Michigan Law Review

Volume 47 | Issue 4

1949

CONTRACTS-DUTY TO MITIGATE DAMAGES UPON ANTICIPATORY BREACH OF FORWARD CONTRACT OF SALE

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COMMENTS

CONTRACTS—DUTY TO MITIGATE DAMAGES UPON ANTICIPATORY BREACH OF FORWARD CONTRACT OF SALE—The theory of our law in regard to damages for breach of contract has been to give the innocent party as nearly as possible what he would have received had the contract been performed. To this end, our courts have worked out a rough formula which has been described by Professor Grismore as follows:

> ". . . The promisee is, in general, entitled to recover the economic equivalent of the performance promised, at the time and place fixed in the contract, plus any losses incurred or gains prevented through not receiving it, less any savings that have resulted to the promisee from not having to perform his own undertakings under the contract."[1]

In the case of contracts of sale, this formula can be expressed in the ordinary situation as the difference between contract price and market price at the time and place for delivery. The authorities are reasonably in accord on this proposition.[2] Expressions indicating market at time

[1] GRISMORE, CONTRACTS, § 191 at p. 306 (1947).

[2] Sedgwick, "Replacement in the Market," 12 COL. L. REV. 519 (1912); 5 WILLISTON, CONTRACTS, rev. ed., § 1397 (1937); 2 SEDGWICK, DAMAGES, 9th ed., § 636 (d) (1912).

of breach as the true measure can often be explained by the fact that market at breach and market at time for performance are identical and used interchangeably by the courts.[3]

When discussing anticipatory breach, however, these dates must be carefully differentiated, since there is often a wide divergence in time and hence a likely change in value between the date of breach and the date for performance. If suit is brought before the time when the contract would have been performed, prices at the date of breach may be the only available evidence on which to base damages; but otherwise, there is no logical reason for distinguishing these cases from the ordinary, present breach, and again the authorities unite in holding that the proper measure of damages is the difference between contract price and market price at time and place for performance.[4]

Another element must be considered at this point, however. As the period of time between breach and expected performance lengthens, so do the opportunities by which the innocent party may avoid or materially reduce the damages arising from the breach. The familiar rule of mitigation[5] seems to indicate that it is his "duty" to take such steps when reasonable. Thus it would seem that upon repudiation of a forward contract in a favorable market, the buyer must cover or the seller must unload to avoid or reduce his damages.

This is the rule in England,[6] but the American textwriters, still in virtual unison, proclaim that the innocent party has no duty to make such a forward contract in mitigation.[7] It will be the purpose of this paper to examine the cases on this proposition and to analyze the American position from the standpoint of precedent and logic.[8]

[3] Sedgwick, "Replacement in the Market," 12 COL. L. REV. 519 (1912); Mutual Rice Co. of Louisiana v. Star Bottling Works, 163 La. 159, 111 S. 661 (1927); Gate City Cotton Mills v. Rosenau Hosiery Mills, 159 Ala. 414, 49 S. 228 (1909).

[4] GRISMORE, CONTRACTS, § 191 (1947); 5 WILLISTON, CONTRACTS, rev. ed., § 1397 (1937); 2 SEDGWICK, DAMAGES, 9th ed., § 636 (d) (1912).

[5] 1 CONTRACTS RESTATEMENT § 336 (1) (1932). "Damages are not recoverable for harm that the plaintiff should have foreseen and could have avoided by reasonable effort without undue risk, expense, or humiliation."

[6] Roth & Co. v. Taysen, Townsent & Co., 73 L.T. 628, 12 T.L.R. 211, 1 Com. Cas. 306 C.A. (1896) (repudiation by buyer); Melochrino v. Nickoll & Knight, (1920) 1 K.B. 693, 89 L.J.K.B. 906, 122 L.T. 545 (repudiation by seller).

[7] 5 WILLISTON, CONTRACTS, rev. ed., § 1397 (1937); 2 SEDGWICK, DAMAGES, 9th ed., § 636 (f); Limburg, "Anticipatory Repudiation of Contracts," 10 CORN. L.Q. 135 (1924).

