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REINVENTING THE DEAL: A SEQUENTIAL APPROACH TO
ANALYZING CLAIMS FOR ENFORCEMENT OF MODIFIED
SALES CONTRACTS

*Irma S. Russell**

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* Irma S. Russell, Professor, The Cecil C. Humphreys School of Law, The University of Memphis. The author extends special thanks to Professors Ian Ayers and William H. Henning for their insightful suggestions relating to the UCC and economics analysis. She is grateful to all the colleagues who read and commented on earlier drafts of the Article, especially Professors Robert H. Jerry, II, William P. Kratzke, Janet L. Richards, Kevin H. Smith, and James R. Smoot. Additionally, she acknowledges with gratitude funding, from the University of Memphis Foundation and she thanks Stephenie Booher, Caroline Critchfield Hunter, and Karen Stachowski for their able research assistance.

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I. INTRODUCTION—THE MODIFICATION PROBLEM

Modification is an accepted adjunct to the right to contract. It provides a flexible and efficient mechanism for changing agreements in response to altered circumstances in the performance stage of a contract. Some modified (or “reinvented”) contracts facilitate an efficient allocation of resources, saving a deal that would otherwise have ended in an inefficient breach. It does not follow, however, that courts should enforce all modifications. In some cases, the reinvented contract is the product of deceit, economic coercion, or the initiating party’s ability to dictate changes. Section 2-209 of the Uniform Commercial Code deals with modifications to contracts for the sale of goods. The text of section 2-209(1) states: “An agreement modifying a contract within this Article needs no consideration to be binding.”¹ The official comments to section 2-209 include the requirement of good faith, stating that modifications “must meet the test of good faith imposed by this Act.”² Although this provision seems to intend to impose a good faith obligation on modifications, it fails to elucidate what constitutes good faith in this context, leaving the question to the discretion of the courts rather than contextualizing the concept.³ Thus, courts are left to tackle the question of how to determine whether a modification should be enforced. In attempting to delineate enforceable from unenforceable modifications, courts have formulated a variety of tests, but their efforts have failed to produce a predictable or workable test for addressing the modification issue.⁴ This

1. U.C.C. § 2-209(1) (1998).

2. See *id.* § 2-209 cmt. 2. Because most states do not adopt the official comments as part of the enactment of the Uniform Commercial Code, see Sean Michael Hannaway, *The Jurisprudence and Judicial Treatment of the Comments to the Uniform Commercial Code*, 75 CORNELL L. REV. 962, 974-86 (1990) (arguing for stronger judicial regard of a comment’s authoritative value), an initiating party may argue that Comment 2 fails to create law. Good faith is inapplicable to the modification setting, this argument runs, because modification is a formation process rather than a performance process. While courts have heretofore rejected this argument, the legislative history of the process of revision of Article 2 may add fuel for the argument. The National Conference of Commissioners on Uniform State Laws (NCCUSL) proposed a version of § 2-209(1) that included the good faith requirement in the text of the provision. Compare U.C.C. § 2-209(1) with U.C.C. § 2-210(a) (proposed NCCUSL draft, Nov. 1, 1996). If the requirement is again relegated to the comment section in the final draft, an initiating party may argue that the drafters categorized modification as outside the reach of the obligation of good faith.

3. See generally Christina L. Kunz, *Frontispiece on Good Faith: A Functional Approach Within the UCC*, 16 WM. MITCHELL L. REV. 1105, 1106-10 (1990) (noting the UCC’s generalized use of good faith).

4. Scholars have criticized section 2-209 for failing to provide a clear model for courts to employ. See Charles J. Goetz & Robert E. Scott, *The Mitigation Principle: Toward a General Theory of Contractual Obligation*, 69 VA. L. REV. 967, 1024 (1983); Robert A. Hillman, *Contract Modification Under the Restatement (Second) of Contracts*, 67 CORNELL L. REV. 680, 699-700

Article considers whether providing additional content to the concept of good faith in this area of modification is possible or desirable.

A representative hypothetical illustrates the problem. Pursuant to a contract with Madison County (Buyer), Steel Perfect (Seller) began manufacturing steel beams for use by Buyer in the construction of a bridge. Before the first delivery, Seller⁵ called Buyer and stated that, because of an increase in the price of iron used in manufacturing steel, Seller would not perform the contract unless Buyer accepted a revised price term, sharing the cost of the price increase. Worried about obtaining cover (a substitute contract), Buyer agreed to the modified price, signed a written modification of the price term in the contract document, and took delivery of the beams. After construction of the bridge was complete, Buyer paid Seller the original contract price, refused to pay the price adjustment, and asserted that the modification was unfair, coercive, or otherwise unenforceable. In response, Seller sued. Should a court enforce the price modification? What standard should it apply in deciding this question?

If the facts indicate that a significant price increase actually occurred, that the risk of such a price increase was not allocated to Seller,⁶ and that Seller did not engage in coercive tactics, a court is likely to enforce the

(1982). Professor Farnsworth explored the ambiguity of the current version of the Code. *See* E. Allan Farnsworth, *Good Faith Performance and Commercial Reasonableness Under the Uniform Commercial Code*, 30 U. CHI. L. REV. 666, 675-76 (1963).

5. Much of this discussion speaks of the initiating party as the seller and the resisting party as the buyer. While many cases in the modification context involve a request by a seller for an enhanced price, the modification question can arise in the reverse setting. For example, a buyer may seek a lower price for the goods or seek other concessions such as an increased quantity of goods, higher quality goods, accommodations relating to payment terms or delivery terms, or other matters advantageous to Buyer.

6. In a general sense, the risk of a price increase is implicitly allocated to Seller and the risk of a price decrease is implicitly allocated to Buyer. In the event of a price increase, Seller regrets the contract, wishes he had not agreed to the lower sales price (i.e., lower than that which he could obtain after the price rise), and wants out of the contract. Conversely, in the event of a price decrease, Buyer regrets the contract, knowing that he now could obtain the same goods for a lower price. In either case, however, the change of affairs does not provide a basis for a refusal to perform. It is fundamental to contract law that the obligation created by a contract endures despite such changing circumstances. *See* E. ALLAN FARNSWORTH, *CHANGING YOUR MIND: THE LAW OF REGRETTED DECISIONS* 20-21 (1998) (defining regret as "the sensation of distress that you feel on concluding that you have done something contrary to your present self-interest"). Contract law allocates the risk of such market changes to each party, obligating each to perform (or pay damages) despite market shifts. Indeed, the ability to lock in stated price is one of the prime motivations for entering a contract. If a price change provided a basis for nonperformance, the reason for entering contracts would be significantly diminished. Exceptions to this allocation are found in the doctrines of mistake, impracticability (also called impossibility) and frustration. Only when a court finds the state of affairs operates unfairly as analyzed under these doctrines will it excuse the regretful party from its obligation to go forward with performance. *See* RESTATEMENT (SECOND) OF CONTRACTS §§ 153, 261, 264 (1981).

modification.⁷ On the other hand, if the facts establish that Seller used the modification to achieve a better deal for himself⁸ or used coercive tactics, the defendant (Buyer) is likely to prevail. When facts clearly establish either a legitimate reason for the modification or economic duress, the judgment by the court is straightforward. Simply stated, easy cases are easy to decide. When the facts present a balance on each side or the proof is problematic, however,⁹ courts lack guidance from the Code on the method for consistently distinguishing between justified (and enforceable) modifications and those that are not justified (and therefore unenforceable). By contrast, the Restatement's corollary provision, section 89, gives useful guidance for courts regarding the type of modification that should be enforced.¹⁰ The Code's test leaves open the question of who needs to prove what and when. Does section 2-209 mean that the plaintiff must prove it had a reason to seek a change? Must plaintiff prove that defendant acted in bad faith when it accepted the proffered modification? Must defendant prove that plaintiff lacked a reason to demand the change? Must defendant prove that plaintiff acted without good faith? Must defendant prove that plaintiff acted in bad faith? Does the absence of good faith mean plaintiff is in bad faith? To justify a refusal to enforce, must defendant show economic duress?

These problems of classifications and burdens¹¹ plague parties and courts dealing with modification contests. As a result, courts sometimes use good faith as a conclusory term to declare the winner of the suit. Courts

7. Coercion in this context could include economic coercion, such as may be present if a seller waited to make the demand for modification until he knew Buyer could no longer find substitute goods to meet other contract commitments.

8. Achieving a better deal after the contract has been formed is sometimes referred to as "recapturing foregone benefits" because the party gains back an advantage given up in the contract. A seller who enters a contract for steel beams at \$150 a ton has foregone the benefit of receiving \$160 a ton for the goods. See Janine S. Hiller, *Good Faith Lending*, 26 AM. BUS. L.J. 783, 803 (1989) (noting that parties "should not attempt to regain benefits that have been willingly foregone"); see also Steven J. Burton, *Breach of Contract and the Common Law Duty to Perform in Good Faith*, 94 HARV. L. REV. 369, 387 (1980); Thomas A. Diamond & Howard Foss, *Proposed Standards for Evaluating When the Covenant of Good Faith and Fair Dealing Has Been Violated: A Framework for Resolving the Mystery*, 47 HASTINGS L.J. 585, 593 (1996); Recent Case, 77 HARV. L. REV. 1142, 1146 (1964) (noting that "forgone benefits represent a cost to the subsidiary of entering the agreement").

9. See Robert A. Hillman, *Policing Contract Modifications under the UCC: Good Faith and the Doctrine of Economic Duress*, 64 IOWA L. REV. 849, 900 (1979).

10. See *infra* Part IV. C.

11. Generally, the drafters of the UCC have been reluctant to speak to the procedural issue of which party should bear the burden of proof on a particular issue. Although there are instances of express allocations of the burden of proof in the Code, see U.C.C. § 2-607(4) (placing the burden of proof on Buyer to establish a breach with respect to goods accepted), such expressions are the exception rather than the rule under the Code.

employ a wide range of tests and techniques for determining whether to enforce a modification. Some require the plaintiff seeking enforcement to make an affirmative showing that the modification was made in good faith.¹² Others grant enforcement unless the defendant is able to establish bad faith or coercion by the initiating party.¹³ This statement of the standard (requiring that defendant bear the burden of establishing bad faith by plaintiff) appears consistent with the general notion that the party asserting a breach by the other (here a breach of the obligation of good faith by the initiating party) bears the burden of showing that breach.¹⁴ On the other hand, a plaintiff (typically the initiating party in a modification) should bear the burden of proof as the party seeking to change the status quo.¹⁵ Thus, application of the general principle that the party asserting a breach should bear the burden fails to produce a clear rule in this context. Moreover, the choice of a good faith or a bad faith standard is more than a semantic distinction; it influences the focus of the court's inquiry and, in close cases, may determine which party prevails.¹⁶

Finding a test for reliably distinguishing between efficient modifications and those that are opportunistic is the challenge of the

12. *E.g.*, *United States v. Progressive Enters., Inc.*, 418 F. Supp. 662, 663 (E.D. Va. 1976) (recognizing good faith in a modification based on rising materials cost); *Lumber Enter., Inc. v. Hansen*, 846 P.2d 1046, 1049-50 (Mont. 1993) (holding modification reasonable where inexperienced seller, after performing for one year, determined that original contract price was below production costs).

13. *E.g.*, *Erie County Water Auth. v. Hen-Gar Constr. Corp.*, 473 F. Supp 1310, 1313 (W.D.N.Y. 1979) (stating that extortion violated obligation of good faith); *Ralston Purina Co. v. McNabb*, 381 F. Supp. 181, 187 (W.D. Tenn. 1974) (holding that a modification resulting in compounding Seller's damages was not in good faith and unenforceable by purchaser who knows or should know that Seller would not be able to complete contract); *Austin Instrument, Inc. v. Loral Corp.*, 272 N.E.2d 533, 536 (N.Y. 1971) (holding that agreement to increase price of equipment unfairly coerced Buyer when Buyer could not obtain goods from other reliable source).

14. The view that defendant bears the burden of showing bad faith (or coercion) by the initiating party finds broad support in the scholarship of this area. For example, Professor Robert S. Summers argues that the concept of good faith is identifiable only by contrasting it with "specific and variant forms of bad faith which judges decide to prohibit." Robert S. Summers, *The General Duty of Good Faith—Its Recognition and Conceptualization*, 67 CORNELL L. REV. 810, 820 (1982); Robert S. Summers, "Good Faith" in *General Contract Law and the Sales Provisions of the Uniform Commercial Code*, 54 VA. L. REV. 195, 201-02 (1968) [hereinafter *Good Faith*] (asserting that the concept of good faith "serves to exclude many heterogeneous forms of bad faith").

15. Here, each party asserts a breach: (1) Plaintiff asserts defendant breached the new obligation of the modification, and (2) Defendant asserts plaintiff breached the obligation of good faith applied under the original contract when he requested or demanded the change.

16. These differing approaches to applying section 2-209 seem to spring from differing judgments regarding the utility of contract modifications and differing intuitions about the significance of the problem of strategic or opportunistic demands for modification. They are apparent in the dualistic view of modification found in the comments to the section. *See infra* Part III. D.

modification puzzle. Like many judgments in the law, the line of enforceable modification may be “ever-shifting”¹⁷ in response to business norms and mores. It can be said with some confidence, however, that one ought not seek to modify a contract unless there is some change of circumstances or revelation that makes the original contract unfair or alters the expectations of the parties—at least from the perspective of the initiating party.¹⁸ The change of circumstances may result from increased costs of performance (making performance more burdensome for promisor) or from increased opportunity costs, as when a seller receives a more profitable offer. Although reasonable minds can differ regarding what constitutes good faith in a particular case, a process requiring initial consideration of the basis for the request to modify seems likely to advance the work of the courts, making their approach to this problem more consistent and focused.

This Article explores the modification puzzle and the issues of erratic justice that result from the nebulous nature of the UCC test. It evaluates an alternative test, called here the sequential approach, that scrutinizes each step of the modification process and imports the standard of reasonable grounds into this context. Based on the Code’s treatment of a related area, assurance of due performance, the sequential approach supplants the vague test of good faith with a requirement that the initiating party prove reasonable grounds for the modification and scrutinizes both the initiating and responsive stages of the modification in sequence.¹⁹ Part II discusses terminology and fundamental concepts in this area of law, including the reasons for seeking a modification, the steps of a modification, and the typical defenses to an action to enforce a modification. Part III of the Article considers the social utility of contract modifications, exploring both the vulnerability of contract parties to each other and the attributes of a

17. *Transatlantic Fin. Corp. v. United States*, 363 F.2d 312, 315 (D.C. Cir. 1966).

18.

If a person is well informed and in secure enjoyment of his rights, then whatever arrangements he chooses to make deserve to be honored. They represent a free man’s rational decision about how to dispose of what is his, how to bind himself Honesty assures, first, that one will not mislead another as to the facts in order to profit by the other’s misinformed decision. It assures also that engagements once made will be honored.

CHARLES FRIED, *CONTRACT AS PROMISE: A THEORY OF CONTRACTUAL OBLIGATION* 77-78 (1981).

19. The test could be characterized as a “shifting burden.” The sequential approach described here is similar to burden-shifting tests under other areas of law, e.g., *McDonnell Douglas Corp. v. Green*, 411 U.S. 792, 802 (1973) (holding that in non-class action suit under Title VII, the complainant bears the initial burden of proving the prima facie case; the burden then shifts to the respondent to show nondiscriminatory motive), with the additional attribute of attending to the sequence of the conduct by the parties.

utility-maximizing rule in this area. Part IV surveys the available standards for judging modifications. It considers good faith and bad faith standards and section 2-209(1) in its current form, parsing the text and comments of the provision and exploring reasons for the provision's failure to achieve a reliable rule. It also discusses the Restatement approach to the modification problem and evaluates the benefits and possible limitations of a "reasonable grounds" standard. Part V compares the traditional approach of the Pre-existing Duty Rule with the current solution of section 2-209(1) and examines the changes in the provision recently proposed by the National Conference of Commissioners on Uniform State Laws (NCCUSL). Part VI summarizes and analyzes decisional law. Part VII formulates language for a sequential test of good faith modeled on the test for assurances of performance under section 2-609. This Part considers the reasons for using section 2-609 as a model for the modification provision and assesses the sequential approach in light of typical defenses and representative hypothetical cases. The conclusion urges the NCCUSL and states to evaluate the sequential approach, considering whether it would facilitate the work of the courts by providing a more consistent and balanced test for enforcement of modified sales contracts.

