

2009

Good Faith Rejection of Goods in a Falling Market Note

Jeffrey M. Dressler

Follow this and additional works at: https://opencommons.uconn.edu/law_review

Recommended Citation

Dressler, Jeffrey M., "Good Faith Rejection of Goods in a Falling Market Note" (2009). *Connecticut Law Review*. 54.

https://opencommons.uconn.edu/law_review/54

CONNECTICUT LAW REVIEW

VOLUME 42

DECEMBER 2009

NUMBER 2

Note

GOOD FAITH REJECTION OF GOODS IN A FALLING MARKET

JEFFREY M. DRESSLER

This Note analyzes the intersection of two fundamental components of American sales law under the Uniform Commercial Code: the perfect tender rule and the duty of good faith. It focuses on cases in which buyers of goods use their right to perfect tender to avoid purchasing goods that have become diminished in value. Some commentators, and, indeed, some courts, have argued that such conduct runs afoul of parties' underlying duty of good faith in the performance of contracts. This Note rejects this position, and, instead, argues that if goods are truly non-conforming—even if only “trivially” non-conforming—buyers should retain their right of rejection irrespective of the hardship this may impose on the seller of goods. In short, this Note suggests that the duty of good faith should never override a party's otherwise tenable right of rejection and advocates a judicial framework that can allow courts to deal with difficult cases in a way that is consistent with the intent of the parties and conducive to the development of a more predictable body of contract law.

NOTE CONTENTS

I. INTRODUCTION	613
II. THE ACADEMIC BACKDROP.....	615
A. THE PERFECT TENDER RULE.....	615
B. THE DUTY OF GOOD FAITH IN PERFORMANCE	621
C. GOOD FAITH IN PERFECT TENDER CASES.....	627
III. JUDICIAL APPLICATION.....	629
IV. A NEW FRAMEWORK.....	633
A. CONSIDERATION OF FALLING MARKET CONDITIONS IS NOT HELPFUL IN DECIDING CASES	633
B. THE ARGUMENT FOR CATEGORICAL EXCLUSION	637
C. POTENTIAL FOR ABUSE CAN BE LIMITED BY OTHER LEGAL DOCTRINES AND PERFECT TENDER RULE CONSTRAINTS	640
V. CONCLUSION	643



GOOD FAITH REJECTION OF GOODS IN A FALLING MARKET

JEFFREY M. DRESSLER*

I. INTRODUCTION

Modern contracts literature is ripe with discussions of the duty of good faith under Article II of the Uniform Commercial Code (“U.C.C.”). Likewise, the rules governing a buyer’s right to reject non-conforming goods under section 2-601—better known as the perfect tender rule—have been vigorously debated. The two issues often intersect. While the perfect tender rule may suggest that a buyer possesses an unwavering right to reject in certain circumstances, the duty of good faith may suggest an obligation to use some degree of equitable restraint in invoking this right so as to not exploit the seller. Nowhere is this dynamic more apparent than in cases where the merits of a particular rejection are challenged against the backdrop of a falling market¹ that might lead a reasonable observer to suspect that the buyer’s rejection was actually motivated by a desire to escape from a bad bargain rather than out of legitimate dissatisfaction with any non-conformities in the goods tendered. Exploring this area requires a survey of the contrasting views of the obligation of good faith, however, this Note does not seek to add to the philosophical debate about what good faith should be. Instead, this Note tackles the more pragmatic task of demonstrating why current conceptions of good faith should not be used to restrict the force of the perfect tender rule, especially in the context of sophisticated commercial parties. Ultimately, the goal is to articulate under what circumstances a buyer may reject goods in a falling market, and whether sellers should be permitted to offer evidence of a falling market in order to establish that the buyer rejected in bad faith.

This Note argues that buyers should be entitled to reject goods that are truly, even if only trivially, non-conforming regardless of the economic hardship this imposes on a seller. Further, this Note argues that plaintiff-sellers should not be permitted to use evidence of a falling market in order to establish that such rejection was made in bad faith. To get there, Part II tackles the sticky issue of defining when goods are non-conforming. It

* University of Connecticut, B.A. 2006; University of Connecticut School of Law, J.D. Candidate 2010. I would like to thank Professor Kurt Strasser for his tremendous guidance in writing this Note and for inspiring my interest in contract law. I would also like to thank my colleagues on *Connecticut Law Review* for their hard work editing this Note. All errors are mine and mine alone. This Note is dedicated to my parents for their unending support.

¹ Throughout this Note, the term “falling market” is used as a shorthand to describe a situation in which the fair market value of goods falls significantly between the time the buyer agrees to purchase them from a seller and the time the goods are actually delivered.

argues that any defect that impinges on the bargain the parties struck should be deemed a non-conformity under the perfect tender rule. As many cases show, this may include “trivial” defects if they do in fact bear such significance to the parties’ bargain. Part II also surveys good faith, ultimately concluding that the most useful model for understanding good faith in this context is an excluder model that repudiates any conduct failing to satisfy the two types of conduct affirmatively required for good faith under the U.C.C.: honesty and commercial reasonableness. Part III then analyzes cases that have dealt with contested rejections and, specifically, cases where sellers relied on arguments that the buyer’s rejection was made in bad faith to escape a bad bargain caused by a falling market for the goods. The cases indicate a divide between courts that factor falling market evidence into their reasoning, and those that either refuse to admit such evidence, or are not persuaded by it. As such, this area of the law is worthy of more study and, hopefully with time, more consistency.

With this as a starting point, Part IV argues that courts should resist the urge to use falling market conditions as evidence of a bad faith rejection because this type of evidence does not help determine if a non-conformity in the goods actually exists; only the terms of the contract and the relevant commercial standards help in this regard. Further—assuming a non-conformity does exist—it is not bad faith to act on it in a falling market because doing so is both honest and commercially reasonable. It is honest because, having already established that a non-conformity exists, the honesty prong of good faith should be treated as a nullity in this narrow context. This is so because, even conceding that the falling market was a factor that made the non-conformity intolerable, ultimately the decision to reject was made in light of the fact that a non-conformity actually existed. Further, particularly in the context of sophisticated parties, around which the majority of this discussion revolves, it is commercially reasonable for a party to consider the value for the goods when deciding whether to enforce his right of rejection to the fullest and, indeed, it is generally commercially reasonable for him to insist on the full benefit of his bargain by rejecting under those circumstances.

Part IV also argues that, in addition to being unhelpful for the ultimate resolution of contracts cases, permitting evidence of falling markets offers little more than an alternate holding to the main holding in perfect tender cases and, as such, detracts from the development of an efficient and predictable law of contracts. Worse still, this uncertainty encourages litigation by lending support to sellers in future cases who tender non-conforming goods in a falling market, only to cry foul when those goods are rightly rejected. This in turn may have the perverse effect of denying buyers the full benefit of the contracts they bargained for. Finally, Part V concludes by testing the framework advocated in the Note against the facts

found in previous judicial decisions.

II. THE ACADEMIC BACKDROP

A. *The Perfect Tender Rule*

U.C.C. section 2-601 provides that in the case of one-shot contracts, buyers may reject the whole “if the goods or the tender of delivery fail in any respect to conform to the contract”² The buyer in turn has a corresponding duty “to accept and pay in accordance with the contract.”³ Courts have agreed that section 2-601 reflects a statutory revival of the perfect tender rule.⁴ The purpose of the perfect tender rule, according to Professor Corbin, is “to secure high performance standards” because without the fear of a buyer’s ability to reject goods, sellers “would be tempted to saddle buyers with unsuitable and defective goods.”⁵ Professor Minter provided a popular example of the unfairness that could result if substantial performance were allowed instead of perfect tender:

A seller might find that it is significantly cheaper to make the machinery capable of operation within a seven percent deviation than to make it operate within only a five percent deviation as required by the contract. He would be gambling that the buyer could not make out a case for substantial impairment independent of the contract and that any damages that the buyer might prove would be less than his cost savings in producing the inferior machine.⁶

The possibility of sub-par performance is considered to be more likely to occur in the performance of one-shot contracts, where the absence of a continuous commercial relationship gives the buyer less leverage as to slightly non-conforming goods. For this reason, only one-shot contracts are subject to the perfect tender rule, while installment contracts are subject to a “substantial performance” requirement.⁷

² U.C.C. § 2-601 (2002). Proper rejection entails not only a simple refusal to accept the goods, but also notification to the buyer. If goods are not accepted when they should be, the refusal is said to be “wrongful.” See U.C.C. § 2-703 (2002). If goods could have been rejected, but notice was improperly given, then the rejection is said to be ineffective. See 67 AM. JUR. 2D *Sales* § 592 (2003).

³ U.C.C. § 2-301 (2002).

⁴ See, e.g., *Ramirez v. Autosport*, 440 A.2d 1345, 1349 (N.J. 1982) (“To the extent that a buyer can reject goods for any nonconformity, the UCC retains the perfect tender rule.”).

⁵ 8 CATHERINE M.A. McCAULIFF, *CORBIN ON CONTRACTS, CONDITIONS* § 33.3 (Joseph M. Perillo ed., 1999).

⁶ Francis A. Minter, *Buyer’s Right of Rejection*, 13 GA. L. REV. 805, 826 (1979). Minter’s hypothetical is based on the facts of *Axion Corp. v. G.D.C. Leasing Corp.*, 269 N.E.2d 664, 666, 668–69 (Mass. 1971).

⁷ Installment contracts are dealt with in U.C.C. § 2-612 (2002). The remainder of this Note discusses only single transaction contracts. For a useful commentary on installment contracts, see

Almost immediately after the first draft of the U.C.C. was approved, commentators challenged the strength of its conception of the rule. For instance, White and Summers are “skeptical of the real importance of the perfect tender rule,” and argue that the law would be “little changed” if courts required a substantial non-conformity for rejection.⁸ Then-Professor Ellen Peters called the U.C.C.’s perfect tender rule “a mere shadow of its formerly robust self.”⁹ Among the many statutory limitations on a buyer’s right to insist on perfection are the fact that goods need not actually be perfect, but rather only need to conform precisely to the terms of the contract (subject to trade usage, course of performance, and course of dealing), the seller’s right to cure, and—perhaps most significantly—the obligation of good faith.¹⁰ Courts, however, have not been nearly as eager to declare the perfect tender rule lifeless, and as Professor William Lawrence has argued, “commentators have greatly exaggerated the extent to which the limitations in Article 2 undercut the application of the perfect tender rule.”¹¹ Nevertheless, a brief sketch of the relevant limitations on the buyer’s otherwise formidable right to reject goods is appropriate.

1. *Distinguishing Between Conforming and Non-Conforming Goods*

a. The Perfection Misnomer

Professor Williston points out that the perfect tender rule “is somewhat of a misnomer” because the goods do not have to be literally perfect, but must merely conform to the terms of the contract.¹² The terms of the contract include both written specifications and supplemental terms that are inferred from trade usage, course of dealing, and course of performance. The more specificity that the parties choose to use in the language of their contract, the less they will have to supplement the understanding of what was to be tendered against more ambiguous concepts such as trade usage. This is a simple point yet it is often overlooked. In essence, parties control their own destiny with respect to the level of perfection required. Parties should be able to bargain for all

JAMES J. WHITE & ROBERT S. SUMMERS, *UNIFORM COMMERCIAL CODE 302-05* (West Publishing Co., 4th ed. 1995).

