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Uniform Commercial Code Annual Survey: General Provisions, Sales, Bulk Transfers, and Documents of Title

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Uniform Commercial Code Annual Survey: General Provisions, Sales, Bulk Transfers, and Documents of Title

By David Frisch,* Fairfax Leary, Jr.,** and John D. Wladis***

GENERAL PROVISIONS

CONFLICT OF LAWS

The 1986 Annual Survey described the “check it back to local law” approach to the Code’s choice of law rules.¹ Recent cases emphasize this. For example, in

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Editor’s note: All citations to the U.C.C. are to the 1978 Official Text, unless otherwise noted.

1. See Frisch, Leary, & Wladis, *Uniform Commercial Code Annual Survey: General Provisions, Sales, Bulk Transfers, and Documents of Title*, 41 Bus. Law. 1363 (1986) [hereinafter 1986 Annual Survey].

Madaus v. November Hill Farm, Inc.,² the U.S. District Court for the Western District of Virginia applied the Virginia pre-Code conflict of laws rules to a dispute between a West German seller of a horse and a Virginia buyer. The court applied the Virginia rule that the law applicable to the validity of a contract is the law of the jurisdiction where the final act necessary to make the contract binding was done. Since this was the sending of a telex from West Germany, under the "mail box" rule, the contract was formed in West Germany and its law applied.³ Equally, since delivery took place in West Germany, that law also governed performance.

In *Richardson v. Clayton & Lambert Manufacturing Co.*,⁴ the court ruled that the Mississippi tort conflict of laws rules applied to indemnity claims based on breach of warranty, as well as common law indemnity claims. On this basis, the court applied what it called the Mississippi "center of gravity" test, which seems not to vary too much from the more general "most significant relationship" test of section 6 of the Restatement (Second) of Conflict of Laws.⁵ Since the case involved the installation of a vinyl liner in a swimming pool in Mississippi, the court ruled that Mississippi law applied despite the fact that the liner was fabricated in Illinois by the third-party defendant from materials produced in Ohio by B.F. Goodrich Co., fourth-party defendant.

Interestingly, one of several factors considered by the court was the state of development of the rules of both common law indemnity and indemnity for breach of warranty. Mississippi's rules were thought to be more developed.⁶ The court also considered the ease of determining and applying the law. Since the court and the attorneys were located in Mississippi, this factor also pointed to Mississippi as the center of gravity.⁷

On the other hand, in *Price v. Litton Systems*,⁸ the Fifth Circuit remanded a case for district court determination of whether Mississippi law or Alabama law

2. 630 F. Supp. 1246, 1 U.C.C. Rep. Serv. 2d (Callaghan) 24 (W.D. Va. 1986).

3. *Id.* at 1249, 1 U.C.C. Rep. Serv. 2d at 28.

4. 634 F. Supp. 1480, 1 U.C.C. Rep. Serv. 2d (Callaghan) 775 (N.D. Miss. 1986).

5. Restatement (Second) of Conflict of Laws § 6 (1971) provides:

- (1) A court, subject to constitutional restrictions, will follow a statutory directive of its own state on choice of law.
- (2) When there is no such directive, the factors relevant to the choice of the applicable rule of law include
 - (a) the needs of the interstate and international systems,
 - (b) the relevant policies of the forum,
 - (c) the relevant policies of other interested states and the relevant interests of those states in the determination of the particular issue,
 - (d) the protection of justified expectations,
 - (e) the basic policies underlying the particular field of law,
 - (f) certainty, predictability and uniformity of result, and
 - (g) ease in the determination and application of the law to be applied.

6. 634 F. Supp. at 1485, 1 U.C.C. Rep. Serv. 2d at 782.

7. *Id.*

8. 784 F.2d 600, 42 U.C.C. Rep. Serv. (Callaghan) 1614 (5th Cir. 1986).

applied in a suit based on manufacturing defects in night vision goggles, which were the alleged cause of a helicopter crash that caused the death of two wearers.

Starting its analysis of the tort claims with the statement that “[a]t least six states have contacts with this litigation,”⁹ the court affirmed the application of the law of Alabama—the place of the accident—to the tort claims. The warranty claims received a different treatment following a Mississippi Supreme Court ruling that the “center of gravity” could vary depending on the issue being considered.¹⁰ The *Price* court concluded that a claim based on breach of warranty “arises in large part under the U.C.C. and not under general tort theory.”¹¹ The court was immediately faced with a Mississippi non-Code statute, which provided that privity was not required to maintain actions for personal injury, property damage, or economic loss on any of three theories, including breach of warranty.¹² It also faced a Mississippi nonuniform amendment to the U.C.C. section 1-105(1) choice of law rules, providing that the law of Mississippi

shall always govern the rights and duties of the parties in regard to . . . the necessity for privity of contract to maintain a civil action for breach of implied warranties of merchantability or fitness notwithstanding any agreement by the parties that the laws of some other state or nation shall govern the rights and duties of the parties.¹³

The court remanded the case for the district court to determine the constitutionality of applying Mississippi law to the case, since Mississippi’s sole contact was its status as the forum state.¹⁴ Also, on remand the district court was to separately address which state’s law should govern the breach of warranty claims.¹⁵

9. The states were Mississippi (forum), Alabama (place of accident), California (place of design), Virginia (place of manufacture), New Jersey (place of execution of contract of purchase), and Texas (domicile of decedent).

10. *Boardman v. United Servs. Auto. Ass’n*, 470 So. 2d 1024 (Miss. 1985).

11. 784 F.2d at 607, 42 U.C.C. Rep. Serv. at 1621.

12. Miss. Code Ann. § 11-7-20 (Supp. 1986).

13. *Id.* § 75-1-105(1) (1972).

14. 784 F.2d at 607, 42 U.C.C. Rep. Serv. at 1622.

15. *Id.* at 608, 42 U.C.C. Rep. Serv. at 1622. The court concluded by citing:

See, e.g., Westerman v. Sears, Roebuck and Co., 577 F.2d 873 (5th Cir. 1978) (Texas wrongful death statute held to govern negligence and strict liability in tort claims; Florida wrongful death statute held to govern breach of warranty claims); *Whitaker v. Harvell-Kilgore Corp.*, 418 F.2d 1010 (5th Cir. 1969) (court applied place of injury rule to the tort claims and U.C.C. § 1-105 choice of law rule to warranty claims; court held Georgia law governed both sets of claims). (Footnotes omitted.)

A footnote listed many other such cases. Also, in the *Whitaker* case on rehearing, the Fifth Circuit’s special concurrence asserted that U.C.C. § 1-105 only applied when a provision of the U.C.C. was dispositive, otherwise a state’s general conflict of laws rules applied. 424 F.2d 549, 550–51 (5th Cir. 1970).

Thus, some courts seem able to apply an issue by issue approach to what state's law governs, despite the reference in U.C.C. section 1-105(1) to the relationship between the law of a state and the transactions. Yet, in view of the confusion on the proper treatment of warranty claims, with two courts reaching different results under the law of the same state, the overall result is not the best. Thus, conflict of laws is not an area in which uniformity in result or prediction of result is made easier by the Uniform Commercial Code.

HYBRID SALES AND SERVICE CASES

The dreary litany of cases applying the so-called "predominant purpose test" to contracts involving some service elements continues. Five of the eight cases examined involved a statute of limitations question. The U.C.C. section 2-725 four-year statute was not always the one applied, although it did prevail in four cases, ranging from the sale of a routinely assembled farm machinery shed,¹⁶ to the sale and assembly of a heat pump,¹⁷ to the assembly, installation, and sale of sprinkler systems and irrigation towers,¹⁸ to the design, sale, and assembly of steel producing services.¹⁹ Services were held to predominate in a contract for the application of herbicides by airplane in view of the selection of that method of application over hand spraying, trailer spraying, and other means.²⁰ In one case, the issue was whether a warranty of workman-like performance existed in a contract to supply and install roofing. There was no such warranty.²¹ Despite the general abolition of privity under the U.C.C. and Restatement (Second) of Torts, the Pennsylvania Superior Court refused to permit a direct suit against a subcontractor for breach of a warranty of workman-like performance.²²

Notwithstanding that a contract to print a magazine is considered a service contract where there was a course of dealing with open price terms, the court applied U.C.C. section 2-305 by analogy to find that the printer's charges were equivalent to the reasonable price at the time of delivery.²³

16. *Bob Neiner Farms, Inc. v. Hendrix*, 141 Ill. App. 3d 499, 490 N.E.2d 257, 1 U.C.C. Rep. Serv. 2d (Callaghan) 634 (1986).

17. *Meeks v. Bell*, 710 S.W.2d 789, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1118 (Tex. Ct. App. 1986).

18. *D.O.M. Farms v. Nakamoto*, 718 P.2d 262, 42 U.C.C. Rep. Serv. (Callaghan) 1680 (Colo. Ct. App. 1986).

19. *Republic Steel Corp. v. Pennsylvania Eng'g Corp.*, 785 F.2d 174, 42 U.C.C. Rep. Serv. (Callaghan) 1319 (7th Cir. 1986).

20. *Grossman v. Aerial Farm Serv.*, 384 N.W.2d 488, 1 U.C.C. Rep. Serv. 2d (Callaghan) 362 (Minn. Ct. App. 1986).

21. *Manor Junior College v. Kallers, Inc.*, 352 Pa. Super. 310, 507 A.2d 1245, 1 U.C.C. Rep. Serv. 2d (Callaghan) 648 (1986).

22. "We too are compelled to conclude that since there was no privity of contract between appellant and Spencer [subcontractor] and since this case does not involve the U.C.C. or Section 402A of the Restatement (Second) of Torts, appellant cannot proceed directly against Spencer for breach of an implied warranty." 352 Pa. Super. at 318-19, 507 A.2d at 1249, 1 U.C.C. Rep. Serv. 2d at 650.

23. *Printers II, Inc. v. Professionals Publishing*, 615 F. Supp. 767, 42 U.C.C. Rep. Serv. (Callaghan) 381 (S.D.N.Y. 1985).

Thus, the predominant purpose test does not provide a bright line, as it is not based on a cost of goods or other cost analysis, but is a judgment call as to the contract's predominant intent. Out of this analysis, courts are apt to evoke that which they most want to find.²⁴

OTHER STATUTES AFFECTING ARTICLES 2 AND 7

An unrepealed Kentucky pre-Code statute came as a surprise to the form drafters in *Consolidated Aluminum Corp. v. Krieger*²⁵ and probably will surprise drafters in other states where such a statute may exist. Seller's reference to the terms and conditions on the reverse side of its acknowledgment form was *below* seller's signature on the form. Hence, the court ruled that all the fine print on the reverse, including condition no. 22 (an exclusion of consequential damages), fell *below* the signature and was not a part of the agreement under Kentucky's interpretation of a statute providing that a writing "shall not be deemed to be signed unless the signature is subscribed at the end or close of the writing."²⁶

The plaintiff counterclaiming for breach of implied and express warranties, in *L. Harvey & Son Co. v. Jarman*,²⁷ failed to show a breach of either type of warranty because of its failure to comply with North Carolina's fertilizer statute. In any damage action, the statute requires evidence, by analysis of a sample, that the fertilizer did not conform to the composition requirements of the statute, unless the Commissioner makes one of three statutory findings.²⁸ Since there had been no compliance with the statute, the counterclaim was dismissed.

24. See *In re Germane Publication Society*, 289 F. 509, 510 (S.D.N.Y. 1922) (similar statement by Learned Hand, J.).

25. 710 S.W.2d 869, 1 U.C.C. Rep. Serv. 2d (Callaghan) 46 (Ky. Ct. App. 1986).

26. *R.C. Durr Co. v. Bennett Indus.*, 590 S.W.2d 338, 339 (Ky. Ct. App. 1979) (quoting *K.R.S. § 466.060(1)*); *Bartelt Aviation v. Dry Lake Coal Co.*, 682 S.W.2d 796, 797 (Ky. Ct. App. 1985).

27. 76 N.C. App. 191, 333 S.E.2d 47, 42 U.C.C. Rep. Serv. (Callaghan) 107 (1985).

28. N.C. Gen. Stat. § 106-662(e)(4) (1978) reads:

No suit for damage claimed to result from the use of any lot of mixed fertilizer or fertilizer material may be brought unless it shall be shown by an analysis of a sample taken and analyzed in accordance with the provisions of this Article, that the said lot of fertilizer as represented by a sample or samples taken in accordance with the provisions of this section does not conform to the provisions of this Article with respect to the composition of the mixed fertilizer or fertilizer material, unless [the Commissioner finds that the manufacturer has engaged in specified prohibited activity].

The three possible findings of prohibited behavior by the manufacturer are (i) employment of ingredients prohibited by the statute in other goods sold in the state, (ii) offering for sale during that season of any kind of dishonest or fraudulent goods, or (iii) violation of any provision of the statute by the manufacturer or any of its representatives or employees. In *Potter v. Tyndall*, 22 N.C. App. 129, 205 S.E.2d 808, *cert. denied*, 285 N.C. 661, 207 S.E.2d 762 (1974), the court held that the statute did not apply when there are false statements that constitute an express warranty of fitness.

In *Abraham v. Volkswagen of America, Inc.*,²⁹ the Second Circuit ruled that plaintiffs could not be included in the "100 named plaintiffs" required for a class action under the Magnuson-Moss Warranty Act.³⁰ Their claims either arose in states still requiring privity for a suit in contract against a manufacturer³¹ or were barred by a time or mileage limitation in an express warranty. The time limit was applicable even where the manufacturer knew of the defect at the time of sale.³² The ruling also required that two joint owners be counted as one.

In remanding the case, the court directed the parties to confer and stipulate on the named plaintiffs to be eliminated within ten days; it also ordered that plaintiffs be given the same opportunity to seek and name new plaintiffs that plaintiffs would have had if the class had been certified and the number of named plaintiffs had then been reduced to seventy-five.

*In re Great American Veal, Inc.*³³ required the court to determine the effect of a special trust fund (created by the Packers & Stockyards Act of 1921, as amended,³⁴ for unpaid cash sellers of livestock) on claims held by the unpaid sellers and a secured creditor of the packer to whom they had sold. A complication was that the operations of the packer had been taken over by a large unpaid consignor of the packer but no funds were paid for the takeover. Since the consignor had not complied with the requirements of U.C.C. sections 2-326 or 9-114, the secured creditor of the packer to whom the livestock had been sold prevailed.

But the court stated that the more important issue was "the validity and priority status of the federal statutory lien asserted by"³⁵ the secured creditor, which had purchased rights making it the subrogee of the unpaid cash sellers. The bankruptcy court refused to apply the usual tracing rules to the secured creditor as subrogee and held that in both its capacity as successor to the claims of the unpaid cash sellers and its secured creditor capacity, it had priority over the claims of the consignor.

29. 795 F.2d 238, 1 U.C.C. Rep. Serv. 2d (Callaghan) 681 (2d Cir. 1986).

30. 15 U.S.C. §§ 2301-2312 (1982); *id.* § 2310(d)(3)(C) (named plaintiffs must number at least 100 to maintain class action).

31. 795 F.2d at 249 n.12, 1 U.C.C. Rep. Serv. 2d at 689 n.12 (listing Illinois, Indiana, New York, Ohio, and Wisconsin as those states still requiring privity).

32. The plaintiffs relied on *Alberti v. General Motors Corp.*, 600 F. Supp. 1026 (D.D.C. 1985), which held that plaintiffs had valid express warranty claims, without regard to when the breakdowns occurred, if the manufacturer knew of the defects at the time of sale. The *Abraham* court rejected the *Alberti* analysis as improperly confusing express and implied warranties. 795 F.2d at 250, 1 U.C.C. Rep. Serv. 2d at 690.

33. 59 Bankr. 27, 1 U.C.C. Rep. Serv. 2d (Callaghan) 565 (Bankr. D.N.J. 1985).

34. 7 U.S.C. § 196(b) (1982).

35. 59 Bankr. at 32, 1 U.C.C. Rep. Serv. 2d at 572.

THE INTERACTION OF TORT AND CONTRACT: ECONOMIC LOSS

Many cases involve factual patterns potentially creating at least three causes of action: negligence, strict liability under section 402A of the Restatement (Second) of Torts, and breach of warranty. Grant Gilmore, when alive, used to suggest that a lawyer suing for breach of warranty when suit could be brought in negligence or strict liability should, perhaps, be considered insane.³⁶ He preferred actions in tort, where there was no (i) requirement of prior notice within a reasonable time after the defect should have been discovered,³⁷ (ii) four-year statute running from the date of delivery,³⁸ or (iii) ability to make contractual disclaimers of warranty and limitations of damages.³⁹ Yet, the courts seem bent on carving out a separate niche for products liability and warranty based on the type of damages involved. On June 16, 1986, the U.S. Supreme Court, in *East River Steamship Corp. v. Transamerica DeLaval Inc.*,⁴⁰ entered the fray. Although the case was in admiralty and any tort would be a maritime tort, the scope and thrust of the opinion applies in other settings. First, the court joined with other authorities in recognizing a cause of action called products liability, including liability based on negligence and strict liability, as a part of general maritime law.⁴¹

The case involved suits in tort by charterers of vessels in which defendant DeLaval had installed turbines that were defective in design and installation, but the only damage was to the product itself and to the vessels' propulsion system.⁴² The opinion states that whether injury to the property itself could be recovered in tort "has spawned a variety of answers," none of which are found either in the Restatement (Second) of Torts or in the Uniform Commercial

36. Professor Leary remembers conversations in which this was frequently said using the word "certified."

37. See U.C.C. § 2-607(3)(a). The penalty for not giving notice is to be barred from any remedy.

38. See U.C.C. § 2-725(1), (2). A discovery rule applies only if two preconditions are satisfied: First, the warranty must explicitly extend to future performance; and second, discovery of the breach must await that future performance.

39. See U.C.C. § 2-316 (warranty disclaimers), § 2-718 (liquidated damages), and § 2-719 (the exclusion or limitation of damages).

40. 106 S. Ct. 2295, 1 U.C.C. Rep. Serv. 2d (Callaghan) 609 (1986).

