goods) may establish a contractual relationship under §2-207(3), and Comment 7 to §2-207. If the seller in *Brown Machine* had by tracking the statutory language succeeded in making only a "conditional acceptance" (and thus in effect a counter-offer), would its proposed indemnification clause have become part of the contract under §2-207(3)?

7. *What are "supplementary terms" under §2-207(3)?* If an offeree's response is deemed to be at most an "expressly conditional" acceptance, and thus in effect a counter-offer, but the parties proceed to performance without an express acceptance of the counter-offer's terms, what then? Under §2-207(3), the contract will consist of those terms on which the writings of the parties agree, "together with any supplementary terms incorporated under any other provisions of this act [i.e., the UCC]." Clearly those "supplementary terms" would include such implied terms under Article 2 as the implied warranties of merchantibility and fitness (§§2-314 and 2-315) and the damages provisions, including seller liability for consequential damages (§2-715), along with more innocuous "gap-filler" provisions of Article 2 (§§2-307, 2-308, etc.). They also may include terms that are deemed part of the parties' agreement by virtue of the Code's provisions regarding "course of performance," "course of dealing," and "usage of trade" (§§1-205, 2-208). See Coastal & Native Plant Specialties, Inc., v. Engineered Textile Products, Inc., 139 F. Supp.2d 1326, 1337 (N.D. Fla. 2001). But mere receipt of forms without objection may not be held to constitute a course of dealing or course of performance sufficient to establish assent to the terms of those forms, under §2-207, even where forms are repeatedly sent over time:

> . . . [A] course of dealing may become part of an agreement, via a type of estoppel, when one party fails to object to the manner in which the other party performs under the agreement. Terms and conditions contained in a form continually sent by one party do not constitute performance and cannot become binding as a course of dealing. . . . The reason for this distinction between (a) a repeated manner of performance and (b) the repeated sending of forms is pragmatic. A party will certainly be cognizant of the manner in which the other side continually performs under the agreement, and if there is no objection to that performance by the first party, over a sufficient period of time, the first party is assumed to have acquiesced to the second party's manner of performance. The same cannot be said of forms continually sent by one party to the other, which are often not read until a dispute arises.

Premix-Marbletite Mfg. Corp. v. SKW Chemicals, Inc., 135 F. Supp.2d 1348, 1356 (S.D. Fla. 2001), citing and quoting Step-Saver Data Systems, Inc. v. Wyse Tech., 939 F.3d 91 (3d Cir. 1991); In re CFLC, Inc., 166 F.3d 1012 (9th Cir. 1999). In later sections of these materials we will return to a closer examination of the concepts of course of performance, course of dealing, and usage of trade.

Dale R. Horning Co. v. Falconer Glass Industries, Inc.

United States District Court
730 F. Supp. 962 (S.D. Ind. 1990)

McKINNEY, District Judge.

This cause comes before the Court after a two day bench trial on the merits on December 18-19, 1989. The plaintiff's complaint seeks recovery of consequential damages for breach of warranty under the Uniform Commercial Code. After hearing

the evidence and reviewing the law, the Court now makes the following findings of fact and conclusions of law.

I. Findings of Fact:

Plaintiff Architectural Glass & Metal Company ("AGM") is an Indiana corporation engaged in the business of installing and glazing commercial glass products. During the summer of 1986, AGM was a subcontractor on the Finance Federal Credit Union construction project in Indianapolis. AGM was to install a curtain wall and other glass in the building, and time was of the essence for AGM because the building could not be completely enclosed until AGM was finished. Pursuant to its subcontract agreement, AGM would incur daily penalties of $150.00 and possibly be terminated as the glazing subcontractor if it did not meet deadlines. AGM was to be substantially finished with its work by October 3, 1986.

On August 4, 1986, Greg Menefee, then president of AGM, telephoned defendant Falconer Glass, a New York corporation. AGM ordered a quantity of 1/4 inch Spandrel, a ceramic-backed glass product. The Spandrel was to be used at AGM's credit union job site. The parties agreed by phone that the product would be delivered by Falconer within three to four weeks of being ordered. There was no discussion of limiting remedies or disclaiming warranties over the phone. Based on Falconer's experience in the industry and the context of AGM's order, Falconer knew or had reason to know of the buyer's general or particular requirements at the time of contracting.

The next day, AGM sent Falconer a confirming order form. This document contained no language regarding warranties or damages, and noted in handwriting that shipment was to be on an "as needed" basis. At the same time, Falconer sent off its form to subcontractor AGM. The front side of Falconer's form indicated that it confirmed "verbal 8/4/86," that the product was due in "3rd Qtr.1986," and that manufacturing time would be four weeks.

Falconer's standard form contained fine print on the reverse side, with 16 separate paragraphs under the heading "General Terms and Conditions of Sale." Paragraph 7 recited that the product would be free from defects. Paragraph 8, however added that the buyer's "exclusive and sole remedy" for defective goods "shall be to secure replacement. . . ." It also added that the seller shall not be liable for "special, direct, indirect, incidental or consequential damages. . . ." This language was in the same small print as the rest of the terms, and was not underlined, bold-faced, or set forth in capital letters.

