

UCC Remedies

Expectation Damages in Sale Agreements

Class 21 · October 29
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TODAY'S BOARD			CONTRACT VS. MARKET		
COMMODITY	UNIT	K	MKT	Δ	
SUNFLOWER SEED	/CWT	13.00	×2	▲	100%
RAISINS	/LB	0.2975	0.80	▲	0.50
ALFALFA	/TON	45.00	62.00	▲	17.00
POPCORN	/CWT	4.75	8.00	▲	3.25
IRON ORE	/DMTU	80.00	50.00	▼	30.00
BOAT	/EA	12,587.40	12,587.40	=	0.00

Original boards inspired by the commodity exchange

Before screens, exchange prices were posted by hand on large boards above the trading floor. Every price on today's boards comes from today's reading.

The Four Arcs of Contract Law

01

Formation

Did we make a
K?

02

Defenses

Should it be
enforced?

03

Breach

Was
performance
due?

04 • TODAY

Remedies

What follows
from breach?

Same expectation interest. Today, the market supplies the measuring stick.

The Remedies Arc

Ch. 23	Intro to Remedies	DONE
Ch. 24	Advanced Measures of Expectation	DONE
Ch. 25	Expectation Damages in Sale Agreements	TODAY
Next	Limits: Foreseeability and Mitigation	
Next	Limits: Mitigation and Certainty	
Next	Reliance and Restitution	
Next	Emotional, Punitive and Liquidated Damages	
Next	Specific Performance	

Where We Left Off

- 01 Expectation asks where performance would have put the victim: expected revenue, plus incidental losses, minus costs avoided.
- 02 *Freund*: no provable royalties, so nothing beyond nominal damages. The Court of Appeals awarded six cents.
- 03 *Peevyhouse*: cost of cure (\$29,000) or diminution in value (\$300)? The majority chose \$300.

For goods, the UCC prices the replacement.

Our Goal Today

- 01 What breach takes from each side: the deal, measured against the next best one.
- 02 Buyer remedies when the seller breaches: cover and market differential.
- 03 Seller remedies when the buyer breaches: market differential and lost profit.

TWO SIDES TO EVERY SALE

Who Loses What?

UCC • TODAY'S SECTIONS		WHO LOSES WHAT
§ 1-305	Remedies liberally administered	
§ 2-703	Seller's remedies in general	
§ 2-708	Seller's damages	
§ 2-711	Buyer's remedies in general	
§ 2-712	Cover	
§ 2-713	Market differential	
§ 2-714	Accepted goods	

Breach Cuts Both Ways

A sale has two sides. Either one can walk away.

THE SELLER BREACHES

The buyer is left without the goods

It still has its money. It needs another seller.

THE BUYER BREACHES

The seller is left holding the goods

It still has the goods. It needs another buyer.

Either way, the victim keeps something. What it loses is the deal.

When the Seller Walks Away

01 The buyer keeps its money. What it lost is the deal.

E.G. You agree to buy a used couch on Marketplace for \$300. The seller backs out. The next best couch costs \$450. You still have your \$300, but you are out \$150.

02 Usually the buyer can still buy. But the next seller is rarely as good: buying in a hurry means a smaller pool of sellers.

03 Buyers shop around and take the best price. The seller who walked away was the best offer.

The buyer's loss: the next best deal, minus this one.

When the Buyer Walks Away

01 The seller keeps the goods. What it lost is the deal.

E.G. You are moving out and sell your couch for \$300, the best of three offers. Two days before move-out, the buyer backs out. The best offer left is \$180. You still have the couch, but you are out \$120.

02 Usually the seller can still sell. But the next buyer is rarely as good: selling in a hurry reaches a smaller pool of buyers.

03 Sellers choose among buyers and take the highest bid. The buyer who walked away was the best offer.

The seller's loss: this deal, minus the next best one.

The Next Best Deal

The seller breaches

The buyer's next best deal: a replacement (cover), or the market price

$\text{next} - K$

The buyer breaches

The seller's next best deal: a resale, or the market price

$K - \text{next}$

Then add incidental and consequential losses, and subtract expenses saved.

Common law: the lost profit. UCC: the next best deal. Usually, same number.

UCC § 1-305(a)

Remedies to Be Liberally
Administered

(a) The remedies provided by [the UCC] must 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**

Formerly § 1-106. Tongish cites it as K.S.A. 84-1-106.