⁸ WHITE & SUMMERS, *supra* note 7, at 300-01.

⁹ Ellen A. Peters, *Remedies for Breach of Contracts Relating to the Sale of Goods Under the Uniform Commercial Code*, 73 *YALE L.J.* 199, 206 (1963).

¹⁰ Other asserted limits on the perfect tender rule include the fact that installment contracts are dealt with in an entirely different section, section 2-504, which provides that an improper shipment contract that causes a late delivery is grounds for rejection only if “material delay or loss ensues.” U.C.C. § 2-504 (2002). Finally, courts may manipulate otherwise acceptable revocations for minor defects under the guise of some other procedural device such as failure to make a proper rejection. See WHITE & SUMMERS, *supra* note 7, at 301.

¹¹ William H. Lawrence, *The Prematurely Reported Demise of the Perfect Tender Rule*, 35 *U. KAN. L. REV.* 557, 558 (1987).

¹² 14 RICHARD A. LORD, *WILLISTON ON CONTRACTS* § 40:6 (4th ed. 2000).

that they want in a transaction. If their negotiations are successful, then courts should have no qualms holding sellers to produce exactly what they promise. Parties that choose to be less descript in the terms they use to reflect that which is to be tendered may find negotiations go smoother; however, this approach leaves more latitude to determine what is and what is not reasonably implied within the definition that the parties did select after the fact.

b. Commercial Practices Help Define What Has to Be Tendered

Often commercial practices play a significant role in defining the required specifications of a particular good. White and Summers refer to these factors as “[a]dditional restrictions” on the perfect tender rule.¹³ In fact, it is more helpful to think of them merely as establishing the terms of the contract in cases where the parties did not exercise enough clarity through their own writings. In other words, these concepts do not change the perfect tender rule, they merely shape the requirements of the contract in a way that makes what at first appeared to be a breach actually turn out to be conforming tender.¹⁴ An example is when a contract specifies delivery of twelve items, but industry custom is that twelve means anywhere between eleven and thirteen. Under these facts, a delivery of eleven would not invoke the perfect tender rule—not because of an “exception” to the rule, but rather because eleven is a conforming tender in this industry. Prior commercial practices can be disclaimed, but this requires clarity and specificity.¹⁵

c. The Debate over “Trivial Defects”

Many commentators have suggested that buyers should not be able to reject goods for “insignificant” or “trivial” defects. For example, Professor Robert Summers claims that “a buyer who openly seizes upon trivial defects to justify his rejection . . . admitting all along that he is rejecting the goods because the price has gone down . . . is certainly [acting in] commercial bad faith.”¹⁶ Courts, on the other hand, have shown a willingness to enforce the perfect tender rule more vigorously and allow

¹³ WHITE & SUMMERS, *supra* note 7, at 300–01.

¹⁴ See John A. Sebert, Jr., *Rejection, Revocation, and Cure Under Article 2 of the Uniform Commercial Code*, 84 NW. U. L. REV. 375, 386–87 (1990).

¹⁵ See U.C.C. § 2-202 cmt. 2 (2002) (commercial practices become an element of the meaning of the words used “[u]nless carefully negated”).

¹⁶ Robert S. Summers, “*Good Faith*” in *General Contract Law and the Sales Provisions of the Uniform Commercial Code*, 54 VA. L. REV. 195, 205–06 (1968); see also Lawrence, *supra* note 11, at 570 (“Many commentators have praised section 2-508(2) as a desirable provision designed to prevent buyers from rejecting goods with trivial nonconformities in order to escape bargains that become unfavorable because the market for the goods falls.”). But see HOWARD O. HUNTER, MODERN LAW OF CONTRACTS § 11:11 (2008) (“Technically, any failure, however small, is a nonconformity that justifies rejection under § 2-601.”).

buyers to reject even for minor or trivial defects. For instance, in *DeJesus v. CAT Auto Tech Corp.*, a New York court rejected White and Summers' view that substantial performance should be the standard, stating that "New York has not adopted this view, and continues to subscribe to the perfect tender rule," which the court described as requiring "exact performance."¹⁷ Likewise, in *KCA Electronics, Inc. v. Legacy Electronics, Inc.*, a California appellate court ruled that "the perfect tender rule imposes 'a very high level of conformity' to the contract on sellers, allowing buyers to 'reject a seller's tender for any trivial defect, whether it be in the quality of the goods, the timing of the performance, or the manner of delivery.'"¹⁸

Some commentators argue these statements are dicta, since the defects in many of the cases containing such language are arguably not insignificant.¹⁹ While this may be true in some cases, there remains ample authority in many jurisdictions to support a buyer's absolute right of rejection as a rule of law. For instance, in *DeJesus*, the buyer had ordered gift certificates to be distributed to its employees. The court upheld the buyer's rejection due to the fact that "the paper was different, and the chosen sample contained a decorative border, whereas the finished product did not."²⁰ And in *KCA Electronics*, which involved the delivery of canopies designed to allow for the stacking of computer chips, the court held that six percent of the delivered parts lacking uniform features was sufficient to allow the buyer to reject the whole.²¹

Courts seem particularly likely to allow rejection based on minor non-conformities in cases where the defect goes to a term expressly agreed to by the parties, or where it is clearly important to the buyer. In *Texas Imports v. Allday*, the parties contracted for the sale of forty-nine cattle.²² The court ruled that ten of the cattle being unsound provided sufficient basis to permit the buyer to reject all of them.²³ This was true in spite of the fact that there was no indication in the record that the buyer had been harmed by the tender of ten less sound animals than originally contracted for, as well as circumstantial evidence indicating that the buyer had

¹⁷ *DeJesus v. CAT Auto Tech Corp.*, 615 N.Y.S.2d 236, 238 (N.Y. Civ. Ct. 1994); see also *Y&N Furniture Inc. v. Nwabuoku*, 734 N.Y.S.2d 382, 384 (N.Y. Civ. Ct. 2001) ("The buyer's right, generally, to reject the goods for any nonconformity, even one that is trivial, is known as the 'perfect tender rule []' . . .").

¹⁸ *KCA Elecs., Inc. v. Legacy Elecs., Inc.*, No. G037285, 2007 WL 2137959, at *1 (Cal. Ct. App. July 26, 2007).

¹⁹ WHITE & SUMMERS, *supra* note 7, at 301–02 n.6; see also Seibert, *supra* note 14, at 384–85.

²⁰ *DeJesus*, 615 N.Y.S.2d. at 237. The court also noted that two of the eight certificates had colors immediately outside the borders but that one was "slightly noticeable" and the other "noticeable only upon close inspection." *Id.*

²¹ *KCA Elecs.*, 2007 WL 2137959, at *2.

²² *Tex. Imports v. Allday*, 649 S.W.2d 730, 732–33 (Tex. App. 1983).

²³ *Id.* at 738.

overbought.²⁴ In another case, a car buyer was permitted to reject tender of a car that did not have a spare tire.²⁵ In that case, the court noted that the buyer was a traveling salesman who traveled extensively in his trade and the spare tire was important to him for safety reasons.²⁶

Part of the problem fueling the disagreement between courts and commentators may be a matter of mere terminology. Buzz words such as “insignificant” or “trivial” do little to advance the analysis of a defect. A close reading of the case law confirms that a particular defect that is trivial can make goods non-conforming, or may be inadequate to make them non-conforming, depending on a close analysis of what was actually contracted for. A defect may be small (and thus “trivial” under lay usage), yet if it goes to an important component of the good, such as the spare tire to the traveling salesman, then it should render that good non-conforming. Another small (trivial) defect that does not affect an important component of the tendered good does not make the good non-conforming. This is not because there is some sort of *de minimus* exception for trivial defects, but rather, because such a defect does not impinge on the bargain the parties struck, and therefore does not make the item legally non-conforming.²⁷ For the duration of this Note, any defect—small, nitpicky, and, yes, even trivial—which goes to the contractually required specifications and thus, if unsatisfied, would permit a buyer to reject will be referred to as “legally significant.” Any non-conformity that is insufficient to trigger a right of rejection—again, not because of the small size of the defect, but because it does not affect what was agreed to be delivered in any meaningful way—will be referred to as “legally insignificant.”

2. Seller's Right to Cure

Section 2-508 of the U.C.C. gives sellers a limited right to cure non-conformities in the goods they tender, thereby maintaining the buyer's obligation to accept pursuant to the terms of the contract.²⁸ This has been called one of the “most significant new intrusion[s] on the perfect tender rule”; however, there remain “substantial uncertainties” about how to apply it.²⁹ Many commentators talk of the right to cure as though it represents a

²⁴ For example, the buyer did not exercise his right to reject all the cattle, nor did he limit his rejection to the ten non-conforming cattle. Instead, he accepted twenty-seven and rejected twenty-two. *See id.* at 738; *see also* Sebert, *supra* note 14, at 385–86 (discussing the buyer's probable motive in *Texas Imports*).

²⁵ *Colonial Dodge, Inc. v. Miller*, 362 N.W.2d 704, 705 (Mich. 1984).

²⁶ *Id.* at 706–07.

²⁷ An example of this can be seen in *Fanok v. Carver Boat Corp.*, where the buyer of a yacht tried to reject for scratches on the kitchen table, dirt on the carpet, and master bath shower doors that “rattle a lot when underway.” 576 F. Supp. 2d 404, 418 (E.D.N.Y. 2008). This attempted rejection was made only after the entire yacht had been destroyed by an unexplained fire. *Id.* Not surprisingly, the court found the alleged defects insufficient under these facts. *Id.* at 406.

²⁸ *See* U.C.C. § 2-508 (2002).

²⁹ Sebert, *supra* note 14, at 389.

drastic limit on the perfect tender rule. But Professor Lawrence argues that these statements exaggerate the practical effect of the cure provision.³⁰ First, section 2-508(1) only allows a seller to cure defects if it can do so “within the contract time.”³¹ Therefore, practically speaking, this section is applicable only when the seller tenders goods early. As such, Professor Lawrence argues that it is “not particularly remarkable in light of prior law and business practices.”³² The more significant right to cure is found under section 2-508(2), which provides sellers additional reasonable time to cure if they “had reasonable grounds to believe” that their initial non-conforming tender would be acceptable.³³ The comment suggests that the drafters intended for this to be a narrow exception.³⁴ Professor Robert Nordstrom has argued that this subsection was only intended to protect sellers who knew of the defect in their goods, but nonetheless had reason to believe that the goods would still be accepted by the buyer.³⁵ At least one court has rejected this view, and other commentators—including White and Summers—have advocated for broader applicability of section 2-508(2).³⁶ However, whatever standard is used to invoke section 2-508(2), once it is successfully invoked, the access to additional time is limited, and as such makes it a difficult provision for sellers to rely on.³⁷ Finally, and perhaps most significantly, under either subsection of 2-508, if a seller is unable (or unwilling) to cure the defect, then the buyer’s rejection stands as valid.³⁸ In other words, the buyer either gets its perfect tender or it gets to reject; in this sense the right to cure is hardly a limit on the effectiveness of

³⁰ See Lawrence, *supra* note 11, at 568.

³¹ U.C.C. § 2-508(1).

³² Lawrence, *supra* note 11, at 563.

³³ U.C.C. § 2-508(2).

