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### Decoupling Sales Law from the Acceptance-Rejection Fulcrum

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# Decoupling Sales Law from the Acceptance-Rejection Fulcrum

Jody S. Kraus<sup>†</sup>

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In a word, the Title-concept lumps so many policy decisions together that the same decision about Title, in two cases having similar facts, would repeatedly lead to unfortunate results in one or the other, according to the issue. . . .

*The quarrel thus is . . . with the insistence on reaching for a single lump to solve all or most of the problems between seller and buyer . . . .*

Karl Llewellyn<sup>1</sup>

The determination of whether the buyer has accepted or rejected goods provides the sales law solution to the problems of allocating burden of proof, assigning duties to salvage goods in failed transactions, and reducing systematic undercompensation. But one doctrine is unlikely to provide the best solution to each of these distinct problems. Decoupling the rules addressing burden of proof, salvage, and undercompensation from the doctrines of

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1. Karl Llewellyn, *Through Title to Contract and a Bit Beyond*, in 3 *LAW: A CENTURY OF PROGRESS 1835-1935*, at 80, 89, 84 (1937) (emphasis added). (The second sentence quoted occurs five pages before the first sentence.)

acceptance and rejection, and thus from one another, would significantly improve sales law.

This strategy has a distinguished precedent in the history of sales law. Karl Llewellyn based his objection to the doctrine of title in large measure on his conviction that the policy issues arising in sales cases called for more fine-grained distinctions than the concept of title allowed.<sup>2</sup> In light of the fact that more than ten separate legal questions turned solely on the determination of the location of title,<sup>3</sup> Llewellyn concluded that “[title] remains, in the Sales field, an alien lump, undigested, and interfering with the digestive process.”<sup>4</sup> When he took principal responsibility for drafting Article 2 of the Uniform Commercial Code (U.C.C.), Llewellyn thus set about the task of ridding the concept of title from substantive sales law. Despite this largely successful effort,<sup>5</sup> however, Llewellyn left in place the doctrines of acceptance, rejection,

2. Llewellyn expressed his frustration with the doctrine of title by likening it to sorting peas with “battered mittens.” *Id.* at 106.

3. As Llewellyn observed, under the Uniform Sales Act (U.S.A.), title governed between the parties, risk [of loss], action for the price, the applicable law in an interstate transaction, the place and time for measuring damages, the power to defeat the other party’s interest, or to replevy, or to reject . . . [and] as against outsiders, levability, rights against tortfeasors, infraction of criminal statutes about sales, incidence of taxation, [and] power to insure *Id.* at 87.

4. Llewellyn adds that “this would be an admirable way to go at it if the Title concept (or other basic integrated concept used) had been tailored to fit the normal course of a *going or suspended situation during its flux or suspension*. But Title was not thus conceived, nor has its environment of buyers and sellers had material effect upon it.” *Id.*

5. Llewellyn’s success in purging the common law concept of title from sales law is apparent from the following statement: “This Article deals with the issues between seller and buyer in terms of step by step performance or non-performance under the contract for sale and not in terms of whether or not ‘title’ to the goods has passed.” U.C.C. § 2-401 cmt. 1 (1993). In addition, § 2-401 states that “[e]ach provision of this Article with regard to the rights, obligations and remedies of the seller, the buyer, purchasers or other third parties applies irrespective of title to the goods except where the provision refers to such title.” *Id.* § 2-401 cmt. 1. For those few provisions that unavoidably rely on the concept of title (e.g., § 2-501, which addresses insurable interests), § 2-401 completely supplants the common law and Sales Act rules governing the passage of title and provides in their place a set of precise default rules governing the passing of title that turn on delivery, tender, and the like.

Article 2’s treatment of risk of loss provides the clearest example of Llewellyn’s success in replacing title with an empirically accessible and policy-driven doctrine. In the Uniform Sales Act, risk of loss turned on the question of the location of title to the goods. U.S.A. § 22 (1906). U.S.A. § 22 allocated risk of loss. According to Mariash, “[s]ection 22 may be summarized in the phrase ‘risk of loss follows the title’ in whomever the title is vested that person bears the risk of loss to the goods.” IRVING MARIASH, A TREATISE ON THE LAW OF SALES § 178, at 418 (1930) (footnote omitted). The precursor to U.C.C. § 2-510 appears in U.S.A. § 22(b): “Where delivery has been delayed through the fault of either buyer or seller the goods are at the risk of the party in fault as regards any loss which might not have occurred but for such fault.” U.S.A. § 22(b). As Mariash puts it, “[t]he qualification stated in the section is one which we would reasonably expect, and the rule will give way where the loss has occurred through the fault of either party. Where one causes loss through his fault, that one must suffer.” MARIASH, *supra*, § 178, at 418-19. Under § 2-509 of the U.C.C., risk of loss for conforming goods turns instead on delivery, tender, acknowledgment, or receipt—concrete acts subject to comparatively easy empirical verification and relevant to the policy of allocating risks to the most efficient risk-bearer:

The underlying theory of this rule is that a merchant who is to make physical delivery at his own place continues meanwhile to control the goods and can be expected to insure his interest in them. The buyer, on the other hand, has no control of the goods and it is extremely unlikely that he will carry insurance on goods not yet in his possession.

and revocation.<sup>6</sup> Whereas title provided one of the most important unifying doctrines of the Sales Act, these doctrines, which I shall refer to collectively as the "acceptance-rejection fulcrum,"<sup>7</sup> constitute the most distinctive and unifying doctrines in Article 2. Although the acceptance-rejection fulcrum considerably improves upon the prior title regime, I will argue that it is vulnerable to the central objection Llewellyn leveled against the title doctrine: it improperly lumps the promotion of several policy goals into a single doctrinal inquiry. By reducing the treatment of burden of proof, salvage, and undercompensation to the question of whether goods have been accepted or rejected, the Code takes an inefficient "one doctrine fits all" approach to disparate problems in sales law.

Despite the "lumpiness" of Code doctrines, early law and economics scholarship argued that the Code's rules are, in general, economically efficient. However, the express terms and rationales of the Code's rules and cases rarely invoke efficiency directly. Therefore, scholars initially argued that common law and Code rules are efficient by demonstrating that the outcomes of cases are efficient.<sup>8</sup> Subsequent scholarship closely examined the content of the rules and argued that efficiency rationales could be supplied for most of them.<sup>9</sup>

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U.C.C. § 2-509 cmt. 3. Similarly, § 2-510 allocates risk of loss for nonconforming goods without regard to the location of title. But Llewellyn's success was not equaled by the doctrines that determine risk of loss under § 2-510. First, under § 2-510, risk of loss turns on whether breach has occurred, a fact that may be difficult to determine. Second, under § 2-510, risk of loss remains on the seller for tender or delivery of nonconforming goods that give rise to a right to reject until the seller cures or the buyer accepts. Similarly, a revoking buyer can "treat the risk of loss as having rested on the seller from the beginning." *Id.* § 2-510(2). Apart from the widely recognized fact that § 2-510's treatment of risk of loss runs contrary to the Code's own policies, the Code's risk of loss provisions exemplify Llewellyn's practice of trading in the doctrine of title for the doctrines of acceptance, rejection, and revocation.

6. The doctrine of revocation is original to Article 2, but it was designed to resolve ambiguities arising under the common law remedy of rescission. See JAMES J. WHITE & ROBERT S. SUMMERS, *UNIFORM COMMERCIAL CODE* § 8-1 (3d ed. 1988).

7. Burden of proof, salvage, and undercompensation can be thought of as balancing on an "acceptance-rejection fulcrum," falling to the buyer's or seller's side of the fulcrum depending on whether acceptance, rejection, or revocation takes place. The metaphor of the "acceptance-rejection fulcrum" also conveys the centrality of these doctrines to Article 2 of the U.C.C.

8. See, e.g., George L. Priest, *Breach and Remedy for the Tender of Nonconforming Goods Under the Uniform Commercial Code: An Economic Approach*, 91 HARV. L. REV. 960 (1978). Priest's central claim is that

[e]conomic efficiency never has been recognized explicitly as a standard of Code interpretation and is seldom mentioned as a criterion of decision in judicial opinions. But the results of decisions interpreting the Code are consistent with minimization of long-run costs of formation of the contract, of delivery and handling of the goods, and of resolution of disputes arising under the contract.

*Id.* at 960.

9. See, e.g., Charles J. Goetz & Robert E. Scott, *Enforcing Promises: An Examination of the Basis of Contract*, 89 YALE L.J. 1261 (1980) [hereinafter *Enforcing Promises*]; Charles J. Goetz & Robert E. Scott, *Measuring Seller's Damages: The Lost Profits Puzzle*, 31 STAN. L. REV. 323 (1979); Charles J. Goetz & Robert E. Scott, *The Mitigation Principle: Toward a General Theory of Contractual Obligation*, 69 VA. L. REV. 967 (1983) [hereinafter *The Mitigation Principle*]; Charles J. Goetz & Robert E. Scott, *Principles of Relational Contracts*, 67 VA. L. REV. 1089 (1981) [hereinafter *Principles of Relational Contracts*]; Thomas H. Jackson, "Anticipatory Repudiation" and the Temporal Element of Contract Law: An Economic Inquiry into Contract Damages in Cases of Prospective Nonperformance, 31 STAN. L. REV. 69 (1978); Anthony T. Kronman, *Mistake, Disclosure, Information, and the Law of Contracts*, 7 J. LEGAL STUD. 1

Although no one argued that drafters or judges consciously designed the rules to be efficient,<sup>10</sup> the implicit assumption underlying these efficiency reconstructions was that inefficient rules governing commercial transactions are unlikely to survive years of common law adjudication and statutory revision.<sup>11</sup> Even Llewellyn acknowledged that courts often overcome the doctrinal hurdle of title when the underlying policy goal is clear.<sup>12</sup> But Llewellyn's instinct nonetheless drove him to reject a number of the received common law rules in favor of rules designed expressly to facilitate commercial transactions. It is something of a puzzle, therefore, why Llewellyn rejected the doctrine of title but incorporated the acceptance-rejection fulcrum into Article 2.<sup>13</sup> Had Llewellyn followed through on his principle of purging lumpy doctrines from the Code and replacing them with doctrines designed directly to achieve relevant policy goals, he might have developed more efficient rules to promote each of the policies advanced by the acceptance-rejection fulcrum. Notwithstanding the often persuasive efficiency reconstructions of sales law, I argue that separate rules, each designed to promote only one of the functions currently served jointly by the acceptance-rejection fulcrum, will be more efficient. My argument finds support in the intuition that rules designed to

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(1978); Alan Schwartz, *The Case for Specific Performance*, 89 YALE L.J. 271 (1979) *But see* Ian Ayres & Robert Gertner, *Filling Gaps in Incomplete Contracts: An Economic Theory of Default Rules*, 99 YALE L.J. 87 (1989); Charles J. Goetz & Robert E. Scott, *Liquidated Damages, Penalties and the Just Compensation Principle: Some Notes on an Enforcement Model and a Theory of Efficient Breach*, 77 COLUM. L. REV. 554 (1977); Charles J. Goetz & Robert E. Scott, *The Limits of Expanded Choice: An Analysis of the Interactions Between Express and Implied Contract Terms*, 73 CAL. L. REV. 261 (1985).

10. Analogously, when political contractarians argue that political association is efficient relative to the state of nature, they rarely argue that the goal of the individuals who create political association in the state of nature is to increase efficiency. For a discussion of the role of collective rationality justifications in social contract theories, see JODY S. KRAUS, *THE LIMITS OF HOBBSIAN CONTRACTARIANISM* 16-18, 48-56 (1993).

