

Sales and Leases
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Sample Exam Questions – Model Answers

1. Tempus Fugit (“Tempus”) is a New Jersey manufacturer of wall clocks. Franks Cranks (“Franks”) is a manufacturer of precision gear works whose factory is in Windsor, Ontario (that’s in Canada, for the geographically challenged). Gearz-R-Us (“Gearz”) is Franks’s authorized dealer for New York and New Jersey. On March 1, 2003, Tempus’s purchasing manager telephoned Gearz and, after describing Tempus’s particular needs, ordered 1,000 sets of precision gear works, at a price of US\$50.00 per set (that’s \$50,000, for the mathematically challenged), to be delivered to Tempus’s plant no later than April 15, 2003. Later that same day, Franks faxed an acknowledgment from Windsor, agreeing to manufacture for and sell to Tempus 1,000 sets of gear works satisfying Tempus’s specifications, at a price of US\$50.00 per set, and to deliver them to Tempus’s plant no later than May 15, 2003. Franks’s acknowledgment also contained a provision requiring Tempus to pay the full contract price, including transportation costs, upon receipt of the gears. There was no further correspondence between the parties. The goods left Franks’s plant on or about April 5, 2003, and arrived at Tempus’s factory on April 12, 2003. Upon receipt of the goods, Tempus paid the carrier \$52,500, representing the full contract price, plus \$2,500 for transportation costs. If a dispute subsequently arises between Tempus and Franks, will their agreement be governed by Article 2 of the UCC or by the CISG? Please explain.

The CISG should govern this contract. Article 1(1) says that the CISG applies to contracts for the “sale of goods between parties whose places of business are in different States.” The U.S. and Canada are different states, both of which are signatories to the CISG. Article 10 says that, in a case where a party has more than one place of business, the place of business is that “which has the closest relationship to the contract and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of the contract.” Here, unless Tempus had no reason to know that it was ultimately contracting with Franks (and that should have been obvious when it received the confirming fax), the place of business with the closest relationship to this contract is Franks’s Ontario plant. Tempus was not purchasing the glass for “personal, family or household use,” so Article 2(a) would not take this international sales contract out of the CISG. And, even though the CISG sets forth a form of the “predominant purpose” test for mixed goods-and-services contracts, Art. 3(2), the CISG is clear that the “service” of manufacture will not preclude coverage of contracts for specially manufactured goods, such as these glass tubes, as long as the buyer is not supplying materials for manufacture of the goods, Art. 3(1) – which Tempus did not.

2. Willy Huff wanted a new pickup truck. However, he lacked the funds to purchase one for cash. So, Willy entered into a Lease Agreement with Lone Mesquite Autoplex (“LMA”). The terms of the Lease Agreement required Willy to pay LMA a cash deposit of \$1,000 plus \$250 per month for 60 months (total lease payments = \$15,000). At the end of the 60-month lease term, Willy could purchase the truck for its then-”blue book” value, or he could return the truck to LMA, which would sell the truck for him. If LMA failed to receive the full “blue book” value of the truck from either Willy or another purchaser, the Lease Agreement obligated Willy to pay LMA the difference between the “blue book” value and the price at which LMA was able to resell the truck. The Lease Agreement also obligated Willy to insure the truck from the date of the Lease Agreement until the end of the lease term. In the event Willy let the insurance on the truck lapse, the Lease Agreement empowered LMA to obtain insurance for the truck and add the cost to Willy’s monthly lease payments. If at any time prior to the end of the lease term Willy wished to terminate the lease, the Lease Agreement required him to give 30 days prior notice to LMA. At the end of the 30 days, Willy could either purchase the truck for its then-”blue book” value, or he could return the truck to LMA, which would sell the truck for him. As would be true at the end of the agreed lease term, if LMA failed to receive the full “blue book” value of the truck from either Willy or another purchaser following Willy’s premature termination of the lease, the Lease Agreement obligated Willy to pay LMA the difference between the “blue book” value and the price at which LMA was able to resell the truck.

A. The same day that Willy signed the Lease Agreement, paid the \$1,000 deposit plus the first month’s lease payment, and drove his new pickup home from LMA’s lot, someone stole Willy’s new truck while it was parked in front of his house. At the time of the theft, who bore the risk of loss: Willy or LMA? Please explain.

As a general rule, risk of loss in a lease governed by Article 2A remains with the lessor. § 2A-219(1). The exception to this general rule for finance leases does not apply in this case, as there is no third-party finance lessor. See § 2A-103(1)(g). This contract is strictly between LMA and Willy. So, if this is a lease, then LMA bore the risk of loss at the time of the theft.

But, is this a lease or a disguised sale? § 1-201(37) definitively settles the lease/sale distinction only when there is “an obligation for the term of the lease *not subject to termination by the lessee*” and (1) the original term of the lease is equal to or greater than the remaining economic life of the goods; (2) the lessee is required to renew the lease for the remaining economic life of the goods or to purchase them; (3) the lessee has the option for no additional consideration or for nominal additional consideration (a) to renew for the remaining economic life of the goods or (b) to purchase the goods. Only in those four cases does § 1-201(37) clearly declare that the transaction at issue is a disguised sale (giving rise to a security interest), rather than a lease. This contract is not definitively a disguised sale because Willy has the right to terminate the lease with 30 days’ notice. Or does he? Willy nominally has the right to terminate the lease early, but if he does he will either have to buy the truck from LMA for its then-”blue book” value or he will have to “guarantee” LMA the “blue book” value of the truck by paying LMA the difference between its “blue book” value and its resale price. Seen in that light, the contract begins to look more like a purchase in installments with LMA agreeing to act as Willy’s

selling agent in the event he chooses not to keep the truck at the (natural or premature) end of the lease. The Nevada Supreme Court reached the same conclusion in *Nevada National Bank v. Huff*, 582 P.2d 364, 368 n.1 (Nev. 1978):

