TORT THEORY AND THE RESTATEMENTS: PRESENTATION OF CATHERINE SHARKEY

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PROFESSOR CATHERINE SHARKEY:

It is a real pleasure to be here. I was quite enthused by several of the opening comments from our very first panel. Dean Darby Dickerson talked about how Southwestern Law School is at the forefront of thinking about the intersection of theoretical foundations and practical impact and how students are taught with that ethos. That resonated very strongly with me as well. Dean Byron Stier talked about the idea of theory enlightening practice. I liked hearing that. I always learn when I listen to Justice Goodwin Liu's speeches, and I learned something new today about the early Restatement project—highlighting the analytical, critical, and constructive—and particularly, its focus on legal theory. So, these inspiring words gave me enormous optimism about the role of theory in the Restatement process.

I would like to begin with a wonderful article that I hope we are going to discuss on our panel that Professors Michael Green and Nora Freeman Engstrom wrote called *Tort Theory and the Restatements: Of Immanence and Lizard Lips*.[1]

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1. *See generally* Nora Freeman Engstrom & Michael D. Green, *Tort Theory and Restatements: Of Immanence and Lizard Lips*, 14 J. TORT L. 333 (2022).

Now first I have to say it is difficult to compete with a title with such eye-catching alliteration. Personally, I would look forward to spending not only a single day, but many days at a conference talking about tort law, but I recognize I am idiosyncratic. So, to draw in the reader with a promise of "lizard lips" when you are talking about the Restatement—that's phenomenal; it is what we all want to achieve.

But on to substance. On the first page of that article, Professors Green and Engstrom say that they are going to talk about the question of what role tort theory plays in their work as Restatement Reporters. Of course, there are several esteemed Restatement reporters and other academics gathered here mainly because of their significant work and contributions. So, here we all are, poised to hear their wisdom; and then they say, our answer is virtually none. Really, that is depressing. I feel like if I were sitting here in the room as a student at Southwestern with this goal of learning how we are going to address the theoretical foundations and integrate them into practice, I would find that pretty deflating.

But then I realized—and here is the thesis of my talk—it is *intuitive* theory that is embedded in the Restatements, so I think the Restatement Reporters protest too much. It is a wonderful article, and when I read it, I say it is exactly showing how they are guided by intuitive theory—dare I say, with a nod to Professor Keith Hylton—intuitive economic or intuitive utilitarian theory and the power that it has had in the doctrine.

Why do I say this? There are two factors. In their article, Professors Green and Engstrom call them "public policy."[2] I will reframe what they deem public policy as "intuitive theory," which manifests itself in tort law and in the modern practice of tort law. I would argue that two fundamental critical factors are guiding courts today, particularly in areas where they are deciding whether to create a new tort or more realistically whether they are expanding the boundaries of a previous antiquated tort like conversion in a new era such as the Internet era.

Two fundamental factors drive the evolution of tort doctrine and practice. First, prevention of harm, or deterrence. The intuitive theory behind that is what Professor Hylton was talking about: positive economic theory. And the second is liability insurance. Here I want to take one quibble with their article. I do not think that liability insurance is "exogenous" to the tort system.[3] What we as scholars need to do more—

2. *See id.* at 345–48.

3. *Id.* at 357 ("Certain changes to the tort liability system are not the product of—or traceable to—a foundational tort principle. Rather, they stem from liability insurance availability: an *exogenous* force that influenced, and continues to influence, the fabric of tort.") (emphasis added).

judges are already doing some of this, and we need to solidify this into theory—is to figure out the incorporation of liability insurance, hitherto a "glaring gap" in most tort theory.[4] Liability insurance could fold in quite readily with this intuitive theory about deterrence and prevention of harm.

I would like to discuss three provocative cases to support my thesis. The first one is a 2019 U.S. Supreme Court case called *Air & Liquid Systems Corporation v. DeVries*.[5] That case fits the paradigm of "simple tort, perplexing problem"—simple to state, perplexing to resolve. It involves a manufacturer of what is called bare metal, a structure like a turbine, for which the manufacturer provides the bare metal. Subsequently, an asbestos-filled part made by a different manufacturer is incorporated into that bare metal structure, which then causes harm to the user. The question arises: Who should be held responsible for the duty to warn of the harm-producing features of the asbestos-laden part? Should it be the original bare-metal manufacturer or the subsequent asbestos part producer?

