1998

Sales

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This Article reviews recent case law under Article 2, Sales, of the Uniform Commercial Code (U.C.C.).

SCOPE OF ARTICLE 2

In *Architectronics, Inc. v. Control Systems, Inc.*,[1] the court declined to apply the U.C.C. Article 2 four-year statute of limitations[2] to licenses pertaining

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1. 935 F. Supp. 425, 33 U.C.C. Rep. Serv. 2d (CBC) 714 (S.D.N.Y. 1996).
2. U.C.C. §2-725(1) (1995).

to the development and distribution of computer software.[3] Architectronics, Inc. (Architectronics) entered a software development and license agreement with Control Systems, Inc. (CSI), a graphics board manufacturer, pursuant to which CSI was to develop a software display driver for CSI's graphics board using Architectronics' technology. CSI would own the copyright for the software under the agreement. Concurrently, CSI gave Architectronics a license to copy and distribute the software to be developed. Shortly thereafter CSI backed out of the agreement and failed to develop the software. Some five years later, Architectronics sued for breach of the agreement. The court concluded that New York's six-year general statute of limitations for breach of contract actions applied.[4] It reasoned that the predominant element of the agreement was the license to copy and distribute the software.[5] The court held that license to be a transfer of intellectual property rights, not a sale of the software; therefore, U.C.C. Article 2 did not apply.[6]

The statute of limitations in the current draft of proposed U.C.C. Article 2B, which will govern software licensing agreements, provides that "[a]n action for breach of contract must be commenced within the later of four years after the right of action accrues or one year after the breach was or should have been discovered, but the action may not be commenced more than five years after the right of action accrues."[7]

In *J.O. Hooker & Sons, Inc. v. Roberts Cabinet Co.*,[8] the Mississippi Supreme Court split a contract for residential renovation involving both a sale of goods and provision of services into two parts, applying the common law parol evidence rule to the services portion of the contract.[9] In *Hooker*, the general contract permitted the owner to keep old cabinets that were to be replaced, and provided that the general contractor, J.O. Hooker & Sons, Inc. (Hooker), was to bear the expense of moving the cabinets to a location designated by the owner. Hooker entered into a sub-contract with a cabinet maker, Roberts Cabinet Co. (Roberts), to tear out the old cabinets, furnish new cabinets, and perform miscellaneous carpentry work. A dispute developed, however, over whether the sub-contract obligated Roberts to move the old cabinets to a location designated by the owner. When the dispute could not be resolved, Hooker terminated the sub-contract, prompting Roberts to bring suit against Hooker. The trial court granted summary judgment for Roberts on liability and proceeded to a trial on

3. *Architectronics*, 935 F. Supp. at 431-32, 33 U.C.C. Rep. Serv. 2d (CBC) at 714.
4. *Id.* at 431, 33 U.C.C. Rep. Serv. 2d (CBC) at 722.
5. *Id.* at 432, 33 U.C.C. Rep. Serv. 2d (CBC) at 722.
6. *Id.*
7. *See* U.C.C. § 2B-705 (June 1, 1998). The 1998 Revised Draft may be found at the following URL: <http://www.law.upenn.edu/library/ulc/ulc.htm>.
8. 683 So. 2d 396, 32 U.C.C. Rep. Serv. 2d (CBC) 92 (Miss. 1996).
9. *Id.* at 400, 32 U.C.C. Rep. Serv. 2d (CBC) at 96.

damages.[10] Hooker appealed, arguing that there was a material issue of fact regarding Roberts' obligation to transport the old cabinets. The Mississippi Supreme Court affirmed.[11] The court declined to apply the parol evidence rule of U.C.C. section 2-202 because the dispute concerned the services component of the contract (transporting the old cabinets).[12] Instead, the court applied the more stringent common law parol evidence rule, thereby barring admission of Hooker's evidence.[13]

Other courts have used the approach of splitting a contract and applying Article 2 only to disputes involving the goods portion of the contract.[14] One may question the wisdom of doing so, however, when the result is the application of different versions of the parol evidence rule to the same written contract.

CONTRACT FORMATION

In 1962, the First Circuit issued the controversial decision of *Roto-Lith Ltd. v. F.P. Bartlett & Co.*,[15] which held that, in a battle of the forms situation, a buyer who accepts the goods after having received the seller's form accepts all of the seller's terms, including the boilerplate.[16] In 1997, the First Circuit overruled the *Roto-Lith* doctrine in a commercial context, in *Ionics, Inc. v. Elmwood Sensors, Inc.*,[17] while the Seventh Circuit, in effect, adopted the *Roto-Lith* doctrine in a consumer context in *Hill v. Gateway 2000, Inc.*[18]

In *Ionics*, Ionics, Inc. (Ionics), purchased sensors for its water dispensers from Elmwood Sensors, Inc. (Elmwood). The sensors allegedly caused fires, prompting Ionics to sue Elmwood for costs associated with the fires. Elmwood defended on the basis of a clause in its acknowledgment form limiting Ionics' remedies to repair of the goods or return of the purchase price. Each time Ionics purchased sensors from Elmwood, Ionics sent a purchase order containing a full remedies clause, and subsequently received Elmwood's responding acknowledgment. Ionics' purchase order stated that the order could be accepted "only on the exact terms" con-

10. *Id.* at 399, 32 U.C.C. Rep. Serv. 2d (CBC) at 94.
11. *Id.* at 403, 32 U.C.C. Rep. Serv. 2d (CBC) at 96.
12. *Id.* at 400, 32 U.C.C. Rep. Serv. 2d (CBC) at 95.
13. *Id.* at 400, 32 U.C.C. Rep. Serv. 2d (CBC) at 95-96.
14. *See e.g.*, JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE 3 n.4 (4th ed. 1995).
15. 297 F.2d 497, 1 U.C.C. Rep. Serv. (CBC) 73 (1st Cir. 1962).
16. The rationale of *Roto-Lith* was that a seller's acknowledgment of a buyer's purchase order that is conditioned on the buyer's assent to the seller's terms constitutes a counteroffer rather than an acceptance. When the buyer accepts the goods after receiving the seller's acknowledgment, it accepts the seller's counteroffer. *Id.* at 500, 1 U.C.C. Rep. Serv. (CBC) at 76. Further, the *Roto-Lith* court held that a seller's acknowledgment is conditional on assent to its terms if it "states a condition materially altering the obligation solely to the disadvantage of the offeror." *Id.*
17. 110 F.3d 184, 32 U.C.C. Rep. Serv. 2d (CBC) 1 (1st Cir. 1997).
18. 105 F.3d 1147, 31 U.C.C. Rep. Serv. 2d (CBC) 303 (7th Cir. 1997).

tained in the order.[19] Elmwood's acknowledgment form stated that Elmwood was willing to sell only on the terms contained in its form and that the acknowledgment was a counter-offer. Ionics accepted the sensors after receiving Elmwood's acknowledgment. Elmwood moved for partial summary judgment on the theory that its limited remedy clause was part of the contract. The district court both denied Elmwood's motion under U.C.C. section 2-207 and certified for appeal the question of whether it had properly applied U.C.C. section 2-207.[20]

The First Circuit affirmed the district court' decision finding that the contract was governed by U.C.C. section 2-207(3),[21] dealing with contracts formed by conduct "although the writings of the parties do not otherwise establish a contract."[22] The court reasoned that no contract was formed by Elmwood's acknowledgment because it was conditioned on assent to its terms, and Ionics' acceptance of the goods was not sufficient to constitute assent.[23] Instead, the court stated that "where the terms in two forms are contradictory, each party is assumed to object to the other party's conflicting clause."[24] The court expressly overruled *Roto-Lith*, finding that its rule was in conflict with "the clear dictates of the Uniform Commercial Code."[25]

In *Hill v. Gateway 2000, Inc.*,[26] the Seventh Circuit held that the seller's boilerplate arbitration clause, included with the shipped goods, was binding on the consumer buyer.[27] In *Hill*, the Hills telephonically agreed to purchase a computer system from Gateway 2000, Inc. (Gateway). When the computer arrived, the box contained Gateway's standard form agreement with boilerplate terms, including a standard arbitration clause and a provision stating that Gateway's terms would govern unless the computer was returned within thirty days. The Hills did not return the computer within that time, but later sued because of their dissatisfaction with the computer's performance. The district court refused to enforce the arbitration clause, finding insufficient evidence that the Hills had agreed to, or had adequate notice of, the clause.[28]

19. *Ionics*, 110 F.3d at 185, 32 U.C.C. Rep. Serv. 2d (CBC) at 2.
20. *Id.* at 187, 32 U.C.C. Rep. Serv. 2d (CBC) at 5.
21. *Id.*, 32 U.C.C. Rep. Serv. 2d (CBC) at 5.
22. U.C.C. § 2-207(3) (1995).
23. *Ionics*, 110 F.3d at 189, 32 U.C.C. Rep. Serv. 2d (CBC) at 8.
24. *Id.*
25. *Id.* The court clearly overruled the doctrine that, by accepting the goods, buyer accepts seller's terms. The other controversial aspect of *Roto-Lith*, the idea that a response materially altering an offer to the detriment of the offeror is an expressly conditional response under U.C.C. § 2-207(1), was not explicitly overruled, presumably because the facts did not implicate this rule.
26. 105 F.3d 1147; 31 U.C.C. Rep. Serv. 2d (CBC) 303 (7th Cir. 1997).
27. *Id.* at 1150, 31 U.C.C. Rep. Serv. 2d (CBC) at 309.
28. *Id.* at 1148, 31 U.C.C. Rep. Serv. 2d (CBC) at 305.

