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Kathleen E. Payne

Michigan State University College of Law, payneka@law.msu.edu

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SIXTH CIRCUIT SURVEY OF CONTRACTS

Kathleen E. Payne†

INTRODUCTION

Within the survey period, the Sixth Circuit Court of Appeals reviewed seven cases involving contract issues. One case from Ohio dealt with the application of the doctrine of promissory estoppel to a statute of frauds defense in a real estate transaction. Three cases examined the recurring issue of the proper measure of damages, discussing specific performance, restitution as appropriate relief in a case involving mutual mistake, and the inappropriateness of fair market value as the measure of damages where a horse auctioneer fails to honor a reserve bid price.

Two other cases faced the problem of distinguishing tort issues from contract issues. The first case addressed the question of whether Michigan law recognizes a cause of action in tort for the negligent performance of a contract. The second case discussed the effectiveness of contract disclaimers in barring recovery for tortious misrepresentation. The final case, and the only one of the survey period decided under Article 2 of the Uniform Commercial Code, allocated risk of loss between sellers and buyers where an underground propane gas storage facility collapsed and the stored gas could no longer be removed.

I. PROMISSORY ESTOPPEL AND THE STATUTE OF FRAUDS

In Seale v. Citizens Savings & Loan Assoc.,¹ the Sixth Circuit Court of Appeals, applying Ohio law in a diversity action, reversed the district court's holding that an oral agreement to repurchase

† B.A., Michigan State University, 1967; M.A., Eastern Michigan University, 1970; J.D., Detroit College of Law, 1977; LL.M., University of Michigan, 1981; Professor of Law, Detroit College of Law.

Ed. Note — Prior to joining the faculty of the Detroit College of Law in 1980, Professor Payne served as law clerk to Justice Blair Moody, Jr. of the Michigan Supreme Court. Professor Payne teaches Commercial Transactions, Secured Transactions, and Bankruptcy. She also serves as Faculty Advisor to the Law Review. Her writing commitment, dedication, and friendship to the students at the Detroit College of Law is greatly appreciated.

¹ 806 F.2d 99 (6th Cir. 1986).
real estate was enforceable. The Sixth Circuit refused to fashion Ohio law that would permit the use of the doctrine of promissory estoppel to override a statute of frauds defense in a real estate context. The statute of frauds was an absolute bar to the contract action; nevertheless, the case was remanded for a new trial on the tort cause of action.

Factually, Seale purchased two buildings from Citizens Saving’s and Loan in 1980, at the suggestion of Robert Rogers, a director of Citizens and Seale’s accountant. The buildings were purchased in a sale-leaseback transaction, documented by a deed, a promissory note, a mortgage, and a lease. Before signing the documents, Seale commented to Rogers about the absence of a written repurchase agreement. At that time and subsequently on repeated occasions, Rogers assured Seale that they had a repurchase agreement, but no writing ever materialized.

Shortly thereafter, Rogers died and Citizens subsequently denied that it had any obligation to repurchase the real estate. Seale filed this suit against Citizens and its directors for breach of contract and fraud. At trial the jury was charged with answering special interrogatories. Their answers to the interrogatories included a finding that Rogers made an oral repurchase agreement with Seale, and that Seale would not have entered into the agreement in the absence of a repurchase agreement. The jury further found that Rogers was Citizens’ agent, and that Rogers did not intend to comply with the oral agreement. Finally, the jury found that failure to enforce the oral agreement would be “grossly unfair.” Based upon the jury’s findings, the district court ordered specific performance of the oral repurchase agreement.

Although Citizens alleged four errors on appeal, only one allega-

2. Id. at 101.
3. Id. at 104.
4. Id. at 106.
5. Id. at 101
6. Undoubtedly, this finding resulted from an interrogatory intended to illicit whether justice requires that the court grant a remedy. Promissory estoppel is an equitable doctrine applied to act as a substitute for consideration or the writing requirement of the statute of frauds. Accordingly, when the doctrine is applied, relief is only granted to avoid unfairness and injustice. See Restatement (Second) of Contracts § 139 comments a & b (1979). Interestingly, the comments note that the requirement of consideration is more easily displaced than the requirement of a writing.
7. 806 F.2d at 101.
tion is significant in the contracts law arena. Citizens argued that Ohio law does not recognize promissory estoppel where the statute of frauds would bar enforcement of an alleged agreement involving real estate. Stating that Ohio courts have never addressed this question, the Sixth Circuit was nevertheless persuaded that Ohio courts would be unwilling to apply the doctrine to statute of frauds cases involving real estate.\(^8\)

In reaching this conclusion, the Sixth Circuit, reviewed Ohio case law dealing with the importance of the statute of frauds writing requirement in a real property transaction. Citing to a 1921 case, *Newman v. Newman*,\(^9\) the court examined the rationale for a writing requirement in a real property transaction, even where equitable relief appeared appropriate. Furthermore, although Ohio has adopted the doctrine of promissory estoppel both as a substitute for consideration\(^10\) and as a substitute for writing,\(^11\) Ohio courts have never dealt directly with the question of dispensing with the writing requirement in a real estate transaction.\(^12\)

The Sixth Circuit's reluctance to extend the application of promissory estoppel to dispense with the writing requirement in a case involving real estate is understandable in light of the very special facts of the instant case. The purpose of the statute of frauds

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8. Id. at 102.
9. 103 Ohio St. 230, 133 N.E. 70 (1921).
10. The Sixth Circuit refers to Mers v. Dispatch Printing Co., 19 Ohio St. 3d 100, 483 N.E. 2d 150 (1985), as a case adopting Restatement (Second) of Contracts § 90 as Ohio law. Section 90 states the classic use of promissory estoppel, that of justifiable reliance dispensing with the requirement of consideration to avoid injustice:

   (1) A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise. The remedy granted for breach may be limited as justice requires.

Id.


11. A new section in the Restatement (Second) of Contracts, § 139, compliments § 90 by applying the reliance theory to an oral contract subject to the statute of frauds writing requirement. The Sixth Circuit opinion refers to Gathagan v. Firestone Tire & Rubber Co., 23 Ohio App.3d 16, 490 N.E. 2d 923 (1985), as the Ohio case adopting the legal principle. The reader might be initially confused when examining the case, since the Ohio Court of Appeals referred to and quoted the Restatement (Second) section with the Tentative Draft section number, § 217A.