41. *Id.* at 2299, 1 U.C.C. Rep. Serv. 2d at 614 (citing *Sieracki v. Seas Shipping Co.*, 149 F.2d 98, 99-100 (3d Cir. 1945) (products liability based on negligence), *aff'd on other grounds*, 328 U.S. 85 (1946); *Pan-Alaska Fisheries, Inc. v. Marine Constr. & Design Co.*, 565 F.2d 1129, 1135 (9th Cir. 1977) (strict liability and adopting Restatement (Second) of Torts § 402A (1965)); *Ocean Barge Transport Co. v. Hess Oil Virgin Islands Corp.*, 726 F.2d 121, 123 (3d Cir. 1984) (strict liability)).

42. The opinion states that "there was no damage to 'other' property. Rather, the . . . defectively designed turbine components damaged only the turbine itself." *Id.* at 2300, 1 U.C.C. Rep. Serv. 2d at 615. Where the defect is in a separately purchased component part of an installed unit, the court ruled that recoverable property damage must be to property other than the unit serviced by the component part. *Id.* (citing *Northern Power and Eng'g Corp. v. Caterpillar Tractor Co.*, 623 P.2d 324, 330 (Alaska 1981)).

Code.⁴³ The Court, referring to "landbased solutions," indicated that the poles were represented by the majority or California position (where a defective product causes only monetary damages, warranty law preempts the field)⁴⁴ and the minority or New Jersey position (allowing tort recovery for injury to the product itself whether or not the defect created an unreasonable risk of harm).⁴⁵ In a footnote, the Court recognized that each pole had taken a step toward the other. It cited New Jersey's decision in *Spring Motors Distributors v. Ford Motor Co.*,⁴⁶ discussed in the 1986 Annual Survey, limiting *Santor* to consumer cases, and a 1979 decision in California recognizing a cause of action for negligent interference with prospective economic advantage.⁴⁷ But the Court rejected intermediate positions, seeking to differentiate between, for example, "the disappointed users" and "the endangered ones,"⁴⁸ or the nature of the defect, the type of risk, and the manner in which the injury arose.⁴⁹ The Court was also not persuaded by the majority of the courts of appeal sitting in admiralty, which had taken the *Santor* position, because those cases concerned fishing vessels and relied on solicitude for fishermen, an attitude "at times" shared by Congress.⁵⁰

The Court found the intermediary and minority landbased positions unsatisfactory where no person or property is damaged other than the product itself, since the losses, repair costs, decreased value, and lost profits are "essentially the failure of the purchaser to receive the benefit of its bargain—traditionally the core concept of contract law."⁵¹ The minority view, said the Court, "fails to

43. 106 S. Ct. at 2300, 1 U.C.C. Rep. Serv. 2d at 616. In note 3, the court cited Wade, *Is Section 402A of the Second Restatement of Torts Preempted by the U.C.C. and Therefore Unconstitutional?*, 42 Tenn. L. Rev. 123 (1974). The Delaware Supreme Court has taken the position that § 402A of the Restatement may not be applied in cases involving sales even where a resulting fire damaged other property. *Cline v. Prowler Indus.*, 418 A.2d 968, 29 U.C.C. Rep. Serv. (Callaghan) 461 (Del. 1980).

44. *Seely v. White Motor Co.*, 63 Cal. 2d 9, 403 P.2d 145, 45 Cal. Rptr. 17, 2 U.C.C. Rep. Serv. (Callaghan) 15 (1965). Five decisions during the survey period followed the California position. See *Republic Steel Corp. v. Pennsylvania Eng'g Corp.*, 785 F.2d 174, 42 U.C.C. Rep. Serv. (Callaghan) 1319 (7th Cir. 1986) (applying Illinois law); *2000 Watermark Ass'n v. Celotex Corp.*, 784 F.2d 1183, 42 U.C.C. Rep. Serv. (Callaghan) 1608 (4th Cir. 1986) (applying South Carolina law); *S.J. Groves & Sons Co. v. Aerospatiale Helicopter Corp.*, 374 S.W.2d 431, 42 U.C.C. Rep. Serv. (Callaghan) 100 (Minn. 1985); *Sharp Bros. Contracting Co. v. American Hoist & Derrick Co.*, 714 S.W.2d 919, 42 U.C.C. Rep. Serv. (Callaghan) 1246 (Mo. 1986); *Johnson v. General Motors Corp.*, 349 Pa. Super. 147, 502 A.2d 1317, 42 U.C.C. Rep. Serv. (Callaghan) 851 (1986).

45. *Santor v. A.&M. Karagheusian, Inc.*, 44 N.J. 52, 207 A.2d 305, 2 U.C.C. Rep. Serv. (Callaghan) 599 (1965).

46. 98 N.J. 555, 489 A.2d 660, 40 U.C.C. Rep. Serv. (Callaghan) 1184 (1985); see 1986 Annual Survey, *supra* note 1, at 1378.

47. *J'Aire Corp. v. Gregory*, 24 Cal. 3d 799, 598 P.2d 60, 157 Cal. Rptr. 407 (1979).

48. See, e.g., *Russell v. Ford Motor Co.*, 281 Ore. 587, 595, 575 P.2d 1383, 1387 (1978).

49. *Pennsylvania Glass Sand Corp. v. Caterpillar Tractor Co.*, 652 F.2d 1165, 1173 (3d Cir. 1981).

50. *East River Steamship Corp.*, 106 S. Ct. at 2301 n.5, 1 U.C.C. Rep. Serv. 2d at 617 n.5.

51. *Id.* at 2302, 1 U.C.C. Rep. Serv. 2d at 618.

account for the need to keep products liability and contract law in separate spheres and to maintain a realistic limitation on damages.”⁵²

This last statement of the Court reaches the core of the matter. There is no need to keep products law and warranty separate, but there is a need to keep separate rules of law serving sound public policy. According to the Court, the need is to prevent tort law from eroding the protections to producers and sellers arising from the contractual ability to restrict liability (within limits) by disclaiming warranties or limiting remedies.⁵³ Having said that, the Court then discussed warranty recovery as permitting recovery of lost profits and did not mention the widespread use of clauses excluding recovery of consequential damages. It stated that a commercial setting generally does not involve large disparities in bargaining power.⁵⁴ Earlier in the opinion, the Court commented that when such losses occur, “the commercial user stands to lose the value of the product, risks the displeasure of its customers . . . or, as in this case, experiences increased costs in performing a service. Losses like these can be insured.”⁵⁵

The real policy question is whether it is socially more efficient to place the loss where the cost of insurance will have a preventive effect and will give an incentive to test before producing, to produce with care, and to limit the asserted purposes that a product may serve.⁵⁶ Placing the burden of insurance on ultimate users may be counterproductive.⁵⁷ First, “chance takers” will not insure and will reduce prices. The loss from a bad product may also be catastrophic to a small retailer who has to compete with the chance takers to survive. Second, the division between economic/monetary loss and personal injury loss will not result in much premium saving to manufacturers, since the verdicts supposedly causing the present alleged insurance crisis are the large personal injury verdicts to which section 402A of the Restatement (Second) of Torts will still apply, as well as U.C.C. section 2-719(3), with its prima facie unconscionability rule for disclaimers of consequential damages involving personal injuries. Since defective products causing personal injury will also cause damage to the product itself, is the court suggesting that there must be two separate causes of action? Where vertical privity remains, in contract but not in

52. *Id.*

53. *Id.* at 2303, 1 U.C.C. Rep. Serv. 2d at 620. Due to the availability of insurance, would it not be better policy to require expert testimony on current insurance cost and coverage in allocating losses? Is separate insurance available for nonpersonal injury products liability and for products liability causing personal injury?

54. *Id.* The Court cited *Henningsen v. Bloomfield Motors*, 32 N.J. 358, 161 A.2d 69 (1960) at this point, thus indicating that cases involving consumer contracts may receive a different treatment. But what of fishing boats and fishermen? See *supra* text accompanying note 50. The implication is that these cases should no longer be followed.

55. 106 S. Ct. at 2302, 1 U.C.C. Rep. Serv. 2d at 619.

56. Professor Leary was present at hearings before the House and Senate during consideration of what ultimately became the Magnusson-Moss Act. The statement in the text was the policy asserted by congressional committee staff members and congressional sponsors of the act.

57. The smaller the amount of the policy, the greater the per-dollar cost of insurance. Also, the gathering of statistics to permit actuarial calculation of risks and the fixing of premiums would be more difficult.

tort, must the damages be itemized so that only the tort damages may be asserted against remote manufacturers?⁵⁸

Perhaps the problems cry out for a proper legislative solution⁵⁹ that is fair to product users, product sellers, and product makers. It should also apply to all product liability situations, abolishing any distinctions inherited from the formulary writ system, such as between contract and tort.⁶⁰

ARTICLE II—SALES OF GOODS

CONTRACT FORMATION AND TERMS

Statute of Frauds

No decisions of great significance appeared in connection with the application of the statute of frauds bar to enforcement, but precedent on the proper solutions to some problems is growing.

*Triangle Marketing v. Action Industries*⁶¹ awarded judgment on the pleadings where the writing pled by the plaintiff was its unsolicited purchase order, which did not confirm an oral contract and to which no response had been made. The court ruled that there was no requirement that the matter await the completion of discovery in the hope that defendant would make an admission.⁶²

58. One should remember that *East River Steamship Corp.* was brought in admiralty and involves only what the court determined to be injuries to the product itself. Perhaps nothing further should be drawn from the decision.

59. In footnote 3, the Court referred to legislation only in Congress, stating in part:

When S. 100, 99th Cong. 1st Sess. (1985) (the Product Liability Act) was introduced, it excluded, § 21(6), recovery for commercial loss. Suggestions have been made for revising this provision. See Amendment 16, 131 Cong. Rec. 3183 (March 19, 1985); Amendment 100, 131 Cong. Rec. 6090, 6091 (May 14, 1985). Other bills also have addressed the issue. See S. 1999, 131 Cong. Rec. 18321 (Dec. 20, 1985); Amendment 1951, 132 Cong. Rec. 5764 (May 12, 1986). See also H.R. 2568, 99th Cong. 1st Sess. (1985); H.R. 4425, 99th Cong. 2d Sess. (1986).

Strangely, no mention is made of the numerous State Product Liability Laws, of which there were 24 at last count. See *Karl v. Bryant Air Conditioning Co.*, 705 F.2d 164, 35 U.C.C. Rep. Serv. (Callaghan) 1494 (6th Cir. 1983) (Michigan's products liability statute applies to warranty claims).

60. Great Britain does not necessarily agree that separate functions must be preserved for tort and contract law. See Headly, *The Myth of Waiver of Tort*, 100 Law Q. Rev. 653, 678 (1984):

A classification of actions that arose in the early nineteenth century is not necessarily a firm basis for judicial policy in the late twentieth century. It is still true (though to an increasingly limited extent) that "the forms of action . . . rule us from their graves," but this is an unavoidable necessity, not an ideal to be emulated. (Footnote omitted.)

The quotation is from F. Maitland, *The Forms of Action at Common Law* 2 n.20 (1936). See also Cane, *Physical Loss, Economic Loss and Products Liability*, 95 Law Q. Rev. 117 (1979); Fridman, *The Interaction of Tort and Contract*, 93 Law Q. Rev. 422 (1977); cf. Wallace, *Tort Demolishes Contract in New Construction*, 94 Law Q. Rev. 60 (1978).

61. 630 F. Supp. 1538, 1 U.C.C. Rep. Serv. 2d (Callaghan) 36 (N.D. Ill. 1986).

62. The claim that the motion must await the completion of discovery was based on the provision in U.C.C. § 2-201(3)(b), satisfying the statute of frauds if there is an admission of the contract in a party's pleadings or otherwise. But where there is a denial of the contract, the plaintiff should at

This demonstrates a touching faith in the observance of the rule that an attorney will not deny an allegation without evidence to support the denial. The case supports a minority view.

In another case, an Arizona court⁶³ found conduct indicating acceptance of an order for building materials in that the supplier's price quotation was used in the purchase order, the order was picked up by the supplier's people at the buyer's office, delivery schedules were discussed, and the employees involved admitted that they believed they had conveyed a message of acceptance to the buyer by reason of a long course of prior dealings. The court concluded that "ordinary people do not speak 'legalese.' They do business. Their conduct implies the legal conclusion."⁶⁴

The court quickly found the statute of frauds to be satisfied based on the absence of an objection to the purchase order confirming an oral understanding of the previous day, the existence of internal memoranda in the seller's office ordering the goods, the preliminary notice of lien filed by the supplier, and the testimony of the seller's agents that the order had been accepted. Nonetheless, on orders of the Phoenix branch of Owens Corning, its retail branch cancelled the contract.⁶⁵

Cases for tortious interference with contract show that attorneys should not litigate on such obviously wrong bases, even when hard pressed by recalcitrant clients who have wrongfully cancelled an order. This case was for tortious interference with contract, as well as breach of contract. The jury awarded

least provide some credible support for a belief that discovery, limited to the statute of frauds issue, would produce the necessary admission or a sufficient writing. Discovery instituted to produce a settlement offer should not be tolerated. Prior cases are divided on this issue.

While neither party in *Triangle* cited cases, the court's law clerk found a number. Denying judgment on the pleadings before discovery were *Garrison v. Piatt*, 113 Ga. App. 4, 147 S.E.2d 374, 3 U.C.C. Rep. Serv. (Callaghan) 296 (1966); *M. & W. Farm Serv. Co. v. Callison*, 285 N.W.2d 271, 275-76, 27 U.C.C. Rep. Serv. (Callaghan) 1239, 1243-44 (Iowa 1979); *Franklin County Coop. v. MFC Servs. (A.A.L.)*, 441 So. 2d 1376, 1378, 37 U.C.C. Rep. Serv. (Callaghan) 1465, 1467-68 (Miss. 1983); *Reissman Int'l Corp. v. J.S.O. Wood Products*, 10 U.C.C. Rep. Serv. (Callaghan) 1165, 1167-68 (N.Y. Civ. Ct. 1972); *Dangerfield v. Markel*, 222 N.W.2d 373, 378, 15 U.C.C. Rep. Serv. (Callaghan) 765, 768-69 (N.D. 1974). Cases permitting a judgment were *Simmons Oil Corp. v. Bulk Sales Corp.*, 498 F. Supp. 457, 460 (D.N.J. 1980); *Presti v. Wilson*, 348 F. Supp. 543, 545, 11 U.C.C. Rep. Serv. (Callaghan) 716, 718 (E.D.N.Y. 1972); *Boylan v. G.L. Morrow Co.*, 63 N.Y.2d 616, 468 N.E.2d 681 (1984). The last case was a memorandum decision of five judges despite a lengthy dissent.

The *Garrison* line of cases would make sense if the rule were that when a party asserts the statute of frauds to prevent enforcement, a limited discovery would be allowed if requested by the other side and restricted to the statute of frauds issue. Then, if no admission is obtained, dismissal would follow without waiting for trial. It is only when discovery covers all other issues that a defendant is subjected to the very litigation the statute was designed to prevent, an argument the *Triangle* court used to justify no discovery at all.

63. *Custom Roofing Co. v. Alling*, 146 Ariz. 388, 706 P.2d 400, 42 U.C.C. Rep. Serv. (Callaghan) 63 (Ct. App. 1985).

64. *Id.* at 390, 706 P.2d at 402, 42 U.C.C. Rep. Serv. at 64.

65. *Id.* at 389, 706 P.2d at 401, 42 U.C.C. Rep. Serv. at 64. Custom was not an "approved contractor" for direct purchases from the manufacturer but had for many years been buying its requirements from the manufacturer's retail outlet, not through the regional branch office.

\$105,000 in punitive damages, and, after a remittitur of compensatory damages, the judgment was affirmed.⁶⁶

Where the sale is by auction to be offered in bulk and later sold in parcels, with ultimate title going to whichever method produces the most money, can the successful bidder for the bulk withdraw before completion of the parcel bidding? In *United States v. Conrad*,⁶⁷ the court was faced with a highest bulk bidder who sought to withdraw his bid while the sale by lots was in progress. To his plea of the statute of frauds, the court ruled that in making a memo of the knockdown to the highest bidder and in signing it, the auctioneer's clerk acted as agent for both buyer and seller. The court also ruled that the sale was final when the hammer fell with a condition precedent to performance that the bulk bid be higher than the total of the parcel bids.⁶⁸

In *Global Truck & Equipment Co. v. Palmer Machine Works*,⁶⁹ the oral discussions covered twenty-five trailers for hauling washed rock and gravel, but the only writing was a purchase order for five. The seller testified that there were only export permits and funding for five and that the buyer had merely indicated orally an intent to contract for an additional twenty at a later date.⁷⁰ When the deal aborted, the suit could only cover the five trailers, as the quantity stated in the writing could not be exceeded. Nor did any of the exceptions help since the suit was by the buyer for failure to deliver and defective delivery. There was no admission by the party to be charged of a contract for twenty-five, nor delivery and payment. The first exception for specially manufactured goods applies only to protect the seller. Some members of the subcommittee wonder why the objective criteria needed to prove this exception should not be equally available to a buyer.⁷¹

While speaking of the exceptions, one case more has ruled that the exception to the statute of frauds applied to goods delivered to and accepted by a "noncontractual" third party.⁷² Stated baldly, the proposition may go too far and may too readily enable the debts of the actual recipient to be foisted off on another. Here, however, the invoices were made out to the defendant, were hand delivered, and were accepted without evidence of any objection. It seems that testimony should have been allowed with this objective corroboration.

In two cases under U.C.C. section 2-201(2),⁷³ the issue was whether a farmer is a merchant; both cases held in the affirmative. The Nebraska court pointed

66. Compensatory damages of \$30,000 were reduced to \$14,000 in the trial court before judgment.

67. 619 F. Supp. 1319, 42 U.C.C. Rep. Serv. (Callaghan) 424 (M.D. Fla. 1985).

68. *Id.* at 1322-23, 42 U.C.C. Rep. Serv. at 429.

69. 628 F. Supp. 641, 42 U.C.C. Rep. Serv. (Callaghan) 1250 (N.D. Miss. 1986).

70. *Id.* at 647, 42 U.C.C. Rep. Serv. at 1258.

71. The objective nature of evidence of commencing work on special materials or special designs should be equally persuasive that a contract existed when suit is brought by the buyer.

