

Widener University Delaware Law School

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1990

General Provisions, Sales, Bulk Transfers, and Documents of Title

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General Provisions, Sales, Bulk Transfers, and Documents of Title

By David Frisch* and John D. Wladis**

EFFECT OF OTHER STATUTES UPON U.C.C.

This year several cases discussed the preemptive effect of the Federal Cigarette Labeling and Advertising Act¹ upon state law tort and contract claims arising from the sale of cigarettes to smokers who contracted cancer. This is aptly illustrated by *Forster v. R. J. Reynolds Tobacco Co.*,² which was decided by the Minnesota Supreme Court. In that case, the smoker (Forster) sued a cigarette manufacturer (R.J. Reynolds) in strict products liability,³ misrepresentation, breach of warranty, and negligence.⁴ The cigarette manufacturer moved for summary judgment on the ground that the Federal Cigarette Labeling and Advertising Act preempted all state tort claims. The trial court agreed and granted summary judgment. On appeal, the Minnesota Court of Appeals reversed, finding no preemption of state tort claims.⁵ The Minnesota Supreme Court granted the cigarette manufacturer's petition for review and, in an en banc decision, affirmed in part and reversed in part. The supreme court ruled that the Federal Cigarette Labeling and Advertising Act preempted only those state claims based on failure to warn theories.⁶ It ruled that the strict products liability, breach of warranty, and negligence counts were not preempted to the

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1. 15 U.S.C. §§ 1331-41 (1988).

2. 437 N.W.2d 655, 8 U.C.C. Rep. Serv. 2d (Callaghan) 370 (Minn. 1989).

3. Apparently this was a strict liability in tort claim. See 437 N.W.2d at 661, 8 U.C.C. Rep. Serv. 2d (Callaghan) at 374.

4. The smoker's wife was also a plaintiff. She alleged loss of consortium. Both plaintiffs also sought punitive damages.

5. 423 N.W.2d 691 (Minn. Ct. App. 1988).

6. The preemption was held not to be retroactive. Thus claims arising before the Federal Cigarette Labeling and Advertising Act was enacted could be asserted even on failure to warn theories. 437 N.W.2d at 66. This holding is consistent with other cases. See, e.g., *Kotler v. American Tobacco Co.*, 685 F. Supp. 15, 18, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1074, 1078 (D. Mass. 1988); *Cipollone v. Liggett Group Inc.*, 649 F. Supp. 664, 668 (D.N.J. 1986) (holding based on agreement of the parties).

extent that they were not based on such theories. In effect this left the smoker free to pursue claims based on defects in cigarettes;⁷ but, the court did not resolve the question of whether cigarettes can be defective because they are addictive and harmful to health.⁸ The court also held that a claim of misrepresentation arising from alleged false statements made in cigarette advertising was not preempted.⁹

THE INTERACTION OF TORT AND CONTRACT ECONOMIC LOSS

The economic loss doctrine continues to make headway. This doctrine bars suit in negligence or strict liability in tort by commercial buyers of defective products who suffer purely economic loss.

Two cases applied the economic loss doctrine to suits on contracts for professional services. In *Employer's Insurance v. Suwannee River Spa Lines, Inc.*,¹⁰ the United States Circuit Court for the Fifth Circuit applied the economic loss doctrine to admiralty claims arising out of contracts for the construction of ocean-going tugbarges. One of the barges sunk and the others could not be used until the cause of the sinking had been ascertained and preventative repairs had been made. The owner of the barges (Occidental), seeking compensation for the sinking, for repairs to the remaining barges, and for loss of use, sued a host of defendants responsible for the construction of the barges. Included among the defendants were the builder (Avondale) and the construction supervisors (Hvide). The owner claimed breach of contract or warranty and negligent performance of contract against each of these defendants. The negligence claims appear to have been pleaded to avoid the limitation of liability clause in each contract. The district court found both the builder and the supervisor to be liable for breach of contract and for negligent performance.¹¹ On appeal, both builder and supervisor alleged that they could not be held liable in negligence. The Fifth Circuit agreed and reversed. It held that the economic loss doctrine

7. *Accord* Kotler v. American Tobacco Co., 685 F. Supp. 15, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1074 (D. Mass. 1988); Cipollone v. Liggett Group Inc., 893 F.2d 541, 578 nn. 46, 51, 52 (3d Cir. 1990).

8. 437 N.W.2d at 661 n.8. The resolution of this question depends, in large measure, on whether or not a court adopts the position set forth in Restatement (Second) of Torts § 402A Comment i, (1965) (products like tobacco and whiskey even though addictive and harmful to health are not defective unless foreign substances added).

9. *But see* Cipollone, 893 F.2d 541 (intentional torts arising from advertising or promotion of cigarettes are preempted).

10. 866 F.2d 752, 8 U.C.C. Rep. Serv. 2d (Callaghan) 659 (5th Cir. 1989).

11. The district court found the builder's liability limitation clause to have effectively disclaimed tort liability; the court found the supervisor's liability limitation clause did not cover tort liability. *Id.* at 757, 8 U.C.C. Rep. Serv. 2d (Callaghan) at 664. The other defendants were dismissed from the suit.

applied to contracts for professional services and barred liability in negligence for the economic loss the plaintiff alleged in this case.¹²

In *Werner & Pfleider Corp. v. Gary Chemical Corp.*,¹³ the United States District Court for the District of New Jersey, applying New Jersey law, also held the economic loss doctrine applicable to a contract for services.¹⁴ In that case, the buyer (Gary Chemical) purchased a plastics processing machine from a distributor (WPC). When the machine failed to perform as expected, the buyer withheld a part of the purchase price. Upon suit by the distributor for the price, the buyer counterclaimed for economic loss based on, inter alia, negligent supervision, negligent design, and fraud.¹⁵ These claims were made to avoid a limitation of liability clause contained in the contract. The court held that under New Jersey law¹⁶ both the negligence and fraud claims were barred. Consequently, it granted summary judgment against the buyer on those claims.

In several cases, buyers of goods sued their sellers in tort for economic loss. Apparently each did so to avoid contractual remedy limitations or limited warranty clauses in their contracts. In each case the courts barred the tort claims. In *Sunnyslope Grading, Inc. v. Miller, Bradford & Risberg, Inc.*,¹⁷ the Wisconsin Supreme Court held that the commercial buyer of a backhoe cannot sue the remote manufacturer in negligence or strict liability in tort for purely economic loss where the buyer has accepted repairs under a manufacturer's warranty which specifically limited liability to the furnishing of replacement parts.

12. The Fifth Circuit also upheld the builder's liability limitation clause. *Id.* at 776–80, 8 U.C.C. Rep. Serv. 2d (Callaghan) at 675–80.

13. 697 F. Supp. 808, 8 U.C.C. Rep. Serv. 2d (Callaghan) 1064 (D.N.J. 1988).

14. Courts are split on whether the economic loss doctrine can apply to contracts for services. In favor of such application are the following cases: *Employers Ins. v. Suwannee River Spa Lines, Inc.*, 866 F.2d 752, 8 U.C.C. Rep. Serv. 2d (Callaghan) 659 (5th Cir. 1989) (applying federal admiralty law); *cf. East River S. S. Corp. v. Transamerica Delaval, Inc.*, 476 U.S. 858, 1 U.C.C. Rep. Serv. 2d (Callaghan) 609 (1986) (same); *Flinkote Co. v. Dravo Corp.*, 678 F.2d 942 (11th Cir. 1982) (applying Georgia law). Cases against such application include: *Consol. Edison Co. v. Westinghouse Elec. Corp.*, 567 F. Supp. 358, 36 U.C.C. Rep. Serv. 2d (Callaghan) 1496 (S.D.N.Y. 1983) (applying New York law); *Morse/Diesel, Inc. v. Trinity Indus. Inc.*, 664 F. Supp. 91 (S.D.N.Y. 1987), *rev'd on other grounds*, 859 F.2d 242 (2d Cir. 1988). Cases reserving judgment include: *Republic Steel Corp. v. Penn. Eng'g Corp.*, 785 F.2d 174, 183 n.13, 42 U.C.C. Rep. Serv. 2d (Callaghan) 1319, 1327–28 n.13 (7th Cir. 1986) (question not reached because contract found to be predominantly for sale of goods); *Adams Laboratories Inc. v. Jacobs Eng'g Co.*, 761 F.2d 1218, 1223–24 (7th Cir. 1985) (question not reached but court described Illinois law on point as “far from clear”).

15. The buyer also counterclaimed for breach of the distributor's warranty and instituted a third party action against the manufacturer of the machine as a third party beneficiary of the express warranty given by the manufacturer to the distributor. The court held that these claims survived summary judgment to the extent that they sought damages permissible under the limitation of liability clauses contained in each warranty.

16. *Spring Motors Distrib. v. Ford Motor Co.*, 98 N.J. 555, 489 A.2d 660, 40 U.C.C. Rep. Serv. 2d (Callaghan) 1184 (1985).

17. 148 Wis. 2d 910, 437 N.W.2d 213, 8 U.C.C. Rep. Serv. 2d (Callaghan) 652 (1989).

In *Rust-Pruf Corp. v. Ford Motor Co.*,¹⁸ the Michigan Court of Appeals rejected a similar claim. In that case, a rust-proofing company, asserting the rights of customers' vehicles it had rust-proofed, sued the manufacturer of the vehicles in tort. The rust-proofing company claimed defective design or manufacture of the vehicles, which it alleged had prevented it from adequately treating the vehicles. The suit was in tort because the manufacturer's sale warranty had expired before the problem surfaced. Based on Michigan law,¹⁹ the court affirmed the granting of summary judgment against the rust-proofer.²⁰

MISCELLANEOUS ISSUES

In *Childs v. Westinghouse Electric Corp.*,²¹ a Virginia circuit court determined that its legislature's enactment of U.C.C. section 2-318 precluded the judicial adoption of strict liability in tort. However, the weight of authority is decidedly against this view.²² Though the few courts adopting this view speak of legislative preclusion or preemption, they do not provide any direct evidence that either the drafters of the article 2 warranty provisions²³ or the particular state legislature intended such effect. The real issues here are not whether enactment of the U.C.C. in any particular jurisdiction has preempted strict liability in tort, for usually there is no indication that the legislature even considered the question. The real issues are whether contract-based defenses, such as warranty disclaimer, should bar suits for personal injury by remote purchasers and, if not, whether the more appropriate institution to adopt strict liability in tort is the judiciary or the legislature. Unfortunately, these issues are not likely to disappear and may even become more pressing now that states have begun to enact the new article 2A. That article codifies personal property leasing and includes warranty sections analogous to those in article 2.²⁴

Misuse of the goods is a defense to both tort and warranty claims against the manufacturer or seller. The effect of the defense can vary between tort and contract, and from jurisdiction to jurisdiction. Sometimes, the defense completely bars any recovery, as under a contributory negligence or assumption of

18. 172 Mich. App. 58, 431 N.W.2d 245, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1058 (1988).

19. *Great Am. Ins. Co. v. Paty's Inc.*, 154 Mich. App. 634, 397 N.W.2d 853, 2 U.C.C. Rep. Serv. 2d (Callaghan) 1526, *appeal denied*, 428 Mich. 874 (1987).

20. *See also* *Earl Brace & Sons v. Ciba Geigy Corp.*, 708 F. Supp. 708, 8 U.C.C. Rep. Serv. 2d (Callaghan) 690 (W.D. Pa. 1989) (apparently applying Pennsylvania law) (former purchaser of herbicide cannot sue remote manufacturer in tort for crop loss allegedly caused by failure of herbicide).

21. 7 U.C.C. Rep. Serv. 2d (Callaghan) 1080 (Va. Cir. Ct. 1988).

22. *See* Annotation, Pre-emption of Strict Liability in Tort by Provisions of U.C.C. article 2, 15 A.L.R. 4th 791 (1982 & 1989 Supp.).

23. For evidence that the drafters of article 2 did not intend preemption, see Wade, *Is Section 402 A of the Second Restatement of Torts Preempted by the U.C.C. and Therefore Unconstitutional?*, 42 Tenn. L. Rev. 123 (1974).

24. *See* U.C.C. §§ 2A-210 to 216. The drafters of article 2A intended not to "change the development of the relationship of" strict liability in tort to the provisions of the U.C.C.; *id.* § 2A-216, Official Comment.

risk system; sometimes it only reduces the amount of recovery, as under a comparative fault system.²⁵ *Coter v. Barber-Green Co.*,²⁶ decided by the Massachusetts Supreme Judicial Court, illustrates this point. In that case, a worker was severely injured while using a machine which he knew to be defective. The worker sued the manufacturer (Barber-Greene) and the seller of the machine (New England). The jury concluded that both defendants were liable in negligence. Since Massachusetts had adopted a comparative fault system for negligence, the jury apportioned the negligence. In so doing it found the worker's conduct in using a machine he knew to be defective to be contributory negligence and reduced the recovery accordingly. On the warranty claim, the jury found that recovery was completely barred by the worker's conduct. After several post-trial motions, the trial judge gave judgment for the worker. On appeal, the seller and the manufacturer contended that the jury's decision on the warranty count required a similar finding on the negligence count. The court rejected this argument, reasoning that each count was based upon a separate theory of liability. In warranty, plaintiff's misuse of a product could bar its recovery. In negligence, however, misuse did not necessarily bar recovery because Massachusetts had enacted a comparative negligence statute. The court concluded its decision by indicating that a comparative fault system perhaps should be adopted in warranty but left that decision to the legislature.

Several recent cases have permitted plaintiffs to assert traditional tort defenses or theories of recovery in breach of warranty actions. In *Castrignano v. E.R. Squibb & Sons, Inc.*,²⁷ the Rhode Island Supreme Court permitted a drug manufacturer to raise the "unavoidably unsafe" defense²⁸ in a personal injury warranty action. In that case, plaintiff sued to recover damages for personal injuries she allegedly suffered in utero when her mother took DES, a synthetic hormone, prescribed for plaintiff's mother to prevent the mother from spontaneously miscarrying the plaintiff. She sued the drug manufacturer in federal court on several theories, of which the trial judge submitted four to the jury; negligence, strict liability in tort, breach of implied warranty of merchantability, and breach of implied warranty of fitness for particular purpose. The jury found for the plaintiff on the strict liability and warranty of merchantability counts. The drug manufacturer moved for a new trial, contending that the jury charge had not included the "unavoidably unsafe" defense. Before ruling on the motion, the

25. See generally B. Clark & C. Smith, *The Law of Product Warranties* ¶ 12.03[8] (1984 and 1988 Cum. Supp.)

26. 403 Mass. 50, 525 N.E.2d 1305, 8 U.C.C. Rep. Serv. 2d (Callaghan) 375 (1988).

27. 546 A.2d 775, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1423 (R.I. 1988).

28. The "unavoidably unsafe" defense is described in Restatement (Second) of Torts § 402A Comment k (1965). Basically, the defense applies to products such as drugs or vaccines which are incapable of being made completely safe for their intended and ordinary use but which nevertheless serve very beneficial functions. For example, the vaccine used in the Pasteur treatment for rabies can itself cause serious injury. However, since the disease if left untreated leads to a horrible death, the unavoidably high risk involved in administering the vaccine is justified, if the product is properly prepared and accompanied by adequate warnings and instructions. Thus Comment k states that the seller of such vaccine is not liable under § 402A.

federal trial judge certified several questions to the Rhode Island Supreme Court. In response to those questions, the supreme court held: (i) the plaintiff could maintain her strict liability and warranty of merchantability claims on these facts; (ii) the "unavoidably unsafe" defense was available against both claims; and (iii) the application of the defense was a mixed question of law and fact on which the defendant bore the burden of proof.

In *Yates v. Norton Co.*,²⁹ the Massachusetts Supreme Judicial Court permitted a plaintiff to assert an implied warranty of merchantability claim on a failure to warn theory. In that case, a worker suffered fatal injury by inhaling noxious fumes while wearing a respirator. The administratrix of the worker's estate sued the manufacturer of the respirator for breach of warranty and negligence. The jury returned a verdict for the manufacturer on both counts. On appeal, the supreme judicial court reversed and remanded for a new trial on both counts. As to the warranty count, the court found the jury charge to have been deficient because it did not clearly tell the jury that failure to give adequate warnings constituted a breach of the implied warranty of merchantability.

ARTICLE TWO—SALES OF GOODS

CONTRACT FORMATION AND TERMS

Statute of Frauds

In view of the questionable need for a modern day statute of frauds,³⁰ it is not surprising to encounter philosophical differences of opinion, often among members of the same court. Consider the majority and dissenting opinions of the New York Court of Appeals in *Bazak International Corp. v. Mast Industries*,³¹ involving the merchant's exception to the statute of frauds under U.C.C. section 2-201(2).³² The confirmatory documents were, according to the buyer (Bazak), five printed purchase-order forms bearing the date of the alleged oral contract. Each contained the handwritten words, "As prisedented [sic] by Karen Fedorko," (a reference to the seller's agent who had dealt with buyer) and in small print,

29. 403 Mass. 70, 525 N.E.2d 1317, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1441 (1988).

