COMMENTS

The Demise of the Integrity of Oral Contracts and Promises in Lender-Borrower Relationships Under California Law

The comment that follows addresses recent developments in California law pertaining to oral contracts and promises between lenders and borrowers. The author analyzes the current legal status of oral agreements, the current legal relationship between lenders and borrowers, and the consequences thereof to those involved in disputes over oral financing agreements. The need for this comment arises from the emergence of a judicial and legislative "attitude" of disfavor toward enforcement of oral contracts, and from the confused and erroneous legal positions taken by both sides in lender liability litigation. These occurrences are especially noteworthy (and probably not coincidentally so) in litigation between parties to agricultural financing agreements. Finally, what follows is not without some sociological significance: The comment suggests that the judiciary and the legislature have combined to institutionalize the previously-informal belief that a borrower should place no trust in the word of the lender.

INTRODUCTION

If farmers[1] ever believed that a man's word was his bond, and that farm business was best done with a smile and a handshake, the validity of such beliefs has been severely shaken by recent developments in the law relating to oral contracts[2] and promises. This ominous and insightful development of human nature[3] nowhere manifests itself more

[1] "Farmer" refers herein to anyone who borrows money for agricultural purposes.

[2] Contracts may be partly written and partly oral. Griffith v. Bucknam, 81 Cal. App. 2d 454, 458, 184 P.2d 179, 182 (1946). As used herein, the terms "oral contract" and "oral agreement" refer to any part of an agreement which is not in writing.

[3] "Law and institutions must go hand-in-hand with the progress of the human

obviously than in the relationship between lenders[4] and farmers. Prospects of enforcing oral promises to lend money have reached an all time low. This comment focuses on the major problems of enforcing oral financing agreements[5] between lenders and farmers.

Lawsuits over oral financing agreements comprise a substantial share of the lender liability[6] cases. These include suits over alleged agreements to lend money for the purchase of land,[7] the purchase of livestock,[8] and to make long-term loans to replace shorter-term loans.[9] Promises to renew short-term credit indefinitely and/or to provide long-term loans on an as needed basis,[10] not to call in a note when due,[11] not to foreclose during workout[12] proceedings,[13] or if the bor-

mind." Thomas Jefferson, letter to Samuel Kercheval, July 12, 1816. J. CONLAN, QUOTATIONS IN AMERICAN HISTORY 160 (Morrow 1984).

[4] "Lender" refers herein to anyone in the business of lending money for agricultural purposes, and their agents.

[5] "Contract" and "agreement" are used interchangeably herein, within the meaning of CAL. CIV. CODE § 1549 (West 1982): "A contract is an agreement to do or not to do a certain thing."

[6] "Lender liability" is the generic term for a body of law wherein a borrower sues the lender for any type of wrongful conduct arising out of the lending relationship. The seminal case of State Nat'l Bank of El Paso v. Farah Mfg. Co., Inc., 678 S.W.2d 661 (Tex. Ct. App. 1984), where the bank slowly took over the borrower's business to the detriment of the borrower and benefit of the bank, is an example of a lender liability case not based on oral contract issues.

[7] Landes Const. Co. Inc. v. Royal Bank of Canada, 833 F.2d 1365 (9th Cir. 1987) All Ninth Circuit cases cited in this comment are based on California law.

[8] Delzer v. United Bank of Bismarck, 459 N.W.2d 752 (N.D. 1990).

[9] Kruse v. Bank of America, 202 Cal. App. 3d 38, 248 Cal. Rptr. 217 (1988), *cert. denied*, Duck v. Bank of America, 488 U.S. 1043 (1989); Mitsui Mfrs. Bank v. Superior Court, 212 Cal. App. 3d 726, 260 Cal. Rptr. 793 (1989). Lenders structure loan duration terms according to the perceived availability of funds to lend. Hence, for example, at the beginning of the 1980's, commercial banks usually preferred to make short-term loans (less than 5 years) because their lendable funds were in deposit accounts subject to immediate withdrawal. G. GRAHAM & C. SCOTT, CALIFORNIA REAL PROPERTY SALES TRANSACTIONS § 6.4, at 421 (California Continuing Education of the Bar, 1981). Life insurance companies derived their flow of funds from a more predictable source, and thus were more interested in making long-term loans (up to 30 years) secured by real property. *Id.* § 6.7, at 425.

[10] *Mitsui*, 212 Cal. App. 3d 726, 260 Cal. Rptr. 793.

[11] Centerre Bank of Kansas City v. Distributors, 705 S.W.2d 42 (Mo. App. 1985); Braten v. Bankers Trust Co., 468 N.Y.S.2d 861, 456 N.E.2d 802 (1983).

[12] "Workout" refers to negotiations to restructure a delinquent loan to avoid a default.

[13] Karlsen v. American Sav. & Loan Ass'n, 15 Cal. App. 3d 112, 92 Cal. Rptr. 851 (1971).

rower found a willing and able buyer,[14] or simply to restructure the debt[15] are common. Lenders have also promised that a guarantor would be released from liability,[16] that loan approval was merely a formality,[17] that a lender's usually-lenient collection policy would continue,[18] to obtain insurance for the borrower,[19] and to lend at a certain rate.[20]

This comment seeks to provide guidance to both laymen and lawyers with respect to enforcement of oral promises similar to those referenced above.[21] It focuses on recent developments in California law, and their effect on established law pertaining to oral promises to lend money. A few recent cases from other states are discussed from a comparative perspective, such that a general overview of the state and direction of the law is also presented.[22] The initial discussion centers around the current legal relationship between lenders and borrowers, and the consequences of this status to the bargaining and litigation processes. Developments in the area of contractual certainty, the statute of frauds, fraud, and the parol evidence rule are then examined.[23] The goal of this comment is to provide useful information about the current status of the law pertaining to oral contracts and promises. The thesis of this comment is that farmers throughout the United States must "get it in writing," or proceed at their own peril.

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[14] Raedeke v. Gibraltar Sav. & Loan Ass'n, 10 Cal. 3d 665, 517 P.2d 1157, 111 Cal. Rptr. 693 (1974).

[15] Price v. Wells Fargo Bank, 213 Cal. App. 3d 465, 261 Cal. Rptr. 735 (1989); Champaign Nat'l Bank v. Landers Seed Co., 165 Ill. App. 3d 1090, 519 N.E.2d 957 (1988), *cert. denied*, 489 U.S. 1019 (1989).

[16] P. E. Calder v. Camp Grove State Bank, 892 F.2d 629 (7th Cir. 1990).

[17] Runnemeade Owners Inc. v. Crest Mortgage Corp., 861 F.2d 1053 (7th Cir. 1988).

[18] United States v. Grayson, 879 F.2d 620 (9th Cir. 1989).

[19] Goehring v. Stockton Morris Plan Co., 93 Cal. App. 2d 417, 209 P.2d 41 (1949); Graddon v. Knight, 138 Cal. App. 2d 577, 292 P.2d 632 (1956).

[20] *Price*, 213 Cal. App. 3d 465, 261 Cal. Rptr. 735.

[21] This comment emphasizes suits by borrowers against lenders for breach of oral agreements to lend money (and affirmative defenses to collection actions). But the same principles may apply to suits by lenders against borrowers for breach of an agreement to borrow. *See* Teachers Ins. & Annuity Ass'n v. Butler, 626 F. Supp. 1229 (S.D.N.Y. 1986).

[22] The law discussed herein is of particular concern to farmers because of the continuous fluctuation of the farm economy, the unique financing needs of farmers, state and federal government policies, and the fact that a substantial number of lender liability suits have arisen in an agricultural context. With few exceptions, the law discussed herein is relevant to all lender-borrower relationships.

[23] The cases discussed herein constitute a representative sample. They are not intended to be a definitive statement of a particular area of the law.

I. A Brief Overview of the Lender-Borrower Relationship

In the mid 1980's, various developments in the law gave rise to the belief that a lender had or may have legal obligations to the borrower which required the lender to place the borrower's interests and needs above those of the lender. In some instances, it was further perceived that the lender was obligated to prevent or solve the borrower's financial problems, even where those problems were self-caused or fell outside the scope of the contractual relationship between the parties. Accordingly, borrowers and the legal community drew the conclusion that borrowers needed special protection from the courts when the lender failed to meet these perceived fiduciary responsibilities. Although there was little or no law upon which to base such conclusions, there was even less to refute them.

This belief that the lender's relationship to its borrower was fiduciary in nature generated the corresponding belief that a lender's breach of the implied covenant of good faith and fair dealing would be deemed tortious by the courts. This, in turn, generated a substantial quantity of litigation against lenders for a wide range of conduct, some of which amounted merely to enforcement of the express terms of the loan contracts between the parties. Sympathetic juries punished lenders by granting huge monetary damage awards to borrowers. But when the appellate courts commenced consideration of whether the relationship between a lender and a commercial borrower was or should be a fiduciary relationship, everything changed. Today, the lender need not subordinate its interests to those of the borrower, and the borrower is not entitled to special protection from the legal system.

California courts currently view the lender-borrower transaction as merely another arms-length commercial transaction. When a lender acts in bad faith toward its borrower with respect to the loan contract between them, the lender has breached the contract, but nothing else. This recently clarified rule severely limits the type and amount of monetary damages that the borrower may recover from the lender. Hence, a lender's motive to be cautious regarding its representations to borrowers in loan negotiations has been sharply curtailed, as has the lender's motive to settle, rather than litigate. This and the competitive nature of the lending industry[24] may lead to borrowers hearing lenders promise "something more" than they can actually deliver. The events giving rise to this state of affairs are discussed below.

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[24] *See* Copesky v. Superior Court, 229 Cal. App. 3d 678, 691, 280 Cal. Rptr. 338, 346 (1991).

