Expectancy – I
Restitution – II

Reliance – III, intermediate recovery theory

generally more lenient measure of damages is to be applied in patient-physician actions based on breach of alleged special agreements to effect a cure, attain a stated result, or employ a given medical method. This measure is expressed in somewhat variant ways, but the substance is that the plaintiff is to recover any expenditures made by him and for other detriment (usually not specifically described in the opinions) following proximately and foreseeably upon the defendant's failure to carry out his promise. Robins v. Finestone, 308 N.Y. 543, 546, 127 N.E.2d 330; Frankel v. Wolper, 181 App. Div. 485, 488, 169 N.Y.S. 15, affd., 228 N.Y. 582, 127 N.E. 913; Frank v. Maliniak, 232 App. Div. 278, 280, 249 N.Y.S. 514; Colvin v. Smith, 276 App. Div. 9, 10, 92 N.Y.S.2d 794; Stewart v. Rudner, 349 Mich. 459, 465-473, 84 N.W.2d 816. Cf. Carpenter v. Moore, 51 Wash. 2d 795, 322 P.2d 125. This, be it noted, is not a "restitution" measure, for it is not limited to restoration of the benefit conferred on the defendant (the fee paid) but includes other expenditures, for example, amounts paid for medicine and nurses; so also it would seem according to its logic to take in damages for any worsening of the plaintiff's condition due to the breach. Nor is it an "expectancy" measure, for it does not appear to contemplate recovery of the whole difference in value between the condition as promised and the condition actually resulting from the treatment. Rather the tendency of the formulation is to put the plaintiff back in the position he occupied just before the parties entered upon the agreement, to compensate him for the detriments he suffered in reliance upon the agreement. This kind of intermediate pattern of recovery for breach of contract is discussed in the suggestive article by Fuller and Perdue, The Reliance Interest in Contract Damages, 46 Yale L.J. 52, 373, where the authors show that, although not attaining the currency of the standard measures, a "reliance" measure has for special reasons been applied by the courts in a variety of settings, including noncommercial settings. See 46 Yale L.J. at 396-401.[4]

Reliance

III

For breach of the patient-physician agreements under consideration, a recovery limited to restitution seems plainly too meager, if the agreements are to be enforced at all. On the other hand, an expectancy recovery may well be excessive. The factors, already mentioned, which have made the cause of action somewhat suspect, also suggest moderation as to the breadth of the recovery that should be permitted. Where, as in the case at bar and in a number of the reported cases, the doctor has been absolved of negligence by the trier, an expectancy measure may be thought harsh. We should recall here that the fee paid by the patient to the doctor for the alleged promise would usually be quite disproportionate to the putative expectancy recovery. To attempt, moreover, to put a value on the condition that would or might have resulted, had the treatment succeeded as promised, may sometimes put an exceptional strain on the imagination of the fact finder. As a general consideration, Fuller and Perdue argue that

4. Some of the exceptional situations mentioned where reliance may be preferred to expectancy are those in which the latter measure would be hard to apply or would impose too great a burden; performance was interfered with by external circumstances; the contract was indefinite. See 46 Yale L.J. at 373-386; 394-396.

expectancy best use for business & goods — not for medical cases

best reliance interest for med.

nothing barring mental distress — not compensable generally but no rule saying it depends on the facts

restitution

the reasons for granting damages for broken promises to the extent of the expectancy are at their strongest when the promises are made in a business context, when they have to do with the production or distribution of goods or the allocation of functions in the market place; they become weaker as the context shifts from a commercial to a noncommercial field. 46 Yale L.J. at 60-63.

There is much to be said, then, for applying a reliance measure to the present facts, and we have only to add that our cases are not unreceptive to the use of that formula in special situations. We have, however, had no previous occasion to apply it to patient-physician cases.

The question of recovery on a reliance basis for pain and suffering or mental distress requires further attention. We find expressions in the decisions that pain and suffering (or the like) are simply not compensable in actions for breach of contract. The defendant seemingly espouses this proposition in the present case. True, if the buyer under a contract for the purchase of a lot of merchandise, in suing for the seller's breach, should claim damages for mental anguish caused by his disappointment in the transaction, he would not succeed; he would be told, perhaps, that the asserted psychological injury was not fairly foreseeable by the defendant as a probable consequence of the breach of such a business contract. See Restatement: Contracts, §341, and comment a. But there is no general rule barring such items of damage in actions for breach of contract. It is all a question of the subject matter and background of the contract, and when the contract calls for an operation on the person of the plaintiff, psychological as well as physical injury may be expected to figure somewhere in the recovery, depending on the particular circumstances. The point is explained in Stewart v. Rudner, 349 Mich. 459, 469, 84 N.W.2d 816. Cf. Frewen v. Page, 238 Mass. 499, 131 N.E. 475; McClean v. University Club, 327 Mass. 68, 97 N.E.2d 174. Again, it is said in a few of the New York cases, concerned with the classification of actions for statute of limitations purposes, that the absence of allegations demanding recovery for pain and suffering is characteristic of a contract claim by a patient against a physician, that such allegations rather belong in a claim for malpractice. See Robins v. Finestone, 308 N.Y. 543, 547, 127 N.E.2d 330; Budoff v. Kessler, 2 A.D.2d 760, 153 N.Y.S.2d 654. These remarks seem unduly sweeping. Suffering or distress resulting from the breach going beyond that which was envisaged by the treatment as agreed, should be compensable on the same ground as the worsening of the patient's condition because of the breach. Indeed it can be argued that the very suffering or distress "contracted for" — that which would have been incurred if the treatment achieved the promised result — should also be compensable on the theory underlying the New York cases. For that suffering is "wasted" if the treatment fails. Otherwise stated, compensation for this waste is arguably required in order to complete the restoration of the status quo ante.

In the light of the foregoing discussion, all the defendant's exceptions fail: the plaintiff was not confined to the recovery of her out-of-pocket expenditures; she was entitled to recover also for the worsening of her condition, and for the pain and suffering and mental distress involved in the third operation. These items were compensable on either an expectancy or a reliance view. We might have been required to elect between the two views if the pain and suffering connected with the first two operations contemplated by the agreement, or the whole difference in value between the present and the promised conditions, were being claimed as elements of damage. But the plaintiff waives her possible claim to the former element, and to so much of the latter as represents the difference in value between the promised condition and the condition before the operations.

Plaintiff's exceptions waived.
Defendant's exceptions overruled.

ANGLIA TELEVISION, LTD. v. REED
Court of Appeals, Civil Division, 1971
3 All Eng. Rep. 690

Lord DENNING. Anglia Television Ltd. were minded in 1968 to make a film of a play for television entitled "The Man in the Wood." It portrayed an American married to an English woman. The American has an adventure in an English wood. The film was to last for 90 minutes. Anglia Television made many arrangements in advance. They arranged for a place where the play was to be filmed. They employed a director, a designer and a stage manager, and so forth. They involved themselves in much expense. All this was done before they got the leading man. They required a strong actor capable of holding the play together. He was to be on the scene the whole time. Anglia Television eventually found the man. He was Mr. Robert Reed, an American who has a very high reputation as an actor. He was very suitable for this part. By telephone conversation on 30th August 1968 it was agreed by Mr. Reed through his agent that he would come to England and be available between 9th September and 11th October 1968 to rehearse and play in this film. He was to get a performance fee of £1,050, living expenses of £100 a week, his first class fares to and from the United States, and so forth. It was all subject to the permit of the Ministry of Labour for him to come here. That was duly given on 2nd September 1968. So the contract was concluded. But unfortunately there was some muddle with the bookings. It appears that Mr. Reed's agent had already booked him in America for some other play. So on 3rd September 1968 the agent said that Mr. Reed would not come to England to perform in this play. He repudiated his contract. Anglia Television tried hard to find a substitute but could not do so. So on 11th September they accepted his repudiation. They abandoned the proposed film. They gave notice to the people whom they had engaged and so forth.

Anglia Television then sued Mr. Reed for damages. He did not dispute his liability, but a question arose as to the damages. Anglia Television do not claim their profit. They cannot say what their profit would have been on this contract if Mr. Reed had come here and performed it. So, instead of claim for loss or profits, they claim for the wasted expenditure. They had incurred the director's fees, the designer's fees, the stage manager's and assistant manager's fees, and so on. It comes in all to £2,750. Anglia Television say [sic] that all that money was wasted because Mr. Reed did not perform his contract.

Mr. Reed's advisers take a point of law. They submit that Anglia Television cannot recover for expenditure incurred *before* the contract was concluded with Mr. Reed. They can only recover the expenditure *after* the contract was concluded. They say that the expenditure *after* the contract was only £854.65, and that is all that Anglia Television can recover. The master rejected that contention; he held that Anglia Television could recover the whole £2,750; and now Mr. Reed appeals to this court.

Counsel for Mr. Reed has referred us to the recent unreported case of Perestrello & Compania Limitada v. United Paint Co. Ltd. (No. 2),[1] in which Thesiger J. quoted the words of Lord Tindal C.J. in 1835 in Hodges v. Earl of Litchfield:[2]

> The expenses preliminary to the contract ought not to be allowed. The party enters into them for his own benefit at a time when it is uncertain whether there will be any contract or not.

Thesiger J. applied those words, saying: "In my judgment pre-contract expenditure, though thrown away, is not recoverable. . . ."

I cannot accept the proposition as stated. It seems to me that a plaintiff in such a case as this had an election: he can either claim for his loss of profits; or for his wasted expenditure. But he must elect between them. He cannot claim both. If he has not suffered any loss of profits — or if he cannot prove what his profits would have been — he can claim in the alternative the expenditure which has been thrown away, that is, wasted, by reason of the breach. That is shown by Cullinane v. British "Rema" Manufacturing Co. Ltd.[3]

If the plaintiff claims the wasted expenditure, he is not limited to the expenditure incurred *after* the contract was concluded. He can claim also the expenditure incurred *before* the contract, provided that it was such as would reasonably be in the contemplation of the parties as likely to be wasted if the contract was broken. Applying that principle here, it is plain that, when Mr. Reed entered into this contract, he must have known perfectly well that much expenditure had already been incurred on director's fees and the like. He must have contemplated — or, at any rate, it is reasonably to be imputed to him — that if he broke his contract, all that expenditure would be wasted, whether or not it was incurred before or after the contract. He must pay damages for all the expenditure so wasted and thrown away. This view is supported by the recent decision of Brightman J. in Lloyd v. Stanbury.[4] There was a contract for the sale of land. In anticipation of the contract — and before it was concluded — the

1. (1969) 113 Sol. Jo. 324.
2. (1835) 1 Bing. N.C. 492 at 498, [1835-42] All E.R. Rep. 551 at 552, 553.
3. [1953] 2 All E.R. 1257 at 1261, 1264, 1265, [1954] 1 Q.B. 292 at 303, 308.
4. [1971] 2 All E.R. 267, [1971] 1 W.L.R. 535.

purchaser went to much expense in moving a caravan to the site and in getting his furniture there. The seller afterwards entered into a contract to sell the land to the purchaser, but afterwards broke his contract. The land had not increased in value, so the purchaser could not claim for any loss of profit. But Brightman J. held that he could recover the cost of moving the caravan and furniture, because it was[5] "within the contemplation of the parties when the contract was signed." That decision is in accord with correct principle, namely, that wasted expenditure can be recovered when it is wasted by reason of the defendant's breach of contract. It is true that, if the defendant had never entered into the contract, he would not be liable, and the expenditure would have been incurred by the plaintiff without redress; but, the defendant having made his contract and broken it, it does not lie in his mouth to say he is not liable, when it was because of his breach that the expenditure has been wasted.

I think the master was quite right and this appeal should be dismissed.

PHILLIMORE L.J. I agree.

MEGAW L.J. I also agree.

Appeal dismissed.

The Restatement (Second) of Contracts provides:

§349. Damages Based on Reliance Interest

As an alternative to the measure of damages stated in §347, the injured party has a right to damages based on reliance interest, including expenditures made in preparation for performance or in performance, less any loss that the party in breach can prove with reasonable certainty the injured party would have suffered had the contract been performed.

QUESTIONS AND NOTES

1. If the expectation measure is the "normal" remedy for the plaintiff, why did the court in *Sullivan* choose the reliance measure as the appropriate measure for the plaintiff? Why did the plaintiff opt for reliance measure over the expectancy measure in *Anglia?* bcc-they didn't know how much profit expectancy they would make

2. In *Anglia* what would be the award if it appeared that the plaintiff was going to lose money on the film? Whose obligation is it to show that a loss of profit is likely to occur?

3. Would it affect the result in *Anglia* if the amount of the reliance interest had been $22 million?

4. For more on the issue of whether preparation costs are recoverable in reliance actions, see Lucian Arye Bebchuk and Omri Ben-Shahar, Precontractual Reliance, 30 J. Legal Stud. 423 (2001); G. Crespi, Recovering Pre-Contractual Expenditures as an Element of Reliance Damages, 49 SMU L Rev. 43 (1995).

5. [1971] 2 All E.R. at 276, [1971] 1 W.L.R. at 547.

NOTE ON THE PRESUMPTION OF BREAKING EVEN

If the expectancy is too difficult to prove, the plaintiff is entitled to recover out of pocket expenses unless the defendant can prove that the contract was a losing one and that the plaintiff would not have made enough from the contract to make up these expenditures. Thus, the courts in effect are indulging in a presumption that the plaintiff will "break even"; that the expectancy would have been at least the amount of the expenditures. See J. Calamari and J. Perrillo, Contracts §14-9 (5th ed. 2003). Reasonable reliance and restitution expenses are awarded on "the assumption that the value of the contract would at least have covered the outlay," C. McCormick, Damages 586 (1935). If the defendant can carry the burden of showing that the contract was really a losing one, the court will deduct the loss from the plaintiff's outlay.

Problem 67

Rogette began drafting the fourteenth edition of her tour guide pursuant to an agreement with White Publishing. After Rogette was one-quarter done, White repudiated the agreement. Rogette sued White for the amount of money she had expended on the book to the time of the repudiation. She also sued White for the "expectancy" — that is, the total amount she expected she would have earned (royalties) on the book. White admits liability but alleges the damages should be measured either by the expectancy or the amount spent but should not include both. Rogette argues that she had suffered the loss of both elements of damages and should receive both. Who is right?

What would the plaintiff have recovered in Problem 66 if the suit there sought recovery for only the reliance interest?

D. Limitations on the Recovery

Along with the type of expectancy damages discussed above — damages representing a "loss in value" to the plaintiff because of the breach (general damages) — *incidental* and *consequential* damages (special damages) may also be included in the final award. Consequential damages are expenses or other losses beyond general damages that the plaintiff would never have incurred but for the breach. For example, if the breach involves a faulty furnace that blows up and injures a family, the consequential damages would include pain and suffering and medical expenses. In a commercial context, consequential damages frequently consist of lost profits for a nonbreaching buyer. If the builder of a motel fails to build a structure as promised, loss in value damages for the owner will consist of the cost of substitute performance or the diminution in value occasioned by the defective performance. In addition, the owner may be entitled to consequential damages such as the profit lost on another contract between the motel owner and a convention group that cancels because the motel is not ready. Incidental damages are consequential damages incurred in ascertaining and trying to prevent the breach. See UCC §2-715. An example would be storage costs incurred by a nonbreaching seller who holds goods for a buyer for a reasonable time after the buyer fails to pick up the goods as promised.

An award of damages in a contracts action, the consequential portion as well as the loss of value portion, is subject to various limitations applied by the courts. Of primary importance are the doctrines of certainty, foreseeability, and avoidability, which lead off this section on limitations. As you review the cases, read them with two purposes in mind: (1) to understand how the limitations work and (2) to get a feel for the losses that may be reimbursed as consequential damages (what types of losses fall into this category of "consequential damages?").