Later on in the month of August, AGM provided Falconer with the precise dimensions for the Spandrel panels. On September 23, 1986, defendant Falconer delivered a shipment of defective Spandrel to AGM. Upon timely inspection AGM determined that some of the glass was defective. AGM notified Falconer, and attempted to correct the defects per Falconer's instructions. Gregory Hass, then an officer of AGM, contacted Falconer and informed them that AGM was going to temporarily install the glass to enclose the structure by the deadline date. If the first shipment had been satisfactory, AGM would have completed the project on time and without extra cost. Falconer's first shipment to AGM was timely under the contract as it was made within four weeks of the date the specifications were given to Falconer.

Hass told Carlo Carmen, Falconer's manufacturing manager, that Falconer would be liable for AGM's extra costs, and Carmen did not object. Hass presumed that Carmen had the authority to bind Falconer, and Hass believed that Falconer would pay AGM's extra costs stemming from the defective glass. AGM then

temporarily installed the Spandrel in order to keep the construction project on schedule and to avoid incurring other costs such as heating expenses. Approximately 37 replacement panels were then shipped on September 29, 1986.

Carmen came to Indianapolis at some point to inspect the glass. Hass picked Carmen up at the airport and the drove to the job site. Hass mentioned the extra charges that would be incurred, and indicated to Carmen that AGM would hold Falconer responsible. Carmen did not object or otherwise respond in any fashion.

Later, AGM's manager, Greg Menefee, stated to Carl Defenderfer, Falconer's midwestern sales representative, that AGM expected Falconer to pay for the extra costs incurred by AGM because of the defects in the product. Defenderfer agreed that Falconer should be responsible but said "take it easy on us."

Through late 1986 and early 1987, several corrective shipments were sent by Falconer to AGM, and on several occasions AGM had to remove defective glass and install new product in its place. During this time, AGM paid for the preparation and installation of the defective glass, the preparation of the replacement product, the removal of the defective glass, and the permanent installation of the replacement glass. AGM eventually invoiced Falconer for the charges relating to the Spandrel installation less the expenses and charges that would have been incurred had the original shipment been satisfactory. AGM's invoice was in the sum of $19,415.67.

No agent or employee of AGM was aware of the restrictive terms and conditions on the back of Falconer's forms, although AGM representatives did know that Falconer and other suppliers placed terms and conditions on the back of their forms. AGM was not expressly aware of the limitation on consequential damages contained on the confirmation form sent by Falconer in this transaction.

In the commercial glass industry, it is common practice for suppliers to place restrictive warranty terms on the back of their forms. Despite such standard terms, suppliers will often work with the buyer to help cover some or all of the extra costs incurred when the product is defective. On several occasions, Greg Menefee has been involved in projects where Falconer or other glass suppliers have paid for extras due to defects in their products. Commercial glass subcontractors are routinely subject to additional costs if their own work is unsatisfactory or untimely.

II. Discussion:

As this Court discussed at length in an earlier opinion, a key issue in this case is whether Falconer's limitation of consequential damages contained on its standard form is a term of the parties' contract under the Code. Resolution of this issue is a question of fact that depends upon the evidence in the case as applied to several key provisions of the Code.

The starting point must be §2-715 of the Code, which provides that consequential damages may be recovered by the buyer for "any loss resulting from general or particular requirements and needs of which the seller at the time of contracting had reason to know and which could not reasonably be prevented by cover or otherwise." The drafters of §2-715 commented that there need not be a "conscious acceptance of an insurer's liability on the seller's part, nor is his obligation for consequential damages limited to cases in which he fails to use due effort in good faith." Uniform Commercial Code Comment to §2-715. Thus, "Any seller who does not wish to take the risk of consequential damages has available the [S]ection [2-719] on contractual limitation of remedy." Id.

In this case, then, because there was no specific agreement reached as to consequential damages on August 4, 1986, and because Falconer knew or had reason to know of AGM's general or particular requirements at that time and such extra costs could not be avoided by cover or otherwise, the initial premise must be that, as of August 4, 1986, AGM could recover consequential damages under §2-715 of the Code.

On August 5, 1986, however, Falconer dispatched one of its standard forms to AGM and attempted to exclude consequential damages per its fine print on the reverse of the document. This raises the question of whether these terms become a part of the parties' agreement by operation of law under §2-207.

A. BATTLE OF THE FORMS UNDER §2-207:

As set forth in this Court's previous opinion, the central issue in this case is whether these additional or different terms become part of the parties' contract. Section 2-207(2) provides that where, as here, both parties are merchants, such terms become part of the contract unless they materially alter the prior agreement. The standard for resolving this question is well settled. An additional term is said to materially alter a contract "if its incorporation into the contract without express awareness by the other party would result in surprise or hardship." Maxon Corp. v. Tyler Pipe Industries, Inc., 497 N.E.2d 570, 576 (Ind. App. 1986); accord Greenberg, Rights and Remedies Under U.C.C. Article 2, at 75 (1987); Annot., What Are Additional Terms Materially Altering Contract Within Meaning of UCC §2-207(b), 72 A.L.R.3d 479, 483 (1976).

As this Court ruled at the summary judgment stage, the case law makes it clear that the seller's attempt to limit the implied warranty of merchantability operates to materially alter the prior agreement as a matter of law. See Official Comment 4 to §2-207; Twin Disc, Inc. v. Big Bud Tractor, 772 F.2d 1329, 1334 (7th Cir. 1985). The case law on consequential damages, however, is not in total agreement.

