

Sellers' and Buyers' Damages under the UCC

The Uniform Commercial Code is a model commercial law statute. Article 2 of the Code governs sales of goods and has been adopted in forty-nine of the fifty United States. Louisiana is the lone outlier. Part 7 of Article 2 governs remedies. The following cases apply provisions from Part 7 to remedies questions where the buyer or seller has breached a contract to buy or sell goods.

As with cases not relating to sales of goods (like service contracts and contracts for real property), courts generally seek to award damages in an amount that will give the promisee the benefit of their bargain. UCC § 1-305(a) provides guidance on that point: “The remedies provided by this code shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed....”

A buyer may breach by wrongfully rejecting or revoking acceptance of conforming delivered goods or failing to make a payment. UCC § 2-703. A seller's remedies for breach include withholding delivery, § 2-703(a); stopping delivery, § 2-705; completing manufacture of goods in process and identifying them to the contract or reselling materials for scrap and salvage value, so long as either is done in a commercially reasonable manner, § 2-704; reselling the goods and recovering any damages, § 2-706; recovering incidental damages in connection with reselling the goods or otherwise resulting from the breach, § 2-710; recovering damages for non-acceptance, § 2-708; recovering the price of the goods in limited cases, § 2-709; or cancelling the contract, § 2-703(f). As discussed in *Neri v. Retail Marine*, below, the UCC also provides a default liquidated damages provision that limits how much of an initial payment the seller can keep, § 2-718(2)(b), which may be offset by damages the seller can establish. § 2-718(3). We'll cover more about § 2-718 when we study liquidate damages directly.

The seller's right to resell the goods and recover damages for non-acceptance are sometimes seen as flip sides of the same coin. First, under § 2-706(1), the seller can resell the goods, and recover the difference between the price the buyer promised and the resale price, plus incidental damages. The remainder of § 2-706 provides rules for how the seller should handle the resale. Second, under § 2-708, the seller can recover the difference between the market price at time and place of tender (when and where the goods were to be delivered) and the unpaid contract price, plus incidental damages.

Consider the following hypothetical. Miles contracts to buy trumpets from Gillespie at a cost of \$200 per trumpet. Miles then breaches the contract. Gillespie resells the promised trumpets to Clark for \$190 per trumpet. Leaving aside incidental damages, and assuming Gillespie's

resale was made in good faith and in a commercially reasonable manner, what are Gillespie's damages per trumpet under § 2-706(1)?

Consider a similar hypothetical. Miles breaches, and when the day for delivery arrives, the market price for trumpets is \$175. Leaving aside incidental damages, what are Gillespie's damages per trumpet under § 2-708(1)?

Neri v. Retail Marine Co.,

30 N.Y.2d 393 (N.Y. Court of Appeals 1972)

GIBSON, Judge.

The plaintiffs contracted to purchase from defendant a new boat of a specified model for the price of \$12,587.40, against which they made a deposit of \$40. They shortly increased the deposit to \$4,250 in consideration of the defendant dealer's agreement to arrange with the manufacturer for immediate delivery on the basis of 'a firm sale', instead of the delivery within approximately four to six weeks originally specified. Some six days after the date of the contract plaintiffs' lawyer sent to defendant a letter rescinding the sales contract for the reason that plaintiff Neri was about to undergo hospitalization and surgery, in consequence of which, according to the letter, it would be "impossible for Mr. Neri to make any payments'. The boat had already been ordered from the manufacturer and was delivered to defendant at or before the time the attorney's letter was received. Defendant declined to refund plaintiffs' deposit and this action to recover it was commenced. Defendant counterclaimed, alleging plaintiffs' breach of the contract and defendant's resultant damage in the amount of \$4,250, for which sum defendant demanded judgment. Upon motion, defendant had summary judgment on the issue of liability tendered by its counterclaim; and Special Term directed an assessment of damages, upon which it would be determined whether plaintiffs were entitled to the return of any portion of their down payment.

Upon the trial so directed, it was shown that the boat ordered and received by defendant in accordance with plaintiffs' contract of purchase was sold some four months later to another buyer for the same price as that negotiated with plaintiffs. From this proof the plaintiffs argue that defendant's loss on its contract was recouped, while defendant argues that but for plaintiffs' default, it would have sold two boats and have earned two profits instead of one. Defendant proved, without contradiction, that its profit on the sale under the contract in suit would have been \$2,579 and that during the period the boat remained unsold incidental expenses aggregating \$674 for storage, upkeep, finance charges and insurance were incurred. Additionally, defendant proved and sought to recover attorneys' fees of \$1,250.

The trial court found ‘untenable’ defendant’s claim for loss of profit, inasmuch as the boat was later sold for the same price that plaintiffs had contracted to pay; found, too, that defendant had failed to prove any incidental damages; further found ‘that the terms of section 2-718, subsection 2(b), of the Uniform Commercial Code are applicable and same make adequate and fair provision to place the sellers in as good a position as performance would have done’ and, in accordance with paragraph (b) of subsection (2) thus relied upon, awarded defendant \$500 upon its counterclaim and directed that plaintiffs recover the balance of their deposit, amounting to \$3,750. The ensuing judgment was affirmed, without opinion, at the Appellate Division, and defendant’s appeal to this court was taken by our leave.