[U]pon his initial entry into the “lease agreement”, Huff became instantaneously liable for the entire value of the truck, either as a direct debtor in the event that he himself chose to “buy” the truck at the end of the 36-month term, or else as guarantor of the total original purchase price in the event that the vehicle was ... sold to someone else. Upon complying with the terms of the lease, therefore, the truck became his at the end of the lease term for nothing more than that for which he was already contractually liable, *i.e.*, for no additional consideration. Upon analysis, this “lease agreement” appears to be nothing other than an installment sales contract arranged for optimum federal tax results

So, if this was a disguised sale, who would bear the risk of loss at the time the truck was stolen from Willy’s curb? The contract does not mention delivery or shipment, and there is no third-party bailee involved, so this is an “everything else” contract for purposes of risk of loss, and is governed by § 2-509(3). LMA is almost certainly a merchant seller; therefore, risk of loss passed to Willy when he received the truck. Therefore, Willy bore the risk of loss.

B. Suppose, instead, that twelve months into the term of the Lease Agreement, Willy has timely made all required payments, and has been routinely driving the truck several hundred miles a week without any performance problems. Nonetheless, after receiving a recall notice from the truck’s manufacturer, Willy took the truck to LMA for the repairs called for in the recall notice, which LMA assured Willy would be performed free of charge. While the truck was at LMA for those repairs, unknown persons vandalized it and several other vehicles, causing more than a thousand dollars’ worth of damage to Willy’s truck. As between Willy and LMA, who bore the risk for the vandalism? Please explain.

A defect sufficient to cause the manufacturer to issue a recall notice would “give a right of rejection,” under § 2-510(1). However, Willy has clearly accepted the truck, so § 2-510(1) does not help him. If Willy accepted the nonconforming truck, but then properly revoked, then LMA would bear the risk of loss to the truck to the extent of any deficiency in Willy’s insurance. § 2-510(2). However, the question does not say that Willy revoked his acceptance, he merely returned the truck to the dealer for repairs. (Notice that, while the buyer’s *right to reject* determines who bears the risk under § 2-510(1), the buyer’s (actual) *revocation* determines who bears the risk under § 2-510(2)). Therefore, the risk of loss should still be on Willy. The good news is that, because the truck was properly on LMA’s property, LMA almost certainly has insurance that will cover the damage to Willy’s truck irrespective of the provisions of § 2-510.

3. **Romeo had been courting Juliet for several years. Finally, he decided to propose marriage. Romeo shopped around to find the best deal on the right ring. Romeo found the ring he was looking for at Old Will’s Jewelers (“OWJ”) for \$10,000. Romeo was unable to pay the entire purchase price immediately. Old Will agreed to sell Romeo the ring for \$2,500 down and \$7,500 to be paid in ten equal monthly installments. Romeo asked Old Will to hold the ring for him and promised to return the next day with the down payment.**

Romeo returned to OWJ the next afternoon with a check for \$2,500, drawn on Romeo’s account at the Padua Bank & Trust (“PB&T”). Old Will agreed to hold Romeo’s check until Romeo picked up the ring the following morning. Later that afternoon, however, Old Will called PB&T to make sure that Romeo’s account contained sufficient funds to cover the check. PB&T informed Old Will that the account had, at that moment, “less than \$500,” and that, “over the past 12 months, the balance in this account has averaged less than \$1,000.” Old Will then called the local credit bureau, which characterized Romeo as “a questionable credit risk” for any amount greater than \$500.

Old Will promptly called Romeo, chastised him for writing “a rubber check,” and demanded that Romeo pay the entire purchase price in cash. Romeo told Old Will that he had transferred funds into his PB&T account to cover the check, but that (because he had done so after 3:00 p.m.) the additional funds would not show up in his account balance until tomorrow. Romeo offered to bring \$2,500 cash when he came to pick up the ring. Old Will would not budge. He insisted that Romeo pay the full price in cash or the deal was off. Romeo refused, bought a ring of comparable size and quality from another jeweler for \$12,500, proposed to Juliet, she accepted, and they are happily married.

Romeo then sued OWJ for breach of contract. OWJ moved for summary judgment, claiming that Romeo anticipatorily repudiated by writing a check without sufficient funds in his account, thus relieving OWJ of any obligation to perform.

A. Assume that (1) each action taken by Old Will is attributable to OWJ; and (2) Romeo transferred \$2,500 into his PB&T account in time to cover the check if OWJ had deposited it the same day that Romeo was to pick up the ring. Did Romeo have an enforceable contract to purchase the ring from OWJ for \$2,500 plus ten monthly payments of \$750 each? Please explain.

Romeo’s ring is both existing and identified, § 2-105(2), and is movable at the time at the time of its identification to the contract, § 2-105(1). Therefore, it is a good, and Article 2 governs the contract for its sale. § 2-102. Unfortunately for Romeo, the contract is for more than \$500; and, therefore, § 2-201(1) requires that it be evidenced by one or more writings signed by Old Will’s Jewelers (“OWJ”), the party against whom Romeo seeks to enforce the contract. There is no such writing. Thus, unless one of the exceptions to § 2-201 applies, Romeo did not have an enforceable contract. The only exception that might save Romeo is § 2-201(3)(b) – the judicial admissions exception. We are told that OWJ “answered with the defense of anticipatory breach, and counterclaimed to recover its reasonable attorneys’ fees.” Anticipatory breach presupposes a contract, as does OWJ’s claim for attorneys’ fees under the relevant statute. Unless OWJ denied the existence of the contract and only pleaded anticipatory

breach and attorneys' fees in the alternative, it would appear that OWJ has necessarily "admit[ted] in [its] pleading . . . that a contract for sale was made."

