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### Uniform Commercial Code Survey: Sales

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## Sales

By Robyn L. Meadows, Keith A. Rowley, Larry T. Garvin, and Carolyn L. Dessin\*

### SCOPE OF ARTICLE 2

Last year's survey noted a trend among courts treating the sale of prepackaged software primarily as a sale of goods but the sale of custom software primarily as a contract for services.<sup>1</sup> In *Mortgage Plus, Inc. v. DocMagic, Inc.*,<sup>2</sup> the court put a bit of a gloss on that trend, holding that an agreement consisting of both a software license and ongoing document preparation services was predominantly a contract for services governed by common law because the software was "worthless without the actual loan preparation services."<sup>3</sup>

In *Lohman v. Wagner*,<sup>4</sup> the court concluded that a contract to raise and sell weaner pigs was a contract for the sale of goods, despite the services involved in tending the pregnant sows during gestation, helping birth, and caring for the newborn piglets until they were ready for delivery to a buyer. The court reasoned that "those services were all incidental to the eventual delivery of the specified pigs and did not constitute the main thrust or predominant purpose of the agreement" which was "the purchase and sale of young pigs."<sup>5</sup>

### CONTRACT FORMATION

In *Bio-Tech Pharmacal, Inc. v. International Business Connections, LLC*,<sup>6</sup> Bio-Tech, a manufacturer of nutritional supplements, purchased raw materials from IBC approximately seventeen times over a four-month period beginning in September 1999. Typically, the parties would discuss availability and price over the telephone.

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1. See Robyn L. Meadows, Carolyn L. Dessin & Larry T. Garvin, *Uniform Commercial Code Survey: Sales*, 59 *BUS. LAW.* 1557, 1558 (2004).

2. 55 U.C.C. Rep. Serv. 2d (West) 58 (D. Kan. 2004).

3. *Id.* at 61-62.

4. 862 A.2d 1042, 54 U.C.C. Rep. Serv. 2d (West) 1057 (Md. Ct. Spec. App. 2004), *cert. denied*, 869 A.2d 865 (Md. 2005).

5. *Id.* at 1047-48, 54 U.C.C. Rep. Serv. 2d (West) at 1064. Both unborn and young pigs are Article 2 "goods." See U.C.C. § 2-105(1) & cmt. 1 (2001).

6. 53 U.C.C. Rep. Serv. 2d (West) 476 (Ark. Ct. App. 2004).

If they reached an agreement, Bio-Tech would issue a purchase order to IBC, which in turn would purchase the desired materials from its own supplier. Once IBC received the materials from its supplier, it would send Bio-Tech an invoice that referenced Bio-Tech's purchase order. Bio-Tech would confirm its receipt of IBC's invoice by telephone. IBC would ship and Bio-Tech would receive and pay for the invoiced materials "without protest or complaint."<sup>7</sup>

The parties' relationship began to break down in early 2000 when Bio-Tech attempted to cancel several orders by writing "CANCEL" across copies of purchase orders previously sent and faxing them to IBC. IBC eventually sued Bio-Tech for the unpaid balances due on three of these purchase orders. Bio-Tech denied liability, arguing that there was no contract because its purchase orders were offers that IBC could accept only by faxing or e-mailing a confirmation, which it had not done. The trial court found for IBC. The court of appeals affirmed, noting that, while purchase orders generally constitute offers, the ones here might well be either acceptances of a telephonic offer or confirmations of an oral agreement reached on the phone.<sup>8</sup> Even if they were offers, under section 2-206 such offers invite acceptance in any manner and by any reasonable medium; thus, IBC was not restricted to accepting the offers by faxed or e-mailed confirmation.

## STATUTE OF FRAUDS

In *Propulsion Technologies, Inc. v. Attwood Corp.*,<sup>9</sup> PowerTech purchased propeller castings from Attwood, which PowerTech used to manufacture boat propellers for sale to third parties. After Attwood notified PowerTech that it was terminating their supply agreement with less notice than the parties' letter agreement required, PowerTech sued. Attwood defended on the ground that the contract was unenforceable under section 2-201.<sup>10</sup> The district court concluded that the agreement was primarily for the purchase of Attwood's services, rather than for goods, and thus the statute of frauds did not apply. It entered judgment in PowerTech's favor based on the jury's finding that Attwood had breached.

The Fifth Circuit reversed, holding that, because specially-manufactured goods are expressly included in the definition of "goods" in section 2-105,<sup>11</sup> contracts for the sale of specially-manufactured goods are, as a matter of law, transactions in goods within the scope of Article 2, notwithstanding the labor and expertise involved in designing and fabricating an item that "is custom designed for the buyer's needs and is not readily marketable to others."<sup>12</sup> It then held that the letter agreement between the parties failed to satisfy section 2-201 because it neither stated a specific quantity nor substituted PowerTech's requirements for a specific

7. *Id.* at 477.

8. *See id.* at 479-80.

9. 369 F3d 896, 53 U.C.C. Rep. Serv. 2d (West) 466 (5th Cir. 2004) (applying Texas law).

10. *See* Appellant-Cross-Appellee's Opening Brief in *Propulsion Technologies, Inc. v. Attwood Corp.*, 369 F3d 896, 53 U.C.C. Rep. Serv. 2d (West) 466 (5th Cir. 2004), available at 2003 WL 23917174.

11. *See* U.C.C. § 2-105(1) (2001).

12. *Propulsion Technologies*, 369 F3d at 901, 53 U.C.C. Rep. Serv. 2d (West) at 469.

quantity term.<sup>13</sup> Inexplicably, the court completely overlooked the specially-manufactured goods exception in section 2-201(3)(a).<sup>14</sup>

*Lohman v. Wagner*, discussed above, also involved a statute of frauds defense. The only writing in the case indicated that the seller (Lohman) would “supply approximately \_\_\_ weaner pigs weekly” to the buyer (Wagner).<sup>15</sup> The trial court refused to enforce the purported agreement because it did not contain a quantity term. On appeal, Lohman argued that the quantity term requirement in section 2-201(1) is intended only to limit enforcement to the extent of the quantity stated, not to bar enforcement in its absence and, alternatively, that the parties’ agreement was an output contract, exempt from stating a specific quantity. The appellate court rejected both arguments and held that the alleged agreement was unenforceable.<sup>16</sup>

### TERMS OF THE CONTRACT

In *Todd Heller, Inc. v. Indiana Department of Transportation*,<sup>17</sup> Heller contracted to supply INDOT with glass beads for use in reflective traffic paint. The contract required the beads to conform to AASHTO M 247-81, an industry standard for moisture resistance and adhesion. Prior to delivery, Heller tested the beads, using an industry-standard testing procedure, to confirm that they conformed to M 247-81. Following receipt, INDOT tested the beads using a different procedure and rejected several batches. Heller retested the rejected beads and found that all of the rejected batches conformed. When Heller demonstrated the industry-standard procedure to INDOT’s senior chemist, the beads again conformed. Independent testing by the Pennsylvania Department of Transportation (“Penn DOT”) confirmed Heller’s results. Nevertheless, INDOT cancelled its agreement with Heller, citing the repeated failure of Heller’s beads to pass INDOT’s testing. Heller sued INDOT for breach of contract and lost at trial. Heller appealed.

A majority of the Indiana Court of Appeals held that the terms of parties’ agreement could be explained or supplemented by usage of trade.<sup>18</sup> Therefore, despite contractual language requiring Heller to be familiar with INDOT’s sampling, testing, and reporting methods,<sup>19</sup> the majority held that Heller had used an industry-standard testing method and that “the existence of a usage of trade in the glass beads industry dictating how the test is to be performed trump[ed] INDOT’s ‘discretionary’ interpretation of the test method.”<sup>20</sup> Therefore, the trial court erred in concluding that there was no relevant trade usage and that INDOT was free to test Heller’s beads by whatever method it chose.

13. *Id.* at 904–05, 53 U.C.C. Rep. Serv. 2d (West) at 468, 473.

14. U.C.C. § 2-201(3)(a) (2001).

15. *See Lohman*, 862 A.2d at 1045, 54 U.C.C. Rep. Serv. 2d (West) at 1060.

16. *Id.* at 1048–49, 54 U.C.C. Rep. Serv. 2d (West) at 1065–67.

