

The Goals of Contract Remedies

Mark P. Gergen*

This article offers a general account of the rules that regulate exit and loyalty in contract disputes to make some fundamental points about the goals of contract remedies.¹ The dominant goal of these rules, like all of contract remedies, is vindicating contracting rights.² When contract rights give way it is almost always for one of two reasons. Rights sometimes give way to advance the goal of efficient performance. This goal is familiarly expressed by the mitigation principle and, in American contract law, by the theory of efficient breach. Rights also give way to advance the goal of remedial simplicity. In a nutshell, the rules that regulate exit and loyalty in contract disputes, like all of contract remedies, vindicate contract rights at the least cost and with the least fuss. This should be utterly unsurprising.

More interesting are the trade offs made when these goals conflict. A contract right's certainty is of crucial significance. I define a contract right as certain when the right to a performance from another is indisputable. There is an important distinction between the right to a performance and the worth of that performance to the right-holder. Often the right a performance is certain while its worth to the right-holder is uncertain. When a contract right is certain or indisputable contract law permits a right-holder to take a self-help measure, such as exiting from a contract, to avoid suffering an uncompensated

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¹ By exit I mean when a person suspends or withholds performance, refuses performance, or obtains substitute performance due to his dissatisfaction with the other's performance or demands. Exit is an important self-help remedy for breach of contract. By loyalty I mean when a person performs, accepts performance, or awaits performance despite his dissatisfaction with the other's performance or demands. Exit and loyalty are regulated by rules that dictate when a person has the power to exit (e.g., material breach and conditions), by rules that dictate when delaying exit will cause a person to lose the power to do so or other rights (e.g., waiver, estoppel, and election of remedies), by rules that dictate that when a person who performs a disputed obligation may recover the value of his performance if it was not due (e.g., the voluntary payment doctrine and a restitution claim on breach), and by rules that dictate when it is appropriate to threaten exit to get a more favorable resolution of a dispute (e.g., accord and satisfaction and duress).

² Usually when we talk about vindicating contract rights we speak of the rights of the non-defaulting party. The stated goal, familiarly expressed by the expectation principle, is to give the non-defaulting party the benefit of his bargain or to put him in the promised position. As you shall see, contract law also is concerned, though not equally concerned, with vindicating the rights and the bargain of the defaulter.

loss even though the measure inflicts a disproportionate loss on the defaulter. In other words, the goal of vindicating rights trumps the goal of efficient performance when it comes to self-help remedies that do not unduly tax courts. More bluntly, the theory of efficient breach is bunk as a descriptive matter when it comes to the rules that regulate self-help responses to an indisputable default.³

The goal of efficient performance drives other aspects of contract remedies. Trivially, the mitigation doctrine and other rules compel a party to vindicate a right in the cheapest way possible.⁴ More interestingly, the goal of efficient performance explains the law's response to loyalty in the face of contract uncertainty. By this I mean when a party performs a disputed obligation or accepts performance of disputed adequacy. I show that performance of a disputed obligation (or acceptance of performance of disputed adequacy) does not preclude the later assertion of a claim of a lesser obligation (or of a greater right), but only if performance (or acceptance of performance) avoids a loss.⁵ This point, which I believe is novel but seems obvious once you think about it, systematizes what now is a very tangled thicket of law.

There is scant authority on the related question whether contract uncertainty warrants withholding or refusing performance. I think this is because courts have not had to confront the question directly. It tended not to arise under traditional common law rules, which made contract rights and obligations certain or unenforceable.⁶ This is changing. I highlight a fascinating decision by Judge Posner that confronts the question and answers that contract uncertainty does warrant exit, indeed his reasoning suggests uncertainty may require exit.⁷ Judge Posner is on to something important. However, putting the issue in a broader frame shows that the power to exit from an uncertain contract is cosseted by other rules that discourage exit when it would result in a consequential loss.

Before I proceed I want to say a few words about the nature of my argument. I am making abstract doctrinal arguments, or, if you will, conceptual arguments.⁸ I am

³ Daniel Friedmann, *The Efficient Breach Fallacy*, 18 J. Legal Stud. 1, 18-23 (1989), argues that the theory of efficient breach is descriptively inaccurate in other respects.

⁴ See Part 3.

⁵ See Part 4.

⁶ Thus Grant Gilmore's wry comment that traditional contract law "seems to have been dedicated to the proposition that, ideally, no one should be liable to anyone for anything." *The Death of Contract* 15 (1974)(1995 ed.).

⁷ *C.L. Maddox, Inc. v. Coalfield Services*, 51 F.3d 76 (7th Cir. 1995).

⁸ A conceptual argument is an odd duck. It does not reproduce the stated or actual reasons for a decision. A highly abstract conceptual argument is not really an argument *of* law if by that we mean an argument that a lawyer would make to a judge, or a judge would make to a litigant, to persuade him of the legal correctness of a decision. But neither is a conceptual argument normative in the sense that it justifies

not making a moral or policy argument regarding what the law ought to be. My argument that the theory of efficient breach misdescribes the law should not be taken as a claim about the irrelevance of a utilitarian or welfarist ethic to contract law. I mean to make no such claim. There are good utilitarian arguments for enforcing indisputable rights to the hilt through self-help (low cost) remedies even though this may seem wasteful in the short run.⁹ I define the goal as efficient performance and not as efficiency to indicate I am not making a larger claim about efficiency. I believe the best normative account of private law is pluralistic in value, but I do not believe any of my arguments here depend on accepting this premise.

The payoff of conceptual analysis is that it helps us to organize and understand the law.¹⁰ A narrower article spun off from this project already has had a concrete payoff in the form of a novel rule I propose that is taken up by the Restatement Third of Restitution and Unjust Enrichment. The rule allows a party who performs a disputed

a decision by reference to some ultimate value or goal such as promoting human welfare. The abstraction of a conceptual argument invites charges of naiveté or reductionism for the law is far messier and more complicated. Its non-normativity invites charges of timidity and triviality. Most damning is the charge of dishonesty in making an argument that some are likely to misunderstand to be an argument of law with normative heft.

⁹ Robert Scott, *The Case for Formalism in Relational Contract*, 94 *Nw. U. L. Rev.* 847 (2000), draws together recent theoretical, empirical, and historical scholarship to justify a formalist turn in contract law. His theoretical argument is that courts are unlikely to do better than sophisticated actors in designing terms when relevant information is unknown or the design of terms involves difficult tradeoffs. *Id.* at 862-866. His empirical argument is that the world is complex – in Scott’s words, it is “a thick environment of many heterogeneous parties.” *Id.* at 865-866. These points lead ineluctably to the conclusion that efficient terms are likely to be individualized, meaning that they cannot be set by courts on a wholesale basis. His historical argument, Scott calls it the failure of Karl Llewellyn’s project, is that courts have not derived individualized rules from trade norms, which might have been a solution to the problem of competence and heterogeneity. *Id.* at 866-869.

The upshot is that Scott touts the old-time virtues of remedial simplicity. He advocates literal interpretation of contracts without regard to context, *id.* at 866, presumably meaning a return to the plain-meaning and four-corners rules and, perhaps, a return to the rule barring enforcement of indefinite terms. See *id.* at 860 and 877 (suggesting some indecision on the last point). He nods sympathetically to the “doctrines of perfect tender, mistake, and excuse [and] the sharply defined rules regarding expectation damages” that “assign risks on an all-or-nothing, binary basis.” *Id.* at 852-853. These are fairly modest changes in the law, but the logic of Scott’s position has radical implications. Any element of contract law that endows a court with adjudicative discretion should go. Terms liquidating damages or limiting remedies should be enforced as a matter of course, the duty of good faith should be abolished, doctrines mitigating conditions should be junked, and with them should go most of the law regarding mistake, impracticability, and frustration of purpose. Heady stuff this and potentially very influential. Pro-business courts in California and Texas have embraced rule formalism in contract law, often in response to excesses of their more populist predecessors. Academic work like Scott’s legitimates this formalist turn. Much argument about this from both the left and right loses sight of the possibility within the traditional common law to achieve a modest sort of justice or fairness in individual cases.

¹⁰ Benjamin Zipursky, *Pragmatic Conceptualism*, 6 *Legal Theory* 457 (2000), has a spirited and thoughtful defense of conceptualism.

obligation to recover the value of his performance if the performance avoids a loss.¹¹ This article situates that rule within a broader frame. The broader frame illuminates the nature of contract rights and how (and perhaps why) contract rights differ from property rights. It also reminds us of the importance of remedial simplicity in contract law.

1. The duty to mitigate and the relative importance of vindicating rights, efficient performance, and remedial simplicity

My old Contracts casebook,¹² like many others, uses *Rockingham County v. Luten Bridge Co.*,¹³ and *Parker v. Twentieth Century-Fox Film Corp.*,¹⁴ to introduce the mitigation doctrine. Their familiarity makes these cases good vehicles for illustrating the interplay between the goals of vindicating rights, efficient performance, and remedial simplicity in contract remedies. What they teach is that a party may act in response to default to protect herself from suffering an uncompensated loss even though her action inflicts a disproportionate loss on the defaulter.

Shirley MacLaine Parker had a contract with Twentieth-Century Fox to play the female lead in *Bloomer Girl*, a musical about gender and racial conflict in the antebellum south with a precociously progressive female lead. The studio cancelled plans for *Bloomer Girl* and offered MacLaine as a substitute the female lead in “*Big Country, Big Man*,” a dramatic western, with the same guaranteed compensation, \$750,000 for fourteen weeks work. MacLaine turned down the second part and sued for the guaranteed compensation. In its defense, the studio argued that MacLaine failed to mitigate damages by not taking the second role. The trial court rejected this defense on a motion for summary judgment. The fighting issue in the case was whether the question of the comparability of the roles (framed as whether the second role was “different and

¹¹ Restatement Third of Restitution and Unjust Enrichment, Council Draft No. 5, § 35 (Nov. 24, 2003). The Reporter’s Note generously credits my Restitution as a Bridge Over Troubled Contractual Waters, 71 Fordham L. Rev. 79 (2002), as having suggested the rule. That article is an extended argument for one point made in this article.

¹² Dawson, Harvey & Henderson, Contracts (7th ed. 1998).

¹³ 35 F.2d 301 (4th Cir. 1929).

¹⁴ 3 Cal.3d 176, 86 Cal. Rptr. 737, 474 P.2d 689 (1970). As often happens to cases in the canon, *Parker* has been used by others to make a variety of points. See Victor Goldberg, *Bloomer Girl Revisited Or How to Frame an Unmade Picture*, 1998 Wisc. L. Rev. 1051 (explaining that the decision should have been rested on the ground that base price in the contract was paid by the studio to have an option on Parker’s time); William J. Woodward, Jr., *Clearing the Brush for Real-Life Contracting*, 24 Law & Social Inquiry 99, 105 (1999)(explaining that the case is a good vehicle for exploring the difference between book law and real life); Mary Joe Frug, *Re-reading Contracts: A Feminist Analysis of a Contracts Casebook*, 34 Am. U. L. Rev. 1065, 1114-25 (1985) (discussing feminist issues raised by the case).

inferior” to the first) should have gone to the jury. The California Supreme Court said no affirming the trial court.¹⁵

The goals of vindicating rights, efficient performance, and remedial simplicity clash in *Parker*. The goal of efficient performance was sacrificed for the others. MacLaine did no work for fourteen weeks at a time when she “was one of the biggest female stars in Hollywood.”¹⁶ The goal of vindicating rights is roughly served. Awarding MacLaine the fee did more than vindicate her rights for she may well have gotten a windfall at the studio’s expense. She got fourteen weeks of pay while she took what may have been a much-needed break. It was a particularly busy time in her career. This outcome was tolerated in the interest in remedial simplicity.¹⁷ There is good reason to believe that MacLaine genuinely preferred the role in “Bloomer Girl” to the role in “Big Country, Big Man.” To protect MacLaine’s from suffering a loss from doing the less desired role while encouraging efficient performance the law might have required her to take the role in the Western while giving her damages for her loss. This the law does not do. Indeed, had MacLaine taken the second role she would have been denied damages for her artistic, political, or reputational loss because it would be too speculative. The only way MacLaine could avoid suffering an uncompensated loss was to do what she did, which is to reject the role in “Big Country, Big Man” and collect the contract price. Remedial simplicity is the self-evident reason for preferring this outcome though it probably is wasteful in the short-run and may give MacLaine a windfall at the studio’s expense.

An important lesson of *Parker* is that a person may refuse substitute, nonconforming performance to avoid suffering an uncompensated loss though her refusal inflicts a disproportionate loss on the defaulter. *Parker* shows that the trope of a contract as a partnership is misleading. Partners are expected to set aside their individual interests for the interests of their firm. The duty to mitigate did not require MacLaine to set aside her reasons for preferring the role in Bloomer Girl for the greater good of the Twentieth-Century Fox/MacLaine partnership. A larger lesson is that the theory of efficient breach is bunk even as a description of the law on the books. The theory comes from focusing

¹⁵ *Parker* is representative of the case law. A survey of recent contract and Title VII cases concludes that courts require that two positions be “virtually identical” before they will require a terminated employee to take another position to mitigate damages. Richard J. Gonzales, *Satisfying the Duty to Mitigate in Employment Cases: A Survey and a Guide*, 69 *Miss. L.J.* 749, 760-762 (1999). The author adds that courts have been more willing to require an employee to relocate when his line of work and past behavior indicated he was not averse to relocating. In Title VII cases (but not breach of contract claims), an employee may be denied full back wages for an extended period of time on the theory that he should have less desirable and lower paying work to mitigate damages.