B. Regardless of your answer to subpart "A," if Romeo and OWJ had an enforceable contract, which one breached their contract, when, and how? Please explain.

Romeo did not breach his contract with OWJ by writing a check without having funds in his account to cover the check at that precise moment, relieving OWJ of its duty to perform. The contract obliged Romeo to make a \$2,500 down payment; so, OWJ could argue that Romeo's action breached the contract, excusing OWJ from any duty to perform. That argument should fail, however, because the funds would have been in the account and the bank would have honored the check if OWJ had waited to negotiate it until the next day, as Old Will promised.

OWJ's failure to deliver the ring on the agreed terms did breach its contract with Romeo. Romeo's action may well have given OWJ "reasonable grounds for insecurity" under § 2-609(1), entitling OWJ to take action to protect its "expectation of receiving due performance." But OWJ did not comply with § 2-609. OWJ failed to demand adequate assurance in writing and went far beyond suspending its own performance while demanding adequate assurance. OWJ demanded, in essence, a change in the contract terms. Only in extraordinary circumstances can a party to use § 2-609 to require the other party to accelerate performance. OWJ could reasonably have demanded that Romeo make the down payment in cash, but OWJ's refusal to turn over the ring without full cash payment breached the contract.

C. Suppose that, shortly after Romeo filed suit against OWJ, Juliet accidentally broke one of the prongs on the (replacement) ring Romeo gave her. Unaware that Romeo was involved in litigation with OWJ, and wanting to get the ring fixed without telling Romeo, Juliet stopped during lunch at the jeweler's store just around the corner from her office – the aforementioned Old Will's Jewelers – to have the ring repaired. The clerk, Henslowe, who took the ring told her it would be ready for her to pick up after 5 p.m. He then tagged the ring and left it on the repair box. Old Will, who was handling repairs that afternoon, read the name on the repair tag, put two and two together, and realized whose ring it was that had been left for him to fix. Steaming over Romeo's suit, Old Will fixed the prong and then put the ring in a display case, at a bargain price, hoping some lucky soul would come along and buy it. Before that could happen, however, one of OWJ's customers, Rosaline, saw the ring and recognized it as one of several that had been stolen from her house several months earlier. Further investigation revealed that the thief had pawned the ring at Fennyman's Friendly Pawn Shop, which sold it to Beth's Fine Jewelry, which sold it to Romeo, who gave it to Juliet. Assuming that the ring was stolen from Rosaline and that Romeo had an enforceable contract with Beth's Fine Jewelry, can Romeo sue Beth's Fine Jewelry for breaching the implied warranty of good title? Please explain.

Yes. A thief takes void title. Someone with void title can never pass anything other than void title to a subsequent purchaser, no matter how innocent. Because a seller of goods impliedly warrants that (1) the title conveyed is good, (2) the transfer of title is rightful, and

(3) the goods are free of any encumbrance, UCC § 2-312(1), a seller who sells goods for which one or more of the foregoing statements is untrue breaches the implied warranty of good title. Beth's could not have voidable title if the ring came – no matter how indirectly – from a thief.

D. Same facts as “C,” except suppose that the ring was not stolen from Rosaline (or anyone else), and was sitting in the display case where Will had maliciously placed it when Kent wandered into the store, looking for an engagement ring for his beloved, Violet. Kent saw Juliet’s ring in the display case and purchased it from another sales clerk, Webster, who was unaware that the ring was not part of the store’s inventory. When Juliet returned to the store to reclaim her ring, she discovered that Webster had inadvertently sold it to Kent, who took it with him. Can Juliet reclaim her ring from Kent, given that she did not authorize OWJ to sell it? Please explain.

No. Juliet entrusted the ring to OWJ, a merchant dealing in goods of the kind. § 2-403(3). While Juliet would be entitled to recover her ring from OWJ, which had only voidable title, Juliet cannot recover it from Kent, who is a BOCB. § 2-403(2).

E. Same facts as “C,” except suppose that, instead of placing Juliet’s ring in a display case at the store, Old Will put the ring in his pocket, took it to the Fennyman’s Friendly Pawn Shop, and gave Fennyman the ring to pay off a prior debt of \$2,500. Around 4 p.m. that same day, Thomas Kent wandered into Fennyman’s, looking for an engagement ring for his beloved, Violet, and purchased Juliet’s ring for \$5,000. Can Juliet reclaim her ring from Kent? Please explain.

Yes. While Kent, a good faith purchaser for value (Kent cannot be a BOCB because the UCC deems pawn shops not to sell in the ordinary course of their business, *see* § 1-201(9)), would take good title from Fennyman if Fennyman had voidable title, because Fennyman had only void title, Kent has only void title. § 2-403(1). Even though OWJ’s had voidable title because Juliet entrusted her ring to OWJ’s, § 2-403(2), Old Will had no right to take the ring from OWJ to Fennyman’s. When he did so, he acted as a thief, not as an entrustee, and so passed only void title to Fennyman’s.

