and then to sue for his costs incurred in obtaining the substitute loan. Such damages would be measured by the excess of the costs and interest rate of the new loan over those of the old loan. Alternatively, damages could be measured by the difference between the market rate at the time of breach and the original agreement's rate. Theoretically, this would enable the borrower to continue in his endeavor, and only if it is impossible for him to do so should the court award lost profits.

57. *Farm Crop*, 38 Wash. App. at 57, 685 P.2d at 1102.

58. Farm Crop had changed plant contractors at ONB's request, was in the process of obtaining the SBA loan guaranty and the inputs and outputs contracts required by the SBA loan guaranty, and a majority of the investors had agreed to the personal guarantees. *See* Record at 56, 57, 99, 100, 1091-94, *Farm Crop*.

59. The court may have felt that ONB was not exercising ordinary care when it made the assurance. It would not necessarily be error to base a holding on this factor. The RESTATEMENT § 90 recognizes fault because the promise is enforced to the extent necessary to avoid injustice. RESTATEMENT (SECOND) OF CONTRACTS § 90 (1981).

60. The punishment would have to be covert, of course, due to the contract rule against awards of punitive damages. *See* 5 A. CORBIN, CONTRACTS § 1077 (1964) (it can

V. IMPLICATIONS OF THE FARM CROP DECISION

Certainly one of a court's primary concerns in making the decision should be what kind of behavior the decision will encourage in the future for parties in similar situations.[61] While it is good policy to discourage banks from making promises that are unlikely to be fulfilled, the result in Farm Crop may have the effect of discouraging economically desirable transactions. Presumably, there are situations in which it would be advantageous to the promisee to make payments to third parties prior to final approval of a loan.[62] Of course, the promisee is not going to make an advance of this nature without some kind of assurance from the bank that he is not risking the loss of his advancement if the loan is not made.[63] Ordinarily, a bank would not make such an assurance, but a bank might be willing to do so in special circumstances.[64]

In light of the *Farm Crop* decision, banks will be unwilling to make such assurances, regardless of the circumstances, because banks will see potentially prohibitive liability flowing from such promises.[65] In *Farm Crop*, the liability beyond reli-

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be laid down as a general rule that punitive damages are not recoverable for breach of contract); RESTATEMENT (SECOND) OF CONTRACTS § 355 (1981) (punitive damages are not recoverable for a breach of contract). *See also* Lincor Contractors v. Hyskell, 39 Wash. App. 317, 320, 692 P.2d 903, 906 (1984) (the purpose of awarding damages for breach of contract is to [not] penalize the defendant).

61. Fuller and Perdue recognized this principle when they said Nietzsche's observation that the most common stupidity is in forgetting what one is trying to do has special applicability to the legal profession. Fuller, *The Reliance Interest*, *supra* note 18, at 54.

62. *Farm Crop* is a prime example of this. Although it was not clear what the savings would have been from the $175,000 advance, it is reasonable to assume they were substantial. Otherwise, Farm Crop would not have gone through the trouble of raising capital to make the advance.

63. This too is exemplified by *Farm Crop* because it is extremely doubtful that ONB would have made the May assurance had it thought it could end up liable for lost profits if it later refused to make the loan.

64. Such circumstances may include situations where the bank forsees nothing in its control that would prevent it from making the loan, such as an undisclosed bad credit history or an unexpected failure of a borrower to satisfy lending conditions. Another situation would be where the proposed advancement is relatively insignificant. Finally, banks may be willing to advance where the advancement would somehow benefit the bank, such as by increasing the value of the bank's security interest in collateral. For example, by allowing the bank to take a purchase money security interest in fixtures which has priority over a subsequently recorded construction lien under WASH. REV. CODE § 62A.9 (1986), as opposed to an ordinary security interest in fixtures which does not have priority over a construction lien.