³⁴ “Such reasonable grounds can lie in prior course of dealing, course of performance or usage of trade as well as in the particular circumstances surrounding the making of the contract.” U.C.C. § 2-508 cmt. 2; see also Lawrence, *supra* note 11, at 564 (arguing that although the comment does not purport to provide an exhaustive list of things that would form the basis for a party to reasonably believe his non-conforming goods would be accepted, it “tends to suggest a narrow range of appropriate criteria”).

³⁵ ROBERT J. NORDSTROM, HANDBOOK OF THE LAW OF SALES 321 (West Publishing Co. 1970).

³⁶ See *Joc Oil USA, Inc. v. Consol. Edison Co.*, 434 N.Y.S.2d 623, 632 (N.Y. Sup. Ct. 1980). White and Summers think that this remedy should be available if a seller can show (1) that he was ignorant of the defect despite his good faith and prudent business behavior or (2) he had some reason to believe that the goods would be acceptable. WHITE & SUMMERS, *supra* note 7, at 324. In contrast, Professor Hawkland focuses on the size of the initial defect, reasoning that a seller should be able to invoke section 2-508(2) if “he can do so without subjecting the buyer to any great inconvenience, risk or loss.” William D. Hawkland, *Curing an Improper Tender of Title to Chattels*, 46 MINN. L. REV. 697, 724 (1962). See generally Michael A. Schmitt & David Frisch, *The Perfect Tender Rule—An “Acceptable” Interpretation*, 13 U. TOL. L. REV. 1375 (1982) (surveying various attempts to reconcile the perfect tender rule with the cure provisions).

³⁷ See White & Summers, *supra* note 7, at 322 (stating that cure can only be made within a “reasonable” period of time).

³⁸ See Lawrence, *supra* note 11, at 567–68 (“The buyer’s right to exact seller performance under the sales contract is not diminished by the right to cure, except for an extension of time [under § 2-508(2)].”).

rejection from the buyer's perspective.

3. *Right to Reject Must Be Exercised in Good Faith*

All aspects of the performance of a contract must be performed in “good faith.”³⁹ Since the rejection of goods is an aspect of performance, rejection—even if otherwise rightful—must be performed in good faith.⁴⁰ Professor Lawrence believes that of all the so-called “exceptions” to the perfect tender rule, the good faith requirement is the most important (and, from his perspective, the most underutilized).⁴¹ Before examining why Professor Lawrence feels this way, it is important to provide some general background on the concept of good faith.

B. *The Duty of Good Faith in Performance*

The general obligation of good faith in the performance of contracts is a relatively new concept.⁴² Section 1-304 of the U.C.C. provides that “[e]very contract or duty within [the Uniform Commercial Code] imposes an obligation of good faith in its performance and enforcement.”⁴³ Under the current Article I, good faith is defined as “honesty in fact and the observance of reasonable commercial standards of fair dealing.”⁴⁴ The duty of good faith in performance has been hailed as “possibly the single most significant doctrinal development in American contract law over the past fifty years.”⁴⁵ A full review of the academic literature on the general obligation of good faith in performance under American contract law is beyond the scope of this Note, although ample literature does exist.⁴⁶

³⁹ U.C.C. § 1-304 (2008).

⁴⁰ See Lawrence, *supra* note 11, at 571 (“Invoking the right to reject avoids [a buyer’s] responsibilities and thus can be exercised legitimately only when it is done in good faith.”); see also Linda J. Rusch, *Qualifications on Perfect Tender Rule*, in 2 WILLIAM D. HAWKLAND, UNIFORM COMMERCIAL CODE SERIES § 2-601:3 (2009) (“[T]here is no doubt that the buyer is under an obligation to act in good faith when he rejects . . .”).

⁴¹ Lawrence, *supra* note 11, at 571.

⁴² See Harold Dubroff, *The Implied Covenant of Good Faith in Contract Interpretation and Gap-Filling*, 80 ST. JOHN’S L. REV. 559, 571 (2006).

⁴³ U.C.C. § 1-304.

⁴⁴ *Id.* § 1-201(20) (2008). Under the U.C.C.’s prior Article I, “good faith” was generally defined to mean only “honesty”; however, Article II has always required merchants to conform with reasonable commercial standards of fair dealing in the trade. See U.C.C. §§ 1-201(19) (2000), 2-103(1)(b) (2002).

⁴⁵ Sebert, *supra* note 14, at 383; see also Robert S. Summers, *The General Duty of Good Faith—Its Recognition and Conceptualization*, 67 CORNELL L. REV. 810, 810 (1982).

⁴⁶ See generally Eric G. Andersen, *Good Faith in the Enforcement of Contracts*, 73 IOWA L. REV. 299 (1988); Steven J. Burton, *Breach of Contract and the Common Law Duty to Perform in Good Faith*, 94 HARV. L. REV. 369 (1980) [hereinafter Burton, *Good Faith I*]; Steven J. Burton, *Good Faith Performance of a Contract Within Article 2 of the Uniform Commercial Code*, 67 IOWA L. REV. 1 (1982) [hereinafter Burton, *Good Faith II*]; Steven J. Burton, *More on Good Faith Performance of a Contract: A Reply to Professor Summers*, 69 IOWA L. REV. 497 (1984) [hereinafter Burton, *Good Faith III*]; Steven J. Burton, *Good Faith in Articles 1 and 2 of the U.C.C.*, 35 WM. & MARY L. REV. 1533 (1994) [hereinafter Burton, *Good Faith IV*]; Thomas A. Diamond & Howard Foss, *Proposed Standards for Evaluating When the Covenant of Good Faith and Fair Dealing Has Been Violated*, 47 HASTINGS

Instead, this Note provides a brief overview of a few aspects of the debate which are most pertinent to answering the questions posed in Part I.

1. *Defining Good Faith*

The most logical place to begin deciphering the term good faith is to look to the intent of the original U.C.C. drafters. In an early draft of the U.C.C., the drafters defined good faith to include both honesty and the observance of reasonable commercial standards. A proposed comment would have explained the standard as requiring the observance of “commercial decencies.”⁴⁷ By the time the first version of the U.C.C. was approved, the definition had been pared down to just “honesty” and the reference to commercial decencies had been abandoned.⁴⁸ Professor Clayton Gillette points out that even without this language, the term “honesty” itself is susceptible to a host of meanings ranging from a very narrow view of honesty in its literal sense, to more liberal conceptions of the term which might themselves include forms of improper commercial behavior deemed dishonest in spirit.⁴⁹ A contrary version of the original drafting suggests that the commercial standards language was removed at the bequest of practitioners specifically because it was viewed as an “unnecessarily broad, moralistic imperative.”⁵⁰ Even if the original drafting had produced a clear “intent of the drafters,” the inquiry would still be incomplete. This is true both because (as discussed above) the most recent version of the U.C.C. does restore the element of “reasonable commercial standards” to all parties, and because, regardless of what the U.C.C.’s drafters believed, it was the individual state legislatures that ratified the U.C.C. and therefore *their* intent that really matters.⁵¹

In his seminal piece on good faith, Professor Robert Summers argues that a definition of good faith cannot be verbally conceptualized in any meaningful way, but rather can be understood only as an “excluder” that

L.J. 585 (1996); Dubroff, *supra* note 42; E. Allan Farnsworth, *Good Faith Performance and Commercial Reasonableness Under the Uniform Commercial Code*, 30 U. CHI. L. REV. 666 (1963); Clayton P. Gillette, *Limitations on the Obligation of Good Faith*, 1981 DUKE L.J. 619 (1981); Seth William Goren, *Looking for Law in All the Wrong Places: Problems in Applying the Implied Covenant of Good Faith Performance*, 37 U.S.F. L. REV. 257 (2003); Howard O. Hunter, *The Growing Uncertainty About Good Faith in American Contract Law*, 20 J. CONT. L. 31 (2004); Christina L. Kunz, *Frontispiece on Good Faith: A Functional Approach Within the UCC*, 16 WM. MITCHELL L. REV. 1105 (1990); Dennis M. Patterson, *A Fable from the Seventh Circuit: Frank Easterbrook on Good Faith*, 76 IOWA L. REV. 503 (1991); Summers, *Good Faith*, *supra* note 16; Summers, *Recognition and Conceptualization*, *supra* note 45; Michael P. Van Alstine, *Of Textualism, Party Autonomy, and Good Faith*, 40 WM. & MARY L. REV. 1223 (1999).

⁴⁷ Gillette, *supra* note 46, at 623 (citing U.C.C. § 1-203 cmt. (May 1949 Draft)).

⁴⁸ However, as discussed, *supra* note 44, Article II has always required merchants to conform with reasonable commercial standards of fair dealing in the trade.

⁴⁹ Gillette, *supra* note 46, at 621–22.

⁵⁰ *Id.* at 624.

⁵¹ *Id.* at 626.

excludes a litany of identifiable instances of bad faith.⁵² Professor Summers believes that this is the only conception that can provide the adequate degree of malleability for courts to “do justice.”⁵³ According to Professor Summers, courts should condemn certain types of action as bad faith “even when the objectionable conduct is within the letter of the contract”⁵⁴ Professor Summers was concerned that judges were distorting more definite areas of contractual jurisprudence in order to reach the just result in difficult cases. This, he argued, created fictions that undermined legal principles and subverted predictability. Instead, he advocated giving courts a flexible doctrine that they could apply at their own discretion and thus leave other contractual doctrines undisturbed.⁵⁵

In an influential series of articles, Professor Steven Burton faulted Summers’s conception for being too nebulous.⁵⁶ Instead, he proposed a more concrete model. Professor Burton believes that whenever a party is entrusted with discretion in contract performance that affects the other party’s benefit, such discretion cannot be exercised to recapture opportunities that were foregone by entering into the contract.⁵⁷ This, Burton argues, would be bad faith. Any exercise of discretion to recapture opportunities which were not foregone as a result of the contract can be considered good faith.⁵⁸ This necessarily requires courts to determine the intent a party had when undertaking a given course of action because the same exact type of conduct could be deemed good faith or bad faith, based on the court’s findings as to *why* the party behaved the way it did.⁵⁹ Though conceding that there are “well-known difficulties” in determining subjective intent, Burton advocated a subjective inquiry until his most recent article in which he candidly changes course and advocates for an objective inquiry into what caused the buyer’s conduct.⁶⁰

Not everyone agrees with such sweeping definitions of good faith as Summers, Burton, and others have advocated. Professor Gillette argues that good faith should be little more than an “ancillary exhortative or

⁵² Summers, *Good Faith*, *supra* note 16, at 196.

⁵³ *Id.* at 198.

⁵⁴ *Id.* at 239.

⁵⁵ *See id.* at 198.

⁵⁶ *See* Burton, *Good Faith I*, *supra* note 46, at 369–70 & n.5; Burton, *Good Faith II*, *supra* note 45, at 1–3; Burton, *Good Faith III*, *supra* note 46, at 497; Burton, *Good Faith IV*, *supra* note 46, at 1535–36. Professor Summers in turn has faulted Professor Burton’s conception for providing little substance to the analysis. *See* Summers, *Recognition and Conceptualization*, *supra* note 46, at 810.

⁵⁷ Burton, *Good Faith I*, *supra* note 46, at 372–73.

⁵⁸ *Id.* at 373.

⁵⁹ *See* Burton, *Good Faith III*, *supra* note 46, at 502–03 (stating that an “act” taken by a party can be “legally neutral” when deciding whether there was a breach and that, in order to make such a determination, the court must determine “whether the discretion-exercising party used its discretion for an improper purpose”).