On the one hand, the Wisconsin Supreme Court has held that an attempt to limit consequential damages materially alters a contract because consequential damages are ordinarily available under §2-715. Air Products and Chemicals, Inc. v. Fairbanks Morse, Inc., 58 Wis. 2d 193, 206 N.W.2d 414, 424 (1973). Other courts have reached similar conclusions. See, e.g., Transamerica Oil Corp. v. Lynes, Inc., 723 F.2d 758, 765 (10th Cir. 1983) ("A limitation of remedy generally constitutes a material alteration"); Westinghouse Electric Corp. v. Nielsons, Inc., 647 F. Supp. 896, 900 (D. Colo. 1986) (limitation of seller's liability for incidental and consequential damages is a material alteration); Album Graphics, Inc. v. Beatrice Foods Co., 87 Ill. App. 3d 338, 42 Ill. Dec. 332, 339, 408 N.E.2d 1041, 1048 (1980) ("A term disclaiming warranties, and we might add a term limiting remedies, is undoubtedly a term that materially alters a contract.").

On the other hand, in Kathenes v. Quick Chek Food Stores, 596 F. Supp. 713 (D.N.J. 1984), the court ruled that a clause limiting consequential damages would not materially alter a contract and was thus binding on both parties. The *Kathenes* court relied heavily on the fact that Official Comment 5 to §2-207 states that a clause limiting a remedy in a reasonable manner is not a material alteration. 596 F. Supp. at 716. The court wrote, "The comment cross-references Section 2-719 on the modification and limitation of remedies." Id. "Thus, [a seller's] terms limiting [a buyer's] remedies would be a part of the contract as long as it is reasonable under Section 2-719." Id.

While this Court recognizes that Official Comment 5 does, in fact, make reference to §2-719, the Court does not find that it necessarily follows that any limitation of consequential damages does not "materially alter" the parties' contract (§2-207 language) just because the limitation would be "reasonable." (§2-719). The statutory language of §2-207 speaking to material alteration focuses on two elements: surprise or hardship. The fact that a clause may be reasonable under the remedy provision of §2-719 does not dictate the outcome of the contract formation analysis under §2-207. The ultimate question remains whether such a limitation would surprise or work a hardship on the buyer; the issue of reasonableness is properly viewed as just one aspect of this material alteration analysis.

The Seventh Circuit Court of Appeals recently confirmed that the material alteration analysis involves the two separate components of surprise or hardship. In Trans-Aire International, Inc. v. Northern Adhesive Co., Inc., 882 F.2d 1254 (7th Cir. 1989), the Seventh Circuit held that an indemnification clause included in the fine print of a standard form constitutes a material alteration, notwithstanding the fact that some course of dealing existed between the parties. In so holding, the court emphasized that Comment 4 to Section 2-207 defines a material alteration as one which would "'result in surprise *or hardship* if incorporated without the express awareness' of the nonassenting party." Trans-Aire Intl., 882 F.2d at 1261 (emphasis added by Seventh Circuit). The Seventh Circuit went on to explain that the surprise and hardship inquiries are separate and distinct analyses. In this case, then, this Court must evaluate both elements independently.

Here, the surprise element simply asks whether the new term would catch the buyer unaware. Course of dealing and usage of trade analysis is properly invoked at this stage, for if the buyer is generally aware that such limitations are imposed in the industry, the buyer cannot be heard to complain of surprise in any individual transaction. The evidence in this case is conflicting on this issue.

For instance, the seller's witnesses, all of whom have extensive experience in the commercial glass industry, testified that suppliers include such restrictive terms and conditions in their standard forms. The buyer's witnesses, on the other hand, stated that while they know standard forms have fine print on the reverse side, they do not know what those conditions are and do not read such forms. Suppliers such as Falconer, they added, often cover extras incurred due to defective products. Moreover, according to AGM's witnesses, the subcontractors are in constant fear of incurring additional costs for delays or defects in their own work.

Thus, the commercial glass industry appears to present a dichotomy in the course of dealing analysis. Suppliers work under the general understanding that replacement is the only remedy for them as against their own suppliers, and that in most cases replacement is their only liability when their own product is defective. Suppliers do, however, seem to make exceptions where it is in their best interest. Subcontractors, on the other hand, live in a world where every subcontractor is responsible to the next for its own delays and mishaps.

With this evidence, the question is whether AGM has proven that the disclaimer of consequential damages was a surprise.[2] On balance, this is a close factual question.

2. The burden of showing surprise appears to be on the nonassenting buyer here, for §2-207 states that between merchants, such terms become a part of the contract unless they materially alter it. In this case, then, if the buyer presented no evidence on surprise, the Code would add the presumption that the term is a part of the agreement. The buyer thus bears the burden of proof on this matter, for as the Seventh Circuit has noted in an unrelated context, "[T]he party who would lose if no evidence were

On the one hand, there is no evidence that AGM subjectively knew of the limitations. There appears, however, to also be an objective element to this inquiry asking whether the buyer should have known that such conditions are included in standard forms. This objective aspect to the surprise inquiry is apparent from the context of §2-207, which in essence supplies a presumption that the additional terms contained in confirmation forms are not read by the opposing party.

Applying this mixed subjective-objective standard, the Court finds that even though the subcontractor expects accountability as among other sub-contractors, it should anticipate and even expect suppliers to attempt to exclude consequential damages. Falconer and most other commercial glass manufacturers routinely attempt to limit their liability for such damages, and even though their methods are less than perfect, it appears that no commercial glass subcontractor can be heard to claim surprise given the course of dealing and usage of trade in the industry. Thus, AGM has not shown that the restrictive terms of Falconer's confirmation form materially alter their agreement under the surprise aspect of §2-207.