¹⁶ Goldberg, 1998 *Wis. L. Rev.* at 1052. I take the facts not found in the opinion from Goldberg’s excellent article. Goldberg argues that there was an alternative basis for decision because the contract had a “play or pay” provision that required the studio to pay MacClaine if it cancelled the project. Goldberg argues this was an easier basis. I think it was an easy mitigation case as well.

¹⁷ The fighting issue in the case – whether the question of comparability of the roles should have gone to the jury – is also over remedial simplicity.

exclusively on how the expectation damage remedy works in principle. The expectation damage remedy may facilitate efficient breach in principle (even this is not true as the law often gives damages that we know over- or under-compensate the aggrieved party's in the interest of remedial simplicity¹⁸), but other rules that regulate an aggrieved party's response to breach, such as the duty to mitigate, tolerate wasteful behavior in order to vindicate rights.

*Rockingham County v. Luten Bridge Co.*¹⁹ is the textbook counter-example. Luten Bridge Co. had just begun work on a bridge for Rockingham County when a rump group of Rockingham County commissioners voted to relocate the road and to cancel the bridge contract. Other commissioners who claimed to speak for the county told Luten Bridge to work on, which it did finishing the bridge. The fighting issue in the case (which is edited down in the casebook) is who spoke for the County. The court held that the rump group did. The opinion goes on to hold that Luten Bridge could recover as damages only its costs up to the time of the cancellation plus its lost profits though it spent much more to finish the bridge. This seems a straight-forward application of the mitigation doctrine. Even an inattentive student can see that Luten Bridge ought to stop because it is wasteful to build a bridge in the middle of nowhere.

If we set aside the conflicting orders,²⁰ then *Luten Bridge* illustrates that the goal of vindicating rights can give way to the goal of efficient performance. We can imagine that requiring a contractor to stop work may leave him with an uncompensated loss if he cannot prove his lost profits to the required degree of certainty. The treatment of *Luten Bridge* in the casebooks and teaching manuals suggests most teachers do not appreciate how exceptional the case is in requiring even this small sacrifice by a right-holder.²¹

¹⁸ A familiar example is when breach causes a defect in an object of intangible or unique value. The only damage options are the cost of repairing the defect or the loss in the market value of the object even if we are sure that one over-compensates and the other under-compensates.

¹⁹ 35 F.2d 301 (4th Cir. 1929). English law is even more protective of the contractor giving him a right to complete performance and recover the contract price unless, perhaps, he has no legitimate interest in performing the contract. *White & Carter (Councils) Ltd. v. McGregor*, [1962] AC 413 (defendants cancelled contract to have plaintiff place advertisements on its litterbins on the day contract was made, plaintiffs went ahead and placed the advertisements for the three-year period of the contract and recovered the contract price). Andrew Burrows, *Remedies for Torts and Breach of Contract* 317-322 (2nd ed. 1994), surveys the inroads on the case. Continued performance is not be allowed if it requires the cooperation of the other or if continuing is "wholly unreasonable" (which is distinguished from being "merely unreasonable") meaning that continuing ran up damages and great deal and was unnecessary to protect the plaintiff's interests under the contract.

²⁰ On this point the case is usefully compared with *Modern Machinery v. Flathead County*, 202 Mont. 140, 656 P.2d 206 (1982). The plaintiff completed manufacturer of a large rock crusher ordered by the county despite attempts by a county official to repudiate the contract. The decision holds that the repudiation was ineffective because it did not go through official channels.

²¹ For example, Farnsworth, Young, and Sanger *Contracts* 494 (6th ed. 2001), present it as unexceptional "that the injured party cannot recover for cost that could have been avoided by simply

There are only a handful of cases like *Luten Bridge* in which a person hired to do work that is uniquely of value to another continues to do work after the other says stop and then sues for the contract price.²² Even in this unusual situation the right-holder will recover the contract price if he must continue work to avoid an uncompensated loss.²³ Indeed, a party may continue work to avoid an uncompensated loss to himself even if this imposes a disproportionate loss on the other. As in *Parker*, courts do not try to balance interests except in the grossest sense.

*Bomberger v. McKelvey*²⁴ illustrates. McKelvey bought a lot from Bomberger and agreed to pay Bomberger \$3,500 to demolish a building on the lot. McKelvey planned to build a large drug store on several lots. McKelvey decided to delay construction of the store and ordered Bomberger not to proceed with demolition. Bomberger demolished the building anyway claiming that he needed skylights salvaged from the building, which were worth around \$540, to fulfill another construction contract. The demolished building was worth around \$26,000 and was generating \$300 monthly rent. The case holds that Bomberger acted reasonably because getting substitute skylights may have delayed completion of his other project by several months. The court made no effort to quantify or to balance the parties' respective losses.

The power to act to protect a contract right is not absolute. English judges, who start from the premise that there is a general right to perform and collect the contract price in the face of a repudiation, have struggled to define when this right gives way. One judge summed it up this way: "How one defines that point is obviously a matter of some difficulty, for it involves drawing a line between conduct which is merely unreasonable and conduct which is *wholly* unreasonable."²⁵ This seems to me an apt description of the balance the courts struck in *Parker v. Twentieth Century Fox* and *Bomberger v. McKelvey*. In countenancing "merely unreasonable" behavior the English

stopping performance" and poses as the difficult case where avoiding loss requires "taking *affirmative steps*"

²² The classic case is *Clark v. Marsiglia*, 1 Denio (N.Y.) 317, 43 Am. Dec. 670 (1845)(holding that a painter who completed painting after stop order could not recover contract price). Corbin cites four other cases. Corbin on Contracts § 1039 n. 18.

²³ *O'Hare v. Peacock Dairies, Inc.*, 26 Cal. App.2d 345, 79 P.2d 433 (1938)(holding that farmer could continue to produce and deliver milk to defendant under long-term contract because he ought not be obliged to sell his herd to stop production); *Southern Cotton-Oil Co. v. Heflin*, 99 Fed. 339 (1900)(holding that manufacturer of cotton seed who contracted to sell manufacturing by-products to defendant could continue production after stop order and recover difference between contract price and market price); *Northern Helix Co. v. United States*, 19 Ct.Cl. 118, 455 F.2d 546 (1972), 207 Ct.Cl. 862, 524 F.2d 707 (1975), cert denied 429 U.S. 866 (1976)(holding that manufacturer could continue to produce and deliver helium under long-term contract where production was inter-related with other operations, manufacturer had no storage facilities, and there were no other buyers).

²⁴ 35 Cal.2d 607, 220 P.2d 729 (1950).

²⁵ *Clea Shipping Corp. v. Bulk Oil International Ltd.*, Queen's Bench [1984] 1 All E.R. 129.

judge is saying that an aggrieved party may act to avoid an uncompensated loss though his action imposes a significantly larger loss on the defaulter.

2. The power to exit to vindicate an indisputable right

In American law, the doctrine of material breach and the cognate doctrines of total breach and substantial performance dictate when a party has the power to withhold or refuse performance in response to default in the absence of an express condition.²⁶ The mitigation doctrine performs a similar function when called upon, as it was in *Parker*, to fault a person for not accepting an offer of substitute performance from a

²⁶. A finding of material or total breach triggers several possible legal responses. They include the power to suspend performance, the power to abandon a contract and find substitute, and the power to recover in Restitution to reverse a bad bargain or perhaps even to compel the defaulting party to disgorge his profits from breach. The Second Restatement of Contract distinguishes between material and total breach on the basis of whether the harm from the breach is curable. Under the Restatement, a material breach that is curable justifies suspending performance. See Restatement, Second, of Contracts § 242, comment a. A total breach – meaning an incurable material breach -- discharges the non-defaulting party, justifying his withdrawal from the contract. Restatement, Second, of Contracts §§ 236, 243(1), (2). It also seems to justify the optional Restitution remedy. Restatement, Second, of Contracts § 373.

It is a mistake to emphasize the possibility of cure in defining when a breach justifies withdrawal from a contract because that derogates from other equally important considerations, such as whether damages are likely to be an adequate remedy if the non-defaulting party accepts performance or continues to perform. I suspect that cure was emphasized in the Restatement to solidify its relevance under the common law. That a party ought to give notice and an opportunity to cure before withdrawing from a contract is well-established in the common law. See, e.g., *Pollard v. Saxe & Yolles Dev. Co.*, 12 Cal.3d 374, 525 P.2d 88, 92, 115 Cal.Rptr. 648, 652 (1974); *Sturdy Concrete Corp. v. Nab Constr. Corp.*, 65 A.D.2d 262, 411 N.Y.S.2d 637, 644 (1978); *United States ex rel. Cortolano & Barone, Inc. v. Morano Constr. Corp.*, 724 F.Supp. 88, 98 (S.D.N.Y.1989); *Cyclo Floor Machine Corp. v. National Housewares, Inc.*, 296 F.Supp. 665, 682 (D.Utah 1968); *McClain v. Kimbrough Construction Company*, 806 S.W.2d 194 (Tenn. App.1990).

The concept of substantial performance is associated with a claim by a party who fails to perform in minor respects to be paid for work done. In most states a party who substantially performs has a right to recover the contract price less damages caused by his breach (the contract remedy), otherwise he recovers in restitution. *Reynolds v. Armstead*, 166 Colo. 372, 443 P.2d 990 (1968); *Levan v. Richter*, 152 Ill. App.3d 1082, 504 N.E.2d 1373 (1987); *Plante v. Jacobs*, 10 Wis.2d 567, 103 N.W.2d 296 (1960). In a few states a party who substantially performs recovers in restitution, otherwise he forfeits compensation. *J.A. Sullivan Corp. v. Commonwealth*, 397 Mass. 789, 494 N.E.2d 374 (1986). The New York rule on construction contracts is a variant. A contractor who substantially performs is paid on the contract (less damages) otherwise he has no claim in restitution. *Steel Storage & Elevator Constr. Co. v. Stock*, 225 N.Y. 173, 121 N.E. 786 (1919). New York law has softened in other settings. *Hadden v. Consolidated Edison Co. of New York*, 34 N.Y.2d 88, 356 N.Y.S.2d 249, 312 N.E.2d 445 (1974), states that willfulness of default is only a factor to be considered in deciding if employee substantially performed and holds that employee who had taken bribes from contractors might not forfeit his pension. The second time round the New York Court of Appeals concluded forfeiture of the pension was appropriate on a technical ground. *Hadden v. Consolidated Edison Co. of New York, Inc.*, 45 N.Y.2d 466, 382 N.E.2d 1136, 410 N.Y.S.2d 274 (N.Y. Oct 26, 1978).

defaulter.²⁷ My major point in this part is that lesson of *Parker* can be generalized. Under the doctrine of material breach a party may withhold or refuse performance in response to an indisputable default to avoid suffering an uncompensated loss though this inflicts a disproportionate loss on the defaulter. A party may be left with an uncompensated loss from breach of a contract right to avoid forfeiture and unjust enrichment, but this is not done in the interest of efficient breach. There is no need to discuss conditions at this point for I take it to be uncontroversial that the law may excuse default of a condition to avoid forfeiture but that it does not excuse default on the ground that fulfilling a condition imposes an unreasonable burden.

The Second Restatement of Contract states five factors that bear on the determination of material breach.²⁸ They are similar to the five factors that bear on the determination of “fundamental breach” under the UNIDROIT principles.²⁹ With no loss

²⁷ Robert A. Hillman, Keeping the Deal Together After Material breach – Common Law Mitigation Rules, The UCC, and the Restatement (Second) of Contracts, 47 Colo. L. Rev. 553 (1976), remains a good article on the topic. Hillman’s article challenges the many cases that state in categorical terms that there is no obligation to do further business with a defaulter. The most famous of these cases is *Canadian Indus. Alcohol Co. v. Dunbar Molasses Co.*, 258 N.Y. 194, 200-201, 179 N.E. 383, 385 (1932)(“The plaintiff replied in substance that it had no longer any faith in the defendant’s readiness or ability to live up to its engagements, and did not wish to add another contract to the one already broken. The law did not charge it with a duty to make such an experiment again.”) See also *W-V Enterprises, Inc. v. Federal Sav. & Loan Ins. Corp.*, 234 Kan 354, 367, 673 P.2d 1112, 1122 (1983)(“there is no obligation to mitigate damages if the mitigation involves dealing with the defaulting party.”)

²⁸ Restatement, Second, of Contracts § 241. The factors are:

- “(a) the extent to which the injured party will be deprived of the benefit which he reasonably expected;
- (b) the extent to which the injured party can be adequately compensated for the part of the benefit of which he will be deprived;
- (c) the extent to which the party failing to perform or to offer to perform will suffer forfeiture;
- (d) the likelihood that the party failing to perform or to offer to perform will cure his failure, taking account of all the circumstances including any reasonable assurances;
- (e) the extent to which the behavior of the party failing to perform or to offer to perform comports with standards of good faith and fair dealing.”

