

# Repudiation and Anticipatory Breach

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Edgar Frederick De La Tour hired Albert Hochster to serve as his courier during a trip to Europe for three months starting on June 1. On May 22, De La Tour notified Hochster in writing that he had changed his mind and that Hochster's services would not be needed. Based on what we have learned so far, when can Hochster sue? A breach, we learned, is the non-performance of a contractual obligation when it is due, and De La Tour seems to have no obligations due until at least June 1. Therefore, at the minimum, Hochster should not be able to sue before June 1, right? But Hochster sued on May 22, and won.

During oral argument before the Queen's Bench, the highest court in England, one of the Justices famously said that:

When a party announces his intention not to fulfill the contract, the other side may take him at his word and rescind the contract ... I am inclined to think that the party may [] say: "Since you have announced that you will not go on with the contract, I will consent that it shall be at an end from this time; but I will hold you liable for the damage I have sustained; and I will proceed to make that damage as little as possible by making the best use I can of my liberty."

*Hochster v. De La Tour*, 118 Eng. Rep. 922 (Q.B. 1853). This passage was even quoted by the U.S. Supreme Court in *Roehm v. Horst*, 178 US 1, 9 (1900). The Queen's Bench ruled unanimously in favor of the plaintiff Hochster, explaining:

If a man promises to marry a woman on a future day, and before that day marries another woman, he is instantly liable to an action for breach of promise of marriage; *Short v Stone*. If a man contracts to execute a lease on and from a future day for a certain term, and, before that day, executes a lease to another for the same term, he may be immediately sued for breaking the contract; *Ford v Tiley* . . . . [W]here there is a contract to do an act on a future day, there is a relation constituted between the parties in the meantime by the contract, and that they impliedly promise that in the meantime neither will do anything to the prejudice of the other inconsistent with that relation. As an example, a man and woman engaged to marry are affianced to one another during the period between the time of the engagement and the celebration of the marriage.

In the present case, of traveller and courier, from the day of the hiring till the day when the employment was to begin, they were engaged to each other; and

it seems to be a breach of an implied contract if either of them renounces the engagement . . . . If the plaintiff has no remedy for breach of the contract unless he treats the contract as in force, and acts upon it down to the 1st June 1852, it follows that, till then, he must enter into no employment which will interfere with his promise “to start with the defendant on such travels on the day and year,” and that he must then be properly equipped in all respects as a courier for a three months’ tour on the continent of Europe.

But it is surely much more rational, and more for the benefit of both parties, that, after the renunciation of the agreement by the defendant, the plaintiff should be at liberty to consider himself absolved from any future performance of it, retaining his right to sue for any damage he has suffered from the breach of it. Thus, instead of remaining idle and laying out money in preparations which must be useless, he is at liberty to seek service under another employer, which would go in mitigation of the damages to which he would otherwise be entitled for a breach of the contract . . . .

[I]t seems reasonable to allow an option to the injured party, either to sue immediately, or to wait till the time when the act was to be done, still holding it as prospectively binding for the exercise of this option, which may be advantageous to the innocent party, and cannot be prejudicial to the wrongdoer. . . .

If it should be held that, upon a contract to do an act on a future day, a renunciation of the contract by one party dispenses with a condition to be performed in the meantime by the other, there seems no reason for requiring that other to wait till the day arrives before seeking his remedy by action: and the only ground on which the condition can be dispensed with seems to be, that the renunciation may be treated as a breach of the contract.

The Queen’s Bench decision in this case is the basis for the modern doctrine of anticipatory breach, which was applied in the following cases.

### **Taylor v. Johnston**

15 Cal.3d 130 (Supreme Court of California, 1975)

SULLIVAN, Justice.

In this action for damages for breach of contract defendants Elizabeth and Ellwood Johnston, individually and as copartners doing business as Old English Rancho, appeal from a judgment

entered after a nonjury trial in favor of plaintiff H. B. Taylor and against them in the amount of \$132,778.05 and costs.

Plaintiff was engaged in the business of owning, breeding, raising and racing thoroughbred horses in Los Angeles County. Defendants were engaged in a similar business, and operated a horse farm in Ontario, California, where they furnished stallion stud services. In January 1965 plaintiff sought to breed his two thoroughbred mares, Sunday Slippers and Sandy Fork to defendants' stallion Fleet Nasrullah. To that end, on January 19 plaintiff and defendants entered into two separate written contracts—one pertaining to Sunday Slippers and the other to Sandy Fork. Except for the mare involved the contracts were identical. We set forth in the margin the contract covering Sunday Slippers.

The contract provided that Fleet Nasrullah was to perform breeding services upon the respective mares in the year 1966 for a fee of \$3,500, payable on or before September 1, 1966. If the stud fee was paid in full and the mares failed to produce a live foal (one that stands and nurses without assistance) from the breeding a return breeding would be provided the following year without additional fee.

On October 4, 1965, defendants sold Fleet Nasrullah to Dr. A. G. Pessin and Leslie Combs II for \$1,000,000 cash and shipped the stallion to Kentucky. Subsequently Combs and Pessin syndicated the sire by selling various individuals 36 or 38 shares, each share entitling the holder to breed one mare each season to Fleet Nasrullah. Combs and Pessin each reserved three shares.

On the same day defendants wrote to plaintiff advising the latter of the sale and that he was 'released' from his 'reservations' for Fleet Nasrullah.<sup>2</sup> Unable to reach defendants by telephone, plaintiff had his attorney write to them on October 8, 1965, insisting on performance of the contracts. Receiving no answer, plaintiff's attorney on October 19 wrote a second letter threatening suit. On October 27, defendants advised plaintiff by letter that arrangements had been made to breed the two mares to Fleet Nasrullah in Kentucky.<sup>3</sup> However, plaintiff later learned that the mares could not be boarded at Spendthrift Farm

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<sup>2</sup> Defendants' letter stated in part: "We wish to inform you that FLEET NASRULLAH has been sold and will stand the 1966 season in Kentucky. You are, therefore, released from your reservations made to the stallion."

<sup>3</sup> Defendants' letter stated in part: "Mr. Johnston has made arrangements for you to breed SANDY FORK . . . and SUNDAY SLIPPERS . . . to FLEET NASRULLAH for the 1966 season. Therefore, you should communicate with Dr. A. G. Pessin of Spendthrift Farm, Lexington, Kentucky to finalize breeding arrangements . . . ."

where Fleet Nasrullah was standing stud and accordingly arranged with Clinton Frazier of Elmhurst Farm to board the mares and take care of the breeding.

In January 1966 plaintiff shipped Sunday Slippers and Sandy Fork to Elmhurst Farm. At that time, however, both mares were in foal and could not be bred, since this can occur only during the five-day period in which they are in heat. The first heat period normally occurs nine days, and the second heat period thirty days, after foaling. Succeeding heat periods occur every 21 days.

On April 17, 1966, Sunday Slippers foaled and Frazier immediately notified Dr. Pessin. The latter assured Frazier that he would make the necessary arrangements to breed the mare to Fleet Nasrullah. On April 26, the ninth day after the foaling, Frazier, upon further inquiry, was told by Dr. Pessin to contact Mrs. Judy who had charge of booking the breedings and had handled these matters with Frazier in the past. Mrs. Judy, however, informed Frazier that the stallion was booked for that day but would be available on any day not booked by a shareholder. She indicated that she was acting under instructions but suggested that he keep in touch with her while the mare was in heat.

Sunday Slippers came into heat again on May 13, 1966. Frazier telephoned Mrs. Judy and attempted to book the breeding for May 16. She informed him that Fleet Nasrullah had been reserved by one of the shareholders for that day, but that Frazier should keep in touch with her in the event the reservation was cancelled. On May 14 and May 15 Frazier tried again but without success; on the latter date, Sunday Slippers went out of heat.

On June 4, the mare went into heat again. Frazier again tried to book a reservation with Fleet Nasrullah but was told that all dates during the heat period had been already booked. He made no further efforts but on June 7, on plaintiff's instructions, bred Sunday Slippers to a Kentucky Derby winner named Chateaugay for a stud fee of \$10,000.