12. 806 F.2d at 102.
writing requirement, as reiterated by the court, is to avoid fraud and mistake. In the Seale case, only Seale and Rogers were privy to the oral repurchase agreement. In light of Rogers’ death, only one party to the oral agreement is available for examination, thereby subjecting the terms of the repurchase agreement to the recollections of one individual. As indicated by the Sixth Circuit, had the agreement been reduced to a writing, there would be little opportunity for fraud, despite Rogers’ death.13

Nevertheless, the Ohio Court of Appeals’ case of Gathagan v. Firestone Tire & Rubber Co.,14 suggests that a different result could have been reached in the instant case. Gathagan adopted Section 139 of the Restatement (Second) of Contracts, to allow promissory estoppel to defeat the statute of frauds as a defense to an oral employment contract for two years. Rather than quoting the Restatement Second section directly, the Ohio court quoted it as used in a 1970 Hawaii case,16 as follows:

A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce the action or forbearance is enforceable notwithstanding the Statute of Frauds if injustice can be avoided only by enforcement of the promise. The remedy granted for breach is to be limited as justice requires.

(2) In determining whether injustice can be avoided only by enforcement of the promise, the following circumstances are significant:

(a) the availability and adequacy of other remedies, particularly cancellation and restitution;
(b) the definite and substantial character of the action or forbearance in relation to the remedy sought;
(c) the extent to which the action or forbearance corroborates evidence of the making and terms of the promise, or the making and terms are otherwise established by clear and convincing evidence;
(d) the reasonableness of the action or forbearance;
(e) the extent to which the action or forbearance was foreseeable by the promisor.16

13. Id. at 104.
14. See note 11 supra.
15. McIntosh v. Murphy, 52 Hawaii 29, 35-36, 469 P.2d 177, 181 (1970). Because the Ohio court quoted the Restatement (Second) section from a 1970 case, it refers to the Tentative Draft section number rather than the official section number. See note 11 supra.
16. Restatement (Second) of Contracts § 139 (1979). Ohio is the only state in the Sixth Circuit with a case cited under this section in the Case Citations to the Restatement
The Ohio Court of Appeals in *Gathagan*, then went on to state that in promissory estoppel cases, since each case turns on its own facts, whether the promisee's reliance is sufficient to justify estopping the promisor from raising the statute of frauds as a defense is a question of fact to be decided by the jury. Therefore, the *Gathagan* case required a remand for the jury to consider the issue of estoppel.

In the *Seale* case, it appears that the estoppel issue was placed before the jury in a series of interrogatories. Therefore, while the Sixth Circuit's reluctance to apply promissory estoppel and Restatement Second section 139 to the Seale oral repurchase agreement in light of Rogers' death appears appropriate, the approach of *Gathagan* will undoubtedly eventually be applied to a real estate transaction. While no case has been found applying section 139 to a real estate repurchase agreement, several cases have been decided applying the section to real property leases. Finally, it should be noted that prior to the drafting of section 139, promissory or equitable estoppel was used to defeat a statute of frauds bar. For example, in the 1965 case of *Oxley v. Ralston Purina Co.*, the Sixth Circuit finding no controlling Michigan law on the problem, affirmed the district court's use of the doctrine of equitable estoppel to avoid a statute of frauds bar to an oral contract which could not be performed within one year. The Sixth Circuit quoted Williston with approval, "We can see no good reason for

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of the Law.

18. 806 F.2d at 101.
21. 349 F.2d 328 (6th Cir. 1965).
22. Michigan cases applying equitable estoppel to oral contracts to convey real property were found.

If one party to an oral contract, in reliance upon the contract, has performed his obligation thereunder so that it would be a fraud upon him to allow the other party to repudiate the contract, by interposing the statute, equity will regard the contract as removed from the operation of the statute [of frauds].

23. 349 F.2d 328, 335-36 (1965).
limiting the operation of this equitable doctrine to any particular class of contracts included within the statute of frauds, provided always the essential elements of an estoppel are present . . . .”

II. THE MEASURE OF DAMAGES

A. Specific Performance

The case of Trans Union Credit Information Co. v. Associated Credit Services,\(^\text{25}\) raises the question of the availability of specific performance as a remedy for breach of a term of years service contract. The controversy arose as a consequence of a contract entered into by Trans Union Credit (TUC) and Credit Bureau of Cincinnati, Inc. (CBC) on September 11, 1985.

TUC is a national electronic data processing and credit reporting company, while CBC is the major local credit bureau in Cincinnati, with almost ninety-five percent of the market. TUC entered into negotiations with CBC to exchange credit reporting services, enabling TUC to postpone its plan to develop its own file of credit information on Cincinnati area residents.\(^\text{26}\) Under the agreement reached, each of the two parties would provide the other with unrestricted access to its computer file of credit information. The original agreement included a five-year term with successive five-year renewals. This term of the agreement was amended to provide for termination of the agreement after three years on six-month notice, if all of CBC’s stock were sold. Two weeks after executing the agreement, Associated Credit Service (ACS) made an offer to purchase all of CBC’s stock for twelve million dollars. Since ACS is a competitor of TUC, TUC attempted to block the sale of CBC’s stock with a temporary restraining order. TUC was unsuccessful in its attempt, and after ACS refused to give TUC assurance that it would perform the CBC-TUC service contract, and after ACS failed to give TUC a “test tape” necessary to transfer CBC’s database of credit information to TUC’s computer system, TUC renewed its motion for injunctive relief.\(^\text{27}\) On January 3, 1986, CBC sent TUC a letter terminating the agreement. The district court

\(^{24}\) Id. at 336 (quoting 3 Williston on Contracts § 533A, at 803 (3d ed. 1960)).
\(^{25}\) 805 F.2d 188 (6th Cir. 1986).
\(^{26}\) Id. at 190.
\(^{27}\) Id. at 191.
granted the injunction, which was subsequently lifted by a compromise of the parties to try all issues regarding the validity of the CBC-TUC credit information exchange agreement. The district court found that this service agreement was enforceable and granted specific performance of the contract to TUC.  