1. Certainty

The plaintiff is generally denied any relief that is too speculative. Requested relief can be too speculative because there is too much uncertainty as to either (1) the fact that the breach caused the type of injury that plaintiff alleges (a "causation" limitation); (2) the extent to which the plaintiff suffered from the breach (the dollar amount of the damage caused); or (3) both the causation and amount. Most cases on certainty concern requests by the plaintiff for consequential damages. Claims for general damages must also have the requisite degree of certainty, though through the years formulas have been developed for measuring general damages in such a way as to satisfy this requirement as to at least the causation issue (number 1 above) without the trouble caused by the same issue when applied to consequential losses. For example, it is generally presumed that the general damage as measured by the cost of substitute performance is caused by a breach by the contractor. The diversity of potential claims for consequential damages (for want of a horse a kingdom was lost, etc.) makes for some hard questions as to certainty as to causation as well as amount. For example, the breach by the contractor does not necessarily cause the owner who hired the contractor to suffer lost profits on third party contracts nor tort damages because the owner fell through a defective floor.

FREUND v. WASHINGTON SQUARE PRESS
Court of Appeals of New York, 1974
34 N.Y.2d 379, 357 N.Y.S.2d 857, 314 N.E.2d 419

RABIN, J. In this action for breach of a publishing contract, we must decide what damages are recoverable for defendant's failure to publish plaintiff's manuscript. In 1965, plaintiff, an author and a college teacher, and defendant, Washington Square Press, Inc., entered into a written agreement which, in relevant part, provided as follows. Plaintiff ("author") granted defendant ("publisher") exclusive rights to publish and sell in book form plaintiff's work on modern drama. Upon plaintiff's delivery of the manuscript, defendant agreed to complete payment of a nonreturnable $2,000 advance. Thereafter, if defendant deemed the manuscript not "suitable for publication," it had the right to terminate the agreement by written notice within 60 days of delivery. Unless so terminated, defendant agreed to publish the work in hard-bound edition within 18 months and afterwards in paperbound edition. The contract further provided that defendant would pay royalties to plaintiff, based upon specified percentages of sales. (For example, plaintiff was to receive 10 percent of the retail price of the first 10,000 copies sold in the continental United States.) If defendant failed to publish within 18 months, the contract provided that "this agreement shall terminate and the rights herein granted to the Publisher shall revert to the Author. In such event all payments theretofore made to the Author shall belong to the Author without prejudice to any other remedies which the Author may have." The contract also provided that controversies were to be determined pursuant to the New York simplified procedure for court determination of disputes (CPLR 3031-3037, Consol. Laws, c.8).

Plaintiff performed by delivering his manuscript to defendant and was paid his $2,000 advance. Defendant thereafter merged with another publisher and ceased publishing in hardbound. Although defendant did not exercise its 60-day right to terminate, it has refused to publish the manuscript in any form.

Plaintiff commenced the instant action pursuant to the simplified procedure practice and initially sought specific performance of the contract. The Trial Term Justice denied specific performance but, finding a valid contract and a breach by defendant, set the matter down for trial on the issue of monetary damages, if any, sustained by the plaintiff. At trial, plaintiff sought to prove: (1) delay of his academic promotion; (2) loss of royalties which would have been earned; and (3) the cost of publication if plaintiff had made his own arrangements to publish. The trial court found that plaintiff had been promoted despite defendant's failure to publish, and that there was no evidence that the breach had caused any delay. Recovery of lost royalties was denied without discussion. The court found, however, that the cost of hardcover publication to plaintiff was the natural and probable consequence of the breach and, based upon expert testimony, awarded $10,000 to cover this cost. It denied recovery of the expenses of paperbound publication on the ground that plaintiff's proof was conjectural.

The Appellate Division (3 to 2) affirmed, finding that the cost of publication was the proper measure of damages. In support of its conclusion, the majority analogized to the construction contract situation where the cost of completion may be the proper measure of damages for a builder's failure to complete a house or for use of wrong materials. The dissent concluded that the cost of publication is not an appropriate measure of damages and consequently, that plaintiff may recover nominal damages only. We agree with the dissent. In so concluding, we look to the basic purpose of damage recovery and the nature and effect of the parties' contract.

It is axiomatic that, except where punitive damages are allowable, the law awards damages for breach of contract to compensate for injury caused by the breach — injury which was foreseeable, i.e., reasonably within the contemplation of the parties, at the time the contract was entered into. (Swain v. Schieffelin, 134 N.Y. 471, 473, 31 N.E. 1025, 1026.) Money damages are substitutional relief designed in theory "to put the injured party in as good a position as he would have been put by full performance of the contract, at the least cost to the defendant and without charging him with harms that he had no sufficient reason to foresee when he made the contract." (5 Corbin, Contracts, §1002, pp. 31-32; 11 Williston, Contracts [3d ed.], §1338, p. 198.) In other words, so far as possible, the law attempts to secure to the injured party the benefit of his bargain, subject to the limitations that the injury — whether it be losses suffered or gains prevented — was foreseeable, and that the amount of damages claimed be measurable with a reasonable degree of certainty and, of course, adequately proven. (See, generally, Dobbs, Law of Remedies, p. 148; see, also, Farnsworth, Legal Remedies for Breach of Contract, 70 Col. L. Rev. 1145, 1159.) But it is equally fundamental that the injured party should not recover more from the breach than he would have gained had the contract been fully performed. . . .

Measurement of damages in this case according to the cost of publication to the plaintiff would confer greater advantage than performance of the contract would have entailed to plaintiff and would place him in a far better position than he would have occupied had the defendant fully performed. Such measurement bears no relation to compensation for plaintiff's actual loss or anticipated profit. Far beyond compensating plaintiff for the interests he had in the defendant's performance of the contract — whether restitution, reliance or expectation (see Fuller & Perdue, Reliance Interest in Contract Damages, 46 Yale L.J. 52, 53-56) an award of the cost of publication would enrich plaintiff at defendant's expense.

Pursuant to the contract, plaintiff delivered his manuscript to the defendant. In doing so, he conferred a value on the defendant which, upon defendant's breach, was required to be restored to him. Special Term, in addition to ordering a trial on the issue of damages, ordered defendant to return the manuscript to plaintiff and plaintiff's restitution interest in the contract was thereby protected. . . .

At the trial on the issue of damages, plaintiff alleged no reliance losses suffered in performing the contract or in making necessary preparations to perform. Had such losses, if foreseeable and ascertainable, been incurred, plaintiff would have been entitled to compensation for them.

As for plaintiff's expectation interest in the contract, it was basically twofold — the "advance" and the royalties. (To be sure, plaintiff may have expected to enjoy whatever notoriety, prestige or other benefits that might have attended publication, but even if these expectations were compensable, plaintiff did not attempt at trial to place a monetary value on them.) There is no dispute that plaintiff's expectancy in the "advance" was fulfilled — he has received his $2,000. His expectancy interest in the royalties — the profit he stood to gain from sale of the published book — while theoretically compensable, was speculative. Although this work is not plaintiff's first, at trial he provided no stable foundation for a reasonable estimate of royalties he would have earned had defendant not breached its promise to publish. In these circumstances, his claim for royalties fails for uncertainty. . . .

Since the damages which would have compensated plaintiff for anticipated royalties were not proved with the required certainty, we agree with the dissent in the Appellate Division that nominal damages alone are recoverable. . . .

. . . Though these are damages in name only and not at all compensatory, they are nevertheless awarded as a formal vindication of plaintiff's legal right to compensation which has not been given a sufficiently certain monetary valuation. . . .

In our view, the analogy by the majority in the Appellate Division to the construction contract situation was inapposite. In the typical construction contract, the owner agrees to pay money or other consideration to a builder and expects, under the contract, to receive a completed building in return. The value of the promised performance to the owner is the properly constructed building. In this case, unlike the typical construction contract, the value to plaintiff of the promised performance — publication — was a percentage of sales of the books published and not the books themselves. Had the plaintiff contracted for the printing, binding and delivery of a number of hardbound copies of his manuscript, to be sold or disposed of as he wished, then perhaps the construction analogy, and measurement of damages by the cost of replacement or completion, would have some application.

Here, however, the specific value to plaintiff of the promised publication was the royalties he stood to receive from defendant's sales of the published book. Essentially, publication represented what it would have cost the defendant to confer that value upon the plaintiff, and, by its breach, defendant saved that cost. The error by the courts below was in measuring damages not by the value to plaintiff of the promised performance but by the cost of that performance to defendant. Damages are not measured, however, by what the defaulting party saved by the breach, but by the natural and probable consequences of the breach *to the plaintiff*. In this case, the consequence to plaintiff of defendant's failure to publish is that he is prevented from realizing the gains promised by the contract — the royalties. But, as we have stated, the amount of royalties plaintiff would have realized was not ascertained with adequate certainty and, as a consequence, plaintiff may recover nominal damages only.

Accordingly, the order of the Appellate Division should be modified to the extent of reducing the damage award of $10,000 for the cost of publication to six cents, but with costs and disbursements to the plaintiff.

NOTE ON NOMINAL DAMAGES

Six cents doesn't go far these days. It would be safe to say that it is a "nominal" amount. Nominal damages are awarded for breach of contract when the plaintiff has a valid cause of action against the defendant but actual damages have not been proven and cannot be presumed (in some types of torts, damages are presumed to have been incurred, for example, when the tort of defamation of a commercial entity has occurred). An award of nominal damages may be better than an outright dismissal of the plaintiff's action. In awarding nominal damages, the court is necessarily finding that the plaintiff's position concerning breach is correct. This may influence other parties' behavior in dealing with the plaintiff.

Problem 68

Suzie Temple entered her dog in the "Perfect Pet" contest at the Savabit store. The grand prize was $25,000. Suzie's dog and three other dogs made it to the finals. Two hours before the final judging among Suzie's dog and the other finalists, the company running the contest, Big Winner, Inc., withdrew. Suzie sues, requesting the money. Big Winner defends, alleging insufficient certainty. Who wins? Cf. Wachtel v. National Alfalfa Journal, 190 Iowa 1293, 176 N.W. 801 (1920).

Lack of certainty as to whose dog would have won
Had the ? definite win, then perhaps — but here doesn't

HUMETRIX, INC. v. GEMPLUS S.C.A.
United States Court of Appeals, Ninth Circuit, 2001
268 F.3d 910

RICHARD C. TALLMAN, Circuit Judge:

Happy contractual relationships are all alike; but every unhappy contractual relationship is unhappy in its own way.[1]

In this case, a United States health care consulting company, Humetrix, Inc. ("Humetrix"), contracted with the world's leading manufacturer of Smart Card technology, Gemplus S.C.A. ("Gemplus"), to provide portable patient data storage solutions to the United States health care market.[2] By all indications, Gemplus and Humetrix were poised on the threshold of a promising business opportunity. Humetrix labored industriously to capitalize on this opportunity, raising finances, increasing its sales staff, and developing a client base in the United States.

1. See Leo Tolstoy, *Anna Karenina* 1 (C. Garnett trans.1933).

2. A Smart Card is a credit card-sized microprocessor that stores data files. With the proper hardware, the data files can be downloaded, viewed, updated, and restored. Smart Cards also contain security protocols that protect the confidentiality of the data stored on them. The initial health care application envisioned by Humetrix and Gemplus permitted a cardholder to maintain his or her current immunization records in this computerized credit card storage medium.

Unbeknownst to Humetrix, however, two events occurred within Gemplus that threatened the vitality of their partnership. First, Guy Guistini, a Gemplus senior manager and the progenitor of the French health care Smart Card program, learned that Humetrix had registered the trademark "Vaccicard" in the United States. Guistini was a 45% shareholder in Inovaction S.A.R.L. ("Inovaction"), a French company that held the French trademarks "Vaccicarte" and "Vaccicard." Second, Gemplus acquired a new U.S. subsidiary that could perform many of the functions that Humetrix was to have performed as Gemplus's American partner.

As a result of these events, Gemplus's cooperative efforts with Humetrix came to a grinding halt. For more than a month, Gemplus ignored Humetrix's increasingly urgent entreaties to honor the parties' agreements. Finally, Gemplus explained that, contrary to its prior representations, it viewed Humetrix not as its partner, but merely as a reseller. Humetrix had already invested significant time and resources in market research, client development, and product development, and had closed contracts with two California counties.

Humetrix sued Gemplus for breach of contract and breach of its fiduciary duty as Humetrix's partner. Humetrix also sued Guistini for intentional interference with contractual relations and Inovaction seeking a declaration that Humetrix was entitled to use the "Vaccicard" trademark in the United States. The jury awarded Humetrix $15 million in damages for breach of contract and breach of fiduciary duty. The jury also declared that Humetrix was entitled to use the trademark "Vaccicard" in the U.S. market.

Gemplus argues on appeal that the district court erred by: (1) allowing the jury to consider evidence of two oral agreements between the parties; (2) allowing the jury to consider evidence of lost profit damages despite Humetrix's use of equitable estoppel to overcome the statute of frauds; (3) allowing the jury to consider the testimony of Humetrix's experts regarding lost profits; (4) excluding evidence of Humetrix's attempts to contract with a replacement supplier of Smart Cards; and (5) entering judgment on a jury verdict that resulted from passion, confusion, or wild speculation.

Inovaction argues on appeal that the district court erred by: (1) holding that Humetrix's trademark application comported with the Lanham Act; and (2) entering judgment based on the jury's determination that Humetrix's trademark application was valid and prior to Inovaction's when there was insufficient evidence to support that determination.

We have jurisdiction under 28 U.S.C. §1291, and we affirm.

I

In 1994, Gemplus's Health Applications Sales Manager, Dr. Bruno Lassus, spoke at a medical conference about health care applications of Smart Card technology. Humetrix's founder, president, and sole shareholder, Dr. Bettina Experton, was among those in attendance. She approached Dr. Lassus after his presentation, and the two struck up a conversation about opportunities in the United States for Smart Card technology. Gemplus had no presence to speak of in the United States, and Dr. Lassus was impressed and enticed by Dr. Experton's suggestions. Humetrix and Gemplus began negotiations that spanned much of the next year. Dr. Experton visited Gemplus's headquarters in France on three occasions. Drs. Experton and Lassus initially envisioned Humetrix only as a U.S. reseller of Gemplus's Smart Card products because Gemplus already had a U.S. subsidiary, Gemplus Card International Corp. ("Gemplus USA"). At Dr. Lassus's request, Humetrix negotiated an Agency Agreement with Gemplus USA.

Dr. Lassus became increasingly impressed, however, with the opportunities available in the United States and with Humetrix's ingenuity and resourcefulness in exploiting those opportunities. As Humetrix earned a more prominent role in Gemplus's efforts to penetrate the U.S. health care market, Drs. Lassus and Experton discussed a new role for Humetrix, a role as Gemplus's partner. The negotiations proceeded, in the words of Dr. Lassus, "discreetly so as not to hurt Gemplus [USA]."

In April 1995, Dr. Lassus visited Gemplus USA and was disappointed to discover that Gemplus USA had not organized any meetings with U.S. health care companies. By contrast, Dr. Lassus reported that during a subsequent visit with Humetrix, Dr. Experton secured meetings with a number of important decision-makers in the U.S. health care industry. Dr. Lassus concluded that Humetrix was uniquely qualified to engineer Gemplus's successful entrance into the U.S. market. He observed, by contrast, that "neither Gemplus [USA] nor our competitors know how to tackle the U.S. health care market." Dr. Lassus continued to feel that "[t]he U.S. represents an extraordinary market for our technology in the health care and social services area."