The issue is governed in the first instance by section 2-718 of the Uniform Commercial Code which provides, among other things, that the buyer, despite his breach, may have restitution of the amount by which his payment exceeds: (a) reasonable liquidated damages stipulated by the contract or (b) absent such stipulation, twenty per cent of the value of the buyer’s total performance or \$500, whichever is smaller (§ 2-718, subsection (2), pars. (a), (b)).

Among ‘the provisions of this Article other than subsection (1)’ are those to be found in section 2-708, which the courts below did not apply. Subsection (1) of that section provides that ‘the measure of damages for non-acceptance or repudiation by the buyer is the difference between the market price at the time and place for tender and the unpaid contract price together with any incidental damages provided in this Article (§ 2-710), but less expenses saved in consequence of the buyer’s breach.’ However, this provision is made expressly subject to subsection (2), providing: ‘(2) If the measure of damages provided in subsection (1) is inadequate to put the seller in as good a position as performance would have done then the measure of damages is the profit (including reasonable overhead) which the seller would have made from full performance by the buyer, together with any incidental damages provided in this Article (§ 2-710), due allowance for costs reasonably incurred and due credit for payments or proceeds of resale.’

The provision of the code upon which the decision at Trial Term rested (§ 2-718, subsection (2), par. (b)) does not differ greatly from the corresponding provisions of the prior statute (Personal Property Law, § 145—a, subd. 1, par. (b)), except as the new act includes the alternative remedy of a lump sum award of \$500. Neither does the present reference (in § 2-718, subsection (3), par. (a)) to the recovery of damages pursuant to other provisions of the article differ from a like reference in the prior statute (Personal Property Law, § 145—a, subd. 2, par. (a)) to an alternative measure of damages under section 145 of that act; but section 145

made no provision for recovery of lost profits as does section 2-708 (subsection (2)) of the code. The new statute is thus innovative and significant and its analysis is necessary to the determination of the issues here presented.

Prior to the code, the New York cases ‘applied the ‘profit’ test, contract price less cost of manufacture, only in cases where the seller (was) a manufacturer or an agent for a manufacturer’ (1955 Report of N.Y.Law Rev.Comm., vol. 1, p. 693). Its extension to retail sales was ‘designed to eliminate the unfair and economically wasteful results arising under the older law when fixed price articles were involved. This section permits the recovery of lost profits in all appropriate cases, which would include all standard priced goods.’ (Official Comment 2, McKinney’s Cons.Laws of N.Y., Book 62 1/2, Part 1, p. 605, under Uniform Commercial Code, § 2-708.) Additionally, and ‘(i)n all cases the seller may recover incidental damages’ (*Id.*, Comment 3). The buyer’s right to restitution was established at Special Term upon the motion for summary judgment, as was the seller’s right to proper offsets, in each case pursuant to section 2-718; and, as the parties concede, the only question before us, following the assessment of damages at Special Term, is that as to the proper measure of damage to be applied. The conclusion is clear from the record—indeed with mathematical certainty—that ‘the measure of damages provided in subsection (1) is inadequate to put the seller in as good a position as performance would have done’ (UCC § 2-708(2)) and hence—again under subsection (2)—that the seller is entitled to its ‘profit (including reasonable overhead) * * * together with any incidental damages * * *, due allowance for costs reasonably incurred and due credit for payments or proceeds of resale.’

It is evident, first, that this retail seller is entitled to its profit and, second, that the last sentence of subsection (2), as hereinbefore quoted, referring to ‘due credit for payments or proceeds of resale’ is inapplicable to this retail sales contract. Closely parallel to the factual situation now before us is that hypothesized by Dean Hawkland as illustrative of the operation of the rules: ‘Thus, if a private party agrees to sell his automobile to a buyer for \$2,000, a breach by the buyer would cause the seller no loss (except incidental damages, i.e., expense of a new sale) if the seller was able to sell the automobile to another buyer for \$2,000. But the situation is different with dealers having an unlimited supply or standard-priced goods. Thus, if an automobile dealer agrees to sell a car to a buyer at the standard price of \$2,000, a breach by the buyer injures the dealer, even though he is able to sell the automobile to another for \$2,000. If the dealer has an inexhaustible supply of cars, the resale to replace the breaching buyer costs the dealer a sale, because, had the breaching buyer performed, the dealer would have made two sales instead of one. The buyer’s breach, in such a case, depletes the dealer’s sales to the extent of one, and the measure of damages should be the dealer’s profit on one sale. Section

2-708 recognizes this, and it rejects the rules developed under the Uniform Sales Act by many courts that the profit cannot be recovered in this case.’ (Hawkland, Sales and Bulk Sales (1958 ed.), pp. 153-154; and see Comment, 31 FORDHAM L. REV. 749, 755-756.).

The record which in this case establishes defendant’s entitlement to damages in the amount of its prospective profit, at the same time confirms defendant’s cognate right to ‘any incidental damages provided in this Article (§ 2-710)’³ (UCC § 2-708(2)). From the language employed it is too clear to require discussion that the seller’s right to recover loss of profits is not exclusive and that he may recoup his ‘incidental’ expenses as well (*Procter & Gamble Distr. Co. v. Lawrence Amer. Field Warehousing Corp.*, 16 N.Y.2d 344, 354). Although the trial court’s denial of incidental damages in the uncontroverted amount of \$674 was made in the context of its erroneous conclusion that paragraph (b) of subsection (2) of section 2-718 was applicable and was ‘adequate * * * to place the sellers in as good a position as performance would have done’, the denial seems not to have rested entirely on the court’s mistaken application of the law, as there was an explicit finding ‘that defendant completely failed to show that it suffered any incidental damages.’ We find no basis for the court’s conclusion with respect to a deficiency of proof inasmuch as the proper items of the \$674 expenses (being for storage, upkeep, finance charges and insurance for the period between the date performance was due and the time of the resale) were proven without objection and were in no way controverted, impeached or otherwise challenged, at the trial or on appeal. Thus the court’s finding of a failure of proof cannot be supported upon the record and, therefore, and contrary to plaintiffs’ contention, the affirmance at the Appellate Division was ineffective to save it.