11. The claim that the common law tends to produce efficient rules is well known in the legal literature. *See, e.g.*, RICHARD A. POSNER, *THE ECONOMICS OF JUSTICE* 103-07 (1981), *General Discussion. Evolution and the Efficiency of Law*, in 4 RESEARCH IN LAW AND ECONOMICS 167 (Paul H. Rubin ed., 1982); William M. Landes & Richard A. Posner, *Adjudication as a Private Good*, 8 J. LEGAL STUD. 235, 259-84 (1979); George L. Priest, *The Common Law Process and the Selection of Efficient Rules*, 6 J. LEGAL STUD. 65 (1977); Paul H. Rubin, *Why Is the Common Law Efficient?*, 6 J. LEGAL STUD. 51 (1977).

12. Llewellyn, *supra* note 1, at 89 ("[T]he courts, whether they talk Title or talk the precise issue, whether they shelter themselves under or disregard the Title-formulae, show in a surprising proportion of the cases a *feel* for the precise issue . . . for a fair portion of the relevant policy.")

In the same vein, Priest argues that courts understand the efficiency stakes in sales cases and interpret rules accordingly:

Where necessary, courts have extended Code principles beyond the letter of the Code in ways which minimize costs. Where no appropriate Code principles existed, courts have themselves created doctrines which reduce costs . . . . In certain cases, courts have refused to adopt interpretations of the Code . . . which increase the costs of sales transactions

Priest, *supra* note 8, at 1001.

13. Although I am unaware of any evidence that Llewellyn objected to the acceptance-rejection fulcrum, it is of course possible that he tried to change it without success. In one article, he wrote

I am ashamed of [the U.C.C.] in some ways . . . there are so many beautiful ideas I tried to get in that would have been good for the law, but I was voted down. A wide body of opinion has worked the law into some sort of compromise after debate and after exhaustive work

Karl Llewellyn, *Why a Commercial Code?*, 22 TENN. L. REV. 779, 784 (1953)

serve particular policy goals are likely to be better than ones produced by an even relatively efficient legal-evolutionary process. It is this intuition, after all, that animated Llewellyn's revision of sales law in the first place.<sup>14</sup>

The central thesis of this Article is that the Code's burden-of-proof, salvage, and undercompensation rules should be decoupled from one another and from the acceptance-rejection fulcrum. I reject the acceptance-rejection fulcrum not only because it inefficiently lumps together the distinct policy goals underlying these rules, but also because it would be inefficient even if it governed only one of these policy goals. In the succeeding parts of this Article, I explain how the acceptance and rejection doctrines<sup>15</sup> serve three distinct purposes.<sup>16</sup> The first is to allocate the burden of proving that a tender of goods was nonconforming. The second is to regulate the salvage of goods in a failed transaction.<sup>17</sup> The third is to accomplish the second without unduly exacerbating the nonbreacher's risk of undercompensation by requiring the nonbreacher to incur additional expenses that are subject to systematic undercompensation.<sup>18</sup>

Part I provides the first part of the case for decoupling burden-of-proof, salvage, and undercompensation rules from each other and from the acceptance-rejection fulcrum. I argue that the Code forces an efficiency trade-off between the allocation of burden of proof and the allocation of salvage duties that can be avoided by decoupling the burden-of-proof and salvage rules from each other. I then argue that the burden-of-proof rule should be decoupled from the acceptance-rejection fulcrum, even if the latter were used

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14. Although it would be anachronistic to claim that Llewellyn was motivated by a concern to improve efficiency as that concept is defined today, it is fair to say that Llewellyn's goal was to reform commercial law so that it would better facilitate commercial transactions. Implicit in this reform effort is a belief that rules designed to facilitate transactions can improve upon some of the common law rules that have evolved over time and that have never been "designed" by anyone.

15. Throughout this Article, I will often equate the acceptance-rejection fulcrum with the acceptance and rejection doctrines only, omitting reference to the revocation doctrine. Under § 2-608(3), buyers who successfully revoke their acceptance have the same rights and duties with regard to the goods as rejecting buyers. Thus, consideration of the consequences of rejection will ordinarily suffice as consideration of the consequences of revocation. Where different requirements for revocation are relevant, I will explicitly incorporate revocation into the analysis.

16. In addition to serving these three purposes, acceptance, rejection, and revocation play a role in the allocation of risk of loss of nonconforming tenders. See *supra* note 5. Section 2-510 allocates risk of loss to the seller before acceptance and to the buyer after acceptance. But this provision is widely regarded as anomalous and is unlikely to survive the next revision of Article 2. See PEB STUDY GROUP, UNIFORM COMMERCIAL CODE ARTICLE 2, at 149-51 (prelim. rep. Mar. 1, 1990); *An Appraisal of the March 1, 1990 Preliminary Report of the Uniform Commercial Code Article 2 Study Group*, 16 DEL. J. CORP. L. 981, 1153-54 (1991) ("[T]here is no obvious connection between the fact of breach and which party is the least cost insurer of the goods. The effect of § 2-510, therefore, is to reallocate the risk from the party in the best position to insure to the contract breacher who, presumably, is not. This result makes little sense in a commercial statute.").

17. The doctrines serve this second purpose in three ways: first, by enabling the parties to signal that their transaction has failed; second, by defining one of the conditions under which the seller is entitled to the price (§ 2-607(1) provides that the buyer has the duty to pay for goods accepted and § 2-709(1)(a) provides that the seller has a right to recover the price of goods accepted); and third, by expressly creating certain salvage duties and limiting others.

18. See *infra* text accompanying notes 79-88.

exclusively to allocate burden of proof. I consider three efficiency rationales for allocating burden of proof and conclude that none of them explains or justifies the Code's use of the acceptance-rejection fulcrum to allocate burden of proof. On balance, these rationales instead support a rule that would allocate burden of proof to the buyer upon tender.

The remaining task is to demonstrate that the salvage and undercompensation rules should be decoupled from one another as well as from the acceptance-rejection fulcrum. Part II takes up that task by considering and rejecting the strongest argument in favor of the Code's regime. That argument is based on what I call the "efficiency trade-off story." This story purports to explain and justify the Code's salvage regime by maintaining that the cases in which the Code fails to require the most efficient salvor to salvage are necessary to avoid increasing the nonbreacher's risk of systematic undercompensation.

Part III sketches an alternative salvage regime in which salvage and undercompensation are decoupled from one another and from the acceptance-rejection fulcrum. I argue that by assigning to the breacher the burden of proving the unreasonableness of the nonbreacher's salvage expenses, this alternative regime can increase the efficiency of the salvage of goods while maintaining at least the same reduction in the nonbreacher's risk of undercompensation that the current regime achieves. I make two standard assumptions throughout the Article: that default rules should impute into contracts the terms that most parties would choose, and that most parties in commercial transactions would choose those terms that maximize the joint net present value of their contracts at the time of formation.<sup>19</sup>

#### I. BURDEN OF PROOF AND THE ACCEPTANCE-REJECTION FULCRUM

The standard of proof for establishing a fact under the Code is "the burden of persuading the triers of fact that the existence of the fact is more probable than its non-existence."<sup>20</sup> If direct evidence of the conformity of the goods

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19. The first of these assumptions is the basic tenet of so-called "majoritarian default analysis." See, e.g., ALAN SCHWARTZ & ROBERT E. SCOTT, SALES LAW AND THE CONTRACTING PROCESS 21-23 (2d ed 1991); Ayres & Gertner, *supra* note 9, at 89-90; Richard Craswell, *Property Rules and Liability Rules in Unconscionability and Related Doctrines*, 60 U. CHI. L. REV. 1, 13 (1993); Robert E. Scott, *A Relational Theory of Default Rules for Commercial Contracts*, 19 J. LEGAL STUD. 597, 606 (1990). The second assumption is basic to the economic analysis of contract law. See, e.g., Goetz & Scott, *The Mitigation Principle*, *supra* note 9, at 971; Goetz & Scott, *Principles of Relational Contracts*, *supra* note 9, at 1097.

20. U.C.C. § 1-201(8). Comment 6 to § 2-607 explains, however, that "this rule becomes one purely of procedure when the tender accepted was non-conforming and the buyer has given the seller notice of breach under subsection (3)." But the standard of proof governs the determination of the nonconformity in the first instance. If the fact of the tender's nonconformity is established, the standard of proof has been met *a fortiori*. Yet some courts at least implicitly take comment 6 to license a variance in the standard of proof. Of the fourteen cases in the U.C.C. reporter that discuss the extent of the burden to be imposed upon the buyer, three appear to impose burdens substantively different from the standard in § 1-201(8). See



at the time of tender is not available, assigning the burden of proof to one party is often tantamount to deciding the case against that party. The parties, therefore, would place particular importance on the term that assigns burden of proof in their contracts. With respect to the question of whether goods tendered are conforming,<sup>21</sup> the Code assigns this burden of proof<sup>22</sup> to the

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*Bickett v. W.R. Grace & Co.*, 12 U.C.C. Rep. Serv. (Callaghan) 629, 646 (W.D. Ky. 1972) (holding that buyer must show causation, cannot pile an "inference upon an inference"); *Heil v. Standard Chem. Mfg. Co.*, 15 U.C.C. Rep. Serv. (Callaghan) 345, 352-53 (Minn. 1974) (holding that, given multiple factors involved in fattening cattle, lack of strong causation evidence with respect to seller's feed fails to meet buyer's burden of proof: "causation cannot be established through negative implication"); *American Fertilizer Specialists v. Wood*, 635 P.2d 592, 594-96 (Okla. 1981) (holding that buyer must show that seller's breach is "more probable . . . than any other possible cause," arguably a lighter burden than "more probable than not," particularly in light of testimony that "there are something like 57 things that control the making of a crop"). These cases—particularly *American Fertilizer* and *Bickett*—appear to invoke whatever standard of proof will accommodate finding against the litigant suspected of bad faith. In *American Fertilizer*, for example, the trial court judge doubted the seller's claim that it had spread fertilizer. 635 P.2d at 597.

21. The task of proving conformity sometimes consists not only in proving that the goods tendered satisfied the performance standard specified in the contract, but also in proving the content of that performance standard. The analysis I provide adduces rationales for allocating the burden of proving the former only. Neither party is likely to have a systematic advantage in proving the content of contractual performance standards, and assigning either party that burden would provide the party to whom it is assigned with an incentive to specify the performance standards optimally at formation. Thus, the analysis of the allocation of burden of proof can focus exclusively on rationales for allocating the burden of proving that the tender conforms to the contractual standard. Whichever party the analysis determines should be allocated that burden will also bear the burden of proving the standard itself. If there are independent considerations supporting a different allocation of the burden of proving the standard, however, those considerations would provide a reason for separating these two burdens and allocating each with separate rules.