⁶⁰ *See* Burton, *Good Faith IV*, *supra* note 46, at 1562 n.131.

precatory function that carries no legal sanctions.”⁶¹ These views mark a significant and—with courts weighing in on both sides—unresolved debate over whether it can ever be bad faith to exercise an option that is provided by the written terms of the contract. This debate can roughly be broken into two camps: the contextualist view and the neoformalist view.⁶²

a. The Contextualist View

Proponents of the contextualist view believe that good faith should have independent substantive content.⁶³ This view tries to encourage a cooperative relationship between the parties in which both sides make efforts to protect the reasonable expectations of the others. Professor Summers’s view fits within this group. Summers believes that good faith should prevent parties from declaring technical breaches.⁶⁴ In other words, even if they technically had the right to declare a breach, parties should forgo that right in certain circumstances out of consideration for the other party.

A district court, applying Utah law, articulated an expansive duty that went beyond the express terms of the agreement. Citing a Utah Supreme Court decision, the court stated:

An examination of express contract terms alone is insufficient to determine whether there has been a breach of the implied covenant of good faith and fair dealing. To comply with his obligation to perform a contract in good faith, a party’s actions must be consistent with the agreed common purpose and the justified expectations of the other party. The purpose, intentions, and expectations of the parties should be determined by considering the contract language and the course of dealings between and conduct of the parties.⁶⁵

Although the court found that the duty of good faith had not been breached in this case, its statement that the “express contract terms alone is insufficient”⁶⁶ demonstrates a contextualist view of striving to honor the spirit of the agreement even if it is contrary to the actual language used to

⁶¹ Gillette, *supra* note 46, at 665.

⁶² HOWARD O. HUNTER, MODERN LAW OF CONTRACTS § 8:8 (2009).

⁶³ *Id.*

⁶⁴ See Summers, *Good Faith*, *supra* note 16, at 234–35; see also Gillette, *supra* note 46, at 619–20 (“[Summers] proposes that good faith be defined to require commercial actors to forbear from declaring technical breaches.”).

⁶⁵ A.I. Trans. v. Imperial Premium Fin., Inc., 862 F. Supp. 345, 348 (D. Utah 1994) (citing St. Benedict’s Dev. Co. v. St. Benedict’s Hosp., 811 P.2d 194, 200 (Utah 1991)).

⁶⁶ *Id.*

express it.⁶⁷

b. The Neoformalist View

Proponents of the neoformalist view argue that good faith is meant only to exclude bad faith and fill gaps, and should not impose affirmative requirements beyond the terms of the agreement. As Professor Dubroff posits, “How can a party be said to be performing or enforcing in bad faith when it does no more or less than what was expressly agreed to and understood by the parties?”⁶⁸ Neoformalists value respecting the allocation of risks which the parties themselves bargained for. Professor Dubroff suggests that expansive good faith conceptions are “unprincipled and may lead to erroneous results in determining rights under the contract.”⁶⁹

In addition to concerns about respecting the private parties’ bargain, there is another more public goal of encouraging the development of a body of commercial law which is clear and predictable. Professor Gillette argues that judicial usage of good faith language “indicates lack of precision in the court’s reasoning and detracts from the judicial development and comprehension of the [Uniform Commercial] Code.”⁷⁰ He argues that it has also contributed to uncertainty in commercial contract disputes. Professor Dubroff agrees that these expansive good faith conceptions “create an environment for deciding cases that may be unnecessarily vague and rootless” and their application “can be a confusing and unsatisfying business.”⁷¹

The Seventh Circuit issued an opinion that closely expresses a neoformalist viewpoint.⁷² In that case, which involved a commercial bank enforcing a particularly harsh contract clause at an unexpected and inopportune time for the borrower, Judge Easterbrook wrote:

Firms that have negotiated contracts are entitled to enforce them to the letter, even to the great discomfort of their trading partners, without being mulcted for lack of “good faith”. Although courts often refer to the obligation of good faith that exists in every contractual relation, this is not an invitation to the court to decide whether one party ought to

⁶⁷ Another example of this type of reasoning can be seen in *Baker v. Ratzlaff*, where the court found a seller to be in breach of the good faith obligation because he declared the buyer in breach “upon a technical pretense.” 564 P.2d 153, 156 (Kan. Ct. App. 1977). Although the terms of their agreement gave the seller the right to declare a breach for the buyer’s non-payment of previous loads, the court was moved by evidence that the market for goods rose sharply and the seller had resold the goods to another party at a higher price. *Id.* at 156–57.

⁶⁸ Dubroff, *supra* note 42, at 602.

⁶⁹ *Id.* at 597.

⁷⁰ Gillette, *supra* note 46, at 630.

⁷¹ Dubroff, *supra* note 42, at 584, 587.

⁷² *Kham & Nate’s Shoes No. 2, Inc. v. First Bank of Whiting*, 908 F.2d 1351, 1357 (7th Cir. 1990).

have exercised privileges expressly reserved in the document. “Good faith” is a compact reference to an implied undertaking not to take opportunistic advantage in a way that could not have been contemplated at the time of drafting, and which therefore was not resolved explicitly by the parties.⁷³

According to Judge Easterbrook, since the parties had addressed the disputed conduct in their contract (by agreeing that the bank possessed such a right), the issue fell beyond the scope of good faith.⁷⁴

2. Good Faith as an Excluder

In spite of the ongoing debate over whether good faith itself has any independent substance, courts have generally agreed that at the very least, good faith requires the absence of bad faith. This view is based on Professor Summers’s “excluder” definition, and results from that fact that acts performed in bad faith are not allowed under contracts governed by the U.C.C.⁷⁵ Then-Judge Scalia took this view in a D.C. Court of Appeals case in which he stated:

We agree with the observation of Professor Summers that the concept of good faith in the performance of contracts is an “excluder.” It is a phrase without general meaning (or meanings) of its own and serves to exclude a wide range of heterogeneous forms of bad faith. In a particular context the phrase takes on specific meaning, but usually this is only by way of contrast with the specific form of bad faith actually or hypothetically ruled out.⁷⁶

Judge Scalia added that “even the permissible act performed in bad faith is a breach only because acts in bad faith are not permitted under the contract.”⁷⁷

The remainder of this Note focuses solely on the excluder issue in the falling market context. In other words, this Note examines whether rejection of goods with a minor defect in a falling market should be considered bad faith, and thus disallowed under *either* the contextualist *or* the neoformalist model. To perform this search for bad faith, we will put aside the academic formulations of what good faith *should* be, and define bad faith more simply as excluding conduct which fails to satisfy the

⁷³ *Id.* at 1357 (internal citations omitted).

⁷⁴ *Id.*; *see also* Wells Fargo Bank v. Citizens Bank of Tex., 181 S.W.3d 790, 804 (Tex. App. 2005) (“Nor can a bank be said to violate its ‘obligation of good faith’ under [former U.C.C. § 1-203] if it acts in accordance with the requirements of the U.C.C.”).

⁷⁵ This is true because regardless of what good faith *does* mean, it certainly *does not* mean bad faith.

⁷⁶ Tymshare, Inc. v. Covell, 727 F.2d 1145, 1152 (D.C. Cir. 1984).

⁷⁷ *Id.* at 1150 n.3.

U.C.C.'s requirement of "honesty" *and* conformity with "reasonable commercial standards of fair dealing."⁷⁸ The honesty requirement has been interpreted as a subjective standard.⁷⁹ For instance, in the context of buyers exercising their right to reject goods, they must do so out of actual dissatisfaction with the tender. By contrast, "commercially reasonable standards of fair dealing in trade" is meant to be an objective measure of conformity based on trade usage, course of dealing, and course of performance.⁸⁰ This inquiry takes into account the reasonable business norms in a given context. For example, in *Hubbard v. UTZ Quality Foods*, the court held that a commercial buyer of potatoes, which the contract required to be within a certain color range, did not reject in bad faith when he failed to measure the potatoes' color with a machine before rejecting on the basis of poor color because, even though the machine would have been much more accurate, it was reasonable within the potato industry to use visual inspections.⁸¹

C. Good Faith in Perfect Tender Cases

Having sketched a brief overview of good faith, one can proceed to examine how it should be applied in perfect tender cases. Professor Lawrence states that good faith "is the most important provision to ensure that the perfect tender rule is applied as a just standard."⁸² Although he was generally a strong proponent of perfect tender (as opposed to the substantial performance standard advocated by many scholars), he nonetheless argued that good faith should act as an important restraint on the rule. Specifically, Professor Lawrence argues that "[a] buyer's insistence upon rejection for a minor contract deviation in order to avoid an unfavorable bargain is an unfair use of buyers' rejection rights that can be attacked best through utilization of the good faith obligation of the buyer."⁸³ Lawrence believes that a buyer whose true subjective reason for rejection is to escape a bad bargain is acting in bad faith because their conduct fails the *honesty* requirement of good faith.⁸⁴

Other commentators have concurred that good faith *should* preclude rejection in order to escape from a bad bargain, however, unlike Professor Lawrence they do not believe it would be "dishonest" for a buyer to behave this way. For instance, Summers believes that it *should* be bad faith for a buyer to reject for a pre-textual reason, however, he argues

⁷⁸ See U.C.C. § 1-201(20) (2008).

⁷⁹ Burton, *Good Faith IV*, *supra* note 46, at 1539; *see also* Schmitt & Frisch, *supra* note 36, at 1397 ("The good faith required of a consumer purchaser is mere honesty in fact—a subjective test.")

⁸⁰ Burton, *Good Faith IV*, *supra* note 46, at 1539.

⁸¹ *Hubbard v. UTZ Quality Foods, Inc.*, 903 F. Supp. 444, 445–51 (W.D.N.Y. 1995).

⁸² Lawrence, *supra* note 11, at 558.

⁸³ *Id.* at 571.

⁸⁴ *Id.*

that—at least with a party who conceded his ulterior motive—“[s]ome judges may say that such conduct simply is not in bad faith, for it is not dishonest.”⁸⁵ Likewise, Professor Sebert concludes:

While I have no difficulty concluding that a merchant buyer who rejects because of a clearly insubstantial nonconformity in a falling market has failed to comply with the *objective* good faith standard . . . I am not sure that that a nonmerchant buyer’s attempt to use the perfect tender rule to escape a bad bargain is, or should be deemed, “dishonest” within the prohibition of the *subjective* standard of good faith.⁸⁶

Professor Sebert makes his conclusion based on the fact that failure to satisfy the perfect tender rule does in fact constitute a breach.⁸⁷

Not all commentators, however, agree that a falling market should be viewed as evidence of a bad faith rejection on the basis of a minor nonconformity. Professor Gillette argues that since the buyer has caused *neither* the non-conformity *nor* the falling market he should have no obligation to abstain from enforcing his rights to the fullest extent. Instead, he argues “that initial, trivial breach emerges from materialization of a risk which the seller assumed, presumably because he believed he was in a superior position to control the occurrence of the risk.”⁸⁸ Professor Gillette believes the effects of this would force contract parties into “forbearance from self-interested action that conflicts with the interests of other parties.”⁸⁹

In addition, Professor Gillette believes this approach is more faithful to the bargain the parties negotiated and, as such, provides clearer standards of contractual interpretation for future disputes. While critics have contended that buyers assume the risk of a falling market and, thus, their rejection in this circumstance deprives the seller of the expected benefits of the contract, Professor Gillette points out that it is equally true that the seller has assumed the risk of failing to make conforming tender.⁹⁰ Professor Gillette argues that “[m]aterialization of that risk should not be avoided any more readily than materialization of the risk of market decline.”⁹¹ Since there is no way that both parties will still receive the expected value of their bargain in a falling market, it seems unclear why the buyer should be held accountable for the occurrence of a risk he did not control, while the seller is not held accountable for the occurrence of a risk

⁸⁵ Summers, *Good Faith*, *supra* note 16, at 249–50.