II. FOUNDATIONAL CONCEPTS

A. Terminology

The modification problem arises when the parties change the contract in a way that provides a new benefit to one party and a new detriment to the other party. The Code applies the test of section 2-209 to both merchant and non-merchant agreements. Typically, the modifying party is the plaintiff seeking enforcement of the modification and the non-initiating party is the defendant.²⁰ Buyer is the obligor of the duty to pay and the obligee of Seller's duty to sell. Seller is the obligor of the duty to sell and the obligee of Buyer's duty to buy. In this Article, the modifying party is called the "initiating party" because the party sought, or initiated, the modification. As to the modified portion of the contract, the plaintiff is the obligee of the changed promise. For example, the seller-plaintiff who has

20. In some cases, however, the non-initiating party seeks to enforce the agreement as modified. *E.g.*, *IPEC, Inc. v. International Lithographing Corp.*, 869 F.2d 1080, 1084 (7th Cir. 1989) (granting damages based on finding modification reducing contract price resulted from buyer's bad faith); *T & S Brass & Bronze Works, Inc. v. Pic-Air, Inc.*, 790 F.2d 1098, 1105-06 (4th Cir. 1986) (enforcing modified contract in favor of buyer when seller initiated modification and later failed to perform); *Fratelli Gardino, S.P.A. v. Caribbean Lumber Co.*, 587 F.2d 204, 206 (5th Cir. 1979) (rejecting commercial impracticability as basis for contract rescission when Seller's sister company could have delivered goods and calculating damages based on modified contract).

secured a promise from Buyer to pay a higher price for goods than originally agreed is the obligee of Buyer's promise to buy at the higher price. In such a case, Buyer is the obligor of the modified promise to pay, and also can be called the "non-initiating" party. If he refuses to act in accordance with the modified contract, he is also a "recalcitrant." For example, Buyer refuses to pay the increment after agreeing to the higher price in a modification and the seller-obligee brings an action to enforce the modified obligation to pay the higher price.²¹

B. *The Steps of a Modification*

The modification process involves two steps: (1) a party seeks a modification, and (2) his contract partner agrees (or capitulates) to the change sought. The non-initiating party has a right to refuse any requested modification, demand performance under the original contract, and—in the event promisor does not perform as promised—sue for damages.²² In such a case, the rule on modification has no application because no modification occurs. The non-initiating party can also remonstrate with the initiating party, encouraging him to perform as promised. The feasibility of the non-initiating party's choices depends on a variety of factors, including the exigencies of future contracts, and (when he is the buyer in a contract) his ability to cover.²³

C. *The Reasons for a Modification*

Parties seek modifications for a variety of reasons—some justified and others not.²⁴ When the modification produces a change on each side and each party benefits from the modification, it has the central attribute of an original contract discussed above: the substance of the transaction is inscrutable. It is difficult to judge because each party apparently receives a bargained-for exchange. Like an original contract, enforcement should be the default for such modifications unless the party resisting enforcement can show that the other engaged in coercive conduct.

21. The reference to Seller as the initiating party is used as an example. *See supra* note 5 and accompanying text.

22. *E.g.*, *Bolin Farms v. American Cotton Shippers Ass'n*, 370 F. Supp. 1353, 1363 (W.D. La. 1974); *Buras v. Canal Constr. & Design Co.*, 470 N.E.2d 1362, 1366 (Ind. Ct. App. 1984) (finding that a non-initiating party may refuse a modification of a construction contract and sue for damages). A court may excuse the defendant's breach by nonperformance if defendant is able to establish the elements of mistake or impossibility.

23. The right to sue does not resolve the problem, however, since parties bargain for more than the right to win a lawsuit. *See* U.C.C. § 2-609 cmt. 1.

24. *See* JAMES J. WHITE & ROBERT S. SUMMERS, *THE UNIFORM COMMERCIAL CODE* 30 (1995).

Modifications that provide a unilateral change benefitting only one party may arise from a variety of circumstances. The party seeking the change may have encountered an unforeseen obstacle to performance or he may seek a change simply to gain a benefit. As a theoretical matter one might argue that modifications based on unforeseen benefits to the other party should also merit recognition. Considering both obstacles and benefits, from the Seller's point of view, two situations are likely: that some obstacle to performance unknown at the time of contracting makes the original contract unfairly burdensome to the Seller (category 1), or some benefit of performance unknown at the time of contracting renders the contract more (unfairly) favorable to the promisee (category 2). From the Buyer's point of view, two corollary possibilities are present: some obstacle to Buyer's performance (paying) unknown at the time of contracting makes the original contract unfairly burdensome to the Buyer (category 3), some benefit of performance unknown at the time of contracting renders the contract more (unfairly) favorable to the Seller (category 4).

Except under the doctrine of mistake, courts are reluctant to transfer unforeseen benefits from one party in a contract to the other; the presence of an unforeseen benefit does not provide a basis for excusing performance or modifying a promise for either Buyer or Seller.²⁵ Thus, categories (2) and (4) are not often litigated. Additionally, cases of Buyer-sought modifications may not be as common as Seller-initiated changes,²⁶ perhaps because obstacles or difficulties of paying are pretty clearly allocable as risks to the Buyer (category 3). Under this process of elimination, the circumstance of Seller's obstacles or burdens (category 1) seems likely to generate the greatest number of disputes.²⁷ Additionally, a party may seek to enforce a promise based on his reliance on that promise.²⁸

25. See *Erin Food Servs., Inc. v. Derry Motel, Inc.*, 553 A.2d 304, 311 (N.H. 1988) (requiring specific performance of a real estate option where there was significant appreciation in value of land between date of contract and trial court's order and transaction proved unexpectedly advantageous to buyer).

26. Nevertheless, buyers sometimes seek enforcement of an agreement as modified. *E.g.*, *Sonfast Corp. v. York Int'l Corp.*, 875 F. Supp. 1099, 1102-03 (M.D. Pa. 1995) (enforcing a modification which required Seller to waive rights to agreement and participate in rebid); *June G. Ashton Interiors v. Stark Carpet Corp.*, 491 N.E.2d 120, 124 (Ill. App. Ct. 1986) (holding that Seller's failure to fulfill the terms of a modified agreement constituted a material breach); *Jones v. Abriani*, 350 N.E.2d 635, 645 (Ind. Ct. App. 1976) (finding that Seller's express warranty constituted modification of a contract and was binding under U.C.C. § 2-209(1)).

27. *E.g.*, *Missouri Pub. Serv. Co. v. Peabody Coal Co.*, 583 S.W.2d 721, 728 (Mo. Ct. App. 1979) (rejecting an unforeseen cost increase which made contract unprofitable for Seller as a basis for a claim of commercial impracticability and granting specific performance in favor of Buyer).

28. See *infra* Part VII. D. 2-3. Such changes may be enforced even though not based on a change of circumstances when they appear to present minor changes or when the initiating party acted in reliance on the promise of the party who accepted the modification.

D. *Typical Defenses to a Modification*

Understanding the categories of defenses applicable to this area and assessing how the defenses are affected by the standard for enforcement provides a basis for judging the available standards for enforcement. The following discussion categorizes typical defenses to modification enforcement. Although the situations in which modification controversies arise are varied, the defenses raised by the defendant (recalcitrant party) generally fall into three distinct categories: (1) the defendant denies that the parties agreed to a modification,²⁹ (2) the defendant asserts that plaintiff lacked reasonable grounds for seeking the modification,³⁰ (3) the defendant admits the modification but asserts it is the product of coercion.³¹ These arguments may be raised singly or in conjunction.

1. Credibility Issues

In the first situation, the defendant (recalcitrant party) alleges that it never assented to the modification. This situation presents a credibility issue. The party attempting to enforce a modification may have a good faith claim to an enhanced price or some other benefit sought by the modification or he may “simply be a liar,”³² or chisler.³³

A separate credibility issue relates to the credibility of promisor's threat to breach. A threat by a seller to breach may lack credibility if the costs of breach (including the expected damages and lost revenues) exceed the net costs of performing. As a practical matter, assessment of this type of credibility depends on the completeness and accuracy of the non-initiating party's knowledge of the initiating party's costs.³⁴ Whether or not a seller's threat is not credible in the abstract (actual costs of breach are greater than costs of performing), buyer will also assess her need for the goods and the likely consequences of breaches she may be forced to commit as a result of her failure to obtain the goods, her ability to cover,

29. *See* *Tosco Corp. v. Oxygenated Mktg. & Trading A.G.*, No. 98C4695, 1999 WL 328342, at *4 (S.D.N.Y. May 20, 1999).

30. *See* *Essen Nutrition v. Electronic Liquid Fillers, Inc.*, No. 95C5486, 1996 WL 535340, *3 (N.D. Ill. Sept. 19, 1996).

31. *See* *Erie County Water Auth. V. Hen-Gar Constr. Corp.*, 473 F. Supp. 1310, 1314 (W.D.N.Y. 1979); *Essen Nutrition*, 1996 WL 535340, at *4.

32. WHITE & SUMMERS, *supra* note 24, at 34.

33. *See* Omri Ben-Shahar, *The Tentative Case Against Flexibility in Commercial Law*, 66 U. CHI. L. REV. 781, 803 (1999) (noting that the party who chisels after receiving goods “up front” exploits the promisee's enforcement costs).

34. Asymmetries of information affect a party's decision-making in many areas. In the increased price situation, asymmetries of information come into play when the non-initiating party attempts to judge the credibility of a threat to breach.

and the importance of the forward contracts to her (possible repeat business, liquidated damages clauses, reputation etc.). Even if the non-initiating party thinks the costs to the initiator should preclude his breach, she may not be willing to take the risk by saying no—in which case the bluff works.

2. The Defense of No Reasonable Ground

The reference to the requirement of good faith made by the Official Comment to section 2-209 suggests that good faith is a necessary element of an enforceable modification. Under the second defense, the defendant alleges that the plaintiff lacked good faith (or a reasonable ground for seeking the modification). For example, in the introductory hypothetical, if Madison County agreed to the change, believing Steel Perfect's representations about the increase in the price of iron (a component of steel) and later learned that the price had not risen, a court should refuse enforcement.³⁵

3. The Defense of Coercion

The issues of coerciveness and the reasonableness of the grounds for a modification are closely linked. It is theoretically possible for a defendant to raise the defense of coercion claim without asserting the defense that plaintiff lacked reasonable grounds to modify. The force of this argument is less powerful in this circumstance, however. If the coercion claimed arises solely from circumstances outside the control of the plaintiff, the defendant's claim is weakened.

III. THE UTILITY OF CONTRACT MODIFICATIONS

Just as parties are free to enter contracts of their own choosing, they are free to modify contracts as they please. Nothing in the Code or contract law prevents freely accepted changes. The option of modification works in conjunction with the principles of efficient breach and legal excuse. If expectancy damages operate to make the injured party whole, he will be indifferent to a breach. Economists and contracts scholars agree that the threat of breach has force only when expectation damages will fall short of the promisee's actual damages caused by a breach.³⁶

When changed circumstances disturb the equilibrium of the deal (by presenting enhanced burdens or a possible efficient breach), parties are free

35. Other settings for this claim are surveyed in Part VII, on application of a sequential approach.

36. *E.g.*, Ian Ayres & J.M. Balkin, *Legal Entitlements as Options: Property Rules, Liability Rules, and Beyond*, 106 *YALE L.J.* 703, 746 (1996).

to bargain around the change. Changes freely entered into presumably reflect utility to each party, whether the asserted need for modification arises from raised costs or raised opportunity cost. In a “raised costs” situation, the seller or supply side learns that it will cost more to perform. In the raised opportunity cost situation, Seller’s performance itself does not cost more but the seller has an opportunity cost that is higher. For example, a seller who can handle only one job at a time is presented with a significantly more profitable contract during the time period for which he has agreed to perform under the original contract.³⁷ In the raised opportunity cost situation, the concept of efficient breach provides protection for both contract parties. If a new opportunity allows the party to make a profit in addition to paying transaction costs and damages to his original (now aggrieved) partner, the substitute transaction presents an efficient breach. Seller has a more profitable use of his time, and his offer to modify can be seen as giving the non-initiating party the option of seeking damages or deciding to pay a higher price to moderate the raised opportunity costs to Seller. The circumstance can be dealt with by Buyer paying more or by Seller buying his way out of the contract through settlement. In the raised cost situation, by contrast, the party seeking to modify is in a losing situation; no better deal presents itself on the horizon. His costs are higher than believed at the time of contracting. Although the doctrine of legal excuse may protect the seller from liability, it does not save the net gain to society that the original contract presented. A subsequent contract may or may not be formed in its place if this transaction fails. If modification allows parties to save the contract by absorbing the raised costs that would otherwise destroy the contract, there is a net benefit in that the contract (as modified) goes forward.

From this perspective, there seems to be no persuasive reason for policing modifications; suggesting that parties who enter a modification should be bound by it. The modified contract may have utility for only one party, however with the other agreeing because of coercion³⁸ or duress.³⁹ The reinvented contract may be a “hold-up” deal.⁴⁰

37. Because the raised opportunity cost scenario seems to present the weaker case for modification, this Article focuses on the raised costs situation rather than the raised opportunity cost situation.

38. Black’s Law Dictionary defines coercion as “compulsion by physical force or threat of physical force.” BLACK’S LAW DICTIONARY 252 (7th ed. 1999).

39. Black’s Law Dictionary defines duress as “physical confinement of a person or the detention of a contracting party’s property,” or “threat of confinement of detention, or other threat of harm, used to compel a person to do something against his or her will or judgment.” *Id.* at 520.

40. *Angel v. Murray*, 322 A.2d 630, 635 (R.I. 1974) (noting that the “primary purpose of the preexisting duty rule is to prevent . . . the ‘hold-up game’”).

A. *The Vulnerability of Contract Parties to Modification*

The heart of the modification problem seems to lie in the vulnerability of contracting parties to each other. Every party to a contract is vulnerable to opportunistic demands for modifications by his contract partner. Furthermore, every party is vulnerable to a hard-nosed refusal to modify a contract despite a justifiable reason for modifying.⁴¹ The non-initiating party has a right to insist on the original agreement and he can enforce the agreement in court unless the initiating party convinces the court that his performance should be excused under the doctrine of mistake or impossibility.⁴² While such vulnerability is most noticeable in long-term sales contracts or contracts for the sale of custom built, high-ticket items, it is present in the basic relationship formed in each contract. The supply side invests significant time and resources in developing and producing a product for sale (in the case of a manufacturer) or in locating and obtaining the goods (in the case of a broker). Likewise, the recipient of the goods incurs reliance costs by rejecting deals with others and by incurring preparation costs. Significant costs and time delays occur when the buyer must try to revive earlier offers from rejected bidders.

One might suppose that the option of refusing to modify protects the non-initiating party. If he needs the goods and does not wish to grant a concession to the party initiating the modification, he should simply refuse the modification request and demand performance as agreed under the original contract. Such a response may not be a realistic choice, however.⁴³ If the initiating party refuses to perform in response to the rejection of the modification, the non-initiating party may find itself in breach on other contracts. He has entered contracts for resale or plans to use the goods as raw materials or component parts. Inability to obtain the goods from Seller harms not only Buyer but also those subsequent purchasers of goods and

41. The principle that courts will not make contracts for the parties limits the protection given to a party who is justified in seeking a modification. Courts will not force even a fair modification on a party who refused to assent to the change. *See Park-Lake Car Wash, Inc. v. Springer*, 394 N.W.2d 505, 510 (Minn. Ct. App. 1986) (holding that Plaintiff was entitled to enforcement on agreement when it refused to assent to second modification); *Solar Motors, Inc. v. First Nat'l Bank*, 545 N.W.2d 714, 721 (Neb. 1996) (finding that mutual assent was required to modify a contract, which substantially changes the liabilities of the parties).

42. Courts will excuse performance of such a party under the doctrines of mistake and impossibility. The doctrines of mistake and impossibility arguably serve to allow breach when it is efficient. Enforcement of modifications to respond to situations of mistake or impossibility is noncontroversial. Similarly, the law of modification seems to allow parties to go forward to performance and, thus, avoid an inefficient breach.

43. *E.g., Austin Instrument, Inc. v. Loral Corp.*, 272 N.E.2d 533, 536 (N.Y. 1971) (noting that the recalcitrant party had no choice but to capitulate to demands for modification because of contracts to provide products to the Navy on schedule).

services further along in the stream of commerce. Likewise, the supply side is vulnerable to demands that he provide more than the original contract required or “settle” for a lower price.

B. *A Utility-Maximizing Rule*

Judicial enforcement of a modification differs from enforcement of an original contract. In deciding whether to enforce an original contract courts employ the validation device of consideration. This doctrine gives parties wide latitude to enter bargains that are efficient from their own unique perspectives, and a court need not deem a bargain fair to enforce it. Additionally, the consideration doctrine prevents the enforcement of contracts not bargained for despite the free assent of the parties. By contrast, the good faith standard applied to modifications seems to call for a judgment by the court that the new agreement meets minimum standards of fairness.⁴⁴ The difference in treatment of these two situations is not haphazard. It reflects a judgment that the situations differ in significant ways.

Every law student knows that a peppercorn⁴⁵ will serve as consideration if a court determines that it was bargained for rather than being a sham⁴⁶ or nominal consideration.⁴⁷ The doctrine of consideration relieves courts of the need to determine whether a transaction is “fair.” Determining fairness in the context of an original contract is burdensome, if not impossible. The difficulty arises in large part because of the lack of a baseline for judging the benefit or detriment of the deal;⁴⁸ the burdens and

44. At first blush, the consideration for the original contract may seem sufficient as a validation device for the modified contract. This justification may prove too broad, however, since its logical extension is that all modifications should be enforced without regard to good faith.

45. *See Williams v. Kansas Dep’t of Soc. & Rehab. Serv.*, 899 P.2d 452, 456 (Kan. 1995) (upholding multi-million dollar trust established with “peppercorn” of ten dollars); *Omaha Nat’l Bank v. Goddard Realty, Inc.*, 316 N.W.2d 306, 310 (Neb. 1982) (noting sufficiency of “peppercorn”); *Weiner v. McGraw-Hill, Inc.*, 443 N.E.2d 441, 445 (N.Y. 1982) (recognizing “proverbial peppercorn” as “adequate consideration”); *Jackson v. Alexander*, 3 Johns. 484, 493 (N.Y. Sup. Ct. 1808).

46. *See* RESTATEMENT (SECOND) OF CONTRACTS § 71 cmt. b, illus. 5 (1981) (noting that neither a “mere pretense of bargain” nor “merely nominal” consideration meets the test of bargained for consideration).

47. The triumph of the bargain theory of contract law imported the use of the process of bargaining for an exchange into formation analysis, rejecting the consideration doctrine as a formalism to justify the use of nominal consideration. *See id.* § 71; *Demasse v. ITT Corp.*, 984 P.2d 1138, 1145 (Ariz. 1999) (recognizing that consideration existed where employer and employee made a “bargained for exchange”); *Schade v. Diethrich*, 760 P.2d 1050, 1057 (Ariz. 1988) (holding that consideration exists where performance or a return promise is bargained for); *Carlisle v. T & R Excavating, Inc.*, 704 N.E.2d 39, 43 (Ohio Ct. App. 1997) (finding that no contract existed where consideration was not bargained for).