By May, Gemplus and Humetrix were engaged in what Dr. Lassus described as a "pure partnership/collaboration." As Dr. Experton wrote shortly thereafter to a potential investor, Humetrix had "already generated firm orders and more interest than [Humetrix's] development and sales forces [we]re able to handle." Dr. Lassus directed Dr. Experton to draft an agreement between Humetrix and Gemplus reflecting their "partnership" and a new compensation scheme pursuant to which, in addition to the commission provided by the Agency Agreement with Gemplus USA, Humetrix was to keep the full margin of each unit sold in the United States. Humetrix drafted such an agreement, entitled the Representative Agreement, and sent it to Gemplus to be signed.

Dr. Lassus also encouraged Dr. Experton to develop a name for the vaccination Smart Card they intended to offer on the U.S. market and to obtain legal protection for that name. After researching market reaction to several names, Dr. Experton settled on "Vaccicard." Humetrix applied to register the trademark "Vaccicard" on June 14, 1995.

In July and August 1995, even as Humetrix closed contracts with two California counties and expanded its sales and development resources to meet the burgeoning supply of U.S. health care clients, its partnership with Gemplus suffered two setbacks.

First, Guy Guistini learned that Humetrix had registered the trademark "Vaccicard" for use in the United States. Guistini was the progenitor of the French Smart Card application that stored vaccination records. In addition to being the "personal adviser" to Gemplus's president, he held 45% of the shares of Inovaction, the French company that registered the trademarks "Vaccicarte" and "Vaccicard" in France. Guistini insisted that Inovaction hold the American trademark as well. He ordered Dr. Experton to withdraw Humetrix's trademark application and to stop using the Vaccicard trademark. When Dr. Experton did not accede to his demands, Guistini resorted to threats and intimidation. Inovaction filed its own American trademark application on July 19, 1995, more than a month after Humetrix's application.

Second, Gemplus acquired a new U.S. subsidiary. At Dr. Lassus's direction, Gemplus USA refrained from mentioning the acquisition to Dr. Experton.

As August drew to a close, Dr. Experton again visited France. Dr. Lassus and Gemplus's president assured her that Gemplus would execute the Representative Agreement at a meeting during her visit. Gemplus first rescheduled, then canceled, the meeting, however, and Dr. Experton returned to the United States without an executed Representative Agreement in hand.

After Dr. Experton returned to the United States, Gemplus's communication and cooperation stopped abruptly. In the ensuing six weeks, Humetrix tried in vain to communicate with Gemplus. As the deadline for performance of Humetrix's contracts with its U.S. purchasers neared, Gemplus ignored Humetrix's entreaties to cooperate or, at the very least, communicate. Humetrix sent increasingly desperate memoranda to Gemplus portending increasingly dire consequences if Gemplus and Humetrix did not re-establish contact and deliver a product to their customers in the United States. In late September, Dr. Experton sent Dr. Lassus a four-page letter, imploring Gemplus to cooperate with Humetrix in meeting customer demands.

Finally, by telephoning Gemplus's office and pretending to be someone else, Dr. Experton succeeded in reaching Dr. Lassus on October 3. Their conversation, as chronicled by Dr. Experton's letter of the following day, was a frustrating procession of dissembling explanations and hollow reassurances. On October 16, Gemplus's president wrote Dr. Experton that the Agency Agreement between Humetrix and Gemplus USA was the only agreement between them, that Humetrix was "not entitled to hold the trademark Vaccicard in the USA since Gemplus already holds a worldwide license to this product," and that Humetrix bore no ownership interest in the Vaccicard software to be marketed in the United States. The letter closed with the rebuke: "It does not seem to me appropriate to maintain hostility with my personal adviser Guy Guistini who originated the Vaccicarte project and who has all of my confidence in this sphere as in other spheres within his competence." A draft of the letter produced during discovery revealed that Guistini himself had dictated the letter for the president's signature. Without Gemplus's cooperation, Humetrix was forced to cancel its contracts with customers in the United States.

In February 1996, Humetrix sued Gemplus, Inovaction, and Guistini. Because Gemplus never executed the Representative Agreement, Humetrix made no claims for breach of its terms. Instead, Humetrix alleged that the discussions between Humetrix and Gemplus culminated in the formation of two oral contracts, the Sales Agreement and the Partnership Agreement, and that Gemplus breached them both. Humetrix attributed Gemplus's breach, in part, to the interference of Guistini, for which Humetrix sought compensatory and punitive damages. Finally, Humetrix sought a declaration that it had properly registered the trademark "Vaccicard" in the United States.

Gemplus countered that the Agency Agreement constituted the sole agreement between Humetrix and Gemplus or its subsidiaries and moved to compel arbitration in accordance with the Agency Agreement's mandatory arbitration clause. The district court denied Gemplus's motion. On interlocutory appeal, we affirmed on the grounds that "Gemplus was not a party to the Agency Agreement that contained the arbitration provision," only Gemplus USA and Humetrix were parties to the Agency Agreement, and that "Humetrix enjoyed a distinct and separate contractual relationship with parent company Gemplus." Humetrix, Inc. v. Gemplus, S.C.A., No. 97-55080, 1997 WL 683301, at *1, *3 (9th Cir. Oct. 23, 1997) (unpublished disposition; see 9th Cir. R. 36-3).

Humetrix's claims against Gemplus, Guistini and Inovaction were tried before a jury. The jury found that Humetrix and Gemplus entered into the Sales Agreement and the Partnership Agreement. The jury further found that:

1. Gemplus breached the Sales Agreement, damaging Humetrix in the amount of $5 million;
2. Gemplus breached the Partnership Agreement, damaging Humetrix in the amount of $10 million;
3. Guistini intentionally interfered with Humetrix's contractual relations, damaging Humetrix in the amount of $1.2 million;
4. Guistini's conduct warranted an award of punitive damages to Humetrix in the amount of $1.3 million; and,
5. Humetrix was the proper legal owner of the Vaccicard trademark in the United States. Gemplus and Inovaction appeal.[3]

II . . .

Under California law, a plaintiff that prevails on a breach of contract claim "should receive as nearly as possible the equivalent of the benefits of performance," meaning the plaintiff should be put "in as good a position as he would have been had performance been rendered as promised." Brandon & Tibbs v. George Kevorkian Accountancy Corp., 226 Cal. App. 3d 442, 277 Cal. Rptr. 40, 47 (Ct. App. 1990). This may include lost profits if the plaintiff can prove that the defendant's failure to perform caused the plaintiff to lose profits. See id. at 48-49.

3. The district court vacated the punitive damages award against Guistini, and Humetrix and Guistini subsequently settled.

C

Gemplus contends that the district court erred by admitting Humetrix's damages experts' testimony regarding lost profits. Gemplus claims that the testimony was speculative and was unsupported by the evidence. District courts, in their capacity as evidentiary gatekeepers, have broad discretion in deciding what evidence is relevant, reliable, and helpful to the trier of fact. Desrosiers v. Flight Int'l of Florida Inc., 156 F.3d 952, 961 (9th Cir. 1998); Shore v. Mohave, Arizona, 644 F.2d 1320, 1322 (9th Cir. 1981). . . .

Both we and California state courts have recognized that lost profits are "necessarily an estimate," Portland 76 Auto/Truck Plaza, Inc. v. Union Oil Co., 153 F.3d 938, 947 (9th Cir. 1998), cert. denied, 526 U.S. 1064, 119 S. Ct. 1454, 143 L. Ed.2d 541 (1999), and that their "amount cannot be shown with mathematical precision." Berge v. Int'l Harvester Co., 142 Cal. App. 3d 152, 190 Cal. Rptr. 815, 822 (Ct. App. 1983). We uphold awards of lost profit damages so long as they are supported by substantial evidence. See Transgo, Inc. v. Ajac Transmission Parts Corp., 768 F.2d 1001, 1024 (9th Cir. 1985); Heiner v. Kmart Corp., 84 Cal. App. 4th 335, 100 Cal. Rptr. 2d 854, 863 (Ct. App. 2000).

Humetrix's request for lost profit damages is supported by the testimony of two experts. The experts based their testimony on contracts Humetrix had closed, pilot projects for which Humetrix had received commitments, and contracts in negotiation at the time of breach; Humetrix's partnership with Gemplus, the world's leading manufacturer of Smart Cards; Gemplus's success in foreign markets; Dr. Experton's contacts with government health care officials; and market forecasts, including Gemplus's own. Their testimony is borne out by Gemplus's own contemporaneous observations that "the real market boom is still ahead of us," and that "the U.S. represents an extraordinary market for our technology in the health care and social services area." Humetrix's request for lost profits was supported by substantial evidence.

To the extent Gemplus sought to challenge the correctness of Humetrix's experts' testimony, its recourse is not exclusion of the testimony, but, rather, refutation of it by cross-examination and by the testimony of its own expert witnesses. Gemplus availed itself of both of these opportunities. Gemplus cross-examined Humetrix's experts and presented its own expert.

Authority to determine the victor in such a "battle of expert witnesses" is properly reposed in the jury. Wyler Summit P'ship v. Turner Broad. Sys., Inc., 235 F.3d 1184, 1192 (9th Cir. 2000) ("Weighing the credibility of conflicting expert witness testimony is the province of the jury."). As one California court of appeal observed:

> As to the reasonableness of the assumptions underlying the experts' lost profit analysis, criticisms of an expert's method of calculation [are] a matter for the jury's consideration in weighing that evidence. It is for the trier of fact to accept or reject this evidence, and this evidence not being inherently improbable provides a substantial basis for the trial court's award of lost profits.

Arntz Contracting Co. v. St. Paul Fire & Marine Ins. Co., 47 Cal. App. 4th 464, 54 Cal. Rptr. 2d 888, 903 (Ct. App. 1996) (internal quotations and citations omitted); see also Flavor Dry, Inc. v. Lines (In re James E. O'Connell Co., Inc.), 799 F.2d 1258, 1261-62 (9th Cir. 1986) (applying California law) (declining to overturn lost profit award based on expert testimony supported by financial statements, data pertaining to similar businesses, and market forecasts). Humetrix's experts based their testimony on substantial evidence. The district court did not abuse its discretion by allowing the jury to weigh the conflicting testimony of the parties' experts regarding lost profit damages.

Gemplus also argues that lost profit damages are inappropriate for a "new business" because, without a record of past performance as a standard, future profits are necessarily speculative. In light of the "new business rule," Gemplus argues, the district court abused its discretion by allowing the jury even to consider Humetrix's future profits in determining its damages.

The new business rule is more empirical than normative, however. As an empirical matter, new businesses often cannot offer reliable proof of prospective profits. As a normative matter, if a business can offer reliable proof of profits, there is no reason to deprive it of the profits it would have garnered had the contract been performed merely because it is "new." As one California court put it: "[T]he [new business] rule is not a hard and fast one and loss of prospective profits may nevertheless be recovered if the evidence shows with reasonable certainty both their occurrence and the extent thereof." Gerwin v. Southeastern California Ass'n of Seventh Day Adventists, 14 Cal. App. 3d 209, 92 Cal. Rptr. 111, 119 (Cal. Ct. App. 1971).

Moreover, Humetrix was not exactly a new business. When it contracted with Gemplus it had been offering health care consulting and information systems services to the California and national markets for ten years. See Maggio, Inc. v. United Farm Workers, 227 Cal. App. 3d 847, 278 Cal. Rptr. 250, 264 (Ct. App. 1991) ("Cases applying the 'new business rule' generally involve businesses which have been in operation only a very short period of time."). Indeed, the experience, the contacts, and the dynamism of its principal, Dr. Experton, led Dr. Lassus to observe that Humetrix was uniquely capable of successfully marketing Smart Card technology in the United States.

Humetrix's experts were also able to draw on Gemplus's own experience introducing Smart Card technology into previously untapped markets. Humetrix's profits were, in a sense, dependent on and derivative of Gemplus's profits so that if one could be determined reliably, the other followed as a matter of course. Under these circumstances, the profits Humetrix could expect to garner from its contracts with Gemplus were not so speculative that the district court abused its discretion by allowing the jury to hear evidence regarding profits. . . .

E

Gemplus argues, finally, that the district erred by entering the jury's $15 million award of damages, an award Gemplus claims could only be the result of passion, confusion, or wild speculation by the jury. Our role in reviewing a jury award entered under California law is limited:

> [A]s a reviewing court, we view the evidence through a different lens than does the trier of fact. The judgment comes to us cloaked with the presumption that it is correct. In assessing a claim that the jury's award of damages is excessive, we do not reassess the credibility of witnesses or reweigh the evidence. To the contrary, we consider the evidence in the light most favorable to the judgment, accepting every reasonable inference and resolving all conflicts in its favor. We may interfere with an award of damage only when it is so large that it shocks the conscience and suggests passion, prejudice or corruption on the part of the jury.

Westphal v. Wal-Mart Stores, Inc., 68 Cal. App. 4th 1071, 81 Cal. Rptr. 2d 46, 48 (Ct. App. 1998).

Humetrix and Gemplus were poised at the inception of a promising business opportunity — to provide a technological breakthrough in personal health care documentation to government and private health care entities around the country. Gemplus's similar foreign endeavors had been very profitable. Gemplus was confident that its campaign in the United States would be equally profitable. Under these circumstances, the jury's determination that Humetrix could have earned $15 million in net profits over the ensuing five years does not shock the conscience or suggest passion, prejudice, or corruption. The district court did not abuse its discretion by entering the jury's verdict on damages as the proper judgment. . . .

For the foregoing reasons, the judgment of the district court is affirmed.

2. Foreseeability

HADLEY v. BAXENDALE
Court of the Exchequer, 1854
9 Exch. 341, 156 Eng. Rep. 145

At the trial before Crompton, J., at the last Gloucester Assizes, it appeared that the plaintiffs carried on an extensive business as millers at Gloucester; and that, on the 11th of May, their mill was stopped by a breakage of the crank shaft by which the mill was worked. The steam-engine was manufactured by Messrs. Joyce & Co., the engineers, at Greenwich, and it became necessary to send the shaft as a pattern for a new one to Greenwich. The fracture was discovered on the 12th, and on the 13th the plaintiffs sent one of their servants to the office of the defendants, who are the well-known carriers trading under the name of Pickford & Co., for the purpose of having the shaft carried to Greenwich. The plaintiffs' servant told the clerk that the mill was stopped, and that the shaft must be sent immediately; and in answer to the inquiry when the shaft would be taken, the answer was, that if it was sent up by twelve o'clock any day, it would be delivered at Greenwich on the following day. On the following day the shaft was taken by the defendants, before noon, for the purpose of being conveyed to Greenwich, and the sum of 2*l.* 4*s.* was paid for its carriage for the whole distance; at the same time the defendants' clerk was told that a special entry, if required, should be made to hasten its delivery. The delivery of the shaft at Greenwich was delayed by some neglect; and the consequence was, that the plaintiffs did not receive the new shaft for several days after they would otherwise have done, and the working of their mill was thereby delayed, and they thereby lost the profits they would otherwise have received.

On the part of the defendants, it was objected that these damages were too remote, and that the defendants were not liable with respect to them. The learned Judge left the case generally to the jury, who found a verdict with 25*l.* damages beyond the amount paid into Court.

Whateley, in last Michaelmas Term, obtained a rule nisi for a new trial, on the ground of misdirection. . . .

ALDERSON, B. We think that there ought to be a new trial in this case; but, in so doing, we deem it to be expedient and necessary to state explicitly the rule which the Judge, at the next trial, ought, in our opinion, to direct the jury to be governed by when they estimate the damages.

