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MITIGATION OF DAMAGES FOR ANTICIPATORY BREACH OF EXECUTORY CONTRACTS

FEW questions in the field of contract law are as unsettled as those involving the measure of damages for breach of an agreement. The basic theory underlying the remedy is to give the innocent party an amount in money that will, as nearly as possible, be the equivalent of the value he would have received had the contract been fully performed. This principle in itself precludes any rigid tests. Each fact situation will vary the value of performance and the loss by breach; proof may be limited and difficult. The problem has received even less agreement in its treatment by the courts where the injury is the result of an anticipatory breach of an executory contract,¹ and in these instances lack of unanimity is largely prompted by opposing views on mitigation of the resulting damages.

This situation has received the attention of the Federal Court of Appeals for the Eighth Circuit in *Reliance Cooperage Corporation v Treat*.² The opinion delivered by Judge Sanborn appears to present a clear, direct statement of the law controlling the situation. However, the total lack of any discussion of opposing doctrine would seem to point up uncertainty.

This Comment is limited to a presentation of the *Treat* case as it affects the divergent opinions that exist relative to the question of whether or not there exists a duty to mitigate damages for anticipatory breach of contract.

In St. Louis, Missouri, on July 12, 1950, A. R. Treat entered into a contract to sell to the Reliance Cooperative Corporation 300,000 white oak bourbon staves at a fixed price, total delivery

¹ The repudiation of a contract by one of the parties before time of performance has arrived amounts to a tender of a breach of the entire contract and, when accepted, is anticipatory breach of the contract as a whole. *Pollack v. Pollack*, 46 S. W. 2d 292 (Tex. Comm. App. 1932).

² 195 F. 2d 977 (1952).

to be completed by December 31, 1950. Treat failed to produce and deliver any staves. In August defendant Treat advised plaintiff Corporation that due to a rise in price he could not produce or deliver any staves unless a new purchase price was set. Plaintiff answered to the effect that it expected complete performance under the contract as originally agreed. After time for performance had expired, the Corporation brought an action to recover damages for the breach. The trial court instructed the jury that plaintiff Corporation had a duty to mitigate the damages and that the measure of entitlement would be the difference between the market value at the time of repudiation and the contract price. The court of appeals reversed and remanded for a new trial limited to ascertaining the amount of damages in keeping with its directions. The court held that there was no duty to mitigate damages and that the amount due the plaintiff would be the difference between market value at the time when performance was due under the contract and the original contract price.

Quoting from *Claes and Lehenbeuter Mfg. Co. v. McCord*,³ the court set out the general rule applied to repudiation of a sales contract prior to performance date:

... The law is that, where the promisor before the time of performance expressly renounces his contract, the promisee is thereby entitled either to treat the contract as broken and sue at once for its breach without averring an offer of readiness to perform, or he may wait until the time of performance has expired, and then sue for the consequences of nonperformance.

On the general subject of anticipatory breach by repudiation, this statement seems accurately to express the basic theory as stated in most jurisdictions.⁴ The doctrine affects the time when suit may be brought and is considered to have no other impact or changing effect on the legal consequences of nonperformance. The

³ 65 Mo. App. 507, 509 (1896).

⁴ *Roehm v. Horst*, 178 U. S. 1 (1900); see Limburg, *Anticipatory Repudiation of Contracts*, 10 Cornell L. Q. 135 (1924). "The doctrine of allowing recovery for an anticipatory breach of contracts is recognized in Texas." *Engelhart v. Volunteer State Life Ins. Co.*, 195 S. W. 2d 798, 802 (Tex. Civ. App. 1946) *er. ref.*

purpose is to afford the injured party an election to accept or reject repudiation without forcing added burdens upon him. It is clear that a party may sue at the time of breach or choose to insist upon performance. If the later election is made, the contract is said to remain binding, and no right to damages arises until the date of performance expires.⁵ The court, in emphasizing that anticipatory breach has no special effect other than on the time of suit, noted the comment in the *Restatement of the Law of Contracts* that "repudiation does not accelerate the time fixed for performance; nor does it change the damages to be awarded . . ."⁶ It would seem that this is too simple an approach.

