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Book Review: Damages Under the Uniform Commercial Code

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Reviewed by Alvin C. Harrell

The story goes that someone asked Albert Einstein what he considered to be the most important event in all of human history. No doubt the inquirer expected an answer that described a great scientific breakthrough or discovery of some kind. Instead, reportedly the answer was: double-entry bookkeeping, the point being that this accounting device permitted development of the large scale enterprises necessary to the emergence of the industrial revolution.

Your reviewer has another candidate for this honor: the common law of contracts, likewise a necessary ingredient for the industrial revolution. Even more specifically: the law of contract damages, because without this remedy the law of contracts would have little meaning. Arguably, the law of contracts was the finest flower of common law jurisprudence, and contract damages its most creative part.

When the great common law judges created the law of contract damages, they crafted something that had never before existed on a societal scale in the western world. Beyond that they broke new ground in deciding to protect something that did not exist, except as an analytical concept: the parties' expectation interests. Today it is difficult for us to appreciate the revolutionary nature of this development. This remarkable system of remedies survives largely intact to this day, of late incarcated in the remedies provisions of the Uniform Commercial Code. The logic of this system has served generations of a legal profession that has long since ceased to fully comprehend the theoretical underpinnings of the principles involved. Likely it will also survive current trends in academia that de-emphasize the entire law of damages as superfluous to the study of modern jurisprudence.

Your reviewer would advance two reasons for this longevity: First, the system is based on theoretical principles that are descriptive of human behavior and expectations, rather than being normative as so frequently is the case with legal theories. Secondly, the law of damages represents a remarkable marriage of legal and economic concepts. After all, the calculation of damages is a quintessentially economic exercise; the purpose of the law of damages is to describe that process in legal terms and relate it to the legal principles that we call the law of contracts. The result is a consistency of analysis and purpose, evidenced by a "litany" of simple legal rules, that has produced several centuries of a "value free" jurisprudence largely untainted by the political winds that have torn to shreds so many 18th century ideals.

The litany that has served to preserve the law of damages is based on a few simple (yet, from a historical perspective, revolutionary) concepts. These concepts, described in terms of seven "critical choices" faced in the course of developing the common law, were outlined 20 years ago by Professor Allan Farnsworth in an article that Professor Anderson justly characterizes as one of the two best scholarly contributions to the law of contract damages in this century. These basic concepts include: the "compensation principle"—the notion that the aggrieved party should be compensated for his or her loss, no more and no less, and without regard to the reason for the breach; protection of contract expectations, rather than merely restoring the status quo (as would a restitutionary remedy); substitutional rather than specific relief (permitting damages in the form of a money judgment rather than a coercive order directed at the person of the defendant); the choice between measurement of economic loss by diminution in value and cost to complete as the basic legal and economic decision in the calculation of damages; the duty of the aggrieved party to mitigate his or her loss (avoidable losses being excluded from the remedy); the requirement of foreseeability as a prerequisite to consequential damages (Hadley v. Baxendale); the necessity of proving the amount of the loss with certainty, while the fact of the loss need only be shown by a preponderance of the evidence.

All of this is part of a comprehensive package, and in fact any number of these "choices" are dependent logically on the others. For example, once a decision is made to focus on compensation rather than punishment, the inquiry naturally shifts to the proper measurement of the value lost by the aggrieved party. This in turn supports a recognition that the value lost as a result of a party's breach is the value of the promised performance (the aggrieved party's expectation—measured inevitably by either diminution in value or cost to complete), less any avoidable costs or losses. Where substitute contracts are available an award of money damages is the "easiest" form of full compensation, and consequential damages are a logical part of this compensation where certain, foreseeable, and unavoidable. In retrospect the system seems natural and inevitable, although the scarcity of historical antecedents suggests otherwise. An understanding of these basic concepts is essential to an understanding of contracts remedies, and in Chapter One of his new treatise Professor Anderson provides a suitable summary of each, which one hopes will be a matter of review rather than revelation for most readers.

In Chapter Two Professor Anderson summarizes the applicability of these principles in the context of sellers' remedies.