The Seventh Circuit vacated the district court's decision and remanded with instructions to compel the Hills to submit their dispute to arbitration.[29] Relying primarily on its recent decision in *ProCD, Inc. v. Zeidenberg*[30] the court held that the Hills' failure to return the computer within the time stated in Gateway's form bound the Hills to all of the terms in that form, including the unread arbitration clause.[31] In support of its decision, the court noted that many commercial transactions, such as the sale of cruise ship or air transportation tickets and insurance policies, follow a "payment first; terms later" pattern, and that Gateway had no practicable means of informing the Hills of its terms before making the deal over the telephone.[32] The court also indicated that the Hills were at fault for not inquiring in advance as to Gateway's standard terms.[33] The court held that U.C.C. section 2-207 did not apply because only one form—that of the seller—was used.[34]

The Seventh Circuit's insistence here and in *ProCD* that U.C.C. section 2-207 does not apply to a sale in which only one party uses a form is curious. The text of U.C.C. section 2-207 contains no such limitation, and the first official comment to U.C.C. section 2-207 indicates the opposite, stating that U.C.C. section 2-207 is intended to apply to the situation in which "an agreement has been reached . . . orally . . . between the parties and is followed by *one or both* of the parties sending formal memoranda embodying the terms so far as agreed upon and adding terms not discussed."[35] This description seems applicable to the facts in *Hill*. The Seventh Circuit's conclusion that U.C.C. section 2-207 does not apply to one-form cases also conflicts with other cases applying U.C.C. section 2-207 in one form, and even in no form, situations.[36] The Seventh Circuit cited only its *ProCD* opinion as authority in support of its conclusion; the *ProCD* opinion does not cite any supporting authority.

The issue of whether U.C.C. section 2-207 applied was significant in *Hill*—had the court applied U.C.C. section 2-207, the arbitration clause would never have been enforced. The parties' deal on the telephone was later confirmed by the seller's form. Under U.C.C. section 2-207, a contract exists on the terms agreed to on the telephone and includes additional

29. *Id.* at 1151, 31 U.C.C. Rep. Serv. 2d (CBC) at 309.

30. 86 F.3d 1447, 29 U.C.C. Rep. Serv. 2d (CBC) 1109 (7th Cir. 1996). For a discussion of the *ProCD* decision, see Thomas McCarthy et al., *Sales*, 52 BUS. LAW. 1493, 1494-96 (1997).

31. *Hill*, 105 F.3d at 1150, 31 U.C.C. Rep. Serv. 2d (CBC) at 309.

32. *Id.* at 1148, 31 U.C.C. Rep. Serv. 2d (CBC) at 306.

33. *Id.* at 1150, 31 U.C.C. Rep. Serv. 2d (CBC) at 309.

34. *Id.*

35. U.C.C. § 2-207 cmt. 1 (1995) (emphasis added).

36. *See, e.g.*, Tri-State Petroleum Corp. v. Saber Energy, Inc., 845 F.2d 575, 582; 6 U.C.C. Rep. Serv. 2d (CBC) 368, 374 (5th Cir. 1988) (involving a draft contract); Dorton v. Collins & Aikman Corp., 453 F.2d 1161, 1169-70; 10 U.C.C. Rep. Serv. (CBC) 585, 596 (6th Cir. 1972) (discussing a one-form situation).

terms under U.C.C. section 2-207(2).[37] Absent binding trade usage, arbitration clauses generally are held to alter the contract materially,[38] and therefore do not become part of the contract.[39]

The Seventh Circuit's reliance on the fact that payment before presentation of the full terms of a contract is common practice in some types of transactions was also unpersuasive.[40] Although it is true that in some transactions, such as transportation tickets and insurance policies, the model is "payment first; terms later," freedom of contract also is generally more restricted in these types of transactions than under Article 2. For example, if the arbitration clause in *Hill* had appeared in a cruise ship ticket, it would have been unenforceable in a negligence action to recover for personal injury.[41]

One might question the wisdom of the rule applied in *Hill* on policy grounds. It binds consumer buyers, and other unfortunates who do not use forms in the contracting process, to unread form clauses, while allowing sophisticated commercial buyers, who do use forms, to evade those same terms under U.C.C. section 2-207. This is *Roto-Lith* with a vengeance.[42]

In fact, *Hill* goes beyond *Roto-Lith* in inferring assent to the seller's terms by continued use of the goods.[43] *Roto-Lith* was a case in which no agreement existed prior to the exchange of forms.[44] In that context, the *Roto-Lith* court held the seller's form to be a counter-offer, which the buyer accepted when it accepted the goods.[45] In *Hill*, however, the seller's form followed the agreement on the telephone. The force of the *Roto-Lith* court's conclusion that the buyer should be held to have accepted the seller's terms when it accepted the goods is weakened by the presence of a preexisting agreement. Continued use of the computer beyond the thirty days stipulated in the seller's form does not necessarily constitute an assent to the seller's terms. The buyer, by virtue of the preexisting contract, had the right to use the computer under the terms agreed to on the telephone.

37. *See* U.C.C. § 2-207 cmt. 6 (1995).

38. *See* William H. Danne, Jr., Annotation, *What Are Additional Terms Materially Altering Contract Within Meaning of UCC § 2-207(2)(b)*, 72 A.L.R.3d 479, § 5, at 496-505 (1976 & Supp. 1997).

39. *See* U.C.C. § 2-207 cmt. 3 (stating that additional terms that materially alter the original bargain do not become part of the agreement unless expressly agreed to by the other party).

40. Hill v. Gateway 2000, Inc., 105 F.3d 1147, 1148, 31 U.C.C. Rep. Serv. 2d (CBC) 303, 306 (7th Cir. 1997).

41. *See* 46 U.S.C.A. § 183c(a)(2) (West Supp 1997).

42. *See supra* notes 15-16 and accompanying text.

43. *Hill*, 105 F.3d at 1151, 31 U.C.C. Rep. Serv. 2d (CBC) at 309.

44. Roto-Lith, Ltd. v. F.P. Bartlett & Co., 297 F.2d 497, 499, 1 U.C.C. Rep. Serv. (CBC) 73, 76 (1st Cir. 1962).

45. *Id.* at 499-500, 1 U.C.C. Rep. Serv. (CBC) at 76.

At the very least, *Hill* and *Ionics* raise the issue of when, absent signature or other unmistakable evidence of assent, one party should be bound by the other party's terms. The drafts of both revised Article 2 and proposed Article 2B attempt to deal with this question. Section 2-204(e) of the current draft of revised Article 2 provides that "if, after the buyer has become obligated to pay for or has taken delivery of the goods, the seller proposes terms in a record that vary those already disclosed or agreed to and to which the buyer agrees, the varying terms become part of the contract unless they are unconscionable under Section 2-105."[46] Section 2-105(b) of the current draft provides that a term is unconscionable if the party had no knowledge of the term and the term "(A) varies unreasonably from applicable industry standards or commercial practices; (B) substantially conflicts with one or more negotiated terms in the agreement; or (C) substantially conflicts with an essential purpose of the contract."[47] Under the revised Article 2 draft, it appears that an arbitration clause on the *Hill* facts would not be enforced. The draft of proposed Article 2B apparently would enforce the arbitration clause; it would permit one party to dictate in its form what affirmative conduct constitutes assent to that form.[48]

A Third Circuit case applying Pennsylvania law sounds a note of warning to forms drafters—be careful what you put into a form, your client may have to live with it. In *Infocomp, Inc. v. Electra Products, Inc.*,[49] the buyer made an offer by signing the seller's form purchase agreement. The purchase agreement contained a parol evidence integration clause and a clause excluding liability for incidental and consequential damages. The form also contained a "home office" clause stating that the agreement was not deemed accepted by seller until signed by seller's authorized agent. Although it furnished the goods described in the agreement to the buyer, the seller never signed the agreement. The buyer subsequently sued the

46. U.C.C. § 2-204(e) (May 1, 1998 Draft) <http://www.law.upenn.edu/library/ulc/ulc.htm>. This provision is bracketed and the reporters' notes to this section indicate that it has not been approved by the drafting committee. *Id.* note 5.

47. *Id.* § 2-105(b)(2). This provision is bracketed and the reporters' notes indicate it has not been approved by the drafting committee. *Id.* note 2. Alternative language would make it applicable "in a consumer contract" or in a "contract between an individual and a merchant." *Id.*

48. *See* U.C.C. §§ 2B-203, 2B-207, 2B-208, 2B-111, and 2B-112 (June 1, 1998 Draft) <http://www.law.upenn.edu/library/ulc/ulc.htm>. Under Article 2B, a party agrees to terms "by manifesting assent or otherwise." *See, e.g., id.* §§ 2B-207, 2B-208. "Manifesting assent" is defined to include engaging "in affirmative conduct or operations that the record conspicuously provides, or the circumstances including the terms of the record clearly indicate, will constitute acceptance," after having had an opportunity to review the record. *Id.* § 2B-111. In the mass-market context, a person does not have an opportunity to review in the situation where a record or term is available for review only after the person is obligated to pay, unless the person has a right of refund. *Id.* § 2B-112(b).

49. 109 F.3d 902, 32 U.C.C. Rep. Serv. 2d (CBC) 97 (3d Cir. 1997).

manufacturer and seller for breach of warranty. The district court enforced the remedy limitation and integration clauses.[50] On appeal, the court of appeals held that neither clause was part of the contract between the buyer and the seller.[51] Resting its decision on Pennsylvania case law,[52] the court concluded the seller's form was not the contract—because the seller failed to accept it by signing it as required by the "home office" clause.[53] The court found a contract formed by performance, and applied the standard code remedies, which permitted the buyer to recover incidental and consequential damages.[54] The lesson to be learned is that home office clauses should be drafted in such a way so that either signing the form *or* commencing performance constitutes acceptance.