In the ordinary breach of a contract of sale the difference between the contract price and market price at the time and place of performance is the accepted measure of damages.⁷ There may appear to be no logical reason for departing from this rule. However, where a contract is repudiated before performance date, there may be a long period of time between date of breach and when performance is due. This circumstance makes likely changes in value of the subject of the contract and certainly affects the opportunity to avoid or materially to reduce the damages resulting from the breach. Arbitrary use of market price at performance date as a measure of damages overlooks two main problems: (1) at what time does the market price of the commodity concerned have a bearing on the damages for nonperformance and what evidence is relevant in determining this? (2) is there a duty to mitigate the damages resulting from repudiation?

Where the courts have held that the market price at the time of repudiation applies, the reasoning has not always been clear.

⁵ *Roehm v. Horst*, *supra* note 4; see authorities collected in 12 AM. JUR., *Contracts*, §§ 392, 397; 17 C. J. S., *Contracts*, § 472.

⁶ 1 RESTATEMENT, *CONTRACTS* (1932) § 338; see 5 WILLISTON, *CONTRACTS* (Rev. ed. 1937) § 1397; 46 AM. JUR., *Sales*, § 688.

⁷ 5 WILLISTON, *CONTRACTS* (Rev. ed. 1937) § 1397; 2 SEDGWICK, *DAMAGES* (9th ed. 1912) § 636 (d); Notes, 44 A. L. R. 215, 218 (1926), 108 A. L. R. 1482, 1485 (1937), and cases cited therein. The question presented by the principal case does not arise in jurisdictions not recognizing the doctrine of anticipatory breach. Price at performance date controls.

In some instances it has been based upon a duty to mitigate the damages;⁸ in others there appeared to be no difference between market price at time of repudiation and on the date of performance.⁹ An indefinite date for performance or no date set out in the agreement has been urged as necessitating use of market price at breach as determinative.¹⁰ Where the trial precedes the performance date, the market price at the time of breach may be the only evidence available for ascertaining the amount of damages.¹¹ The opinions indicate that using a date other than this produces too speculative a problem for the jury. This attitude appears unsound when one considers jury findings concerning damages in other types of actions, such as for mental anguish. At least one writer suggests that using the market price on the date of breach is treating the breach as a failure to give performance at that time and has the effect of calling for an obligation other than that which the parties originally undertook.¹²

The court was on firm ground in asserting that normally no duty to mitigate damages can arise until there are damages to mitigate. However, this premise does not necessarily lead to the court's conclusions. In stating that in the instant case damages accrued on the date performance was due under the contract, the opinion points out that, despite his repudiation, defendant Treat was obligated to produce and deliver staves; if he had done so, the plaintiff would have had to accept and pay for them. "There is no justification for ruling that, after the plaintiff was advised that the defendant did not intend to perform, it must hold itself in readiness to accept performance from him and at the same time, at its own

⁸ Cox & Sons Co. v. Crane Iron Works, 5 F. 2d 314 (3d Cir. 1925), *later proceedings*, 28 F. 2d 328 (3d Cir. 1928); Goldsmith v. Stiglitz, 228 Mich. 255, 200 N. W. 252 (1924).

⁹ Lompoc Produce and Real Estate Co. v. Brown, 41 Cal. App. 607, 182 Pac. 166 (1919); Sharpville Furnace Co. v. Snyder, 223 Pa. 372, 72 Atl. 786 (1909).

¹⁰ O'Dell v. Nelson & Myers, 182 Okla. 563, 79 P. 2d 212 (1928); Benedict v. Harris, 158 Ore. 613, 77 P. 2d 442 (1938).

¹¹ *In re Marshall's Garage*, 63 F. 2d 759 (2d Cir. 1933); Cox & Sons Co. v. Crane Iron Works, cited *supra* note 8; Goldfarb v. Campe Corp., 99 Misc. 475, 164 N. Y. Supp. 583 (1917).

