Contracts in the Sixth Circuit - 1998

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*Columbia University, L.L.M., 1989; J.D. Indiana University - Indianapolis, 1983. Professor of Law, Michigan State University - Detroit College of Law. This article is the better for my many conversaions with Charles Consaulus, my late colleague who generously shared his insights from many years as a contracts teacher. His off-beat perspective and irreverent wit will be sadly missed. I owe much to my colleague Mae Kuykendall, President of the Barrett Society, for her inspiration, encouragement and insight. I am also indebted to Carol Parker for her expert and swift responses to my research requests and Chad DePetro for his able research assistance.

1. 135 F.3d 1077 (6th Cir. 1998).
2. 145 F.3d 755 (6th Cir. 1998).
3. 139 F.3d 1080 (6th Cir. 1998).
4. 135 F.3d 1069 (6th Cir. 1997).
5. 135 F.3d 421 (6th Cir. 1998).
6. 158 F.3d 354 (6th Cir. 1998).
7. 139 F.3d 1080 (6th Cir. 1998).
8. 143 F.3d 1013 (6th Cir. 1998).
9. 146 F.3d 367 (6th Cir. 1998).
INTRODUCTION

During the survey period, November 1, 1997 to October 31, 1998, the Sixth Circuit considered an array of contract issues, spanning a gamut from intent to contract to time limits on actions for breach. While many opinions during this period include references to contract, sometimes brief or tangential, this survey addresses only those cases which, in the author's view, raise predominant or otherwise noteworthy contract issues, usually in the context of a traditional contract cause of action.

Especially interesting are three opinions in which the Sixth Circuit concluded that the statute of frauds barred enforcement of alleged oral agreements, demonstrating the continuing viability of this much-maligned doctrine. Also interesting is the Sixth Circuit's repeated invocation of the "plain-meaning rule" in several cases involving disputed contract terms. Noteworthy also is the court's reference to the "meeting of the minds" test of intent to contract, its relaxed distinction between contract and tort, and its restrictive definition of a requirements contract.

10. 135 F.3d 1077 (6th Cir. 1998).
11. 135 F.3d 421 (6th Cir. 1998).
12. 142 F.3d 926 (6th Cir. 1998).
13. 146 F.3d 398 (6th Cir. 1998).
14. 154 F.3d 573 (6th Cir. 1998).
15. 133 F.3d 433 (6th Cir. 1998).
I. ENFORCEABILITY OF PROMISES

A. Intention to be Bound

_Tschira v. Willingham_\(^{16}\) involved a sale of property in Tennessee to Klaus and Gerda Tschira, German residents. The seller, Corim, Inc., through its president, Willingham, had offered to obtain buildings in the southeastern United States for purchase at a "fair market price." Corim allegedly planned to realize a profit by subsequently leasing these properties from their new owners and then subleasing them to third parties at higher rental rates. In 1990, the Tschiras agreed to buy from Corim a piece of property in Nashville, at a price of $1,985,000. The parties' agreement was evidenced by a letter from Willingham to the Tschiras. This letter, transcribed in German, and originally drafted by the Tschira's tax advisor, characterized the nature of the parties' relationship\(^{17}\) and specified that German law would govern.\(^{18}\)

Several years later, the Tschiras discovered Corim and Willingham had purchased the Nashville property for $774,000, through a shell company, on the same day they sold it to the Tschiras, thus recognizing "an instant profit of $1,211,000."\(^{19}\)

The Tschiras consequently brought an action against Corim and Willingham, charging breach of fiduciary duty and intentional misrepresentation.\(^{20}\) Applying German law, the district court found a fiduciary relationship between the parties and so instructed the jury, which returned a verdict for the Tschiras.\(^{21}\)

On appeal to the Sixth Circuit, Corim and Willingham initially argued that the district court improperly applied German law to the controversy. Willingham's letter was not a binding choice-of-law agreement invoking German law, they urged, because Willingham had no intent to contract and the requisite "meeting of the minds" was therefore lacking.\(^{22}\)

The Sixth Circuit rejected Willingham's argument, quoting his trial testimony, which included the following statement:

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16. 135 F.3d 1077 (6th Cir. 1998).
17. See _id._ at 1080-81. The interpretation of the German word used to define the parties' relationship was hotly disputed. See _infra_ text accompanying notes 20-25.
18. See _id._
19. _Id._ at 1081.
20. _Tschira_, 135 F.3d at 1081. The misrepresentation claim alleged that Corim and Willingham fraudulently misrepresented the fair market value of the property and made false statements regarding coverage under title insurance and liability policies. _Id._ at 1087-88.
21. See _Tschira_, 135 F.3d at 1082.
22. _Tschira_, 135 F.3d at 1083.
[The Tschira's tax advisor] felt like the contract should be governed under German law and that's my interpretation of the sentence that refers to the purchase agreement, which is to be concluded, will be subject to German law. I saw nothing to our detriment in that. We fully intended to live up to the letter and spirit of that contract, and did.23

Willingham's testimony, concluded the court, demonstrated his intent that the letter be binding and German law apply. Although the court cited Willingham's "meeting of the minds" test, it did not address the legitimacy of this test, which has been harshly criticized.24

B. Policing the Agreement

1. Misrepresentation, Fraud

In Menuskin v. Williams,25 a development corporation ("DWCC")26 sold several properties which were encumbered by a construction lien, contrary to the sales contract and warranty deeds. Upon discovering the encumbrance, the purchasers sued DWCC, the title company (National Title) and its attorney (Sartain) who prepared the warranty deeds.27 Included among the purchasers' claims was a claim for fraud and misrepresentation.

23. Id.
24. See E. ALLAN FARNSWORTH, CONTRACTS § 3.6 (3d ed. 1999) (characterizing "meeting of the minds" as a much-abused metaphor and urging its abandonment). Criticism of "meeting of the minds" as a test of intent to contract stems fundamentally from its suggestion that intent depends on an actual (subjective) assent to be bound. As Judge Learned Hand explained in 1911:

A contract has, strictly speaking, nothing to do with the personal, or individual, intent of the parties. A contract is an obligation attached by the mere force of law to certain acts of the parties, usually words, which ordinarily accompany and represent a known intent. If, however it were proved by twenty bishops that either party when he used the words intended something else than the usual meaning which the law imposes on them, he would still be held, unless there were mutual mistake or something else of the sort.