17. 819 N.E.2d 140, 55 U.C.C. Rep. Serv. 2d (West) 464 (Ind. Ct. App. 2004).

18. *Id.* at 146, 55 U.C.C. Rep. Serv. 2d (West) at 471 (citing IND. CODE §§ 26-1-2-105(1) & -202).

19. *See id.* at 141–42, 55 U.C.C. Rep. Serv. 2d (West) at 465.

20. *Id.* at 148 n.3, 55 U.C.C. Rep. Serv. 2d (West) at 473 n.3.

In dissent, Judge Vaidik focused on the language in the Heller-INDOT agreement requiring Heller to “be familiar with INDOT’s testing methods.” She construed this language to trump the trade usage on which Heller and the majority relied.<sup>21</sup> While the majority opinion does not address Judge Vaidik’s conclusion, it might not be irreconcilable with the majority’s opinion. The express terms of the contract required Heller to “be familiar with” INDOT’s testing methods, not to *follow* or *satisfy* INDOT’s testing methods. Indeed, one could easily argue that Heller made a good faith effort to educate INDOT on how to perform the tests and that INDOT’s refusal to accept the results of Heller’s industry-standard testing was contrary to INDOT’s duty to perform its contract with Heller in good faith.

In 1990, the parties in *RGJ Associates, Inc. v. Stainsafe, Inc.*<sup>22</sup> entered into a letter agreement whereby Stainsafe would purchase from Williamsville all of the furniture care products Stainsafe needed for the domestic retail market. In 1998, Stainsafe decided to produce its own leather furniture care products and so informed Williamsville, which continued supplying Stainsafe with wood, fabric, and lacquer furniture care products until May 2001, when Stainsafe ceased paying for products. Williamsville then withheld further shipments and Stainsafe filed suit.<sup>23</sup> Finding that the letter agreement was only partially integrated,<sup>24</sup> the trial court allowed extrinsic evidence regarding the parties’ course of performance and any relevant trade usages to explain or supplement the terms of the written agreement—most particularly, the scope of Stainsafe’s obligation to promote Williamsville’s “product line.” In doing so, the court correctly ruled that “[a] sale contract need not be ambiguous for the admission of evidence of course of dealing, course of performance, or usage of trade.”<sup>25</sup>

## BATTLE OF THE FORMS

Courts continue to encounter—and, at times, struggle with—section 2-207. For example, in *Montgomery Rubber & Gasket Co. v. Belmont Machinery Co.*,<sup>26</sup> Belmont orally offered to sell a boring mill to Montgomery for \$29,500. This price included having Belmont rewire the machine and allowing Montgomery to inspect it before Belmont shipped it to Montgomery. Montgomery orally replied that it would pay Belmont \$25,000 for the boring mill, would forego preshipment in-

21. See *id.* at 150 (citing IND. CODE § 26-1-1-205(4)) (Vaidik, J., dissenting) (The editors of the *Uniform Commercial Code Reporting Service* did not publish Judge Vaidik’s dissent.).

22. 338 F. Supp. 2d 215 (D. Mass. 2004).

23. See *id.* at 226–32.

24. See *id.* at 244–45.

25. *Id.* at 243; see also U.C.C. § 2-202 cmt. 1(c) (2001) (“This section definitely rejects . . . [t]he requirement that a condition precedent to the admissibility of the type of evidence specified in paragraph (a) is an original determination by the court that the language used is ambiguous.”).

Not every court grasps that U.C.C. § 2-202 does not require a court to inquire whether the written agreement is ambiguous, much less find ambiguity, before considering the admissibility of extrinsic evidence. See, e.g., *Benedict Mfg. Co. v. Aeroquip Corp.*, 53 U.C.C. Rep. Serv. 2d (West) 888, 891 (Mich. Ct. App. 2004) (per curiam) (describing “whether contract language is clear or ambiguous” as “the threshold issue” in interpreting a sales contract (emphasis added)). The *RGJ Associates* court clearly got this point right.

26. 308 F. Supp. 2d 1293 (M.D. Ala. 2004).

spection, and would either wire the machine itself or make arrangements for a third party to do so. Belmont then faxed Montgomery a confirmation of Montgomery's terms, and Montgomery tendered payment to the party Belmont designated.<sup>27</sup> The district court rightly concluded that a contract existed between Belmont and Montgomery. However, rather than finding that the parties reached an oral agreement that Belmont confirmed with its fax, or that Belmont's fax accepted Montgomery's oral counteroffer, the court, ignoring the language of section 2-207(1), ruled that Belmont's fax was a counteroffer—despite the fact that it did not contain any language expressly conditioning its effect on Montgomery's acquiescence to any additional or different terms contained therein nor did it contain any additional or different terms.<sup>28</sup>

## WARRANTIES AND DISCLAIMERS

### IMPLIED WARRANTIES

In a case of first impression, the New York Supreme Court held that a restaurant patron could maintain an action for breach of the implied warranty of merchantability<sup>29</sup> for injuries sustained when a complimentary glass of water served with a meal allegedly broke in the customer's hand.<sup>30</sup> The restaurant moved for summary judgment arguing the restaurant was not in the business of selling water or glasses. The court denied the restaurant's motion, reasoning that although the water was provided free of charge, it was an indispensable part of the meal, the cost of which was presumably built into customers' bills, and thus a sale of the water had occurred.<sup>31</sup> On the issue of whether the warranty extended to the glass, the court, relying on two similar cases from other jurisdictions,<sup>32</sup> ruled that, if the glass in which the water was served was defective, then the water was not adequately contained or packaged as required for a good to be merchantable.<sup>33</sup>

27. *See id.* at 1295, 1300.

28. *See id.* at 1300. The court reasoned that, while Belmont's fax contained essentially the same terms Montgomery proposed, "the content of the fa[x] demonstrates that it was intended to be a counteroffer, not an acceptance. The document is entitled 'proposal,' refers to the terms as a 'quote,' and states that the machine 'is offered subject to prior sale.'" *Id.* at 1300 n.11.

29. *See* U.C.C. § 2-314(1) (2001) (providing that "[t]he serving for value of food or drink to be consumed either on the premises or elsewhere" gives rise to the implied warranty).

30. *Gunning ex rel. Gunning v. Small Feast Caterers, Inc.*, 777 N.Y.S.2d 268, 53 U.C.C. Rep. Serv. 2d (West) 502 (N.Y. Sup. Ct. 2004).

31. *Id.* at 271, 53 U.C.C. Rep. Serv. 2d (West) at 504.

32. *See Levondosky v. Marina Associates*, 731 F. Supp. 1210, 1213, 11 U.C.C. Rep. Serv. 2d (Callaghan) 487 (D.N.J. 1990) (holding casino that served complimentary drink to gambling patron could be liable for breach of implied warranty of merchantability when patron swallowed glass chips from rim of glass because gambling by patron was value given for drink and container must be fit for ordinary purpose); *Shaffer v. Victoria Station, Inc.*, 588 P.2d 233, 234–35, 25 U.C.C. Rep. Serv. (Callaghan) 427 (Wash. 1978) (holding that a wine glass that broke when served to a customer made the wine not adequately contained or packaged, and thus not merchantable).

33. *See Gunning*, 777 N.Y.S.2d at 271, 53 U.C.C. Rep. Serv. 2d (West) at 504; *see also* U.C.C. § 2-314(2)(e) (2001) ("Goods to be merchantable must be . . . adequately contained, packaged, and labeled as the agreement may require . . .").