Three errors are raised on appeal. First it is contended that TUC repudiated the contract prior to CBC’s letter of January 3, formally terminating the agreement. Second, it is alleged that specific performance is an improper remedy because it compels long continuing performance between two adversarial parties. Finally, it is claimed that the district court’s specific performance decree is too imprecise and lacking in specificity to be enforceable.

With respect to the first issue, although the Sixth Circuit refers to several cases holding that a disagreement over contract interpretation does not constitute a contract repudiation, the court actually decides the case on the basis of the specific facts. The January 3rd letter sent by CBC to TUC attempting to terminate the agreement did not mention the subsequently claimed repudiation. Accordingly, the court found that if the repudiation had actually occurred, CBC would have mentioned it in the judicial proceedings or in its letter of January 3.

The more interesting question presented is whether specific performance is appropriate in light of the long-termed continuing nature of the service agreement. The Sixth Circuit correctly states the standard for determining whether specific performance should be awarded; specific performance is an equitable remedy awarded only where there is no adequate remedy at law. The problem is the lack of ability to compensate with dollars for the loss of CBC’s database. Because of CBC’s monopolistic position, TUC is unable to contract with a competitor and obtain the cover differential as a remedy.

The problem with the grant of specific performance in this case is not that there is an adequate remedy at law, but the compelled continuing performance obligations of the parties under the contract. Assuming the proper six month notice, the contract term be-

28. Id.
29. Id. at 192. DAN B. DOBBS ON REMEDIES 57 (1973) [hereinafter DAN B. DOBBS].
30. It should be noted that TUC does have access to this information outside the service agreement through procedures prescribed by the credit reporting trade association. Id.
between the parties is three years. The issue turns on whether the case requires too much continuing supervision by the court. Judicial resources are limited, accordingly, specific performance is frequently denied if the contract involves a lengthy performance which would require continuing supervision by the court. Historically in the construction contract arena, courts have denied specific performance stressing the difficulties of long-term supervision of a decree which orders a defendant to build or repair. The modern trend, however, is towards greater liberality in decreeing specific performance of such contracts. On the other hand, specific performance continues to be unavailable in personal service contracts, because of the inability of a court decree to create a good working relationship, and because such a decree is suggestive of involuntary servitude.

The service contract in the instant case is more similar to the construction contract than the personal service contract, since a relationship of individual employer and employee is not involved. Nevertheless, the problem of long continuing performance between competitive parties does exist. The Sixth Circuit answers this concern without case citation, by pointing to the trade association guidelines by which other competing credit bureaus must abide. The decision is consistent with the willingness of courts in recent decades to take on the supervision of complex school desegregation and legislative reapportionment plans.

Finally, the Sixth Circuit addressed the question of a lack of specificity with respect to the district court order. Every order granting injunctive relief must be specific in its terms. The court

32. Courts refused to specifically enforce contracts that call for complex acts over a period of time. This has particularly been true in cases seeking specific performance of construction contracts but also in contracts requiring continuing services of various kinds and in contracts requiring long term delivery of goods. This last category clearly appears to have been overturned by the Uniform Commercial Code, where it had not already been overturned by judicial decision. CALAMARI & PERRILLO, supra note 31, at 672-73 (footnotes omitted).
33. 5A CORBIN ON CONTRACTS §§ 1171-1172 (1963).
34. DAN B. DOBBS, supra note 29, at 63.
35. Although the services in the instant contract are unique, justifying specific performance, the services of a specific person are not required.
36. 805 F.2d at 193.
37. FED. R. CIV. P. 65(d) requires the specificity.
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rule applies to every decree of specific performance, and thus, such decrees, unlike other contract remedy orders, require specificity. Since the district court merely directed the parties to comply with the terms of the service agreement, the Sixth Circuit remanded the instant case with instructions that the district court expressly enumerate the obligations of each of the parties under the decree.38

B. Restitution

The case of Shearson/American Express, Inc. v. Mann,39 required an analysis of the appropriateness of restitution as a remedy in light of a mutual mistake of fact. In September of 1980, Mann contacted Shearson to get advice about selling Cox Electronic Systems stock. Although the knowledge of the parties at the time is unclear, it is undisputed that Cox Electronics had been purchased by a Utah corporation, Universal Energy, Inc.40 Shearson's employee quoted Mann a price per share in Universal Energy Corporation, a Washington corporation, and two months later, Mann directed the employee to sell the stock. Shearson took possession of Mann's Cox Electronics stock certificates, believing that they represented shares of Universal Energy Corporation. Mann received $26,500 for the stock, less a commission of $500 charged for the transaction. The sale proceeds were used by Mann as a down payment on three real estate investments.

Shearson eventually discovered the mistake regarding the two Universal Energy concerns. Since the brokered stock was actually worthless, Shearson purchased 4,000 shares of Universal Energy Corporation on the open market for $64,000 to cover the loss resulting from the mistaken sale.41 Shearson demanded that the sale be rescinded on the basis of mutual mistake, that Mann return the $26,500 and pay $64,000, the cost of purchasing the stock to cover Shearson's loss. Mann refused, and this cause of action was filed in the district court. The original complaint sought both restitution of the $26,500 and payment of $64,836.40.42 However, after numer-

38. 805 F.2d at 194.
39. 814 F.2d 301 (6th Cir. 1987).
40. Id. at 303.
41. Id.
42. Id. at 304. The $64,836.40 represented the cost of purchasing the stock on the open market plus a brokerage commission. Id.
ous pre-trial motions and orders, a hearing was held in December of 1985, at which time Shearson maintained that it only sought restitution. In January of 1986, the district court granted Shearson's motion for summary judgment. The district court held that Shearson was entitled to restitution of the $26,500, since it paid the money under the mistaken belief that the stock represented shares in Universal Energy Corporation, a Washington corporation, when in fact the stock represented shares in Universal Energy, Inc., a Utah corporation. The instant appeal to the Sixth Circuit resulted from this summary judgment.