Sandy Fork, plaintiff's other mare awaiting the stud services of Fleet Nasrullah, foaled on June 5, 1966. Frazier telephoned Mrs. Judy the next day and received a booking to breed the mare on June 14, the ninth day after foaling. On June 10, 1966, however, she cancelled the reservation because of the prior claim of a shareholder. Frazier made no further attempts and on June 14 bred Sandy Fork to Chateaugay.

Shortly after their breeding, it was discovered that both mares were pregnant with twins. In thoroughbred racing twins are considered undesirable since they endanger the mare and are themselves seldom valuable for racing. Both mares were therefore aborted. However, plaintiff

was not required to pay the \$20,000 stud fees for Chateaugay's services because neither mare delivered a live foal.

The instant action for breach of contract proceeded to trial on plaintiff's fourth amended complaint, which alleged two causes of action, the first for breach of the two written contracts, the second for breach of an oral agreement. Defendants' cross-complained for the stud fees. The court found the facts to be substantially as stated above and further found and concluded that by selling Fleet Nasrullah defendants had 'put it out of their power to perform properly their contracts,' that the conduct of defendants and their agents Dr. Pessin and Mrs. Judy up to and including June 13, 1966, constituted a breach and plaintiff "was then justified in treating it as a breach and repudiation of their contractual obligations to him," and that defendants unjustifiably breached the contracts but plaintiff did not. The court awarded plaintiff damages for defendants' breach in the sum of \$103,122.50 (\$99,800 net damage directly sustained plus \$3,322.50 for reasonable costs and expenses for mitigation of damages) . . . . This appeal followed.

Defendants' main attack on the judgment is two-pronged. They contend: First, that they did not at any time repudiate the contracts; and second, that they did not otherwise breach the contracts because performance was made impossible by plaintiff's own actions. To put it another way, defendants argue in effect that the finding that they breached the contracts is without any support in the evidence. Essentially they take the position that on the uncontradicted evidence in the record, as a matter of law there was neither anticipatory nor actual breach. As will appear, we conclude that the trial court's decision was based solely on findings of anticipatory breach and that we must determine whether such decision is supported by the evidence.

Nevertheless both aspects of defendants' argument require us at the outset to examine the specifications for performance contained in the contracts. We note that the reservation for "one services" for Fleet Nasrullah was "for the year 1966." As the evidence showed, a breeding is biologically possible throughout the calendar year, since mares regularly come into heat every 21 days, unless they are pregnant. The contracts therefore appear to contemplate breeding with Fleet Nasrullah at any time during the calendar year 1966. The trial court made no finding as to the time of performance called for by the contracts. There was testimony to the effect that by custom in the thoroughbred racing business the breeding is consummated in a "breeding season" which normally extends from January until early July, although some

breeding continues through August. It is possible that the parties intended that the mares be bred to Fleet Nasrullah during the 1966 breeding season rather than the calendar year 1966.<sup>8</sup>

However, in our view, it is immaterial whether the contract phrase “for the year 1966” is taken to mean the above breeding season or the full calendar year since in either event the contract period had not expired by June 7 and June 14, 1966, the dates on which Sunday Slippers and Sandy Fork respectively were bred to Chateaugay<sup>9</sup> and by which time, according to the findings defendants had repudiated the contracts. There can be no Actual breach of a contract until the time specified therein for performance has arrived. Although there may be a Breach by anticipatory repudiation; “by its very name an essential element of a true anticipatory breach of a contract is that the repudiation by the promisor occur before his performance is due under the contract.” (Gold Min. & Water Co. v. Swinerton, *supra*, 23 Cal.2d 19, 29(1943)) In the instant case, because under either of the above interpretations the time for performance had not yet arrived, defendants’ breach as found by the trial court was of necessity an anticipatory breach and must be analyzed in accordance with the principles governing such type of breach. To these principles we now direct our attention.

Anticipatory breach occurs when one of the parties to a bilateral contract repudiates the contract. The repudiation may be express or implied. An express repudiation is a clear, positive, unequivocal refusal to perform; an implied repudiation results from conduct where the promisor puts it out of his power to perform so as to make substantial performance of his promise impossible.

When a promisor repudiates a contract, the injured party faces an election of remedies: he can treat the repudiation as an anticipatory breach and immediately seek damages for breach of contract, thereby terminating the contractual relation between the parties, or he can treat the repudiation as an empty threat, wait until the time for performance arrives and exercise his remedies for actual breach if a breach does in fact occur at such time. However, if the injured party disregards the repudiation and treats the contract as still in force, and the repudiation is retracted prior to the time of performance, then the repudiation is nullified and the injured party is left with his remedies, if any, invocable at the time of performance.

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<sup>8</sup> Perhaps the fact that the stud fees were due to be paid September 1, 1966, at the close of the breeding season supports such a conclusion. Moreover, defendants concede without argument that the trial court impliedly found the time of performance to be the breeding season.

<sup>9</sup> Both Sunday Slippers and Sandy Fork would have had at least one more heat during the 1966 breeding season—that of Sunday Slippers commencing on June 26, 1966, and that of Sandy Fork commencing on July 7, 1966

As we have pointed out, the trial court found that the whole course of conduct of defendants and their agents Dr. Pessin and Mrs. Judy from the time of the sale of Fleet Nasrullah up to and including June 13, 1966, amounted to a repudiation which plaintiff was justified in treating as an anticipatory breach. However, when the principles of law governing repudiation just described are applied to the facts constituting this course of conduct as found by the trial court, it is manifest that such conduct cannot be treated as an undifferentiated continuum amounting to a single repudiation but must be divided into two separate repudiations.

First, defendants clearly repudiated the contracts when, after selling Fleet Nasrullah and shipping him to Kentucky, they informed plaintiff “(y)ou are, therefore, released from your reservations made to the stallion.” However, the trial court additionally found that “(p)laintiff did not wish to be ‘released’ from his ‘reservations’ . . . insist(ed) on performance of the stud service agreements . . . (and) threaten(ed) litigation if the contracts were not honored by defendants . . .” Accordingly defendants arranged for performance of the contracts by making Fleet Nasrullah available for stud service to plaintiff in Kentucky through their agents Dr. Pessin and Mrs. Judy. Plaintiff elected to treat the contracts as in force and shipped the mares to Kentucky to effect the desired performance. The foregoing facts lead us to conclude that the subsequent arrangements by defendants to make Fleet Nasrullah available to service plaintiff’s mares in Kentucky constituted a retraction of the repudiation. Since at this time plaintiff had not elected to treat the repudiation as an anticipatory breach and in fact had shipped the mares to Kentucky in reliance on defendants’ arrangements, this retraction nullified the repudiation. Thus, plaintiff was then left with his remedies that might arise at the time of performance.

The trial court found that after the mares had arrived in Kentucky, had delivered the foals they were then carrying and were ready for servicing by Fleet Nasrullah, plaintiff was justified in concluding from the conduct of defendants, their agent Dr. Pessin, and their subagent Mrs. Judy, that “defendants were just giving him the runaround and had no intention of performing their contract in the manner required by its terms” and in treating such conduct “as a breach and repudiation of their contractual obligation to him.” Since, as we have explained, defendants retracted their original repudiation, this subsequent conduct amounts to a finding of a second repudiation.

There is no evidence in the record that defendants or their agents Dr. Pessin and Mrs. Judy ever stated that Sunday Slippers and Sandy Fork would not be serviced by Fleet Nasrullah during the 1966 breeding season or that they ever refused to perform. Frazier, plaintiff’s agent who made arrangements for the breeding of the mares admitted that they had never made

such a statement to him. Accordingly, there was no Express repudiation or unequivocal refusal to perform.