The trial court correctly denied defendant’s claim for recovery of attorney’s fees incurred by it in this action.

It follows that plaintiffs are entitled to restitution of the sum of \$4,250 paid by them on account of the contract price less an offset to defendant in the amount of \$3,253 on account of its lost profit of \$2,579 and its incidental damages of \$674.

³ Incidental damages to an aggrieved seller include any commercially reasonable charges, expenses or commissions incurred in stopping delivery, in the transportation, care and custody of goods after the buyer’s breach, in connection with return or resale of the goods or otherwise resulting from the breach’ (UCC § 2-710).

The order of the Appellate Division should be modified, with costs in all courts, in accordance with this opinion, and, as so modified, affirmed.

FULD, C.J., and BURKE, SCILEPPI, BERGAN, BREITEL and JASEN, JJ., concur.

Notes and Questions

1. How do the following hypotheticals differ from *Retail Marine*, and what are the seller's damages (if any) under UCC § 2-708?
 - a. Gillespie owns a painting by the famous painter, J. Coltrane. He contracts to sell the painting to Thelonious for \$1M US. Thelonious repudiates the contract and refuses to pay the promised sum or take delivery of the painting. Gillespie subsequently sells the painting to Ellington for \$1.1M US. What are Gillespie's damages?
 - b. McKinley agrees to build a custom car for Waters with unique touches like a marble dash, dual tires on the back, and a working 8-track cassette player. The contract price is \$200K. After spending \$100K building the car, Waters repudiates the contract and refuses to accept delivery. It would cost \$60K to finish making the car. A salvager offers \$20K for parts. Under § 2-708, what can McKinley do if no other reasonable person would purchase the custom car?
2. Some courts have expressed skepticism that market-based damages under § 2-708(1) would have been inadequate to compensate a "lost volume" seller like *Retail Marine*. See *R.E. Davis Chemical Corp. v. Diasonics, Inc.*, 826 F.2d 678 (7th Cir. 1987). For more on the question of lost volume damage claims, see, e.g., Victor P. Goldberg, *An Economic Analysis of the Lost-Volume Retail Seller*, 57 S. CAL. L. REV. 283 (1984).
3. Can we ensure that *Retail Marine* is a "lost volume seller" rather than a regular old reseller? Should the courts develop a test to identify a lost volume seller or leave it up to aggrieved sellers to pick their remedy? Does § 2-703 suggest the seller can pick its remedy? Read the official comments to § 2-703 before you answer.
4. How did the court here blink away the language from § 2-708(2) requiring "due credit for payments or proceeds from resale"? Is it appropriate for unelected judges on the Court of Appeals of New York to rewrite a democratically passed law of the New York

legislature? What do you think counts as “due credit for payment” according to the court in *Neri*?

5. Consider the following text of § 2-709. Is it clear to you why Retail Marine could not recover the price of the boat under that section?

UCC § 2-709. Action for the Price.

(1) When the buyer fails to pay the price as it becomes due the seller may recover, together with any incidental damages under the next section, the price

(a) of goods accepted or of conforming goods lost or damaged within a commercially reasonable time after risk of their loss has passed to the buyer; and

(b) of goods identified to the contract if the seller is unable after reasonable effort to resell them at a reasonable price or the circumstances reasonably indicate that such effort will be unavailing.

(2) Where the seller sues for the price he must hold for the buyer any goods which have been identified to the contract and are still in his control except that if resale becomes possible he may resell them at any time prior to the collection of the judgment. The net proceeds of any such resale must be credited to the buyer and payment of the judgment entitles him to any goods not resold.

6. This is what we will come to know as the seller’s “specific performance” remedy. When should the law allow a seller to get this remedy and why? We’ll get there. But look at the comments to § 2-709. What is the relationship, do you think, between the statutory text and the official comments?
7. Consider the following hypothetical: Gillespie contracts to sell his J. Coltrane painting to Thelonious for \$1M US. Thelonious refuses to pay or take delivery. Gillespie cannot find another buyer. What are Gillespie’s damages on an action for the price under UCC § 2-709?

* * *

The following cases present injured buyers who seek remedies for the sellers' respective breaches.

KGM Harvesting Co. v. Fresh Network

36 Cal. App. 4th 376 (Court of Appeal of California 1995)

COTTE, Presiding Justice

Facts

In July 1989 buyer and seller entered into an agreement for the sale and purchase of lettuce. Over the years, the terms of the agreement were modified. By May 1991 the terms were that seller would sell to buyer 14 loads of lettuce each week and that buyer would pay seller 9 cents a pound for the lettuce. (A load of lettuce consists of 40 bins, each of which weighs 1,000 to 1,200 pounds. Assuming an average bin weight of 1,100 pounds, one load would equal 44,000 pounds, and the 14 loads called for in the contract would weigh 616,000 pounds. At 9 cents per pound, the cost would approximate \$55,440 per week.)

