

Essay Question No. 7

Answer the question in booklet No. 7

PetroPipe is one of only a handful of manufacturers in the world to produce *BelowZero*, an arctic-grade petroleum pipeline system designed to transport oil overland in harsh temperatures and other adverse conditions. Identifying Alaska as a desirable market, *PetroPipe* spent most of 2012 courting representatives from *OkayOil*, one of the major oil producers in the state. *PetroPipe* emphasized the benefits of using *BelowZero* in Alaska and provided specifications for the extensive preparatory work *OkayOil* would have to undertake to update and enhance its existing infrastructure before the new system could be operational. *PetroPipe* quoted a price of \$2 million for the system.

On January 5, 2013, the President of *PetroPipe* sent *OkayOil*'s CEO an email containing a scanned copy of a signed letter offering to sell her company a *BelowZero* system for a total cost of \$1.8 million, with delivery to be completed no later than March 1, 2013. The letter went on to state that the system would be under warranty for five years and that payment could be made in monthly installments beginning on April 1, 2013. *PetroPipe* closed the letter by saying the offer would remain open for a period of 14 days.

OkayOil's CEO was thrilled to see the letter with the offer of a better price and she immediately telephoned *PetroPipe*'s president and left a message saying: "Your proposal looks wonderful and I accept. Please give me a call when you are next in the office to go over the details."

OkayOil immediately began the process of preparing its stations in the exact manner that *PetroPipe* had specified, including construction of several new buildings and hiring new engineers that were trained in using *BelowZero*.

On January 15, 2013, *OkayOil*'s CEO received an email from *PetroPipe* stating: "All outstanding *BelowZero* pipeline system offers are rescinded." The CEO immediately called *PetroPipe* and left an angry message on the President's answering machine. *PetroPipe* later telephoned and offered to sell the system to *OkayOil* for \$2.5 million.

1. Was a valid contract formed between *PetroPipe* and *OkayOil* for the sale of the *BelowZero* system for \$1.8 million? Discuss.

2. Assuming for the purposes of this question only that a valid contract was formed, what potential remedies are available to *OkayOil* for *PetroPipe*'s breach? Discuss.

Graders' Guide
*****Question No. 7*****
Contracts

1. Did PetroPipe and OkayOil form a valid contract for the sale of the BelowZero system for \$1.8 million? Discuss. (50 points)

Yes, the parties formed a valid contract for the sale of BelowZero because the necessary elements for contract formation were present and satisfied, as was the statute of frauds.

A. The Elements of Contract Formation (20 points)

Under Alaska law, the following four elements are required to form a valid contract: (1) an offer encompassing all essential terms; (2) an unequivocal acceptance of those terms by the offeree; (3) consideration; and (4) a mutual intent to be bound by the contract. *Sykes v. Melba Creek Mining, Inc.*, 952 P.2d 1164, 1167 (Alaska 1998). Examinees should present some brief analysis as to whether the agreement between *PetroPipe* and *OkayOil* formed a valid contract – without a contract, there can be no breach.

Here, the elements of a valid, express contract appear to be present. The letter that *PetroPipe* emailed to *OkayOil's* CEO included all essential terms: product identification, price, delivery schedule, warranties and payment terms. Examinees may discuss the fact that the *OkayOil* CEO's acceptance was not unequivocal based on her closing comment that *PetroPipe* should contact her to "go over the details." On the other hand, the CEO opened her message by saying "I accept." Based on these facts, an examinee could argue that at the time of the offer and acceptance, both parties intended to be bound by the contract and that the sale price of \$1.8 million served as appropriate consideration.

B. Uniform Commercial Code (20 points)

The Uniform Commercial Code (UCC) applies to this particular sale. Alaska Statute 45.02.102 provides that the UCC applies to transactions in "goods" which are defined by AS 45.02.105 as "all things, including specially manufactured goods that are moveable at the time of identification of the contract for sale...." A petroleum pipeline system would fall within this category of "goods."

Pursuant to Alaska Statute 45.02.204, "[a] contract for sale of goods may be made in any manner sufficient to show agreement, including conduct by both parties that recognizes the existence of the contract." Such an agreement maybe formed even if "the moment of its making is undetermined" and there may be terms left open. AS 45.02.204(b), (c). Here, examinees may argue that *OkayOil's* renovation efforts and new hires demonstrated an agreement to the terms set out in *PetroPipe's* email. Taken along with *OkayOil* CEO's response

to the email stating “I accept”, the fluid communications between the parties in this case constitute strong evidence that they formed a contract.

Alaska Statute 45.02.204 pertains to offer and acceptance under the UCC. An offer to make a contract shall be construed as inviting acceptance in any manner and by any medium reasonable in the circumstances. AS 45.02.206(a)(1). There is nothing in the facts to suggest that the immediate telephone call to *PetroPipe* accepting the offer was anything other than reasonable under the circumstances.

C. Statute of Frauds (10 points)

Under AS 45.02.201, a contract for the sale of goods for the price of \$500 or more “is not enforceable by action or defense unless there is a writing sufficient to indicate that a contract for sale has been made between the parties and signed by the party against whom the enforcement is sought or by an authorized agent or broker of that party.”

Courts have uniformly interpreted the statute of frauds in a manner that does not require a formal written contract. The statute has been applied on a case-by-case basis and in a flexible way to accept most any writing that realistically dispels the danger of fraud. *See Fleckenstein v. Faccio*, 619 P.2d 1016, 1020 (Alaska 1980) (quoting 2 Arthur Corbin, *Corbin on Contracts* § 498, at 681 (1950)(internal citations omitted)).