A. *The Implied Covenant of Good Faith and Fair Dealing*

Every contract to lend money carries with it an "implied covenant of good faith and fair dealing."[25]

> "Simply stated, the burden imposed is that neither party will do anything which will injure the right of the other party to receive the benefit of the agreement. . . . Or, to put it another way, the implied covenant imposes upon each party the obligation to do everything that the contract presupposes they will do to accomplish its purpose."[26]

Breach of the implied good faith covenant in a lending contract occurs when a party to the contract consciously and deliberately fails or refuses to perform his express or implied-by-law contractual duties, thereby depriving the other party of the reasonably-expected benefits of the agreement.[27] For example, a lender who agrees to lend, accepts a large loan fee, and then imposes an additional condition on the borrower, such as a substantial prepayment penalty, has breached the implied covenant of good faith and fair dealing.[28]

California courts had decided that breach of this implied covenant could be considered tortious[29] in the insurance[30] and employment[31] contract contexts only. In 1984, the California Supreme Court cautiously "invited" lower courts to find a tortious breach of the implied covenant in other commercial transactions,[32] as long as the relationship between the contracting parties was a "special relationship." Such a relationship

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[25] Wagner v. Benson, 101 Cal. App. 3d 27, 33, 161 Cal. Rptr. 516, 520 (1980); Careau & Co. v. Security Pac. Business Credit Inc., 222 Cal. App. 3d 1371, 1393, 272 Cal. Rptr. 387, 398 (1990).

[26] *Careau*, 222 Cal. App. 3d at 1393, 272 Cal. Rptr. at 398.

[27] *Id.* at 1395, 272 Cal. Rptr. at 399-400. Such conduct need not always constitute the breach of an express term of the contract.

[28] 999 v. C.I.T. Corp., 776 F.2d 866, 868-70 (9th Cir. 1985). *See also*, notes 45, 46, 55, 56 and 57, and the accompanying text, for other examples of breach of the implied covenant by a lender.

[29] "Tortious" conduct (a tort) generally refers to wrongful and injurious conduct which is actionable at law, but which is something different, and more culpable, than a breach of contract. The significance of whether breach of the implied covenant is deemed tortious, or merely contractual, lies in the measure of damages that may be awarded to redress such conduct.

[30] Comunale v. Traders & Gen. Ins. Co., 50 Cal. 2d 654, 663, 328 P.2d 198, 203 (1958); Gruenberg v. Aetna Ins. Co., 9 Cal. 3d 566, 575, 510 P.2d 1032, 1038, 108 Cal. Rptr. 480, 487 (1973).

[31] Cleary v. American Airlines, Inc., 111 Cal. App. 3d 443, 454-56, 168 Cal. Rptr. 722, 728-29 (1980), *disapproved by* Foley v. Interactive Data Corp., 47 Cal. 3d 654, 765 P.2d 373, 254 Cal. Rptr. 211 (1988).

[32] Seaman's Direct Buying Servs., Inc. v. Standard Oil Inc., 36 Cal. 3d 752, 768-69, 686 P.2d 1158, 1166-67, 206 Cal. Rptr. 354, 362-63 (1984).

would be characterized by elements of public interest, adhesion and fiduciary responsibility,[33] the same elements impliedly present in an insurance contract.[34] The special relationship doctrine focuses on the control that an insurance company has over the insured party, and the corresponding need for special protection, in the form of both a remedy and a deterrent, against breach of the implied covenant of good faith by the insurance company. Hence, if the courts concluded that a commercial lending agreement created a special (or "fiduciary") relationship, and that the borrower was hence in need of special protection against the lender's potential bad faith breach of their agreement, a lender's breach of the implied covenant could be tortious.

Both the courts and commentators predicted a continuous expansion of the "bad faith tort."[35] In *Commercial Cotton Co. v. United California Bank*,[36] an appellate court imposed tort liability for bad faith breach by a bank toward its depositor. This 1985 decision found such a relationship to be "special." The bank thus owed a "quasi-fiduciary"

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[33] *Id.* These elements were expanded on in Wallis v. Superior Court, 160 Cal. App. 3d 1109, 1118, 207 Cal. Rptr. 123, 129 (1984), *criticized in* Careau & Co. v. Security Pac. Business Credit, Inc., 222 Cal. App. 3d 1371, 272 Cal. Rptr. 387 (1990), as follows:

> "For purposes of serving as predicates of 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; and (5) the other party is aware of this vulnerability."

[34] Egan v. Mutual of Omaha, 24 Cal. 3d 809, 820, 598 P.2d 452, 457, 157 Cal. Rptr. 482, 487 (1979), *cert. denied*, 445 U.S. 912 (1980).

[35] White v. Western Title Ins. Co., 40 Cal. 3d 870, 900, 710 P.2d 309, 327, 221 Cal. Rptr. 509, 527 (1985) (Kaus, J., concurring and dissenting) (Justice Kaus wrote: "[T]here is tremendous pressure on the courts, particularly this court, to extend bad faith liability to other contractual relationships" [other than the insurance relationship]). *See also*, E. Wright, Symposium, *The Future of Tort Litigation in California; Part II: Bad Faith and Punitive Damages*, 29 SANTA CLARA L. REV. 545, 546 (1989).

[36] 163 Cal. App. 3d 511, 515-16, 209 Cal. Rptr. 551, 553-54 (1985), *overruled sub silentio in* Foley v. Interactive Data Corp., 47 Cal. 3d 654, 765 P.2d 373, 254 Cal. Rptr. 211 (1988), and *dissapproved in* Copesky v. Superior Court, 229 Cal. App. 3d 678, 280 Cal. Rptr. 338 (1991).

duty[37] to its depositor, and breached it by setting forth an unjustified excuse for not acting fairly. *Commercial Cotton Co.* was repeatedly cited without criticism,[38] while the courts simultaneously refused to extend the bad faith breach tort to other commercial relationships.[39] *Commercial Cotton Co.* was then followed in *Barrett v. Bank of America*: The same appellate court found that a fiduciary relationship could exist between a lender and a borrower under certain circumstances, one of the few California decisions to that effect.[40]

In *Barrett*, the borrower trusted and relied on the lender, and thus shared confidential information with the loan officer, who, in turn, gave financial advice to the borrower, even though the lender had a personal stake in the borrower's action on that advice. The borrower relied on this advice. This created a fiduciary relationship, which obligated the lender not to use that information to its advantage or to the detriment of the borrower.[41]

As the court noted in *Copesky v. Superior Court*,[42] the existence of a fiduciary relationship in lender-borrower/depositor transactions appeared to have a healthy future after *Barrett*. However, the grounds for such a belief were eliminated in *Foley v. Interactive Data*.[43] *Foley* did not reference lending transactions; but the California Supreme Court was "not convinced that a 'special relationship' analogous to that between insurer and insured" existed outside of the insurance context.[44]

Relying on *Foley*, the courts have since consistently held that breach

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[37] A fiduciary relationship in law is ordinarily synonymous with a "confidential relation." It is founded upon the trust or confidence reposed by one person in the integrity and fidelity of another, and likewise precludes the idea of profit or advantage resulting from the dealings of the parties and the person in whom the confidence is reposed. Rickel v. Schwinn Bicycle Co., 144 Cal. App. 3d 648, 654, 192 Cal. Rptr. 732, 735 (1983).

[38] *See* Copesky v. Superior Court, 229 Cal. App. 3d 678, 688, 280 Cal. Rptr. 338, 344 (1991), and cases cited therein. The court noted, however, that two student-written Law Review comments had found fault with *Commercial Cotton Co.*

[39] *Id.* at 687, 688, 280 Cal. Rptr. at 344.

[40] Barrett v. Bank of America, 183 Cal. App. 3d 1362, 1369-70, 229 Cal. Rptr. 16, 20-21 (1986); *See also*, Rutherford v. Rideout Bank, 11 Cal. 2d 479, 486, 80 P.2d 978, 982 (1938); Bank of America v. Sanchez, 3 Cal. App. 2d 238, 242-43, 38 P.2d 787, 789-90 (1935).

[41] 183 Cal. App. 3d at 1369, 229 Cal. Rptr. at 20-21.

[42] 229 Cal. App. 3d 678, 688, 280 Cal. Rptr. 338, 344 (1991).

[43] 47 Cal. 3d 654, 765 P.2d 373, 254 Cal. Rptr. 211 (1988) (a wrongful discharge from employment case, where only two of the seven justices remained from the Supreme Court which decided *Seaman's Direct Buying Servs., Inc. v. Standard Oil, Inc.*, 36 Cal. 3d 752, 686 P.2d 1158, 206 Cal. Rptr. 354 (1984)).

[44] 47 Cal. 3d at 692, 765 P.2d at 395, 254 Cal. Rptr. at 234.

of the implied covenant in the lender-borrower relationship is not tortious, but merely contractual. In *Mitsui Manufacturers Bank v. Superior Court*,[45] the borrowers alleged that the bank tortiously breached the implied covenant of good faith and fair dealing. The bank allegedly reneged on an oral promise to renew short-term credit until the borrowers obtained long-term financing elsewhere.[46] Following *Foley*, the *Mitsui* court examined the nature of the lending relationship between the parties, found it lacking in the characteristics of an insured-insurer relationship, and thus concluded that nothing more than a standard arms-length commercial contract existed.[47] The court said:

> "It is the nature of the contract that is critical, whether it reflects unequal bargaining strength between the parties, an inadequacy of ordinary contract damages or other remedies, adhesiveness of contract provisions adversely impacting the damaged party which are either neutral toward or benefit the other, public concerns that parties to certain types of contracts conduct themselves in a particular manner, the reasonable expectations of the parties or a fiduciary relationship in which the financial dependence or personal security by the damaged party has been entrusted to the other. There are undoubtedly other significant factors and it may be that not all must be present in every case which might give rise to tort damages. Real parties have cited us to no fact of this transaction which takes it out of the ordinary commercial context."[48]

The court found the bank's conduct, although possibly a breach of contract, not to be tortious.[49]

The lack of a special relationship was again missing in *Careau & Co. v. Security Pacific Business Credit, Inc.*[50] Following *Wallis*, *Foley*, and *Mitsui*, the *Careau* court found plaintiffs' attempt to obtain financing from a bank for the purchase of the "Egg City" egg production facility to be a "rather common commercial banking transaction."[51]

The plaintiffs' profit motive in entering into the transaction, the

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[45] 212 Cal. App. 3d 726, 260 Cal. Rptr. 793 (1989).