⁸⁶ Sebert, *supra* note 14, at 387.

⁸⁷ *See id.* at 387 & n.77.

⁸⁸ Gillette, *supra* note 46, at 641.

⁸⁹ *Id.*

⁹⁰ *Id.* at 655.

⁹¹ *Id.*

that he and he alone controlled. If the seller had feared his ability to deliver goods of a certain quality or within a certain specified time, he could have struck his bargain differently.

Finally, Professor Gillette's argument should not be taken to excuse a buyer who claims a defect when none exists. This would be a breach of the buyer's obligation to accept conforming goods.⁹² Professor Gillette merely points out that it would be "pointless" to also consider the actor's good or bad faith because "when courts speak of bad faith breaches, they impose remedies based solely on the breach that are not connected to the breacher's good or bad motives."⁹³

III. JUDICIAL APPLICATION

A current U.C.C. treatise article describes the process of judicial perfect tender analysis as a two part inquiry: "(1) Do the goods conform to the contract? (2) If the answer to (1) is no, did the buyer reject in good faith?"⁹⁴ As the author points out, "Since the rejection of goods is a matter of performance, there is no doubt that the buyer is under an obligation to act in good faith."⁹⁵ In practice, courts tend to agree with this basic model. For example, in *GE Packaged Power v. Readiness Management Support*,⁹⁶ Readiness Management Support ("RMS") was accused of bad faith rejection of power generators built by GE. The court denied summary judgment to GE citing *two* genuine issues of fact: "(i) whether the generators conformed . . . and (ii) whether RMS believed the generators to be nonconforming."⁹⁷ In the court's view, ascertaining the buyer's "belief" regarding the conformity of the goods was a necessary precursor to evaluating its' right of rejection.⁹⁸ Likewise, another court that had found fabric to be non-conforming nonetheless speculated that if the buyer had rejected for a pre-textual reason "its rejection would certainly not have been in good faith."⁹⁹ A number of other cases confirm these results.¹⁰⁰

Perhaps unavoidably, courts in these cases are forced to determine whether buyers who reject are truly acting honestly. Since it is inherently

⁹² See U.C.C. § 2-301 (2002).

⁹³ Gillette, *supra* note 46, at 638.

⁹⁴ Rusch, *supra* note 40.

⁹⁵ *Id.*

⁹⁶ *GE Packaged Power v. Readiness Mgmt. Support*, 510 F. Supp. 2d 1124 (N.D. Ga. 2007).

⁹⁷ *Id.* at 1134.

⁹⁸ See *id.* at 1133-34 (stating that "[a] rejection of goods must be made in good faith" and "[t]o reject goods in bad faith, a buyer must have no good-faith belief that the goods are conforming").

⁹⁹ *Matrix Int'l Textiles, Inc. v. Jolie Intimates Inc.*, No. 316107/03, 2005 WL 1074774, at *6 (N.Y. Civ. Ct. May 5, 2005).

¹⁰⁰ See, e.g., *Clark v. Zaid, Inc.*, 282 A.2d 483, 484-85 n.1 (Md. 1971) ("The buyer's judgment [as to rejection of goods] would have to be exercised in good faith."); *Y&N Furniture Inc. v. Nwabuoku*, 734 N.Y.S.2d 382, 385 (N.Y. Civ. Ct. 2001) ("[T]he buyer's rejection of the goods must be made in good faith.").

difficult to know another party's subjective motivations, courts have relied on circumstantial evidence out of necessity. For instance, in *Matrix International Textiles v. Jolie Intimates*, the buyer of fabric rejected delivery, claiming it did not conform to the contract specifications.¹⁰¹ The seller suggested that this reason was pre-textual and that the buyer was simply trying to avoid delivery because it was discontinuing the operations of the division that would have used it. The court noted that the buyer had subsequently ordered the item from another supplier at a higher price as circumstantial evidence that rebutted the seller's claim.¹⁰² In another case challenging the rightfulness of a buyer's rejection, the court ruled for the buyer after finding that the seller "has failed to convince [the court] that [the buyer's] motivation for rejecting his potatoes was to obtain similar potatoes but at a reduced cost."¹⁰³ The court cited a lack of "compelling evidence" that the buyer had purchased from other suppliers at lower market prices after rejecting the seller's product.¹⁰⁴

Several courts have suggested that evidence of falling market conditions prior to the buyer's rejection may be used as circumstantial evidence that the buyer rejected for a dishonest purpose. One leading case is *Joc Oil USA v. Consolidated Edison Co. of New York*¹⁰⁵ In that case, Joc Oil contracted to sell a large quantity of oil with a specified maximum sulfur content to Con Ed. When the oil arrived it contained too much sulfur. By the time Con Ed rejected delivery the time for performance had passed, and although Joc Oil offered to cure one day later, Con Ed declined this offer. In the subsequent contract suit, Joc Oil alleged that Con Ed had refused to accept the replacement delivery because foreign market forces had caused the value of the oil to decline and that Con Ed was attempting to escape from a bad deal.¹⁰⁶ The court seemed to agree, finding that "[t]here can be no doubt that this dispute would not exist if the market had risen at the time."¹⁰⁷ The precise issue on which the court decided the case was *not*, however, whether the rejection itself was in bad faith, but rather whether Joc Oil had a reasonable basis to believe that their initial delivery would be accepted and therefore, under U.C.C. section 2-508(2), should have been allotted additional time beyond the specified time of performance to make cure. Concluding that "[i]t is difficult to believe that a construction rewarding culpability and penalizing innocence is

¹⁰¹ *Matrix Int'l Textiles*, 2005 WL 1074774, at *1,*3.

¹⁰² *Id.* at *6.

¹⁰³ *Hubbard v. UTZ Quality Foods, Inc.*, 903 F. Supp. 444, 450 (W.D.N.Y. 1995).

¹⁰⁴ *Id.*

¹⁰⁵ *Joc Oil USA, Inc., v. Consol. Edison Co.*, 434 N.Y.S.2d 623, 630 (N.Y. Sup. Ct. 1980).

¹⁰⁶ *See id.* at 626 (noting the rise in spot oil purchase prices due to the Arab oil embargo and indicating that the main source of contention between the parties appeared to be the price Con Ed would pay for Joc Oil's delivery).

¹⁰⁷ *Id.* at 630.

preferable, or consistent with the remedial intent of the creators of this remedy,” the court found that *Joc Oil* *did* have a reasonable basis to believe the oil would be accepted and therefore should have been given additional time for cure.¹⁰⁸

Although the court likely did not mean to suggest that falling market conditions were evidence of bad faith rejection, its disjointed discussion of good faith, culpability, and the underlying falling market make the opinion ambiguous. Even on appeal, the New York Court of Appeals further obscured the issue when it opined that “the premise [for *Con Ed*’s argument] ignores the policy of the code to prevent buyers from using insubstantial remediable or price adjustable defects to free themselves from unprofitable bargains”¹⁰⁹ At least one plaintiff’s lawyer has cited the case for the proposition that “[t]he Court determined that the buyer used the excuse of the higher sulfur content as a pretext for rejecting the delivery and as an attempt to escape its bad bargain.”¹¹⁰

Other cases *do* seem to have explicitly endorsed the proposition that a falling market for the goods can be used as evidence of a bad faith motivation for rejection. For instance, in *Neumiller Farms v. Cornett*,¹¹¹ *Cornett* and other small potato farmers in Alabama contracted to sell potatoes suitable for “chipping” at a price of \$4.25 per hundred-weight. The buyer, a commercial potato broker, accepted the first several shipments when the market value was \$4.25 per hundred-weight, but when the market price fell to \$2.00 per hundred-weight, the buyer began rejecting delivery claiming that the potatoes did not chip satisfactorily.¹¹² Upon hearing evidence from the seller’s expert that the potatoes were suitable in all respects, the court ruled that the buyer had breached by rejecting delivery in bad faith. The court stated that “[t]he law requires such a claim of dissatisfaction to be made in good faith, rather than in an effort to escape a bad bargain.”¹¹³ Likewise, in *Printing Center of Texas v. Supermind Publishing*, a court stated that “evidence of rejection of the goods on account of a minor defect in a falling market would in some instances be sufficient to support a finding that the buyer acted in bad faith when he rejected the goods.”¹¹⁴ Finally, in *Oil Country Specialists v. Philipp Bros.*, a buyer rejected pipe that was required to meet specified

¹⁰⁸ *Id.* at 630, 632.

¹⁰⁹ *T.W. Oil, Inc. v. Consol. Edison Co.*, 443 N.E.2d 932, 938 n.8, 940 (N.Y. 1982).

¹¹⁰ Trial Brief of Plaintiff Austrian Airlines, *Austrian Airlines Oesterreichische Luftverkehrs AG v. UT Fin. Corp.*, No. 04 Civ. 3854 (LAK) (S.D.N.Y. Feb. 20, 2008), 2008 WL 872782.

¹¹¹ *Neumiller Farms, Inc. v. Cornett*, 368 So. 2d 272 (Ala. 1979).

¹¹² *Id.* at 274.

¹¹³ *Id.* at 275; *see also Baker v. Ratzlaff*, 564 P.2d 153, 157 (Kan. Ct. App. 1977) (noting that evidence of a buyer’s “hasty resale of the popcorn to another buyer at a price nearly double the contract price, provided the trial court with ample evidence upon which to find an absence of good faith”).

¹¹⁴ *Printing Ctr. of Tex., Inc. v. Supermind Publ’g Co.*, 669 S.W.2d 779, 784 (Tex. App. 1984).

industry standards.¹¹⁵ When the pipe did not conform, the buyer rejected the entire inventory. After hearing evidence that a falling market made the transaction “highly unfavorable” to the buyer, a jury concluded that the buyer had rejected in bad faith.¹¹⁶ A Texas appeals court affirmed the decision, finding that the buyer was entitled to reject “only if it did so in good faith[, t]hat is, if it did so with honesty in fact or in keeping with the observance of reasonable commercial standards of fair dealing in the trade.”¹¹⁷ Unfortunately, the court did not specify which of these two criteria the buyer had failed, instead concluding perfunctorily that the evidence was legally and factually sufficient. Other cases suggest the same result.¹¹⁸

Other courts have not been persuaded by evidence of falling market conditions. One representative case is *Austrian Airlines v. UT Finance*. In that case, Austrian Airlines agreed to sell a plane to UT Finance (“UTF”) in a contract which required delivery by a specific date and recited that time was of the essence.¹¹⁹ Austrian Airlines could not deliver the plane in perfect condition on time and UTF rejected delivery, effectively denying Austrian Airlines any chance to cure. Part of Austrian Airlines’ subsequent contract suit argued that UTF’s rejection was made in bad faith because they had only done so to escape a bad bargain. Austrian Airlines pointed to two facts in support of this argument. First, UTF had not yet found a suitable secondary purchaser for the plane and thus there was no practical need for UTF to insist on timely performance. Second, Austrian Airlines pointed out that the plane had been ordered prior to the terrorist attacks of September 11, and in the wake of the resulting turmoil on the airline industry, the value of the plane to UTF had been reduced to two-thirds of its expected value.¹²⁰

The court was unmoved by Austrian Airlines’ evidence, and though it stated that “[t]he Court assumes that UTF, quite understandably, was motivated by the decline in market value,” it held that this was not in bad faith.¹²¹ The court refused to read *Joc Oil USA* and similar cases as establishing that subjective motivations could be dispositive of the issue of

¹¹⁵ *Oil Country Specialists, Ltd. v. Philipp Bros.*, 762 S.W.2d 170, 172–73 (Tex. App. 1988).