WHEN THE SELLER BREACHES

Buyer Remedies

WHEN THE SELLER BREACHES			BUYER REPLACES	
COMMODITY	UNIT	K	MKT	Δ
FRONT DOOR	/EA	2,000	2,200	▲ 200
WHEAT	/BU	5.00	8.00	▲ 3.00
COVER	cover price - K			
MARKET	Mkt - K			
WARRANTY	warranted - accepted			

The Front Door

You order a fancy front door for your home.

Purchase order

One front door, as shown in the catalog, for \$2,000.

The seller breaches.

The same door sells elsewhere for \$2,200.

What do you need to be made whole?

\$200: enough to buy the same door from someone else.

Two Ways to Price the Next Best Deal

COVER

What did it cost me to buy a replacement?

You buy the same door elsewhere for \$2,200. You recover the extra \$200.

MARKET DIFFERENTIAL • $MKT - K$

What would a replacement cost at today's market price?

You buy nothing. You prove the market price is \$2,200. You recover $\$2,200 - \$2,000 = \$200$.

Same answer here. When would the two come apart?

UCC § 2-711(1)

Buyer's Remedies in General

(1) Where the seller fails to make delivery or repudiates or the buyer rightfully rejects or justifiably revokes acceptance . . . the buyer may **cancel** and whether or not he has done so may in addition to **recovering so much of the price as has been paid**

(a) “**cover**” and have damages under the next section as to all the goods affected whether or not they have been identified to the contract; or

(b) **recover damages for non-delivery** as provided in this Article (Section 2-713).

UCC § 2-712

“Cover”; Buyer's
Procurement of Substitute
Goods

(1) After a breach within the preceding section the buyer may “cover” by making **in good faith and without unreasonable delay** any **reasonable purchase** of or contract to purchase goods in substitution for those due from the seller.

(2) The buyer may recover from the seller as damages **the difference between the cost of cover and the contract price** together with any incidental or consequential damages as hereinafter defined (Section 2-715), but **less expenses saved** in consequence of the seller's breach.

(3) Failure of the buyer to effect cover within this section **does not bar him from any other remedy**.

2-712: Breakdown

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- 01 Cover – K: the replacement's cost minus the K price.
 - 02 The cover must be in good faith, without unreasonable delay, and reasonable: goods substantially similar to the original.
 - 03 Add incidental and consequential damages (§ 2-715); subtract expenses saved.
 - 04 An option, not a duty: failing to cover does not bar other remedies (§ 2-712(3)). But no consequential damages that cover would have prevented (§ 2-715(2)(a)).

UCC § 2-713

Buyer's Damages for Non-delivery or Repudiation

(1) Subject to the provisions of this Article with respect to proof of market price (Section 2-723), the measure of damages for non-delivery or repudiation by the seller is the difference between **the market price at the time when the buyer learned of the breach** and **the contract price** together with any incidental and consequential damages provided in this Article (Section 2-715), but less expenses saved in consequence of the seller's breach.

(2) Market price is to be determined as of **the place for tender** or, in cases of rejection after arrival or revocation of acceptance, as of the place of arrival.

2-713: Breakdown

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- 01 Mkt – K: the market price when the buyer learned of the breach, minus the K price.

 - 02 Market price is taken at the place for tender (or, if the buyer rejects after arrival or revokes acceptance, at the place of arrival).

 - 03 Never negative. If the market falls below the K price, the differential is zero.

 - 04 Courts apply it routinely: alfalfa sold at \$45 against a \$62 market (*Panhandle*); popcorn at \$4.75 against \$8 (*Baker v. Ratzlaff*).

The x10 Lawyer

Cover and market sound the same. That is only true in the classroom.

What gets the client more money?

Prices rise after the breach: cover. Prices fall: $\text{Mkt} - K$, fixed when the buyer learned of the breach, if the client has not covered.

What is easier to prove?

An established market: $\text{Mkt} - K$. A thin market: cover.

What is less risky?

Cover can be attacked as unreasonable. Market proof can be volatile.

Keeping Defective Goods

A different problem: the seller delivers, the goods are defective, and the buyer keeps them.

Value as warranted	\$1,000
What the machine would be worth as promised	

Value as accepted	\$600
What the machine is actually worth	

Damages under § 2-714(2)	\$400
Plus any incidental or consequential loss (§ 2-715)	

Non-delivery: §§ 2-712 and 2-713. Accepted but defective goods: § 2-714.