65. Lost profits can run as high as hundreds of millions of dollars depending on the type of business, the size of investment and various other factors. Unlike reliance expenditures, which are generally small and controllable to some degree by the

ance was only $120,000,[66] but it is not difficult to imagine a case in which the lost profits would be significantly higher. Additionally, liability for lost profits is likely to be highly disproportionate to the expenditures made in reliance on the promise.[67] Therefore, banks will be unlikely to make this type of assurance and many opportunities to save resources will be unnecessarily foregone. Protection of the reliance interest, on the other hand, would discourage most of these types of assurances, but would still allow banks the option of making assurances based on their own assessment of the potential costs.[68] This would be more efficient than protection of the expectation interest[69] while still deterring banks from making promises they only marginally intend to fulfill.[70]

VI. THE PROBLEMS IN THE COURT'S ANALYSIS

Assuming the court correctly concluded that ONB should be held liable under the doctrine of promissory estoppel based on the May assurance, several problems arise from the court's analysis of the appropriate remedy. The first of these problems is whether it is appropriate to attribute Farm Crop's lost profits to ONB's refusal to perform.[71] A second question is whether the showing of lost opportunity should be the single requirement necessary to support an award of lost profits on a non-contractual theory of recovery.[72] Finally, the court pays little heed to what the parties may have contemplated at the

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promisor, there is no predicting what lost profits may be and the promisor has no way of controlling their amount. It is unlikely that banks will be willing to underwrite reliance expenditures knowing they will be liable for lost profits, but not knowing the amount of the lost profits or how to limit them.

66. *Farm Crop*, 38 Wash. App. at 53, 685 P.2d at 1099 ($295,000 (award) - $175,000 (reliance) = $120,000 attributable to lost profits).

67. Indeed, some commentators have advocated that this be a factor to be considered in determining whether to award lost profits. *See Into the Breach*, *supra* note 12, at 564 n.35; *Expanded Application of Promissory Estoppel in Restatement of Contracts, Section 90*, 65 MICH. L. REV. 351, 356 (1966).

68. In this situation, the bank presumably would look at the benefits of the advance, the amount of reliance the loan will induce, and the likelihood that the loan will be made. *See infra* notes 125-131 and accompanying text.

69. *See infra* notes 125-130 and accompanying text.

70. *See infra* notes 125-130 and accompanying text.

71. This raises the issue of causation. Assuming that ONB's failure to perform caused Farm Crop to lose its opportunity, it is appropriate to say in light of all the circumstances that it caused the loss of profits.

72. This addresses one of the unintended consequences of the *Farm Crop* decision. In the opinion, the court seems to support a per se type of liability that would attach any time a finding of lost opportunity is made.

time the May assurance was made or to what their expectations were in light of the already existing commitment letter.[73]

The causation issue is a key point in the analysis. In other commercial cases using promissory estoppel as the basis of recovery, lost profits are awarded on the rationale that they are a direct result of the breach.[74] That analysis fails in the instant case.[75] Implicit in a finding that profits were lost as a direct result of the breach is a finding that there was some close relationship between the representation[76] and the lost profits.[77] In the franchise and firm offer cases, profits are the sole purpose for the representation being made. As a result, they are the primary factor in guiding the promisee's decision to rely on a representation.[78] When the promisor fails to perform, the promisee has lost that which induced him to rely on the representation, the profits he would have enjoyed by having the promisor perform.[79]

When this analysis is applied to a loan case, a number of

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73. In light of the fundamental theory underlying contract law (the theory that the courts should enforce the agreement as the parties would have at the time the promise was made), such an oversight is a serious one. *See* RESTATEMENT (SECOND) OF CONTRACTS § 344 comment a, for the proposition that "The law of contract remedies implements the policy in favor of allowing individuals to order their own affairs by making legally enforceable promises".

74. *See* Walters v. Marathon Oil Co., 642 F.2d 1098, 1100-01 (7th Cir. 1981) (lost profits awarded because plaintiff suffered a loss of profits as a result of plaintiffs' reliance upon the defendant's promise); Chrysler Corp. v. Quimby, 51 Del. 264, 277, 144 A.2d 123, 134, *reargument denied*, 144 A.2d 885 (1958) (loss of three months profits direct result of breach); Gerson Elec. Constr. Co. v. Honeywell, Inc., 117 Ill. App. 3d 309, 312, 453 N.E.2d 726, 728 (1983) (finding promisees entitled to lost profits when they have suffered lost profits as a direct result of the reliance on the promise).