These facts represent the classic case of mutual mistake, where the parties are mistaken as to the identity of the subject matter of the contract. A mutual mistake occurs when both parties are under substantially the same erroneous belief as to the facts. In deciding whether a contact is based upon a mistake of both of the parties, three factors are considered: whether the mistake is to a basic assumption on which the contract is made; whether the mistake has a material effect on the agreed exchange; and whether the risk of mistake has not been allocated to the disadvantaged party. The adversely affected party's remedy for mutual mistake is avoidance of the contract, entitling both parties to restitution.

Although the term restitution has a very flexible meaning, the basic premise of restitution is that a party must restore a benefit conferred to avoid unjust enrichment. The basic aim of a restitu-

43. Id.
45. Sherwood v. Walker, 66 Mich. 568, 33 N.W. 919 (1887), is a renowned case on mutual mistake. The contract involved the sale of a cow for $80. According to the seller, both he and the buyer believed the cow to be barren; the cow was in fact with calf. Accordingly, the Michigan Supreme Court held that the seller was entitled to avoid the contract if it was entered into with the understanding of both parties that the cow was barren and not capable of breeding.
46. This standard is set forth as follows in the RESTATEMENT (SECOND) OF CONTRACTS:
   Where a mistake of both parties at the time a contract was made as to a basic assumption on which the contract was made has a material effect on the agreed exchange of performances, the contract is voidable by the adversely affected party unless he bears the risk of the mistake under the rule stated in § 154.
tionary recovery is to place the plaintiff in the same economic position as he was in prior to the contracting.\(^49\) Finally, a mistaken party is not barred for relief because his negligence and failure to exercise reasonable care caused the mistake. In order to be precluded from relief, the mistaken party's fault must amount to a failure to act in good faith and in accordance with reasonable standards of fair dealing.\(^60\)

The Sixth Circuit correctly applied the law of mutual mistake and restitution to the instant facts. The mistaken fact was indeed a material one, going to the essence of the contract. Both parties were mistaken, and the stockbroker's negligence in failing to discover the mistake and resultant delay in giving notice of the mistake does not bar recovery unless it results in a detrimental change in position. As illustrated by the court, while it is true that Mann incurred new debt obligations as a consequence of the stock sale, the value of the mistaken payment has not been lost.\(^51\) Accordingly, Mann did not detrimentally change his position in reliance on the sale.

In reaching its decision, the Sixth Circuit relied heavily upon two Ohio cases.\(^52\) One of those cases, *Ohio Co. v. Rosemeier*,\(^53\) is almost exactly on point. In that case, a stock brokerage firm sought return of money paid to a client by mistake. The client had used the money to pay off her mortgage, a situation in which she argued constituted detrimental reliance, preventing the court from granting a recovery. The Ohio Court of Appeals found no detrimental reliance since the client had retained the value of the payment although it had changed form.\(^54\) From an analytical standpoint, the Sixth Circuit found the *Rosemeier* case indistinguishable from the

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49. **Calamari & Perrillo, supra** note 31, at 649.
50. A mistaken party's fault in failing to know or discover the facts before making the contract does not bar him from avoidance or reformation under the rules stated in this Chapter, unless his fault amounts to a failure to act in good faith and in accordance with reasonable standards of fair dealing. **Restatement (Second) of Contracts** § 157 (1979). As indicated by the comments to this section, the availability of relief would be severely circumscribed if barred by negligence.
51. 841 F.2d at 306.
53. *Id.*
54. 32 App.2d at 120, 288 N.E.2d at 329.
Finally, Mann asserted on appeal that restitution should not have been granted because Shearson only requested rescission and money damages. The Sixth Circuit responded by noting that Shearson's complaint also requested any additional relief to which it was entitled. The relationship between rescission and restitution should be noted. Rescission is an avoidance of a transaction, generally accompanied by restitution on both sides of the transaction. Accordingly, rescission is a part of many claims for restitution, particularly in circumstances involving mutual mistake, fraud and duress.

C. Damages Under a Reserve Bid Clause

One case during the survey period involving a damage question was decided solely on its facts within the unique and prestigious Kentucky industry of horse breeding. In *Mizan Arabians v. Pyramid Society*, the Sixth Circuit was faced with calculating the correct damages where a horse auctioneer has breached the consignment contract by selling a horse for less than the reserve bid price.

Mizan is in the business of breeding, showing, and selling Arabian horses. Mizan entered into a consignment agreement with Pyramid, a nonprofit organization dedicated to the breeding and promotion of purebred Egyptian and Egyptian-related horses, whereby one of Mizan’s horses was to be sold at auction by Pyramid. Under the terms of the agreement, Mizan could establish a minimum sale price for the horse by placing a “reserve bid” on the horse. A reserve bid of $65,000 was placed on this horse, by letter dated March 5, 1984. Furthermore, the agreement provided that Pyramid was entitled to receive a minimum commission fee of 12% of the reserve bid, regardless of whether the horse was sold at

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55. 814 F.2d at 306.
56. Id. at 307.
58. 821 F.2d 357 (6th Cir. 1987).
59. Id. at 358.
60. A reserve bid is used in auction sales to insure that a minimum price is arrived at. Reserve bids are used in conjunction with an auction with reserve. In an auction with reserve the auctioneer may withdraw the goods at any time until he announces completion of the sale. See U.C.C. § 2-238 (1978).
Prior to the auction, Pyramid requested that Mizan remove the reserve bid. It is disputed whether Mizan ever orally removed the reserve bid; the reserve bid was not revoked in writing. Nevertheless, Pyramid's auctioneer sold the horse for a final bid of $30,000, which was $35,000 less than the reserve bid. Mizan protested the sale to no avail, and eventually brought suit in the federal district court of Arkansas against the prospective buyers and Pyramid. A settlement agreement was reached with the buyers and legal title was conveyed by Mizan. Following this settlement, the instant cause of action was transferred to the Eastern District of Kentucky, where the case was resolved by a bench trial. The district court found that since there was no unequivocal revocation of the reserve bid, Pyramid had breached the consignment agreement by selling the horse for less than the reserve bid price. In computing the damage award, the district court determined that the fair market value of the horse was $30,000, and that the appropriate remedy was the difference between the sale price of $30,000 and the reserve bid of $65,000. The amount of $35,000 was then reduced by the $5,000 paid in settlement by the purchasers, and by $7,800, representing Pyramid's 12% commission.