It is, indeed, of the last importance that we should do this; for, if the jury are left without any definite rule to guide them, it will, in such cases as these, manifestly lead to the greatest injustice. The Courts have done this on several occasions; and, in Blake v. Midland Railway Company (18 Q.B. 93), the Court granted a new trial on this very ground, that the rule had not been definitely laid down to the jury by the learned Judge at Nisi Prius.

"There are certain established rules," this Court says, in Alder v. Keighley (15 M.&W. 117), "according to which the jury ought to find." And the Court, in that case, adds: "and here there is a clear rule, that the amount which would have been received if the contract had been kept, is the measure of damages if the contract is broken."

Now we think the proper rule in such a case as the present is this: — Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, i.e., according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it. Now, if the special circumstances under which the contract was actually made were communicated by the plaintiffs to the defendants, and thus known to both parties, the damages resulting from the breach of such a contract, which they would reasonably contemplate, would be the amount of injury which would ordinarily follow from a breach of contract under these special circumstances so known and communicated. But, on the other hand, if these special circumstances were wholly unknown to the party breaking the contract, he, at the most, could only be supposed to have had in his contemplation the amount of injury which would arise generally, and in the great multitude of cases not affected by any special circumstances,

knowledge
key to issue

from such a breach of contract. For, had the special circumstances been known, the parties might have specially provided for the breach of contract by special terms as to the damages in that case; and of this advantage it would be very unjust to deprive them. Now the above principles are those by which we think the jury ought to be guided in estimating the damages arising out of any breach of contract. It is said, that other cases such as breaches of contract in the non-payment of money, or in the not making a good title to land, are to be treated as exceptions from this, and as governed by a conventional rule. But as, in such cases, both parties must be supposed to be cognisant of that well-known rule, these cases may, we think, be more properly classed under the rule above enunciated as to cases under known special circumstances, because there both parties may reasonably be presumed to contemplate the estimation of the amount of damages according to the conventional rule. Now, in the present case, if we are to apply the principles above laid down, we find that the only circumstances here communicated by the plaintiffs to the defendants at the time the contract was made, were, that the article to be carried was the broken shaft of a mill, and that the plaintiffs were the millers of that mill. But how do these circumstances show reasonably that the profits of the mill must be stopped by an unreasonable delay in the delivery of the broken shaft by the carrier to the third person? Suppose the plaintiffs had another shaft in their possession put up or putting up at the time, and that

actual cause

they only wished to send back the broken shaft to the engineer who made it; it is clear that this would be quite consistent with the above circumstances, and yet the unreasonable delay in the delivery would have no effect upon the intermediate profits of the mill. Or, again, suppose that, at the time of the delivery to the carrier, the machinery of the mill had been in other respects defective, then, also, the same results would follow. Here it is true that the shaft was actually sent back to serve as a model for a new one, and that the want of a new one was the only cause of the stoppage of the mill, and that the loss of profits really arose from not sending down the new shaft in proper time, and that this arose from the delay in delivering the broken one to serve as a model. But it is obvious that, in the great multitude of cases of millers sending off broken shafts to third persons by a carrier under ordinary circumstances, such consequences would not, in all probability, have occurred; and these special circumstances were here never communicated by the plaintiffs to the defendants. It follows, therefore, that the loss of profits here cannot reasonably be considered such a conequence of the breach of contract as could have been fairly and reasonably contemplated by both the parties when they made this contract. For

what know is a factor

such loss would neither have flowed naturally from the breach of this contract in the great multitude of such cases occurring under ordinary circumstances, nor were the special circumstances, which, perhaps, would have made it a reasonable and natural consequence of such breach of contract, communicated to or known by the defendants. The Judge ought, therefore, to have told the jury, that, upon the facts then before them, they ought not to take the loss of profits into consideration at all in estimating the damages. There must therefore be a new trial in this case.

special circumstance

Rule absolute.

NOTES AND QUESTIONS

1. Baron Alderson refers to "other cases" in which the usual consequential damages are measured by different standards. These are, first, the nonpayment of money, in which the typical consequential loss is limited to unpaid interest, and, second, the failure of a seller of realty to deliver good title, where most courts will allow the seller who makes this mistake in good faith to repay the buyer's expenses but not give the buyer the loss of bargain damages.

2. Does the rule of Hadley v. Baxendale apply in UCC suits for breach of warranty alleging personal injury? See §2-715(2)(b).

Problem 69

Bill Gilbert was offered $50,000 for his new play *Engaged* if he could get it to the producer, Dick Carte, by October 12. He finished writing the play on October 10, and called up a private courier, Overnight Delivery, Inc., telling the woman he talked to on the phone all of the above details. He ended the conversation by saying, "I'll lose $50,000 if this package does not arrive by October 12." She told him not to worry. The Overnight Delivery courier picked up the package on October 11 and put it on board its airplane for delivery the next day. That night the plane crashed, and the package was never delivered. Gilbert's play was not produced, and he sued Overnight Delivery, Inc. for $50,000. Are either of the following defenses valid?

(a) Mere *knowledge* of the possible damages flowing from the breach is not the same thing as an *agreement* to accept the liability for such damages. Before the liability attaches, there must be at least a tacit agreement under which the defendant assumes the risk of the consequential loss.

(b) The plane crash was totally unforeseeable, so that Overnight Delivery is not liable for the consequential damages.

AM/PM FRANCHISE ASSN. v. ATLANTIC RICHFIELD CO.
Pennsylvania Supreme Court, 1990
526 Pa. 110, 584 A.2d 915, 14 UCC Rep. Serv. 2d 11

CAPPY, J. Before us is an appeal by members of a franchisee association from an order of the Superior Court of Pennsylvania at No. 01958 Philadelphia 1987, issued April 14, 1988, affirming the order of the Court of Common Pleas at No. 157 November Term 1986, dated June 16, 1987, sustaining defendant's preliminary objections in the nature of a demurrer and dismissing the action.

We granted allocatur to determine whether the named appellants ("plaintiffs") have alleged sufficient facts to sustain a cause of action when they aver that the gasoline they purchased from the appellee ("ARCO") was not in conformance with the warranties made and resulted in their suffering economic harm. In making such a determination, we address the question of whether such damages constitute a "loss of good will," and whether good will damages are too speculative as a matter of law to permit recovery. For the reasons set forth herein, we find that the plaintiffs have alleged sufficient facts to entitle them to proceed with their claim and that the damages claimed are not good will nor so speculative as to deny them an attempt at recovery. We reverse the decision of the Superior Court in part and affirm in part.

Procedural History

ARCO filed preliminary objections in the nature of a demurrer to appellants' complaint, claiming that the damages sought by appellants stemmed from a loss of good will, which are speculative and not recoverable as a matter of law. Additionally, the defendants claim that the plaintiffs should not be entitled to recover under a tort theory.

The trial court sustained ARCO's preliminary objections and dismissed appellants' complaint.

The Superior Court affirmed the ruling of the trial court, holding that under current Pennsylvania law, damages sought for the breach of warranty claims due to a loss of good will are not recoverable as they have traditionally been considered to be too speculative. Additionally, the Superior Court held that the plaintiff was not entitled to recover in tort, finding that the duty of the parties to act in good faith arises under contract and not tort principles.

In the dissent to the opinion of the Superior Court, Judge Brosky remarked that the majority characterizes the claim as one for loss of good will, while he "view[s] appellants' claim as a request for lost profits occasioned by appellee's delivery of an unmerchantable product." 373 Pa. Super. 572, 580, 542 A.2d 90, 94 (1988). Additionally, Judge Brosky disagreed with the characterization of the loss as speculative, stating "[a]lthough calculating damages may have been a problem in the past, and in certain cases, may still be a problem, I cannot see that it presents a problem here. . . . Further, a comparison of the business profits before and after the delivery of the unmerchantable gasoline should prove to be enlightening." Id. at 581, 542 A.2d at 94-95.

Factual History

The Plaintiffs claim to represent a class of over 150 franchisees of ARCO that operated AM/PM Mini Markets in Pennsylvania and New York during a three and one-half year period.

ARCO entered into franchise agreements with the plaintiffs which were comprised of a premises lease, a lessee dealer gasoline agreement, and an AM/PM mini-market agreement. The products agreement mandated that the franchisees sell only ARCO petroleum products.

The complaint sets forth the following facts: ARCO began experimenting with its formula for unleaded gasoline and provided its franchisees with an unleaded gasoline blended with oxinol, consisting of 4.5% methanol and 4.5% gasoline grade tertiary butyl alcohol (hereinafter "the oxinol blend") from early 1982 through September 30, 1985.

During this three and a half year period, the franchisees were required to sell the oxinol blend to their clients who desired unleaded gasoline. The franchisees were given no opportunity to buy regular unleaded gasoline from ARCO during that period.

Plaintiffs claim that numerous purchasers of the oxinol blend gasoline experienced poor engine performance and physical damage to fuel system components. Specifically, plaintiffs claim that the oxinol gasoline permitted an excess accumulation of alcohol and/or water which interfered with the efficiency of gasoline engines and, in certain vehicles, caused swelling of plastic or rubber components in the fuel delivery system and resulted in engine damage. The plaintiffs claim that the gasoline did not conform to ARCO's warranties about the product.

As the problems with the oxinol blend became known, the plaintiffs claim to have suffered a precipitous drop in the volume of their business and an attendant loss of profits. Specifically, plaintiffs point to the rise in sales from 1973 until 1982, when sales began to fall dramatically; allegedly due to defective oxinol blend gasoline.

In their complaint, plaintiffs allege three counts of breach of warranty, breach of implied duty, misrepresentation, and exemplary damages. They request damages for "lost profits, consequential and incidental damages."

Discussion

The point at which we start our inquiry is the Uniform Commercial Code ("the U.C.C."), codified at 13 Pa C.S. §1101 et seq. Section 2-714, entitled "Damages of buyer for breach in regard to accepted goods" is one of the governing provisions in the case before us, and provides, in pertinent part:

> (2) Measure of damages for breach of warranty. 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) Incidental and consequential damages. In a proper case any incidental and consequential damages under section 2-715 (relating to incidental and consequential damages of buyer) may also be recovered.

Section 2-715 is entitled "Incidental and Consequential Damages of Buyer" and provides, in pertinent part:

> (1) Incidental damages. Incidental damages resulting from the breach of the seller include: . . .
>
> (c) any other reasonable expenses incident to the delay or other breach.

(2) Consequential damages. Consequential damages resulting from the breach of the seller 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.

Pursuant to the provisions of the U.C.C., plaintiffs are entitled to seek "general" damages, so-called, under §2-714(2), and consequential damages as provided by §2-714(3).

There has been substantial confusion in the courts and among litigants about what consequential damages actually are and what types of consequential damages are available in a breach of warranty case. Where a buyer in the business of reselling goods can prove that a breach by the seller has caused him to lose profitable resales, the buyer's lost profits constitute a form of consequential damages. We now hold that in addition to general damages, there are three types of lost profit recoverable as consequential damages that may flow from a breach of warranty: (1) loss of primary profits; (2) loss of secondary profits; and (3) a loss of good will damages (or prospective damages, as they are sometimes termed).

In order to alleviate the confusion that has developed concerning the various damages, we use an example to help illustrate the different types.

General damages in the case of accepted goods (such as occurred here) are the actual difference in value between the goods as promised and the goods as received. Thus, suppose a buyer bought five hundred tires from a wholesaler that were to be delivered in good condition, and in that condition would be worth $2,500. The tires were delivered with holes in them which rendered them worthless. The buyer would be entitled to $2,500 from the seller — the difference between the value of the tires as warranted and the value of the tires as received; those would be the general damages.

Consequential damages are generally understood to be other damages which naturally and proximately flow from the breach and include three types of lost profit damages: (1) lost primary profits; (2) lost secondary profits; and (3) loss of prospective profits, also commonly referred to as good will damages.

Lost primary profits are the difference between what the buyer would have earned from reselling the goods in question had there been no breach and what was earned after the breach occurred. Thus, if the buyer of the tires proved that he would have resold the tires for $5,000, he would be able to claim an additional $2,500 for loss of tire profits; the difference between what he would have earned from the sale of the tires and what he actually did earn from the sale (or lack of sales) from the tires.

If the buyer of the tires also sold, for example, hubcaps with every set of tires, he would also suffer a loss of hubcap profits. These types of damages are what we term "loss of secondary profits."

If the buyer's regular customers were so disgruntled about the defective tires that they no longer frequented the buyer's business and began to patronize a competitor's business, the buyer would have suffered a "loss of good will" beyond the direct loss of profits from the nonconforming goods; his future business would be adversely affected as a result of the defective tires. Thus, ~~good will damages refer to profits lost~~ on future sales rat~~her than on sales of the defective~~ goods themselves.

While this example provides a simple framework to understand the different types of possible damages in a breach of warranty case, it does not encompass the myriad of circumstances in which a claim for damages can arise, nor does it specify which of these different damages have been allowed in Pennsylvania.

In addition to recognizing general damages under §2-714 of the Code, Pennsylvania allows consequential damages in the form of lost profits to be recovered.

Pennsylvania has, however, disallowed good will damages; finding them to be too speculative to permit recovery. In the cases disallowing good will damages, part of the reason we found them too speculative is that the damages were not contemplated by the parties at the time the contract was made. . . .

Turning to the case at hand, we must determine whether the plaintiffs have alleged sufficient facts to permit them to proceed with a claim for consequential damages. . . .

Loss of Profits for Gasoline Sales

The first claim the plaintiff makes for damages is for the profits lost from the sales of gasoline. The plaintiffs claim that the breach of warranty by the defendant concerning the gasoline caused the plaintiffs to lose sales during a three and one half year period while they received nonconforming gasoline from ARCO. In the case of Kassab v. Central Soya, 432 Pa. 217, 246 A.2d 848 (1968), we permitted lost profits for cattle sales when the plaintiff showed that the defective feed caused harm to their cattle, causing the public to stop buying their cattle. The allegation here is similar. When the gasoline buying public discovered that the gasoline was defective, many stopped purchasing ARCO gasoline.

Employing the reasoning of *Kassab* and taking it one step further, we believe that the plaintiffs here are entitled to show that the gasoline buying community did not buy their gasoline from 1982 through 1985 because of the reasonable belief that the gasoline was defective and would harm their engines. The lost gasoline sales are comparable to the lost cattle sales in *Kassab.* The distinction between the two cases is that the Kassabs had bought the feed all at one time and thus all their livestock was affected. The instant plaintiffs bought their gasoline in regular intervals and could only earn a profit on what they could sell per month. The defendant's argument — that the plaintiffs sold all the gasoline they bought — misses the point. While they may have sold every gallon, they sold significantly fewer gallons during the period that ARCO allegedly delivered nonconforming gasoline. Thus, during this period, the plaintiffs' lost sales were just as directly attributable to the defective gasoline as the lost profits were attributable to the defective tires in the example we used previously.

Thus, if prior to the manufacture of defective gasoline the plaintiffs sold 100,000 gallons per month every month and then as a result of the defective gasoline, they sold only 60,000 gallons per month every month until ARCO discontinued that gasoline, then the plaintiffs have lost the profits they would have received on 40,000 gallons per month for the three year claimed period. Lost profits are, in fact, the difference between what the plaintiff actually earned and what they would have earned had the defendant not committed the breach. Because the gasoline was allegedly not in conformance with the warranties, the plaintiffs may be entitled to lost profits for the gasoline on a breach of warranty theory. The lost gasoline sales are what we have termed "loss of primary profits," and they are recoverable pursuant to §2-715 of the U.C.C. upon proper proof. . . .

Furthermore, we note that §1-106 of the U.C.C. provides:

> [t]he remedies provided by this title shall be *liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed* but neither consequential or special nor penal damages may be had except as specifically provided in this title or by other rule of law. (Emphasis supplied.)