[8] In re Marshall's Garage, Inc., First Nat. Bank of North Bennington v. Surdam, (C.C.A. 2d, 1933) 63 F. (2d) 759; Stephen M. Weld & Co. v. Victory Mfg. Co., (D.C. N.C. 1913) 205 F. 770; Barnett v. Elwood Grain Co., 153 Mo. App. 458, 133 S.W. 856 (1911).

I

JUDICIAL DECISIONS

A. *Denying the Duty to Mitigate.* The cases on this point are particularly difficult to analyze; first, because the date employed in measuring damages is often the only indication that the court is imposing a duty to mitigate,[9] and in many of the cases the question of fluctuation in the market has not been considered, so that it is impossible to tell what date the court is using; and second, because other elements in the doctrine of anticipatory breach may enter the picture to cloud the result.

The latter factor is illustrated particularly by a number of Pennsylvania cases which, adopting the language of Cockburn, J., in *Frost v. Knight*,[10] have refused to find a breach until the repudiation was unequivocally accepted.[11] The question of repudiation is beyond the scope of this comment, but, since these decisions have not regarded the contract as being breached, their dicta denying a duty to mitigate cannot be accepted as significant authority.[12] In fact, there is dictum in one Pennsylvania case which suggests that a duty might be imposed once the repudiation was accepted.[13] Furthermore, the English authorities make it clear that a court may require an unequivocal acceptance of repudiation and still impose a duty to mitigate.[14]

A line of decisions in New York flatly refuses to impose a duty,[15] but the results are based squarely on the language of the Uniform Sales Act,[16] and there is evidence that such was not always the law of that state.[17]

[9] In view of the rules discussed supra, it would seem that the only reasons for basing damages on market value at the time of repudiation are either that the plaintiff has covered and the court is protecting his privilege or that the court is imposing a duty of mitigation.

[10] (1872), L.R. 7 Exch. Ill.

[11] Zuck v. McClure & Co., 98 Pa. 541 (1881); Honesdale Ice Co. v. Lake Lodore Improvement Co., 232 Pa. 293 (1911) 81 A. 306; Barber Milling Co. v. Leichthammer Baking Co., 273 Pa. 90, 116 A. 677 (1922).

[12] A similar position has been taken by the Illinois courts, Roebling's Sons' Co. v. Lock Stitch Fence Co., 130 Ill. 660, 22 N.E. 518 (1889); Reid, Murdoch & Co. v. Somerset Canning Co., 182 Ill. App. 112 (1913); Kadish v. Young, 108 Ill. 170 (1883). The majority of modern American decisions requires the innocent party to accept the repudiation as a breach when failure to do so would result in increasing the damages. See GRISMORE, CONTRACTS, § 196 (1947) and cases cited. Also 66 A.L.R. 746 (1930).

[13] Kahn & Feldman, Inc. v. Herbert, 279 Pa. 440, 124 A. 125 (1924).

[14] Roth & Co. v. Taysen, Townsent & Co., 73 L.T. 628, 12 T.L.R. 211, 1 Com. Cas. 306 C.A. (1896) (no duty to mitigate until plaintiff actually accepted the repudiation by bringing suit).

[15] Segall v. Finlay, 245 N.Y. 61, 156 N.E. 97 (1927); Goldfarb v. Campe Corp., 99 Misc. 475, 164 N.Y.S. 583 (1917).

[16] N.Y. Consol. Laws (McKinney, 1938). Personal Property Act §§ 145, 148.

[17] Dillon v. Anderson, 43 N.Y. 231 (1870) (actually not a contract of sale); Farrish Co. v. Harris Co. 122 Misc. 611, 204 N.Y.S. 638 (1924) (not clear that this was anticipatory breach).