75. *See* Bixler v. First Nat'l Bank of Oregon, 49 Or. App. 195, 200, 619 P.2d 895, 899 (1980) (plaintiff failed to prove lost profits with sufficient particularity); Wheeler v. White, 398 S.W.2d 93, 96-97 (Tex. 1966) (loan case where court refused to award lost profits under promissory estoppel).

76. Hereinafter, a promise that justifies enforcement under promissory estoppel will be referred to as a "representation" to avoid any confusion with a promise that is enforceable as a contract.

77. That is, profits are usually what induce the reliance on the representation and are usually a point of bargaining between the parties.

78. For an example of promissory estoppel in a subcontractor bid case, *see Gerson*, 117 Ill. App. 3d at 312, 453 N.E.2d at 728. For examples in precontractual franchise negotiations, *see also Walters*, 642 F.2d at 1100-01 (allowing recovery of lost profits); Walker v. KFC Corp., 515 F. Supp. 612, 616 (S.D. Cal. 1981) (allowing recovery); *Chrysler*, 51 Del. at 277, 144 A.2d at 134 (allowing recovery of lost profits). *Contra* Goodman v. Dicker, 169 F.2d 684, 685 (D.C. Cir. 1948) (denying lost profits); Klinke v. Famous Recipe Fried Chicken Co., 94 Wash. 2d 255, 259, 616 P.2d 644, 646 (1980) (denying lost profits); Hoffman v. Red Owl Stores, 26 Wisc. 2d 683, 692, 133 N.W.2d 267, 274 (1965) (denying lost profits).

79. *See Into the Breach*, *supra* note 16, at 567.

problems arise. Because the bank represents only that it will make a loan, the connection between profits and the representation is more tenuous than in other commercial cases. There are four reasons for this. First, in a lending transaction the borrower is bargaining for the use of money and the lender is bargaining for the profit gained by allowing the borrower to use his money. The purpose of the loan ordinarily is to invest in capital goods, and therefore is only indirectly related to profits.[80] Second, profits would be the same regardless of the lender and it is doubtful that profits are a factor in the borrower's determination to rely.[81] Third, because banks do not make representations as to profits, the borrower would not consider that a factor in selecting between potential lenders.[82] Finally, in most commercial situations, the representation is likely to be the culmination of the parties' bargaining process, whereas in lending cases the representation is probably collateral to the parties' primary bargaining.[83] Thus, the connection between the representation and profits is not as close in loan cases as it is in some other commercial cases.

Another major problem with the court's analysis is its conclusion that a lost opportunity justifies an award of lost profits.[84] In so concluding, the court implies that the benefits foregone in entering the agreement are equal to the benefits

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80. That is, although the parties bargain for a loan they do not bargain over what profits the loan will generate. The borrower bargains for the use of the lender's money so he can invest in assets that will generate income. Obviously, if the borrower cannot generate profits it is unlikely that he would borrow the money. However, the borrower's profit motive makes no difference to the lender as the lender bargains only for the highest rate of return on the loaned money. The lender gets that rate of return regardless of whether the loan generates any profits for the borrower or not. Thus, profits are only incidentally related to the transaction.

81. This is because of the fungible nature of a bank loan. The bank makes the loan because it feels it will make a profit off the interest charged on the loan; as long as the borrower can meet the payment schedule, the bank is indifferent to whether it makes a profit or not. When the borrower seeks the money to finance his venture, his profits depend more on factors extrinsic to the bank loan than on the loan itself. This is because the law assumes the same legal interest rate may be obtained elsewhere.

82. *See supra* note 81.

83. That is, the parties will usually have some kind of agreement as to when and under what conditions the loan is to be made. The borrower then comes in and tells the lender he can save money by advancing money to the contractor or seller before the loan closes, as was done in *Farm Crop*. This type of promise, which is made outside the context of the parties' negotiations (yet forms a basis for liability), is not the same as a promise that culminates the parties' bargaining, but is unenforceable due to a technicality such as the statute of frauds. The latter situation frequently occurs in franchise cases. *See infra* note 94.