[46] *Id.* at 728-29, 260 Cal. Rptr. at 794-95. The bank also allegedly promised that it would make a long-term loan if the borrowers could not obtain satisfactory financing from another lender. Plaintiffs also claimed the bank's failure to provide long-term financing without a blanket deed of trust on all plaintiffs' real property was in bad faith.

[47] *Id.* at 730-32, 260 Cal. Rptr. at 795-97. The court found no commercial uniqueness or unfairness in the bank's oral promise to provide short-term credit if plaintiffs placed their banking accounts with Mitsui and borrowed from Mitsui for other purposes.

[48] *Id.* at 731, 260 Cal. Rptr. at 796.

[49] *Id.* at 730, 260 Cal. Rptr. at 795.

[50] 222 Cal. App. 3d 1371, 272 Cal. Rptr. 387 (1990).

[51] *Id.* at 1400, 272 Cal. Rptr. at 403.

arms-length negotiations between parties of roughly equal bargaining power, the lack of an adhesive agreement[52] or vulnerability on the part of either party, and a corresponding absence of a need for special protection convinced the court that no special relationship existed: "[T]here is neither authority nor reason for according such characterization to the relationship between a bank and a commercial borrower."[53] The court found that since no special relationship existed, no tortious breach of the implied covenant of good faith and fair dealing could possibly have occurred.[54]

Finally, in *Price v. Wells Fargo Bank*,[55] the borrower claimed the bank tortiously breached the implied covenant of good faith by taking a "hard line" in repayment negotiations: "[T]he bank owed (and breached) a reasonable duty of forbearance in enforcing its creditor's remedies,"[56] which forced them to sell beehives, cattle, grazing land, and farm equipment at distressed prices.[57] The borrowers failed to allege factors giving rise to a special relationship. Rather, they simply claimed that because they had bank accounts and loans with Wells Fargo, a fiduciary relationship existed sufficient to establish tort liability.[58] Their claim was dismissed.

In sum, the courts have concluded that because a typical commercial borrower is not vulnerable to a lender in the same manner that an insured is vulnerable to an insurer, the lender should not ordinarily be burdened with fiduciary responsibility toward its borrower, as the borrower is not in need of or entitled to special protection from the law. Therefore, the lender's breach of the implied covenant of good faith and fair dealing will not amount to tortious conduct.

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[52] An "adhesive" contract typically signifies a standardized contract, drafted by the party with superior bargaining power, which relegates to the weaker party only the opportunity to accept or reject the contract. Perdue v. Crocker Nat'l Bank, 38 Cal. 3d 913, 925, 702 P.2d 503, 511, 216 Cal. Rptr. 345, 353 (1985), *appeal dismissed*, 475 U.S. 1001 (1986).

[53] *Careau*, 222 Cal. App. 3d at 1400, 272 Cal. Rptr. at 404. The question remains open as to whether a small farmer might not be a commercial borrower.

[54] *Id.* at 1400-01, 272 Cal. Rptr. at 404.

[55] 213 Cal. App. 3d 465, 261 Cal. Rptr. 735 (1989).

[56] *Id.* at 479, 261 Cal. Rptr. at 742.

[57] *Id.* at 474, 261 Cal. Rptr. at 738.

[58] *Id.* at 478, 261 Cal. Rptr. at 741.

B. *The Difference in Remedies for Tortious and Contractual Bad Faith Breach is Substantial*

The significance of *Mitsui, Careau* and *Price* is that a lender's breach of the implied covenant, if not tortious, is merely a breach of contract.[59] The damages available for breach of contract are much more limited than for tortious breach of the implied covenant.

A farmer injured by a breach of contract or by a tortious bad faith breach may recover damages in an amount which will compensate him for all harm actually and legally caused by the defendant's wrongful acts.[60] But a farmer attempting to recover for breach of contract must also prove that the resulting injuries were reasonably foreseeable by both parties at the time the contract was made; no such requirement exists for tortious conduct.[61]

A farmer's failure to obtain a loan, which he expected as a result of an agreement with his lender, may adversely affect his ability to repay other loans, to obtain additional financing, to keep the farm going, and to make a profit. It could destroy the farm. But the parties may not have anticipated and/or not discussed these consequences during negotiations. The farmer might not mention all the consequences of not obtaining the loan (for fear of scaring the lender into perceiving that the farmer is in a precarious financial position). Similarly, the forces giving rise to such events may be unknowable at the time of contracting. If so, recovery for these losses will not be allowed where the lender's acts are not deemed tortious.

Even where the consequences are foreseeable, recovery is difficult. For example, an expectation of profit is typically foreseeable with a

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[59] Contractual breach of the implied covenant is simply a breach of contract. Price v. Wells Fargo Bank, 213 Cal. App. 3d at 478-79, 261 Cal. Rptr. at 741-42; 999 v. C.I.T. Corp., 776 F.2d 866, 870 (9th Cir. 1985); Mitsui Mfrs. Bank v. Superior Court, 212 Cal. App. 3d 726, 729, 260 Cal. Rptr. 793, 795 (1989) (After finding alleged bad faith breach not tortious, the court concluded that a contractual bad faith cause of action would be superfluous because that claim was already alleged as an affirmative defense); Careau & Co. v. Security Pac. Business Credit, Inc., 222 Cal. App. 3d 1371, 1392, 1395, 1401, 272 Cal. Rptr. 387, 397, 398, 400, 404 (1990) (dismissing non-tortious claim without leave to amend where borrower alleged nothing more than a duplicative claim for contract damages, because the grounds giving rise to the bad faith breach amounted to the same conduct as breach of bargained-for contract term).

[60] CAL. CIV. CODE §§ 3300, 3333 (West 1991).

[61] Mendoyoma Inc. v. City of Mendocino, 8 Cal. App. 3d 873, 879-80, 87 Cal. Rptr. 740, 744 (1970) (citing Hadley v. Baxendale, 9 Ex. 341, 156 Eng. Rep. 145); CAL. CIV. CODE § 3333 (West 1991).

commercial farm loan. The problem lies in predicting the amount of that profit, especially if the contemplated venture does not have an established business history. The likelihood and amount of such potential profit must be established with reasonable certainty: The courts will not place the injured party in a better position than he would be in had the lender performed.[62]

Because farm income is historically volatile, a trustworthy degree of certainty as to the amount of lost profits may be difficult to establish. Projections of future profits require speculation as to various factors which can affect farm profits.[63] These factors are further complicated because the profit to be derived as a direct consequence of a particular loan will not be realized for many years. The difficulty of projecting such a stream of income could create judicial reluctance to allow recovery of lost profits.[64] Further, injured borrowers are required to mitigate their damages by obtaining alternative financing, if available. If they do so, then their damages consist merely of the cost of obtaining the new loan, e.g., an increase in the interest rate,[65] and the consequences of delay, if any.

Noneconomic losses are also nonrecoverable in breach of contract actions. The emotional consequences of financial distress are obvious, and the failure to obtain expected financing that may save the farm can be devastating.[66] Although damages for emotional distress may be recovered for tortious conduct,[67] they are unavailable for breach of contract.[68]

Most importantly, a mere breach of contract will not give rise to an award of punitive damages. But such damages may be assessed for tor-

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[62] CAL. CIV. CODE § 3301 (West 1990); Fisher v. Hampton, 44 Cal. App. 3d 741, 747, 752, 118 Cal. Rptr. 811, 814, 817 (1975).

[63] Landes Const. Co. Inc. v. Royal Bank of Canada, 833 F.2d 1365, 1373 (9th Cir. 1987). These factors might include future crop prices, interest rates, market conditions, inflation, taxes, weather conditions, and numerous other factors, including all costs and expenses.

[64] *See generally*, *Landes*, 833 F.2d at 1373 (where an award of damages for lost profits was affirmed), and cases cited therein; *Fisher*, 44 Cal. App. 3d 741, 118 Cal. Rptr. 811.

[65] *See Price*, 213 Cal. App. 3d at 483, 261 Cal. Rptr. at 745.

[66] *Id.* at 474, 261 Cal. Rptr. at 738; *Kruse*, 202 Cal. App. 3d at 44-51, 248 Cal. Rptr. at 219-24.

[67] *See generally*, Jarchow v. Transamerica Title Ins. Co., 48 Cal. App. 3d 917, 932-38, 122 Cal. Rptr. 470, 481-85 (1975).

[68] Sawyer v. Bank of America, 83 Cal. App. 3d 135, 139, 145 Cal. Rptr. 623, 625 (1978).

tious acts, if such conduct was malicious, fraudulent, or oppressive.[69] Punitive damages punish wrongful conduct, serve to deter actual and potential defendants from repeating such conduct, are calculated based on the defendants' financial worth, the harm caused, and the degree of culpability involved, and are frequently substantial.[70] Punitive damages are what lenders fear most. The possibility of such damages ostensibly deters lenders from promising more than they can deliver, and from acting unfairly toward the borrower. They also increase the probability that settlement, rather than protracted litigation, will occur.

Consequently, the fact that a lender's conduct in breaching an agreement to lend money will not be deemed tortious provides lenders with a strong negotiating posture, both before and after a problem develops. Borrowers must proceed at their own risk, and take every possible step to protect themselves.