22. The doctrine of the burden of proof is actually twofold. First, it provides a standard of proof in order to establish the truth of propositions the parties allege in court. That standard allocates the risk of nonpersuasion. The risk of nonpersuasion directs the trier of fact to resolve in the defendant's favor any uncertainty that falls below the threshold defined by the standard of proof. Second, it assigns to the parties the burden of going forward with the evidence—or what is often called the "burden of production." In a civil suit, the plaintiff has the burden of production. The party assigned the burden of production must provide evidence sufficient to justify a reasonable trier of fact finding in its favor. Failure to provide such evidence results in summary judgment for the defendant. Once the plaintiff establishes his *prima facie* case, the plaintiff has satisfied his burden of production. Even if the defendant fails to introduce any further evidence, the case will be tried and resolved on the weight of the evidence presented by the plaintiff. But if the evidence presented is sufficient for a directed verdict against the defendant, the burden of production shifts to the defendant, who must satisfy it in order to avoid a finding against him. See generally FLEMING JAMES, JR. ET AL., CIVIL PROCEDURE §§ 7.12-16 (4th ed. 1992); GRAHAM C. LILLY, AN INTRODUCTION TO THE LAW OF EVIDENCE § 3.1 (1987). This shift occurs automatically when satisfaction of the plaintiff's *prima facie* case creates a presumption against the defendant that, if not overcome, will result in the defendant being found guilty. See, e.g., *St. Mary's Honor Ctr. v. Hicks*, 113 S. Ct. 2742, 2747 (1993):

Under the *McDonnell Douglas* scheme, "[e]stablishment of the *prima facie* case in effect creates a presumption that the employer unlawfully discriminated against the employee." To establish a "presumption" is to say that a finding of the predicate fact (here, the *prima facie* case) produces "a required conclusion in the absence of explanation" (here, the finding of unlawful discrimination).

*Id.* (alteration in original) (citations omitted).

Except for affirmative defenses, counterclaims, and the like, the plaintiff bears the burden of production and the risk of nonpersuasion in sales cases. The leading case discussing the burden of proof for summary judgment is *Celotex Corp. v. Catrett*, 477 U.S. 317 (1986). For applications of *Celotex* to sales cases, see *Dowty Communications Inc. v. Novatel Computer Sys. Co.*, 19 U.C.C. Rep. Serv. 2d (Callaghan) 73 (D. Md. 1992); *Lenox, Inc. v. Triangle Auto Alarm*, 738 F. Supp. 262 (N.D. Ill. 1990); see also Ronald J. Allen & Robert Hillman, *Evidentiary Problems In— And Solutions For— the Uniform Commercial Code*, 1984 DUKE L.J. 92, 105 (proposing amendment to U.C.C. establishing burdens of production and

seller of rejected goods and the buyer of accepted goods.<sup>23</sup> Under the Code, a buyer has accepted goods if she<sup>24</sup> “after a reasonable opportunity to inspect the goods signifies to the seller that the goods are conforming or that [she] will take or retain them in spite of their non-conformity,”<sup>25</sup> or if she “fails to make an effective rejection . . . [but not before she] has had a reasonable opportunity to inspect them,”<sup>26</sup> or if she “does any act inconsistent with the seller’s ownership.”<sup>27</sup> A buyer has rejected goods if “[r]ejection of goods [is] within a reasonable time after their delivery or tender” and “the buyer seasonably notifies the seller.”<sup>28</sup> A buyer who has accepted goods and then revokes her acceptance has the same obligations with respect to the goods as an effectively rejecting buyer.<sup>29</sup> A buyer can revoke acceptance if the nonconformity of a good accepted “substantially impairs its value to [her]”<sup>30</sup> and she accepted either “on the reasonable assumption that its non-conformity would be cured and it has not been seasonably cured”<sup>31</sup> or “without discovery of such non-conformity if [her] acceptance was reasonably induced either by the difficulty of discovery before acceptance or by the seller’s assurances.”<sup>32</sup> In addition, “[r]evocation of acceptance must occur within a reasonable time after the buyer discovers or should have discovered the ground for it and before any substantial change in condition of the goods which is not caused

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persuasion for proof of facts at trial).

23. “The burden is on the buyer to establish any breach with respect to the goods accepted” U.C.C. § 2-607(4). Courts and commentators agree that by negative implication, the burden is on the seller to establish the conformity of rejected goods. *See, e.g.,* *Miron v. Yonkers Raceway, Inc.*, 400 F.2d 112, 119 n.17 (2d Cir. 1968); *Ramirez v. Autosport*, 440 A.2d 1345, 1351 (N.J. 1982); *Flowers Baking Co. v. R-P Packaging Inc.*, 329 S.E.2d 462, 467 (Va. 1985); ROBERT J. NORDSTROM, *HANDBOOK ON THE LAW OF SALES* § 142, at 431 (1970); SCHWARTZ & SCOTT, *supra* note 19, at 267-68.

24. In order to distinguish sellers from buyers in ambiguous contexts, I will assume male sellers and female buyers throughout this Article.

25. U.C.C. § 2-606(1)(a).

26. *Id.* § 2-606(1)(b).

27. *Id.* § 2-606(1)(c).

28. *Id.* § 2-602(1).

29. *Id.* § 2-608(3). The burden of proof shifts to the buyer upon acceptance, it is unclear, however, whether a buyer who has accepted goods shifts the burden of proof back to the seller by revoking acceptance. Although § 2-608(3) states that revoking buyers have the same rights and duties with regard to the goods as rejecting buyers, it is not clear whether the burden of proof is a “right or duty with respect to the goods.” If it is, once the buyer revokes, she no longer bears the burden of proof. But this shift of the burden of proof would be of little practical value. Section 2-608(1) presupposes that a buyer will be allowed to revoke only after she has proved not only that the goods tendered were nonconforming but also that the nonconformity substantially impaired the goods’ value to her. Thus, I will assume that revocation does not provide the accepting buyer with an effective option of avoiding the burden of proof. Even if, in theory, the burden of proof shifts back to the seller upon revocation, the buyer would already have had to carry the burden in order to revoke in the first place. This analysis assumes that it is impossible to revoke acceptance effectively but wrongfully. For an analysis of § 2-608 and the argument for this conclusion, see *infra* text accompanying notes 116-28 in Part II.D.

30. U.C.C. § 2-608(1).

31. *Id.* § 2-608(1)(a).

32. *Id.* § 2-608(1)(b).

by their own defects.”<sup>33</sup> Finally, a revocation is effective only if “the buyer notifies the seller of it.”<sup>34</sup>

In this Part, I present two objections to the Code’s burden-of-proof rule. First, I argue that it unnecessarily forces courts to choose between the efficient allocation of the burden of proof and the efficient allocation of the duty to salvage goods. Yet decoupling the Code’s burden-of-proof rule from the Code’s salvage rules, both of which are currently linked to the acceptance-rejection fulcrum, avoids this Hobson’s choice. Second, I consider the possibility of decoupling the burden-of-proof rule from the salvage rules by severing the link between the acceptance-rejection fulcrum and salvage while preserving the link between the acceptance-rejection fulcrum and the allocation of burden of proof. This approach would require the creation of a new rule for allocating salvage duties and would use the acceptance-rejection fulcrum exclusively to allocate burden of proof. I reject this possibility, however. There is no economic justification for allocating the burden of proof to the seller before acceptance and to the buyer after acceptance. Given the economic rationales for allocating burden of proof, I claim that a rule allocating the burden of proof to the buyer upon tender would be more efficient.

#### A. *Decoupling Burden-of-Proof from Salvage Rules*

Given that acceptance and rejection<sup>35</sup> turn on the rather vague questions of whether a “reasonable time” for inspection has elapsed following tender, whether notification of rejection was “seasonable,” and whether the buyer acted “inconsistently with seller’s ownership,” one might suppose that the Code effectively gives the trier of fact the discretion to allocate the burden of proof as it sees fit. Indeed, the claim that judges, for example, might simply decide the acceptance-rejection question with an eye toward the appropriate allocation of burden of proof is, in some cases, undoubtedly true. Especially in cases in which acceptance and rejection are unclear, a court may have considerable discretion to rule according to whatever burden-of-proof policy it finds controlling. The celebrated case of *Miron v. Yonkers Raceway, Inc.*<sup>36</sup> provides a clear illustration of this kind of judicial reasoning. In that case, the

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33. *Id.* § 2-608(2).

34. *Id.*

35. The text excludes revocation from the discussion of the factors affecting the allocation of burden of proof because of the previous assumption that revocation does not provide the accepting buyer with an effective avenue for avoiding the burden of proof. *See supra* note 29. If an effective but wrongful revocation is possible, then the accepting buyer could avoid bearing the burden of proof, and the discussion in the text would include the vague conditions that establish revocation, such as whether the nonconformity “substantially impairs” the goods’ value to the buyer, whether the seller’s cure was “seasonable,” whether acceptance was “reasonably induced” by difficulty of discovery of the defect or the seller’s assurances, whether revocation occurred within a “reasonable time” after the buyer discovered or should have discovered the defect, and so forth.

36. 400 F.2d 112 (2d Cir. 1968).

buyer bought a horse at an auction in the afternoon and immediately had the horse transported to his barn. The next morning he discovered the horse had a broken splint bone, a condition that rendered the horse unsound. In order to allocate the burden of proving the horse was unsound at tender, the court first had to determine whether the buyer had accepted or rejected the horse. If the buyer's rejection did not take place "within a reasonable time,"<sup>37</sup> the court would have had to find that the buyer had accepted the horse and that the buyer therefore bore the burden of proof. If the rejection did take place within a reasonable time, the court would have had to hold that the burden of proof remained on the seller. The court virtually equated the task of determining whether rejection occurred within a reasonable time with the task of allocating the burden of proof:

We conclude that rejection did not take place within a reasonable time after delivery, and [the buyer] thus accepted the horse. In short, since one of the consequences of acceptance is that the buyer bears the burden of proving any breach, the fairness of allocating the burden one way or the other is relevant in determining whether acceptance has occurred—here, whether rejection took place within a reasonable time.<sup>38</sup>

Thus, the Court based its decision that acceptance had occurred almost entirely on its preferred policy for allocating the burden of proof in the case.

*Miron* illustrates the point that courts sometimes simply manipulate the acceptance-rejection fulcrum to suit the policies underlying the allocation of burden of proof. Although the Code's rule does not explicitly direct courts to provide an efficient allocation of the burden of proof, courts might nonetheless effect such an allocation in each case by deciding acceptance and rejection accordingly.

Llewellyn, of course, would be the first to object to the *Miron* approach. He would no doubt argue that this sort of adjudication would lead to a less clear, less predictable allocation of burden of proof.<sup>39</sup> Llewellyn's concern in part reflects the fact that not all judges will share the same policy goals. In the present context, the concern is that some judges will not intuit the efficient

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37. U.C.C. § 2-602(1).

38. 400 F.2d at 119.

39. Llewellyn argued that despite the efforts of right-minded judges, a system of rules not directly designed to facilitate commercial transactions is unlikely to lead to optimal results. In the case of title, Llewellyn claimed:

The necessary result of such a situation is that a rule on passage of Title, worked out commonly in a situation where its implication fitted the issue well enough, is either (1) applied blindly to situations in which a different implication is concerned, with regrettable consequence, or (2) is sleight-of-handed into inconsistent use in the new situation, to achieve a consequence deemed desirable. Even the process of qualifying and distinguishing throw[s] into confusion any lines of *predictable* presuming about *Title*.

Llewellyn, *supra* note 1, at 89 (citations omitted).

allocation of burden of proof, much less interpret the acceptance-rejection fulcrum to accommodate that allocation. But even if they did, the questions of acceptance and rejection are often decided by juries, which are much less likely to base their decision on its effect in allocating burden of proof efficiently. Moreover, the acceptance-rejection fulcrum is not infinitely malleable. There are many cases in which acceptance is express or the conditions for rejection are indisputably met. In those cases, courts will not be able to allocate burden of proof as they see fit.

