

EXAMINERS' ANALYSIS OF QUESTION NO. 13

Test-x's defense

Test-x argues that it did not breach the contract because its 3% estimate fulfilled its promise to be "accurate to within 5%," as stated in its written report to Mellow-Glo. This argument fails, however, because the contract between Test-x and Mellow-Glo required Test-x's determination to be "accurate to within 1%," and Test-x's determination did not satisfy that requirement. While Test-x may claim that the contract was modified by Test-x's statement in its report to Mellow-Glo, that statement did not constitute a valid contract modification.

"[A] party alleging waiver or modification must establish a mutual intention of the parties to waive or modify the original contract." *Quality Prods & Concepts Co v Nagel Precision, Inc*, 469 Mich 362, 372 (2003); see also *Port Huron Educ Ass'n, MEA/NEA v Port Huron Area Sch Dist*, 452 Mich 309, 326-327 (1996) ("[I]n the same way a meeting of the minds is necessary to create a binding contract, so also is a meeting of the minds necessary to modify the contract after it has been made."). "Simply put, one cannot unilaterally modify a contract because by definition, a unilateral modification lacks mutuality." *Quality Prods*, 469 Mich at 373. "This mutuality requirement is satisfied where a waiver or modification is established through clear and convincing evidence of a written agreement, oral agreement, or affirmative conduct establishing mutual agreement to modify or waive the particular original contract." *Id.* at 364-365.

Here, Test-x attempted to unilaterally modify the contract by including a provision in its written report to Mellow-Glo that directly conflicted with a provision addressing the same subject matter in its contract with Mellow-Glo. There is no evidence – written, oral, or through affirmative conduct – that Mellow-Glo agreed to modify the "accurate to within 1%" language. Indeed, Mellow-Glo was unaware of the "accurate to within 5%" statement because no one at the company read the written report (nor did anyone have a duty to do so). The contract was thus not validly modified, and Test-x's claim that it did not breach the contract fails.

Test-x's claim for damages

A. Duty to mitigate

After it learned of the inaccuracy of its labels, Mellow-Glo had a duty to mitigate any damages. "Where one person has committed a tort, breach of contract, or other legal wrong against another, it is incumbent upon the latter to use such means as are reasonable under the circumstances to avoid or minimize the damages. The person wronged cannot recover for any item of damage which could thus have been avoided." *Morris v Clawson Tank Co*, 459 Mich 256, 263-264 (1998); see also *Farm Credit Servs, PCA v Weldon*, 232 Mich App 662, 680 (1998) ("It has long been recognized that the law should encourage a potential plaintiff to take reasonable actions to minimize the extent of damages arising from the wrongful breach of a contract."); *Lawrence*, 445 Mich at 15 ("At common law . . . a plaintiff has a duty to mitigate his loss . . .").

Here, once Mellow-Glo discovered that the labels on its products were inaccurate, it was required to use reasonable means to avoid the damages that would result from that inaccuracy. This could include recalling the mislabeled products, removing the labels, covering the labels, or taking some other step to avoid violating the truth-in-advertising statute. Mellow-Glo would thus not be entitled to recover for any damages incurred after it learned of the error. However, it would be able to recover from Test-x any costs of mitigation (for example, the cost of recalling the mislabeled products or removing the inaccurate labels).

B. Mellow-Glo's claim for lost profits

Mellow-Glo can recover lost profits as part of normal expectation damages.

"[T]he damages recoverable for breach of contract are those that arise naturally from the breach or those that were in the contemplation of the parties at the time the contract was made." *Kewin v Mass Mut Life Ins Co*, 409 Mich 401, 414 (1980); see also *Frank W Lynch & Co v Flex Technologies*, 463 Mich 578, 586 n 4 (2001) (same). "Lost profits resulting from a breach of contract are proper items of loss to be considered . . . in determining damages." *Lorenz Supply Co v Am Standard, Inc*, 100 Mich App 600, 611 (1980), *aff'd*, 419 Mich 610 (1984). Such profits are recoverable if "the defendants reasonably knew or should have known

that in the event of breach this plaintiff would lose profits." *Lawrence v Will Darrah & Assocs, Inc*, 445 Mich 1, 14-15 (1994). "[E]ven where lost profits are difficult to calculate and are speculative to some degree, they are still allowed as a loss item." *Bonelli v Volkswagen of Am, Inc*, 166 Mich App 483, 511 (1988). "Furthermore, Michigan case law indicates that doubts as to the certainty of damages must be resolved against the wrongdoer." *Lorenz*, 100 Mich App at 612.

Here, the contract stated that Mellow-Glo intended to use Test-x's analysis on its labels "to differentiate its products in a very competitive market." Thus, when Test-x and Mellow-Glo entered into the contract, they were both aware that the accuracy of Test-x's analysis would clearly affect the ability of Mellow-Glo to earn profits based on that analysis. Because both parties realized the potential for lost profits in the event of breach, Mellow-Glo can recover those lost profits, excluding lost profits attributed to Mellow-Glo's failure to mitigate its damages upon learning of the breach.

Alternative credit was given for arguing that Mellow-Glo cannot recover lost profits because even if Test-X had not breached, Mellow-Glo's manufacturing flaw meant that its products contained no CBD and thus would not have been profitable in any event.

C. Mellow-Glo's claim for the amount of the fines for statutory violations

Mellow-Glo can likely recover for the amount of any fines imposed before it discovered Test-x's error. As explained above, damages "that arise naturally from the breach" are recoverable. *Kewin*, 409 Mich at 414. Fines imposed for selling inaccurately labeled products can be said to "arise naturally" from the use of inaccurate labels that resulted from breach of a contract.

D. Mellow-Glo's claim for the costs of defending the DoRite lawsuit

Mellow-Glo probably cannot recover the costs of defending the lawsuit because the lawsuit was likely unforeseeable. As explained above, damages "which can reasonably be said to have been in contemplation of the parties at the time the contract was made" are recoverable. *Kewin*, 409 Mich at 419. Courts apply an "objective

standard" of foreseeability, under which damages are recoverable if "the defendants reasonably knew or should have known that in the event of breach," such damages would result. *Lawrence*, 445 Mich at 13, 14-15.

This lawsuit by the new organization, DoRite, was likely unforeseeable: The group was "new," and it brought lawsuits against "select" companies. The facts do not support the conclusion that either Test-x or Mellow-Glo could have reasonably anticipated that this new group would decide to target Mellow-Glo in its litigation campaign. Consequently, Mellow-Glo cannot recover for the costs of defending against this lawsuit.

E. Mellow-Glo's claim for punitive damages

Mellow-Glo cannot recover punitive damages because they are not available for breach of contract. "[T]he goal in contract law is not to punish the breaching party, but to make the nonbreaching party whole." *Corl v Huron Castings, Inc*, 450 Mich 620, 625-626 (1996). "[A]bsent allegation and proof of tortious conduct existing independent of the breach, exemplary damages may not be awarded in common-law actions brought for breach of a commercial contract." *Kewin*, 409 Mich at 420-421 (citation omitted); see also *Valentine v Gen Am Credit, Inc*, 420 Mich 256, 263 (1984) (same). Punitive damages in the absence of a statutory authorization are not recoverable in Michigan. *Casey v Auto Owners Ins Co*, 273 Mich App 388, 400 (2006).

Here, there is no evidence of tortious conduct by Test-x independent of its breach, so Mellow-Glo cannot recover exemplary/punitive damages.