¹¹⁶ *Id.* at 178.

¹¹⁷ *Id.*

¹¹⁸ For example, a New York district court opined that “[a]lthough it [is] true that the Code generally obligates a buyer to act in good faith in rejecting goods, plaintiff has introduced no evidence indicating that the defendants’ motivation in rejecting the fuel oil was a bad faith effort to escape the bargain.” *Warren Co. v. Olco Oil Co.*, No. 86-CV-660, 1988 WL 28940, at *3 (N.D.N.Y. Mar. 15, 1988); *see also* *Matrix Int’l Textiles, Inc. v. Jolie Intimates Inc.*, No. 316107/03, 2005 WL 1074774, at *6 (N.Y. Civ. Ct. May 5, 2005); *Hubbard v. UTZ Quality Foods Inc.*, 903 F. Supp. 444, 451 (W.D.N.Y. 1995).

¹¹⁹ *Austrian Airlines Oesterreichische Luftverkehrs AG v. UT Fin. Corp.*, 567 F. Supp. 2d 579, 582–83 (S.D.N.Y. 2008), *aff’d*, No. 08-4176-cv., 2009 WL 1940715 (2d Cir. July 2, 2009).

¹²⁰ *Id.* at 581–82, 591–93.

¹²¹ *Id.* at 599–600.

bad faith.¹²² The court went on to opine that such a rule would not make commercial sense.¹²³ In the court's view, UTF's conduct was "entirely reasonable" since the presence of defects was now even more significant to the buyer than in a normal market.¹²⁴ Noting the sophistication of the parties, the court found "no reason not to give the buyer the benefit of its bargain."¹²⁵ The UTF court's decision was affirmed on appeal by the Second Circuit in a brief opinion that referred to the lower court's decision as "careful," "thorough," and "well-reasoned."¹²⁶

Similarly, a California trial court prohibited a plaintiff from offering proof of an "ulterior motive" by the buyer when rejecting the goods.¹²⁷ In *KCA Electronics*, the court focused strictly on the non-conformities alleged—namely, that six percent of the small computer components lacked the necessary uniformity—and based its decision to grant summary judgment in favor of the buyer strictly on the defect.¹²⁸ Not only did this approach produce a rational and well-reasoned decision, but perhaps most significantly, the absence of extraneous discussions regarding *why* the seller thought the buyer had rejected the goods makes the opinion more precise and helpful to businessmen and lawyers who will have to litigate similar issues in the future.

IV. A NEW FRAMEWORK

A. *Consideration of Falling Market Conditions Is Not Helpful in Deciding Cases*

1. *A Falling Market Does Not Impact Whether a Defect Actually Exists*

Nothing within the text or comments of U.C.C. section 2-601 requires any mental state on the part of either the buyer or the seller in order for the perfect tender rule to apply.¹²⁹ The rule is triggered "if the goods or the tender of the delivery fail in any respect to conform"¹³⁰ Hence, any review of whether a good is or is not conforming is necessarily an objective one. It is only the separate good faith obligation that contains the

¹²² Specifically, the court narrowly read *Joc Oil USA* to apply only in the context of determining a seller's reasonable basis to believe his goods would be accepted under the section 2-508(2) standard, and it distinguished *Neumiller Farms* and *Printing Center of Texas*. *Id.* at 600.

¹²³ *Id.*

¹²⁴ *Id.* at 599.

¹²⁵ *Id.* at 600.

¹²⁶ See *Austrian Airlines*, 2009 WL 1940715, at *1–2.

¹²⁷ *KCA Elecs., Inc. v. Legacy Elecs., Inc.*, No. G037285, 2007 WL 2137959, at *4 (Cal. Ct. App. July 26, 2007).

¹²⁸ *Id.*

¹²⁹ See U.C.C. § 2-601 (2002).

¹³⁰ *Id.*

requirement that the buyer reject the non-conforming tender with the right state of mind. As such, inquiries into the conformity of the goods and the good or bad faith of the rejection are two separate inquiries.¹³¹ A falling market (arguably) is relevant to the latter, but not the former. The initial objective determination of whether a defect is present should not be affected by any external factors including the economy. If such factors are to be taken into account at all, it should be within the context of the actor's good or bad faith.¹³²

Any analysis of whether a good is objectively non-conforming must begin with the terms of the contract. All descriptions of the good being contracted for should be vigorously enforced. In addition, courts should fill in the gaps by resorting to common trade usage and other established commercial practices for the item purchased.¹³³ In comparing what the contract requires to be tendered and what was actually tendered, courts should avoid falling into the trap of using buzz words such as "trivial," which does not aid in the analysis. A small defect that goes to the basis of the bargain should be viewed as legally significant and should permit rejection. By contrast, a defect that does not offend the basis of the bargain should be viewed as legally insignificant and should not permit rejection, even though it could be said to render the good defective under ordinary usage.¹³⁴ In this sense, this author does not disagree with Professor Lawrence's argument that buyers should not be able to reject for what he calls "inconsequential deviations" or defects of "no actual importance to the buyer."¹³⁵ This Note contends that the so-called "trivial defects" may be consequential depending upon the circumstances and, in such cases, buyers should not be restrained from acting upon those small but consequential defects simply because the market for the goods has fallen. This is consistent with the underlying goal of the perfect tender rule: to "create[] an incentive for sellers to produce goods that conform to contract specifications."¹³⁶

¹³¹ See *supra* Part III.

¹³² See, e.g., *GE Packaged Power v. Readiness Mgmt. Support*, 510 F. Supp. 2d 1124, 1134 (N.D. Ga. 2007) (denying summary judgment based on *two* genuine issues of fact: (i) whether the generators conformed . . . and (ii) whether [the buyer] believed the generators to be nonconforming").

¹³³ See U.C.C. § 1-303 (2008).

¹³⁴ Compare *Marlowe v. Argentine Naval Comm'n*, 808 F.2d 120, 124 (D.C. Cir. 1986) (noting a six day delay in delivering an airplane was enough to warrant rejection because time was of the essence), and *Vitol S.A., Inc. v. Koch Petroleum Group, L.P.*, No. 01CV2184(GBD), 2005 WL 2105592, at *9 (S.D.N.Y. Aug. 31, 2005) ("Since time was of the essence in the performance of the parties' contract, defendant's late delivery violated the perfect tender rule because defendant's 'tender of delivery fail[ed] in any respect to conform to the contract.' (alteration in the original)), with *Burgess Steel Prods. Corp. v. Modern Telecomms., Inc.*, 205 A.D.2d 344, 346 (N.Y. App. Div. 1994) (noting that where plaintiff contended that time was *not* of the essence: "a trial is necessary to determine whether the deadline contained in the contract was so inflexible that the plaintiff's late performance constituted a breach of a material element of the contract").

¹³⁵ See Lawrence, *supra* note 11, at 572.

¹³⁶ *Id.* at 578.

2. *If a Defect Does Exist, a Party Cannot Be Said to Be Dishonest in Rejecting Because of It*

Surely it would be dishonest to claim the right to reject by claiming a defect that does not exist. *Neumiller Farms* illustrates this point. In that case, Neumiller Farms rejected potatoes, claiming they did not chip satisfactorily, as required by the contract. After hearing expert testimony, the court concluded that the potatoes were suitable for chipping and, thus, Neumiller Farms received exactly what it bargained for and had been dishonest in claiming otherwise.¹³⁷

Some commentators argue that even if there is a legally significant defect, a buyer must actually be rejecting because of his own subjective dissatisfaction with the defect rather than because of some other factor (such as a falling market). Proponents of this view would suggest that even if the potatoes at issue in *Neumiller Farms* did not chip satisfactorily, if the court was convinced that Neumiller Farms' true reason for rejection was the falling price of potatoes, then the farm would be stuck with them because the right to reject (although present) would have been exercised in bad faith.

A better approach is to treat the honesty prong of the good faith obligation as a nullity in rejection cases because before the question of good faith even arises in this context, it must first be shown that a legally significant defect does in fact exist. Thus, the honesty of the buyer's assertion of a rejection should be decided in light of the initial inquiry into the conformity of the goods. Once it is shown that some legally significant defect does in fact exist, it is inevitable that a buyer who claims the right to reject a good because of the presence of a defect is being honest; were it not for the defect, the right to reject would not and could not be claimed. Certainly a falling market for the goods would have influenced the decision that a particular defect was too much for the buyer to tolerate,¹³⁸ but this should not negate the fact that the defect was ultimately what triggered the rejection; the falling market merely triggered the fact that it was made with a light heart. This very literal approach avoids the complex task of attempting to discern a party's overriding motivation on some deep philosophical level.¹³⁹ This approach also avoids a potentially absurd outcome whereby two identically situated buyers both reject non-conforming goods, one claiming, "I am invoking the perfect tender rule

¹³⁷ See *Neumiller Farms, Inc. v. Cornett*, 368 So. 2d 272, 274–75 (Ala. 1979).

¹³⁸ Toleration of defects admittedly becomes much more difficult in a falling market, a point which is explored more in the subsection that follows.

¹³⁹ It also avoids the flawed assumption that any particular course of action can be explained by one principle motivational factor. This is a questionable assumption even in the context of individual decision making, let alone in the context of commercial business decisions where multiple players (e.g., CEO, in-house counsel, sales manager) with potentially different motivations, each contribute to a decision to reject a particular shipment of goods.

because of defect [X],” and the other claiming, “I am invoking the perfect tender rule because the market for these goods has declined.” If we take seriously the notion of honesty in this setting, then the former buyer has breached his contractual obligations whereas the latter has not. There is no reason to think that the U.C.C. was ever intended to produce such a result and potentially push buyers to claim that they acted for the most insidious reasons imaginable simply to guard against potential liability under the honesty prong of the good faith obligation.¹⁴⁰

3. *It Is Commercially Reasonable to Expect the Full Benefit of One's Original Bargain in a Falling Market*

The second prong of contractual good faith—that the parties abide by “commercially reasonable standards of fair dealing in trade”—is very context- and industry-specific. Nonetheless, there is no reason to think that there cannot be some generalization across industries on some broad points. Particularly with respect to large commercial parties the reasonable commercial standards are likely somewhat homogenous.¹⁴¹

In a falling market, the value of what the buyer is receiving is already, by definition, reduced. Therefore, any defects in the goods are even more significant to a buyer than they ordinarily would be because they necessarily reduce the already deflated value of the goods even further. Having already received the short end of the stick with respect to the market value of the goods, it is all the more reasonable for the buyer to ensure that at the very least the goods are what the contract requires them to be.¹⁴² On the whole, the case law shows that buyers are permitted to reject goods with trivial defects so long as they are legally significant. To deny this right *because of* a falling market would have the perverse effect of denying this otherwise tenable course of action at a time when it is most reasonable for the buyer to want to exercise it.