C. *The Tort of Bad Faith Denial of Contract is Also of Little Avail to Borrowers Seeking to Enforce an Oral Contract*

In 1984, the California Supreme Court created a new tort called "bad faith denial of contract." A party to a contract may incur tort remedies when, in addition to breaching a valid contract, it seeks to avoid liability by denying the contract's existence in bad faith and without probable cause.[71] Borrowers frequently allege bad faith denial of contract when suing lenders.[72] But recent judicial clarification of the

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[69] *Id.* at 139, 145 Cal. Rptr. at 626. *Price*, 213 Cal. App. 3d at 475, 261 Cal. Rptr. at 739; CAL. CIV. CODE § 3294 (West 1991).

[70] Downey Savings & Loan Ass'n v. Ohio Casualty Ins. Co., 189 Cal. App. 3d 1072, 1096-98, 234 Cal. Rptr. 835, 848-50 (1987); In cases involving agricultural borrowers, California juries have had little difficulty understanding that an award of punitive damages must be large enough to actually punish and deter the financial institution in question. Kruse v. Bank of America, 202 Cal. App. 3d 38, 44, 248 Cal. Rptr. 217, 219 (1988), *cert. denied*, Duck v. Bank of America, 488 U.S. 1043 (1989) (Jury award of $26,675,000 in punitive damages, reduced to $6 million by trial judge); Conlan v. Wells Fargo Bank, No. 82852 (Cal., Monterey Cty. Super. Ct. June 10, 1987) ($50 million punitive damages award by jury, reduced to $25 million by trial judge). Stanghellini Ranches, Inc. v. Bank of America, No. 35448 (Cal., Sutter Cty. Super. Ct. June 19, 1987) ($30 million punitive damages award by jury) *rev.d*, No. 3 Civil C003244 (Cal. Ct. App. Nov. 9, 1989, modified Dec. 1, 1989).

[71] Seaman's Direct Buying Servs., Inc. v. Standard Oil, 36 Cal. 3d 752, 769, 686 P.2d 1158, 1167, 206 Cal. Rptr. 354, 363 (1984).

[72] *See, e.g.*, *Kruse*, 202 Cal. App. 3d at 57, 248 Cal. Rptr. at 228. One reason for the tort's popularity is its complete lack of definition, thus allowing for plenty of creativity. *Okun v. Morton*, 203 Cal. App. 3d 805, 823-25, 250 Cal. Rptr. 220, 231-33 (1988) concludes the new tort is merely a species of breach of the implied covenant of

nature and scope of this tort remedy suggests it will also be of little or no assistance in oral contract cases against lenders.

A claim of bad faith denial of contract is similar to an action for malicious prosecution of a lawsuit. Each attacks a legal position taken without any legal justification therefor.[73] In the lending context, this tort occurs when the lender completely denies that a loan contract was formed, or unreasonably claims that it is legally unenforceable.[74]

Proof of bad faith and lack of probable cause are essential elements. Hence, it is not a tort if the denial is made in good faith[75] or where probable cause for denial exists.[76] Probable cause exists where any legitimate defense exists: These defenses include the lack of proof of any essential element of the loan contract, that the oral agreement is barred by the statute of frauds, or barred by the parol evidence rule.[77] Because, as discussed below, a claim of an oral contract usually gives rise to these defenses, plaintiffs will seldom prevail on a claim that such defenses were made in bad faith.

II. The Problem of Contractual Certainty: Of What Does a Contract to Lend Money Consist?

A contract or agreement, in the eyes of the law, is neither written nor oral. A description of a contract as written or oral is simply a method of indicating how proof of its existence and its terms are to be established.[78] Absent express statutory authority to the contrary, oral

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good faith and fair dealing; In contrast, *Air-Sea Forwarders, Inc. v. Air Asia Co. L.T.D.*, 880 F.2d 176, 187 (9th Cir. 1989), *cert. denied*, 493 U.S. 1058 (1990) found bad faith denial to be a wholly distinct tort. The tort is also attractive because, as most courts conclude, the special relationship is not required. *E.g.*, Martin v. U-Haul Co. of Fresno, 204 Cal. App. 3d 396, 412, 251 Cal. Rptr. 17, 25-26 (1988); ***Okun v. Morton***, however, found the special relationship is required. These and other infirmities perhaps led Ninth Circuit Judge Alex Kozinski to write: "In inventing the tort of bad faith denial of contract, the California Supreme Court has created a cause of action so nebulous in outline and so unpredictable in application that it more resembles a brick thrown from a third story window than a rule of law." Oki America, Inc. v. Microtech Intern Inc., 872 F.2d 312, 315 (9th Cir. 1989) (Kozinski, J., concurring).

[73] Careau & Co. v. Security Pac. Business Credit, Inc., 222 Cal. App. 3d 1371, 1402, 272 Cal. Rptr. 387, 405 (1990).

[74] *Id.* at 1403-04, 272 Cal. Rptr. at 405-07.

[75] *Seaman's*, 36 Cal. 3d at 770, 686 P.2d at 1167, 206 Cal. Rptr. at 363.

[76] *Careau*, 222 Cal. App. 3d at 1403-04, 272 Cal. Rptr. at 405-07.

[77] *Id.* at 1402, 272 Cal. Rptr. at 405. *Kruse*, 202 Cal. App. 3d at 57-60, 248 Cal. Rptr. at 228-30; Issac v. A & B Loan Co., 201 Cal. App. 3d 307, 313, 247 Cal. Rptr. 104, 108 (1988).

[78] Lande v. Southern Cal. Freight Lines, 85 Cal. App. 2d 416, 420, 193 P.2d 144,

contracts are binding and enforceable.[79] The difficulty in enforcing oral contracts typically lies in the lack of certainty as to what the parties actually agreed to do.

Before a loan agreement can be enforced, it must be reasonably certain as to most, if not all, of the essential elements of the agreement, i.e., the material rights and obligations of each party.[80] Where an essential element of the contract is left to future agreement by *both* parties, all that exists is an unenforceable agreement to make an agreement.[81] The policy behind the "certainty" rule lies in the fact that a court examining a vague and indefinite agreement cannot tell what the agreement was, whether it has been breached, or what should be done about the breach.[82] For example, an alleged contract to lend money which failed to clarify when the money must be paid back could not be enforced because the borrower's obligation to repay the money would never accrue.[83] The threshold question, then, is what are the essential elements of a lending agreement? Judicial answers to this question lack consistency, completeness, and a reasoned analysis.

A. *The Clarification of What a Contract to Lend Money Must Consist*

Although the trend in the few relevant cases has been toward requiring certain key elements in oral lending contracts, a definitive consensus as to what those elements are has never been reached. Common sense suggests that a legally-sufficient lending contract would require that the parties agree on how much would be loaned, how much must be paid back, and when and how these events would occur. If those terms were agreed to, it would seem that other peripheral terms would not be the *sine qua non* to formation of a binding agreement. Such is not the case.

In *Transamerica Equipment Leasing Corp. v. Union Bank*,[84] a bus-

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147 (1948).

[79] Empire etc. Bldgs. Co. v. Harvey Mach. Co., 122 Cal. App. 2d 411, 415, 265 P.2d 32, 34 (1954).

[80] Ablett v. Clauson, 43 Cal. 2d 280, 284-85, 272 P.2d 753, 756 (1954). Peterson Dev. Co. v. Torrey Pines Bank, 233 Cal. App. 3d 103, 115, 284 Cal. Rptr. 367, 374 (1991).

[81] *Ablett*, 43 Cal. 2d at 284-85, 272 P.2d at 756. A binding agreement may be made where an essential term is left to the option of *one* party.

[82] Apablasa v. Merritt & Co., 176 Cal. App. 2d 719, 723, 1 Cal. Rptr. 500, 503 (1959).

[83] *See* Transamerica Equip. Leasing Corp. v. Union Bank, 426 F.2d 273, 274-75 (9th Cir. 1970).

[84] *Id.*

iness sued a bank for breach of an oral agreement to make a loan. The court found only an unenforceable agreement to make an agreement because the questions of when the money must be repaid and who would receive the first payment of income from the source for which loan funds would be used, and the status of the bank's loan fee were either reserved for future agreement or never discussed. The court also noted that a written contract was contemplated, but never made.

The lack of repayment schedule is clearly problematic; but *Transamerica* implies that uncertainty as to who could receive the first payment or how the bank's fee would be paid could void formation of a contract, regardless of the existence of other key terms. Did the court mean to establish a rule that an otherwise certain agreement should be unenforceable for lack of these peripheral details? The court's decision is made without authority or analysis; no indication exists as to why these terms are essential.

In *Laks v. Coast Federal Savings & Loan Ass'n*,[85] a developer sued for breach of a commitment to provide two loans. Plaintiffs argued a promissory estoppel theory, which provides relief when a legally binding contract has not been formed, but it would be unfair not to enforce the bank's promise. The would-be borrowers argued that they reasonably and foreseeably relied to their detriment on the promise by not seeking alternative financing and by proceeding with the development.

But just as a contract requires definite terms, promissory estoppel requires a "clear and unambiguous promise" about the loan. The exact amount of the loan, disbursement and repayment schedules, the interest rate, the security for the loan, prepayment rules, and the bank's rights under a default were not set forth clearly and unambiguously. The court emphasized that, while none of these missing terms were in themselves determinative, the lack of all of them added up to a vague, ambiguous, and unenforceable promise to make a loan.[86]

Taken literally, *Laks* implies that the loan amount (or some other key term) could have been left out, but that the promise would nevertheless have been enforced if the other elements were present. How much money, then, would the lender be obligated to loan? As of 1976, the courts were not concerned with providing guidance to lenders and borrowers as to what terms must be confirmed to create a binding and enforceable lending contract. Subsequent cases have done little to clarify this issue.

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[85] 60 Cal. App. 3d 885, 131 Cal. Rptr. 836 (1976).
[86] *Id.* at 891, 131 Cal. Rptr. at 839.