In *Spain v. Brown & Williamson Tobacco Corp.*,<sup>34</sup> the Eleventh Circuit held that the Federal Cigarette Labeling and Advertising Act (FCLAA)<sup>35</sup> did not preempt a smoker's estate's claim that cigarettes were not fit for their ordinary purpose and, therefore, not merchantable under Article 2. The district court granted the cigarette manufacturer's motion to dismiss all claims and the estate appealed. On the issue of the breach of the implied warranty, the Eleventh Circuit noted that the Alabama Supreme Court, in answer to the court's earlier certified question, opined that the estate could state a valid claim that the cigarettes breached the implied warranty of merchantability by alleging cigarettes were not fit for the ordinary purpose for which they were used.<sup>36</sup> Because a determination as to breach of the warranty of merchantability is "fact-intensive," and the record contained no evidence that the cigarettes smoked by the deceased were fit, the district court erred in dismissing the merchantability claim. Moreover, the court ruled that the FCLAA did not preempt the estate's merchantability claims because the implied warranty does not impose any duty or obligation on the manufacturer "with respect to advertising or promotion" as required by the FCLAA. The legal duty imposed by the warranty is to not market unsafe products, not to warn that one is doing so.<sup>37</sup>

In an interesting case involving the proper method for disclaiming implied warranties, the Indiana Court of Appeals held that a car dealer had validly disclaimed all implied warranties. In *Wilson v. Royal Motor Sales, Inc.*,<sup>38</sup> the court addressed whether a disclaimer on the back of a purchase agreement was conspicuous. For a year and a half, the car purchased by the plaintiff from the defendant dealer had many problems. Finally, the buyer stopped driving the car, notified the dealer she was revoking her acceptance of the car, and then filed suit alleging breach of the implied warranty of merchantability. The trial court granted the dealer's motion for summary judgment, concluding that the dealer had disclaimed the warranty. On appeal, the buyer argued that the window sticker on the car at the time of purchase did not indicate the car was being sold "As Is," merely that it was being sold with a factory warranty. However, the purchase agreement she signed indicated that she had read the back of the agreement. The back of the agreement included the following: "THIS VEHICLE IS SOLD 'AS IS—NOT EXPRESSLY WARRANTED OR GUARANTEED' AND THE SELLER HEREBY DISCLAIMS ALL WARRANTIES, INCLUDING ANY IMPLIED WARRANTY OF MERCHANTABILITY OR FITNESS FOR A PARTICULAR PURPOSE."<sup>39</sup> Additionally, the purchase agreement provided, in all capital letters, that all warranties were the manufacturer's or supplier's and not the dealer's and that only the manufacturer or supplier would be liable for the warranties and not the dealer. The appellate court concluded that language on the back of a written agreement is

34. 363 F.3d 1183 (11th Cir. 2004) (applying Alabama law).

35. 15 U.S.C. § 1334(b) (2000).

36. *Spain*, 363 F.3d at 1198 (citing *Spain v. Brown & Williamson Tobacco Corp.*, 872 So. 2d 101, 50 U.C.C. Rep. Serv. 2d (West) 1091 (Ala. 2003)).

37. *Id.* at 1199.

38. 812 N.E.2d 133, 54 U.C.C. Rep. Serv. 2d (West) 473 (Ind. Ct. App. 2004).

39. *Id.* at 134, 54 U.C.C. Rep. Serv. 2d (West) at 474.

conspicuous if it is printed in a conspicuous manner, such as in bold or capitalized text larger than the surrounding text.<sup>40</sup> It then concluded that the language used in this case did not conflict with the language on the window sticker and satisfied the requirements of section 2-316(2).<sup>41</sup>

### EXPRESS WARRANTIES

In *Sharp v. Tamko Roofing Products, Inc.*,<sup>42</sup> the court considered whether claims made in advertising created express warranties. Plaintiffs owned homes on which the defendant manufacturer's shingles had been used. The homeowners alleged the shingles did not seal properly and therefore blew off of roofs and were subject to cracking, curling, excessive deterioration, and premature aging. The homeowners sued for breach of express and implied warranties in addition to other common law and statutory claims. The shingles came with a manufacturer's express limited warranty of twenty-five or thirty years, depending on the type of shingles used, through which the manufacturer would pay only a prorated amount for the shingles, based on the shingles' age. The plaintiffs' express warranty claim was not based on this limited warranty, but on statements made in the product brochures and advertisements, such as "proven to last a long, long time," "long lasting," "years of maintenance free protection," and "durable."<sup>43</sup> Although general statements such as these seem more properly regarded as classic puffery than as something that rises to the level of a warranty,<sup>44</sup> the court did no more than suggest this, instead relying on the fact the plaintiffs failed to present any evidence that the plaintiffs relied on the statements in purchasing the shingles.<sup>45</sup> The court held that, to prove breach of an express warranty, there must be evidence that "the sale would not have been made but for the representations."<sup>46</sup> The court equated the "basis of the bargain" requirement in section 2-313(1)(a) with reliance,<sup>47</sup> a questionable determination given the official comments to section 2-313,<sup>48</sup> but perhaps

40. *Id.* at 137, 54 U.C.C. Rep. Serv. 2d (West) at 476-77 (discussing the definition of "conspicuous" in Indiana's version of pre-revised U.C.C. § 1-201(10)).

41. *See id.* at 137-39, 54 U.C.C. Rep. Serv. 2d (West) at 477-79.

42. 55 U.C.C. Rep. Serv. 2d (West) 226 (Iowa Ct. App. 2004).

43. *Id.* at 228.

44. For a case finding statements such as "premium quality," "a masterpiece," and "ready to take you thundering down the road" constituted classic advertising puffery and therefore could not be the basis of a deceptive trade practices claim, see *Tietsworth v. Harley-Davidson, Inc.*, 677 N.W.2d 233, 246, 53 U.C.C. Rep. Serv. 2d (West) 721, 735 (Wis. 2004).

45. *See Sharp*, 55 U.C.C. Rep. Serv. 2d (West) at 228-29.

46. *Id.* at 229.

47. *See id.*

48. U.C.C. § 2-313 cmt. 2 (2001) (noting "no particular reliance" on statements made during the bargain need be shown and any fact that takes statements out of the agreement requires "clear affirmative proof"); *see also, e.g., Felley v. Singleton*, 705 N.E.2d 930, 934, 37 U.C.C. Rep. Serv. 2d (West) 586, 591 (Ill. Ct. App. 1999) ("[R]epresentations by the seller such as the car 'is in good mechanical condition' are presumed to . . . become part of the bargain . . . unless the seller shows by clear affirmative proof that the representations did not become part of the basis of the bargain."). *But see, e.g., Hillcrest Country Club v. N.D. Judds Co.*, 461 N.W.2d 55, 61, 12 U.C.C. Rep. Serv. 2d (Callaghan) 990, 999 (Neb. 1990) ("Since an express warranty must have been 'made part of the basis of the bargain,' it is essential that the plaintiffs prove reliance upon the warranty." (quoting *Wendt v. Beardmore Suburban Chevrolet*, 366 N.W.2d 424, 428 (Neb. 1985))).



justified in this case given there was no evidence the consumer plaintiffs had ever seen the brochures or advertising.

### PRIVITY

In several cases, courts considered whether Article 2 warranties protected persons other than the immediate buyer. In *Fortune View Condominium Ass'n v. Fortune Star Development Co.*,<sup>49</sup> a general contractor sued the manufacturer of an allegedly defective siding system used by the contractor in a condominium project. The general contractor asserted a breach of warranty claim based on express warranties created by statements in the manufacturer's brochures. These brochures contained information on the physical properties of the siding system, including test results for water penetration and resistance. The brochures also indicated that the siding was designed for use in the residential and light commercial markets and included a five-year limited warranty. The contractor was shown the brochures by the distributor of the siding systems, who sold the system to the siding subcontractor. By affidavit, the general contractor testified that it relied on the brochures when submitting its bid for the condominium project. Based on these warranties, the general contractor sought indemnity from the siding manufacturer and the subcontractor for any liability it may have to the condominium association or developer for damages caused by defects in the siding. The trial court granted summary judgment in favor of the siding manufacturer and the subcontractor. Affirming the court of appeals' reversal of the summary judgment in favor of the manufacturer, the Washington Supreme Court noted that, unlike implied warranties, express warranties created by advertising do not require privity of contract.<sup>50</sup> A majority of the court ruled that the general contractor's claim for implied indemnity based on the manufacturer's express warranties, likewise, did not require privity of contract.<sup>51</sup>

In *Inter Impex S.A.E. v. Comtrade Corp.*,<sup>52</sup> a federal district court ruled that New York law requires privity of contract in cases which do not involve personal injury. It therefore dismissed claims against a manufacturer for breach of express and implied warranties for improper packaging. Finding the manufacturer was not a party to the sales agreement and had made no warranties directly to the buyer, the court held the buyer could not recover damages for economic loss arising from breach of warranty.<sup>53</sup>

49. 90 P.3d 1062, 53 U.C.C. Rep. Serv. 2d (West) 792 (Wash. 2004).