4. Mercury Rising (“Mercury”) is an Illinois manufacturer of indoor and outdoor thermometers. On April 2, 2003, Will Bruce, Mercury’s purchasing agent, faxed a purchase order to the Glass Manufacturie (“GM”), a Michigan manufacturer of precision glass tubing. Mercury ordered 5,000 1-foot lengths of glass tubing, at a price of \$5.00 per foot, to be delivered to Mercury’s plant no later than May 1, 2003. Later that same day, GM faxed a written acknowledgment, agreeing to manufacture and deliver 5,000 1-foot lengths of glass tubing, at a price of \$5.00 per foot to Mercury’s plant no later than May 1, 2003. GM’s acknowledgment also contained (1) a disclaimer of all implied warranties, (2) a provision requiring Mercury to pay the cost of having the tubing shipped from GM’s plant to Mercury’s, and (3) a provision requiring Mercury to pay the full contract price, including transportation costs, upon receipt of the tubing. The parties did not correspond further. GM shipped the goods to arrive on May 1, 2003.

A. Before the goods reached Mercury, Mercury found another seller, Glaz Emporium (“Glaz”), who offered to provide the same quantity and quality of glass tubing, no later than May 2, 2003, at a price of \$4.50 per foot. Mercury agreed on April 15, 2003 to purchase the tubing from Glaz, and refused to receive the shipment from GM when it arrived on May 1, 2003. GM wants to sue Mercury for breach of contract. Did Mercury and GM have an enforceable contract for the glass tubing? If so, why and what were its terms? If not, why not?

There are two issues here: (1) did the parties have an enforceable contract; and, if so, (2) what were its terms? The first issue breaks down into two sub-issues: (a) was a contract formed by the parties’ correspondence and/or actions; and, if so, (b) did that contract satisfy the statute of frauds, to the extent the statute of frauds applied to this transaction?

(1)(a) Did the parties form a contract?

At common law, an acceptance which added qualifications or conditions or which in any way varied the terms of the original offer is treated as a counteroffer, not an acceptance. However, this contract is for the sale of goods; and, therefore, is governed by Article 2 of the UCC. Article 2 rejects the common law “mirror image” rule. Under § 2-207(1), a contract is formed even though the acceptance or confirmation contains additional or different terms, as long as the offeree’s intent to accept the offer is definitely expressed and the offeree’s acceptance is not expressly conditioned on the offeror’s assent to the additional or different terms. Here, there was a contract despite the additional, material terms, and Mercury’s refusal to accept is a breach. Mercury’s purchase order constituted an offer. GM’s acknowledgement was an acceptance, despite the additional terms, because it was not made expressly conditional on Mercury’s agreement to the additional terms.

(1)(b) Did the contract satisfy the statute of frauds?

Because this contract was for the sale of goods in an amount greater than \$500, there must be one or more writing(s), signed by Mercury, evidencing the contract, identifying the goods, and stating the quantity to be sold. § 2-201. Here, Mercury’s purchase order should satisfy the statute of frauds. We know that it was written, identified the 1-ft. lengths of glass

tubing to be sold, and stated a quantity of 5,000. We don't know for certain that it was signed, but "signed" for purposes of § 2-201 includes most things that identify the sender. Therefore, if the PO had Mercury's name and address on it, or was on Mercury's letterhead or a Mercury form, or, perhaps, accompanied a fax cover sheet with Mercury's name on it and/or displayed Mercury's name on the "banner" at the top or bottom of each faxed page, § 2-201 would probably be satisfied. Furthermore, because both parties are merchants, even if Mercury did not "sign" its PO, GM's acknowledgment was a written confirmation for purposes of § 2-201(2), to which Mercury did not timely object in writing. Therefore, GM's acknowledgment would satisfy § 2-201 even if Mercury's PO did not.

(2) *What were the terms?*

Because both parties are merchants, the terms of the contract will be determined by referring to § 2-207(1) and (2). Certainly, the agreed terms are "in." So, we know quantity (5,000), price (\$5.00/ft.), and delivery deadline (5/1/2003). What about the terms in GM's acknowledgment? If they "materially alter" the offer, they will not become part of the contract. § 2-207(2)(b) & cmt. 3. If they do not "materially alter" the original bargain, then they will become part of the contract unless (i) Mercury's offer expressly limited GM's acceptance to the terms of the offer, § 2-207(2)(a), which it did not; or (ii) Mercury objected to the additional terms within a reasonable time, § 2-207(2)(c), which it did not. GM's acknowledgement contained three new terms: (1) a disclaimer of all implied warranties, (2) a provision requiring Mercury to pay the cost of having the tubing shipped from GM's factory to Mercury's, and (3) a provision requiring Mercury to pay the full contract price, including transportation costs, upon receipt of the tubing (*i.e.*, "C.O.D."). The disclaimer of warranties – which may not have ultimately been effective under § 2-316 – was a material alteration, per § 2-207 cmt. 4, and will not become part of the contract. The other two terms do not appear to materially alter the original bargain, unless there is some prior course of dealing between these parties or some trade usage or custom that is so contrary to these terms as to make these terms "result in surprise or hardship if incorporated without [Mercury's] express awareness." § 2-207 cmt. 4. Any other terms necessary to complete the contract will be supplied by UCC "gap-fillers."

B. Assuming, for purposes of this subpart, that GM and Mercury had an enforceable contract, did Mercury's refusal to accept GM's May 1, 2003 shipment constitute a breach of Mercury's contract with GM? If so, when? Please explain.

A buyer who "wrongfully rejects ... goods or fails to make a payment due on or before delivery" commits a breach per § 2-703, entitling the seller to any remedy authorized by § 2-703. § 2-602(3). A buyer may only rightfully reject goods if the goods themselves, or the manner of their tender, fail(s) to conform to the contract. § 2-601(a). Here, neither the goods nor the tender were nonconforming.