30. The future of U.C.C. § 2-201 is one of the many areas being considered by the study committee formed by the Permanent Editorial Board to review article 2 and to consider whether it should be revised. This subject was also one of the topics of discussion at the meeting of the Subcommittee on General Provisions, Sales, Bulk Sales, and Documents of Title in Houston, Texas (Spring, 1989). Of those present, some thought the statute should be retained in its present form; some were of the opinion it should be retained, but revised; and some favored scrapping it altogether.

31. 7 U.C.C. Rep. Serv. 2d (Callaghan) 1380 (N.Y. Ct. App. 1989).

32. Other such cases decided during this survey period include *Hilord Chemical Corp. v. Ricoh Electronics, Inc.*, 875 F.2d 32, 8 U.C.C. Rep. Serv. 2d (Callaghan) 904 (2d Cir. 1989); *Polygram, S.A. v. 32-03 Enter. Inc.*, 697 F. Supp. 132, 8 U.C.C. Rep. Serv. 2d (Callaghan) 914 (E.D.N.Y. 1988); *Adams v. Petrade Int'l Inc.*, 754 S.W.2d 696, 7 U.C.C. Rep. Serv. 2d (Callaghan) 369 (Tex. Ct. App. 1988). See also Comment, *The Merchant's Exception to the Uniform Commercial Code's Statute of Frauds*, 32 Vill. L. Rev. 133 (1987).

the following: "This is only an offer and not a contract unless accepted in writing by the seller, and subject to prior sale."³³

The first task for the court of appeals was to formulate the applicable standard for determining whether a document qualifies as a confirmation.³⁴ It rejected the conclusion reached by several courts that explicit words of confirmation or an express reference to the prior agreement is necessary.³⁵ Rather, the court was of the opinion that the degree of explicitness required under subsections (1) and (2) of U.C.C. section 2-201 should be the same. That is, a document is a confirmation under subsection (2) if it is "sufficient against the sender" under subsection (1). Such would be the case if, assuming the other requirements are met, the document is "sufficient to indicate that a contract for sale has been made."³⁶ According to the court, this standard was met.³⁷ The date and specificity of the orders, along with the mention of a presentation by Karen Fedorko, suggested that a previous agreement had been reached. The "offer" language on the forms was thought to be irrelevant since it appeared that much of the content of each form, including this language, was intended to be effective only when buyer was acting in the capacity of a seller.

The dissent saw things quite differently. The point made was that, notwithstanding the standard adopted by the court, the orders were at best ambiguous. According to Justice Alexander, they did not lead one to conclude that an existing contract was more probable than not.³⁸

The court's decision that a document's sufficiency under U.C.C. section 2-201(2) should depend on its sufficiency under subsection (1) seems correct. The purpose of the merchant's exception was to take from the recipient of the confirmation the opportunity to speculate at the sender's expense. If the sender has lost the statute's protection, the recipient should also, unless the existence of a contract is timely disavowed. To require more from a confirmation than satisfaction of subsection (1) is to expose the sender to the risk of the same inequitable conduct that the drafters in subsection (2) sought to eliminate. However, the court's conclusion that the purchase orders met the test of subsection (1) was questionable. Because of the inherent indeterminacy of that test, much will depend upon the decisionmaker's attitude toward the statute. In

33. Furthermore, each purchase order was transmitted to seller through facilities located at the office of its own parent company in New York. 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1384.

34. The court excluded from consideration parol evidence on the theory that to permit evidence extrinsic to the documents would frustrate the purposes of the statute. *Id.* at 1383.

35. See *Trilco Terminal v. Prebuilt Corp.*, 167 N.J. Super. 449, 400 A.2d 1237, 26 U.C.C. Rep. Serv. 2d (Callaghan) 616, *aff'd without opinion*, 174 N.J. Super. 24, 415 A.2d 356 (1980); *Normanjil Sportswear Corp. v. TG & Y Stores Co.*, 644 F. Supp. 1 (S.D.N.Y. 1985).

36. U.C.C. § 2-201(1).

37. At the outset, the court was careful to remind the reader that its disposition of the statute of frauds issue was in no way intended to resolve the underlying dispute. The plaintiff must still prove that a contract existed. 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1383.

38. This, it was argued, is a finding that even the most liberal construction of U.C.C. § 2-201(1) requires. 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1392. Justice Alexander stated that, at best, the documents allowed "for equally probable inferences that the parties negotiated only in negotiations or entered a contract." *Id.* at 1394.

any event, the lesson of the case is clear: to guarantee the protection of the statute, the only safe course is to respond to all communications addressing the sale or purchase of goods.

A difference in attitude also divided the Second Circuit in *Trebor Sportwear Co. v. The Limited Stores, Inc.*³⁹ The issue was whether a cover letter and draft agreement, prepared as part of an effort to settle an ongoing dispute between the parties, were properly admissible to satisfy the statute of frauds. The trial court refused to consider either document on the grounds that they constituted an offer of settlement, and thus were inadmissible under rule 408 of the Federal Rules of Evidence. The Second Circuit affirmed, holding that exclusion of this evidence was not an abuse of discretion. Although the proffer was for a purpose other than to prove or disprove the validity of the underlying claim, the court was of the opinion that the policy of rule 408 militated against consideration of this material.⁴⁰

While it is certainly true, as the majority suggests, that satisfying the statute is the first step toward ultimate victory, it is doubtful whether admission of documents for this purpose will impact in any significant way on settlement negotiations. Although a statute of frauds defense matters when litigation ensues, it seems reasonable to assume that preservation of that defense is not a major pre-litigation concern.

In *DF Activities Corp. v. Brown*,⁴¹ the Seventh Circuit was faced with the "judicial admission" exception to the statute.⁴² The members of this court, too, could not agree on the result. The facts were simple. Plaintiff alleged an oral contract to buy a chair designed by Frank Lloyd Wright. Defendant moved to dismiss and filed in support, thereof, an affidavit that she never agreed to sell the chair to plaintiff. The trial court entered judgment for the defendant despite plaintiff's contention that it should be given the opportunity to depose defendant in order to elicit an involuntary admission.

The Seventh Circuit, on appeal, affirmed. Rejecting a statement by J. White and R. Summers that a statute of frauds' defense must always be determined at trial because the defendant might, in cross-examination, admit the making of the contract,⁴³ the court distinguished the case before it from one where there is only an unsupported assertion that no contract had been made. Where, as in

39. 7 U.C.C. Rep. Serv. 2d (Callaghan) 975 (2d Cir. 1989).

40. Conceding that evidence offered for "another purpose" is not necessarily barred by rule 408, the court was quick to adopt the cautionary warning that "care should be taken that an indiscriminate and mechanistic application of this 'exception' to rule 408 does not result in undermining the rule's public policy objective." *Id.* at 982 (citing 2 J. Weinstein & M. Berger, Weinstein's Evidence 408[05], 408-31 (1988)). Since overcoming the statute of frauds is the first step toward establishing liability, the court felt constrained to decide the case the way it did. The dissent, on the other hand, saw the nexus between being able to satisfy the statute and being able to prove the existence of an oral contract as too attenuated to implicate the policy considerations underlying rule 408 if evidence is offered solely to establish the former. *Id.* at 983 (Oakes, C.J., dissenting).

41. 851 F.2d 1396, 1397 (7th Cir. 1988). 7 U.C.C. Rep. Serv. 2d (Callaghan) 1396 (7th Cir. 1988).

42. See U.C.C. § 1-301(3)(b).

43. 851 F.2d 1396, 1397 (7th Cir. 1988). 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1398.

this case, the denial is under oath, the remote possibility of a subsequent admission does not justify further litigation.⁴⁴ The dissent thought otherwise. In the opinion of Judge Flaum, the decision whether to allow further discovery should lie within the trial court's discretion. In this case, Judge Flaum believed the district court abused that discretion.⁴⁵

Perhaps a compromise position is possible. Why not allow discovery limited to the statute of frauds' issue? If no admission is obtained, the case could then be dismissed.

Parol Evidence Rule

Everybody knows that section 2-202 (the U.C.C. version of the parol evidence rule) has discarded the requirement that a final⁴⁶ writing's terms be ambiguous before extrinsic evidence can be introduced to explain the meaning of the terms. Well not quite. The Official Comment to that section throws out the ambiguity prerequisite only for "the type of evidence specified in paragraph (a)"; that is, course of dealing, usage of trade, and course of performance.⁴⁷ Each of these terms is defined in the Code.⁴⁸ As for extrinsic evidence, such as statements, or other conduct of parties during their negotiations which do not fit into one of these three categories, courts still require that the writing be ambiguous before such evidence is admissible.⁴⁹

This point is illustrated in *Apple Valley Red-E-Mix, Inc. v. Mills-Winfield Engineering Sales, Inc.*,⁵⁰ decided by the Minnesota Court of Appeals. In that case, the plaintiff leased a cement unloading machine. The contract contained

44. The diverse views on this subject are discussed in *Triangle Mktg., Inc. v. Action Indus., Inc.*, 630 F. Supp. 1578, 1 U.C.C. Rep. Serv. 2d (Callaghan) 36 (N.D. Ill. 1986).

45. Missing from defendant's affidavit was a blanket denial that an agreement had been reached. Defendant stated only that she did not accept plaintiff's offer to purchase the chair and did not recall having a particular conversation with plaintiff's representative.

46. "Final" here means that the writing is integrated. In Code terms it is "intended by the parties as a final expression of their agreement." U.C.C. § 2-202.

47. Uniform Commercial Code § 2-202 Official Comment 1(c).

48. For definitions of "course of dealing" and "usage of trade" see U.C.C. § 1-205; for "course of performance" see U.C.C. § 2-208.

49. See, e.g., *Shephard v. Top Hat Land & Cattle Co.*, 560 P.2d 730, 21 U.C.C. Rep. Serv. (Callaghan) 760 (Wyo. 1977); *Central Jersey Dodge Truck Center, Inc. v. Sightseer Corp.*, 608 F.2d 1106, 27 U.C.C. Rep. Serv. (Callaghan) 1256 (6th Cir. 1979); *Durbano Metals Inc. v. A&K R.R. Materials, Inc.*, 574 P.2d 1159, 23 U.C.C. Rep. Serv. (Callaghan) 299 (Utah 1978); *Rainer Nat'l Bank v. Inland Mach. Co.*, 29 Wash. App. 725, 631 P.2d 389, 32 U.C.C. Rep. Serv. (Callaghan) 287 (1981); *Paragon Resources Inc. v. Nat'l Fuel Gas Distrib. Corp.*, 723 F.2d 419, 37 U.C.C. Rep. Serv. (Callaghan) 1482 (5th Cir. 1984); *Harper v. Calvert*, 687 S.W.2d 227, 39 U.C.C. Rep. Serv. (Callaghan) 1655 (Mo. Ct. App. 1984); *Island Creek Coal Co. v. Lake Shore, Inc.*, 636 F. Supp. 285, 2 U.C.C. Rep. Serv. 2d (Callaghan) 59 (W.D. Va. 1986) *rev'd*, 884 F.2d 1388 (4th Cir. 1989); *Cibro Petroleum Prods, v. Sohio Alaska Petroleum Co.*, 602 F. Supp. 1520, 40 U.C.C. Rep. Serv. (Callaghan) 1220 (N.D.N.Y. 1985).

50. 436 N.W.2d 121, 8 U.C.C. Rep. Serv. 2d (Callaghan) 21 (Minn. Ct. App. 1989). For a similar ruling, see *Warnaco Inc. v. Farkas*, 872 F.2d 539, 8 U.C.C. Rep. Serv. 2d (Callaghan) 427 (2d Cir. 1989) (evidence of proposal made during negotiations inadmissible to explain language of written guarantee where language was unambiguous).

an express warranty of merchantability, effectively disclaiming all other warranties, and included a merger clause stating that the written lease contained the entire contract of the parties. The lessee sued for breach of warranty, claiming that the machine failed to meet an unloading rate stated by the lessor but not included in the lease. The trial court found the machine's description in the lease, "Docksider II-V," to be ambiguous, and so admitted extrinsic evidence of the seller's unloading rate statement. It then found for the buyer. On appeal, the Minnesota Court of Appeals reversed. It concluded that the description was not ambiguous and that the lease was not so incomplete on warranties as to permit evidence of the extrinsic statement.⁵¹

Buyers who fail to read invoices packaged with goods sent to them may be bound by the terms of the invoice. A court could hold the invoice to be a final expression of the terms contained in the invoice with the consequence that the buyer cannot introduce extrinsic evidence, written or oral, to contradict or explain its terms.⁵² This is precisely what happened to the buyer in *Polygram, S.A. v. 32-03 Enterprises, Inc.*, decided by the United States District Court for the Eastern District of New York.⁵³ In that case, the buyer had been a distributor of seller's phonograph records, tapes, and compact discs for some time. It received several shipments of these goods, each of which was accompanied by an invoice. Each invoice contained a clause requiring any claim concerning the goods (including claims of defects) to be made within three calendar months after delivery. The buyer did not object to any of the terms in the invoices and eventually issued checks to pay for each shipment. When these checks were dishonored, the seller sued for the contract price of each shipment. The buyer defended asserting the statute of frauds and defects in the goods. The seller moved for summary judgment which the trial court granted. The court disposed of the statute of frauds defense on the grounds that the buyer's failure to give written notice of objection to the invoices foreclosed it from asserting that

51. The court applied common law and cited § 2-202 in passing, apparently because this was a lease rather than a sale. Minnesota has since enacted article 2A which governs leases of goods. Minn. Stat. Ann. §§ 336.2A-101-531 (West 1990). However this would not change the result here, because the article 2A parol evidence rule (§ 2A-202) is identical to the article 2 parol evidence rule.

52. Compare the effect of an invoice under subsection 2-201(2) (see 2 R. Anderson, Anderson on the U.C.C. §§ 2-201:133-134 (3d ed. (1982)) and under § 2-207; e.g., *Interlake, Inc. v. Kansas Power & Light Co.*, 7 Kan. App. 2d 16, 637 P.2d 464, 33 U.C.C. Rep. Serv. (Callaghan) 171 (1981) *rev'd*, 231 Kan. 251, 644 P.2d 385 (1982); *Transamerica Oil Corp. v. Lynes, Inc.*, 723 F.2d 758, 37 U.C.C. Rep. Serv. (Callaghan) 1076 (10th Cir. 1983); *Therma-Coustics Mfg., Inc. v. Borden, Inc.*, 167 Cal. App. 3d 282, 213 Cal. Rep. 611, 40 U.C.C. Rep. Serv. (Callaghan) 1640 (1985); *Rangen, Inc. v. Valley Trout Farms, Inc.*, 104 Idaho 284, 658 P.2d 955, 35 U.C.C. Rep. Serv. (Callaghan) 52, 35 U.C.C. Rep. Serv. (Callaghan) 1129 (1983); *Offen, Inc. v. Rocky Mt. Constructors Inc.*, 765 P.2d 600, 7 U.C.C. Rep. Serv. 2d (Callaghan) 47 (Colo. Ct. App. 1988). But see *Trust Co. Bank v. Barrett Distrib., Inc.*, 459 F. Supp. 959, 25 U.C.C. Rep. Serv. (Callaghan) 986 (S.D. Ind. 1978) (contract formed when seller shipped goods); *In re Isis Foods, Inc.*, 38 Bankr. 48, 38 U.C.C. Rep. Serv. (Callaghan) 1134 (W.D. Mo. 1983) (same).

53. 697 F. Supp. 132; 8 U.C.C. Rep. Serv. 2d (Callaghan) 914 (E.D.N.Y. 1988).

defense under section 2-201.⁵⁴ The court disposed of the defects in the goods defense on the grounds that the buyer had not timely notified the seller of breach. The court also declined to consider a letter sent by seller to buyer prior to the shipments in question, which the buyer characterized as permitting an open-ended return policy. It did so on the grounds that the invoice was, under section 2-202, a final expression of the parties' agreement on the return policy which could not be contradicted by the letter.⁵⁵ In the court's view, the buyer assented to the terms of the invoice by accepting the goods which accompanied the invoice.⁵⁶ This case is consistent with others that have held invoices to be final expressions for purposes of section 2-202.⁵⁷

Battle of the Forms

Often in battle of the forms cases, one side will sign the other side's form. Usually the signing party is held to be bound to the terms of the form he signed regardless of whether he read the form.⁵⁸ In one case decided this year, *Weyher/Livsey Constructors, Inc. v. International Chemical Co.*,⁵⁹ the United States Court of Appeals for the Eleventh Circuit indicated that this is not always so. In that case, the buyer (Weyher) purchased coal for use in testing boilers it was manufacturing for the army. It sent a purchase order for the coal to the seller, who signed it without objection. The purchase order set forth coal size specifications. On the back of the form was a clause in which the seller was said to warrant the goods sold for one year. The clauses on the back were very difficult to read and, in the words of trial court, "border on being illegible."⁶⁰ Several months after the last delivery of coal, the buyer notified the seller that the coal did not conform to the size specifications. The buyer resold the coal, covered, and sued for damages. After the buyer had finished presenting its evidence at trial, the trial court granted the seller's motion for an involuntary dismissal. It held that the warranty clause was unenforceable, because it was not conspicuous under the U.C.C. The basis for the dismissal apparently was a failure of the

54. The court applied subsection 2-201(2) (written confirmation under some circumstance can disable recipient from asserting statute of frauds if he does not object to it in writing within 10 days of receipt).