Buyer sold all of the lettuce it received from seller to a lettuce broker named Castellini Company who in turn sold it to Club Chef, a company that chops and shreds lettuce for the fast food industry (specifically, Burger King, Taco Bell, and Pizza Hut). ***

In May and June 1991, when the price of lettuce went up dramatically, seller refused to supply buyer with lettuce at the contract price of nine cents per pound. Instead, it sold the lettuce to others at a profit of between \$800,000 and \$1,100,000. Buyer, angry at seller's breach, refused to pay seller for lettuce it had already received. Buyer then went out on the open market and purchased lettuce to satisfy its obligations to Castellini Company. Castellini covered all of buyer's extra expense except for \$70,000. Castellini in turn passed on its extra costs to Club Chef which passed on at least part of its additional costs to its fast food customers.

In July 1991 buyer and seller each filed complaints under the Perishable Agricultural Commodities Act (PACA). Seller sought the balance due on its outstanding invoices (\$233,000), while buyer sought damages for the difference between what it was forced to spend to buy replacement lettuce and the contract price of nine cents a pound (approximately \$700,000).

Subsequently, seller filed suit for the balance due on its invoices, and buyer cross-complained for the additional cost it incurred to obtain substitute lettuce after seller's breach. At trial, the parties stipulated that seller was entitled to a directed verdict on its complaint for \$233,000,

the amount owing on the invoices. Accordingly, only the cross-complaint went to the jury, whose task was to determine whether buyer was entitled to damages from seller for the cost of obtaining substitute lettuce and, if so, in what amount. The jury determined that seller breached the contract, that its performance was not excused, and that buyer was entitled to \$655,960.22, which represented the difference between the contract price of nine cents a pound and what it cost buyer to cover by purchasing lettuce in substitution in May and June 1991. It also determined that such an award would not result in a windfall to buyer and that buyer was obligated to the Castellini Company for the additional costs. The court subtracted from buyer's award of \$655,960.22 the \$233,000 buyer owed to seller on its invoices, leaving a net award in favor of buyer in the amount of \$422,960.22. The court also awarded buyer prejudgment interest commencing 30 days before trial.

Discussion

Section 2711 of the California Uniform Commercial Code provides a buyer with several alternative remedies for a seller's breach of contract. The buyer can "cover" by making in good faith and without unreasonable delay any reasonable purchase of ... goods in substitution for those due from the seller." (§ 2712, subd. (1).)* In that case, the buyer "may recover from the seller as damages the difference between the cost of cover and the contract price...." (§ 2712, subd. (2).) If the buyer is unable to cover or chooses not to cover, the measure of damages is the difference between the market price and the contract price. (§ 2713.) Under either alternative, the buyer may also recover incidental and consequential damages. (§§ 2711, 2715.) In addition, in certain cases the buyer may secure specific performance or replevin "where the goods are unique" (§ 2716) or may recover goods identified to a contract (§ 2502).

In the instant case, buyer "covered" as defined in section 2712 in order to fulfill its own contractual obligations to the Castellini Company. Accordingly, it was awarded the damages called for in cover cases—the difference between the contract price and the cover price. (§ 2712.)

In appeals from judgments rendered pursuant to section 2712, the dispute typically centers on whether the buyer acted in "good faith," whether the "goods in substitution" differed

* When the state of California implemented Articles 1 and 2 of the UCC into the California Commercial Code, the drafters converted the UCC's Article-Section format (§ 2-712) into a four-digit number (§ 2712). Thus, as it cites the Cal. Comm. Code, the statutory provisions cited in this case have no dashes between the article and section number. But they refer to the same provisions. Eds.

substantially from the contracted for goods, whether the buyer unreasonably delayed in purchasing substitute goods in the mistaken belief that the price would go down, or whether the buyer paid too much for the substitute goods. (See generally White & Summers, Uniform Commercial Code (3d ed. 1988) Buyer's Remedies, Cover, § 6–3, pp. 284–292 [hereafter White & Summers], and cases cited therein.)

In this case, however, none of these typical issues is in dispute. Seller does not contend that buyer paid too much for the substitute lettuce or that buyer was guilty of “unreasonable delay” or a lack of “good faith” in its attempt to obtain substitute lettuce. Nor does seller contend that the lettuce purchased was of a higher quality or grade and therefore not a reasonable substitute.

Instead, seller takes issue with section 2712 itself, contending that despite the unequivocal language of section 2712, a buyer who covers should not necessarily recover the difference between the cover price and the contract price. Seller points out that because of buyer's “cost plus” contract with Castellini Company, buyer was eventually able to pass on the extra expenses (except for \$70,000) occasioned by seller's breach and buyer's consequent purchase of substitute lettuce on the open market. It urges this court under these circumstances not to allow buyer to obtain a “windfall.”

The basic premise of contract law is to effectuate the expectations of the parties to the agreement, to give them the “benefit of the bargain” they struck when they entered into the agreement. In its basic premise, contract law therefore differs significantly from tort law.

“The basic object of damages is compensation, and in the law of contracts the theory is that the party injured by breach should receive as nearly as possible the equivalent of the benefits of performance.” (*Lisec v. United Airlines, Inc.*, 10 Cal.App.4th 1500, 1503 (1992)).