48. Professor Trebilcock has noted the difficulty of distinguishing between offers and threats.

benefits are inscrutable, and contract law has advisedly chosen a standard which presumes benefit when each party bargained for the deal. Thus, the minimal standard of consideration relieves courts of the need to evaluate the burdens and benefits of the deal to the parties.⁴⁹

The law of modification rejects such a hands-off approach, perhaps because parties already bound together in a contract are especially vulnerable to pressure from each other. A primary reason for entering a contract is to lock in the price or performance offered.⁵⁰ After parties enter a contract, they stop the search for a contracting partner and prepare to perform. Absent some constraint imposed by law, the hard (some would say “unscrupulous”) bargainer could enter an agreement and then seek seriatim, modifications to achieve a more favorable deal or to reinstate conditions rejected by the other in the original bargain.⁵¹ Thus, greater judicial oversight may be desirable in this context. Additionally, courts can make more confident judgments about the fairness of a modification because the original contract provides the baseline for judging benefits and burdens. It is relatively easy to see whether the modification has a clear winner and a clear loser, at least when the modification involves a single change.⁵² On the other hand, when each party receives a sought-for change, the situation presents inscrutability on a level comparable to that of original contracts. In such cases, as with original contracts, the free bargaining principle seems to require enforcement.⁵³

MICHAEL J. TREBILCOCK, *THE LIMITS OF FREEDOM OF CONTRACT* 80 (1997) (citing CHARLES FRIED, *CONTRACT AS PROMISE: A THEORY OF CONTRACTUAL OBLIGATION* 92-111 (1981)). He explains this difficulty by taking an example from Fried. *See id.* A pianist who has given free recitals for a church states that he will require a fee for recitals in the future. *See id.* Is the status quo (baseline) free recitals or is this a new offer to give something (a recital for a fee)? *See id.*

49. The presumption is that parties who enter into a voluntary private exchange are each better off because of the exchange or they would not have entered it. *See Whitney v. Stearns*, 16 Me. 394, 397 (1839) (noting the sufficiency of a peppercorn to satisfy consideration doctrine).

50. *See David V. Snyder, The Law of Contract and the Concept of Change: Public and Private Attempts to Regulate Modification, Waiver, and Estoppel*, 1999 WIS. L. REV. 607.

51. If modifications are judged by too lenient a standard, parties will not be able to rely on an agreement or to plan with confidence future business transactions.

52. This is not to say that complexity never arises in modifications. Some modifications involve a change that is arguably beneficial to both parties such as when both performance and price are changed. This situation takes on characteristics of the original contracting process and reinserts the difficulty of determining fairness.

53. Other factors may lessen the likelihood of opportunistic conduct on the part of the initiating party. For example, the opportunity for repeat contracting between the parties encourages good faith in modifications. Likewise, because the sharing of information within a trade group enhances the importance of the reputation of a trader, opportunistic modifications are less likely in such settings. Finally, the Code provides some protection for the non-initiating party against unfair demands for modification. Conversely, in cases where parties are unlikely to contract again, the incidence of opportunistic conduct may be heightened. *See infra* Part VII. B. It is likely that a party presented with a request or demand for modification has reasonable grounds to demand assurances

Obstacles to performance do not, in and of themselves change contract obligations. That a contract is more difficult to perform than anticipated does not justify a refusal to perform; nor does it create a right to modify. Rather, such obstacles to performance raise the difficult qualitative question of whether the nature and extent of the obstacle or additional burden provide a basis for a court to excuse performance. The doctrines of mistake and impossibility deal with such issues effectively,⁵⁴ excusing performance only when the burden is sufficiently significant.⁵⁵ This is not to say that the fixed-price contract can never be modified but rather that the reason for seeking a modification should be a primary concern of the court in determining whether a modification is a reasonable request or a “hold-up game.”⁵⁶

of performance from the other party. *See* U.C.C. § 2-609.

54. The doctrine of mistake deals with an unallocated risk, which creates a problem that neither party knew of at the time of contracting. *See* RESTATEMENT (SECOND) OF CONTRACTS §§ 152-154 (1981). Impossibility, further divided into impracticability and frustration, deals with the problem of obstacles that arise after contracting. *See id.* at §§ 261, 265, 266; *see also* Northern Ind. Pub. Serv. Co. v. Carbon County Coal Co., 799 F.2d 265, 275 (7th Cir. 1986) (holding that doctrines of frustration or impracticability are not applicable where contract specifically assigns a particular risk to contracting party); Florida Power & Light Co. v. Westinghouse Elec. Corp., 517 F. Supp. 440, 446 (E.D. Va. 1981) (refusing to recognize defenses of impossibility, impracticability, frustration or mutual mistake where contractor assumed risk of difficulty of performance); Aluminum Co. of Am. v. Essex Group, Inc., 499 F. Supp. 53, 59 (W.D. Pa. 1980) (recognizing the doctrines of impracticability and frustration where Seller’s nonlabor production costs rose beyond foreseeable limits and reforming agreement between parties); Sunflower Elec. Coop., Inc. v. Tomlinson Oil Co., 638 P.2d 963, 971 (Kan. Ct. App. 1981) (denying relief under the impracticability of performance doctrine where the risk was foreseeable to seller and circumstances of contract indicated seller assumed risk).

55. A rich and detailed body of law relating to the classification of obstacles deemed sufficient to excuse performance inhabits the doctrine of impossibility. *See* Steven L. Schooner, *Impossibility of Performance in Public Contracts: An Economic Analysis*, 16 PUB. CONT. L.J. 229, 265 (1986) (asserting that courts should consider which party is primary risk bearer to determine whether performance failure should be excused in public contracts); Gerhard Wagner, *In Defense of the Impossibility Defense*, 27 LOY. U. CHI. L.J. 55, 63-89 (1995) (discussing the impossibility doctrine in light of current economic theory); Susan E. Wuorinen, Case Comment, Northern Indiana Public Serv. Co. v. Carbon County Coal Company: *Risk Assumption in the Claims of Impossibility, Impracticability, and Frustration of Purpose*, 50 OHIO ST. L.J. 163, 177-78 (1989) (arguing that courts should consider the totality of the circumstances at contract formation in determining whether performance failure should be excused). Code provisions on mistake, impossibility, and the right of assurances present a template for weighing the performing party’s need for change against the needs of the recipient. Thus, while these doctrines place a burden on the party seeking to change the baseline of the contract, they provide significant judicial leeway. They assess “the ever-shifting line, drawn by courts hopefully responsive to commercial practices and mores, at which the community’s interest in having contracts enforced according to their terms is outweighed by the commercial senselessness of requiring performance.” *Transatlantic Fin. Corp. v. United States*, 363 F.2d 312, 315 (D.C. Cir. 1966).

56. *Angel v. Murray*, 322 A.2d 630, 635 (R.I. 1974) (recognizing that a preexisting duty rule

A standard that makes modifications too difficult creates a brake on the economy, making parties reluctant to enter future contracts for fear they will be held to performance in changed circumstances. Likewise, a rule that allows frivolous or opportunistic modification is a disincentive to trade. A standard that allows easy modifications (unsupported by a reason for the change) undermines the certainty of contracts and erodes confidence in contracting.⁵⁷ Certainty is a relative concept,⁵⁸ however, describing a principle that is not always desirable. Indeed some contract principles deliberately embrace a standard of uncertainty to encourage continuity and stability, pushing the parties toward working out their problems rather than abandoning the contractual relationship they have entered.⁵⁹

When an unallocated contingency occurs, the appropriate starting point in the analysis of modification is the contract itself.⁶⁰ It defines the rights of the parties. This fact suggests that the initiating party should not be allowed to enhance his position under the contract absent an affirmative showing of reasonable grounds or detrimental reliance.⁶¹ The party who unilaterally declares the contract at an end or seeks to excuse his

seeks “to prevent . . . the ‘hold-up game’”); *see also* Jason Scott Johnston, *Default Rules/Mandatory Principles: A Game Theoretic Analysis of Good Faith and the Contract Modification Problem*, 3 S. CAL. INTERDISCIPLINARY L.J. 335, 342-50 (1993) (explaining the “hold-up” game and noting incentives to pay when remedy for breach is not fully compensatory); Barry J. Kusnitz, *Damages in Construction Litigation*, 38-May R.I. B.J. 13, 25-6 (1990) (pointing to *Alaska Packers Assoc. v. Domenico*, 117 F. 99 (9th Cir. 1902), as a classic example of the hold-up game and noting examples of such behavior in the construction industry).

57. The modifying party would argue for a more lenient standard than impracticability, pointing to the assent of the contract partner as a reason for enforcing a modification. While this argument has appeal, a lenient standard may encourage parties to contract without sufficiently investigating the possibility of a change in the market price of the good or in the cost of raw materials needed to manufacture the good.

A contractual regime must maintain the integrity of bargains, and this means not reversing the allocation of risks on which the parties evaluated their bargain when they made them. Bargains are struck and their prices evaluated on the assumption that they will be kept. If they are not kept, the injured party may claim expectation damages.

FRIED, *supra* note 18, at 117.

58. Complete certainty is never attainable in the contracts context in the sense of ensuring that parties go through with the deal as originally agreed. After all, the power of rescission always lies within the joint decision-making of the parties. In the face of a stringent rule regarding what constitutes an enforceable modification, parties may retreat from the contract via rescission.

59. *See infra* Part IV.

60. In contracting, parties may allocate risks of contingencies occurring. Likewise, they may designate the types of changes in circumstances that justify a modification to their contract. By doing so, parties produce a further allocation of the risks under the contract.

61. *See* WHITE & SUMMERS, *supra* note 24, at 35.

performance based on mistake or impracticability is changing the baseline of the status quo agreed to by the parties. Accordingly, he bears the burden of persuading the court that his claim of excuse is justified. Likewise, a party who seeks a modification is changing the baseline of the contract, and, absent mitigating circumstances, should bear the initial burden of establishing a need for the change.⁶²

One way to assess the influence of a modification rule is to hypothesize the extreme cases. Assume, for example, that modifications are enforceable without regard to the good faith or reasonable grounds for requesting the modification. In such a system, there would be little reason to enter contracts other than those for immediate performance. The existence of a contract would merely indicate that parties have agreed to go forward together with likely future changes to the arrangement. Such a scheme fails to provide security for contracting parties or to encourage advance planning by businesses and individuals. Conversely, a system which allows no modifications also discourages contracting by failing to allow changes in response to changing needs and circumstances. Thus, courts need a standard that strikes a balance, minimizing the likelihood of opportunistic modification but allowing efficient modifications.

IV. STANDARDS FOR JUDGING MODIFICATIONS

The variety of approaches employed by courts, legislative bodies, and scholars in judging modifications is evidence of the difficulty of finding a satisfactory test for assessing the interests present in the modification problem.

A. *The Good Faith Standard*

Professor Farnsworth noted that the term “good faith” has a “faintly pious ring to it”⁶³ that may seem out of place in commercial law.⁶⁴ Nevertheless, good faith has long been recognized by courts as a requirement in commercial transactions, binding parties not only to the express terms of an agreement but also to those “naturally implied” in the agreement.⁶⁵ Clearly a wide range of opinion exists regarding what

62. White and Summers apply the label of “extortionist” to the party who requires additional payment without justifiable cause. *See id.*

63. Farnsworth, *supra* note 4, at 669.

64. *See id.* (identifying good faith with terms such as “faith,” “morals,” and “honor” may seem “curious” in describing commercial conduct).

65. F.H. LAWSON, A COMMON LAWYER LOOKS AT THE CIVIL LAW 124-25 (1955); *see also* Amoco Oil Co. v. Ervin, 908 P.2d 493, 498 (Colo. 1995) (noting widespread use of the good faith performance doctrine to effectuate intentions of parties); Wood v. Lucy, Lady Duff-Gordon, 118 N.E. 214, 214 (N.Y. 1917) (recognizing an implied duty to use reasonable efforts); Hayden v.

constitutes good faith. For example, Professor Charles Fried reasons that the duty of good faith requires a “forthcoming attitude.”⁶⁶ Professor Robert S. Summers argues persuasively that good faith can best be understood in terms of the conduct it excludes.⁶⁷ Professor Robert Jerry notes the “near tautological qualities of any definition of good faith.”⁶⁸ Professor Ian Ayres reasons that contract parties have the power to alter the expectations or defaults of contract law, adding detail to what comprises good faith in their agreement.⁶⁹

1. The Code’s Use of Good Faith

The general requirement of good faith for transactions governed by the UCC is set forth in section 1-203: “Every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement.”⁷⁰ Good faith can be regarded as a larger set than consideration because it can embrace gratuitous promises as well as ones supported by consideration. It also comprises a smaller set than consideration because contracts for which consideration exists may fall short of the good faith requirement if

Hoadley, 111 A. 343, 345 (Vt. 1920) (implying a duty to complete work in reasonable time when a contract lacked completion date).

66. “The concept of good faith is regularly invoked not only to condemn deception and lack of candor at the time a bargain is concluded, but also to require a forthcoming attitude, to condemn chicanery and sharp practice in the carrying out of contractual obligations.” FRIED, *supra* note 18, at 85. Similarly, Professor Gillette notes that “[m]any scholars advocate an expansive interpretation of good faith.” Clayton P. Gillette, *Limitations on the Obligation of Good Faith*, 1981 DUKE L.J. 619, 619.

67. See Summers, *supra* note 14.

68. Robert H. Jerry, II, *The Wrong Side of The Mountain: A Comment on Bad Faith's Unnatural History*, 72 TEX. L. REV. 1317, 1336, 1343 (1994) (suggesting that treating insurer bad faith “as a contract breach and invoking contract remedies would give insurers more certainty about outcomes . . . [and] reduce system-wide costs”). Professor Clayton Gillette argues that the obligation of good faith that inheres in every contract does not impose a duty to be a commercial good Samaritan or to rescue one’s contract partner from economic peril when the obligor did not create the peril and had no duty under the contract to assume a risk of the peril. See Gillette, *supra* note 66, at 656; see also Susan D. Gresham, “Bad Faith Breach”: A New and Growing Concern for Financial Institutions, 42 VAND. L. REV. 891, 913-16 (1989); Eileen A. Scallen, *Sailing the Uncharted Seas of Bad Faith: Seaman’s Direct Buying Serv., Inc. v. Standard Oil Co.*, 69 MINN. L. REV. 1161, 1165-76 (1985); Kevin M. Teeven, *Development of Reform of the Preexisting Duty Rule and Its Persistent Survival*, 47 ALA. L. REV. 387, 441-53 (1996).

69. See Ian Ayres, & Stewart Schwab, *Economic Analysis of State Employment Law Issues Symposium*, 8 KAN. J.L. & PUB. POL’Y 71, 85 (1999) (noting unenforceability of clause “Seller waives duty of good faith performance”).

70. U.C.C. § 1-203; *Conoco Inc. v. Inman Oil Co.*, 774 F.2d 895, 909 (8th Cir. 1985) (defining good faith to mean parties must “do nothing destructive” of other party’s right to enjoy fruits of contract and must do “everything the contract presupposes it will do to accomplish the contractual purpose and finding Conoco breached obligation of good faith by underpricing competitor”).

the transaction does not meet minimum standards of fairness.⁷¹ The term “good faith” carries a variety of meanings within the Code. The drafters refer to good faith approximately fifty times⁷² within the 400 provisions of the Code.

In imposing a standard of good faith under the Code, section 1-203 differentiates between the formation of the contract and the enforcement or performance of the contract. While good faith inheres in the enforcement and performance stages of contract, the Code imposes no good faith obligation in contract formation,⁷³ leaving the policing of formation to equity concepts⁷⁴ and doctrines imported from tort law.⁷⁵

The meaning of good faith is also influenced by the status of the party evaluated, further complicating the inquiry under section 2-209.⁷⁶ The Code includes a general definition of “good faith” as “honesty in fact in the conduct or transaction concerned.”⁷⁷ This threshold standard of section 1-201(19) requires subjective good faith in every Code transaction. Article 2 also includes a definition relating specifically to merchants. Good faith in the case of a merchant under Article 2 means “honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade.”⁷⁸ This definition adds the objective requirement of “reasonable commercial standards” to judge the conduct of merchants. Thus, the standard applicable to merchants combines subjective and objective elements. It requires that the merchant establish that his conduct was both

71. See U.C.C. § 2-209, cmt. 1 (rejecting consideration as a substitute for good faith); see also *Permanent Ed. Board Commentary 10*, reprinted in *SELECTED COMMERCIAL STATUTES* 790, 792 (West 2000).

72. See Farnsworth, *supra* note 4, at 667. Because of the numerous references, Farnsworth calls good faith “the darling of draftsman.” *Id.*

73. Although the comments to U.C.C. § 2-209 leave unclear the choice of a standard, the choice of good faith seems to dispel the argument that the standard is inapplicable to the modification process. The courts that have dealt with the requirement have applied the good faith requirement to modification cases. See *Northern Fabrication Co. v. Unocal*, 980 P.2d 958, 962 (Alaska 1999) (noting the court’s desire to preserve good faith agreements); *Hendlin v. Fairmount Constr. Co.*, 72 A.2d 541, 556 (N.J. Super. Ct. Ch. Div. 1950) (recognizing common law rule of good-faith contract modification); *Enserch Corp. v. Rebich*, 925 S.W.2d 75, 83 (Tex. Ct. App. 1996) (noting that consideration is not required for good-faith modification).

74. Courts may refuse to enforce a contract specifically based on equity concepts. *E.g.* *Harper, Drake & Assoc., Inc. v. Jewett & Sherman Co.*, 182 N.W.2d 551, 561-62 (Mich. Ct. App. 1970) (holding agreement void for lack of consideration).