Some decisions state a much higher standard to justify termination that “the breach [must] destroy the entire purpose of the contract.” See, e.g., *Peters v. Blagden Homes Inc.*, 151 A.2d 183 (D.C. 1959); *Ervin Const. Co. v. Van Orden*, 125 Idaho 695, 700, 874 P.2d 506, 511 (Idaho 1993). Another version of the standard asks if “the contract would not have been made if default in that particular had been expected or contemplated.” *Huffman v. Saul Holdings Ltd.*, 194 F.3d 1072, 1081 (8th Cir. 1999), following *Berland’s, Inc. of Tulsa v. Northside Village Shopping Ctr., Inc.*, 378 P.2d 860, 865 (Okla.1963).

²⁹ UNIDROIT Article 7.3.1(2): In determining whether a failure to perform an obligation amounts to a fundamental non-performance regard shall be had, in particular, to whether: (a) the non-performance substantially deprives the aggrieved party of what it was entitled to expect under the contract unless the other party did not foresee and could not reasonably have foreseen such result; (b) strict compliance with the obligation which has not been performed is of essence under the contract; (c) the non-performance is intentional or reckless; (d) the non-performance gives the aggrieved party reason to believe that it cannot

of substance these two lists of five can be reduced to three factors: (1) whether the aggrieved party needs to withhold or refuse performance to avoid suffering an uncompensated loss³⁰; (2) the burden imposed on the defaulter by withholding or refusing performance³¹; and (3) whether the default was willful or in bad faith.³²

The Restatement is conspicuously opaque about the relative weight assigned to these factors when they cut in different directions.³³ It is as we saw in Part One. A party may refuse non-conforming performance or withhold performance in response to default to avoid suffering an uncompensated loss though his action inflicts a disproportionate loss on the defaulter. Sales law on the power to revoke acceptance provides a telling example. Revocation is more troublesome than rejection because the seller is likely to incur a loss when it must recover and resell goods that have been used by the buyer. Under the Uniform Commercial Code, a buyer may revoke acceptance for a hidden defect only if the defect ‘substantially impairs’ the value of the goods to him.³⁴ Commentators who have looked closely at the cases have found that courts are very

rely on the other party's future performance; (e) the non-performing party will suffer disproportionate loss as a result of the preparation or performance if the contract is terminated.

³⁰ Restatement factors (a), (b), and (d); UNIDROIT factors (a), (b), and (d).

³¹ Restatement factor (c) states the principle against forfeiture. UNIDROIT factor (e) speaks of avoiding a “disproportionate loss” to the defaulter. It is much the same thing. The Second Restatement defines forfeiture as “the denial of compensation that results when the obligee loses his right to the agreed exchange after he has relied substantially.” Restatement, Second, of Contracts, § 227 comment b. The Restatement’s definition of forfeiture suggests two baselines for measuring forfeiture. The reference to “reliance” and “the denial of compensation” suggests a baseline of the defaulter’s pre-contractual position. The reference to the defaulter’s “right to the agreed exchange” suggests a baseline of the defaulter’s position if the contract was fully performed by both sides. I think the latter view is more in accord with the law. Countless insurance cases invoke the principle opposing forfeiture to protect the right of an insured to collect on what is in effect a winning bet notwithstanding his default on a technical term of the bet. Sales cases that prevent a buyer from rejecting goods because of a minor defect to get out of a losing bargain are similar. See James J. White & Robert S. Summers, Uniform Commercial Code 355-357 (3d ed. 1988)(concluding that “relatively little is left” of the UCC perfect tender rule because courts have used a variety of devices to prevent sellers from rejecting goods in bad faith to escape a disadvantageous bargain).

³² Restatement factor (e); UNIDROIT factor (c). It is uncontroversial that the quality of the defaulter’s conduct is relevant when his misconduct bears on the likelihood that the aggrieved party will suffer a loss if he does not withhold or refuse performance. Less clear is whether forfeiture may be countenanced to punish willful or intentional breach.

³³ Restatement, Second, of Contracts, § 241, comment (a)(“This Section therefore states circumstances, not rules, which are to be considered in determining whether a particular failure is material.”); comment (b)(“ no simple rule based on the ratio of the one to the other can be laid down, and here, as elsewhere under this Section, all relevant circumstances must be considered.”)

³⁴ UCC 2-608(1). The CISG has a fundamental default standard.

protective of buyer's rights in applying this seemingly seller-friendly standard so long as a buyer acts to revoke promptly upon discovering a defect.³⁵

*Colonial Dodge Inc v Miller*³⁶ nicely illustrates. Miller bought a station wagon with special ordered extra wide tires. The car was delivered without a spare extra wide tire. Miller discovered the tire was missing within a day but after he had driven the car four hundred miles. He demanded a spare from the dealer and was told that it could not be supplied because of a strike at the factory. Miller immediately parked the car in front of his house and demanded that the dealer retrieve it. Eventually the car was towed from the street by the police where it was impounded for a number of years as the case passed through the courts. The dealer sued for the price. He won in the trial court, lost on appeal, won on rehearing, and finally lost at the state supreme court by a vote of six to three. The expected loss to Miller from the temporary lack of a spare was small but, perhaps, meaningful to him.³⁷ Much of the loss would have been in worrying while driving without a spare. There was also a small chance that Miller would be stranded without a spare. None of these losses were compensable in damages. Returning the car imposed a large loss on the dealer for the car could no longer be sold as new. That the case was thought close despite the imbalance between Miller's likely loss if he drove the car for a short while without the spare and the loss to the dealer from returning the car – the thirteen judges who heard the case split seven to six with one switching – is telling evidence of the unwillingness of judges to require a party to take and pay for clearly defective performance when that might leave him with even a small uncompensated loss though the defaulter is subjected to a certain larger loss.

There are counter-examples of cases where a person is required to accept and pay for non-conforming performance. Perhaps the most famous counter-example is *Jacobs & Young v. Kent*.³⁸ Kent was made to pay the full contract price for the construction of a home though the builder substituted Cohoes pipe for Redding pipe specified in the contract. But it may not be a good example. There is a plausible argument that Redding pipe was specified as a standard making the substitution of equivalent Cohoes pipe not a default. A better counter-example is *Plante v Jacobs*³⁹ for it is undeniable that the Jacobs

³⁵ JA Sebert Jr 'Rejection, Revocation, and Cure Under Article 2 of the Uniform Commercial Code: Some Modest Proposals' 84 Northwestern U L Rev 375, 399–408 (1990), is a good review of the case law. DW Garland, 'Determining Whether a Nonconformity Substantially Impairs the Value of Goods: Some Guidelines', 26 Uniform Commercial Code L J 129 (1993), comes to much the same conclusions.

³⁶ 420 Mich 452, 362 NW 2d 704 (1984).

³⁷ The dealer and the manufacturer thought Miller was returning the car on a pretext. Local newspaper and television had reported that dealers were delivering new cars without spares because of the auto strike. This being Detroit it was understandably big news. MacCauley, Kidwell, and Whitford, *Contracts Law in Action: The Concise Course* 130-131 (Lexis-Nexis 2003).

³⁸ *Jacob and Youngs v Kent* 230 NY 239, 129 NE 889 (1921).

³⁹ 10 Wis 2d 567, 103 NW 2d 296 (1960).

were made to pay the contract price for non-conforming performance though that left them with an uncompensated loss. This is another case involving construction of a home. The builder, Plante, misplaced a living room wall by one foot on the narrow side. The case holds that the Jacobs had to pay the balance due on the contract for the work done (around \$5,000) and that they could not recover the price of moving the wall (around \$4,000) because narrowing the room did not lower their home's market value. Whatever loss the Jacobs suffered from having a smaller living room was uncompensated.

Plante v. Jacobs involves two rules that excuse minor defaults. The court applied the rule of substantial performance to give the builder a right to the contract price and it applied the rule measuring damages by loss in market value when remedial cost is much greater to allow the builder to recover most of the balance due.⁴⁰ The second rule sometimes is said to be concerned with avoiding the economic waste that would result from repairing a defect when the cost of doing so is much greater than actual loss from the defect.⁴¹ It is well known that this misstates the purpose of both rules, which is to avoid forfeiture and unjust enrichment.⁴² In *Plante v. Jacobs* the impression that the wall is not worth moving and the fact that the Jacobs chose not to move the wall combine to raise a strong inference that allowing the Jacobs to retain the unpaid contract price or to recover the cost of moving the wall would give them a windfall at the builder's expense.

⁴⁰ *Peevyhouse v Garland Coal and Mining Co.*, 382 P.2d 109 (Okla. 1962), cert. denied 375 US 906 (1963), is a famous and troublesome illustration of an application of the second rule. Garland failed to fulfill its promise to restore seven acres of farmland that it had strip mined. The Peevyhouses were left with a large water-filled pit that barred access to other land they owned and leased. The cost of restoring the land was estimated as \$29,000 while the market value of the seven acres taken by the pit was only \$350 at the time. The jury had awarded \$5,000. The Oklahoma Supreme Court reduced the award to \$350 reasoning that damages were limited to loss in market value when remedial cost was grossly disproportionate. *Peevyhouse* often paired with *Groves v John Wunder* 205 Minn. 163, 286 N.W. 235 (1939), which holds that a defendant who willfully fails to perform must pay the remedial cost though it is far in excess of loss in market value.

Decisions such as *Peevyhouse* and *Groves* are testament to the value placed on remedial simplicity in American law. Often in these cases the loss to the aggrieved party is between remedial cost and loss in market value. The rule requires choosing one or the other objective measure of damages though we are confident one over-compensates and the other under-compensates. While the aggrieved party is entitled to put on evidence that he has abnormal interests or preferences that justify an award of remedial costs the rule requiring the choice of one of two objective measures of damages makes it possible for a judge to resolve the issue.

⁴¹ Carol Chomsky, *Of Spoil Pits and Swimming Pools: Reconsidering the Measure of Damages for Construction Contracts*, 75 Minn. L. Rev. 1445, 1451-1460 (1991), reviews many similar cases and concludes that the primary focus is avoiding economic waste.

⁴² See, e.g., Restatement (Second) of Contracts, § 348, comment c ("It is sometimes said that the award would involve "economic waste," but this is a misleading expression since an injured party will not, even if awarded an excessive amount of damages, usually pay to have the defects remedied if to do so will cost him more than the resulting increase in value to him."); Alan Farnsworth, *Contracts* 619 (2nd ed. 1990) ("the concept of substantial, as opposed to strict, performance evolved in response to the risk of forfeiture."). *Hancock v. Northcutt*, 808 P.2d 251 (Alaska 1991), follows this reasoning to the logical conclusion that if the jury concludes that the hirer will make the repair it must award cost of repair whatever the loss in market value.

If you remain unconvinced that these rules are not about avoiding economic waste, an often overlooked companion rule clinches the point. This rule applies when the aggrieved party actually repairs the defect. The law denies recovery of money spent on substitute performance on the ground that the substitute is better than the promised performance, but it does not deny recovery of money spent on substitute performance on the ground that the loss in market value from the defect in the original performance does not warrant the outlay.⁴³ If the aggrieved party spends the money to fix a defect, the law does not question his reasons. Ironically, the combination of this rule and the rule sometimes limiting damages to loss in market value if a defect is not repaired may actually encourage wasteful repair for the two rules give the aggrieved party an incentive to repair a defect to avoid being under-compensated for a subjective loss.⁴⁴

Another feature of the law on material breach and substantial performance strengthens the point that these rules do not promote efficient breach. Under the traditional rule, a defaulter may recover the contract price or in restitution for defective performance only if the defect in his performance is inadvertent.⁴⁵ A plausible account of this rule is that it discourages a party from unilaterally modifying a contract by denying him compensation for a knowing deviation.⁴⁶ This is without regard to the

⁴³ Kirkpatrick v. Temme, 98 Nev. 523, 654 P.2d 1011 (1982)(awarding \$84,333.73 spent to complete construction where contract price was \$175,000 despite defaulter's testimony that work was 80% complete and that he could have finished for \$39,2000 where the owner and second contractor testified original plans and specifications were followed); Hi-Valley Constructors, Inc. v. Heyser, 163 Colo. 1, 428 P.2d 354 (1967)(awarding cost of repainting exterior of house); Carlin v. Comstock, 38 Conn. Super. 424, 450 A.2d 875 (1982)(awarding \$2,106.44 to complete porch though only \$143 was due on the original contract).

⁴⁴ For example, the rules seem to give the Plantes an incentive to spend \$4,000 to move the wall, though they place only a \$1,000 value on having the wall moved, because the Plantes bear the \$1,000 loss if the wall is not moved while Jacobs bears the \$4,000 cost of moving the wall. But the law tempers the incentive to make wasteful repairs by allowing the hirer to keep the balance due on the contract or recover remedial cost as damages unless those amounts are substantially disproportionate to the hirer's loss from the faulty construction. So, for example, if the Plantes had personal reasons to move the wall that would justify them spending a sum as substantial as \$1,000, then they might think they have a fair chance of keeping the \$5,000 balance due if they do not make the repairs and present their reasons for wanting the wall moved as good enough to retain the balance. Your guess is as good as mine as to how people actually respond to these rules.