¹² See Beale, *Anticipatory Repudiation of Contracts*, 17 Yale L. J. 443, 448 (1908).

risk and expense, buy the staves . . . upon the open market. . . ."¹³

This view fails to consider the limits to nullification of an anticipatory breach.¹⁴ True, one who repudiates an executory contract prior to performance date may nullify his repudiation, but this right or privilege does not continue indefinitely. If, in considering the repudiation as an "offer to terminate," the other party accepts such offer, there can then be no nullification — only a new contract. Similarly, if the position of the other party is so changed by the repudiation that it could not reasonably be supposed that he will agree to nullification, the contract is considered terminated. Following this reasoning, it is logical to point out that had the plaintiff Corporation gone out on the open market and bought staves other than those contracted for, nullification of the breach would have been precluded.

To present what it considered to be the general rule on mitigation of damages in this country, the court of appeals turned to another federal case, *Continental Grain Co. v. Simpson Feed Co.*,¹⁵ and quoted from it:

. . . [T]he general rule in the United States is that a buyer who refuses to accept a seller's anticipatory refusal to deliver the commodities contracted for, and who insists upon performance by the latter, is not required to go upon the open market and purchase upon receipt of notice that the seller does not intend to perform. He has a right to treat the notice as inoperative, to wait until the time for performance has passed, and then buy on the open market, charging the seller with the difference between the contract price of the goods and the market price which prevailed at the time that performance should have been forthcoming.¹⁶

An imposing group of authorities is listed in support of this rule.¹⁷

¹³ 195 F. 2d at 982.

¹⁴ Rothschild, *Anticipatory Contract Repudiation and its Nullification—State and Federal Courts*, 31 Iowa L. Rev. 383 (1946).

¹⁵ 102 F. Supp. 354 (E. D. Ark. 1951).

¹⁶ *Id.* at 363.

¹⁷ Including *Callan v. Andrews*, 48 F. 2d 118 (2d Cir. 1931); *Mission Furnace Co. v. Cochran*, 8 Fed. 463 (W. D. Pa. 1881); *Walker-Smith Co. v. Bilao*, 204 S. W. 777 (Tex. Civ. App. 1918); 15 AM. JUR., *Damages*, § 50; 46 AM. JUR., *Sales*, §§ 678, 681, 688; 5 WILLISTON, *CONTRACTS* (Rev. ed. 1937) §§ 1337, 1383, 1387; 1 RESTATEMENT, *CONTRACTS* (1932) § 338.

There can be no doubt that there are strong grounds for this conclusion. *Roehm v. Horst*,¹⁸ often cited for this view, is one of the first cases to distinguish between the privilege to cover for self-protection and the duty to mitigate and lessen damages. On the risky basis that the case involved the former problem only, it was deemed to support a rule denying the duty to mitigate. Any distinction between privilege and duty in this instance is at most tenuous. The same criticism can be made of the claim that certain other cases deny a duty to mitigate,¹⁹ where, in effect, it has been said that a party is not under a duty to avoid additional damages, but rather is prevented from recovering those which he might have avoided. This is simply verbiage used for purposes of justification.

A 1949 federal case,²⁰ in considering mitigation, stated that the market price at the date performance was due, not at the time of the anticipatory breach, was the measure of damages. Both *Bartolotta v. Calvo*²¹ and *Segall v. Finlay*²² held the general rule to be that the buyer is under no obligation to buy similar goods from other sources where seller's refusal to deliver is made known prior to performance date. In an 1887 United States Supreme Court case²³ the duty to mitigate was clearly denied. More recently, the author of a treatise on contract law rejects the rule establishing a duty to mitigate, largely on the basis of the financial risk resulting from the unknown and precarious character of the market.²⁴

¹⁸ 178 U. S. 1, 20 (1900): "As to questions of damages, if the action is not premature, the rule is applicable that plaintiff is entitled to compensation based, as far as possible on the ascertaining of what he would have suffered by the continued breach by the other party down to the time of complete performance, less any abatement by reason of circumstances of which he ought reasonably to have availed himself."

¹⁹ *Rock v. Vandine*, 106 Kan. 588, 189 Pac. 157 (1920); *Craig, Thompson & Jefferies v. Barreda*, 200 S. W. 868 (Tex. Civ. App. 1917).

²⁰ *Joseph Denunzio Fruit Co. v. Crane*, 79 F. Supp. 117 (S. D. Cal. 1948).