25. 145 F.3d 755 (6th Cir. 1998).
26. See id. at 759. The corporation's full name was Don Williams Construction Company.
27. See id. at 761. The purchasers' claims against Don Williams were previously settled.
claims were charges of breach of contract and breach of warranty. The district court entered summary judgment for all defendants on these two claims. 28

On appeal to the Sixth Circuit, the purchasers argued that DWCC employees, National Title and Sartain were liable under Tennessee contract law for falsely representing that the title was unencumbered. The Sixth Circuit rejected this contract claim, finding no contractual relationship between the purchasers and defendants. DWCC employees, the court reasoned, acted as known agents of DWCC and thus were not themselves contractually bound to the purchasers. As for National Title and Sartain, no evidence established an agreement between these defendants and the purchasers. 29

The Sixth Circuit also rejected the purchasers' claim that National Title and Sartain were liable for inducing a breach of the purchasers' contract with DWCC. In rejecting this third-party claim, the court explained that under Tennessee law a purchaser of real property who "has notice or with ordinary diligence should have had notice of a problem with the real estate [cannot] attack the validity of the contract for fraud, misrepresentation, or concealment of that problem." 30 Since the purchasers here could have performed their own title search, the court reasoned, they could not complain. 31

Moreover, the Sixth Circuit added, the purchasers' requested remedy for third-party misrepresentation was inappropriate. The purchasers raised this claim not to attack the validity of the contract, but rather to impose liability on National Title and Sartain. The Sixth Circuit explained, however, that the contractual remedy for third-party misrepresentation is contract avoidance. 32 The court found no authority to support the purchasers' position that liability was appropriate because recission would not make them whole. The court advised the purchasers that while their requested remedy might be available in tort, it is not available in contract. 33

The purchasers' inappropriate request for a remedy on their third-party claim is one instance of a pervasive blending, in Menuskin, of elements of contract and tort. Indeed, the purchasers themselves explained that their claims for breach "are 'essentially the same as that made for the fraud and

28. Id.
29. See Menuskin, 145 F.3d at 769.
30. Id. (quoting Winstead v. First Tennessee Bank N.A., Memphis, 709 S.W.2d 627, 631 (Tenn. Ct. App. 1986)). The Sixth Circuit found a genuine issue of material fact, however, as to National Title's and Sartain's liability for negligent misrepresentation in preparation and delivery of the warranty deeds. See Menuskin, 145 F.3d at 763.
31. See id. at 759-70.
32. See id. at 770 (citing RESTATEMENT (SECOND) OF CONTRACTS § 164).
33. See Menuskin, 145 F.3d at 770.
negligent misrepresentation claims." A similar blending of claims in contract and tort was more problematic for the plaintiffs in *GBJ Corp. v. Eastern Ohio Paving Co.*, where the Sixth Circuit affirmed dismissal of plaintiffs' fraud claim because it did not "have an identity independent from a related contract claim." Under New York law, explained the court, a fraud claim can be maintained with a claim for breach of contract only if the fraudulent "promise was 'collateral or extraneous' to the contract."

Another interesting aspect of *Menuskin* is its suggestion that important consequences may flow from failure to distinguish carefully a claim based on inappropriate behavior during *contract formation* from one based on a failure of *contract performance*. The distinction between these two claims may be important because, under classic contract law, they trigger different remedies. A claim based on fraud or misrepresentation during contract formation may entitle the claimant to contract recission, while a claim based on a failure of performance may trigger damages measured by the lost performance. As a practical matter, this distinction may be measured in dollars. Upon contract recission, a claimant may be entitled to restitution of benefits conferred (either in kind or as a money judgment) plus incidental or consequential damages caused by the misrepresentation. In turn, the claimant must make restitution of benefits received. This recovery upon contract recission may be a small sum. Upon proof of breach of an enforceable contract, however, a claimant may be entitled to damages measured by lost expectation, i.e., the difference between what was promised and what was received.

Curiously, the *Menuskin* purchasers apparently attempted to demonstrate misrepresentation, which would have entitled them to recission, and yet requested that the defendants be liable on the contract. This blending of misrepresentation and breach in *Menuskin* probably did not much matter, given the Sixth Circuit's conclusion that plaintiffs had no contractual relationship with the defendants. Having found no contract, neither recission nor damages was appropriate. In another case, however, the blurring of claims within contract may have significant consequences since an unfortunate characterization of a claim may foreclose a preferred remedy.

34. *Id.* at 769.
35. 139 F.3d 1080 (6th Cir. 1998). This case is more fully discussed in the section on the statute of frauds. *See infra* text accompanying notes 52-89.
36. *GBJ Corp.*, 139 F.3d at 1087.
37. *Id.* at 1088.
40. *See id.* at § 4.15.
41. *See id.*
42. *See* FARNSWORTH, *supra* note 24, at § 12.8.
Menuskin may thus send an important message to practitioners. While a misrepresentation (of an existing fact) clearly differs from a promise (of future action), these two fact patterns sometimes overlap. As a simple example, a party may misrepresent that land is unencumbered and also promise to convey unencumbered land. If the land ultimately is conveyed subject to an encumbrance, a claim stated in terms of misrepresentation may result in recission of the sales contract and the possible refund of any deposit. A claim stated in terms of a broken promise, however, may produce damages, measured by the difference in value between encumbered and unencumbered land. The message of Menuskin may therefore be that care should be taken in stating a contract claim based on a false representation and promise, as much may be gained or lost in this process.

2. Unconscionability

In Forsythe v. BancBoston Mortgage Corp., the plaintiff and her husband executed a real estate mortgage requiring them to make monthly payments of $437.24. This sum included principal, interest, and an additional amount to be held in escrow to fund property taxes, special assessments and insurance premiums. Unfortunately, the settlement agent at closing underestimated the appropriate escrow costs, and this error continued undetected for twenty-eight months. A few months after acquiring the Forsythe mortgage, BancBoston discovered the shortage and notified the Forsythes that their monthly payments would increase by $124.97 for twelve months. The Forsythes apparently were unable to pay this additional amount. BancBoston refused to accept smaller payments and, in June of 1989, commenced foreclosure proceedings against the Forsythes. In October 1989, the Forsythes filed for bankruptcy and Thomas Forsythe's wages were garnished, partly to pay BancBoston. In April of 1990, Thomas Forsythe committed suicide. Six months later, BancBoston again instituted a foreclosure action, which Darlene Forsythe and BancBoston settled in 1992. As part of this settlement agreement, Darlene Forsythe was to pay $8,000 and sign a release agreeing never to institute any action against BancBoston. In return, BancBoston deemed the mortgage current and dismissed the foreclosure action without prejudice.

43. 135 F.3d 1069 (6th Cir. 1997)
44. See id. at 1072.
45. See id. at 1072-73.
46. See id. at 1073.
In 1993, Darlene Forsythe filed an action against BancBoston on behalf of herself and the estate of her deceased husband, alleging breach of contract, breach of the implied covenant of good faith, breach of fiduciary duty and intentional infliction of emotional distress. The district court found that Forsythe signed a valid release and granted BancBoston's motion for summary judgment against her. The court further granted summary judgment against the estate of Thomas Forsythe.  