On appeal the only issue before the Sixth Circuit was the method of calculating damages. Pyramid argued that the damages should be limited to the difference between the fair market value of the horse and the sale price of the horse, thus resulting in a recovery of zero damages. Pyramid argued that since it was unable to return the horse, the remedy should be limited to damages equal to the fair market value of the horse, found by the trial court to be the sale price of $30,000. The Sixth Circuit correctly and succinctly rejected this flawed argument. Mizan bargained for a minimum sale price of $65,000 (the reserve bid) or the return of the horse. Mizan did not bargain for the fair market value of the horse.

61. Mizan paid $5,000 as a pre-sale consignment fee, which was to be credited towards the 12% commission. 821 F.2d at 358.
62. Id.
63. The suit was started in Arkansas because the horse had been moved there, and Mizan sued to restrain its further movement until title rights could be adjudicated.
64. 821 F.2d at 359.
65. Fair market value was the sale price of the horse at auction in light of the fact that over four hundred prospective buyers had an opportunity to bid on the horse. Id.
In order to fulfill expectation interests, the proper measure of damages for contract breach must put the non-breaching party in the same position she would have been in had the contract been fully performed. Damages which are awarded for this purpose are called expectation or loss of the bargain damages because they are an attempt to give the aggrieved party the full value of her bargain which is the net gain she would have enjoyed had the contract not been breached. In the instant case, the $65,000 reserve bid is the standard against which such damages must be measured. As observed by the Sixth Circuit, adoption of Pyramid’s measure of damages would encourage auctioneers to disregard reserve bids, since the fair market value would generally equal the auction price. Damages would always equal zero, even though the auctioneer clearly violated the consignment agreement.

Consistent with the overall goal of maintaining the integrity of Kentucky’s leading industry, the Sixth Circuit held that an auctioneer who sells a horse for less than the reserve bid, and refuses to return the horse, is liable for the difference between the reserve bid and the price for which the horse sold at auction.

III. THE FINE LINE SEPARATING CONTRACTS FROM TORTS

A. Negligent Performance of a Contract

In Brock v. Consolidated Biomedical Laboratories, a diversity cause of action, the Sixth Circuit addressed the question of whether Michigan law recognizes a cause of action in tort for the negligent performance of a contract. The majority of the panel concluded that no cause of action exists in Michigan, commenting that if such an action existed there would be “no need for contract law”. The dissenter voted to reverse the district court’s dismissal.

66. At least in principle, a party’s expectation is measured by the actual worth that performance of the contract would have had to him, not the worth that it might have had to some hypothetical reasonable person. Damages based on expectation should therefore take account of any circumstances peculiar to the situation of the injured party, including his own needs and opportunities, his personal values, and even his idiosyncracies.

Farnsworth, supra note 47. See also Restatement (Second) of Contracts § 344 (1979).
67. 821 F.2d at 360.
68. 817 F.2d 24 (6th Cir. 1987).
69. Id. at 26.
of the negligence claim,\textsuperscript{70} for reasons set forth in the dissent to \textit{Haas v. Montgomery Ward}.\textsuperscript{71}

Factually, Brock agreed in writing to sell Clinical Biotest Laboratories, Inc. and its customer accounts to Consolidated Biomedical Laboratories (Consolidated). The contract provided that Brock would receive a percentage of Consolidated's revenues to be paid out of the business derived from Brock's previous accounts. However, the contract did not contain a due diligence clause. After the sale Consolidated engaged in allegedly faulty billing practices which Brock claimed drove away business. Brock filed this suit alleging three causes of action: breach of implied condition of the contract, negligent performance of the contract, and misrepresentation. A district court judge dismissed the first two claims for failure to state a cause of action.\textsuperscript{72} Subsequently Brock amended the complaint to allege breach of the contract by failing to perform in good faith, and retained the misrepresentation claim. The district court trial judge, following a bench trial, found for Consolidated on both counts, since Consolidated neither performed the contract in bad faith nor made any fraudulent misrepresentations.\textsuperscript{73} Brock's appeal in the instant case raised only the dismissal of the negligent performance of contract claim.

Accordingly, the only question before the Sixth Circuit was whether Michigan law recognizes a cause of action in tort for negligent performance of a contract. The failure of the panel to arrive at a unanimous decision, results from the frequently confusing fact that a tort action may arise in the context of misperformance of a contract. The classic fact pattern involved the common carrier, where the carrier would not only be liable for breach of contract when the train derailed, but also in tort for negligent injury to a passenger.\textsuperscript{74} As caselaw developed, American courts extended tort

\textsuperscript{70} Id.

\textsuperscript{71} 812 F.2d 1015 (6th Cir. 1987). The \textit{Haas} case involved an employment discrimination, wrongful discharge fact pattern. The case was decided by the same panel of judges as that of the instant case. The panel split on the same issue, the existence of a tort cause for negligent performance of contract. In \textit{Haas}, the tort claim charged negligent wrongful discharge based on negligent evaluation of job performance.

\textsuperscript{72} 817 F.2d at 25.

\textsuperscript{73} Id.