55. In passing, the court noted that, even if the letter had been considered, the result would be no different, since the letter did not support the buyer's characterization of it.

56. The court also held that the invoice term on giving notice of returns was not unconscionable and that the time period allowed by that term for giving notice was not manifestly unreasonable under U.C.C. § 1-204.

57. See, e.g., *Battista v. Radesi*, 112 A.D.2d 42, 491 N.Y.S.2d 81, 41 U.C.C. Rep. Serv. (Callaghan) 748 (App. Div. 1985); *General Motors Acceptance Corp. v. Fairway Dodge Sales, Inc.*, 80 A.D.2d 740, 437 N.Y.S.2d 171 (App. Div. 1981); *Matthew Bender & Co. v. Jaiswal*, 93 A.D.2d 969, 463 N.Y.S.2d 78, 35 U.C.C. Rep. Serv. (Callaghan) 1414 (App. Div. 1983); *Morrison v. Devore Trucking, Inc.*, 68 Ohio App. 2d 140, 428 N.E.2d 438, 32 U.C.C. Rep. Serv. (Callaghan) 779 (1980); *Liberty Enters., Inc. v. Moore Transp. Co.*, 679 S.W.2d 779, 40 U.C.C. Rep. Serv. (Callaghan) 773 (Tex. App. 1984), *aff'd in part*, 690 S.W.2d 570 (1985).

58. See generally J. Calamari & J. Perillo, *The Law of Contracts* 410 (3d ed. 1987).

59. 864 F.2d 130, 8 U.C.C. Rep. Serv. 2d (Callaghan) 646 (11th Cir. 1989).

60. *Id.* at 132, 8 U.C.C. Rep. Serv. 2d (Callaghan) at 648.

buyer to give timely notice of breach, and the buyer seems to have argued that the warranty clause gave it at least one year to notify of breach. On appeal, the Eleventh Circuit reversed and remanded. It held that the trial court applied the wrong standard in determining whether the warranty clause was part of the contract. The U.C.C. requires that only certain clauses, such as warranty disclaimers, be conspicuous; there is no U.C.C. requirement for express warranties. The court stated that the trial court should apply general contract principles to determine whether the warranty was enforceable. Under general contract principles, courts traditionally do not enforce clauses against signers if the clauses are not legible or if they have not sufficiently been called to the attention of the signer.⁶¹ Thus on remand, the seller may well be held not to be bound to the warranty clause even though he signed the form containing the clause.

Warranties

Warranty Of Title

Does the warranty of title run to remote purchasers or only to immediate purchasers? The courts are split.⁶² The text and Official Comments to U.C.C. section 2-312 are silent on the question; nor do the drafters seem to have had the warranty of title in mind when they devised U.C.C. section 2-318 which permits certain classes of persons to sue as third party beneficiaries of express or implied warranties.⁶³

According to Williston, under pre-Code law the warranty of title ran only to the immediate buyer.⁶⁴ Even if the immediate buyer assigned its rights under the warranty to the next purchaser, that purchaser could recover only for the injury to the immediate buyer and not for its own injury, since it was asserting the rights of the immediate buyer, not its own rights.⁶⁵ Yet even though the warranty did not run to the remote purchaser, the seller could not escape liability for injury to that purchaser. The remote purchaser could recover from its seller, the immediate buyer, who in turn could recover from its seller compensation for direct injury to it and also for damages which the immediate buyer had to pay to the remote purchaser. Thus, the original seller ultimately would be liable for the injury caused to each successive purchaser. This result

61. Calamari & Perillo, *supra* note 58, at 411-14.

62. See Frisch & Wladis, *General Provisions, Sales Bulk, Transfers, and Documents of Title*, 44 Bus. Law. 1445, 1455 n.46 (1989). See also *Crook Motor Co. v. Goolsby*, 703 F. Supp. 511, 8 U.C.C. Rep. Serv. 2d (Callaghan) 363 (N.D. Miss. 1988) (holding that warranty of title runs only to immediate purchaser).

63. The drafting history of U.C.C. § 2-318 indicates that the drafters were concerned with the warranties of quality, not the title warranty. See, e.g., A.L.I., *Uniform Revised Sales Act, Comment on Section 43* (Proposed Final Draft No. 1 Apr. 27, 1944); reprinted in 2 Uniform Commercial Code: Drafts 163-67 (1984).

64. 1 S. Williston, *The Law Governing Sales of Goods at Common Law and Under the Uniform Sales Act* § 244, at 645, 648 (1948).

65. *Id.* at 647.

required a multiplicity of actions. This cumbersome procedure, together with the demise of the privity requirement for warranties of quality, may well account for those cases which hold that the warranty of title under U.C.C. section 2-312 runs to the remote purchaser.

In *Brokke v. Williams*,⁶⁶ the Montana Supreme Court held that the warranty of title is not disclaimed where the goods were sold “as is.” In that case, the buyer purchased a camera from a pawnbroker, who had posted large fluorescent signs on his premises stating that he sold merchandise “as is.”⁶⁷ He wrote similar legends on his sales slips. Later, it was determined that the camera had been stolen and the buyer surrendered it to the police. The buyer then sued the seller for breach of the warranty of title. The court gave judgment for the buyer. On appeal, the Montana Supreme Court affirmed. It held that the posting of “as is” signs was not sufficient to disclaim the warranty of title under U.C.C. subsection 2-312(2). It also emphasized that the warranty of title could not be disclaimed under U.C.C. section 2-316 (which permits “as is” disclaimers to be effective).⁶⁸ This decision is consistent with other cases requiring that, to be an effective disclaimer under subsection 2-312(2), language or circumstances must specifically call to the buyer’s attention the fact that the seller is not claiming that he has title or that the seller is selling only such right or title as he is able to sell. Thus, typical quitclaim language in bills of sale, which recites that the seller is transferring his “right, title and interest,” has been held to be ineffective to disclaim the warranty of title.⁶⁹

Implied Warranties

In *Gall v. Allegheny County Health Dept.*,⁷⁰ the Pennsylvania Supreme Court held the implied warranty of merchantability attached to the sale of water by a municipality through its municipal water system. It also held that the implied warranty of fitness for a particular purpose did not attach to such a sale. In that case, plaintiffs became ill with giardiasis⁷¹ after drinking water furnished by the municipality. They sued the municipality and the municipal water authority for breach of both implied warranties. The trial court dismissed the complaint. On appeal, the commonwealth court affirmed on the ground that the complaint failed to state a claim upon which relief might be granted. On

66. 766 P.2d 1311, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1404 (Mont. 1989).

67. There was a factual dispute as to whether the signs were in place when the buyer entered the pawn shop. *Id.* at 1312, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1405. The court said this dispute was irrelevant and treated the case as if the signs had been in place.

68. See Uniform Commercial Code § 2-312 Official Comment 6 (title warranty not subject to U.C.C. § 2-316(3)).

69. See Clark & Smith, *supra* note 25 at ¶ 3.03 (1984 & 1988 Cum. Supp.).

70. 521 Pa. 68, 555 A.2d 786, 8 U.C.C. Rep. Serv. 2d (Callaghan) 379 (1989). See also *Miller v. McKeesport Mun. Water Auth.*, 521 Pa. 77, 555 A.2d 790 (1987) (municipality and its water authority could be held liable in negligence and breach of contract for illness and economic loss caused by same tainted water involved in *Gall* case).

71. Giardiasis is a disease caused by parasitic protozoa that attack the intestines. See IV Encyclopaedia Britannica-Micropaedia 528 (1974) (entry under “*Giardia lamblia*”).

further appeal, the supreme court affirmed in part and reversed in part. It concluded that the sale of water by a municipality was a sale of goods within U.C.C. article 2. The court then concluded that the implied warranty of merchantability⁷² was attached to the sale.⁷³ Lastly, the court ruled that the implied warranty of fitness for a particular purpose⁷⁴ did not attach to a sale of water for drinking or household purposes.⁷⁵

In *Koperwas v. Publix Supermarkets, Inc.*,⁷⁶ a Florida court of appeals, applying the "reasonable expectation" test, held that the presence of a clam shell in a can of clam chowder, as a matter of law, did not constitute lack of reasonable care in the manufacture of the chowder. In that case, the plaintiff injured her tooth when she bit down on the shell while eating the chowder. She sued both the supermarket from which she purchased the chowder and the manufacturer for breach of implied warranty. At the close of plaintiff's case, the trial court directed a verdict for the defendants. On appeal, the court affirmed, stating that a consumer could reasonably anticipate and guard against a piece of clam shell in a bowl of clam chowder.⁷⁷

Warranty Disclaimers

Conspicuousness is one of the requirements under U.C.C. section 2-316(2) for disclaiming or modifying the implied warranties of merchantability or of fitness for a particular purpose. Whether a clause is conspicuous is a question of law.⁷⁸ The definition of "conspicuous" provides that, "[a] term or clause is conspicuous when it is so written that a reasonable person against whom it is to operate ought to have noticed it."⁷⁹ The definition continues by declaring that a printed heading in capitals, or language in the body of a form that is printed in larger or other contrasting type or color, is conspicuous.⁸⁰ Suppose that the disclaimer language in a form is printed in contrasting type or color but is located on the back of the form so that a reasonable person might not have noticed it. Is it conspicuous? Courts are divided on the question. Some courts

72. U.C.C. § 2-314. The court did not discuss whether either of the defendants was a merchant, possibly because the matter was not made an issue by the parties.

73. *Accord* 35 Op. Comptroller, No. 79-880, 28 U.C.C. Rep. Serv. (Callaghan) 330 (N.Y. Compt. 1980); *contra* *Coast Laundry Inc. v. Lincoln City*, 9 Or. App. 521, 497 P.2d 1224, 10 U.C.C. Rep. Serv. (Callaghan) 1379 (1972) (no implied warranties on theory that sale of water by municipality is not a sale of goods).

74. U.C.C. § 2-315. *Contra* 35 Op. Comptroller, No. 79-880, 28 U.C.C. Rep. 330 (N.Y. Compt. 1980).

75. The court also ruled that plaintiffs had stated a claim under Pennsylvania's Governmental Immunities Act, 42 Pa. Cons. Stat. Ann. § 8542(b)(5) (Purdon 1982).

76. 534 So. 2d 872, 7 U.C.C. Rep. Serv. 2d (Callaghan) 733 (Fla. Dist. Ct. App. 1988).

77. *Accord* *Webster v. Blue Ship Tea Room, Inc.*, 347 Mass. 421, 198 N.E.2d 309, 2 U.C.C. Rep. Serv. (Callaghan) 161 (1964) (presence of fish bone in fish chowder does not constitute breach of implied warranties). *But see* *O'Brien v. Ferguson Catering*, 6 U.C.C. Rep. Serv. 2d (Callaghan) 1434 (Mass. Dist. Ct. 1988) (presence of bone in chicken pie constitutes breach of warranty).

78. U.C.C. § 1-201(10).

79. *Id.*

80. *Id.*

find location on the back of the form to be a factor in determining that the disclaimer is not conspicuous.⁸¹ Other courts find the clause not to be conspicuous if there is not an adequate reference on the front of the form to the terms appearing on the back.⁸² The application of these principles is illustrated by *Sierra Diesel Injection Service, Inc. v. Burroughs Corp.*,⁸³ decided by the United States Court of Appeals for the Ninth Circuit. In that case, the buyer purchased a computer and software for bookkeeping and invoicing. The purchased items did not perform as promised so the buyer purchased another computer from the same seller, which also did not perform as promised. A computer consultant retained by the buyer informed it that the computer was incapable of performing as promised. Consequently, the buyer purchased a replacement computer from another seller and sued the first seller. The trial court found for the buyer, concluding that the seller had breached its contract and the implied warranty of merchantability. On appeal, the Ninth Circuit affirmed and held that the seller's warranty disclaimers, which were printed in bold contrasting type, but on the reverse side of the form signed by the buyer, were not conspicuous. In so doing, the court relied upon the buyer's relative unsophistication in the areas of computers and contracts.⁸⁴

Third Party Beneficiaries Of Warranties

Almost 25 years ago Prosser proclaimed the fall of the citadel of privity⁸⁵ in warranty actions. Yet the passage of time has demonstrated that pockets of resistance still remain. This is so because lack of privity is still a defense in certain circumstances in many jurisdictions. The article 2 section intended to deal with privity (section 2-318) does not, in any of its recommended versions, abolish privity entirely. Further, some courts have declined to extend the partial abolition embodied in their state's version of section 2-318 to situations beyond that version.

Thus in *Gowen v. Cady*,⁸⁶ the Georgia Court of Appeals ruled that lack of privity was a complete defense to a personal injury warranty action where the plaintiff was not within the class of persons for whom Georgia's U.C.C. section 2-318 abolished privity. Georgia's section 2-318 abolishes privity for family members and guests in the buyer's home who might reasonably be expected to use and be injured by the product.⁸⁷ Mr. and Mrs. Cady sued the manufacturer

81. Annot., 73 A.L.R. 3d 248 § 12[b] at 293-95 (1976 and 1989 Supp.). Often the buyer's lack of sophistication in legal matters is a factor as well. *Id.* § 16[a] at 299-300 (1976 & 1989 Supp.).

82. *Id.* at 294-95 (1976 & 1989 Supp.). See also Clark & Smith, *supra* note 25, at ¶ 8.03[2], text at nn.50, 51 (1984 & 1988 Cum. Supp.).

83. 874 F.2d 653, 8 U.C.C. Rep. Serv. 2d (Callaghan) 617 (9th Cir. 1989).

84. The court also affirmed the breach of contract count. It concluded that the promise breached, which was contained in a letter sent by the seller to the buyer, had not been superceded by the buyer's later signing of the seller's form even though that form contained a merger clause.

85. Prosser, *The Fall of the Citadel*, 50 Minn. L. Rev. 791 (1966).

86. 189 Ga. App. 473, 376 S.E.2d 390, 8 U.C.C. Rep. Serv. 2d (Callaghan) 384 (1989), *cert. denied*, 189 Ga. App. 912 (1989).

87. Ga. Code Ann. § 11-2-318 (1982).

of a medical device used by Mrs. Cady's doctor in a voluntary sterilization procedure performed upon Mrs. Cady. After the procedure, Mrs. Cady became pregnant and this suit ensued. The trial court granted summary judgment for the manufacturer on the warranty claim. On appeal, the court affirmed this decision upon the ground that neither plaintiff had been in privity with the manufacturer. The Georgia Supreme Court denied certiorari.⁸⁸

However, it is possible to evade privity limitations through the use of either an assignment or agency principles. The Illinois Supreme Court decision, *Collins Co. v. Carboline Co.*,⁸⁹ illustrates how an assignment of rights can be used to avoid a lack of privity. In that case, the court held that a plaintiff who was not within the class of those for whom the privity requirement had been abolished could satisfy the privity requirement by taking an assignment of rights from one who was in privity. There, the owners of a warehouse (Chicago Title and Wachovia) had a contractor install a new roofing system manufactured by Carboline. The manufacturer issued a written 10-year warranty to the owners. Some three years later, Collins purchased the warehouse. Two years after this purchase, the roof began to leak which limited Collins' use of the warehouse and required repair of the roof. Collins took an assignment of the original owners' warranty rights against the manufacturer. Collins then sued the manufacturer for economic loss in federal district court.⁹⁰ That court gave judgment on the pleadings for the manufacturer. It ruled that Collins lacked privity and that the assignment of warranty did not create privity. On appeal, the Seventh Circuit found Illinois law to be uncertain on whether the assignment created privity.⁹¹ It certified this issue to the Illinois Supreme Court, which decided that the assignment would place Collins in privity with the manufacturer.⁹² The supreme court left for the trial court to decide under U.C.C. subsection 2-210(2) whether the assignment was effective.⁹³ Subsequently, based upon the Illinois Supreme Court's decision, the Seventh Circuit reversed the district court's judgment on the pleadings and remanded the case for further proceedings.⁹⁴

Agency principles also can be used to evade privity requirements. If there is just one party between the plaintiff and the manufacturer in the distribution chain, and if it can be shown that the intervening party is the agent of the

88. See *supra* note 86.

89. 125 Ill. 2d 498, 532 N.E.2d 834, 7 U.C.C. Rep. Serv. 2d (Callaghan) 616 (1988).