⁴⁵ There is a fair amount of old case law countenancing forfeiture to punish willful default. Corbin, who strongly condemned these cases, gave as an extreme example *McNeal-Edwards Co. v. Frank L. Young Co.*, 35 F.2d 829 (1st Cir. 1929). The seller delivered defective oil causing the buyer \$10,730 in damages. In response the buyer retained possession of drums belonging to the seller causing the seller \$100 in damages. The court held that this was wrong (and indeed that the buyer committed the tort of conversion) and as a consequence it denied the buyer's larger claim for damages. Corbin on Contracts § 1254.

⁴⁶ Andrew Kull, *Restitution's Outlaws*, 78 Chi.-Kent L. Rev. 17 (2003), makes the general point that restitution punishes wrong-doers by withholding a claim that it would otherwise allow to prevent unjust enrichment. The Restatement Third of Restitution and Unjust Enrichment points in this direction in stating that restitution to the builder who knowingly deviates from plans should be qualified or denied in order to avoid subjecting the owner to a forced exchange. Council Draft No. 5, § 36(b) and comment b.

efficiency of the modification. While American law may be softening towards knowing default (more on this in a moment), it seems to remain the law that a builder will not recover the contract price or in restitution for a knowing deviation from a contract absent a default or other conduct by the other justifying the deviation.⁴⁷ A contract right is treated like a property right in that a knowing default is subject to the punitive sanction of forfeiture.⁴⁸

The Second Restatement of Contracts does not condemn knowing default tout court. Rather it makes the defaulter's bad faith one factor among several to be weighed in deciding if a default is material.⁴⁹ This in itself means little. More significant is the implicit drift of the Restatement's comments, which never suggest forfeiture may be justified to punish knowing default.⁵⁰ The leading treatises delve a little deeper and intimate that moderate forfeiture is preferred to a risk of leaving the aggrieved party with an uncompensated particularly if the breach is knowing or in bad faith.⁵¹ But this is not

(Nov. 24, 2003). This analogizes the builder who deviates from plans to the knowing trespasser who builds an improvement.

⁴⁷ Many cases state the rule though there seem to be few occasions to apply it. *Tolstoy Constr. Co. v. Minter*, 78 Cal. App. 3d 665, 671, 143 Cal. Rptr. 570 (Cal. App. 1978); *Moore's Builder and Contractor, Inc. v. Hoffman*, 409 N.W.2d 191, 195 (Iowa Ct. App. 1987); *Peabody N.E., Inc. v. Town of Marshfield*, 426 Mass. 436, 689 N.E.2d 774 (1998); *Sear-Brown Associates, P.C. v. Blackwatch Development Corp.*, 492 N.Y.S.2d 266 (N.Y.A.D. 1985)(applying the rule); *Merrill Iron & Steel, Inc. v. Minn-Dak Seeds, Ltd.*, 334 N.W.2d 652 (N.D. 1983); *Ahlers Bldg. Supply, Inc. v. Larsen*, 535 N.W.2d 431, 435 (S.D. 1995); *Uhlir v. Golden Triangle Development Corp.*, 763 S.W.2d 512 (Tex. Civ. App.-Fort Worth, 1988). Cf. *Hayeck Bldg. & Realty Co. v. Turcotte*, 361 Mass. 785, 282 N.E.2d 907 (1972)(requiring good faith and countenancing switch to less costly method of doing work). In *Mathis v. Thunderbird Village*, 236 Or. 425, 389 P.2d 343 (1964), which is the basis for Restatement, Second, § 241, illustration 7, a builder's intentional failure to complete the work in a minor respect was excused because it was prompted by the hirer's failure to pay. *Vincenzi v. Cerro*, 186 Conn. 612, 442 A.2d 1352, 1354 (1982), excuses failure to complete work in a timely fashion though it was alleged to be willful.

There is also a fair amount of case law for the proposition that a willful deviation warrants an award of remedial cost however disproportionate this amount may be to the apparent loss. *Kangas v. Trust*, 100 Ill. App. 3d 876, 65 Ill. Dec. 757, 441 N.E.2d 1271 (1982); *Roudis v. Hubbard*, 176 App. Div. 2d 388, 574 N.Y.S.2d 95 (NYAD 1991); *Fidelity & Deposit Co. v. Stool*, 607 S.W.2d 17 (Tex. Civ. App. 1980). To the contrary is *Grossman Holdings, Ltd. v. Hourihan*, 414 So.2d 1037 (Fla. 1982)(denying remedial cost though contractor built house facing in wrong direction over repeated protests of owner).

⁴⁸ Even property rights can give way if an infringement is minor and enjoining the infringement would inflict an undue hardship on the infringer. *Mannillo v Gorski* 54 NJ 378, 255 A2d 258 (1969)(innocent encroacher is only made to pay the market value of what he has taken). Typically the doctrine of undue hardship protects only innocent infringers. *Ariola v Nigro* 16 Ill 2d 46, 156 NE 2d 536 (1959)(relying on rule that an intentional encroachment will always be enjoined).

⁴⁹ Restatement, Second, of Contracts § 241(e).

⁵⁰ Restatement, Second, of Contracts § 241, comment (d).

⁵¹ A. Farnsworth, *Contracts* § 8.12 (2nd ed. 1990); J. Perillo, *Calamari and Perillo on Contracts*, § 11.18 (5th ed. 2003).

the same thing as countenancing the use of forfeiture to punish knowing default. This is, or at least could be, a subtle change in the law that follows from accepting the general position that it is not wrong to break a contract.

This account accurately describes the law in an important and general situation.⁵² This is where a defaulter renders part performance and then abandons a contract. Two staples of the Contracts course, *Britton v. Turner*⁵³ and *Vines v. Orchard Hills, Inc.*,⁵⁴ are in this mold. In *Britton*, a worker abandoned a contract for a year's employment after working nine and one half months. In *Vines*, a condominium buyer backed out of the contract after paying a hefty deposit. Both cases allow the defaulter to recover for the value of his part performance less whatever holdback is necessary to put the other in the promised position. Construction contracts are no different. A builder who abandons a job may recover the contract price less the other's cost of completing the work.⁵⁵ All are cases of knowing default.

Forfeiture is unjustified in these cases because generally the aggrieved party is indifferent to who completes performance so long as he ends up paying no more than the contract price for what he buys or receiving no less than the contract price for what he sells. Thus, the rejection of forfeiture in these cases is consistent with the position that the sole justification for forfeiture is to avoid a risk of leaving the aggrieved party with an uncompensated loss. In some of these cases there are good independent reasons to reject punitive forfeiture. If someone were to argue that an employee who quits a job should be punished by forfeiture to vindicate the employer's right to the employee's labor, we would answer him: "No. The employer has a right to be compensated for his loss because the employee left work in breach of his contract, but it is the employee's time."

It is easy to think of reasons why the law might use forfeiture to punish a builder who knowingly deviates from an owner's plans while it does not to use forfeiture to punish a worker who walks off a job.⁵⁶ Exploring these reasons would take us pretty far

⁵² This account also accurately describes the law regarding forfeiture of property for non-payment of a debt. A forfeiture clause is tested much like a stipulated damages clause and will be enforced only if it is reasonable effort to measure otherwise immeasurable damages. *Ebbert v. Mercantile Trust Co. of California*, 2 P.2d 776 (Cal. 1931).

⁵³ 6 N.H. 481 (1834).

⁵⁴ 181 Conn. 501, 435 A.2d 1022 (1980).

⁵⁵ Restatement, Second, of Contracts § 348, illustration 2. This is true even in New York, which is stern towards a builder who knowingly deviates from a contract. *Mirisiv v. Renda*, 83 App. Div.2d 572, 441 N.Y.S.2d 138 (App. Div. 1981).

⁵⁶ There is an efficiency argument for treating the cases differently because there is a greater risk of social loss in deviating from construction plans than in withholding labor. There is a moral argument because penalizing a worker who walks off a job infringes his personal liberty. There is a legal argument for treating the cases differently because deviant construction may be said to infringe on the owner's property right. One can also liken a contractor who knowingly deviates from plans to an officious intermeddler or a trespasser who builds an improvement.

afield. One point to be taken from this is that contractual obligations differ on multiple dimensions that affect their enforcement at multiple points. This is commonplace in the remedy of specific performance where different rules apply to the sale of land and labor. The modern tort of bad faith breach applies to a limited class of contracts that has at its core insurance. Forfeiture is the traditional way to punish knowing breach. That this is thought appropriate for some contractual obligations but not others is unsurprising. Nor need all contractual obligations be treated the same in respect to the degree of tolerance of forfeiture to avoid a risk of under compensating the aggrieved party. In construction cases, some states assign to the builder the burden of establishing the cost of completing undone work at pain of forfeiture if he cannot.⁵⁷ This should not commit them to assigning to a worker who leaves a job the burden of proving his employer's damages for it is easy to think of reasons for treating these cases differently.

It may seem that the Second Restatement unnecessarily confuses the issue of the culpable state of mind by targeting bad faith default rather than knowing default. Generally, knowing trespass merits punitive damages⁵⁸ and the punitive sanction of forfeiture of a restitution claim for improvements.⁵⁹ But the bad faith standard is apt when the default is on a doubtful obligation, as it often is. In Part Four we will see that an honest belief a performance is not owed cuts against treating default as material. We will come to this. The point for now is that the rules on material breach and substantial performance come down hard on a person who knowingly defaults on an indisputable contractual obligation. Occasionally forfeiture is used to punish knowing default. Generally forfeiture is preferred to a risk of leaving the aggrieved party with an uncompensated loss. None of this is consistent with promoting efficient breach.

3. Mitigation redux: efficient vindication of rights

While contract law does not promote efficient breach, it does promote efficient vindication of rights. Thus, sales law encourages a buyer and a seller to make a substitute transaction and recover the difference in price on repudiation because this usually is the cheapest and simplest way to achieve the promised position. Cases that twist the text of the Code to achieve this end attest to the strength of the basic idea. The Dawson casebook highlights a trio of cases where courts read the text in different ways to encourage a buyer to make a substitute transaction on anticipatory repudiation.⁶⁰ Sales law encourages a

⁵⁷ *Miris v. Renda*, 83 A.D.2d 572, 441 N.Y.S.2d 138 (2d Dep't 1981); *BPR Const. & Engineering, Inc. v. Rivers*, 608 S.W.2d 248, 249-250 (Tex.Civ.App.-Dallas 1980). Often the burden of establishing forfeiture is placed on the party seeking relief from forfeiture. *MacFadden v. Walker* 97 Cal.Rptr. 537, 5 Cal.3d 809, 488 P.2d 1353 (1971).

⁵⁸ *Jacque v. Steenberg Homes, Inc.*, 563 N.W.2d 154 (Wisc. 1997).

⁵⁹ Restatement, Third, Restitution and Unjust Enrichment, Tent. Draft No. 1, § 10, comment e and illustrations 5 and 6 (2001).

⁶⁰ *Oloffson v. Coomer*, 11 App.3d 918, 296 N.E.2d 871 (1973)(reasoning that damages are measured at time of repudiation is final under § 2-713 because that is when buyer "learned of the breach"); *Cargill, Inc. v. Stafford*, 553 F.2d 1222 (10th Cir. 1977)(reasoning that while damages are measured at time

buyer to make a substitute transaction when that appears to be the easiest way to vindicate his rights even if the seller wants to continue. Thus, a buyer is encouraged to reject a tender of non-conforming goods by rules that strip him of prerogatives if he accepts a tender of goods he knows are non-conforming unless he has good reason to believe that continuing with the transaction will be a cheap and easy way eventually to get what he was promised.⁶¹ These rules function like the mitigation doctrine in that they encourage the aggrieved party to pursue the cheapest path to vindicating his rights. The difference is that the mitigation doctrine cuts off the right to damages while these rules cut off the power to return goods.

The doctrines of waiver and equitable estoppel sometimes serve the same function. They deprive a party of a right or prerogative when his negligence in asserting the right or prerogative inflicts a loss on the other. Few areas of private law are as poorly mapped as these two, particularly the law of waiver.⁶² One of the better American Contracts treatises states that “contractual *rights* are not waivable, *conditons* are.”⁶³ At best this is misleading, at worst it is deeply confused.⁶⁴ On a more practical level cases

of performance under § 2-713 (which was the common law rule), if buyer could have covered through forward contract they should be measured at what the cover price would have been under § 2-712); *Cosden Oil & Chemical Co. v. Karl O. Helm Aktiengesellschaft*, 736 F.2d 1064 (5th Cir. 1984)(laying down a rule to require cover without trying to find a textual hook in the UCC).

⁶¹ Much of this is in UCC § 2-608(1), which bars revocation of acceptance if a buyer accepted goods knowing of a non-conformity unless he did so on the seller’s assurances the non-conformity would be cured. Even if a buyer satisfies this requirement, revocation is prohibited under § 2-608(2) if there has been a substantial change in the value of the goods not caused by the defect. This is buttressed by § 2-605(1), which preclude a buyer from relying on ascertainable defect to justify rejection or establish breach if he fails to notify the seller of the defect and the seller could have cured had he been notified.