C. Assuming, for purposes of this subpart, that GM and Mercury had an enforceable contract and that Mercury's refusal to accept GM's May 1, 2003 shipment constituted a breach of Mercury's contract with GM, and that

1. On May 15, 2003, GM entered into a contract to sell 4,000 feet of the glass tubing originally destined for Mercury to another customer, Video Matrix, for \$6.00 per foot, to be delivered no sooner than June 1, 2003, with Video Matrix to pay transportation costs from GM's plant,
2. the market price of the glass tubing on April 2, 2003 was \$5.25 per foot,
3. the market price of the glass tubing on April 15, 2003 was \$5.00 per foot,
4. the market price of the glass tubing on May 1, 2003 was \$5.50 per foot
5. the market price of the glass tubing on May 15, 2003 was \$6.00 per foot,
6. the cost of transporting the glass tubing from GM's plant to Mercury's plant (or vice versa) is \$500, and
7. GM's cost of manufacturing the tubing Mercury ordered was \$4.50 per foot.

What remedy or remedies does Article 2 afford GM against Mercury? Please explain.

Mercury's wrongful rejection entitles GM to cancel the contract. In addition, GM may (1) sell the goods to another buyer and recover resale damages; (2) recover contract-market damages; (3) recover lost profits; and/or (4) sue for price.

(1) Resale Damages (§ 2-706)

Section 2-706 entitles GM to resell the goods in good faith, and in a commercially reasonable manner. If GM does so, it may recover from Mercury the difference between the contract price (KP) and the resale price (RP), plus any incidental damages (ID) permitted by § 2-710, minus expenses saved (ES) by GM as a result of Mercury's nonperformance. GM is not accountable to Mercury for any profit made on the resale. So,

$$\text{Damages} = (\text{KP} - \text{RP}) + \text{ID} - \text{ES}.$$

Here, $\text{KP} = 25,000$; $\text{RP} = (4,000 \times 6.00) = 24,000$; $\text{ID} = 500$ (the cost of transporting the glass from Mercury back to GM), *plus* the cost of storing the 1,000 ft. of tubing that GM couldn't resell; and $\text{ES} = 0$. So,

$$\text{Damages} = 25,000 - 24,000 + (500 + \text{storage}) - 0 = \$1,500 + \text{storage}.$$

In order to recover resale damages, GM must notify Mercury of GM's intent to resell the goods, if GM plans to do so in a private sale, § 2-706(3); alternatively, if GM intends to resell

through a public sale, GM must comply with the requirements of § 2-706(4). If GM fails to satisfy the requirements of § 2-706 – that is, fails to (i) resell in good faith, (ii) resell in a commercially reasonable manner, and/or (iii) give Mercury the requisite notice – GM may not recover under § 2-706, but may recover under § 2-708(1).

GM arranged within two weeks to resell 4,000 of the 5,000 ft. of tubing Mercury ordered to Video Matrix, to be delivered as shortly as one month after Mercury was to take possession, at a price greater than that offered by Mercury and comparable to the market price at the time GM made the deal with Video Matrix. Therefore, the resale appears to be in good faith and commercially reasonable. But, because GM did not properly notify Mercury of its intent to resell, GM did not comply with § 2-706(3) and cannot recover under § 2-706.

(2) *Contract-Market Differential Damages* (§ 2-708(1))

Under § 2-708(1), GM may recover the difference between the contract price and the market price at the time and place for tender (MP), plus any incidental damages permitted by § 2-710, minus expenses saved by GM as a result of Mercury's nonperformance. That is,

$$\text{Damages} = (\text{KP} - \text{MP}) + \text{ID} - \text{ES}.$$

Here, $\text{KP} = 25,000$; $\text{MP} = (5,000 \times 5.50) = 27,500$; $\text{ID} = 500$ (the cost of transporting the glass from Mercury back to GM), *plus* the cost of storing all 5,000 ft. of tubing until the sale to Video Matrix and the 1,000 ft. of tubing that GM couldn't resell thereafter; and $\text{ES} = 0$. So,

$$\text{Damages} = 25,000 - 27,500 + (500 + \text{storage}) - 0 = \text{storage} - 2,000.$$

Because the market price was greater at the time and place of tender (May 1st) than the contract price, GM will not have any recoverable damages unless the cost of storing the tubing is greater than \$1,500. And, of course, we can make a strong argument that storage cost should not be included because § 2-708(1) presumes a hypothetical sale at the market price at the time of tender. If such a sale took place, GM would not have incurred any storage costs. (Recall Problem 22.4, involving the cost of feeding cattle after the date of tender.)

(3) *Lost Profits* (§ 2-708(2))

Because the recovery permitted GM under § 2-708(1) appears to be inadequate to put GM in as good a position as it would have been absent Mercury's breach, GM may recover, in the alternative, any profits (π) that GM would have realized had Mercury performed, plus any incidental damages permitted by § 2-710, minus expenses saved by GM as a result of Mercury's nonperformance, minus any credit due Mercury for partial payment (PP), and minus the proceeds (read "profits") from the resale to Video Matrix (RP) *if* GM could not have otherwise sold to both Mercury and Video Matrix. So,

$$\text{Damages} = \pi + \text{ID} - \text{ES} - \text{PP} - \text{RP}.$$

Here, $\pi = \text{KP} - \text{DC}$ (direct cost of producing the tubing) $= \$25,000 - (5,000 \times 4.50) = 2,500$; $\text{ID} = 500$ (the cost of transporting the glass from Mercury back to GM), *plus* the cost of storage; $\text{ES} =$

0; and $PP = 0$. The trick is, what is the value of RP ? If GM could have sold to both Mercury and Video Matrix, then $RP = 0$ and

$$\text{Damages} = 2,500 + (500 + \text{storage}) - 0 - 0 - 0 = \$3,000 + \text{storage}.$$

If GM could not have sold to Video Matrix but for Mercury's breach, then $RP = \$6,000$ and

$$\text{Damages} = 2,500 + (500 + \text{storage}) - 0 - 0 - 6,000 = \text{storage} - \$3,000.$$

If $RP = \$6,000$, GM will not be able to recover any damages under § 2-708(2) unless the cost of storing the tubing is greater than \$3,000.