50. See *id.* at 1064 n.3, 53 U.C.C. Rep. Serv. 2d (West) at 795 n.3. The Washington Supreme Court did not decide whether the manufacturer's brochures contained express warranties. See *id.* at 1064, 53 U.C.C. Rep. Serv. 2d (West) at 794-95.

51. See *id.* at 1065-66, 53 U.C.C. Rep. Serv. 2d (West) at 796-97.

52. No. 00 Civ. 0133 (GBD), 2004 WL 2793213 (S.D.N.Y. Dec. 6, 2004).

53. See *id.*, 2004 WL 2793213, at \*\*4-5.

## CONTRACT PERFORMANCE

There were several interesting cases this year on acceptance, rejection, and revocation. In *Dan J. Sheehan Co. v. Ceramic Technics, Ltd.*,<sup>54</sup> Sheehan ordered \$178,532.32 worth of tiles from Ceramic, which Ceramic shipped to Sheehan, and Sheehan promptly installed in a shopping mall food court. Despite installing all of the tiles it ordered from Ceramic, Sheehan paid Ceramic only \$124,532.32. When Ceramic sued for the unpaid balance of \$54,000, Sheehan answered that some of the tiles were nonconforming. The trial court granted summary judgment in favor of Ceramic and Sheehan appealed. The court of appeals affirmed, holding that (1) Sheehan failed to timely notify Ceramic of any allegedly nonconforming tiles;<sup>55</sup> and (2) Sheehan accepted the allegedly nonconforming tiles by installing them in the food court, an act inconsistent with Ceramic's continued ownership of the tiles.<sup>56</sup>

In *Montgomery Rubber & Gasket Co. v. Belmont Machinery Co.*, discussed above,<sup>57</sup> the district court denied the seller's (Belmont) motion for summary judgment on the ground that the buyer (Montgomery) had accepted the boring mill under section 2-606(1)(b) by failing to timely reject, finding that (1) the timeliness of a buyer's rejection is generally a matter for the trier of fact; (2) a factual dispute existed regarding whether and how often Montgomery complained to Belmont about the boring mill's failure to perform before Montgomery attempted to reject; and (3) even if the court were to take as true Belmont's allegations that Montgomery did not complain for at least 90 days after receipt, "[b]ecause the boring mill required complicated assembly and new wiring, 90 days may have been required to give Montgomery . . . a reasonable time to inspect."<sup>58</sup>

In *H.A.S. of Fort Smith, LLC v. J.V. Manufacturing, Inc.*,<sup>59</sup> J.V. sold H.A.S. a linear press brake system and agreed to install it on November 10-12, 2000. J.V. did not actually begin installation until December 18, and was unable, over the next three weeks, to make the system work. On January 5, 2001, H.A.S. terminated the agreement and reinstalled the old system. Thereafter, H.A.S. asked J.V. to refund its down payment and to reimburse it for out-of-pocket costs incurred during J.V.'s failed attempt to install the new system. When J.V. refused to pay, H.A.S. sued and prevailed in a bench trial. The Arkansas Court of Appeals affirmed, holding that H.A.S. had properly revoked its acceptance of J.V.'s press brake system after J.V.'s efforts to cure<sup>60</sup> the problems with the press brake system proved unsuccessful. The only real question for the appellate court was whether H.A.S., despite the obvious substantial impairment, had waited too long after

54. 605 S.E.2d 375, 54 U.C.C. Rep. Serv. 2d (West) 523 (Ga. Ct. App. 2004), cert. denied, (Jan. 10, 2005).

55. *Id.* at 377, 54 U.C.C. Rep. Serv. 2d (West) at 525-26.

56. *See id.* at 378, 54 U.C.C. Rep. Serv. 2d (West) at 526; *see also* U.C.C. § 2-606(1)(c) (2001) (any act inconsistent with the seller's ownership of the goods constitutes an acceptance of the goods).

57. *See supra* text accompanying notes 26-28.

58. *Montgomery Rubber*, 308 F. Supp. 2d at 1301.

59. 54 U.C.C. Rep. Serv. 2d (West) 1007 (Ark. Ct. App. 2004).

60. *Id.* at 1015.

acceptance to revoke.<sup>61</sup> The court held that three weeks was not too long under the circumstances.<sup>62</sup>

In *Campbell v. Ag Finder Iowa Nebraska*,<sup>63</sup> Campbell contracted to sell his 1997 crop of "human food quality" organic soybeans "F.O.B. farm" to Ag Finder, which in turn contracted to resell Campbell's soybeans to Manna. Ag Finder took delivery of Campbell's soybeans and tendered them to Manna, which had them transported out of state. Upon receipt, Manna rejected the soybeans, because they were not "human food quality," and shipped them back to Ag Finder. When Ag Finder resold the soybeans for use as feed, and paid Campbell based on their value as feed, less Ag Finder's expenses incurred following Manna's rejection, Campbell sued for breach. Campbell prevailed in a bench trial, despite having tendered nonconforming soybeans, because the trial court found that Ag Finder accepted the soybeans without first testing them to see whether they were "human food quality" and failed to revoke its acceptance on grounds permitted by section 2-608. The Iowa Court of Appeals affirmed, holding that: (1) absent an effective rejection, Ag Finder must be deemed to have accepted Campbell's nonconforming soybeans;<sup>64</sup> and (2) because Ag Finder could have easily discovered the nonconformity before accepting the soybeans and did not fail to reject them due to any assurances by Campbell, Ag Finder could not revoke its acceptance.<sup>65</sup>

In *Smith v. Monaco Coach Corp.*,<sup>66</sup> the buyers of a Monaco motor home sought to revoke their acceptance after noticing a number of defects in the motor home that Monaco's authorized dealers were unable to repair. Recognizing a split of authority, the *Smith* court chose to follow *Kutzler v. Thor Industries, Inc.*,<sup>67</sup> which in turn followed the Virginia Supreme Court's decision in *Gasque v. Mooers Motor Car Co.*,<sup>68</sup> in holding that section 2-608 does not permit a buyer to revoke acceptance against a manufacturer that did not sell directly to the buyer.<sup>69</sup> Of course,

61. See U.C.C. § 2-608(2) (2001) ("Revocation of acceptance must occur within a reasonable time after the buyer discovers or should have discovered the ground for it and before any substantial change in condition of the goods which is not caused by their own defects. It is not effective until the buyer notifies the seller of it.")

62. *H.A.S. of Fort Smith*, 54 U.C.C. Rep. Serv. 2d (West) at 1014–15. Although the time period at issue here was much shorter, this case is reminiscent of *North American Lighting, Inc. v. Hopkins Manufacturing Corp.*, 37 F.3d 1253, 24 U.C.C. Rep. Serv. 2d (Callaghan) 1061 (7th Cir. 1994) (applying Illinois law). There, the court allowed the buyer to revoke acceptance nearly two years after the buyer purchased the seller's headlight aiming system—despite knowing that there were problems with the seller's prototype and despite using the system while the seller and some of the buyer's employees collaborated to try to resolve the unacceptably high error rate—because the buyer balked at revoking acceptance earlier due to the seller's continued assurances and apparent good faith efforts to cure. The buyer revoked acceptance only after it became clear that the system's flaws were incurable.

63. 53 U.C.C. Rep. Serv. 2d (West) 235 (Iowa Ct. App. 2004).

64. *Id.* at 238–40.

65. *Id.* at 240–41.

66. 334 F. Supp. 2d 1065 (N.D. Ill. 2004).

67. 51 U.C.C. Rep. Serv. 2d (West) 141 (N.D. Ill. 2003).

68. 313 S.E.2d 384, 38 U.C.C. Rep. Serv. (Callaghan) 120 (Va. 1984).