The Wheat Trader

A buyer agrees to buy wheat at \$5 a bushel. She plans to resell it at \$6.

Sale contract

Wheat, at \$5 per bushel.

The seller breaches when the market hits \$8.

The buyer does nothing.

Planned profit: \$1 a bushel. Market differential: \$3. Which should she get?

Under § 2-713: \$3 a bushel, triple her planned profit. Hold that thought.

23

Tongish v. Thomas

Court of Appeals of Kansas • 1992



Helianthus annuus

Seller, Middleman, Buyer

Three parties, two contracts. Follow the seeds and the money.



IF THE MARKET PRICE DOUBLES TO \$26 / CWT

▼ sells at \$13

= keeps \$0.55 / cwt

▲ buys at \$13

IF IT FALLS TO \$6.50 / CWT

▲ sells at \$13

= keeps \$0.55 / cwt

▼ buys at \$13

Coop has no stake in the market price. Bambino does.

Then the Market Doubled

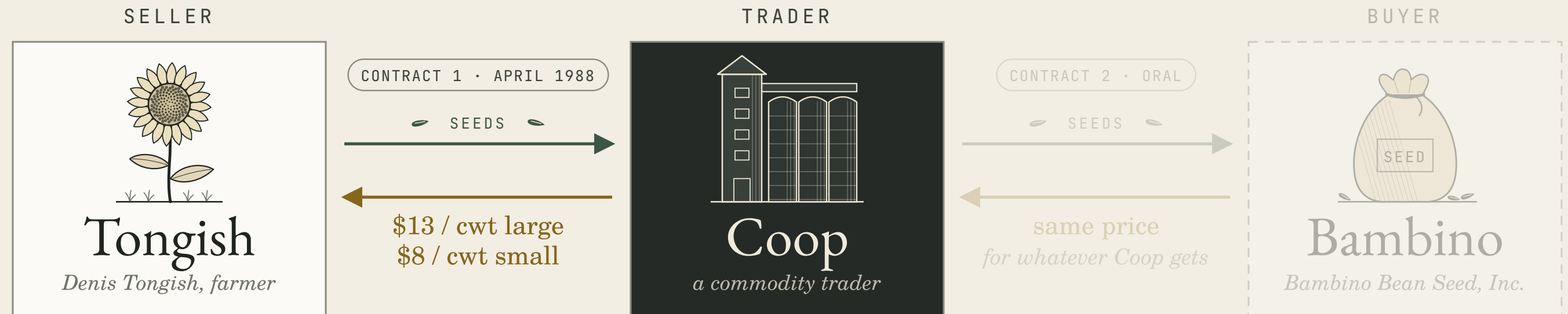
January 1989: the price has doubled, and Tongish walks away.



Trial court: \$455.51, the lost handling fees. Coop appeals for Mkt – K.

First, Imagine There Is No Bambino

Coop as a trader: it buys seeds now to resell later.



IF THE MARKET PRICE DOUBLES TO \$26 / CWT

▼ sells at \$13

▲ buys at \$13

no Bambino

What are Coop's lost profits? What is Mkt – K? Does Mkt – K make Coop whole?

The same number: the seeds' market value minus the K price. The Thomas sale puts it at about \$5,153.

Bambino buys whatever Coop gets, at the same price.



IF THE MARKET PRICE DOUBLES TO \$26 / CWT

▼ sells at \$13

= keeps \$0.55 / cwt

▲ buys at \$13

Now what are Coop's lost profits? What is $Mkt - K$?

Lost profit shrinks to the handling fees: \$455.51. Mkt – K stays the same.

Which Number?

Lost profit · trial court · § 1-305
The handling fees Coop expected to earn

\$455.51

Market – K · § 2-713
The spread Tongish captured by selling to Thomas. The exact figure was left for remand.

about
\$5,153

An elevenfold gap. Which does the court adopt? Is it a windfall?

Two Provisions, One Conflict

GENERAL · § 1-106 (NOW § 1-305)

As good a position as performance

Measured by actual loss, Coop recovers its handling fees.

\$455.51

SPECIFIC · § 2-713

Market price minus contract price

Measured by the market, Coop recovers the spread. At the Thomas price:

≈ \$5,153

The specific statute controls the general one, unless the legislature intended otherwise.