(4) Action for Price (§ 2-709)

As to goods identified to the contract that GM is unable to resell after reasonable effort at a reasonable price, GM may recover the price (P) of those identified, un-resold goods, plus any incidental damages permitted by § 2-710. Here, since GM was able to resell to Video Matrix 4,000 ft. of the tubing originally identified to its contract with Mercury, GM can only recover the price of the unsold 1,000 ft. So, $P = (\$5.00 \times 1,000) + \$5,000$;† and $ID = 500$ (the cost of transporting the glass from Mercury back to GM), *plus* the cost of storing the 1,000 ft. of tubing that GM couldn't resell. So,

$$\text{Damages} = P + ID = 5,000 + (500 + \text{storage}) = \$5,500 + \text{storage}.$$

If GM eventually resells any or all of the remaining 1,000 ft., it must credit the proceeds against its judgment against Mercury.††

† It's tempting to say $P = \$25,000$, because that is the entire contract price. But GM could only recover \$25,000 if Mercury accepted the shipment and did not pay for it or if the entire shipment of identified and conforming goods was destroyed within a commercially reasonable time after risk of loss shifted to the buyer. § 2-709(1)(a). Otherwise, GM is limited, as here, to suing for the price of unaccepted, unsold, conforming goods – here, the 1,000 ft. of glass tubing originally slated for Mercury which GM was not able to resell to Video Matrix.

†† It is also tempting to treat the \$24,000 sale to Video Matrix as proceeds to be credited against GM's damages under § 2-709(2). But, again, the only goods for which GM can seek price are the ones that it did not resell to Video Matrix. So there is no offset against the unsold 1,000 ft. unless GM eventually sells that 1,000 ft. to someone else. Mercury will likely bear the burden of proving that any tubing subsequently sold by GM is part of the 1,000 not accepted by Mercury and not sold to Video Matrix.

D. Return to the original facts. Now, suppose that Mercury did not refuse to receive GM's May 1, 2003 shipment; instead, Mercury properly paid the carrier \$25,500 (including \$500 for transportation). Shortly thereafter, however, Mercury determined that 80% of tubing GM supplied was of inferior quality and unfit for the use for which Mercury bought it. Assuming, for purposes of this subpart, that GM and Mercury had an enforceable contract, what recourse does Article 2 afford Mercury with respect to the inferior tubing? Please explain.

If Mercury discovered the nonconformity prior to accepting the tubing, it could (1) reject the entire shipment, § 2-601(a), provided that it did so within a reasonable time after delivery and that it seasonably notified GM of its rejection, § 2-602(1), and pursue any of the remedies set forth in § 2-711; (2) accept the entire shipment, § 2-601(b), seasonably notify GM of the nonconformity, § 2-607(3)(a), and sue GM for damages due to nonconformity, § 2-714; or (3) accept those units that conformed to the contract and reject those that did not, § 2-601(c), again, provided that Mercury rejected within a reasonable time after delivery and that it seasonably notified GM of its rejection, § 2-602(1), and pursue any of the remedies set forth in § 2-711 as to the rejected portion of the delivery. Because the contract required Mercury to pay in full on receipt, the mere fact that Mercury paid does not mean it has accepted. § 2-512(2). § 2-606(1) gives Mercury a reasonable opportunity to inspect the goods before accepting.

If Mercury did not discover the nonconformity prior to accepting the tubing, or if it failed to give GM the notice required by § 2-602(1), and thereby failed to properly reject, it could revoke its acceptance, § 2-608(1)(b), provided that Mercury revokes within a reasonable time after it discovered or should have discovered the nonconformity and that Mercury timely notifies GM of its revocation, § 2-608(2). Following revocation, Mercury can sue GM for any damages due to nonconformity allowed by § 2-714.

If Mercury did not discover the nonconformity in time to revoke acceptance, or if Mercury elected not to revoke, it could pursue GM for breach of warranty. The unfit tubing would appear to violate the implied warranty of merchantability, § 2-314, plus any express warranty that GM might have made to Mercury regarding the quality of the tubing, § 2-313. Let's start with the latter. The facts do not indicate that GM made any express warranty. Unless the facts are incomplete, Mercury would appear to have no recourse under § 2-313. What about the IWOM? GM's acknowledgment disclaims all implied warranties. Mercury's PO is silent on implied warranties. Therefore, GM's warranty disclaimer is an additional, rather than different term, for purposes of § 2-207. As discussed above, both parties are merchants. Thus, we look to § 2-207(2) to determine whether the warranty disclaimer is part of the parties' contract. As discussed in I.A, a disclaimer of implied warranties "materially alters" the original bargain, per § 2-207 cmt. 4; and, therefore, does not become a part of the parties' contract. So, absent an effective disclaimer, GM is bound by the IWOM, and Mercury can sue to recover those damages permitted for breach of warranty by § 2-714(2).

