

CONTRACTS: NOTES ON THE EXAM

SECTION A (60% of the exam grade) Each question counts for 12 points.

1. Roby Heath wants to claim \$20,000 from Anna. Do you think he will succeed in this claim? What arguments can Anna make to counter his claim?

The question says it is a binding contract. Therefore I do not think this question requires a discussion of whether or not there is a contract. [There could be an issue as to whether the contract is between Emily and Heath or whether Anna was a party to the contract - this is the sort of agency issue we discussed in the context of Hoffman v Red Owl.] This contract is not governed by the UCC. It is a contract whereby a singer agrees to give a performance for a fee. He agrees to be available to give the performance (similar to Shirley Maclaine's agreement in the Parker case). I don't think it makes sense to discuss unilateral contracts in this situation. Making the discussion of possible legal issues more complex than is justified by the facts you are given suggests you have less, rather than more, relevant knowledge. Writing about what is relevant is critical in answering a hypothetical.

Anna's decision not to have Roby Heath sing is a breach of contract. Anna can argue Heath has a duty to mitigate. She does not seem to be offering any substitute employment, but Roby Heath does have a duty to mitigate his loss. Cases: Parker v Twentieth Century Fox (CB p 51) , In Re Worldcom (CB p 77). What does he need to do ? Some discussion of the similarities and differences between the cases and these facts could be appropriate. The question does not say whether Heath made any effort at all to mitigate.

Many answers analyzed whether Heath could be considered to be a lost volume seller (cf. Michael Jordan in the Worldcom case). But Heath is in a different situation from Jordan's: a person can have multiple endorsement contracts in effect at any one time, but it is not possible for a singer to sing at two different events at the same time.

2. What issues of contract law does Anna's firing of Emily raise?

Terms of Emily's employment: the question states "Anna reminded Emily that when she was hired Emily agreed that for a period of five years after termination of her employment with Tropical Barbecue she would not work for any restaurant in the capital city of Arcadia or in any barbecue restaurant in the state." and "Tropical Barbecue has a reputation as an excellent place to work, and Anna has arranged for employment experts to write the restaurant's staff manual, which specifies detailed disciplinary procedures for staff."

Was the firing valid? Is there any argument she was not properly fired? Not told of any relevant contract terms, although the non-compete discussion suggests there is some sort of a contract. Contract - e.g. McIntosh v Murphy (CB p. 430). If this is employment at will - Wagenseller (CB p 447) - implied terms from personnel policies etc. [public policy, duty of good faith]

Non-compete- 5 years, no restaurant in capital, no barbecue restaurant in the state. Case: Fullerton Lumber (CB p 511). The facts of the hypothetical contrast with the facts of Fullerton Lumber. Emily does not appear to be nearly such an important

employee for the business: she is relatively recently employed, does not seem to have special knowledge about the business/the locality or the customers. We are not told she is privy to any trade secrets or anything which would mean that her working for a competitor would be problematic. There's a real question as to whether there is any need for such a restriction, let alone the issues of whether the restrictions are excessive with respect to time or geography.

3. What claims can Anna bring against Carl for his failure to deliver the fruits?

Her losses: "Carl fails to deliver the fruits, including the tamarinds and rare mangoes that are crucial ingredients in Anna's recipes. Anna frantically contacts other suppliers she knows to see if she can obtain the fruits she needs. Eventually, after a lot of stress, she does manage to find substitute fruits from a number of different suppliers. Because she is ordering the fruits at the last minute she has to pay much higher prices than she originally expected to pay. She has to hire extra drivers to go to collect the fruits. When the mangoes arrive they are clearly not of the high quality Anna requires. She worries that the recipes using the inferior mangoes will not impress the guests at the gala and that she will lose a number of potential franchisees as a result."

The question suggests a number of different types of damage Anna has suffered as a result of Carl's non-delivery (nb. some answers discussed whether there was a contract in place here): costs involved in contacting other suppliers, stress, the difference between the contract price and the price she pays to cover, hiring extra drivers (incidental damages) and damages associated with the inferior quality of the substitute fruits (if the event were less successful as a result and she loses potential franchisees this raises an issue with respect to consequential damages).

Fruits are goods covered by the UCC (though they are perishable which sometimes has implications for how a party should act this really relates to the disappointed seller rather than to the disappointed buyer). Anna's purchase of substitute fruits constitutes cover under UCC § 2-712. Under the statute she can claim damages for "the difference between the cost of cover and the contract price together with any incidental or consequential damages ... but less expenses saved in consequence of the seller's breach" provided that the cover consisted of "making in good faith and without unreasonable delay any reasonable purchase" of substitute goods. Nothing in the facts suggests she acted unreasonably or with unreasonable delay or otherwise than in good faith. The extra costs associated with hiring drivers are incidental damages which she may claim (UCC § 2-715 states that "Incidental damages resulting from the seller's breach include expenses reasonably incurred in inspection, receipt, transportation and care and custody of goods rightfully rejected, any commercially reasonable charges, expenses or commissions in connection with effecting cover and any other reasonable expense incident to the delay or other breach.") The question does not suggest any expenses saved due to Carl's breach.