The most serious obstacle preventing courts from using the acceptance-rejection fulcrum to allocate burden of proof efficiently, however, is that the acceptance-rejection fulcrum not only determines which party bears the burden of proof, but also determines the parties' duties to salvage goods in failed transactions. In some cases, the optimal allocation of the burden of proof may not coincide with the optimal allocation of the parties' salvage duties. For example, suppose that the allocation of the burden of proof to the buyer in *Miron* was efficient, perhaps because of the difficulty the seller would have proving that events subsequent to tender caused the horse's injury.<sup>40</sup> Imagine, however, that the buyer was a nonmerchant, with no expertise in selling horses. In that case, the professional breeder arguably would be the most efficient reseller. If the *Miron* case matched these facts, the court would have been unable to achieve both an efficient allocation of the burden of proof (i.e., to the buyer) and an efficient allocation of the duty to resell the goods (i.e., to the seller). In order to allocate the burden of proof to the buyer, the court would have to find that the buyer accepted the goods, as the court in fact found in *Miron*. Once the court finds that the buyer has accepted and that the horse was conforming at tender, there would be no way to compel the seller to resell the horse. Sellers are entitled to the price of conforming goods accepted, and once sellers are held to be entitled to the price, they are thereby discharged from any obligation to resell the goods.<sup>41</sup> In this case, allocating the burden of proof to the buyer prevents the court from allocating the duty to resell to the seller, and vice versa. The court must forgo either the efficient allocation of the burden of proof or the efficient salvage of the goods.

But why should this dilemma arise? The trade-off of one efficiency goal against the other is entirely unnecessary. The lumping of the completely unrelated tasks of allocating burden of proof and allocating salvage responsibilities into the single task of determining whether acceptance or rejection occurred is simply an artifact of the English common law.<sup>42</sup> By

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40. This rationale for allocating burden of proof is discussed *infra* part I.B.3.

41. The seller has the right to the price of accepted goods under § 2-709(1)(a). For a discussion of this provision and the seller's salvage duties, see *infra* part II.D.

42. Section 2-607(4) of the U.C.C. adopts the same allocation of burden of proof provided in the Uniform Sales Act. The U.S.A. allocated the burden of proof to the buyer upon acceptance. See 1 SAMUEL WILLISTON, THE LAW GOVERNING SALES OF GOODS AT COMMON LAW AND UNDER THE UNIFORM SALES ACT § 255 (2d ed. 1924); see also U.S.A. § 255 stating that "if the buyer accepts delivery of the goods

decoupling the allocation of burden of proof from salvage rules, the Code will never force a judge to choose between the efficient allocation of burden of proof and the efficient allocation of salvage duties.

### B. *An Efficiency Analysis of the Code's Allocation of Burden of Proof*

My objective in the previous Section was to demonstrate the efficiency advantages of decoupling the rule for allocating burden of proof from the rules that governed salvage. The Code's burden-of-proof and salvage rules can be decoupled in two different ways: by abandoning the acceptance-rejection fulcrum entirely and replacing it with two new and distinct doctrines for allocating burden of proof and salvage duties, respectively, or by continuing to use the acceptance-rejection fulcrum for allocating either burden of proof or salvage duties, but not both. In this Section, I consider and reject the latter possibility. Thus, given the argument in the previous Section, Part I presents the case for the first half of this Article's overarching claim that burden-of-proof, salvage, and undercompensation rules should be decoupled from one another as well as from the acceptance-rejection fulcrum. It demonstrates that burden of proof should be decoupled not only from salvage rules, but from the acceptance-rejection fulcrum as well.

At least three efficiency rationales for allocating burden of proof have potential application in sales cases. Respectively, they recommend allocating the burden of proof to the party (1) with superior access to evidence, (2) who can create cost-effective evidence, and (3) who is most likely to be asserting a false claim. I argue that none of these rationales can explain or justify the Code's allocation of the burden of proof according to whether acceptance or rejection has taken place.<sup>43</sup> Instead, these rationales would support a rule

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other than for the mere purpose of explanation . . . [he] has the burden of establishing that the goods are not equal to sample . . . ." The U.S.A. reflected American common law, see ALPHONSE M. SQUILLANTE & JOHN R. FONSECA, 1 WILLISTON ON SALES § 7-3, at 219-20 (4th ed. 1973), and closely followed the English Sale of Goods Act of 1893, which codified the English common law of sales, see Zipporah Batshaw Wiseman, *The Limits of Vision: Karl Llewellyn and the Merchant Rules*, 100 HARV. L. REV. 465, 475 (1987). The definition of acceptance remained virtually identical from its origin in the English common law and Sale of Goods Act through its incorporation into the U.S.A. and the U.C.C. The definition of acceptance in U.C.C. § 2-606 is remarkably similar to the definition of acceptance in U.S.A. § 48, which is identical to the definition of acceptance in § 35 of the English Sale of Goods Act:

The buyer is deemed to have accepted the goods when he intimates to the seller that he has accepted them, or when the goods have been delivered to him, and he does any act in relation to them which is inconsistent with the ownership of the seller, or when after the lapse of a reasonable time, he retains the goods without intimating to the seller that he has rejected them

Sale of Goods Act of 1894, 56 & 57 Vict., ch. 71, § 35 (Eng.), reprinted in 2 WILLISTON, *supra*, at 1792

43. The three rationales I consider derive from three of the traditional rationales for allocating burden of proof presented and discussed in JOHN M. MAGUIRE, EVIDENCE 179 (1947) and STEPHEN C. YEAZELL ET AL., CIVIL PROCEDURE 772-74 (3d ed. 1992). The first, the "access-to-evidence" rationale, reflects the objectives underlying the practices of assigning the burden of proof to the party (1) who has superior access to relevant facts, and (2) to the defendant seeking to sustain an affirmative defense by relying on matters such as release, statute of limitations, discharge in bankruptcy, *res judicata*, or the like. Most instances in which a party seeks to sustain an affirmative defense are ones in which the defendant has greater access

shifting the burden of proof from seller to buyer upon tender. I conclude that the acceptance-rejection fulcrum should play no role in allocating burden of proof: the Code's burden-of-proof rules should be decoupled not only from salvage rules, but also from a version of the acceptance-rejection fulcrum that no longer allocates salvage duties, but is exclusively used to allocate burden of proof.

### 1. *The Access-to-Evidence Rationale for Allocating Burden of Proof*

The "access-to-evidence" rationale recommends allocating the burden of proof to the party with superior access to evidence. This traditional rationale can be defended on efficiency grounds. If one party has superior access to evidence, that party can more cheaply provide that evidence. Given that contractual parties share the goal of maximizing the joint value of their contract at the time of formation, they have an interest at the time of formation in cost-effectively increasing the likelihood that all breaches will be remedied with optimal compensation.<sup>44</sup> They would therefore seek to minimize the costs of accurate adjudication.<sup>45</sup> That goal would lead them to allocate the duty to produce evidence to the party able to produce it at least cost.

The strength of this rationale, however, has diminished since the advent of modern discovery law.<sup>46</sup> Any comparative advantage one party would

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to the evidence of whether the conditions for the defense are satisfied. The second, the "evidence-creation" rationale, is simply an economic variant on the access-to-evidence rationale. The third rationale, which assigns the burden to the party most likely to be asserting a false claim, underlies the traditional rationale of assigning the burden to the party asserting conduct that is out of the ordinary. The only reason to assign the burden to such a party is that the conduct alleged is less likely to have occurred because it is out of the ordinary. Thus, the burden is assigned to the party who is, all other things equal, most likely to be asserting a false claim.

I ignore the remaining practices of assigning the burden of proof to the party (1) who must plead a particular claim, (2) asserting a disfavored contention, e.g., defendant has to plead the truth of an allegedly defamatory statement, (3) attempting to change the status quo, and (4) alleging the wrongdoing. The first is inapplicable to sales law because the pleading rules affecting Article 2 have no apparent relationship to any plausible goal served by allocating the burden of proof. The second is likewise inapplicable because there is no reason to disfavor claims of breach that turn on the goods' nonconformity. The third and fourth approaches can be dismissed because they offer no efficiency-based rationale for allocating burden of proof. But they can also be dismissed because they are inapplicable to sales cases.

44. The joint maximization of contractual value requires that all cost-effective measures be taken to ensure that all breaches are optimally compensated. *See infra* note 84.

45. *Cf.* Louis Kaplow, *The Value of Accuracy in Adjudication: An Economic Analysis*, 23 J. LEGAL STUD. 307, 400 (1994) (arguing that "[a]ccuracy in determining liability affects deterrence and the costs of imposing sanctions").

46. *See, e.g.,* FLEMING JAMES JR. ET AL., *supra* note 22, § 7.16, at 344. According to the authors: Access to evidence is a much diminished basis for allocating burden of proof in modern liberal discovery. Whatever testimony is available from an opposing party ordinarily can be elicited through deposition before trial and be at hand for use in evidence. Also, in this era of reporting and recordkeeping, large amounts of relevant evidence are compiled in documents accessible by subpoena duces tecum and, in the case of public records, freedom of information laws. From this perspective, the critical element in allocation is not the burden of coming forward with the evidence but the burden of persuasion in the face of evidence of ambiguous significance.

*Id.*

otherwise have in gaining access to evidence is to a great extent reduced by the availability of discovery. Nonetheless, the access-to-evidence rationale might still explain why the Code's burden-of-proof rule is efficient.

In order to determine whether the Code's use of the acceptance-rejection fulcrum to allocate burden of proof can be defended on the ground that it allocates the burden to the party most likely to have access to evidence of whether a tender was conforming, we must first determine the kind of evidence that might be available to contractual parties. Then we can determine whether one party is more likely to have access to it than the other, and in turn, whether the Code's rule allocates the burden of proof to that party.

a. *Access to Evidence as Access to the Goods*

One promising example of evidence central to many sales disputes is the goods themselves. The party in possession of the goods presumably has easier access to them than the other party, and given that the goods are rarely in the possession of both parties simultaneously, one party typically will have superior access to them than the other. This rationale might explain the Code's burden-of-proof rules since it is plausible that buyers who have accepted the goods are typically in possession of them, and that sellers whose goods have been rejected are more often in possession of the goods than buyers who rejected the goods.

But this explanation for the Code's allocation of burden of proof is rather weak. First, the condition of the goods at some time following tender is likely to provide significant evidence of the conformity of the goods tendered only where a latent defect is alleged. In suits alleging patent defects, evidence of the condition of the goods long after tender provides only indirect evidence for the claim that the goods were nonconforming at the time of tender. The significance of such evidence is questionable and the importance of insuring that such evidence is brought forward by the party able to do so at least cost is less significant as well. Second, any party who denied the other access to the goods following a claim of breach would be acting in bad faith<sup>47</sup> and contravening the Code's express requirement to provide access to goods subject to dispute.<sup>48</sup> Moreover, such a denial would undermine that party's credibility before the trier of fact. Thus, although the party in possession of the goods has superior access to them in principle, both parties have the same

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47. Such conduct would likely violate the party's obligation of good faith created by § 1-203