90. Collins also sued the contractor who had installed the roof, as well as the architect whom Collins had hired to inspect the warehouse prior to purchasing it and who had opined that the roofing "looked in good shape." The claims against these parties were not in issue in the present case.

91. *Collins Co. v. Carboline Co.*, 837 F.2d 299, 5 U.C.C. Rep. Serv. 2d (Callaghan) 273 (7th Cir. 1988).

92. The opinion contains a useful collection and discussion of state and federal cases addressing the issue of assignability of warranty rights, 125 Ill. 2d at 513-14, 532 N.E.2d at 840-41, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 625-26.

93. U.C.C. § 2-210(2) permits assignment of all rights of seller or buyer unless either the parties agreed otherwise or the assignment would have a material adverse effect upon the nonassigning party.

94. 864 F.2d 560, 7 U.C.C. Rep. Serv. 2d (Callaghan) 629 (7th Cir. 1989).

plaintiff or of the manufacturer, then the plaintiff is in privity with the manufacturer.⁹⁵

PERFORMANCE

Title, Creditors, and Good Faith Purchasers

Creditors continue to ignore available protection against third party claims. In *In re BRI Corp.*,⁹⁶ a creditor-consignor asserted priority to the proceeds from the clothing it supplied to the debtor-consignee who subsequently filed for bankruptcy. Under U.C.C. section 2-326(3), a consignor must prove one of three things in order to protect its interest from the claims of consignee's creditors: (i) that he complied with a "sign law";⁹⁷ (ii) that the debtor was "generally known by his creditors to be substantially engaged in selling the goods of others"; or (iii) that he made an article 9 filing.⁹⁸ Since there was no sign law in Pennsylvania and the consignor had not made an article 9 filing, consignor had to prove that subsection 2-326(3)(b) was satisfied in order to protect his interests in the case.

Courts tend to strictly interpret the language of U.C.C. section 2-326(3)(b). The factual test of proving that the buyer is "generally known by the buyer's creditors to be substantially engaged in selling the goods of others" is almost never met.⁹⁹ *BRI Corp.* reinforces this trend. Despite proof that 250 of 600 suppliers of BRI Corp. supplied goods on a consignment basis, the court said that this was not "most" of the suppliers. Moreover, the debtor had many nonsupplier creditors, and there was no evidence that any of these knew that the debtor generally sold goods on a consignment basis. Given the scant evidence on which to base a decision that the buyer was "generally known" to sell on consignment, the court's conclusion seems correct.

Although goods have never attained the status of full negotiability, the predominance of ostensible ownership concerns has been the impetus behind a gradual move toward a form of quasi-negotiability. Whether this halfway status is presently deserved is unclear, its hold on the judicial psyche is not. A perfect example is *MBank-Waco, N.A. v. L. & J., Inc.*¹⁰⁰ The dispute was over the respective rights of MBank and the Mamot family to the proceeds from the sale

95. See, e.g., *Costa v. Volkswagen of Am.*, 150 Vt. 213, 214 n.1, 551 A.2d 1196, 1197-98 n.1, 8 U.C.C. Rep. Serv. 2d (Callaghan) 389, 391 n.1 (1988) (buyer in privity with manufacturer where intervening dealer is agent of manufacturer); *Irwin v. Lowe's, Inc.*, 165 Ga. App. 828, 302 S.E.2d 734, 36 U.C.C. Rep. Serv. (Callaghan) 450 (1983) (buyer in privity with manufacturer if intervening purchaser from manufacturer was acting as agent of buyer).

96. 88 Bankr. 71, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1441 (E.D. Pa. 1988).

97. Only North Carolina and Mississippi have such laws. See N.C. Gen. Stat. § 66-72 (1975); Miss. Code Ann. § 15-3-7 (1972 & 1989 Cum. Supp.).

98. U.C.C. § 9-408 permits a creditor to make an article 9 filing without prejudicing its right to assert that the transaction was a true consignment outside the transactional scope of article 9.

99. See, e.g., *Logan Paving Co. v. Massey-Ferguson Credit Corp.*, 172 Ga. App. 368, 323 S.E.2d 259, 40 U.C.C. Rep. Serv. (Callaghan) 116 (1984); *In re Hoover Co.*, 16 Bankr. 435, 33 U.C.C. Rep. Serv. (Callaghan) 906 (M.D. Pa. 1982).

100. 754 S.W.2d 245, 6 U.C.C. Rep. Serv. 2d (Callaghan) 1476 (Tex. Ct. App. 1988).

of cattle ostensibly owned by Arnold Young, the "thief." Young and the Mamots had "a-man's-word-is-his-bond" type of relationship.¹⁰¹ The Mamots supplied him with money to purchase cattle which he would fatten and sell with the understanding that the Mamots would be paid back from the proceeds. The cattle always bore Young's registered brand.¹⁰² Unfortunately, as Young's financial condition began to deteriorate so did his honesty. During the 1980-1981 cattle year, the Mamots were asked to pay for cattle that Young never intended to buy. Some of this money was returned to the Mamots to cover the previous year's obligations and the rest was used to finance all phases of Young's cattle business. Also during this period, Young gave MBank a security interest in "all cattle now owned or hereafter acquired." When his entire herd was later sold by MBank, the Mamots claimed equitable ownership of the proceeds under a constructive trust.¹⁰³ The trial court, emulating the wisdom of Solomon, divided the proceeds equally between MBank and the Mamots.

The Texas Court of Appeals reversed. Without deciding whether the circumstances justified the imposition of a constructive trust,¹⁰⁴ the court determined that MBank was a good faith purchaser for value and as such would prevail over an existing equitable title or interest.¹⁰⁵ Moreover, we are told that MBank would also prevail under article 9. In the view of the court, the beneficiary of a constructive trust is an unperfected lien creditor whose interest is subordinate to that of a perfected secured party.¹⁰⁶ With respect to the position of the Mamots that Young (a thief) could pass no interest in the cattle to MBank, the court

101. This characterization is the court's. *Id.* at 247, 6 U.C.C. Rep. Serv. 2d (Callaghan) at 1479. Surprisingly (considering that approximately \$1.8 million was involved), no aspect of their relationship was reduced to writing.

102. The Mamots knew this and admitted that their cattle was indistinguishable from the rest of Young's cattle.

103. The Mamots argued that once they were able to trace their stolen funds to the purchase of some cattle, the burden shifted to MBank to identify the cattle purchased with and without their funds. Failing this, the Mamots laid claim to the entire herd. One could argue, however, that U.C.C. § 9-315 places the burden of identification squarely on the shoulders of the Mamots. *See generally* Frisch, *U.C.C. Section 9-315: A Historical and Modern Perspective*, 70 Minn. L. Rev. 1 (1985).

104. For a discussion of the grounds for imposing a constructive trust, see generally G. Bogert, *The Law of Trust and Trustees* 471 et seq. (Rev. 2d ed. 1978); 5 A. Scott, *Trusts* 461 et seq. (4th ed. 1989).

105. The court was careful to point out that MBank, as a preexisting secured creditor, did not qualify for protection under U.C.C. § 2-403(2) as a "buyer in ordinary course of business." MBank was, however, a good-faith purchaser. *See* U.C.C. § 1-201(32) ("['p]urchase' includes taking by . . . mortgage, pledge, lien."). As such, it "acquire[d] all title which [its] transferor had or had power to transfer." U.C.C. § 2-403(1). In this case, the court relied on pre-Code rules to reach the conclusion that Young had the "power" to transfer an interest, free of the alleged constructive trust.

106. The court cited U.C.C. § 9-201. *See also* U.C.C. § 9-301(1)(b) ("[A]n unperfected security interest is subordinate to the rights of . . . a person who becomes a lien creditor before the security interest is perfected.").

decided that their conduct as a matter of law estopped them from disputing the priority interest of MBank.¹⁰⁷

The twin assumptions on which the court's opinion rests are troubling, not because they are necessarily wrong but because they are made with a blind faith in their correctness. In the context of an existing constructive trust, it is by no means certain whether a secured party who has not relied on the debtor's ostensible ownership of property or who has not given value subsequent to the trust coming into existence is entitled to the protection accorded historically to good faith purchasers.¹⁰⁸ As far as the article 9 analysis is concerned, it might be argued that resolution of this sort of priority dispute is outside its scope.¹⁰⁹

Cases continue to accumulate involving the extent to which non-Code law governs the transfer of title to goods. Again this year, the Nebraska Supreme Court has asserted the primacy of the Code.¹¹⁰ In *Alford v. Neal*,¹¹¹ the court held that, as between buyer and seller, noncompliance with the motor vehicle certificate of title act does not prevent the transfer of title. The certificate is no more than prima facie evidence of ownership. In another case, *In re Bellanca Aircraft Corp.*,¹¹² the Eighth Circuit ruled that the Code, not the Federal Aviation Act, determined whether the transfer of an interest in a plane is valid against creditors of the seller. Similarly, in *Brink v. McNeil*,¹¹³ the Colorado Court of Appeals decided that the state's livestock bill of sale laws did not affect the U.C.C. mandated result.

107. That conduct consisted of entrusting Young with possession and allowing him to place his brand on the cattle.

108. Although a dissenting voice is occasionally heard (*see In re Emery Corp.*, 38 Bankr. 489, 38 U.C.C. Rep. Serv. (Callaghan) 834 (E.D. Pa. 1984), *rev'd*, 52 Bankr. 944, 41 U.C.C. Rep. Serv. (Callaghan) 1172 (D.C. Pa. 1985)), it is now well settled that the secured creditor has purchaser status when the competing claimant is a reclaiming seller (*see infra* notes 100–09 and accompanying text) but different policy considerations may call for a more restrictive reading of the Code's definition of purchaser when a constructive trust is at issue. *See* U.C.C. § 1-201 (definitions applicable “unless the context otherwise requires”).

109. In the first place, it seems that the court is confusing a constructive trust with the dissimilar but functionally related (both serve to prevent unjust enrichment) equitable lien. Secondly, even if a constructive trust can properly be viewed as generating a lien, it does not seem to be one of the type to which the priority rule of U.C.C. § 9-301(1)(b) is directed. *See* U.C.C. § 9-301(3) (“[A] ‘lien creditor’ means a creditor who has acquired a lien on the property involved by attachment, levy or the like . . .”). If not governed by a specific priority rule, can we say with confidence that the drafters intended for this contest to be settled by the general priority rule of U.C.C. § 9-201?

110. *See* Frisch & Wladis, *General Provisions, Sales, Bulk Transfers, and Documents of Title*, 44 Bus. Law. 1445, 1462–63 (1989).

111. 229 Neb. 67, 425 N.W.2d 325, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1457 (1988).

112. *In re Bellanca Aircraft Corp.*, 850 F.2d 1275, 7 U.C.C. Rep. Serv. 2d (Callaghan) 656 (8th Cir. 1988).

113. 7 U.C.C. Rep. Serv. 2d (Callaghan) 1466 (Colo. Ct. App. 1988).

Tender, Cure, and Notice of Breach

In *Leitchfield Development Corp. v. Clark*,¹¹⁴ a Kentucky appellate court, for the first time, had the opportunity to construe the relationship between U.C.C. sections 2-601 and 2-508. The court held that the "perfect tender rule" set forth in U.C.C. section 2-601 does not necessarily require a perfect tender in the first instance.¹¹⁵ If the seller properly exercises its right of cure, a rejection of a nonconforming tender will not be permitted. In the case before it, the court reversed a judgment for the buyers of a mobile home which was predicated on an instruction to the jury that the buyers had the right to reject their home if it failed to "conform to their purchase contract in any respect." The alleged nonconformity was minor damage to one corner of the home which occurred during its delivery and which could have been repaired for \$75.

What makes *Leitchfield* a case worth reviewing is not so much what the court decided but, rather, what it did not decide. Under U.C.C. section 2-508(1), cure is allowed only if it can be accomplished within the "time for performance." The majority opinion is silent on when the seller's performance was due.¹¹⁶ The conclusion of Judge Wilhoit in a concurring opinion that in the absence of a specified delivery date, the actual delivery date was the time for performance, seems incorrect. It would be better to imply a reasonable delivery term under U.C.C. section 2-309(1).¹¹⁷ Also missing from the decision is a recognition of the divergence of opinion surrounding the application of subsection (2) of U.C.C. section 2-508.¹¹⁸ Must the seller show that it knew of the nonconformity at the time of delivery, or is it sufficient to prove only that it believed the home would be acceptable?¹¹⁹ Finally, the court assumes that cure precludes an effective rejection. As another case in this year's survey teaches, this is probably not true.¹²⁰ Cure only makes the rejection wrongful. There is a difference.

114. 757 S.W.2d 207, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1092 (Ky. Ct. App. 1988).

115. By its terms, U.C.C. § 2-601 permits the buyer to reject "if the goods or the tender of delivery fail in any respect to conform to the contract."

116. The court does include the issue of whether the intention to cure was communicated to the buyers within the time allowed for performance as one of the questions of fact that may have to be decided by the jury on remand. 757 S.W.2d at 212, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1099.

117. U.C.C. § 2-309(1) provides: "The time for shipment or delivery or any other action under a contract if not provided in this Article or agreed upon shall be a reasonable time."

118. U.C.C. § 2-508(2) provides: "Where the buyer rejects a non-conforming tender which the seller had reasonable grounds to believe would be acceptable with or without money allowance the seller may if he seasonably notifies the buyer have a further reasonable time to substitute a conforming tender."

119. Compare *Meads v. Davis*, 22 N.C. App. 479, 206 S.E.2d 868, 15 U.C.C. Rep. Serv. (Callaghan) 40 (1974) ("Obviously this section deals with the situation in which the seller knows prior to delivery that the goods are not in conformity . . .") with *Joc Oil USA, Inc. v. Consolidated Edison Co.*, 107 Misc. 2d 376, 434 N.Y.S.2d 623, 30 U.C.C. Rep. Serv. (Callaghan) 426 (N.Y. Sup. Ct. 1980) ("compelling equitable considerations exist to extend the § 2-508(2) remedy to those innocent sellers who have no prior predelivery knowledge of nonconformity").

120. See the discussion of *Integrated Circuits Unlimited v. E.F. Johnson Co.*, 8 U.C.C. Rep. Serv. 2d (Callaghan) 695 (2d. Cir. 1989), *infra* notes 139-49 and accompanying text.

The Code requires that “[t]he buyer must within a reasonable time after he discovers or should have discovered any breach, notify the *seller* of breach or be barred from any remedy.”¹²¹ One recurring question is whether the need to give notice extends to persons who are not “buyers” of the goods involved, but are rather warranty beneficiaries. The answer continues to be in dispute.¹²² In both *Carlson v. Armstrong World Industries*¹²³ and *Morgan v. Sears, Roebuck & Co.*,¹²⁴ the courts determined that non-privity plaintiffs are not required to give timely notice of breach.¹²⁵ In another case, *Cooley v. Big Horn Harvestore Systems, Inc.*,¹²⁶ the Colorado Court of Appeals followed the middle-of-the-road position taken by that state’s supreme court.¹²⁷ Recognizing that the need to give notice might depend upon the circumstances of the particular case, the court of appeals held that notice is necessary where the buyer is a commercial buyer and the damage is to property. At the other end of the spectrum is *Allen v. G.D. Searle & Co.*¹²⁸ The district court, applying Oregon law, ruled that even where the plaintiff is a consumer who is seeking to recover for personal injuries, notice must be given.¹²⁹

Another issue on which courts cannot agree concerns the sufficiency of notice if given in a pleading. In *Bednarski v. Hideout Homes & Realty, Inc.*,¹³⁰ the court, anticipating how the Pennsylvania Supreme Court would decide the matter, could see no reason why a litigation filing, if timely made, could not serve as adequate notification. On the other hand, the *Allen*¹³¹ court on reconsideration, held that notice given for the first time in a complaint is insufficient under Oregon law, as a matter of law. If the latter rule is accepted, exceptions

121. U.C.C. § 2-607(3)(a) (emphasis added).

122. The majority of courts hold that warranty beneficiaries need not give notice. *See, e.g.,* *Simmons v. Clemco Indus.*, 368 So. 2d 509, 25 U.C.C. Rep. Serv. (Callaghan) 1088 (Ala. 1979) (notice not required); *Chaffin v. Atlanta Coca-Cola Bottling Co.*, 127 Ga. App. 619, 194 S.E.2d 513, 11 U.C.C. Rep. Serv. (Callaghan) 737 (1972) (same); *Mattos v. Hash*, 279 Md. 371, 368 A.2d 993, 21 U.C.C. Rep. Serv. (Callaghan) 473 (1977) (same). *But see* *Parillo v. Giroux Co.*, 426 A.2d 1313, 31 U.C.C. Rep. Serv. (Callaghan) 108 (R.I. 1981) (notice is required). *See also* Uniform Commercial Code § 2-607 Official Comment 5 (“the reason of the section does extend to requiring the beneficiary to notify the seller that an injury has occurred”).

123. 693 F. Supp. 1073, 7 U.C.C. Rep. Serv. 2d (Callaghan) 751 (S.D. Fla. 1987).