On appeal to the Sixth Circuit, Forsythe argued that the settlement agreement, which would preclude her recourse against BancBoston, was unconscionable, violated public policy, and lacked consideration. The Sixth Circuit rejected each of Forsythe's claims. Applying Kentucky law, the court described an unconscionable contract as one "no man in his senses, not under delusion, would make, on the one hand, and which no fair and honest man would accept, on the other." Forsythe, observed the court, was represented by counsel in negotiating the settlement agreement, which benefitted her by waiving more than $9,000 in past due payments and allowing her to retain her house. Since Forsythe's alleged injuries occurred prior to the signing of the release, the court declined to address Forsythe's charge that the settlement agreement unconscionably barred all future claims. The court then concluded that the release did not violate public policy, observing that courts should be slow to allow parties to escape their contract obligations on the basis of pretextual policy violations.

The Sixth Circuit swiftly rejected Forsythe's argument that the settlement agreement lacked consideration, finding substantial consideration in BancBoston's agreement to allow Forsythe to keep her house. BancBoston's dismissal of its forfeiture action without prejudice supplied further consideration under Kentucky authority that consideration may consist of the relinquishment of the right to engage in an activity to which one would otherwise have been legally entitled.

Additionally, the court affirmed summary judgment against Thomas Forsythe's estate. BancBoston, reasoned the court, had no duty under the mortgage agreement to accept partial payments or to provide a yearly analysis of the escrow. BancBoston did not breach its implied duty of good faith and fair dealing; indeed, noted the court, BancBoston was more lenient toward the Forsythes than the covenant of good faith and fair dealing required. Finally,

47. See Forsythe, 135 F.3d at 1073.
49. See id. at 1074.
50. See id.
BancBoston did not breach a fiduciary duty to the Forsythes in the court’s view, since the relationship between a mortgagor and mortgagee is not a fiduciary one under Kentucky law.  

C. Statute of Frauds

1. Requirements Contracts

Does the Article 2 statute of frauds bar enforcement of a non-exclusive contract for the requirements of a new business? The Sixth Circuit answered this question affirmatively in Orchard Group, Inc. v. Konica Med. Corp., by far the most interesting statute of frauds case before the court during the survey period. The alleged contract provided for Konica’s sale of medical x-ray film at a forty-five percent discount off list price "in return for [Orchard Groups’s] film commitment of 36 months." This alleged language of contract appeared in a letter sent to Orchard Group by a Konica sales representative. Three weeks after the date of this letter, Konica informed Orchard Group that it would not approve the deal. Unable to find an alternate supplier, Orchard Group soon went out of business and sued Konica for breach of contract and fraudulent misrepresentation. Konica responded that Orchard Group’s claim was barred by Ohio’s Article 2 statute of frauds. The district court denied Konica’s motion for summary judgment and a jury subsequently returned a $1,000,000 verdict for Orchard Group on its breach of contract claim.

On appeal to the Sixth Circuit, Konica initially argued it was not bound by the alleged letter of contract with Orchard Group since the sales representative who sent the letter had no authority to bind Konica. Applying Ohio law, the court rejected this argument, finding apparent authority in the Konica sales representative.

The Sixth Circuit, however, agreed with Konica that Ohio’s Article 2 statute of frauds barred enforcement of the alleged contract. Finding no specific ruling by the Ohio Supreme Court, the Sixth Circuit undertook the

51. See Forsythe, 135 F.3d at 1077.
52. 135 F.3d 421 (6th Cir. 1998).
53. Orchard Group, 135 F.3d at 423.
55. See Orchard Group, 135 F.3d at 422. At this point, Konica moved for judgment as a matter of law, re-asserting its statute of frauds claim. The district court denied Konica’s motion, as well as Orchard Group’s motion for pre-judgment interest. Both parties appealed to the Sixth Circuit. See id.
56. See Orchard Group, 135 F.3d at 427.
task of determining whether Ohio would enforce a contract for the requirements of a new business where the contract contained no quantity term.\(^{57}\)

The court initially observed that a contract for the sale of goods for \$500 or more generally fails to satisfy the statute of frauds unless there is a writing stating the quantity of goods sold. The court noted that Konica’s letter on its face contained no quantity term.\(^{58}\) Orchard Group contended however, that the agreement was a requirements contract and, therefore, was enforceable without a specific quantity term.

The Sixth Circuit began its analysis by quoting U.C.C. section 2-306(1), which sets forth the standard for a requirements contract:

\[\text{A term which measures the quantity by the output of the seller or the requirements of the buyer means such actual output or requirements as may occur in good faith, except that no quantity unreasonably disproportionate to any stated estimate or in the absence of a stated estimate to any normal or otherwise comparable prior output or requirements may be tendered or demanded.} \(^{59}\)\]

Applying this section, the court determined that Konica’s letter "fails as a requirements contract because [(1)] it lacks a specific quantity term - estimate or -- otherwise and [(2)] there is no prior course of dealing from which a quantity term could be implied" since Orchard Group is a new business.\(^{60}\)

The court’s statement can be narrowed by coupling it with the courts’ subsequent conclusion that the arrangement between Konica and Orchard Group was not exclusive. This lack of exclusivity, reasoned the court, together with the absence of "any identifiable quantity term, or one that may be implied from a prior course of dealings," made the contract unenforceable as a requirements contract.\(^{61}\)

Although the text of U.C.C. section 2-306(1) does not expressly require exclusivity,\(^{62}\) case law has long recognized this feature as essential to the mutuality necessary for an enforceable contract.\(^{63}\) Indeed, the definition of a requirements contract typically includes a reference to exclusivity.\(^{64}\) orchard

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\(^{57}\) See id. at 427.

\(^{58}\) See id. at 428.

\(^{59}\) Orchard Group, 135 F.3d at 428 (citing Cyril Bath Co. v. Winters Indus. 892 F.2d 465 (6th Cir. 1989)).

\(^{60}\) Id. at 428.

\(^{61}\) Id. at 430.

\(^{62}\) Cf. U.C.C. § 2-306(2) which addresses "exclusive" dealings.

\(^{63}\) See JAMES J. WHITE & ROBERT S. SUMMERS, UNIFORM COMMERCIAL CODE § 3-9 n.3 & accompanying text (4th ed. 1995).

\(^{64}\) Professor Farnsworth has defined a requirements contract as "one under which the seller agrees to sell and the buyer to buy all of the goods of a particular kind that the buyer may require in its business." FARNsworth, supra note 24, at § 2.15.
Group may thus be cited for its holding that a non-exclusive contract for the requirements of a new business is unenforceable without a stated estimate.

Another interesting aspect of the Sixth Circuit opinion in Orchard Group is the court's conclusion that parol evidence of exclusivity was inadmissible to counter the "plain language" of Konica's letter. In the Sixth Circuit's view, nothing in the letter "even remotely suggests exclusivity." The court found conclusive Orchard Group's ability to order zero units of film without committing a breach, which, according to the court "completely foreclosed" the possibility of exclusivity. Contract drafters thus may be well-advised to avoid Orchard Group by expressing in clear terms the exclusivity of a requirements arrangement, especially one involving a new business.