As to consequential damages, there are a number of issues. UCC § 2-715(2) states: "Consequential damages resulting from the seller's breach include (a) any loss resulting from general or particular requirements and needs of which the seller at the time of contracting had reason to know and which could not reasonably be prevented by cover or otherwise; and (b) injury to person or property proximately

resulting from any breach of warranty.” The question states that Anna told Carl how important the gala was for her, that she would be using it as a showcase for the franchise and that everything must be perfect. Thus it seems that Carl is aware of Anna’s “particular requirements and needs” However there are two other issues that seem less clear. One relates to the question whether any lack of interest in the franchises “result.. from the seller’s breach” (how can we tell whether Anna would have generated more interest in franchises than she did if everything had been perfect?). The other relates to the issue of quantification of damages (how much did she lose, and can she establish the amount with reasonable certainty). We saw this second issue in the context of new business cases (Evergreen, Chung). Here, it may be possible to establish how much she might have lost from each lost franchise (even though the franchise business is a new business for Anna), but it is likely harder to establish how many more franchise applications she would have generated had everything been perfect.

4. Will Anna be able to return the brochures to the printer and obtain a refund of the price?

Question states: “The brochures, which arrive on the day of the gala, contain a number of typographical errors. Because she needs to be able to distribute information at the gala Anna accepts the brochures, but she decides that she will return those she does not use to the printer after the gala and demand a refund of the price she paid for the brochures.” Cases: Colonial Dodge v Miller (CB p 162), Armstrong Rubber (CB p 148) (cf. Class struggle game example CB p 157).

The brochures are goods covered by the UCC. The question is whether Anna accepted the goods under UCC § 2-606 and, if so, did she effectively revoke her acceptance of the brochures.

UCC § 2-606. What Constitutes Acceptance of Goods.

- (1) Acceptance of goods occurs when the buyer
 - (a) after a reasonable opportunity to inspect the goods signifies to the seller that the goods are conforming or that he will take or retain them in spite of their non-conformity; or
 - (b) fails to make an effective rejection (subsection (1) of Section 2-602), but such acceptance does not occur until the buyer has had a reasonable opportunity to inspect them; or
 - (c) does any act inconsistent with the seller's ownership; but if such act is wrongful as against the seller it is an acceptance only if ratified by him.
- (2) Acceptance of a part of any commercial unit is acceptance of that entire unit.

UCC § 2-608. Revocation of Acceptance in Whole or in Part.

- (1) The buyer may revoke his acceptance of a lot or commercial unit whose non-conformity substantially impairs its value to him if he has accepted it
 - (a) on the reasonable assumption that its non-conformity would be cured and it has not been seasonably cured; or
 - (b) without discovery of such non-conformity if his acceptance was reasonably induced either by the difficulty of discovery before acceptance or by the seller's assurances.
- (2) Revocation of acceptance must occur within a reasonable time after the buyer discovers or should have discovered the ground for it and before any substantial change in condition of the goods which is not caused by their own defects. It is not effective until the buyer notifies the seller of it.
- (3) A buyer who so revokes has the same rights and duties with regard to the goods involved as if he had

rejected them.

UCC § 2-708. Seller's Damages for Non-acceptance or Repudiation.

(1) Subject to subsection (2) and to the provisions of this Article with respect to proof of market price (Section 2-723), the measure of damages for nonacceptance or repudiation by the buyer is the difference between the market price at the time and place for tender and the unpaid contract price together with any incidental damages provided in this Article (Section 2-710), but less expenses saved in consequence of the buyer's breach.

(2) If the measure of damages provided in subsection (1) is inadequate to put the seller in as good a position as performance would have done then the measure of damages is the profit (including reasonable overhead) which the seller would have made from full performance by the buyer, together with any incidental damages provided in this Article (Section 2-710), due allowance for costs reasonably incurred and due credit for payments or proceeds of resale.

UCC § 2-714. Buyer's Damages for Breach in Regard to Accepted Goods.

(1) Where the buyer has accepted goods and given notification (subsection (3) of Section 2-607) he may recover as damages for any non-conformity of tender the loss resulting in the ordinary course of events from the seller's breach as determined in any manner which is reasonable.

(2) The measure of damages for breach of warranty is the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted, unless special circumstances show proximate damages of a different amount.

(3) In a proper case any incidental and consequential damages under the next section may also be recovered.

5. Would the answers to any of these questions be different if an Arcadian statute makes it a criminal offense to sell franchises if the franchise documentation has not been filed with the Secretary of State (and Anna has not filed any documentation)?

To which claims is this illegality relevant? If Anna sold franchises to any applicants in circumstances where the sale violated a criminal statute, then the franchisees would be entitled to invoke the illegality to avoid paying the franchise fees. The circumstances in the hypothetical are not so closely connected to the illegality. Does the illegality with respect to sales of franchises mean that Anna can avoid paying Roby Heath? Does the illegality help Emily (cf. the Wagenseller case)? Is the provision of fruits or brochures connected to an illegal activity problematic? Cases: Carroll v Beardon (CB p 494), Coma Corp v Kansas Department of Labor (CB p 499), Karpinski v Collins (CB p 508).