72. *Dykes Restaurant Supply v. Grimes*, 481 So. 2d 1149, 42 U.C.C. Rep. Serv. (Callaghan) 1603 (Ala. Civ. App. 1985).

73. *Thunderbird Farms, Inc. v. Abney*, 178 Ga. App. 335, 343 S.E.2d 127, 1 U.C.C. Rep. Serv. 2d (Callaghan) 360 (1986) (doctor owner had incorporated farm to keep it separated from his

out that Nebraska's nonuniform change excluding certain sellers of their own crops from the merchant coverage of U.C.C. section 2-201(2)⁷⁴ was not in effect at the time of the transactions and so was not applicable.

Two cases correctly took the position that a failure to respond to a confirmatory memorandum did not bar a trial on the defense of no contract.⁷⁵ In one of these two, *Spinnerin Yarn Co. v. Apparel Retail Corp.*, the court applied the statute of frauds provision of U.C.C. section 1-206 to the sale of a business that was largely personal property.

*Seminole Peanut Co. v. Goodson*⁷⁶ ruled that uncertainty as to price in the writings did not preclude a contract because, for statute of frauds purposes, only a quantity term need be stated and the conduct of the parties evidenced a sufficient intent to have an open price contract. The court also ruled that, despite full performance by the peanut growers, they could still sue for damages for fraud in inducing them to make the contract.⁷⁷

In other litigation, a party claimed that because the contractual relationship arose out of a settlement agreement terminating a nonmarital relationship, the statute of frauds did not apply to its modification.⁷⁸ The claim was not successful, even though unusual.

Equitable estoppel raised its ugly head in one case. *Renfro v. Ladd*⁷⁹ arose under U.C.C. section 8-319 and the court reiterated its holding in a prior case under U.C.C. section 2-201 that to permit equitable estoppel as to the statute of frauds would be a judicial amendment of the statute. It is difficult to explain the holding in light of U.C.C. section 1-103's specific mention of estoppel as a supplementary rule of law.

Unconscionability

Unconscionability is but one method of policing sales agreements between parties.⁸⁰ An ancient concept,⁸¹ unconscionability is codified in section 2-302 of

medical practice); *Agrex, Inc. v. Schrant*, 221 Neb. 604, 379 N.W.2d 751, 42 U.C.C. Rep. Serv. (Callaghan) 1213 (1986) (owner regularly marketed grain and followed market).

74. 6 Neb. Rev. Stat. U.C.C. § 2-201(2)(b) (1980), added by 1963 Neb. Laws 544.

75. *Spinnerin Yarn Co. v. Apparel Retail Corp.*, 614 F. Supp. 1174, 42 U.C.C. Rep. Serv. (Callaghan) 65 (S.D.N.Y. 1985) (U.C.C. § 2-201); *Russell v. Dean Witter Reynolds, Inc.*, 200 Conn. 172, 510 A.2d 972, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1298 (1986) (U.C.C. § 8-319).

76. 176 Ga. App. 42, 335 S.E.2d 157, 42 U.C.C. Rep. Serv. (Callaghan) 74 (1985).

77. *Id.* at 45-46, 335 S.E.2d at 160, 42 U.C.C. Rep. Serv. at 78.

78. *LaRosa v. Fortier*, 492 So. 2d 425, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1094 (Fla. Dist. Ct. App. 1986).

79. 701 S.W.2d 148, 42 U.C.C. Rep. Serv. (Callaghan) 547 (Ky. Ct. App. 1985) (action under U.C.C. § 8-319 relying on cases under U.C.C. § 2-201).

80. Fraud, misrepresentation, warranty liability, and various statutory protections afforded by such acts as the State Retail Installments Sales Acts, the Uniform Consumer Credit Code, and the Federal Consumer Credit Protection Act, all provide protection to an unwary buyer in the marketplace. *See generally* J. White & R. Summers, *Uniform Commercial Code* (2d ed. 1980).

81. *Earl of Chesterfield v. Janssen*, 28 Eng. Rep. 82,100 (Ch. 1750).

the Code.⁸² In applying its provisions, most courts follow the procedural-substantive unconscionability dichotomy developed by Professor Leff.⁸³

While consumers have brought most of the successful cases against merchants under section 2-302, merchants can likewise benefit from the section. By reliance on section 2-302, merchants can avoid the operation of substantively unreasonable contract terms where the relative bargaining power, economic strength, or the availability of alternative sources of supply unduly favors the other party.

The ability of merchants to recover under section 2-302 is illustrated by the Michigan Court of Appeals decision in *Gianni Sport Ltd. v. Gantos, Inc.*⁸⁴ In *Gianni*, a small manufacturer in the apparel industry successfully challenged the cancellation clause in the buyer's standard form purchase contract. The challenged clause reserved the buyer's right to terminate, by notice, any purchase orders submitted to the seller either prior to shipment by seller or prior to an untimely delivery.⁸⁵ The trial court made several findings supporting both substantive and procedural unconscionability. The findings were based upon a marked disparity in both the relative bargaining power and economic strength of the parties and the absence of an alternative market for plaintiff's goods. Substantive unconscionability arose from the nature of the garment industry itself: The "big sharks" are able to impose such clauses because small independent manufacturers such as plaintiff have no clout to demand otherwise. Procedural unconscionability arose from plaintiff's testimony that he had not read the clause and would not have entered into the contract if he had. For these reasons, the trial court held the clause unenforceable. The Michigan Court of Appeals affirmed the decision per curiam.⁸⁶

Unconscionability often arises where one party to a contract seeks (i) to disclaim either the implied warranties⁸⁷ of fitness for a particular purpose⁸⁸ or merchantability⁸⁹ or (ii) to limit liability for consequential damages.⁹⁰ Despite a

82. U.C.C. § 2-302 provides:

(1) If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.

(2) When it is claimed or appears to the court that the contract or any clause thereof may be unconscionable the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose and effect to aid the court in making the determination.

83. Leff, *Unconscionability and the Code—The Emperor's New Clause*, 115 U. Pa. L. Rev. 485 (1967).

84. 151 Mich. App. 598, 391 N.W.2d 760, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1433 (1986).

85. *Id.* at 600, 391 N.W.2d at 761, 1 U.C.C. Rep. Serv. 2d at 1436.

86. *Id.* at 604, 391 N.W.2d at 763, 1 U.C.C. Rep. Serv. 2d at 1436.

87. U.C.C. § 2-316 requires that a disclaimer of implied warranties be either conspicuous and use the word "merchantability" or use words that clearly indicate that no warranty exists.

88. *Id.* § 2-315.

89. *Id.* § 2-314.

90. *Id.* § 2-719.

historic disdain for enforcing such disclaimers and limitations where a personal injury is involved,⁹¹ an injured consumer was denied relief when he was shown to have understood the contract well enough to modify some of its other terms and to have understood the risks inherent in purchasing the product by virtue of his education and special training. In *Mullan v. Quickie Aircraft Corp.*,⁹² the defendant sold the parts and machinery necessary to construct small passenger airplanes. The plaintiff was an expert woodmaker who constructed airplane propellers. While he specifically modified several of the terms of defendant's form contract, there was no evidence that he attempted to modify the terms of defendant's limitation of liability language.⁹³ Plaintiff made a thorough investigation of the product before purchasing it and was a member of the Associates Flying Club and the Experimental Aircraft Association. Given these circumstances, the Tenth Circuit found the disclaimer provision of the contract to be conscionable and, therefore, enforceable against the consumer. Thus, the Tenth Circuit reversed this portion of the lower court's decision.⁹⁴

Many courts have recognized the applicability by analogy of article 2 to transactions not involving the sale of goods. Two cases this year are worthy of mention: *John Deere Leasing Co. v. Blubaugh*,⁹⁵ an equipment leasing case, and *Best v. United States National Bank of Oregon*,⁹⁶ a class action by consumer depositors of a bank challenging the conscionability of nonsufficient funds charges assessed against their bank accounts.

John Deere Leasing involved an adhesion contract in which elements of both procedural and substantive unconscionability were established. The lease agreement between the parties entitled the lessee to exercise an option to purchase the equipment at a predetermined price only at the termination of the lease period. Despite this limitation, the lease gave the lessor the right to claim as damages upon default of the lessee not only the amount remaining due on the lease plus interest but also the option-to-purchase price of the equipment. These default provisions were in light-colored fine print on the back of the lease. This fine print was illegible because the darker print on the front side of the lease showed through to the back. While the lessee admitted to having signed the front of the lease, he denied having read the back. He testified that he assumed that he was

91. *Id.* § 2-719(3).

92. 797 F.2d 845, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1540 (10th Cir. 1986).

93. The pertinent disclaimer language read as follows: "Buyer expressly waives any and all claims arising from structural integrity, performance, flight characteristics, mechanical failures, and safety against QUICKIE AIRCRAFT CORPORATION." *Id.* at 848, 1 U.C.C. Rep. Serv. 2d at 1549.

94. The finding was not a total bar to the consumer's recovery. The plaintiff argued and the court agreed that if one or more theories of liability were preserved, despite the disclaimer provision, the jury's verdict and the court's judgment with respect to those issues should not be challenged. Since no authority was found for plaintiff's assertion that strict product liability claims could not be destroyed by disclaimers of the type presented, the court remanded the case to the district court with instructions to certify this question to the Colorado Supreme Court. *Id.* at 852, 1 U.C.C. Rep. Serv. 2d at 1550-51.

95. 636 F. Supp. 1569, 1 U.C.C. Rep. Serv. 2d (Callaghan) 658 (D. Kan. 1986).

96. 78 Ore. App. 1, 714 P.2d 1049, 1 U.C.C. Rep. Serv. 2d (Callaghan) 6 (1986).

entering into the usual lease with an option contract and that he did not expect to be liable for the purchase price should he default.

Lessee defaulted after making two payments on the lease. Since the lease had not yet expired, the option to purchase the equipment had not matured and could not validly be exercised by defendant. The lessor repossessed the equipment, sold it, and claimed the above amounts as damages under the terms of the lease.

Under these circumstances, the federal district court found both procedural and substantive unconscionability and, therefore, refused to enforce the lease default provision. The court premised its finding of procedural unconscionability on the defendant's lack of knowledge and the involuntary nature of his assent at the formation of the contract. The court found substantive unconscionability because the promisor had imposed a penalty on the lessee for terminating the lease and failing to exercise the option.

Best is unique because plaintiffs attempted to use the historically defensive provisions of section 2-302 in an affirmative challenge to the bank's allegedly exorbitant charges for processing nonsufficient funds checks. Plaintiffs argued that the charges were a penalty assessed against bank customers who wrote checks on nonsufficient funds, thereby breaching their contracts with the bank. Plaintiffs accordingly requested restitution of those amounts. The Oregon Court of Appeals held that while there was a genuine issue of fact as to the bank's good faith in assessing charges that greatly exceeded the bank's processing costs, section 2-302 does not provide the basis for affirmative relief.

Battle of the Forms

Courts seem to try to make U.C.C. section 2-207 do a lot more than Karl Llewellyn ever dreamed of in developing his philosophy. Dean John Murray has recently characterized the results as the "Chaos of the Battle of the Forms."⁹⁷ He leans toward rewriting the section.

But perhaps much can be done to improve the situation if courts would apply a few ancient, but prescient, rules to the Code and not try to force U.C.C. section 2-207 as a solution in all matters involving an exchange of forms. Following Lord Coke's maxims, expressed in *Heydon's Case*,⁹⁸ the first inquiry should be into two things. First, identify the "mischief . . . for which the common law did not provide [a remedy],"⁹⁹ and second, identify precisely the remedy "the Parliament hath resolved."¹⁰⁰ And it is suggested that all of the expressed underlying policies of the Code should also be considered.¹⁰¹

97. Murray, *The Chaos of the "Battle of the Forms": Solutions*, 39 Vand. L. Rev. 1307 (1986).

98. 3 Co. Rep. 7b, 637 (1584). Also relevant is *Eyston v. Studd*, 2 Plowden 459, 465 (1573), referring to rules of law as composed of both words and spirit and requiring application in accordance with the spirit.

99. 3 Co. Rep. 7b, at 638.

100. *Id.*

101. U.C.C. §§ 1-102(1), (2)(a), (b), (c). The definition of "agreement" in U.C.C. § 1-201(3) is based on "the bargain of the parties in fact" (emphasis added). Throughout the sections in parts 2

Had the Ninth Circuit panel in *Diamond Fruit Growers v. Krack Corp.*¹⁰² pursued this approach in Krack Corp.'s claim for indemnity against its suppliers, the result might have been drastically different on at least two possible alternatives. One of these approaches would have involved judicial legerdemain instead of a rather complete judicial rewrite of the section.¹⁰³

Before the court was a case involving a refrigeration unit manufactured by Krack using a tubing coil made by Metal-Matic. An undiscovered or later developed pinhole caused an ammonia leak, which damaged Diamond's fruit while held for storage. Apparently there was no disclaimer of the warranty of merchantability, and suit was in a jurisdiction requiring a comparative negligence solution in indemnity cases.¹⁰⁴

Forms were exchanged as they had been for some years.¹⁰⁵ Krack sent a purchase order to Metal-Matic with no provision concerning consequential damages. Metal-Matic replied with an acknowledgment form containing a very conspicuous reference to its terms on the reverse. Two were significant. One tracked the "unless" clause with which the text of U.C.C. section 2-207(1) concludes.¹⁰⁶ The other tracked U.C.C. section 2-719(1)(a), excluding all consequential damages and providing a limited repair, replace, or refund of the purchase price limitation on damages recoverable.¹⁰⁷ Apparently, neither clause was in Krack's form with the fruit wholesaler. The court held that the evidence demonstrated that Krack's purchasing manager sometime before the particular transaction had read the terms on the forms and had attempted unsuccessfully to have the clauses removed, after which there was no further protest.¹⁰⁸

and 3 of article 2, there are references in the text and comment to "the intent of the parties," or what the parties have intended. *See, e.g.*, U.C.C. § 2-204(3) & comment (para. 3); *id.* § 2-202; *id.* § 2-305(1).

102. 794 F.2d 1440, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1073 (9th Cir. 1986).

103. The Ninth Circuit's interpretation of U.C.C. § 2-207 puts the section in a position contra to several fundamental Code policies. Note that U.C.C. § 2-207 indeed runs counter to several fundamental approaches of the Code—particularly the "freedom of contract" principle, the right of an offeree to make a counteroffer, and the general rule that consequential damages are not recoverable unless so provided "in this Act or in other rule of law." *See infra* notes 112, 113, & 120 and accompanying text.

104. As between manufacturer and supplier, the consequential damages were allocated 70:30.

105. The exchange of forms here was a bit unusual. At the beginning of each year, Krack sent Metal-Matic a form of purchase order setting forth its estimated needs for the coming year. There was no reply. The parties agreed no contract was thereby made. Then, as tubing was needed, Krack sent a specific order for a quantity on a definite delivery date and Metal-Matic responded on an acknowledgement of order form.

106. Metal-Matic's form on the reverse side provided: "Metal-Matic Inc.'s acceptance of purchaser's offer or its offer to purchase is hereby expressly made conditional to purchaser's acceptance of the terms and provisions of the acknowledgement form." 797 F.2d at 1441, 1 U.C.C. Rep. Serv. 2d at 1074. At the bottom of the front of the form in bold face capitals was: "SEE REVERSE SIDE FOR TERMS AND CONDITIONS OF SALE." *Id.*

107. *Id.* at 1442-43, 1 U.C.C. Rep. Serv. 2d at 1076-77.

108. *Id.* at 1441, 1 U.C.C. Rep. Serv. 2d at 1075. How many subsequent transactions there were is not stated.

The Ninth Circuit ruled that the exclusion of consequential damages was not a part of "the contract" but apparently an additional proposal to the contract to which there was no specific and express assent by Krack, who fired the "first shot." Hence, the forms excluding consequential damages did not become part of the contract.¹⁰⁹ The court was apparently convinced that the pre-Code "mischief" to be remedied by U.C.C. section 2-207 was the common law result that favored the last shot.¹¹⁰ It apparently felt that the appropriate remedy should be an enforced application of the Code gap-filling provisions and damage recovery rules, on the ground that such provisions were neutral to the differences between the "shots." Here, however, the court actually adopted a first shot rule.

There is a total disregard of the grammatical reading of section 2-207(1)'s "unless" clause. The subsection states that a form "operates as an acceptance . . . unless acceptance is expressly made conditional on assent to the additional or different terms." When the unless clause is used, the phrase—"operates as an acceptance"—is negated.¹¹¹ Thus, we are dealing with a counteroffer, not an offer and an acceptance with variant terms.

Nowhere does the Code expressly negate the effect of counteroffers in rejecting and terminating an offer.¹¹² The policy of the Code on freedom of contract, and hence freedom to make counteroffers, is set forth in U.C.C. section 1-102(3) and emphasized in comment 2 as stating "affirmatively at the outset

109. *Id.* at 1445, 1 U.C.C. Rep. Serv. 2d at 1081. U.C.C. § 2-719(1) provides for exclusion of consequential damages by contract and this right to contract out of liability is referred to in comments to both the unconscionability and warranty sections, as well as in the comment to U.C.C. § 1-106. *See* U.C.C. § 1-102 & comment (referring to freedom of contract as a key principle).

110. 794 F.2d at 1445, 1 U.C.C. Rep. Serv. 2d at 1080.

111. Indeed, it is also possible to construe the unless clause as modifying all that precedes it, thus defeating the "Definite and seasonable expression of acceptance" clause. The court, however, said:

Further, in a case such as this one, requiring the seller to assume more liability than it intends is not altogether inappropriate. The seller is most responsible for the ambiguity because it inserts a term in its form which requires assent to additional terms and then does not enforce that requirement. If the seller truly does not want to be bound unless the buyer assents to its terms, it can protect itself by not shipping until it obtains that assent.

Id. at 1445, 1 U.C.C. Rep. Serv. 2d at 1081. This truly shows the lengths to which a result-oriented court will go to justify an improper result. First, the court maintained that following a procedure dictated by the Code created an ambiguity. Then, it said that a failure to obtain a form of assent first enunciated years later in this opinion, and reliance on continued dealing after a negotiation that failed to remove the clause, supports a conclusion that the seller did not "truly" mean what the grammar of the Code says the language meant. All of this is contra to the plain meaning of the rules in U.C.C. §§ 2-204 and 2-206 that make a contract on the terms of the offer if followed by acceptance of a shipment or other conduct indicating acceptance.