84. *Farm Crop*, 38 Wash. App. at 57, 685 P.2d at 1102.

that would accrue to the promisee by entering the agreement, and for that reason alone, lost profits should be awarded. But by its nature, a foregone opportunity is inferior to the alternative selected and presumably would yield a smaller amount of profits.[85] If that is the case, then the profits under the second opportunity should be calculated and awarded as damages. As some commentators have pointed out, however, this type of calculation is so difficult, and the difference between it and the expectancy interest is normally so small, that the expectancy interest is awarded as a matter of expediency.[86] Thus, the promisee who is allowed to realize more than the value of his lost opportunity fares considerably better than a plaintiff in a traditional action who must generally show more than lost opportunity to recover lost profits.[87] Generally, the promisee should be required to show that there was a mutually beneficial exchange and that it would be economically beneficial to award lost profits.[88]

A third problem with the court's analysis is its finding that lost profits were in the contemplation of the parties.[89] Although it is probable that lost profits were in the contemplation of Farm Crop, it is not as clear that lost profits were in the contemplation of ONB.[90] The fact that ONB asked for a number of personal guarantees and other collateral at the time of the original agreement implies that ONB was not as impressed with the potential profitability of the plant as the Farm Crop investors were. Additionally, as pointed out earlier,

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85. *See Into the Breach*, *supra* note 12, at 568.

86. *See* Drennan v. Star Paving Co., 51 Cal. 2d 409, 333 P.2d 757 (1958) (where the court applied this formula to a subcontractor bid case). *See also Into the Breach*, *supra* note 12, at 568.

87. Aside from the factors below, there are the requirements of certainty, forseeability, and mitigation. The court should not forget these points merely because the court is applying promissory estoppel rather than contract principles.

88. This is a recognition that the bargaining process and the requirement of consideration allows the parties to determine what rights and obligations are most efficient as between them and to determine at the point of exchanging consideration whether they want those rights and obligations to become permanently fixed. *See generally* J. CALAMARI AND J. PERILLO, CONTRACTS § § 1-1 through 1-5 (1977); A. KRONMAN AND R. POSNER, THE ECONOMICS OF CONTRACT LAW 1-67 (1979).

89. *Farm Crop*, 38 Wash. App. at 58, 685 P.2d at 1103.

90. The doctrine is that lost profits are contemplated by both parties, not just one party. The plurality takes on added significance in loan cases. *See* Larsen v. Walton Plywood Co., 65 Wash. 2d 1, 15, 390 P.2d 677, *modified on r'hng*, 65 Wash. 2d 21, 396 P.2d 879 (1964) (test cited *supra* note 56). *See also* C. MCCORMICK ON DAMAGES § 25 (1935) (lost profits may be allowed as damages if in contract cases they were within the contemplation of the parties when the contract was made).

profits were not a point of bargaining between the parties. Finally, because the May assurance was collateral to the parties' negotiations, it is doubtful that ONB anticipated being liable for lost profits based on the assurance alone.[91] Thus, it is unlikely that ONB considered lost profits in its risk equation when it made the assurance to Farm Crop.

The court's analysis in *Farm Crop* leaves much to be desired. The ambiguous "appropriate circumstances" language provides no guidance to businesspersons, litigants, or judges, and can only lead to confusion. The effect of such confusion ultimately will be to discourage a number of economically efficient transactions that otherwise would occur if an understandable measure of damages were imposed under promissory estoppel.[92] Additionally, by limiting the analysis to a finding of lost opportunity, the court ignores many of the purposes of commercial law and the inherently flexible nature of promissory estoppel.[93] In some cases, the value of the doctrine consists solely in the certainty of enforcing an otherwise unenforceable promise and presumably expectation damages would be the proper remedy.[94] However, in other cases the primary value of the doctrine is the flexibility it allows in the creation and enforcement of unorthodox commercial transactions.[95] Any test for measuring damages under promissory estoppel should be sensitive to both the need for certainty and the need for flexibility.

VII. Proposed Analysis For Measuring Damages Under Promissory Estoppel In The Future

The problem with the court's holding in *Farm Crop* lies not in the recognition that remedies should be administered

91. *See infra* notes 122-124 and accompanying text.

92. Parties are generally risk averse, even in situations of certainty, as is illustrated by the amount of negotiating that goes into today's business transactions. Uncertainty as to potential liability can only exacerbate that tendency.