69. See *Smith*, 334 F. Supp. 2d at 1070. But see, e.g., *Larry J. Soldinger Assocs., Ltd. v. Aston Martin Lagonda of N. Am. Inc.*, No. 97 C 7792, 1999 WL 756174 (N.D. Ill. Sept. 13, 1999); *Durfee v. Rod Baxter Imports, Inc.*, 262 N.W.2d 349, 357, 22 U.C.C. Rep. Serv. (Callaghan) 945, 957–58 (Minn. 1977) (en banc); *Volkswagen of Am., Inc. v. Novak*, 418 So. 2d 801, 804, 34 U.C.C. Rep. Serv. (Callaghan) 1150, 1154 (Miss. 1982); *Ventura v. Ford Motor Corp.*, 433 A.2d 801, 811–12, 32 U.C.C.

a buyer may also lose the ability to revoke acceptance because of specific language in or incorporated into the sales contract effectively disclaiming warranties and prohibiting the buyer from returning the goods to the seller for any reason (at least in Michigan).<sup>70</sup>

Finally, a number of cases decided in 2004 turned on the timeliness of an injured party's notice to the seller or manufacturer of nonconforming goods.<sup>71</sup>

## BREACH OF CONTRACT

In *Indeck Energy Services, Inc. v. NRG Energy, Inc.*,<sup>72</sup> Indeck ordered three generator step-up transformers—used to change the voltage of electricity supplied by an electrical generator so that the generator may be connected to an electrical grid<sup>73</sup>—from Waukesha, to be used at a power plant Indeck was developing and would later sell to NRG. Waukesha acknowledged Indeck's purchase order. After Indeck made the required 10% progress payment, Waukesha manufactured and shipped the transformers according to Indeck's instructions (and, eventually, re-shipped them to another location at Indeck's instruction), and issued invoices to Indeck for the balance due. Indeck refused to pay and sued seeking a declaration that it was not liable for any unpaid sums because Waukesha had previously breached their contract by refusing to agree to allow Indeck to assign all of its rights and liabilities to NRG's subsidiary. Waukesha counterclaimed to recover the balance due plus re-shipping, handling, and storage costs incurred because neither Indeck nor anyone else had accepted the transformers, and moved for summary judgment.

Rep. Serv. (Callaghan) 57, 70–71 (N.J. Super. Ct. App. Div. 1981); *Gochey v. Bombardier, Inc.*, 572 A.2d 921, 923, 11 U.C.C. Rep. Serv. 2d (Callaghan) 870, 874–75 (Vt. 1990) (all allowing buyers to revoke against manufacturers based on manufacturers' express warranties).

70. See, e.g., *Parsley v. Monaco Coach Corp.*, 327 F. Supp. 2d 797, 803, 54 U.C.C. Rep. Serv. 2d (West) 301, 306–07 (W.D. Mich. 2004); *Ducharme v. A & S RV Ctr., Inc.*, 321 F. Supp. 2d 843, 855–56 (E.D. Mich. 2004), *aff'd*, 127 Fed. Appx. 204 (6th Cir. 2005) (per curiam).

71. See, e.g., *Allstate Ins. Co. v. Daimler Chrysler*, 53 U.C.C. Rep. Serv. 2d (West) 226, 228–29 (N.D. Ill. 2004) (barring a breach of express warranty claim because the buyers failed to allege either that they satisfied the notice requirement of U.C.C. § 2-607 or that they were excused from doing so because the seller had actual knowledge of the defect or because the plaintiffs suffered personal injuries as a result of the defect); *Carfaro v. Emergency Svcs. Holding, Inc.*, 782 N.Y.S.2d 806, 808 (N.Y. App. Div. 2004) (sellers entitled to judgment as a matter of law because buyer “first notified them that the products were defective more than 16 months after discovery of the alleged defect and that the notification was thus untimely as a matter of law”), *leave to appeal dismissed*, 824 N.E. 2d 52 (N.Y. 2004); see also, e.g., *Zeigler v. Sony Corp. of Am.*, 849 A.2d 19, 24 (Conn. Super. Ct. 2004) (opining, in dicta, that a buyer that seeks to sue a manufacturer for breach of implied warranty must give the manufacturer the notice U.C.C. § 2-607(3) requires, that the “plaintiff, as well as the other class members, is required to give individualized notice . . . not simply . . . of a defect—of which the defendants may already be aware—but notice of this plaintiff's claim the alleged defects constituted a breach of warranty,” and that “the plaintiff's argument that ‘generalized’ knowledge satisfies the requirement of notice is . . . contrary to the plain language of this state's law and seriously undermines the U.C.C. policy of avoiding lawsuits by encouraging negotiation and promoting timely cure of defects by sellers and manufacturers”).

72. 54 U.C.C. Rep. Serv. 2d (West) 990 (N.D. Ill. 2004).

73. *Id.* at 992.

The district court granted Waukesha's motion for summary judgment, holding that (1) Indeck and Waukesha had a valid contract, based both on their exchange of forms and each party's performance; (2) Waukesha discharged all of its obligations under the contract by timely designing, manufacturing, and shipping (and then re-shipping) conforming transformers as instructed by Indeck; and (3) Indeck materially breached the contract when it refused to pay the balance due.<sup>74</sup> The district court found no merit to Indeck's claims that Waukesha breached the contract by refusing to agree to allow Indeck to assign all of its rights and liabilities to a subsidiary of NRG that was, at the relevant time, a shell company established by Indeck for tax purposes. Indeck's contract with Waukesha provided that neither party could assign its contractual rights and duties without the other party's prior written consent, but that such consent would "not be unreasonably withheld."<sup>75</sup> The district court found that Waukesha did not unreasonably withhold its consent when, after investigating the creditworthiness of the proposed assignee, Waukesha was unwilling to agree to transfer the liability for more than \$3,000,000 to a "shell company" with no credit history and for which Indeck refused to act as surety.<sup>76</sup> Moreover, even if Waukesha had unreasonably withheld its consent, the court ruled that Indeck had waived any such breach by not asserting it until after Waukesha sought to recover the balance due.<sup>77</sup>

In *RGJ Associates, Inc. v. Stainsafe, Inc.*, discussed previously,<sup>78</sup> the court found that one party's material breach of an exclusive dealing contract gave the non-breaching party (Williamsville) "the choice of either continuing the contract or suing for breach."<sup>79</sup> Because Williamsville continued to sell its products to the breaching party (Stainsafe)—all but those that Stainsafe had wrongfully refused to purchase—the court concluded that the contract survived the breach and both parties remained bound to it.<sup>80</sup> In the alternative, the court ruled that the parties agreed to modify the preexisting contract to exclude the product line that Stainsafe had chosen to produce for itself.<sup>81</sup>

## REMEDIES

### SELLER'S REMEDIES

In a sparse group of damages discussions, one stands out. In *Honeywell International, Inc. v. Air Products & Chemicals, Inc.*,<sup>82</sup> the court dealt with the collapse

74. See 2004 WL 2095554, at \*8–9 (the *Uniform Commercial Code Reporting Service* did not publish parts II and III of the opinion—hence, the citation to the Westlaw version in this and the following footnotes).

75. *Id.* at \*9.

76. *See id.* at \*10.

77. *Id.* at \*9.

78. *See supra* text accompanying notes 22–25.

79. *RGJ Associates*, 338 F. Supp. 2d at 226.

80. *See id.* at 226–27.

81. *See id.* at 227. Because the Williamsville-Stainsafe contract was for the sale of goods, U.C.C. § 2-209(1) would require no additional consideration to make a modification binding. *See* U.C.C. § 2-209(1) (2001); *RGJ Associates*, 338 F. Supp. 2d at 227 & n.26.

82. 858 A.2d 392, 54 U.C.C. Rep. Serv. 2d (West) 541 (Del. Ch. 2004), *aff'd in part, rev'd in part and remanded*, 872 A.2d 944 (Del. 2005).

of a strategic alliance between Honeywell and Air Products. Pursuant to the parties' deal, Air Products purchased its requirements of certain chemicals used in manufacturing semiconductors from Honeywell. Air Products agreed to use reasonable efforts to promote the sale of Honeywell's chemicals to its customers and also agreed not to enter into other strategic alliances or similar arrangements with other manufacturers of the chemicals. Honeywell, however, was not so tightly limited. It could enter into similar arrangements with Air Products' rivals, but only if the strategic alliance failed to meet its sales targets. Both parties had the right to terminate the agreement upon two years' notice if various targets were not met. From the start, the alliance failed to meet its goals and Honeywell continued to sell a great deal of chemicals outside the alliance. The fractious relationship ended when Air Products bought the electronic chemicals division of Ashland, one of Honeywell's rivals. Honeywell thereupon gave notice of termination and sued, though Air Products and Honeywell continued to do business for some time after. Air Products likewise gave notice of termination.<sup>83</sup>