TONGISH: WHY THE MARKET RULE

“While application of the rule may not reflect the actual loss to a buyer, it encourages a more efficient market and discourages the breach of contracts.”

Walton, J. • Tongish v. Thomas, 16 Kan. App. 2d 809 (1992)

Allied Canners: The Other Way

ALLIED CANNERS • CAL. CT. APP. 1984

A good-faith failure

Rain destroyed Victor's raisin crop; it had nothing to sell anyone. Allied's own buyers released it. Actual loss: \$4,462.50. Market differential: about \$150,000. Recovery: actual loss.

TONGISH • KAN. CT. APP. 1992

A breach without valid reason

The market doubled, and Tongish sold the seeds to Thomas for more. No bad-faith finding was needed. Recovery: the market differential.

In both cases the seller knew of the resale K. What really separates them?

Tongish: Main Takeaways

Holding

Coop recovers market minus contract under § 2-713, not its lost handling fees.

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- 01 The specific formula (§ 2-713) controls the general principle (§ 1-305).
 - 02 Market damages can exceed actual loss. They discourage breach when the market moves the seller's way.
 - 03 Minority rule (*Allied Cannery*): actual loss, when the seller knew of the resale K and did not breach in bad faith. *Tongish* rejects it.
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Tongish: The Debate

- 01 Childres (1978): repeal § 2-713. Market damages make “no sense whatever when applied to real life situations.”
- 02 Simon and Novack (1979): courts have divided “for over sixty years.” They side with market damages: deterrence and efficient markets.
- 03 After *Tongish*, courts are still divided. California follows *Allied*, faintly; other courts sit on the fence.

SCOTT, THE CASE FOR MARKET DAMAGES (1990)

“Market damages measure the expectancy ex ante, and thus reflect the value of the option; lost profits, on the other hand, measure losses ex post, and thus only reflect the value of the completed exchange.”

Quoted in *Tongish v. Thomas*, 16 Kan. App. 2d 809 (1992)

An Option or an Exchange?

PRICE THE OPTION • § 2-713

Coop's right to buy at the K price

A right to buy at the K price, wherever the market went. Its value: the market-contract spread. Bambino is irrelevant.

PRICE THE EXCHANGE • § 1-305

What would have changed hands

A \$0.55 per cwt handling fee. Anything more is a windfall.

Exam heuristic: a gap between $Mkt - K$ and lost profit? Ask whether the victim lost an option or a completed exchange.

x10 Lawyer: Know Thy Client

What is Coop doing? How does it make money? What is its exposure?

01 Coop is a pass-through: buy at the K price, resell at the same price, keep \$0.55 per cwt.

02 Bambino, not Coop, bore the price risk. Who really lost the spread?

03 Drafting: if you represent Bambino, what do you put in the Coop contract?

WHEN THE BUYER BREACHES

Seller Remedies

WHEN THE BUYER BREACHES		SELLER IS LEFT HOLDING		
COMMODITY	UNIT	K	MKT	Δ
IRON ORE	/DMTU	80.00	50.00	▼ 30.00
BOAT	/EA	12,587.40	12,587.40	= 0.00
MARKET	K - Mkt			
LOST PROFIT	if K - Mkt is inadequate			

UCC § 2-703

Seller's Remedies in General

[On the buyer's breach, the aggrieved seller may]

(a) withhold delivery of such goods; (b) stop delivery by any bailee . . . (Section 2-705); (c) proceed under the next section respecting goods still unidentified to the contract; (d) **resell and recover damages** as hereafter provided (Section 2-706); (e) **recover damages for non-acceptance** (Section 2-708) or in a proper case **the price** (Section 2-709); (f) **cancel**.

Today: § 2-708. Resale (§ 2-706) and the price (§ 2-709) another day.

Gussie's Iron Ore

Gussie trades in iron ore. He mines it at \$20 per unit.

Sale agreement

Josephine buys 100 dmtu of iron ore from Gussie at \$80 per unit.

The day before delivery, prices crash to \$50.

Josephine emails: she is no longer interested.

Read § 2-708(1). What does Gussie get?

K – Mkt: \$8,000 – \$5,000 = \$3,000.

UCC § 2-708(1)

Seller's Damages for Non-acceptance or Repudiation

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

Two Roads to \$3,000

$K - M_{kt}$

\$8,000 contract price, minus \$5,000 market value

\$3,000

Lost profit

\$8,000 expected, minus the ore he keeps (worth \$5,000). Not the \$6,000 mining profit: he still owns the ore.