2. Exception for Specially Manufactured Goods

In Webcor Packaging Corp. v. Autozone, Inc. the Sixth Circuit again found an alleged agreement unenforceable under the statute of frauds. In this case, Webcor contracted over several years with various vendors to manufacture cartons with the Autozone trade name, Duralast. The changing group of vendors who bought the Duralast cartons used them to package their own automobile parts which they then sold to Autozone as "retail ready" items. Autozone fostered Webcor's role in this production chain by directing vendors to Webcor and by supplying Webcor with artwork and specifications for Duralast packaging. Occasionally, Autozone purchased cartons from Webcor for its own use.

In late 1990, vendor demand for Duralast cartons increased and Webcor's normal thirty-day inventory was depleted. Subsequently, in a telephone conversation initiated by a Webcor sales representative, Autozone allegedly assured Webcor that if Webcor increased its inventory to a sixty-day supply in order to meet vendor demand, Autozone would "cover" payment if the cartons became obsolete. In 1993, Autozone decided to change the Duralast brand name and symbol, and Webcor's inventory did indeed become obsolete. Webcor was unable to sell a portion of its Duralast sixty-day inventory and claimed damages from Autozone.

Following a one-day bench trial, the district court ruled that Michigan's statute of frauds governing sale of goods precluded enforcement of

65. Orchard Group, 135 F.3d at 429.
66. See id.
67. 158 F.3d 354 (6th Cir. 1998).
68. See Webcor Packaging Corp., 158 F.3d at 355.
69. See id.
70. See id.
Autozone's alleged oral agreement to compensate Webcor for its obsolete inventory. The district court found no signed writing to satisfy the statute of frauds, and further determined that the alleged agreement did not fall within the exception for specially-manufactured goods.

Upon Webcor's appeal, the Sixth Circuit found a "sound basis" for the district court's conclusion that the specially-manufactured goods exception was inapplicable. The court noted, however, a "significant wrinkle" presented by the "series of three-layered transactions involving multiple parties" and seized the opportunity "to refine and extend" the lower court's analysis.

The specially-manufactured goods exception to the statute of frauds allows enforcement of a contract without a writing:

if the goods are to be specially manufactured for the buyer and are not suitable for sale to others in the ordinary course of the seller's business and the seller, before notice of repudiation is received and under circumstances which reasonably indicate that the goods are for the buyer, has made either a substantial beginning of their manufacture or commitments for their procurement.

The Sixth Circuit began its analysis under this section with the traditional "look to the goods" test. The relevant question under this test, explained the court, is whether "the goods themselves have some feature that makes the product marketable only to the buyer." The focus is thus on the goods rather than on the regularity or irregularity of the manufacturing process. The court further noted a circularity in requiring evidence to establish both that goods are "specially made for the buyer" and that they are "unsuitable for sale to others in the ordinary course of the seller's business." "Specially manufactured goods," reasoned the court, are "necessarily goods unsuitable for sale to others in the ordinary course of the seller's business."

72. See id. at § 440.2201(3)(a).
73. Webcor Packaging Corp., 158 F.3d at 357.
74. Id. at 355.
76. Webcor Packaging Corp., 158 F.3d at 357.
77. Id. at 357
78. The focus, explained the court, is not on "[w]hether the goods were made in an unusual, as opposed to the regular, business operation or manufacturing process of the seller." Id. at 357 (quoting Impossible Elec. Techniques, Inc. v. Wackenhut Protective Sys., Inc., 669 F.2d 1026, 1037 (5th Cir. 1982)).
79. Webcor Packaging Corp., 158 F.3d at 356.
80. Id. at 357.
81. Id. at 357.
In Webcor's case, the Sixth Circuit found no easy answer in the traditional "look to the goods," approach since the buyer's identity was unclear. While the cartons themselves displayed Autozone's Duralast logo, multiple purchasers had an interest in purchasing them. The court observed that a buyer might be identified through either: (1) an "ultimate purchaser" theory, urged by Webcor or (2) a "single buyer" theory, adopted by the district court. In the district court's view, the specially-manufactured goods exception contemplates manufacture for a single buyer and, therefore, did not apply to the multiple buyers of Duralast cartons. While criticizing the "single buyer" theory as "overly rigid in a world of increasingly complex business transactions," the Sixth Circuit found the specially-manufactured goods exception inapplicable on another ground.

The Duralast cartons, the Sixth Circuit reasoned, were not specially manufactured for Autozone, but rather for the multiple vendors who then used them to package the parts they sold to Autozone. Thus, even if Autozone were identified as "the buyer," the relationship between Webcor and Autozone was too attenuated to demonstrate that the cartons were produced for Autozone. Consequently, Webcor could not claim protection from the statute of frauds under the specially-manufactured goods exception and, concluded the Sixth Circuit, Webcor's action against Autozone was properly barred.

3. Contracts for the Sale of Securities -- Article 8

In GBJ Corp. v. Eastern Ohio Paving Co., the district court applied the wrong statute of frauds to plaintiffs' contract claims. Plaintiffs' claims were indeed barred, according to the Sixth Circuit, but not by the statute of frauds governing suretyships, as the district court held. The alleged contract, explained the Sixth Circuit, was not a promise to answer for a debt (owed by another party), but rather, a bilateral agreement to assume a debt. Because this alleged agreement involved an exchange of stock for capital, it fell within Article 8, which governs sales of securities. Section 8-319 of New York's U.C.C. imposes a writing requirement on such transactions, thus rendering the alleged oral contract unenforceable.

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82. Webcor Packaging Corp., 158 F.3d at 357.
83. Id. at 359.
84. See id. at 360.
85. See id. at 360.
86. 139 F.3d 1080 (6th Cir. 1998).
87. At the time GBJ was decided, U.C.C. § 8-319 provided in part: A contract for the sale of securities is not enforceable by way of action or defense unless (a) there is some writing signed by the party against whom enforcement is
The precedential effect of GBJ is limited, since the Article 8 statute of frauds which snagged the plaintiff there, was replaced by the New York legislature in October of 1997. The current version, relocated at U.C.C. section 8-113, follows the uniform revision to Article 8 in making the statute of frauds generally inapplicable to contracts for the sale of securities. The New York enactment, however, departs from the uniform version in imposing a writing requirement for certain contracts for the sale of securities involving real property.

sought or by his authorized agent or broker sufficient to indicate that a contract has been made for sale of a stated quantity of described securities at a defined or stated price.