In *Landes Construction Co., Inc. v. Royal Bank of Canada*,[87] a borrower successfully sued the bank for breach of an oral agreement to lend seven million dollars for the purchase of land. The bank argued on appeal that the evidence was insufficient to support the jury's finding of an oral agreement. The court's opinion simply states that the borrower testified that he and the lender reached an agreement on the essential terms of the loan contract, and that the lender testified otherwise. Applying the substantial evidence test and California law, the appellate court affirmed the jury's finding of an oral contract because the evidence supported such a conclusion.[88] But the court failed to define what the essential terms of the loan contract were. The evidence established that the amount of the alleged loan was not in dispute.[89] The court (in its discussion of the statute of frauds issue) also assumed, without indicating why such an assumption was made, that the jury concluded that the borrower promised to pay interest and loan fees, to repay the principal, and to grant the lender a security interest in the property to be purchased.[90]

Enough evidence was presented to prove that a contract was formed. But exactly what elements were necessary to establish a contract and which elements were merely supportive, and why, was left unclear. What is clear is that in December of 1987, the essential elements of a lending agreement are not well established, if they exist at all.

Six months later, *Kruse v. Bank of America*[91] failed to clearly establish the essential terms of a contract to lend money, despite an opportunity to do so. The *Kruse* opinion memorializes the truly sad saga of an apple grower's good-hearted, but economically-unsound attempt to rescue a financially-distressed neighbor, an apple processor. Both sued the bank when financing negotiations collapsed. Plaintiffs successfully convinced a jury that numerous conversations between the bank and the borrowers, which were enhanced with optimistic or hopeful expressions of future financing, coupled with evidence of the parties' prior course of financial dealings, amounted to two contracts to lend money; the jury then concluded that when the bank denied that such contracts existed, it did so in bad faith.[92]

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[87] 833 F.2d 1365 (9th Cir. 1987).
[88] *Id.* at 1371.
[89] *Id.* at 1368, 1371.
[90] *Id.* at 1370.
[91] 202 Cal. App. 3d 38, 248 Cal. Rptr. 217 (1988), *cert. denied*, Duck v. Bank of America, 488 U.S. 1043 (1989).
[92] *Id.* at 57-58, 248 Cal. Rptr. at 228-29.

The appellate court reversed. The bad faith denial tort was inapplicable because there were no underlying contracts upon which it could be based. The court found "a complete lacuna in the proof of essential terms [in one] of the loan agreement[s]: Namely, the amount of the loan, the rate of interest, the terms of repayment, applicable loan fees and charges."[93]

B. *The Elements of a Lending Contract After Kruse Are Still Unclear*

Application of the essential loan terms articulated in *Kruse* to other cases is unknown. Are these terms essential to all lending contracts? Would a court find that no enforceable agreement existed merely because the loan fees and charges were left for future determination, where it otherwise appeared that a binding agreement was made? Conversely, did the *Kruse* court mean to imply that identification of the security[94] for a commercial loan was not an essential term?[95] And was the loan disbursement schedule[96] also unessential, even though the terms of repayment were necessary? If so, a binding contract to lend money could be formed, even though the bank's obligation to actually fund the loan never accrues.

Exactly what constitutes a lending agreement in California, and why, is still vague. In 1991, *Peterson Development Co. v. Torrey Pines Bank* followed *Laks v. Coast Federal Savings & Loan Ass'n* to find that the identities of the borrower and lender, the amount of the loan and the terms for repayment were essential terms of a lending contract. The opinion suggests the court approves of these limited essential elements which it derived from *Laks*, but does not reference the other *Laks* terms, discuss why the enumerated terms are essential, or even mention the *Kruse* case.[97]

Where an essential contractual element is missing, the courts prefer to find certainty by looking at the intent of the parties.[98] Courts will

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[93] *Id.* at 60, 248 Cal. Rptr. at 230. The court failed to accept the argument that the terms contained in a previously-prepared report for a different loan for different purposes on different property should be applied to the loan contract in question.

[94] The apple grower had repeatedly refused to encumber his ranch; *Id.* at 56, 248 Cal. Rptr. at 227; thus, it cannot be inferred that the ranch would secure the loan.

[95] Identified in *Laks*, 60 Cal. App. 3d at 891, 131 Cal. Rptr. at 839, as an essential loan term in the promissory estoppel context.

[96] Also an essential element in *Laks*. *Id.*

[97] 233 Cal. App. 3d 103, 115, 284 Cal. Rptr. 367, 374 (1991).

[98] Okun v. Morton, 203 Cal. App. 3d 805, 817, 250 Cal. Rptr. 220, 227 (1988).

occasionally supplement an incomplete contract with "reasonable terms," as long as this does not create a contract beyond what the parties intended.[99] Whether and to what extent this policy will be applied to oral lending contracts remains to be seen. Such a policy would not have saved the plaintiffs in *Kruse* or *Laks*, but it would be of tremendous importance when only one or two contractual elements are difficult to prove.

To date, the courts have failed to articulate either the minimum or the preferred terms which borrowers and lenders must agree on before a binding obligation to lend money will obtain. Yet, the cases discussed above make it equally apparent that the courts require more "essential" terms than are strictly necessary for the court to determine that an agreement was made, or whether it was breached. Therefore, every reason exists for California's judiciary to define with consistency what must be pleaded and proved to establish that the parties entered into a binding agreement to lend money. Although rigid enforcement of an essential element list might result in an injustice, lenders and borrowers need both guidance as to what the law requires, and consistency in the enforcement of such requirements. Such clarification could prevent ambiguous negotiations in the lending process, and numerous lawsuits as well.

The law discussed above offers the lesson that unless the borrower can show an agreement on a substantial number of loan terms (which should probably include the amount of the loan, the range of interest rates that might be applied, disbursement and repayment schedules, the collateral, and everything else that either party has indicated to be essential), no contract will be found. Accordingly, if the borrower has not obtained a firm commitment from the lender on a substantial number of significant terms, he should not conclude that he has anything more than an unenforceable agreement to agree in the future.

C. *Cases From Other States*

In contrast to California, Illinois has developed a line of cases which establish specific criteria for a contract to lend money in the future. At least five cases in the previous decade found oral lending agreements unenforceable for lack of the same essential terms: loan duration, interest rate, mode of repayment, and when and how repayment would oc-

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[99] *Id.* (citing 1 CORBIN ON CONTRACTS § 95, at 400 (1963)); *see also*, *Kruse*, 202 Cal. App. 3d at 60, 248 Cal. Rptr. at 230, and *Peterson*, 233 Cal. App. 3d at 115, 284 Cal. Rptr. at 374-75, wherein supplementation of reasonable terms in order to find certainty in lending agreements is apparently approved, although not implemented.

cur.[100] Hence, *some* consistency in the law has been established for lenders and borrowers to rely on. These cases involved extensions of existing loans, which accounts for the absence of the loan amount as an essential element. For example, in *Champaign v. Landers Seed Co. Inc.*, the court equated an oral agreement to refinance or rollover a debt with an oral agreement to lend money in the future.[101]

Several North Dakota cases have also established a rather flexible doctrine, requiring the amount and duration of the loans, interest rates, and "where appropriate," methods of repayment and collateral, if any.[102] The "where appropriate" language and the court's indication that none of these are completely essential may, as in California, leave litigants confused as to where they stand. North Dakota prefers to find certainty as to essential terms by supplementing the contract where reasonable terms can be established.[103]

III. The Statute of Frauds

The phrase "statute of frauds" refers collectively to various statutory provisions which require that certain types of contracts be put in writing, and signed by the party to be bound. The goal the statute of frauds is to concretely preserve evidence of the terms the parties have mutually agreed upon.[104] The purpose behind the goal is to prevent fraud and perjury.[105]

Until recently, the statute of frauds had fallen into disfavor with the courts; perceived as unfair, its abolition was consistently urged.[106] In 1987, the California Supreme Court confirmed the viability of the statute by acknowledging that the legislative preference for written con-

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[100] *See* Delcon Group v. Northern Trust Corp., 187 Ill. App. 3d 635, 543 N.E.2d 595, 600 (1989); Champaign Nat'l Bank v. Landers Seed Co., Inc., 165 Ill. App. 3d 1090, 519 N.E.2d 957, 960 (1988) *cert. denied*, 489 U.S. 1019 (1989).

[101] 519 N.E.2d at 960.

[102] *See* Union State Bank v. Woell, 434 N.W.2d 712, 717 (N.D. 1989).

[103] Delzer v. United Bank of Bismarck, 459 N.W.2d 752, 758-59 (N.D. 1990). The court found that a jury could reasonably infer the interest rate from prevailing rates offered in the ranching and farming sector, and the amount, collateral, and loan duration period from documents generated by the parties, including the borrower's cash flow projections.

[104] Sherwood v. Lowell, 34 Cal. App. 365, 375, 167 P. 554, 558-59 (1917).

[105] Riley v. Bear Creek Planning Comm., 17 Cal. 3d 500, 509, 551 P.2d 1213, 1220, 131 Cal. Rptr. 381, 388 (1976).

[106] Sunset-Sternau Food Co. v. Bonzi, 60 Cal. 2d 834, 838 n.3, 389 P.2d 133, 136 n.3, 36 Cal. Rptr. 741, 744 n.3 (1964).

tracts is stronger than ever before.[107] The California legislature itself indicated such a preference in 1988 by adding a new section to the code.[108]

To comply with the statute, the essential terms of the contract must be in writing; the agreement, the context in which its made, and the subsequent conduct of the parties determine what is essential to satisfy the requirements of the statute.[109] The writing need not be formal, but must usually be signed by the party who is to be obligated.[110] A contract which does not comply with the statute is voidable or unenforceable, but its formation or existence remains intact.[111]

A. *Recent Developments in the Statute of Frauds*

Several provisions of the statute of frauds are applicable to lender-borrower contracts.[112] Significant aspects of these provisions which affect borrowers attempting to enforce oral agreements are as follows:

An agreement that by its terms is not to be performed within one year from its making must be in writing, and signed by the party to be charged or that party's agent.[113] *Foley v. Interactive Data Corp.* reaffirmed that this rule will only be enforced when the agreement, by its terms, *cannot possibly be performed* within one year.[114]

In 1990, the North Dakota Supreme Court declined to apply a similar statute of frauds provision because the terms of the agreement could theoretically be performed within one year. The borrowers alleged the bank orally promised to grant a $300,000 line of credit for the purchase of cattle, and the evidence suggested the parties believed that both disbursement and repayment of the funds would take more than one year.