As the Seventh Circuit made clear in *Trans-Aire International,* however, this does not end the inquiry, for the question of hardship remains. Hardship, of course, is defined as something "hard, oppressive, toilsome, [or] distressing." Webster Encyclopedic Dictionary. In the sale of goods setting, this analysis necessarily focuses on whether a limitation of consequential damages would impose "substantial economic hardship" on the nonassenting party. *Trans-Aire International,* 882 F.2d at 1262. In this situation, where Falconer knew or had reason to know that AGM could incur substantial liability for delays in finishing its subcontract, there can be no doubt that a limitation of consequential damages would work a hardship on the buyer.

It must be remembered that where, as here, the seller knew or had reason to know of the buyer's general or particular requirements, Section 2-719 of the Code supplies the presumption that consequential damages are recoverable. Thus, the starting premise again is that because the parties did not specifically agree to exclude consequentials, AGM could recover them. AGM thus had the Code's implied protection of substantial economic rights.

Falconer's attempt to limit AGM's right to these damages must fail because it would work a hardship on AGM. As the Seventh Circuit explained in *Trans-Aire International,* "Clearly, a shift in legal liability which has the effect of relieving one party of the potential for significant economic hardship and placing this burden upon another party is an important term in any contract." Id. at 1263. "Thus, it is not surprising that such a term, if it is to be included in a contract, is ordinarily the subject of active negotiation between the parties." Id. "We therefore do not believe that a party charged with legal duties and obligations may reasonably rely upon a boilerplate clause in a boilerplate form and a corresponding operation of law to shift substantial economic burdens from itself to a nonassenting party when it had every opportunity to negotiate such a term if it desired." Id.

This reasoning is equally applicable here, and is supported by additional case law cited previously for the proposition that a limitation of consequential damages is a material alteration under the Code. See, e.g., Transamerica Oil Corp. v. Lynes, Inc., 723 F.2d 758, 765 (10th Cir. 1983) ("A limitation of remedy generally constitutes a material alteration"); Westinghouse Electric Corp. v. Nielsons, Inc., 647 F. Supp.

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presented has the burden [of proof]." Auburndale State Bank v. Dairy Farm Leasing Corp., 890 F.2d 888, 893 (7th Cir. 1989).

896, 900 (D. Colo. 1986) (limitation of seller's liability for incidental and consequential damages is a material alteration); Album Graphics, Inc. v. Beatrice Foods Co., 87 Ill. App. 3d 338, 42 Ill. Dec. 332, 339, 408 N.E.2d 1041, 1048 (1980) ("A term disclaiming warranties, and we might add a term limiting remedies, is undoubtedly a term that materially alters a contract.").

AGM faced thousands of dollars in potential liability for consequential damages if its supplier's product was defective and caused delays. Falconer knew or had reason to know of this because of its experience in the industry and the context of the sale. When the oral agreement was consummated on August 4, 1986, AGM had the legal right under the Code to obtain consequential damages from the supplier. Falconer attempted to shift this substantial economic burden back to AGM not through negotiation, but instead by inserting fine print boilerplate on the reverse side of a confirming standard form.

Under the Code, such a shift in liability would impose hardship on AGM. Accordingly, the purported limitation of consequential damages would materially alter the parties original agreement, and is thus not a part of their contract under Section 2-207. AGM has thus proven that it is entitled to recover consequential damages caused by Falconer's defective product.

As the Code makes clear, it is no consolidation [sic; "consolation"?] to Falconer in this sale of goods setting that it acted in good faith and made every effort to replace the glass as quickly as possible. Falconer agreed to supply a quality product in a short period of time in an industry in which defective products can cause construction delays and corresponding extra costs. Falconer did not meet its contractual obligations, and under the Code it is liable for all consequential damages proximately resulting from its breach.

B. DAMAGES:

The buyer has the burden of proof to show the amount of consequential damages sustained. Official Comment 4 to §2-715; Bob Anderson Pontiac, Inc. v. Davidson, 155 Ind. App. 395, 293 N.E.2d 232, 237 (1973). However, the Code does not require mathematical precision, and the loss may be shown in any manner reasonable under the circumstances. Official Comment 4 to §2-715; *Bob Anderson Pontiac,* 293 N.E.2d at 237. The trier of fact must be able to estimate the damages with a reasonable degree of certainty and exactness. Uebelhack Equipment, Inc. v. Garrett Bros., Inc., 408 N.E.2d 136, 140 (Ind. App. 1980).

In this case, the proof of damages presented by the parties is conflicting. AGM's calculations result in a figure of $19,145.67, while Falconer's produce a value of $6,730.00. Both parties' evidence has probative value on the measure of damages, and the Court is not constrained to accept one side's figures over the other's. Instead, in this case, the Court finds it appropriate to make its own estimation of damages using the evidence presented by both parties on each aspect of damages. For the reasons set forth in the accompanying footnote, the Court awards total damages of $12,303.17 to the plaintiff.

C. PREJUDGMENT INTEREST:

Finally, plaintiff seeks to recover prejudgment interest, arguing that such an award is appropriate under Ind. Code §24-4.6-1-103. . . . In this case where

plaintiff's request is grounded in equity rather than a mandatory statute, the Court in its discretion determines that the goals of full and just compensation have been met and that an award of prejudgment interest is not appropriate as an equitable remedy.