¹⁴⁰ To the extent that parties claimed such an insidious purpose, even while actually believing themselves to be acting for just reasons, this would produce a somewhat paradoxical result of lying in order to be deemed honest.

¹⁴¹ To the extent that this is not true—for there are surely examples where it is not—courts should always elevate the specific industry practices above the more general business norms.

¹⁴² The *Austrian Airlines* court stated:

Nor would the rule for which [the seller] argues make much commercial sense. Where a buyer pursuant to a contract calling for future delivery is presented with non-conforming goods, price movements intervening between the agreement and the time for delivery often are taken into consideration in determining whether to reject. It makes sense to consider them because nonconformities often go not to the ultimate utility of the goods, but to their value, especially resale value. Where the parties . . . contract in terms that give the buyer the right to walk away from the deal in the event of a non-conforming tender, there is no reason not to give the buyer the benefit of its bargain.

Austrian Airlines Oesterreichische Luftverkehrs AG v. UT Fin. Corp., 567 F. Supp. 2d 579, 600 (S.D.N.Y. 2008), *aff'd*, No. 08-4176-cv., 2009 WL 1940715 (2d Cir. July 2, 2009).

B. *The Argument for Categorical Exclusion*

Thus far, this Note has posited that evidence of a falling market is not helpful in the adjudication of disputes over rejection of goods. One could fairly ask why we should categorically exclude such evidence. After all, in some sense it is true that totally removing this circumstantial evidence from the equation could invite some buyers to use their rejection right strategically as a means of avoiding the contract. Conversely, if such evidence is allowed in contract disputes, it is unlikely that sellers would have a similar strategic response; they are unlikely, after all, to intentionally produce goods which fail to conform to the terms of the contract simply because they would be armed with a factually difficult argument that those goods were really rejected on the basis of a falling market. Given this reality, it is fair to ask, “Why not just allow evidence of a falling market to enter these cases for what it is worth?” The response is two-fold. First, to say that a decision to reject in a falling market is “strategic” is not to say that it is wrong or unjustified.¹⁴³ Second, the inclusion of falling markets evidence in rejection cases hurts the overall body of contract law.

When goods that are slightly non-conforming are tendered, a buyer is left with two options. First, he can ask the seller to repair the defect.¹⁴⁴ The second option—assuming this is not an instance where the right to cure is present—the buyer can reject the goods outright and risk the dual possibilities of destroying his relationship with this seller and potentially facing litigation. Given the apparent downsides to the second option, buyers are likely to think carefully before taking that course. It is certainly true that the market for the goods is a factor that will play into the analysis. Clearly, if the value of goods had risen rather than fallen, a buyer would be less insistent on enforcing his rights to the fullest degree. He would likely forego his right to rejection and instead permit extra time to make cure or negotiate a cash payment as damages for acceptance of slightly non-conforming goods.¹⁴⁵ However, just because the buyer has the ability not to enforce his rights to the fullest extent does not mean that he does not possess those rights in the first place. Parties in voluntary transactions always have the ability to waive their rights against one another, or they have the ability to enforce them exactly. That market circumstances dictated which course they selected should not detract from the fact that they did actually possess the right to take the action they took under the

¹⁴³ Likewise, saying that conduct was not entered into strategically by the other party does not mean that that the conduct was rightful under the terms of the contract.

¹⁴⁴ Indeed, this is sometimes, but certainly not always, required under the seller’s right to cure. See discussion *supra* Part II.A.2.

¹⁴⁵ U.C.C. section 2-714 (2002) allows buyers to accept non-conforming goods and sue under the warranty for the damage caused by the non-conformity.

terms of the contract, that the exercise of this right was honest, and that it was commercially reasonable. As Professor Gillette suggests, “That the buyer receives a windfall from the fortuitous breach does not necessarily mean that he is not entitled to it.”¹⁴⁶

In addition, while it may be a stretch to believe that a seller will actually go out of his way to strategically saddle a buyer with non-conforming goods, the perfect tender rule is itself an acknowledgement that in the case of one-shot contracts, buyers need a pretty big stick in order to protect themselves from shoddy workmanship. This is particularly true when the defects are small and, therefore, a substantial performance requirement would be inadequate to protect buyers’ rights. It is consistent with this policy to deny the use of falling market evidence, which would tend to undermine the strength of the rule by giving credence to an excuse for lax quality standards (even if those lax quality standards were not undertaken strategically).

Finally, there are other consequences of allowing sellers to introduce evidence that rejection was motivated by a falling market which are, on balance, bad for contract law.

1. *Detracts from the Development and Clarity of U.C.C. Case Law*

Judge Learned Hand once opined that words such as “good faith . . . obscure the issue.”¹⁴⁷ Indeed, cases such as *Joc Oil USA*, *Neumiller Farms*, and *TX Printing* are difficult to read because the presence of discussions regarding the market for the goods detracts from, and confuses, the discussion of the conformity of the goods. It is difficult to tell if the reason for the court’s holding is the existence of a non-conformity, or the existence of evidence of a falling market. If a future case arises where a buyer notices a non-conformity that has previously been held to be legally insignificant and, thus, insufficient to allow for rejection in a falling market, it is unclear how much weight to give such a holding if the value of the goods in the current case has remained steady.¹⁴⁸ This lack of clarity has needlessly impaired the ability of practitioners to advise their clients as to when they can comfortably reject a good that they deem non-conforming. Professor Gillette has summarized the dilemma by saying:

It is unclear whether the attorney can advise his client that cancellation of the contract with the defaulting seller is

¹⁴⁶ Gillette, *supra* note 46, at 655.

¹⁴⁷ *Thompson-Starrett Co. v. La Belle Iron Works*, 17 F.2d 536, 541 (2d Cir. 1927). See also *Market St. Assocs. v. Frey*, 941 F.2d 588, 593 (7th Cir. 1991), a case in which Judge Posner quotes Judge Hand and agrees with his sentiment.

¹⁴⁸ Obviously, this type of common law problem is in no way unique to perfect tender rule cases. My point here is only that in perfect tender rule cases, perhaps unlike other cases, there is no need for courts to engage in two parallel lines of reasoning. In this context, one discussion would suffice, and therefore should be deemed preferable.

appropriate under an expansive good faith standard. He must determine whether the client will be affected adversely—beyond the loss of a better bargain—by the nonconformity. Regardless of the difficulty of such a determination, the need to make the inquiry at all introduces into sales law the notion of material breach that is rejected explicitly by the host of provisions concerning perfect tender and cure.¹⁴⁹

Professor Sebert argues that the lack of cases using the duty of good faith as a basis for denying buyers a right to rejection may be evidence of the influence the doctrine is having “at the point of decision by a buyer.”¹⁵⁰ Such a result may well be tolerable, but it should not be preferable.

Courts should be careful to keep discussions of conformity of the goods separate from discussions of the good faith of the actors, and since a falling market has no bearing on either, it should be left out of decisions all together. If there is clear evidence that a good was conforming (as in *Neumiller Farms*), then rejection should be deemed wrongful irrespective of the motive of the buyer. In such cases, courts need not, and should not, even reach the issue of bad faith. If the good is found non-conforming then an inquiry into good faith is justified, however, since the presence or absence of a falling market should have no impact on this determination, it remains an inappropriate subject matter. *KCA Electronics* is an example of a case that follows just this model and the holding is made much clearer because of it.¹⁵¹

2. *Encourages Litigation at the Expense of Voluntary Settlement*

For businessmen, even a case that is won in litigation generally represents (at best) an unwanted annoyance. One of the chief goals of the U.C.C. is to provide consistency and predictability in American contract law.¹⁵² This predictability is important to help guide parties’ conduct, both in the ordinary course of business, as well as in their decision making after a dispute has arisen (such as when deciding whether to sue or what litigation theories to utilize).¹⁵³ Ideally, parties should be able to resolve their commercial differences without resorting to judicial intervention; however, realization of this goal requires a predictable outcome if they fail

¹⁴⁹ Gillette, *supra* note 46, at 652–53.

¹⁵⁰ Sebert, *supra* note 14, at 389.

¹⁵¹ *KCA Elecs., Inc. v. Legacy Elecs., Inc.*, No. G037285, 2007 WL 2137959, at *5 (Cal. Ct. App. July 26, 2007).

¹⁵² See U.C.C. § 1-103 (2008) (“The [U.C.C.] must be liberally construed and applied to promote its underlying purposes and policies, which are: (1) to simplify, clarify, and modernize the law governing commercial transactions . . . [and] (3) to make uniform the law among the various jurisdictions.”).

¹⁵³ See Gillette, *supra* note 46, at 621 (“The Code . . . is a tool for businessmen and their attorneys to predict the legal consequences of voluntary transactions.”).

to agree. This in turn requires “precision of definition and certainty of the effects of performance and nonperformance.”¹⁵⁴ Without this certainty of effect, parties may be tempted to abandon the cooperative channels more readily in hopes of imposing a superior result upon their trading partner by judicial decree.

Allowing bad faith to void an otherwise tenable right of rejection, encourages litigious behavior by undeserving sellers who have tendered non-conforming goods. As Professor Burton has observed, the imprecise boundaries of good faith have produced “[j]ust enough unorthodox judgments . . . to inspire ever-optimistic plaintiffs’ counsel to keep the lawsuits coming.”¹⁵⁵ Ambiguity breeds test cases. Sometimes ambiguity is necessary or even appropriate, but in the commercial contracts context it often leads to inefficiency. For instance, the extraneous discussion of good faith and the falling market in *Joc Oil USA* turned what could have been a straightforward U.C.C. section 508(2) case into a disjointed discussion that was later cited—erroneously—by a plaintiff in a multi-million dollar contract dispute.¹⁵⁶ As has been explained, there is no need for the ambiguity posed by judicial opinions discussing falling markets in cases contesting the rightfulness of rejection, and, therefore, such ambiguity should be readily avoided.

C. *Potential for Abuse Can Be Limited by Other Legal Doctrines and Perfect Tender Rule Constraints*

Nothing in this Note should be taken to suggest that cases such as *Neumiller Farms* (which considered the falling market in determining that the buyer had made a bad faith rejection) reached an incorrect result; indeed the reverse is true. As Professor Gillette opines, “If there were no other safety valve available to prevent the waste inherent in the possibility of rejections for trivial defects, use of the good faith obligation might therefore appear justifiable.”¹⁵⁷ The problem that has been posited is that such cases inadvertently and unnecessarily complicate the issues. Several other “safety valves” exist and should be utilized to produce clearer decisions in future falling market rejection cases.

First and foremost, courts should recognize that they do not need to address the issue of good faith unless a legally significant non-conformity is found to exist. *Neumiller Farms* is illustrative. There, Neumiller Farms contracted for the purchase of potatoes suitable for chipping, and that is exactly what the court found it had received.¹⁵⁸ Therefore, Neumiller

¹⁵⁴ *Id.*

¹⁵⁵ Burton, *Good Faith IV*, *supra* note 46, at 1535.

¹⁵⁶ See *supra* note 110 and accompanying text.

¹⁵⁷ Gillette, *supra* note 46, at 653.