112. The purpose of the unless clause in U.C.C. § 2-207(1) was to permit a seller to make a counteroffer if so desired, but the seller must do so explicitly. There is no indication that § 2-207(1) purports to change basic counteroffer rules where the unless clause is used. For the proposition that common law rules prevail in the interstices of the Code, see *G & R Corp. v. American Security & Trust Co.*, 523 F.2d 1164, 18 U.C.C. Rep. Serv. (Callaghan) 33 (D.C. Cir. 1975); *Goldstein v. S & A Restaurant Corp.*, 622 F. Supp. 139, 42 U.C.C. Rep. Serv. 81 (D.D.C. 1985).

that freedom of contract is a principle of the Code.”¹¹³ What then was the “mischief” that section 2-207 was designed to prevent? It was the unintended counteroffer effect under common law¹¹⁴ where a reply expressing acceptance had only minor differences from the offer; that is, suggestions or terms that in business dealings did not, and in business thinking ought not, result in a counteroffer, especially when the reply to the offer did not signal a counteroffer¹¹⁵ but contained a definite and seasonal expression of acceptance.

The *Diamond Fruit* court seems to suggest that shipment of the tubing by the seller operated as a waiver of the condition altogether,¹¹⁶ unless there was an expressed definite assent to the terms in the acknowledgment.¹¹⁷ This is a new limit on the rules for the acceptance of offers found in the Code, which opt heavily in favor of acceptance by conduct.¹¹⁸

Where the issue is the exclusion of consequential damages, one should not talk of placing the buyer in as good a position as it would have been in had the seller performed,¹¹⁹ without mentioning the immediately following clause of section 1-106(1): “but neither consequential or special nor penal damages may be had except as specifically provided in this Act or by other rule of law.”¹²⁰ Also not mentioned by the court were the provisions of U.C.C. section 2-719(1)(a), expressly permitting a disclaimer of consequential damages, and section 2-719(3), indicating that where personal injuries are not involved, one claiming unconscionability would have to show that the exclusion was unconscionable.¹²¹ If U.C.C. section 2-302 on that subject is the guide, then the plaintiff must overcome the comment’s statement that it is not the purpose of the section to disturb the “allocation of risks because of superior bargaining

113. U.C.C. § 1-102 comment 2. The section itself does preclude a disclaimer of “the obligations of good faith diligence, reasonableness and care prescribed by this Act.” Making a reply to an offer a counteroffer and disclaiming consequential damages does not violate any of the specified obligations. There are also specific exceptions to freedom of contract, as in U.C.C. § 9-501(3), and “fair reading” exceptions, such as oral waivers of the statute of frauds, none of which apply here.

114. The object was merely to eliminate cases such as *Poel v. Brunswick Balke Collender Co.*, 216 N.Y. 310, 110 N.E. 619 (1915), where a clause asked for prompt acknowledgment of the acceptance. The so-called “mirror image” rule.

115. Under the common law, an acceptance merely requesting a change was clearly not a counteroffer. Restatement (Second) of Contracts § 61 (1981). U.C.C. § 2-207(1) and (2) seems to change the emphasis; the response is not a counteroffer unless the party says so by using the unless clause.

116. Waiver contemplates a relinquishment of a right by a person having at least reason to know that the right exists and is being relinquished. See *Barliant v. Follet Corp.*, 138 Ill. App. 3d 756, 483 N.E.2d 1312, 42 U.C.C. Rep. Serv. (Callaghan) 1206 (1985). Given seller’s refusal to remove the clause, and U.C.C. §§ 2-204 and 2-206, it is sophistry to find a basis for imposing a greater liability than intended because the seller did not take “enforcement” procedures not required by the Code.

117. 794 F.2d at 1445, 1 U.C.C. Rep. Serv. 2d at 1080.

118. See U.C.C. §§ 2-204, 2-206, 1-205, 2-207(3).

119. See *id.* § 1-106(1).

120. *Id.* § 1-106(1) (last lines).

121. See *id.* § 2-713 comment 3.

power.”¹²² The effect of liability for consequential damages on pricing is well known. The Code appears to treat it as one of the risks to be allocated by agreement, both in U.C.C. section 2-719(1)(a)’s statement that the “agreement may provide” for exclusion of consequential damages, and in the reference to that statement in comment 3 to U.C.C. section 2-715: “Any seller who does not wish to take the risk of consequential damages has available the section on contractual limitation of remedy.” Finally in comment 5 to U.C.C. section 2-207, among the examples of clauses that “involve no element of unreasonable surprise and which therefore are to be incorporated in the contract unless notice of objection is seasonably given, [is a clause] otherwise limiting remedy in a reasonable manner.”

Was the remedy here limited unreasonably and, thus, may the court have erroneously reached a proper result? By the terms of U.C.C. section 2-714, damages for breach of warranty are the difference “between the value of the goods accepted and the value they would have had if they had been as warranted.” We can assume that the value of tubing with a pinhole is zero, so that a refund of the purchase price is what should be awarded under the Code. Hence, the limitation is not unreasonable, as it follows the Code rule.

Thus, the Code seems to consider that who pays consequential damages is a matter for contract allocation. A seller following the Code’s provision on how to make it clear that the acknowledgment form is a counteroffer should not be forced to bear the risk of excludable consequential damages. This is especially true where the damages are for the benefit of a buyer who knew the exclusion was in the form and had not been successful in having it eliminated.

The Ninth Circuit could have taken a second approach in most cases, although it would not have been applicable in this case. This alternative flows from the fact, emphasized in Dean Murray’s article, that a very large majority of purchasing agents do not read the conditions on the reverse sides of either their own or the other contracting parties’ forms.¹²³ Hence, neither party’s terms were called specifically to the attention of the other, including the unless clause.¹²⁴ Thus, following a policy of implementing the intent of the parties, or that contractual relations are based on a meeting of the minds, the court could have applied U.C.C. section 2-207(3) as a fair resolution of the problem when the goods are shipped and accepted, and no terms mutually agreed upon apply to the problem. But this approach, too, should not be applied in favor of a party who had read the reverse of the other party’s form and had unsuccessfully negotiated for removal of the exclusion of consequential damages, but who nonetheless continued to accept and pay for goods shipped afterwards under the same form.¹²⁵

122. *See id.* § 2-302 comment 1 (discussion following citation of *Campbell Soup Co. v. Wentz*, 172 F.2d 80 (3d Cir. 1948)).

123. *See Murray, supra* note 97, at 1317–18 n.47 (referring to the practices of some 5,000 purchasing agents).

124. The “not called to the attention” technique is usually reserved for nonreading consumers.

125. Instead of a nonreader, the case involves a post-reading negotiator.

Of course, the Code could have provided that the front of the form, to be effective, must have a conspicuous reference to the fact that disclaimers of warranties and of consequential damages were on the reverse side,¹²⁶ or that the unless clause, to be effective, should be conspicuously stated above the signature on the face of any acknowledgment.¹²⁷ But the Code did not take this route. Nor did it specify that acceptances of counteroffers were to be made in any way different from acceptances of offers. Judicial decision is not an appropriate way to amend Code text. Nor should a court, in effect, find waivers of the unless clause that are not knowingly made with intent to waive.¹²⁸

In contrast to the analysis of prior dealing in *Diamond Fruit*, an Illinois appellate court in *Barliant v. Follett Corp.*¹²⁹ was faced with an invoice, issued under an agreement for a sale of books F.O.B. seller's warehouse, Chicago, adding charges for book post, transportation, and insurance. The court held that under U.C.C. section 2-207(2) these terms were not material alterations to the contract. The contract documents were, according to buyer-Barliant, the seller's terms of sale in its catalogue and Barliant's order, including reimbursement of the cost of transportation from the warehouse to the plaintiff's retail stores. The suit claimed that the charges added were in excess of the costs to be reimbursed.

For more than eighteen months the added charges were paid in full on twenty-four invoices by Barliant, an attorney, who testified that as a matter of general management he examined invoices and packing slips before making payment.¹³⁰ The trial court found "incredible" his testimony that he had not noticed the increased nature of the charges, and it also ruled that he had accepted them by a course of dealing.¹³¹ It is not clear from the opinion whether the invoices were treated as acceptances or whether the catalogue's terms were such that the order was the acceptance. In any event, there was no need to rule on the material alteration point. As proposals for addition to the contract, or as modifications under U.C.C. section 2-209, they were accepted by a course of dealing based on a reason to know.¹³²

*Mace Industries v. Paddock Pool Equipment Co.*¹³³ suggested a better approach in some ways but went too far in others. The court indicated that for a return form to constitute a counteroffer, "the conditional nature of the accep-

126. It may be difficult to see why disclaimers of warranties require type that is conspicuous and the use of the word merchantability, when limitations of damages do not. Yet, the plain meaning of the Code's language makes this distinction, perhaps because the latter limitations so often occur. Also, in comment 5 to U.C.C. § 2-207, a reasonable limitation of damages is an example of a nonmaterial term. Yet, a refund of the cost of a piece of tubing seems quite immaterial as compared with damages to the fruit in a wholesale cooler, but courts should not reverse legislative decisions plainly enacted.

127. See *supra* text accompanying notes 25–26 (Kansas rule on signatures).

128. See *supra* note 116.

129. 138 Ill. App. 3d 756, 483 N.E.2d 1312, 42 U.C.C. Rep. Serv. 1206.

130. *Id.* at 761, 483 N.E.2d at 1316, 42 U.C.C. Rep. Serv. at 1211.

131. *Id.* at 759, 761, 483 N.E.2d at 1314, 1317, 42 U.C.C. Rep. Serv. at 1209, 1211.

132. See U.C.C. § 1-205.

133. 288 S.C. 62, 339 S.E.2d 527, 42 U.C.C. Rep. Serv. (Callaghan) 825 (Ct. App. 1986).

tance must be clearly expressed in a manner sufficient to notify the offeror that the offeree is unwilling to proceed with the transaction unless the additional or different terms are included in the contract.”¹³⁴ The difficulty is how to characterize the so-called “purchase order” containing no reference to warranties sent in response to a “quotation” document called a “sales agreement” containing a limited warranty and which was referred to in the purchase order.

The sender of the purchase order argued that it was a counteroffer accepted by an acknowledgment that (i) did not limit warranties (thereby accepting all of its terms and implications) and (ii) objected to only two of the conditions on the purchase order.¹³⁵ This characterization of the purchase order as a counteroffer was based on a statement on the reverse of the form, “THE SELLER AGREES TO ALL OF THE FOLLOWING TERMS AND CONDITIONS,” and on a provision that the terms constituted the entire agreement of the parties. The court ruled that, despite the objection of Mace to two of the purchase order terms, Paddock was willing to go through with the agreement, and that this demonstrated “that Paddock was willing to proceed with the purchase of the equipment even though Mace did not assent to all the terms” of the purchase order.¹³⁶ Even if correct, does not this reasoning demonstrate treatment of the purchase order as an acceptance and not a counteroffer? This treatment is probably correct since the expression of acceptance in the purchase order, if there was one, was not expressly conditioned on a seller’s agreement to its terms.

Then, the court treated Paddock as accepting Mace’s limited warranty, which was only stated in the quotation sales agreement. If the purchase order was an offer, did not the “conspicuous” language satisfy U.C.C. section 2-207(2)(a) and negate any terms in the seller’s acceptance that were different or additional to the offer?¹³⁷ The reference to the prior proposed sales agreement could have been considered as an ambiguity resolved against the sender of the order.

It seems odd that where nothing about a warranty is stated in a purchase order, or nothing as to exclusion of consequential damages, the provisions of the Code are incorporated as objections to a reply, but when not stated in an acceptance, the terms are not effective as objections to a limited warranty in the offering documents.

Equally, it seems that in *Diamond Fruit* something more than proceeding with the deal was needed for assent to a counteroffer, but in *Mace*, proceeding with a deal was sufficient to constitute a withdrawal of a counteroffer.

Dean Murray is right. There is chaos in the battle of the forms. Perhaps the Permanent Editorial Board for the Code should reconsider whether U.C.C. section 2-207 provides the appropriate results intended.

134. *Id.* at _____, 339 S.E.2d at 530, 42 U.C.C. Rep. Serv. at 828–29.

135. *Id.* at _____, 339 S.E.2d at 530, 42 U.C.C. Rep. Serv. at 827.

136. *Id.* at _____, 339 S.E.2d at 530, 42 U.C.C. Rep. Serv. at 829.

137. True, the language does not object to specific terms one by one. But is this required in an offer? Is the exact language of the unless clause necessary to create a counteroffer?

Warranties

General

Again, the litigation on warranty issues was mostly routine, although a few cases dealt with questions of interest. Several cases involving warranty issues arose out of the sale of used automobiles. In *Crothers v. Cohen*,¹³⁸ the Minnesota Court of Appeals affirmed a judgment for Crothers based on a jury finding that Cohen breached an express warranty made by Cohen's agent to Crothers. After upholding the trial court's decision to submit the issue of the existence of an express warranty to the jury, the court of appeals, relying on a line of cases concluding that use of the word "good" created an express warranty, affirmed the jury's finding that the statement that a 1970 Dodge had a rebuilt carburetor and was a good runner was sufficient to create an express warranty, covering a stuck accelerator that caused the car to crash into a tree and injure the plaintiff. Yet, nowhere did the court explain just exactly how a warranty that a car is a good runner covered a stuck accelerator. However, there were jury findings that there was a breach, that the breach caused the accident, and that, in a comparative negligence state, the plaintiff was five percent at fault and the seller ninety-five percent.

The North Carolina Court of Appeals, in *Bailey v. LeBeau*,¹³⁹ suspended its own rules of appellate procedure to prevent what it termed a "manifest injustice,"¹⁴⁰ and created what the dissenting judge might have characterized as the same thing. In *Bailey*, the court reversed a judgment for plaintiff under the North Carolina Deceptive Trade Practice Act,¹⁴¹ trebling damages of \$2,200 and awarding attorneys' fees based on a warranty claim arising from the sale of a Honda Civic. The appellate court noted that the uncontroverted evidence was clearly sufficient to support a jury's finding (i) that the salesman's statement that certain engine parts had been replaced within the last six months constituted an express warranty and (ii) that this warranty had been breached. But the court remanded the case for a new trial, reasoning that there was no evidence that the breach of the warranty (that parts had actually been replaced about eighteen months before the sale instead of the six months warranted) caused the failure that occurred.¹⁴² One judge dissented, noting that (i) plaintiff was assured that the car was suitable for effective and economical long-distance driving, (ii) plaintiff paid \$1,400 for a car that would not run, (iii) title and possession of the auto was still in defendant, (iv) plaintiff was stranded 120 miles from home and had to get back the best way he could, (v) plaintiff returned to get the car and tow it back, all at cost to himself, and (vi) plaintiff

138. 384 N.W.2d 562, 1 U.C.C. Rep. Serv. 2d (Callaghan) 72 (Minn. Ct. App. 1986).

139. 79 N.C. App. 345, 339 S.E.2d 460, 1 U.C.C. Rep. Serv. 2d (Callaghan) 378 (1986).

140. *Id.* at _____, 339 S.E.2d at 462, 1 U.C.C. Rep. Serv. 2d at 381.

141. N.C. Gen. Stat. § 75-1.1 (1977). Attorneys' fees could be awarded under *id.* § 75-16.1. The basis was willfully engaging in the deceptive act (lying about how recently the act was done and that there was unwarranted refusal to resolve the matter). Plaintiff was "put off" by claims of repair work for over 45 days while no work was being done.

142. 79 N.C. App. at _____, 339 S.E.2d at 464, 1 U.C.C. Rep. Serv. 2d at 384.

was deprived of the use of the auto during a delay of eighteen months. Since the evidence established that plaintiff suffered out-of-pocket expenses, much inconvenience, lost time, and \$1,400 for the car, Judge Phillips felt that rather than waive rules for a deceptive defendant the law required that the judgment be affirmed.¹⁴³

In *Foley v. Dayton Bank & Trust*,¹⁴⁴ the Tennessee Court of Appeals dismissed a claim for breach of express warranty arising out of the sale by the bank of a used truck it had repossessed. The court decided that a statement by a bank employee that to the best of his knowledge the truck was in good condition was merely an opinion that did not create an express warranty. Conversely, the New York Justice Court in *Bernstein v. Sherman*,¹⁴⁵ held that the statement by a private seller's mechanic that the frame of a Datsun 280Z that had recently been in an accident was in good condition, created an express warranty, "at least to the extent that the frame was in 'good condition,'" ¹⁴⁶ even though the bill of sale contained an "as is" clause.¹⁴⁷

Two cases dealt with express warranties arising out of sales where the seller agreed to deliver goods in accordance with a buyer's required specifications. In the first, *Northern States Power Co. v. ITT Meyer Industries*,¹⁴⁸ a panel of the Eighth Circuit affirmed a jury verdict for Northern States based on a claim of breach of an express warranty. The express warranty was found in the technical specifications created jointly by buyer and seller and in the statement in the proposal for a contract (that was accepted) that the items supplied would meet the contract specifications.¹⁴⁹ In the second case, *Phillips Petroleum Co., Norway v. Bucyrus-Erie Co.*,¹⁵⁰ the Wisconsin Supreme Court reversed a decision of the court of appeals and reinstated a verdict for Phillips Petroleum for in excess of \$1,600,000 for breach of an express warranty on reasons different than those of the trial court. Here, the court found that an express warranty had been created where Bucyrus-Erie's confirmation of a modification in effect certified that crane pedestal adapters would be made of a specified

143. *Id.* at —, 339 S.E.2d at 464–66, 1 U.C.C. Rep. Serv. 2d. at 384–87 (Phillips, J., dissenting).

144. 696 S.W.2d 356, 42 U.C.C. Rep. Serv. (Callaghan) 92 (Tenn. Ct. App. 1985).

145. 130 Misc. 2d 741, 497 N.Y.S.2d 298, 1 U.C.C. Rep. Serv. 2d (Callaghan) 375 (Just. Ct. 1986).