\textsuperscript{74} See Kelly v. Metropolitan St. R. R., 1 Q.B. 944 (1895); Webber v. Herkimer & Mohawk St., 109 N.Y. 311, 16 N.E. 358 (1888); Williamson v. Pacific Greyhound Lines, 67 Cal. App. 2d 250, 153 P.2d at 990 (1945).
liability for misfeasance to virtually every type of contract where defective performance may injure the promisee.\textsuperscript{75} Thus, physicians treating patients, beauty shops giving permanent waves, and suppliers of defective goods, just to mention a few examples, have been held liable in tort for their negligence which arose in a contract setting.\textsuperscript{76}

In order to establish a cause of action in negligence, three elements are required: a legal duty must exist, the defendant must fail to exercise ordinary care in the performance of that duty, and damage to the plaintiff must proximately result from the failure.\textsuperscript{77}

The problem element with establishing negligence in a contract context is the existence of a legal duty.

\begin{quote}
[While this duty of care, as an essential element of actionable negligence, arises by operation of law, it may and frequently does arise out of a contractual relationship, the theory being that accompanying every contract is a common-law duty to perform with ordinary care the thing agreed to be done, and that a negligent performance constitutes a tort as well as a breach of contract.\textsuperscript{78}]
\end{quote}

Based upon the quoted language, it would appear at least in Michigan that every breach of contract would also constitute a breach of the duty of care element, thereby establishing the tort claim. To the contrary, Michigan cases clearly differentiate between misfeasance of a contract performance, which is actionable in tort, and nonfeasance of a contractual obligation, which gives rise only to an action on the contract.\textsuperscript{79}

Thus, the tort action naturally arises in some contract breaches and not in others. While the line is not always clear as to where inaction ceases and misfeasance begins, the line appears to distin-

\begin{footnotes}
\footnote{75. \textsc{Prosser and Kee\textsuperscript{2}ton on the Law of Torts} § 92, at 660 (W. Keeton, D. Dobbs, R. Keeton \& D. Owen 5th ed. 1984) [hereinafter \textsc{Prosser \& Kee\textsuperscript{2}ton}).}
\footnote{76. Over the years, these numerous fact patterns developed into the specialized and individual tort claims of medical malpractice and product liability.}
\footnote{77. \textsc{Restatement (Second) of Torts} § 281 (19 ) \textsc{See}, \textit{e.g.}, Knight v. United States, 498 F. Supp. 315 (E.D. Mich. 1980).}
\footnote{78. The language is from the Michigan Supreme Court opinion in Clark v. Dalman, 379 Mich. 251, 261, 150 N.W.2d 755, 760 (1967), and is cited in the dissent to Haas v. Montgomery Ward, 812 F.2d at 1017. For a discussion of the case, see \textsc{supra} note 71.}
\end{footnotes}
guish whether the defendant’s performance, as distinct from her promise, has affected interests of the plaintiff beyond the expected benefits of the contract.\textsuperscript{80} When applied to employment discharge cases, “the affirmative act of discharging an employee is uniformly considered to be no more than non-performance of the agreement to continue employment,”\textsuperscript{81} and therefore not actionable as a tort.

When this demarcation is applied to the instant facts, the majority properly affirmed the district court’s dismissal for failure to state a cause of action. Consolidated’s alleged failure to properly perform the contract affected only Brock’s expected benefits under the contract itself. There was no breach of duty distinct from the breach of contact to create an actionable tort.

B. Disclaimers of Reliance

The case of \textit{AgriStor Leasing v. Saylor},\textsuperscript{82} addressed without determining the effect of a disclaimer of reliance in a contract on a claim for tortious misrepresentation. The concurring opinion drew a definite distinction between disclaimers of liability and disclaimers of reliance, and found that a contract which contains a valid disclaimer of reliance, in the absence of competent evidence to the contrary, may be enough to justify granting a motion for judgment notwithstanding the verdict of a tortious misrepresentation action.\textsuperscript{83} The majority opinion deferred to the decision of the district court construing Tennessee law to hold contract disclaimers ineffective to limit liability for misrepresentations.\textsuperscript{84}

Early in 1980, the Saylors, were approached by Dowdy, a sales representative of Hermitage Harvestore Systems, to purchase feed storage structures and related equipment for their dairy farm. The Harvestore feed storage system was represented to the Saylors, through the literature of the manufacturer, A.O. Smith Harvestore Products, Inc. (AOSHPI), and orally by Dowdy, as being “oxygen limiting”.\textsuperscript{85} This feature of the Harvestore feed storage system was supposed to keep the feed virtually airtight, prevent spoilage, and

\textsuperscript{80} \textsc{Prosser} \& \textsc{Keeton}, \textit{supra} note 75, § 92, at 661-62.

\textsuperscript{81} \textit{Id.} Accordingly, the majority opinion correctly decided \textit{Haas v. Montgomery Ward}, an employment discharge case, discussed at note 71 \textit{supra}.

\textsuperscript{82} 803 F.2d 1401 (6th Cir. 1986).

\textsuperscript{83} \textit{Id.} at 1410.

\textsuperscript{84} \textit{Id.} at 1407.

\textsuperscript{85} \textit{Id.} at 1403.
increase milk production in dairy cows. Dowdy showed the Saylors a film called “The Harvestore System” and a book published by AOSHPI entitled *The Winning System*. Both the movie and the book were promotional materials which praised the capabilities of the Harvestore structures. ⁸⁶ In March, the Saylors contacted to purchase the Harvestore system from Hermitage. The contract was subsequently financed through AgriStor Leasing Company.

The Harvestore structures were operational by July, and within one month the Saylors’ dairy herd began to develop problems. In the following year the cows’ condition steadily worsened, and veterinarians contacted to treat the problem could not ascertain the source of the cows starvation. ⁸⁷ Early in 1982, the Saylors finally liquidated the remaining herd, and defaulted on their payments to AgriStor. AgriStor repossessed the equipment and in October of 1983, filed this suit for the deficiency. The Saylors answered and filed a third-party complaint against the instant appellants; Dowdy, Hermitage and AOSHPI, seeking damages caused by the defective product and the misrepresentations made about the product.

The Saylors confessed judgment on the AgriStor claim and a summary judgment was granted as to the remaining payments. The Saylors’ claim against the three appellants were tried to a jury, which returned joint and several verdicts against all three appellants for one million dollars in compensatory and punitive damages.