The U.S. Supreme Court was sharply divided. It is a six-to-three decision. But—and this is key—both the majority and the dissent use a Calabresian cheapest-cost-avoider framework to decide the issue.[6] So, it is not just an ivory tower tort theory. The majority says that the product manufacturer will often be in a better position than the parts manufacturer to warn of danger from the integrated product. The majority decides that there should be liability on the bare-metal producer on those grounds. The dissent says we should instead rely on traditional common law rules that still make the most sense today. At first, you might think the dissent takes the position of a Restatement Reporter saying, do not be carried away by Calabresian cheapest-cost-avoider tort theory; instead, let us stick with precedent and tort doctrine basics. But Justice Gorsuch in his dissent goes on to say the subsequent part manufacturer is liable for the duty to warn. Why? They are in the best position to understand and warn users about its risks. In the language of law and economics, those who make the parts are

4. Kenneth S. Abraham & Catherine M. Sharkey, *The Glaring Gap in Tort Theory*, 133 YALE L.J. (forthcoming 2024) (manuscript at 3–4) (on file with *Southwestern Law Review*) ("The glaring gap in tort theory is its failure to take adequate account of liability insurance. Although liability insurance plays a substantial role in the life cycle of tort claims, it does not feature prominently in any leading tort theory. Liability insurance . . . influences judicial decisions about whether and when there should be liability . . . .").

5. 139 S. Ct. 986 (2019).

6. *See* Catherine M. Sharkey, *Modern Tort Law: Preventing Harms, Not Recognizing Wrongs*, 134 HARV. L. REV. 1423, 1424 (2021) (reviewing JOHN C. P. GOLDBERG & BENJAMIN C. ZIPURSKY, RECOGNIZING WRONGS (2020)) ("[W]hile the [*DeVries*] majority and dissent disagreed as to which party—the bare-metal product manufacturer or the subsequent parts manufacturer—was in fact the cheapest cost avoider, they were unanimous in using the lens of law-and-economics, incentive-driven tort theory.").

generally the "least cost avoiders" of their risks.[7] The U.S. Supreme Court may be the last place you would look for tort theory, but it is our first salient data point.

The next two cases are from the California State Supreme Court, which is fitting because here we are in California. We have Justice Liu amongst us. We can talk about the U.S. Supreme Court, and some might say they do not understand tort doctrine and theory, but the Justices on the California Supreme Court have a history of understanding tort law and tort doctrine. The first case is the 2017 case called *T.H. v. Novartis Pharmaceuticals Corporation*[8] from the California Supreme Court. This is a case in which a pregnant woman has taken a generic asthma medication, which badly harms fetal development. Her children bring a lawsuit. The mother took the generic version of this medication, but by the time her children bring the lawsuit, they cannot sue the generic manufacturer. There is a complicated question of federal preemption, but the key issue is whether those plaintiffs should be able to sue the brand name manufacturer for failure to warn. If the brand name manufacturer had incorporated the warning, the generics would have automatically had to do so because generics must follow the warnings of the brand name manufacturers. In this decision, the California Supreme Court says if the policy of preventing harm has special relevance to any particular endeavor, surely prescription labeling is the place. So, they are really driven by prevention of harm in that decision and their holding to extend liability into that situation.

What else is on their mind? Insurability. They say there is no reason why the brand name manufacturer would be unable to insure against the risk of warning liability.[9]

The third and final case is a 2019 California State Supreme Court case, *Southern California Gas*.[10] Southern California Gas (SoCalGas) had an

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7. *DeVries*, 139 S. Ct. at 997 (Gorsuch, J., dissenting) (stating that "[t]he manufacturer of a product is in the best position to understand and warn users about its risks; in the language of law and economics, those who make products are generally the least-cost avoiders of their risks," and emphasizing that "[b]y contrast, we dilute the incentive of a manufacturer to warn about the dangers of its products when we require other people to share the duty to warn and its corresponding costs" (citing STEVEN SHAVELL, ECONOMIC ANALYSIS OF ACCIDENT LAW 17 (1987); GUIDO CALABRESI, THE COSTS OF ACCIDENTS 135 & n.1 (1970); Italia Societa per Azioni di Navigazione v. Oregon Stevedoring Co., 376 U.S. 315, 324 (1964)).

8. 407 P.3d 18 (Cal. 2017).