With these rules in mind, we examine the contract at issue in this case to ascertain the reasonable expectations of the parties. The contract recited that its purpose was “to supply [buyer] with a consistent quality raw product at a fair price to [seller], which also allows [buyer] profitability for his finished product.” Seller promised to supply the designated quantity even if the price of lettuce went up (“We agree to supply said product and amount at stated price regardless of the market price or conditions”) and buyer promised to purchase the designated quantity even if the price went down: (“[Buyer] agrees to purchase said product and amounts

at stated price regardless of the market price or conditions, provided quality requirements are met”). The possibility that the price of lettuce would fluctuate was consequently foreseeable to both parties.

Although the contract does not recite this fact, seller was aware of buyer’s contract with the Castellini Company and with the Castellini Company’s contract with Club Chef. This knowledge was admitted at trial and can be inferred from the fact that seller shipped the contracted for 14 loads of lettuce directly to Club Chef each week. Thus, seller was well aware that if it failed to provide buyer with the required 14 loads of lettuce, buyer would have to obtain replacement lettuce elsewhere or would itself be in breach of contract. This was within the contemplation of the parties when they entered into their agreement.*

As noted earlier, the object of contract damages is to give the aggrieved party “as nearly as possible the equivalent of the benefits of performance.” (*Lisec v. United Airlines, Inc.*, *supra*, 10 Cal.App.4th at p. 1503; see also § 1106** [“The remedies provided by this code shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed....”].) In the instant case, buyer contracted for 14 loads of lettuce each week at 9 cents per pound. When seller breached its contract to provide that lettuce, buyer went out on the open market and purchased substitute lettuce to fulfill its contractual obligations to third parties. However, purchasing replacement lettuce to continue its business did not place buyer “in as good a position as if the other party had fully performed.”

This is the measure of damages set forth in section 2712.

In this case, the damage formula of section 2712 put buyer in the identical position performance would have: it gave buyer the contracted for 14 loads of lettuce with which to carry on its business at the contracted for price of 9 cents per pound.

* A promisor can sometimes argue that damages should not be awarded if they are not foreseeable. That argument did not prevail here. We’ll spend more time on this concept, but the rules for when consequential damages are foreseeable are found in UCC § 2-715(2).

** The text of the former UCC § 1-106 was adopted as Cal. Comm. Code § 1106. Now, that language is found in UCC § 1-305 and Cal. Comm. Code. § 1305. Eds.

Despite the obvious applicability and appropriateness of section 2712, seller argues in this appeal that the contract-cover differential of section 2712 is inappropriate in cases, as here, where the aggrieved buyer is ultimately able to pass on its additional costs to other parties. Seller contends that section 1106's remedial injunction to put the aggrieved party "in as good a position as if the other party had fully performed" demands that all subsequent events impacting on buyer's ultimate profit or loss be taken into consideration (specifically, that buyer passed on all but \$70,000 of its loss to Castellini Company, which passed on all of its loss to Club Chef, which passed on most of its loss to its fast food customers). ***

...[S]ection 2712 "will often put buyer in the identical economic position that performance would have." (White & Summers, *supra*, § 6-3, p. 285.) In contrast, the contract-market differential of section 2713 "bears no necessary relation to the change in the buyer's economic status that the breach causes. It is possible that this differential might yield the buyer a handsome sum even though the breach actually saved him money in the long run (as for example when a middleman buyer's resale markets dry up after the breach). It is also quite possible that the buyer's lost profit from resale or consumption would be greater than the contract-market difference." (Id., § 6-4, at p. 294.)

White and Summers argue that the drafters of section 2713 could *not* have intended to put the buyer in the same position as performance since "[p]erformance would have given the buyer certain goods for consumption or resale" (White & Summers, *supra*, at p. 294) which would have resulted in "either a net economic gain for the buyer or a net economic loss." (Ibid.)

With these prefatory comments in mind, we look to the *Allied Cannery* case. In *Allied Cannery*, [a raisin seller, Victor Packing, breached a contract] to sell raisins in 1976. The buyer, Allied Cannery, had contracts to resell the raisins it bought from Victor to two Japanese companies for its cost plus 4 percent. Such a resale would have resulted in a profit of \$4,462.50 to Allied. When Victor breached the contract, Allied sued for the difference between the market price and the contract price as authorized by section 2713. As the market price of raisins had soared due to the disastrous 1976 rains, the market-contract price formula would have yielded damages of approximately \$150,000. Allied did not purchase substitute raisins and did not make any deliveries under its resale contracts to the Japanese buyers. One of the Japanese buyers simply released Allied from its contract because of the general unavailability of raisins. The other buyer did not release Allied, but it did not sue Allied either. By the time Allied's case against Victor went to trial, the statute of limitations on the Japanese buyer's claim had run.

Under these circumstances, the court held that the policy of section 1106 (that the aggrieved party be put in as good a position as if the other party had performed) required that the award of damages to Allied be limited to its actual loss. It noted that for this limitation to apply, three conditions must be met: (1) “the seller knew that the buyer had a resale contract”; (2) “the buyer has not been able to show that it will be liable in damages to the buyer on its forward contract”; and (3) “there has been no finding of bad faith on the part of the seller...” (*Allied Cannery & Packers, Inc. v. Victor Packing Co.*, *supra*, 162 Cal. App. 3d at p. 915)

We believe that this focus on the good or bad faith of the breaching party is inappropriate in a commercial sales case. As our California Supreme Court recently explained, courts should not differentiate between good and bad motives for breaching a contract in assessing the measure of the non-breaching party’s damages. (*Applied Equipment Corp. v. Litton Saudi Arabia Ltd.* (1994) 7 Cal. 4th 503, 513–515.) Such a focus is inconsistent with the policy “to encourage contractual relations and commercial activity by enabling parties to estimate in advance the financial risks of their enterprise.” (*Id.* at p. 515, 28 Cal. Rptr. 2d 475.)