Numerous issues were appealed to the Sixth Circuit, however, the instant opinion discussed only three in detail, one being dispositive and requiring a new trial. The Sixth Circuit determined that the district court’s failure to instruct the jury concerning the statute of limitations constituted reversible error. Throughout the trial the appellants maintained that the action was barred by the statute of limitations because Saylor knew of the cause of injury to the cows and of the alleged tortfeasors more than three years prior to filing the complaint. Testimony adduced at trial was conflicting on this question. Accordingly, the jury should have been instructed to decide when the Saylors knew the occasion, manner and means

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⁸⁶ *Id.*
⁸⁷ *Id.*
by which the injury to their property occurred.\textsuperscript{88}

The Sixth Circuit also addressed the award of punitive damages. Tennessee law permits punitive damages in cases involving fraud.\textsuperscript{89} Thus, the misrepresentations would have to be fraudulent in order to approve punitive damages. The Sixth Circuit found that there was sufficient evidence presented to go to the jury on the question of whether the misrepresentations were fraudulent, and therefore, the instructions on punitive damages was proper. Two of the appellants contended that punitive damages could not be awarded, because their financial condition had not been established at trial. The Sixth Circuit applied Tennessee law that punitive damages may be awarded against joint tortfeasors when the financial worth of only one of the tortfeasors is introduced in evidence.\textsuperscript{90}

From a contracts law standpoint, the most interesting discussion in the instant case involved the disclaimer language of the purchase agreement:

\begin{quote}
ACKNOWLEDGEMENT AND RELIANCE
I HAVE READ AND UNDERSTOOD THE TERMS AND CONDITIONS OF THIS PURCHASE ORDER INCLUDING THE WARRANTIES, DISCLAIMERS AND TERMS AND CONDITIONS HEREIN GIVEN TO ME, EITHER BY THE MANUFACTURER OR THE SELLER. I RELY ON NO OTHER PROMISES OR CONDITIONS AND REGARD THAT AS REASONABLE BECAUSE THESE ARE FULLY ACCEPTABLE TO ME.\textsuperscript{91}
\end{quote}

Appellants argued that they were not liable to the Saylors on the fraudulent misrepresentation claim because this disclaimer clause precluded the Saylors from relying on the published and oral representations concerning the Harvestore system. Since reliance is a necessary element in a misrepresentation cause of action,\textsuperscript{92} a failure to rely on the representation would prevent recovery. The district court, however, refused to give this effect to the disclaimer, denied the request for summary judgment, submitted the tortious misrepresentation claims to the jury, and subsequently denied a directed verdict on the basis of the disclaimer.\textsuperscript{93} The Sixth Circuit,

\textsuperscript{88} Id. at 1406.
\textsuperscript{89} Inland Container Corp. v. March, 529 S.W.2d 43 (Tenn. 1975).
\textsuperscript{90} Huckeby v. Spangler, 563 S.W.2d 555 (Tenn. 1978).
\textsuperscript{91} 803 F.2d at 1406.
\textsuperscript{92} PROSSER & KEETON, supra note 75, § 105, at 728.
\textsuperscript{93} 803 F.2d at 1407.
affirmed the district court, reiterating the deference which is given to district judges sitting in diversity cases interpreting state law. The concurrence viewed the disclaimer language as a disclaimer of reliance rather than a disclaimer of liability, and found "no reason that a contractual disclaimer of reliance cannot be used as evidence . . . of whether the plaintiff had relied upon the misrepresentation."94

Undoubtedly, there is a difference between a disclaimer of liability and a disclaimer of reliance, although the Tennessee cases do not clearly differentiate between the two.95 Nevertheless, it is indeed troublesome to permit the appellants to disclaim all reliance that the Saylors may have placed on the movie and book used to describe the Harvestore system with a paragraph in the standard form contract used by the manufacturer and dealer. The appellants extensively used these promotional marketing materials, expecting that they would help to consummate sales. Permitting such reliance to be negated by a disclaimer is akin to permitting all express warranties to be disclaimed including a description of the goods which amounts to an express warranty. Both the Uniform Commercial Code and its chief commentators disapprove of such an inconsistent and unfair analysis.96 The manufacturer and dealer used substantially more than salesperson's puffing to sell the feed storage system. It is unlikely that the reliance based upon these extensive marketing tools is negated by a paragraph in the standard contract drafted by the manufacturer or dealer.

94. Id. at 1410.


96. We hope courts will reach similar conclusions and strike down attempted disclaimers in cases in which the seller includes a description of the article which amounts to a warranty and then attempts to disclaim all express warranties. To illustrate further: assume that the sales contract describes machinery to be sold as a "haybaler" and then attempts to disclaim all express warranties. If the machine failed to bale hay and buyer sued, we would argue that the disclaimer is inoperative. In our judgment, the description of the machine as a "haybaler" is a warranty that the machine will bale hay and, in the words of 2-316, a negation or limitation ought to be "inoperative" since it is inconsistent with the warranty.

IV. RISK OF LOSS

In Commonwealth Propane Co. v. Petrosol International, Inc., the Sixth Circuit applied Ohio's version of the Uniform Commercial Code to allocate risk of loss among an original seller, a middleperson, and the ultimate buyer where an underground propane gas storage facility collapsed and the stored gas could no longer be removed.

In 1982, Cal Gas Corporation (Cal Gas) contracted to sell Petrosol International, Inc. (Petrosol) 10,000 barrels of propane stored at an underground storage facility for a price of fifty-seven cents per gallon, to be delivered on demand on or before March 31, 1983. According to the purchase acknowledgment form:

Deliveries shall be made as, when and where specified on the reverse hereof. Title to products delivered shall pass to Buyer upon completion of loading thereof into tank trucks furnished by Buyer, upon delivery thereof in a tank car to carrier, upon arrival thereof in a tank truck furnished by Seller alongside unloading facilities at destination, or as specified on the reverse hereof, as the case may be.

Petrosol immediately sold the propane to Commonwealth Propane Company (Commonwealth) for fifty-eight cents per gallon. The sales acknowledgment form sent by Petrosol to Commonwealth provided in relevant part:

Title to products delivered shall pass to Buyer upon completion of loading the same into tank trucks, upon delivery of products in a tank car to carrier, upon delivery thereof in a tank truck furnished by Seller alongside Buyer's storage facilities at destination, or as stipulated on the face hereof, as the case may be. Thereafter Buyer shall bear all risk of and be solely liable for any loss or damage caused by or attributable to said products, or to their transportation, care, handling, resale or use.