48. U.C.C. § 2-515 states that "[i]n furtherance of the adjustment of any claim or dispute (a) either party . . . for the purpose of ascertaining the facts and preserving evidence has the right to inspect, test and sample the goods including such of them as may be in the possession or control of the other . . ." *Id.* § 2-515(a). In addition, the first buyer's right to discovery gives her the right of access to the goods in the second buyer's possession. *See* FED. R. CIV. P. 34(a), 26(a)(1)(B). Finally, a buyer who denied a seller access to goods following an allegation of breach might violate the seller's right to cure under § 2-508



access to the goods in practice. Third, suppose that notwithstanding the above criticisms, the burden of proof should be allocated to the party with superior access to the goods and that the party in possession of the goods is most likely to have such access. In that case, the Code's rule allocating burden of proof according to acceptance and rejection would be inferior to a rule that simply assigns the burden of proof to the party in possession of the goods when the breach is alleged. Not all sellers of rejected goods and buyers of accepted goods have possession when breach is alleged. The possession rule would allow both the parties and the court to determine who bears the burden of proof without the administrative and error costs of assigning it according to rejection and acceptance. There is no need to use the acceptance-rejection fulcrum as a proxy for possession when possession can be even more easily and accurately determined than rejection and acceptance.<sup>49</sup>

b. *Access to Evidence as Access to Inspection Evidence*

The rationale of allocating the burden of proof to the party with superior access to the goods is most plausible for cases in which a latent defect is alleged. If the defect alleged is patent, the contested issue will be whether the defect existed at the time of tender. The most relevant evidence on the question of patent conformity at the time of tender would be evidence revealed by an inspection at that time, not evidence of the condition of the goods following tender. We might therefore reinterpret the access-to-evidence rationale in sales cases as requiring that the burden of proof be allocated to the party with superior access to the evidence provided by inspection at the time of tender. If there were an inspection at the time of tender, would one party have superior access to the results of that inspection? Perhaps in some cases only the party who conducted or arranged for the inspection would know the identities of persons who made or witnessed the inspection, documents produced by the inspection, and the like. Of course, this is precisely the sort of information that is readily available through discovery. Any advantage the party who directed the inspection might have in gaining access to inspection-related evidence would be largely eliminated by the opposing party's access to that evidence through discovery. But notwithstanding the prospect of discovery, suppose we thought that one party nonetheless had systematically and significantly lower costs of gaining access to inspection-related evidence,

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49. If neither party has possession of the goods, the access-to-evidence rationale would suggest that control of the goods should be the criterion for assigning the burden of proof. Thus, the seller who retains control over goods in transit would bear the burden of proof, and the buyer who ships goods to third parties and subsequently alleges their nonconformity would bear the burden of proving nonconformities because she would have a right of access to the goods in *her* buyer's possession. That right is attendant to the buyer's right to cure and is expressly provided by the broad right of access granted by § 2-515 and by discovery rules, at least in cases governed by the federal rules of discovery. *See supra* note 48.

sufficient to justify allocating the burden of proof to that party. Is it plausible that one party's access to inspection-related evidence explains the Code's burden-of-proof rule? Unfortunately, the answer is no.

The reason is that the party most likely to have superior access to inspection-related evidence is the party most likely to have conducted an inspection at the time of tender. The Code's rule shifts the burden of proof from sellers of rejected goods to buyers of accepted goods. Therefore, the Code's burden-of-proof rule allocates the burden of proof to the party with superior access to inspection-related evidence only if sellers of rejected goods and buyers of accepted goods have superior access to inspection-related evidence. But buyers are more likely than sellers to have conducted an inspection at the time of tender, irrespective of whether rejection or acceptance has taken place. First, and most important, the Code provides that "the buyer must within a reasonable time after he discovers or should have discovered any breach notify the seller of breach or be barred from any remedy."<sup>50</sup> Therefore, if a buyer fails to inspect the goods, she will be unable to recover for any nonconformities that a seasonable<sup>51</sup> and reasonable inspection would have revealed because she would not have been able to provide the seller with the required seasonable notice of the breach. Second, the Code precludes buyers from relying on a defect ascertainable by reasonable inspection to justify rejection or to establish breach if the buyer fails to state that defect upon rejection and (1) the seller might have cured the defects, or (2) if between merchants, the seller after rejection has made a request in writing for a statement of the defects on which the buyer proposes to rely.<sup>52</sup> Thus, the buyer's failure to inspect exposes her to the risk of being barred from using subsequently discovered defects to prove breach in certain cases. Third, apart from Code provisions, it is almost always in the buyer's interest, irrespective of who bears the burden of proof, to discover and notify the seller of defects seasonably.<sup>53</sup> The more time that elapses between the buyer's receipt of the goods and the buyer's allegation of breach, the higher the probability that any

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50. U.C.C. § 2-607(3)(a).

51. If the inspection was delayed and therefore unseasonable, the seller can argue that any defects revealed by such an inspection should have been discovered earlier and that they thus fall under the remedy bar of § 2-607(3)(a). In addition, if the buyer has an incentive to conduct a reasonable inspection of the goods, it is to her advantage to conduct such an inspection seasonably in order to be able to reject the goods and thus, *inter alia*, avoid bearing the burden of proof.

52. *Id.* § 2-605(1).

53. Although the buyer will never have an incentive to delay inspection of the goods, there is one reason she might intentionally delay notifying the seller of defects discovered by that inspection. If she unreasonably (and presumably unintentionally) delayed inspection following tender, and thereby is held to have accepted under § 2-606(1)(b), she might hope to represent the defects as latent and therefore not discoverable by a seasonable and reasonable inspection. This strategy would allow her to escape the consequences of failure to seasonably notify the seller of breach under § 2-607(3)(a) and failure to particularize under § 2-605. Moreover, it would allow her to revoke her acceptance instead of suing for damages as a buyer of accepted goods. For discussion of the revocation doctrine, see *infra* text accompanying notes 116-28 in Part II.D.

defects in the goods reported subsequent to delivery have been caused by events subsequent to delivery for which the seller bears no responsibility. The smaller the interval of time between receipt of goods and notification of defects, the stronger the buyer's claim that the defect existed at the time of tender. From a purely evidentiary perspective, then, the buyer has a considerable incentive to undertake an inspection of the goods at the time of delivery. All three of these reasons suggest that buyers are more likely than sellers to conduct inspections at the time of tender. In most cases where goods have been tendered, buyers will have conducted an inspection and therefore will have superior access to inspection-related evidence, irrespective of whether they have accepted or rejected the goods. Therefore, if we interpret the access-to-evidence rationale as requiring the allocation of burden of proof in sales cases to the party with superior access to inspection-related evidence, the Code should allocate the burden of proof to buyers following tender. By allocating the burden of proof to sellers of rejected goods, the Code's rule conflicts with the requirements of this access-to-evidence rationale.

2. *Allocating Burden of Proof to the Cheapest Producer of Cost-Effective Evidence*

The second rationale for allocating burden of proof, related to the access-to-evidence rationale, is to provide the party best able to create cost-effective evidence with the incentive to do so. By assigning one party the burden of proof at the beginning of a transaction, that party will have the incentive to take measures to ensure the existence of evidence of facts he or she may need to prove in court. Given the parties' goal of efficiently minimizing the costs of accurate adjudication, they might use the allocation of the burden of proof to create an incentive for the party best able to produce cost-effective evidence to do so. For example, allocating the burden of proof to the buyer might provide her with sufficient incentive to ensure a credible inspection at the time of tender. If it is cost-effective, the buyer will secure a third-party inspection acceptable to the seller in order to buttress her ability to prove nonconformity at the time of tender should the need arise. Similarly, allocating this burden to the seller might provide him with the incentive to take all cost-justified measures to ensure the creation of evidence to prove the state of the goods at the time of tender. The optimal default rule for assigning the burden of proof would therefore allocate the burden to the party who can cost-effectively produce the evidence most likely to lead to effective adjudication.

Because an inspection at the time of tender is the single most valuable piece of evidence of patent defects at the time of tender, the burden of proof should be assigned to the party who is the most efficient provider of inspections. Given that both parties are able to arrange for inspections at the time of tender, it is tempting to conclude that merely assigning the burden of

proof to one party or the other will lead to the desired inspection. But parties might systematically face different costs for inspections. One party might be the most efficient provider of inspections because it might be more costly to arrange a long-distance inspection than a local one. Thus, the party able to secure the most efficient inspection at tender is likely to be the party whose place of business is the place of tender.<sup>54</sup>

One might doubt that the burden of proof should be allocated so as to provide the most efficient producer of cost-effective evidence with an incentive to produce such evidence.<sup>55</sup> But apart from its own merits, this rationale cannot provide a justification for the Code's allocation of the burden of proof. First, the Code's allocation does not even approximate an assignment of the burden of proof to the party whose place of business is the place of tender. There is no correlation between tender at seller's place of business and rejection of goods, or tender at buyer's place of business and acceptance of goods. In any case, if ability to produce evidence were the sole criterion for ensuring the optimal allocation of the burden of proof, there would be little need for a doctrinal proxy. Simply adopting a rule that allocates the burden of proof to the party whose place of business is the place of tender would achieve the desired result directly. It would motivate the party able to secure the cost-

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54. Recall *Miron v. Yonkers Raceway, Inc.*, 400 F.2d 112 (2d Cir. 1968), in which the court held that the buyer of a racehorse at an auction who failed to inspect the horse upon tender had accepted the horse and thus bore the burden of proving the horse was lame at the time of tender. Schwartz and Scott suggest that

*Miron* is consistent with the goal of minimizing the costs of breach. In *Miron*, much of the loss sustained by both parties, including the sunk costs of litigation, was caused by uncertainty as to whether the horse was lame when sold. As the party better able to have avoided that uncertainty *ex ante*, [the buyer] should bear the loss, and *Miron* appropriately provides incentives for future buyers to inspect goods as soon as it is cost-effective to do so

ALAN SCHWARTZ & ROBERT E. SCOTT, COMMERCIAL TRANSACTIONS 270 (2d ed. 1991) But this argument fails to demonstrate that the buyer had the comparative advantage at securing an inspection at the time of tender. Had *Miron* found that the buyer had rejected, and thus assigned the burden of proof to the seller, future sellers would have the incentive to obtain a third-party inspection or to insist on the buyer's inspection at the time of tender. The goal of ensuring that one party or the other has the incentive to secure an inspection at tender cannot provide a reason for allocating the burden of proof, for any allocation will accomplish that goal. Instead, the focus must be on which party is able to secure the inspection at least cost. My claim is that the party whose place of business is the place of tender is likely to be the least-cost provider of such an inspection. In *Miron*, tender did not take place at the buyer's place of business, rather, it took place at the seller's auction. Either the seller had the comparative advantage of inspecting at tender or neither had a comparative advantage. In any event, the claim that the buyer had the comparative advantage at inspecting, and that therefore *Miron* was correctly decided for that reason, is unfounded

55. Moreover, allocating the burden of proof to the least-cost provider of cost-effective inspections would not lead that party to take all cost-justified measures to document the actual condition of the goods at tender. Allocating the burden of proof to a party only provides him with an incentive to create evidence likely to persuade a trier of fact that his subsequent allegation of breach is credible. Thus, a buyer who bears the burden of proof would want an inspection that appears objective but is in fact intended to lead to proof of nonconformity to preserve the buyer's option to allege breach. And a seller bearing the burden of proof would want an apparently objective inspection that in reality assured a finding of conformity. An allocation of the burden of proof will provide a party with an incentive to ensure the existence of evidence likely to reveal the truth only if either he believes the truth is likely to favor his possible claim of breach, or the expected benefits of biased evidence, because less credible, are less than the expected benefits of unbiased evidence, despite the possibility that such evidence will undermine his possible claim of breach

effective inspection that is most likely to constitute the best evidence of the good's condition at the time of tender to secure such an inspection. And it is a rule that is simple and comparatively easy to administer.

But even the rule allocating the burden of proof to the party whose place of business is the place of tender is unlikely to induce the most efficient inspector to inspect if the seller is the most efficient inspector. As long as the Code bars buyers from recovery for any nonconformity that would have been revealed by a reasonable and seasonable inspection, shifting the burden of proof to the seller when tender is at his place of business will not shift the incentive to conduct an inspection from the buyer to the seller. The buyer will still have an overriding incentive to conduct inspections and the seller will know this. Notwithstanding a rule allocating the burden of proof to the seller whenever tender is at the seller's place of business, the strong likelihood that the buyer will conduct the inspection anyway will diminish the seller's incentive to inspect in such cases.