9. *Id.* at 45 (noting that "Novartis identifies no reason why it could not insure against the effects of any negligence related to the warning label for its drug" and "[c]ommercial general liability insurance policies cover injuries that accrue from multiple occurrences over a period of years, and tail coverage is available for injuries caused by the insured that did not manifest themselves until well after the manufacturer either sold the product or shut down its operations" (citations omitted)).

underground storage tank that leaked and residents from Porter Ranch, which I take it is not that far from here, had to be evacuated. There were claims for personal injuries and property damage but there were also a lot of claims for business or purely financial losses. The businesses that were in this area where everyone had been evacuated lost their customer traffic, lost lots of money as a result, and brought a lawsuit. The case raises what is known in tort law as the economic loss rule, addressing when people should be able to recover their purely financial losses when they have not suffered physical injury or property damage. Interestingly, in this case, the California Supreme Court decides not to allow for recovery. The Court affirms the application of the economic loss rule, striking a balance between the risk of under-deterrence (*i.e.*, "exposure to liability often provides an important incentive for parties to internalize the social costs of their actions") and the risk of over-deterrence (*i.e.*, "resulting universe of potential claims . . . might deter socially beneficial behavior").[11]

So, the first point is just to suggest that this is a powerful paradigm. I agree with Professor Hylton that Richard Posner and Guido Calabresi deserve much credit for originating the theory. But the deterrence paradigm goes well beyond them and their judicial decisions. It has now reached the U.S. Supreme Court, and it has infiltrated the most prestigious state supreme courts. It is a powerful intuitive theoretical paradigm.

The economic loss rule illustrates the convergence of the prevention of harm rationale and the role of liability insurance because one of the most powerful arguments for why courts should not grant recovery for purely financial losses is that the victims themselves should have an incentive to get first-party insurance. So, for example, businesses should get business-interruption insurance. Businesses should be encouraged to do so because they will encounter disruptions in their commerce even in the absence of any negligent conduct by others, so it would be economically sound to incentivize them in certain areas to get their own first-party insurance. If you read very carefully, in *Southern California Gas*, the Court itself comes out and says that by denying recovery in this case for negligently inflicted purely economic losses, it will increase the incentive to buy insurance for the businesses operating near the natural gas facility, or more generally, thinking ahead to future cases, businesses operating near "a dam, shipping lane, oil well, and so forth."[12]

Now, here is the rub, and what is so interesting: One might be persuaded that this is an incredibly powerful paradigm or framework for

10. 441 P.3d 881 (2019).
11. *Id.* at 888.
12. *Id.* at 895.

courts to use, but it does not necessarily point to who wins in a particular dispute. Recall the U.S. Supreme Court *DeVries* case. Both the majority and the dissent use the same framework, and they come to the opposite conclusion of which entity is the cheapest cost avoider and should have given the warning. In *Southern California Gas*, there is a really interesting question about whether the particular type of insurance would or would not have been available for the businesses in the first instance. The trial court judge, whose decision to impose a duty on SoCalGas to prevent the businesses' economic losses was overturned by the California Supreme Court, talked about how the kind of risks that the businesses were being exposed to were not ordinary business interruption ones. Therefore, according to the trial judge, it made sense to impose liability on SoCalGas, which could insure for this kind of risk.[13]

So, it is not necessarily going to get clear answers. That said, I not only think it is a powerful intuitive theoretical paradigm, but it has reached a kind of ascendancy in the courts. To return to the *Lizard Lips* article, when the Reporters talk aloud about the public-policy-inflected principles like prevention of harm and insurance, I see these factors as intuitive theory working itself out in tort law.

The challenge, then, is to figure out how to help judges motivated by intuitive theory. When judges use that kind of framework, there are underlying empirical metrics that might help them to decide. I have done a deep dive looking at a lot of different cases in which courts talk about prevention of harm and talk about the role of insurance, but oftentimes they resort—because the parties have not served them up the necessary materials—to doing a kind of armchair empiricism. Sometimes they get it right, and sometimes they get it wrong regarding whether a particular risk is today insurable or not. It would be helpful for the parties to submit evidence on this question. I think the framework is very sound. It leads to contestable empirical propositions, and parties can help judges by presenting some record evidence to resolve those contestable junctures. Thank you very much.

13. *In re* Coordination Proceedings Special Title (Rule 3.550) S. Calif. Gas Leak Cases, No. JCCP4861, 2017 WL 2361919, at *3–5 (Super. Ct. L.A. Cnty. May 8, 2017).