124. 693 F. Supp. 1154, 7 U.C.C. Rep. Serv. 2d (Callaghan) 464 (N.D. Ga. 1988).

125. Their conclusion follows from taking U.C.C. § 2-607(3)(a)’s use of the word “buyer” literally. *See* U.C.C. § 2-103(1)(a) (“‘Buyer’ means a person who buys or contracts to buy goods.”).

126. 7 U.C.C. Rep. Serv. 2d (Callaghan) 1051 (Colo. Ct. App. 1988).

127. The court of appeals cited *Prutch v. Ford Motor Co.*, 618 P.2d 657, 29 U.C.C. Rep. Serv. (Callaghan) 1507 (Colo. 1980) (need to give notice might vary with the facts) and *Palmer v. A. H. Robins Co.*, 684 P.2d 187, 38 U.C.C. Rep. Serv. (Callaghan) 1150 (Colo. 1984) (consumer excused from having to give notice).

128. 708 F. Supp. 1142, 8 U.C.C. Rep. Serv. 2d (Callaghan) 983 (D. Or. 1989).

129. The court relied on *Redfield v. Mead, Johnson & Co.*, 266 Or. 273, 512 P.2d 776, 13 U.C.C. Rep. Serv. (Callaghan) 10 (1973), as evidence that the pre-Code requirement of notice remains an essential element of a warranty claim.

130. 709 F. Supp. 90, 8 U.C.C. Rep. Serv. 2d (Callaghan) 1040 (M.D. Pa. 1988).

131. 8 U.C.C. Rep. Serv. 2d (Callaghan) 1046 (D. Or. 1989). For an earlier decision in this case, see *supra* note 128 and accompanying text.

will invariably be required. For example, in *Quaker Alloy Casting Co. v. Gulfco Industries*,¹³² the court believed that a pleading can be an acceptable means of notice in situations where the breach cannot reasonably be discovered until after the commencement of litigation.¹³³

Finally, for those who have not yet learned to appreciate the importance of U.C.C. section 2-607(3)(a) (both to buyers, as a prerequisite to recovery, and to sellers, as a basis for an affirmative defense), there is *Fairhaven Textile Corp. v. Sheehan, Phinney, Bass & Green, P.A.*¹³⁴ *Fairhaven* involved a legal malpractice action against the law firm that had represented the seller in a previous case. The district court held that the defendant firm's failure to raise the issue of notice was malpractice as a matter of law. Query whether the court's holding would be equally applicable to an attorney who fails to give notice on behalf of the buyer?

Repudiation

Although U.C.C. section 2-609 was intended to free the aggrieved party from having to make the oftentimes difficult decision whether the other party has "repudiated" the contract, the section has as much potential to be a mine field as it does a haven.¹³⁵ A case that makes this point very nicely is *Scott v. Crown*.¹³⁶ Buyer (Crown) and seller (Scott) entered into a series of contracts for the sale of U.S. No. 1 wheat. Each contract provided for full payment by buyer 30 days after complete performance by seller. Seller, after having performed the first contract, but before payment was due, was told by his banker that buyer was not the "best grain trader" and was informed by the Department of Agriculture of a pending complaint against buyer concerning payments to other farmers. As a consequence of this information and nonpayment by another buyer, seller told buyer's driver, who had come for more wheat, that there would be no further deliveries until contact was made with Mr. Crown "to settle some questions." Buyer responded with two letters. In the first, he demanded performance; in the second, he cancelled the contracts subject to reinstatement should seller resume performance. Seller, through counsel, replied with a letter demanding assurances of performance, that is, early payment for all wheat that had previously been delivered. When payment was not made, seller filed suit and the buyer

132. 686 F. Supp. 1319, 7 U.C.C. Rep. Serv. 2d (Callaghan) 429 (N.D. Ill. 1988).

133. In addition, the court stated two rules regarding notice; one for merchants, another for retail consumers. Consumers can, even in the unexceptional case, give notice through litigation filings. 686 F. Supp. at 1340, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 449.

134. 695 F. Supp. 71, 7 U.C.C. Rep. Serv. 2d (Callaghan) 780 (D. N.H. 1988).

135. To obtain a clear repudiation, a party who has "reasonable grounds for insecurity" may "demand adequate assurance of due performance" under U.C.C. § 2-609(1). Subsection (4) of § 2-609 provides that "failure to provide within a reasonable time not exceeding thirty days such assurance of due performance" is a "repudiation of the contract." But when does one have reasonable grounds for insecurity and what assurances are adequate? These are only two of the several new issues that the section creates.

136. 7 U.C.C. Rep. Serv. 2d (Callaghan) 464 (Colo. Ct. App. 1988).

counterclaimed. The trial court gave judgment for seller on both its claim and the counterclaim.

On appeal, the Colorado Court of Appeals reversed. Although it conceded that reasonable grounds for seller's insecurity might have existed, the court ruled that the timing, form, and content of the demand for assurances of performance were fatally defective. First, the court addressed the adequacy of the statement made to buyer's driver. Despite the fact that the Code mandates a written demand for assurances, the court recognized the possibility that an oral demand would suffice.¹³⁷ Such would be the case if, for example, it were clearly understood that if assurances were not forthcoming there would be a suspension of performance. Unfortunately for seller, the statement to the driver did not unequivocally indicate what was required and the consequences of noncompliance. Nor did the later written demand justify a suspension of performance. According to the court, the seller had no right to force a modification of the contract by requesting payment before it was due. Therefore, it was seller who repudiated and was in breach of the contracts.

The court's conclusion that a demand for assurances is ineffective if compliance would effect a modification of the contract is less than convincing.¹³⁸ It seems that the very concept of assurances envisions the giving of something to which the demanding party was not originally entitled. Also unclear is why a requested assurance which is later deemed excessive should vitiate the demand entirely. Perhaps the demanding party would be wise to leave the choice of assurances to the other party, making only suggestions as to what would be acceptable.

REMEDIES

Rejection and Revocation of Acceptance

Does the delivery of conforming goods to the buyer necessarily entitle the seller to the purchase price? The Second Circuit Court of Appeals said it did not in *Integrated Circuits Unlimited v. E. F. Johnson Co.*¹³⁹ Involved was the purported rejection of 174 microprocessors which the district court found to be in conformity with contract specifications.¹⁴⁰ Following their rejection, buyer

137. *Id.* at 468. Not all courts would agree. In fact, during this survey period two courts decided otherwise. See *Quaker Alloy Casting Co. v. Gulfco Indus.*, 686 F. Supp. 1319, 7 U.C.C. Rep. Serv. 2d (Callaghan) 429 (N.D. Ill. 1988); *USX Corp. v. Union Pacific Resources Co.*, 753 S.W.2d 845, 7 U.C.C. Rep. Serv. 2d (Callaghan) 100 (Tex. Ct. App. 1988).

138. A similar conclusion has surfaced in at least one other case. See, e.g., *Pittsburgh-Des Moines Steel Co. v. Brookhaven Manor Water Co.*, 532 F.2d 572, 18 U.C.C. Rep. Serv. 931 (Callaghan) (7th Cir. 1976).

139. 8 U.C.C. Rep. Serv. 2d (Callaghan) 695 (2d Cir. 1989).

140. It is interesting to note that 1,973 microprocessors had been delivered and, except for 174, all were found to be unacceptable although only 130 microprocessors were actually tested. This was held to be statistically sufficient to justify a conclusion that the similar untested devices were also defective. See generally Cohen, *Conceptualizing Proof and Calculating Probabilities: A Response to Professor Kaye*, 73 Cornell L. Rev. 78 (1987); Kay, *Apples and Oranges: Confidence Coefficients*

held the microprocessors in storage for three months, during which time the seller refused to accept their return.¹⁴¹ The Second Circuit found no error in the trial court's conclusion that although buyer's rejection of the 174 units was substantively wrongful, it was, nevertheless, procedurally effective.¹⁴² The distinction is significant. If the goods have been effectively rejected, that precludes, by negative implication, their acceptance under U.C.C. section 2-606(1)(b).¹⁴³ If there has been no acceptance, the seller is barred from recovering the contract price under U.C.C. section 2-709.¹⁴⁴ Still, a wrongful rejection is a breach and the buyer remains liable for damages. Unfortunately for the seller in *Integrated Circuits*, it could establish none. Not having retaken possession of the goods, the seller could not resell the goods and recover under U.C.C. section 2-706; recovery under U.C.C. section 2-708(1) was precluded because the contract and market prices were, at all relevant times, the same; and loss volume seller status could not be established which would entitle the seller to its lost profit under U.C.C. section 2-708(2). The end result was a net credit and judgment in favor of the buyer for \$10,359.¹⁴⁵

Although the decision in *Integrated Circuits* appears to be consistent with the language of the Code¹⁴⁶ and the intention of its drafters,¹⁴⁷ as a matter of policy, its soundness is questionable. If the buyer has accepted the tender before seeking to return the goods, their return can be refused by the seller and the buyer remains liable for the price.¹⁴⁸ If the buyer has not accepted the goods, then their

and the Burden of Persuasion, 73 Cornell L. Rev. 54 (1987); James, *Relevancy, Probability and the Law*, 29 Calif. L. Rev. 689 (1941).

141. U.C.C. § 2-602(2)(b) imposes on a buyer the duty to hold rejected goods, in which he does not have a security interest, "with reasonable care at the seller's disposition for a time sufficient to permit the seller to remove them." Because buyer had done all that it was required to do, the district court held that any loss occasioned by a subsequent fall in the market price of microprocessors must be borne by seller. The district court's opinion appears at 691 F. Supp. 630, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1478 (E.D.N.Y. 1988).

142. An effective rejection refers to a rejection timely made and properly communicated to the seller without regard to its justification.

143. U.C.C. § 2-606(1)(b) provides, in pertinent part:

(1) Acceptance of the goods occurs when the buyer . . . fails to make an *effective* rejection (subsection (1) of § 2-602 . . . (emphasis added).

144. The statement in the text assumes that the goods have not been lost or damaged and that a substitute disposition for a reasonable price is possible. See U.C.C. § 2-709.

145. The credit was the difference between the total contract price of all parts rejected by the buyer (\$171,084) and payments withheld on seller's account (\$160,725). The judgment of the district court in favor of the seller for \$4638.73 was reversed because no credit was given for the parts wrongfully, but effectively, rejected. As the Second Circuit correctly pointed out, to refuse a credit "would be tantamount to awarding [seller] the price of the goods returned or of its lost profits which, on these facts . . . is unauthorized by the Code." 8 U.C.C. Rep. Serv. 2d (Callaghan) at 700.

146. See *supra* note 143.

147. See, e.g., Peters, *Remedies for Breach of Contracts Relating to the Sale of Goods Under the Uniform Commercial Code: A Roadmap for Article Two*, 73 Yale L.J. 199, 241 (1963).

148. It would seem from a reading of the Code that it is not possible to avoid liability for the contract price by making procedurally effective but substantively wrongful revocation of acceptance. See J. White & R. Summers, *Uniform Commercial Code* 296-97 (3d ed. 1988).

return cannot be refused by the seller. It is not clear that the seller's usual ability to effect a more efficient disposition of the goods justifies making the seller choose, at its risk, which course to pursue.¹⁴⁹

*Andover Air Ltd. Partnership v. Piper Aircraft Corp.*¹⁵⁰ considered several issues involving the remedy of revocation. Andover Air Limited Partnership ("Andover") purchased a Piper Cheyenne 1A aircraft with a five-year warranty from a Piper dealer. Approximately one year later, the plane was forced to make a gear-up landing, necessitating substantial repairs. Andover sued Piper Aircraft Corporation ("Piper"), the manufacturer of the plane, alleging that a defective uplock hook assembly caused the accident.

The first issue concerned the right of Andover to seek both revocation and damages for breach of warranty. Piper argued that to assert two mutually exclusive remedies in a pleading is an act of bad faith and should not be permitted. The court correctly rejected this contention.¹⁵¹ Although the aggrieved party's freedom to choose its remedy is not unlimited, there is no reason why the remedial flexibility inherent in article 2 should not be preserved, at least through the pleading stage.

The next issue in *Andover Air* concerned the availability of revocation against Piper, a non-privity manufacturer. The statutory impediment is the use of the words "the seller" in U.C.C. section 2-608. The Code defines a seller as one who "sells or contracts to sell goods,"¹⁵² and defines a "sale" as "the passing of title from the seller to the buyer for a price."¹⁵³ As a consequence, most courts have held that a buyer can revoke only against its immediate seller.¹⁵⁴ Apparently seeing no significance in the assumption of warranty liability by Piper, the district court assumed that Massachusetts courts would agree with the majority of cases. Hence, in the absence of a principal/agent relationship between the manufacturer and dealer,¹⁵⁵ revocation is available only against the latter.

Another issue was whether Andover's use, repair, and maintenance of the plane prior to the accident or its use of the plane following the accident precluded revocation. The court stated that the questions of substantial change

149. As a practical matter, depending upon the buyer's solvency and other factors, the seller may wish to retake possession of the goods regardless of its obligation to do so.

150. 7 U.C.C. Rep. Serv. 2d (Callaghan) 1494 (D. Mass. 1989).

151. In reaching its conclusion, the court cited rules 8(e)(2) & 8(a)(2) of the Federal Rules of Civil Procedure and several cases, including *Fargo Machine & Tool Co. v. Kearney & Trecker Corp.*, 428 F. Supp. 364, 21 U.C.C. Rep. Serv. (Callaghan) 80 (E.D. Mich. 1977) and *General Motors Acceptance Corp. v. Anaya*, 103 N.M. 72, 703 P.2d 169, 41 U.C.C. Rep. Serv. (Callaghan) 824 (N.M. 1985).

152. U.C.C. § 2-103(1)(d).

153. U.C.C. § 2-106(1).

154. See, e.g., *Voytovich v. Bangor Punta Operations, Inc.*, 494 F.2d 1208, 15 U.C.C. Rep. Serv. (Callaghan) 45 (6th Cir. 1974); *Seekings v. Jimmy GMC of Tucson, Inc.*, 130 Ariz. 596, 638 P.2d 210, 32 U.C.C. Rep. Serv. (Callaghan) 1450 (Ariz. 1981); *Gasque v. Mooers Motor Car Co.*, 227 Va. 154, 313 S.E.2d 384, 38 U.C.C. Rep. Serv. (Callaghan) 120 (1984).

155. Such a relationship was found and revocation was permitted against the manufacturer in *Costa v. Volkswagen of Am.*, 150 Vt. 213, 551 A.2d 1196, 8 U.C.C. Rep. Serv. 2d (Callaghan) 389 (1988).

caused by preaccident use and the reasonableness of the postaccident use presented questions of fact for resolution at trial.¹⁵⁶

U.C.C. section 2-608 permits revocation "of a lot or commercial unit." What constitutes a "lot"¹⁵⁷ was before the Ninth Circuit Court of Appeals in *S & R Metals, Inc. v. C. Itoh & Co. (America)*.¹⁵⁸ In that case, C. Itoh contracted to sell to S & R 5,500 metric tons of steel in coils of varying widths and thickness. After having sold about 35% of the steel, S & R learned from a customer that the 14-gauge steel was defective. It then sought to revoke acceptance of the entire amount of steel still in its possession, including gauges that were not shown to be nonconforming. The district court permitted revocation and the Ninth Circuit affirmed. The circuit court refused to limit revocation to those "commercial units" that proved to be nonconforming, that is, the 14-gauge steel. The court held that the provision pertaining to revocation of a lot does not depend upon multiple deliveries. Where goods are delivered in a single lot, the right to revoke extends to the entirety.

To conclude, one other case is worth mention. In *Herbert v. Harl*,¹⁵⁹ the buyers sought to revoke their acceptance of a used automobile. What they did not do was tender a properly executed reassignment of the certificate of ownership that complied with the state's motor vehicle and licensing statutes. In dicta, the Missouri Supreme Court determined that this rendered the attempted revocation ineffective.¹⁶⁰ This seems wrong on two counts. First, U.C.C. section 2-401(4) provides that title automatically reverts in the seller upon revocation. Second, a requirement that the buyer tender a completed certificate of ownership does not give recognition to the buyer's security interest under U.C.C. section 2-711(3). This case is simply another example of the growing tension between the Code and the plethora of commercial statutes external to the Code.

Reclamation

The cases continue to demonstrate the tenuous nature of the reclamation rights of unpaid sellers. In particular, consider the frequent efforts of sellers to

156. Whether continued use of goods is at odds with revocation of acceptance will *often depend on the following factors*:

[T]he seller's instructions to the buyer after revocation of acceptance; the degree of economic and other hardship that the buyer would suffer if he discontinued using the good; the reasonableness of continued use after revocation as a method for mitigating damages; the degree of prejudice to the seller; and whether the seller acted in good faith.