75. For example, a contract based on fraud or misrepresentation is voidable. *E.g.* *Germantown Mfg. v. Rawlinson*, 491 A.2d 138, 141 (Pa. 1985) (noting that contract was voidable on showing of fraudulent or material misrepresentation).

76. The approach suggested in this Article simplifies the inquiry of good faith while maintaining the distinction between transactions involving a consumer or consumers and those involving two merchants. See *infra* Part VI.

77. U.C.C. § 1-201(19) (1998).

78. U.C.C. § 2-103(1)(b).

honest and consistent with “reasonable commercial standards.”⁷⁹ The Code defines merchant as follows:

Merchant means a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction or to whom such knowledge or skill may be attributed by his employment of an agent or broker or other intermediary who by his occupation holds himself out as having such knowledge or skill.⁸⁰

Applying these standards to the introductory hypothetical case illustrates the variation in the meaning of good faith. Steel Perfect (Seller) appears to fit the definition of “merchant” under the Code; it “deals in goods of the kind” (i.e., steel in this transaction) and also apparently “holds [itself] out as having knowledge or skill peculiar to the practices or goods involved in the transaction.”⁸¹ Thus, Steel Perfect’s conduct in the modification process is subject to the requirement applicable to merchants, that is “honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade.”⁸² The Buyer, Madison County, may or may not fall within the Code’s definition of “merchant.” Probably the County does not hold itself out as having special expertise in steel, but it may hold itself out “as having knowledge or skill peculiar to the practices” of contracting for public improvements such as bridges.⁸³ Additionally, it

79. *Id.* Additionally, a third standard of “good faith and within limits set by commercial reasonableness” inheres in some settings. Farnsworth, *supra* note 4, at 676.

80. U.C.C. § 2-104.

81. *Id.*

82. *Id.* § 2-103(1)(b).

83. Comment 2 to U.C.C. § 2-104 provides support for holding Madison County is a “merchant” for purposes of the modification contest. It provides:

The special provisions as to merchants appear only in this Article and they are of three kinds. Sections 2-201(2), 2-205, 2-207 and 2-209 dealing with the statute of frauds, firm offers, confirmatory memoranda and modification rest on normal business practices which are or ought to be typical of and familiar to any person in business. For purposes of these sections almost every person in business would, therefore, be deemed to be a “merchant” under the language “who . . . by his occupation holds himself out as having knowledge or skill peculiar to the practices . . . involved in the transaction . . .” since the practices involved in the transaction are non-specialized business practices such as answering mail. In this type of provision, banks or even universities, for example, well may be “merchants.” But even these sections only apply to a merchant in his mercantile capacity; a lawyer or bank president buying fishing tackle for his own use is not a merchant.

may have contracted through “an agent or broker or other intermediary who by his occupation holds himself out as having such knowledge or skill.”⁸⁴ If the County held itself out as having such special knowledge or hired such an intermediary, it will also be held to the higher standard of both “honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade.”⁸⁵ If the County did not act through an intermediary and did not hold itself out as having expertise, it would be held to the more subjective (and more lenient) standard of “honesty in fact in the conduct or transaction concerned.”⁸⁶

Just as background expectations cannot be fully articulated at the outset of any transaction,⁸⁷ the concept of good faith cannot be exhaustively defined without context.⁸⁸ It is, of necessity, somewhat amorphous. Nevertheless, it may have greater precision and determinateness within a specific context.⁸⁹ In specific settings, courts can discern content in the “protean concept”⁹⁰ of good faith and determine a baseline or minimum for comporting with the requirement in a well-defined issue.⁹¹ Indeed, the parties may add specific content to the meaning of good faith used in their contract.⁹² In the area of settlements, for example, the fact of assent is insufficient to enforce a settlement. The party seeking enforcement must show that he held a good faith belief in the claim he surrendered, not simply that the parties bargained for that surrender. The good faith required to support a settlement is generally based on a test requiring honesty and reasonableness.⁹³ Enforcing settlements without such a showing of good

Id. § 2-104 cmt. 2.

84. *Id.* § 2-104.

85. *Id.* § 2-103(1)(b).

86. *Id.* § 1-201(19).

87. FRIED, *supra* note 18, at 87.

88. See *Good Faith*, *supra* note 14, at 215. (“If an obligation of good faith is to do its job, it must be open-ended rather than sealed off in a definition.”).

89. See *Permanent Ed. Board Commentary* 10, *supra* note 71, at 792; Christina L. Kunz, *Frontispiece on Good Faith: A Functional Approach Within the UCC*, 16 WM. MITCHELL L.REV. 1105, 1117 (1990) (urging drafters revising UCC to “re-examine the ‘grab-bag’ use of good faith” and adopt instead a functional analysis to make it “easier to ascertain” within the context of particular sections).

90. Farnsworth, *supra* note 4, at 668.

91. See Kunz, *supra* note 89, at 1110-14.

92. See Ian Ayres, *Empire or Residue: Competing Visions of the Contractual Canon*, 26 FLA. ST. U. L. REV. 897, 901-02 (1999) (noting that “many prophylactic rules that are initially characterized as mandatory often can be modified to give even more protection to one of the contracting parties. For example, the mandatory duty of good faith can be contracted around to enhance a promisor’s fiduciary duties.”).

93. See E. ALLAN FARNSWORTH, *CONTRACTS* § 2.12, at 72-73 (2d. ed. 1990) (noting that courts generally require both an honest belief and a doubtful claim, i.e., one that has some substance in fact). Although *Restatement Second* seems, by its literal language, to endorse enforcement based on good faith alone, see *RESTATEMENT (SECOND) OF CONTRACTS* § 74(1) (1981), many courts

faith would establish a system of “anything goes” so long as the party seeking enforcement obtained the assent of the obligor. In such a system, nuisance lawsuits would provide the basis for an enforceable settlement.

In the area of modification the irreducible minimum of good faith should be that the initiating party has a legitimate reason for seeking the modification. Whatever drives trading partners—egoism, zero sum wagering, or cooperative risk sharing⁹⁴—the obligations set by the original contract provide the baseline of expectations.⁹⁵ Thus, the analysis of whether to enforce the modification should begin with the reason for the change. A test of reasonable grounds, like that used in the settlement context, would provide a scenario that stops short of a “free card” or “anything goes” for the initiating party. While such a standard would not provide iron-clad insurance against opportunism, it would, provide a platform for judicial scrutiny of the transaction and reduce the likelihood of opportunistic conduct without unduly restricting modifications.⁹⁶

2. Good Faith in Section 2-209

Comment 2 to section 2-209 speaks of the good faith requirement in general terms, creating the impression that the good faith of both parties is required for an effective modification. Further consideration of the issue suggests, however, that only the initiating party’s good faith should be considered in the modification context. It makes no sense for a court to refuse to enforce a modification on the ground that the defendant (capitulating party) lacked good faith and never intended to live up to the modification.⁹⁷ When the initiating party meets the requirements noted, the capitulating party’s lack of good faith should not constitute a defense for enforcement. Taking the introductory hypothetical as an illustration, assume that the parties agreed to Steel Perfect’s requested modification based on a significant price change, that the risk of such a change was unallocated by the contract, and that Steel Perfect used no coercive tactics. Assume further that Madison County never intended to pay the increased price. This lack of good faith by Madison County should not constitute a defense to the claim for enforcement by Steel Perfect when Steel Perfect meets the requirements noted above.⁹⁸ Making the capitulating party’s good faith an element of the claim benefits the party in the wrong, giving

require the showing of reasonableness of the plaintiff’s belief as well. *See* FARNSWORTH, *supra*, § 2.12, at 72-74.

94. *See* Gillette, *supra* note 66, at 651.

95. *See* Fried, *supra* note 18, at 17-21.

96. Limiting modifications to cases in which the excuse of impossibility or mistake is established is too restrictive.

97. *See* THE RESTATEMENT (SECOND) OF CONTRACTS § 89.

98. *See supra* text accompanying notes 5-8.

that party a “free card” to renounce the modification at will.⁹⁹ The capitulating party’s intention to perform, *vel non*, should be irrelevant to the inquiry of enforcement under section 2-209. Moreover, an investigation of the party’s subjective intent is at cross purposes with the accepted standard of objective manifestation of intent.¹⁰⁰

The requirement of good faith springs from the obligations formed by the contract; it does not encompass an element necessary for enforcement. Good faith is applicable to both parties once they modify the contract just as the requirement of good faith inheres in every contract once the parties create it. Thus, a party seeking to enforce a contract need not establish the good faith of the parties in the formation of the contract. Likewise, in a modification, the capitulating party’s obligation of good faith should be seen as a mandate rather than a test for enforceability. The initiating party’s good faith, on the other hand, goes to the heart of the issue whether circumstances justified the modification sought by the initiating party.

B. *The Competing Standard of Bad Faith*

The comments to section 2-209(1) also refer to the standard of bad faith, that evil twin often lurking in the shadows of good faith issues. The concept of bad faith has garnered its share of commentary and judicial notice.¹⁰¹ Courts deciding modification cases sometimes focus on whether the modification was the result of bad faith by the modifying party.¹⁰² In the *Wisconsin Knife* case, for example, Judge Posner noted that the UCC drafters “took a fresh approach” to the issue of modification “by making modifications enforceable even if not supported by consideration . . . and looking to the doctrines of duress and bad faith for the main protection

99. It is not surprising that courts have not rejected modifications on this basis.

100. See *Laserage Tech. Corp. v. Laserage Lab., Inc.*, 972 F.2d 799, 802 (7th Cir. 1992) (holding that assent is determined by “reference to what parties expressed to each other in their writings, not by their actual mental processes”); *Lucy v. Zehmer*, 84 S.E.2d 516, 522 (Va. 1954) (noting that a party’s “undisclosed intention is immaterial except when an unreasonable meaning which he attaches to his manifestations is known to the other party”).

101. E.g., Linda Curtis, *Damage Measurements for Bad Faith Breach of Contract: An Economic Analysis*, 39 STAN. L. REV. 161, 163-72 (1986); Gresham, *supra* note 68, at 913-16; Jerry, *supra* note 68, at 1318-37; Eileen A. Scallen, *Sailing the Uncharted Seas of Bad Faith: Seaman’s Direct Buying Serv., Inc. v. Standard Oil Co.*, 69 MINN. L. REV. 1161, 1165-76 (1985).

102. See *Wisconsin Knife Works v. National Metal Crafters*, 781 F.2d 1280, 1288 (7th Cir. 1986) (holding that an attempted oral modification of contract operated as waiver of written modification requirement only if there was a showing of reliance, and absent a showing of reliance, judgment in favor of seller could not stand); *Oskey Gasoline & Oil Co. v. Continental Oil Co.*, 534 F.2d 1286, 1288 (8th Cir. 1976); *Pirrone v. Monarch Wire Co.*, 497 F.2d 25, 29 (5th Cir. 1974); *United States ex rel. Crane C. v. Progressive Enters., Inc.*, 418 F. Supp 662, 664 (E.D. Va. 1976) (holding that modification was enforceable when request for modification was justified by Seller’s increased cost and that Buyer engaged in bad faith conduct when refusing to pay adjusted price).

against exploitive or opportunistic attempts at modification.”¹⁰³ When facts establish duress or coercion, courts refuse enforcement under section 2-209.¹⁰⁴ The distinction between the good faith and bad faith standards often seems to be a matter of allocating the burden of proof.

C. *The Restatement Approach to Modification*

The Restatement sets forth its analysis of the modification problem in section 89, which provides:

A promise modifying a duty under a contract not fully performed on either side is binding (a) if the modification is fair and equitable in view of circumstances not anticipated by the parties when the contract was made; or (b) to the extent provided by statute; or (c) to the extent that justice requires enforcement in view of material change of position in reliance on the promise.¹⁰⁵

In comparison with section 2-209, the Restatement approach provides more guidance for courts. It endorses enforcement of a modification that is “fair and equitable in view of circumstances not anticipated by the parties when the contract was made.”¹⁰⁶ This approach to modification is more helpful than that of the UCC approach in two distinct ways. First, the standard focuses on the modification itself rather than on the contract as modified, drawing attention to the event of significance. Additionally, the standard fleshes out the meaning of fair and equitable by noting the context relates to “circumstances not anticipated by the parties.”¹⁰⁷ This statement of the standard focuses the court on evaluating the ground for a

103. *Wisconsin Knife Works*, 781 F.2d at 1285-86.

104. The refusal to enforce a coercive modification is noncontroversial and, for that matter, available without resort to section 2-209. In other words, coercion and duress provide an independent basis for refusing to enforce a contract. Contract law has developed policing doctrines that invalidate obligations assumed as a result of duress or coercion. *See* *Norton v. Michigan State Highway Dept.*, 24 N.W.2d 132 (Mich. 1946) (defining duress and coercion); *Mancino v. Friedman*, 429 N.E.2d 1181 (Ohio Ct. App. 1980) (finding economic duress sufficient to void contract); *Crane*, 1999 WL 701393 *4 (distinguishing duress and coercion; defining duress as a “threat that arouses such fear as to preclude a party from exercising free will and judgment; coercion as that which “implies compulsion or restraint”); *Rush v. Derrick*, 1999 WL 111782 *8 (Tex. App.) (unpublished opinion) (defining duress as “threat to do some act which the threatening party has no legal right to do” (quoting *Tenneco Oil Co. v. Gulsby Eng’g Inc.*, 809 S.W.2d 599, 604 (Tex. 14 D.C.A. 1993)) involving “open coercion,” and noting that “duress” “destroy[s] the free agency of the party to whom it is directed; causes imminent restraint; and that the person to whom it is directed has no present means of protection”).

105. RESTATEMENT (SECOND) OF CONTRACTS § 89 (1981).

106. *Id.*

107. *Id.*

modification. The comment to the section notes that the requirement of the section “goes beyond absence of coercion and requires an objectively demonstrable reason for seeking a modification.”¹⁰⁸

The scope of the section is limited to a “contract not fully performed on either side.”¹⁰⁹ The Restatement does not explain the reason for this limitation.¹¹⁰ The official comments to section 89 of the Restatement do not analyze or mention the limitation. This limitation may indicate a view that a dispute regarding a contract fully performed on one side presents a setting for settlement rather than modification. Or it may acknowledge the greater vulnerability of a party who has fully performed compared with one who owes an executory duty. A party who has performed can no longer modify his performance. Accordingly, he lacks leverage in negotiations to change a contract. For example, assume that a party has paid in advance \$10,000 for another to excavate a basement. Upon hitting rock, the excavation company seeks an increase in the price. If the Buyer of services has already paid the \$10,000, he is worse off than if he has paid nothing. If he chooses not to go forward with the modification, he will need to seek return of the payment in addition to finding a substitute deal. In such a case, Seller can exploit all of the usual pressures on Buyer (the difficulty of opening negotiations again with other sellers, the exigencies of needing the goods) and, additionally, the leverage that Buyer no longer has the payment price to offer others and that Buyer’s money (as well as the goods) is held up. Similarly, the seller who has fully performed before receiving payment may be more vulnerable to Buyer’s demands to do a bit more since Buyer is holding on to the money and Seller has invested reliance costs in performing. He may capitulate rather than resist Buyer in this situation.

108. *Id.* at § 89, cmt. b.

109. *Id.* § 89.

110. The UCC makes no mention of such a limit in scope in the sale of goods context. Professor Teeven argues that the limitation allowing modification only of contracts not fully performed on one side may not serve the logic of the Code:

If section 89 is going to permit a modification of a partially executed contract, then why not permit a modification when it has been fully performed on one side or the other? . . . The possibility of extortion should no longer be a concern once the performance is completed, but it is a factor to consider when the partial performer refuses to proceed unless he is paid more. If a modification is freely consented to after a party has fully performed, why not enforce it if the promisor finds a benefit or consents to recompense because of the unforeseen difficulties it will overcome?

Kevin M. Teeven, *Development of Reform of the Preexisting Duty Rule and Its Persistent Survival*, 47 ALA. L. REV. 387, 431-32 (1996).

In the case of *Angel v. Murray*,¹¹¹ the Rhode Island Supreme Court enforced a modification of a contract between the City of Newport and a company under contract to haul the city's waste, finding that a modification is justified without consideration (or nominal consideration) when changed circumstances make the modified contract fair and equitable.¹¹² It required that the circumstances "which prompted the modification were unanticipated by the parties, and the modification is fair and equitable,"¹¹³ and noted that the scope of modification is limited to executory contracts.¹¹⁴

D. *The Reasonable Ground Standard*

Some courts refuse enforcement of modifications absent a showing that the plaintiff had a justifiable cause (here referred to as "reasonable ground") for seeking the change. The standard of reasonable grounds presents a more specific inquiry than the generalized standard of "good faith." Although the term "reasonable grounds" is, itself, a relative term, subject to variation based on the circumstances presented in individual cases, the Code imposes this requirement in the area of assurances of performance.¹¹⁵

Whether substitution of this test of "reasonable grounds" in place of "good faith" advances the analysis of this area is, of course, open to debate. Contract law does not require reasonable grounds for contract formation or for a decision by the parties to rescind the contract. But it does require that the party have "reasonable grounds" to seek assurances from the other that he will perform as promised. In the case of contract formation or termination by rescission, joint action is required. Together the parties change the baseline of their relationship. When a party is dissatisfied with the contractual arrangement and wishes to make a change, he can urge the other party to rescind and form a new contract or rescind and end the relationship. The distinction of joint action versus unilateral action may not

111. 322 A.2d 630 (R.I. 1974).

112. The *Angel* case is a precursor to the *Restatement Second* treatment of modification. The *Angel* court cited comment (b) to section 89 of *Restatement Second* in tentative draft form. 322 A.2d at 637 n.3.

113. *Id.* at 637.