- E. Same facts as “D,” except that GM’s acknowledgment clearly stated that it would accept Mercury’s purchase order only on the condition that Mercury agree to all terms set forth in GM’s acknowledgment. Assuming, for purposes of this subpart, that GM and Mercury had an enforceable contract, should Mercury prevail against GM on a claim of breach of warranty? Please explain.**

Yes. GM’s acknowledgment disclaims all implied warranties. GM’s acknowledgement also makes its acceptance expressly conditional on Mercury’s assent to GM’s new terms. As a consequence, GM’s acknowledgement is not an acceptance, but a counteroffer. § 2-207(1). Now for Mercury to have a valid IWOM claim against GM, we must find that a contract was formed under § 2-207(3) – that is, by the parties’ actions, rather than their correspondence. Here, GM shipped the tubing without having received either an assent or objection from Mercury, and Mercury took delivery of and paid for the tubing, despite being aware of GM’s warranty disclaimer. These actions are “[c]onduct by both parties which recognizes the existence of a contract ... although the writings of the parties do not otherwise establish a contract.” § 2-207(3). Therefore, the terms of the contract are those on which the writings agree – here, price, quantity, identity of the goods, and delivery deadline – plus any necessary UCC “gap-fillers.” One such gap-filler is the IWOM.

- F. Same facts as “D,” except that, after discovering the inferior glass tubing, Mercury made arrangements to return the unfit tubing to GM. While the tubing was en route from Mercury’s plant back to GM’s, the truck overturned and all of its contents were destroyed. Assuming, for purposes of this subpart, that GM and Mercury had an enforceable contract, who would bear the risk of loss for the destroyed tubing and to what extent? Please explain.**

Because Mercury was obligated to pay transportation costs, this was a shipment contract. Risk of loss would normally shift to Mercury once GM (1) made a “reasonable” contract with a third-party carrier; (2) gave possession of the goods to the carrier; (3) provided Mercury with any documents necessary for Mercury to take possession of the goods from the carrier; and (4) promptly notified Mercury that the goods had been shipped. § 2-504. Mercury would then be liable for any damage or destruction of the goods in transit, § 2-509(1)(a), or thereafter. This is not a normal case. Here, the entire shipment of goods was received undamaged by Mercury, but 80% of the shipment was nonconforming. Under § 2-510(1), if the delivery “so fails to conform to the contract as to give a right of rejection,” GM continues to bear the risk of loss until Mercury accepted the goods or until GM cured the nonconformity. If Mercury had accepted the nonconforming tubing, but then properly revoked, then GM would bear the risk of loss to the nonconforming tubing to the extent of any deficiency in Mercury’s insurance. § 2-510(2). So, the question here is whether Mercury rejected or revoked. If Mercury rejected, GM bears the entire loss. If Mercury revoked, GM bears the risk of any loss that exceeds Mercury’s insurance.

5. On May 5, 2006, Hester Quill, a law professor at Sagebrush State University, located in the western United States, received an e-mail from Quality Books (“QBooks”), an internet book reseller specializing in books about law and related fields, whose booth Hester had visited at the Western Law Schools Association’s annual meeting in San Diego earlier this year. Among the items advertised in QBooks’s e-mail (Item # 164258) was a “Signed first edition of Charles W. Kingsfield, Jr.’s most famous and rarest book, *The “Hairy Hand” and Other Ruminations on Contract*, published by the Harvard Law Review Association, Cambridge, Massachusetts in celebration of its 75th anniversary (1962).” The e-mail indicated the “list price” of the book was US\$500.00 and that, until June 30, 2006, the “sale price” of the book was US\$400.00.

The order form included with the e-mail indicated that recipients could order advertised books by completing the online order form at http://www.qbooks.com/store/order_form.htm or by printing out the order form included with the e-mail and faxing it to 1-877-LAW-BOOK. Nothing in the e-mail indicated, nor did its toll-free number disclose, QBooks’s physical location. The online order form, likewise, did not indicate QBooks’s physical location. However, clicking on the “Terms of Use” link on Quality’s home page (<http://www.qbooks.com>), and then reading through the numerous terms and conditions, would eventually lead the reader to the following:

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On May 6, 2006, using the online order form and a credit card, and without ever reading QBooks’s Terms of Use but clicking “I Agree” when prompted to agree or disagree to be bound by QBooks’s Terms of Use, Hester ordered the book (Item # 164258) for \$400.00, plus \$9.95 shipping and handling, clicking “Purchase” when prompted to authorize QBooks to bill her credit card the amount indicated on the order form when QBooks’s shipped the book she ordered.

On May 6, 2006, QBooks sent Hester an e-mail indicating that it received her order and that it would send a follow-up e-mail when the book was ready to ship. On May 9, 2006, QBooks sent Hester an e-mail indicating that the book was ready to ship and providing a link to allow her to track the shipment’s progress. Following the link would lead Hester to a page on the shipping company’s website indicating that her shipment

originated in Burnaby, British Columbia. Likewise, the shipping documents accompanying the box, which Hester received on May 15, 2006, indicated that the shipment originated in Burnaby, British Columbia. The day after QBooks shipped Hester's book, it billed Hester's credit card in the amount of \$409.95.

A. What law should govern Hester's transaction with QBooks and any dispute that might arise from it? Please explain.

The book is a tangible, movable object. Therefore it is a good, § 2-105(1), and UCC Article 2 will govern its sale, § 2-102, unless the CISG preempts Article 2. Hester is located in the U.S. QBooks shipped the book from Canada. However, Hester did not order the book from QBooks' Canadian warehouse, she ordered it from QBooks. All of Hester's personal contacts with QBooks had occurred in the U.S. The book was advertised on a web site that, elsewhere on the same site, indicated that QBooks' place of business was in Washington state. Therefore, the CISG should not preempt Article 2 because (1) QBooks' relevant place of business (per CISG art. 10) was in Washington, or (2) even if QBooks' relevant place of business was in Canada, Hester did not know or have reason to know that she was dealing with a Canadian entity (per CISG art. 1(2)), and, in any event, (3) Hester purchased the book for her personal use, taking its sale outside the scope of the CISG (per CISG art. 2(a)) – unless QBooks neither knew nor had reason to know at any relevant time that Hester was purchasing the book for her personal use.