146. *Id.* at 743, 497 N.Y.S.2d at 300, 1 U.C.C. Rep. Serv. 2d at 377. *See also* Redmac, Inc. v. Computerland of Peoria, 140 Ill. App. 3d 741, 489 N.E.2d 380, 42 U.C.C. Rep. Serv. (Callaghan) 1242 (1985) (court affirmed an award for breach of an express warranty for Redman who relied on statements that a computer system would be free of defects and would work for a reasonable period of time; the computer never worked).

147. As to the consistency between the mechanic's statement and the as is clause, the court found they were not necessarily inconsistent, and alternatively, that the "as is" disclaimer was invalid against public policy since the defect caused an accident from which the plaintiff was fortunate to escape without serious personal injury. 130 Misc. 2d at 743, 497 N.Y.S.2d at 301, 1 U.C.C. Rep. Serv. 2d at 378. *See also infra* text accompanying note 156.

148. 777 F.2d 405, 42 U.C.C. Rep. Serv. (Callaghan) 1 (8th Cir. 1985).

149. *See* discussion of *Northern States Power Co.* *infra* text accompanying note 158.

150. 131 Wis. 2d 21, 388 N.W.2d 584, 1 U.C.C. Rep. Serv. 2d (Callaghan) 667 (1986).

grade of steel as required by Phillips's specifications. This warranty was breached when that grade of steel was inadvertently not used.¹⁵¹

The question of whether reliance on an express warranty is a prerequisite for a claim of breach was examined in several cases. In *Keith v. Buchanan*,¹⁵² a California appellate court reversed a judgment for defendant, rendered at the close of plaintiff's case, where the buyer did not show any reliance on affirmations made in an advertising brochure disseminated to the public in order to induce sales of an oceangoing yacht. In reversing the judgment for defendant, the court held that actual reliance on the seller's factual representations in advertising brochures need not be shown under section 2-313 of the California Commercial Code. Rather, the seller must show that the representations formed no part of the bargain.¹⁵³ In *Global Truck and Equipment Co. v. Palmer Machine Works*,¹⁵⁴ a federal court in the Northern District of Mississippi denied recovery for breach of an express warranty arising out of the sale of dump trucks by Palmer to Global, where Global failed to prove that statements contained in the Palmer brochure were relied upon or induced the sale prior to or contemporaneously with the making of the contract,¹⁵⁵ an approach directly contra to that used in *Keith*.

Disclaimers and Limited Remedies

In *Bernstein v. Sherman*,¹⁵⁶ as discussed previously, the court held that a written disclaimer in the form of an "as is" clause in a bill of sale was not inconsistent with the seller's mechanic's statement that the frame of an automobile was in good condition. Alternatively, the court, upon the assumption of an inconsistency, held the as is disclaimer invalid as contrary to public policy where the defect had the potential to cause serious bodily injury. The Wisconsin Supreme Court, in *Phillips Petroleum Co., Norway v. Bucyrus-Erie Co.*,¹⁵⁷ held that a limited remedy for replacement of defective crane pedestal adapters failed to make the injured party whole where the damages provided for were unconscionably low. Evidence established damages in excess of \$1,600,000 and the limited remedy provisions would have put a ceiling on plaintiff's damages at \$10,400.

151. See discussion of *Phillips Petroleum* *infra* text accompanying note 157.

152. 173 Cal. App. 3d 13, 220 Cal. Rptr. 392, 42 U.C.C. Rep. Serv. (Callaghan) 386 (1985).

153. The fact that the buyer had several boat builders inspect the yacht before purchasing it did not negate the "basis of the bargain" requirement, but it did negate the reliance element a plaintiff must show when claiming breach of a warranty of fitness for a particular purpose.

154. 628 F. Supp. 641, 42 U.C.C. Rep. Serv. 1250.

155. See *Khan v. Velsicol Chem. Corp.*, 711 S.W.2d 310, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1114 (Tex. Ct. App. 1986) (reliance is not a necessary element of a claim for breach of the implied warranties of U.C.C. § 2-314 or § 2-315). See also *Bernstein v. Sherman*, 130 Misc. 2d at 742, 497 N.Y.S.2d at 300, 1 U.C.C. Rep. Serv. 2d at 377; *Northern States Power Co. v. ITT Meyer Indus.*, 777 F.2d at 412, 42 U.C.C. Rep. Serv. at 11.

156. 130 Misc. 2d 741, 497 N.Y.S.2d 298, 1 U.C.C. Rep. Serv. 2d 375.

157. 131 Wis. 2d 21, 388 N.W.2d 584, 1 U.C.C. Rep. Serv. 2d 667.

Finally, in *Northern States Power Co. v. ITT Meyer Industries*,¹⁵⁸ a panel of the Eighth Circuit affirmed a decision of the district court holding that the contractual disclaimer of warranties and limitation of remedies were inconsistent with an express warranty arising out of the acceptance of Northern States's technical specifications. The court concluded that the disclaimers written in the contract do not apply to a breach of the warranty of compliance with the specifications. In particular, the court declined to rule that, as a matter of law, the limited remedy in a separate paragraph referring to the warranties in that paragraph was the sole remedy under the contract for breach of the express warranty pertaining to the specifications.

Third-Party Beneficiaries

In *Johnson v. General Motors Corp.*,¹⁵⁹ a Pennsylvania court applied alternative A to U.C.C. section 2-318 to deny standing to a widow who inherited a car bought by her late husband and attempted to sue for damages (not involving personal injury) as a third-party beneficiary. The court reasoned that section 402A of the Restatement (Second) of Torts was also inapplicable as the loss was economic.

On the other hand, where vertical privity was concerned, the purchaser of a warehouse who, by virtue of an assignment clause in the purchase contract, succeeded to the buyer's rights, was able to defeat defendant's motions for summary judgment in *Pack & Process, Inc. v. Celotex Corp.*¹⁶⁰ Although the twenty-year roofing bond had expired, summary judgment could not be granted because a question of fact existed as to whether the representations made in connection with the roofing bond "were warranties extending to future performance."¹⁶¹

Notice of Breach to Remote Sellers or Manufacturers

Section 2-607(3)(a) requires a buyer to give a seller notice of breach within a reasonable time after the buyer discovers or should have discovered the breach. Failure to give the specified notice bars a buyer from any remedy for breach.

The case law has not been uniform in its application of this section to remote sellers and manufacturers. Some decisions have limited the section to require the buyer to notify only his immediate seller of any breach.¹⁶² These decisions allow a buyer, who has given the necessary notice of breach to his immediate seller, to then seek relief from remote sellers and manufacturers up the distribution chain who may not receive any notice of the alleged breach until litigation begins.

158. 777 F.2d 405, 42 U.C.C. Rep. Serv. 1.

159. 349 Pa. Super. 147, 502 A.2d 1317, 42 U.C.C. Rep. Serv. (Callaghan) 851 (1986).

160. 503 A.2d 646, 42 U.C.C. Rep. Serv. (Callaghan) 462 (Del. Super. 1985).

161. *Id.* at 656, 42 U.C.C. Rep. Serv. at 471.

162. *See, e.g., Tomczuk v. Town of Cheshire*, 26 Conn. Sup. 219, 217 A.2d 71, 3 U.C.C. Rep. Serv. (Callaghan) 147 (1965); *Piercefield v. Remington Arms Co.*, 375 Mich. 85, 133 N.W.2d 129, 2 U.C.C. Rep. Serv. (Callaghan) 611 (1965).

However, a recent case illustrates the apparent trend toward a more expansive interpretation of the section that requires a buyer to notify all sellers or manufacturers in the distribution chain of any breach for which the buyer may seek relief.

In *Wilcox v. Hillcrest Memorial Park*,¹⁶³ the Texas Court of Appeals held that a buyer must notify a remote manufacturer of any breach in order to recover. At trial, the jury found that the “sealer-type casket” that the manufacturer produced and sold to plaintiff’s immediate vendor was unfit for its ordinary purposes. The jury also specifically found that plaintiff had failed to notify the manufacturer of the casket’s unfit condition within a reasonable time. The appellate court reasoned that the purpose of the mandated notice—to afford an opportunity to inspect the goods and cure a breach—was as applicable to remote sellers and manufacturers as to the buyer’s immediate seller.¹⁶⁴

While the Texas Supreme Court affirmed the holding of the court of appeals in *Wilcox* in a per curiam opinion,¹⁶⁵ it specifically refused to consider whether the notice requirement of section 2-607(3)(a) applies to remote sellers and manufacturers, thereby contributing to the uncertainty surrounding this issue. The court of appeals decision in *Wilcox* is a reminder, though, that buyers cannot assume that their immediate sellers will bear the buyers’ burden of providing notice to remote parties and that the failure to give such notice can be fatal.

PERFORMANCE

Creditors

The Third Circuit recently considered whether New Jersey would adopt the subjective “pure heart and empty head” standard for determining good faith purchaser status in *Johnson & Johnson Products v. Dal International Trading Co.*¹⁶⁶ In that case, operating subsidiaries of Johnson & Johnson obtained a preliminary injunction as part of an effort to bar the distribution of Johnson & Johnson products after the goods had worked their way into the so-called “gray market.”¹⁶⁷ Although the route by which the goods came into the hands of defendant, Quality King, was unclear, their journey began when Dal International Trading Co., an instrumentality of the Polish government, acquired them from Johnson & Johnson, Ltd., a British corporation. According to the plaintiffs, J & J, Ltd. sold to Dal only because of Dal’s fraudulent representation that the goods would be distributed solely in Poland.¹⁶⁸ The district court believed

163. 696 S.W.2d 423, 42 U.C.C. Rep. Serv. (Callaghan) 169 (Tex. Ct. App. 1986).

164. *Id.* at 424, 42 U.C.C. Rep. Serv. at 170–71.

165. 701 S.W.2d 842, 42 U.C.C. Rep. Serv. (Callaghan) 1303 (Tex. 1986).

166. 798 F.2d 100, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1082 (3d Cir. 1986).

167. As described by the court, the gray market is “where imported products are sold in the United States outside the manufacturer’s distribution system, often contrary to the wishes of the manufacturer.” *Id.* at 101, 1 U.C.C. Rep. Serv. 2d at 1083.

168. Because the contract was fraudulently induced, the court correctly assumed that Dal obtained voidable title.

that Quality King was not a good faith purchaser under U.C.C. sections 2-403(1) and 2-103(1) and, hence, acquired only the voidable title of Dal.¹⁶⁹ The court's conclusion was premised on its finding that the transaction was conducted under "suspicious circumstances" that "cried out for inquiry."¹⁷⁰

The Third Circuit reversed, holding that whether Quality King was honest in fact is to be determined by what it actually knew or suspected, not by what an investigation into the facts would have arguably disclosed.¹⁷¹ Stating that the purpose of the good faith purchaser doctrine is the promotion of commerce by the reduction of transaction costs, the court thought the doctrine would be ill-served by the imposition on a purchaser of a duty to investigate the conditions surrounding its transferor's acquisition.

Title and Entrusting

*Executive Financial Services v. Pagel*¹⁷² raised the question of whether a buyer who does not take free of an existing security interest under U.C.C. section 9-307(1)¹⁷³ nevertheless can rely on the entrustment theory of U.C.C. section 2-403(2)¹⁷⁴ to render his interest superior to that of the secured creditor. In *Pagel*, the secured creditor purchased several tractors from a John Deere dealership, then "leased"¹⁷⁵ the tractors to a partnership consisting of the two principals of the dealership. The secured creditor expected that the partnership would sublease the tractors to farmers, but instead, the tractors, which never left the dealership's lot, were sold by the dealership in the ordinary course of its business. Because the security interest was not created by the dealership, the buyers did not qualify for the preferred treatment of U.C.C. section 9-307(1).¹⁷⁶ If their interest was protected, it could only be because of U.C.C. section 2-

169. See U.C.C. § 2-403(1): "A purchaser of goods acquires all title which his transferor had or had power to transfer A person with voidable title has power to transfer a good title to a good faith purchaser for value."

170. 798 F.2d at 103, 1 U.C.C. Rep. Serv. 2d at 1085 (citing district court opinion).

171. Although good faith on the part of a merchant requires both "honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade," U.C.C. § 2-103(1)(b), only the first part of the definition received the court's attention. The district court did not find, nor did the plaintiffs produce, evidence that it was the practice in the gray market to investigate the chain of title. 798 F.2d at 106 n.4, 1 U.C.C. Rep. Serv. 2d at 1090 n.4. Nor was there any discussion of whether the failure to investigate was based on fear of what would be found, thus negating good faith.

172. 238 Kan. 809, 715 P.2d 381, 42 U.C.C. Rep. Serv. (Callaghan) 1185 (1986).

173. U.C.C. § 9-307(1) allows a buyer in the ordinary course of business to take free of a security interest created by his seller.

174. U.C.C. § 2-403(2) provides: "Any entrusting of possession of goods to a merchant who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in ordinary course of business."

175. Although the transaction was denominated by the parties as a lease, the court found that it was actually a sale and the creation of a security interest.

176. It could possibly have been argued that the dealership was the alter ego or agent of the partnership, thus making U.C.C. § 9-307(1) applicable.

403(2). Adopting the view of Professor Barkley Clark,¹⁷⁷ the Kansas Supreme Court held that the resolution of priority disputes between secured creditors and subsequent buyers is not the exclusive domain of article 9. Where, as in this case, the secured creditor is the actual entruster, its rights as such are transferred to a buyer in the ordinary course of business.

Although comment 2 to U.C.C. section 2-403 suggests that goods must become part of a merchant's inventory before there can be an entrustment, it does not follow that physical possession by the merchant is needed. *Schneider v. J.W. Metz Lumber Co.*¹⁷⁸ involved the sale of prefabricated log cabin kits. The lumber was provided by a wholesale lumber company and delivered directly to the buyers of the kits. However, it was the log cabin company that was solely responsible for paying the wholesaler. When the log cabin company filed for bankruptcy without having paid the wholesaler, the wholesaler sought recovery from the buyers. In reversing both the trial and intermediate appellate courts, the Colorado Supreme Court held that the effect of the wholesaler's delivery to the buyers was an entrustment to the log cabin company.¹⁷⁹ As a result, the buyers had no difficulty qualifying for buyer in ordinary course treatment under U.C.C. section 2-403(2).

Tender, Cure, and Notice

Few cases of any interest were decided on the issue of tender.¹⁸⁰ In one involving the running of a bankruptcy time period (now repealed), the court held that the period started when delivery was tendered.¹⁸¹ But, as the court said, the repeal of the section made its holding of little precedential value.¹⁸²

Seller's right to cure a defective tender arose in a revocation of acceptance case,¹⁸³ which did not discuss or mention the recently adopted "lemon law."¹⁸⁴ Whether the car was a new car (it was a "demonstrator" with 2,915 miles on it) was not an issue, since the Renault was sold with the AMC limited new car warranty. Also, unlike the "same defect" three times requirement in the lemon laws, many of the numerous returns were for more than ten different defects, with one return requiring a wait of twenty-two days for parts. The trial judge

177. B. Clark, *The Law of Secured Transactions Under the Uniform Commercial Code* § 3.4[3] (1987 Cum. Supp. No. 1). The act of entrustment was the secured creditor's acquiescence in what it believed would be the temporary retention of possession of the tractors by the dealership. *See* U.C.C. § 2-403(3).

178. 715 P.2d 329, 42 U.C.C. Rep. Serv. (Callaghan) 1648 (Colo. 1986).

179. *Id.* at 333, 42 U.C.C. Rep. Serv. at 1651.

180. One case is discussed *infra* notes 194-198 and accompanying text.

181. *Production Steel, Inc. v. Sumitomo Corp.*, 54 Bankr. 417, 42 U.C.C. Rep. Serv. (Callaghan) 1285 (Bankr. M.D. Tenn. 1985).

182. *Id.* at 419 n.1, 42 U.C.C. Rep. Serv. at 1289 n.1. The 45-day period in 11 U.S.C. § 547(c)(2)(B) (1982) had been eliminated by the Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, § 462(c), 98 Stat. 355, 378.

183. *Rester v. Morrow*, 491 So. 2d 204, 1 U.C.C. Rep. Serv. 2d (Callaghan) 751 (Miss. 1986).

184. The Motor Vehicle Warranty Enforcement Act, Miss. Code Ann. §§ 63-17-151 to 63-17-165 (Supp. 1986) (effective July 1, 1985).

granted the dealer's motion for a directed verdict on the ground that the buyer had not shown that any substantial defects remained unrepaired. The Mississippi Supreme Court reversed and remanded by a vote of six to one. Accepting the subjective standard to determine "the unique circumstances of the buyer" but placing a reasonable man in those circumstances, the court ruled that "our law does not allow a seller to postpone revocation in perpetuity by fixing everything that goes wrong with the automobile."¹⁸⁵ At the final rejection, the buyer referred to three minor defects that were still unrepaired.¹⁸⁶ But the court said that emphasis on these defects only concentrated on the "straw [that broke] the camel's back. In our view, the whole camel—including its performance over the five month period [of plaintiff's] use of the Renault—is relevant to the question of whether [plaintiff] had a right to revoke."¹⁸⁷ The dissenting judge did not enter an opinion, stating in a footnote that the case "has been in the bosom of this court far too long."¹⁸⁸

*T & S Brass & Bronze Works v. Pic-Air, Inc.*¹⁸⁹ involved an installment sale of door handles made with tooling supplied by buyer and a defective third installment that was rejected for nonconformity. Buyer did not return the goods after rejection but was entitled to keep the goods until it was paid the cost of inspecting and sorting the conforming from the defective products.¹⁹⁰ The handles were made available at buyer's facility, constituting no acceptance or waiver of the right to reject. Seller refused to acknowledge responsibility to cure until past the time for performance. This not only lost seller the right to cure but also rendered seller liable in conversion for failure to return the tooling on demand. The buyer's acceptance of the first two shipments was asserted as the basis for seller's belief that the third installment was acceptable and that seller had a further reasonable time to cure. The failure to give any notice of intent to cure forfeited the reasonable time and the failure to give notice of intent to cure destroyed the defense to conversion of the tooling as no notice was given by the bailee that retention after a demand for return was to enable fulfillment of the purpose of the bailment.¹⁹¹

Two cases, however, protect the seller's right to cure. Where the buyer failed to state particular defects and refused to permit seller to inspect the defective

185. 491 So. 2d at 210, 1 U.C.C. Rep. Serv. 2d at 759.