SECTION B (40% of the exam grade)

ONE QUESTION

Some answers to the part B question were relatively short as a component of the exam answers as a whole (or extremely short). But this question carries 40% of the total marks available for the exam. If an exam shows how marks are to be allocated you should use this as a guide to how you allocate your time in the exam.

There were some different types of answer to these questions which could be described as follows:

- i. Description of the question and of arguments about the issues raised by the question with no real substantial examples.

- ii. Description of the question using examples of cases to illustrate the issues raised by the question.
- iii. Critical evaluation of the question with an argument about how one should think about the issues, and with a number of examples to illustrate the argument.

These three examples illustrate different levels of complexity in the response to the question. More complex answers are better (provided they are comprehensible).

1. The materials we have studied this semester suggest that in contract law there is often a tension between efficiency and fairness. Do you agree?

(3/5 of total answers)

Answers to this question often did not examine what was meant by the words “efficiency” and “fairness”. At least two different ideas of efficiency were considered in the answers. One was the idea of economic efficiency: that contract law should promote the efficient allocation of resources (as exemplified in a number of decisions we read by Judges Posner and Easterbrook). Another idea of efficiency related to the allocation of the resources of the court system, and to efficiency of dispute settlement. This second idea was not what I intended to ask about in drafting the question, and was not really the focus of the course materials, but some answers used this concept of efficiency effectively. The materials in the case book sometimes reflected courts’ unwillingness to intervene in resolving disputes, this did not seem to me to be based on conserving the resources of the justice system, although that is clearly an issue one can raise in this context. Some answers used the materials on arbitration to illustrate businesses interests in managing disputes, which is clearly related to the idea of economic efficiency.

Answers which explained how they were defining efficiency received better grades than answers which did not. So, answers which used both concepts of efficiency noted above and distinguished between the different types in discussing cases received better grades than answers which bundled everything together. Answers which used more examples from the course materials - especially where the examples were explained to show how they illustrated the argument in the answer - received better grades than those which used fewer, less well explained examples.

Answers tended to assume (perhaps with the question) that efficiency and fairness would tend to pull in different directions. It would be possible to argue that this is not the case. So, those who argue that the law should promote economic efficiency would often say that it makes sense to enforce the contracts people make (particularly when they negotiate at arm’s length) because the contracting parties’ assessment of their own interests is likely to be more reliable than a court’s.

There are many different examples that could be used to illustrate this seeming tension. One example in our casebook was Judge Posner’s decision in *Lake River Corporation v Carborundum* (CB p 100). Judge Posner argues that even imposing penalties might be “essential to inducing some value-maximizing contracts to be made”. Posner suggests that the refusal to enforce penal clauses may be “paternalistic” but he applies Illinois law because the courts in Illinois are not troubled by his own “academic skepticism”. The case seems to suggest an opposition between efficiency (Posner) and fairness (the Illinois rule). But is the Illinois rule really fairer? After all it allows one

contracting party to get out of the deal it agreed to. The other party might not have agreed to the deal at the outset without the term later treated as invalid.

2. The materials we studied suggest that courts sometimes decline to give effect to contracts in the family setting by refusing to treat such contracts as enforceable, or by deferring to the legislature to make or change the law. One way of characterizing such approaches would be to say that the courts are being neutral. Do you agree that this is an appropriate characterization?

(2/5 of total answers).

The question invited discussion of the cases we read during the semester which relate to family rather than commercial matters. The question therefore asks about how contracts fit within the domestic setting (the enforceability issue) and what the respective roles of courts and legislatures are with respect to family matters (the deference question). Many answers to the question described a number of the cases we read during the semester. But as with the other essay question, I was really looking for more than descriptions of relevant cases. I wanted to see evidence of thought about the materials and analysis of the question.

The two approaches identified are different: in one set of cases the courts see the formal legal process as inappropriate to resolve certain sorts of disputes between family members (a distinction between private matters which don't belong in the courts, and more public matters which do - one might contrast these domestic cases with cases involving commercial contracts which are treated as being within the public or legal sphere) and in the other set of cases courts are suggesting that the issues involved are general issues of policy which should be resolved by legislatures rather than by courts. Ideally an answer to this question would take on both sets of idea.

The question ends by asking whether it is appropriate to characterize what the courts have done in these family cases as being neutral - this is the core of the question. It does not ask for a description of the various domestic contracts cases we read but an assessment of whether when courts choose not to enforce contracts in the domestic context or to leave complex issues to the legislature it is appropriate to characterize what they are doing as being neutral. But many answers to this question did not address what the concept of neutrality might mean. This is a very difficult question: as a lawsuit is an adversarial proceeding anything the court does tends to favor one side or another. So the question really invites you to think about the role of the court in a broader sense and consider the relationship between courts and legislatures.