88. See N.Y. U.C.C. § 8-113 (McKinney 1997).

89. The Official Comment to the revised Uniform Act explains:

This section provides that the statute of frauds does not apply to contracts for the sale of securities, reversing prior law which had a special statute of frauds in Section 8-319 (1978). With the increasing use of electronic means of communication, the statute of frauds is unsuited to the realities of the securities business. For securities transactions, whatever benefits a statute of frauds may play in filtering out fraudulent claims are outweighed by the obstacles it places in the development of modern commercial practices in the securities business.


90. See id. N.Y.U.C.C. § 8-113 provides:

Statute of Frauds Generally Inapplicable
(a) Except as provided in subsection (b) a contract or modification of a contract for the sale or purchase of a security is enforceable whether or not there is a writing signed or record authenticated by a party against whom enforcement is sought, even if the contract or modification is not capable of performance within one year of its making.

(b) A contract for the sale of a security constituting an ownership interest or a proprietary lease or either of the foregoing from a corporation or partnership formed for the purpose of cooperative ownership of real property is not enforceable by way of action or defense unless:

(1) there is some writing signed by the party against whom enforcement is sought which describes the security and states its price; or

(2) the party against whom enforcement is sought admits in its pleading, testimony, or otherwise in court that a contract was made for the sale of the security and the admission describes the security and states its price.

Id.
II. INTERPRETING THE AGREEMENT: WHAT IS...  

Like Judge Friendly, who mused, "The issue is, what is chicken?" the Sixth Circuit was asked in several cases to interpret contract language. In several of these surveyed cases, the Sixth Circuit found the disputed terms had a plain meaning, which sometimes precluded admission of parol evidence to establish a different meaning.92  

A. What is "Existed"?  

In Equitable Life Assurance Soc'y of the United States v. Poe,93 the Sixth Circuit was asked to interpret an incontestability clause placed in an insurance contract pursuant to Michigan statute.94 In pertinent part, the clause provided: "[n]o claim for Loss incurred or Disability that starts after two years from the Effective Date will be reduced or denied on the grounds that a sickness or physical condition existed prior to the Effective Date."95  

Equitable Life urged the court to interpret the word existed in the above clause to include only conditions that were not yet manifested. Under such an interpretation, Equitable Life could properly deny a claim based on a condition manifested prior to the effective date of the policy. Finding no interpretation of this clause by the Michigan Supreme Court, the Sixth Circuit determined that Michigan would join the "growing minority of courts" that have rejected the "first manifest" doctrine urged by Equitable Life.96  

The contract language, observed the Sixth Circuit, had a plain meaning. Nothing in the clause, noted the court, "suggest[s] that the term 'existed' should be read in any way except in its plain, ordinary, and popular sense."97 A manifested condition, reasoned the court, also exists.98 The court further noted that if there were any ambiguity in the term existed, it would be resolved in favor of the insured.99

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92. See generally E. ALLAN FARNSWORTH, supra note 24, at § 7.12.
93. 143 F.3d 1013 (6th Cir. 1998).
94. See MICH. COMP. ANN. § 500.3408 (West 1993).
95. Equitable Life Assurance Soc'y, 143 F.3d at 1017 (emphasis supplied).
97. Id.
98. See Equitable Life Assurance Soc'y of the U.S. v. Bell, 27 F.3d 1274 (7th Cir. 1994).
99. See Equitable Life Assurance Soc'y, 143 F.3d at 1018.
Finally, the court found contextual support for its interpretation in an earlier section of the insurance policy (also mandated by Michigan law) which specifically mentioned fraudulent misstatements. Because this reference to fraud was not repeated in the incontestibility clause, the court discerned a legislative intent that the clause would protect even already-manifested conditions. Thus, concluding that the word exists includes both manifested and unmanifested conditions, the court affirmed the district court's holding that the incontestability clause barred Equitable Life from denying coverage of the insured's disability as a preexisting condition.100

B. What is "Exclusive Right to Operate"?

In *Sault Ste. Marie Tribe of Chippewa Indians v. Engler*,101 several Michigan Indian tribes claimed the 1996 passage of the Michigan Gaming Control and Revenue Act (the "Act") released them from their obligation to pay the state a percentage of the net win from their electronic casino games. The Tribes' payment obligation stemmed from a 1993 consent judgment, which conditioned the Tribes' obligation on their "exclusive right to operate"102 electronic games of chance in Michigan. The Tribes argued that these exclusive rights terminated when the Act empowered the Michigan Gaming Control Board to grant licenses for casinos in Detroit. When several of the Tribes notified the State they would make no further payments, Governor Engler filed a motion to compel compliance. The district court concluded that the Tribes retained the exclusive right to operate casinos and therefore must continue to share their winnings with the state. One Tribe appealed to the Sixth Circuit.103

The Sixth Circuit adopted a posture of "deferential de novo" review toward the district court's interpretation of its own consent judgment.104 "[F]ew persons," reasoned the Sixth Circuit, "are in a better position to understand the meaning of a consent decree than the district judge who oversaw and approved it."105 Not surprisingly, the court ultimately affirmed the district court's conclusion that the Tribes' exclusivity continues until a non-Tribal entity receives a casino license.106

100. See id. at 1020.
101. 146 F.3d 367 (6th Cir. 1998).
103. See id. at 371.
104. Id. at 371.
105. Id. at 372 (quoting Brown v. Neeb, 644 F.2d 551, 558 n.12 (6th Cir. 1981)).
106. See *Sault Ste. Marie Tribe*, 146 F.3d at 372.
Observing a plain meaning in the words "exclusive right to operate," the Sixth Circuit further affirmed the district court's exclusion of evidence offered to support the Tribes' interpretation. The Tribes' claim of ambiguity, observed the court, does not in itself create ambiguity. Moreover, the court found the Tribes' proffered evidence irrelevant to the interpretation issue since it did not relate to formation of the contract, but rather consisted of post-hoc contract interpretations.

C. What is "Auftragsverhaltnis"?

The Sixth Circuit was asked in Tschira v. Willingham to interpret a contract between a U.S. seller and foreign buyers. The term at issue, "auftragsverhaltnis," was central to the plaintiff-buyers' claim that the parties stood in a fiduciary relationship. Under German law, invoked under a choice-of-law clause, the buyers claimed use of the term "auftragsverhaltnis" created a "mandate relationship," which is similar to an agency relationship under U.S. law, with consequent fiduciary obligations. The sellers, on the other hand, claimed the use of the term "auftragsverhaltnis" created only a "contractual relationship." The district court interpreted "auftragsverhaltnis" to impose fiduciary duties, and after a verdict for the buyers, the sellers appealed.

The Sixth Circuit agreed with the district court that the parties intended to create a fiduciary relationship. Key to the court's conclusion was a provision in the contract recognizing a power of attorney in the seller. Such a right, reasoned the court, evidenced the parties' intent to create a mandate relationship.