186. These were soiled carpet (from water leaking on it), a fallen fuse panel, and a missing piece of chrome. *Id.* at 208, 1 U.C.C. Rep. Serv. 2d at 759.

187. *Id.* at 210, 1 U.C.C. Rep. Serv. 2d at 760.

188. *Id.* at 212 n.1, 1 U.C.C. Rep. Serv. 2d at 762 n.1 (Hawkins, J., dissenting). The car was purchased in April 1981 and the opinion remanding for a new trial on all issues was rendered in June 1986. Justice delayed is justice denied.

189. 790 F.2d 1098, 1 U.C.C. Rep. Serv. 2d (Callaghan) 433 (4th Cir. 1986).

190. U.C.C. § 2-603(1), requiring a rejecting buyer to follow reasonable instructions, is subject to U.C.C. § 2-711(3), giving the buyer a security interest in the rightfully rejected goods for payments made and expenses reasonably incurred in their inspection, receipt, transportation, care, and custody.

191. 790 F.2d at 1106, 1 U.C.C. Rep. Serv. 2d at 444. Under neither the common law of bailments nor the U.C.C., had Pic-Air shown a right to retain the tooling.

goods, buyer was not allowed to rely on these defects as a defense to a suit for the purchase price.¹⁹² The court based its denial on U.C.C. section 2-605, which has three bases for precluding the assertion of unstated defects. The first is that the defects must be ascertainable by reasonable inspection. The second and third are in the alternative (but one must be shown), either that the defect could have been cured, as in the case under discussion, or (as between merchants) that a written demand for a full and final inspection has been made and is answered.

The second case involved a rejection of one installment of concrete sewer pipe for failure to meet buyer's specifications.¹⁹³ There was a prompt shipment of cure with fully complying pipe. Buyer attempted to cancel the entire contract since the supplier also had been obliged to cure prior defective shipments. The buyer also attempted to recover for excess costs in ordering cover. Because the supplier covered promptly and within the time for delivery of each installment, the court refused a subjective test for "substantial impairment" under U.C.C. section 2-612(2) and reversed the judgment below, which had awarded the buyer the costs of cover.

Risk of Loss

Only one case discussed risk of loss as a major issue. In *Ladex Corp. v. Transportes Aereos Nacionales, S.A.*,¹⁹⁴ frozen shrimp was to be sold by a Honduras company to Ladex in Miami. The shrimp arrived at Miami International Airport and were turned over to a trucking firm for delivery to Ladex's warehouse. The court then observed that "although the facts are somewhat sketchy on the record before us, we perceive that the truck containing the shipment of shrimp was hijacked while still in the loading area of the airport."¹⁹⁵ Suit was brought by Aetna Insurance Company (as subrogee of Ladex) for common law conversion against the carriers. The carriers contended that since Ladex had never paid for the shrimp, it had suffered no loss. On this basis, the trial court entered a final summary judgment for the carriers.

A Florida appellate court reversed on the ground that the all-important issue was whether Ladex had title to the shrimp at the time they were hijacked.¹⁹⁶ Thus, despite the rule of U.C.C. section 2-401—that the provisions of the Code apply irrespective of title to the goods—courts still are swayed by concepts of title. The real problem was, when did risk of loss pass to the buyer? This was governed by U.C.C. section 2-509(1) and depended on whether the contract was a shipment contract or a destination contract—without regard to title. Carrier liability for common law conversion may still depend on title, however.

192. *A.F.L. Falck, S.p.A. v. E.A. Karay Co.*, 639 F. Supp. 314, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1500 (S.D.N.Y. 1986).

193. *Bodine Sewer, Inc. v. Eastern Ill. Precast, Inc.*, 143 Ill. App. 3d 920, 493 N.E.2d 705, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1480 (1986).

194. 476 So. 2d 763, 42 U.C.C. Rep. Serv. (Callaghan) 133 (Fla. Dist. Ct. App. 1985).

195. *Id.* at 764, 42 U.C.C. Rep. Serv. at 134.

196. *Id.* at 764, 42 U.C.C. Rep. Serv. at 135.

The court correctly ruled that the fact that Ladex had not paid for the goods, if title had passed, was not an issue available to the carriers in a common law conversion action under U.C.C. section 1-103. Yet, the court noted that if the action had been for nondelivery by the consignee of a nonnegotiable bill, U.C.C. section 7-301 would limit recovery to one who has paid value.¹⁹⁷ In dicta, which may be the law of the case, the court stated that a contract C.I.F. or C&F is a shipment contract on the normal contract terms that are so well known that any variation using those letters should be read as a shipment contract, if reasonably possible. A destination contract was the variant contract and must be expressly agreed upon by the parties.¹⁹⁸ But since the record was not fully developed on the type of contract (again referred to in the context of determining who had title as a matter of law), the case was remanded for further proceedings.

The court does not make clear who had rights of recovery if title passes contractually under U.C.C. section 2-401 at a different time from the risk of loss under U.C.C. section 2-509(1).

Repudiation

Despite the fact that the doctrine of anticipatory repudiation is well over a hundred years old, courts appear reluctant to permit suit on that basis without a very clear refusal by a party to perform. Hence, to obtain a clear repudiation, use is made of the demand for assurances in U.C.C. section 2-609(1). But its requirements that the demand be in writing, be based on reasonable grounds for insecurity, and be for "adequate" assurances only create issues as to whether the failure to reply, or what is offered in reply, really triggers a repudiation.

Seldom are the facts as clear as those before the court in *Barclays American / Business Credit v. E & E Enterprises*.¹⁹⁹ On July 16, 1982, a seller of wood products informed the buyer/cabinet maker that it was closing its plant that day and would not deliver under two purchase orders for delivery in July and August. The seller added that the only way to receive the deliveries was to talk to the vice president of Barclays, which was the company financing seller's receivables. Despite the reference to a way of receiving delivery, the court ruled that July 16, 1982 was the date of the repudiation. The date of the repudiation was important as buyer was claiming that its damages for the repudiation could be set off against some \$76,105 it owed seller on prior contracts. Buyer received notice of the assignment of the accounts receivable to Barclays on July 28, 1982.²⁰⁰ Had the buyer used a U.C.C. section 2-609 demand on July 16, 1982,

197. U.C.C. § 7-301(1) states: "A consignee of a non-negotiable bill who has given value in good faith . . . may recover from the issuer damages caused by . . . non-receipt . . . of the goods." This section contains an exception not significant in the case being discussed. The implication is: no value given, no recovery. But, if risk of loss passes, the contractual obligation to pay becomes fixed and so would be value.

198. 476 So. 2d at 765, 42 U.C.C. Rep. Serv. at 135-36.

199. 697 S.W.2d 694, 42 U.C.C. Rep. Serv. (Callaghan) 706 (Tex. Ct. App. 1985).

200. This was by letter. 697 S.W.2d at 696, 42 U.C.C. Rep. Serv. at 709. The court said that the primary issue was whether the buyer's setoff was good against the assignee of the wood products

thirty days would not have expired until August 15, 1982, and the repudiation and consequent setoff would not have occurred before receipt of the notice of the assignment. Thus, the appellate court found no error in the trial court's finding.

Indeed, in a footnote,²⁰¹ the court said that even if the statement about talking to the vice president was notice of an assignment, it came after the statement that the plant was closed. Hence, the repudiation would still have occurred before the account debtor received notice of the assignment.

Interestingly, the court relied on the timing of the repudiation as a breach and did not rule on the effect of a promise, stipulated to have been made, to give the buyer sixty days notice before shutting down the plant, which also occurred on the same day as the conversation about no more deliveries.²⁰²

In *T & S Brass & Bronze Works v. Pic-Air, Inc.*,²⁰³ fortunately no great issue hung on when breach occurred. Pic-Air was the seller in a case involving the third delivery of allegedly nonconforming goods under an installment contract. Pic-Air attempted to claim buyer's repudiation by reason of a letter that summarized a conference three days before and said that "we [T & S] would be happy to take the parts provided they passed inspection" and added that "'T & S' could not make any further payments to Pic-Air until such time as this entire matter is cleared-up." The court upheld (as not clearly erroneous) the magistrate's conclusion that these sentences, in context, constituted only a demand for assurances.²⁰⁴ Thus, factual issues seem inevitable in anticipatory repudiation cases.

Impossibility and Frustration

There was both good news and bad news this year for those seeking excuse based on impracticability under U.C.C. section 2-615.

First the good news. Two cases excused sellers under U.C.C. section 2-615. In *Waldinger Corp. v. CRS Group Engineers*,²⁰⁵ the mechanical subcontractor (Waldinger) on a water treatment facility construction project sued its supplier of sludge dewatering equipment (Ashbrook) for breach of contract. Ashbrook

company's receivables, i.e., that the right to set off "ripened" before receipt of notice of the assignment. Cf. U.C.C. § 9-318.

201. 697 S.W.2d at 700 n.3, 42 U.C.C. Rep. Serv. at 714 n.3.

202. Barclays, on appeal, argued that the 60-day notice promise did not constitute a contract because there was no consideration to support the promise. Thus, by finding it unnecessary to decide whether the evidence supported the trial court's findings, the court chose to prefer an anticipatory repudiation over a present breach to support its affirmance.

203. 790 F.2d 1098, 1 U.C.C. Rep. Serv. 2d 433.

204. *Id.* at 1194, 1 U.C.C. Rep. Serv. 2d at 441. *Universal Builders Corp. v. United Methodist Convalescent Homes*, 7 Conn. App. 318, 1 U.C.C. Rep. Serv. 2d (Callaghan) 763 (1986), is a similar case. Roof trusses were to be supplied on a continuous basis. When deliveries were slow, buyer wrote the seller saying, among other things, "Unless a minimum of 200 trusses are delivered by July 5, 1983, you may consider your order cancelled." *Id.* at —, 1 U.C.C. Rep. Serv. 2d at 765. The court interpreted this not as a repudiation, but as a request for assurances. By not giving such assurances, the seller repudiated, but at a date 30 days later.

205. 775 F.2d 781, 42 U.C.C. Rep. Serv. (Callaghan) 172 (7th Cir. 1985).

defended on the ground that its performance had been made impracticable by the project engineer's arbitrary interpretation of the contract specifications. Waldinger also sued the project engineer. Before Ashbrook bid on the project, it knew that the project engineer might not approve the machine it intended to use. Ashbrook also signed a purchase order prepared by Waldinger stating that the machine would be subject to the project engineer's approval and that the machine would be "in strict accordance" with the specifications. When Ashbrook failed to perform, Waldinger had to cover at an additional cost of about \$370,000. At trial, Waldinger prevailed against the project engineer, but Ashbrook was excused for impracticability. On appeal, the Seventh Circuit affirmed on the impracticability question (Judge Pell dissenting) and remanded the question of the project engineer's liability for reconsideration in light of case law decided after the trial court's judgment. Perhaps the decision on the impracticability question can be explained upon the ground that on remand Waldinger will almost certainly recover damages from the project engineer.

The second case is *Alimenta (U.S.A.), Inc. v. Gibbs Nathaniel (Canada) Ltd.*²⁰⁶ Here the parties, both international dealers in agricultural commodities, made three contracts for fixed quantities of "1980 crop U.S. runner split peanuts." The seller (Gibbs) was unable to perform fully because extensive drought in the peanut growing areas had reduced the crop. The seller prorated and eventually delivered eighty-seven percent of the contract quantity. It would have cost the seller \$3.8 million to purchase peanuts to fulfill the remainder of its obligations under the contracts; yet, seller's net worth was only \$2.4 million. Further, the seller had anticipated a profit of only \$18,000 on the Alimenta contracts. On these facts, the trial court excused the seller under U.C.C. section 2-615. On appeal, the Eleventh Circuit affirmed. This court (and the parties) appear to have treated the contract as one stipulating an agreed source ("1980 crop U.S. runner split peanuts") that had partially failed, thus, permitting the seller to allocate.²⁰⁷

In two cases, buyers sought excuse from long-term installment contracts that had become burdensome because of changed circumstances. In both cases, the courts refused to excuse. The first case was *Northern Indiana Public Service Co. v. Carbon County Coal Co.*²⁰⁸ In 1978, when oil prices were high, a utility company entered into a twenty-year contract for 1.5 million tons of coal per year. The price was fixed subject to escalation. The court noted that the utility company entered into a contract fixed as to both quantity and price rather than a requirements contract because it was eager to have an assured source of low-sulphur coal. With falling oil prices in the early 1980s, the contract had become

206. 802 F.2d 1362, 2 U.C.C. Rep. Serv. 2d (Callaghan) 490 (11th Cir. 1986).

207. Another case involving the failure of an agreed source of supply was *Selland Pontiac-GMC, Inc. v. King*, 384 N.W.2d 490, 1 U.C.C. Rep. Serv. 2d (Callaghan) 463 (Minn. Ct. App. 1986) (seller excused under U.C.C. § 2-615 from performance of contract for sale of school bus bodies that seller was to obtain from specified manufacturer, who subsequently went out of business).

208. 799 F.2d 265, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1505 (7th Cir. 1986).

expensive relative to the utility company's other alternatives for obtaining electricity. The Indiana Public Service Commission, which regulated the utility company's rates, declined to permit the utility company to continue to pass that expense on to its customers. The utility company then ceased to purchase coal under the contract. The seller obtained a preliminary injunction requiring the utility company to continue buying coal. After a jury trial, the seller won a judgment of \$181 million. On appeal, Judge Posner, writing for the court, affirmed the trial finding that the utility was not excused from its obligations under the contract.

In the second case, *Scullin Steel Co. v. Paccar, Inc.*,²⁰⁹ the buyer sought excuse from its obligations under a two-year (later extended to four-year) contract to purchase a fixed monthly quantity of railroad "car sets" because the buyer's market for railroad cars had evaporated. The trial court refused to excuse the buyer. On appeal, the Missouri Court of Appeals affirmed. This case is a good example of explicit risk allocation. The appellate court stressed that the seller wanted (as the buyer knew) a long-term contract in which the buyer guaranteed to take delivery so that the seller could obtain financing to make capital improvements to its plant. Thus, the seller proposed a contract stipulating that it could not be cancelled by either side. The buyer responded with a clause permitting it to withdraw from the contract should it cease manufacturing rail cars, but the seller refused to agree to such a clause. Eventually, the buyer signed the contract with the noncancellation clause. Under the circumstances, it is apparent that the buyer assumed the risk that its market might disappear.²¹⁰

REMEDIES

Rejection and Revocation of Acceptance

Central to a buyer's right of rejection or revocation of acceptance is the statutory mandate that the relevant intention must be communicated to the seller.²¹¹ *Oda Nursery v. Garcia Tree & Lawn, Inc.*²¹² provides a lesson on the need to make explicit that the goods are no longer wanted. That case involved the purchase of spreading juniper plants. Following their receipt by the buyer, the plants were inspected but were not removed from their shipping containers until planted some four months later. When sued for the purchase price, the buyer argued that the plants were root-bound and had been rejected shortly after delivery. Relying on the testimony of one of the buyer's employees that she had immediately notified the seller that the plants did not look "up to snuff," the trial judge found a timely and effective rejection.

On appeal, the New Mexico Supreme Court reversed. The court felt that the statement of the employee was insufficient to put the seller on notice that the

209. 708 S.W.2d 756, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1172 (Mo. Ct. App. 1986).

210. The court also addressed an issue concerning computation of the seller's lost profits under U.C.C. § 2-708(2).

211. See U.C.C. §§ 2-602, 2-608.

212. 103 N.M. 438, 708 P.2d 1039, 42 U.C.C. Rep. Serv. (Callaghan) 163 (1985).

plants were being rejected or that their acceptance was being revoked.²¹³ Furthermore, the court found the notice lacking under U.C.C. section 2-605 because the employee did not mention the plants' deteriorating or root-bound condition.

The result is correct but the court's reference to section 2-605 is puzzling. Because notice to the seller of a breach is required even if the buyer wishes to retain the goods,²¹⁴ it is logical to impose on the buyer a further obligation to let the seller know if the goods are not wanted. In the absence of a request by the seller, however, specificity of defects is needed only to enable the seller to exercise its right of cure.²¹⁵ Nowhere in its opinion does the court explain its apparent assumption that that right existed.

On the subject of notice, uncertainty exists as to whether it must be given in writing to be effective. Although the Code's definition of notice²¹⁶ would seem to allow oral notice and nothing in article 2 suggests otherwise, some courts have held that a written communication is essential.²¹⁷

Reclamation

The intermesh of Bankruptcy Code section 546(c)²¹⁸ and state law continues to be the subject of frequent litigation. Consider, for example, the recurring efforts of unpaid sellers to reclaim goods that are subject to the lien of a secured party who financed the inventory of the debtor. The vast majority of courts hold that the unpaid seller's right of reclamation under U.C.C. section 2-702 is subordinate to the interest of a secured party (as a good faith purchaser) in those same goods.²¹⁹ Not willing to concede the worthlessness of a subordinated reclamation right, sellers have now begun to seek solace in Bankruptcy Code section 546(c)(2), which authorizes substitution of an administrative expense claim or alternative lien for the claim of a right of reclamation.

213. The court stated that even if the plants had been effectively rejected, their subsequent planting was an act of dominion inconsistent with the seller's ownership, thus amounting to a reacceptance. *Id.* at 442, 708 P.2d at 1043, 42 U.C.C. Rep. Serv. at 168-69. The court also rejected the buyer's contention that its answer, filed as part of the lawsuit, was a sufficient notice of revocation of acceptance. As a matter of law, the court concluded that notice given approximately one year after delivery of the plants is clearly unreasonable. *Id.*

214. See U.C.C. § 2-607(3)(a).

215. The seller's limited right to cure a defective tender is found in U.C.C. § 2-508.

216. U.C.C. § 1-201(26).

217. *American Fast Print Ltd. v. Design Prints*, 288 S.C. 46, 339 S.E.2d 516, 42 U.C.C. Rep. Serv. (Callaghan) 1294 (Ct. App. 1986). The court felt constrained to rule as it did by that state's supreme court opinion in *Southeastern Steel Co. v. Burton Block & Concrete Co.*, 273 S.C. 634, 258 S.E.2d 888, 26 U.C.C. Rep. Serv. (Callaghan) 1151 (1979). The need for written notice was squarely rejected in *Badger Produce Co. v. Prelude Foods Int'l*, 130 Wis. 2d 230, 387 N.W.2d 98, 1 U.C.C. Rep. Serv. 2d (Callaghan) 422 (Ct. App. 1986).