93. The court specifically overlooks the interest in having the parties fully bargain before reaching an agreement, the policy of allowing the parties autonomy, and the general goal of completing the transaction in the fashion that the parties contemplated when the agreement was made.

94. For example, in a franchise case where a contract had not been formed because of a statute of frauds requirement. *See generally* Walters v. Marathon Oil Co., 642 F.2d 1098 (7th Cir. 1981).

95. *Farm Crop* is an example of this. *See supra* notes 61-70 and accompanying text.

flexibly under promissory estoppel,[96] but rather in the uncertainty created by the sweeping appropriate circumstances language. While the test for damages should allow flexibility, it should also provide guideposts that provide some certainty. The analysis should begin with the premise that if the promisee is entitled to recover under promissory estoppel, he should recover at least his expenditures made in reliance on the promise.[97] From there, criteria should be provided that distinguish promises that deserve enforcement beyond reliance from those that do not.[98] Because the action is contractual in nature, considerations similar to those underlying contract damage awards should be applied in promissory estoppel cases. Therefore, an understanding of the considerations underlying the enforcement of contracts is necessary to the development of a rational theory of damages under promissory estoppel.[99]

A number of considerations underlying contract enforcement deserve close attention when transferring the rationale of enforcing expectation damages to promissory estoppel. The bargaining process and the requirement of consideration provide the parties with a great deal of control over their agreement and provide a method by which the parties can be certain when their legal rights and obligations are fixed.[100] Thus, when parties agree to contract they are aware of the entire extent of their obligation. Another factor is the presumption that in the normal contract situation, both parties have mutually maximized the value they expect to realize from the contract through the bargaining process.[101] Therefore, awarding expectation damages provides both certainty as to performance and economic efficiency between the parties and in the market.[102]

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96. As stated before, RESTATEMENT (SECOND) OF CONTRACTS § 90, (1981) comment d recognizes this.

97. *See supra* note 10.

98. *See infra* notes 111-114 and accompanying text.

99. *See infra* notes 100-110 and accompanying text.

100. *See Into the Breach*, *supra* note 16, at 573-575.

101. A. POLINSKY, AN INTRODUCTION TO LAW AND ECONOMICS, 25 (1983) [hereinafter cited as POLINSKY] (parties would have included contract terms that maximize their joint benefits net of their joint costs assuming they bargain costlessly and cooperatively).

102. Expectation damages encourage efficiency in two ways. First, the possibility of expectation damages encourages the parties to bargain to the point where neither party could be better off under any other arrangement. Second, it discourages parties from breaching their agreements unless they can realize a higher value in the marketplace. If they can, then it is efficient to breach and pay expectation damages.

Fuller and Purdue pointed out two primary rationales for enforcing the expectation interest in contract actions in their landmark article on damages.[103] First, enforcing the expectation interest is the most effective way of curing and preventing the harms occasioned by reliance.[104] The expectancy measure is more effective than the reliance measure because it is easier to administer and more likely to fully compensate the promisee, given the difficulty of proving the individual acts and forbearances caused by reliance on the contract.[105] Second, the expectancy measure facilitates reliance on business agreements, whereas the reliance measure would discourage this because of the difficulty of proving reliance.[106] Presumably, if the reliance measure were used, fewer contracts would be entered into and there would be less willingness to act in reliance on the contracts that were made.[107]

Consolidation of all these factors reveals three considerations that underlie an award of expectation damages in a contract action. One consideration is the appropriateness of enforcing the parties' bargained agreement in the event of breach.[108] Second, because the parties have gone through a bargaining process, it is presumed that enforcement of the expectation interest will promote economic efficiency.[109] Finally, by protecting the expectation interest, people are more willing to enter contractual agreements because they know they will not have to go through the difficulty of proving reliance, and their expectations will be protected.[110]

In light of these considerations, the court should ask the following three questions when analyzing whether a promise in the context of promissory estoppel is deserving of protection beyond an award of reliance damages. First, the court should ask if the parties went through a bargaining process, with regard to the particular promise, that resulted in maximization of benefits.[111] If not, the expectation interest should

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Only when a party knows what the damages will be can a party make this decision. *See* POLINSKY, *supra* note 101, at 25.