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[107] Phillippe v. Shapell Indus., 43 Cal. 3d 1247, 1265, 743 P.2d 1279, 1289, 241 Cal. Rptr. 22, 32 (1987), *cert. denied*, 486 U.S. 1011 (1988).

[108] CAL. CIV. CODE § 1624(g) (West 1991).

[109] Seaman's Direct Buying Servs., Inc. v. Standard Oil Co., 36 Cal. 3d 752, 762, 763, 686 P.2d 1158, 1162, 206 Cal. Rptr. 354, 358 (1984).

[110] Harper v. Goldschmidt, 156 Cal. 245, 246-47, 104 P. 451, 452 (1909).

[111] Masin v. Drain, 150 Cal. App. 3d 714, 717, 198 Cal. Rptr. 367, 369 (1984).

[112] CAL. CIV. CODE §§ 1624(a),(f) and (g) (West 1990), CAL. CODE CIV. PROC. § 1971 (West 1990). *See also*, Remainders, Inc. v. Bartlett, 215 Cal. App. 2d 295, 298-99, 30 Cal. Rptr. 191, 194 (1963).

[113] CAL. CIV. CODE § 1624(a) (West 1990). The authority of an agent to enter into a contract required by law to be in writing must itself be given in writing. CAL. CIV. CODE § 2309 (West 1990); Ripani v. Liberty Loan Corp., 95 Cal. App. 3d 603, 610, 157 Cal. Rptr. 272, 277 (1979).

[114] 47 Cal. 3d 654, 671-75, 765 P.2d 373, 381-83, 254 Cal. Rptr. 211, 219-21 (1988) (Emphasis added).

The court refused to apply the statute of frauds, finding that the contract, by its terms, could be performed within one year, even though the parties intended performance to extend beyond one year, performance did in fact take more than one year, and the possibility of performance within one year was extremely remote.[115]

But even under such a liberal interpretation, a borrower who enters a short-term (but longer than one year) written loan agreement accompanied by an oral agreement that long-term financing will be provided when the short-term note becomes due, will not be able to enforce that rollover agreement because the short-term note can't possibly be due within one year: The contract, by its terms, cannot possibly be performed within one year.

Another key rule was also recently reaffirmed in *Landes Construction Co. Inc. v. Royal Bank of Canada*[116]: The statute will be enforced only where the alleged oral agreement is precisely covered by the statutory language. Although this rule favors borrowers, the ultimate consequences of this case favor the lender. In *Landes*, the lender's chief defense to an oral lending-contract claim was based on the statute of frauds. The borrower orally agreed to give the bank a security interest in the property to be purchased with the loan funds. Such an agreement conveys an interest in the real estate, and must be in writing.[117] The bank argued that the statute of frauds thus prevented the borrower from presenting evidence of the alleged oral contract.

Following California precedent, the *Landes* court held that when promises not within the statute of frauds are coupled with one that is, the former are enforceable if they are divisible or separable. In 1987, an oral agreement to lend money was not covered by the statute of frauds. Because, as the court assumed, the jury found that the borrower had promised to pay interest and loan fees and to repay the principal (in addition to its promise to grant the bank a security interest), the court concluded that such promises were a separable part of the agreement and thus not barred by the statute of frauds. Plaintiffs were thus allowed to present evidence of an oral agreement. This reaffirmed California's policy of restricting application of the statute to only those situations precisely covered by the express language of the subject code

[115] Delzer v. United Bank of Bismarck, 459 N.W.2d 752, 754 (N.D. 1990) (following Bergquist-Walker Real Est. v. W. M. Clairmont, 33 N.W.2d 414, 418 (N.D. 1983), and Zimmerman v. First Federal Sav. and Loan Ass'n, 848 F.2d 1047, 1054 (10th Cir. 1988)).

[116] 833 F.2d 1365 (9th Cir. 1987).

[117] CAL. CODE CIV. PROC. § 1971 (West 1991).

section.[118]

While *Landes* was good news for borrowers, it (along with extensive lobbying by the lending industry) convinced the California legislature to amend the statute of frauds in 1988.[119] Today, a contract, promise, undertaking, or commitment to lend money for commercial use in an amount over $100,000 by a commercial lender must be in writing to be enforceable.[120] On its face, this new law strongly favors lenders.

B. The Consequences of this New Statute of Frauds Provision is Unknown

No published appellate court decision has addressed this new provision; many questions exist as to how its language will be interpreted. The typical means of circumventing the statute (the doctrines of estoppel, part or full performance, etc.) may or may not apply. Although the new section favors lenders, disgruntled borrowers should not ignore their rights. The courts may strictly apply the letter of the statute.

Threshold issues of statutory interpretation arise in the context of the revolving crop loan: How many transactions will constitute "a contract, promise, undertaking, or commitment to loan money or to grant or extend credit," within the meaning of the new section? And how will the $100,000 break point be calculated with respect to each transaction deemed "a" contract, etc.?[121]

These questions are important because agricultural borrowers frequently rely on revolving crop loans, wherein financing is renewed periodically. Oral commitments of this type are extremely common. Borrowers need to know about future financing, and lenders typically give oral assurances before anything is written. Will the courts interpret each periodic disbursement as a single transaction, which, if less than $100,000, would fall outside the statute of frauds? Or will they aggregate all disbursements tied to a single initial agreement to find such loans are within the $100,000 range of the statute?

The most important issues yet to be resolved about the new statute are whether and to what extent a borrower can circumvent the harsh

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[118] *Landes*, 833 F.2d at 1370.

[119] *See* 9 MILLER & STARR, CALIFORNIA REAL ESTATE § 28: 2, at 6 n.20 (2d ed. 1990).

[120] CAL. CIV. CODE § 1624(g) (West 1990). A loan secured solely by residential property is exempt, as are loans to be used primarily for personal, family or household use.

[121] A second issue focuses on retroactivity. Will the statute apply to suits brought to trial, suits filed, or loans made before the enactment?

result of the statute, and enforce an oral agreement. Logic suggests the doctrines of estoppel, fraud, partial performance, and waiver by admission will allow a borrower to allege the breach of an oral agreement; but these doctrines do not always apply equally to all sections of the statute.

The doctrine of "estoppel to assert the statute of frauds" allows the borrower to allege an oral lending contract if 1) the borrower has materially changed his position in reliance on the oral promise, and the lender is aware of this change in position; and 2) an unconscionable injury would result to the borrower if the promise is not enforced.[122] For example, if a borrower purchases land or pays off a loan in reliance on a lender's oral promise that a new loan would be made, the borrower suffers extreme financial hardship when the new loan is not made, and the lender is aware of these facts, the oral promise may be enforced (assuming it can be proved), even though the statute of frauds applies.

The statute of frauds will also not prevent the borrower from claiming that the lender fraudulently induced him into borrowing money.[123] When the lender's agent makes a promise, which he has no intention of keeping or has no reasonable grounds for believing the promise will be kept, for the purpose of inducing the borrower to enter into a lending contract, the borrower may sue for fraud, even though the contract is unenforceable under the statute of frauds.

The doctrine of part performance[124] allows circumvention of the statute of frauds when the parties' actions establish that a contract was made because, if no agreement existed, one or both of the parties would not have done what they otherwise did.[125] The acts constituting part performance must actually prove the agreement. That is, the parties must have acted in a manner which 1) indicates an agreement did exist; and 2) is not consistent with some other explanation for the conduct.[126]

A California decision regarding the waiver by admission exception to

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[122] *In re* Destro, 675 F.2d 1037, 1040 (9th Cir. 1982); Monarco v. Lo Greco, 35 Cal. 3d 621, 220 P.2d 737 (1950).

[123] *See* Tenzer v. Superscope, Inc., 39 Cal. 3d 18, 28-31, 702 P.2d 212, 218-19, 216 Cal. Rptr. 130, 135-37 (1985); *see also*, CAL. CIV. CODE § 1623 (West 1990).

[124] Some courts allow use of the part performance doctrine in equity actions only. Becker v. First Am. State Bank of Redwood Falls, 420 N.W.2d 239, 240-41 (Minn. Ct. App. 1988).

[125] Pearsall v. Henry, 153 Cal. 314, 318, 95 P. 154, 160 (1907); *Destro*, 675 F.2d at 1039-40.

[126] Foster v. Maginnis, 89 Cal. 264, 266, 26 P. 828, 829 (1891); Paul v. Layne & Bowler Corp., 9 Cal. 2d 561, 564, 71 P.2d 817, 819 (1937).

the statute of frauds is insightful, not because of its relevance to lending or oral contracts, but because the case enforced the technical letter of the law, rather than its spirit. In *Isaac v. A & B Loan Co.*,[127] a prospective purchaser of property sought to circumvent the statute of frauds by showing that the defendant had expressly admitted the existence of the oral contract in question in an affidavit filed in a previous judicial proceeding.

Plaintiffs relied on the rule that when a defendant admits an oral contract in an answer to a complaint on that oral contract, without asserting the statute of frauds as a defense, the defense is waived because the admission ostensibly meets the writing requirement of the statute. The court refused to apply this rule because the admission occurred in a separate case.[128] This decision appears to be in serious conflict with the goal of the statute: to prevent fraud and perjury. It also conflicts with the logic behind the exceptions, which do not allow the defendant to avoid valid obligations by using the statute as a shield to perpetrate its own fraud.[129] The alleged oral contract clearly existed. The court had no reason to invoke the statute.