TITLE

Three recent cases illustrate the continued importance of passage of title in Article 2 transactions, particularly with respect to the interaction of Article 2 and competing security interests. *In re Surplus Furniture Liquidators Inc.*,[55] illustrates the importance of title to a pre-paying buyer. Surplus Furniture Liquidators, Inc. (Surplus), a furniture retailer, filed for bankruptcy. As a debtor in bankruptcy, Surplus filed a motion seeking approval to sell some of its inventory. Four retail customers filed objections, claiming that the furniture was their property and as such, should be turned over to them. In each instance, Surplus had sold the furniture to the buyers, receiving full payment and tagging the furniture as sold to the customer. The buyers claimed that Surplus' actions were sufficient to transfer title to the furniture.

The court held that the furniture was the property of the bankruptcy estate, and granted leave to sell the furniture, free of liens.[56] The liens were transferred to the proceeds of the furniture sale.[57] Each sale was made pursuant to the terms of Surplus' "Sales Order," which provided for delivery to the buyer's home. No specific provision with respect to passage of title was provided, title therefore passed pursuant to U.C.C. section 2-401(2)(b), which provides that "if the contract requires delivery at destination, title passes on tender there."[58] The furniture was deemed

50. *Id.* at 905, 32 U.C.C. Rep. Serv. 2d (CBC) at 100.
51. *Id.* at 909, 32 U.C.C. Rep. Serv. 2d (CBC) at 106-07.
52. *See* Cucchi v. Rollins Protective Servs. Co., 546 A.2d 1131, 1135-36, 6 U.C.C. Rep. Serv. 2d 1448, (Pa. Super. Ct. 1988), *rev'd*, 574 A.2d 565, 11 U.C.C. Rep. Serv. 2d 737 (Pa. 1997); Franklin Interiors v. Wall of Fame Management Co., 511 A.2d 761, 762-62 (Pa. 1986).
53. *Infocomp*, 109 F.3d at 906, 32 U.C.C. Rep. Serv. 2d (CBC) at 102.
54. *Id.*, 32 U.C.C. Rep. Serv. 2d (CBC) at 103.
55. 199 B.R. 136, 31 U.C.C. Rep. Serv. 2d (CBC) 396 (Bankr. M.D.N.C. 1995).
56. *Id.* at 140, 31 U.C.C. Rep. Serv. 2d (CBC) at 399.
57. *Id.* at 145, 31 U.C.C. Rep. Serv. 2d (CBC) at 405.
58. U.C.C. § 2-401(2)(b) (1995).

to be part of Surplus' bankruptcy estate because title had not passed under Article 2.[59]

The court also rejected the buyers' arguments that U.C.C. section 2-502, which provides "a buyer who has paid . . . all of the price of the goods in which he has a special property . . . may . . . recover them from the seller if the seller becomes insolvent within ten days after receipt of the first installment of their price,"[60] gave the buyers a right to reclaim the goods.[61] The court held that U.C.C. section 2-502 did not apply because Surplus was already insolvent at the time of the sales.[62] The buyers were left with an equitable lien on the proceeds and their bankruptcy claims.[63]

Alofs Manufacturing Co. v. Toyota Manufacturing, Kentucky Inc. (In re Alofs Manufacturing Co.)[64] presented similar issues, distinguishing title and acceptance for purposes of determining whether tooling was part of the debtor/buyer's estate in bankruptcy.[65] In *Alofs*, Hi-Tech Tool and Die (Hi-Tech) manufactured tooling to be used in the manufacture of automobile parts. The tooling was initially sold to Alofs Manufacturing Co. (Alofs) or a related company, and then resold to Toyota Manufacturing, Kentucky, Inc., (Toyota). The tooling was delivered to Alofs for testing. After the testing was successfully completed, the tooling was returned to Hi-Tech for final preparation—application of a protective coating and installation of sensors. After the tooling was returned for finalization, Alofs filed for bankruptcy protection, and moved the court, on an emergency basis, for turnover of the tooling on the grounds that title had passed to Alofs. The court initially granted the motion from the bench, but reversed itself on a motion for reconsideration.[66]

As in *In re Surplus Furniture*, the court in *Alofs Manufacturing* found no specific agreement as to passage of title.[67] Alofs alleged they had accepted the tooling by returning it for completion after successful testing. The court noted that "[a]cceptance of goods and passage of title are not necessarily coterminous," although acceptance might be relevant to the extent that the evidence of acceptance also established an explicit agreement with regard to passage of title.[68] It rejected Alofs' argument, however, finding that successful completion of testing did not constitute acceptance under the facts of the case.[69] The court also rejected Alofs's argument that title

59. *Surplus Furniture Liquidators*, 199 B.R. at 140, 31 U.C.C. Rep. Serv. 2d (CBC) at 399.
60. U.C.C. § 2-502(1).
61. *Surplus Furniture Liquidators*, 199 B.R. at 141, 31 U.C.C. Rep. Serv. 2d (CBC) at 399.
62. *Id.* at 143, 31 U.C.C. Rep. Serv. 2d (CBC) at 401.
63. *Id.* at 144-45, 31 U.C.C. Rep. Serv. 2d (CBC) at 403-07.
64. 209 B.R. 83, 32 U.C.C. Rep. Serv. 2d (CBC) 790 (Bankr. W.D. Mich.1997).
65. *Id.* at 93, 32 U.C.C. Rep. Serv. 2d (CBC) at 799.
66. *Id.* at 79, 32 U.C.C. Rep. Serv. 2d (CBC) at 806.
67. *Id.* at 93, 32 U.C.C. Rep. Serv. 2d (CBC) at 799.
68. *Id.* at 94, 32 U.C.C. Rep. Serv. 2d (CBC) at 800-01.
69. *Id.*, 32 U.C.C. Rep. Serv. 2d (CBC) at 801.

to the tooling had passed upon its delivery by Hi-Tech for testing, holding instead that the tooling was not finally delivered in accordance with the contract, which specified delivery as "F.O.B. TARGET DOCK #22."[70] Applying U.C.C. section 2-401(2), which states that title passes "at the time and place at which the seller completes his performance with reference to the physical delivery of the goods,"[71] the court held that, because final delivery of the goods had not occurred, title had not passed.[72] The tooling, therefore, was not a part of Alofs' bankruptcy estate.[73]

A third case, *Cooperative Finance Association v. B&J Cattle Co.*,[74] illustrates the pitfalls facing an unpaid cash seller seeking to reclaim goods subject to the claims of a secured lender relying on an after-acquired property clause. Passage of title was again critical to the determination of priorities. Cooperative Finance Association (Cooperative) held a promissory note given by the MRC-Sheaf Corporation (MRC) and secured by, among other things, an interest in all of MRC's livestock " 'whether now owned or hereafter acquired by [MRC] and where ever located.' "[75] Cooperative's security interest was properly perfected. MRC defaulted and Cooperative commenced a replevin action. MRC purchased 203 heifers from B&J Cattle Company (B&J) for immediate resale to an identified buyer after commencement of the action. MRC was to wire immediate payment for the heifers, which were delivered by B&J to a feed lot designated by MRC. MRC failed to wire the money and subsequently sent two checks, but subsequently stopped payment on both. Cooperative amended its action to claim the additional 203 heifers. The parties stipulated to the sale of the heifers with the proceeds deposited into an account for disposition by the court.

The court held that Cooperative's interests as a secured party took precedence over those of B&J.[76] Under U.C.C. section 2-401(2), the court concluded that title had passed to MRC upon B&J's completion of delivery to the feed lot because delivery at the destination designated by MRC

70. *Id.* at 96, 97, 32 U.C.C. Rep. Serv. 2d (CBC) at 803, 805. The court found the tooling was substantially complete at the time of its delivery to Alofs for testing but that this fact was not dispositive of whether title had passed. *Id.* at 95, 32 U.C.C. Rep. Serv. 2d (CBC) at 802-03. The court stated that "the issue is not whether the goods were complete at the time of delivery; rather, the issue is whether 'the seller completes his performance with respect to the physical delivery of the goods.' " *Id.* (quoting MICH. COMP. LAWS ANN. § 440.2401(2) (West 1994)).

71. U.C.C. § 2-401(2) (1995).

72. *Alofs Manufacturing*, 209 B.R. at 97, 32 U.C.C. Rep. Serv. 2d (CBC) at 805.

73. *Id.* The court noted that Alofs did have an equitable interest in the tooling; however, to obtain the tooling, Alofs would have to assume the contract and pay the remaining contract price. *Id.* n.12.

74. 937 P.2d 915, 32 U.C.C. Rep. Serv. 2d (CBC) 808 (Colo. Ct. App. 1997).

75. *Id.* at 916, 32 U.C.C. Rep. Serv. 2d (CBC) at 809 (quoting the promissory note securing the livestock).