103. Fuller, *The Reliance Interest*, *supra* note 18, at 52.

104. *Id.* at 62.

105. *Id.* at 60.

106. *Id.* at 62.

107. *Id.*

108. *See Into the Breach*, *supra* note 12, at 573-75.

109. *See supra* notes 101-102 and accompanying text.

110. *See* Fuller, *The Reliance Interest*, *supra* note 18, at 60-62.

111. The idea here is that the court should only enforce promises when the parties

probably not be protected because it is not clear that both parties maximized their value in the agreement. Second, the court should ask what the parties reasonably could have contemplated at the time the promise was made about the rights and obligations they were to incur.[112] Finally, the court should ask what effect an award of expectation damages would have on parties in similar circumstances and whether that is the result to which the parties would have agreed themselves.[113] Utilizing the above inquiries will provide a guided analysis for determining whether expectation damages should be awarded. If the parties reached the culmination of a bargaining process when the promise was made and reasonably appeared to have contemplated that they would be liable for expectation damages in the event of breach, then expectation damages should be awarded unless such an award would discourage similar transactions that otherwise would be entered into.[114]

While this analysis would require a number of factual inquiries, such inquiries are no more burdensome to jurors than asking them to determine whether a case presents appropriate circumstances for an award of lost profits with no further guidance.[115] The proposed analysis is advantageous because it provides some certainty while still allowing for the flexibility needed to give a remedy that approximates the obligation the parties anticipated when the promise was made.[116] The advantage results because the court is forced to look at the

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have gone through some degree of bargaining. Otherwise, the courts may end up enforcing promises that do not maximize the mutual benefits to the parties, and therefore would not be furthering the goal of economic efficiency. *See supra* note 101.

112. This encourages the court to go through the same cost-benefit analysis the parties did at the time they entered the contract. If the cost of entering a contract is equal to (the cost of performance times the probability of performance) plus (the cost of breach times the probability of breach), then the expected damages play a significant role in determining whether it is prudent to enter a contract. Consequently, the court should be aware of what the parties perceived as the different potential costs of the contract and on which measure of damages the parties based their decision to enter the contract. *See* A. KRONMAN & R. POSNER, THE ECONOMICS OF CONTRACT LAW 10-67.

113. This is the first part of the test proposed above. The rationale here is that the court should only enforce commercially desirable promises as it is the purpose of contract law to encourage socially desirable commercial transactions. *See supra* note 88.

114. The first clause of this sentence embodies the contractual analysis of promissory estoppel and the need for certainty, while the second clause permits the use of the inherently flexible nature of the doctrine.

115. This was the *exact* result of *Farm Crop* decision.

116. *See supra* notes 92-95 and accompanying text.

position of the parties when the promise was made and what their expectations were at that time. Thus, the damage award is more likely to approximate the obligations and rights the parties felt they had when the promise was made, as opposed to damages awarded based on the consequences of breach, as was done in *Farm Crop*.[117] This can be demonstrated by applying the proposed analysis to the Farm Crop facts. It should be kept in mind, however, that the remedy is meant to be equitable and that a finding of fault on the part of either party may be determinative of the measure of damages.[118]

Under the proposed analysis the correct measure of damages in *Farm Crop* would be the reliance interest. The parties had not gone through a bargaining process that had culminated in the making of the promise.[119] Therefore, the parties had probably not maximized the value they were receiving from the transaction. Indeed, the fact that the parties had a prior agreement that was different from the one being enforced indicates that ONB had definitely not maximized its value.[120] Therefore, enforcement of the expectation interest would not necessarily promote efficiency in the marketplace or between the parties.[121]

Another factor weighing against the award of expectation damages is that the promise was not made in a bargaining context.[122] The promise was not a logical step in the parties' negotiations, but rather was collateral to such negotiations. Consequently, the parties had much less autonomy in determining what rights and obligations were being created, and when they were fixed. In fact, ONB's liability was unknown

117. This is what the court is asserting when it says Farm Crop lost its opportunity as a result of ONB's breach. *Farm Crop*, 38 Wash. App. at 57, 685 P.2d at 1102.