U.C.C. Rep. Serv. 2d (Callaghan) at 1501 (citing *Johannsen v. Minnesota Valley Ford Tractor Co.*, 304 N.W.2d 654, 658, 31 U.C.C. Rep. Serv. (Callaghan) 558, 563 (Minn. 1981)).

157. The term "lot" is defined as "a parcel or a single article which is the subject matter of a separate sale or delivery, whether or not it is sufficient to perform the contract." U.C.C. § 2-105(5).

158. 7 U.C.C. Rep. Serv. 2d (Callaghan) 61 (9th Cir. 1988).

159. 757 S.W.2d 585, 7 U.C.C. Rep. Serv. 2d (Callaghan) 740 (Mo. 1988).

160. *Id.* at 590, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 746. The court failed to recognize that revocation is not an ordinary course transfer of ownership. One suspects that the statutes were never intended to govern transfers to involuntary transferees.

reclaim, under U.C.C. section 2-702, goods that are subject to the interest of a secured party (as a good faith purchaser) who financed the buyer's inventory. Despite the fact that the vast majority of courts hold that the interest of the unpaid seller is subordinate to the lien of the secured party,¹⁶¹ sellers still do battle, emboldened either by the factual nuances of their respective cases or the cleverness of their arguments.

A somewhat different factual setting was involved in *O'Brien v. Chandler*.¹⁶² What distinguished this case from most was the method of delivery and the alleged terms of the agreement between the seller and buyer. Neither of those matters prevented the New Mexico Supreme Court from affirming the trial court's entry of summary judgment in favor of the secured party. The seller of cattle delivered them to a feedlot for later delivery to the buyer. All the buyer ever received were invoices which described the cattle and set out the sale price. In his deposition, the seller testified that the buyer could, after inspection, reject any or all of the cattle.¹⁶³ After the buyer inspected the cattle, but before selecting those which he would keep, he used the cattle as collateral to secure a loan from his bank.

The court started its analysis with the statement that "[t]he specific agreement between buyer and seller is simply not a material issue. What is material is the fact that delivery was made by a seller to a buyer, and that fact is not in dispute."¹⁶⁴ With that said, the case was cast in the mold of the familiar and so, too, was most of the court's reasoning. It concluded that the buyer obtained voidable title to the cattle with the consequent power to transfer good title (security interest) to the bank, a bona fide purchaser without notice of the seller's claim.¹⁶⁵ The court was also not persuaded by the seller's position that it had a perfected article 2 security interest¹⁶⁶ under U.C.C. section 9-113¹⁶⁷ because of a state statute providing that possession of livestock without a

161. Although involving an attempt at reclamation by an unpaid *cash* seller under U.C.C. § 2-507, *In re Samuels & Co.*, 510 F.2d 139, 16 U.C.C. Rep. Serv. (Callaghan) 577 (5th Cir. 1975), *rev'd on reh'g en banc*, 526 F.2d 1238, 18 U.C.C. Rep. Serv. (Callaghan) 545 (5th Cir.), *cert. denied*, 429 U.S. 834 (1976), is generally considered the landmark case upholding the priority of the secured creditor.

162. 107 N.M. 797, 765 P.2d 1165, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1450 (1988).

163. The seller also testified that notwithstanding the fact that the invoices set out the sale price, it was expected that a price would be negotiated for any cattle which the buyer chose to keep.

164. *Id.* at 799, 765 P.2d at 1167, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1453. The court went on to characterize the transaction as a "sale or return." *Id.* at 799, 765 P.2d at 1167, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1454. Once the court decided that a contract for sale existed, it is surprising that it even considered parol evidence concerning the return aspect of the agreement. *See* U.C.C. § 2-326(4) ("Any 'or return' term of a contract for sale is to be treated as a separate contract for sale within the statute of frauds section of this Article . . . and as contradicting the sale aspect of the contract within the provisions of this Article on parol or extrinsic evidence . . .").

165. The seller also contended that it had successfully stopped delivery of the cattle under U.C.C. § 2-705 before the buyer was notified by the feedlot that goods were being held for him. There was, however, no evidence that any attempt was made to stop delivery before the security interest was given to the bank.

166. Although the court never mentions the source of the alleged article 2 security interest, it presumably would have arisen under U.C.C. § 2-401 ("Any retention or reservation by the seller of

document of title is prima facie evidence that possession is unlawful.¹⁶⁸ Even if a perfected article 2 security interest existed, the seller could not reclaim after the expiration of the 10-day period provided by U.C.C. section 2-702.

Perhaps the seller would have met with more success had he not characterized himself as a "seller." Could he not have argued that, prior to the buyer's selection of cattle there was no contract of sale, but rather an offer to sell cattle then bailed with the feedlot? The case also serves as a reminder of how poorly U.C.C. section 9-113 works to bridge the gap between articles 2 and 9.¹⁶⁹

In *Estate of Schomer v. Piggot*,¹⁷⁰ the seller attempted to use an equal protection challenge to the secured party's priority. Seller argued that equal protection of the laws was denied because the Code gives sophisticated and experienced bankers an unfair advantage over less sophisticated and experienced farmers. The Iowa Supreme Court quite properly rejected this attempt to make the operation of the Code's rules vary with the relative business savvy of the parties.

Buyer's Money Remedies and Their Limitations

The basic statutory formula of U.C.C. section 2-714(2) is simple: "[t]he measure of damages for breach of warranty is the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted, unless special circumstances show proximate damages of a different amount." Reflection on a trio of recent cases involving this subsection reveals that its application is oftentimes not so simple.

In the first case, *Nelson v. Logan Motor Sales, Inc.*,¹⁷¹ Nelson sued for breach of an implied warranty of merchantability on a used car. The jury awarded Nelson \$3500. The trial judge set aside the verdict for lack of sufficient evidence on damages.¹⁷² On appeal, the West Virginia Supreme Court of Appeals reversed. The court found no merit in Nelson's contention that the jury could infer that the car was essentially worthless¹⁷³ on the basis of his testimony that

the title (property) in goods shipped or delivered to the buyer is limited in effect to a reservation of a security interest.").

167. U.C.C. § 9-113 provides that an article 2 security interest is perfected "so long as the debtor does not have or does not lawfully obtain possession of the goods."

168. See N.M.S.A. §§ 77-9-21 and 77-9-22 (1978).

169. See generally Jackson & Peters, *Quest for Uncertainty: A Proposal for Flexible Resolution of Inherent Conflicts Between Article 2 and 9 of the Uniform Commercial Code*, 87 Yale L.J. 907 (1978).

170. 8 U.C.C. Rep. Serv. 2d (Callaghan) 513 (Iowa 1989).

171. 370 S.E.2d 734, 7 U.C.C. Rep. Serv. 2d (Callaghan) 116 (W. Va. 1988).

172. One can readily see what motivated the trial judge to set aside the verdict. The jury's award gave Nelson the purchase price and let him keep the car.

173. In this regard the supreme court's opinion is inconsistent. At the outset we are told that the jury returned a verdict in the amount of \$3500. *Id.* at 735, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 116. Later in the opinion, the court refers to a \$3400 award which presumably was based on a

he did not drive the car due to its condition.¹⁷⁴ The trial judge erroneously failed to admit repair bills in the amount of \$455.04. The appellate court made the point that if the contract price represents value that a good should have had, the contract price less repair costs may be the actual value of the good accepted.¹⁷⁵ Thus, no special circumstances are needed for justifying the admissibility of repair costs.¹⁷⁶

In the second case, *Crook Motor Co. v. Goolsby*,¹⁷⁷ the district court was faced with a claim for damages for breach of the warranty of title and fraud. J. W. Goolsby sold a truck tractor to Crook Motor Co. for \$48,000. Crook Motor sold the tractor to Battle Creek Ford for \$54,000. Battle Creek sold to another person for more than \$69,000. Events established that the vehicle had been stolen before the sale to Crook Motor. Crook Motor was obliged to refund the purchase price to Battle Creek. Crook Motor then sued Goolsby and all others in the chain of preceding sales for breach of warranty of good title under U.C.C. section 2-312(1) and fraud.

Against both Goolsby and Buddy Simmons (the initial seller of the truck), the court awarded damages of \$54,000. Goolsby's liability under U.C.C. section 2-714(2) was assumed to be the \$48,000 purchase price. Since Crook Motor never received good title, the actual value was zero and the court assumed the truck's value would have been \$48,000, which was the purchase price. The remainder of the award consisted of incidental and consequential damages under U.C.C. section 2-715.¹⁷⁸ The court computed Simmons's liability differently. The court purported to assess damages using a "benefit of the bargain" formula.¹⁷⁹ Although the tractor on resale had eventually brought \$69,793, the court

finding that the car, when delivered, was worth \$100. *Id.* at 736 n.4, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 118 n.4.

174. Although admissible on the issue of value, the testimony of Nelson, *standing alone*, was held insufficient to establish the value of the vehicle.

175. Obviously this may not always be true. The value goods would have had may be more or less than the contract price. The actual diminished value of goods may not, in some cases, be captured by repair costs. Nonetheless, repair costs are certainly relevant and with proper foundation should be admitted in a damage case built on U.C.C. § 2-714(2).

176. The trial court apparently believed that the admissibility of repair bills depended upon a showing of "special circumstances." The supreme court correctly recognized that a showing of special circumstances is necessary only if one is attempting to show that the entire formula of U.C.C. § 2-714(2) is inappropriate.

177. 703 F. Supp. 511, 8 U.C.C. Rep. Serv. 2d (Callaghan) 363 (N.D. Miss. 1988).

178. Because Goolsby knew he was selling to a used truck dealer he was liable to Crook Motor for its out-of-pocket expenses in preparing the truck for resale (\$450.57) and the lost profit on the resale to Battle Creek (\$5,549.43). Crook Motor's claim for damages for loss of good will and business reputation was held to be too speculative to be allowed.

179. Buddy Simmons was held liable on a non-Code misrepresentation theory. Crook Motor could not recover for breach of the warranty of title since that warranty was held to protect only the immediate purchaser and not run with the goods. U.C.C. § 2-721, however, states that "[r]emedies for material misrepresentation or fraud include all remedies available under this Article for non-fraudulent breach." Although no mention was made of U.C.C. § 2-714(2), it seems reasonable to assume that because of the stated equivalency between fraud and contract remedies, it was the governing section. It should also be mentioned that, in addition to the general damages award of

refused to use that figure as a benchmark. Rather, it used the price of \$54,000 for which Crook Motor sold to Battle Creek as an upper limit on recovery. According to the court, anything else would have been a windfall.

The decision in *Crook Motor* is of interest insofar as it forces a rethinking of a basic remedial policy issue. To what extent should the actual loss established by events subsequent to the breach cap or mandate the application of a particular measure of damages?¹⁸⁰ If it is a correct inference that the value of the tractor at the time and place of acceptance (assuming good title) exceeded the \$54,000 sale price, then the higher value rather than the purchase price should have been the benchmark for damage calculations under section 2-714(2). Yet, later events showed that an award based on this figure would have yielded more than the buyer would have obtained by the seller's full performance. Whether the court's adjustment of the damage formula of section 2-714(2) under these circumstances is good policy is a question far too complex for adequate treatment in the context of this survey.¹⁸¹ It suffices to say that an award which appears overcompensatory may not be once the costs of litigation (both those that are measurable but not legally recoverable and those that are immeasurable) are taken into account.

The third case, *Costa v. Volkswagen of America*,¹⁸² highlights the judicial system's inadequacies all too clearly. Costa bought an Audi 5000 in 1979 for \$11,530. During the next several months he noticed many problems. After unsuccessful repair attempts, Costa revoked acceptance. He then commenced this suit for breach of express warranty. The jury awarded Costa \$13,000, and on the verdict form wrote: "The Jury's verdict for plaintiff is with the stipulation that the title to the 1979 Audi 5000 be awarded to Volkswagen of America, Inc." The trial judge granted a new trial in the belief that the jury wrongly based its award upon a theory of rescission. The case was retried to the court and this time a judgment for the defendant was entered.

On appeal, the Vermont Supreme Court determined that there should have been no new trial on the issue of liability. The jury had been correctly instructed on the requirements for an effective revocation and the mandate on the verdict form was consistent with that remedy. The trial court had compounded its error by instructing the jury that damages after revocation were to be calculated using the formula of section 2-714(2).¹⁸³ This is obviously wrong. That formula

\$54,000, Simmons was found liable for punitive damages of \$80,000 and a reasonable attorney's fee yet to be assessed.

180. For a sampling of some of the many different fact patterns involving this problem, see J. White & R. Summers, *Uniform Commercial Code*, 243-265 (3d ed. 1988).

181. This subject was one of the topics discussed at the meeting of the subcommittee on General Provisions, Sales, Bulk Transfers, and Documents of Title in Houston, Texas (Spring 1989).

182. 150 Vt. 213, 551 A.2d 1196, 8 U.C.C. Rep. Serv. 2d (Callaghan) 389 (1988).

183. Where the buyer "rightfully rejects or justifiably revokes acceptance" general damages are recoverable under U.C.C. § 2-712 (cover) or U.C.C. § 2-713 (market price/contract price differential). U.C.C. §§ 2-711(1)(a) & (b). Another case where the court failed to fully understand the remedial scheme of article 2 is *Andover Air Ltd. Partnership v. Piper Aircraft Corp.*, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1494 (D. Mass. 1989) (mistaken assumption that revocation does not permit

applies only if the buyer retains the goods. Thus, a third trial was necessitated on the issue of damages.

The case shows a plaintiff heading toward trial for a third time after eight years of litigation. The root of the problem was the trial judge's lack of appreciation for the distinction among remedies allowed under article 2. In particular, the judge instructed the jury on section 2-714(2) when it was inapplicable.

Protracted litigation was also a fate faced by the buyers in *Nachazel v. Miraco Manufacturing*.¹⁸⁴ The case arose from the purchase of hog farrowing houses and nurseries known as Mirahuts. The buyers alleged and the jury found that the plaintiff stopped using the huts after two years because they were worthless. The jury awarded damages under U.C.C. section 2-714(2) for the decrease in value, and under U.C.C. section 2-715 for lost profits. Additionally, the trial court allowed the jury to consider, as items of consequential damages, interest on a purchase price loan and the cost of installing the defective huts. The court of appeals disagreed. It held that since the warranty was breached after the interest and installation expenses were incurred, the requisite causal connection between the breach and the loss was lacking.

However, the Iowa Supreme Court thought differently.¹⁸⁵ Turning first to the issue of interest, the court drew a distinction between a buyer who retains the goods and one who revokes acceptance or rejects the goods.¹⁸⁶ With respect to the former, the court determined that as a matter of policy (what policy we are never told) interest is not recoverable.¹⁸⁷ Why not, however, permit the buyer to recover interest on that portion of the purchase price which is effectively rebated in the form of diminished value damages under section 2-714(2)?¹⁸⁸ To the court's credit, this is seen as an option. To its discredit, it is rejected as too difficult to ascertain.¹⁸⁹ Turning next to the cost of installation, the court held that it may be recovered provided the seller was credited with whatever value or benefit the buyer received.

A final observation: rather than remand for an inevitable second trial, buyers were given the opportunity to file a remittitur in an amount equal to the interest

recovery of benefit of the bargain damages). For more on this case see *supra* notes 150–56 and accompanying text.

184. 7 U.C.C. Rep. Serv. 2d (Callaghan) 469 (Iowa 1988).

185. Regardless of the type of consequentials involved, there must be a showing that the seller at the time of contracting had reason to know of the possible loss. U.C.C. § 2-715(2)(a). Although the jury was never instructed on this requirement, the point was not raised on appeal.

186. The seller argued that no expense could be recovered if it would have been incurred in spite of the breach. If this narrow view of consequentials had been accepted by the court, the distinction drawn would have been unnecessary.

187. What policy considerations mandate that interest should be recoverable when the goods are returned to the seller is equally unclear. The opinion is helpful in that it does contain quite a number of citations to cases on both sides of the issue.

188. A portion of the interest expense will be returned to the buyer in the guise of statutory prejudgment interest which, in Iowa, accrues from the date of the commencement of the action. Iowa Code § 535.3 (1987).

189. 7 U.C.C. Rep. Serv. 2d (Callaghan) at 477.

cost and one-half the installation cost. The court's ultimate disposition of the appeal reflects a refreshing pragmatism that should serve as a lesson to others.

*Schmaltz v. Nissen*¹⁹⁰ involved a sale of corn seed where there were disclaimers of warranties and limitations on damages. The buyer argued unconscionability under U.C.C. sections 2-302(2) and 2-719, because he was left with the dismally inadequate remedy of return of the purchase price when the defective seed did not produce a crop. A similar case was decided in favor of the buyer-farmer in South Dakota in 1985¹⁹¹ but was overruled by statute in 1986.¹⁹² However, in *Schmaltz*, the Supreme Court of South Dakota held that the 1986 legislation should not be applied retroactively since the cause of action arose in 1981. The 1986 legislation did not specifically provide that it was to apply retroactively, so the court affirmed the decision of the trial court, holding the disclaimer of warranties and limitation of damages unconscionable.

