

## **EXAMINERS' ANALYSIS OF QUESTION NO. 6**

This question raises three issues related to breach of contract:

(1) When is one party's breach serious enough to excuse the other party from continuing to perform its contractual obligations?

(2) What conduct constitutes waiver of a party's intention to expect strict performance of a contract, and can a waiver be effectively revoked?

(3) What remedy or remedies can Zenith likely obtain on the facts provided?

### **I. Legal Background:**

The general rule is that when performance of a duty under a contract is due, any non-performance is a breach. *Woody v Tamer*, 158 Mich App 764, 771 (1987), citing Restatement 2d, Contracts, § 235. But the fact that one or both parties breach does not necessarily terminate the contract. Only a substantial (sometimes called "material") breach permits the nonbreaching party to declare the contract ended without becoming liable for its own nonperformance. Restatement 2d, Contracts, § 237.

In Michigan the first party who substantially breaches a contract cannot maintain an action against the other contracting party for the other's subsequent breach or failure to perform. *Able Demolition, Inc v City of Pontiac*, 275 Mich App 577, 585 (2007), citing *Michaels v Amway Corp*, 206 Mich App 644, 650 (1994). A critical factor in determining whether a particular breach is substantial is "whether the nonbreaching party obtained the benefit which he or she reasonably expected to receive [from the contract]." *Able Demolition*, at 585, quoting *Holtzlander v Brownell*, 182 Mich App 716, 722 (1990). Other factors that may be relevant to determining whether a particular breach is substantial include:

(1) the extent to which damages will adequately compensate the nonbreaching party for the lack of complete performance;

(2) the extent to which the breaching party has partly performed;

(3) the comparative hardship on the breaching party if the contract is terminated;

(4) the willfulness of the breaching party's conduct; and

(5) the degree of uncertainty that the breaching party will perform the remainder of the contract.

*Omnicom of Michigan v Giannetti Investment Co*, 221 Mich App 341, 348 (1997), citing *Walker & Co v Harrison*, 347 Mich 630, 635 (1957). (These factors are also enumerated in Restatement 2d, Contracts, § 241.)

A party to a contract may waive contractual terms that favor it, and thus not require strict performance of the contract by the other party. *Cobbs v Fire Ass'n of Philadelphia*, 68 Mich 463 (1888). A waiver is a voluntary, intentional relinquishment of a known right. *Grand Rapids Asphalt Paving Co v City of Wyoming*, 29 Mich App 474, 483 (1971). A waiver may be proven by express language indicating a waiver or by conduct of a party that is inconsistent with a purpose to demand strict performance. *Id.* A waiver of strict performance that is not supported by consideration may be revoked as to performances that are due in the future by giving reasonable notice to the other party. *Goldblum v UAW*, 319 Mich 30, 37 (1947).

## **II. Application to the Facts:**

### **a. Substantial Breach**

The threshold question to consider is whether Zenith substantially breached the contract first, thereby barring Zenith from suing Able. Although the examiners believe that the facts are more supportive of a "No" answer, particularly on the sales goal issue, the question allows examinees to take either position. Points will be awarded based on the cogency of the

argument applying the law to the facts, not on the result advocated.

It can be argued that weekly sales reports and projections were an essential benefit of the contract to Able because the sales projections were important to Able's programming planning, and that Zenith's failure to provide these materials was a substantial breach. Able's January 2013 letter pointed to this breach as well as low sales. On the other hand, an examinee may argue that Able did not view Zenith's failures as depriving it of something it critically needed; its complaints to Zenith had emphasized insufficient sales and less consistently remarked on untimely and incomplete sales reports and projections.

Looking to the other Restatement factors used to determine whether a breach is substantial, factors (1), (4) and (5) weigh modestly in favor of Able. (1) It would have been difficult for Able to quantify the injury it suffered from not receiving timely sales reports and projections, so suing Zenith for damages would have been an ineffective remedy. (4) Zenith's repeated failures to provide timely and complete sales reports and projections, even after reminders and a stern warning, are arguably "willful conduct." (5) Zenith's history of inadequate performance creates substantial uncertainty that Zenith would perform the contract any more diligently during the rest of its term. Factor (3) strongly favors Zenith, since Able's terminating the contract is a significant economic loss for Zenith. Factor (2), the extent of part performance, is not often informative in situations that involve a series of discrete performances, as opposed to a single undertaking like a construction project. Nevertheless, it can be argued that Zenith partially performed by providing reports much of the time and did not, therefore, materially breach. In sum, an examinee could strike the balance on this particular breach in favor of either Able or Zenith.