It is almost impossible to assign a definite stand on this matter to the federal courts. *Missouri Furnace Co. v. Cochran*[18] denies the duty. However, this case also denies the privilege of covering (i.e., plaintiff is not allowed damages for losses incurred by him in an effort to avoid injury by entering a substitute contract), and it is so much out of line with modern authorities on this point[19] that its holding on the collateral issue of a duty to mitigate is open to question. *Roehm v. Horst*[20] was one of the first cases to distinguish between a privilege to cover for self protection and a duty to cover in mitigation of damages. Since it involved solely the former problem, its expressions on the question of duty are no more than dicta, and even as such are not explicit.

The position expressed by Judge Learned Hand in *Callan v. Andrews*[21] is particularly perplexing. The decision would seem to limit the duty or even the privilege to those peculiar cases in which there is an organized market for futures (e.g. cotton, grains, etc.), yet his analysis indicates support of a more extensive application.[22] *Hinckley v. Bessemer Steel Co., Ltd.*,[23] is often cited as denying a duty to mitigate, but the decision may be distinguished on its facts. The state of the market was such that it might well have been considered unreasonable for plaintiff to proceed, and it further appears that, even had he acted, plaintiff would have been able to retain any profits on the theory that they were independent of the contract in question.

B. *Recognizing the Duty to Mitigate.* A careful search of the American cases has failed to reveal any which imposes a duty to mitigate on such unequivocal facts as those present in the English cases.[24] There are so many, however, announcing it obiter dicta or adopting analogous principles, one is led to believe that imposition of the duty has more merit than is generally attributed to it.

The difficulty in finding case authority stems from the fact that there are a number of decisions in which plaintiff is insisting on his right to recover for injury sustained through actually making a substitute forward contract;[25] and, as pointed out above, granting a privilege to cover differs greatly from imposing a duty. Such decisions aside, there are still many courts which in effect, if not in terms, impose a duty. Thus, the Michigan

[18] (C.C. Pa., 1881) 8 F. 463.

[19] Roehm v. Horst, (C.C.A. 3d, 1898) 91 F. 345, affirmed, 178 U.S. 1, 20 S.Ct. 780 (1899); 5 WILLISTON, CONTRACTS, rev. ed., § 1397 (1937).

[20] (C.C.A. 3d, 1898) 91 9. 345, 178 U.S. 1, 20 S.Ct. 780 (1899).

[21] (C.C.A. 2d, 1931) 48 F. (2d) 118.

[22] Id. at 120.

[23] 121 U.S. 264, 7 S.Ct. 875 (1887).

[24] See note 6, supra.

[25] Cron & Dehn, Inc. v. Chelan Packing Co., 158 Wash. 167, 290 P. 999 (1930); Hebron Mfg. Co. v. Powell Knitting Co., (C.C.A. 3d, 1909) 171 F. 817; Renner Co. v. McNeff Bros., (C.C.A. 6th, 1939) 102 F. (2d) 664; United States v. Harris, In re Chinook Lumber & Mfg. Co., (C.C.A. 9th, 1938) 100 F. (2d) 268.

court, in *Goldsmith v. Stiglitz*,[26] held that it was error to measure damages as of the last day for delivery when the seller, after repudiation, held the goods in a falling market. An Alabama court imposed a duty by measuring damages on the basis of market price at the time of repudiation; this was confirmed in principle on appeal, although reversed because present rather than forward prices were used in computing the amount of recovery.[27] In Georgia, the duty was imposed in a case directly in point.[28] Two Kansas cases clearly specify the duty, although this was not essential to their holdings.[29]

It was pointed out in the preceding section that some federal cases indicate an absence of duty in this situation, but there are decisions in the federal courts giving an opposite slant. In *Skeele Coal Co. v. Arnold*,[30] the court charged plaintiff with the profit he could have made from production after the repudiation, although he did not actually produce up to the amount indicated in the contract. The decision in *Crane Iron Works v. Cox & Sons Co.*[31] also indicated that the seller is required to mitigate, but the court did not actually impose the duty, since the question of reasonable measures of mitigation was left for the jury. *Samuels v. E. F. Drew & Co., Inc.*,[32] although probably not a case of anticipatory breach, contains significant language bearing on this question.[33]

II

COMPARISON OF OTHER APPLICATIONS OF THE DUTY TO MITIGATE

Turning from the cases, which are manifestly inconclusive, one may gain some insight by re-examining the duty to mitigate damages as a general proposition. The rule is firmly established that the innocent party must take steps to mitigate after a present breach,[34] and it further appears settled that under the proper circumstances he may be required

[26] 228 Mich. 255, 200 N.W. 252 (1924) (sale of rice).