### 3. *Allocating Burden of Proof Against the Party Likely To Be Asserting a False Claim*

The third rationale for allocating the burden of proof is to assign it to the party most likely to be asserting a false claim.<sup>56</sup> Like the access-to-evidence and evidence-production rationales considered above, this rationale seeks cost-effectively to increase the likelihood of accurate adjudication. If particular kinds of claims are known to be probably false, then assigning the burden of proof to the party asserting such claims might increase the accuracy of adjudication. Whatever reasons justify the *ex ante* belief that the sort of claim being advanced is probably false would also justify a rebuttable legal presumption that the claim is false. The allocation of the burden of proof to the party asserting such a claim creates that presumption. As a result, the party most likely to be correct will be more likely to prevail.

This rationale would explain the Code's allocation of the burden of proof if the fact that a buyer has rejected goods makes it more probable than not that the goods are nonconforming, and if the fact that a buyer has accepted goods makes it more probable than not that the goods are conforming. However, assuming that most buyers act in good faith and make reasonable inspections at tender, those who reject goods must believe the goods to be nonconforming. Similarly, assuming that most buyers do not want nonconforming goods, most buyers who accept goods believe the goods to be conforming when they accept them. In the vast majority of cases, then, when a buyer rejects goods, the

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56. This rationale seems to underlie the practice of assigning the burden of proof to the party asserting conduct that is out of the ordinary. If conduct alleged is out of the ordinary, then it is by definition less than probable.

goods are nonconforming and the seller will concede this fact; and when a buyer accepts goods, the goods are conforming and the buyer will concede this fact. But it does not follow that in those cases in which the parties dispute conformity at tender, the fact of rejection makes nonconformity more likely than not and the fact of acceptance makes conformity more likely than not.

When the buyer rejects goods and the seller claims the goods were conforming, there is no reason to believe the seller is probably wrong. Both the buyer's and the seller's claims could be wrong because they are either innocently mistaken or strategically lying. There is no reason to believe that when goods are rejected, buyers are less likely than sellers to be mistaken about the condition of the goods<sup>57</sup> or less likely to be acting in bad faith. Similarly, when the buyer accepts the goods and then asserts their nonconformity, there is no reason to believe the buyer is probably wrong. First, suppose the accepting buyer alleges a patent defect, which we can define as a nonconformity that would have been detected by a reasonable and seasonable inspection at tender. The buyer's allegation of a patent defect can be explained by good faith or bad faith stories. One good faith story is that the goods were nonconforming at tender and, even though the buyer accepted the goods, she either failed to inspect the goods before acceptance<sup>58</sup> or inspected them but failed to detect their nonconformity. Another good faith story is that the goods were conforming, but because the buyer failed to inspect or inadequately inspected the goods, she subsequently came to the mistaken conclusion that the goods were nonconforming at tender. The bad faith story is that the buyer

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57. If the physical presence or absence of a party at an inspection decreases the probability of that party being mistaken about the condition of goods at tender, then sellers are less likely than buyers to be mistaken about the condition of goods at tender in contracts requiring carriage of goods. In contracts requiring carriage of goods, the parties probably will not jointly inspect the goods. In shipment contracts, in which tender takes place when the seller duly delivers goods to the carrier, *see* U.C.C. §§ 2-319(1)(a), 2-504, 2-503(2), it would be unusual for the buyer to be present at tender. Thus, if there is an inspection at tender, the seller will be more likely than the buyer to be present at the inspection and will be less likely than the buyer to be mistaken about the condition of the goods at tender. On the other hand, in destination contracts, in which the contract requires shipment and tender takes place at the buyer's place of business, *see id.* §§ 2-319(1)(b), 2-503(3), the seller is less likely to be present at an inspection at tender. Thus, if there is an inspection at tender, the buyer will be less likely than the seller to be mistaken about the condition of the goods at tender. Although it is difficult to know which of these kinds of contracts are more common, the Code's rule presuming that contracts requiring carriage of goods are shipment rather than destination contracts, *see id.* § 2-503 cmt. 5, might indicate that the shipment contract is more common. Moreover, in destination contracts, the seller is more likely to negotiate a contractual provision specifying that inspection is to take place at the point of shipment and will be exclusive. *See generally id.* § 2-513(4), *Bartlett & Co., Grain v. Merchants Co.*, 323 F.2d 501 (5th Cir. 1963) (holding that where parties agreed to inspection at selling point, that inspection is conclusive). Thus, even in destination contracts, we might expect sellers more often than buyers to be present at the controlling inspection. The rationale of assigning the burden of proof to the party most likely to be mistaken about the good's condition, then, would assign the burden of proof to the buyer in contracts requiring carriage of goods. Of course, this rationale cannot explain or justify the Code's burden-of-proof rule. The Code's rule makes no distinction between contracts requiring carriage of goods and other contracts, and allocates the burden to the seller of rejected goods.

58. The buyer might have intentionally accepted without inspecting or might have intended to inspect but been found by a court to have constructively accepted either by failing to reject and waiting too long to inspect under §§ 2-602(1) and 2-606(1)(b), respectively, or by acting inconsistently with the seller's ownership of the goods under § 2-606(1)(c).

regrets the contract and is lying in order to escape liability. There is no reason to believe that the first good faith story, in which the accepting buyer's allegation of a patent defect is true, is less common than the other stories, in which the allegation is false. However, even if the accepting buyer's allegations of patent defects were more likely than not to be false, there would be little point in assigning such a buyer the burden of proof. Under the Code, an accepting buyer who fails to notify a seller of a defect that should have been detected by a reasonable and seasonable inspection is barred from recovery, regardless of who bears the burden of proof.<sup>59</sup>

Now suppose an accepting buyer alleges a latent defect, which we can define as a nonconformity that would not have been revealed by a reasonable and seasonable inspection at tender. Again, there are both good and bad faith stories to explain the buyer's allegation. One good faith story is that the goods were latently nonconforming at tender and that the nonconformity became apparent only after acceptance. Another good faith story is that the goods were conforming at tender but, unbeknownst to the buyer, were damaged subsequent to acceptance by the buyer's negligence or by accident. The buyer then in good faith falsely alleges the goods were latently nonconforming at tender. The bad faith story is that the accepted goods were conforming at tender but the buyer subsequently regrets the contract, either because the goods were damaged after acceptance or because the contract is otherwise less profitable than she expected. The buyer then knowingly makes the false allegation that the goods were latently nonconforming at tender. There is no reason to believe that the first good faith story, in which the buyer's claim is true, is less common than the two other stories, in which the buyer's claim is false. It is true that the probability that the goods were damaged by the buyer increases the longer the buyer has possession of the goods. But the probability that the nonconformity of a good was caused by a latent defect is independent of the probability that the nonconformity was caused by some event following acceptance. Thus, the accepting buyer's allegation of a latent defect is probably false only if the probability of a nonconformity resulting from intervening events and not from a latent defect is greater than fifty percent. There is no reason to believe this will be the case, however. The mere fact that the buyer has accepted the goods therefore provides no reason for believing the buyer's allegation of a latent defect is false.

#### 4. *Summary*

I have considered three economic rationales for allocating the burden of proof in sales cases and have argued that each fails to provide a justification for the Code's burden-of-proof rule. The first is the access-to-evidence

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59. U.C.C. § 2-607(3)(a).

rationale. The first interpretation of the access-to-evidence rationale suggests allocating the burden of proof to the party who has possession of the goods when breach is alleged because that party will have superior access to the goods as evidence. The Code's burden-of-proof rule does not achieve the allocation suggested by this version of the access-to-evidence rationale because acceptance and rejection at best serve as rough proxies for possession at the time breach is alleged. Such a proxy is inferior to a direct possession rule that avoids the costs of administering an indirect proxy and increases the likelihood that the burden will be assigned to the party who has possession.

The second interpretation of the access-to-evidence rationale suggests allocating the burden of proof to buyers following tender because they are most likely to have conducted an inspection and therefore will have superior access to inspection-related evidence. The Code fails to achieve this allocation because it assigns the burden of proof to sellers of rejected goods. The Code therefore sometimes places the burden of proof on sellers following tender. Yet buyers are more likely to have superior access to inspection-related evidence.

The second rationale calls for allocating the burden of proof to the cheapest producer of cost-effective evidence. According to this rationale, the burden of proof should be allocated to the party whose place of business is the place of tender because that party is likely to be able to conduct the cheapest, most cost-effective inspection. The Code does not achieve this allocation either, because there is no reason to believe that sellers of rejected goods and buyers of accepted goods will more often be the parties whose place of business is the place of tender. Moreover, because of buyers' overriding incentives to conduct inspections even when they do not bear the burden of proof, the burden-of-proof rule is unlikely to achieve the incentive effects contemplated by the "efficient evidence-creation" rationale.

The third rationale would allocate the burden of proof to the party most likely to be asserting a false claim. Although I did not describe the burden-of-proof rule this rationale would support in sales cases, I have argued that it cannot explain the Code's rule. There is no reason to believe that, in general, the seller's claim that rejected goods are conforming and the buyer's claim that accepted goods are nonconforming are probably false. In the final analysis, none of the available economic rationales for allocating burden of proof in sales cases provides an explanation of or justification for the Code's current regime.

What is the best rule to substitute in place of the Code's burden-of-proof rule? The rationale of assigning the burden to the party likely to be asserting a false claim has no obvious application in sales cases, and is misguided. Only the "access-to-evidence" rationale remains. Therefore, the choice is between the two rules suggested by the two different interpretations of the "access-to-evidence" rationale: the "access-to-the goods" rule, which requires the party in possession to bear the burden, and the "access-to-inspection-evidence" rule,



which requires the buyer to bear the burden following tender. In the absence of empirical data, it is difficult to choose between them; fortunately, they are likely to converge in most cases. Whenever the buyer alleges nonconformity, the allegation is likely to be made after tender and after the buyer has taken possession of the goods. I would therefore support a rule allocating the burden of proof to the buyer upon tender.

### C. *Conclusion*

The Code uses the acceptance-rejection fulcrum to allocate the burden of proof, to allocate salvage duties, and to reduce undercompensation. My objective is to demonstrate that the rules that serve these three functions should be decoupled from one another and from the acceptance-rejection fulcrum as well. In this Part, I have accomplished the first half of this objective. First, I argued that the burden-of-proof rule should be decoupled from the salvage rules. Second, I argued that the burden-of-proof rule should be decoupled from the acceptance-rejection fulcrum, even if the acceptance-rejection fulcrum were decoupled from the salvage rules and served exclusively to allocate the burden of proof. In the remainder of this Article, I argue for decoupling salvage from undercompensation rules and decoupling both from the acceptance-rejection fulcrum.

## II. REGULATING THE SALVAGE OF FAILED TRANSACTIONS: THE CODE'S SALVAGE REGIME

The case for decoupling the Code's salvage regime from the acceptance-rejection fulcrum emerges from consideration of the strongest argument in the Code's defense. That argument derives from a standard economic story that can explain how the Code's salvage regime advances the goal of maximizing the joint value of contracts. According to this story, the Code usually provides the party who is the most efficient salvor with the incentive to salvage goods in failed transactions. In some cases, however, the Code allows the most efficient salvor to avoid salvaging the goods. The story explains that the Code's treatment of the latter can be defended as a means of reducing the nonbreacher's exposure to the systematic risk of undercompensation in contracts. Given that this risk leads to deadweight losses, contractual default rules that reduce it thereby reduce the deadweight losses in contracts. The gains achieved by reducing such deadweight losses are, the story goes, greater than the losses caused by exempting the most efficient salvor from the duty to salvage goods in failed transactions. The story concludes that the Code's salvage regime contributes to the goal of maximizing the joint value of contracts, in some cases by providing incentives for the most efficient salvor to salvage goods, and in other cases by relieving the nonbreacher of the duty

to salvage, even when he is the most efficient salvor, in order to reduce his risk of undercompensation.