118. *See* RESTATEMENT (SECOND) OF CONTRACTS § 90, (1981) *Goodman*, 169 F.2d at 685 (D.C. Cir., 1948). *See also Hoffman*, 26 Wis. 2d at 692, 133 N.W.2d at 274. If either party was not dealing in good faith it would probably be equitable to award damages based on that fact alone.

119. The parties did not bargain as to the value of the promise to each party thereby maximizing the efficient use of resources.

120. That is, ONB previously felt that a number of conditions were necessary for them to realize their desired value at the time the original agreement was negotiated. It is doubtful that the need for these conditions had dissipated between the time of the February commitment and the May assurance, particularly in light of Farm Crop's inability to fulfill the conditions. *Farm Crop*, 38 Wash. App. at 52, 685 P.2d at 1100.

121. This is because efficiency between the parties had not been achieved. *See supra* note 102.

122. The assurance was made three months after the original agreement had been negotiated. *Farm Crop*, 38 Wash. App. at 52, 685 P.2d at 1100.

until the court found the promise to be enforceable.[123] In light of this, it is unlikely that the parties seriously contemplated the full extent of their obligation at the time the promise was made. Thus, enforcement of the expectation interest would be inequitable because the parties were not clearly aware that they were incurring such an obligation when the promise was made.[124]

On the other hand, the type of transaction that occurred in *Farm Crop* is economically desirable to encourage.[125] However, expectation awards would actually discourage these transactions because of the unpredictable potential for large damage awards.[126] Conversely, reliance damages are relatively easy to ascertain and control by the promisor.[127] Therefore, lenders such as ONB would be more willing to make these types of advances under a reliance measure because they would be able to make a rational cost-benefit analysis.[128] Borrowers, having sought out the advance, presumably would be willing to accept the potentially lower damage award as a cost of receiving an "unbargained" for benefit.[129] Thus, the proposed test, unlike the *Farm Crop* analysis, would discourage only those transactions in which either the cost of reliance or the possibility of not making a loan were so high that the bank felt the costs outweighed the benefits.[130] This result would permit many more efficient transactions to occur than if the remedy were an expectation award.

Therefore, under the proposed analysis, Farm Crop's recovery should have been limited to their $175,000 reliance expenditure.[131] This result is not only fair as between the parties, but also has a limited effect of encouraging these types of transaction. Although the result would not be the same in every case, the flexibility of the proposed analysis does not necessarily mean there is no certainty to the test. The focus of the analysis is on definite factors that arise in nearly every

123. *See supra* note 100 and accompanying text.

124. *See supra* note 100 and accompanying text.

125. *See supra* notes 61-70 and accompanying text.

126. *See supra* notes 65-67 and accompanying text.

127. *See supra* notes 67-70 and accompanying text.

128. *See supra* notes 61-70 and accompanying text.

129. That is, borrowers in certain situations will be willing to forego recovery of lost profits in the event the loan is made because they anticipate that the benefits from the advance are worth the risk. *See, e.g., supra* note 101.

130. *See supra* notes 61-70 and accompanying text.

131. *See Farm Crop*, 38 Wash. App. at 52, 685 P.2d at 1100.

commercial transaction. By looking at these factors closely, business people can structure their transactions efficiently, and courts can fashion remedies that are both equitable and efficient in light of today's commercial realities. In any event, the purposes of awarding damages will be more closely served under the proposed analysis than they would be under the appropriate circumstances test, which invites the trier of fact to decide the question based on whim.

VIII. CONCLUSION

The measure of damages under promissory estoppel has created numerous problems for courts ever since the creation of the doctrine. The *Farm Crop* court is not the first to struggle with the problem, and the court's endorsement of a flexible approach indicates it is well aware of the problems of enforcing this type of promise. However, the court's proposed test is so ambiguous that it is meaningless. The court should have proposed a test that requires courts to look at the commercial realities of the situation and that would provide individuals some guidance in structuring their relationships as they see most beneficial. This Note has proposed some factors the court should take into consideration when deciding what measure of damages should be applied. The list is not intended to be exhaustive. Rather, it is intended to convey the notion that the court should focus on two things: The posture of the parties when the promise was made, and the type of behavior the decision will encourage in the future.

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