[27] Jebeles & Colias Confectionary Co. v. Stephenson, 6 Ala. App. 103, 60 S. 437 (1912).

[28] Mendel v. Converse & Co., 30 Ga. App. 549, 118 S.E. 586 (1923).

[29] Central Lumber Co. v. Arkansas Valley Lumber Co., 86 Kan. 131, 119 P. 321 (1911) (appears to be a present breach); York-Draper Mercantile Co. v. Lusk, 6 Kan. App. 629, 49 P. 788 (1897); 45 Kan. 182, 25 P. 646 (1891) [duty not actually imposed since seller (defendant) failed to prove that market at repudiation was actually favorable].

[30] (C.C.A. 2d, 1912) 200 F. 393.

[31] (C.C.A. 3d, 1928) 28 F. (2d) 328; see also Cox & Sons Co. v. Crane Iron Works, (C.C.A. 3d, 1925) 5 F. (2d) 314.

[32] (C.C.A. 2d, 1923) 292 F. 734.

[33] Id. at 738: "When it is established that on the date of the breach the claimant could have entered into similar contracts for similar deliveries, the only damages to which he is entitled are represented by the difference between the contract price and the price at which he could have secured such contracts."

[34] CONTRACTS RESTATEMENT, § 336 (1932); GRISMORE, CONTRACTS, § 194 (1947).

to take positive steps looking far into the future.[35] It also seems to be fairly well accepted that the rule of mitigation extends in full force to a case of anticipatory breach when the contract is one for the manufacture of goods or for work and labor.[36] Why does the same rule not apply in the case of anticipatory breach of a forward contract of sale?

Even the authorities who deny the duty in the case of such contracts recognize an exception where commodities for which there is a standard futures market are concerned.[37] Although the explanation offered is that such a futures contract has a present value which is the true measure of damage, the distinction is no more than one of degree in either theory or practice. Some commodities are dealt with in terms of futures more regularly, but the very fact that the basic problem treated here is breach of forward contracts would seem to limit discussion to goods in which there is a potential market for future deliveries.[38]

Another seemingly inconsistent distinction is made by those authorities who deny the duty to mitigate when plaintiff seeks only the normal measure of damages (i.e., contract price less market at time for performance), but impose a duty if the plaintiff is seeking consequential damages (e.g., loss of resale).[39] Again it seems doubtful that this is any more than a difference in degree, since the aim in either case is to give the plaintiff what he has lost by default of the contract.

III

POLICY CONSIDERATIONS

The reasons generally assigned for the denial of a duty in the case of a forward contract of sale are: (1) that it would be an undue burden to require an innocent party to guess the future turnings of a fickle market; and (2) that the innocent party should be able to use any money or credit available to him for his own benefit.[40]

[35] Jefferson Storage Corp. v. Kessler, (C.C.A. 6th, 1941) 125 F. (2d) 108; National Surety Corp. v. State, 169 Misc. 479 (1938), 8 N.Y.S. (2d) 77; Pandaleon v. Brecker, 227 Mich. 297, 198 N.W. 953 (1924); Thayer Export Lumber Co. v. S. E. Naylor, 100 Miss. 841, 57 S. 227 (1911); Northern Supply Co. v. Wangard, 123 Wis. 1, 100 N.W. 1066 (1904).

[36] 5 WILLISTON, CONTRACTS, rev. ed., §§ 1298, 1397 (1937); GRISMORE, CONTRACTS, § 196 (1947) and cases cited.