The Code itself compels us to be liberal in our interpretation of the types of damages we permit. We would therefore allow the plaintiffs to proceed with their claims for lost gasoline profits during the period ARCO supplied allegedly nonconforming gasoline.

Loss of Profits for Items Other than Gasoline Sales

The plaintiffs allege that in addition to a loss of profits for sales of gasoline, they had a concomitant loss of sales for other items that they sold in their mini-marts during the period of time that ARCO supplied nonconforming gasoline. Their rationale is that when the number of customers buying gasoline decreased, so did the number of customers buying items at the mini-mart. In other words, related facets of their business suffered as a result of the defective gasoline. This type of injury is what we characterize as "loss of secondary profits"; meaning that the sales of other products suffered as a result of the breach of warranty. This court has not had an opportunity to address whether these types of damages are recoverable.

In the case before us, the essence of plaintiffs' allegations is that customers frequent the mini-marts because it is convenient to do so at the time they purchase gasoline. Customers of the mini-mart are foremost gasoline buying patrons; gasoline is their primary purchase and sundries are their incidental purchases. Here, the plaintiffs claim that the *primary product* sales so affected the incidental sales as to create a loss in other aspects of their business. It is reasonable to assume that if the gasoline sales dropped dramatically, there was a ripple effect on the mini-mart sales. Additionally, when a primary product does not conform to the warranty, we believe that it is foreseeable that there will be a loss of secondary profits. Thus, permitting these damages would correspond with the requirement of foreseeability as set forth in *Lampus,* supra, and the Code. It is much less foreseeable to assume there will be a loss of secondary losses are too indirect

secondary profits when the nonconforming products are not the primary ones. We believe that unless it is a primary product that does not conform to the warranty, the causal relationship between the breach and the loss is too attenuated to permit damages for the loss of secondary profits.[12]

We also find that the fact situation before us presents a further problem in that the plaintiffs were not able to mitigate the harm in any way by buying substitute goods or "cover." Thus, the plaintiffs' primary product was defective and they were unable to remedy the situation by buying gasoline from another supplier.

We find that the present case presents compelling reasons for permitting damages for loss of secondary profits. Henceforth, in a breach of warranty case, when a primary product of the plaintiff is alleged to be nonconforming and the plaintiff is unable to cover by purchasing substitute goods, we hold that upon proper proof, the plaintiff should be entitled to sue for loss of secondary profits.[13]

Loss of Good Will

Historically, Pennsylvania has disallowed recovery for loss of good will damages or prospective profits in breach of warranty cases. The cases generally relied upon for this proposition are Michelin Tire Co. v. Schultz, 295 Pa. 140, 145 A. 67 (1929); Harry Rubin & Sons, Inc. v. Consolidated Pipe Co. of America, 396 Pa. 506, 153 A.2d 472 (1959); and Kassab v. Central Soya, 432 Pa. 217, 246 A.2d 848 (1968). . . .

As one commentator aptly noted, "[l]oss of good will is a mercurial concept and, as such, is difficult to define. In a broad sense, it refers to a loss of future profits."[14] Other jurisdictions have considered loss of good will to be a loss of profits and reputation among customers.[15] Generally, good will refers to the reputation that businesses have built over the course of time that is reflected by the return of customers to purchase goods and the attendant profits that accompanies such sales. Thus the phrase "good will damages" is coextensive with prospective profits and loss of business reputation.

Secondly, we must decide when good will damages arise in a breach of warranty situation. Essentially, damage to good will in a case in which

12. As with all cases involving breach of warranty, the plaintiff is charged with the burden of proving that the defendant's breach is the proximate cause of the harm suffered. Thus, in order to proceed with their case, the plaintiffs here must prove that the alleged nonconformance of the gasoline caused both their loss of gasoline sales as well as their loss of mini-mart sales. This requirement is an arduous one and we render no opinion as to whether the plaintiffs can meet this burden. However, we note that this is for the trial court, in its wisdom, to decide whether the plaintiffs have met the threshold of proof to submit the case to the factfinder.

13. What constitutes a "primary product" will be dependent on the facts of each case. However, we would define a "primary product" as an item upon which the aggrieved party relies for a substantial amount of its revenue. The plaintiff must show that without that product, his business would be severely incapacitated.

14. Anderson, Incidental and Consequential Damages, 7 J. L. & Com. 327, 420 (1987).

15. Texsun Feed Yards, Inc. v. Ralston Purina Co., 447 F.2d 660 (5th Cir. 1971).

the seller supplies a quantity dictated by the buyer's requirements arises only *after* the seller has ceased providing nonconforming goods — or the buyer has purchased substitute goods. Damage to good will in this case would refer to the loss of business sales that occurred after the buyer was able to provide acceptable goods to his customers; it does not refer to the period of time during which he is forced to sell the nonconforming goods.

Thirdly, we must address whether good will damages are too speculative to permit recovery, as we held in Michelin, Rubin & Sons, supra, and *Kassab,* supra. Although we disallowed good will damages in those cases, they are not recent. They were written in a time when business was conducted on a more simple basis, where market studies and economic forecasting were unexplored sciences.

We are now in an era in which computers, economic forecasting, sophisticated marketing studies and demographic studies are widely used and accepted. As such, we believe that the rationale for precluding prospective profits under the rubric of "too speculative" ignores the realities of the marketplace and the science of modern economics. We believe that claims for prospective profits should not be barred ab initio. Rather, plaintiffs should be given an opportunity to set forth and attempt to prove their damages.

Twenty years ago, the Third Circuit Court of Appeals noted in a case disallowing claims for prospective profits that damages once considered speculative may not be in the future:

> This is not to say we approve the Pennsylvania view or believe it will be the Pennsylvania position in the future [prohibiting good will damages]. Considering the advances made in techniques of market analysis and the use of highly sophisticated computers it may be that lost profits of this nature are no more speculative than lost profits from the destruction of a factory or hotel, and perhaps Pennsylvania will reconsider the reason for its rule in a future case.

Neville Chemical Co. v. Union Carbide Corp., 422 F.2d 1205, 1227 (1970).

We believe the time has come to reconsider that rule. In doing so, we find our position on recovery for good will damages (or prospective profits) to be out of step with modern day business practices and techniques, as well as the law of other jurisdictions. As noted by Professor Anderson in his well-crafted article on incidental and consequential damages,

> [t]o date, only the Pennsylvania courts have categorically denied recovery for loss of goodwill under any circumstances, an issue which has been oft-litigated in Pennsylvania. If one removes the Pennsylvania cases from the count, a significant majority of the cases have allowed for the recovery of lost goodwill in proper circumstances.[17]

Furthermore, our rule has been repeatedly criticized by other courts and commentators.[18] In reviewing our case law on the issue of prospective profits, we have not had a significant case come before us since *Kassab* was decided in 1968. Since that time, astronauts have walked on the moon, engineers have developed computers capable of amazing feats and

17. Anderson, Incidental and Consequential Damages, 7 J.L. & Com. 327, 421 (1987).

18. See, e.g., Neville Chemical Co. v. Union Carbide Corp., 422 F.2d 1205, 1227 (3d Cir. 1970); Comment, Loss of Goodwill and Business Reputation as Recoverable Elements of

biomedical engineers and physicians have made enormous strides in organ transplantation and replacement. It is evident that the world of 1990 is not the same world as it was in 1929 when the *Michelin* case was decided, nor even the same world as it was in 1968 when *Kassab* was decided. While these rapid technological developments have not been without their concomitant problems, they have made possible many things that were not possible before; including the calculation of prospective profits. For these reasons, we overrule *Michelin,* supra, *Rubin & Sons, Inc.,* supra, and *Kassab,* supra, to the extent they prohibit a plaintiff from alleging a claim for damage to good will as a matter of law.

Inextricably entwined with the issue of speculation is the difficulty in proving the damages are causally related to the breach. As we stated earlier, difficulty in proving causation should not operate as a bar to permitting plaintiffs to claim the damages. Furthermore, we note that pursuant ~~to our case law and~~ the Uniform Commercial Code, damages need not be proved with mathematical certainty. ~~As long as the~~ plaintiffs can provide a reasonable basis ~~from which the jury can calculate damages~~, they will be permitted to pursue ~~their~~ case.

scary
+cat
reasonable

Thu~~s, we now hold that plaintiffs~~ should be entitled to try to prove good will damages; provided they are able to introduce sufficient evidence (1) to establish that the such profits were causally related to a breach of warranty and (2) to provide the trier of fact with a reasonable basis from which to calculate damages.

Turning to the facts of this case, we note that the plaintiffs have made no claim for good will damages, since none was incurred; ARCO having cured the breach by stopping the supply of the nonconforming gasoline. The damages claimed are only for the period of time that the plaintiffs were forced to purchase the gasoline with oxinol. Thus, we reverse the decision of the lower courts in holding that the plaintiffs' claim was for good will damages.

Conclusion

We now hold that there are three types of lost profits recoverable as consequential damages available under §2-714 and §2-715 of the Uniform Commercial Code: (1) loss of primary profits; (2) loss of secondary profits; and (3) good will damages, defined as a loss of prospective profits or business reputation. While this categorization of damages represents a new direction for the court, we believe it is the better direction. . . .

It is so ordered. . . .

Problem 70

When their young daughter died in a tragic accident, the parents contracted with a funeral home to prepare her body for burial. When they

Damages Under Uniform Commercial Code §2-715 — The Pennsylvania Experience, 75 Dick. L. Rev. 63 (1970); Peters, Remedies for Breach of Contracts, 73 Yale L.J. 199, 276-77 (1963).

went to the funeral home to view the body, the mortician was apologetic. He had misplaced the body, and "I think she's in Ohio" was all that he could say. Both parents suffered extreme mental anguish because of this mishap. Can they recover consequential damages for their suffering? The actual case is Renihan v. Wright, 125 Ind. 536, 25 N.E. 823 (1890); Annot., 54 A.L.R. 4th 901; see Whaley, Paying for the Agony: The Recovery of Emotional Distress Damages in Contract Actions, 26 Suffolk U. L. Rev. 935 (1992).

Note the following excerpt from the Restatement (Second) of Contracts:

§353. Loss Due to Emotional Disturbance

Recovery for emotional disturbance will be excluded unless the breach also causes bodily harm or ~~the contract or the~~ breach is of such a kind that serious emotional ~~disturbance was a~~ particularly likely result.

Problem 71

On graduating from law school, Andrew Advocate received a gift of $25,000 from his wealthy parents and used it to buy a sports car that he had long desired. The car proved to be a lemon; four times it stalled and stranded Andrew in dangerous traffic situations. He took time off from his new job 18 times to take the car to and from the dealer's repair shop. Finally, when it stalled for the fifth time and made him miss a court appearance, he parked the car at the dealership and gave notice that he was revoking his acceptance (UCC §2-608) and wanted his money back (UCC §§2-711 and 2-715). When the dealer ignored him, he sued, asking for a return of his purchase money plus consequential damages of $5,000 for "mental anguish." Is this last element of damages recoverable? Compare Volkswagen of Am., Inc. v. Dillard, 579 So. 2d 1301, 14 U.C.C. Rep. Serv. 2d 475 (Ala. 1991) (yes), with Kwan v. Mercedes-Benz of N. Am., Inc., 28 Cal. Rptr. 371, 23 Cal. App. 4th 174 (1994) (no, distinguishing *Volkswagen* in part because of nonuniform language in Alabama's UCC).

In Bogner v. General Motors Corp., 117 Misc. 2d 929, 459 N.Y.S.2d 679 (N.Y. Civ. Ct. 1982), the plaintiff alleged damages for emotional harm for being stranded in a remote area of Nova Scotia for three days of her vacation while waiting for a part needed to repair her auto. The car was under warranty, but the manufacturer had excluded liability for: "loss of the use of the car during warranty repairs. This includes lodging bills, car rentals, other travel costs, or loss of pay." The court held that this disclaimer was not broad enough to disclaim damages for emotional distress. Further, the court held that although general principles of contract law normally dictate no damages for emotional injury because of a breach of contract, exceptions relating to public policy exist. The court then cited a couple of cases concerning defective caskets and the like. The court added: "This court feels that similar considerations apply when the rendering of automobile warranty service is unreasonably delayed, such that the customer has to languish in the boondocks for several days."

What if a Vermont resident were stranded in New York City? A member of Gamblers Anonymous in front of Caesar's Palace? Do not most individual plaintiffs suffer great inconvenience and mental turmoil because of breaches of contract?

3. Avoidability

ROCKINGHAM COUNTY v. LUTEN BRIDGE CO.

United States Circuit Court of Appeals, Fourth Circuit, 1929

35 F.2d 301

PARKER, Circuit Judge. This was an action at law instituted in the court below by the Luten Bridge Company, as plaintiff, to recover of Rockingham county, North Carolina, an amount alleged to be due under a contract for the construction of a bridge. The county admits the execution and breach of the contract, but contends that notice of cancellation was given the bridge company before the erection of the bridge was commenced, and that it is liable only for the damages which the company would have sustained, if it had abandoned construction at that time. The judge below refused to strike out an answer filed by certain members of the board of commissioners of the county, admitting liability in accordance with the prayer of the complaint, allowed this pleading to be introduced in evidence as the answer of the county, excluded evidence offered by the county in support of its contentions as to notice of cancellation and damages, and instructed a verdict for plaintiff for the full amount of its claim. From judgment on this verdict the county has appealed.

The facts out of which the case arises, as shown by the affidavits and offers of proof appearing in the record, are as follows: On January 7, 1924, the board of commissioners of Rockingham county voted to award to plaintiff a contract for the construction of the bridge in controversy. Three of the five commissioners favored the awarding of the contract and two opposed it. Much feeling was engendered over the matter, with the result that on February 11, 1924, W. K. Pruitt, one of the commissioners who had voted in the affirmative, sent his resignation to the clerk of the superior court of the county. The clerk received this resignation on the same day, and immediately accepted same and noted his acceptance thereon. Later in the day, Pruitt called him over the telephone and stated that he wished to withdraw the resignation, and later sent him written notice to the same effect. The clerk, however, paid no attention to the attempted withdrawal, and proceeded on the next day to appoint one W. W. Hampton as a member of the board to succeed him.

After his resignation, Pruitt attended no further meetings of the board, and did nothing further as a commissioner of the county. Likewise Pratt and McCollum, the other two members of the board who had voted with him in favor of the contract, attended no further meetings. Hampton, on the other hand, took the oath of office immediately upon his appointment and entered upon the discharge of the duties of a commissioner. He met regularly with the two remaining members of the board, Martin and Barber, in the courthouse at the county seat, and with them attended to all of the business of the county. Between the 12th of February and the first Monday in December following, these three attended, in all, 25 meetings of the board.

At one of these meetings, a regularly advertised called meeting held on February 21st, a resolution was unanimously adopted declaring that the contract for the building of the bridge was not legal and valid, and directing the clerk of the board to notify plaintiff that it refused to recognize same as a valid contract, and that plaintiff should proceed no further thereunder. This resolution also rescinded action of the board theretofore taken looking to the construction of a hard-surfaced road, in which the bridge was to be a mere connecting link. The clerk duly sent a certified copy of this resolution to plaintiff.

At the regular monthly meeting of the board on March 3d, a resolution was passed directing that plaintiff be notified that any work done on the bridge would be done by it at its own risk and hazard, that the board was of the opinion that the contract for the construction of the bridge was not valid and legal, and that, even if the board were mistaken as to this, it did not desire to construct the bridge, and would contest payment for same if constructed. A copy of this resolution was also sent to plaintiff. At the regular monthly meeting on April 7th, a resolution was passed, reciting that the board had been informed that one of its members was privately insisting that the bridge be constructed. It repudiated this action on the part of the member and gave notice that it would not be recognized. At the September meeting, a resolution was passed to the effect that the board would pay no bills presented by plaintiff or any one connected with the bridge. At the time of the passage of the first resolution, very little work toward the construction of the bridge had been done, it being estimated that the total cost of labor done and material on the ground was around $1,900; but, notwithstanding the repudiation of the contract by the county, the bridge company continued with the work of construction.