⁶² The doctrine of equitable estoppel is perplexing because of the old saw that estoppel may be used as a shield but not as a sword. *Dickerson v. Colgrove*, 100 U.S. 578, 580-581 (1879)(“This remedy . . . is available only for protection, and cannot be used as a weapon of assault.”) In the insurance context the upshot of the old saw is that estoppel can be used to override a condition to coverage but it cannot be used to expand coverage. *Martinelli v. Travelers Insurance Companies*, 687 A.2d 443, 447 (R.I.1996); *ABCD ... Vision, Inc. v. Fireman's Fund Insurance Companies*, 304 Or. 301, 744 P.2d 998, 1001-02 (1987). The old saw is not a categorical rule. *Potesta v. United States Fidelity & Guaranty Co.*, 202 W. Va. 308, 504 S.E.2d 135 (1998), notes three exceptions: estoppel based on an agent’s misrepresentation of the scope of coverage when the policy was made; estoppel based on a liability insurer tendering a defense without a reservation of rights; and, estoppel based on bad faith by an insurer in failing to settle a claim.

⁶³ John D. Calamari & Joseph M. Perillo, *The Law of Contracts* 442 (4th ed. 1998).

⁶⁴ A right to a performance is described as a condition when default allows the right-holder to withhold or refuse performance. If the statement quoted in text was correct, then it would be more accurate to say that what is waived is the power to withhold or refuse performance on default. UCC § 2-607(2) is consistent for it states that a person who accepts non-conforming goods waives his right to reject the goods while retaining his right to damages. But sometimes the concept of waiver is used to deny a right-holder damages for infringement of a right. For example, under UCC § 2-605 a buyer who fails to inform the seller of curable defects is said to waive his right to damages. Of course, the rule in UCC § 2-605 could be restated as a rule of mitigation. The concept of waiver tends to be associated with conditions (meaning the power to withhold or refuse performance on default) because other doctrinal tools exist to

disagree on such basic questions as whether a material term can be waived,⁶⁵ whether waiver must be overt and knowing⁶⁶ or can be implied and inadvertent,⁶⁷ and whether waiver requires detriment to the other.⁶⁸

The truth of the matter is that the considerations of materiality, fault, and harm intertwine as waiver and estoppel are called upon to do several different tasks. Waiver sometimes is used to override a condition when default clearly does not expose the obligee to the harm or risk that the condition was meant to protect against. In these cases waiver is found with little regard for the responsibility of the obligor for bringing about the situation in which enforcement of a condition would result in forfeiture.⁶⁹ The rule overriding a condition to avoid disproportionate forfeiture would be a more candid basis for these cases.⁷⁰ Quite different are cases in which waiver or equitable estoppel is used to enforce an informal or defective agreement that has been acted upon. Often these

deny a right-holder damages if his failure to act upon his right contributes to his loss or makes his loss difficult to measure.

⁶⁵ *Ludwig v. Nynex Service Co.*, 838 F. Supp. 769, 796 (S.D.N.Y. 1993)(“Conditions that are crucial to the original bargain cannot be waived in the absence of fresh consideration or a consideration substitute such as promissory estoppel.”), citing *Clark v. West*, 193 N.Y. 349, 86 N.E. 1, 5 (1980). Compare *Nassau Trust Co. v. Montrose Concrete Products Corp.*, 56 N.Y.2d 175, 436 N.E.2d 1265, 451 N.Y.S.2d 663 (1982), which finds that a lender waived the power to declare a default and foreclose on a loan in substantial arrearage when the borrower was advised orally to continue to try to sell the property and not to lower its asking price.

⁶⁶ *Magic Valley Foods, Inc. v. Sun Valley Potatoes, Inc.*, 134 Idaho 785, 10 P.3d 734 (2000)(holding that seller does not waive term requiring timely payment by failing to object to late payment where buyer allowed amount in arrearage to build up).

⁶⁷ *John D. Calamari & Joseph M. Perillo, The Law of Contracts* 442 (4th ed. 1998)(“many, if not most waivers are intentional and frequently do not involve a ‘right’ that the party is aware of.”)

⁶⁸ Judges Posner and Easterbrook disagree on this point in *Wisconsin Knife Works v. National Metal Crafters*, 781 F.2d 1280 (7th Cir. 1986). Easterbrook (dissenting) advances the traditional view that a waiver of executory obligations is retractable if the obligor if the obligor has not changed his position in reliance on the waiver in a way that would make retraction unjust. This is essentially what UCC § 2-209(5) states.

⁶⁹ *Schultz v. Los Angeles Dons*. 107 Cal. App.2d 718, 723-725, 238 P.2d 73 (1951)(team discharged player shortly after lapse of period in which he was required to give written notice of injury, held condition was waived because team had knowledge of injury through physician and coach).

⁷⁰ Section 229 of the Restatement, Second, of Contracts. *Aetna Cas. & Sur. Co. v. Murphy*, 206 Conn. 409, 538 A.2d 219 (1988), is a leading case applying this doctrine. *Clementi v. Nationwide Mut. Fire Ins. Co.*, 16 P.2d 223, 230-232 (Colo. 2001), and *Alcazar v. Hayes*, 982 S.W.2d 845, 856 (Tenn. 1998), show how the doctrine has been worked out as regards a condition of notice of an insurance claim. *Oppenheimer & Co., Inc. v. Oppenheim, Appel, Dixon & Co.*, 86 N.Y.2d 685, 692-693, 660 N.E.2d 415, 636 N.Y.S.2d 734 (1995), emphasizes the relevance of forfeiture or unjust enrichment for it holds that a condition strictly applies absent forfeiture. Timely oral notice of acceptance was held not to satisfy a condition requiring written notice. The case also states that forfeiture requires both a loss to the person claiming forfeiture and a gain to the other. *Id.* at 694-5.

cases involve agreements to accept substitute performance.⁷¹ In these cases waiver and estoppel go to important terms but require something close to assent by the obligor and a change of position by the obligee.⁷² The similarity to promissory estoppel is obvious.

A third use of waiver and estoppel is to deny a person of a contractual right or prerogative when his negligence in asserting the right or prerogative causes a loss to the defaulter. A familiar example already noted is the rule that bars a buyer from returning accepted goods when he should have known the goods were defective.⁷³ In this setting, unlike the other two, waiver and estoppel do not require unjust enrichment or an overt act or a deliberate choice by the right-holder. The doctrines may be used to strip a person of contractual prerogative, such as the power to return goods or to exit from a contract, to cast upon him a loss he caused inadvertently but negligently.⁷⁴ The gist of the doctrines is neglect in asserting a power or right and resulting harm. The obvious parallel between the mitigation doctrine and the negligence doctrine and this last use of waiver and

⁷¹ *Wisconsin Knife Works v. National Metal Crafters*, 781 F.2d 1280 (7th Cir. 1986), illustrates. The case involves an apparent agreement by buyer to stretch out delivery dates that could not be enforced as such because of a no oral modification clause in the original contracts. The statute of frauds was not an issue because there was a writing by the seller acknowledging the modification, which satisfies the statute as against the buyer under UCC 2-201(2). The case plays out as a waiver case under UCC 2-209(4) and (5) because a no oral modification clause can be waived. This suggests a justification for Judge Posner's conclusion that waiver requires a showing of reliance. Historically waiver does not require reliance, but in this context waiver is being used to get around the absence of a writing signed by the defendant attesting to the modification. This, of course, is usually done by estoppel, where reliance is the heart of the matter. Reliance should be the heart of the matter because of its evidentiary value.

⁷² There is also an overlap with the doctrine of ratification, which requires apparent assent but does not require reliance. *Merrill v. DeMott*, 113 Nev. 1390, 1396-97, 951 P.2d 1040 (1997).

⁷³ This is codified in Sales law. A buyer who accepts goods must pay for them unless he has the power to revoke his acceptance. The buyer is said to have waived his power to reject. UCC 2-607(2). The power to revoke is conditioned upon the buyer having been ignorant of the defect or having been assured of its repair by the seller at the time of the acceptance. UCC 2-608. The buyer is left with a claim for breach of warranty under UCC 2-614. A buyer waives his claims for damages if the seller could have cured the defects upon notification. UCC 2-605. Avoidable damages may also be denied through the mitigation doctrine.

⁷⁴ *Mahban v. MGM Grand Hotels*, 100 Nev. 593, 691 P.2d 421 (1984), is an example. A lease gave either party the power to cancel in event the premises were destroyed. After a fire the lessor sent a letter to the lessee indicating that it planned to rebuild and asking the lessee to advise it of any plans it had to do work on the space. Relying on the letter the lessee ordered new merchandise. A month later the lessor cancelled the lease. The trial court held that the lessor had waived this power. The court of appeals held that the lessor was estopped from canceling.

Pike v. Howell Building Supply, Inc., 748 So.2d 710 (Miss. 1999), is a striking example of the use of waiver to do the work of the doctrines of contributory negligence or assumption of risk. An owner of gas station sued a contractor when concrete poured by the contractor buckled rupturing a gas line. The contractor had warned the owner of the risk of this happening but the owner had instructed him to proceed. Reasoning that the claim sounded in Contract and not Tort the court refused to apply the doctrines of contributory negligence and assumption of risk. Instead it held that the owner waived claim he might have for unworkmanlike construction.

estoppel suggest that forbearance in asserting a right or power should not trigger waiver or estoppel if the forbearance was a reasonable effort to mitigate loss. Judge Posner has drawn this connection.⁷⁵ Of course, it also is written into sales law rule on rejection and revocation of nonconforming goods.

There is a curious asymmetry in how the law treats avoidable losses and avoidable remedial uncertainty. While it is commonplace to speak of a duty to mitigate,⁷⁶ it would be quite odd to say that Shirley MacLaine had a duty not to take the role in *Big Man, Big Country* to avoid being in a situation where her loss was too speculative to compensate. We do not think about the choice MacLaine is put to in *Parker* in such terms because speculative damages are denied without regard to their avoidability. Perhaps this is a testament to the strength of the interest in remedial simplicity. This may change. There is a movement to liberalize the law to allow awards of speculative damages. This creates a space for a rule that conditions a person's right to recover speculative damages on his having no other simpler remedial option. There are intimations of such a rule in the law of equity on specific performance.⁷⁷ If such a rule were to enter the law, then it would squarely pose the conflict between the goal of

⁷⁵ *McElroy v. B.F. Goodrich*, 73 F.3d 722 (7th Cir. 1996)(declining to find waiver or estoppel where the plaintiff “was simply making the best of a bad deal—and incidentally mitigated his damages.”) This point was unnecessary to reach the holding for the decision goes on to find the plaintiff's claim of default was unfounded.

⁷⁶ The description of mitigation as a duty is thought to be misleading for two reasons. One is that failure to mitigate triggers no obligation or liability. The other is that the mitigation rule is really a rule of causation. Charles McCormack, *Handbook on the Law of Damages* section 33, at 127 (1935), Corbin on Contracts section 1039 at 241 (1964); Restatement, Second, of Contracts section 350 comment b. Neither reason holds water to my mind. The mitigation doctrine is more than a rule of causation for it requires a determination that the claimant was at fault in not avoiding a loss. The first reason assumes that an obligation can be described as a duty only if breach is sanctioned by imposition of a secondary obligation. This is not self-evident. We might well say that a person has a duty to perform a contract even if the only consequence of non-performance is forfeiture of his rights under the contract.

Michael B. Kelly, *Living Without the Avoidable Consequences Doctrine in Contract Remedies*, 33 *San Diego L. Rev.* 175 (1996), has a more challenging argument for why it is misleading to speak of avoidable consequences or duty to mitigate. The gist of his argument is that when a person fails to take curative action in response to breach he reveals that the value to him of the position he is on breach is worth more than the value to him of the promised position (which the corrective measure would put him in). The cost of untaken curative action is denied to avoid putting the aggrieved party in better than his rightful position. This is an interesting way to think about a person who intelligently chooses not to take curative action in response to breach. But this way for framing the issue generates needless complexities if a person stupidly fails to take curative actions.

⁷⁷ The availability of specific performance will justify a court requiring greater certainty of proof if a plaintiff elects to recover damages. Restatement, Second, of Contracts section 352, comment 8. Further, egregious behavior by a defaulter may justify an award of speculative damages. *Native Alaskan Reclamation and Pest Control*, 685 P.2d 1211, 1222 (1987), endorsing Restatement, Second, of Contracts section 352, comment a (“A court may take into account all the circumstances of the breach, including willfulness, in deciding whether to require a lesser degree of certainty, giving greater discretion to the trier of the facts.”)

efficient performance and the goal of remedial simplicity. In *Parker*, a court would have to balance the difficulty and uncertainty of compensating MacLaine's loss if she took the second role against the loss (and unjust enrichment) avoided by compelling her to do the second role if she wants to collect the contract price.

4. Efficient performance and contract uncertainty

This part examines the rules that regulate exit and loyalty when there is a bona fide dispute regarding the adequacy of performance due, tendered, or demanded. It shows that the law permits a party to perform or accept performance in a dispute, and later seek redress in a court through a claim that he was obligated to do less or he was entitled to receive more, but only if his performance or acceptance of performance was necessary to avoid a loss. The goal of efficient performance is central to understanding this area of law. The next part considers whether contract uncertainty warrants exit.