By presenting and evaluating this “efficiency trade-off” story, I show that the Code’s salvage regime should be replaced with one that addresses the goals of efficient salvage and reduced undercompensation with independent doctrines. In this Part, I provide a formal presentation of the efficiency trade-off story that explains precisely how the Code’s salvage regime might be defended as advancing the goal of joint maximization. In Section A, I explain how combining the common law mitigation rule with the Code’s specific salvage provisions defines the Code’s salvage regime. In Section B, I describe the problem of systematic undercompensation in contracts and illustrate the familiar trade-off strategy of seeking to reduce this risk by exempting the nonbreacher from certain mitigation responsibilities. In Sections C and D, I demonstrate that the Code’s salvage regime conforms to the efficiency trade-off story so long as the parties can determine their salvage duties with reasonable certainty at the time they must make their salvage decisions. Together, Sections A through D provide the strongest efficiency defense of the Code’s salvage regime.

In turn, I make two objections to the defense of the Code’s salvage regime provided by the efficiency trade-off story. Both objections turn on empirical questions. The first objection is that the Code’s regime is unlikely to achieve the results envisioned by the efficiency trade-off story. In Section E, I demonstrate that the Code will fail to achieve the results contemplated by the efficiency trade-off story whenever the parties, at the time of their salvage decision, have difficulty determining whether acceptance, rejection, or revocation occurred and whether the buyer or seller is the breacher. I argue that parties will have such difficulty in a sufficiently large number of cases so as to call into question the claim that the Code achieves the results contemplated by the efficiency trade-off story.

The second and more fundamental objection to the efficiency trade-off story takes issue with the premise that the efficiency of the salvage of goods should be compromised in order to reduce the nonbreacher’s risk of undercompensation. In Part III, I argue that the Code’s trade-off between efficient salvage and reduced undercompensation is no more necessary than the trade-off between the efficient allocation of the burden of proof and the efficient allocation of salvage duties, a trade-off I rejected in Part I.

#### A. *The Code’s Salvage Regime*

One of the most important roles played by the acceptance-rejection fulcrum is the regulation of failed transactions. A successfully completed transaction is one in which the seller fulfills his obligation to tender conforming goods by the contract deadline and the buyer fulfills her obligation

to pay for them when payment is due under the contract.<sup>60</sup> A transaction fails when one party breaches or when a “regret contingency” occurs: that is, an event that causes one party to regret entering into the agreement.<sup>61</sup> If the regret contingency occurs before the successful completion of the transaction, it may lead one party to breach the agreement.<sup>62</sup> A party can breach either by failing to perform or by anticipatorily repudiating the contract. If most parties want to maximize the expected joint value of their contract, then majoritarian default rule analysis<sup>63</sup> would suggest that the rules governing the regulation of failed transactions ought to be those that reduce the parties’ expected joint costs of a failed transaction.<sup>64</sup> I will refer to the goal of minimizing the joint costs of a failed transaction as the goal of efficiently “salvaging the transaction.”

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60. Under § 2-607(1), payment is due when the buyer accepts the goods. Therefore, a successfully completed transaction under the Code is one in which the seller tenders conforming goods on time and the buyer accepts and pays for them on time.

61. Goetz and Scott coined the term “regret contingency.” See Goetz & Scott, *Enforcing Promises*, *supra* note 9, at 1273. In the context of mitigation, they substitute the term “readjustment contingency.” See Goetz & Scott, *The Mitigation Principle*, *supra* note 9, at 972–73 n.15. They define “regret contingency” as “the future occurrence of an event or condition that would motivate the promisor to breach the contract if breach were costless. Such an occurrence implies that either the promisor or promisee must bear a cost.” *Id.*

62. Even if no regret contingency occurs a party might breach unintentionally, for example, by mistakenly tendering nonconforming goods.

63. See *supra* note 19.

64. In their seminal article, Goetz and Scott argue that “the contractual obligee and obligor would agree in advance to minimize the joint costs of adjusting to prospective contingencies, assigning the responsibility of mitigating to whoever is better able to adjust to the changed conditions.” Goetz & Scott, *The Mitigation Principle*, *supra* note 9, at 971. This loss-minimization principle is entailed by their more general joint maximization principle: that rational parties would want to maximize the joint net expected value of their contract at the time of formation. In theory, the loss-minimization principle would require contractual partners to agree to undertake efficient, joint loss-reducing activity even if a regret contingency occurs after a contract has been successfully completed. Rational parties would agree that even after the buyer has paid for conforming goods tendered by the seller, each party can require the other to take cost-effective measures to reduce the joint losses if any regret contingency materializes following the completion of a successful transaction. Thus, if the seller regrets the sale, he ought to be able to enlist the buyer’s aid in reducing his losses. If the seller has a higher valued use than the buyer’s use, he should have a right to reclaim the goods and pay damages even after the transaction has been successfully completed. Similarly, if the buyer regrets the sale, she should have a right to revoke acceptance and pay damages.

Such a contract would require the parties perpetually to “stand ready” to undertake whatever joint loss-reducing activity might be required in the event that one party comes to regret the successfully completed transaction in the future. The expected gains from the mutual right to enlist loss-reduction assistance in perpetuity from a contractual partner, however, are outweighed by the expected costs to each party of forever bearing the risk of adjustment. At some point following the successful completion of the contract, the marginal costs of standing ready exceed the expected benefits of more efficient loss reduction. Therefore, contracting parties might agree to some limit on their exposure to the risk of participating in joint loss-reduction. The Code limits parties’ exposure to this risk by terminating their mutual obligation to reduce the joint costs of a regret contingency upon the successful completion of the transaction. Once conforming goods have been tendered and paid for, the parties have no further contractual obligations to each other. Although the successful completion of a contract almost certainly does not mark the point at which the marginal costs and benefits of a mutual loss-reduction obligation are equal, it provides a salient and relatively clear point at which to limit the parties’ risk of adjustment. Note, however, that even this limitation requires the seller to stand ready, in perpetuity, to participate in joint loss reduction when goods tendered turn out to be nonconforming. The buyer’s right of revocation requires the seller to participate in salvaging the transaction irrespective of the time between tender and the buyer’s rightful revocation. The seller’s risk, however, decreases significantly as that time interval increases.

The classic doctrine designed to promote the efficient salvage of failed transactions is the common law mitigation rule. It bars nonbreachers from recovering any losses resulting from breach that they might reasonably have avoided.<sup>65</sup> According to economic analysis, a loss is reasonably avoidable if it could have been cost-effectively avoided.<sup>66</sup> If a nonbreacher fails to take cost-justified measures to reduce his losses from breach, he fails to reduce the joint costs of breach efficiently. The goal of efficiently salvaging failed transactions thus yields the mitigation rule.

The mitigation rule does not, however, suffice to ensure that the nonbreacher will be required to undertake all those activities necessary to salvage a failed transaction efficiently. In particular, there is one important activity that nonbreachers may need to undertake to salvage a failed transaction efficiently, although the common law duty to mitigate damages does not always require it.<sup>67</sup> Whenever goods are identified to the contract underlying a failed transaction, the efficient salvage of the transaction requires what I will call the "efficient salvage of the goods," which requires the parties to maximize the value of the goods. As an initial matter, this value maximization requires that the parties at least take cost-effective measures to prevent any diminution in the goods' value, for example, by not allowing perishable goods to rot. It may also require affirmative steps such as reselling the goods or making adjustments to use nonconforming goods. The efficient salvage of goods thus requires a comparison between the value of the goods if resold and their value if used by one of the parties. If one party has a comparative advantage at *reselling*, the expected value of that party's resale of the goods is the "maximum net resale value." If one party has a comparative advantage in *using* the goods, for example by virtue of a superior capacity to adjust a factory to utilize nonconforming goods, that party's expected value of use is the "maximum net use value" and should be compared to the maximum net resale value. The larger of these two values determines the optimal salvage value of the goods. The efficient salvage of the goods, then, requires some

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65. The common law mitigation rule provides the breacher with a defense to the nonbreacher's claim for damages, rather than providing the breacher with an affirmative right of action. See *Rock v. Vandine*, 189 P. 157 (Kan. 1920); JUDSON A. CRANE, *CASES ON DAMAGES* 102 n.1 (1928); CHARLES T. MCCORMICK, *HANDBOOK ON THE LAW OF DAMAGES* § 33, at 128 (1935); E. Allan Farnsworth, *Legal Remedies for Breach of Contract*, 70 COLUM. L. REV. 1145, 1184 (1970).

66. Most courts have generally adopted the economic construction of "reasonable." See Goetz & Scott, *The Mitigation Principle*, *supra* note 9, at 973-74 & n.19.

67. "Cover" is another activity sometimes required to salvage a failed transaction efficiently, but not always required by the duty to mitigate damages. Whenever a seller breaches, the buyer must effect any cost-effective substitute or "cover" transaction to mitigate her damages. Even when the buyer breaches, however, the efficient salvage of the transaction may, at least in principle, require the seller to undertake a "cover" transaction on the buyer's behalf. That is, if the seller's costs of effecting the breaching buyer's substitute transaction are less than the buyer's costs, the joint reduction of the costs of breach requires the seller to make the purchase on the buyer's behalf and seek reimbursement from her. For an analysis of the conditions under which efficient "cover" transactions will be required by mitigation and when they will not, see *infra* note 77.

party either to use the goods notwithstanding their possible nonconformity, or to resell them at least cost to realize their highest value. The optimal alternative is the one that yields the greatest net expected value for the goods. Thus, in addition to requiring the nonbreacher cost-effectively to minimize his own damages by mitigating his losses, thereby reducing the breacher's cost of compensation, the efficient salvage of a failed transaction may also require the nonbreacher to take action to minimize the costs the breacher sustains other than those the breacher incurs in compensating the nonbreacher. The goal of efficiently salvaging the transaction may require the nonbreacher not only to mitigate his own losses but to "mitigate" the breacher's losses by salvaging the breacher's goods.

If the parties are not required by contract to undertake the efficient salvage of goods in a failed transaction, they nonetheless may bargain *ex post* for that result. Because *ex post* bargains can be costly, however, the optimal contract will be one that requires the efficient salvage of goods.<sup>68</sup> Whether or not the common law mitigation rule will force the buyer to salvage nonconforming goods depends on whether she has accepted or rejected<sup>69</sup> the goods. If a buyer accepts nonconforming goods, the mitigation rule prevents her from recovering losses she could have cost-effectively avoided. As a result, if the buyer inefficiently salvages the goods by, for example, incorporating them instead of reselling them when the latter would have obviously maximized their value and minimized buyer's loss, the buyer will be unable to recover her losses attributable to that inefficient salvage decision. If the accepting buyer determines that the most efficient salvage of the nonconforming goods is for the seller to use or resell the goods, she has no power to compel the seller to salvage them.<sup>70</sup> But if the seller's use or resale is the most efficient alternative for salvaging the goods, he ordinarily might cooperate with the buyer and salvage the goods in order to reduce his own costs of breach.<sup>71</sup> If a buyer rejects a nonconforming tender, however, the mitigation rule cannot provide her incentive to salvage the goods. The salvage of the goods will

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68. I explicitly consider the possibility of *ex post* bargains in note 78 and accompanying text, and in Part II.C. The present analysis is designed to uncover the extent to which the common law and Code's default rules impute efficient salvage terms into contracts *ex ante*.

69. Unless otherwise stated, for purposes of the analysis that follows I assume that the buyer's rejection leaves the seller no right to cure. If the seller does have the right to cure, the transaction need not fail and the need to salvage the goods may not arise. This assumption is not essential to the analysis in the text, however. See *infra* text preceding note 72.