The chancery court held that Air Products breached the agreement to purchase its requirements for chemicals from Honeywell when it acquired the competing portion of Ashland. Honeywell sought lost profits for the sales it would have made had Air Products purchased all its needs for chemicals from Honeywell. But this, the court held, was far too broad, for it included the sales that Air Products made solely because of its purchase of Ashland. Adverting to New York common-law decisions on consequential damages and causation, the court ruled that these profits were not fairly within the parties' contemplation when they entered into their alliance, so Honeywell could not recover them.<sup>84</sup> Allowing damages for customers previously served by the alliance was entirely proper, the court concluded, but not those who had not been served before.<sup>85</sup>

There are so few opinions that calculate damages for breach of a requirements contract that this is worth some attention, and the recent rise of strategic alliances makes the opinion all the more timely. The result is not unsound, though it is not reached ideally. It seems correct to award damages based on lost profits here, because Honeywell essentially complained of lost volume. The court's task was, thus, to calculate the sales Honeywell lost due to Air Products' breach. In doing so, the chancellor properly excluded sales attributable to Air Products' purchase of the Ashland division. The court's goal is ultimately expectation,<sup>86</sup> and Honeywell can hardly argue that, had Air Products not breached, Honeywell would have gained all the Ashland sales. This conclusion comes from the Code itself, which uses as benchmarks stated estimates or, in their absence, normal or comparable prior requirements.<sup>87</sup> The mystery is why the court used common-law

83. See 858 A.2d at 396–405, 54 U.C.C. Rep. Serv. 2d (West) at 543–54.

84. *Id.* at 421–22, 54 U.C.C. Rep. Serv. 2d (West) at 557–58, 560.

85. The Delaware Supreme Court affirmed this portion of the decision, although it lengthened the time period for which Air Products was liable from two years (the length required for notification of termination) to the end of the original contract period. See 872 A.2d at 958.

86. See U.C.C. § 1-305(a) (2001); see also U.C.C. § 1-106 (2000).

87. See U.C.C. § 2-306(1) (2001).

consequential damages cases to guide its discussion of direct damages. Its defense for doing so was that an earlier case used them in computing a buyer's damages under section 2-713, which the court stated was the counterpart to section 2-708(2).<sup>88</sup> However, section 2-713 is analogous to section 2-708(1), not to section 2-708(2). Moreover, the case the *Honeywell* court relied upon dealt with a claim for consequential damages.<sup>89</sup> Buyers get consequential damages under Article 2; sellers do not.<sup>90</sup> The Code is sufficiently clear in its treatment of direct damages that the court should not have strained to import marginally relevant common-law decisions that yield the same result.

### LIMITATIONS ON LIABILITY

The main issue raised this year on limitations on liability is how the subsections of the statute fit together. Section 2-719(2) provides that if a limited remedy fails of its essential purpose, the default remedies apply. Section 2-719(3) provides that consequential damages limitations are valid unless unconscionable. If an agreement contains both a limitation on remedies and a disclaimer of consequential damages, and the limited remedy then fails of its essential purpose, what happens to the disclaimer of consequential damages? Is it invalidated, with the result that the contract reverts to Code's default rule, which allows a buyer to recover consequential damages that are foreseeable and not reasonably preventable?<sup>91</sup> Is it left intact, subject to an unconscionability test? Or is some intermediate test used, sometimes invalidating it, sometimes not?

Courts have split on this issue, generally favoring the second approach. In *Piper Jaffray & Co. v. SunGard Systems International, Inc.*,<sup>92</sup> SunGard supplied computer software to Piper Jaffray for use in securities trading. The software license agreement limited SunGard's liability to the amount of the license fees and contained a separate exclusion of consequential damages. The software never worked as promised, despite extensions of time and many attempts at repair. Piper Jaffray sued for breach of contract and SunGard moved to dismiss based on the liability limitations.<sup>93</sup>

The court assumed, for the purposes of the motion, that Article 2 governed, that the limitation of liability clause was exclusive, and that the clause failed of its essential purpose. Nevertheless, it held that Piper Jaffray's claims for consequential damages were barred by the independent disclaimer. In doing so, it treated subsections (2) and (3) of section 2-719 as independent for four reasons. First, it observed that the subsections apply different standards, suggesting that

88. *Honeywell*, 858 A.2d at 423 n.108, 54 U.C.C. Rep. Serv. 2d (West) at 560 n.108.

89. See *Canusa Corp. v. A & R Lobosco, Inc.*, 986 F. Supp. 723, 731-33, 35 U.C.C. Rep. Serv. 2d (West) 73, 84-87 (E.D.N.Y. 1997).

90. Compare U.C.C. § 2-710 (2001) with U.C.C. § 2-715 (2001); see also U.C.C. § 1-305(a)(2001) (authorizing an award of consequential damages only in cases where the Code expressly provides for it); U.C.C. § 1-106 (2000) (same).

91. See U.C.C. § 2-715(2)(a) (2001).

92. 54 U.C.C. Rep. Serv. 2d (West) 1088 (D. Minn. 2004) (applying Pennsylvania law).

93. See *id.* at 1089-91.

they must behave independently. Second, it stated that reading the clauses as interdependent would render section 2-719(3) meaningless, deleting a consequential damages disclaimer without regard to its conscionability. Third, it pointed to comments one and three, which it thought were consistent with allowing the parties to allocate unknown risks freely, so long as they did not do so unconscionably. Finally, it found this holding consistent with the trend in the case law and the opinions of learned commentators.<sup>94</sup> Once it concluded that the clauses were independent, the court readily upheld the waiver of consequential damages because Piper Jaffray did not claim that the waiver was unconscionable, the parties were sophisticated firms, it would be difficult to find a lack of meaningful choice or manifest oppression, and the parties negotiated the terms of the agreement.<sup>95</sup>

The result in the case was not peculiar. When sophisticated parties contract in the face of a clear risk of consequential damages, courts should honor their risk allocations in the absence of fraud or the like. Still, one may applaud the result and deprecate the method. Just because the subsections use different standards does not mean they must be independent; it merely means that a limitation of only consequential damages may properly be treated differently than a limitation of other sorts of damages. In addition, one may ask whether reading the clauses as independent truly gives effect to the parties' intent. A buyer's willingness to give up consequential damages may be linked to the seller's willingness to repair defective goods within a reasonable time, so the seller should not be able to avoid its own duties and still insist on the liability limitation.<sup>96</sup> Nor does a close reading of the text inexorably lead to independence; after all, section 2-719(2) and comment 1 do state that the default remedies apply when a limited remedy fails of its essential purpose, and neither states that this is subject to subsection (3).

An intermediate method may be more appropriate. Many courts—indeed, a line that, according to one treatise, is “gaining momentum”<sup>97</sup>—employ case-by-case analysis to determine how the parties intended to allocate the risk of consequential damages when the exclusive remedy has failed of its essential purpose. These courts look at such factors as bargaining power, the extent to which the seller attempted in good faith to carry out the remedy, the complexity of the goods, and the language of the agreement.<sup>98</sup> Indeed, one could make still finer distinctions between consequential damages caused by the breach of warranty, which

94. See *id.* at 1095–97 (citing 1 JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE § 12.10(c), at 666–68 (4th ed. 1995)).

95. *Piper Jaffray*, 54 U.C.C. Rep. Serv. 2d (West) at 1098.

96. See, e.g., *Clark v. Int'l Harvester Co.*, 581 P.2d 784, 800–02, 25 U.C.C. Rep. Serv. (Callaghan) 91, 111–12 (Idaho 1978); *Kelynack v. Yamaha Motor Corp.*, 394 N.W.2d 17, 21–22, 2 U.C.C. Rep. Serv. 2d (Callaghan) 166, 171 (Mich. Ct. App. 1986).

97. GREGORY M. TRAVALIO ET AL., *NORDSTROM ON SALES & LEASES OF GOODS* § 4.08[D][1], at 489 (2d ed. 2000).

98. See, e.g., *Fiorito Bros., Inc. v. Fruehauf Corp.*, 747 F.2d 1309, 1315, 39 U.C.C. Rep. Serv. (Callaghan) 1298, 1305–06 (9th Cir. 1984) (applying Washington law); *AES Tech. Sys., Inc. v. Coherent Radiation*, 583 F.2d 933, 941, 24 U.C.C. Rep. Serv. (Callaghan) 861, 871–72 (7th Cir. 1978) (applying identical provisions of California's and Illinois's U.C.C.); *Ritchie Enters. v. Honeywell Bull, Inc.*, 730 F. Supp. 1041, 1049–50, 11 U.C.C. Rep. Serv. 2d (Callaghan) 1170, 1181 (D. Kan. 1990) (applying Massachusetts law).



might plausibly be barred, and those caused by the failure to remedy, which might not.<sup>99</sup> Both methods come closer to giving effect to the parties' intent than either the independent or interdependent approaches.