The trial court's finding of repudiation, expressly based on the "conduct of the defendants" and their agents suggests that the court found an implied repudiation. However, there is no implied repudiation, i.e., by conduct equivalent to an unequivocal refusal to perform, unless the promisor Puts it out of his power to perform. Once the mares arrived in Kentucky, defendants had the power to perform the contracts; Fleet Nasrullah could breed with the mares. No subsequent conduct occurred to render this performance impossible. Although plaintiff was subordinated to the shareholders with respect to the priority of reserving a breeding time with Fleet Nasrullah, there is no evidence in the record that this subordination of reservation rights rendered performance impossible. Rather it acted to postpone the time of performance, which still remained within the limits prescribed by the contracts. It rendered performance more difficult to achieve; it may even have cast doubt upon the eventual accomplishment of performance; it did not render performance impossible.<sup>12</sup>

Because there was no repudiation, express or implied, there was no anticipatory breach. Plaintiff contends that defendants' conduct, as found by the trial court, indicated that "defendants were just giving him the runaround and had no intention of performing their contract" and therefore that this conduct was the equivalent of an express and unequivocal refusal to perform. Plaintiff has not presented to the court any authority in California in support of his proposition that conduct which has not met the test for an implied repudiation, i.e. conduct which removed the power to perform, may nonetheless be held to amount to the equivalent of an express repudiation and thus constitute an anticipatory breach. Without addressing ourselves to the question whether some conduct could ever be found equal to an express repudiation, we hold that defendants' conduct in this case as a matter of law did not constitute an anticipatory breach.

To constitute an express repudiation, the promisor's statement, or in this case conduct, must amount to an unequivocal refusal to perform . . . To justify the adverse party in treating the renunciation as a breach, the refusal to perform must be of the whole contract . . . and must be distinct, unequivocal, and absolute . . .

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<sup>12</sup> . . . Assuming arguendo that [the defendants' delays] might have amounted to a breach of contract by improperly delaying performance, at most it would have constituted only a partial breach—insufficiently material to terminate the contracts. It did not constitute a repudiation of the contracts which was the sole basis of the trial court's decision since to justify the adverse party in treating the renunciation as a breach, the refusal to perform must be of the whole contract or of a covenant going to the whole consideration . . .



Sunday Slippers foaled on April 17, 1966, first came into heat on April 26 and then successively on May 13 and June 4, 1966. Mrs. Judy informed Frazier that she would breed Sunday Slippers on any day that one of the shareholders did not want to use the stallion. Frazier unsuccessfully sought to breed the mare on April 26, May 14, May 15 and June 4, 1966, Fleet Nasrullah being reserved on those dates. Mrs. Judy continued to assure Frazier that the breeding would occur. Sunday Slippers was due to come into heat again twice during the breeding season: June 25 and July 16, 1966. At most this conduct amounts to delay of performance and a warning that performance might altogether be precluded if a shareholder were to desire Fleet Nasrullah's services on all the remaining days within the period specified for performance in which Sunday Slippers was in heat. We conclude that as a matter of law this conduct did not amount to an unequivocal refusal to perform and therefore did not constitute an anticipatory breach of the contract covering Sunday Slippers.

In sum, we hold that there is no evidence in the record supportive of the trial court's finding and conclusion that defendants repudiated and therefore committed an anticipatory breach of the contracts . . . .

The judgment is reversed.

WRIGHT, C.J., and McCOMB, TOBRINER, MOSK, CLARK and RICHARDSON, JJ., concur.

### Notes and Questions

1. The California Supreme Court explained that repudiation can be either in a statement (an express repudiation) or by an action that makes performance impossible (an implied repudiation). Those two possible ways to repudiate a contract were discussed in *Hochster v. De La Tour* as well. Because repudiation gives the injured party significant power—to sue for anticipatory breach before a promise is due—courts are careful and apply quite a high threshold before finding repudiation. For example, the Restatement explains that when a party states that it “will not perform,” that statement can be considered repudiation, but the statement “I am not sure that I can perform, and I do not intend to do so unless I am legally bound to” is not. Restatement (Second) of Contracts § 250, cmt. b.
2. Another requirement concerning both express and implied repudiation has to do with the gravity of the threatened breach. The threat needs to be of a breach that would be considered a total breach (one that allows the promisee to discharge the contract).

For example, consider a contract for a sale of land that requires the seller to deliver possession of the property, free of any third parties' rights, no later than July 1 at noon. Is it a repudiation if the seller tells the buyer that he will not be able to deliver possession until the afternoon of July 1? Is it a repudiation if the seller leases the property to a third party until July 1 at 2 pm? We think that, in most cases, the answer is no. Unless there are special circumstances (what would they be?), a buyer is unable to discharge a sale of land contract for a two-hour delay in performance and, if that is the case, a threat of such a breach is not a repudiation. If *and when* the seller is late in delivering possession, the buyer will be entitled to be compensated for the harm caused by this partial breach and nothing more.

3. With that in mind, do you understand why Johnson's October 4 letter was a repudiation? The court explained that at that moment in time, Tyler had the choice between suing "immediately" for an anticipatory breach or waiting for the Johnsons to perform, thus allowing them to retract their repudiation. Considering that Tyler could have immediately sued (and probably knew it, as he was represented by a lawyer), why didn't he? Doesn't the case itself show that the recipient of a repudiation should always immediately sue?
4. On October 27, 23 days after the repudiation, the Johnsons announced that they had made arrangements to perform the contract. This is considered retraction or nullification of the repudiation, which the repudiating party is free to do "before [the injured party] materially changes his position in reliance on the repudiation or indicates to the other party that he considers the repudiation to be final." Restatement (Second) of Contracts § 256.
5. The court in *Taylor* mentions that the injured party *can* "immediately" sue for anticipatory breach. Does it *have* to sue immediately? Does the injured party lose its right to sue for anticipatory breach by waiting? While that question is not settled everywhere, a California Court of Appeal answered both questions in the negative, holding that as long as the repudiating party does not retract the repudiation, the injured party can still sue for anticipatory breach. *Central Valley General Hospital v. Smith*, 162 Cal.App.4th 501 (2008). The facts of that case nicely support that conclusion. In that case, a seller of a business warranted that certain representations would be true upon closing, including that it managed its businesses legally. It turned out that he did not. That was, of course, not fixable, and it was guaranteed that the seller would be in breach as soon as the transaction closed. Under those circumstances, it would have been

unreasonable to require the buyer to close (and pay!) before it could bring a claim for total breach.

6. The court mentions that the Johnsons counter-sued for the breeding fee (which was quite substantial). Are they entitled to it?
7. Shouldn't we have some sympathy for Taylor? Doesn't this California case feel a little like New-York-style formalism? After all, wasn't Taylor wronged? Do you think he envisioned, when entering the contract, that he would find himself with two mares boarding in Kentucky for months while chasing third parties that kept rescheduling their performance? Is there anything Taylor could have done differently? One clue is in footnote 12. Another, and maybe a superior course of action, is to ask for assurances for future performance. The next case discusses this possibility.

**Norcon Power Partners, L.P. v. Niagara Mohawk Power Corp.**

92 N.Y.2d 458 (Court of Appeals of New York, 1998)

BELLACOSA, Judge.

The doctrine, known as demand for adequate assurance of future performance, is at the heart of a Federal lawsuit that stems from a 1989 contract between Norcon Power Partners, L.P., an independent power producer, and Niagara Mohawk Power Corporation, a public utility provider. Niagara Mohawk undertook to purchase electricity generated at Norcon's Pennsylvania facility. The contract was for 25 years, but the differences emerged during the early years of the arrangement.

The case arrives on this Court's docket by certification of the substantive law question from the United States Court of Appeals for the Second Circuit. Our Court is presented with an open issue that should be settled within the framework of New York's common-law development. We accepted the responsibility to address this question involving New York contract law:

“Does a party have the right to demand adequate assurance of future performance when reasonable grounds arise to believe that the other party will commit a breach by non-performance of a contract governed by New York law, where the other party is solvent and the contract is not governed by the U.C.C.?” (*Norcon Power Partners v. Niagara Mohawk Power Corp.*, 110 F.3d 6, 9 (2nd Cir.1997).)

As framed by the particular dispute, we answer the law question in the affirmative with an appreciation of this Court's traditional common-law developmental method, and as proportioned to the precedential sweep of our rulings.

I.

[The court describes the rather complex compensation structure. During the first period of the contract the price is fixed. During the second period the price fluctuates according to "avoided costs" (a formula that is partly based on certain market prices), but it is also subject to a floor (and a ceiling, which turns out to be irrelevant). The parties also kept a "Cumulative Avoided Cost Account" to track the difference between payment actually made and the avoided costs formula. In the third period the price was the avoided costs, without a floor. In addition, they agreed that the credit that the buyer had in the "Cumulative Avoided Cost Account" (if any) will be credited to it during the third period and, if anything remains, be paid to the buyer within 30 days after the end of the third period.]