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4. Professor Anderson aptly notes this trend in his Preface. See Anderson, Damages under the Uniform Commercial Code (Calif. 1966) (hereinafter 'Anderson, or Damages Under the U.C.C.')
5. Id. at x-xii. Professor Anderson recognizes this as well, even while "pointing at law and economics" as a science.
6. Professor Anderson cites this as a weakness of economic theory, pointing out that the law should be concerned with "statutes." See Anderson, supra note 4, at 106. But it is precisely this litigation from equity, political, and moralistic considerations that gives the law of damages unique consistency, a point recognized by Professor Anderson in his introduction at §163.
7. Farnsworth, Legal Remedies for Breach of Contract, 70 Colum. L. Rev. 1385 (1970); See Farnsworth, supra, note 4, at 1-2. The other article is Farnsworth, The Rule of foreseeability in Contract Damages, 46 Yale L.J. 521 (1936); cited in Anderson, supra note 6, at 1-2.
providing a catalog of specific U.C.C. remedies for an aggrieved seller in order to help him get back the money he has lost due to the breach of the contract. Professor Anderson immediately isolates and explains three basic questions to be considered in each case and four basic propositions that describe sellers' remedies under Article 2. He also introduces the formula for calculating damages, so beautifully described by Professor Farwar in his landmark article, and gives the recovery of value in the case of some troublesome bling events, e.g., the recovery of overhead. Chapter Two also includes a graphic illustration that serves as a kind of "roadmap to each remedy," and a quite thorough summary of incidental damages, and the recovery of interest. He also discusses the rules that generally deny consequence damages to sellers and other limitations on remedies. Chapter Three (Action for the Price) describes the limitations on a seller's right to recover the contract price under Article 2.702. Although this is an action in law and not an equitable remedy, it is the seller's equivalent of specific performance and as such it is available only in the most unusual circumstances.8 However, where applicable this is likely to be the seller's exclusive remedy.9 And similar concepts are discussed in Damages Under the U.C.C. in the context of the concept of the remedy, and in recent cases to relate these time-honored principles to modern commercial practice. The broad scope of the treatment is further illustrated by its treatment of "acceptance." One of the rare instances where an action for the price is appropriate is where the goods have been accepted by the buyer. This leads to an extended discussion in Chapter Three of Damages Under the U.C.C. Article Two. While acceptance is in many ways a matter of contract performance, it is not that simple at the early stage of performance that a chain of events begins which has consequences for the ultimate recovery. It is illustrative of the comprehensive nature of Damages Under the U.C.C. that this chain of events is traced throughout the performance, process of acceptance, rejection, vigorous objection, and possible revocation of acceptance, with careful attention being devoted to the significance of title and possession, burden of proof, and rightful versus wrongful actions. This coverage provides valuable guidance for a seller faced with urgent questions about how to respond to problems with a defective shipment. For example, there are separate sections dealing with Effective but Wrongful Rejection (§3:11); Wrongful Rejection of Acceptable Goods (§3:14); and Substantively Irrevocable Acceptance (§3:15). Once again this is all of it that is covered in examples and citations to recent cases to illustrate the practical effects of the pertinent rules of law. This is inherently a practical work, and other practical concerns are also noted: the seller's duty to resell goods (§3:16); breach of the warranty of merchantability (§3:17); and measure of damages (§3:18). The review of the case and the court's decision on the matter of whether or not the seller's remedies have been exhausted is a kind of broad legal analysis.10 It serves to illustrate the complexity of the remedies available to a seller. The breach occurs by the failure of some item of goods to be delivered within the term of the contract. 11

1. For further details, see supra, pages 1-2. 2. See supra, pages 1-2. 3. The remedies of specific performance, damages, and constructive acceptance are not discussed in Chapter Two, although they are considered in Chapter Five. 4. See supra, page 1-2. 5. For an analysis of the question of whether a seller has a right to resell or enact damages for breach of contract, see supra, page 1-2. 6. See supra, pages 1-2. 7. See supra, pages 1-2. 8. See supra, pages 1-2. 9. See supra, pages 1-2. 10. See supra, pages 1-2. 11. For an analysis of the question of whether a seller has a right to resell or enact damages for breach of contract, see supra, page 1-2.
the contract goods until his cost for them had substantially decreased. 35

Professor Anderson goes on to advocate that the breach be done under subsection 2-708(2), rather than under subsection 2-708(1) as in Trans World Metals. He also points out that there is no valid factual distinction between Trans World and Nobs Chemical, and notes some recent authority that has favored the latter over the former. This excellent discussion should be very helpful to any practitioner trying to sort out these issues in the context of a new case. While your reviewer might tend to quibble regarding minor points of this analysis (favoring for example, greater consideration of whether Nobs Chemical could have reconciled its differing calculations by a more consistent application of subsections 2-708(1) and (2)), the reader will not find a more concise or practice-oriented explanation of these difficult cases and issues. Chapter Six then discusses similar problems and issues in the context of the "market formula" at subsection 2-708(1).