My basic point in this part, while novel, seems obvious once you think about it. Picture a contract as two people undertaking to row a boat across a river. In the middle of the river a dispute arises over whether one is pulling his weight. The law has two different sets rules of engagement for the dispute. If the river is placid and the day is clear, the law encourages the rowers to resolve the dispute themselves in the boat as best they can. The law permits one rower to stop rowing until the other concedes, and if the rowers manage to make it across the river, the law treats this as the end of the matter and will not allow either rower to seek redress in court unless both rowers clearly agree to stay their dispute until they got to shore. If the river is dangerous the law encourages the rowers to put their dispute to the side and row to safety where a court will hear their dispute and try to set matters right. If a rower stops, he is likely to be held responsible for the resulting loss even if he was in the right on the dispute. The law discourages threats to stop. In extreme circumstances the law permits a rower to lie by pretending to submit to a threat to stop in order to induce the rower making the threat to continue rowing.

The rules of engagement we are about to look at presuppose an honest dispute. Quite different rules kick in if a person makes a dishonest demand for performance or refuses to perform an obligation that he knows is due. Thus a note given to settle a dishonest claim or a release given by a creditor in return for part payment of an undisputed debt may be unenforceable for lack of consideration.⁷⁸ Unjustified non-payment of a debt will strip a debtor of contract rights. For example, it will give the

⁷⁸ Lack of consideration was the argument eventually adopted in *Hackley v. Headley*, 50 Mich. 43, 14 N.W. 693 (1883), to excuse a creditor from a release extracted by the debtor by a threat to withhold money that was not in dispute. For a more recent case in the same mold see *Wickman v. Kane*, 136 Md.App. 554, 766 A.2d 241, 246-247 (2001)(finding no valid accord and satisfaction where undisputed sum was paid to obtain release of a disputed claim on grounds of lack of consideration). The weight of authority is that refusal to pay money even in bad faith is not economic duress. *Selmer Co. v. Blakesell-Midwest Co.*, 704 F.2d 924 (7th Cir. 1983). For an exceptional case to the contrary see *Capps v. Georgia Pacific Corp.*, 253 Or. 248, 453 P.2d 935 (1969).

creditor the right to accelerate future payments.⁷⁹ In Part Two we saw that knowing breach of an indisputable obligation may justify forfeiture. And there is the late twentieth innovation of the tort of bad faith breach of contract. This tort exposes an insurer who unjustifiably denies a claim to liability for emotional distress damages and sometimes punitive damages. Dangerous legal shoals these but they do not threaten if a refusal to perform or a demand for performance is honest. So non-payment of insurance is a tort only if it is in bad faith. The tort of bad faith breach permits an insurer to test a questionable claim in court no matter how hard the decision to fight may be on the insured and no matter how small the claim.⁸⁰

The voluntary payment doctrine is a good place to start. It is an exemplar of the rules that encourage immediate resolution of a dispute when withholding performance will not have ruinous consequences. The doctrine cuts off the claim of a debtor who pays a disputed debt.⁸¹ Its rationale is to ensure “that those who desire to assert a legal right do so at the first possible opportunity; this way, all interested parties are aware of that position and have the opportunity to tailor their own conduct accordingly.”⁸² Other rules cut off the claim of a creditor who accepts part payment. The rules on accord and satisfaction permit what has been described as “an exquisite form of commercial torture.”⁸³ They enable a debtor to tender part payment of a disputed debt that the creditor can take only if he relinquishes his claim for the balance.⁸⁴ And a creditor has

⁷⁹ Couch on Insurance § 232:43. See *Williams v. Mutual Ben. Health & Acc. Ass'n*, 100 F.2d 264, 265 (5th Cir. 1938)(When one who is obligated by contract to make money payments to another, absolutely repudiates and abandons the obligation without just excuse, the obligee is 'entitled to maintain his action in damages at once for the entire default)(Texas law); *Needham v. American Nat. Ins. Co.*, 97 S.W.2d 1016 (Tex. Civ. App. Dallas 1936), writ dismissed.

⁸⁰ William T. Barker, *Evidentiary Insufficiency in Insurance Bad Faith Suits*, 6 Conn. Ins. L.J. 81, 110 (1999).

⁸¹ Restitution and Unjust Enrichment, Tentative Draft No. 1, § 6, comment e (stating that voluntary payment rule will bar recovery of payment of disputed claim) and illustration 18. Reporter's Note e provides authority.

⁸² *Randazo v. Harris Bank Palatine*, 262 F.3d 663, 668 (7th Cir. 2001).

⁸³ James White & Robert S. Summers, *Handbook of the Law under the Uniform Commercial Code* § 13-21, at 544 (2d ed. 1980). This sentiment is echoed in *Horn Waterproofing Corp. v. Bushwick Iron & Steel Co.*, 66 N.Y.2d 321, 326, 488 N.E.2d 56, 59, 497 N.Y.S.2d 310, 313 (1985).

⁸⁴ The history of Uniform Commercial Code § 1-207 attests to the strength of this practice. The statute allows a party to reserve his rights while accepting performance offered by the other party. Though the statute made no exception many courts held this provision did not apply to an accord and satisfaction. Courts had split on whether the statute changed the common law doctrine of accord and satisfaction. *Air Van Lines, Inc. v. Buster*, 673 P.2d 774 (1984), is a leading case holding that the statute did not alter the common law rule. For a contrary case that reviews the arguments and authority on both sides see *Horn Waterproofing Corp. v. Brunswick Iron & Steel Co., Inc.*, 66 N.Y.2d 321, 497 N.Y.S.2d 310, 488 N.E.2d 56 (1985). An explicit exception was added in 1990.

little hope of avoiding a release on ground of duress because of a precept foreclosing claims of financial distress.⁸⁵

The voluntary payment doctrine has the familiar stickiness of an interpretive presumption. Payment is final unless the parties' state clearly that this was not their intent. The rule is sticky in another more unusual way. Under the traditional rule, a debtor cannot avoid the voluntary payment doctrine by saying when he pays that he reserves his right to recover the money.⁸⁶ The rules on accord and satisfaction (and the precept foreclosing a duress claim) are similar in that they prevent the creditor from unilaterally reserving his right to sue for the balance if he takes part payment. The upshot of these rules is that avoiding finality on payment requires both parties' expressed assent.

Another body of rules permits a party to perform or accept performance in a dispute and still have his day in court. The unusual facts of *Henrici v. South Feather Land & Water Co.*⁸⁷ serve to illustrate most of these rules. South Feather assumed a long-

⁸⁵ An often litigated question involves the effectiveness of a release given by a creditor to settle a disputed debt when in exchange for the release the debtor pays a sum that was not in dispute. The weight of the authority is that a release is valid in these circumstances if there is a single debt or closely related debts. *Kilander v. Blickle Co.*, 280 Or. 425, 428-429, 571 P.2d 503, 504-505 (Or. 1977). However there is authority that "circumstances of unfair pressure or economic coercion" cut in the other direction. *Flagel v. Southwest Clinical Physiatrists*, 157 Ariz. 196, 202, 755 P.2d 1184, 1190 (Ariz. App. 1988).

⁸⁶ For clear statements that a reservation of rights does not avoid the voluntary payment doctrine see *Rowe v. Union Central Life Ins. Co.*, 194 Miss. 328, 12 So.2d 431, 433-34 (1943), and 75 ALR 658 (stating that a payment may not be recovered "though the payer makes the payment with an express reservation of his right to litigate the claim.") This rule is codified in Georgia. OCGA § 13-1-13. The Third Restatement of Restitution will take this position.

A handful of cases hold that a reservation of rights avoids the bar of the voluntary payment doctrine. See *Community Convalescent Center Of Naperville, Inc., v. First Interstate Mortgage Company Of Illinois*, 181 Ill. App.3d 996, 999, 537 N.E.2d 1162, 1164, 130 Ill. Dec. 833, 835 (1989) ("since plaintiff paid the 30 days' interest 'under protest,' plaintiff is not barred from recovery under the voluntary-payment doctrine."); *Avianca, Inc. v. Corriea*, 1992 WL 93128 (D.D.C. 1992) ("The voluntary payment doctrine does not generally apply, however, when a party has expressly reserved a right to take some legal action or when the party has paid under protest.") A few other cases state in dicta that a debtor could have reserved his rights. *Prenalta Corp. v. Colorado Interstate Gas Co.*, 944 F.2d 677 (10th Cir. 1991); *Randozo v. Harris Bank Palatine, NA*, 262 F.3d 663, 671 (7th Cir. 2001); *Getto v. City of Chicago*, 86 Ill.2d 39, 49, 55 Ill.Dec. 519, 426 N.E.2d 844 (1981); *Putnam v. Time Warner Cable of Southeastern Wisconsin*, 274 Wis. 2d 41, 59, 663 N.W.2d 254, 263 (2001); *City of Miami v. Keton*, 115 So.2d 547, 552 (Fla.1959).

The older cases tend to treat a protest as evidence of duress. This comes from framing the issue as a problem in restitution. If the issue is framed as a problem in contract, then the question is what it takes to establish an agreement by the payee that the payment is conditional upon the validity of his claim. Such an agreement avoids the bar of the voluntary payment doctrine. See Restatement of Restitution § 45, comment e, ("The rule stated in this Section does not apply if the parties have agreed that the payment is conditional upon the validity of the transferee's claim.") The general principle that the offeror is master of the offer supports the conclusion that if the payor conditions payment on a reservation of rights than the payee acquiesces in that when she accepts the payment. *Prenalta Corp.* approaches the issue on this basis.

⁸⁷ 177 Cal. 442, 170 P. 1135 (1918).

term contract to supply water to Henrici's farm. It proposed a new pricing scheme that would have slightly increased Henrici's payments. It was not clear South Feather had this right. Henrici refused to take water on the new terms and allowed his farm to wither. He had no other source of water for irrigation. The case holds that even though Henrici was in the right on the dispute he could not recover for the damages to his farm because he should have mitigated damages by taking the water and later suing to recover the over-payment.⁸⁸ Crucial to the decision is the court's assumption that Henrici would not have waived his right to challenge price had he taken the water and paid what South Feather asked. While the court did not explain presumably it would have allowed a restitution claim by Henrici to recover the over-payment. I will say more about this claim shortly.

Changing the facts in *Henrici* brings to the fore several rules that encourage cooperation in a dispute when non-cooperation would be harmful. What would have happened had South Feather told Henrici that taking the water constituted acceptance of the new price and a waiver of his claim to the old price? This is the accord and satisfaction gambit. It is clear that Henrici could recover for his losses if he refused the water and was in the right on price. His duty to mitigate would not require him to relinquish his claim of a right to pay less.⁸⁹ By casting the loss back on South Feather the rule punishes South Feather for escalating the dispute.

Moreover, under UCC § 1-308⁹⁰ Henrici might still be able to take the water and reserve his rights by saying he was doing so notwithstanding South Feather's insistence that taking the water means he relinquishes the claim.⁹¹ This response enables Henrici to test South Feather's resolve because South Feather would have to follow through on its threat to stop delivery of water. The law might even allow Henrici to deceive South Feather to defuse the conflict. If Henrici agreed to South Feather's demand to get water

⁸⁸ As we shall see, Henrici had another option. He might have tendered the old price pending resolution of the dispute. Had South Feather responded to this tender by cutting off the water supply that would be a material breach by it and it would be responsible for the damage to Henrici's farm. Henrici's tender of the old price would not be a material breach by him justifying suspension of performance by South Feather because any loss from under-payment is easily compensated should South Feather be in the right. Further, Henrici's tender of the old price is in good faith. In sum, Henrici had two choices in the case – he could pay either the new or the old price pending resolution of the dispute – between which the law is indifferent. This is sensible for, putting issues like insolvency and collection to the side, there is no reason to prefer one party over the other when we ask who should hold money in dispute pending resolution of the dispute.

⁸⁹ Contracts 2nd § 350, comment e (“If the party in default offers to perform the contract for a different price, this may amount to a suitable alternative. But this is not the case if the offer is conditioned on surrender by the injured party of his claim for default.”), and Illustration 15, which is based on *Gilson v. F.S. Royster Guano Co.*, 1 F.2d 82 (3d Cir. 1924). See also Corbin on Contracts § 1043 at 274-275 (stating that there is no duty to take substitute performance from defaulting party if it would involve a surrender of rights, compromise, or accord and satisfaction).

⁹⁰ Former § 1-207.

⁹¹ UCC § 1-308 (formerly § 1-207). This is implicit in the line of cases holding that a creditor could use 1-207 to take payment offered in satisfaction and then sue for the balance.

he desperately needed he might be able to avoid the contract by claiming duress. South Feather's threat to withhold water is border-line extortion and a core instance of bad faith because the threatened act would inflict a large loss on Henrici while yielding a small benefit to South Feather.⁹² The doctrine of duress and UCC § 1-308 in effect allow a party unilaterally to dictate that performance is not final to preserve a claim of right. This is the mirror image of the voluntary payment rule and its associates, which require both parties express assent to preserve a claim.

There is more. Even if South Feather was in the right in the underlying dispute, its refusal to deliver the water unless Henrici relinquished his claim of a right to the old price would likely be considered a material breach by South Feather. It would have no right to withhold the water though Henrici persisted in paying the old price because the slight underpayment would not be a material breach by Henrici. Often when a contractual relationship breaks down it is a result of reciprocal escalation of a dispute. In this situation a court may assign the entire loss from the breakdown to one party by holding that he was the first to materially breach the contract. This will be whoever the court believes inappropriately escalated the dispute. As the result in *Henrici v. South Feather Land & Water Co.* illustrates, it need not be the party who is in the wrong in the underlying dispute.