On the front of the acknowledgment form was the caption “to be delivered” next to five boxes indicating types of delivery methods. However, none of the boxes were marked.

After receiving Petrosol’s payment, Cal Gas sent a confirmation

97. 818 F.2d 522 (6th Cir. 1987).
98. Id. at 524.
99. Id. at 526. The district court found this language from the purchase acknowledgment form to be determinative of when risk of loss passed.
100. Id. at 528. The district court found this language from the sales acknowledgment form to be determinative of when risk of loss passed.
of distribution form to the underground facility indicating a product flow from Cal Gas to Petrosol to Commonwealth. A confirmation of distribution form was also mailed to Petrosol. A second transaction with the same three parties for an additional 10,000 barrels of propane on the same contract terms occurred in November of 1982. Identical paper work was used by the parties. In February of 1983, a wall in the underground storage facility collapsed, and the 20,000 barrels of propane subject to the agreements of these three parties was lost or destroyed before Commonwealth was able to remove it. Commonwealth brought the instant action against Petrosol and Cal Gas for damages based upon breach of contract. Both parties defended by asserting that the propane had been delivered to Commonwealth and that risk of loss had passed upon delivery. Petrosol also cross-claimed against Cal Gas, contending that Cal Gas had not delivered the propane, and that consequently, risk of loss fell on Cal Gas. The district court granted Commonwealth summary judgment against Petrosol, and Petrosol was granted summary judgment against Cal Gas, on the basis of the previously quoted purchase acknowledgment and sales acknowledgment forms. In both cases the district court found that risk of loss was governed by the agreements of the parties, and that risk of loss had not passed from the seller to the buyer in either transaction.

The major issue on appeal was which of the three parties bore the risk of loss as to the stored propane. The Sixth Circuit correctly looked to the Uniform Commercial Code as adopted in Ohio to resolve the issue. In applying that provision, the first question

101. Id. at 525.
102. The Ohio version of § 2-509 of the Uniform Commercial Code provides as follows:

(A) Where the contract requires or authorizes the seller to ship the goods by carrier:

(1) if it does not require him to deliver them at a particular destination, the risk of loss passes to the buyer when the goods are duly delivered to the carrier even though the shipment is under reservation as provided in section 1302.49 of the Revised Code; but

(2) if it does require him to deliver them at a particular destination and the goods are there duly tendered while in the possession of the carrier, the risk of loss passes to the buyer when the goods are there duly so tendered as to enable the buyer to take delivery.

(B) Where the goods are held by a bailee to be delivered without being moved, the risk of loss passes to the buyer:

(1) on his receipt of a negotiable document of title covering the goods; or
is whether the agreement of the parties allocates risk of loss.\textsuperscript{103} Under the Code's overall philosophy of freedom of contract, the parties are free to allocate risk of loss in their agreement. However, in the absence of agreement, the Code allocates risk of loss among the parties, based upon the fact pattern of the individual case. Different subsections apply, depending on whether the contract involves: (1) goods delivered by a common carrier; (2) goods held by a third party bailee to be delivered without being moved; or (3) goods delivered directly from seller to buyer without the participation of a third party carrier or bailee. These three fact patterns cover the subsections of the risk of loss provisions.

In the instant case, if the agreement of the parties does not govern, the Code subsection dealing with goods held by a third party bailee applies, since the goods were stored at Lake Underground Storage.\textsuperscript{104}

The Sixth Circuit addressed each contract separately. First, the court examined the contract between Cal Gas and Petrosol, and specifically the purchase acknowledgment language relied on by the district court. The Sixth Circuit rejected the finding of the district court that the language concerning passage of title from the purchase acknowledgment constituted a contrary agreement of the parties allocating the risk of loss. Under the Code, risk of loss is a separate and distinct question from passage of title. Accordingly, title passage does not determine when risk of loss passes. Since the contract between Cal Gas and Petrosol did not allocate risk of loss, the Code subsection covering goods held by a third party bailee

\begin{itemize}
\item[(2)] on acknowledgment by the bailee of the buyer's right to possession of the goods; or
\item[(3)] after his receipt of a non-negotiable document of title or other written direction to deliver, as provided in division (D)(2) of section 1302.47 of the Revised Code.
\item[(C)] In any case not within division (A) or (B) of this section, the risk of loss passes to the buyer on his receipt of the goods if the seller is a merchant; otherwise the risk passes to the buyer on tender of delivery.
\item[(D)] The provisions of this section are subject to contrary agreement of the parties and to the provisions of sections 1302.40 and 1302.54 or the Revised Code.
\end{itemize}


\textsuperscript{103} Subsection (D) of § 1302.53, \textit{supra} note 102, authorizes controlling contrary agreement of the parties.

\textsuperscript{104} Subsection (B) of § 1302.53, \textit{supra} note 102, allocates risk of loss when goods are held by a third party bailee, like a warehouse or grainary, or in this case, an underground storage facility.
governed. The propane was held by a bailee to be delivered without being moved, and the risk of loss passed when Cal Gas sent its confirmation of distribution form to both Petrosol and Lake Underground, the storage facility. At that time, both the buyer, Petrosol, and the bailee, Lake Underground, knew that the goods were being held for the buyer rather than for the seller, Cal Gas, and under the Code provision risk of loss passed to the buyer, Petrosol. Accordingly, the Sixth Circuit reversed the district court’s grant of summary judgment for Petrosol, and remanded the case for entry of summary judgment in favor of Cal Gas.

Allocation of risk of loss between Petrosol and Commonwealth was not as easy according to the court. The sales acknowledgment form did allocate risk, but only in conjunction with delivery of the goods. Since no method of delivery box was checked on the form, the language on the sales acknowledgment form was not conclusive. Furthermore, the term of the agreement, providing free storage for five months, was inconsistent with the sales acknowledgment’s risk of loss language. The Sixth Circuit held, in light of this factual dispute, that the issue of risk of loss was inappropriate for summary disposition. Therefore, the court reversed the district court’s grant of summary judgment to Commonwealth, and remanded the action for further proceedings.

105. Id.
106. 818 F.2d at 528.
107. Id. at 531.