²¹ 112 Conn. 385, 152 Atl. 306 (1930).

²² 126 Misc. 625, 213 N. Y. Supp. 540 (1925), *aff'd*, 218 N. Y. Supp. 895 (App. Div. 1926).

²³ *Huckley v. Bessemer Steel Co., Ltd.*, 121 U. S. 264.

²⁴ 5 CORBIN, CONTRACTS (1951) § 1053: "In the case of contracts for the future delivery of goods, it has been suggested by a number of courts that, if either the buyer or the seller commits an anticipatory breach, the other party must attempt to mitigate his losses by making another forward-looking contract to buy or sell similar goods, provided that such an attempt seems reasonable under the circumstances. This suggested

On careful analysis, it seems that at least two authorities may not uphold the proposition for which they are cited in the principal case and in many other opinions. In *Callan v. Andrews*²⁵ Judge Learned Hand stated:

That there may be circumstances which will impose on the promisee a duty to cover, we need not deny, though they must be indeed rare. Ordinarily we cannot agree that it is reasonable to require him to divine the course of an 'obviously' changing market about which no one's judgment is of any value.

He then referred to an organized market in futures of grain and cotton on the exchange as the "circumstances" which he noted. Aligning this statement with the advocates of no mitigation demands that Judge Hand meant to limit any duty to mitigate to such instances as he specified. It is equally reasonable, however, to read Judge Hand's language as excluding extremely speculative exchange transactions as were considered in that case, and implying a duty to mitigate where the market has any substantial degree of certainty, as do most commodities ordinarily contracted for sale.

The second authority is Section 338 of the *Restatement of the Law of Contracts*, which possibly is misinterpreted. Support for denying a duty to mitigate the damages resulting from repudiation apparently rests on the general rule of the Section.²⁶ But the inquiry must go deeper. Comment (c) cannot be ignored, and it robs the devil of his cloak:

After an anticipatory breach is known to the injured party, just as in the case of other kinds of breach, the damages that will be awarded are limited by the rule as to avoidable harm. He is not permitted, merely because the breach is anticipatory, to enhance his damages by

rule should not be accepted; and, in several cases, the courts have in fact refused to follow it. It requires the injured party to forecast the unknown future for the benefit of the repudiator. If his forecast is wrong, either he suffers extra loss or such extra loss is thrown on the repudiator, depending on the jury's idea of whether or not the plaintiff was a bad prophet. There is financial risk involved in the making of any such forward contract; and no contractor should be required by the law to run such a risk. . . ."

²⁵ 48 F. 2d 118, 120 (2d Cir. 1931).

²⁶ In effect it says that the rules for determining the damages recoverable for an anticipatory breach are the same as in the case of a breach at the time fixed for performance.

unreasonably continuing his own performance or unreasonably omitting action that would prevent harm.

A line of decisions in New York agree with the principal case in holding that there is no duty to mitigate damages for anticipatory breach.²⁷ These opinions, however, are based on language of a section of the Uniform Sales Act, enacted in that jurisdiction.²⁸ The section is almost identical with the corresponding section of the English Act.²⁹ England has long held that there exists a duty to mitigate in instances of repudiation — the buyer must cover, the seller must unload.³⁰ The one difference in the American and English sections is the added language of the American statute, Section 67 (3), "in the absence of special circumstances showing proximate damages of a greater amount." This clause is the apparent justification for the New York holdings. Although this interpretation is convenient, it hardly seems necessary.

Made glaringly evident by their complete omission in the instant opinion are sound bases for recognizing a duty to mitigate the damages resulting from repudiation of an executory contract of sale. The general rule of mitigation extends to a present breach

²⁷ Including *Segall v. Finlay*, 245 N. Y. 61, 156 N. E. 97 (1927); *Goldfarb v. Campe Corp.*, 99 Misc. 475, 164 N. Y. Supp. 583 (1917).

²⁸ Sec. 67 (Action for failing to deliver goods.)

(1) Where the property in the goods has not passed to the buyer, and the seller wrongfully neglects or refuses to deliver the goods, the buyer may maintain an action against the seller for damages for non-delivery.