## STATUTE OF LIMITATIONS

Tolling cases dominated limitations litigation this year.<sup>100</sup> *Jones v. Ford Motor Co.*<sup>101</sup> applied the Article 2 four-year statute of limitations<sup>102</sup> to a Magnuson-Moss action arising from the sale of a motor home. The sales contract required Jones to submit any dispute to a Dispute Settlement Board before going to court. Jones did, and his request for arbitration was denied six days later. Jones then filed suit. The trial court granted Ford's motion for summary judgment. In affirming that ruling, the appellate court followed the overwhelming body of case law by applying the Article 2 statute of limitations to a Magnuson-Moss claim.<sup>103</sup> It then concluded that Jones's action was untimely. Although Jones argued that the limitations period was tolled during the mandatory arbitration, an argument to which the court seemed sympathetic, the court pointed out that Jones had provided no evidence that he initiated the arbitration before the limitations period had expired. In dictum, it added that, had Jones done so, then equitable tolling should apply; but, in any case, the tolling period was shorter than the lateness of Jones's complaint, so the result would have been the same.<sup>104</sup>

The dictum seems sound. As the court pointed out, "[t]o find otherwise would place plaintiff in a 'Catch 22' position whereby he would face either rejection of his claim in the trial court for having failed to comply with the terms of the warranty or expiration of the four-year statute of limitations while he awaited a decision from the DSB."<sup>105</sup> Moreover, that might encourage overhasty resort to formal dispute resolution, rather than the informal methods that should be encouraged.<sup>106</sup> A simple alternative is to suspend the limitations period when the

99. See, e.g., *Waters v. Massey-Ferguson, Inc.*, 775 F.2d 587, 591-92, 41 U.C.C. Rep. Serv. (Callaghan) 1553, 1557-61 (4th Cir. 1985) (applying South Carolina law); *Bishop Logging Co. v. John Deere Indus. Equip. Co.*, 455 S.E.2d 183, 191-93, 28 U.C.C. Rep. Serv. 2d (Callaghan) 190, 198-200 (S.C. Ct. App. 1995); *TRAVALIO ET AL.*, *supra* note 97, § 4.08[D][1], at 490.

100. The year provided the usual collection of routine cases as well. See, e.g., *Auto Chlor Sys. of Minn., Inc. v. JohnsonDiversey*, 328 F. Supp. 2d 980, 54 U.C.C. Rep. Serv. 2d (West) 443 (D. Minn. 2004) (applying Tennessee law) (no tolling of statute without fraudulent concealment); *Meron v. Ward Lumber Co.*, 779 N.Y.S.2d 597, 54 U.C.C. Rep. Serv. 2d (West) 55 (N.Y. App. Div. 2004) (warranty that shingles will last for twenty years falls within the discovery rule of U.C.C. § 2-725(2)).

101. 807 N.E.2d 520, 53 U.C.C. Rep. Serv. 2d (West) 255 (Ill. Ct. App. 2004).

102. See U.C.C. § 2-725 (2001).

103. See, e.g., *Murungi v. Mercedes Benz Credit Corp.*, 192 F. Supp. 2d 71, 79-80 (W.D.N.Y. 2001); *Poli v. DaimlerChrysler Corp.*, 793 A.2d 104, 111, 47 U.C.C. Rep. Serv. 2d (West) 260, 269-70 (N.J. Super. Ct. App. Div. 2002).

104. See *Jones*, 807 N.E.2d at 523, 53 U.C.C. Rep. Serv. 2d (West) at 258.

105. *Id.* at 523, 53 U.C.C. Rep. Serv. 2d (West) at 258.

106. Indeed, one could generalize this to allow tolling during all attempts to resolve disputes informally. By doing so, courts could avoid prematurely ending informal dispute resolution, or, alternatively, depriving a buyer of an otherwise meritorious claim. Some states provide for this by statute, and Llewellyn suggested as much in a draft of the Code. See Larry T. Garvin, *Uncertainty and Error in the Law of Sales: The Article Two Statute of Limitations*, 83 B.U. L. Rev. 345, 393 n.217, 398 n.240 (2003).

contract provides for mandatory arbitration, requiring that the buyer pursue its claim early enough to allow for an arbitral decision and the seller's response, should the arbitration be non-binding.<sup>107</sup>

In *PPG Industries, Inc. v. JMB/Houston Centers Partners Limited Partnership*,<sup>108</sup> PPG sold over 12,000 windows for use in a 46-story skyscraper completed in April 1978. By July 1982, many of the windows were discolored and fogged. PPG replaced a quarter of the windows under the warranty, a project that took over two years. The building was sold as is in December 1989. The windows continued to fail, and in 1994 the new owner sued PPG.

PPG asserted a limitations defense to the breach of warranty claim. The warranty provided that the windows would be free from defect for five years from April 1, 1978, and that PPG would repair or replace the defective windows upon notice. The court held that the warranty claim was time-barred. Because the warranty explicitly guaranteed future performance, limitations did not start to run until the buyer was or should have been aware of a problem and that the problem was not isolated. The court concluded that "the problems here were not isolated, and 3,000 defective windows is not a few."<sup>109</sup>

For four reasons, the court also rejected the argument that PPG's attempts to repair the windows between 1982 and 1989 tolled the statute of limitations. First, Texas courts had held for almost a century that repair attempts do not toll a statute of limitations, and the courts of most other states had held the same. Second, tolling limitations during repair attempts would render a warranty period perpetual, making sellers reluctant to attempt any repairs. Third, faulty repairs are actionable under either an implied warranty for repair services or the state statute on unfair and deceptive acts and practices. Fourth, the plaintiff had not argued breach of a repair warranty. If it had, such a claim would fall outside the U.C.C. because repair promises are services, not sales of goods, and would accrue not when the goods were sold, but upon the failure to repair.<sup>110</sup>

Most of these arguments are less than compelling, particularly if one seeks to export them. The court correctly pointed out that the bulk of reported opinions support its holding, but bulk and weight are not synonyms. Its argument that repair tolling will reduce repair is odd. If a seller refuses to repair goods under warranty, it will breach its contract and be liable for damages in a costly legal action. Surely that, rather than the threat of a somewhat extended limitations

107. Magnuson-Moss allows mandatory non-binding arbitration. 15 U.S.C. § 2310(a) (2000). The FTC has consistently read Magnuson-Moss to ban binding arbitration. 16 C.F.R. §§ 703.2(a), 703.5(j) (2004). Courts have, of late, split on this issue, with some ruling that the statute's mechanism for non-binding arbitration does not foreclose binding arbitration. *See, e.g., Southern Energy Homes, Inc. v. Ard*, 772 So. 2d 1131, 1135 (Ala. 2000).

108. 146 S.W.3d 79, 54 U.C.C. Rep. Serv. 2d (West) 166 (Tex. 2004); *see also Sandy Springs Toyota v. Classic Cadillac Atlanta Corp.*, 604 S.E.2d 303, 54 U.C.C. Rep. Serv. 2d (West) 844 (Ga. Ct. App. 2004) (same approach for warranty of title).

109. *See PPG Industries*, 146 S.W.3d at 94, 54 U.C.C. Rep. Serv. 2d (West) at 173.