B. At what point in time did Hester and QBooks have an enforceable contract such that, if QBooks did not fill Hester's order, she would have a breach of contract claim against QBooks and, if Hester did not pay for the book she ordered, QBooks would have a breach of contract claim against her? Please explain.

QBooks' e-mail was an invitation to offer. Hester offered when she submitted her purchase order. QBooks accepted when it promptly shipped the book in response to Hester's purchase order. § 2-206(1)(b).

Each party sent the other electronically-signed records evidencing the contract for the book. Collectively, they would satisfy the relevant statute of frauds (§ 2-201) – except that the price of the book was too low to trigger the relevant statute of frauds.

C. If the book was lost or destroyed in transit from QBooks to Hester, who would bear the risk of loss under that governing law? Please explain.

Hester paid \$9.95 for shipping and handling. That suggests that this is a shipment contract and that Hester bore the risk of loss once QBooks made a reasonable contract for the book's transport, delivered the book to the carrier, and notified Hester that the book was on its way. See §§ 2-319(1)(a), 2-504 & 2-509(1)(a). However, the mere fact that Hester paid \$9.95 per item (or per order) for shipping and handling does not make this a shipment contract for which she bore the risk of loss. (Suppose that the \$9.95 shipping and handling charge was per order, and Hester ordered 20 books, which QBooks had to ship from five different warehouses, racking up transport costs well in excess of \$9.95.) In the absence of language requiring or authorizing QBooks to ship the book by carrier, risk of loss passes from a merchant seller to a

buyer when the buyer receives the goods. § 2-509(3). Where in the language of the purchase order, Terms of Use, or order acknowledgement described above is the passage requiring or authorizing QBooks to ship the goods by carrier? See § 2-509(1). If you can find it, you have a keener eye than me.

Thus, absent some contract language authorizing QBooks to ship by carrier and shift the risk of loss to Hester once QBooks made a reasonable contract for the book's transport, delivered the book to the carrier, and notified Hester that the book was on its way, QBooks bore the risk of loss until Hester received the book.

When her box arrived, Hester opened it and found inside a first edition of Kingsfield's, *Ruminations*. When she turned to the frontispiece, however, she saw that the book was signed by "James Hart, HLS Class of '73" rather than Kingsfield, making the book considerably less valuable both to "the market" and to Hester.

D. Assuming that Hester had an otherwise enforceable contract with QBooks, on what ground or grounds, if any, can Hester avoid her contract with QBooks, return the book they sent her, and demand that QBooks send her the correct book immediately or issue her a refund? Please explain.

QBooks stated that the book was a "Signed first edition of Charles W. Kingsfield, Jr.'s most famous and rarest book, *The "Hairy Hand" and Other Ruminations on Contract*, published by the Harvard Law Review Association, Cambridge, Massachusetts in celebration of its 75th anniversary (1962)." While that statement is technically true – after all, *someone* had signed the book – a reasonable person in Hester's position would assume that QBooks was representing that *the author* (Kingsfield) had signed the book. Therefore, Hester should be able to **reject** the books as nonconforming. § 2-602. If Hester failed to properly reject in a timely fashion, she would likely not be able to revoke because the nonconformity, while arguably substantial, was easy to detect when she received the book and she accepted anyway. § 2-608.

By making a misleading statement of fact that, undoubtedly, was part of the basis of the bargain, QBooks may have breached an **express warranty**. § 2-313. Because QBooks is a merchant, and must perform its contracts in good faith, Hester could argue that selling her a book signed by someone other than the author, at a price that reflected the market value of a copy signed by the author, breached QBooks' duty of **good faith**, § 1-203, entitling Hester to reject QBooks' nonconforming delivery, § 2-601. Because QBooks is a merchant, it also makes an **implied warranty of merchantability** that the books it sells, *inter alia*, will pass without objection in the trade *under the contract description*. § 2-314(2)(a).

Hester also has grounds to avoid the contract based on material **mistake**, material **misrepresentation**, and, possibly, **frustration of purpose**. UCC § 1-103 incorporates these common law defenses into Article 2 by reference. Frustration of purpose is a bit tricky, because Hester will have to prove that her principal purpose in purchasing the book was to have a copy signed by Kingsfield and that the book being signed by someone else instead was an "event the non-occurrence of which was a basic assumption on which the contract was made." R2 § 265.

After receiving her shipment from QBooks, Hester visited online bookseller Nile.com's website and found another first edition of Kingsfield's *Ruminations* "Signed by author" advertised for \$600.00.

E. If, instead of promptly notifying QBooks of its error and demanding that QBooks send her the correct book immediately or issue her a refund, Hester purchased the more expensive book from Nile.com and then sued QBooks because she ended up having to pay more for a first edition signed by Kingsfield, on what ground or grounds could QBooks avoid liability to Hester for breach of contract? Please explain.

Section 2-602(1) requires Hester to timely notify QBooks of any nonconformity. Armed with such notice, QBooks could attempt to cure by seasonably making a conforming delivery (at QBooks's expense). § 2-508(1). By failing to notify QBooks before she purchased a book from another seller, Hester has deprived QBooks of its statutory right to cure and may have accepted QBooks's book by not properly rejecting it in a timely manner, § 2-606(1)(b), in which case Hester would breach by not paying QBooks at least the fair market value of the book QBooks sent her.