\$3,000

Usually, $K - M_{kt}$ equals lost profit. Usually.

UCC § 2-708(2)

Seller's Damages for Non-acceptance or Repudiation

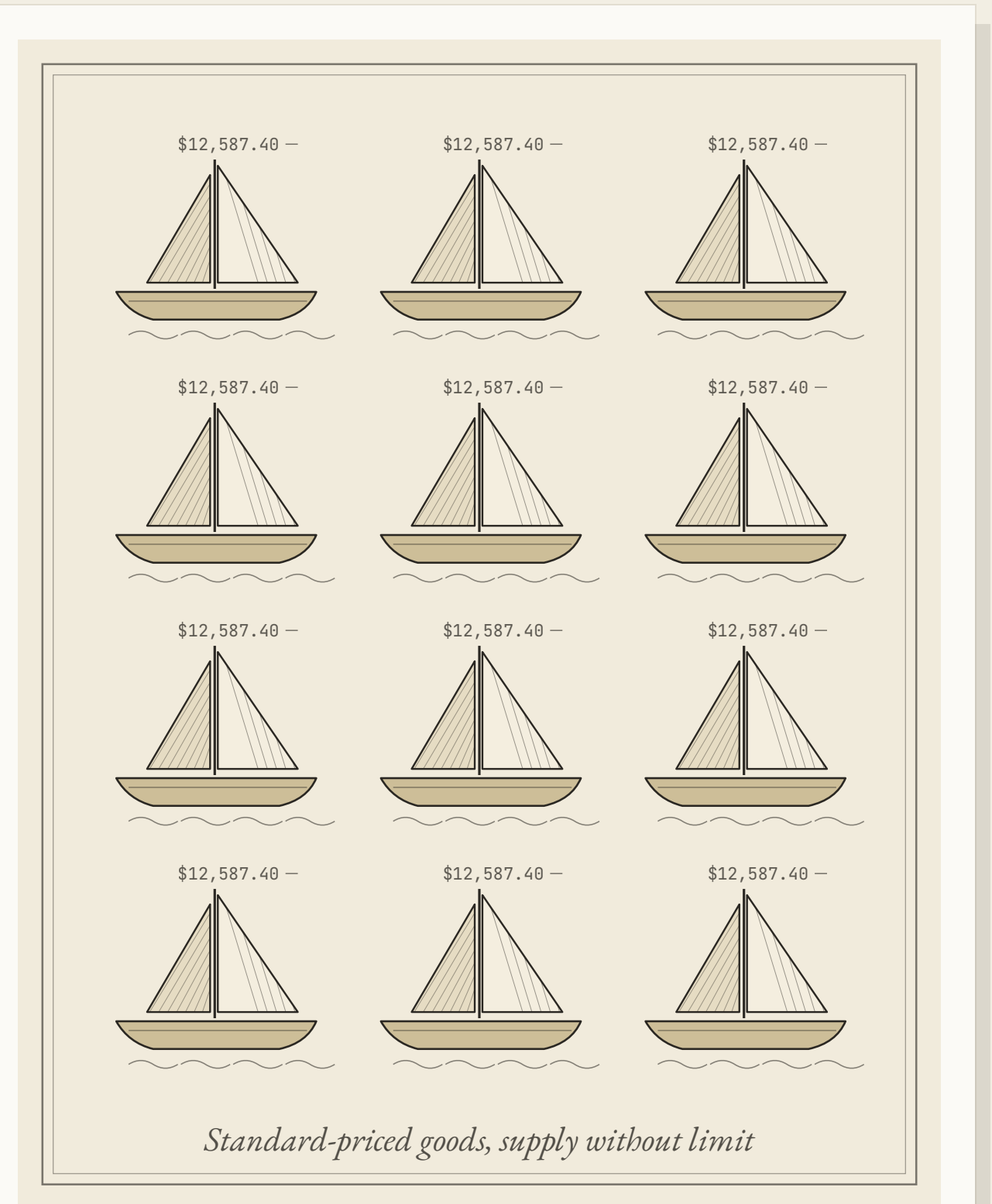
(2) If the measure of damages provided in subsection (1) is **inadequate** to put the seller in as good a position as performance would have done then the measure of damages is **the profit (including reasonable overhead)** which the seller would have made from full performance by the buyer, together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

2-708: Breakdown

- 01 Primary measure: $K - \text{Mkt}$ at the time and place for tender (§ 2-708(1)).
- 02 If that measure is inadequate to put the seller where performance would have: lost profit, including reasonable overhead (§ 2-708(2)).
- 03 Under (1): plus incidental damages (§ 2-710), minus expenses saved. Under (2): plus incidental damages and costs reasonably incurred; the profit already nets out saved costs.