114. The *Angel* case involved a contract entered by the City of Newport and Alfred Angel, a refuse hauler. *Id.* at 631. When the city grew at an unanticipated rate, Angel sought a modification to the contract to pay him additional compensation of \$10,000 per year. *See id.* The trial court refused enforcement of the modified contract on the basis that Angel had not fulfilled the process for approval by the city, and additionally, because the plaintiff had a pre-existing duty under the original contract to haul all of the waste generated by both old and new homes. *See id.* The reviewing court reversed on the ground that the changes in compensation were justified because the "extra collection resulted from actions completely beyond [plaintiff's] control." *Id.* at 638.

115. *See* U.C.C. § 2-609 (1998).

tell the full story, however. As a practical matter, someone goes first in exploring any change, including exploring the possibility of entering a contract, dissolving a contract, or entering a modification. Every formation or rescission begins when one of the parties initiates it—a unilateral act. Nevertheless, in the cases of contract formation or rescission the significant step is taken by the parties jointly. The policies of freedom underlying the free bargain theory of contracting accept this joint decision, and the doctrine of consideration dispenses with detailed inquiry into the benefits and burdens of the decision—when the parties have bargained for that change.

This analysis also applies to modifications when there is some beneficial change on each side. In such circumstances, it seems to make sense to treat modification like formation and rescission. In cases where there is a new benefit to only one party, however, the context presents a situation closer to that of the assurance of performance area. When a modification presents a unilateral benefit to one party, it parallels the context of a demand for assurances. In response to an obstacle to performance or some dissatisfaction, one party takes a unilateral action to attempt to regain equilibrium (or an opportunistic party seeks to gain some advantage). In the assurances context, the Code looks squarely at the question of the basis for the first volley in the sequence: the ground upon which an individual sought assurances. Like the assurances area, scrutiny of the reason for a demand to modify limits the power of a party to engage in a hold-up game.

Any rule devised to balance the rights of the parties in this area should be constructed with careful knowledge that too stringent a doctrine may push parties to rescind their contract and re-contract to avoid the doctrine. This move, which could be referred to as the “rescission-reformation” trick, reduced the power of the pre-existing duty rule.¹¹⁶ Thus, construing reasonable grounds too narrowly creates new problems accompanying an overly-rigorous test. For example, a reasonable grounds standard that accepts only a situation justifying excuse of performance may not give sufficient leeway for modification.¹¹⁷ The reasonable grounds test need not

116. The pre-existing duty rule has no effect on a change when the parties rescind the original contract and enter a new contract to achieve a change. Because the parties have rescinded the contract containing the original duty, no existing duty is changed by the second contract. See Hillman, *supra* note 4, at 685 (noting that “mutual rescission” theory is “perhaps the most frequently invoked exception to the preexisting-duty rule”) (citing *Schwartzreich v. Bauman-Basch, Inc.*, 131 N.E. 887, 889 (N.Y. 1921)).

117. Excuse of performance is based on the doctrines of mistake, impracticability (also called impossibility) or frustration. “Traditional doctrine distinguishes two kinds of surprises: mistake, and frustration or impossibility. Mistake relates to a false assumption about how things are at the time of contracting; frustration and impossibility relate to incorrect assumptions about how things will be later, when it comes time to perform.” FRIED, *supra* note 18, at 58; *supra* note 44.

be so restrictive. It is satisfied by a judicial consideration of the grounds for the change to provide a way of separating the unfair demands to alter a contract from reasonable requests for a change.

E. *Voluntariness as a Standard for Judging Modifications*

Another way of addressing the good faith required for an enforceable modification is by focusing on the voluntariness, *vel non*, of the party who assents to the modification.¹¹⁸ The controlling assumption is that one who freely assents to a requested modification should be held to it. This approach has difficulties of its own, of course. Voluntariness is a relative concept. Even assuming a clear case of a justified modification, the capitulating party's assent may be involuntary in a sense. The party agreeing to pay a higher price for goods certainly does not like the change that now requires the higher payment. Moreover, the defendant resisting enforcement can be depended upon to assert that his assent was not voluntary. Courts rightly refuse to determine such questions of mental disposition by the declarations of the parties to a controversy. Just as issues of intent should not be determined by "a tour of Walters' cranium, with Walters as the guide,"¹¹⁹ the issue of the voluntariness of a modification rightly requires stronger proof than the assertions of an interested party.

F. *The Effects of the Nebulous Test*

Absent the protections of a reliable test separating reasonable from opportunistic modifications, the existence of a contract does little more than set the stage for a series of additional negotiations during the time period between contracting and performance. Modifications that allow the initiating party to gain new advantages undermine the certainty of contracts.¹²⁰ Allowing modifications without sufficient justification destabilizes the expectations of contracting parties and diminishes the efficiency of contracting. On the other hand, certainty is a relative concept. Modern contract law has rejected the formalistic stance of Williston and the early tradition of formalism, which favored certainty over flexibility. Moreover, complete certainty is never attainable in the sense of ensuring

118. See *Angel v. Murray*, 322 A.2d 630, 634 (R.I. 1974); *Watkins & Son v. Carrig*, 21 A.2d 591, 594 (N.H. 1941) (enforcing a modification and noting that defendant "intentionally and voluntarily yielded to a demand" for a higher price after plaintiff encountered rock in its excavation of a cellar for defendant).

119. *Skycom Corp. v. Telstar Corp.*, 813 F.2d 810, 814-15 (7th Cir. 1987).

120. The benefits of certainty can be overstated. Certainty is a relative concept and one that does not always enhance efficient contracting. See *supra* Part III. The Utility of Contract Modification.

that parties go through with the deal as originally agreed.¹²¹ Indeed, certainty is not always a good thing in contract law. In some settings, contract law fosters uncertainty. For example, under the doctrine of material breach, a party to a contract is not free to cancel the contract with impunity. Unless the other party has materially breached the contract, the decision to declare a contract terminated is “fraught with peril.”¹²² This fact leads to great uncertainty for a person considering whether to terminate the contract. The decision whether a material breach has occurred involves balancing several factors to assess the positions and conduct of each party.¹²³ The canceling party should also know that the court’s judgment—rather than his own—controls the decision of whether the termination is itself a material breach.¹²⁴ The intentionally nebulous standard of material breach is desirable because it encourages the parties to resolve their differences and go forward with the contract, maintaining their contractual relationship.

In the context of modification, by contrast, uncertainty destabilizes contracting by increasing the likelihood of demands for modification. A party who knows that considerable uncertainty surrounds the issue of whether the initiating or capitulating party bears the burden of proof at trial may be emboldened to demand changes. If he can wrest an agreement from the other, the modifying party may prevail simply because of a dearth of proof from the defendant. In a contest involving a nebulous rule, every fact is significant and the role of advocacy is enhanced. This fact enhances, in turn, the likelihood of unsystematic and haphazard results and greater temptations to demand modifications.

V. THE CURRENT UCC SOLUTION TO THE MODIFICATION PROBLEM

In 1952, the National Conference of Commissioners on Uniform State Laws (NCCUSL) and the American Law Institute (ALI) approved the Uniform Commercial Code. As the states adopted the Code thereafter, section 2-209 changed the common law relating to modification of sales contracts by dispensing with the requirement of consideration. Now enacted in virtually all U.S. jurisdictions, the provision allows parties to

121. The power of rescission always lies within the joint decision-making of the parties. In the face of a stringent rule regarding what constitutes an enforceable modification, parties may retreat from the contract via rescission.

122. *Walker & Co. v. Harrison*, 81 N.W.2d 352, 355 (Mich. 1957).

123. These include the extent to which the injured party will be deprived of the benefit he expects under the contract, the ability to adequately compensate the injured party, the likelihood of forfeiture by the party failing to perform, the likelihood of cure by the party failing to perform, and good faith and fair dealing. *See* RESTATEMENT (SECOND) OF CONTRACTS § 241 (1981).

124. *See id.* §§ 241-242. If the termination constitutes a material breach, it may justify a claim for damages and the discharge of the injured party’s duty to perform.

create an enforceable modified agreement without establishing consideration for the change of obligation.¹²⁵

A. *The Change From the Common Law*

Traditional common law looked to whether the original contract had been rescinded or modified on both sides, requiring the party seeking enforcement to satisfy the doctrine of consideration as a way of protecting the non-initiating party from coercion.¹²⁶ The common law recognized that the potential for coercion is present in the modification context.¹²⁷ Having entered a contract, the parties have ceased negotiations with others and their ability to make a substitute arrangement may be severely curtailed. In business slang, the non-initiating party may be “over a barrel,”¹²⁸ or the initiating party may be chiseling or playing a “hold-up game.”¹²⁹ At common law, a party could defeat enforcement of a modification unless the plaintiff established that the modification was supported by consideration. The doctrine establishing this power, the Pre-Existing Duty Rule, continues to operate at common law in some jurisdictions, but it appears to be of decreased importance generally.¹³⁰ Although the sweeping

125. A Westlaw search conducted on Sept. 7, 1999 found forty-nine states have adopted some form of section 2-209, dispensing with the requirement of consideration in the modification of sales contracts. Louisiana has not adopted section 2-209, but Louisiana case law supports dispensing with consideration in the contract modification context. *See Pennzoil Co. v. Fed. Energy Reg. Comm.*, 789 F.2d 1128, 1144 (5th Cir. 1986) (referring to U.C.C. § 2-209 in recognizing that modification may occur when buyer complies with seller’s request for price increase); *Snedegar v. Noel Estate*, 438 So. 2d 677, 679 (La. Ct. App. 1983) (noting that contracts may be modified by mutual consent of the parties).

126. *See Alaska Packers’ Ass’n v. Domenico*, 117 F. 99, 102 (9th Cir. 1902) (holding a contract modification unenforceable absent revocation and new agreement or additional consideration).

127. The difficulty of determining whether particular conduct amounts to coercion is a separate, difficult topic. Professor Trebilcock asserts that the “prior determination” of rights necessary to determine whether a move is coercive “takes issues of coercion outside the domain of contract law.” TREBILCOCK, *supra* note 48, at 80-81.

128. “[W]hen a businessman is poorly educated, ‘over a barrel,’ or the victim of fine print, a court may invalidate a clause that would otherwise stand up between ordinary business persons.” WHITE & SUMMERS, *supra* note 24, at 157; *see also Oldenburger v. Del E. Webb Dev. Co.*, 765 P.2d 531, 534 (Ariz. Ct. App. 1988) (finding no contract repudiation in plaintiff’s statement that she was “over a barrel”); *Gooch v. Am. Sling Co.*, 902 S.W.2d 181, 187 (Tex. Ct. App. 1995) (holding a claim of being “over a barrel” failed to demonstrate duress sufficient to void contract).

129. *See Angel v. Murray*, 322 A.2d 630, 635 (R.I. 1974).

130. *See Gregory E. Maggs, Ipse Dixit: The Restatement (Second) of Contracts and the Modern Development of Contract Law*, 66 GEO. WASH. L. REV. 508, 513 (1998) (reviewing twenty-one cases that relied on section 89 and predicting that “most courts will follow” the section). At common law, parties can create an enforceable modified contract by revoking their original agreement and entering a new (modifying) agreement. *But see Teeven, supra* note 110, at 387 (noting the “400-year survival of the much-criticized . . . rule”).

principle imposed by the Pre-Existing Duty Rule may go too far in the direction of protecting against extortion,¹³¹ a rule requiring the party opposing enforcement to show coercion may swing the test too far in the other direction.¹³²

B. *The Goals of the UCC*

The Code seeks to attain both flexibility and stability in the rules governing contracts for the sale of goods.¹³³ In situations in which the parties agree that a modification is justified, no countervailing social issue requires stability or maintenance of the original contract. Thus, no tension exists between the goals of stability and flexibility in freely entered modifications. But tension between flexibility and stability is present in disputes that go to court with the parties disagreeing about whether the modification was the product of free will. When a party resists

131. See Charles L. Knapp, *Reliance in the Revised Restatement: The Proliferation of Promissory Estoppel*, 81 COLUM. L. REV. 52, 72 (1981) (noting "glaring flaws" of the Pre-existing Duty Rule, including "abuse that can be practiced by one who apparently assents to the modification of an existing contract, knowing that he can repudiate it with impunity").

132. See Hillman, *supra* note 9, at 849-50 (stating that "[d]espite the restrictiveness of the pre-existing duty rule," it "did provide to contracting parties some protection from unfair demands to alter contract terms already freely agreed upon"); WILLIAM D. HAWKLAND, HAWKLAND UNIFORM COMMERCIAL CODE SERIES § 2-209:03 (1999) (noting "elimination of the need for consideration to make a binding agreement to modify . . . also eliminated a safeguard that existed at common law against fraudulent or mistaken allegations that the parties had agreed to changes in the original contract"); Richard A. Posner, *Gratuitous Promises in Economics and Law*, 6 J. LEGAL STUD. 411, 422 (1977).

133. See Robert A. Hillman, *A Study of Uniform Commercial Code Methodology: Contract Modification Under Article Two*, 59 N.C. L. REV. 335, 336 (1981). Professor Hillman's point is undoubtedly correct although the Code does not include flexibility or stability in its list of goals to be attained. The Code lists its general purposes in section 1-102:

- (1) This Act shall be liberally construed and applied to promote its underlying purposes and policies.
- (2) Underlying purposes and policies of this Act are
 - (a) to simplify, clarify and modernize the law governing commercial transactions;
 - (b) to permit the continued expansion of commercial practices through custom, usage and agreement of the parties;
 - (c) to make uniform the law among the various jurisdictions.
- (3) The effect of provisions of this Act may be varied by agreement, except as otherwise provided in this Act and except that the obligations of good faith, diligence, reasonableness and care prescribed by this Act may not be disclaimed by agreement but the parties may by agreement determine the standards by which the performance of such obligations is to be measured if such standards are not manifestly unreasonable.

U.C.C. § 1-102 (1998).

enforcement, his position in court is that he did *not* freely assent to the modification.

C. *The Standard of Section 2-209*

The drafters of the Code used broad standards as a way of incorporating flexibility to the Code.¹³⁴ The good faith standard is an example of such intentional flexibility.¹³⁵ By imposing a requirement of good faith, the drafters of the Code supplanted the validation device of consideration in the modification context,¹³⁶ allowing courts to consider fairness in this setting.¹³⁷ Although the text of the provision makes no mention of good faith,¹³⁸ the requirement appears in the official comment to the provision. Thus, when a party enters a modification as a result of economic duress or coercion,¹³⁹ a court should refuse to enforce the modification.¹⁴⁰ Often the evidence regarding the modification will not present a clear picture, however. In such cases, the meaning of good faith employed by a court is likely to be determinative. Professor Hillman pointed out the failure of the Uniform Commercial Code to provide protection from unfair demands to alter contract terms.¹⁴¹ Noting that the approaches to modification formulated by both the Code and the Restatement (Second) of Contracts

134. See Hillman, *supra* note 9, at 851.

135. *Id.*; *Good Faith*, *supra* note 14, at 215. ("If an obligation of good faith is to do its job, it must be open-ended rather than sealed off in a definition.")

136. U.C.C. § 2-209 cmt. 1.

137. "[T]he occasions and pressures for contract changes are numerous and diverse. A contract modifier may be motivated by changed circumstances, unforeseen circumstances, or mere change of mind. And not all contract modifiers are honest. Extortionists, chiselers, and whiners also come to feed at § 2-209."

138. The comment also notes that "good faith" as applied to merchants includes an objective standard. U.C.C. § 2-209 cmt. 1. The test of "good faith" between merchants or as against merchants includes "observances of reasonable commercial standards of fair dealing in the trade." *Id.* § 2-103.

139. See *Rich & Whillock, Inc. v. Ashton Dev., Inc.*, 204 Cal. Rptr. 86, 90-91 (Cal. Ct. App. 1984) (enforcing an original agreement on grounds that the settlement agreement and release were products of economic duress).

140. See Hillman, *supra* note 9, at 849-50 (stating that "[d]espite the restrictiveness of the pre-existing duty rule . . . the rule did provide to contracting parties some protection from unfair demands to alter contract terms already freely agreed upon").

141. *Id.* at 850. In his 1979 article, Professor Hillman noted that conflicting paradigms pointed to the failure of the Uniform Commercial Code to "provide to contracting parties some protection from unfair demands to alter contract terms already freely agreed upon." *Id.* The proposed revision to section 2-209(1) addresses this problem by expressly incorporating a good faith standard as a requirement of an effective modification. Professor Hillman also delineated the difficulty of determining which of the good faith standards under the Code applies in this setting, and of assessing modifications under either of the standards. *Id.*

“have been off the mark,”¹⁴² he criticized section 2-209(1) for failing to offer guidance in determining which modifications should be enforced and concluded that “the Code’s approach has not been very successful in supporting voluntary modifications or in precluding coerced ones.”¹⁴³ Commentators have offered a variety of approaches for defining an inquiry that would separate worthy and enforceable modifications from undesirable and unenforceable modifications. For example, Professor Hillman suggested that a modification “that produces a material net loss on the contract to the promisor . . . should be presumed to be the result of coercion.”¹⁴⁴

D. *The Dichotomy of Approaches and Mixed Messages of Section 2-209*

The experience of over four decades suggests that the lack of precision of a generalized good faith standard deprives section 2-209 of force and tends toward an undependable application of its principles. Indeed, the generalized nature of the provision is not the only problem. The confusion of this area springs in large part from the mixed messages and dual tests of the comments to this section. The potential for confusion in the language of the comments can best be seen through a line-by-line analysis of Comments 1 and 2 to section 2-209. To facilitate analysis of the language, each sentence of Comments (1) and (2) is indented.