D. CONCLUSION:

In sum, the parties' failure to fully discuss the terms of their contract at the time of agreement has resulted in numerous hours of legal work, several lengthy opinions from this Court, a two-day trial on the merits, and a judgment for $12,303.17. The lesson to be learned from this case is that merely inserting boilerplate provisions into standard forms is not the end-all way to deal with the U.C.C. Such post-agreement action, it is seen once again today, is not always enough to force one party's desires upon the other.

Despite the Code's rejection of the mirror-image rule, it is apparent that the best, and, in some instances, the only way to get a preferable term into a contract is *to actually propose the term and reach a meeting of the minds* on the issue. The Code did not completely abolish the concept of mutual assent. In this setting, for instance, if suppliers such as Falconer want to exclude consequential damages from all their contracts, they can simply adopt and enforce a policy that all sales representatives must inform the prospective buyer at the time of bidding that such damages will not be recoverable. On the other hand, if buyers such as AGM want to ensure that they can recover such extras without complex litigation, they can demand such provisions in all agreements. In both instances, counsel planning such action for the client would need to have an eye towards, among other things, the admissibility requirements for regularly recorded business records.

This case also shows once again that a call to an attorney for preventive advice is often more cost-effective than the call made months or years later after the situation has become impenetrable and stubbornness has taken root. It also demonstrates that attorneys called upon to render such planning advice should probably do more than just draft fine print boilerplate. Today's decision shows that the U.C.C. requires more in this particular setting anyway.

As the Indiana Court of Appeals noted in the related area of indemnification more than a decade ago, "Lawyers who specialize in this field are well aware that clauses such as those under consideration in this case demand laborious judicial parsing, in an effort to distill the intent of the parties." Indiana State Highway Commission v. Thomas, 169 Ind. App. 13, 346 N.E.2d 252, 263 (1976) quoting Jordan v. City of New York, 3 A.D.2d 507, 162 N.Y.S.2d 145, 152 (1957). The *Thomas* court added, "Surely, at this stage, it is not too much to require them to stop waging verbal warfare and to state unmistakably whether or not a contract purports to burden the indemnitor with another's negligence." Id.

So, too, in this context, it is not too much to require something more than "form warfare." The Code requires more than burying a party's preferred terms in boilerplate. Contrary to popular belief, §2-207 does not always condone nor justify the battle of the forms. In fact, as this case shows, the Code often requires the parties to actually agree to their preferred contractual terms.

Judgment for the plaintiff shall be entered accordingly. Pursuant to Rule 54(d), costs shall be allowed to the plaintiff as a prevailing party.

It is so ordered.

Notes and Questions

1. *The use of confirmations.* In *Brown Machine,* the court was concerned with the application of UCC §2-207 to offers, acceptances, and conditional acceptances. In *Dale Horning*, we see the other principal occasion for application of §2-207: the case where an oral agreement is followed up by one or more written "confirmations." Because post-agreement confirmations pose questions of policy similar to those raised by the "battle of forms," the drafters of the Code chose to combine treatment of the two situations in one section. Their choice was not entirely a felicitous one, however; one result was the apparent suggestion in §2-207(1) that a "confirmation"—which by definition comes after an agreement has been reached — could somehow operate as a conditional acceptance (in effect, a counteroffer), with the possible result that its rejection (or non-acceptance) by the offeror could result in no contract. The better view here appears to be that a confirmation cannot in fact be a counteroffer because a contract has already been formed. See Air Products & Chemicals, Inc. v. Fairbanks Morse, Inc., 206 N.W.2d 414, 422-423 (Wis. 1973); White & Summers, Uniform Commercial Code §1-3, at 43 (5th ed. 2000). Where a confirmation is sent (or the parties have traded confirmations), the real issue is simply: What happens to the additional terms under §2-207(2)?

2. *Materiality of terms.* The UCC, like the Uniform Sales Act before it, provides that "implied warranties" of various types may arise from a sale of goods. These include: a warranty that the seller has and can rightfully convey good "title" to (ownership of) the goods in question (UCC §2-312); a warranty that the goods will be "merchantable," in cases where the seller is a "merchant" dealing in such goods (§2-314); and a warranty that the goods will be fit for the purpose for which they are being purchased, if the seller knows that the buyer is relying on the seller's skill and judgment in selecting the goods (§2-315). In addition, the Code provides that the buyer may enforce any "express warranties" made by the seller, whether by words or by conduct (§2-313).

A seller wishing to avoid liability for some or all of these warranties may do so if it makes a valid "disclaimer" pursuant to §2-316; instead of (or in addition to) such a disclaimer, the seller may by agreement limit its liability for damages of various types that would otherwise be appropriate in the event of a breach of warranty or other breach of the sales agreement (§2-719). Because of their potential magnitude, the seller is particularly likely to want to avoid liability for "consequential damages" (§2-715), like the ones claimed by the buyer in the *Dale Horning* case. (We will more closely examine the notion of consequential damages in Chapter 11.)