In February 1994, Niagara Mohawk presented Norcon with a letter stating its belief, based on revised avoided cost estimates, that substantial credits in Niagara Mohawk's favor would accrue in the adjustment account during the second pricing period. "[A]nalysis shows that the Cumulative Avoided Cost Account \* \* \* will reach over \$610 million by the end of the second period." Anticipating that Norcon would not be able to satisfy the daily escalating credits in the third period, Niagara Mohawk demanded that "Norcon provide adequate assurance to Niagara Mohawk that Norcon will duly perform all of its future repayment obligations."

Norcon promptly sued Niagara Mohawk in the United States District Court, Southern District of New York. It sought a declaration that Niagara Mohawk had no contractual right under New York State law to demand adequate assurance, beyond security provisions negotiated and expressed in the agreement. Norcon also sought a permanent injunction to stop Niagara Mohawk from anticipatorily terminating the contract based on the reasons described in the demand letter. Niagara Mohawk counterclaimed. It sought a counter declaration that it properly invoked a right to demand adequate assurance of Norcon's future payment performance of the contract.

The District Court granted Norcon's motion for summary judgment. It reasoned that New York common law recognizes the exceptional doctrine of demand for adequate assurance only when a promisor becomes insolvent, and also when the statutory sale of goods provision under UCC § 2-609, is involved. Thus, the District Court ruled in Norcon's favor because neither exception applied, in fact or by analogy to the particular dispute.

The Second Circuit Court of Appeals preliminarily agrees with the District Court that, except in the case of insolvency, no common-law or statutory right to demand adequate assurance exists under New York law which would affect non-UCC contracts, like the instant one. Because of the uncertainty concerning this substantive law question the Second Circuit certified the question to our Court as an aid to its correct application of New York law, and with an eye toward settlement of the important precedential impact on existing and future non-UCC commercial law matters and disputes.

## II.

Our analysis should reference a brief review of the evolution of the doctrine of demands for adequate assurance. Its roots spring from the doctrine of anticipatory repudiation (*see*, Garvin, *Adequate Assurance of Performance: Of Risk, Duress, and Cognition*, 69 U. Colo. L. Rev. 71, 77 [1998]). Under that familiar precept, when a party repudiates contractual duties prior to the time designated for performance and before all of the consideration has been fulfilled, the repudiation entitles the nonrepudiating party to claim damages for total breach (*see*, II Farnsworth, Contracts § 8.20; Restatement [Second] of Contracts § 253; UCC § 2–610). A repudiation can be either “a statement by the obligor to the obligee indicating that the obligor will commit a breach that would of itself give the obligee a claim for damages for total breach” or “a voluntary affirmative act which renders the obligor unable or apparently unable to perform without such a breach” (Restatement [Second] of Contracts § 250; *see*, II Farnsworth, Contracts § 8.21; UCC § 2–610, Comment 1).

That switch in performance expectation and burden is readily available, applied and justified when a breaching party’s words or deeds are unequivocal. Such a discernible line in the sand clears the way for the nonbreaching party to broach some responsive action. When, however, the apparently breaching party’s actions are equivocal or less certain, then the nonbreaching party who senses an approaching storm cloud, affecting the contractual performance, is presented with a dilemma, and must weigh hard choices and serious consequences. One commentator has described the forecast options in this way:

“If the promisee regards the apparent repudiation as an anticipatory repudiation, terminates his or her own performance and sues for breach, the promisee is placed in jeopardy of being found to have breached if the court determines that the apparent repudiation was not sufficiently clear and unequivocal to constitute an anticipatory repudiation justifying nonperformance. If, on the other hand, the promisee continues to perform after perceiving an apparent repudiation, and it is subsequently determined that an

anticipatory repudiation took place, the promisee may be denied recovery for post-repudiation expenditures because of his or her failure to avoid those expenses as part of a reasonable effort to mitigate damages after the repudiation” (Crespi, *The Adequate Assurances Doctrine after U.C.C. § 2–609: A Test of the Efficiency of the Common Law*, 38 Vill. L. Rev. 179, 183 [1993]).

### III.

The Uniform Commercial Code settled on a mechanism for relieving some of this uncertainty. It allows a party to a contract for the sale of goods to demand assurance of future performance from the other party when reasonable grounds for insecurity exist (see, UCC § 2–609; II Farnsworth, *CONTRACTS* § 8.23). When adequate assurance is not forthcoming, repudiation is deemed confirmed, and the nonbreaching party is allowed to take reasonable actions as though a repudiation had occurred.

UCC § 2–609 provides, in relevant part:

“(1) A contract for sale imposes an obligation on each party that the other’s expectation of receiving due performance will not be impaired. When reasonable grounds for insecurity arise with respect to the performance of either party the other may in writing demand adequate assurance of due performance and until he receives such assurance may if commercially reasonable suspend any performance for which he has not already received the agreed return. \* \* \*

“(4) After receipt of a justified demand failure to provide within a reasonable time not exceeding thirty days such assurance of due performance as is adequate under the circumstances of the particular case is a repudiation of the contract.”

In theory, this UCC relief valve recognizes that “the essential purpose of a contract between commercial [parties] is actual performance . . . and that a continuing sense of reliance and security that the promised performance will be forthcoming when due, is an important feature of the bargain” (UCC § 2–609, Comment 1). In application, section 2–609 successfully implements the laudatory objectives of quieting the doubt a party fearing repudiation may have, mitigating the dilemma flowing from that doubt, and offering the nonbreaching party the opportunity to interpose timely action to deal with the unusual development.

Indeed, UCC § 2–609 has been considered so effective in bridging the doctrinal, exceptional and operational gap related to the doctrine of anticipatory breach that some States have imported the complementary regimen of demand for adequate assurance to common-law

categories of contract law, using UCC § 2–609 as the synapse (see, e.g., *Lo Re v. Tel–Air Communications*, 200 N.J.Super. 59, 490 A.2d 344 [finding support in UCC § 2–609 and Restatement (Second) of Contracts § 251 for applying doctrine of adequate assurance to contract to purchase radio station]; *Conference Ctr. v. TRC—The Research Corp. of New England*, 189 Conn. 212, 455 A.2d 857 [analogizing to UCC § 2–609, as supported by Restatement (Second) of Contracts § 251, in context of constructive eviction]).

Commentators have helped nudge this development along. They have noted that the problems redressed by UCC § 2–609 are not unique to contracts for sale of goods, regulated under a purely statutory regime. Thus, they have cogently identified the need for the doctrine to be available in exceptional and qualifying common-law contractual settings and disputes because of similar practical, theoretical and salutary objectives (e.g., predictability, definiteness, and stability in commercial dealings and expectations).

The American Law Institute through its Restatement (Second) of Contracts has also recognized and collected the authorities supporting this modern development. Its process and work settled upon this black letter language:

“(1) Where reasonable grounds arise to believe that the obligor will commit a breach by non-performance that would of itself give the obligee a claim for damages for total breach under § 243, the obligee may demand adequate assurance of due performance and may, if reasonable, suspend any performance for which he has not already received the agreed exchange until he receives such assurance.

“(2) The obligee may treat as a repudiation the obligor’s failure to provide within a reasonable time such assurance of due performance as is adequate in the circumstances of the particular case” (Restatement [Second] of Contracts § 251).

Modeled on UCC § 2–609, Restatement § 251 tracks “the principle that the parties to a contract look to actual performance “and that a continuing sense of reliance and security that the promised performance will be forthcoming when due, is an important feature of the bargain” (Restatement [Second] of Contracts § 251, comment a, quoting UCC § 2–609, Comment 1). The duty of good faith and fair dealing in the performance of the contract is also reflected in section 251 (see, Restatement [Second] of Contracts § 251, comment a ).