*K&G Construction Co v Harris*⁹³ shows how the doctrine of material breach assigns the loss to the party who inappropriately escalates a dispute. Harris had a contract with K&G to excavate and move dirt in K&G's multi-house construction project. Harris' bulldozer damaged a house and Harris and his insurer denied liability. In response, K&G withheld progress payments totaling less than the amount of its claim. Harris in turn stopped work and K&G hired another company to finish the job. Both parties suffered a loss. K&G paid the substitute more than it would have paid Harris; Harris lost the profit he would have made completing the job. If the court thought that K&G acted inappropriately in withholding progress payments, then it could hold this was a material breach. Harris would then have been in the right in leaving the job and he would recover his lost profits. Instead the court concluded that Harris materially breached the contract when it withdrew from the job. K&G recovered the additional cost of the substitute.

In cases like *K&G Construction* the question may arise whether a party's honest but incorrect belief that he is acting within his rights is relevant to determining the quality of his breach. Two apparently contradictory propositions bracket the answer. One is

⁹² Restatement, Second, of Contracts, § 176(2)(a) defines a threat as improper "if the resulting exchange is not on fair terms" and "the threatened act would harm the recipient and would not significantly benefit the party making the threat." *Silsbee v. Webber*, 171 Mass. 378, 50 N.E. 555 (1898)(threat by employer directed at employee's mother to tell his ill-father of his theft if mother did not payoff the loss), is an example in the blackmail mold. John Dawson, *Economic Duress—An Essay in Perspective*, 45 Mich. L. Rev. 253 (1947), proposes disproportionality as an organizing principle.

⁹³ 223 Md 305, 164 A2d 451 (1960).

from the Second Restatement of Contracts: “Generally, a party acts at his peril if, insisting on what he mistakenly believes to be his rights, he refuses to perform his duty.”⁹⁴ The other is from Corbin: “Disputes often arise as to what performance the contract requires; and the plaintiff’s default is not willful if he performs in accordance with his own honest interpretation, even though he knows the other party holds a different one.”⁹⁵ Each proposition is true to a point. The apparent contradiction largely disappears once you realize they are speaking of different responses to breach.⁹⁶ The

⁹⁴ Contracts 2nd, § 250 (When a Statement or an Act Is a Repudiation), comment d. Illustration 9 states that A’s good faith belief that he is not obligated to deliver a deed until August 1 does not protect A when he threatens not to deliver the deed at all unless B agrees to accept it on August 1 rather than July 30, the date the deed is actually due to be delivered. The example misfires. The threat may be inappropriate even if A is correct in his belief that the deed is not due until August 1.

⁹⁵ 5A Corbin on Contracts § 1123, p. 9 (1964). Corbin does not cite case authority. For some see *W. J. Walker v. Shasta Minerals & Chemical Co.*, 352 F.2d 634, 638 (10th Cir. 1965); *Golf Carts, Inc. v. Mid-Pacific Country Club*, 493 P.2d 1338, 1340 (Haw.1972); *Hanson v. Duffy*, 106 Ill.App.3d 727, 62 Ill.Dec. 401, 435 N.E.2d 1373, 1378 (1982); *Berke & Co. v. Griffin, Inc.*, 116 N.H. 760, 765, 367 A.2d 583, 586-587 (1976); *Kiriakides v. United Artists Communications, Inc.*, 440 S.E.2d 364, 367 (S.C. 1994). *New York Life Ins. Co. v. Viglas*, 297 U.S. 672, 676-77 (1936), famously holds that an insured cannot accelerate payments due under an insurance policy when the insurer fails to make a payment in the honest belief it is not due. Cardozo explains:

“Repudiation there was none as the term is known to the law. Petitioner did not disclaim the intention or the duty to shape its conduct in accordance with the provisions of the contract. Far from repudiating those provisions, it appealed to their authority and endeavored to apply them. . . . If it made a mistake, there was a breach of a provision of the policy with liability for any damages appropriate thereto. We do not pause at the moment to fix the proper measure. Enough in this connection that at that stage of the transaction there had been no renunciation or abandonment of the contract as a whole.”

The converse proposition is that bad faith in an offer of performance is a reason for treating the offer as a material breach. For authority see *Peter Kiewit Sons' Co. v. Summit Constr. Co.*, 422 F.2d 242, 257 (8th Cir. 1969)(“ Kiewit's meager offer of \$143,000 on June 29 as compensation for all the extra backfill work is so lacking in good faith as to constitute a repudiation of the Subcontract. * * * Kiewit's lack of good faith is evident from its \$143,000 offer, which was but 10 per cent of Summit's estimate”); *Pacific Coast Eng'r Co. v. Merritt-Chapman & Scott Corp.*, 411 F.2d 889 (9th Cir. 1969)(holding that persistent assertion of position party had been told by third parties was unjustified is a repudiation).

⁹⁶ Corbin’s proposition should be distinguished from the proposition that the presentation of a wrong claim or demand in good faith standing alone is not a breach of contract. *Reiss v. Murchison*, 503 F.2d 999 (9th Cir. 1974), cert denied 420 U.S. 993 (1975)(holding that the filing of a claim of total breach does not give the party against whom the claim is asserted the right to halt performance); *Oak Ridge Const. Co. v. Tolley*, 351 Pa.Super. 32, 504 A.2d 1343, 1348 (1985); *Dixie Roof Decks, Inc. v. Borggren/Dickson Const., Inc.*, 195 Ga. App. 881, 395 S.E.2d 19 (1990); *In re Chateaugay Corp.*, 104 B.R. 637 (S.D.N.Y. 1989). Similarly, it is not a breach of contract or a tort to use legal process to resolve a dispute or to protect one’s position pending resolution even though the use of process harms the other party at least so long as the process is used in good faith. *Wachter v. Gratech Co., Ltd.*, 608 N.W.2d 279, 288-289 (ND 2000)(holding that it is not abuse of process to file a mechanic’s lien that turned out to be grossly excessive in amount if the filing was done in good faith).

Restatement speaks to whether a defaulter's belief that he performed his obligation saves him from liability to the other for damages. The answer generally is no. Corbin speaks to whether a defaulter's belief that he performed his obligation is relevant to deciding whether his breach was material giving the other the power to exit. The answer is yes, but it is only one factor among several.

The boundaries between these competing rules of engagement for contract disputes are not well defined. There is little in the voluntary payment rule to preclude its application had Henrici paid what South Fork demanded.⁹⁷ The best argument is that Henrici's payment is not voluntary, but this argument runs into the counter-arguments that South Fork did nothing improper in demanding a payment it thought within its rights and that Henrici had other options that would have adequately protected his interests. One court has drawn a boundary between the rule in UCC § 1-308(1),⁹⁸ which allows a party to perform or accept performance in a dispute while reserving his rights, and the common law rule of accord and satisfaction, which does not. The case holds that § 1-308(1) applies in a continuing dispute on an executory contract.⁹⁹ This is a bit overbroad. It means that Henrici could not try to force a settlement on his terms by tendering a check for the old price in satisfaction, which seems right.¹⁰⁰ But it also means that a lessee could never rely on payment in satisfaction to resolve a dispute over past rent on a continuing lease. A concern with threats that would inflict disproportionate harm if carried out is an important strand in the law of duress.¹⁰¹ As you shall see, this gets at the

Two of these propositions clash in *Woodar Investment Development Ltd. v. Wimpey Constr. U.K. Ltd.*, House of Lords [1980] 1 W.L.R. 277; [1980] 1 All E.R. 571. Lord Wilberforce echoes the proposition just above: "it would be a regrettable development of the law of contract to hold that a party who bona fide relies on an express stipulation in a contract in order to rescind or terminate a contract should, by that fact alone, be treated as having repudiated his contractual obligations if he turns out to be mistaken as to his rights." Lord Salmon, quoting Lord Denning in an earlier case, echoes the Restatement: "I have yet to learn that a party who breaks his contract can excuse himself by saying that he did it on advice of his lawyers; or that he was under an honest misapprehension. Nor can he excuse himself on these grounds from the consequences of a repudiation."

⁹⁷ Palmer argues that doubt about a debt should not always bar recovery of a payment. He cites *Pilot Insurance Co. v. Cudd*, 208 S.C. 6, 36 S.E.2d 860 (1945), where an insurer was allowed to recover death benefits paid for a sailor missing at sea after the government issued a certificate stating the insured "is presumed to have died." A policy favoring quick payment of insurance claims is said to support such decisions. As important is the war-time setting, which makes it impractical for the insurer to investigate the claim to resolve the uncertainty. Palmer adds that the result should be otherwise if the insurer paid less than in full for that would suggest the payment was a compromise of a disputed claim. George E. Palmer, *Law of Restitution* § 14.7.

⁹⁸ Formerly § 1-207(1).

⁹⁹ *Air Van Lines, Inc. v. Buster*, 673 P.2d 774 (1984).

¹⁰⁰ The concern is that after rightfully rejecting the check South Feather would halt delivery of water for total non-payment.

¹⁰¹ Restatement, Second, of Contracts § 176(2)(a), defines a threat as improper "if the resulting exchange is not on fair terms" and "the threatened act would harm the recipient and would not significantly

crucial factor. But the law of duress is quite fuzzy once one gets beyond a few core cases of classically wrongful threats, and there are cases stating categorically that “it is not duress for a party to insist upon what he believes to be his legal rights.”¹⁰²

A rule proposed in a draft of the Restatement Third of Restitution and Unjust Enrichment identifies the key factor. The rule addresses the case where a party renders a performance he disputes he owes and later brings a restitution claim to recover its value. The rule allows the restitution claim but only if nonperformance by either party would impose consequential harms.¹⁰³ In cases covered by the voluntary payment rule, which cuts off the restitution claim, withholding payment imposes no such harm. This rule supplies a basis for the restitution claim in *Henrici v. South Feather Land & Water Co.* An article I published in 2002 proposes such a rule and makes a doctrinal and policy argument for it.¹⁰⁴ That article also shows that the rule is an alternative basis for many cases that allow a party to rescind a contract and recover damages for the cost of his performance when such cost is in excess of the contract price, including the notorious *Boomer v. Muir*.¹⁰⁵ In a substantial majority of the cases in which the optional restitution claim is used to recover costs exceeding the contract price the cost overrun is attributable to the other’s breach.

Whether a party’s decision to withhold or refuse performance imposes a consequential loss is decisive in the assignation of fault under the rules of material breach and mitigation when parties escalate an honest dispute. You will recall *K&G Construction*. A subcontractor damaged the general contractor’s property and denied legal responsibility. The general contractor withheld progress payments totaling less than the amount of its claim. The subcontractor then stopped work forcing the general contractor to hire another firm to do the work. The court cast the loss on the subcontractor. The rules on material breach and mitigation compel the result. In the absence of bad faith, the rules on material breach and mitigation ask a court to balance a party’s need to withhold or refuse performance to avoid suffering an uncompensated loss with the resulting burden on the other party. Neither the subcontractor’s denial of responsibility for the damage to the property nor the general contractor’s withholding of money due was a material breach because there was no net loss from the delay in payment and each party’s individual loss could easily be compensated. The

benefit the party making the threat.” Comment f misfires by suggesting the concern is with malice or vindictiveness rather than with coercion. Illustration 12 gives as an example an employer’s threat to prevent an employee from working elsewhere if he does not release a claim. The employer makes the threat for his own gain and not out of malice. If he carries out the threat he probably does it to retain his credibility.

¹⁰² *Jacobs v. Atlantco Ltd. Partnership No. 1*, 36 Md. App. 335, 347, 373 A.2d 1255, 1261 (1977).

¹⁰³ Restatement Third Restitution and Unjust Enrichment, Council Draft No. 5, § 35, comment b.

¹⁰⁴ Mark P. Gergen, *Restitution as a Bridge Over Troubled Contractual Waters*, 71 *Fordham L. Rev.* 79 (2002).

¹⁰⁵ 24 P 2d 570 (Cal App 1933).

subcontractor's abandonment of the job was both a failure to mitigate damages and a material breach because it caused a significant joint net loss. The common principle is that performance or acceptance of performance in a dispute is not final – it will not cut off a claim that less was owed or more was due – if the performance or acceptance of performance avoids a consequential or joint loss.

5. Is there a right to exit from an uncertain contract?

The rules discussed in Part Four speak to when a person may perform (or accept performance) in a dispute and later bring a claim for reimbursement (or damages) asserting that his obligation was less (or his right more). We saw that the law generally permits a person to perform and then litigate when performance avoids a loss and does not unduly complicate the litigation. This part looks at the other side of the coin. What effect, if any, does uncertainty about rights have on the law's response to exit? There is not the same clear pattern as in the law's response to loyalty.