In its earlier opinion, the court in *Dale Horning* had already decided that the seller's attempt to disclaim warranties was unavailing under §2-207(2), because such a provision was "material" as a matter of law. The materiality of the seller's attempted limitation of liability, on the other hand, the court viewed as a question of fact, not to be determined without a trial on the merits. Both approaches have been and continue to be used by courts in applying §2-207. Sometimes, as in the *Dale Horning* court's treatment of the warranty disclaimer, a court will take the position that a particular clause is so clearly important and adverse to the other party that it should be regarded as material per se, not to be included in the agreement unless shown to be consciously and expressly assented to. (Warranty disclaimers are particularly likely to receive such treatment, because of their inclusion in the list in Comment 4 of clauses likely to be material.) Or, a court may decide that the term in question must

be material just because it means a lot of money to one party or the other, enough to justify litigation. Sometimes, however, the court will view the issue as one of fact, which could go either way (although still, typically, an issue to be decided by the court, rather than by a jury). In that event, the court must find some standard by which materiality is to be judged. Increasingly, it would appear, the courts are doing as the *Dale Horning* court did, seizing on the references in Comment 4 to "surprise or hardship" as the markers for materiality. Is the *Dale Horning* court's analysis on this score a convincing one? Or should it have concluded that "hardship" alone is not sufficient unless accompanied by "surprise?" Compare the language in Comment 1 to §2-302, the "unconscionability" section: "the principle [of §2-302] is one of the prevention of oppression and unfair surprise."

3. *Other types of added terms.* We noted after the *Brown Machine* case that other courts have viewed indemnification clauses as being material, for the purpose of applying §2-207(2). Warranty disclaimers and limitations of liability have of course been litigated over and over, usually (but not always, especially as to the latter) being held material. In the first *Dale Horning* opinion, 710 F. Supp. 693, the court also held material, and therefore ineffective, the seller's choice of law and forum selection clause, which would not only have subjected their contract to New York law (itself probably a relatively minor matter, assuming identical or similar UCC provisions in both states) but would also have required the Indiana buyer to bring suit in New York state. Other courts have held choice of forum clauses to be material under §2-207(2). E.g., General Instrument Corp. v. Tie Manufacturing, Inc., 517 F. Supp. 1231 (S.D.N.Y. 1981); TRWL Financial Establishment v. Select International, Inc., 527 N.W.2d 573 (Minn. Ct. App. 1995).

Clauses requiring arbitration of disputes are also commonly included in standard forms; some courts regard such a provision as material per se, others as potentially includable under §2-207(2). E.g., Marlene Industries Corp. v. Carnac Textiles, Inc., 380 N.E.2d 239 (N.Y. 1978) (arbitration clause requires express assent under New York law, material as a matter of law); contra Schulze & Burch Biscuit Co. v. Tree Top, Inc., 831 F.2d 709 (7th Cir. 1987) (arbitration clause not material because prior course of dealing gave notice that arbitration clause would likely be included in confirmation). The ruling of the New York Court of Appeals in the *Marlene Industries* case that an arbitration clause is per se material has been held by the Second Circuit Court of Appeals to have been preempted by the Federal Arbitration Act. Aceros Prefabricados, S.A. v. Tradearbed, Inc., 282 F.3d 92, 99-102 (2d Cir. 2002) (federal statute proscribes state law burdens on arbitration; arbitration clause not shown to result in any hardship or oppression where arbitration is custom and practice within relevant industry). Compare PCS Nitrogen Fertilizer, L.P. v. Christy Refractories, L.L.C., 225 F.3d 974 (8th Cir. 2000) (where writings of parties did not establish contract, arbitration clause in seller's form did not become part of contract under §2-207(3); even if "supplementary terms" may include terms found under "course of dealing," buyer's repeated receipt of seller's forms with arbitration clause does not constitute sufficient course of dealing for this purpose).

Other provisions sometimes found in standard forms (especially of a seller) are those calling for payment of interest on amounts owing and overdue, and provisions that the losing party shall be liable for the other's attorney fees in the event of a litigated dispute. Clauses like these appear to have received a mixed reception; interest provisions are commonly regarded as nonmaterial by virtue of the reference to them in Comment 5, while attorney fee clauses are more likely to be regarded with

disfavor. E.g., Herzog Oil Field Service, Inc. v. Otto Torpedo Co., 570 A.2d 549 (Pa. Super. Ct. 1990) (18 percent interest charge not material, but attorney fee of 25 percent of amount recovered is; even a "reasonable attorney fee" clause might be held material, and this one imposes a much higher cost than the more usual 10 to 15 percent).

4. *The issue of "different" terms.* Although not raised in *Dale Horning,* there is another issue that can arise in cases where the parties have traded confirmations: What happens if the two forms contain directly opposed terms? Comment 6 gives a sensible answer: Each party's term is presumed to be objected to by the other, and the conflicting terms do not become part of the agreement but simply cancel each other out. Their subject matter will therefore not be part of the parties' agreement, except that any appropriate "gap-filling" term in Article 2 will then be applicable. Where the conflicting forms are not confirmations, however, but offer and (nonconditional) acceptance, a different sort of problem is created. We have earlier seen that the Code was clearly attempting in §2-207 to redress the balance between offeror and offeree (who are often, but not always, buyer and seller, respectively) by replacing the "last shot" rule with a rule requiring explicit consent to material additional terms in the offeree's responding form. Does §2-207 replace the "last shot" rule with a "first shot" one, giving precedence to the terms of the offer, no matter how buried in boilerplate they may be? In Daitom, Inc. v. Pennwalt Corp., 741 F.2d 1569 (10th Cir. 1984), the court had to decide whether express warranties in a buyer's *acceptance* form could become part of the contract even though the seller's *offer* had contained express disclaimers of warranty and limitations of remedy. After concluding that the buyer's terms did indeed "differ" from those in the seller's offer, the court went on to discuss the application of §2-207 to such "different" terms.