Some States have adopted Restatement § 251 as their common law of contracts, in varying degrees and classifications (see, e.g., *Carfield & Sons v. Cowling*, 616 P.2d 1008 [Colo] [construction contract]; *L.E. Spitzer Co. v. Barron*, 581 P.2d 213 [Alaska] [construction

contract]; *Drinkwater v. Patten Realty Corp.*, 563 A.2d 772 [Me] [sale of real estate]; *Jonnet Dev. Corp. v. Dietrich Indus.*, 316 Pa.Super. 533, 463 A.2d 1026 [real estate lease]; but see, *Mollohan v. Black Rock Contr.*, 160 W.Va. 446, 235 S.E.2d 813 [declining to adopt section 251, except to the extent that failure to give adequate assurance on demand may be some evidence of repudiation]).

#### IV.

New York, up to now, has refrained from expanding the right to demand adequate assurance of performance beyond the Uniform Commercial Code. The only other recognized exception is the insolvency setting. Hence, the need for this certified question emerged so this Court could provide guidance towards a correct resolution of the Federal lawsuit by settling New York law with a modern pronouncement governing this kind of contract and dispute.

Niagara Mohawk, before our Court through the certified question from the Federal court, urges a comprehensive adaptation of the exceptional demand tool. This wholesale approach has also been advocated by the commentators. Indeed, it is even reflected in the breadth of the wording of the certified question.

This Court's jurisprudence, however, usually evolves by deciding cases and settling the law more modestly (*Rooney v. Tyson*, citing Cardozo, *Nature of the Judicial Process*, in *Selected Writings of Benjamin Nathan Cardozo*, at 115, 134 [Margaret E. Hall ed. 1947] [observing that Judges proceed interstitially]). The twin purposes and functions of this Court's work require significant professional discipline and judicious circumspection.

We conclude, therefore, that it is unnecessary, while fulfilling the important and useful certification role, to promulgate so sweeping a change and proposition in contract law, as has been sought, in one dramatic promulgation. That approach might clash with our customary incremental common-law developmental process, rooted in particular fact patterns and keener wisdom acquired through observations of empirical application of a proportioned, less than absolute, rule in future cases.

It is well to note the axiom that deciding a specific case, even with the precedential comet's tail its rationale illuminates, is very different from enacting a statute of general and universal application.

Experience and patience thus offer a more secure and realistic path to a better and fairer rule, in theory and in practical application. Therefore, this Court chooses to take the traditionally subtler approach, consistent with the proven benefits of the maturation process of the



common law, including in the very area of anticipatory repudiation which spawns this relatively newer demand for assurance corollary.

This Court is now persuaded that the policies underlying the UCC § 2–609 counterpart should apply with similar cogency for the resolution of this kind of controversy. A useful analogy can be drawn between the contract at issue and a contract for the sale of goods. If the contract here was in all respects the same, except that it was for the sale of oil or some other tangible commodity instead of the sale of electricity, the parties would unquestionably be governed by the demand for adequate assurance of performance factors in UCC § 2–609. We are convinced to take this prudent step because it puts commercial parties in these kinds of disputes at relatively arm’s length equilibrium in terms of reliability and uniformity of governing legal rubrics. The availability of the doctrine may even provide an incentive and tool for parties to resolve their own differences, perhaps without the necessity of judicial intervention. Open, serious renegotiation of dramatic developments and changes in unusual contractual expectations and qualifying circumstances would occur because of and with an eye to the doctrine’s application.

The various authorities, factors and concerns, in sum, prompt the prudence and awareness of the usefulness of recognizing the extension of the doctrine of demand for adequate assurance, as a common-law analogue. It should apply to the type of long-term commercial contract between corporate entities entered into by Norcon and Niagara Mohawk here, which is complex and not reasonably susceptible of all security features being anticipated, bargained for and incorporated in the original contract. Norcon’s performance, in terms of reimbursing Niagara Mohawk for credits, is still years away. In the meantime, potential quantifiable damages are accumulating and Niagara Mohawk must weigh the hard choices and serious consequences that the doctrine of demand for adequate assurance is designed to mitigate. This Court needs to go no further in its promulgation of the legal standard as this suffices to declare a dispositive and proportioned answer to the certified question.

Accordingly, the certified question should be answered in the affirmative.

Chief Judge KAYE and Judges SMITH, LEVINE, CIPARICK and WESLEY concur.

### **Notes and Questions**

1. Professor Victor Goldberg explored some of the facts underlying this litigation. Both federal and state laws heavily regulate the energy industry. As part of this complex scheme, utility companies (like Niagara) were required to buy energy from smaller

alternative power producers, called qualified suppliers (Norcon being one of them). Like the one litigated here, those agreements were subject to and approved by state and federal regulators. Many of those agreements were front-loaded, meaning that the supplier received higher payments early on and lowered payments later on.

In this case, the agreement turned out to be significantly more front-loaded than expected. The contract set forth three periods for performance, and things got off the rails in the second period. The contract stated a floor based on the expected market price in the second period. It turned out that the market prices were much lower than envisioned in that period, and, therefore, Niagara was overpaying. By a lot. \$610 million by one estimation. Niagara was supposed to receive this amount as credit during the third period, but would it? According to Niagara's calculations, paying it back would have required Norcon to provide Niagara with free electricity during the ten years of the third period plus between \$25 million and \$125 million a year. A Niagara expert suggested that Norcon will be operating at a loss of \$23.2 million to \$108.9 million in each of the last ten years of the agreement.

As the court noted, Niagara held a security interest over Norcon's plant, but even if it could have foreclosed it, it would have reduced Norcon's debt from \$610 million to \$412 million. Interestingly, during the formation of this contract, Niagara was concerned that it was not provided with enough security for front-loading nature of the agreement, but the regulators did not allow it to demand more significant guarantees during formation.

If you were in Niagara's position, wouldn't you be afraid that after years of overpaying, Norcon's shareholders would just step away, abandon their company, and leave Niagara with a breached contract and a large unpaid debt?

You can find many more details about this agreement and litigation, including how similar it was to other transactions between utility companies and their supplier at the time, in Victor P. Goldberg, *A Precedent Built on Sand: Norcon v. Niagara Mohawk*, 2013 COLUM. BUS. L. REV 38.

2. The New York Court of Appeals listed multiple benefits for the doctrine of adequate assurance, but at the end of the opinion, it refused to adopt it in its entirety, opting for an incremental approach. While the court explained some of the advantages of such an approach, one clear disadvantage is that parties to non-UCC transactions might not know if they can request adequate assurances. Indeed, The New York Court of Appeals

mentions that the adequate assurances doctrine provides parties with some reliance and security. Is that true even when it is adopted in this incremental way?

3. Read the last two paragraphs in the opinion and try to identify factors that led the court to apply the doctrine in the case of *Niagara*. Try to apply those factors in other situations. For example, can parties to a real estate purchase agreement ask for adequate assurances? Can a general contractor ask a landowner for them? Can it ask its subcontractors?
4. One of the motivations for adopting the adequate assurances mechanism is to give some security to parties that are unsure if the other party repudiated or not (think of Tyler's situation in *Tyler v. Harrison*). However, the doctrine creates its own uncertainty. It is considered a repudiation of the contract when adequate assurances are (i) allowed, (ii) justifiably demanded, and (iii) not provided. The other side (the obligee) can treat such a repudiation as an anticipatory breach, stop performing its own obligations, and sue. But what if the obligee is not sure whether the jurisdiction would recognize the doctrine of adequate assurance, whether its doubts concerning performance are meaningful enough to justify a demand for adequate assurances, or whether the assurances it was provided are adequate? An unjustified request for assurances is likely repudiation in itself (do you see why?) and stopping performance by mistakenly believing the other side repudiated is a breach.
5. Are you surprised to learn that the New York Court of Appeals has not revisited the adequate assurances doctrine since *Norcon v. Niagara Mohawk* was decided? Lower courts in the state addressed it from time to time. The Appellate Division (the mid-tier courts in the New York system) refused to extend the doctrine in cases involving a long-term construction loan agreement, *Bank of New York v. River Terrace Associates, LLC*, 23 A.D.3d 308 (2005), and a real estate purchase agreement, *Peng v. Willets Point Asphalt Corp.*, 81 A.D.3d 618 (2011).
6. In many states it is unclear whether the adequate assurances doctrine applies outside of sales of goods (where UCC § 2-609 mandates it). Those states include California and, as might be relevant for our next case, Arkansas. That case addresses several concepts we have tackled in the last two sections.