On November 24, 1924, plaintiff instituted this action against Rockingham county, and against Pruitt, Pratt, McCollum, Martin, and Barber, as constituting its board of commissioners. Complaint was filed, setting forth the execution of the contract and the doing of work by plaintiff thereunder, and alleging that for work done up until November 3, 1924, the county was indebted in the sum of $18,301.07. On November 27th, three days after the filing of the complaint, and only three days before the expiration of the term of office of the members of the old board of commissioners, Pruitt, Pratt, and McCollum met with an attorney at the county seat, and, without notice to or consultation with the other members of the board, so far as appears, had the attorney prepare for them an answer admitting the allegations of the complaint. This answer, which was filed in the cause on the following day, did not purport to be an answer of the county, or of its board of commissioners, but of the three commissioners named.

On December 1, 1924, the newly elected board of commissioners held its first meeting and employed attorneys to defend the action which had been instituted by plaintiff against the county. . . .

At the trial, plaintiff, over the objection of the county, was allowed to introduce in evidence the answer filed by Pruitt, Pratt, and McCollum, the contract was introduced, and proof was made of the value under the terms of the contract of the work done up to November 3, 1924. The county elicited on cross-examination proof as to the state of the work at the time of the passage of the resolutions to which we have referred. It then offered these resolutions in evidence, together with evidence as to the resignation of Pruitt, the acceptance of his resignation, and the appointment of Hampton; but all of this evidence was excluded, and the jury was instructed to return a verdict for plaintiff for the full amount of its claim. The county preserved exceptions to the rulings which were adverse to it, and contends that there was error on the part of the judge below in denying the motion to strike out the answer filed by Pruitt, Pratt, and McCollum; in allowing same to be introduced in evidence; in excluding the evidence offered of the resignation of Pruitt, the acceptance of his resignation, and the appointment of Hampton, and of the resolutions attempting to cancel the contract and the notices sent plaintiff pursuant thereto; and in directing a verdict for plaintiff in accordance with its claim.

As the county now admits the execution and validity of the contract, and the breach on its part, the ultimate question in the case is one as to the measure of plaintiff's recovery, and the exceptions must be considered with this in mind. Upon these exceptions, three principal questions arise for our consideration, viz.: (1) Whether the answer filed by Pruitt, Pratt, and McCollum was the answer of the county. If it was, the lower court properly refused to strike it out, and properly admitted it in evidence. (2) Whether, in the light of the evidence offered and excluded, the resolutions to which we have referred, and the notices sent pursuant thereto, are to be deemed action on the part of the county. If they are not, the county has nothing upon which to base its position as to minimizing damages, and the evidence offered was properly excluded. And (3) whether plaintiff, if the notices are to be deemed action by the county, can recover under the contract for work done after they were received, or is limited to the recovery of damages for breach of contract as of that date.

[The court decided the first issue in the negative and the second affirmatively.]

Coming, then, to the third question — i.e., as to the measure of plaintiff's recovery — we do not think that, after the county had given notice, while the contract was still executory, that it did not desire the bridge built and would not pay for it, plaintiff could proceed to build it and recover the contract price. It is true that the county had no right to rescind the contract, and the notice given plaintiff amounted to a breach on its part; but, after plaintiff had received notice of the breach, it was its duty to do nothing to increase the damages flowing therefrom. If A enters into a binding contract to build a house for B, B, of course, has no right to rescind the contract without A's consent. But if, before the house is built, he decides that he does not want it, and notifies A to that effect, A has no right to proceed with the building and thus pile up damages. His remedy is to treat the contract as broken when he receives the notice, and sue for the recovery of such damages as he may have sustained from the breach, including any profit which he would have realized upon performance, as well as any other losses which may have resulted to him. In the case at bar, the county decided not to build the road of which the bridge was to be a part, and did not build it. The bridge, built in the midst of the forest, is of no value to the county because of this change of circumstances. When, therefore, the county gave notice to the plaintiff that it would not proceed with the project, plaintiff should have desisted from further work. It had no right thus to pile up damages by proceeding with the erection of a useless bridge.

The contrary view was expressed by Lord Cockburn in Frost v. Knight, L.R. 7 Ex. 111, but, as pointed out by Prof. Williston (Williston on Contracts, vol. 3, p. 2347), it is not in harmony with the decisions in this country. The American rule and the reasons supporting it are well stated by Prof. Williston as follows:

> There is a line of cases running back to 1845 which holds that, after an absolute repudiation or refusal to perform by one party to a contract, the other party cannot continue to perform and recover damages based on full performance. This rule is only a particular application of the general rule of damages that a plaintiff cannot hold a defendant liable for damages which need not have been incurred; or, as it is often stated, the plaintiff must, so far as he can without loss to himself, mitigate the damages caused by the defendant's wrongful act. The application of this rule to the matter in question is obvious. If a man engages to have work done, and afterwards repudiates his contract before the work has been begun or when it has been only partially done, it is inflicting damage on the defendant without benefit to the plaintiff to allow the latter to insist on proceeding with the contract. The work may be useless to the defendant, and yet he would be forced to pay the full contract price. On the other hand, the plaintiff is interested only in the profit he will make out of the contract. If he receives this it is equally advantageous for him to use his time otherwise.

The leading case on the subject in this country is the New York case of Clark v. Marsiglia, 1 Denio (N.Y.) 317, 43 Am. Dec. 670. In that case defendant had employed plaintiff to paint certain pictures for him, but countermanded the order before the work was finished. Plaintiff, however, went on and completed the work and sued for the contract price. In reversing a judgment for plaintiff, the court said:

> The plaintiff was allowed to recover as though there had been no countermand of the order; and in this the court erred. The defendant, by requiring the plaintiff to stop work upon the paintings, violated his contract, and thereby incurred a liability to pay such damages as the plaintiff should sustain. Such damages would include a recompense for the labor done and materials used, and such further sum in damages as might, upon legal principles, be assessed for the breach of the contract; but the plaintiff had no right, by obstinately persisting in the work, to make the penalty upon the defendant greater than it would otherwise have been.

And the rule as established by the great weight of authority in America is summed up in the following statement in 6 R.C.L. 1029, which is quoted with approval by the Supreme Court of North Carolina in the recent case of Novelty Advertising Co. v. Farmers' Mut. Tobacco Warehouse Co., 186 N.C. 197, 119 S.E. 196, 198:

> While a contract is executory a party has the power to stop performance on the other side by an explicit direction to that effect, subjecting himself to such damages as will compensate the other party for being stopped in the performance on his part at that stage in the execution of the contract. The party thus forbidden cannot afterwards go on, and thereby increase the damages, and then recover such damages from the other party. The legal right of either party to violate, abandon, or renounce his contract, on the usual terms of compensation to the other for the damages which the law recognizes and allows, subject to the jurisdiction of equity to decree specific performance in proper cases, is universally recognized and acted upon.

This is in accord with the earlier North Carolina decision of Heiser v. Mears, 120 N.C. 443, 27 S.E. 117, in which it was held that, where a buyer countermands his order for goods to be manufactured for him under an executory contract, before the work is completed, it is notice to the seller that he elects to rescind his contract and submit to the legal measure of damages, and that in such case the seller cannot complete the goods and recover the contract price.

We have carefully considered the cases upon which plaintiff relies; but we do not think that they are at all in point. . . . It follows that there was error in directing a verdict for plaintiff for the full amount of its claim. The measure of plaintiff's damage, upon its appearing that notice was duly given not to build the bridge, is an amount sufficient to compensate plaintiff for labor and materials expended and expense incurred in the part performance of the contract, prior to its repudiation, plus the profit which would have been realized if it had been carried out in accordance with its terms.

Our conclusion, on the whole case, is that there was error in failing to strike out the answer of Pruitt, Pratt, and McCollum, and in admitting same as evidence against the county, in excluding the testimony offered by the county to which we have referred, and in directing a verdict for plaintiff. The judgment below will accordingly be reversed, and the case remanded for a new trial.

Reversed.

Problem 72

The Garland Coal Company signed a contract with Willie and Lucille Peevyhouse by which they agreed to let the company strip mine their farm at an agreed price. Garland also agreed to restore the land to its former appearance at the conclusion of the mining. When it failed to do so, offering instead to pay the Peevyhouses $300 (this being the market value lost by the failure to replace the strip mines), the Peevyhouses immediately hired another company to cover up the strip mines. This work cost $29,000. The Peevyhouses then brought suit against the Garland Coal Company for that amount. Should they recover it?

Problem 73

For the Cleveland World's Fair, Balloons of America had contracted with the government of Cuba to build a giant balloon in the shape of a cigar. It was halfway finished when Cuba decided to abandon the project. Balloons of America phones you, its attorney, and wants to know whether it should complete the cigar-shaped balloon (contract price: $13,000) or stop now (when it has expended only $8,000) and sell the partially completed balloon for its scrap value ($120). The cost of completion is $2,500 and the salvage value after completion is $1,000. Read UCC §§2-704 and 2-709 and advise your client.

PARKER v. TWENTIETH CENTURY-FOX FILM CORP.
Supreme Court of California, 1970
3 Cal. 3d 176, 89 Cal. Rptr. 737, 474 P.2d 689

BURKE, J. Defendant Twentieth Century-Fox Film Corporation appeals from a summary judgment granting to plaintiff the recovery of agreed compensation under a written contract for her services as an actress in a motion picture. As will appear, we have concluded that the trial court correctly ruled in plaintiff's favor and that the judgment should be affirmed.

Plaintiff is well known as an actress, and in the contract between plaintiff and defendant is sometimes referred to as the "Artist." Under the contract, dated August 6, 1965, plaintiff was to play the female lead in defendant's contemplated production of a motion picture entitled "Bloomer Girl." The contract provided that defendant would pay plaintiff a minimum "guaranteed compensation" of $53,571.42 per week for 14 weeks commencing May 23, 1966, for a total of $750,000. Prior to May 1966 defendant decided not to produce the picture and by a letter dated April 4, 1966, it notified plaintiff of that decision and that it would not "comply with our obligations to you under" the written contract.

By the same letter and with the professed purpose "to avoid any damage to you," defendant instead offered to employ plaintiff as the leading actress in another film tentatively entitled "Big Country, Big Man" (hereinafter, "Big Country"). The compensation offered was identical, as were 31 of the 34 numbered provisions or articles of the original contract.[1]

1. Among the identical provisions was the following found in the last paragraph of Article 2 of the original contract: "We [defendant] shall not be obligated to utilize your [plaintiff's] services in or in connection with the Photoplay hereunder, our sole obligation, subject to the terms and conditions of this Agreement, being to pay you the guaranteed compensation herein provided for."

Unlike "Bloomer Girl," however, which was to have been a musical production, "Big Country" was a dramatic "western type" movie. "Bloomer Girl" was to have been filmed in California; "Big Country" was to be produced in Australia. Also, certain terms in the proffered contract varied from those of the original.[2] Plaintiff was given one week within which to accept; she did not and the offer lapsed. Plaintiff then commenced this action seeking recovery of the agreed guaranteed compensation.

The complaint sets forth two causes of action. The first is for money due under the contract; the second, based upon the same allegations as the first, is for damages resulting from defendant's breach of contract. Defendant in its answer admits the existence and validity of the contract, that plaintiff complied with all the conditions, covenants and promises and stood ready to complete the performance, and that defendant breached and "anticipatorily repudiated" the contract. It denies, however, that any money is due to plaintiff either under the contract or as a result of its breach, and pleads as an affirmative defense to both causes of action plaintiff's allegedly deliberate failure to mitigate damages, asserting that she unreasonably refused to accept its offer of the leading role in "Big Country."

Plaintiff moved for summary judgment under Code of Civil Procedure section 437c, the motion was granted, and summary judgment for $750,000 plus interest was entered in plaintiff's favor. This appeal by defendant followed.

The familiar rules are that the matter to be determined by the trial court on a motion for summary judgment is whether facts have been presented which give rise to a triable factual issue. The court may not pass

2. Article 29 of the original contract specified that plaintiff approved the director already chosen for "Bloomer Girl" and that in case he failed to act as director plaintiff was to have approval rights of any substitute director. Article 31 provided that plaintiff was to have the right of approval of the "Bloomer Girl" dance director, and Article 32 gave her the right of approval of the screenplay.

Defendant's letter of April 4 to plaintiff, which contained both defendant's notice of breach of the "Bloomer Girl" contract and offer of the lead in "Big Country," eliminated or impaired each of those rights. It read in part as follows:

> The terms and conditions of our offer of employment are identical to those set forth in the "Bloomer Girl" Agreement, Articles 1 through 34 and Exhibit A to the Agreement, except as follows:
>
> 1. Article 31 of said Agreement will not be included in any contract of employment regarding "Big Country, Big Man" as it is not a musical and it thus will not need a dance director.
>
> 2. In the "Bloomer Girl" agreement, in Articles 29 and 32, you were given certain director and screenplay approvals and you had preapproved certain matters. Since there simply is insufficient time to negotiate with you regarding your choice of director and regarding the screenplay and since you already expressed an interest in performing the role in "Big Country, Big Man," we must exclude from our offer of employment in "Big Country, Big Man" any approval rights as are contained in said Articles 29 and 32; however, we shall consult with you respecting the director to be selected to direct the photoplay and will further consult with you with respect to the screenplay and any revisions or changes therein, provided, however, that if we fail to agree . . . the decision of [defendant] with respect to the selection of a director and to revisions and changes in the said screenplay shall be binding upon the parties to said agreement.

upon the issue itself. Summary judgment is proper only if the affidavits *or* declarations in support of the moving party would be sufficient to sustain a judgment in his favor and his opponent does not by affidavit show facts sufficient to present a triable issue of fact. The affidavits of the moving party are strictly construed, and doubts as to the propriety of summary judgment should be resolved against granting the motion. Such summary procedure is drastic and should be used with caution so that it does not become a substitute for the open trial method of determining facts. . . .

As stated, defendant's sole defense to this action which resulted from its deliberate breach of contract is that in rejecting defendant's substitute offer of employment plaintiff unreasonably refused to mitigate damages.

The general rule is that the measure of recovery by a wrongfully discharged employee is the amount of salary agreed upon for the period of service, less the amount which the employer affirmatively proves the employee has earned or with reasonable effort might have earned from other employment. However, before projected earnings from other employment opportunities not sought or accepted by the discharged employee can be applied in mitigation, the employer must show that the other employment was comparable, or substantially similar, to that of which the employee has been deprived; the employee's rejection of or failure to seek other available employment of a different or inferior kind may not be resorted to in order to mitigate damages.

In the present case defendant has raised no issue of *reasonableness of efforts* by plaintiff to obtain other employment; the sole issue is whether plaintiff's refusal of defendant's substitute offer of "Big Country" may be used in mitigation. Nor, if the "Big Country" offer was of employment different or inferior when compared with the original "Bloomer Girl" employment, is there an issue as to whether or not plaintiff acted reasonably in refusing the substitute offer. Despite defendant's arguments to the contrary, no case cited or which our research has discovered holds or suggests that reasonableness is an element of a wrongfully discharged employee's option to reject, or fail to seek, different or inferior employment lest the possible earnings therefrom be charged against him in mitigation of damages.