Finally, borrowers should also note that one of the most effective means to circumvent the statute of frauds is to use the otherwise inadmissible evidence of the oral contract to support a legal theory not based on an oral contract. One court allowed the plaintiff to introduce evidence of an oral agreement to prove agency and fiduciary responsibility, in support of a constructive trust theory.[130]

The statute of frauds, and especially the new section pertaining to loans over $100,000, compounds the difficulty of enforcing oral agreements, even where the terms are sufficiently certain. Judicial response to the statute is best described as mixed. It seems fair to say that the courts favor the concept of the statute of frauds in general because it ostensibly prevents specious claims of oral contracts. Conversely, the courts favor enforcement of the statute of frauds only where the facts of the case fit precisely within the letter of the various code provisions that comprise the statute. This should offer some, but not much, hope to aggrieved borrowers.

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[127] 201 Cal. App. 3d 307, 247 Cal. Rptr. 104 (1988).

[128] *Id.* at 311, 247 Cal. Rptr. at 106-07.

[129] *Tenzer*, 39 Cal. 3d at 29-30, 702 P.2d at 218-19, 216 Cal. Rptr. at 136; Monarco v. Lo Greco, 35 Cal. 2d 621, 623, 220 P.2d 737, 739-40 (1950); Seymour v. Oelrichs, 156 Cal. 782, 794, 106 P. 88, 92-93 (1909).

[130] Walter H. Leimert Co. v. Woodson, 125 Cal. App. 2d 186, 190-91, 270 P.2d 95, 98 (1954).

The peculiarity of the statute of frauds lies in the legislature's choices as to which types of contracts must be in writing. Why are lending contracts deserving of such treatment? Are they intrinsically different than other contracts, or is it simply that lending industry lobbyists were successful in their attempts to protect the banks and insurance companies? In any event, the legislature has indicated its distaste with lender liability suits based on oral contract claims, and their accompanying huge damage awards. Judicial application of the statute of frauds is likely to continue in that vein.

IV. Fraudulent Promises

Lenders are frequently accused of fraudulently inducing borrowers into various arrangements pertaining to potential or existing loans. Three basic types of fraud likely to occur in the lending context are: 1) the promisor has no intention of keeping the promise, or no reasonable grounds for believing that the promise will be kept; 2) the promisor conceals key facts from the promisee to the extent that the promisee does what he would not otherwise do had he known the truth; and 3) the promisor fails to disclose information which, by reason of the parties' relationship, he had a duty to disclose.

To establish fraud, the borrower must conjunctively prove that the false promise was material to the agreement, was made intentionally or negligently, that the promise actually induced the borrower to rely on the promise, that such reliance was justified in light of the circumstances, and that the promise was the actual and legal cause of the borrower's injuries.[131] Each of these elements has been problematic for borrowers in recent cases involving farm loans, but proving justifiable reliance on an oral promise has become especially difficult.

A. *Justifiable Reliance*

A borrower's reliance on a lender's fraudulent promise must be justified. Courts frequently state: "If the conduct of the plaintiff in the light of his own intelligence and information was manifestly unreasonable, he will be denied recovery."[132]

In *Kruse v. Bank of America*, plaintiffs contended that "the bank fraudulently induced them to undertake short-term borrowing without disclosing the possibility that their request for long-term financing

[131] Gonsalves v. Hodgson, 38 Cal. 2d 91, 100-01, 237 P.2d 656, 662 (1951).
[132] *Kruse*, 202 Cal. App. 3d at 54, 248 Cal. Rptr. at 226.

would be denied."[133] They had borrowed over one million dollars in short-term loans in reliance on statements of a bank officer known by plaintiff to have limited lending authority. The bank officer implied that the short-term loans would be rolled over into long-term loans. The grower claimed these statements, coupled with the bank's failure to disclose that the loans might be denied, lulled them into a false sense of security that long-term financing would be available.[134]

The *Kruse* court found a complete lack of justifiable reliance because the apple grower knew that any long-term financing must be approved by bank superiors of the officer upon whom he claimed to have relied. This approval requirement necessarily implied the possibility that the loan could be denied. The plaintiff's reliance on the bank's failure to disclose that the loan would be denied was unreasonable. The court implied that even if the bank had a legal obligation to tell him that the loans might be denied, his awareness of the loan-approval process required that he investigate the facts for himself.[135]

The Missouri Court of Appeals reached a similar decision in *Centerre Bank of Kansas City v. Distributors.*[136] The bank allegedly promised that if certain guarantees were executed, the bank would continue to extend credit and not call in the notes. The guarantors' claim of fraud was dismissed for lack of justifiable reliance because they knew that credit extension was a committee decision beyond the authority of the loan officer making the suspect representation.[137]

The borrower's behavior is also a factor in determining whether reliance on a promise is justified under California law. In *Price v. Wells Fargo Bank*, plaintiff ranchers contended the bank orally promised to restructure delinquent loans. The bank also allegedly concealed that the loan officer who negotiated with them did not have the authority to renew the loans at issue, that renewal of one loan was conditioned on two other loans being paid off, and that those loans would be considered in default if not paid when due.[138] The borrowers claimed the written loan terms varied from what the bank had orally promised. However, the ranchers had consistently complied with the terms of the written agreements by making payments of both principal and interest, and not disputing the bank's demand for payment when the borrowers

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[133] *Id.*

[134] *Id.* at 46-49, 55, 248 Cal. Rptr. at 221-23, 226-27.

[135] *Id.* at 55, 55 n.10, 248 Cal. Rptr. at 226-27, 226 n.10.

[136] 705 S.W.2d 42 (Mo. App. 1985).

[137] *Id.* at 49-50.

[138] 213 Cal. App. 3d at 471-72, 480, 261 Cal. Rptr. at 736-37, 742-43.

fell behind. Also the ranchers clearly understood both the maturity dates of the notes and that they had failed to make payment when due.[139] Hence, the court affirmed summary judgment in the bank's favor because the borrowers' reliance, if any, was unjustified.

Borrower sophistication is also a factor in determining whether reliance is justified when fraud is claimed. In *Wagner v. Benson*,[140] the jury found a lack of justifiable reliance because the borrowers' financial sophistication rendered their "inexperienced investor" claim disingenuous. Plaintiffs alleged that they borrowed from the bank to invest in the cattle-raising business only because the bank assured them that the investment was safe, and that margin calls would be minimal. The borrowers appealed the admission at trial of evidence of their previous investment experience. The court found such evidence directly relevant to the issue of justifiable reliance.[141]

In *Runnemede Owners, Inc. v. Crest Mortgage Corp.*, the court applied Illinois law to find no justified reliance (which must be proved by clear and convincing evidence in Illinois) by sophisticated borrowers on a loan officer's boastful statements to the effect that loan approval was merely a formality. The statement flatly contradicted the conditional nature of the commitment letter provided by the bank.[142]

Finally, reliance on an indefinite promise will not be justified. The lesson of *Laks v. Coast Federal Savings & Loan Ass'n* applies here. *Laks* required a clear and unambiguous promise to make a loan, finding the amount of the loan, disbursement and repayment schedules, interest rates, and the security to be essential terms of an enforceable promise.[143] While the promise need not contain every detail, it must be specific and positive. Vague predictions or promises about what might happen in the future should not be relied on.

These cases teach that the courts will not allow a borrower to blindly rely on a lender's promises when the truth is within their own grasp. A borrower must use common sense, logic and business experience. He must evaluate for himself the promises he contemplates; and if he suspects a problem, he must investigate to his own satisfaction. In today's lending climate, this means seeking confirmation of the oral promise in writing, from someone with the authority to confirm the promise.

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[139] *Id.* at 480-81, 261 Cal. Rptr. at 742-44.

[140] 101 Cal. App. 3d 27, 31-32, 161 Cal. Rptr. 516, 519 (1980).

[141] *Id.* at 36, 161 Cal. Rptr. at 521-22.

[142] 861 F.2d 1053, 1058-59 (7th Cir. 1988).

[143] 60 Cal. App. 3d 885, 891, 131 Cal. Rptr. 836, 839 (1976).

V. The Parol Evidence Rule

The all too common scenario finds a borrower confronted with a written contract which contains terms he did not know he agreed to, or does not contain terms he thought were essential. The parol evidence rule severely restricts the borrower's ability to argue that the written contract should not be taken as the complete and only agreement between the parties.

The logic behind the rule is that the act of embodying the complete terms of an agreement in writing *becomes the contract of the parties.* Parol ("oral" or other extrinsic matter) evidence is inadmissible because it cannot add anything: The writing is the contract.[144] The doctrine has undergone numerous changes and has been presented in just as many variations, but is now codified in California.[145]

Condensed to its relevant essentials, the rule might function as follows: a borrower and lender meet and negotiate the terms of a potential lending agreement. If a tentative agreement is reached, the lender sends a "commitment letter" to the borrower, which ostensibly contains all the terms of the agreement. If the borrower signs it, the question raised is whether the signed writing is an integrated agreement.

Integration occurs when the parties intended the writing to serve as the final, exclusive embodiment of their agreement.[146] Integration frequently occurs by way of a merger clause; the agreement itself may state, for example, that: "This agreement contains the entire agreement between the bank and the borrower. There are no oral or collateral agreements or understandings of any kind."[147] Contracts drawn by commercial lenders almost always contain such language. Integration may also be established absent an explicit statement to that effect. Evidence of the negotiations and the circumstances in which they occurred are relevant as to whether the parties intended the writing to be the

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[144] Estate of Gaines, 15 Cal. 2d 255, 264-65, 100 P.2d 1055, 1060 (1940); Tahoe Nat'l Bank v. Phillips, 4 Cal. 3d 11, 22-23, 480 P.2d 320, 329, 92 Cal. Rptr. 704, 713 (1971).

[145] Cal. Code Civ. Proc. § 1856 (West 1983); Cal. Civ. Code § 1625 (West 1985); *see generally*, FPI Development Inc. v. Nakashima, 231 Cal. App. 3d 367, 386-87, 282 Cal. Rptr. 508, 519 (1991).