Starting at Chapter Seven, Professor Anderson then does the same things for buyers' remedies, starting with a basic catalog and description of buyers' U.C.C. remedies, 36 and providing a comparison to the sellers' remedies. 37 Space does not permit a detailed description of this coverage, but it should be said that once again there is an overview (in Chapter Seven) followed by extensive treatment of each significant topic and problem area. For example, sellers are urged to "back-up" a section 2-712 claim with the proof necessary to an alternative recovery under section 2-713 or 2-714, 38 and sellers are warned to beware of pitfalls inherent in a buyer's claim under section 2-713. 39

In another example that illustrates the book's treatment of a troublesome issue, sections 9:17 and 9:18 of Damages Under the U.C.C. deal with the problem of anticipatory repudiation. This concept becomes important under U.C.C. section 2-713 as a means of identifying the point in time at which to measure the value of the seller's performance, where the seller repudiates before the performance is due. U.C.C. section 2-713 states that this value should be measured at "the time when the buyer learned of the breach." When the seller repudiates the contract prior to the contract delivery date, a seller may seek to equate "breach" with "repudiation" in order to avoid liability for post-repudiation price increases. Despite ample evidence that the drafters intended to recognize the common law differences between "breach" and "repudiation" (see, e.g. U.C.C. section 2-723), not all courts have given effect to this distinction. Professor Anderson discusses the various views that have come to hold prominence, explaining the consequences and defects of those cases that were not properly decided. This is powerful ammunition in the battle for proper and uniform interpretation of the Code.

In Chapter Ten Damages Under the U.C.C. moves into its third major topic area: the measurement of damages for breach of warranty. This has been another problem area, and Professor Anderson sorts through the various theories for determining "the differential between the value of the goods as warranted and as accepted." 40 These theories include cost of repair, 41 value "as warranted," 42 value "as accepted," 43 and the "special circumstances" exception, 44 and this discussion is followed by analysis of the major cases in this area. 45 There is a special section on the warranty of title, 46 followed by extensive coverage of incidental and consequential damages. 47

As noted, 48 Chapter Eleven deals with incidental and consequential damages and in many ways is the most important chapter in the treatise. The subject matter of this chapter is at the same time often the most difficult and the most crucial for the parties to the lawsuit, yet less has been written in this area from a practical standpoint than any other area of the law of remedies. This chapter alone should be worth the price of the book for most practitioners.

In Chapter Twelve another major topic area is covered, namely the three types of contractual limitations on remedies. In one sense the law of disclaimers, liquidated damages provisions, and limitation on liability clauses has swamped the law of warranties, since most "warranty" provisions consist largely of a limitation feature.

Lenders, in particular, need to be familiar with the rules governing these issues, as they become increasingly liable for warranty breaches by the seller. 49 Again specific problem areas receive detailed treatment, including the requirements for proper limitation clause, 50 the choice between repair and replacement, 51 seller defenses, 52 the problem of latent defects, liability for personal injury in consumer cases, 53 and the impact of federal law. 54

Finally Damages Under the U.C.C. delves into a topic that remains an area of mystery for many lawyers: reliance damages, restitution at law, and the impact of promissory estoppel. Chapter Fourteen provides a concise and comprehensive look at the relationship between these equity-based legal concepts and the common law system that swallowed them. This review and update covers an area untouched by many lawyers since their first years of law school and should be a valuable addition to any law library.

The same can be said of Damages Under the U.C.C. as a whole. Along with the landmark articles by Farnsworth, Fuller and Purdey, and Peters, 55 the two volumes of Damages Under the U.C.C. have become an important part of the literature in this area. Although as an academic your reviewer might ask for more theoretical analysis of the economic foundations for our law of remedies, and more theoretical discussion of the Farnsworth formulas, probably such changes would detract from the value of this work to practitioners. As it is, the combination of comprehensive coverage, scholarly thoroughness, and practical orientation is rare if not unique in this area of the law. The inclusion of recent developments is icing on the cake. This is an area of law that lenders and their counsel probably will need to know more about; in that sense we are fortunate to have this concise treatise as a source for both review of the law and practical advice on how to deal with emerging issues.

35. Anderson, supra note 4, at 5-30.
36. Id. at §§ 702-703.
37. Id. at § 704.
38. Id. at § 711.
39. Id. at § 712.
40. Id. at § 1040.
41. Id. at § 1040.
42. Id. at § 1040.
43. Id. at § 1040.
44. Id. at § 1010.
45. Id. at §§ 1009 and 1011.
46. Id. at § 1012.
47. Id. at §§ 1013 and all of Chapter 11. See also supra note 14.
48. See supra note 14.
49. See, e.g., O'Neill, Holders-in-Due-Course and the U.C.C. Role From Consumer Borrower to Lender Debtor, 42 Conn. L. J. 1 (1965).
50. Anderson, supra note 4, § 12-12.
51. Anderson, supra note 4, § 12-12.
52. Id. § 12-12; by definition these would also be buyers' defenses.
53. Id. §§ 12-12 and 12-22.
54. Id. § 12-24.
55. Id. § 12-26 (primarily this covers the Magnuson-Moss Warranty Act).
56. See supra note 4.
57. See Peters, supra note 13.