Finding ample evidence of intent in the power-of-attorney provision, the Sixth Circuit did not directly respond to the seller's interesting argument that he should be held to the ordinary rather than the legal meaning of "auftrag." Although "auftragsverhaltnis" means "mandate" under the German Civil Code, it has various meanings in the German language. The seller had argued that "auftrag" should be given its "ordinary" rather than its "legal" meaning since, as an "ordinary businessman," he would not have used the term in its

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107. Id. at 373.
108. See id.
109. 135 F.3d 1077 (6th Cir. 1998). The facts of Tschira are presented in more detail in the section on intention to be bound. See supra text accompanying notes 17-21.
110. See Tschira, 135 F.3d at 1081.
111. See id.
112. See id. at 1082.
legal sense. The court thus noted without resolving the issue of whether a contracting party unfamiliar with legal usage should be held to the legal meaning of a contract term.

D. What is "Commitment"?

In another invocation of the plain meaning rule, the Sixth Circuit held parol evidence inadmissible "to counter the force of plain language." In Orchard Group, a supplier of x-ray film raised the statute of frauds as a defense against an alleged buyer. The buyer's ability to satisfy the statute of frauds depended upon proof that a requirements contract was exclusive. To establish this exclusivity, the buyer sought to introduce evidence to establish that use of the term "commitment" in a letter of contract created an exclusive relationship. In holding such evidence inadmissible, the Sixth Circuit observed that the language "is not unclear; it simply does not suggest, even impliedly, an exclusive relationship." To permit parol evidence in such a case, added the court, would allow "post-litigation revision of a contract which is not the least unclear."

E. What is "Any Questions"? "All Controversies and Claims"?

In Ferro Corp. v. Garrison Industries Inc., the Sixth Circuit was asked to determine the reach and interplay of a choice-of-law clause and an arbitration clause in the parties’ requirements contract. Under the terms of the contract, Garrison agreed to manufacture for Ferro a flame-retardant additive known as PyroCheck LM. The contract, which specified a quantity range and a two-year initial term, contained a standard arbitration clause and an Ohio choice-of-law clause. After several months in which Garrison produced insufficient quantities of PyroCheck LM, sometimes of inferior quality, Ferro sent Garrison a contract termination letter. When Ferro subsequently refused to pay for approximately 2.2 million pounds of PyroCheck LM, Garrison invoked the arbitration clause. Before arbitration commenced, however, Ferro filed an action in state court charging Garrison with fraudulent inducement

113. See Tschira, 135 F.3d at 1084.
115. See Orchard Group, 135 F.3d at 429. Orchard Group is more fully discussed in the section on the statute of frauds. See supra text accompanying notes 52-89.
116. See id. at 429.
117. Id. at 429-30.
118. Id. at 430.
119. 142 F.3d 926 (6th Cir. 1998).
and seeking to enjoin arbitration and rescind the contract. Garrison then removed the action to the Federal District Court for the Northern District of Ohio and asked that court to refer the complaint to arbitration.

After a "whirlwind" of procedural maneuvers, and partially parallel hearings before both the district court and an arbitration panel, the district court determined that Garrison had, indeed, fraudulently induced Ferro to enter the agreement and ordered the contract rescinded to the extent not performed. Subsequently, the arbitration panel found Ferro liable to Garrison for damages exceeding $1.6 million. The district court then vacated the arbitration award.

The key issue before the Sixth Circuit was whether Ferro's allegations of fraudulent inducement were arbitrable. Under the choice-of-law clause, the parties agreed that "all of the provisions of this Agreement and any questions concerning its interpretation and enforcement shall be governed by the laws of the State of Ohio, USA exclusive of its choice of law rules . . . ." The contract also provided for arbitration of "[a]ll controversies and claims arising out of or relating to this agreement." The district court determined that under the terms of the contract, the fraudulent inducement issue was not arbitrable. The district court reasoned that Ohio law, applicable under the parties' choice-of-law clause, required judicial resolution of a charge of fraudulent inducement.

The Sixth Circuit disagreed with the district court, reasoning that the choice-of-law clause did not preclude application of federal arbitration law, under which the fraud claim was arbitrable. The Circuit Court explained that if the parties' arbitration clause were subject to the Federal Arbitration Act (FAA), as an agreement involving interstate commerce, an issue of fraudulent inducement of the entire contract would be resolved through arbitration, but an issue of fraudulent inducement of the arbitration clause would be for judicial adjudication. Therefore, unless the parties opted out of this interpretation of the FAA, the issue of fraudulent inducement should have been resolved through arbitration.

120. *Id.* at 928. Ferro contended that Garrison falsely represented that: (1) it was capable of manufacturing the minimum quantities of PyroCheck LM, and (2) it sustained only minor damage from a tornado. *Id.* at 929.

121. *See id.* at 928-29.

122. *See id.* at 928. The district court determined that Ferro was not entitled to return of the $250,000 it paid Garrison upon execution of the contract. *See id.* at 930.

123. *See Ferro Corp.* 142 F.3d at 931.

124. *Id.* at 931-32, n.7 (emphasis added).

125. *Id.* at 931.


127. *See Ferro Corp.* 142 F.3d at 933.
The Sixth Circuit rejected Ferro's argument that the parties' Ohio choice-of-law provision was intended to avoid federal arbitration law. Mindful of the teaching that "any doubts concerning the scope of arbitrable issues should be resolved in favor of arbitration," the Sixth Circuit found no indication that the parties intended that Ohio law would determine whether fraud should be judicially adjudicated. The court noted the conspicuously broad language of the arbitration clause, which applied to "[a]ll controversies and claims arising out of or relating to this Agreement . . . ." If Ferro had intended to limit issues subject to arbitration, reasoned the court, it could have expressly so provided in the contract.

As a matter of policy and common sense, added the Sixth Circuit, interpreting the parties' contract to require judicial adjudication of claims of fraudulent inducement would allow a party to avoid arbitration simply by pleading fraudulent inducement, thus vitiating "the primary benefit of arbitration, i.e., the expeditious, inexpensive resolution of disputes." Moreover, the court noted that since most contracts contain a choice-of-law clause, interpreting these clauses to avoid federal arbitration law would leave the FAA applicable in only a very small number of cases. "Arbitration," concluded the court, "is a creature of contract, and parties should, absent the most extenuating and explicit of circumstances, be required to arbitrate those disputes which they agree to arbitrate."