[37] 2 SEDGWICK, DAMAGES, 9th ed., § 636 (e) (1912); 3 WILLISTON, SALES, rev. ed., § 588 (1948); see also the language of Judge Learned Hand in Callan v. Andrews, (C.C.A. 2d, 1931) 48 F. (2d) 118 at 120 et seq.

[38] Compare the language in Samuels v. E. F. Drew & Co., In re El Dorado Oil Works, (C.C.A. 2d, 1923) 292 F. 734 at 739: "The rule is applicable not only to commodities dealt in on the exchange where futures are bought and sold, but extends to all standard commodities having a market for future deliveries."

[39] 2 SEDGWICK, DAMAGES, 9th ed. § 636 (f) at 1257 (1912); Barnett v. Elwood Grain Co., 153 Mo. App. 458, 133 S.W. 856 (1911).

[40] 5 WILLISTON, CONTRACTS, rev. ed., § 1397 (1937); Limburg, "Anticipatory Repudiation of Contracts," 10 CORN. L.Q. 135 (1924).

Admittedly, the motive to protect the innocent party is justifiable, but it is submitted that adequate protection is given under a normal application of the doctrine of mitigation. If the market is in a state of agitation so that any predictions for the future would be pure guesswork, it would seem clear that making a forward contract would be unreasonable, and the rule of mitigation would not require such a step. If it is said that this still leaves to the innocent party the burden of determining when such a state of agitation has been reached, the rule, as usually expressed, provides that if plaintiff has taken reasonable steps in mitigation and has lost thereby, such added losses may be shown as part of his damages.[41] In this connection, the courts have been justifiably disposed to resolve any but the clearest of cases in favor of the innocent party and have further protected him by placing on the defendant the burden of showing his action to be unreasonable.[42]

In rebuttal of the second reason assigned stands the qualification that mitigation calls into play only those facilities which have been released to the plaintiff as a result of the breach.[43] If money, credit, or capacity is not released to the innocent party by the termination of his obligation, any other contracts he may make should not be considered as reducing his damages. However, if the repudiation has left him with credit or cash in excess of what he would have had, no reason is seen why this should not be put to use for defendant's benefit.

It is suggested that there is another reason, never expressed, but often lurking behind any flat denial of duty to mitigate in these forward contract situations. That is a general aversion in many quarters to the entire doctrine of anticipatory breach. It is evidenced particularly in those cases which require actual election to treat the repudiation as a breach but may take shape in many other forms.

There is an apparent incongruity in placing a burden to act on the innocent party, especially in the case of a forward contract of sale. But in spite of this, our theory of contract damages would seem to call for such an approach.

> "The object of compelling a contract breaker to pay damages is not to punish him for anti-social conduct, but to protect the promisee against undeserved injury, and so to render possible the smooth working of social and economic arrangements . . . if one appeals to

[41] 1 CONTRACTS RESTATEMENT, § 336 (1) (1932): "Damages are recoverable for special losses incurred in a reasonable effort, whether successful or not, to avoid harm that the defendant had reason to foresee as a probable result of his breach when the contract was made."

[42] McCORMICK, DAMAGES, § 42 (1935).

[43] GRISMORE, CONTRACTS, § 194 (1947); Grinnell Co. v. Vorhees, (C.C.A. 3d, 1924) 1 F. (2d) 693; Mount Pleasant Stable Co. v. Steinberg, 238 Mass. 567, 131 N.E. 295 (1921).

> the assistance of a court of law against the other, he must show a reasonable spirit. He must prove that he is actuated not by motives of vindictiveness, but by a desire to escape loss and to promote the general welfare of society as well as his own. That being so, it is not unreasonable that a court of law shall ask him to consider the interest of the vendor as well as his own, and when he has received a clear notice of vendor's intention to repudiate, to take any obviously prudent steps to protect himself against the consequences of the breach."[44]

Under such an analysis, there appears to be no reason why the same standards of reasonableness cannot be applied to a forward contract of sale as to any type of contract. It is no doubt true that mitigation will often be a greater burden when dealing with a forward contract, but the flexibility in the suggested standard can meet this problem without flatly denying a duty to mitigate.