(2) The measure of damages is the loss directly and naturally resulting in the ordinary course of events, from the seller's breach of contract.

(3) When there is an available market for the goods in question, the measure of damages, in the absence of special circumstances showing proximate damages of a greater amount, is the difference between the contract price and the market or current price of the goods at the time or times when they ought to have been delivered, or, if no time was fixed, then at the time of the refusal to deliver.

The UNIFORM COMMERCIAL CODE (Official Draft, Text & Comments Ed. 1952) §§ 2-706 and 2-711, -712 provides methods for determining damages for repudiation by either party to a contract for the sale of goods. It permits resale by the seller or "covering" purchases by the buyer. However, the Code does not require this action, but rather affords such as an alternative to the remedy set forth in § 2-713.

²⁹ Sale of Goods Act, 56 & 57 Vict. c. 71, § 51 (1894).

³⁰ *Melachrino v. Nickoll & Knight*, [1920] 1 K. B. 693, 89 L. J. K. B. 906, 122 L. T. 545 (repudiation by seller).

and certainly implies a duty.³¹ The duty has been widely accepted as applicable to anticipatory breach of contracts for the manufacture of goods and for labor.³² There is no good reason to limit the doctrine to those types of contracts. Indeed, there is nothing unreasonable or unjust in asking a party to take steps looking far ahead to mitigate his losses when the very contract he originally made and the conduct of normal business transactions require maximum farsightedness. Any such business transaction has a certain element of "crystal-gazing." This is borne out in the relatively few cases like the principal decision. Most views on mitigation appear in decisions where the injured party has made a substitute forward contract and sues for loss thereunder, not where there has been inaction until after the performance date of the original contract and a suit for damages is brought thereafter.³³ Most parties to a breached contract of sale go ahead in some alternative manner to continue their productivity and to keep alive and active their commercial enterprises, looking to a recovery of the difference between the value of the second contract or act of substitution and the value of the original contract.

In jurisdictions where the Uniform Sales Act prevails, there would appear every reason to follow the English rule (that the injured party must mitigate), since the pertinent sections in the two Acts are almost identical. The fallacy of finding justification for a different interpretation based on slight changes in wording has already been pointed out.

There is a strong line of cases recognizing the propriety and duty

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

³² 5 WILLISTON, CONTRACTS (Rev. ed. 1937) §§ 1298, 1397.

³³ *Hebron Mfg. Co. v. Powell Knitting Co.*, 171 Fed. 817 (3d Cir. 1909); *Renner Co. v. McNeff Bros.*, 102 F. 2d 664 (6th Cir. 1939); *In re Chinook Lumber & Mfg. Co.*, 100 F. 2d 268 (9th Cir. 1938).

of mitigation.⁸⁴ In *Mogilensky v. Abramson*⁸⁵ the court plainly stated that there was a duty to buy other goods between the time of breach and the date when performance was due. In several instances the federal courts have sustained this theory.⁸⁶

In concluding its opinion in the principal case the court again looked to the *Continental Grain Co.* decision for reasons behind the rule it adopted. These reasons were, first, to prevent the encouragement of repudiation by buyers or sellers as the market fluctuates; second, to prevent possible enhancing rather than lessening of the injured party's damages. The first reason is faulty in that it presupposes all parties to an executory sales contract to be ready, if not anxious, to default on their promises. It is hoped this is not true. Also, the reasoning does not consider the business value of sales contracts themselves, and the normal economic compulsion on businesses to abide by their undertakings. The second reason loses weight in face of the rule that the injured party may recover for losses sustained through reasonable acts of mitigation.⁸⁷

Other bases have been advanced for denying a duty to mitigate in this situation.⁸⁸ One is the argument of an undue burden on an innocent party. This is refuted by the protection afforded under the usual application of the mitigation doctrine. The duty to mitigate goes no further than the limits of reasonableness. Still another argument states that the innocent party should be allowed to use