... [W]e have serious reservations about whether the result in *Allied Cannery*, with its emphasis on the good faith of the breaching party, is appropriate in an action seeking damages under section 2713. We have no reservations, however, in not extending the *Allied Cannery* rationale to a section 2712 case. As noted earlier, no section 2712 case ... has ever held that cover damages must be limited by section 1106. The obvious reason is that the cover-contract differential puts a buyer who covers in the exact same position as performance would have done. This is [] precisely what is called for in section 1106. In this respect, the cover/contract differential of section 2712 is very different than the market/contract differential of section 2713, which “need bear no close relation to the plaintiff’s actual loss.” (White & Summers, *supra*, at p. 295.)

In summary, we hold that where a buyer “cover[s]” by making in good faith and without unreasonable delay any reasonable purchase of ... goods in substitution for those due from the seller, ... [that buyer] may recover from the seller as damages the difference between the cost of cover and the contract price...” (§ 2712.) This gives the buyer the benefit of its bargain. What the buyer chooses to do with that bargain is not relevant to the determination of damages under section 2712. . . .

The judgment is affirmed. Costs on appeal to buyer.

PREMO and ELIA, JJ., concur.

Notes and Questions

1. A seller of goods will typically breach in one of two ways. First, the seller may deliver goods that fail to “conform” to the contract in some way, breaching an express or implied warranty about the nature of the goods it will deliver. Second, the seller may fail to make proper “tender” of the goods, which might include failing to deliver on time, delivering too few or too many of the goods promised, or failing to deliver at all. The buyer’s remedies for breach include canceling the contract, § 2-711; recovering as much of the price as has been paid, § 2-711; buying goods to “cover” or replace buyer’s goods, and recovering the difference in price between the promised goods and the acquired goods, § 2-712; recovering the difference between the promised goods and their market value at the time the buyer learned of the breach, including consequential and incidental damages, less buyer’s expenses saved from seller’s breach, § 2-713; recovering damages for non-conforming, accepted goods, § 2-714; recovering goods identified to the contract, § 2-502;* obtaining specific performance or replevy of the goods, § 2-716; and reselling non-conforming goods in the buyer’s possession, § 2-711(3).
2. Reconsider *Hawkins v. McGee*. In that case, the court reasoned by analogy, comparing Hawkins’ post-surgery hand to a machine delivered by the seller that does not conform with the warranty, i.e., that is not as the seller promised. As the court in *Hawkins* stated the general rule, “the measure of the vendee’s damages is the difference between the value of the goods as they would have been if the warranty as to quality had been true, and the actual value at the time of the sale, including gains prevented and losses sustained....” UCC § 2-714 provides a similar remedy for delivery of non-conforming goods that the buyer accepts. The seller may recover “the difference at the time and place of acceptance between the value of the goods accepted and the value they would

* It’s more complicated than this, but when the goods are identified to the contract, title or ownership passes from the manufacturer to the buyer, even though the manufacturer is still in possession of the goods. For goods not yet manufactured, there are default rules about when title passes. The parties can set other default rules by contract. Thus, the goods are the buyers to recover. You are likely to learn the details of identification in a course about the sales of goods. Eds.

have had if they had been as warranted, unless special circumstances show proximate damages of a different amount.”

3. Recall *Peeryhouse* and *Kent*. Did those cases similarly find good faith and bad faith wholly irrelevant to damages calculations? Why might the UCC take a different position from the common law here? Why did the court here ignore UCC § 1-304 which requires that “[e]very contract or duty within the Uniform Commercial Code imposes an obligation of good faith in its performance and enforcement”?

Fertico Belgium S.A. v. Phosphate Chemicals Export Association, Inc.

70 N.Y.2d 76 (N.Y. Court of Appeals 1987)

Bellacosa, Judge.

... In October 1978, appellant Fertico Belgium S.A. (Fertico), an international trader of fertilizer, contracted with Phosphate Chemicals Export Association, Inc. (Phoschem), a corporation engaged in exporting phosphate fertilizer, to purchase two separate shipments of fertilizer for delivery to Antwerp, Belgium. The first shipment was to be 15,000 tons delivered no later than November 20, 1978 and the second was to be 20,000 tons delivered by November 30, 1978. Phoschem knew that Fertico required delivery on the specified dates so that the fertilizer could be bagged and shipped in satisfaction of a secondary contract Fertico had with Altawreed, Iraq’s agricultural ministry. Fertico secured a letter of credit in a timely manner with respect to the first shipment. After Phoschem projected a first shipment delivery date of December 4, 1978, Fertico advised Phoschem, on November 13, 1978, that the breach as to the first shipment presented “huge problems” and canceled the second shipment which had not as of that date been loaded, thus ensuring its late delivery. The first shipment did not actually arrive in Antwerp until December 17 and was not off-loaded until December 21, 1978. Despite the breach as to the first shipment, Fertico retained custody and indeed acquired title over that first shipment because, as its president testified “[w]e had no other choice” as defendant seller Phoschem had presented Fertico’s \$1.7 million letter of credit as of November 17, 1978, and the same had been honored by the issuer (*see*, UCC 5–114).*