218. 11 U.S.C. § 546(c) (Supp. III 1985).

219. Although involving the respective rights of unpaid *cash* sellers and a secured creditor, *In re Samuels & Co.*, 510 F.2d 139 (5th Cir. 1975), *rev'd on reh'g en banc*, 526 F.2d 1238 (5th Cir.), *cert. denied*, 429 U.S. 834 (1976), is considered the landmark case upholding the priority of the secured creditor.

In *In re Misco Supply Co.*,²²⁰ the district court held that the unpaid seller was entitled to an administrative priority or a lien on all of the debtor's unencumbered assets. Recognizing that application of Bankruptcy Code section 546(c)(2) depends upon a right of reclamation under state law, the court reached the dubious conclusion that although "subject to" the secured party's interest, the right of reclamation, nevertheless, continued to exist.²²¹ It is difficult to understand the court's logic. It makes little sense to compensate a seller for a right having no value and, by so doing, give that seller more than it would be entitled to in the absence of a bankruptcy. Fortunately, not all courts have been so magnanimous.²²²

Finally, courts continue to grapple with the question of whether the drafters used "insolvency" in Bankruptcy Code section 546(c) in the sense in which it is used in U.C.C. section 2-702,²²³ or in the sense in which it is generally used in the Bankruptcy Code.²²⁴ Authority for either position is growing.²²⁵

Buyer's Money Remedies

The proper measure of damages for breach of the warranty of title was considered for the first time by a Maryland court in *Metalcraft, Inc. v. Pratt*.²²⁶ The case arose out of the sale of a marine hardware casting business. As things turned out, the seller did not own a number of marine hardware casting patterns it purportedly sold, leaving the buyer little choice but to return these items to their respective owners. The trial court awarded as damages the value of the patterns at the date of dispossession. The buyer asserted, however, that U.C.C. section 2-714(2) was controlling and that damages should be measured by the "difference at the time and place of acceptance between the value of the goods accepted and the value they would have had . . . as warranted."²²⁷

220. 42 U.C.C. Rep. Serv. (Callaghan) 1662 (D. Kan. 1986).

221. District Judge Kelly distinguished the present case from one where the right of reclamation is *lost* as a result of the debtor's *sale* of the goods to a good faith purchaser. If the right of reclamation is *lost*, then there is no right to priority treatment under § 546(c)(2). *Id.* at 1667.

222. See *In re Lawrence Paperboard Corp.*, 52 Bankr. 907, 42 U.C.C. Rep. Serv. (Callaghan) 185 (Bankr. D. Mass. 1985) (if secured party's lien precludes reclamation there is no right to alternative relief); *In re FCX, Inc.*, 62 Bankr. 315, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1193 (Bankr. E.D.N.C. 1986) (same).

223. See U.C.C. § 1-201(23): "A person is 'insolvent' who either has ceased to pay his debts in the ordinary course of business or cannot pay his debts as they become due or is insolvent within the meaning of the federal bankruptcy law."

224. See 11 U.S.C. § 101(29) (Supp. III 1985): "[A]n entity other than a partnership" is insolvent if "the sum of such entity's debts is greater than all of such entity's property."

225. Compare *In re Flagstaff Foodservice Corp.*, 56 Bankr. 899, 1 U.C.C. Rep. Serv. 2d (Callaghan) 96 (Bankr. S.D.N.Y. 1986) (Bankruptcy Code definition is controlling) with *In re AIC Photo, Inc.*, 57 Bankr. 56, 1 U.C.C. Rep. Serv. 2d (Callaghan) 90 (Bankr. E.D.N.Y. 1986) (the U.C.C. definition should be applied).

226. 65 Md. App. 281, 500 A.2d 329, 42 U.C.C. Rep. Serv. (Callaghan) 14 (1985).

227. U.C.C. § 2-714(2). According to the buyer, the value of the patterns when accepted was zero because the seller did not own them. Thus, the buyer claimed damages in an amount equal to

Therefore, the point of contention was over whether the buyer should be permitted to enjoy the use of the patterns without any offset for depreciation.

On appeal, the appellate court held that the measure of damages selected by the trial court was correct. Notwithstanding case law supporting the buyer's position²²⁸ and uncertainty among scholars concerning the applicability of U.C.C. section 2-714(2) to a breach of warranty of title,²²⁹ the court thought the section "plain and unambiguous" and manifesting a legislative intent that it apply to all breaches of warranty under the U.C.C.²³⁰ The court next turned to the question of whether there were "special circumstances" to take the case out of the ordinary U.C.C. section 2-714(2) rule.²³¹ Because the buyer had use and possession of the unique patterns for varying periods of time before title defects surfaced, the court concluded that the case did fall within the special circumstances clause of U.C.C. section 2-714(2) and that only the measure of damages selected by the trial court would give the buyer the benefit of its bargain without overcompensation.

At issue in "one of the longest relative to the stakes" lawsuits,²³² was a disappointed buyer's duty of mitigation. In *Cates v. Morgan Portable Building Corp.*,²³³ the buyers, owners of a motel, ordered portable buildings that would add ten rooms to the motel. The buildings were delivered in defective condition in September 1970. The seller made feeble attempts at repair until March 1971. Suit was filed in August 1971. In September 1973, the parties agreed that the seller would again try to repair the rooms. Between that date and April 1975, intermittent attempts at repair were made but without success. The rooms were finally put into working order by the buyers, at their own expense, sometime after April 1975. The trial judge awarded lost profits for two periods: September 1, 1970, to September 30, 1971, and September 11, 1973, to April 30, 1975. The court denied lost profits for the intervening period, October 1, 1971, to September 10, 1973, because the buyers had failed to mitigate their damages.

In an opinion heavily laden with common law references, the Seventh Circuit Court of Appeals affirmed. Writing for the court, Judge Posner agreed with the

the value of the patterns at the time of the sale. 65 Md. App. at 291, 500 A.2d at 335, 42 U.C.C. Rep. Serv. at 19.

228. See, e.g., *Murdock v. Godwin*, 154 Ga. App. 824, 269 S.E.2d 905, 31 U.C.C. Rep. Serv. (Callaghan) 572 (1980).

229. The court cited several scholars who argue that U.C.C. § 2-714(2) is irrelevant to breach of warranty of title claims. 65 Md. App. at 292, 500 A.2d at 335, 42 U.C.C. Rep. Serv. at 19 (citing R. Anderson, *Uniform Commercial Code* § 2-714:26 (3d ed. 1983); 2 A. Squillante & J. Fonseca, *Williston on Sales* § 16-8(2) (4th ed. 1974)).

230. *Id.* at 293, 500 A.2d at 336, 42 U.C.C. Rep. Serv. at 20-21.

231. The measure of damages provided by U.C.C. § 2-714(2) was never intended to be an exclusive measure. That same subsection permits use of an alternative formula if "special circumstances show proximate damages of a different amount."

232. This was Judge Posner's characterization of the case, which, when he authored the court's opinion, was in its fifteenth year of life. *Cates v. Morgan Portable Bldg. Corp.*, 780 F.2d 683, 685, 42 U.C.C. Rep. Serv. (Callaghan) 451, 452 (7th Cir. 1985).

233. *Id.*

trial court that although the U.C.C. imposes a duty to mitigate,²³⁴ that duty was suspended when the seller promised to fix the homes shortly after they were delivered.²³⁵ This suspension ended, however, at the expiration of a reasonable period of time after April 1971, when it first became clear that the seller would not make the necessary repairs. Judge Posner was unwilling to say that the trial court's "guess" that six months was a reasonable period was clearly erroneous.²³⁶ Therefore, it was not until October 1971 that the buyers had to take steps to mitigate their losses. This duty was again suspended from September 1973 to April 1975, when the buyers were once more led to believe that the seller would remedy the situation. The court squarely rejected the buyers' argument that a duty of mitigation never arose because the seller always had an equal opportunity to mitigate. As the court saw it, recognition of a so-called equal opportunity doctrine is "discordant with common law principles, which demand a reason for not letting losses lie where they fall."²³⁷ In particular, the doctrine would take from buyers the incentive to cut losses even though the buyer can do so more efficiently than the seller.

U.C.C. section 2-718(1) provides that "[d]amages for breach by either party may be liquidated in the agreement." The parties are warned, however, that not every liquidated damages provision will be acceptable. If it is a "penalty" it is void.²³⁸ To be labelled nonpenal, the liquidated amount must be "reasonable in the light of the anticipated *or* actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy."²³⁹

Whether the agreed upon formula met this standard was the issue before the Ninth Circuit in *California and Hawaiian Sugar Co. v. Sun Ship, Inc.*²⁴⁰ The buyer, an agricultural cooperative in the business of transporting raw sugar from Hawaii to California, ordered an oceangoing barge for delivery no later than June 30, 1981. The parties agreed that the seller would pay, as liquidated damages, the sum of \$17,000 per day should delivery be delayed. The barge was

234. See U.C.C. § 1-106 comment 1.

235. On this point, the court stated that "the seller may not insist on mitigation when by its words or deeds it has led the buyer to believe that it has assumed what would otherwise be the buyer's burden of mitigation." 780 F.2d at 687, 42 U.C.C. Rep. Serv. at 454.

236. The appellate court disagreed with the district court's ruling that under Illinois law the burden of proof on the issue of mitigation rested with the buyers, but it thought the error harmless since allocation of the burden did not seem to affect the trial judge's decision. *Id.* at 688, 42 U.C.C. Rep. Serv. at 455-56. Although one other case decided during this survey period reached a similar conclusion, see *Carnation Co. v. Olivet Egg Ranch*, 229 Cal. Rptr. 261, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1531 (Ct. App. 1986), not all courts place the burden of proof on the mitigation of damages issue on the breaching seller, see, e.g., *M.K. Metals, Inc. v. Container Recovery Corp.*, 645 F.2d 583, 31 U.C.C. Rep. Serv. (Callaghan) 487 (8th Cir. 1981); *Cargill, Inc. v. Fickbohm*, 252 N.W.2d 739, 21 U.C.C. Rep. Serv. (Callaghan) 1226 (Iowa 1977).

237. 780 F.2d at 689, 42 U.C.C. Rep. Serv. at 457.

238. U.C.C. § 2-718(1): "A term fixing unreasonably large liquidated damages is void as a penalty."

239. *Id.* (emphasis added).

240. 794 F.2d 1433, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1211 (9th Cir. 1986).

not delivered when promised and liquidated damages grew to the not insignificant sum of approximately four million dollars. Although the provision was admittedly reasonable when the contract was negotiated, the seller claimed it was operatively a penalty when, as things turned out, the net actual loss sustained by the buyer was \$368,000.²⁴¹

Looking to Pennsylvania law for guidance,²⁴² the Ninth Circuit thought that, despite the statutory disjunctive for testing the validity of the provision, state courts would take into account equitable considerations along with the difficulty of establishing actual damages if the clause was rejected. But this professed willingness to read U.C.C. section 2-718 in light of common law principles proved to be of no help to the seller. In the end, the court was swayed by the relative sophistication of the parties and its belief that “[c]ontracts are contracts because they contain enforceable promises, and absent some overriding public policy, those promises are to be enforced.”²⁴³ The district court’s judgment upholding the enforceability of the liquidated damages provision was affirmed in all respects.

In *Frank B. Bozzo, Inc. v. Electric Weld Division of the Fort Pitt Division of Spang Industries*,²⁴⁴ the Pennsylvania Superior Court was called upon to decide whether a buyer is entitled to have tacked on to its judgment interest from the date on which the contract was breached. The seller contended that such recovery is unavailable where the amount of damages occasioned by the breach was, before judgment, neither liquidated nor ascertainable. The court disagreed. In its opinion, the award was not interest but rather “compensation for delay” measured by the legal rate of interest.²⁴⁵ As such, it is an appropriate item of incidental damages under U.C.C. section 2-715 if necessary to put the buyer in “as good a position as if the other party had fully performed.”²⁴⁶ The court offered the illustration of a buyer unable to earn interest on money that had to be spent to meet the expenses incident to the seller’s breach.²⁴⁷ The court then remanded the case to the trial court to determine whether the circumstances warranted an award of compensation for delay.

241. The anticipated damages were based on expectations of rotting sugar and sugarless customers if the barge could not be used to transport the sugar from Hawaii to California. Substantial losses were avoided only because the buyer succeeded in finding other shipping.

242. The contract made Pennsylvania law controlling, presumably because the seller’s principal place of business was in Pennsylvania.

243. 794 F.2d at 1438, 1 U.C.C. Rep. Serv. 2d at 1218. The buyer also claimed that it suffered \$3,732,000 in lost charter revenues. The trial court made no finding on this claim and the Ninth Circuit was apparently under the impression that the exact loss, if any, would be difficult to prove. What effect the presence of this claim had on the outcome of the case is difficult to measure. *See id.* at 1439, 1 U.C.C. Rep. Serv. 2d at 1219.

244. 345 Pa. Super. 423, 498 A.2d 895, 42 U.C.C. Rep. Serv. (Callaghan) 213 (1985).

245. *Id.* at 431, 498 A.2d at 899, 42 U.C.C. Rep. Serv. at 218. The court refused to decide whether this distinction is of any significance.

246. The quoted portion in the text is that part of U.C.C. § 1-106 that the court found persuasive.

247. 345 Pa. Super. at 430, 498 A.2d at 898, 42 U.C.C. Rep. Serv. at 216.

The superior court was correct in its observation that at times full compensation cannot be had without delay damages. But if full compensation is the goal, should not the recovery be measured by the rate of interest the buyer would otherwise have received rather than what will often be a lower statutory rate of interest?

Seller's Money Remedies

The Supreme Court of Washington, in *Sprague v. Sumitomo Forestry Co.*,²⁴⁸ discussed several questions pertaining to a seller's U.C.C. section 2-706 right to resell goods (that are the subject of a breach) at a private sale and recover the difference between the resale price and the contract price. In August 1980, the parties entered into a contract for the sale of timber with an agreed upon delivery date of "1980." In October 1980, the buyer, without justification, sent a letter to the seller unequivocally cancelling the contract. Suit soon followed. In its answer, the buyer alleged only that seller was under a duty to mitigate its damages. The seller responded by selling the timber to five different purchasers at private sales. The major thrust of the buyer's argument, rejected by the trial court and asserted on appeal, was the seller's failure to give the statutory mandated "reasonable notification of his intention to sell."²⁴⁹

First, the court held that because notice of intent to sell is part of the seller's prima facie case, the buyer is not required to plead lack of notice as a defense.²⁵⁰ It then concluded that neither the filing of the complaint nor the buyer's knowledge that the goods would be sold can substitute for the statutory notice.²⁵¹ Despite the seller's nonentitlement to damages under U.C.C. section 2-706, the court affirmed on the basis of U.C.C. section 2-708(1).²⁵² By concluding that the resale price sufficed as proof of market price, the court was able to alter the measure of damages but not the result.²⁵³

The case nicely illustrates the remedial flexibility of the U.C.C. No election of remedies is required and the aggrieved party may freely assert alternative measures of damages. But one party's flexibility can easily become a trap for the other. The party in breach must be always alert to the different potential uses of the same evidentiary fact.

Because the Code provides alternative measures of damages, it is inevitable that the aggrieved party will claim the applicability of the measure that provides the highest award. The extent to which a seller is permitted to pick and choose

248. 104 Wash. 2d 751, 709 P.2d 1200, 42 U.C.C. Rep. Serv. (Callaghan) 202 (1985).

249. U.C.C. § 2-706(3).

250. 104 Wash. 2d at 757, 709 P.2d at 1204, 42 U.C.C. Rep. Serv. at 206.

251. *Id.* at 758, 709 P.2d at 1204, 42 U.C.C. Rep. Serv. at 207. The court was careful to limit its decision to the form of complaint before it. The complaint made no mention of an intention to resell but sought only damages for breach. *Id.*

252. U.C.C. § 2-708(1) establishes damages by computing the difference between the market price and the contract price.

253. 104 Wash. 2d at 758, 709 P.2d at 1205, 42 U.C.C. Rep. Serv. at 208.

was before the court in *Union Carbide Corp. v. Consumers Power Co.*²⁵⁴ The case involved a contract for the purchase of large quantities of residual fuel oil. The seller, Union Carbide, planned to obtain the oil from Petrosar Limited and resell to Consumers at a price computed on the basis of the amount paid to Petrosar. As a result, Union Carbide was guaranteed a fixed profit on each barrel of oil that Consumers accepted. Subsequently, there was a sharp drop in the market price of the oil, which, because it was not passed on to Consumers, prompted Consumers to refuse further deliveries.

Crucial to a determination of the extent of Consumers's liability was which subsection of U.C.C. section 2-708 controlled. Atypically, it was the seller, Union Carbide, who argued for application of subsection (1). A market price differential measure of damages would yield the hefty sum of approximately \$120 million, whereas the profit actually lost on account of the breach amounted to a mere \$30 million. Relying on the remedial policy expressed in U.C.C. section 1-106,²⁵⁵ the court ruled that the reference in the preamble to subsection (2) to the "inadequacy" of subsection (1)'s damages formula was intended to include cases of overcompensation as well as undercompensation.²⁵⁶ Emphasizing the limited applicability of the decision, the court held that where, as here, the seller acts as a middleman who assumes no risk of price fluctuations and the buyer proves that market price damages will result in overcompensation, damages should be calculated under U.C.C. section 2-708(2).