F. What is Indemnification for "All Loss"?

Can a contracting party recover for its own negligence and for its violation of environmental statutes under the terms of an indemnity agreement? These were the issues before the court in Olin Corp. v. Yeargin Inc., where the Sixth Circuit was again asked to interpret the meaning of disputed contract language. Olin had contracted with Yeargin to perform specified on-site construction and maintenance tasks in Olin's chlorine production facility. While Yeargin employees were replacing a dilute caustic header pipe, toxic material escaped, contaminating the clothes and skin of

129. Id. at 931 (emphasis added). The arbitration agreement at issue provided, "All controversies and claims arising out of or relating to this Agreement, shall be settled by arbitration in Cleveland, Ohio, in accordance with Commercial Arbitration Rules of the American Arbitration Association." Id. (emphasis added).
130. See id. at 938.
131. Id. at 938.
132. Ferro Corp., 142 F.3d at 939.
133. 146 F.3d 398 (6th Cir. 1998).
Yeargin employees and producing toxic vapors which they inhaled. After failing to decontaminate before leaving Olin's premises, these employees subsequently contaminated their motor vehicles and homes and exposed their spouses to the toxins. These Yeargin employees and their spouses brought actions against Olin, seeking recovery under various theories, including negligence and misrepresentation. These actions were ultimately settled. In addition to amounts paid under these settlement agreements, Olin paid various fines, attorneys' fees and expenses in connection with three complaints relating to its violation of environmental statutes. 134

Olin subsequently sought indemnity from Yeargin under the following contract provision:

(a) Contractor agrees to protect, indemnify and hold Owner harmless from any and all loss, damage, liability, claims, demands, costs, or suits of any nature whatsoever asserted by employees of Contractor or any third persons (including employees of Owner) for property damage, personal injury or death, or otherwise in each case arising out of, in connection with or incidental to Work performed under this Contract.

(b) This indemnity shall apply to the extent that said loss, damage, liability, claims, demands, costs, or suits are occasioned, brought about or caused, in whole or in part, by negligence of Contractor, its agent, directors, officers, employees or servants and regardless of whether such negligence be active or passive, primary or secondary. 135

Yeargin argued that subsection (b) required it to indemnify Olin only as to costs incurred as a result of Yeargin's fault and, thus, did not require it to indemnify Olin for Olin's own negligence. The district court agreed, noting that Tennessee law requires a clear and unequivocal intent to indemnify the indemnitee's own negligence. 136 The Sixth Circuit agreed with the district court's conclusion, observing no express reference in the contract to Yeargin's responsibilities for losses caused by Olin's own negligence. If the parties intend this result, added the Sixth Circuit, "it would only take a few seconds for the attorneys . . . to use appropriate express language such as 'including indemnitees' acts of negligence." 137


135. Olin Corp., 146 F.3d at 403.

136. See id. at 404.

137. Id. (quoting Wajtasiak v. Morgan County, 633 S.W.2d 488, 490 (Tenn. Ct. App. 1982)).
The Sixth Circuit determined, however, that Olin was entitled to indemnification for costs stemming from its violation of environmental statutes, reversing the district court on this point. The Sixth Circuit noted the general rule that broad language in an indemnity agreement indicating an intent to include all liabilities includes environmental liabilities even without specific reference. However, an indemnity agreement that is not broadly stated, but rather limits liability to specific types of claims, will not include environmental liability absent a clear and unambiguous reference. While the language in the Olin/Yeargin indemnification clause did not specifically refer to environmental liabilities, it was broad enough to encompass them. The costs, fines and penalties Olin incurred, reasoned the court, arose because toxic material caused property damage and personal injury. They thus fell within the broad language of subsection (a) and supported Olin's claim for indemnification. One judge dissented on this issue, reasoning that "property damage, personal injury, or death" listed in subsection (a) all refer to tort claims and thus, under the doctrine of ejusdem generis, only other tort claims (and not claims for violation of environmental statutes) were subject to indemnification.\(^\text{138}\)

III. NONPERFORMANCE - - "FIRST SUBSTANTIAL BREACH"

The dispute in Chrysler Int'l Corp. v. Cherokee Export Co.\(^\text{139}\) involved an export sales agreement under which Cherokee obtained the nonexclusive right to buy vehicles from Chrysler for export to customers in listed countries. This agreement, formalized in 1989 and renewed in 1993, barred Cherokee from selling vehicles to customers in non-listed countries, including the U.S. Additionally, Cherokee was specifically barred from selling vehicles to any customer for resale. Chrysler's stated goal was to establish a "foothold" in the listed countries, and eventually, a worldwide network of distributors. Once dealerships were established in a foreign market, Chrysler, upon thirty days notice, would remove that country from Cherokee's list of approved markets.\(^\text{140}\)

During the course of its relationship with Chrysler, Cherokee made numerous sales in unlisted areas, in violation of the parties' agreement, sometimes creating "strawman" documentation to hide its misdeeds. Upon learning of these sales, Chrysler claimed to have expressed concern to Cherokee, which Cherokee characterized as "a slap on the wrist."\(^\text{141}\)

\(^{138}\) Id. at 409 (Contie, J., dissenting).
\(^{139}\) 134 F.3d 738 (6th Cir. 1998).
\(^{140}\) See id. at 740-41.
\(^{141}\) Chrysler, 134 F.3d at 741.
The principal disagreement between the parties arose in connection with a 1992 contract between Chrysler, Cherokee, and Beijing Jeep Corporation (BJC). This contract provided for Chrysler's purchase of 150 BJC-produced Jeeps, to be delivered in two shipments to Cherokee in Tanzania, Africa. Cherokee claimed both shipments were defective. According to Cherokee, the final shipment in July of 1994 was so defective that twenty of the 100 vehicles received had to be "cannibalized" for parts to render the remaining vehicles saleable.

By October of 1994, Chrysler had become concerned about the extent of Cherokee's exposure, which exceeded 5.5 million in accounts payable to Chrysler. Consequently, Chrysler asked Cherokee to double its $750,000 letter of credit, due to expire in February of 1995.¹⁴² Cherokee characterized Chrysler's demand as a unilateral decision to terminate the parties' agreement with Cherokee without the required notice by placing Cherokee on "finance hold,"¹⁴³ which caused Cherokee to breach agreements with its customers. In February of 1995, when Cherokee still owed Chrysler over $3 million, Chrysler drew on the $750,000 letter of credit and, in March, sued Cherokee for breach of contract.¹⁴⁴

Chrysler and Cherokee both claimed the other breached the 1993 renewal agreement. Chrysler claimed Cherokee sold in unapproved areas and to resellers and failed to pay for the BJC vehicles. Cherokee, in turn, claimed Chrysler improperly terminated its relationship with Cherokee, and breached its agreement by declining Cherokee's post-1994 orders and rejecting Cherokee's warranty claims. The district court granted summary judgment for Chrysler.¹⁴⁵

On appeal, the Sixth Circuit affirmed. Noting that both parties may have been in breach, the court found "no question" that Cherokee committed the first substantial breach through its many out-of-area sales.¹⁴⁶ Michigan law, stated the court, is well-settled: "He who commits the first substantial breach of a contract cannot maintain an action against the other contracting party for failure to perform."¹⁴⁷ A breach is substantial, observed the court, where it has "effected such a change in essential operative elements of the contract that