Here, based on the facts presented, examinees should recognize that there is a writing signed by the party to be charged, *PetroPipe*. There is no real basis to object to the writing under these facts, and the email signals *PetroPipe*’s intent to be bound by its offer. Examinees should conclude that the statute of frauds is satisfied in this instance.

2. Assuming for the purposes of this question only that a valid contract was formed, what potential remedies are available to OkayOil for PetroPipe’s breach? Discuss. (50 points)

A. General Principles of Damages for Breach (10 points)

Courts award damages for a breach of contract with the aim of placing the injured party in as good a position as he or she would have been in had the contract been fully performed. *McBain v. Pratt*, 514 P.2d 823, 828 (Alaska 1973); *Green v. Koslosky*, 384 P.2d 591 (Alaska 1963). The Alaska Supreme Court has adopted the terms of the Restatement (Second) of Contracts, which provides:

Subject to the limitations stated in Sections 350-53, the injured party has a right to damages based on his expectation interest as measured by

- a) the loss in the value to him of the other party's performance caused by its failure or deficiency, plus
- b) any other loss, including incidental or consequential loss, caused by the breach, less
- c) any cost or other loss that he has avoided by not having to perform.

Restatement (Second) of Contracts, § 347, at 112 (1981); *cited in Alaskan Reclamation and Pest Control, Inc. v. United Bank Alaska*, 685 P.2d 1211, 1223 (Alaska 1984); *American Computer Inst., Inc. v. State*, 995 P.2d 647 (Alaska 2000).

B. Expectation Interest (15 points)

The ordinary measure of damages in contract law is the expectation interest, which strives to give the benefit of the bargain to the non-breaching party. *Alaska Const. Equip., Inc. v. Star Trucking, Inc.*, 128 P.3d 164 (Alaska 2006). *See also Restatement (Second) of Contracts* § 347 & cmt. a (1981) ("Contract damages are ordinarily based on the injured party's expectation interest and are intended to give him the benefit of his bargain by awarding him a sum of money that will, to the extent possible, put him in as good a position as he would have been in had the contract been performed.").

Expectation damages may be in the form of (1) the difference between the cost of obtaining a replacement from another source and the contract price or (2) the difference between market price at the time of the breach and the contract price. AS 45.02.712, 713.

Here, *OkayOil* may attempt to enter into a reasonable purchase of *BelowZero* from another manufacturer, in which case it could seek the difference between the cost of cover and the contract price, along with any incidental or consequential damages, less expenses saved as a result of the seller's breach. *See* AS 45.02.712. *OkayOil* may also seek to recover the difference between the market price at the time of *Petropipe's* breach and the contract price, along with any incidental or consequential damages, less expenses saved. *See* AS 45.02.713.

C. Consequential Damages (15 points)

Alaska courts regularly award consequential damages in breach of contract actions. *See, e.g. Hancock v. Northcutt*, 808 P.2d 251, 257 (Alaska 1991) (consequential damages generally available); *American Computer Institute, Inc. v. State*, 995 P.2d 647, 655 (Alaska 2000) (plaintiffs awarded consequential damages as part of generally recoverable contract damages). "Consequential losses which the seller could reasonably have anticipated when the contract was made are also recompensable." *Guard v. P & R Enterprises*,

Inc., 631 P.2d 1068, 1071 (Alaska 1981) (citations omitted). Generally, consequential damages will only be excluded from the range of a plaintiff's potential recovery if they are specifically excluded by contractual agreement. *Pierce v. Catalina Yachts, Inc.*, 2 P.3d 618, 621 (Alaska 2000). That is not an issue under the facts presented as the parties' agreement did not mention damages.

Alaska's UCC, AS 45.02.715, provides for incidental and consequential damages resulting from the seller's breach that include "expenses reasonably incurred in inspection, receipt, transportation, and care and custody of goods rightfully rejected, any commercially reasonable charges, expenses, or commissions in connection with effecting cover and other reasonable expense incident to the delay or breach." Additionally, Alaska courts will award prejudgment interest as a form of consequential damages. *Farnsworth v. Steiner*, 638 P.2d 181, 184 (Alaska 1981).

Here, *OkayOil* would likely seek consequential damages based on the actions undertaken in reliance upon *PetroPipe*'s offer under the contract. *PetroPipe* would respond by pointing out that the changes *OkayOil* made to its infrastructure and staffing could be applied to a substitute system, one other than *BelowZero*, and therefore damages should not be available. *OkayOil* would respond that it is entitled to recover expenses associated with the very specialized construction of new buildings and the hiring of specially trained personnel for the particular purpose of utilizing the unique *BelowZero* system.

D. Specific performance (10 points)

Specific performance is an equitable remedy that is available in Alaska "where the goods are unique or in other proper circumstances." AS 45.02.716; *Gudenau v. Bierria*, 868 P.2d 907 (Alaska 1994). "The decree for specific performance may include such terms and conditions as to payment of the price, damages, or other relief as the court considers just" and the buyer has a right to enforce the contract "if after reasonable effort the buyer is unable to effect cover for the goods or the circumstances reasonably indicate that such effort will be unavailing...." AS 45.02.716.

Historically, specific performance has been available only where money damages were inadequate, but the modern trend has been to relax that requirement. *Gudenau*, 868 P.2d at 912. Here, the legal remedies discussed above are probably not inadequate. However, examinees may recognize that specific performance is an avenue of recovery that *OkayOil* could pursue under Alaska law, particularly in light of the discussion of the unique nature of the *BelowZero* system set out in the fact pattern.

Conclusion

The examinees' ultimate conclusions on most points are not as important as the analysis they perform in reaching those conclusions.