> The difficulty in determining the effect of different terms in the acceptance is the imprecision of drafting evident in §2-207. . . .
>
> Section 2-207(2) is silent on the treatment of terms stated in the acceptance that are *different,* rather than merely additional, from those stated in the offer. It is unclear whether "different" terms in the acceptance are intended to be included under the aegis of "additional" terms in §2-207(2) and, therefore, fail to become part of the agreement if they materially alter the contract. Comment 3 suggests just such an inclusion. However, Comment 6 suggests that different terms in exchanged writings must be assumed to constitute mutual objections by each party to the other's conflicting terms and result in a mutual "knockout" of both parties' conflicting terms; the missing terms to be supplied by the U.C.C.'s "gap-filler" provisions. At least one commentator, in support of this view, has suggested that the drafting history of the provision indicates that the word "different" was intentionally deleted from the final draft of §2-207(2) to preclude its treatment under that subsection. The plain language, comments, and drafting history of the provision, therefore, provide little helpful guidance in resolving the disagreement over the treatment of different terms pursuant to §2-207.
>
> Despite all this, the cases and commentators have suggested three possible approaches. The first of these is to treat "different" terms as included under the aegis of "additional" terms in §2-207(2). Consequently, different terms in the acceptance would never become part of the contract, because, by definition, they would materially alter the contract (i.e., the offeror's terms). Several courts have adopted this approach. . . .
>
> The second approach, which leads to the same result as the first, is that the offeror's terms control because the offeree's different terms merely fall out; §2-207(2) cannot rescue the different terms since that subsection applies only to *additional* terms. Under this approach, Comment 6 (apparently supporting a mutual rather than a single

term knockout) is not applicable because it refers only to conflicting terms in confirmation forms following *oral* agreement, not conflicting terms in the *writings* that form the agreement. This approach is supported by Professor Summers. J. J. White and R. S. Summers, Uniform Commercial Code, §1-2, at 29 (2d ed. 1980).

The third, and preferable approach, which is commonly called the "knock-out" rule, is that the conflicting terms cancel one another. Under this view the offeree's form is treated only as an acceptance of the terms in the offeror's form which did not conflict. The ultimate contract, then, includes those non-conflicting terms and any other terms supplied by the U.C.C., including terms incorporated by course of performance (§2-208), course of dealing (§1-205), usage of trade (§1-205), and other "gap fillers" or "off-the-rack" terms (e.g., implied warranty of fitness for particular purpose, §2-315). As stated previously, this approach finds some support in Comment 6. Professor White supports this approach as the most fair and consistent with the purposes of §2-207. White and Summers, supra, at 29. Further, several courts have adopted or recognized the approach.

Id. at 1578-1579. The court in *Daitom* went on to apply the "knock-out" approach, holding that the seller's express disclaimers and the buyer's express warranties canceled each other out, with the result that the Code's provisions on implied warranties and remedies governed the case. While the "knock-out" rule may not be the most reasonable construction of §2-207, it may appear the preferable approach where (as in *Daitom*) the seller's form was the *offer,* rather than — as is probably more often the case — the acceptance. Otherwise, as the court in *Daitom* points out, §2-207 will have succeeded in replacing the "last-shot" rule with a "first-shot" one, posing policy problems of its own. Id. at 1580. See Reilly Foam Corp. v. Rubbermaid Corp., 206 F. Supp. 643 (E.D. Pa. 2002) (no controlling state authority, but in light of superior policy reasons favoring knockout rule and "vast majority" of jurisdictions adopting it, court predicts that Pennsylvania Supreme Court would adopt it, and applies it to this case); Superior Boiler Works, Inc. v. R.J. Sanders, Inc., 711 A.2d 628, 635 (R.I. 1998) ("prudence and weight of authority" favor knock-out rule adopted by *Daitom*); but see Caroline N. Brown, Restoring Peace in the Battle of the Forms: A Framework for Making Uniform Commercial Code Section 2-207 Work, 69 N.C.L. Rev. 893 (1991) (§2-207 does indeed give primacy to the offer, and should be so construed; "knock-out" approach should not be employed in different-terms cases).

5. *Lawyering issues.* As many commentators have pointed out, the structure of §2-207 makes it likely that the "well-counseled" buyer will include in its "order" (offer) form a provision objecting in advance to any and all different and additional terms in the seller's response, while an equally well-counseled seller will respond with an "acknowledgment" (acceptance) form that is expressly conditional on the buyer's assent to all its terms, no matter how "different" or "additional" those may be. See generally E. Hunter Taylor, Jr., U.C.C. Section 2-207: An Integration of Legal Abstractions and Transactional Reality, 46 Cin. L. Rev. 419, 438 (1977). What will be the result of such a strategy? If the parties stop bargaining at this point, preferring to proceed to performance without stopping to iron out the differences between their forms, should either "shot" have priority? And does it make any sense in such a case to talk about the "intent" of the parties, or to look for their "bargain," as to the conflicting terms? At this point, it might be useful to recall the lecture delivered by District Judge McKinney at the end of the *Dale Horning* opinion: "Attorneys," he suggested, "should probably do more than just draft fine print boilerplate," waging "form warfare." In this area, the judge concluded, "the Code often requires the

parties to actually agree to their preferred contractual terms." What is the judge suggesting the attorneys should have done? What do you think would have happened if they had?