⁸⁴ *Jebeles & Colias Confectionery Co. v. Stephenson*, 6 Ala. App. 103, 60 So. 437 (1912); *Mendel v. Converse & Co.*, 30 Ga. App. 549, 118 S. E. 586 (1923); *Central Lumber Co. v. Arkansas Valley Lumber Co.*, 86 Kan. 131, 119 Pac. 321 (1911); *York-Draper Mercantile Co. v. Lusk*, 6 Kan. App. 629, 49 Pac. 788 (1897); *Goldsmith v. Stiglitz*, 228 Mich. 255, 200 N. W. 252 (1924); *Oklahoma Candy & Commission Co. v. Liquid Carbonic Co.*, 107 Okla. 100, 230 Pac. 250 (1924); *Key v. Kingswood Oil Co.*, 110 Okla. 178, 236 Pac. 598 (1924).

⁸⁵ 164 N. Y. Supp. 700 (Sup. Ct., App. Term, 1917).

⁸⁶ *Crane Iron Works v. Cox & Sons Co.*, 28 F. 2d 328 (3d Cir. 1928); *Samuels v. E. F. Drew & Co., Inc.*, 292 Fed. 734 (2d Cir. 1923); *Skeele Coal Co. v. Arnold*, 200 Fed. 393 (2d Cir. 1912).

⁸⁷ "Damages are recoverable for special losses incurred in a reasonable effort, whether successful or not, to avoid harm that the defendant had reason to foresee as a probable result of his breach when the contract was made." 1 RESTATEMENT, CONTRACTS (1932) § 336 (2).

⁸⁸ See Note, 47 Mich. L. Rev. 538 (1949).

his money or credit as he sees fit. It must be recognized that the money or credit available to him is free for use only because of the premature breach. Perhaps one further reason might be offered, *i.e.*, that a rule denying a duty to mitigate damages, while negative in its approach, is certain and easy to apply. This logic has certainly never met great favor with American courts in other fields of law.

The principle held forth by the court of appeals goes too far — becomes too rigid. It requires only inaction by the injured party irrespective of how long the time may be between breach and performance date, regardless of how advantageous a substitute contract might be, and without conscience in the matter of a fall in prices. On the other hand, the rule recognizing the duty adjusts itself to the reasonableness of anticipating damages as governed by the nature of the commodity and the market.

Today's trend and development of the theory and practice of contract law would seem to point toward recognition of a duty to mitigate damages in these situations. The control and regulation of business by government steadily works toward standardization of business practices and conduct, which include contracts of sale. Mobility and freedom of the right to contract are sacrificed for security and stability. As the government promotes business operation which recognizes broad social-economic needs and subsidizes its very existence, it demands more regimented production and stable, constant commercial activity. Where sales contracts are prematurely breached, such policy would demand a new forward contract to prevent interruption of commerce. Where the government itself is contracting with the injured party for the commodity which is subject of the breach, it would demand acts of mitigation to secure and assure its receipt of the goods. Where price controls exist, the "crystal-gazing" nature of the market, said to burden unjustly the innocent party, may not be a reality. Too, although

impossibility has normally been no excuse for failure to perform,³⁹ except in certain limited categories,⁴⁰ the doctrine of frustration has been broadened because of the impact of government participation on many business contracts. Since the seller has the benefit of this extended frustration doctrine and since the government expects performance by the buyer with whom it is dealing, mitigation becomes not an onerous duty placed on the injured party, but rather a means of his protection — to save what he can.

Even if government control of economic activity lessens, the duty to mitigate damages flows from a sound general principle, one attuned to a free economy. The freedom of the individual to contract without impairment is a right to contract "wisely or unwisely as long as lawfully." Mitigation of damages when a contract is breached is not an unjust imposition but is a proper exercise of that right.

The *Treat* decision will undoubtedly lend support to proponents denying the duty. This seems to be in opposition to the best interests of contracting parties and to the promotion of sound economic aims.

Charles Burgman.

³⁹ *Powell v. State*, 118 S. W. 2d 960 (Tex. Civ. App. 1938) *er. ref.*; *American Fidelity and Gas Co. v. Williams*, 34 S. W. 2d 396 (Tex. Civ. App. 1930) (hardship does not excuse failure to perform).

⁴⁰ 6 WILLISTON, CONTRACTS (Rev. ed. 1938) § 1935.