Comment 1: This section seeks to protect and make effective all necessary and desirable modifications of sales contracts without regard to the technicalities which at present hamper such adjustments.¹⁴⁵

Comment 1 limits the protection and endorsement of the provision to “all necessary and desirable modifications,” providing some content to the concept of good faith in this context.¹⁴⁶ The comment expressly rejects “the

142. Hillman, *supra* note 4, at 686. Professor Newell called the provision a “mess,” and declared its drafting “perhaps the worst in Article 2.” Douglas K. Newell, *Cleaning up U.C.C. Section 2-209*, 27 IDAHO L. REV. 487, 487 (1990-91). Professors Goetz and Scott noted that the Code test of §2-209(1) is “substantially more difficult to enforce” than the Pre-existing Duty Rule and “may not deter extortionate renegotiation as effectively.” Charles J. Goetz & Robert G. Scott, *The Mitigation Principle: Toward a General Theory of Contractual Obligation*, 67 VA. L. REV. 967, 1024 (1983).

143. Hillman, *supra* note 4, at 686.

144. Hillman, *supra* note 9, at 884.

145. U.C.C. § 2-209 cmt. 1.

146. *Id.*

technicalities which at present hamper such adjustments," an apparent reference to the Pre-existing Duty Rule.¹⁴⁷

Comment 2, sentence 1: Subsection (1) provides that an agreement modifying a sales contract needs no consideration to be binding.¹⁴⁸

The first sentence of Comment 2 simply restates the provision's effect of dispensing with the doctrine of consideration for purposes of modification, emphasizing the drafters' rejection of the Pre-existing Duty Rule.

Comment 2, sentence 2: However, modifications made thereunder must meet the test of good faith imposed by this Act.¹⁴⁹

The second sentence of Comment 2 provides the clearest focus on the good faith requirement, stating that modifications "must meet the test of good faith."¹⁵⁰ This sentence seems to set the applicable test. Its form is mandatory, suggesting that the plaintiff seeking enforcement of a modification bears the burden of establishing good faith. The reference seems to identify good faith as a non-negotiable element of the test. Indeed, it appears to point to good faith as the full test of the enforceability of a modification.

Comment 2, sentence 3: The effective use of bad faith to escape performance on the original contract terms is barred, and the extortion of a "modification" without legitimate commercial reason is ineffective as a violation of the duty of good faith.¹⁵¹

The third sentence of Comment 2 states the converse and creates redundancy. It states an example that clearly does not meet the standard noted in the previous sentence: A modification motivated by bad faith is not enforceable. It should go without saying that, if the test is good faith, then it is not met by a showing of bad faith. The comment states that "extortion of a 'modification' without legitimate commercial reason is ineffective."¹⁵² By discussing an extreme, this statement inserts confusion

147. *Id.*

148. *Id.* § 2-209 cmt. 2.

149. *Id.*

150. *Id.*

151. *Id.*

152. *Id.*

regarding who must carry the burden of proof under section 2-209(1). Are the drafters championing the obvious, or setting a burden on the shoulders of the defendant who opposes enforcement of the modification? Some courts have read this sentence as a paradigm for enforcement, putting defendants in the position of producing evidence of an initiating party's bad faith.¹⁵³

Comment 2, sentence 4: Nor can a mere technical consideration support a modification made in bad faith.¹⁵⁴

Sentence 4 rejects "mere technical consideration" to support a bad faith modification, emphasizing the Code's total rejection of consideration as a validation device in the modification context.¹⁵⁵ The rejection operates on two levels. Consideration is neither necessary nor sufficient to support a modification. In other words, plaintiff need not show consideration, and the fact that the plaintiff establishes technical consideration is irrelevant. Consideration is thus rejected as a substitute for the good faith standard. Without this point, an opportunistic party could urge enforcement of a bad faith modification based on the doctrine of consideration. Nevertheless, the comment's reference to "bad faith" further muddies the water, encouraging courts to require that defendants establish bad faith to defeat enforcement of a modification.

Comment 2, sentence 5: The test of "good faith" between merchants or as against merchants includes "observance of reasonable commercial standards of fair dealing in the trade" (section 2-103), and may in some situations require an objectively demonstrable reason for seeking a modification.¹⁵⁶

Sentence 5 to Comment 2 deals with merchants. Consistent with section 2-103, the sentence notes that merchants are held to the objective standard of the "observance of reasonable commercial standards of fair dealing in the trade."¹⁵⁷ But the Comment's statement that the court "may in some situations require an objectively demonstrable reason for seeking

153. *Wisconsin Knife Works v. Nat'l Metal Crafters*, 781 F.2d 1280 (7th Cir. 1986) (announcing need for showing of bad faith to defeat modification); *Jamestown Farmers Elevator v. General Mills, Inc.*, 522 F.2d 1285 (8th Cir. 1977) (requiring economic duress to overcome modification); *Agroindustrias Vezel v. H.P. Schmid*, 1994 WL 12342 (holding that claim of economic duress hinges on showing of a wrongful act "sufficiently coercive to cause a reasonably prudent person faced with no reasonable alternative to succumb to the perpetrator's pressure").

154. U.C.C. § 2-209 cmt. 2.

155. *Id.*

156. *Id.*

157. *Id.*

a modification,”¹⁵⁸ adds confusion, suggesting that such an “objectively demonstrable reason” is sometimes—but not always—necessary. This comment sets up a standard for enforcement, and, in the same breath, denies it force, leaving unclear whether plaintiff must produce evidence of a legitimate reason for the modification. The comment gives no guidance regarding when courts should require a reason for the modification.

Comment 2, sentence 6: But such matters as a market shift which makes performance come to involve a loss may provide such a reason even though there is no such unforeseen difficulty as would make out a legal excuse from performance under sections 2-615 and 2-616.¹⁵⁹

Sentence 6 continues the trend toward confusing dualism. It draws out the analysis to the point at which clear guidance seems just around the corner, but stops short of an explanation. The sentence indicates that a market shift in the cost of performance that does not present a legal excuse may provide a basis for enforcement.¹⁶⁰ While this sentence makes clear that the set of enforceable modifications includes promises given in circumstances that would not justify the modifying party in withholding performance, it fails to set any parameters on the concept, leaving courts to wonder if “anything goes.” Does every market shift justify a demand for a modification? If so, is there any reason to enter a fixed price contract? If not, in what circumstance might a market shift fall short of a reason for modifying?

It may be that the drafters intended to define a situation in which the initiating party ultimately fails to establish the legal excuse of impracticability although he had a good faith belief that he could rightly withhold performance. Like the law of settlement, this interpretation gives leeway to the initiating party without setting up an “anything goes” system.¹⁶¹ To assume that the comment endorses enforcement for the

158. *Id.* (emphasis added).

159. *Id.*

160. Here, the drafters use the phrase “market shift” to refer to a market shift in input prices, constituting raised cost to the seller. A market shift may, by contrast, relate to the price of the goods contracted for. Such a shift creates an increased opportunity cost of performing—a circumstance less likely to justify modification.

161. A focus on the good faith belief of the plaintiff achieves the kind of balance endorsed in the settlement area by case law and § 74 of *Restatement (Second) of Contracts*. In addition to showing that the defendant settler assented to the agreement, the party seeking to enforce a settlement must show that he held a good faith belief at the time of the settlement that this claim was well-founded. *See* *Nationwide Mut. Ins. Co. v. Volland*, 653 A.2d 484, 488 (Md. Ct. Spec. App. 1995); *United Cal. Bank v. E. Mountain Sports, Inc.*, 546 F. Supp. 945, 962 (Mass. 1982). Similarly, section 76 of *Restatement (Second) of Contracts* focuses on good faith in a context in which a claim is doubtful. *See* *Fiege v. Boehm*, 123 A.2d 316, 321-22 (Md. 1956). Without this

initiating party who knows he has no right to withhold performance allows the clear risk of enforcement although the initiating party acted to recapture benefits foregone in the original contract.

The comments to section 2-209 present a mixed message. The confusion engendered by the dual approaches is particularly troubling because it leaves open the question of choice of an enforcement paradigm. Thus, the stage is set for indeterminacy in litigated cases and in the marketplace.

E. NCCUSL's Provision

As part of its revision of Article 2—the first comprehensive reevaluation of the Article since the 1950s¹⁶²—the National Conference of Commissioners on Uniform State Laws (NCCUSL) and the ALI proposed a change that expressly incorporated the obligation of good faith into the text of section 2-209.¹⁶³ The text of the proposal states: “An agreement made in good faith modifying a contract under this article needs no consideration to be binding.”¹⁶⁴ A newly formed committee is now beginning again the task of revising Article 2, including this proposal.¹⁶⁵

It could be argued that, rather than effecting a real change, the revised provision merely made the good faith requirement more conspicuous by moving it from commentary to text.¹⁶⁶ Nevertheless, by clarifying its purpose, the revision improved the provision significantly. Moreover, since states do not ordinarily adopt the Code's official comments, moving the requirement to text defeats the possible argument that good faith is not mandated by this provision. Although the change proposed would improve the provision dramatically, it falls short of the goal of a reliable rule. The proposed change perpetuates the confusion of the original text regarding which party bears the burden of establishing good faith or the absence of good faith. The history of the Code, the variety of approaches found in decisional precedent, and judicial ambivalence toward modification are likely to perpetuate the current confusion in this area of law. Against this backdrop, the comments to the proposed revision fail to clarify the test. The only comment to section 2-209 relevant to modified agreements is a

check of good faith, pure nuisance settlements and modifications made without legitimate reason would be enforceable.

162. See Amelia H. Boss & Jean Braucher, *Significant Changes in the Proposed Revisions of Article 2 on Sales*, SB29 ALI-ABA 143, 145 (1996).

163. See William C. Smith, *Selling Contract Revisions, Again*, 85 A.B.A.J. 26, 26 (Dec. 1999).

164. U.C.C. § 2-209 (proposed NCCUSL draft, Mar. 1, 1999).

165. See Smith, *supra* note 163, at 26.

166. The Reporter's Comments note that the intent of the current revision of the Code is to clarify the law and address the need for internal harmony among the provisions of the Code. U.C.C. § 2-209 (proposed NCCUSL draft, Mar. 1, 1999).

reference to the *Roth Steel* case.¹⁶⁷ This case is an example of economic coercion. It is a clear cut case that provides no guidance to courts trying to decide which party has the burden of going forward in less than clear-cut circumstances. Thus, confusion regarding modified contracts is likely to persist in the market and in the courts, and intractable problems of predicting the enforceability of modifications will continue even if the change is eventually adopted.

VI. REPRESENTATIVE CASES

A review of the cases that have arisen in the modification context demonstrates the wide variety of judicial approaches to the issue of modification. Some courts focus on free assent as the core of the modification inquiry. Others look for a justifiable reason for the modification or consider whether a change in market conditions was foreseeable. Still others focus on the availability of reasonable alternatives to the defendant or apply a waiver theory.¹⁶⁸

A. *Cases Enforcing an Agreement as Modified*

While courts often invoke a good faith standard in applying section 2-209,¹⁶⁹ they have failed to find a common thread for what constitutes good faith in this context.¹⁷⁰ In *Angel v. Murray*,¹⁷¹ the Rhode Island Supreme Court approved (the then proposed) section 89 of *Restatement (Second) of Contracts* and delineated the test for modification, requiring that circumstances “which prompted the modification were unanticipated by the parties, and the modification is fair and equitable.”¹⁷² The court noted that the rule applied to a modification made “during the course of performance of a contract;”¹⁷³ that is, before the contract modified was

167. *Roth Steel Prods. v. Sharon Steel Corp.*, 705 F.2d 134, 148 (6th Cir. 1983) (holding a contract modification ineffective due to seller's failure to establish he acted honestly).

168. *See Mott Equity Elevator v. Svihovec*, 236 N.W.2d 900, 908 (N.D. 1975).

169. *E.g.*, *Pirrone v. Monarch Wine Co.*, 497 F.2d 25, 29 n.5 (5th Cir. 1974) (referencing GA. CODE ANN. §§ 109A-1-103 and 109A-2-209, which apply good faith test); *Allapattah Servs., Inc. v. Exxon Corp.*, 61 F. Supp. 2d 1308, 1316-17 (S.D. Fla. 1999) (noting that modifications must meet test of good faith); *Palmer v. Safe Auto Sales, Inc.*, 452 N.Y.S.2d 995, 996 (Civ. Ct. 1982) (recognizing that modification must be made in good faith).

170. *E.g.*, *T & S Brass & Bronze Works v. Pic-Air, Inc.*, 790 F.2d 1098, 1105 (4th Cir. 1985) (applying a good faith requirement from a standard of “legitimate commercial reason”); *Gardino v. Caribbean Lumber Co.*, 687 F.2d 204, 209 (5th Cir. 1979) (suggesting that evidence establishing bad faith demonstrates lack of good faith); *Erie County Water Auth. v. Hen-Gar Constr. Corp.*, 473 F. Supp. 1310, 1313 (W.D.N.Y. 1979) (finding that extortion violated good faith obligation).

171. 322 A.2d 630 (R.I. 1974).

172. *Id.* at 636-37.

173. *Id.* at 636.

fully performed on either side.¹⁷⁴ In cases of executory contracts, rescission is an open possibility while some performance remains to be accomplished on each side of the deal.¹⁷⁵ If a contract is fully executed on one side, courts are likely to treat the dispute as one for settlement rather than one for modification,¹⁷⁶ or they may refuse to enforce the modification, viewing it as a “hold-up game.”¹⁷⁷

Other courts determine whether changed circumstances existed at the time of the modification and whether such circumstances justified a change in the contract. In *Agroindustrias Vezel v. H.P. Schmid, Inc.*,¹⁷⁸ the court held that the modification of a supplier of sesame seed did not amount to bad faith or a wrongful act of the type required under the economic duress doctrine. There, the supplier contracted with the defendant for the sale of seed at a price of \$28.50 per 100 pounds. Before shipping, the supplier contacted the defendant and requested that the contract be modified to increase the price to \$29.50 per 100 pounds, basing the change on the fact that floods had destroyed forty percent of the sesame seed crop. The defendant agreed to the price increase “under protest.”¹⁷⁹ After rumors that the supplier was not fulfilling other contracts, the defendant withheld part of its payment and demanded assurances of performance. The supplier refused the defendant’s demands and sued for the modified contract price. The court focused on the issue of bad faith, rejecting the defendant’s claim of bad faith and reasoning that the supplier’s “request for a less than four percent price increase in the wake of severe crop damage from natural forces was not bad faith.”¹⁸⁰

Similarly, courts focus on the concept of economic duress. In *Jamestown Farmers Elevator, Inc. v. General Mills, Inc.*,¹⁸¹ a seller of grain brought an action to recover the difference between the market price at the time of delivery and the contract price claiming it was compelled to deliver under the contract because the buyer, a large corporation, threatened to put the seller out of business and to institute criminal or regulatory proceedings. The court found the seller had failed to establish duress, stating that to establish business compulsion requires “more than

174. *See id.* (quoting proposed revision of § 89 of *Restatement (Second) of Contracts*).

175. *See id.*

176. Section 89 of *Restatement (Second) of Contracts* excludes contracts fully performed on one side from the scope of the rule on modification.

177. When a party has fully performed its promise under a contract, the other party has more leverage to make demands regarding the performance it has yet to render.

178. No. 92-15078, 1994 WL 12342 (9th Cir. Jan. 18, 1994).

179. *Id.* at *2.

180. *Id.* at *3; *see also* *Louisiana-Pacific Corp. v. United States*, 656 F.2d 650, 653 (U.S. Ct. Cl. 1981) (finding that mere economic pressure to modify a contract is not duress sufficient to invalidate a modification when plaintiff had reasonable alternatives to agreeing to the modification).

181. 552 F.2d 1285 (8th Cir. 1977); *supra* text accompanying notes 30-31.

a mere threat which might possibly result in injury.”¹⁸² The court listed three requirements necessary to establish a claim of economic duress: (1) that the party asserting duress involuntarily accepted the terms, (2) under circumstances that permitted no alternative, and (3) those circumstances were the result of wrongful coercive acts on the part of the modifying party.¹⁸³

Some courts focus on the failure of the recalcitrant party to protest the requested modification. In *United States ex rel. Crane Co. v. Progressive Enterprises, Inc.*,¹⁸⁴ the court upheld a modification which increased the price of the goods, finding that the defendant-purchaser had acted in bad faith. The parties entered a contract for the sale and purchase of a machine which the defendant intended to resell to the United States. After the defendant accepted plaintiff’s price of approximately \$5,000, the plaintiff-Seller notified the defendant that the price of the machine had risen to \$7,000. Without protest, defendant submitted a purchase order at the revised price. After delivery, defendant paid the original price and resisted demands for the increase on the basis that the changed price was ineffective. The court found the increased cost of the machine justified and held that the defendant (recalcitrant party) had acted in bad faith by failing to communicate its objection to the plaintiff.

B. Cases Refusing to Enforce a Modified Agreement

A decision that the party seeking to enforce a modification acted in bad faith provides a basis for refusing to enforce the modification. In *Roth Steel Products v. Sharon Steel Corp.*,¹⁸⁵ the court refused to enforce a modification because it found that the seller failed the test of honesty in fact. The seller sought to modify a contract to sell steel by raising its prices. Despite its finding that the seller’s ultimate loss on the contract, as modified, demonstrated that the modification was commercially reasonable, the court regarded the seller’s threat to sell no more steel to the buyer as evidence of bad faith and refused enforcement. The detail of evidence produced may have provided the lynchpin for this decision. Defendant was able to establish statements by Plaintiff indicating that it would not perform under the contract originally agreed to. While a threat of non-performance may be implicit in a modification request, making the threat of non-performance explicit is likely to give the non-initiating party

182. *Jamestown Farmers*, 552 F.2d at 1290.

183. *Id.*

184. 418 F. Supp. 662 (E.D. Va. 1976).