76. *Id.* at 921, 32 U.C.C. Rep. Serv. 2d (CBC) at 816.

constituted completion of performance by B&J.[77] Because title passed at delivery, MRC had an interest in the heifers, to which Cooperative's security interest attached.[78] B&J had only an unpaid seller's right of reclamation under U.C.C. section 2-507, "which is in the nature of a lien."[79] Cooperative's status as a perfected secured creditor won out over B&J's unperfected lien rights.[80]

NOTICE OF BREACH

Two cases were decided during the survey period which are instructive on the continued importance of giving prompt notice of defects to preserve a buyer's remedy for non-conformance. In *Gragg Farms & Nursery v. Kelly Green Landscaping*,[81] Kelly Green Landscaping (Kelly Green) purchased a shipment of oak and pine trees shipped C.O.D. Kelly Green was required to pay delivery charges before inspecting the trees. Upon inspection, however, the oaks were found to be in poor condition, and although Kelly Green properly attempted to preserve the oaks, they ultimately died and required proper disposal. Kelly Green had called the seller, Gragg Farms & Nursery (Gragg), the day after delivery, telling Gragg that the oaks were "junk" and refusing payment. The court held this telephone call to be sufficient notice of rejection, entitling Kelly Green to recovery of the freight costs and the costs incurred in both the preservation and destruction of the trees.[82] Requisite payment of the freight charges prior to inspection was held not to be acceptance.[83]

The buyer in *Aqualon Co. v. MAC Equipment, Inc.*[84] did not fare as well as the buyer in *Gragg*. Aqualon Co. (Aqualon), a chemical products manufacturer, ordered rotary airlock valves for incorporation into manufacturing equipment from MAC Equipment, Inc. (MAC). The valves were specifically designed for Aqualon and passed through several design stages. Aqualon's "Request for Quotation" neither specified air leakage rates for the valves nor supplied drawings; however, Aqualon argued that it supplied sufficient information to allow MAC to determine if its valves met the

77. *Id.* at 920, 32 U.C.C. Rep. Serv. 2d (CBC) at 815.

78. *Id.*

79. *Id.* at 919, 32 U.C.C. Rep. Serv. 2d (CBC) at 813 (quoting COLO. REV. STAT. § 4-2-507(2) cmt. 3 (1992)).

80. *Id.* at 921, 32 U.C.C. Rep. Serv. 2d (CBC) at 816. The court also rejected the argument that MRC's voidable title was an insufficient interest to permit attachment of the security interest, finding that, under COLO. REV. STAT. 4-2-403(1), MCR had a sufficient interest in the livestock to convey good title to a good faith purchaser free of any interest retained by B&J. *Id.*

81. 674 N.E.2d 785, 32 U.C.C. Rep. Serv. 2d (CBC) 1119 (Ohio Mun. Ct. 1996).

82. *Id.* at 787, 32 U.C.C. Rep. Serv. 2d (CBC) at 1120-21.

83. *Id.*, 32 U.C.C. Rep. Serv. 2d (CBC) at 1121.

84. 32 U.C.C. Rep. Serv. 2d (CBC) 818 (E.D.Va. 1997), *aff'd*, No. 97-1693, 1998 WL 378257 (4th Cir. Jul. 8, 1998).

contract specifications. MAC provided air leakage rates but declined to provide a performance warranty. The parties disagreed about whether the valves were suitable and met specifications. MAC notified Aqualon that it would proceed with the design it had because it could not see an appropriate modification. Aqualon accepted delivery, although it required MAC to do more testing. After delivery, MAC fixed some problems with blower noise, but believed the valves to be in proper working order and made no further changes. Aqualon insisted that its equipment worked only because it had been re-designed to accommodate problems created by excessive air leakage from the valves, alleging MAC had known about the problems since 1992. Aqualon did not, however, serve notice of breach of warranty or contract, or of revocation of acceptance from the date of its acceptance of the valves in June 1993, until notice of the lawsuit was served in 1996.

The court held, on the facts, that MAC had not offered a performance warranty, and that, as a matter of law, a three-year delay in notice of breach was excessive and barred all recovery.[85] The court rejected Aqualon's argument that MAC's knowledge that the leakage rates did not meet the contract specifications constituted knowledge of the breach.[86] The court declined to follow those courts which hold no notice is necessary where a party has actual knowledge of a breach.[87] The court further declared that knowledge of the underlying facts is insufficient; the buyer must give notice that it believes the facts constitute a breach of the agreement.[88]

ECONOMIC LOSS DOCTRINE

One of the leading cases in the development of the economic loss doctrine is the 1986 decision of *East River Steamship Corp. v. Transamerica Delaval Inc.*,[89] in which the U.S. Supreme Court held that a tort plaintiff in admiralty could not recover for the physical damage a defective product caused to itself, as opposed to damage that it caused to other property.[90] In 1997, in *Saratoga Fishing Co. v. J.M. Martinac & Co.*,[91] the Court addressed the question of whether equipment added by the initial user of a product should be considered part of the product itself under the *East River* doctrine, or should be considered other property for which recovery in tort would be allowed.[92] The loss at issue in *East River* was the defective product, a ship that was destroyed when it exploded. Despite the presence of physi-

85. *Id.* at 828.
86. *Id.* at 829-30.
87. *Id.*
88. *Id.*
89. 476 U.S. 858, 1 U.C.C. Rep. Serv. 2d (CBC) 609 (1986).
90. *Id.* at 871, 1 U.C.C. Rep. Serv. 2d (CBC) at 618.
91. 117 S. Ct. 1783, 33 U.C.C. Rep. Serv. 2d (CBC) 778 (1997).
92. *Id.* at 1785-86, 33 U.C.C. Rep. Serv. 2d (CBC) at 778-79.

cal harm, the *East River* Court found this loss to be an economic one "very much like the loss of the value of a product that does not work properly or does not work at all."[93] The Court concluded, therefore, that the law of contract, particularly the law of warranty, was "well suited" to deal with such losses, and denied recovery in tort.[94]

In *Saratoga*, a fishing vessel owned by the plaintiff, Saratoga Fishing Co. (Saratoga Fishing), sank due to an engine room fire and flood caused by a defective hydraulic system. J.M. Martinac & Co. (Martinac) had constructed the vessel and sold it to Joseph Madruga in the early 1970s. Madruga added additional equipment to the vessel, including a skiff and seine net; and, after using the vessel for a time for tuna fishing, resold it with the extra equipment to Saratoga Fishing in 1974. Saratoga Fishing continued to use the vessel for tuna fishing until it sunk in 1986. The district court awarded Saratogo Fishing damages, including loss of the equipment added by Madruga.[95] The Ninth Circuit reversed, holding that under *East River* Saratoga Fishing could not recover in tort for the added equipment because that equipment was part of the defective product—the vessel.[96]

In a split decision, the U.S. Supreme Court reversed the Ninth Circuit, with Justice Breyer writing the majority opinion.[97] The majority declined to extend the *East River* holding to any property subsequently added by a user to the manufacturer's product.[98] The defense had conceded that if the additional property had been added by Saratoga Fishing it clearly would not have been part of the property sold and, thus, Saratoga Fishing would not have been denied damages in tort for its loss. The majority considered the fact the additional property had been added instead by an intermediate user to be a mere "fortuity" insufficient to warrant a different result.[99]

Justice Scalia, joined by Justices O'Connor and Thomas, expressed concern over the lack of lower court decisions on the issue presented in the case, and suggested that the Court should have denied certiorari and awaited the experience of the state courts in their dissent.[100] The dissent also took issue with the majority's "mere fortuity" argument, suggesting that the majority was itself relying on a fortuity—Madruga's use of the vessel before selling it.[101] Madruga, who had added the additional equipment, was a reseller. Therefore, had he not used the modified vessel before

93. *Id.* at 1786, 33 U.C.C. Rep. Serv. 2d (CBC) at 780 (citing *East River*, 476 U.S. at 870, 1 U.C.C. Rep. Serv. 2d (CBC) at 618).
94. *Id.*, 33 U.C.C. Rep. Serv. 2d (CBC) at 780-81.
95. *Id.* at 1785, 33 U.C.C. Rep. Serv. 2d (CBC) 779.
96. *Id.*
97. *Id.* at 1786, 33 U.C.C. Rep. Serv. 2d (CBC) at 779.
98. *Id.* at 1789, 33 U.C.C. Rep. Serv. 2d (CBC) at 784.
99. *Id.* at 1787, 33 U.C.C. Rep. Serv. 2d (CBC) at 782.
100. *Id.* at 1789, 33 U.C.C. Rep. Serv. 2d (CBC) at 785 (Scalia, J., dissenting).
101. *Id.* at 1790-91, 33 U.C.C. Rep. Serv. 2d (CBC) at 786-87 (Scalia, J., dissenting).

reselling it, there would have been no question that the economic loss doctrine, as articulated in *East River,* would have precluded tort recovery for the added equipment as part of the vessel.[102] The dissent proposed that a better rule would be one that defined the product itself for economic loss purposes in commercial transactions as whatever was the product purchased or bargained for by the plaintiff.[103]

Decisions by several other federal courts have identified other types of damages and costs covered by the economic loss doctrine. In *Cooper Power Systems, Inc. v. Union Carbide Chemicals & Plastics Co.*,[104] for example, the U.S. Court of Appeals for the Seventh Circuit, applying Wisconsin law, held that the substantial costs incurred by plaintiff Cooper Power Systems, Inc. (Cooper) to correct, by sandblasting and repainting, blistered and delaminated paint which it had applied to thousands of electric transformers were economic losses.[105] Thus, Cooper could not, under the economic loss doctrine, maintain a tort action against the defendant paint manufacturer, Union Carbide Chemicals & Plastics Co. (Union Carbide). The Seventh Circuit also found that Cooper was not a third party beneficiary of the contract under which Union Carbide sold paint to the plaintiff's seller, Premium Finishes, Inc. (Premium Finishes).[106] Cooper was, therefore, left to its contractual rights against Premium Finishes.[107]

The U.S. Court of Appeals for the Fourth Circuit, applying Virginia law, held in *Redman v. John D. Brush & Co.*[108] that the theft of plaintiff Michael Redman's coin collection from an allegedly negligently designed safe manufactured by the defendant, John D. Brush & Co., was an economic loss for which a tort action would not lie.[109] The plaintiff was left to his warranty claim, which was barred by the applicable statute of limitations.[110]

In *Valleyside Dairy Farms, Inc. v. A. O. Smith Corp.*,[111] the U.S. District Court for the Western District of Michigan, applying that state's law, held oxygen degradation of plaintiff Valleyside Dairy Farms, Inc.'s (Valleyside's) alfalfa stored in silos purchased from defendant A.O. Smith Corp. (Smith) and the resultant decrease in dairy production from Valleyside's dairy herd constituted economic loss not actionable in tort.[112] The alfalfa degradation was caused by the fact that, contrary to Smith's representations and ad-