**Crystal Clear Computer Solutions, LLC v. City of Helena-West Helena**

559 F.Supp.3d 837 (E.D. Arkansas, 2021)

LEE P. RUDOFISKY, Judge.

Crystal Clear Computer Solutions, LLC (“Crystal Clear”) and its President, Trever Simes, brought this lawsuit against the City of Helena-West Helena (“the City”) for breach of contract and against Mayor Kevin Smith for tortious interference with an existing contractual relationship. Before the Court today are cross-motions for summary judgment on the breach of contract claim and Mayor Smith’s Motion for Summary Judgment on the tortious interference claim. For the reasons explained in this Order, Crystal Clear’s Motion for Summary Judgment on the breach of contract claim is GRANTED in part and DENIED in part. Crystal Clear is owed payment for the time the contract was still in effect (i.e., up to July 15, 2019). The City’s Motion for Summary Judgment is GRANTED as to the remainder of the breach of contract claim. Mayor Smith’s Motion for Summary Judgment is GRANTED as to the tortious interference claim.

**I. BACKGROUND**

Crystal Clear is a Mississippi LLC that provides information technology (“IT”) support and services. On November 7, 2017, the City Council selected Crystal Clear to provide the City with IT services. The City Council approved a contract (“the Agreement”) with Crystal Clear for “a period of five years at a rate of \$5,795.00 per month.” On November 8, 2017, the Agreement was signed by then-Mayor Jay Hollowell (on behalf of the City) and Mr. Simes (on behalf of Crystal Clear).

The Agreement stated that it would become effective on “January 1, 2018, [and] shall remain in force for a period of five years.” Crystal Clear was given the power to terminate the Agreement “upon ninety (90) days written notice.” The City’s power to terminate the Agreement, on the other hand, was more limited. The City also had to provide ninety-days’ written notice to terminate, but it could only do so in certain circumstances: (1) if Crystal Clear failed “in any material respect” to satisfy its obligations and did not cure the failure within ninety days of written notice; (2) if Crystal Clear breached “any material term or condition” and did not remedy the breach within ninety days of written notice; or (3) if Crystal Clear terminated or suspended its business operations “unless it is succeeded by a permitted assignee under this Agreement.” The Agreement further stated:

Fees will be \$5,975.00 per month, invoiced to [the City] on a monthly basis and will become due and payable on the first day of each month . . . Services will be suspended if payment is not received within 5 days following date due.

The first year of the contract was largely uneventful, and City employees provided Crystal Clear with positive feedback. Perhaps the only noteworthy thing about the first year was the City's relatively routine late payments. In his deposition testimony, Mr. Simes noted that late payments from the City were not unusual. The City's "Vendor Ledger" certainly indicates that late payments (sometimes days late, sometimes weeks late, and sometimes months late) were the norm. Despite the inconsistent frequency of payment, there is no indication that Crystal Clear suspended services in 2018.

Mayor Hollowell was defeated in the 2018 election, and Mayor Kevin Smith was chosen as the next Mayor of Helena-West Helena. It is at this point the relationship between Crystal Clear and the City began to sour. Around the start of his term, Mayor Smith began discussing the legality of the contract with the Arkansas Municipal League. Mayor Smith also sought an "apples to apples" quote from Sophicity, an IT services provider that works with the Arkansas Municipal League and various municipalities. These discussions with the Arkansas Municipal League and Sophicity began, at the latest, on December 31, 2018.

In January 2019, Mr. Simes met with Mayor Smith (at Mayor Smith's request) to discuss the Agreement. Mayor Smith asked Mr. Simes to rebid the contract after learning "there were less costly options available to the City." Mr. Simes did not agree to rebid. There is no suggestion that, at this time, the Mayor told Mr. Simes that the City would not honor the Agreement.

The City was late paying its January and February 2019 bills. These months were not paid until the end of March 2019 at the earliest. The City did not pay its March 2019 bill on time. It is unclear whether the City paid its March 2019 bill late or did not pay this bill at all. The City has not paid its April, May, and June 2019 invoices.

While Crystal Clear went unpaid, Mayor Smith caused the City to pay \$3,410.00 to Global Technology Service Providers ("Global") for IT services on May 8, 2019. Global is owned by John Dalencourt, a friend and political supporter of Mayor Smith. While the exact nature of the relationship between Global and the City is disputed, Mayor Smith's Chief of Staff told Sophicity (the other IT service provider that submitted a bid to Mayor Smith) that "[t]he mayor has decided for the time being to go with an IT proposal from a local vendor on a month to month basis."

The IT situation soon came to a head, as evidenced by a series of e-mails exchanged on May 14, 2019. Mayor Smith's Chief of Staff e-mailed Mr. Simes requesting that he "connect with John Dalencourt about IT transition." The word "transition" is something of a buzzword in this context, because the Agreement between Crystal Clear and the City says that if the contract is terminated, Crystal Clear would "assist [the City] in the orderly termination of services, including timely transfer of the services to another designated provider."

Mr. Simes protested, noting that he was still under contract for four years, and refused to coordinate with Mr. Dalencourt "until I get an official letter from the City." Mayor Smith then reached out to Mr. Simes directly, demanding that within twenty-four hours Mr. Simes "turn over all passwords and usernames, any other security and access permissions regarding all work you have done with the City of Helena-West Helena to the Office of Mayor." At this time, Mr. Simes did not turn over the data, Crystal Clear did not suspend services, and Mayor Smith did not take further action on May 14. It appears instead that Mr. Simes or his allies went to the City Council for assistance.

During a heated City Council meeting on May 21, 2019, members of the City Council and City Attorney Andre Valley confronted Mayor Smith about the payment made to Mr. Dalencourt and the payments due to Crystal Clear. Mr. Valley advised Mayor Smith that paying Mr. Dalencourt was unauthorized spending and that the City's primary focus should be to "pay the people we owe." Mr. Valley and members of the City Council forcefully and repeatedly reminded Mayor Smith that the City was under contract with Crystal Clear and cautioned Mayor Smith against attempts to terminate the Agreement due to the potential of litigation against the City.

Mayor Smith justified his solicitation of bids from Mr. Dalencourt and Sophicity by saying he was given legal advice that doing so was necessary to determine if the contract with Crystal Clear violated the Arkansas Constitution. Mayor Smith maintained that he had a constitutional duty to not make payments to Crystal Clear given the City's financial condition and the cheaper options available. Mayor Smith also said that the payments to Crystal Clear were being "held up until he turns over this information we requested," not because the City had terminated the contract but because the City owns the information.

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On May 30, 2019, Mr. Simes sent a letter to City Clerk Sandi Ramsey and members of the City Council notifying them that services would be suspended if the City did not become current on payments. The letter stated:

If payments are not received by June 3rd we will have to suspend all services per the agreement. We truly hope that we can continue our long relationship with the city.

However, if we received [sic] full payments by June 7th we will continue with our support. If not we will have to take further actions. We will have to completely delete all of your data backups and will not be able to get them back. We will remove all of your systems from our tools, and all of our usernames from all of your systems.

Mr. Simes made good on his threat to suspend services on June 3, 2019. . . . No payments were made by June 7, the second deadline Mr. Simes gave the City. It is not clear whether Mr. Simes took all, part, or none of the “further” actions threatened in his letter.

An eighteen-day long silence between the parties was broken on June 21, 2019, when City Treasurer Derrick Turner contacted Mr. Simes in an attempt to bring the City current with all payments. [On several occasions in late June Turner told Simes that the company is going to be paid.] Mr. Turner had the expectation that Crystal Clear would resume services once the City was made current on its payments.

[Starting on June 28, 2019, Turner made repeat attempts to pay Crystal Clear. Simes first agreed to meet to be paid but then asked Turner to mail the payment. Simes also implied that once that happened the services would resume. The checks that were mailed on July 1 were not received by the company. Turner continued to try and meet with Simes. On July 11, however, Simes cancelled their scheduled meeting and stopped answering Turner’s messages.]

What Mr. Turner did not know when he made [his] final inquiry is that the previous day, July 15, 2019, Mr. Simes sent an e-mail and letter to Mayor Smith and City Attorney Valley notifying them of Crystal Clear’s immediate cancellation of the contract. The Notice of Cancellation of the Contract stated:

Dear Mayor Kevin Smith:

As a result of the City’s repudiation and prevention of the January 1, 2018, Managed Services Agreement . . . Crystal Clear Computer hereby cancels the Managed Services Restatement Agreement and gives notice that it will seek recovery of the damages incurred, including attorneys’ fees, as a result of the material and total breach of contract by the City.