110. *See id.* at 95–96 nn.81–83, 54 U.C.C. Rep. Serv. 2d (West) at 174 nn.81–83 (collecting cases).

period, will drive its actions—not to mention its desire to maintain good relations with its customers.<sup>111</sup> If anything, not tolling the statute would impede dispute resolution, because the buyer would be impelled to sue in order to protect its rights even while repairs went on.<sup>112</sup> Nor would a warranty become perpetual, as repeated failures to repair goods should and do yield breach under both the U.C.C. and consumer protection statutes.<sup>113</sup> The alternative causes of action that the court dangled in front of the plaintiff are only sporadically available; indeed, few if any UDAP statutes have the breadth of Texas's, and would not normally apply to the sale of windows in an office building.<sup>114</sup> The final argument is the most successful, suitably adapted. The court is surely not correct to say that a repair promise falls outside Article 2, at least when it arises as part of a sale of goods in a predominant purpose jurisdiction.<sup>115</sup> However, remedial promises, though within Article 2, are still distinct from warranties. The better-reasoned line of authority holds that remedial promises are breached when the seller does not honor its obligation to repair.<sup>116</sup> Here, there was both a warranty of quality and a remedial promise, and the plaintiffs should have pleaded breaches of each. When the seller supplies only a warranty, though, this argument does not apply, and repair tolling should be available.<sup>117</sup>

## ECONOMIC LOSS DOCTRINE

The economic loss rule typically operates to bar tort actions in cases based on a contractual relationship unless there is personal injury or damage to property

111. The court might have argued instead that repair tolling might limit the length of a warranty, should a seller wish to reduce the duration of its warranty exposure. This would at least be correct, but the effect would be to make the nominal warranty period more realistic rather than to do any harm to the buyer.

112. See, e.g., *Curragh Queensland Mining Ltd. v. Dresser Indus., Inc.*, 55 P.3d 235, 240, 47 U.C.C. Rep. Serv. 2d (West) 1065, 1069 (Colo. Ct. App. 2002).

113. See, e.g., *Conte v. Dwan Lincoln-Mercury, Inc.*, 374 A.2d 144, 148–49, 20 U.C.C. Rep. Serv. (Callaghan) 899, 906 (Conn. 1976); *Guerdon Indus., Inc. v. Gentry*, 531 So. 2d 1202, 1208, 7 U.C.C. Rep. Serv. 2d (Callaghan) 67, 75 (Miss. 1988).

114. TEX. BUS. & COM. CODE ANN. § 17.45(4) (Vernon 2002) (defining “consumer” to include corporations with assets of up to \$25 million). See generally JONATHAN SHELDON & CAROLYN L. CARTER, UNFAIR AND DECEPTIVE ACTS AND PRACTICES § 2.1.8 (5th ed. 2001). Even Texas's broad statute, contrary to the court's suggestion, would not cover this action. It requires that the putative defendant knowingly have made false or misleading statements of fact concerning the need for repair or have represented that work was done that had not been done. TEX. BUS. & COM. CODE ANN. § 17.46(b)(13), (22) (Vernon 2002), amended by 2005 Tex. Sess. Law. Serv. Ch. 728, § 11.101 (H.B. 2018) (Vernon). Neither was the case here; the windows needed repairing, and PPG never represented that they did not or that it had fully repaired them. In addition, this dispute exceeds the amount covered by the Texas statute. TEX. BUS. & COM. CODE ANN. § 17.49(g) (Vernon 2002).

115. Texas follows the predominant purpose test. *G-W-L, Inc. v. Robichaux*, 643 S.W.2d 392, 394, 35 U.C.C. Rep. Serv. (Callaghan) 342, 345 (Tex. 1982), overruled on other grounds by *Melody Home Mfg. Co. v. Barnes*, 741 S.W.2d 349 (Tex. 1987).

116. See, e.g., *Long Island Lighting Co. v. Imo Indus., Inc.*, 6 F.3d 876, 890, 22 U.C.C. Rep. Serv. 2d (Callaghan) 205, 219–21 (2d Cir. 1993) (applying New York law); *Versico, Inc. v. Engineered Fabrics Corp.*, 520 S.E.2d 505, 509–10, 39 U.C.C. Rep. Serv. 2d (West) 1112, 1114 (Ga. Ct. App. 1999); 4B LARY LAWRENCE, LAWRENCE'S ANDERSON ON THE UNIFORM COMMERCIAL CODE § 2-725:101 (3d ed. 2001). This result is preserved in revised Article 2. See U.C.C. § 2-725(2)(c) (2003).

117. This reasoning is more fully developed in Garvin, *supra* note 106, at 377–81.

other than the property that is the subject of the contract.<sup>118</sup> Courts decided several cases involving the economic loss rule in 2004.

With respect to raising the economic loss rule as a defense in a tort action, the court in *Kalmes Farms, Inc. v. J-Star Industries, Inc.*<sup>119</sup> held that a pleading stating “the damages Plaintiff may recover are limited and controlled by the provisions of the Uniform Commercial Code” was sufficient.<sup>120</sup> Further, the court held that Minnesota’s statute governing the economic loss rule, which does not bar tort actions “based upon fraud or fraudulent or intentional misrepresentation,” did not bar an action based on negligent misrepresentation.<sup>121</sup>

In *Robinson Helicopter Co. v. Dana Corp.*,<sup>122</sup> the plaintiff purchased sprag clutches, a safety component of helicopters that allows the rotor to continue turning after a loss in power, from the defendant seller. The clutches had to be manufactured to a specific level of hardness to avoid problems but the seller changed the hardness level for a time without notifying the buyer. Nevertheless, the seller continued to represent that the clutches complied with the hardness specifications. The non-conforming clutches failed at a higher rate than the conforming clutches, although the failures did not cause any personal injury or damage to other property. The buyer spent about \$1.5 million to recall and replace the non-conforming clutches. A jury awarded the buyer approximately \$7.5 million in damages, including \$6 million in punitive damages based on a finding that the seller had made false representations of fact and had knowingly misrepresented or concealed material facts with the intent to defraud. The court of appeals affirmed in part and reversed in part, upholding the damages for breach of contract and breach of warranty, but reversing the judgment based on the misrepresentation claim because of the economic loss rule.

The California Supreme Court reversed, reasoning that the claims for fraud and misrepresentation were tort claims, independent of the contract, and therefore not barred by the economic loss rule.<sup>123</sup> Specifically, the court held that the seller’s provision of false certificates of compliance was independent tortious conduct.<sup>124</sup> The court then noted that public policy requires the imposition of tort remedies in situations in which the actions that amount to breach of contract also violate social policies.<sup>125</sup> One justice dissented, arguing that the existence of an independent tort was not enough to evade the economic loss rule.<sup>126</sup>

One high-profile 2004 case involved the economic loss doctrine in a somewhat unusual setting. In *City of Chicago v. Beretta U.S.A. Corp.*,<sup>127</sup> the Illinois Supreme

118. See, e.g., *Redarowicz v. Ohlendorf*, 441 N.E.2d 324, 327 (Ill. 1982); *Suffolk Cty. v. Long Island Lighting Co.*, 728 F.2d 52 (2d Cir. 1984) (applying New York law).

119. 52 U.C.C. Rep. Serv. 2d (West) 845 (D. Minn. 2004).

120. See *id.* at 849.

121. See *id.* at 852 (quoting MINN. STAT. ANN. § 604.10(e)).

122. 102 P.3d 268 (Cal. 2004).

123. *Id.* at 268.

124. *Id.* at 274.

125. *Id.* at 275.

126. *Id.* at 276 (Werdegarr, J., dissenting).

127. 821 N.E.2d 1099 (Ill. 2004).

Court considered a suit brought by the City of Chicago and Cook County against gun manufacturers, distributors, and dealers seeking damages and injunctive relief for public nuisance. The court refused to recognize an exception to the economic loss rule when, as the plaintiffs contended, "defendant's conduct 'creates an unreasonable threat to public health, safety, and welfare.'"<sup>128</sup> Thus, because the plaintiffs alleged no personal injury or harm to property, the court held their claim barred by the economic loss rule.<sup>129</sup>

In *Inter Impex S.A.E. v. Comtrade Corp.*, discussed above,<sup>130</sup> the court recognized New York's exception to the economic loss rule when there is an allegation of negligent performance of a contract. The plaintiff, a purchaser of dried milk, argued that the milk had been improperly and negligently packaged, causing economic loss. In dismissing the negligence claim, the court noted that, although New York has a negligent performance exception to the economic loss rule, the exception applies only to contracts for the provision of services, not to contracts for the provision of goods.<sup>131</sup> Further, the court noted that the negligent performance exception requires a duty independent of the contract, and that no such duty was alleged in the case before it.<sup>132</sup>

128. *Id.* at 1141.

129. *Id.* at 1142.

130. *See supra* text accompanying notes 52–53.

131. *Inter Impex S.A.E.*, No. 00 Civ. 0133 (GBD), 2004 WL 2793213, at \*6 (S.D.N.Y. Dec. 6, 2004).

132. *Id.*