Applying the foregoing rules to the record in the present case, with all intendments in favor of the party opposing the summary judgment motion — here, defendant — it is clear that the trial court correctly ruled that plaintiff's failure to accept defendant's tendered substitute employment could not be applied in mitigation of damages because the offer of the "Big Country" lead was of employment both different and inferior, and that no factual dispute was presented on that issue. The mere circumstance that "Bloomer Girl" was to be a musical review calling upon plaintiff's talents as a dancer as well as an actress, and was to be produced in the City of Los Angeles, whereas "Big Country" was a straight dramatic role in a "Western Type" story taking place in an opal mine in Australia, demonstrates the difference in kind between the two employments; the female lead as a dramatic actress in a western style motion picture can by no stretch of imagination be considered the equivalent of or substantially similar to the lead in a song-and-dance production.

Additionally, the substitute "Big Country" offer proposed to eliminate or impair the director and screenplay approvals accorded to plaintiff under the original "Bloomer Girl" contract (see fn. 2, ante), and thus constituted an offer of inferior employment. No expertise or judicial notice is required in order to hold that the deprivation or infringement of an employee's rights held under an original employment contract converts the available "other employment" relied upon by the employer to mitigate damages, into inferior employment which the employee need not seek or accept. . . .

In view of the determination that defendant failed to present any facts showing the existence of a factual issue with respect to its sole defense — plaintiff's rejection of its substitute employment offer in mitigation of damages — we need not consider plaintiff's contention that for various reasons, including the provisions of the original contract set forth in footnote 1, ante, plaintiff was excused from attempting to mitigate damages.

The judgment is affirmed.

McComb, Peters, and Tobriner, JJ., and Kaus, J. pro tem., and Roth, J. pro tem., Roth, J. pro tem., concur.

Sullivan, Acting Chief Justice (dissenting). The basic question in this case is whether or not plaintiff acted reasonably in rejecting defendant's offer of alternate employment. The answer depends upon whether that offer (starring in "Big Country, Big Man") was an offer of work that was substantially similar to her former employment (starring in "Bloomer Girl") or of work that was of a different or inferior kind. To my mind this is a factual issue which the trial court should not have determined on a motion for summary judgment. The majority have not only repeated this error but have compounded it by applying the rules governing mitigation of damages in the employer-employee context in a misleading fashion. Accordingly, I respectfully dissent.

The familiar rule requiring a plaintiff in a tort or contract action to mitigate damages embodies notions of fairness and socially responsible behavior which are fundamental to our jurisprudence. Most broadly stated, it precludes the recovery of damages which, through the exercise of due diligence, could have been avoided. Thus, in essence, it is a rule requiring reasonable conduct in commercial affairs. This general principle governs the obligations of an employee after his employer has wrongfully repudiated or terminated the employment contract. Rather than permitting the employee simply to remain idle during the balance of the contract period, the law requires him to make a reasonable effort to secure other employment.[1] He is not obliged, however, to seek or accept any and

1. The issue is generally discussed in terms of a duty on the part of the employee to minimize loss. The practice is long-established and there is little reason to change despite Judge Cardozo's observation of its subtle inaccuracy. "The servant is free to accept employment or reject it according to his uncensored pleasure. What is meant by the supposed duty is merely this: That if he unreasonably reject, he will not be heard to say that the loss of wages from then on shall be deemed the jural consequence of the earlier discharge. He has broken the chain of causation, and loss resulting to him thereafter is suffered through his own act." (McClelland v. Climax Hosiery Mills (1930) 252 N.Y. 347, 359, 169 N.E. 605, 609, concurring opinion.)

all types of work which may be available. Only work which is in the same field and which is of the same quality need be accepted.[2]

Over the years the courts have employed various phrases to define the type of employment which the employee, upon his wrongful discharge, is under an obligation to accept. Thus in California alone it has been held that he must accept employment which is "substantially similar.". . .

For reasons which are unexplained, the majority cite several of these cases yet select from among the various judicial formulations which contain one particular phrase, "Not of a different or inferior kind," with which to analyze this case. I have discovered no historical or theoretical reason to adopt this phrase, which is simply a negative restatement of the affirmative standards set out in the above cases, as the exclusive standard. Indeed, its emergence is an example of the dubious phenomenon of the law responding not to rational judicial choice or changing social conditions, but to unrecognized changes in the language of opinions or legal treatises. However, the phrase is a serviceable one and my concern is not with its use as the standard but rather with what I consider its distortion.

. . . It has never been the law that the mere existence of *differences between two jobs in the same field* is sufficient, as a matter of law, to excuse an employee wrongfully discharged from one from accepting the other in order to mitigate damages. Such an approach would effectively eliminate any obligation of an employee to attempt to minimize damage arising from a wrongful discharge. The only alternative job offer an employee would be required to accept would be an offer of his former job by his former employer.

Although the majority appear to hold that there was a difference "in kind" between the employment offered plaintiff in "Bloomer Girl" and that offered in "Big Country," an examination of the opinion makes crystal clear that the majority merely point out differences between the two *films* (an obvious circumstance) and then apodically assert that these constitute a difference in the *kind* of *employment.* The entire rationale of the majority boils down to this: that the *"mere circumstances"* that "Bloomer Girl" was to be a musical review while "Big Country" was a straight drama "demonstrates the difference in kind" since a female lead in a western is not "the equivalent of or substantially similar to" a lead in a musical. This is merely attempting to prove the proposition by repeating it. It shows that the vehicles for the display of the star's talents are different but it does not prove that her employment as a star in such vehicles is of necessity different *in kind* and either inferior or superior.

I believe that the approach taken by the majority (a superficial listing of differences with no attempt to assess their significance) may subvert a valu-

2. This qualification of the rule seems to reflect the simple and humane attitude that it is too severe to demand of a person that he attempt to find and perform work for which he has no training or experience. Many of the older cases hold that one need not accept work in an inferior rank or position nor work which is more menial or arduous. This suggests that the rule may have had its origin in the bourgeois fear of resubmergence in lower economic classes.

able legal doctrine.[5] The inquiry in cases such as this should not be whether differences between the two jobs exist (there will always be differences) but whether the differences which are present are substantial enough to constitute differences in the *kind* of employment or, alternatively, whether they render the substitute work employment of an *inferior kind*.

It seems to me that *this* inquiry involves, in the instant case at least, factual determinations which are improper on a motion for summary judgment. Resolving whether or not one job is substantially similar to another or whether, on the other hand, it is of a different or inferior kind, will often (as here) require a critical appraisal of the similarities and differences between them in light of the importance of these differences to the employee. This necessitates a weighing of the evidence, and it is precisely this undertaking which is forbidden on summary judgment.

This is not to say that summary judgment would never be available in an action by an employee in which the employer raises the defense of failure to mitigate damages. No case has come to my attention, however, in which summary judgment has been granted on the issue of whether an employee was obliged to accept available alternate employment. Nevertheless, there may well be cases in which the substitute employment is so manifestly of a dissimilar or inferior sort, the declarations of the plaintiff so complete and those of the defendant so conclusionary and inadequate that no factual issues exist for which a trial is required. This, however, is not such a case.

It is not intuitively obvious, to me at least, that the leading female role in a dramatic motion picture is a radically different endeavor from the leading female role in a musical comedy film. Nor is it plain to me that the rather qualified rights of director and screenplay approval contained in the first contract are highly significant matters either in the entertainment industry in general or to this plaintiff in particular. Certainly, none of the declarations introduced by plaintiff in support of her motion shed any light on these issues. Nor do they attempt to explain why she declined the offer of starring in "Big Country, Big Man." Nevertheless, the trial court granted the motion, declaring that these approval rights were "critical" and that their elimination altered "the essential nature of the employment."

The plaintiff's declarations were of no assistance to the trial court in its effort to justify reaching this conclusion on summary judgment. Instead, it was forced to rely on judicial notice of the definitions of "motion picture," "screenplay" and "director" (Evid. Code, §451, subd. (e)) and then on judicial notice of practices in the film industry which were purportedly of "common knowledge." (Evid. Code, §451, subd. (f) or §452, subd. (g).) This use of judicial notice was error. Evidence Code section 451, subdivision (e) was never intended to authorize resort to the dictionary to solve essentially factual questions which do not turn upon

5. The values of the doctrine of mitigation of damages in this context are that it minimizes the unnecessary personal and social (e.g., nonproductive use of labor, litigation) costs of contractual failure. If a wrongfully discharged employee can, through his own action and without suffering financial or psychological loss in the process, reduce the damages accruing from the breach of contract, the most sensible policy is to require him to do so. I fear the majority opinion will encourage precisely opposite conduct.

conventional linguistic usage. More important, however, the trial court's notice of "facts commonly known" violated Evidence Code section 455, subdivision (a). Before this section was enacted there were no procedural safeguards affording litigants an opportunity to be heard as to the propriety of taking judicial notice of a matter or as to the tenor of the matter to be noticed. Section 455 makes such an opportunity (which may be an element of due process, see Evid. Code, §455, Law Revision Com. Comment (a)) mandatory and its provisions should be scrupulously adhered to. "Judicial notice can be a valuable tool in the adversary system for the lawyer as well as the court" (Kongsgaard, Judicial Notice (1966), 18 Hastings L.J. 117, 140) and its use is appropriate on motions for summary judgment. Its use in this case, however, to determine on summary judgment issues fundamental to the litigation without complying with statutory requirements of notice and hearing is a highly improper effort to "cut the Gordion knot of involved litigation.". . .

The majority do not confront the trial court's misuse of judicial notice. They avoid this issue through the expedient of declaring that neither judicial notice nor expert opinion (such as that contained in the declarations in opposition to the motion) is necessary to reach the trial court's conclusion. *Something*, however, clearly *is* needed to support this conclusion. Nevertheless, the majority make no effort to justify the judgment through an examination of the plaintiff's declarations. Ignoring the obvious insufficiency of these declarations, the majority announce that "the deprivation or infringement of an employee's rights held under an original employment contract" changes the alternate employment offered or available into employment of an inferior kind.

I cannot accept the proposition that an offer which eliminates *any* contract right, regardless of its significance, is, as a matter of law, an offer of employment of an inferior kind. Such an absolute rule seems no more sensible than the majority's earlier suggestion that the mere existence of differences between two jobs is sufficient to render them employment of different kinds. Application of such per se rules will severely undermine the principle of mitigation of damages in the employer-employee context.

I remain convinced that the relevant question in such cases is whether or not a particular contract provision is so significant that its omission creates employment of an inferior kind. This question is, of course, intimately bound up in what I consider the ultimate issue: whether or not the employee acted reasonably. This will generally involve a factual inquiry to ascertain the importance of the particular contract term and a process of weighing the absence of that term against the countervailing advantages of the alternate employment. In the typical case, this will mean that summary judgment must be withheld.

In the instant case, there was nothing properly before the trial court by which the importance of the approval rights could be ascertained, much less evaluated. Thus, in order to grant the motion for summary judgment, the trial court misused judicial notice. In upholding the summary judgment, the majority here rely upon per se rules which distort the process of determining whether or not an employee is obliged to accept particular employment in mitigation of damages.

I believe that the judgment should be reversed so that the issue of whether or not the offer of the lead role in "Big Country, Big Man" was of employment comparable to that of the lead role in "Bloomer Girl" may be determined at trial.

NOTES AND QUESTIONS

1. In his dissent Judge Sullivan objects to the majority's use of *judicial notice*. Judicial notice means the ability of the court to apply its own knowledge (without the need of evidence being introduced) of things within the common knowledge of all humankind. For example, the court can take judicial notice that the litigants are on the planet Earth, or that people breathe oxygen. What is Judge Sullivan's complaint with the majority's application of judicial notice in this case? Is he right? Would the Supreme Court of North Dakota have had as easy a time with the issue as the Supreme Court of California did?

2. The "well-known actress" in this case is Shirley MacLaine (whose married name is "Parker"). The musical *Bloomer Girl* (with music by Harold Arlen and lyrics by E. Y. Harburg, the same duo that wrote the songs for *The Wizard of Oz*) was a Broadway hit in 1944, running 654 performances. It tells the story of the American feminist reformer Amelia Jenks ("Dolly") Bloomer (1818-1894). Ms. Bloomer was the founder and editor of a monthly journal, the *Lilly*, the first American magazine published by and for women. Among the many issues raised by the magazine were temperance, unjust marriage laws, inadequate education for women, and woman's suffrage. Ms. Bloomer became most famous for her advocacy of a reform in woman's clothing, appearing in public in a short dress with trousers gathered at the ankle (called "bloomers"), intended to reduce the weight and discomfort of the usual female dresses of the period.

3. Would the court have reached the same result if instead of a western, the studio had offered Ms. MacLaine the part of Scarlett O'Hara in a remake of *Gone With the Wind?* What if the substituted picture were *My Fair Lady* and Ms. MacLaine was given the chance to play Eliza Doolittle?

4. Contractual provisions in which a party agrees that the other has no duty to mitigate may be unenforceable as a matter of public policy. Durman Realty Co. Ltd. Partnership, 865 F. Supp. 1093 (S.D.N.Y. 1994) (interpreting New Jersey law).

5. If the plaintiff elects to take a new job that is inferior to the one promised in the original contract are the earnings from it a mitigation of her damages?

Problem 74

Hearing a report that Alice Chalk, a popular high school teacher, was a drug dealer on the side, the school's principal marched down to her classroom and fired Alice on the spot. Her horrified students' jaws dropped open when the principal accused her of selling drugs and ordered her from the building. Later that day, the principal learned that the report was false, and he phoned Alice at home, apologized, and offered her her job back. She declined and took a job as an evening waitress in an all-night diner. She also sued the school for wrongful termination. Is it a defense that she refused to return to her job? Is the salary she receives as a waitress a mitigating factor? See John Call Engineering v. Manti City Corp., 795 P.2d 678 (Utah Ct. App. 1990). What if she had accepted unemployment compensation? See Corfl v. Huron Castings, Inc., 450 Mich. 620, 544 N.W.2d 278 (1996).

4. Damages by Agreement

RESTATEMENT (SECOND) OF CONTRACTS

§356(1). Liquidated Damages and Penalties

Damages for breach by either party may be liquidated in the agreement but only at an amount that is reasonable in the light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss. A term fixing unreasonably large liquidated damages is unenforceable on grounds of public policy as a penalty.

LAKE RIVER CORP. v. CARBORUNDUM CO.
United States Court of Appeals, Seventh Circuit, 1985
769 F.2d 1284

Posner, Circuit Judge. This diversity suit between Lake River Corporation and Carborundum Company requires us to consider questions of Illinois commercial law, and in particular to explore the fuzzy line between penalty clauses and liquidated-damages clauses.

Carborundum manufactures "Ferro Carbo," an abrasive powder used in making steel. To serve its midwestern customers better, Carborundum made a contract with Lake River by which the latter agreed to provide distribution services in its warehouse in Illinois. Lake River would receive Ferro Carbo in bulk from Carborundum, "bag" it, and ship the bagged product to Carborundum's customers. The Ferro Carbo would remain Carborundum's property until delivered to the customers.

Carborundum insisted that Lake River install a new bagging system to handle the contract. In order to be sure of being able to recover the cost of the new system ($89,000) and make a profit of 20 percent of the contract price, Lake River insisted on the following minimum-quantity guarantee:

> In consideration of the special equipment [i.e., the new bagging system] to be acquired and furnished by Lake-River for handling the product,

> Carborundum shall, during the initial three-year term of this Agreement, ship to Lake-River for bagging a minimum quantity of [22,500 tons]. If, at the end of the three-year term, this minimum quantity shall not have been shipped, Lake-River shall invoice Carborundum at the then prevailing rates for the difference between the quantity bagged and the minimum guaranteed.