¹⁴². See id. The district court so found, although the parties apparently disputed this fact. See id.
¹⁴³. Id.
¹⁴⁴. See id. at 742.
¹⁴⁵. See Chrysler, 134 F.3d at 740.
¹⁴⁶. See id. at 743.
further performance by the other party is thereby rendered ineffective or impossible . . . . " 148

The essential purpose of the Chrysler/Cherokee contract, observed the Sixth Circuit, was to establish Chrysler's foothold in new markets. Cherokee was therefore specifically barred from selling to out-of-area markets because Chrysler wanted to reserve those markets for Chrysler dealerships. Although Cherokee was aware of Chrysler's essential purpose, it made numerous sales to unapproved markets, disguising some such sales through "bogus paperwork." 149 Under these circumstances, concluded the court, Cherokee committed a material breach as a matter of law, and was thus precluded from asserting rights under its contract with Chrysler. 150

IV. ENFORCEMENT OF PROMISES

A. Damages

Basic hornbook law teaches that contract damages generally are measured by an injured party's lost expectation, i.e., by the difference between what was promised and what was actually received. 151 Such a traditional measure of damages would have made a defaulting commercial tenant liable for over $900,000 in damages in Highland Superstores, Inc. v. Unsecured Creditors' Comm. of Highland Superstores, Inc. v. Strobeck Real Estate, Inc. 152 This was not good news to Highland’s unsecured creditors who were competing with the landlord for Highland’s assets upon its Chapter 11 petition. Consequently, the Unsecured Creditors’ Committee fashioned "an elegant and creative," though ultimately unsuccessful, argument that would have reduced the landlord’s damages to zero. 153

The landlord's damages were based primarily on the difference between payments due under the remaining (approximately) fourteen years of Highland’s lease and payments due under a new lease negotiated by the landlord upon Highland’s default. The Committee urged the bankruptcy court

149. See id. at 743.
150. See id.
151. See FARNSWORTH, supra note 24, at §12.9 (loss in value is measured by the "difference between the value to the injured party of the performance that should have been received and the value to that party of what, if anything, actually was received . . . "). As Professor Farnsworth explains, this loss in value may be qualified by considerations of other loss, cost avoid and loss avoided. See id. See also RESTATEMENT (SECOND) OF CONTRACTS § 347 (1981).
152. 154 F.3d 573 (6th Cir. 1998)
153. Highland Superstores, 154 F.3d at 581.
to base its calculation of this differential in lease revenues on the discounted present value of the stream of future payments, and to use discount rates that reflected the relative creditworthiness of the two tenants. If creditworthiness were thus considered, the value of the new lease would exceed the value of the Highland lease, given Highland’s "C" credit rating and the new lessee’s "A" credit rating. Thus, according to the Committee, the landlord’s position actually improved, making damages inappropriate.154

The bankruptcy court rejected the Committee’s argument, basing its calculation of damages on the lease terms and Illinois contract law. On appeal, the district court reversed. While acknowledging the "utter lack" of precedent for the Committee’s calculation, the district court adopted the Committee’s methodology to "see whether the law does develop in the [Committee’s] direction..."155

The Sixth Circuit declined the district court’s invitation "to turn a blind eye toward fundamental principles of contract law."156 The ability of a breaching party to pay, explained the court, does not affect the calculation of damages. If collectibility were a factor in measuring damages, a destitute promisor would owe very little in damages, because of the high nonpayment risk, while a creditworthy promisor would owe much more. The Sixth Circuit thus declined "to jettison well-established principles of state contract law in favor of the creative, yet radical, approach advanced by the Committee."157

B. Statute of Limitations

Largely a conflicts case, Cole v. Mileti158 sends an important message to those drafting choice-of-law clauses. The transaction at issue began in 1983, when Mileti co-produced a motion picture in which Cole invested $475,000. Cole’s investment in the corporation, organized to purchase and distribute this film, was funded through a bank loan. Unfortunately for the parties, the film failed. Soon thereafter, in 1984, Mileti and Cole entered an agreement requiring Cole to transfer his stock and indebtedness to Mileti, in exchange for Mileti’s promise to repay Cole’s investment loan.159 The written agreement

154. See id. at 580.
155. Id. at 576.
156. Id. at 579-80.
157. Highland Superstore, 154 F.3d at 580.
158. 133 F.3d 433 (6th Cir. 1998).
159. See Cole, 133 F.3d at 435. It is not clear why the court refers to this agreement as a suretyship, as the facts seem to describe an indemnification. See FARNSWORTH, supra note 24, at § 6.3 ("In a contract of indemnity, the promise runs to an obligor or a prospective obligor rather than to an obligee, as is typically the case in a contract of suretyship.") Id.
between Cole and Mileti contained a clause specifying that their "contract would "be governed and construed in accordance with the laws of the State of California."¹⁶⁰ Mileti failed to repay Cole's loan as promised, prompting Cole to make sporadic payments until 1992, when the bank sued Cole to recover the balance due. Cole settled with the bank for $310,000 and in 1994, nine years after Mileti's alleged breach, sued Mileti for breach of the 1984 contract. The district court for the northern district of Ohio denied Mileti's motion to dismiss and a U.S. Magistrate ultimately granted summary judgment to Cole.¹⁶¹

On appeal to the Sixth Circuit, Mileti challenged both the Magistrate's exercise of personal jurisdiction over him and the Magistrate's determination that Cole's action was not time-barred. Mileti argued that the Magistrate improperly applied Ohio's fifteen-year statute of limitations rather than California's four-year statute.

In affirming the Magistrate, the Sixth Circuit initially noted the familiar rule that federal courts sitting in diversity apply the choice-of-law rules of the forum state. Ohio law, observed the court, requires Ohio courts to apply Ohio's statute of limitations to breach of contract actions brought in Ohio. The court rejected Mileti's argument that Ohio common law preserved a long-repealed Ohio borrowing statute, which would have required application of a foreign state's shorter statute of limitations.

The importance of Cole from a contract perspective is the Sixth Circuit's answer to Mileti's final charge that the parties' California choice-of-law clause triggered California's statute of limitations. In rejecting Mileti's argument, the Sixth Circuit explained that "contractual choice-of-law clauses incorporate only substantive law, not procedural provisions such as statutes of limitations."¹⁶² The message for contract drafters? An express statement that another state's statute of limitations will apply, observed the court, will change the Cole result.

¹⁶⁰  Cole, 133 F.3d at 435.
¹⁶¹  Upon Cole's death in 1995, his wife was substituted as plaintiff. See Cole, 133 F.3d at 433.
¹⁶²  Cole, 133 F.3d at 437 (citing Phelps v. McClellan, 30 F.3d 658, 662 (6th Cir. 1994) and Charash v. Oberlin College, 14 F.3d 291, 299 (6th Cir. 1994)).