Another factor in favor of the rule denying the duty is that such a rule is certain and easy to apply. That there is merit in such an approach is not denied, but it is readily recalled that, in many connections, Anglo-American law has not allowed this aim to dominate all others. A typical example, and one which holds surprising analogies for our subject, is the doctrine of "last clear chance" in the field of torts. In each case there is a wrongdoer at the mercy of an innocent party, and in each case the law places a duty on the innocent party to take reasonable steps to avoid the injury.

The paucity of cases bearing directly on this matter might be said to indicate that the problem is largely academic. It is suggested, however, that the explanation can be found in the fact that most business people are reasonable men interested primarily in production and the continuity of commercial activity; and when faced with an anticipatory breach, they have instinctively taken steps to mitigate. This is borne out by the fact that in most of the cases plaintiff has actually proceeded, and the only question is the reasonableness of his action.

What should be sought is to avoid the denial of a duty as a rule of law, so that the courts will feel justified in coping with the situation of the vindictive plaintiff. To clarify this position, consider one situation, typical but not exclusive, where it seems that there should be a positive duty to mitigate:

D is vendor. *P* is vendee. Contract to deliver goods in December. Unequivocal repudiation by *D* in September. Suppose further that the agreed price is $100, but the same contract would cost $150 at the time of repudiation. Very likely, *P* should not be required to make an imme-

[44] 66 THE SOLICITORS' JOURNAL & WEEKLY REPORTER 247 (1922).

diate substitute contract. But suppose prices fall so that in October a similar contract can be acquired for $100, and *P* has credit which was released to him by the repudiation. There is no reason why *P* should not then be required to cover or, on failure, should not have his damages measured as of that date. If prices continue to fall, *P* will be recompensed for his loss, while, if prices rise between then and the date for performance, he will have realized a profit and *D*'s liability will be nominal.

IV

EFFECT OF THE UNIFORM SALES ACT

Before concluding, further consideration should be given to the effect of the Uniform Sales Act on this question. As to the measure of damages for either buyer or seller, the act follows the general rule (i.e., difference between contract price and market price at time for performance).[45] In this respect, the language is almost identical with comparable provisions of the English Sales of Goods Act,[46] but for one very unfortunate difference. Where the English act makes the normal measure "prima facie," the Uniform Sales Act appears to make it conclusive "in the absence of special circumstances showing proximate damages of a *greater* amount."

This distinction might well lead one to believe that the act imposes no duty to mitigate on breach of a forward contract of sale, and indeed, the New York courts seem to have found that meaning.[47] However, such a construction would not appear inevitable in light of other provisions of the same section of the act: "The measure of damages is the loss directly and naturally resulting in the ordinary course of events from the seller's breach of contract."[48]

Refusing to find in the act a conclusive denial of the duty to mitigate, the court said in *Crane Iron Works v. Cox & Sons Co.*:[49]

> "The act does not expressly repeal the rule of law as to mitigation of damages, nor is the act inconsistent with it, and so it is not repealed by implication."

[45] Uniform Sales Act § 64 (3) (seller's remedy), § 67 (3) (buyer's remedy).

[46] Sale of Goods Act, 1893 (56 & 57 Vict. C. 71), § 50 (seller's remedy), § 51 (buyer's remedy).

[47] Segall v. Finlay, 245 N.Y. 61, 156 N.E. 97 (1927); Goldfarb v. Campe Corp., 99 Misc. 475, 164 N.Y.S. 583 (1917); see note 14, supra.

[48] Uniform Sales Act § 64 (2), § 67 (2).

[49] (C.C.A. 3d, 1928) 28 F. (2d) 328 at 330. The court was referring to 2 Rev. Statutes of N.J. (1937) 46: 30—70, which is identical with § 64 of the Uniform Sales Act.

If the view of the New York courts is followed, it is submitted that the act has gained a measure of certainty only at the expense of essential flexibility.

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