102. *Id.* at 1791, 33 U.C.C. Rep. Serv. 2d (CBC) at 786-87 (Scalia, J., dissenting).
103. *Id.* at 1792, 33 U.C.C. Rep. Serv. 2d (CBC) at 790 (Scalia, J., dissenting).
104. 123 F.3d 675, 33 U.C.C. Rep. Serv. 2d (CBC) 803 (7th Cir. 1997).
105. *Id.* at 681, 33 U.C.C. Rep. Serv. 2d (CBC) at 810.
106. *Id.* at 680, 33 U.C.C. Rep. Serv. 2d (CBC) at 808-09.
107. *Id.* at 680-81, 33 U.C.C. Rep. Serv. 2d (CBC) at 809-10.
108. 111 F.3d 1174, 32 U.C.C. Rep. Serv. 2d (CBC) 785 (4th Cir. 1997).
109. *Id.* at 1181-83, 32 U.C.C. Rep. Serv. 2d (CBC) at 787-89.
110. *Id.* at 1182-83, 32 U.C.C. Rep. Serv. 2d (CBC) at 787-89.
111. 944 F. Supp. 612, 31 U.C.C. Rep. Serv. 2d (CBC) 357 (W.D. Mich. 1995).
112. *Id.* at 615-17, 31 U.C.C. Rep. Serv. 2d (CBC) at 361-64.

vertising, Smith's silos were not "air tight." Valleyside argued that the representations constituted fraud in the inducement. The court disagreed, concluding that the representations were simply provisions of the contract that had been breached. Valleyside was therefore limited to its contractual rights.[113]

Two other courts considered whether the economic loss doctrine applied to consumers as well as commercial parties, and came to somewhat different conclusions. The U.S. District Court for the District of Vermont held in *Mainline Tractor & Equipment Co. v. Nutrite Corp.*[114] that Vermont law exempted consumers from the doctrine's prohibition against tort action.[115] The loss in question was recognized as clearly economic in nature—a drop in crop yield of silage corn due to ineffective control of crabgrass by a herbicide sold by the Nutrite Corporation and manufactured by the Monsanto Company. Vermont defines "consumer" to include one " 'who purchases . . . for his use . . . in connection with the operation of . . . a farm whether or not the farm is conducted as a trade or business.' "[116] Consumers were simply not intended to be subjects of the economic loss doctrine, according to the court's reading of the relevant case law, including the *East River* case.[117]

The New Jersey Supreme Court reached the opposite conclusion in *Alloway v. General Marine Industries, L.P.*[118] *Alloway* concerned the sinking and loss of a thirty-three-foot luxury power boat purchased by Samuel P. Alloway, III (Alloway) as a result of a defective leaking seam. The loss was clearly economic, not recoverable in tort unless Alloway was exempted from that result on the grounds that he was a consumer.[119] The court declined to grant a consumer exemption, finding, contrary to *Mainline Tractor*, that nothing in the relevant case law and commentary justified such an exemption.[120] The court, however, stressed Alloway's sophistication and bargaining power in the transaction, and noted that the case did not reach the issue of precluding a tort claim "when the parties are of unequal bargaining power, the product is a necessity, no alternative source for the product is readily available, and the purchaser cannot reasonably insure against consequential damages."[121] This suggests that, while the court did not appear inclined to find a general consumer exception to the

113. *Id.* at 616-17, 31 U.C.C. Rep. Serv. 2d (CBC) at 362-63.

114. 937 F. Supp. 1095, 32 U.C.C. Rep. Serv. 2d (CBC) 763 (D. Vt. 1996).

115. *Id.* at 1104, 32 U.C.C. Rep. Serv. 2d (CBC) at 775.

116. *Id.* at 1102, 32 U.C.C. Rep. Serv. 2d (CBC) at 772 (quoting VT. STAT. ANN. tit. 9 § 2451a(a) (1984 & Supp. 1992)).

117. *Id.* at 1103-04, 32 U.C.C. Rep. Serv. 2d (CBC) at 774-75; *see also supra* note 89-103 and accompanying text.

118. 695 A.2d 264, 32 U.C.C. Rep. Serv. 2d (CBC) 1040 (N.J. 1997).

119. *Id.* at 275, 32 U.C.C. Rep. Serv. 2d (CBC) at 1055-56.

120. *Id.* at 270-72, 32 U.C.C. Rep. Serv. 2d (CBC) at 1048-51.

121. *Id.* at 273, 32 U.C.C. Rep. Serv. 2d (CBC) at 1054.

economic loss doctrine, it left open the possibility that a narrower exception might be found in certain circumstances.

CONSEQUENTIAL ECONOMIC LOSS DAMAGES—PRIVITY REQUIREMENT

In 1997, the Supreme Courts of Virginia and Minnesota addressed another question concerning "economic loss:" whether a party, who otherwise qualifies as a third party beneficiary under the particular state's version of U.C.C. section 2-318,[122] may sue for damages for breach of warranty under that section if those damages are economic losses only. In *Beard Plumbing & Heating, Inc. v. Thompson Plastics, Inc.*,[123] the plaintiff, Beard Plumbing & Heating, Inc. (Beard), was a subcontractor who installed polyvinyl chloride plumbing fittings in a condominium development. The fittings were manufactured by defendants Thompson Plastics, Inc. (Thompson) and NIBCO, Inc. (NIBCO) but purchased by Beard from supply houses. The fittings cracked and leaked when hot water was introduced into the system. The prime contractor for the development forced Beard to replace the fittings and repair the related damage, and then fired him from the job. Beard sued Thompson and NIBCO in the U.S. District Court for the Eastern District of Virginia for breach of warranty under Virginia's version of U.C.C. section 2-318, and for negligence, claiming as damages the costs of replacement and repair, loss of the remainder of the contract, $165,000 paid to settle a lawsuit by the prime contractor, damage to business reputation, and legal fees. The court correctly found all of these damages to be economic loss, and dismissed the tort action under the economic loss doctrine.[124] The warranty action was also dismissed due to a lack of privity.[125]

Beard appealed to the U.S. Court of Appeals for the Fourth Circuit, which certified the following question to the Virginia Supreme Court: "Is privity required to recover economic loss under Va. Code § 8.2-715(2) due to the breach of the implied warranty of merchantability, notwithstanding the language of Va. Code § 8.2-318?"[126] In its response to the certified question, the Virginia Supreme Court first noted that section 8.2-715(2) defined consequential damages to include " 'any loss resulting from general or particular requirements and needs of which the seller *at the time of contracting* had reason to know. . . .' "[127] The court concluded that the phrase "at the time of contracting" created a privity requirement because

122. *See* VA. CODE ANN. § 8.2-318 (Michie 1991); MINN. STAT. ANN. § 336.2-318 (West Supp. 1998).

123. 491 S.E. 2d 731, 33 U.C.C. Rep. Serv. 2d (CBC) 691 (Va. 1997).

124. *Id.* at 734, 33 U.C.C. Rep. Serv. 2d (CBC) at 694.

125. *Id.*, 33 U.C.C. Rep. Serv. 2d (CBC) at 695-96.

126. *Id.* at 733, 33 U.C.C. Rep. Serv. 2d (CBC) at 693.

127. *Id.* (quoting VA. CODE ANN. § 8.2-715(2)(a)) (emphasis added).

it demonstrated the "presumption that there is a contract between the parties."[128] The court then considered whether section 8.2-318 overrode that privity requirement, concluding that it did not.[129] Section 8.2-318 provides in pertinent part that "[l]ack of privity between plaintiff and defendant shall be no defense in any action . . . for breach of warranty, express or implied, . . . if the plaintiff was a person whom the manufacturer or seller might reasonably have expected to use . . . the goods. . . ."[130] The court held that under rules of statutory construction the specific language of section 8.2-715(2) prevailed over the more general language of section 8.2-318.[131] The court explained that the latter section addressed the general ability of the plaintiff to maintain its action, whereas section 8.2-715(2) addressed the more specific issue of what was needed to recover economic damages.[132] The court also held that section 8.2-318 eliminated the common law requirement of privity, not a privity requirement imposed by statute, such as that in section 8.2-715(2).[133]

In *Minnesota Mining & Manufacturing Co. v. Nishika Ltd.*,[134] the Texas Supreme Court, applying Minnesota law, certified to the Minnesota Supreme Court the question of "whether a plaintiff who never used, purchased, or otherwise acquired goods from the seller could recover lost profits unaccompanied by physical injury or property damage."[135] The plaintiffs were Nishika Ltd. (Nishika) and three related companies who sued defendant Minnesota Mining & Manufacturing Co. (3M), because 3M's allegedly defective products caused their three-dimensional photography venture to fail. They sued only for lost profits, clearly an economic loss. The certified question related to two of the four plaintiffs, Nishika and American 3D, who had neither used nor purchased the defective goods from 3M.[136] Minnesota's nonuniform version of U.C.C. section 2-318 provides: "A seller's warranty whether express or implied extends to any person who may reasonably be expected to use, consume or be affected by the goods and who is injured by breach of the warranty. A seller may not exclude or limit the operation of this section."[137] The Minnesota Supreme Court

128. *Id.*, 33 U.C.C. Rep. Serv. 2d (CBC) at 694.

129. *Id.* at 734, 33 U.C.C. Rep. Serv. 2d (CBC) at 696.

130. VA. CODE ANN. § 8.2-318. Virginia has a nonuniform version of U.C.C. § 2-318, which is similar substantively to U.C.C. § 2-318 alternative C.