Although the result seems sound, the court can be faulted for its failure to recognize the true problem. U.C.C. section 2-708(1) was never intended to apply and its use, therefore, is never appropriate where the seller has never acquired the contract goods.²⁵⁷

Although the U.C.C. does not expressly recognize a seller's right to recover consequential damages,²⁵⁸ such a recovery is possible if the "lost profit" language of U.C.C. section 2-708(2) is liberally applied. In *Rogerson Aircraft Corp. v. Fairchild Industries*,²⁵⁹ the seller agreed to manufacture component parts for an aircraft being developed by the buyer. Following the buyer's wrongful termination of the contract, seller sought recovery for lost profits, including what it claimed to have lost as a consequence of being shut out of the existing aftermarket for spare parts and profits it would have earned on prospective parts supply contracts with third-party aircraft manufacturers. Quite clearly, both claims are essentially for consequential damages. Neverthe-

254. 636 F. Supp. 1498, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1202 (E.D. Mich. 1986).

255. U.C.C. § 1-106 states: "The remedies provided by this act shall be liberally administered."

256. U.C.C. § 2-708(2) is applicable only "[i]f the measure of damages provided in subsection (1) is inadequate to put the seller in as good a position as performance would have done."

257. The formula of U.C.C. § 2-708(1) is premised on the ability of the seller to recoup a portion of its loss by making a substitutionary disposition of the contract goods. This is, of course, impossible if, at the time of the breach, the seller has not yet put itself into position to resell the goods.

258. U.C.C. § 2-715 only addresses the buyer's right to incidental and consequential damages.

259. 632 F. Supp. 1494, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1512 (C.D. Cal. 1986).

less, only the latter was denied, not because of its basic nature, but because damages of this sort were unforeseeable and too uncertain for computation.

STATUTES OF LIMITATIONS

Past years provided no shortage of cases dealing with the time of accrual of a cause of action for breach of warranty, and this year proved to be no exception. The basic rule of U.C.C. section 2-725 is that the cause of action accrues and the limitations period begins to run "when tender of delivery is made."²⁶⁰ What of the buyer who is unlucky enough to discover the defect after suit is time-barred under this basic rule? The answer in most cases is that he is without a remedy, that is, unless the buyer can show that the warranty "explicitly extends to future performance of the goods and discovery of the breach must await the time of such performance."²⁶¹ If it does, then the statute of limitations begins to run "when the breach is or should have been discovered."²⁶² Unfortunately, the difference between ordinary warranties and "future performance" warranties is frequently difficult to discern.

In *Safeway Stores v. Certainteed Corp.*,²⁶³ a roof, which the seller advertised as "bondable up to 20 years," first began to leak seven years after it was completed. Two years later, suit was filed. Both the trial court and the court of appeals ruled that the buyer's action was barred by the four-year limitations period as suit was brought nine years after the roof was delivered.

The Texas Supreme Court reversed. The court concluded that although an *implied* warranty cannot *explicitly* extend to future performance,²⁶⁴ an express warranty, quite clearly, can. It remanded the case for a determination of whether the ambiguous warranty, "bondable up to 20 years," is an explicit reference to future performance.²⁶⁵ Similarly, representations made in connection with a twenty-year bond required rejection of a motion for summary judgment and raised a question of fact as to whether there was a "prospective

260. U.C.C. § 2-725(2).

261. *Id.*

262. *Id.*

263. 710 S.W.2d 544, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1237 (Tex. 1986).

264. The bulk of case law is in accord on this point. Courts reaching a similar conclusion during this survey period include: *Britt v. Schindler Elevator Corp.*, 637 F. Supp. 734, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1554 (D.D.C. 1986); *City of Carlisle v. Fetzer*, 381 N.W.2d 627, 42 U.C.C. Rep. Serv. (Callaghan) 1676 (Iowa 1986); *Allan v. Massey-Ferguson, Inc.*, 221 Neb. 528, 378 N.W.2d 664, 42 U.C.C. Rep. Serv. (Callaghan) 873 (1985).

In a concurring opinion, Justice Robertson took exception to this commonly held view because "[u]nder § 2-725 the extension to future performance, not the warranty, must be explicit, whether the warranty arises expressly or by implication." 710 S.W.2d at 549, 1 U.C.C. Rep. Serv. 2d at 1244.

265. In a dissenting opinion, Justice Wallace asserted that this phrase does not create a future performance warranty but is an unambiguous statement that the roof is "*capable* of being bonded for a period of up to 20 years." *Id.* at 551, 1 U.C.C. Rep. Serv. at 1246 (Wallace, J., dissenting).

warranty," i.e., a type that need not necessarily be all that explicit about future performance.²⁶⁶

As an alternative to a future performance warranty, buyers often seek to extend the limitations period by arguing that the seller is for some reason estopped to raise the statute as a defense. As was pointed out in last year's survey, these arguments are rarely successful.²⁶⁷ In *Roy Stone Transfer Corp. v. Budd Co.*,²⁶⁸ the buyer of trailers asserted that the seller was equitably estopped from pleading the statute because of (i) its attempted repairs and (ii) its delivery of a letter two years after the trailers were delivered, in which the seller gave assurance that it would stand behind its product. The trial court rejected buyer's argument. On appeal, the Fourth Circuit affirmed. First, it held that the district court's finding that the letter was not an unconditional promise to repair was not clearly erroneous. Next, it emphasized the complete absence of evidence that the buyer was lulled into inaction by either the letter or the attempted repairs.

*Ogle v. Caterpillar Tractor Co.*²⁶⁹ joins with the cases holding U.C.C. section 2-725 applicable to warranty claims involving personal injury. Recognizing the possibility that the statute could bar a suit even before the injury occurs, the Wyoming Supreme Court nevertheless thought that the plain language of U.C.C. section 2-725 and the discernable legislative intent²⁷⁰ command the conclusion that the type of damages claimed has no operative effect on the statute's scope. A reading of the opinion gives the impression that the court might have ruled the way it did because it believed its decision to be of little practical importance. As the court observed, an injured party "can still bring an action in either negligence or strict liability within four years after the injury."²⁷¹ Unfortunately, this sort of reasoning only continues to foster the often artificial distinction between tort and contract.

The division of authority on whether U.C.C. section 2-725 is controlling when the action is for indemnity is further reinforced as more courts are called upon to decide the issue.²⁷²

266. *Pack & Process, Inc. v. Celotex Corp.*, 503 A.2d 646, 42 U.C.C. Rep. Serv. (Callaghan) 462 (Del. Super. 1985).

267. 1986 Annual Survey, *supra* note 1, at 1392-93.

268. 796 F.2d 720, 1 U.C.C. Rep. Serv. 2d (Callaghan) 1234 (4th Cir. 1986).

269. 716 P.2d 334, 42 U.C.C. Rep. Serv. (Callaghan) 1668 (Wyo. 1986).

270. According to the court, "If the Wyoming legislature did not intend the UCC's explicit statute of limitations to apply to . . . actions involving tortious injury or damage, then it could have said so in the same manner as have many other state legislatures." *Id.* at 339, 42 U.C.C. Rep. Serv. at 1673-74. For a discussion of the statutory diversity and a listing of precedent, see *id.* at 338 n.4, 42 U.C.C. Rep. Serv. at 1672 n.4.

271. *Id.* at 339-40, 42 U.C.C. Rep. Serv. at 1674-75. Wyoming's basic tort statute is four years. Wyo. Stat. § 1-3-105(a)(iv)(C) (1977).

272. *Compare* *Richardson v. Clayton & Lambert Mfg. Co.*, 634 F. Supp. 1480, 1 U.C.C. Rep. Serv. 2d (Callaghan) 775 (N.D. Miss. 1986) (a claim for indemnity based on breach of warranty is governed by U.C.C. § 2-725) *with* *Wingo v. Norfolk & W. Ry. Co.*, 638 F. Supp. 107, 1 U.C.C. Rep. Serv. 2d (Callaghan) 389 (W.D. Va. 1986) (implied contract of indemnity is outside the U.C.C. and not governed by U.C.C. § 2-725). It is interesting to note that, in *Richardson*, the court found a "future performance warranty" even though the basis of the indemnity claim was breach of

BULK TRANSFERS

The revision of article 6 is still under active consideration as Professor Steven Harris details in his discussion of the "new approach" immediately following this portion of the 1987 Annual Survey.²⁷³

*Sbar's, Inc. v. New Jersey Art & Craft Distributors*²⁷⁴ again indicates the need for a new approach for the buyer at a bulk sale who has not sent the necessary notices. The case was complicated by the bankruptcy of the debtor and the fact that the bulk sale buyer had paid the consideration into the bankruptcy court pursuant to an order of that court. The bankruptcy court paid the moneys out in satisfaction of an IRS lien and administrative expenses, but the state court noted that there were insufficient moneys left to answer the claims of unsecured creditors.

Plaintiff sued the bulk sales purchaser in the state court and was awarded the full amount of its claim. On appeal, the New Jersey Superior Court reversed²⁷⁵ but required the trial court to determine the fair value of the property transferred. The court reasoned that the "defendant may be ordered to satisfy the debt . . . only to the extent of the fair value of the goods transferred,"²⁷⁶ with credit for all payments made by the trustee in bankruptcy to creditors through the bankruptcy court and pursuant to its order. Presumably this would include the administrative expenses.

On one score, the buyer who fails to give notice is subject to liability if the resulting appraisals show he made a good bargain even though it was not good enough to result in a fraudulent conveyance.²⁷⁷ But at least one other creditor is suing the buyer, and in a footnote the court carefully expressed no opinion as to how the proceeds should be divided. But should the matter be left to state law when a bankruptcy has intervened? Should not recovery, if any, go to the trustee in bankruptcy for the benefit of all creditors?²⁷⁸

There were no other cases of sufficient interest under article 6.

an implied warranty. The reason was the presence of an express statement in the contract making the term of implied warranties coextensive with that of the 10-year express warranty.

273. Harris, *The Article 6 Drafting Committee's New Approach to Asset Acquisitions*, *infra*. There appears to be considerable opposition to the proposed approach.

274. 205 N.J. Super. 516, 501 A.2d 560, 42 U.C.C. Rep. Serv. (Callaghan) 535 (App. Div. 1985).

275. The court stated that the bulk purchaser was not discharged by payment into the bankruptcy court. The discharge under N.J. Stat. Ann. § 12A:6-106(4) (West Supp. 1986) operates "only where the consideration is paid into the County Court and written notice thereof by certified or registered mail is given to the creditors. Defendant has not satisfied either of these conditions." 205 N.J. Super. at 518, 501 A.2d at 561, 42 U.C.C. Rep. Serv. at 536.

276. 205 N.J. Super. at 518, 501 A.2d at 561, 42 U.C.C. Rep. Serv. at 536.

277. Indeed, if not sold for a "reasonably equivalent value," would not the proper claimant be the bankruptcy trustee under 11 U.S.C.A. § 548 (West 1979 & Supp. 1987) as the debtor was insolvent on the date of the transfer and filed one month thereafter? Would not a payment to a successful plaintiff in a state court also be a preference? *Id.* § 547. The transfer is "on account of an antecedent debt," it would seem. *Id.* § 547(b)(2) (1982).

278. While the cause of action is vested in the creditor, not the debtor, the payments are clearly for debts of the bankrupt.

DOCUMENTS OF TITLE

Two cases under article 7 discussed the effect in bankruptcy of a warehouseman's lien under U.C.C. section 7-209 where a warehouseman fails to issue a warehouse receipt covering the stored property.

In *Cataldo v. Casey & Hayes, Inc. (In re Knoware, Inc.)*,²⁷⁹ one week before it filed for bankruptcy, the debtor had the warehouseman move and store a portion of its personal property. A warehouse receipt covering the goods was not mailed to the debtor until after the debtor had filed for bankruptcy. The warehouseman asserted a lien on the stored goods for moving and storage charges, and the bankruptcy trustee challenged the validity of the lien on the ground that no warehouse receipt had been issued before bankruptcy. The bankruptcy court ruled for the trustee under subsection 545(2) of the Bankruptcy Code.²⁸⁰ The court reasoned that since U.C.C. section 7-209 creates a lien on "goods covered by a warehouse receipt" and since U.C.C. section 1-201(45) defines a warehouse receipt as an "issued" receipt, the lien under section 7-209 is dependent upon the issuance of a warehouse receipt. The court further held that "issuance" required mailing of the receipt. Since the warehouseman proved only that an envelope containing the receipt had been placed in the warehouseman's outgoing mail bin and not that the envelope had been deposited in the U.S. mails, the court held that there was no evidence that the warehouse receipt had been mailed before bankruptcy.²⁸¹ Therefore, the warehouseman had no lien under U.C.C. section 7-209 valid against the trustee in bankruptcy.

*In re Charter Co.*²⁸² concerned a similar dispute in bankruptcy. In that case, the debtor oil company made contractual arrangements with the warehouseman for storage of its petroleum products inventory. Inventory was being constantly added to and sold from the inventory stored with the warehouseman, who kept records of inventory receipts and disbursements and rendered monthly inventory statements. When the debtor filed for bankruptcy, the warehouseman claimed a lien for various charges under U.C.C. section 7-209. The debtor challenged the validity of the lien, and the court ruled for the debtor. It found that the lien was

279. 57 Bankr. 163, 42 U.C.C. Rep. Serv. (Callaghan) 998 (Bankr. D. Mass. 1986).

280. Section 545 of the Bankruptcy Code provides, in pertinent part:

The trustee may avoid the fixing of a statutory lien on property of the debtor to the extent that such lien—

....

(2) is not perfected or enforceable at the time of the commencement of the case against a bona fide purchaser that purchases such property at the time of the commencement of the case, whether or not such a purchaser exists

11 U.S.C. § 545(2) (Supp. III 1985).

281. Testimony by a competent witness that it was office custom for an employee to retrieve envelopes from the outgoing mail bin and deposit them in the U.S. mails might have sufficed to prove that the receipt had been mailed. See *Leasing Assocs. v. Slaughter & Son, Inc.*, 450 F.2d 174 (8th Cir. 1971) and authorities cited therein.

282. 56 Bankr. 91, 42 U.C.C. Rep. Serv. (Callaghan) 280 (Bankr. M.D. Fla. 1985).

not perfected and, thus, voidable under section 545(2) of the Bankruptcy Code. The court held the issuance of a warehouse receipt by a warehouseman to be a condition to the existence of a lien under U.C.C. section 7-209. It then concluded that the various inventory records were not warehouse receipts for two reasons: (i) They did not contain certain terms required by U.C.C. section 7-202(2); and (ii) some of the documents had not been issued as required by U.C.C. section 1-201(45).

Both of these cases hold that a warehouseman does not have a lien on stored goods under U.C.C. section 7-209 that is valid in bankruptcy if the warehouseman does not issue a warehouse receipt covering the goods.²⁸³

These cases are correct as far as they go. They do not preclude the warehouseman from prevailing in bankruptcy on a theory of common law warehouseman's lien. At common law, the warehouseman had a possessory lien on stored goods. The lien was specific, that is, it was only for charges on the stored goods and not for charges on other transactions with the bailor.²⁸⁴ Yet, the lien conferred no right to sell the stored goods to satisfy the lien; the warehouseman merely had the right to keep the goods until he was paid.²⁸⁵

The sections in the Uniform Warehouse Receipts Act ("U.W.R.A.") governing the warehouseman's lien (upon which U.C.C. section 7-209 is based) were not expressly premised upon the issuance of a warehouse receipt. These sections made the common law lien general²⁸⁶ and added a right of sale²⁸⁷ but did not otherwise displace the common law lien.²⁸⁸ In the same fashion, U.C.C. section 7-209 does not expressly displace the common law lien. Nor does the drafting history of that section indicate such an intention; rather, the intention was to expand the coverage of the common law lien.²⁸⁹ Although even the earliest draft of this section expressly presumed the issuance of a warehouse receipt,²⁹⁰ there is no mention of the reason for this change from the U.W.R.A. in any of the notes or comments to the section. Probably the reason is that the drafters intended the article 7 refinements of the common law warehouseman's lien to apply only if a warehouse receipt were issued. Absent such a receipt, the drafters probably would have agreed that the common law lien survived.²⁹¹

283. See also *Richwagen v. Lilienthal*, 386 So. 2d 247 (Fla. Dist. Ct. App. 1980); *Dathar Corp. v. Lemkin*, 14 U.C.C. Rep. Serv. (Callaghan) 1207 (N.Y. Sup. Ct. 1974).

284. 1 L. Jones, *A Treatise on the Law of Liens* 981-1002 (3d ed. 1914).

285. *Id.* at 990-91.

286. *Unif. Warehouse Receipts Act* § 27, 3 U.L.A. 139 (1959).

287. *Id.* § 33, 3 U.L.A. 152.

288. *State v. Amarillo Transfer & Storage Co.*, 94 S.W.2d 590 (Tex. Civ. App. 1936); *cf. Jewett v. City Transfer & Storage Co.*, 128 Cal. App. 556, 18 P.2d 351 (1933).

289. A.L.I. & N.C.C.U.S.L., *Commercial Code, Tentative Draft No. 1—Article VI, § 13* (Apr. 19, 1948), *reprinted in* 4 A.L.I. & N.C.C.U.S.L., *Uniform Commercial Code—Drafts* § 13, at 239, & note, at 262-63 (Kelly ed. 1984).

290. *Id.*

291. *Cf.* 1 A.L.I. *Proceedings, 26th Annual Meeting* 81 (1949) (colloquy between Messrs. Flory, Schnader, and Pepper).

This result accords with reason. Certainly a creditor cannot claim that the lien is secret. The warehouseman's possession of the stored goods is sufficient to put creditors of the bailor on notice.²⁹² The issuance of a warehouse receipt to the bailor does not further the policy of notice to creditors. Thus, the failure to issue a warehouse receipt should not invalidate an otherwise valid common law warehouseman's lien.

The assertion of a common law lien would probably allow the warehouseman to prevail against the trustee in bankruptcy. Generally, common law possessory liens are respected in bankruptcy.²⁹³ Thus, had the warehousemen in *Cataldo* and *In re Charter Co.* asserted common law lien rights, they might well have prevailed.

This is not to say that there is no reason to issue a warehouse receipt. Good business practice would dictate that. Further, if no receipt is issued, U.C.C. section 7-210, which permits the warehouseman to sell the goods, is inapplicable. This remits the warehouseman to his limited common law rights as they may have been supplemented by non-Code statutes.

292. Cf. U.C.C. § 9-305 (possession of goods perfects security interest).

293. 4B W. Collier, *Collier on Bankruptcy* 1007, n.19c (14th ed. 1978).