Neri v. Retail Marine Corp.

Court of Appeals of New York • 1972



Synopsis

Neri

Contract	The Neris order a new boat for \$12,587.40 and raise their deposit from \$40 to \$4,250 for immediate delivery.
Repudiation	Six days later their lawyer rescinds: Mr. Neri faces surgery, and the letter says payments would be “impossible.”
Resale	Four months later the dealer sells the boat to another buyer, at the same price.
Claim	Lost profit of \$2,579, plus \$674 for storage, upkeep, finance charges, and insurance.

The boat sold for the same price. What did the dealer lose?

NERI: THE LOST-VOLUME SELLER

“If the dealer has an inexhaustible supply of cars, the resale to replace the breaching buyer costs the dealer a sale, because, had the breaching buyer performed, the dealer would have made two sales instead of one.”

Dean Hawkland, quoted in *Neri v. Retail Marine Corp.*, 30 N.Y.2d 393 (1972)

One Car, Two Sellers

PRIVATE SELLER

One car to sell

The buyer breaches. He resells for the same \$2,000. His loss: the cost of a new sale.

DEALER

An inexhaustible lot

The buyer breaches. He resells for \$2,000. His loss: one sale. He would have made two.

For the private seller, the resale is the next best deal. For the dealer, it is an extra deal, not a substitute.

Neri: Main Takeaways

Holding

The dealer offsets its lost profit (\$2,579) and incidental costs (\$674); the Neris recover \$997 of their \$4,250 deposit.

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- 01 For a lost-volume seller, $K - M_{kt}$ is inadequate, so § 2-708(2) awards the lost profit.
 - 02 The test: could and would the seller have made both profitable sales? If the later buyer would have bought anyway, the resale does not replace the lost sale.
 - 03 “Due credit for . . . proceeds of resale” means the scrap value of components, not the resale of the finished boat.

Who Is a Lost-Volume Seller?

Could the seller have made both sales? Would it have?

- A A car dealer with a lot full of identical sedans.
- B A neighbor selling her only car.
- C A shipyard booked solid for two years with custom yachts.
- D A gallery selling a one-of-a-kind painting.

Summary

BUYER • WHEN THE SELLER BREACHES

Cover – K § 2-712

A reasonable substitute's cost, minus the K price. Plus incidental and consequential, minus expenses saved.

Mkt – K § 2-713

Market when the buyer learned of the breach, minus the K price. Never below zero. *Tongish*: even above actual loss.

Warranted – accepted value § 2-714

For defective goods the buyer keeps.

SELLER • WHEN THE BUYER BREACHES

K – Mkt § 2-708(1)

K price minus market at the time and place for tender. Plus incidental, minus expenses saved.

Lost profit § 2-708(2)

When K – Mkt is inadequate. *Neri*: the lost-volume seller.

Resale § 2-706

Another day.

The Coffee Contract

Gaia roasts coffee in Wynwood. She contracts to buy 1,000 pounds of green beans from Tom, an importer, at \$4 a pound, delivery March 1. She also agrees to sell the roasted coffee to a café chain at a fixed price.

On February 10, frost hits Brazil. The market jumps to \$7.

TOM *“I found a buyer at \$7. You’ll get your deposit back.”*

Gaia waits until March 20, then buys replacement beans at \$8. Meanwhile, the café chain releases her from the resale deal.

What can Gaia recover? Cover or market? Does the café's release matter? What if the frost had destroyed Tom's own beans?

The Coffee Contract, Flipped

Back to February. This time the market collapses to \$3, and Gaia refuses delivery.

GAIA *“Sell your beans to someone else. You won’t lose a thing.”*

Tom resells the 1,000 pounds to another roaster at \$3. Tom pays \$2.50 a pound for his beans. His warehouse holds 50,000 pounds, and he has never turned a customer away.

What does § 2-708(1) give Tom? Is that adequate? Is Tom a lost-volume seller, and what would § 2-708(2) give him?