Acts constituting the repudiation of the Managed Services Agreement:

- 1) The City demanded in January 2019 that Crystal Clear Computer rebid the Managed Services Agreement;
- 2) The City solicited bids from other service providers in January 2019;
- 3) The City failed to pay invoices for services provided April through May of 2019;
- 4) On May 14, 2019, the City requested that Crystal Clear Computer meet with John Dalencourt so that IT transition to Dalencourt could be executed; and
- 5) The City failed to pay the June invoice for services provided in June of 2019.

Acts by the City constituting prevention of contract performance by Crystal Clear Computer:

- 1) On May 14, 2019, the City demanded the return of all passwords, usernames, and security and access permissions.

Plaintiffs then filed suit in this Court against the City for breach of contract and against Mayor Kevin Smith for tortious interference with an existing contractual relationship. Both sides have moved for summary judgment on the breach of contract claim against the City, and Mayor Smith has moved for summary judgment on the tortious interference claim against him.

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### III. BREACH OF CONTRACT

Crystal Clear primarily argues that the months of unpaid invoices constituted a material breach such that it could immediately end the Agreement and bring suit. Crystal Clear also contends that Mayor Smith's actions, coupled with "the City Council's failure to enjoin or remove Kevin Smith," amounted to a repudiation of the Agreement by the City. The City maintains that it was making efforts to "become current on payments due," and thus the Agreement "ended at the behest of Mr. Simes."

#### A. The City's Late Payments Did Not Entitle Crystal Clear to End the Agreement

Any nonperformance of a duty contemplated under a contract is a breach. Thus, the City did breach the Agreement when it failed to pay its April, May, and June 2019 invoices. But was



the breach material? Only a material breach relieves the other party's full contractual obligations.<sup>75</sup>

A material breach is a failure to perform an essential term or condition that substantially defeats the purpose of the contract for the other party. An influential circumstance in the determination of the materiality of a failure to fully perform a contract is the extent to which the injured party will obtain the substantial benefit that she reasonably anticipated. This wording is nearly identical to the first of five "circumstances significant in determining whether a failure is material" from the Restatement (Second) of Contracts section 241. Crystal Clear argues that the late payments were a material breach by weighing this and the remaining factors listed in section 241 . . .

The first factor for this court to consider is the extent to which Crystal Clear will be deprived of the benefit which it reasonably expected. The sole benefit expected under the Agreement was money in exchange for services each month. Thus, when the City breached by failing to pay, Crystal Clear was deprived entirely of the benefit it reasonably expected. This factor weighs in favor of a material breach.

The second factor is the extent to which Crystal Clear could be adequately compensated for the part of the benefit of which it will be deprived. Because the benefit of which it will be deprived is money, and because it is an easily measured amount of money, Crystal Clear could be adequately compensated. This factor weighs against a material breach.

The third factor is the extent to which the City would suffer forfeiture if the breach were deemed material. The City would not suffer any forfeiture here. There were no investments or preparations made with the expectation of the Agreement continuing, nor did the City pay in advance for any services that Crystal Clear ultimately did not perform. This factor weighs in favor of a material breach.

The fourth and, in this case, critical factor is the likelihood that the City would have cured the breach, considering "all circumstances, including any adequate assurances that the failure will be cured." The facts of this case establish that the City intended to become current on its payments with the expectation that the Agreement would continue. Mr. Simes knew this. No rational juror could conclude otherwise on this record.

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<sup>75</sup> It is sometimes said that the materiality of a breach is a question of fact. However, the Arkansas Supreme Court has ruled on the substantiality of a breach as a matter of law. . . .

From the beginning, it was not unusual for the City to fall behind on payments. This was the case even before Mayor Smith took office and expressed his displeasure with the Agreement. After Mayor Smith took office, the City fell behind for the months of January, February, and March but Crystal Clear continued under the Agreement and eventually received payment (certainly for January and February, and Crystal Clear maintains it was paid for March). Moreover, before Mr. Simes sent the Notice of Cancellation on July 15, 2019, the City Treasurer had already printed and mailed one batch of checks and was making efforts to hand-deliver the replacement batch. Mr. Simes knew this. In fact, the day after Mr. Simes sent the cancellation notice, Mr. Turner (who did not know of the cancellation at the time) made another attempt to bring the City current on payments. It is clear, then, that the City had every intention and ability to make the back payments and continue with the Agreement. Recall also that, just weeks before, the City Council made clear to the Mayor that the Agreement was still in effect and had to be honored. This factor weighs heavily against a material breach.

The final factor to consider is the extent to which the City's behavior was "consistent with standards of good faith and fair dealing." Crystal Clear argues that bad faith has been established because the City engaged in "subterfuges and evasion," the Mayor was determined to terminate the contract "by any means," and Mr. Turner's "equivocation frustrated what might otherwise have been an effort to keep the agreement intact and suggests that his actions were unauthorized."

Crystal Clear does not specify exactly what acts by the City amount to subterfuges and evasions. The record before the Court shows that late payments were the normal course of dealing between the parties. As far as Mayor Smith is concerned, it is clear he was not a fan of the 2017 contract. Nevertheless, Mayor Smith's actions do not establish bad faith by the City when considering all the facts. When the City Council members and City Attorney Valley learned about Mayor Smith's actions they forcefully and repeatedly told him those actions were unauthorized and that the City was under contract with Crystal Clear. Mr. Simes claims that, after this City Council meeting, a city employee told him that Mayor Smith had instructed them not to make payments to Crystal Clear. Even if this were an undisputed fact, the City Treasurer had checks printed and had made multiple efforts to deliver them to Mr. Simes so that Crystal Clear's services would continue when Mr. Simes sent the notice of cancellation. Thus, even if Mayor Smith had instructed city employees not to pay Crystal Clear, the City still made efforts to become current on payments and continue with the Agreement.

Finally, any "equivocation" by Mr. Turner certainly does not indicate that "his actions were unauthorized," and Mr. Simes is at least equally responsible. It was Mr. Simes who decided to have the first round of checks mailed instead of meeting Mr. Turner in person, as had originally

been planned in their June 30, 2019 phone call. Likewise, it was Mr. Simes who canceled the July 11, 2019 meeting with Mr. Turner. Afterwards, it was Mr. Simes who did not respond to multiple attempts by Mr. Turner to deliver the checks.

The Court concludes that the City's failure to pay the April, May, and June 2019 invoices was not a material breach. Thus, Crystal Clear and Mr. Simes were still obligated to abide by the contract's terms. The Agreement contemplated the possibility of late payments and gave Crystal Clear the ability to suspend services until payments were made current. This power was rightfully exercised on June 3, 2019. Crystal Clear always had the option to terminate the Agreement—but only with ninety-days' written notice. However, Crystal Clear was not entitled, either under the contract or Arkansas law, to immediately declare the Agreement over because of the City's late payments.

Even if the City's failure to pay its April, May, and June 2019 invoices was a material breach, Crystal Clear still could not immediately end the Agreement because it waived the breach. No rational juror could conclude otherwise. The Arkansas Supreme Court has long recognized the “elemental” principle that when one party to a contract knows of another party's breach, yet continues to perform and expects the other party to continue performing, the non-breaching party has waived its right to “insist on the breach.” Crystal Clear knew the City was consistently late in making its monthly payments. Mr. Simes stated as much in his deposition, and the City's vendor ledger shows that late payments were the norm. Canceling the Agreement for failure to pay on time after over a year of lax enforcement of the payment deadlines requires giving “reasonable notice of intent to cancel” so that the City would have “the opportunity to bring [its] payments up to date and to be aware that in the future, no delinquent payments would be accepted.”