185. 705 F.2d 134 (6th Cir. 1983).

the right to terminate the contract and seek damages on the basis of anticipatory repudiation.¹⁸⁶

In a preliminary comment to a revision to section 2-209, NCCUSL drafters endorsed the approach taken in the *Roth* case without explanatory commentary.¹⁸⁷ This approach places a heavy burden on the defendant, and may result in enforcement in some cases despite the absence of a commercially viable reason for the modification.

Similarly, in *Austin Instrument, Inc. v. Loral Corp.*,¹⁸⁸ the New York Court of Appeals refused to enforce a modification, finding that the seller unfairly coerced the buyer to increase the price of component parts that the buyer needed for a contract with the Navy. The court focused on the inability of the buyer to obtain the goods from other dependable suppliers, holding that the seller's threat to stop delivery of materials absent a price adjustment deprived the buyer of free will. Because the buyer needed the parts to produce sophisticated military machinery for the Navy to the "strictest engineering standards,"¹⁸⁹ the court found it would be unreasonable to require the buyer to cover with parts from other dealers not on its approved list.

The absence of an objective commercial reason for demanding a modification may also provide a basis for refusal to enforce. In *T & S Brass & Bronze Works, Inc. v. Pic-Air, Inc.*,¹⁹⁰ the court refused to regard a delay in production as a legitimate commercial reason for the seller's modification that shifted air freight charges to the buyer. The court based its decision on the fact that the seller, after ordering production to begin, had twice assured the buyer that the installments would be delivered on time. The court held that the buyer's failure to object at the time the seller sought the modification did not preclude its subsequent objection because the seller had no legitimate commercial reason for modifying the contract.

In *Ralston Purina Co. v. McNabb*,¹⁹¹ the Tennessee Supreme Court refused to enforce a modification, holding that the purchaser (Ralston) knew or should have known that the defendant would not be able to complete his contract and that the modification would result in compounding plaintiff's damages. The plaintiff-purchaser alleged that defendant-seller failed to deliver 3,000 bushels due under two contracts.

186. Farnsworth notes that a demand for modification accompanied by a statement that the party seeking the modification will not perform absent assent to that modification constitutes an anticipatory repudiation. See FARNSWORTH ON CONTRACTS (3d ed. 1999). Even though the concession sought by the party demanding modification "may be a minor one, the breach that it threatens in order to extract it is not." *Id.*

187. U.C.C. § 2-209 cmt. 1 (proposed NCCUSL draft, Dec. 1, 1998).

188. 272 N.E.2d 533 (N.Y. 1971).

189. *Id.* at 537.

190. 790 F.2d 1098 (4th Cir. 1985).

191. 381 F. Supp. 181 (W.D. Tenn. 1974).

After the seller made a short delivery, the plaintiff-buyer sent letters of extension to the defendant, and defendant made eleven additional deliveries, leaving 771 bushels undelivered. Each time the plaintiff-buyer offered to extend the contract, the defendant indicated his acceptance of the extension by delivering soybeans after the date of the offer and accepting the contract price although the market price was then higher. The plaintiff demanded \$11,000 as cover damage under T.C.A. 47-2-713. The defendant asserted that damages should be calculated as of the last date set for performance. Also, the defendant contended that by urging the defendant to accept an extension, plaintiff had failed the good faith test because the extensions allowed the plaintiff to maximize damages in anticipation of a foreseeable rise in prices. Refusing to uphold the modification, the court held that the purchaser (Ralston) knew or should have known that the defendant would not be able to complete his contract. It refused recognition of Ralston's modifying agreements that would compound its damages. Based on this reasoning, the court calculated damages as of the November deadline and refused to give effect to the modified delivery dates.

C. *Critique of the Cases*

The declaration of a court that the good faith of a party requires the enforcement of a modification or that the lack of good faith of a party justifies a refusal to enforce the modification does little more than declare the winner of the controversy. This brief sampling of cases illustrates the variety of approaches employed by courts to assess modification claims and demonstrates the various facts that can capture the attention of advocates and courts in this area. The cases suggest that courts ordinarily enforce a modification if the parties agreed to modify in circumstances that establish a reason for the modification outside the control of the parties. Nevertheless, uncertainty inheres in the decisional law. In cases that do not fit neatly into the categories of coercion or a modification based on a change of circumstances, a significant risk exists that a court will enforce a modification without a showing of justifying circumstances. A party facing a demand for a modification has little guidance from the courts regarding whether his capitulation to the demand will be a basis for enforcement or not. While judicial discretion is indispensable in contract law, the nebulous nature of the modification test has resulted in inconsistent treatment. The wide range of tests¹⁹² used to assess

192. *Agroindustrias Vezel v. H.P. Schmid, Inc.*, No. 92-15078, 1994 WL 12342, at *3 (9th Cir. Jan. 18, 1994) (holding that claim of economic duress hinges on showing of a wrongful act "sufficiently coercive to cause a reasonably prudent person faced with no reasonable alternative to succumb to the perpetrator's pressure"); *T & S Brass*, 790 F.2d at 1106 (holding that failure of

modifications suggests the need for clarification, and the conclusory nature of the test encourages a non-systematic approach to modification cases.

VII. THE SEQUENTIAL APPROACH

A sequential test presents a mix of procedural¹⁹³ and substantive elements,¹⁹⁴ requiring first that the initiating party demonstrate a reasonable ground for seeking a modification, such as a change of circumstances creating a new and unallocated burden. If the initiating party successfully establishes such a reason for the modification, the court should grant enforcement unless the defendant can show that plaintiff's request was coercive. This test provides a more specific rule and may yield a better mix of stability and flexibility in modifications.

Buyer to object to modification does not preclude subsequent objection when Seller had no legitimate commercial reason for modifying); *Wisconsin Knife Works v. Nat'l Metal Crafters*, 781 F.2d 1280, 1287 (7th Cir. 1986) (requiring a showing of reliance by plaintiff to enforce the oral modification of a contract as waiver of written modification requirement and announcing a need for a showing of bad faith to defeat modification); *Jamestown Farmers Elevator v. Gen. Mills, Inc.*, 522 F.2d 1285, 1290 (8th Cir. 1977) (requiring economic duress to overcome modification and reasoning business compulsion is more than a mere threat which might result in injury at some future time); *Louisiana-Pacific Corp. v. United States*, 656 F.2d 650, 653-54 (U.S. Ct. Cl. 1981) (holding that economic pressure to modify a contract does not rise to the level of economic duress when plaintiff makes no showing of dependence upon supply or impact upon business and reasonable alternatives to the modification are available); *United States ex rel. Crane Co. v. Progressive Enter., Inc.*, 418 F. Supp. 662, 664 (E.D. Va. 1976) (holding a modification enforceable when request for the modification was justified by Seller's increased cost and that Buyer engaged in bad faith conduct when refusing to pay the adjusted price for goods received); *Business Incentives Co. v. Sony Corp.*, 397 F. Supp. 63, 69-70 (S.D.N.Y. 1975) (finding economic duress must be proven to be the result of the defendant's conduct and not that of the plaintiff's necessities); *Ralston Purina Co. v. McNabb*, 381 F. Supp. 181, 183 (W.D. Tenn. 1974) (holding modification that results in compounding injury to Seller is not in good faith and is unenforceable by purchaser who knows or should know that Seller would not be able to complete the contract); *Lumber Enters., Inc. v. Hansen*, 846 P.2d 1046, 1049 (Mont. 1993) (holding a modification reasonable where inexperienced Seller, after performing on a contract for one year, determined that the original contract price was below production costs); *Austin Instrument*, 272 N.E. at 536-37 (holding that agreement to increase price of equipment was unfairly coerced where Buyer was unable to obtain goods from other reliable source).

193. The procedural aspect of this test turns on the fact that Plaintiff bears the initial burden of showing a good faith reason for modification. If Plaintiff fails to carry this burden, the court need not inquire further and should dismiss the action based on Plaintiff's failure to establish this point. Similarly, Professor Hillman proposed that courts should entertain a presumption against modification when the capitulating party suffered a material loss from the original contract. *See Hillman, supra* note 9, at 884.

194. The substantive aspect of this test involves the court's judgment regarding the sufficiency of the plaintiff's proof to establish a reasonable ground for modification. This test necessarily involves a judgment by the court that the reasonable ground asserted is sufficient and was advanced by the plaintiff in good faith.

Generally, parties may allocate risks under the contract. For example, if the parties allocate the risk of a rise in the price of materials necessary for the production of goods to Seller, a rise in price of those materials would not provide a reasonable ground for modification. Similarly, parties can provide their own rules in the contract relating to modification—to the common sense limits of good faith. The comments provided below indicate that the sequential approach is contractible rather than mandatory. In attempting to level the playing field for the non-initiating party, the provision should avoid creating new obligations on the part of that party. For example, a provision that creates a duty on the non-initiating party to consider a request and make a judgment or respond to the request for modification should also consider the consequence of the non-initiating party's failure to act. A system that pushes the parties toward resolving their differences together rather than resorting to judicial resolution enhances efficiency. It would work an injustice, however, to insert greater uncertainty for the parties regarding the rights of a party in responding to a modification request. Similarly, a complicated provision may create unfairness by advantaging a party who is particularly savvy or who happens to be represented by savvy counsel.¹⁹⁵

A. *Proposed Text and Comments*

The following proposed text and accompanying comments are modeled on section 2-609 and the official comments to that provision.¹⁹⁶ They present a new approach to modification under section 2-209(1). This approach simply presents one way of framing a sequential test for

195. Karl Llewellyn, one of the primary drafters of Article 2, took seriously concerns about processes that favored wealthy litigants. In a statement to a joint meeting of ALI and NCCUSL on the topic of whether records should be kept of the various drafts of Article 2, Llewellyn made the following statement:

We [the Editorial Board] have been worried to the bottom of our souls by the conception of the use of the successive drafts of this Code as a guide to legislative intent. If you will remember that the Code in one form or another has been under heavy consideration for more than five years, with a prior five years of preliminary work on one of the articles, you can see that the course of successive drafts would be a course of confusion, of trouble and, as I see it, of tremendous advantage to the wealthy litigant over the non-wealthy litigant whose lawyer could not afford to spend the time or take the necessary trips to where collections of this material could be found.

THE KARL LLEWELLYN PAPERS: A GUIDE TO THE COLLECTION (R. Ellinwood & W. Twining, rev. ed. 1970).

196. The provision relating to assurances of performance is section 2-711 under NCUSL's proposed revision. It is substantially similar to the approach taken in section 2-609.

modification contests. It is not intended to supplant or affect subsequent provisions of the modification provision (section 2-209(2)-(5), or the Code's approach to the right to assurances of performance (section 2-609). Another alternative would be to merge the modification treatment into section 2-609. Like most UCC provisions, the requirements of this section may be changed by express declaration of the parties unless their changes would violate fundamental rights or abrogate the obligation of good faith. Language imported verbatim from section 2-609 and section 2-209 appears in regular font. Changes and additions to the language suggested to conform the principles to the modification context are in italics.

§ 2-209. Right to Request Modification

(1) An agreement modifying a contract within this Article needs no consideration to be binding. *However*, 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 *modification* arise with respect to the performance of either party, that party may in writing request a *modification*. Until the parties resolve the issue of *modification* (*for example, by agreeing to modify, by continuing under the original agreement, or by settlement*) either party may, if commercially reasonable, suspend any performance *when that party* has not already received the agreed return. Between merchants the reasonableness of grounds for *modification* and the adequacy of *the request* shall be determined according to commercial standards.¹⁹⁷

OFFICIAL COMMENT

Purposes:

1. The section rests on the recognition that (1) the essential purpose of a contract between commercial *entities* is actual performance; (2) the parties do not bargain merely for a promise, or for a promise plus the right to win a lawsuit; and (3) a continuing sense of reliance and security that the promised performance will be forthcoming when due is an important feature of the bargain. If either the willingness or the ability of a party to perform declines materially between the time of contracting and the time for performance, the other party is threatened with the loss of a substantial part of what he has bargained for.¹⁹⁸ *The unwillingness or inability of a*

197. Combination of text from U.C.C. §§ 2-209, 2-609 with proposed revisions added in italics.

198. The party receiving a modification request is, in the words of the comment to section 2-609, "threatened with the loss of a substantial part of what he has bargained for" by the implicit threat of non-performance. U.C.C. § 2-609 cmt. 1 (1998). Indeed, the request to modify is likely to create more profound insecurity than that presented in the assurance area since there the

party to perform has application to the context of modification. If the circumstances upon which the contract is predicated change significantly, the party affected by the changed circumstances may be justified in seeking a change in the contract terms. In such a case, the initiating party may request a modification. In contracting, parties may designate the types of changes in circumstances that justify modification. By doing so, parties allocate the risks under the contract. Additionally, nothing in this section prevents or limits a promisee from volunteering a modification to benefit promisor. An example would be a volunteered modification to share an increased cost that would otherwise fall on the promisor.

2. Measures have been adopted to meet the needs of commercial entities in such situations. First, each party is permitted to suspend his own performance and any preparation therefor, with excuse for any resulting necessary delay, until the situation has been clarified. "Suspend performance" under this section means to hold up performance pending the outcome of the request to modify and includes also the holding up of any preparatory action. Second, the parties are given the right to assess the effect of the change of circumstances on the rights and duties of each under the contract. When held within the limits of reasonableness and good faith, this procedure actually expresses no more than the fair business meaning of any commercial contract, which the parties may designate or alter by contract within the limits of good faith. The present section merges these principles¹⁹⁹ of law and commercial practice into a single theory of general application to all sales agreements looking to future performance and connects the issues of modification and those of the closely related area of demand for adequate assurance of performance. The effect of a request for adequate assurances of performance is to be determined by reference to section 2-609.

3. Subsection (2) of the section requires that "reasonable" grounds as used in subsection (1) be defined by commercial rather than legal standards. The express reference to commercial standards carries no connotation that the obligation of good faith is not equally applicable here. Rather, this provision provides guidance on what constitutes good faith in the context of modification. In this context, the good faith requirement demands that modifications should be denied enforcement absent either some change in circumstances that provides a reasonable ground for the request or a party's reasonable reliance on a promise to modify the contract. This provision substitutes the standard of "reasonable grounds" for the more general standard of "good faith," requiring a change outside

insecurity springs from some source other than the declarations of the obligor.

199. Like the comments to section 2-609, this comment refer to "measures" and, additionally, to "principles," to refer back to the measures a party may undertake in this context. U.C.C. § 2-609 cmt. 2.

*the control of the promisee to enforce a modification. The case of a price increase provides an example. A party who enters a contract to sell widgets for \$5.00 per hundred and later urges a modification of the contract price to \$6.00 per hundred for no reason other than the desire for a higher price has not sought a good faith modification. This result is different in the area of modification than in the area of original contract formation. Seller has a right to reject an offer of \$5.00 per hundred and to urge a contract price of \$6.00 per hundred for the sole reason that he wishes to obtain a higher price. The freedom to demand more is constrained, however, once the parties commit to a contract. Seller is bound to sell for the price of the original contract (\$5.00 per hundred) and he can no longer assert his desire for a higher price for its own sake. Under commercial standards and in accord with commercial practice, a ground for modification must arise from or be directly related to the contract in question. If the obstacle to performance is sufficiently significant, the obligor has a non-frivolous argument that he should be excused under the doctrines of mistake or impracticability and a request for modification is justified. A request may also be justified based on a change that does not constitute legal excuse. The fact that a court ultimately holds that the doctrine of mistake is not applicable should not resolve the modification question. For an example outside the sale of goods setting, see *Watkins & Sons v. Carrig*, 21 A.2d 591 (N.H. 1941).*

4. What constitutes reasonable grounds for modification is subject to the test of factual conditions. For example, a party's attempt to secure some new benefit or to transfer some risk to the other party by means of a modification, fails the reasonable grounds test.²⁰⁰ When plaintiff-obligee establishes a reasonable ground, the burden shifts to the obligor to show that his assent to the modification resulted from economic coercion by the obligee.

5. The rule set forth here is devised to balance the rights of the parties when one demands a modification. It would create too rigorous a test to construe reasonable grounds to require the party requesting a change to prove excuse of performance under the doctrines of impracticability, mistake or frustration.²⁰¹

200. Under the sequential approach, the plaintiff has the burden of establishing his reason for seeking a change in the contract he now seeks to enforce. Accordingly, if there is a gap in the facts on this point, the plaintiff cannot carry his burden and the suit will be dismissed. This may seem a harsh result until one realizes that the plaintiff initiated the modification, inevitably has access to information regarding the need for the modification, and stands to benefit from the modification.

201. U.C.C. § 2-209 (proposed revisions added in italics).

B. *Reasons for Modeling the Approach on Section 2-609*

Section 2-609 is particularly well-suited to serve as a model for the treatment of modification. This section has more in common with section 2-209 than meets the eye under the current arrangement of the Code. Section 2-609 deals with uncertainty about another's willingness or ability to perform. Section 2-209 deals with the flip side of the coin: uncertainty about one's own ability or willingness to perform. Additionally, in the "what goes around" world of contract law, section 2-609 and section 2-209 are intimately intertwined. When a party states a desire to modify, the other party is made insecure by the request. The request to modify may include an implicit threat that the initiating party will not perform without the modification. If such a threat is explicitly disavowed, the request for modification loses much of its force. Few people would agree to modify when the requesting party makes clear that she will go forward with performance as promised if the other refuses to modify.²⁰² Thus, it is likely that a recalcitrant party who refuses to accede to the modification will also demand assurances of performance from the initiating party pursuant to UCC § 2-609. The power of the non-initiating party under section 2-609 evens the balance of power to some extent. Moreover, use of section 2-609 may develop facts that will assist a court in determining whether a request for modification includes an explicit or implied threat of breach or generate other evidence useful to a court in determining whether the initiating party was coercive.²⁰³ Courts have held that a request for modification coupled with an explicit threat not to perform constitutes anticipatory repudiation,²⁰⁴ justifying the non-initiating party in terminating the contract

202. Applying this point to the introductory hypothetical, it is likely that Seller's request for a higher price will give rise to insecurity on the part of Purchaser (Madison County). A court may find that this insecurity justifies a demand by Purchaser of written assurances of performances.