131. *Beard Plumbing & Heating,* 491 S.E.2d at 734, 33 U.C.C. Rep. Serv. 2d (CBC) at 696.

132. *Id.*, 33 U.C.C. Rep. Serv. 2d (CBC) at 695.

133. *Id.*

134. 953 S.W.2d 733, 33 U.C.C. Rep. Serv. 2d (CBC) 817 (Tex. 1997).

135. *Id.* at 735, 33 U.C.C. Rep. Serv. 2d (CBC) at 818.

136. *Id.* at 737, 33 U.C.C. Rep. Serv. 2d (CBC) at 822.

137. MINN. STAT. ANN. § 336.2-318 (West Supp. 1998). Minnesota's nonuniform version of U.C.C. § 2-318 is similar to but broader than U.C.C. § 2-318 alternative C because it does not contain the alternative's language limiting the prohibition on exclusion or limitation of the section "to injury to the person of an individual to whom the warranty extends." U.C.C. § 2-318 alternative C (1995).

held that only "those who purchase, use, or otherwise acquire warranted goods have standing to sue for purely economic losses."[138] All other plaintiffs "must demonstrate physical injury or property damage before economic losses are recoverable."[139] The court stated that this interpretation "comports with legislative intent, provides a clear rule of law, and identifies a sensible limit to liability without disrupting settled precedent."[140] The Texas Supreme Court accordingly held against Nishika and American 3D on their warranty claims.[141]

STATUTE OF LIMITATIONS—WARRANTY OF FUTURE PERFORMANCE

U.C.C. section 2-725 provides that parties to a contract of sale must commence an action within four years from the date on which the cause of action accrues.[142] An action for breach of warranty accrues "when tender of delivery is made, except that where a warranty explicitly extends to future performance of the goods . . . the cause of action accrues when the breach is or should have been discovered."[143] In 1997, two cases addressed the question of whether a particular warranty was a warranty of future performance. In each case, the defendant moved for summary judgment because the plaintiff's action had not been commenced within four years from the date of delivery of the goods, although the action had been commenced within a year of discovery of the defect. In each case the language of the particular warranty was determinative.

Wienberg v. Independence Lincoln-Mercury, Inc.,[144] concerned a Lincoln Town Car with a defective transmission. The motion for summary judgment by defendants Independence Lincoln-Mercury, Inc., and Ford Motor Company (Ford) was granted by the trial judge, and plaintiff Wienberg appealed.[145] Ford's limited warranty stated that it covered all parts found to be defective in materials or workmanship, provided that defects "occur under normal use of the car during the warranty coverage period . . . [which] begins at the warranty start date and lasts four years or 50,000 miles, whichever occurs first."[146] The Missouri Court of Appeals for the

138. Minnesota Mining & Mfg. Co. v. Nishika Ltd., 565 N.W.2d 16, 21, 33 U.C.C. Rep. Serv. 2d (CBC) 58, 64 (Minn. 1997).

139. *Id.*

140. *Id.*

141. Minnesota Mining & Mfg. Co. v. Nishika Ltd., 953 S.W.2d 733, 740, 33 U.C.C. Rep. Serv. 2d (CBC) 817, 826 (Tex. 1997). The court remanded the case for a new trial with regard to the other two plaintiffs in order to give them an opportunity to establish their individual damages. *Id.*

142. U.C.C. § 2-725(1).

143. *Id.* § 2-725(2).

144. 948 S.W.2d 685, 32 U.C.C. Rep. Serv. 2d (CBC) 851 (Mo. Ct. App. 1997).

145. *Id.* at 687, 32 U.C.C. Rep. Serv. 2d (CBC) at 851.

146. *Id.*, 32 U.C.C. Rep. Serv. 2d (CBC) at 851-52.

Western District had no difficulty concluding that Ford was "warranting the future performance of the goods for a specified period of time."[147] It reversed the lower court's grant of summary judgment and remanded the case for trial.[148]

Anderson v. Crestliner, Inc.[149] arose from a twenty-one foot Crestliner fiberglass power boat with a defective hull. The breach of warranty action was brought six years after purchase, but within four years of discovery of the breach. The trial court granted defendant Crestliner Inc.'s motion for summary judgment based on the running of the statute of limitations, and the plaintiff appealed.[150] The warranty stated that the boat "shall be free from any defect in material or workmanship *according to the following guidelines.*"[151] One of those guidelines stated that "*[t]he warranty period* for defects in material or workmanship of the hull and deck structure *is 5 years.*"[152] The Minnesota Court of Appeals released its decision that the warranty "explicitly" extended to future performance on the emphasized language,[153] and reversed the summary judgment order.[154]

WARRANTIES

CREATION OF WARRANTY

Several cases decided during the survey period illustrate the principles governing creation of express warranties and the role of reliance under U.C.C. section 2-313. In *Weng v. Allison*,[155] the plaintiffs purchased a car from the defendant, who told the plaintiffs that the car was " 'mechanically sound,' 'in good condition,' 'a good, reliable car,' and had 'no problems.' "[156] The plaintiffs subsequently learned that the car was unsafe, requiring extensive repairs. The trial court entered judgment for the seller, reasoning that no one could reasonably have relied on statements that the car was mechanically sound, given its 10-year age, 96,000 miles, and $800 purchase price.[157] The Illinois Appellate Court reversed, holding that the seller's statements constituted express warranties as affirmations of fact and descriptions under U.C.C. section 2-313(1),[158] and that the trial court misconstrued the role of reliance in determining whether such affirmations

147. *Id.* at 689, 32 U.C.C. Rep. Serv. 2d (CBC) at 855.
148. *Id.* at 690, 32 U.C.C. Rep. Serv. 2d (CBC) at 856.
149. 564 N.W.2d 218, 32 U.C.C. Rep. Serv. 2d (CBC) 99 (Minn. Ct. App. 1997).
150. *Id.* at 220, 33 U.C.C. Rep. Serv. 2d (CBC) at 101.
151. *Id.*, 33 U.C.C. Rep. Serv. 2d (CBC) at 100 (emphasis added).
152. *Id.* (emphasis added).
153. *Id.* at 221, 32 U.C.C. Rep. Serv. 2d (CBC) at 102.
154. *Id.* at 223, 32 U.C.C. Rep. Serv. 2d (CBC) at 106.
155. 678 N.E.2d 1254, 32 U.C.C. Rep. Serv. 2d (CBC) 755 (Ill. Ct. App. 1997).
156. *Id.* at 1255, 32 U.C.C. Rep. Serv. 2d (CBC) at 755.
157. *Id.*, 32 U.C.C. Rep. Serv. 2d (CBC) at 756.
158. U.C.C. § 2-313(1)(a), (b) (1995).

or promises become part of the "basis of the bargain."[159] The court stated:

> Affirmations of fact made during the bargain are presumed to be part of the basis of the bargain unless clear, affirmative proof otherwise is shown. . . . It is not necessary, therefore, for the buyer to show reasonable reliance upon the seller's affirmations in order to make the affirmations part of the basis of the bargain. . . . The burden is upon the seller to establish by clear, affirmative proof that the affirmations did not become part of the basis of the bargain.[160]

The court concluded that the seller failed to satisfy this burden, and that a car with the age and mileage of the car sold could nevertheless be mechanically sound.[161]

Reliance was also at issue in *Martin v. American Medical Systems, Inc.*[162] The plaintiff, a penile implant recipient, was injured when the implant, which proved not to be sterile, caused a severe infection. The plaintiff sued the manufacturer for, *inter alia*, breach of an express warranty made by the manufacturer to the plaintiff's' urologist that "[t]he AMS Dynaflex Penile Prosthesis . . . [is] delivered to the hospital prefilled and sterile."[163] The defendant contended that no warranty was made because the plaintiff was not even aware of the warranty's until the start of the existing litigation. Because of the plaintiff's ignorance, he could not have possibly relied upon it.

The Fourth Circuit rejected this argument, noting that any description of goods is part of the basis of the bargain, and therefore an express warranty even without reliance by the buyer.[164] The court cited *Daughtrey v. Ashe*,[165] in which a jeweler described a diamond as being of a higher quality than it actually was. The seller defended on the ground that the buyer was unaware of the description and did not rely upon it. The Virginia Supreme Court rejected this argument, holding that absent clear proof that the parties did not intend their bargain to include the description, the description created an express warranty.[166] The Fourth Circuit concluded that:

159. *Weng*, 678 N.E.2d at 1256, 32 U.C.C. Rep. Serv. 2d (CBC) at 756-57.

160. *Id.*, 32 U.C.C. Rep. Serv. 2d (CBC) at 757 (citations omitted).

161. *Id.*, 32 U.C.C. Rep. Serv. 2d (CBC) at 757. *Weng* is similar to the pre-U.C.C. classic case *Wat Henry Pontiac Co. v. Bradley*, 210 P.2d 348 (Okla. 1949), in which the court held that a used car dealer's representations that the car was " 'in A-1 shape' " and " 'mechanically perfect' " constituted express warranties. *Id.* at 35-52.

162. 116 F.3d 102, 32 U.C.C. Rep. Serv. 2d (CBC) 1101 (4th Cir. 1997).

163. *Id.* at 103 n.1, 32 U.C.C. Rep. Serv. 2d (CBC) at 1103 n.1.

164. *Id.* at 105, 32 U.C.C. Rep. Serv. 2d (CBC) at 1105.

165. 413 S.E.2d 336, 16 U.C.C. Rep. Serv. 2d (CBC) 294 (Va. 1992).

166. *Id.* at 338-39, 16 U.C.C. Rep. Serv. 2d (CBC) at 299.