The court analyzed the situation as one of unequal bargaining power, and found that the buyer-farmers were not in a position to bargain for more favorable terms.¹⁹³ At a loss for a remedy in a case that presented a sympathetic buyer, the court found unconscionability even in the face of contrary legislative intent. The court's opinion, read with the two concurring opinions, seems to suggest that warranty exclusions on seed are unconscionable virtually as a matter of law.¹⁹⁴ Presumably this attitude by the court is what gave rise to the express legislative abrogation in 1986.

*Envirotech Corp. v. Halco Engineering, Inc.*¹⁹⁵ reexamines the much-debated question of what happens when a contract contains both a "limited remedy" provision and an exclusion of consequential damages, and the limited remedy fails in its essential purpose. The Virginia Supreme Court sided with those courts which have respected consequential damage exclusions even where lim-

190. 431 N.W.2d 657, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1061 (S.D. 1988).

191. See *Hanson v. Funk Seeds Int'l*, 373 N.W.2d 30, 41 U.C.C. Rep. Serv. 2d (Callaghan) 1244 (S.D. 1985).

192. The new law provides: "The ruling in . . . *Hanson v. Funk Seeds International* . . . is hereby abrogated." 1986 S.D. Laws 410.

193. In two other cases decided during this survey period buyer-farmers did not fare as well. See *Peacock v. Ciba-Geigy Corp.*, 8 U.C.C. Rep. Serv. 2d (Callaghan) 688 (E.D. Ark. 1980) (exclusion of consequentials in the directions for use of herbicide was not unconscionable); *Earl Brace & Sons v. Ciba-Geigy Corp.*, 708 F. Supp. 708, 8 U.C.C. Rep. Serv. 2d (Callaghan) 690 (W.D. Pa. 1989) (same).

194. The concurring opinion of Justice Sabers, for example, attacks the crafty ways in which the packaging industry tries to bypass the U.C.C. requirement of conspicuousness in warranty disclaimers. It is suggested that a possible method for making these disclaimers conscionable and giving the buyer a real choice is to sell a product with a warranty for x amount, and to sell the same product without a warranty for the same amount less the value of the warranty. 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1073.

195. 234 Va. 583, 364 S.E.2d 215, 6 U.C.C. Rep. Serv. 2d (Callaghan) 1494 (1988).

ited remedies have failed.¹⁹⁶ The court held that it should not “rewrite the agreement”¹⁹⁷ of the parties.

Seller's Money Remedies

*North American Foreign Trading Corp. v. Direct Mail Specialist*¹⁹⁸ considered a seller's right to recover prejudgment interest on the unpaid portion of the contract price as incidental damages.¹⁹⁹ North American Foreign Trading Corp. (“NAFTC”) entered into an agreement to sell 164,968 units of a blackjack game to Direct Mail Specialist (“DMS”). DMS gave NAFTC a \$100,000 deposit to be applied only to the last shipment. DMS repudiated the contract after NAFTC had delivered only 60,000 units. NAFTC commenced this action shortly thereafter, in late 1983. According to NAFTC, its attempts to resell the undelivered units were largely unavailing until mid-1986 when a single purchaser began buying the units at a price below the original price. Before the district court was NAFTC's motion for a determination of the proper method of calculating the amount of prejudgment interest to which it would be entitled should it prevail.

The court had two methods to choose from. NAFTC urged that interest was recoverable on the full contract price until the resale in mid-1986 and thereafter on the difference between the contract price and the resale price. DMS, on the other hand, took the position that interest was permitted on the net amount of damages only, that is, the contract price less the amount received upon resale.²⁰⁰ The court agreed with NAFTC.²⁰¹ Relying on the language of U.C.C. section

196. This survey period saw the division of authority grow even greater. *Compare* Fidelity & Deposit Co. of Maryland v. Krebs Engineers, 859 F.2d 501, 7 U.C.C. Rep. Serv. 2d (Callaghan) 89 (7th Cir. 1988) (exclusion of consequential held to be invalid) *and* Andover Air Ltd. Partnership v. Piper Aircraft Corp., 7 U.C.C. Rep. Serv. 2d (Callaghan) 1494 (D. Mass. 1989) (withdrawn as a result of settlement) *with* Employers Ins. v. Suwanee River SPA Lines, Inc., 866 F.2d 752, 8 U.C.C. Rep. Serv. 2d (Callaghan) 659 (5th Cir. 1989) (exclusion of consequential remains valid). *See generally* Foss, *When to Apply the Doctrine of Failure of Essential Purpose to an Exclusion of Consequential Damages: An Objective Approach*, 25 Duq. L. Rev. 551 (1987) and Mather, *Consequential Damages When Exclusive Repair Remedies Fail: Uniform Commercial Code Section 2-719*, 38 S.C.L. Rev. 673 (1987).

197. 234 Va. at 593, 364 S.E.2d at 220, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1502.

198. 697 F. Supp. 163, 8 U.C.C. Rep. Serv. 2d (Callaghan) 1055 (S.D.N.Y. 1988).

199. Authorization for the seller's recovery of incidental damages is found in U.C.C. § 2-710.

200. If the three-year delay was reasonable, the measure of NAFTC's recovery would be the difference between the resale price and the contract price under U.C.C. § 2-706. DMS argued that the applicable New York statute restricted any computation of interest to this amount. *See* N.Y. Civ. Prac. Law § 5001(a) (McKinney 1963) (“Interest shall be recovered upon a sum awarded because of a breach of performance of a contract. . .”).

201. The court finessed its way around the limiting New York statute by juggling labels. Rather than label the time value of money loss as statutory damages, it considered it “incidental” damages recoverable under the Code without regard to any external statute. The court did, however, view the statute as setting the appropriate rate of interest.

2-709,²⁰² it held that interest could be recovered on the contract price (less the \$100,000 deposit) "from the date of breach until the time at which the seller could reasonably have resold the goods with reasonable effort for a reasonable price."²⁰³

Despite its inconsistency with the language of New York's prejudgment interest statute, the decision makes good sense. If a remedy is to substitute for performance,²⁰⁴ the seller's actual ability to resell must be considered. The assumption underlying U.C.C. sections 2-706 and 2-708 is that a ready market for the goods exists. Thus, the buyer should have to pay interest on only that portion of the original contract price which cannot be recaptured from the marketplace. Where this assumption proves incorrect, the Code makes the buyer responsible for the contract price and liability for delay damages for the buyer's nonpayment should follow. This is true even if the buyer's principal obligation is subsequently modified because of a later resale. To hold otherwise would have the untoward effect of reducing the seller's overall recovery if the invitation to resell under U.C.C. section 2-709(2) is accepted.²⁰⁵

On rare occasion, a case will come to trial before the time for the seller's tender of the goods. If the market price of the goods is needed to calculate the seller's damages, U.C.C. section 2-723(1) directs that the relevant date for its determination is "the time when the aggrieved party learned of the repudiation." This provision was considered in *Manchester Pipeline Corp. v. Peoples Natural Gas Co.*²⁰⁶

Peoples Gas allegedly contracted with Manchester to purchase natural gas. The contract was to run for a period of 10 years and contained several provisions which are commonly found in long-term gas purchase contracts and which impact on the price during its term.²⁰⁷ Soon after negotiations had been completed, Peoples Gas perceived a "softening" of the market, denied the contract's existence, and refused to buy. Manchester then attempted to mitigate its damages by entering into a one-year "spot market" contract with a third party.²⁰⁸ The trial court instructed the jury that it was to determine the seller's damages based on the difference between the market price at the time and place Peoples Gas would have taken delivery of the gas and the agreed price.

202. According to U.C.C. § 2-709(1)(b), the seller may recover the full contract price if it "is unable after reasonable effort to resell [the goods] at a reasonable price or the circumstances reasonably indicate that such effort would be unavailing."

203. 697 F. Supp. at 167, 8 U.C.C. Rep. Serv. 2d (Callaghan) at 1060.

204. See U.C.C. § 1-106(1) ("The remedies provided by this Act shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed. . . .").

205. The seller would lose the difference between the amount of interest computed on the full contract price and the amount computed on the contract price/resale price differential for the period during which it was unable to effectuate a reasonable resale.

206. 862 F.2d 1439, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1000 (10th Cir. 1989).

207. One such provision was the so-called "market-down" or "market-out" provision which permits the buyer to reduce the price for gas taken in order to remain competitive in the gas market.

208. A spot market contract has a term from one month to one year, and provides the seller with a lower price than it would get under a long-term contract.

The Tenth Circuit reversed, holding that the district court's reliance on the Official Comment to U.C.C. section 2-723 to justify a departure from its mandate was misplaced.²⁰⁹ Market price should be determined at the time Manchester learned of the repudiation.²¹⁰ Still to be decided was the controlling market. At trial, the parties seemed to assume that damages should be decided by reference to the spot market price under a spot market contract. Not so said the Tenth Circuit. The comparison should be with the higher market price of gas under a similar long-term contract.²¹¹ One wonders whether the decision would have been the same if the higher price was obtainable by a dissimilar spot market sale.

Statutes of Limitations

This year, the courts continued to misinterpret and misapply the "future performance" warranty provision of U.C.C. section 2-725(2).²¹² Lining up behind the other jurisdictions, the Alabama Supreme Court, in a case of first impression, held that a repair and replacement new car warranty does not explicitly extend to the future performance of the car.

In *Tittle v. Steel City Oldsmobile BMC Truck, Inc.*,²¹³ the plaintiff had purchased an Oldsmobile covered by General Motor's 12 month/12,000 mile "1981 New Car Warranty."²¹⁴ The warranty provided that the dealer, Steel City, would repair and adjust defects within the agreed-upon period. The car turned out to have numerous defects which were never successfully repaired.

209. The Comment instructs that "[t]his section is not intended to exclude the use of any other reasonable method of determining market price or of measuring damages if the circumstances of the case make this necessary." Uniform Commercial Code § 2-723 Official Comment. The district court pointed to the uniqueness of gas purchase agreements and the volatility of the gas market as reasons for allowing the jury to speculate on future market conditions.

210. In the court's opinion, the rule of U.C.C. § 2-723 has "the virtue of certainty." 862 F.2d at 1447, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1012.

211. The only rationale given was that long-term contracts are more predictable. The court summarily rejected the contrary position taken by at least one scholar who argues that the controlling comparison price should be the spot price. *Id.* at 1448 n.12. 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1013 n.12 (citing Jackson, "Anticipatory Repudiation" and the Temporal Element of Contract Law: An Economic Inquiry into Contract Damages in Cases of Prospective Nonperformance, 31 Stan. L. Rev. 69 (1978)).

212. U.C.C. § 2-725(2) provides:

A cause of action accrues when the breach occurs regardless of the aggrieved party's lack of knowledge of the breach. A breach of warranty occurs when tender of delivery is made, except that where a warranty explicitly extends to future performance of the goods and discovery of the breach must await the time of such performance the cause of action accrues when the breach is or should have been discovered.

213. 8 U.C.C. Rep. Serv. 2d (Callaghan) 701 (Ala. 1989).

214. Tittle also purchased additional protection from his lender, General Motors Acceptance Corporation ("GMAC"), in the form of a supplemental warranty for 36 months or 36,000 miles.

Eventually, Tittle sued for breach of warranty,²¹⁵ and the trial court granted the defendants' motion for a summary judgment²¹⁶ based upon the statute of limitations defense. The Alabama Supreme Court framed the U.C.C. section 2-725(2) issues on appeal as: did the repair warranty explicitly extend to the car's future performance?; and, if not, did a breach of the repair warranty occur upon tender of the car or upon failure to subsequently repair the defects?

After reviewing the case law from other jurisdictions, the court adopted the majority view that such warranties do not guarantee the future performance of the car.²¹⁷ If anything, they imply "that the goods may fall into disrepair or otherwise malfunction. No warranty that the goods will not, is to be inferred from the warranty to make needed repairs."²¹⁸ Since the warranty did not extend to the car's future performance, that exception to the time of tender rule was inapplicable. As to the issue of whether the statute began to run upon tender or when the promise to repair was breached, the court found the answer in the subsection's "plain meaning."²¹⁹ The repair or replace clause is a warranty, but it does not explicitly extend to the future performance of the good. Therefore, it must run from the time of tender.

In *Crouch v. General Electric Co.*,²²⁰ the United States District Court for the Southern District of Mississippi, applying Mississippi law, held that neither of the two express warranties covering a helicopter engine explicitly extended to future performance. Again, since the statute of limitations began to run upon tender of the helicopters, the plaintiff's six-year-old personal injury claim was time-barred. The *Crouch* court relied upon many of the same cases cited in *Tittle* to reach the same conclusion that a "maximum term of liability of

215. The defendants were Steel City Oldsmobile GMC Truck, Inc., General Motors Corporation ("GM"), and GMAC. Query whether U.C.C. § 2-725 is even applicable where the warranty is given by someone other than the seller?

216. Only Steel City and GM filed motions; Tittle's case remained pending against GMAC.

217. See, e.g., *Ontario Hydro v. Zallea Sys.*, 569 F. Supp. 1261, 36 U.C.C. Rep. Serv. (Callaghan) 1222 (D. Del. 1983); *Voth v. Chrysler Motor Corp.*, 218 Kan. 644, 545 P.2d 371, 18 U.C.C. Rep. Serv. (Callaghan) 954 (1976); *Owens v. Patent Scaffolding Co.*, 77 Misc. 2d 992, 354 N.Y.S.2d 778, 14 U.C.C. Rep. Serv. (Callaghan) 610 (1974), *rev'd on other grounds*, 50 A.D.2d 866, 376 N.Y.S.2d 948, 18 U.C.C. Rep. Serv. (Callaghan) 699 (1975); *Carabello v. Crown Controls Corp.*, 659 F. Supp. 839, 4 U.C.C. Rep. Serv. 2d (Callaghan) 101 (D. Colo. 1987); *New England Power Co. v. Riley Stoker Corp.*, 20 Mass. App. 25, 477 N.E.2d 1054, 40 U.C.C. Rep. Serv. (Callaghan) 1735 (1985).

But see *Standard Alliance Indus. v. Black Clawson Co.*, 587 F.2d 813, 25 U.C.C. Rep. Serv. (Callaghan) 65 (6th Cir. 1978), *cert. denied*, 441 U.S. 923 (1979) (repair or replace warranty which extends a specific period of time explicitly warrants future performance so that the cause of action accrues when the buyer discovered or should have discovered the defect within the warranty period).

218. 8 U.C.C. Rep. Serv. 2d (Callaghan) at 709.

219. *Id.* at 712.

220. 699 F. Supp. 585, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1113 (S.D. Miss. 1988).

warranty” provision²²¹ is a repair and replace warranty, and the maximum term simply indicates the time the buyer has to exercise his remedy.²²²

The *Tittle* and *Crouch* courts (as have others) failed to realize that the promise to repair or replace, if it is any *one* thing, is actually a remedy, not a warranty.²²³ Yet it makes no sense to speak of a remedy without a breach.²²⁴ Perhaps the obligation is simply another way of saying the goods will function properly for the term of the repair or replace warranty. In other words, underlying the remedy is a warranty of future performance.²²⁵

The holding of *Tittle* on when the statute of limitations begins to run is contrary to common sense. Imagine an optimistic car buyer with a 5 year/60,000 mile warranty. If the statute begins to run from the time of tender, the buyer cannot sue on the contract even though he still has one year of protection remaining. There is no compelling policy reason for this result.

In *Hanscome v. Perry*,²²⁶ the appellant, an interior decorator, sued the manufacturer and wholesaler for negligence after a damaged console was delivered to her customer. The action was dismissed by the trial court as time-barred by the three-year tort statute of limitations. She filed a second suit for breach of contract, and express and implied warranties. That too was dismissed; by then four years had passed since the delivery of the console.

221. The warranty in *Crouch* read as follows: “The warranty on each of the . . . 170 . . . engines shall cease three (3) years from the date the Government accepts the first engine. . . .” In the event of a defect, GE is only required to repair or replace the part. *Id.* at 593–94, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1121.

222. The plaintiff’s implied warranty claim was dismissed in a footnote; an implied warranty obviously cannot explicitly refer to future performance of the good. *Id.* at 593 n.8, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1121 n.8.

Courts and commentators agree that implied warranties cannot explicitly extend to the future performance of the good as a matter of law. However, under pre-Code law prospective, implied warranties could extend to the future performance of the goods. The statute of limitations did not begin to run until there was knowledge of the breach. Comment, *The Sales Statute of Limitations in the Uniform Commercial Code—Does it Preclude Prospective Implied Warranties?* 37 Fordham L. Rev. 247, 250 (1968).

223. Under U.C.C. § 2-313(1)(a), “[a]ny affirmation of fact or promise made by the seller to the buyer which relates to the goods and becomes part of the basis of the bargain creates an express warranty that the goods shall conform to the affirmation or promise.” The promise to repair or replace relates to the seller’s undertaking, not to the condition of the goods.