* A letter of credit is an instrument issued by a bank at a customer’s request. The bank agrees to honor a draft or demand for payment made by the beneficiary of the letter, if the draft or demand complies with certain conditions, and regardless

Fertico's predicament from the breach by delay of even the first shipment, a breach which Phoschem does not deny, was that it, in turn, would breach its contract to sell to Altawreed unless it acquired substitute goods. In an effort to avoid that secondary breach, Fertico took steps in mid-November to cover the goods by purchasing 35,000 tons of the same type fertilizer from Unifert, a Lebanese concern. The cost of the fertilizer itself under the Phoschem-to-Fertico contract was \$4,025,000, and under the Unifert-to-Fertico contract \$4,725,000, a differential of \$700,000. On the same day Fertico acquired cover, November 15, 1978, Fertico's president traveled to Baghdad, Iraq, to renegotiate its contract with Altawreed. In return for a postponed delivery date and an additional payment of \$20.50 per ton, Fertico agreed to make direct inland delivery rather than delivery to the seaport of Basra. Fertico fulfilled its renegotiated Altawreed contract with the substitute fertilizer purchased as cover from Unifert.

In addition to the problems related to its Altawreed contract, Fertico was left with 15,000 tons of late-delivered fertilizer which it did not require but which it had been compelled to take because Phoschem had received payment on Fertico's letter of credit. This aggrieved international buyer-seller was required to store the product and seek out a new purchaser. Fertico sold the 15,000 tons of the belatedly delivered Phoschem fertilizer to another buyer, Janssens, on March 19, 1979, some three months after the nonconforming delivery, and earned a profit of \$454,000 based on the cost to it from Phoschem and its sale price to Janssens.

In 1981, Fertico commenced this action against Phoschem seeking \$1.25 million in damages for Phoschem's breach of the October 1978 agreement. A jury returned a verdict of \$1.07 million which the trial court refused to overturn on a motion for judgment notwithstanding the verdict. The Appellate Division vacated the damage award, ordered a new trial on the damages issue only and ruled, as a matter of law, that the higher purchase price paid by Altawreed to Fertico was an expense saved as a consequence of the Phoschem breach; and that the Fertico damages had to be reduced by the profits from the Janssens' sale (*Fertico Belgium v. Phosphate Chems. Export Assn.*, 501 N.Y.S.2d 867). Fertico appealed to this court on a stipulation for judgment absolute. We disagree... and conclude that the Uniform Commercial Code and our analysis support a modification and reinstatement of \$700,000 of the damage award in a final judgment resolving this litigation between the parties.

of whether any contract or agreement between the customer and beneficiary is a satisfied. Thus, when Phoschem presented the letter of credit to the bank, it was paid even though the parties disputed whether Phoschem had breached the contract.

Failure by Phoschem to make delivery on the contract dates concededly constituted a breach of the contract. The Uniform Commercial Code § 2-711 gives the nonbreaching party the alternative of either seeking the partial self-help of cover along with recovery of damages (UCC §2-712), or of recovering damages only for the differential between the market price and the contract price, together with incidental and consequential damages less expenses saved (UCC §2-713). Fertico exercised its right as the wronged buyer-trader to cover in order to obtain the substitute fertilizer it required to meet its obligation under its Altawreed contract (see, UCC §2-712, Comment 1).

A covering buyer's damages are equal to the difference between the presumably higher cost of cover and the contract price, plus incidental or consequential damages suffered on account of the breach, less expenses saved (UCC §2-712(2)). Fertico is thus entitled to a damage remedy under this section because its cover purchase was made in good faith, without unreasonable delay, and the Unifert fertilizer was a reasonable substitute for the Phoschem fertilizer (UCC §2-712(1); *Reynolds Sec. v. Underwriters Bank & Trust Co.*, 44 N.Y.2d 568, 572-573).

The additional compensation to Fertico, an international trader, from Altawreed is not, however, an expense saved as a consequence of the seller Phoschem's breach for which Phoschem is entitled to any credit (UCC §2-712(2)). In most instances, and particularly in this case, saved expenses must be costs or expenditures which would be anticipated had there been no breach. For example, if a seller were to breach a contract to deliver an unpackaged product to the buyer and the buyer were to cover with the same product prepackaged, the cost of packaging which the buyer would have had to perform is an expense saved as a consequence of the breach (*see*, 3 Hawkland, Uniform Commercial Code Series § 2-712:02, at 362). The increased remuneration from Altawreed was compensation for the additional shipment responsibilities incurred by Fertico, not a cost or expenditure anticipated in the absence of a breach, and therefore was erroneously analyzed and credited in Phoschem's favor by the Appellate Division.

[Another] prong of the damages analysis relates to the profit made from the independent sale of the Phoschem fertilizer to Janssens. The Appellate Division erred in offsetting this profit against the damages otherwise suffered since that court mistakenly concluded that the sale stemmed from and was dependent upon Phoschem's breach. This offset, on these peculiar facts, would severely disadvantage Fertico, a trader in fertilizer who both buys and sells, and who would have pursued such commercial transactions had there been no breach by

Phoschem. It would be anomalous to conclude that had it not been for Phoschem's breach Fertico would not have continued its trade and upon such reasoning to counterpoise the profits from the Janssens' sale against the damages arising from Phoschem's breach. Inasmuch as the facts here are exceptional because Fertico met its subsale obligations with the cover fertilizer and yet acquired title and control over the late-delivered fertilizer from Phoschem, our decision does not fit squarely within the available Uniform Commercial Code remedies urged by the dissent. Thus, strict reliance on *Neri v. Retail Mar. Corp.*, 30 N.Y.2d 393 (*supra*) and on Hawkland's commentary (3 Hawkland, Uniform Commercial Code Series § 2-714:05, at 384), as undertaken by the dissent, does not provide an adequate resolution to the particular problem presented in this case.