[146] *Nakashima*, 231 Cal. App. 3d at 386, 282 Cal. Rptr. at 518; Masterson v. Sine, 68 Cal. 2d 222, 225, 436 P.2d 561, 563, 65 Cal. Rptr. 545, 547 (1968).

[147] *See* Gerdlund v. Electronic Dispensers Int'l, 190 Cal. App. 3d 263, 268, 235 Cal. Rptr. 279, 280 (1987). The mere existence of an integration clause (merger clause) does not automatically render the contract integrated, especially where it is obvious that key terms are missing.

sole and complete agreement.[148] The agreement may be partially integrated, final as to some aspects, but not as to others.[149]

If the parties have intended the written agreement to constitute their final, complete, and exclusive agreement with respect to certain terms, parol evidence may not be used to contradict, explain, or supplement the agreement; if the written agreement is not to be a complete and exclusive statement of the agreement, its terms may be explained or supplemented, but not contradicted.[150] However, parol evidence may be introduced to determine the meaning of the writing, including the question of whether the agreement should be considered integrated, even where the writing appears unambiguous on its face.[151] And where more than one writing is involved, parol evidence is admissible to show several papers constitute the contract.[152]

A. *Recent Lender Liability Cases Reaffirm the Harshness of the Parol Evidence Rule*

In 1935, *Bank of America v. Pendergrass* established that integration does not prevent admission of evidence to show the agreement was procured by fraud, unless that evidence contradicts the terms of the agreement.[153] Despite harsh criticism, this is still the law in California.

In *Price v. Wells Fargo Bank*, the borrowers had an established lending relationship with the bank. The Bank of America offered them a thirteen percent interest rate on a new loan. A Wells Fargo loan officer then countered with an offer to make a loan "at a better rate than Bank of America." In reliance thereon, the borrowers applied for the loan with Wells Fargo. But when Wells Fargo presented the promissory note, the rate was higher than Bank of America's rate. At that

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[148] Wagner v. Glendale Adventist Medical Center, 216 Cal. App. 3d 1379, 1386, 265 Cal. Rptr. 412, 416 (1989).

[149] Wallis v. Farmers Group, Inc., 220 Cal. App. 3d 718, 730, 269 Cal. Rptr. 299, 305 (1990).

[150] CAL. CODE CIV. PROC. §§ 1856(a) and (b) (West 1983); Continental Airlines, Inc. v. McDonnell Douglas Corp., 216 Cal. App. 3d 388, 418, 264 Cal. Rptr. 779, 795 (1989).

[151] *Nakishima*, 231 Cal. App. 3d at 389, 282 Cal. Rptr. at 521. Pacific Gas & Elec. Co. v. G. W. Thomas Drayage etc. Co., 69 Cal. 2d 33, 38-39, 442 P.2d 641, 644-45, 69 Cal. Rptr. 561, 564-65 (1968).

[152] Roberts v. Reynolds, 212 Cal. App. 2d 818, 824, 28 Cal. Rptr. 261, 266 (1963).

[153] Bank of America v. Pendergrass, 4 Cal. 2d 258, 263, 48 P.2d 659, 661-62 (1935); *see also*, Bank of America v. Lamb Finance Co., 179 Cal. App. 2d 498, 502, 3 Cal. Rptr. 877, 880 (1960) (Evidence of fraud directly contradicting personal guaranty held inadmissible).

point, Bank of America's rates had gone up, and the borrowers had no alternative but to take the Wells Fargo loan.[154]

While acknowledging the well-publicized harshness of the *Pendergrass* rule, the *Price* court followed it for two reasons. First, the "liberal," landmark parol evidence cases of the late 1960's cannot be construed to overrule *Pendergrass*.[155] Secondly, *Pendergrass* represents an awkward but necessary choice favoring the policy considerations of the parol evidence rule over those of common law fraud. In this situation, the sanctity of the written contract prevails over the potential harm of fraudulent promises,[156] a truly political decision favoring lenders and not their borrowers. The *Price* court applied *Pendergrass*, and dismissed the borrowers' claim of fraud because the bank's promise to beat another bank's rate was a contemporaneous oral agreement which contradicted the interest rate in the integrated promissory note.[157]

Other jurisdictions have reached similar results. In *Centerre Bank of Kansas City v. Distributors, Inc.*,[158] the bank's collection action was met with the borrower's counterclaim for breach of an oral contract, the terms of which were incompatible with the written loan guaranty. The alleged oral agreement required the bank to grant further credit and to not call in a note when due. The guaranty was integrated, said nothing about extensions of credit or restrictions on enforcing the note, but did state that the guaranty carried no conditions or limitations not expressly set forth therein. The court applied the parol evidence rule and enforced the guaranty.[159]

In so holding, the *Centerre Bank* court followed *Braten v. Bankers Trust Co.*, wherein individual guarantors of a promissory note sought to introduce evidence of an oral promise that the bank would continue to extend credit until some date beyond the date set forth in the note. The oral promise was inadmissible because it contradicted the due date in the note.[160]

Calder v. Camp Grove State Bank[161] tells the same story. Applying

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[154] *Price*, 213 Cal. App. 3d at 483, 261 Cal. Rptr. at 744-45.

[155] *Id.* at 485-86; (referring to Masterson v. Sine, 68 Cal. 2d 222, 436 P.2d 561, 65 Cal. Rptr. 545 (1968); Pacific Gas & Elec. Co. v. G. W. Thomas Drayage etc. Co., 69 Cal. 2d 33, 442 P.2d 641, 69 Cal. Rptr. 561 (1968); and Delta Dynamics, Inc. v. Arioto, 69 Cal. 2d 525, 446 P.2d 785, 72 Cal. Rptr. 785 (1968)).

[156] *Price*, 213 Cal. App. 3d at 483-86, 261 Cal. Rptr. at 744-46.

[157] *Id.*

[158] 705 S.W.2d 42 (Mo. App. 1985).

[159] *Id.* at 51-52.

[160] 468 N.Y.S.2d 861, 864, 456 N.E.2d 802, 805 (1983).

[161] 892 F.2d 629 (7th Cir. 1990).

Illinois law, the court found that the testimony of four Calder officers that the bank orally promised that a guaranty would no longer be in effect was inadmissible because it contradicted an integrated agreement. Illinois holds parol evidence inadmissible to contradict an integrated agreement unless the document is ambiguous on its face.[162]

California law is more liberal on this last point. Parol evidence may be used to determine the meanings of the document's language, even if the document is unambiguous on its face. *Trident Center v. Connecticut General Life Ins.*[163] criticized but then followed a radical, landmark California case which held that it is the intention of the parties, and not the writing itself, which ultimately determines the contractual obligations of the parties.[164]

In *Trident Center*, the borrower sought to prove that it was entitled to prepay on a $56,500,000 note, despite the note's express language that Trident "shall not have the right to prepay the principal hereof in whole or in part before January, 1996." The *Trident Center* court, while expressing its distaste for the *Thomas Drayage* rule, followed it. Despite the size of the loan, the parties' sophistication, the fact that the contract was negotiated with aid of counsel, and the contract's unambiguous facial appearance, Trident Center was entitled to introduce extrinsic evidence to determine the meaning of the prepayment clause.[165] Extrinsic evidence can be used for the purpose of determining whether the apparently integrated writing does in fact memorialize the true intent of the parties.[166]

Written loan agreements must be scrutinized for the purpose of ensuring that each and every bargained-for term is included. The borrower must also question to his or her satisfaction the need and/or purpose of other non-negotiated terms. In all probability, the borrower must live with the terms of the written document.

CONCLUSION

Judicial and legislative policy in California and elsewhere strongly favors written lending contracts. Disputes over oral claims become swearing contests. Written agreements minimize judicial guesswork as

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[162] *Id.* at 631-32; Rakowski v. Lucente, 104 Ill. 2d 317, 323, 472 N.E.2d 791, 794 (1984).

[163] 847 F.2d 564, 568-70 (9th Cir. 1988).

[164] *Thomas Drayage*, 69 Cal. 2d at 38, 442 P.2d at 644, 69 Cal. Rptr. at 564.

[165] *Trident Center*, 847 F.2d at 568-69.

[166] FPI Dev., Inc. v. Nakishima, 229 Cal. App. 3d 367, 389-90, 282 Cal. Rptr. 508, 521-22 (1991).

to the intent of the parties, and the manner of implementation of that intent. The policy behind the law discussed in this comment above seeks to prevent sympathetic juries from awarding irrationally-huge amounts of money to borrowers with legally unsupportable claims. In principal, such policy also encourages the parties to memorialize their agreements. The courts have decided that the importance of written contracts overrides any harsh treatment that may befall borrowers who have legitimate grievances with lenders who promised one thing, and delivered another. This marks an important change in the social relationship between lender and borrower.

Traditional values held some esteem for a person's word. A request to put a promise in writing once carried the stigma of doubting the promissor's integrity. It probably still does. But the judicial decisions of recent years have now institutionalized the proposition that borrowers have no right to trust their lender's word with respect to agreements to lend money.

Whether such a state of affairs will ultimately be beneficial or detrimental to the business relationships between lenders and borrowers or to the social relationships between humans is beyond the scope of this comment. But today's borrowers must negotiate with the realization that if its not in writing, its not enforceable. Every step of the lending transaction should be approached with that fact in mind.

Despite the fact that the torts of breach of the implied covenant of good faith and fair dealing and bad faith denial of contract are of little or no assistance to an aggrieved borrower, the short period in which they were perceived as viable remedies in oral contract cases brought much-needed publicity and judicial scrutiny to a serious situation. Without the possibility of tort and punitive damages, the wrongful conduct of powerful financial institutions would never have been questioned. As things currently stand, *caveat emptor* now defines the lender-borrower relationship; borrowers have little recourse when they believe they have been mistreated. The question is: How will the lenders respond to all this?

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