The closest thing to such notice came in the form of the letter that Mr. Simes sent to City Clerk Sandi Ramsey on May 30, 2019. That letter, however, does not notify the City that Crystal Clear intends on canceling the Agreement as a result of late payments. Instead, it notifies the City that Crystal Clear will exercise its contractual right to suspend services—a right already available under the Agreement due to the City's non-payment for the months of April and May 2019. Moreover, the letter shows that Crystal Clear was willing to continue accepting late payments by stating that services would continue if payment was received by June 7. True, the letter does go on to state that if payment is not received by June 7, the Agreement would effectively be canceled because Crystal Clear would permanently “delete all of [the City's] data backups.” While this could be seen as notice of intent to cancel . . . In any event, Crystal Clear effectively reaffirmed the waiver when Mr. Simes did not delete the data

after June 7, agreed to accept the back payments in late June and early July, and sent the City a link to resume services.

When Mr. Simes made the decision to cancel the Agreement, the City Council had very recently taken Mayor Smith to task about interfering the Agreement. The City Treasurer had made several attempts to pay Crystal Clear and Mr. Simes resumed services once the back payments were in the mail. This clearly shows both parties' intention to continue with the Agreement. It was Mr. Simes who abruptly refused to accept the back payments at the last minute. Thus, it was Mr. Simes who wrongfully brought the Agreement to an early end.

#### B. The City Did Not Otherwise Repudiate the Agreement

Stitching together some underdeveloped assertions scattered across the papers, one can just about deduce that Crystal Clear has an alternative argument—that other various acts or omissions by Mayor Smith and the City amounted to a repudiation of the contract. Specifically, these are: Mayor Smith soliciting bids from third parties; Mayor Smith's "unauthorized withholding of [Crystal Clear's] payments from January 2019 through March of 2019;" Mayor Smith asking Crystal Clear to rebid the contract; Mayor Smith hiring Global Technology Service Providers in May 2019; Mayor Smith's office requesting that Crystal Clear give information to Global in order to transition services; Mayor Smith demanding return of all passwords, usernames and other access; and the City Council's failure to enjoin or remove Kevin Smith.

Considered in the light of the facts of this case, none of these acts—alone or in combination—establish that the City definitely manifested an intention not to perform such that Crystal Clear and Mr. Simes could treat the contract as ended. No rational juror could conclude otherwise. Of all the acts that Plaintiffs list, the only one that could be said to definitely manifest an intent not to perform would be the May 14, 2019 e-mail from Mayor Smith's Chief of Staff requesting that Mr. Simes work with Mr. Dalencourt on a "transition." Still, even Mr. Simes did not attribute this act to the City at the time. He states in his reply e-mail that he would not comply unless he were to receive "an official letter from the City." The City Council members and City Attorney Valley, for their part, made it clear at the May 2019 City Council meeting that they did not authorize or approve Mayor Smith's actions and instead emphasized their desire to avoid litigation and continue with the Agreement they had awarded to Crystal Clear in 2017.

Moreover, every act listed by Crystal Clear took place before it first exercised the contractual right to suspend services for nonpayment on June 3, 2019. Despite all of Mayor Smith's

actions, Crystal Clear did not treat the Agreement as ended and instead availed itself of the rights provided by the Agreement. Accordingly, even if a repudiation occurred, Crystal Clear waived it when it, with full knowledge of [the City's] repudiation, elected to stand on the contract. Crystal Clear cannot choose to continue with the contract then later make a second and inconsistent election to treat it as abrogated. Moreover, the City was attempting to make back payments, and Crystal Clear was willing to accept those back payments and keep going with the Agreement until Mr. Simes sent the cancellation letter on July 15, 2019. Mr. Simes either did not consider Mayor Smith's May 2019 conduct to be a repudiation of the Agreement or Mr. Simes waived the alleged repudiation. Thus, the first party to the Agreement to definitely manifest an intention not to perform was Crystal Clear, not the City.

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For these reasons, Crystal Clear's Motion for Summary Judgment for breach of contract is GRANTED in part. The City failed to pay for services rendered in the months of April, May, June, and half of July 2019. It owes Crystal Clear for the unpaid months. The City's Motion for Summary Judgment is GRANTED as to the remainder of Crystal Clear's breach of contract claim.

[The court goes on and rejects the tortious interference claim against Mayor Smith]

### Note and Questions

1. The facts of this case are rather complex, and it entails multiple legal issues. This is not unusual. Disputes in contract law (and beyond contract law) often entail multiple (and often entangled) legal theories, especially before trial courts.
2. Read the plaintiff's July 15 letter, attempting to terminate the agreement. Does it argue that this is a termination for a failure to cure a material breach, as the injured party successfully did in *K&G*, or one for anticipatory breach, as the injured parties unsuccessfully tried to do in *Taylor*? The court treats it as both, which we think makes sense, but the letter could have been clearer on which set of facts supports which claim. Can you redraft the termination letter?
3. The heart of this opinion is the court's application of Restatement (Second) of Contracts § 241. However, note that this provision doesn't fully answer the question pending before the court. The factor listed in Section 241 assists courts in determining when a breach is material. The materiality of the breach is a required but not sufficient

element for termination of the agreement. The Restatement (and the common law, and as we will soon see, the UCC) encourages the breaching party to attempt to cure even a material breach and thus return both parties to performance. In that respect, even if the city's breach was held to be material, the court should have applied the factors listed in Restatement (Second) of Contracts § 242 (which partly overlap those listed in section 241) to determine the right of termination. Would the result have been different if the court had done so?

4. The rules concerning material breach and termination are default rules. In *Ke&G*, the breach had to be material under the common law to allow the breached-against party to suspend its performance. Here, in contrast, the agreement itself provided for a right to suspend performance upon any failure to pay. Like most courts, the court in *Crystal* notes that this provision is enforceable.

The Supreme Court of Indiana explained:

[T]he default common law Restatement factors [listed in Section 241] do not apply in this case because the plain language of the [agreement] provides for evaluating the materiality of a breach . . . Applying the specific terms agreed to by the parties rather than the common law default rule is consistent with Indiana contract law principles. Indiana courts zealously defend the freedom to contract.

... other jurisdictions provide some persuasive authority in this area. For instance, Vermont has recognized that “[c]ontracting parties can define what will constitute a material breach of their contract.” *McGee Const. Co. v. Neshobe Dev., Inc.*, 156 Vt. 550, 594 A.2d 415, 417 (1991) Also, Williston on Contracts provides: “[w]here the contract itself is clear in making a certain event a material breach of that contract, a court must ordinarily respect that contractual provision.” 23 Williston on Contracts § 63:3 (4th ed.) (citing *Dunkin’ Donuts of America, Inc. v. Middletown Donut Corp.*, 100 N.J. 166, 495 A.2d 66, 75 (1985)).

*State v. International Business Machines Corp.*, 51 N.E.3d 150, 160–61 (Ind. 2016). Indeed, it is not unusual for parties, especially to commercial agreements, to include provisions expressly dealing with the consequences of a breach. Those provisions typically address the injured party’s rights to suspend and terminate the agreement. Can one argue that

in *Crystal*, the parties didn't just contract around the common law rules concerning the suspension of performance but also around those concerning termination?

5. We considered waivers of express conditions when we discussed *Oppenheimer*. Implied conditions can similarly be waived. In fact, as the court in *Crystal* notes, both types of conditions can be implicitly waived by the other party's actions. The Restatement gives the following example:

A, an insurance company, issues to B a policy of automobile liability insurance, under which it is a condition of A's duty to pay that B notify A "as soon as practicable" after an accident. An accident occurs, but B does not notify A as soon as practicable. Without any statement concerning the non-occurrence of the condition, A begins to defend B in an action brought against B as a result of the accident. A's beginning to defend B operates as a promise to pay in spite of the non-occurrence of the condition.

Restatement (Second) of Contracts § 84, cmt. e. Read how the court in *Crystal* applies this doctrine and consider whether you agree with it. Does this doctrine mean that no good deed goes unpunished? Note that this is a waiver of the condition, not of the breach itself. In other words, even if a party waives the condition, meaning waives its right to suspend its performance, this, by itself, does not preclude it from suing for its damage.

6. As we noted, Arkansas has not yet adopted or rejected the adequate assurance doctrine outside of UCC. If it had adopted it, would you at any point have advised Crystal to ask for such assurances?
7. The court held that the city did not repudiate the agreement. However, didn't Crystal repudiate it? Why or why not, and if so, why didn't the city act on that repudiation?