6. *Scholarly commentary.* If anything is clear at this point about §2-207, it is that this section has been a strong candidate for revision. Indeed, commentators have been clamoring for modification of the section for years. See Symposium, Ending "The Battle of the Forms": A Symposium on the Revision of Section 2-207 of the Uniform Commercial Code, 49 Bus. Law. 1019 (1994). In an article that is part of this symposium issue, Thomas J. McCarthy, the Chair of the American Bar Association's Task Force on the revision of Article 2, contends that developments in electronic communications are making the issue of the battle of the forms largely irrelevant to business. Mr. McCarthy argues that transactions increasingly occur electronically without the inclusion of boilerplate found in paper transactions. Thomas J. McCarthy, An Introduction: The Commercial Irrelevancy of the "Battle of the Forms," 49 Bus. Law. 1019 (1994). See also Marianne M. Jennings, The True Meaning of Relational Contracts: We Don't Care About the Mailbox Rule, Mirror Images, or Consideration Anymore — Are We Safe?, 73 Den. U. L. Rev. 3 (1995) (importance of supply relationships makes rules of contract law largely irrelevant).

7. *Revision of section 2-207.* The partial revision of Article 2 that is now (as of this writing) awaiting final approval from the American Law Institute would make significant changes in present §2-207. What is now §2-207(1) would be moved up into new §2-206(3), which would read: "A definite and seasonable expression of acceptance in a record operates as an acceptance even if it contains terms additional to or different from the offer." That of course is only half of the substance of present §2-207(1); the second part would be reflected in a new Comment 2 to §2-206: "The mirror image rule is rejected in subsection (3), but any responsive record must still be fairly regarded as an 'acceptance' and not as a proposal for a different transaction such that it should be construed to be a rejection of the offer." This Comment is apparently intended as a replacement for the reference in present §2-207(1) to the possibility of an "expressly conditional acceptance." Whether this new combination of section and comment represents an improvement in clarity over present §2-207(1) is obviously debatable.

New §2-207 would read as follows:

> If (i) conduct by both parties recognizes the existence of a contract although their records do not otherwise establish a contract, (ii) a contract is formed by an offer and acceptance, or (iii) a contract formed in any matter is confirmed by a record that contains terms additional to or different from those in the contract being confirmed, the terms of the contract, subject to Section 2-202 [the Code's parol evidence rule], are:
>
> (a) terms that appear in the records of both parties;
>
> (b) terms, whether in a record or not, to which both parties agree; and
>
> (c) terms supplied or incorporated under any provision of this Act.

The proposed new section 2-207 would thus be a restated and somewhat expanded version of the present §2-207(3). A lengthy set of Comments would provide some illustrations and guidance for courts in sorting through various types of communications. Present §2-207(2), with its three-pronged formula for dealing with additional terms as between merchant parties, would simply vanish into oblivion (taking with it, presumably, several decade's worth of student- or faculty-generated flow charts).

The intent of new §2-207 is to avoid favoring either the first or the last shot, as stated in new Comment 2:

> When forms are exchanged before or after performance, the result from the application of this section differs from the original Section 2-207 and the common law in that this section gives no preference to the first or the last form; it applies the same test to the terms in each.

The difference in approach between the old and new versions of §2-207 (plus the new §2-206(3)) can also be glimpsed in the following statement at the end of Comment 3 to the proposed new version:

> There is a limitless variety of verbal and nonverbal behavior that may be claimed to be an agreement to another's record. Th[is] section leaves the interpretation of that behavior to the wise discretion of the courts.

How do you think the *Brown Machine* and *Dale Horning* cases would have been decided under the rules of new sections 2-206 and 2-207?

PROBLEM 3-4

How would the following dispute be resolved under UCC §2-207?

Mendoza Construction Company is a general contractor that handles major commercial construction projections. Mendoza is the general contractor for the construction of several buildings on the "campus" of Wintel, Inc., a major communications company that is consolidating its operations outside of Columbus.

G&P Industries is a supplier of various industrial products, including roofing materials and compounds.

On September 15, Margaret Noon, the Mendoza supervisor for the Wintel project, called Frank Park at G&P to determine the price, availability, and delivery schedule for various roofing materials and compounds for the Wintel project. Park provided Noon with the information she requested and told her that if she wished to place an order she should do so as soon as possible because demand for the company's products was very brisk. On the morning of October 1 Noon sent a fax to Park. The fax stated that Mendoza wished to place an order for various roofing products and compounds. The price and delivery schedule stated in Noon's fax were as quoted by Park in the conversation on September 15. Delivery of all materials was to be made by November 15.

On the afternoon of October 1, Park sent a fax back to Noon confirming receipt of Noon's order. In addition to confirming the basic terms of Noon's order, the fax also stated:

Acceptance of Your Order Is Subject to the Following Terms and Conditions

1. 10% payment due in 10 days. Payment in full of balance due 7 days after completion of delivery.
2. Any unpaid amounts accrue interest at the rate of 1% per month.
3. Purchaser agrees to pay reasonable attorneys fees and costs of collection should that be necessary.