203. See *Roth Steel Prods. v. Sharon Steel Corp.*, 705 F.2d 134, 148 (6th Cir. 1983); *Guzzello v. Venteau*, 789 F. Supp. 112, 117 (E.D.N.Y. 1992) (recognizing anticipatory repudiation based on "unlawful increase" in price and coercion).

204. Courts hold that a demand for modification coupled with the threat of breach absent acceptance of the modification constitutes anticipatory repudiation. See *WBZE, Inc. v. Arab Network of Am.*, 220 B.R. 568, 572 (D. Md. 1998) (noting that demand of performance not required by contract coupled with statement that party will not render performance unless demand is met constitutes anticipatory repudiation); *Humphrey v. Placid Oil Co.*, 142 F. Supp. 246, 254 (E.D. Tex. 1956) (holding that Defendant's statement that it would not perform contract unless Plaintiff agreed to additional terms constituted anticipatory repudiation); *Twenty-Four Collection, Inc. v. M. Weinbaum Constr. Inc.*, 427 So. 2d 1110, 1111-12 (Fla. Dist. Ct. App. 1983) (holding that demand for modification coupled with threat to walk off job was anticipatory repudiation); see also *Bill's Coal Co. v. Board of Pub. Utils. of Springfield*, 682 F.2d 883, 886 (10th Cir. 1982) (noting that bad faith urging of erroneous interpretation to hold other in a contract does not constitute anticipatory repudiation).

or urging the breaching party to retract the repudiation.²⁰⁵ In such a circumstance, the initiating party has a choice: he can provide assurances that he will perform as originally promised and proceed with performance or he may repudiate the contract (breaching by anticipatory repudiation) and defend on the doctrines of impossibility or mistake.

Section 2-609 deals with the issue of uncertainty *in media res*, providing a step-by-step roadmap for dealing with uncertainty when it arises. Despite the striking similarity of the settings of modification and assurances of performance, section 2-209 addresses uncertainty in a *post hoc* fashion, stating a test that applies only after a modification is challenged in court. The Code comments to section 2-209 and section 2-609 give no reason for providing more guidance in the assurances setting than in the modification setting.

A party to a contract has no right to demand assurances from the other party unless circumstances create a reasonable ground for insecurity regarding whether the other will perform.²⁰⁶ This right to assurance is constrained not only by the required showing that reasonable grounds for the insecurity exist, but also by the requirement of a written demand by the insecure party. Thus, the general rule (no right to assurances) is modified in limited circumstances.²⁰⁷ By contrast, section 2-209 does not insert itself into the process of modification. The current version of section 2-209 and that proposed by NCCUSL take the *post hoc* perspective of the time of trial, judging the decision after the parties have acted. Unlike section 2-609, this approach fails to give guidance to parties as they deal with the problem. Moreover, it engenders the current dichotomous approach to resolving the enforcement cases, creating uncertainty regarding whether modifications are enforceable and heightening the likelihood of demands for modifications.²⁰⁸

205. See *Gaglia v. Kirchner*, 721 A.2d 1028, 1031 (N.J. 1999) (finding that a statement by purchaser's attorney that he would not approve signed contract but would approve with modifications constituted anticipatory repudiation, justifying injured party in treating the communication as a termination or urging breaching party to retract the repudiation).

206. See UCC § 2-609; *Smyers v. Quartz Works Corp.*, 880 F. Supp. 1425, 1433-34 (D. Kan. 1995).

207. See U.C.C. § 2-609.

208. Section 2-609 also specifies the standard by which courts should judge the reasonableness of the insecure party's actions. Subsection (2) states that "[b]etween merchants the reasonableness of grounds for insecurity and the adequacy of any assurance offered shall be determined according to commercial standards." *Id.* The objective standard created by section 2-609 for judging the relative rights of the parties when post-contractual issues arise would be equally effective in the area of modification.

C. *Application of the Sequential Approach to Typical Defenses*

One way to assess the usefulness of the suggested approach is to consider how it would affect the typical defenses discussed earlier in this article.²⁰⁹ The following discussion takes up each of the defenses explored above, considering how the sequential approach would be dealt with in each setting.²¹⁰

1. Credibility Issues

In the first category, the defendant denies that the parties agreed to a modification. Although a credibility dispute can arise under any test, a statutory provision (like section 2-609) requiring that the initiating party make its request in writing provides some evidence of the modification sought. Under the sequential approach, it is likely that a plaintiff will identify and preserve evidence of the ground asserted by setting forth the basis for the change in the written modification request required by the statute.²¹¹ A recalcitrant may, despite the documentation, argue that the parties did not reach final agreement on the modification sought by Plaintiff. It cannot argue effectively, however, that no modification was sought by Plaintiff. Because evidence is available to prove that the claim rests on a real transaction between the parties, a recalcitrant's ability to argue that Plaintiff is manufacturing the claim out of whole cloth is limited.

2. The Defense of No Reasonable Ground

The second category of defenses is presented when defendant claims that plaintiff lacked good faith (or a reasonable ground) to seek the modification. The sequential test judges this claim head-on by requiring the plaintiff to establish proof of the change of circumstances that gave rise to its request for modification. In a context as specific as modification, the conduct required to comport with the good faith standard is identifiable.²¹² Rather than employing the generalized and amorphous test of good faith, the sequential approach achieves greater precision by stating the standard for good faith in this particular context, i.e., a written request based on a reasonable ground for the modification.

209. *See supra* Part II. D.

210. *See supra* Part II. D.

211. Hawkland suggests that a writing should be required for modifications. *See* HAWKLAND, *supra* note 132.

212. *See supra* Part III.

3. The Defense of Coercion

The third category of defenses is presented when defendant claims that Plaintiff coerced Defendant's assent to the modification sought. The sequential approach gives needed context to this inquiry as well. It places the burden on Defendant to show coercive conduct on the part of Plaintiff. The sequential approach focuses the inquiry of the court by specifying the burden for each party and establishing the initial need of the modifying party to establish the reasonable grounds for the modification.

D. Application of the Sequential Approach to Representative Hypotheticals

Applying the sequential analysis to the introductory hypothetical and other hypotheticals clarifies the effect of the sequential test and allows easy comparison of the test with the current scheme under section 2-209. While other circumstances of modifications may occur, the four situations set forth below address typical concerns in this area of law.

1. The Steel Perfect Hypothetical

If the request for a modification made by Steel Perfect (Seller) was based on an unforeseen and unallocated increase in the market price of iron that gave rise to a good faith belief in Seller that it had a basis for refusing to perform, Seller's circumstances seem to present a reasonable ground for seeking modification. If, on the other hand, no price increase had actually occurred or Steel Perfect accepted the risk of the price increase at the time of contracting, Steel Perfect lacked a reasonable ground for seeking the modification.

If Madison County (Buyer) rejected Seller's request and Seller then refused to perform, a court will not force the modification on the parties, even if Seller had a reasonable ground for requesting the change. If Buyer rejects the modification and Seller does not perform, Buyer may seek damages for the Seller's breach by nonperformance. If the court finds that Seller had reasonable grounds for a modification that constituted legal excuse under the doctrines of mistake or impossibility, a court will excuse Seller's performance. Thus, the initiating party who seeks a modification based on a reasonable ground (such as mistake or impossibility) has protection against the recalcitrant party's refusal to modify. Refusing to perform is, nevertheless, a second best choice because the initiating party prefers to continue with the contract in a modified form. If a court finds that Seller's request, though reasonable, did not amount to legal excuse by mistake or impossibility, it should grant Buyer (injured party) damages for Seller's refusal to perform.

2. A Hypothetical Based on Reliance on a Promise of Enhanced Performance

As in the area of enforcement of original contracts, a plaintiff's reliance on a gratuitous promise may provide a basis for enforcement of a modification.²¹³ *Restatement* section 90 and many jurisdictions extend protection to promisees who rely on a promise that meets the requirements of this section without regard to whether the promise arises as part of a new transaction or as part of a modification. Reasonable reliance may arise from circumstances in which a party relies on promises of his contracting partner to give some additional benefits not encompassed within the original bargain. For example, if Seller agreed to modify a contract by promising to provide seasonal packaging for goods (such as a red, holiday bow), Seller should be held to the promise if Buyer relied, for example by purchasing the packaging materials—even though the modifying promise was gratuitous. Applying this principle to the introductory hypothetical, if Seller relies on Buyer's promise to pay the higher price by continuing to manufacture the goods and ultimately delivering the goods to Buyer, a court may enforce the Buyer's promise to pay the higher price if it finds this reliance was reasonable. It is unlikely, however, that a court would find a party's reliance reasonable if that party coerced the modification or used the modification to gain a benefit or to transfer a burden to the other party.

3. A Hypothetical Based on Reliance on a Promise Reducing a Performance Burden

Reasonable reliance may also arise from circumstances in which a party relies on promises of his contracting partner to lessen a burden or forgive an element of performance. For example, Seller may have timing problems that would require overtime or other expenses to deliver goods on time. Suppose that Seller called Buyer, explained that the promised delivery would increase his costs dramatically, and Buyer gave assurances that delivery on the following Monday would be acceptable. In the event of a price decline during the interim, Buyer might claim that Seller repudiated the contract by not delivering on time. If Buyer makes a substitute purchase and claims repudiation, the court should scrutinize Seller's reliance on the promise, holding Buyer to the extension of the delivery time. Although the difficulty relating to Seller's performance (i.e., the expense of overtime workers) might not justify excuse of performance based on impossibility or mistake, Seller's reliance on the modification should provide a basis for

213. RESTATEMENT (SECOND) OF CONTRACTS § 90 (1981). The protection of this section provides a basis for enforcement for promises that are original or modifications.

enforcement without requiring a reasonable ground for modifying. Arguably, Seller's reliance in such a case is reasonable because the accommodation was treated by the parties as negligible and not of sufficient importance to disturb the allocation of benefits of the original contract.

4. A Hypothetical Based on Bad Faith of the Capitulating Party

Although good faith of the capitulating party is not an element to be established to enforce a modification, clear bad faith on the part of the capitulating party may be taken into account in comparing the conduct of the two parties. The capitulating party may be acting in bad faith even when the initiating party lacked a reason for modification. For example, at the time of a modification, the capitulating party may intend to refuse to perform the contract as modified. In such a case, the initiating party may have an action against the non-initiating party based on promissory fraud.²¹⁴

Assume the defendant agreed to the modification only to insure that plaintiff would perform, never intending to live up to the change. Each party alleges the other acted wrongfully: (1) Defendant alleges that the Plaintiff sought an unjustified modification and (2) Plaintiff alleges that Defendant's assent was a misrepresentation of his intentions. This situation calls for a court to compare the conduct of the two parties. If the modification resulted in the parties sharing a burden created by an unforeseen and unallocated obstacle rather than simply improving the deal for the initiating party, the reliance of the plaintiff on the modified contract seems reasonable. In other words, the initiating party's reliance on the promise of the capitulating party is reasonable when the net effect is for the parties to share an unforeseen and unallocated burden. Conversely, it is unlikely that the initiating party's reliance is reasonable if the modification shifts a burden originally allocated to the initiating party or shifts a benefit allocated to the non-initiating party.

214. See *Tejani v. Allied Princess Bay Co.*, 204 A.2d 618, 620 (N.Y. App. Div. 1994) (recognizing an action based on modifying agreement with intent to defraud); *Fraught v. Norvell*, 258 P.2d 642, 644 (Okla. 1953) (rejecting Plaintiff's claim of promissory fraud based on failure to show that, at the time of contracting, defendant intended not to perform); *Tran v. Tehrani*, 781 P.2d 393, 394 (Or. Ct. App. 1989) (requiring, as element of fraud, intent not to perform at time of contract modification). Similarly, the initiating party may be guilty of promissory fraud if at the time she entered the original contract, she intended to seek a modification.

E. *Comparison of the Sequential Approach and the Current Approach*

In applying a sequential standard to judge a modification, courts still face the question of fairness, but, under this standard, the inquiry has more specificity and substance. It is informed by the standards for such obstacles and burdens developed in the area of excuse of performance.²¹⁵ Some courts would undoubtedly engage in the sequential analysis described here as a matter of common sense. Even so, adoption of a sequential approach and its methodical assessment of the rights of each party may facilitate modification cases. Focusing initially on the reason the initiating party sought a modification encourages the party contemplating a modification to restrict his choices to situations in which he had reasonable grounds to modify—or at least a good faith belief in his grounds. If the party lacks confidence in its ability to convince a court that it should be entitled to modify, it is likely to go forward with performance as agreed rather than seeking a modification. The sequential approach is an improvement over the current regime of a generalized good faith inquiry because its more specific and reliable test discourages parties from seeking to modify contract obligations without a demonstrable change in circumstances. Although the reasonable grounds test provides a larger scope than that of legal excuse, this larger scope is justified because it allows the party assessing the offer to determine whether going forward with performance as modified prevents an inefficient breach. In other words, although the initiating party ultimately fails to establish legal excuse, the modification should be deemed enforceable if the initiating party held a non-frivolous belief that the change in circumstances presented a basis for a refusal to perform. Like the law of settlement, the offeror's good faith belief in the offer is requisite to judicial enforcement.

VIII. CONCLUSION

A clash of competing principles or paradigms is not an unusual phenomenon in the law.²¹⁶ The conflicting principles at work in the

215. Modification can be seen as an appropriate self-help remedy in which the parties employ the reasoning of the areas of mistake and impossibility and construct a new contract. See Christine Jolls, *Contracts as Bilateral Commitments: A New Perspective on Contract Modification*, 26 J. LEGAL STUD. 203, 224-27 (1987) (arguing that modification represents an inappropriate self-help remedy circumventing damages rules). But see Subha Barasimhan, *Modification: The Self-Help Specific Performance Remedy*, 97 YALE L.J. 61, 77-94 (1987) (examining modification as a self-help remedy and arguing that modification must be integrated within the system of legal remedies for contract breach).

216. Paradigms pervade the law, as well as scientific reasoning, providing an ordering mechanism. In his study of the scientific method, *THE STRUCTURE OF SCIENTIFIC REVOLUTIONS* (2d ed. 1970), Thomas Kuhn explores the use of the paradigm in science, comparing it to tests or

modification area reflect strong and recurring themes in contract enforcement. The laissez-faire provision of private ordering predominant in American contract law underlies the idea that courts should enforce modifications absent coercion. On the other hand, the evaluation of the fairness of a modification is also consistent with private ordering. A requirement that Plaintiff make an affirmative showing of fairness (i.e., that he had a reasonable ground for seeking a modification) preserves the original expectations of the parties and prevents the destabilizing influence of unpoliced modifications. Thus, the sequential test allocates the burden of proof initially to the plaintiff and shifts the burden to the defendant only when the plaintiff establishes that it had a reasonable ground for seeking the modification.

Law that is difficult to apply is difficult to predict and is also likely to result in indeterminacy and dissonance in both the courts and the marketplace. The current approach to the modification area leads to a range of tests and comparisons of the conduct of the parties. A sequential approach, by contrast, proceeds methodically to consider each step of the modification process in order. First, it supplants the vague good faith standard with the standard of reasonable grounds, fastening the court's attention on the situation of the initiating party and requiring that party to establish its need to modify. Second, it requires the creation of a writing by the initiating party, providing some evidence of the conduct of the parties. In this context, the nature of the test *in media res* helps inform the judgment of parties regarding how the conduct of each will be judged by a court after the fact. Third, the test turns to the capitulating party, allowing that party to defend on the ground of coercion when the circumstances compelling the defendant to act are traceable to the plaintiff. Thus, the sequential approach provides guidance for the decision-making by parties as well by courts.

In its current state of development, the good faith standard of section 2-209 seems to operate merely as a label for the outcome chosen by a court. Like many areas which require good faith, the modification area presents a need for balancing the interests of the parties and calls for sensitive application by judges. While application of any test must depend on the practical wisdom of judges, the analysis of good faith can be made more predictable and straight-forward in a particularized context such as

models set forth in judicial decisions. The use of paradigms in judicial reasoning has been noted by many scholars. *E.g.*, Juan F. Perea, *The Black/White Binary Paradigm of Race: The Normal Science of American Racial Thought*, 85 CAL. L. REV. 1213, 1216-19 (1998). The benefit of models carries with it a detriment, however. The narrow focus of a paradigm carries the risk of oversimplification. In fact, the bounded nature of paradigms may be part of the reason the law often raises up twin or competing paradigms, allowing courts to choose the competing reality that it believes most appropriately applies to the circumstances in a given case.

modification. A test that expressly requires a showing of a reasonable ground for modification focuses on the minimum of good faith in this context. The sequential approach also sharpens the test, minimizes the importance of advocacy, and makes clear to a party pressing for a modification that it bears a risk. Like the decisions to terminate or to demand assurances, the determination to seek a modification should not be undertaken lightly, particularly if the modification sought significantly changes the baseline of the contract. A party who seeks a modification in such circumstances—like the party who demands assurances of performance or terminates a contract—should bear the initial burden of convincing the court that it acted on reasonable grounds.²¹⁷ In cases where a modification benefits one party and creates a detriment for the other, the sequential approach provides a more dependable test than the current good faith standard of the Code. Such an approach is in harmony with the Code's consistent theme of commercial reasonableness and gives appropriate consideration to the dual needs of certainty and flexibility in this area of law.

217. *See Walker & Co. v. Harrison*, 81 N.W.2d 352, 355 (Mich. 1957) (noting that the determination by one party to repudiate a contract is "fraught with peril" because the court in the claim of its contemplation may not agree that the other had breached first).