Fertico learned of Phoschem's breach after Phoschem had negotiated Fertico's \$1.7 million letter of credit, which constituted complete payment for the first shipment. With no commercially reasonable alternative, Fertico took custody of the first shipment but canceled the second (UCC §2-601(c)), having previously notified Phoschem of its breach (UCC §2-607). The loss resulting to Fertico by having to acquire cover, even in the face of its acceptance of a late-delivered portion of the fertilizer, is properly recoverable under section 2-714(1) (3 Hawkland, Uniform Commercial Code Series § 2-714:05, at 384-385). At the same time, Uniform Commercial Code § 1-106 directs that the remedies provided by the Uniform Commercial Code should be liberally administered so as to put the aggrieved party in as good a position as if the other party had fully performed. Had Phoschem fully performed, Fertico would have had the benefit of the Altawreed transaction and, as a trader of fertilizer, the profits from the Janssens' sale as well. "Gains made by the injured party on other transactions after the breach are never to be deducted from the damages that are otherwise recoverable, unless such gains could not have been made, had there been no breach" (5 Corbin, Contracts § 1041, at 256; *see also*, *Steen Indus. v. Richer Communications*, 226 Pa. Super. Ct. 219). Fertico's profit made on the sale of a nonspecific article such as fertilizer, of which the supply in the market is not limited, should not therefore be deducted from the damages recoverable from Phoschem (5 Corbin, Contracts § 1041, at 258-260; *see also*, *Neri v. Retail Mar. Corp.*, 30 N.Y.2d 393, 401, *supra*).

Fertico was concededly wronged by Phoschem's breach and Fertico resorted to Uniform Commercial Code remedies which are rooted in what we perceive to be the realities of the marketplace. Fertico did what reasonable traders would do and would like to do in mitigating risks inflicted in this case by Phoschem and in exerting its commercial resourcefulness. That is, it took steps to save its business, its customers, its good will and its deals and ultimately to also recover appropriate damages from a wrongdoer. That did not produce a "windfall" or a

“double benefit” to the aggrieved party as the dissenting opinion asserts. The result we reach today countenances no such thing. On the contrary, to deprive the buyer-trader Fertico of its rightful differential damages of \$700,000 and to credit this transactionally independent profit to Phoschem would perversely enrich the wrongdoer at the expense of the wronged party, a result those in the marketplace would find perplexing and a result which the generous remedial purpose of the Uniform Commercial Code does not compel or authorize. The dissent’s characterization of the recovery by an injured party of damages for a breach of contract as a “benefit” is wrong, since that functionally attributes a kind of lien against the independently pursued benefit derived out of that separate transaction.

Accordingly, the order of the Appellate Division affirming liability but vacating, on the law, the damage award and remanding the matter for a new trial on the issue of damages, as appealed to this court on a stipulation for judgment absolute, should be modified and damages awarded to Fertico in the amount of \$700,000 in accordance with this opinion.

TITONE, Judge dissenting.

At issue in this appeal is the relationship among the various remedies that article 2 of the Uniform Commercial Code provides for buyers aggrieved by sellers’ defaults. Central to the analysis is the principle that the Code’s remedies “shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed” (UCC 1-106(1) [emphasis supplied]). Here, the majority concluded that the aggrieved buyer may retain both cover damages and the profit from the resale of the late-delivered goods, in effect, securing the benefit of its bargain twice. Since that result is not required by, and indeed is not even consistent with, the purpose of Code’s generous remedial provisions, I must respectfully dissent.

WACHTLER, C.J., and SIMONS, KAYE and HANCOCK, JJ., concur with BELLACOSA, J.

TITONE, J., dissents and votes to affirm in a separate opinion in which ALEXANDER, J., concurs.

Notes and Questions

1. Many buyers like KGM and Fertico are also sellers of the goods they purchased, but not every seller has a cost-plus deal like the deal KGM secured with Castellini. Likewise, not every seller can make a profit on goods left in its hands by a breaching buyer like

Fertico. To better understand the courts' reasoning in *KGM* and *Fertico*, consider the following hypotheticals, based on *Acme Mills & Elevator Co. v. Johnson*, 141 Ky. 718 (Ky. App. 1911):

- a. Mingus grows grain, and contracts to sell his grain to Fitzgerald for \$1.03 per bushel on July 24. On July 2, the price for grain has spiked, and Mingus makes a deal with Sarah to sell his grain for \$1.16. Mingus does not inform Fitzgerald. On the day Mingus should deliver the grain, he repudiates. Fitzgerald finds grain on the market for \$0.97 per bushel. Under UCC § 2-712, what are Fitzgerald's damages?
- b. Same as above, but on delivery day, Fitzgerald covers for \$1.16 per bushel. What are Fitzgerald's damages under § 2-712?
- c. Same as above, but on July 2, Fitzgerald makes a forward contract to deliver the grain she will buy from Mingus to Vaughan for \$1.16. On delivery day, Fitzgerald offers to pay Mingus the agreed \$1.03 for his grain. Mingus argues Fitzgerald owes him \$1.16. If Mingus sues, what result?