If Carborundum had shipped the full minimum quantity that it guaranteed, it would have owed Lake River roughly $533,000 under the contract.

After the contract was signed in 1979, the demand for domestic steel, and with it the demand for Ferro Carbo, plummeted, and Carborundum failed to ship the guaranteed amount. When the contract expired late in 1982, Carborundum had shipped only 12,000 of the 22,500 tons it had guaranteed. Lake River had bagged the 12,000 tons and had billed Carborundum for this bagging, and Carborundum had paid, but by virtue of the formula in the minimum-guarantee clause Carborundum still owed Lake River $241,000 — the contract price of $533,000 if the full amount of Ferro Carbo had been shipped, minus what Carborundum had paid for the bagging of the quantity it had shipped.

When Lake River demanded payment of this amount, Carborundum refused, on the ground that the formula imposed a penalty. At the time, Lake River had in its warehouse 500 tons of bagged Ferro Carbo, having a market value of $269,000, which it refused to release unless Carborundum paid the $241,000 due under the formula. Lake River did offer to sell the bagged product and place the proceeds in escrow until its dispute with Carborundum over the enforceability of the formula was resolved, but Carborundum rejected the offer and trucked in bagged Ferro Carbo from the East to serve its customers in Illinois, at an additional cost of $31,000.

Lake River brought this suit for $241,000, which it claims as liquidated damages. Carborundum counterclaimed for the value of the bagged Ferro Carbo when Lake River impounded it and the additional cost of serving the customers affected by the impounding. The theory of the counterclaim is that the impounding was a conversion, and not as Lake River contends the assertion of a lien. The district judge, after a bench trial, gave judgment for both parties. Carborundum ended up roughly $42,000 to the good: $269,000 + $31,000 − $241,000 − $17,000, the last figure representing prejudgment interest on Lake River's damages. (We have rounded off all dollar figures to the nearest thousand.) Both parties have appealed.

[The court first decided that Lake River did not have a valid lien on the bagged powder.]

The hardest issue in the case is whether the formula in the minimum-guarantee clause imposes a penalty for breach of contract or is merely an effort to liquidate damages. Deep as the hostility to penalty clauses runs in the common law, see Loyd, Penalties and Forfeitures, 29 Harv. L. Rev. 117 (1915), we still might be inclined to question, if we thought ourselves free to do so, whether a modern court should refuse to enforce a penalty clause where the signator is a substantial corporation, well able to avoid improvident commitments. Penalty clauses provide an earnest of performance. The clause here enhanced Carborundum's credibility in promising to ship the minimum amount guaranteed by showing that it was willing to pay the full contract price even if it failed to ship anything. On the other side it can be pointed out that by raising the cost of a breach of contract to the contract breaker, a penalty clause increases the risk to his other creditors; increases (what is the same thing and more, because bankruptcy imposes "deadweight" social costs) the risk of bankruptcy; and could amplify the business cycle by increasing the number of bankruptcies in bad times, which is when contracts are most likely to be broken. But since little effort is made to prevent businessmen from assuming risks, these reasons are no better than makeweights.

A better argument is that a penalty clause may discourage efficient as well as inefficient breaches of contract. Suppose a breach would cost the promisee $12,000 in actual damages but would yield the promisor $20,000 in additional profits. Then there would be a net social gain from breach. After being fully compensated for his loss the promisee would be no worse off than if the contract had been performed, while the promisor would be better off by $8,000. But now suppose the contract contains a penalty clause under which the promisor if he breaks his promise must pay the promisee $25,000. The promisor will be discouraged from breaking the contract, since $25,000, the penalty, is greater than $20,000, the profits of the breach; and a transaction that would have increased value will be forgone.

On this view, since compensatory damages should be sufficient to deter inefficient breaches (that is, breaches that cost the victim more than the gain to the contract breaker), penal damages could have no effect other than to deter some efficient breaches. But this overlooks the earlier point that the willingness to agree to a penalty clause is a way of making the promisor and his promise credible and may therefore be essential to inducing some value-maximizing contracts to be made. It also overlooks the more important point that the parties (always assuming they are fully competent) will, in deciding whether to include a penalty clause in their contract, weigh the gains against the costs — costs that include the possibility of discouraging an efficient breach somewhere down the road — and will include the clause only if the benefits exceed those costs as well as all other costs.

On this view the refusal to enforce penalty clauses is (at best) paternalistic — and it seems odd that courts should display parental solicitude for large corporations. But however this may be, we must be on guard to avoid importing our own ideas of sound public policy into an area where our proper judicial role is more than usually deferential. The responsibility for making innovations in the common law of Illinois rests with the courts of Illinois, and not with the federal courts in Illinois. And like every other state, Illinois, untroubled by academic skepticism of the wisdom of refusing to enforce penalty clauses against sophisticated promisors, see, e.g., Goetz & Scott, Liquidated Damages, Penalties and the Just Compensation Principle, 77 Colum. L. Rev. 554 (1977), continues steadfastly to insist on the distinction between penalties and liquidated damages. To be valid under Illinois law a liquidation of damages must be a reasonable estimate at the time of contracting of the likely damages from breach, and the need for estimation at that time must be shown by reference to the likely difficulty of measuring the actual damages from a breach of contract after the breach occurs. If damages would be easy to determine then, or if the estimate greatly exceeds a reasonable upper estimate of what the damages are likely to be, it is a penalty. See, e.g., M.I.G. Investments, Inc. v. Marsala, 92 Ill. App. 3d 400, 405-406, 47 Ill. Dec. 265, 270, 414 N.E.2d 1381, 1386 (1981). Rule

The distinction between a penalty and liquidated damages is not an easy one to draw in practice but we are required to draw it and can give only limited weight to the district court's determination. Whether a provision for damages is a penalty clause or a liquidated-damages clause is a question of law rather than fact, Weiss v. United States Fidelity & Guaranty Co., 300 Ill. 11, 16, 132 N.E. 749, 751 (1921); M.I.G. Investments, Inc. v. Marsala, supra, 92 Ill. App. 3d 400, 406, 47 Ill. Dec. 265, 270, 414 N.E.2d 1381, 1386, and unlike some courts of appeals we do not treat a determination by a federal district judge of an issue of state law as if it were a finding of fact, and reverse only if persuaded that clear error has occurred, though we give his determination respectful consideration.

Mindful that Illinois courts resolve doubtful cases in favor of classification as a penalty, we conclude that the damage formula in this case is a penalty and not a liquidation of damages, because it is designed always to assure Lake River more than its actual damages. Holding The formula — full contract price minus the amount already invoiced to Carborundum — is invariant to the gravity of the breach. When a contract specifies a single sum in damages for any and all breaches even though it is apparent that all are not of the same gravity, the specification is not a reasonable effort to estimate damages; and when in addition the fixed sum greatly exceeds the actual damages likely to be inflicted by a minor breach, its character as a penalty becomes unmistakable. This case is within the gravitational field of these principles even though the minimum-guarantee clause does not fix a single sum as damages.

Suppose to begin with that the breach occurs the day after Lake River buys its new bagging system for $89,000 and before Carborundum ships any Ferro Carbo. Carborundum would owe Lake River $533,000. Since Lake River would have incurred at that point a total cost of only $89,000, its net gain from the breach would be $444,000. This is more than four times the profit of $107,000 (20 percent of the contract price of $533,000) that Lake River expected to make from the contract if it had been performed: a huge windfall.

Next suppose (as actually happened here) that breach occurs when 55 percent of the Ferro Carbo has been shipped. Lake River would already have received $293,000 from Carborundum. To see what its costs then would have been (as estimated at the time of contracting), first subtract Lake River's anticipated profit on the contract of $107,000 from the total contract price of $533,000. The difference — Lake River's total cost of performance — is $426,000. Of this, $89,000 is the cost of the new bagging system, a fixed cost. The rest ($426,000 − $89,000 = $337,000) presumably consists of variable costs that are roughly proportional to the amount of Ferro Carbo bagged; there is no indication of any other fixed costs.

Assume, therefore, that if Lake River bagged 55 percent of the contractually agreed quantity, it incurred in doing so 55 percent of its variable costs, or $185,000. When this is added to the cost of the new bagging system, assumed for the moment to be worthless except in connection with the contract, the total cost of performance to Lake River is $274,000. Hence a breach that occurred after 55 percent of contractual performance was complete would be expected to yield Lake River a modest profit of $19,000 ($293,000 − $274,000). But now add the "liquidated damages" of $241,000 that Lake River claims, and the result is a total gain from the breach of $260,000, which is almost two and a half times the profit that Lake River expected to gain if there was no breach. And this ignores any use value or salvage value of the new bagging system, which is the property of Lake River — though admittedly it also ignores the time value of money; Lake River paid $89,000 for that system before receiving any revenue from the contract.

To complete the picture, assume that the breach had not occurred till performance was 90 percent complete. Then the "liquidated damages" clause would not be so one-sided, but it would be one-sided. Carborundum would have paid $480,000 for bagging. Against this, Lake River would have incurred its fixed cost of $89,000 plus 90 percent of its variable costs of $337,000, or $303,000. Its total costs would thus be $392,000, and its net profit $88,000. But on top of this it would be entitled to "liquidated damages" of $53,000, for a total profit of $141,000 — more than 30 percent more than its expected profit of $107,000 if there was no breach.

The reason for these results is that most of the costs to Lake River of performing the contract are saved if the contract is broken, and this saving is not reflected in the damage formula. As a result, at whatever point in the life of the contract a breach occurs, the damage formula gives Lake River more than its lost profits from the breach — dramatically more if the breach occurs at the beginning of the contract; tapering off at the end, it is true. Still, over the interval between the beginning of Lake River's performance and nearly the end, the clause could be expected to generate profits ranging from 400 percent of the expected contract profits to 130 percent of those profits. And this is on the assumption that the bagging system has no value apart from the contract. If it were worth only $20,000 to Lake River, the range would be 434 percent to 150 percent.

Lake River argues that it would never get as much as the formula suggests, because it would be required to mitigate its damages. This is a dubious argument on several grounds. First, mitigation of damages is a doctrine of the law of court-assessed damages, while the point of a liquidated-damages clause is to substitute party assessment; and that point is blunted, and the certainty that liquidated-damages clauses are designed to give the process of assessing damages impaired, if a defendant can force the plaintiff to take less than the damages specified in the clause, on the ground that the plaintiff could have avoided some of them. It would seem therefore that the clause in this case should be read to eliminate any duty of mitigation, that what Lake River is doing is attempting to rewrite the clause to make it more reasonable, and that since actually the clause is designed to give Lake River the full damages it would incur from breach (and more) even if it made no effort to find a substitute use for the equipment that it bought to perform the contract, this is just one more piece of evidence that it is a penalty clause rather than a liquidated-damages clause. See Northwest Collectors, Inc. v. Enders, 74 Wash. 2d 585, 594, 446 P.2d 200, 206 (1968).

no mitigatn

But in any event mitigation would not mitigate the penal character of this clause. If Carborundum did not ship the guaranteed minimum quantity, the reason was likely to be — the reason was — that the steel industry had fallen on hard times and the demand for Ferro Carbo was therefore down. In these circumstances Lake River would have little prospect of finding a substitute contract that would yield it significant profits to set off against the full contract price, which is the method by which it proposes to take account of mitigation. At argument Lake River suggested that it might at least have been able to sell the new bagging equipment to someone for something, and the figure $40,000 was proposed. If the breach occurred on the first day when performance under the contract was due and Lake River promptly sold the bagging equipment for $40,000, its liquidated damages would fall to $493,000. But by the same token its costs would fall to $49,000. Its profit would still be $444,000, which as we said was more than 400 percent of its expected profit on the contract. The penal component would be unaffected.

With the penalty clause in this case compare the liquidated-damages clause in Arduini v. Board of Education [93 Ill. App. 3d 925, 49 Ill. Dec. 460, 418 N.E.2d 104 (1981)], which is representative of such clauses upheld in Illinois. The plaintiff was a public school teacher whose contract provided that if he resigned before the end of the school year he would be docked 4 percent of his salary. This was a modest fraction of the contract price. And the cost to the school of an untimely resignation would be difficult to measure. Since that cost would be greater the more senior and experienced the teacher was, the fact that the liquidated damages would be greater the higher the teacher's salary did not make the clause arbitrary. Even the fact that the liquidated damages were the same whether the teacher resigned at the beginning, the middle, or the end of the school year was not arbitrary, for it was unclear how the amount of actual damages would vary with the time of resignation. Although one might think that the earlier the teacher resigned the greater the damage to the school would be, the school might find it easier to hire a replacement for the whole year or a great part of it than to bring in a replacement at the last minute to grade the exams left behind by the resigning teacher. Here, in contrast, it is apparent from the face of the contract that the damages provided for by the "liquidated damages" clause are grossly disproportionate to any probable loss and penalize some breaches much more heavily than others regardless of relative cost.

We do not mean by this discussion to cast a cloud of doubt over the "take or pay" clauses that are a common feature of contracts between natural gas pipeline companies and their customers. Such clauses require the customer, in consideration of the pipeline's extending its line to his premises, to take a certain amount of gas at a specified price — and if he fails to take it to pay the full price anyway. The resemblance to the minimum-guarantee clause in the present case is obvious, but perhaps quite superficial. Neither party has mentioned take-or-pay clauses, and we can find no case where such a clause was even challenged as a penalty clause — though in one case it was argued that such a clause made the damages unreasonably *low.* See National Fuel Gas Distribution Corp. v. Pennsylvania Public Utility Commn., 76 Pa. Commw. 102, 126-127 n.8, 464 A.2d 546, 558 n.8 (1983). If, as appears not to be the case here but would often be the case in supplying natural gas, a supplier's fixed costs were a very large fraction of his total costs, a take-or-pay clause might well be a reasonable liquidation of damages. In the limit, if *all* the supplier's costs were incurred before he began supplying the customer, the contract revenues would be an excellent measure of the damages from breach. But in this case, the supplier (Lake River, viewed as a supplier of bagging services to Carborundum) incurred only a fraction of its costs before performance began, and the interruption of performance generated a considerable cost saving that is not reflected in the damage formula.

The fact that the damage formula is invalid does not deprive Lake River of a remedy. The parties did not contract explicitly with reference to the measure of damages if the agreed-on damage formula was invalidated, but all this means is that the victim of the breach is entitled to his common law damages. See, e.g., Restatement, Second, Contracts §356, comment a (1981). In this case that would be the unpaid contract price of $241,000 minus the costs that Lake River saved by not having to complete the contract (the variable costs on the other 45 percent of the Ferro Carbo that it never had to bag). The case must be remanded to the district judge to fix these damages. . . .

NOTES

1. For another excellent case setting out the history and policy behind liquidated damages, clauses, see Wasserman's Inc. v. Township of Middletown, 137 N.J. 238, 645 A.2d 100 (1994). There the court concludes, after citing several commentators, that the real issue is one of reasonableness and that the categorization of the parties of a clause as one for "liquidated damages" v. "penalty" is of no import and adds little to the overall analysis.

2. The court distinguishes "take and pay" contracts, which historically have not been held to be unenforceable. For an excellent case on the distinction between take-and-pay contracts and contracts with an unenforceable penalty, read Superfos Investments Ltd. v. Firstmiss Fertilizer, Inc., 821 F. Supp. 432 (S.D. Miss. 1993) (liquidated damage clause really a penalty and not like take-and-pay contract because contract at issue (1) specifically relieved seller of risk of its producer's failure to supply product and (2) buyer was not given the right to purchase additional product in future to make up any quantity of product not purchased by the buyer in previous years).

3. The 2003 revision of Article 2 has the same tests that are in the original version of §2-718(1) for consumer contracts, but for commercial