> The facts of this case militate even more strongly in favor of an express warranty than in *Daughtrey*. In both cases, the seller described the goods, but the buyer was unaware of the description. Here, though, unlike in *Daughtrey*, Martin surely did rely on and expect *the fact warranted* to be true: i.e. the implant was sterile. Martin may assert a claim for breach of express warranty.[167]

CONTENT OF WARRANTY

The content, rather than the existence, of an express warranty was at issue in two interesting cases: *Miller v. Pettibone Corp.* (*In re Miller*)[168] and *McDonnell Douglas Corp. v. Thiokol Corp.*[169] In *Miller*, the plaintiff logger purchased from the Pettibone Corporation (Pettibone) a feller-buncher—a $100,000 tractor-type vehicle used in the forestry industry to cut and stack trees. Express warranties covered the entire machine for defects in material and workmanship and a separate component warranty covered the hydrostatic motor and pump. From the first day of operation, the machine experienced a variety of problems including numerous hydrostatic failures. Although the machine warranty had expired by the time of the machine's final breakdown, the component warranty had not, and its scope was at issue in Miller's breach of express warranty action.

The component warranty stated that the hydrostatic motor and pump " '*shall be warranted* to the original owner,' " that Pettibone would "replace any *failed* units," and that any "charges for repairs to *failed* pumps and/or motors which are not warrantable" would be borne by Miller.[170] Pettibone alleged, and the appellate court agreed, that Miller had failed to present substantial evidence of any " 'warrantable defect' " in the hydrostat.[171] In rejecting this contention, the Alabama Supreme Court noted that the component warranty at issue warranted against " 'failure' " not " 'defects,' " and that a seller wishing to warrant against only defects in material and workmanship can easily do so.[172] Given the broad language used, the court concluded that Miller met his burden of proving that the hydrostat failed by presenting testimony of operators of the feller-buncher and of persons who worked on the hydrostat after its many breakdowns.[173]

167. *Martin*, 116 F.3d at 105, 32 U.C.C. Rep. Serv. 2d (CBC) at 1106. The reliance issue under U.C.C. § 2-313 has proven difficult for the courts to resolve. For an extended discussion, see Steven Z. Hodaszy, Note, *Express Warranties Under the Uniform Commercial Code: Is There a Reliance Requirement?*, 66 N.Y.U. L. REV. 468 (1991); *see also* Rogath v. Siebenmann, 129 F.3d 261 (2d Cir. 1997) (stating that the factual issue concerning whether the buyer relied upon the seller's warranty of a painting's authenticity precluded summary judgment for the buyer).

168. 693 So. 2d 1372 (Ala. 1997).

169. 124 F.3d 1173, 33 U.C.C. Rep. Serv. 2d (CBC) 768 (9th Cir. 1997).

170. *Miller*, 693 So. 2d at 1376.

171. *Id.*

172. *Id.*

173. *Id.*

McDonnell Douglas involved a contract in which the Thiokol Corporation (Thiokol) contracted to manufacture motors for inclusion in McDonnell Douglas Corporation's (McDonnell Douglas') upper-stage payload assist module, a device designed to propel satellites from a space shuttle to geosynchronous orbit. Thiokol warranted that the motors would be free of defects in material, labor, and manufacture and would comply with the contract drawings and specifications. McDonnell Douglas sued Thiokol for breach of warranty after two satellites failed to reach orbit.

The motors were manufactured according to specification control drawings provided by McDonnell Douglas. In order to keep the weight within design specifications, Thiokol designed the motors using a carbon-carbon exit cone, rather than the heavier and more common carbon-phenolic exit cone. McDonnell Douglas ultimately approved the design.

After a motor meeting the contract specifications failed, a government investigation concluded that " '[t]he state of knowledge about the material properties of carbon/carbon involute exit cones is such that a meaningful margin of safety cannot be established.' "[174] The investigation recommended that McDonnell Douglas revise its testing procedures to detect density variations in cones that otherwise met technical standards. McDonnell Douglas ignored those recommendations when entering into a production contract with Thiokol to manufacture the motors that failed in space due to density variations.

After finding no defect in materials, labor, or manufacture, the Ninth Circuit turned to the case's major issue—whether Thiokol breached the provisions of the specification control drawings, which stated that " '[a]ll rocket motor components shall be suitable for the purpose for which they are intended. . . . The nozzle [which includes the exit cone] shall be capable of withstanding the thermal mechanical loads during motor burn without any detrimental structural failure.' "[175]

The Ninth Circuit concluded that these statements were not intended as additional performance warranties because "[t]he state-of-the-art of carbon-carbon technology, which is one of the facts and circumstances surrounding the formation of the contract, indicates that a performance warranty was not technically feasible;" therefore, "McDonnell Douglas could not have bargained for a performance warranty because it knew that, given the state-of-the-art of carbon-carbon technology, such a promise was impossible to fulfill."[176] The court therefore held that Thiokol breached neither of its warranties, citing in addition to the facts and circumstances surrounding contract formation, the testimony of McDonnell Douglas' agents, understandings prevalent in the aerospace industry, and McDonnell Douglas' own post-failure conduct.[177]

174. McDonnell Douglas, 124 F.3d at 1175, 33 U.C.C. Rep. Serv. 2d (CBC) at 770.
175. *Id.* at 1178, 33 U.C.C. Rep. Serv. 2d (CBC) at 775.
176. *Id.*, 33 U.C.C. Rep. Serv. 2d (CBC) at 776.
177. *Id.* at 1178-79, 33 U.C.C. Rep. Serv. 2d (CBC) at 776-77.

PRIVITY

Privity was at issue in *Johnson v. Anderson Ford, Inc.*[178] The plaintiff, Johnson, purchased a new Ford F-250 diesel truck from Anderson Ford, Inc. (Anderson). The truck's engine failed after expiration of the warranty, prompting Johnson to ask Anderson's service manager for assistance in acquiring a replacement. Johnson later met with a representative of the Ford Motor Company (Ford), who offered to sell him a rebuilt engine for $500 if Johnson would (i) install it himself and (ii) agree to buy Ford products in the future. Johnson accepted the Ford representative's offer. As an accommodation to Johnson and Ford, Anderson acted as an intermediary for the purchase of the rebuilt engine from Fred Jones Manufacturing Company (Jones), which had purchased the engine in plastic wrap from Dealers Manufacturing Company, a Ford-authorized remanufacturer. Jones warranted the engine "to be free from defects in material and workmanship performed by the factory," and shipped it to Anderson, which delivered it to Johnson, who had it installed by his own employees.

After experiencing problems with the replacement engine, Johnson presented it to Anderson, and the engine subsequently failed. Inspection revealed a piston and cylinder housing in the engine had cracked. Johnson sued Jones for breach of an express warranty, and both Anderson and Jones for breach of the implied warranties of merchantability and fitness. The trial court granted summary judgment for the defendants and Johnson appealed.[179] On the implied warranty issue, the Alabama Supreme Court affirmed the trial court noting that Johnson's contract was with Ford, not Anderson or Jones.[180] Accordingly, because only economic harm was alleged, lack of privity defeated Johnson's implied warranty claim.[181] On the express warranty claim, however, the court held that entry of summary judgment was inappropriate, noting that although no buyer-seller relationship existed between Jones and Johnson, Jones's warranty was a manufacturer's warranty intended to extend directly to Johnson as the ultimate purchaser.[182]

DISCLAIMER OF WARRANTY

Two cases, *NEC Technologies, Inc. v. Nelson*,[183] and *Cox v. Lewiston Grain Growers, Inc.*,[184] used traditional unconscionability analysis to determine the enforceability of warranty disclaimers. In *NEC Technologies*, television

178. 686 So. 2d 224, 31 U.C.C. Rep. Serv. 2d 376 (Ala. 1996).
179. *Id.* at 225, 31 U.C.C. Rep. Serv. 2d (CBC) at 376.
180. *Id.* at 227, 31 U.C.C. Rep. Serv. 2d (CBC) at 380-81.
181. *Id.* at 227-28, 31 U.C.C. Rep. Serv. 2d (CBC) at 381.
182. *Id.* at 228, 31 U.C.C. Rep. Serv. 2d (CBC) at 382.
183. 478 S.E.2d 769, 31 U.C.C. Rep. Serv. 2d 992 (Ga. 1996), *vacated sub nom.* Nelson v. C.M. City, Inc., 493 S.E. 2d 569 (Ga. Ct. App. 1997).
184. 936 P.2d 1191, 33 U.C.C. Rep. Serv. 2d 443 (Wash. Ct. App. 1997).

buyers sued a television manufacturer and its components importer for breach of warranty for property damage resulting from a fire allegedly caused by a defect in the televisions. The language in the express warranty covering the televisions excluded "all incidental and consequential damages." This exclusion raised the issue of whether the language was even enforceable. The Georgia Supreme Court noted that limitations or exclusions of consequential damages are unenforceable if unconscionable, and that limitations for personal injury in the case of consumer goods are prima facie unconscionable.[185] Because this limitation involved property damage, however, its enforceability was governed by general unconscionability principles stated in U.C.C. section 2-302.[186]

The court concluded that neither substantive nor procedural unconscionability was present.[187] With regard to procedural unconscionability, the court found that "[t]he language setting forth the warranty exclusion was conspicuous and comprehensible; the warranty apprised consumers that the absolute language in an exclusion may not apply to them; and the warranty itself provided a source to be contacted if further information or clarification was desired."[188] On the substantive unconscionability issue, the court stated:

> There is nothing in the record to indicate that at the time the Nelsons executed the sales contract for their television set, they were not aware of the normal hazards associated with the use of any electrical appliance. . . . Thus, while it has been recognized that a contractual term "is substantively suspect if it reallocates the risks of the bargain in [an] objectively unreasonable or unexpected manner," . . . we cannot conclude under the circumstances in this case that the allocation of the risk of property damage to the Nelsons was unconscionable. We recognize that to hold this exclusion of consequential property damages unconscionable could necessitate voiding as unconscionable such exclusions in the warranties of virtually every type of electrical appliance sold to a consumer. . . .[189]

In *Cox*, the plaintiff farmer Cox, a farmer, purchased certified winter wheat seed from Lewiston Grain Growers, Inc. (LGG). The delivery tickets accompanying the seed disclaimed express and implied warranties, and limited LGG's liability to the seed's purchase price. After the crop failed, Cox sued LGG for breach of warranty. LGG asserted the disclaimer as a defense, but the trial court found it unconscionable.