Imagine in *Parker* that it was uncertain whether the studio had the power to substitute Big Man, Big Country for Bloomer Girl. Does this uncertainty affect the evaluation of the reasonableness of MacClaine's refusal to do the second role even if the underlying issue is resolved in her favor? The loose structure of the doctrine of material breach – the defaulter's good faith is one factor among several with no assigned weights – makes this possible in theory but impossible to tell in practice. In the cases I know of where courts do grasp the nettle, holding that a person was in the right on the disputed point but in the wrong in exiting a contract, exit was not necessary to vindicate the disputed right.¹⁰⁶ But no negative inference should be drawn from this. A judge who thinks it unreasonable for a person to withhold or refuse performance in response to the other's performance may avoid the nettlesome issue by finding there was no breach. The uncertain nature of the right always leaves this door open.¹⁰⁷

Rules that allow judges to decline to enforce uncertain obligations provide another out. The indefiniteness doctrine, which has fallen on hard times,¹⁰⁸ is one such rule. Formal requirements for a contract (e.g., the statute of frauds) or for assent (e.g., the

¹⁰⁶ *Henrici v. South Feather Land & Water Co.*, 177 Cal. 442, 170 P. 1135 (1918), is an example. The case is discussed supra at nn. xxx – xxx. In *Golf Carts, Inc. v. Mid-Pacific Country Club*, 493 P.2d 1338 (Haw.1972), the dispute was over money and nothing in the opinion suggests that delay in payment posed a greater risk of default to the creditor.

¹⁰⁷ *Jacob & Youngs v. Kent*, 230 N.Y. 239, 129 N.E. 889 (1921), is a famous example. This strategy is crystallized in the presumption against interpreting a term as a condition when it would result in forfeiture.

¹⁰⁸ UCC 1-204(3). *Denver D. Darling, Inc. v. Controlled Environments Construction, Inc.*, 89 Cal. App. 4th 1221, 1238, 108 Cal. Rptr.2d 213, 224-225 (2001), is more in tune with the modern approach to indefinite agreements, though like Judge Posner in *C.L. Maddox*, the court abjured deciding who had the better case on the underlying dispute. The case holds that in a dispute where a contract is so indefinite that it is not fair to say that either party was in the wrong a court should be flexible and try to fashion a remedy that will "effect justice under the circumstances" to both parties.

mirror image rule) eliminate other sources of uncertainty. They too have fallen on hard times.

C.L. Maddox, Inc. v. Coalfield Services,¹⁰⁹ in an opinion by Judge Posner, is noteworthy because it blesses exit in the face of contract uncertainty without relying on the old doctrines. Maddox subcontracted with Coalfield to do underground mine demolition work at a price of \$230,000. Coalfield faxed a contract stating that it would do the work in three weeks provided it could work day and night seven days a week. Maddox asked for and got a change in a term that was irrelevant to the eventual dispute and said that it would sign and return the contract. This it never did despite repeated requests by Coalfield. Coalfield worked for over two weeks and found the work going much slower than expected partly because it could not work Sundays. Coalfield estimated the job was 45 percent complete at this point and submitted its first bi-weekly bill. At the same time it pulled its men off the site. It is not clear how much this stoppage delayed work.¹¹⁰ Maddox offered to pay the amount requested less 10 percent but asked Coalfield to sign a letter agreeing to extend the deadline by one week and to pay \$1,000 liquidated damages per day after this deadline.¹¹¹ Coalfield refused to go back to work on these terms telling Maddox that the job would take five to six more weeks to finish. The trial judge initially concluded that Coalfield broke the contract, but he got qualms about this conclusion and passed the case over to a magistrate, who decided that Maddox broke the contract. The court of appeals affirmed with Judge Posner writing for the court. The specific factual and legal arguments for the result do not stand up, though unreported facts may well justify thinking Maddox more at fault in the affair though it was Coalfield that walked.¹¹²

¹⁰⁹ 51 F.3d 76 (7th Cir. 1995).

¹¹⁰ Coalfield argued that it could have put men back to work immediately. Posner inferred that the stoppage entailed at least an eight day delay based on a Coalfield fax. 51 F.3d at 80.

¹¹¹ It is not clear from the opinion how strongly Coalfield insisted upon this. On this potentially crucial point the opinion says: “he appeared to condition this promise [to pay the invoice] on Coalfield’s signing an ‘acceptance letter’ that Maddox enclosed.” 51 F.3d at 78.

¹¹² Judge Posner concluded “that the most plausible interpretation of Maddox’s action is that it was seeking excuses for not paying Coalfield anything.” 51 F.3d at 80. Maddox’s failure to sign and return the contract hardly suggests this. Given Maddox’s acquiescence in Coalfield starting no one could reasonably question that there was some sort of contract under which Maddox would pay for the work that was done. Nor does the letter “demanding” that Coalfield agree to pay liquidated damages support Judge Posner’s conclusion. Maddox offered to pay for the work done less 10 percent of the contract price. Liquidated damages were only \$1,000 per day. Had the job taken the eight weeks predicted by Coalfield liquidated damages would have been \$28,000 on a \$230,000 contract.

The decision is on weak legal grounds as well. Judge Posner was forced to rest on UCC § 2-609 because he reasoned that the stoppage occurred before the demand letter. This provision allows a person to suspend performance if he asks for and does not get adequate assurances when he has reasonable grounds for insecurity regarding the other’s performance. The difficulty with this argument is that the only basis for insecurity was Maddox’s failure to sign and return the form contract and the only demands for

What is striking about the case is that Judge Posner refused to decide who was in the right in the underlying dispute, which turned on whether Coalfield had promised to do the work in three weeks and whether Coalfield had a legal excuse for falling behind. Maddox had raised the general issue by arguing that Coalfield seized upon the demand letter to get out of what it knew was a losing contract. Judge Posner rejected the argument reasoning that how litigation under the contract would have come out was uncertain.¹¹³ Also striking is Judge Posner's argument that Coalfield was justified in halting work once litigation loomed because of the risk of a screwy result in litigation.¹¹⁴ His reasoning treats parties to a contract who dispute a material term in good faith as if they had no contract. The upshot is that a party has no duty to incur substantial costs in the face of legal uncertainty.

*Hope's Architectural Products, Inc., v. Lundy's Construction, Inc.*¹¹⁵ is an example of a very different response to exit in the face of uncertainty. Lundy's hired Hope's to manufacture custom-build window fixtures for a school construction project. Production was to take twelve to fourteen weeks but it was delayed for reasons that Hope's claimed were outside its control. In late September Lundy's requested that installation begin by October 19. Lundy's repeated this demand on October 14 and threatened to charge liquidated damages for delay though the contract did not provide for liquidated damages. Hope's shipped the windows on October 28 to be delivered on November 4. On November 1, Lundy's again called Hope's asking where the windows were and warning that there might be a substantial back-charge.¹¹⁶ Hope's responded by

assurances were Coalfield's requests that the contract be signed. This puts a great deal of weight on nonperformance of an act that is often a formality.

The opinion does not disclose the contents or tenor of Coalfield's repeated requests that the contract be signed. Perhaps those requests made it clear that getting the signed contract was important to Coalfield, which it might well have been because the contract had terms, such as an indemnity clause, protecting Coalfield from significant risks of doing underground mine work. If this is so, then Coalfield's decision to walk is more reasonable.

¹¹³ 51 F.3d at 81-82.

¹¹⁴ 51 F.3d at 80 ("Every day that Coalfield continued working, it put itself further in Maddox's power. Had it finished the job it would have found itself owed \$230,000 with no leverage over Maddox to extract the money short of a suit to enforce what, depending on Mr. Maddox's testimony and its reception by a jury, might be merely a vague oral contract.")

¹¹⁵ 781 F. Supp. 711 (D. Kans. 1991). The prologue to the decision says a fair amount about the judge's approach:

"This case presents a familiar situation in the field of construction contracts. Two parties, who disagreed over the meaning of their contract, held their positions to the brink, with litigation and loss the predictable result of the dispute. What is rarely predictable, however, (and what leads to a compromise resolution of many construction disputes when cool heads hold sway) is which party will ultimately prevail. The stakes become winner-take-all." 781 F. Supp. at 711-712.

¹¹⁶ Hope's said a 20 percent back-charge was threatened. Lundy's said a back-charge of an unspecified amount was discussed. 781 F. Supp. at 712.

refusing to deliver the windows unless the contract price was first paid in full, placed in escrow, or given to the architect. Lundy's refused saying it could not get the money on short notice from the school district. Hope's did not deliver the windows and Lundy's bought substitutes elsewhere. Hope's sued for the contract price.¹¹⁷ Hope's disputed the delivery date, whether time was of the essence, and excuse. The court resolved each point against Hope's.¹¹⁸ A decision for Lundy's followed with two more steps. The court reasoned that Hope's default gave Lundy's the right to withhold damages¹¹⁹ and that this made Hope's demands for pre-payment in full unreasonable.¹²⁰ Presumably the result would have been different had Hope's been in the right in claiming that the two-week delay in delivering the window's was not a breach of contract or at least not a material breach. Then Lundy's would have been acting unreasonably in threatening to charge liquidated damages (which it would have no right to do) making Hope's demands for pre-payment more reasonable.

C.L. Maddox and *Hope's Architectural Products* appear irreconcilable.¹²¹ *C.L. Maddox* says that uncertainty about a contract may justify walking. *Hope's Architectural Products* proceeds from the premise that a person who stands on uncertain rights to justify withholding performance gambles. If he is found to be wrong on the underlying dispute, then he will be made to bear the resulting loss. In *Hope's Architectural Products*, the judge decided who was in the right on the underlying dispute, and then he used that information to evaluate the reasonableness of what each party did to protect his rights. In *C.L. Maddox*, Judge Posner asked what was reasonable conduct in light of contract uncertainty. He did not try to resolve the underlying dispute. Neither decision can be dismissed. *Hope's Architectural Products* is a thoughtful decision by a trial judge who conscientiously works through the arguments. *C.L. Maddox* is a typically bold and argumentative decision by Judge Posner.

The unusual path taken by Judge Posner in *C.L. Maddox*, if taken in other cases, could grow into a doctrine that could come to occupy a space opened up by the decline of doctrines that preclude or limit enforcement of uncertain contracts. Before the Uniform Commercial Code, Judge Posner could have found no contract by invoking the mirror

¹¹⁷ It is mistake to infer from the absence of a counter-claim by Lundy's that Lundy's suffered no loss from having to purchase the windows from another source. Lundy's might not have filed a counter-claim fearing that would raise the issue of whether it should have mitigated damages by taking the windows from Hope's.

¹¹⁸ 781 F. Supp. at 714-715.

¹¹⁹ UCC § 2-717 gives a buyer this right. There is no case law explicitly addressing whether this provision protects a buyer who withholds payment wrongly but in good faith.

¹²⁰ The court analyzed the demand as a demand for reasonable assurances under UCC § 2-609. There is authority that a party in default cannot invoke § 2-609. See *Palmco Corp. v. American Airlines, Inc.*, 983 F.2d 681 (5th Cir. 1993).

¹²¹ The two cases have one feature in common. In both cases the law left the parties where it found them.

image rule or by ruling that the contract was conditioned upon Maddox returning Coalfield's form.¹²² This new doctrine would bless exit when uncertainty makes it reasonable to walk away from a contract. It could take several forms. It might resemble the rules governing preliminary judicial remedies, which weigh the probability that a right will be established and the risk of irreparable injury if the right is not respected. Or it might condemn a threat to walk away from a relationship to coerce the other to surrender his claim of right. Or it might require people to work together despite uncertainty when the gains from cooperation are large. The common thread is the interest in efficient performance. These formulations differ in how they treat uncertain rights. The first discounts an uncertain right. The second protects claims of right so they can be presented to a court. The third is agnostic about uncertain rights.

6. Conclusion

The rules that regulate exit and loyalty in contract disputes show the common law method at its best and worst. I know of few areas in the common law that are so muddled. The common law got off on a very bad foot in dealing with these problems.¹²³ Much of the relevant law is organized around the law's response – e.g., restitution, estoppel, discharge, and waiver – rather than the conduct that provokes that response.¹²⁴ And we are uncomfortable with some of the theoretical issues raised in these cases. We are uncomfortable sacrificing rights to prudential concerns. And we are uncomfortable with the idea of uncertain rights.¹²⁵ Still judges seem to do a fine job despite the clumsy doctrinal tools. They do a better job than theoreticians who come to the cases with larger points to make. They do fine job because the relevant interests – to execute the bargain with the least cost and fuss – are intuitive.

¹²² UCC 2-207(3) clearly forecloses the first argument and probably forecloses the second.

¹²³ Consider Williston's qualms over allowing a claim to be brought on a repudiated contract before the time of performance. Williston, *Repudiation of Contracts*, 14 Harv. L. Rev. 421, 428 (1901). Or the odd response of implying a subsidiary promise not to do anything inconsistent with the obligation. *Hochster v. De La Tour*, 118 Eng. Rep. 922, 926 (Q.B. 1853).

¹²⁴ Peter Birks, *Unjust Enrichment and Wrongful Enrichment*, 79 Tex. L. Rev. 1767 (2001), makes a related but more general point that the general headings of law should be organized around the causative event (Contract, Wrong, Unjust Enrichment, and Miscellany) and not the law's response (not Restitution).

¹²⁵ It might be better if we could purge the term rights from the analysis and speak instead of relevant interests. Peter Westen, *The Rueful Rhetoric of Rights*, 33 UCLA L. Rev. 977, 996-1008 (1986), explores how the confusion between the two distinct meanings of rights – rights as entitlements and rights as legally protected interests – confounds the analysis of unconstitutional conditions.