224. See U.C.C. § 1-106(1) (“The remedies provided by this Act shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed. . . .”) (emphasis added).

225. According to White and Summers, “many courts would interpret this [discussing a typical new car warranty] as a warranty that explicitly extends to future performance and would therefore grant four years from the time of the occurrence of the defect.” 1 J. White & R. Summers, *Uniform Commercial Code*, 553 (3d ed. 1988). Yet in an earlier discussion it is suggested such warranties do not explicitly extend to the future since “all warranties in a sense apply to the future performance of goods.” *Id.* at 551. The exception would swallow the rule.

226. 75 Md. App. 605, 542 A.2d 421, 7 U.C.C. Rep. Serv. 2d (Callaghan) (1988).

On appeal, the decorator relied on the earlier tort filing to invoke the tolling provision of U.C.C. section 2-725(3).²²⁷ The Maryland Court of Special Appeals affirmed the dismissal. In order to meet the exception, the first action must have been "for the same breach," that is, another contract claim. By its own terms, the section can only apply to actions for breach of contract or warranty. U.C.C. section 2-725 has no bearing on tort and other unrelated claims.

Two final cases bear witness to the fact that not all exceptions are easily found within the four corners of the statute. The North Carolina Court of Appeals held that U.C.C. section 2-725 does not apply to arbitration proceedings.²²⁸ The court relied on the definition of "action"²²⁹ to find that it covers only judicial proceedings, and distinguished arbitration as an out-of-court proceeding.²³⁰ Lastly, the Seventh Circuit held that a five-year-old counterclaim was not barred by U.C.C. section 2-725(1), given that a specific statutory exception to that provision existed under Illinois law.²³¹

ARTICLE SEVEN (DOCUMENTS OF TITLE)

U.C.C. section 7-209(1) gives the warehouseman a lien on bailed goods "covered by a warehouse receipt." Section 7-202(2) lists the terms that must appear in a warehouse receipt. Suppose a warehouseman issues a receipt that does not contain all of the required terms. Does that mean that the warehouseman has no lien on the bailed goods under section 7-209? Under these circumstances the New Jersey Superior Court Appellate Division upheld the warehouseman's lien in *Evergreen International Services Corp. v. Wallant International Trade, Inc.*²³² In that case, the bailor entered into an arrangement with the warehouseman under which inventory was stored in the warehouse, removed from time to time, and replaced with additional inventory. The warehouseman issued invoices for each delivery to the warehouse. Eventually, the bailor refused to pay storage charges claiming that some of its inventory was missing from the warehouse. In the ensuing litigation, the bailor argued that the

227. U.C.C. § 2-725(3) provides: "[W]here an action commenced within the time limited by subsection (1) is so terminated as to leave available a remedy by another action for the same breach such other action may be commenced after the expiration of the time limited and within six months after the termination of the first action. . . ."

228. *Cameron v. Griffith*, 90 N.C. App. 164, 370 S.E.2d 704, 7 U.C.C. Rep. Serv. 2d (Callaghan) 486 (1988). This holding may be dicta since the majority opines that an arbitrator's decision is not reviewable by a court of law. *Id.* at 165, 370 S.E.2d at 705, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 487.

229. U.C.C. § 2-725(1) and U.C.C. § 1-201(1).

230. Query whether this result is correct when U.C.C. § 1-201(1) includes "any other proceedings in which rights are determined"?

231. *Bethlehem Steel Corp. v. Chicago Eastern Corp.*, 863 F.2d 508, 7 U.C.C. Rep. Serv. 2d (Callaghan) 399 (7th Cir. 1988).

The Illinois Statute (Ill. Rev. Stat. ch. 110, para. 13-207 (1987) provided that the defendant's counterclaim was not time-barred as long as the plaintiff's claim arose before the cause of action brought as counterclaim was barred.

232. 288 N.J. Super. 477, 550 A.2d 175, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1603 (1988).

warehouseman did not have a lien on the goods remaining in the warehouse because the invoices did not contain all of the terms required to be in a warehouse receipt. The trial court held that the warehouseman had a lien. On appeal, the court affirmed. It held that the invoices need only identify the bailor and warehouseman, and describe the goods and their location,²³³ which these invoices did. The sanction for omitting required terms was only that specified in subsection 7-202(2): liability “for damages caused by the omission to a person injured thereby.”

Under article 7, the duty of care owed by carriers and warehousemen toward goods in their possession is essentially the same: they must exercise the same degree of care as a reasonably careful man would exercise under like circumstances.²³⁴ However, article 7 does not displace any state law rule that imposes a higher duty of care.²³⁵ Some states hold either carrier or warehouseman or both to higher standards of care.²³⁶ Consequently, it is possible that in a given state the standards of care for carriers and warehousemen will not be the same. This circumstance creates a problem where a bailee of goods is transporting and storing the goods at different times. If the goods are lost, destroyed, or damaged while in its possession, is the bailee liable as a carrier or as a warehouseman? The Nebraska Supreme Court discussed this issue in *Fisher Corp. v. Consolidated Freightways, Inc.*²³⁷ Under Nebraska law, a carrier is liable for any losses to the goods with certain exceptions not applicable in this case. A warehouseman, however, is liable only for losses caused by his negligence. In this case, Consolidated Freightways (“Consolidated”) received a quantity of VCRs for interstate shipment to the buyer. Upon arrival, the buyer rejected the goods because they duplicated earlier deliveries. Consolidated returned the goods to its terminal for storage until it received instructions from the seller. Some time later, the seller requested that the goods be shipped back to it. During the time the goods were stored at Consolidated’s terminal, unknown persons stole some of the goods. It could not be ascertained whether the theft had occurred before or after Consolidated received the seller’s instructions to reship. The trial court left it to the jury to decide whether Consolidated was liable as a carrier or

233. This holding was based upon a New Jersey case decided under the Uniform Warehouse Receipts Act, which was superseded by U.C.C. Article 7. *See* N.J. Title Guar. & Trust Co. v. Rector, 75 A 931, 76 N.J. Eq. 587 (1910).

234. U.C.C. § 7-204(1) (warehouseman’s duty of care); U.C.C. § 7-309(1) (carrier’s duty of care).

235. U.C.C. § 7-204(4) and Official Comment; U.C.C. § 7-309(1) and Official Comment.

236. In many states, the carrier is an insurer of the safety of the goods except for acts of God or public enemies, fault of the shipper, inherent defect, or causes excepted by contract. R. Riegert & R. Braucher, Documents of Title 39 (3d ed. 1978). These state rules apply to intrastate shipments of goods. 1 S. Sorkin, Goods in Transit § 1.24[1] (1988). Additionally, federal legislation modifies some aspects of the carriers’ liability. *See generally* 10 S. Williston, A Treatise on the Law of Contracts § 1083 (3d ed. 1967); Sorkin, *supra*.

Several states also impose higher standards of care on warehousemen. *See* Riegert & Braucher, *supra* note 236 at 30 and n.22.

237. 230 Neb. 832, 434 N.W.2d 17, 8 U.C.C. Rep. Serv. 2d (Callaghan) 148 (1989). Prof. Tang Thi Thanh Trai Le contributed to the discussion of this case.

warehouseman, and the jury returned a verdict for Consolidated. On appeal the court affirmed, finding no error. In the course of its opinion, the court discussed whether Consolidated was liable as a carrier or a warehouseman. Citing cases from other jurisdictions, the court ruled that once the consignee of goods (here, the buyer) refused to accept a tender of delivery by the carrier, the carrier ceases to be a carrier and becomes a warehouseman. Thus when the buyer rejected the goods, Consolidated became a warehouseman and was liable only for losses attributable to its own negligence. The court then ruled that when the carrier-turned-warehouseman accepts instructions from the bailor (here, the seller) to ship the goods to the specified location, he again becomes a carrier.

ARTICLE SIX (BULK SALES)

For the most part, the article 6 cases decided during the survey period grappled with issues that are familiar to bulk sales aficionados. The provision that spawned the most reported cases during this survey period is section 6-103(3), which excepts from article 6 "[t]ransfers in settlement or realization of a lien or other security interest." This exception is no stranger to the appellate courts, having given rise to a number of different interpretations.²³⁸

Aligning itself with several other courts that have considered the issue, the Kentucky Court of Appeals held that section 6-103(3) exempts from article 6 the transfer of collateral encumbered by a perfected security interest when all the consideration paid by the transfer goes to satisfy the secured debt, regardless of whether the collateral is transferred to a person other than the secured party.²³⁹ Inasmuch as the secured party's priority over the unsecured creditors would have entitled the secured party to reach the entire proceeds of an article 9 foreclosure sale, the unsecured creditors also are not entitled to share in the proceeds when the collateral is liquidated at a bulk sale.

Affording similar deference to article 9 security interests, a recent Oklahoma opinion applied section 6-103(3) to a noncomplying bulk transfer of collateral when the proceeds exceeded the size of the secured indebtedness.²⁴⁰ The defendant bought the collateral (inventory of an auto parts store) for \$55,000, of which \$51,027.90 was paid to the secured party in full satisfaction of the secured debt. Interpreting section 6-103(3) to exclude a bulk sale "only if settlement of a security interest is the purpose of the transfer,"²⁴¹ the court held that payment of the secured debt was "merely an incident of the sale of the parts store assets to defendant"²⁴² and therefore that the bulk transfer was not within

238. For a synopsis of the various constructions that courts have given to § 6-103(3), see Harris, *Practicing Under Existing Bulk Sales Law—And a Look at the Future of Article 6*, 22 U.C.C. L.J. 195, 204 (1990).

239. *River City Prods., Inc. v. AEJ, Inc.*, 774 S.W.2d 452, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1600, 9 U.C.C. Rep. Serv. 2d (Callaghan) 1319 (Ky. Ct. App. 1989).

240. *Mid-America Indus., Inc. v. Ketchie*, 767 P.2d 416, 7 U.C.C. Rep. Serv. 2d (Callaghan) 1174 (Okla. 1989).

241. 767 P.2d at 418, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1176.

242. *Id.* at 419, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1177.

the exception of section 6-103(3). As a consequence of his failure to comply with article 6, the noncomplying buyer-defendant became personally liable for the value of the property transferred or the amount paid therefore.²⁴³ Although that amount was \$55,000, the court reduced the buyer's liability by the amount paid to the secured party. Its reasoning was similar to that of the Kentucky Court of Appeals: article 6 neither impairs a valid article 9 security interest nor affects article 9 remedies.²⁴⁴ Accordingly, the holder of a perfected security interest in the transferred property is entitled to recover the proceeds of the sale.

The West Virginia Supreme Court of Appeals recently addressed yet another variation of this theme.²⁴⁵ Kizer granted a security interest in existing and after-acquired inventory to Malone & Hyde, Inc. ("M&H"). Among the debts secured by the collateral was Kizer's obligation to pay for inventory he bought from M&H. Following his default, Kizer signed a Notice of Default and Transfer of Possession Agreement, pursuant to which Kizer transferred to M&H certain property, including the collateral, in return for a release of his liability to M&H. Adopting the view that the exception in section 6-103(3) applied only when the entire consideration is used to satisfy the secured debt, the court held that section 6-103(3) excluded the transfer at issue from article 6. In so holding, the court acknowledged that "an unsecured creditor of the transferor is not prejudiced by a transfer of assets that satisfies the security interest of a transferee who already has priority over the unsecured creditor."²⁴⁶

Revised article 6, which has been approved for enactment by the American Law Institute and the National Conference of Commissioners on Uniform State Laws, clarifies the applicability of article 6 to sales of collateral.²⁴⁷ It specifically provides that revised article 6 does not apply to (a) a transfer of collateral to a

243. Article 6 provides that a noncomplying bulk transfer is "ineffective" against the creditors of the transferor. U.C.C. §§ 6-104(1), 6-105. In the view of some courts, the only remedies available to aggrieved creditors are those that enable the creditors to reach the transferred goods. Other courts permit the imposition of personal liability on the noncomplying transferee in bulk. *See generally* Harris, *supra* note 1, at 216–17. The opinion under discussion relies on *Darby v. Ewing's Home Furnishings*, 278 F. Supp. 917, 5 U.C.C. Rep. Serv. (Callaghan) 198 (W.D. Okla. 1967), which relied upon Oklahoma's enactment of optional § 6-106 as a ground for imposing personal liability on the noncomplying buyer.

244. *See Mid-American Indus.*, 767 P.2d at 420, 7 U.C.C. Rep. Serv. 2d (Callaghan) at 1179; *River City Prods.*, 774 S.W.2d at 453, 9 U.C.C. Rep. Serv. (Callaghan) at 1322. For an exhaustive discussion of the effect of article 6 on article 9 security interests, see Harris, *The Interaction of Articles 6 and 9 of The Uniform Commercial Code*, 39 Vand. L. Rev. 179 (1986).

245. *Peerless Packing, Inc. v. Malone & Hyde, Inc.*, 376 S.E.2d 161, 8 U.C.C. Rep. Serv. 2d (Callaghan) 196 (W. Va. 1988).

246. 376 S.E.2d at 165, 8 U.C.C. Rep. Serv. 2d (Callaghan) at 201. In addition, the court treated the transaction as a retention of collateral by the secured party pursuant to § 9-505, notwithstanding that the Transfer of Possession Agreement authorized the secured party to sell the collateral at a private sale after a reasonable period. The court also affirmed the directed verdict entered in favor of the secured party on the creditor's claim of unjust enrichment.

247. Revised article 6 (cited herein as "revised U.C.C. § ") was promulgated for those states that are reluctant to follow the sponsors' primary recommendation that article 6 be repealed and bulk sales left unregulated. Highlights of the revised article are summarized in Frisch & Wladis, *General Provisions, Sales, Bulk Transfers, and Documents of Title*, 44 Bus. Law. 1445, 1496–97

secured party pursuant to section 9-503;²⁴⁸ (b) a sale of collateral pursuant to section 9-504;²⁴⁹ (c) retention of collateral pursuant to section 9-505;²⁵⁰ and, (d) a sale of an asset encumbered by a security interest if (i) all the proceeds of the sale are applied to the secured debt or (ii) the security interest is enforceable against the asset after it has been sold to the buyer and the net contract price is zero.²⁵¹ Additionally, the revised article excludes a sale of assets having a value, net of liens and security interests, of less than \$10,000.²⁵² This exception would have excluded the transaction in the Oklahoma case altogether, on the theory that the recovery to creditors from relatively small sales is unlikely to justify the costs of compliance with the article.²⁵³

A final case worthy of note is the second appeal in *Stone's Pharmacy, Inc. v. Pharmacy Accounting Management, Inc.*²⁵⁴ That case revolved around a typical fact pattern: the transferor in bulk had filed for bankruptcy.²⁵⁵ Applying Texas law, the Eighth Circuit held that the bankrupt transferor was not a necessary party to an aggrieved creditor's action against a noncomplying bulk buyer and that the automatic stay did not affect the creditor's right to seek to assemble all the transferred assets for proper distribution. Although the transferor's bankruptcy trustee might have enjoyed the right to avoid the bulk transfer under the Bankruptcy Code,²⁵⁶ the court observed that the transferor's bankruptcy trustee appears not to have pursued the bulk transfer claim in the bankruptcy proceeding or otherwise. Had the trustee done so, the aggrieved creditor probably would have been precluded from asserting its claim against the noncomplying transferee. Nothing in revised article 6 would change the result in *Stone's Pharmacy*.

(1989). For a more detailed discussion, see Harris, *supra* note 1, *passim*. Utah has enacted revised article 6.

248. Revised U.C.C. § 6-103(3)(b).

249. Revised U.C.C. § 6-103(3)(c).

250. Revised U.C.C. § 6-103(3)(d). This would have excluded the transaction in West Virginia case.

251. Revised U.C.C. § 6-103(3)(e)(i) & (ii). Subsection (i) would have excluded the transaction in Kentucky case. Subsection (ii) excludes sales in which the only consideration passing to the seller is the assumption of the secured debt.

252. Revised U.C.C. § 6-103(3)(1)(i).

253. See revised Uniform Commercial Code § 6-103 Official Comment 7.

254. 875 F.2d 665, 8 U.C.C. Rep. Serv. 2d (Callaghan) 1179 (8th Cir. 1989). The prior appeal appears at 812 F.2d 1063, 3 U.C.C. Rep. Serv. 2d (Callaghan) 206 (8th Cir. 1987).

255. For example, this was the case in *Peerless Packing, Inc. v. Malone and Hyde Inc.*, 376 S.E.2d 161, 8 U.C.C. Rep. Serv. 2d (Callaghan) 196 (W. Va. 1988).

256. 11 U.S.C. § 544(b) (1988). Section 6-107(8) of revised article 6 attempts to preclude a bankruptcy trustee from attacking a noncomplying bulk sale. It provides in part that "[a] buyer's failure to comply with the requirements of Section 6-104(1) does not . . . (ii) render the sale ineffective, void, or voidable . . ."