¹⁵⁸ *Neumiller Farms, Inc. v. Cornett*, 368 So. 2d 272, 274–75 (Ala. 1979).

Farms had a contractual obligation to do as it had agreed.¹⁵⁹ This should have ended the analysis. It is irrelevant to inquire *why* Neumiller Farms performed the way it did or what market factors were to blame. By discussing the falling market conditions and imploring notions of good faith, the court turned an easy case into a hard one. Simply put, if a tendered good conforms to the terms of the parties' bargain it should always be a breach for the buyer to reject delivery.

In addition, courts should enforce the seller's remedy of cure in appropriate cases. Although, as stated in Part II, sellers often do not have any time allotted to make cure, sometimes they do.¹⁶⁰ Buyers who recognize the possibility of a court finding *them* in breach for not permitting a seller to exercise its right to cure will be more willing to bargain and negotiate acceptable remedies without resorting to legal doctrines, and, more importantly, without using precious judicial resources to get there. As Professor Gillette points out, "A buyer seeking to avoid his bad bargain would be unlikely to invest time or resources in discovering a nonmaterial defect if the known consequence of his rejection is to give the seller an additional opportunity to tender conforming goods."¹⁶¹ To the extent that time for cure is still available, courts should fully utilize it.

Further, although this Note has advocated that, in a general sense, it should not violate any broad standards of commercial dealing for a buyer to reject for small non-conformities when it suits his interests, the argument should not be read to dismiss reasonable commercial standards as an ineffective restraint on the perfect tender rule. Indeed, commercial practices such as trade usage, course of performance, or course of dealing, may be very compelling on a case-by-case basis. For example, a buyer who is contractually entitled to silver widgets but has always accepted bronze widgets from a particular seller should not be able to suddenly insist on silver simply because the price of widgets falls. In that case, the parties would be said to have a clear course of performance establishing that bronze widgets are in fact conforming under the contract—the written terms notwithstanding—and, as such, the buyer would not be entitled to the right of rejection.

Finally, the majority of the discussion throughout this Note has assumed a transaction involving two large sophisticated parties. In this context we can, and should, readily expect these parties to take care of themselves. These types of parties should not be able to use good faith as a means of crying foul in a falling market simply because they failed to

¹⁵⁹ *Id.*

¹⁶⁰ *See, e.g.,* *Joc Oil USA, Inc., v. Consol. Edison Co.*, 434 N.Y.S.2d 623, 632 (N.Y. Sup. Ct. 1980) (stating that Joc Oil made "a reasonable and timely offer to cure").

¹⁶¹ Gillette, *supra* note 46, at 654.

properly plan their transactions with the necessary specificity in good economic times. Given the resources of sophisticated commercial parties, it is not too much to ask them to safeguard their own interests. It may, however, be too much to ask of a smaller, less sophisticated, buyer. Indeed, one plausible way of reconciling decisions protecting sellers in falling markets and those declining to, are that—as best the records indicated—the sellers in the former category tend to be smaller entities, while those in the latter category tend to be more sophisticated businesses.¹⁶²

If it is true that the real concern is protecting smaller sellers who lack the bargaining power to protect themselves from being exploited by unfair rejection in a falling market, then courts would be better served by simply saying as much. Instead of accomplishing this aim through the obligation of good faith—which, under the revised U.C.C. section, one applies the same to all parties, whether merchant or non-merchant, sophisticated or unsophisticated—courts could use another doctrine that is more readily understood as a tool to alleviate otherwise harsh results for parties with disparate bargaining power: unconscionability.¹⁶³ To the extent that a rejection right seems to give a large commercial buyer a patently unjust right of rejection over an individual seller with little bargaining position, it may be appropriate for courts to declare that right of rejection unconscionable under certain facts.¹⁶⁴ This will achieve the same goal of protecting weaker parties, without undermining the clear application of the perfect tender rule to more sophisticated sellers who could have protected themselves—*but chose not to*—by bargaining for a more precise description of goods, or a longer time in which to tender them.

¹⁶² Compare *Neumiller Farms*, 368 So. 2d 272 (involving a dispute between individual potato farmers in DeKalb County, Alabama and a corporate buyer), and *Printing Ctr. of Tex., Inc. v. Supermind Publ'g Co.*, 669 S.W.2d 779 (Tex. App. 1984) (involving a dispute between an independent publisher and a local printing company), with *Austrian Airlines Oesterreichische Luftverkehrs AG, v. UT Fin. Corp.*, 567 F. Supp. 2d 579 (S.D.N.Y. 2008) (involving a dispute between a multi-national airline and a multi-national conglomerate), and *KCA Elecs., Inc. v. Legacy Elecs., Inc.*, No. G037285, 2007 WL 2137959 (Cal. Ct. App. July 26, 2007) (involving a dispute between two high-tech California companies). *But see Oil Country Specialists, Ltd. v. Philipp Bros.*, 762 S.W.2d 170 (Tex. App. 1988) (involving a dispute between two oil companies).

¹⁶³ See *Cont'l Airlines, Inc. v. Goodyear Tire & Rubber Co.*, 819 F.2d 1519, 1527 (9th Cir. 1987) (“The doctrine of unconscionability cannot be invoked by so sophisticated a party as [the plaintiff] in reference to a contract so laboriously negotiated.”); see also *Geldermann & Co. v. Lane Processing, Inc.*, 527 F.2d 571, 576 (8th Cir. 1975) (noting that unconscionability does not protect a sophisticated investor); *AMF Inc. v. Computer Automation, Inc.*, 573 F. Supp. 924, 930 (S.D. Ohio 1983) (finding unconscionability inapplicable in a contract between “large, sophisticated merchants”).

¹⁶⁴ Consider the following example: an adhesion contract between a large company and an individual seller that contained a vague description of the goods, which the large buyer then used to reject goods in a falling market at will, could potentially be deemed unconscionable.

V. CONCLUSION

Despite the fact that the issue of contested rejection of goods against the backdrop of a falling market for the goods is likely a reoccurring issue for many businesses, the issues presented have not been adequately resolved. This is surely—at least in part—a function of businesses’ understandable reluctance to engage in costly litigation, especially when the harm caused by any particular contractual transgression often pales in comparison to the attention necessary to satisfy the business’s other obligations. Hopefully, this Note represents a step in the direction of further examination, debate, and clarification. The framework proposed is meant to be a subtle attempt to refine future judicial opinions to achieve a more focused pool of case law from which future business lawyers can discern precisely where their clients stand. Though the framework suggested may appear to be pro-buyer, nothing argued in Part IV should be seen as particularly radical¹⁶⁵ and to illustrate this point, this Note concludes by examining two previously discussed cases, *Austrian Airlines* (which supports this Note’s position) and *Joc Oil USA* (which does not) to see what would happen if the alternative rule had been applied to the facts.

In *Austrian Airlines*, the court was unmoved by the seller’s evidence of a severe decline in the value of the plane, which was tendered and subsequently rejected by the buyer. The defects to the plane included the lack of a required FAA Certificate of Airworthiness, without which the plane was useless. If the court had found UTF’s rejection to be a bad faith effort to escape from the bargain, then its rejection of the plane would have been deemed an acceptance and it would have been the not-so-proud owner of a plane, the value of which had been severely deflated not just by uncontrollable market fluxuations, but also by the seller’s own incompetent ability to build it correctly. Some readers may find no trouble with this result—it is, after all, hard to be outraged by the slight unfairness this would impose upon a sophisticated entity such as UTF. However, this result is not contemplated by the contract that two sophisticated parties negotiated and entered into. In the contract they struck, *Austrian Airlines* assumed the risk of failing to make perfect tender. UTF obviously contemplated the value of the plane in the current market when making its decision to reject delivery, but the court was correct to hold that this was nothing more than a reasonable business decision based on a negotiated contract and that there was “no reason not to give the buyer the benefit of

¹⁶⁵ Specifically, I do not wish to suggest any sort of departure from Professor Corbin’s wise admonition that “[t]he law seeks to be neutral between the competing interests of seller and buyer.” Instead, I strive only to promote a framework to accomplish, as Professor Corbin also advocates, the perfect tender rule’s purpose of “protect[ing] the buyers of goods against sellers who would be tempted to saddle buyers with unsuitable and defective goods if buyers could not reject.” ARTHUR L. CORBIN, CORBIN ON CONTRACTS § 33.3 (2009).

its bargain.”¹⁶⁶

In *Joc Oil USA*, the contract required delivery of oil meeting maximum sulfur content requirements with delivery during a specified period. The seller delivered oil with sulfur in excess of this amount and the buyer rejected. Since the stated time for performance had passed, the buyer refused to allow the seller any additional time to cure. In finding that the seller had a reasonable basis to believe his initial tender would be acceptable, the court frequently referenced the sharp decline in the oil market as evidence of the buyer’s unsavory motives.¹⁶⁷ Regardless of whether the court meant to suggest a rule of law that rejection for minor defects in a falling market could be grounds for a finding of bad faith, these passing comments did provide fodder for such claims. In reality, the court never needed to go down the path of discussing the falling market for oil because, even without it, there was ample evidence to support the seller’s position.

The court noted that the seller had no knowledge that the oil contained too much sulfur and, in fact, had received a report from their supplier indicating that the oil would conform.¹⁶⁸ This would seem to satisfy the test advocated by White and Summers that the buyer be unaware of the defect despite his good faith and prudent business behavior.¹⁶⁹ In addition, even under the more restrictive approach advocated by Nordstrom,¹⁷⁰ the seller likely had reason to believe that his oil would be acceptable with a cash allowance because even the non-conforming shipment had a sulfur content within a range that the seller knew that the buyer was authorized to buy.¹⁷¹ From this evidence alone, the court could have inferred a reasonable basis to believe that the initial delivery would be acceptable.¹⁷²

Since the buyer failed to provide the seller with the additional time to cure, which the court found he was entitled to, it had breached the contract regardless of its motives. Similarly, had the seller been unable to cure within a reasonable amount of additional time, then the buyer would have been fully within its rights—falling market or not—to reject delivery. To do otherwise would run contrary to the parties’ contract and force the buyer to accept poorer quality oil, when it had already suffered the misfortune of seeing the value of its purchase decline in the world oil market.

¹⁶⁶ *Austrian Airlines*, 567 F. Supp. 2d at 600.

¹⁶⁷ See *supra* notes 105–08 and accompanying text.

¹⁶⁸ *Joc Oil USA, Inc. v. Consol. Edison Co.*, 434 N.Y.S.2d. 623, 630 (N.Y. Sup. Ct. 1980).

¹⁶⁹ See *WHITE & SUMMERS*, *supra* note 7, at 324.

¹⁷⁰ See *NORDSTROM*, *supra* note 35, at 321.

¹⁷¹ *Joc Oil USA, Inc.*, 434 N.Y.S.2d. at 626.

¹⁷² If anything, the evidence of a falling market for oil, which the court included in this portion of its discussion, actually seems to cut the other way. The seller’s knowledge that the market was falling should have made the possibility of the buyer’s rejection less of a surprise.

In short, no harm is caused by ignoring the presence of a falling market in a case where the buyer's rejection has been contested; however, significant confusion, litigation, and unfairness to the contractual rights of buyers may result from its inclusion. As such, courts would be prudent to follow decisions such as *Austrian Airlines* and *KCA Electronics* and make their perfect tender rule discussions more about the conformity of the goods and less about market conditions that have only a sentimental impact on the outcome.