In determining the enforceability of the clause, the Washington Court of Appeals noted that exclusionary clauses in commercial contracts are

185. *Nelson*, 478 S.E.2d at 771, 31 U.C.C. Rep. Serv. 2d (CBC) at 443.
186. *See* U.C.C. § 2-302 (1995).
187. *Nelson*, 478 S.E.2d at 773, 31 U.C.C. Rep. Serv. 2d (CBC) at 998.
188. *Id.* at 772, 31 U.C.C. Rep. Serv. 2d (CBC) at 997.
189. *Id.* at 773-774 (citation omitted).

presumed conscionable; thus, the party attacking the clause has the burden of proving unconscionability based on the totality of the circumstances.[190] These circumstances include "(1) the manner in which the contract was entered; (2) whether the parties had a reasonable opportunity to understand the terms of the contract; and (3) whether important terms were hidden in fine print."[191] In affirming the trial court's ruling that the disclaimer was unconscionable, the court of appeals stated that, although the term was not hidden in the fine print, the contract involved no lengthy precontract negotiation, and LGG represented the seed as certified.[192] The disclaimer was not discussed with Cox, and he was unaware of it. Indeed, his first opportunity to familiarize himself with the terms was when he picked up the seed, which occurred shortly before planting.[193]

WARRANTY OF TITLE

The warranty of title was at issue in *Simmons v. Fanello*[194] and *Landmark Motors, Inc. v. Chrysler Credit Corp.*[195] In *Simmons*, Fanello sold restaurant equipment to Simmons; equipment that had previously been sold by Fanello and repossessed when the first buyer failed. At the time of the repossession, the original purchaser owed over $80,000 in tax liabilities, recorded as liens against the property. Fanello sold the equipment to Simmons warranting that the property was " 'free and clear of any and all liens, security agreements, encumbrances, claims, demands, taxes and charges of every kind and character whatsoever.' "[196] Simmons later encountered financial difficulty, and sought a buyer for the property, whose lawyer discovered the tax liens. The sale then collapsed, and Simmons defaulted on his notes. Fanello filed a petition for writ of immediate possession of the equipment, and Simmons counterclaimed alleging breach of the warranty of title. The trial court granted Fanello's motion for summary judgment on the counterclaim, and Simmons appealed.[197]

In affirming the trial court, the Georgia Court of Appeals held that even if Fanello breached his title warranty, Simmons suffered no damage.[198] The only damage Simmons claimed for breach of warranty was his inability to sell to his buyer. It was undisputed that Simmons made no payments on the note after October 1993, and was in default when he

190. Cox v. Lewiston Brain Growers, Inc., 936 P.2d 1191, 1197, 33 U.C.C. Rep. Serv. 2d (CBC) 443, 450 (Wash. Ct. App. 1997).

191. *Id.*, 33 U.C.C. Rep. Serv. 2d (CBC) at 450. (citing Schroeder v. Fageol Motors, Inc., 544 P.2d 20, 18 U.C.C. Rep. Serv. 2d 584 (Wash. 1975)).

192. *Id.* at 1197-98, 33 U.C.C. Rep. Serv. 2d (CBC) at 450.

193. *Id.* at 1198, 33 U.C.C. Rep. Serv. 2d (CBC) at 450.

194. 477 S.E.2d 334, 31 U.C.C. Rep. Serv. 2d 731 (Ga. Ct. App. 1996).

195. 662 N.E.2d 971, 31 U.C.C. Rep. Serv. 2d 1026 (Ind. Ct. App. 1996).

196. *Simmons*, 477 S.E.2d at 335, 31 U.C.C. Rep. Serv. 2d (CBC) at 732.

197. *Id.* at 334, 31 U.C.C. Rep. Serv. 2d (CBC) at 731.

198. *Id.* at 335, 31 U.C.C. Rep. Serv. 2d (CBC) at 732.

attempted to sell the personalty in April 1994. Both the note and the security agreement had acceleration clauses which provided that upon default Fanello could opt for payment of the entire obligation. In addition, the restaurant lease provided that Simmons could not sublet or assign without Fanello's prior written consent. Further, Fanello had a statutory right to take possession of the personalty upon default under the state's version of U.C.C. section 9-503.[199] Because these circumstances demonstrated that Simmons could not have completed the transaction without Fanello's cooperation, the court reasoned that the alleged breach of warranty of title, even if proven, caused him no damage.[200]

In *Landmark*, Chrysler Credit Corporation (Chrysler) entered into a financing agreement with a car dealership, Preston Highway Chrysler/Plymouth, Inc. (Preston). The security agreement gave Chrysler a perfected security interest in, *inter alia*, Preston's equipment. Preston subsequently defaulted and surrendered all of its assets to Chrysler, including a car wash manufactured by Brite-O-Matic. Chrysler's title check of the property revealed no markings that would indicate the car wash belonged to anyone other than Preston. Furthermore, no claim was asserted against it.

Subsequently, Chrysler hired an auctioneer to liquidate Preston's assets, including the car wash. Fliers advertising the auction disclaimed all warranties regarding the items to be sold. Landmark Motors, Inc. (Landmark), an existing Brite-O-Matic car wash lessee, saw one of the fliers and informed Brite-O-Matic that it intended to bid on the unit offered for sale. Landmark, however, declined Brite-O-Matic's offer to supply Landmark with information regarding this unit.

After Landmark purchased the car wash unit at the auction, Brite-O-Matic informed Chrysler that it owned the auctioned unit, alleging that it was merely leased to Preston. After Landmark refused Chrysler's offer to refund the purchase price, Brite-O-Matic sued Chrysler for damages and Landmark for return of the unit. Landmark thereafter filed a cross-claim against Chrysler, seeking damages for Brite-O-Matic's successful motion for replevin. The trial court ruled that Brite-O-Matic had superior title, that Chrysler had not warranted title, and that Landmark had actual notice that the title was questionable.[201] In affirming the trial court, the Indiana Court of Appeals noted that: (i) the flier advertising the auction explicitly disclaimed all warranties; (ii) Landmark made no attempt to inspect or discover information about the unit; and (iii) at the auction, the auctioneer explicitly informed bidders that no warranties accompanied the auctioned items.[202]

199. GA. CODE ANN. § 11-9-503 (1994).
200. *Simmons*, 477 S.E.2d at 335, 31 U.C.C. Rep. Serv. 2d (CBC) at 733.
201. *Landmark Motors*, 662 N.E.2d at 974, 31 U.C.C. Rep. Serv. 2d (CBC) at 1028.
202. *Id.* at 975, 31 U.C.C. Rep. Serv. 2d (CBC) at 1029-30.

WARRANTY AGAINST INFRINGEMENT

Bonneau Co. v. AG Industries, Inc.[203] involved a rare judicial excursion into the warranty against infringement contained in U.C.C. section 2-312(3).[204] The Bonneau Company (Bonneau) manufactured non-prescription reading glasses of varying designs to be sold from point-of-purchase display stands using a "hang-tag" system. AG Industries, Inc. (AGI) manufactured the stands pursuant to Bonneau's specifications. Subsequently, Magnavision, Inc. (Magnavision) brought suit against Bonneau for an alleged violation of Magnavision's patents. Bonneau thereafter sued AGI for breach of the warranty against infringement. The trial court granted summary judgment for AGI.[205]

An appeal was brought to determine the applicability of the exception to the warranty against infringement when the buyer furnishes specifications to the seller, and the infringement claim arises out of compliance with the specifications.[206] Bonneau asserted on appeal that it merely supplied a "sketch" of the system to AGI, which designed and manufactured the system under AGI's own "engineer-like" specifications.[207] In rejecting this argument and affirming the trial court, the Fifth Circuit found that the hang-tag design furnished by Bonneau to AGI constituted a specification under U.C.C. section 2-312(3):

> The record discloses that the hang-tag design (which was central to the display system) was created by Alice Myer, Bonneau's advertising and display manager, and other Bonneau executives in late January 1991. Myer's hang-tag design delineates the use and shape of a "T-Hook" and two cantilever support arms projecting from the display stand on which the hang-tag is suspended. There is no dispute that Myer did not receive any assistance from AGI in the design of the hang-tag. Thus, Myer's hand-tag design was solely Bonneau's design. . . . Accordingly, we concluded that Myer's design contains sufficient specificity for a competent manufacturer to construct the product, and thus, constitutes a "specification" pursuant to [U.C.C. section 2-312(3)].[208]

203. 116 F.3d 155, 33 U.C.C. Rep. Serv. 2d 411 (5th Cir. 1997).
204. U.C.C. § 2-312(3) states:

> Unless otherwise agreed a seller who is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third person by way of infringement or the like but a buyer who furnishes specifications to the seller must hold the seller harmless against any such claim which arises out of compliance with the specifications.

U.C.C. § 2-312(3) (1995).
205. *Bonneau*, 116 F.3d at 156, 33 U.C.C. Rep. Serv. 2d (CBC) at 412.
206. *Id.*
207. *Id.* at 158, 33 U.C.C. Rep. Serv. 2d (CBC) at 415.
208. *Id.*