As for Zenith's repeated failure to meet sales goals, especially after Able's letter, some examinees may conclude that this is a substantial breach. The benefit that any broadcaster expects to get from advertising sales is an adequate and dependable stream of revenue. Zenith's 2012 sales were well below the goal set in the contract, and Able's consistent complaints to Zenith underscored its importance. However, failure to meet the sales "goal" was not a breach of the

contract. The number was described as a "goal." Zenith did not promise to perform at that level, and the contract had no provision to terminate it for inadequate sales. Examinees who recognize this distinction between the goal and promise should conclude that there was no breach of this nature by Zenith, let alone a substantial breach that would excuse Able's duty to perform.

Examinees who miss the goal/promise distinction will likely go on to conclude that Zenith's unsatisfactory sales performance substantially breached the contract and will prevent Zenith from prevailing. Fewer points will likely be awarded for this conclusion because even if achieving prescribed sales were a term of the contract, it would be difficult to meet the substantial breach standard. Able's damages would be easily measured, Zenith partially performed, and Zenith's failure would not be "willful." The facts state that Zenith was making a good faith effort to meet its sales goals.

#### **b. Waiver**

Able's failure to insist strongly on Zenith's full performance of the weekly sales report/projections requirements during 2012 is conduct amounting to a waiver of Zenith's breaches in 2012, although no specific statement of waiver was made. (The same would be true of Able's approach to meeting the sales goals, if that were a contractual requirement.) However, Able's January 2013 letter clearly and effectively expressed its intention to require strict performance in the future. *Goldblum, supra*. At that point, Zenith could no longer rely on Able's leniency in the past. Some examinees may come to the opposite conclusion. Credit will be awarded for a well-reasoned argument.

Some examinees may analyze the question as involving a demand by Able for adequate assurance of due performance under Restatement 2d, §251. The question did not seek that response, but nearly full credit may be given if an examinee provides solid treatment of the January 2013 letter as such a demand, and Zenith's lapsing back into breach as a failure to give such assurances – and hence, a repudiation of the contract by Zenith.

### **c. Remedies**

Assuming Zenith did not commit the first substantial breach, it can recover damages from Able. Ordinarily, this is the amount of money that will put Zenith in the position it would have been in had the contract been fully performed - usually called the "expectation interest." In this case that means the amount that Able would have paid Zenith for sales made between April 1, 2013, and December 31, 2013, the end of the contract term. Zenith must prove its damages with reasonable certainty, but not with mathematical exactness. It will need to introduce evidence to support its projected sales level for the rest of the year, especially if it claims its sales would have improved over its recent track record. Any expenses saved by Zenith because it did not have to perform the contract (e.g., the compensation of laid off salespersons) would be deducted from its lost revenue. Restatement 2d, Contracts, § 347(c). As the breaching party, Able must bear the risk of a reasonable degree of uncertainty as to the amount of damages. *Lopatrone v Roma Catering Co*, 20 Mich App 250 (1969).

Some applicants may raise specific performance. No points should be awarded for arguing specific performance can be ordered because Zenith would not succeed in having Able ordered to specifically perform the balance of the contract. Specific performance is unavailable because Zenith has an adequate legal remedy in damages, which can be determined with reasonable accuracy. *Ruegsegger v Bangor Twp Relief Drain*, 127 Mich App 28, 31 (1983). A point may be awarded for this correct statement of law. Applicants who assert that specific performance by Zenith cannot be ordered because the contract is a services contract also receive no points for that statement. That rule applies only to "contracts for service or supervision that [are] personal in nature," not to contracts like this one between two business entities. Restatement 2d, Contracts, §367.