70. However, she might attempt to revoke her acceptance in order to compel the seller to salvage the goods.

71. This conclusion ignores the possibility that the seller might anticipate the likelihood of undercompensating the buyer's incidental costs of salvage. It is possible that the expected gains of undercompensating the buyer's incidental expenses would exceed the expected gains of undertaking the least costly salvage of the goods. In that event, a strategically breaching seller might refuse to salvage nonconforming, accepted goods even if he is the least-cost salvor. The same reasoning applies to a breaching buyer who wrongfully rejects or, if possible, wrongfully revokes even though she is the more efficient salvor. See *infra* text accompanying note 124.

affect the seller's losses but not the buyer's. As a result, the buyer's failure to salvage the goods will not constitute a failure to mitigate her damages under the common law mitigation rule. The mitigation rule requires only that the nonbreacher cost-effectively reduce his damage bill, not that he take every cost-effective measure to reduce the joint costs of breach. Thus, even when the most efficient salvage of nonconforming goods in a failed transaction is for the buyer to resell or use the goods, she is nonetheless free to reject the goods<sup>72</sup> and therefore cannot be required to salvage the goods under the common law mitigation rule.<sup>73</sup>

Similarly, the mitigation rule does not ensure the efficient salvage of conforming goods that the buyer no longer desires. If a buyer accepts a conforming tender but no longer desires the goods, she lacks the power to compel the seller to take back or resell the goods, even if that would effect the most efficient salvage of the goods. Under the Code, the buyer's acceptance of conforming goods entitles the seller to the price of the goods and thus frees the seller of his obligation to mitigate his damages by participating in the salvage of the goods.<sup>74</sup> And the seller has no incentive to agree to salvage the goods unless he can profit from doing so.<sup>75</sup> If a buyer rejects conforming goods, the seller has to salvage the goods in order to mitigate his damages. Of course, if the most efficient salvage is for the buyer to resell or use the goods, she ordinarily will accept the goods and salvage them.<sup>76</sup>

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72. The Code's cure provision might appear to affect the analysis of the rejecting buyer's mitigation responsibilities, but it does not. The buyer's unconditional right of rejection is subject to the Code's provision allowing the seller to cure a nonconforming tender if time for performance has not elapsed or if he reasonably believes the tender would be acceptable with or without a money allowance. See U.C.C. § 2-508. Nevertheless, whether or not nonconforming goods tendered are subject to the seller's right of cure, both the buyer's and the seller's responsibilities to salvage them remain the same. These responsibilities also hold for goods tendered as a cure under § 2-508.

Further, the Code's provision governing the buyer's consequential damages might be thought to constrain her incentive to exercise her right of rejection. Section 2-715 prevents a buyer from recovering consequential damages that "could not reasonably be prevented by cover or otherwise." U.C.C. § 2-601. If this section were interpreted to mean that the buyer cannot recover consequential damages when accepting the nonconforming goods and adjusting to them would reduce damages, then, strategic scenarios aside, she would exercise her right of rejection only when she believed the seller was the most efficient salvor. But this interpretation of § 2-715 is unsound. The buyer who rightfully rejects goods is not barred from consequential damages that she could have avoided by accepting and reselling or using the goods. Section 2-601 gives the buyer an unconditional right to reject the whole of the nonconforming goods the seller tenders. An interpretation of § 2-715 according to which the buyer's decision to reject nonconforming goods might operate to bar her from recovering consequential damages undermines the Code's policy of assigning the nonbreacher the unilateral right to reject or accept and runs contrary to the Codes' rejection of the election-of-remedies doctrine.

73. If the buyer is the most efficient salvor, the seller could, in principle, strike a bargain with her to salvage the goods. See discussion *infra* part II.C.1. For a discussion of the efficiency of *ex post* bargains, see *infra* note 78 and accompanying text.

74. See discussion of § 2-709 and the common law mitigation rule, *infra* text accompanying notes 107-115.

75. If the seller is the most efficient salvor, the buyer could, in principle, strike a bargain with the seller to salvage the goods. See discussion *infra* part II.C.2. For a discussion of the efficiency of *ex post* bargains, see *infra* note 78 and accompanying text.

76. This assumes that the buyer is not strategically rejecting and hoping to benefit by threatening to litigate the adequacy of the seller's mitigation and the reasonableness of his incidental damage bill.

For practical purposes, then, there are two relatively common cases in which the mitigation rule does not ensure the efficient salvage of goods in a failed transaction.<sup>77</sup> The first is when a buyer rightfully rejects nonconforming goods; the second is when a buyer regrets acceptance of conforming goods. In the former case, the mitigation rule does not apply and so does not force the buyer to salvage the goods even if it is efficient for her to do so; in the latter case, the action for the price under the Code exempts the seller from the common law mitigation requirement to salvage the goods. The former problem is alleviated to some extent by specific doctrines in Article 2 that impose a duty of salvage upon the rightfully rejecting buyer under certain circumstances. The analysis in Sections C and D demonstrates that the Code's salvage rules in general assign the duty of salvaging rightfully rejected goods and accepted goods to the party most likely to be the most efficient salvor. But the analysis also demonstrates that in some cases, the Code does not allocate the salvage duty to the most efficient salvor. There are two defenses of the Code's treatment of these cases. The first is the standard response that, in these cases,

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77. The other case in which the mitigation principle fails to require the parties to salvage a failed transaction efficiently is when efficient salvage of the transaction requires a "cover" transaction. *See supra* note 67. Suppose a cover transaction is required to salvage a failed transaction efficiently. If the seller breaches, there is no need to compare the buyer's ability to cover with the seller's in order to ensure the most efficient cover transaction. For if the seller could "cover" more cheaply than the buyer, he would ordinarily do so to avoid breach. Whenever a seller breaches a contract, the failure of the buyer to undertake a possible cost-effective cover transaction constitutes a failure to mitigate damages. Thus, whenever the buyer undertakes the most cost-effective cover transaction available to her, thereby satisfying her mitigation obligation, that transaction is likely to be the most cost-effective transaction available to the parties.

If the buyer breaches, however, there is, at least in principle, a need to compare the buyer's and seller's ability to undertake any substitute transaction the breaching buyer may wish to make. Ordinarily, the question of who should bear the costs of any alternate purchase a buyer might make following her own breach is never asked. It typically goes without saying that the buyer cannot enlist the seller's assistance to reduce the costs that attend any alternate transaction the buyer might wish to enter in place of the transaction forgone through her breach. Moreover, this view gains support from the fact that the seller certainly has no mitigation obligation to provide such assistance to the breaching buyer. But this view is inconsistent with the goal of efficiently salvaging failed transactions. However rare it may be, in the event a seller is better able to undertake the alternative purchase that the buyer is making in place of the purchase contemplated by the contract she has breached, the goal of reducing the joint costs of failed transactions requires the seller to undertake that transaction on the buyer's behalf. It certainly strains ordinary usage to term such a purchase a "cover" transaction, but like a cover transaction, the cost of undertaking the breaching buyer's substitute transaction is no less a cost attending the failure of the initial transaction. If the seller's costs of making that purchase are less than the buyer's, efficient salvage of their transaction requires the seller to conduct the transaction for the buyer and entitles the seller to compensation from the buyer for his costs of undertaking the transaction.

The claim that the efficient salvage of failed transactions will sometimes require the seller to conduct the breaching buyer's post-breach, substitute "cover" transaction is counter-intuitive, but it is no less a requirement of the efficient salvage of transactions than the requirement that a rightfully rejecting buyer must sometimes salvage nonconforming goods. In both cases, the parties must undertake certain actions not in mitigation of their losses, but in "mitigation" of losses of the breacher other than those the breacher sustains in compensating the nonbreacher. These actions are required to reduce the joint costs of a failed transaction, and are no less essential to the joint maximization of the expected value of a contract than is the requirement that the parties mitigate their losses following breach. Of course, the likelihood that the seller will have an appreciable comparative advantage in effecting a substitute transaction for the breaching buyer of accepted goods is quite low.

the parties will bargain *ex post* around the inefficient initial allocation of salvage duties and the efficient salvor eventually will salvage. The well-known problem with this response is that such *ex post* bargains require the parties to incur transaction costs which constitute a deadweight loss. As a result, contracts with inefficient initial terms will, everything else being equal, have a lower expected joint value than ones with efficient initial allocations. Although it is not without its detractors, I assume that this generally accepted argument, or some acceptable variant, suffices to make the case for preferring efficient to inefficient default rules.<sup>78</sup> Thus, I reject the *ex post* bargain defense of the Code's inefficient allocation of salvage duties. The second defense for the Code's inefficient salvage rules relies on the efficiency trade-off story.

### B. *The Efficiency Trade-Off Story and the Tension Between Mitigation and Systematic Undercompensation*

The efficiency trade-off story has its origins in standard contracts literature. Much of the scholarship in contracts and sales law has directly addressed the problem of systematic undercompensation. It has been well understood for some time that the law of contracts and sales is systematically undercompensatory.<sup>79</sup> Under the default rules of Article 2, nonbreachers ordinarily cannot recover attorney's fees,<sup>80</sup> historically have been unable to

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78. Although everyone agrees that *ex post* negotiations will create transaction costs that constitute a deadweight loss, some have suggested that equal deadweight losses are created even by default rules that provide an efficient initial allocation of rights. See, e.g., Richard Craswell, *Insecurity, Reputation, and Cure*, 19 J. LEGAL STUD. 399, 409-10 (1990); Ian R. Macneil, *Efficient Breach of Contract: Circles in the Sky*, 68 VA. L. REV. 947 (1982). This critique holds that even with an efficient default rule, the parties will incur some costs in determining their rights under that rule. Moreover, in order to make rules less susceptible to disagreement, rules will have to use bright-line categories. But such rules necessarily will provide a less efficient allocation of rights and duties because they will be less tailored. Finally, even those bright-line rules that allocate rights efficiently in most cases will sometimes provide an inefficient allocation of rights. Given this fact, parties will incur costs to determine whether in their case the default rule is efficient or not, in order to take advantage of any mutually beneficial efficient trade that might be possible.

There are two objections to this critique. First, the bright-line rules that are efficient in most cases will use proxies that will lead the parties, typically, to believe that the default rule is probably efficient in their case. The same reason the default rule is generally efficient will, in most cases, provide the parties with reason to avoid investigating the possibility that the rule is inefficient in their case. Second, although a clear rule that deters disputes over the initial allocation of rights is preferable, all other things equal, to an unclear rule, a clear rule that in most cases allocates rights efficiently is preferable, all other things equal, to one that does not. A clear rule that is efficient in most cases will occasion fewer *ex post* renegotiations than a clear but inefficient rule, and both will occasion the same low cost for the parties to determine their rights initially.

79. For a general discussion of undercompensation in contracts, see Daniel A. Farber, *Reassessing the Economic Efficiency of Compensatory Damages for Breach of Contract*, 66 VA. L. REV. 1443, 1444-45 (1980); John A. Sebert, Jr., *Punitive and Nonpecuniary Damages in Actions Based Upon Contract: Toward Achieving the Objective of Full Compensation*, 33 UCLA L. REV. 1565, 1571-84 (1986).

80. Sellers may not recover attorney's fees as incidental damages under § 2-710. See *East Girard Sav Ass'n v. Citizens Nat'l Bank & Trust Co.*, 26 U.C.C. Rep. Serv. (Callaghan) 475, 484 (5th Cir. 1979) (applying Texas law); *Bossier Bank & Trust Co. v. Union Planters Nat'l Bank*, 21 U.C.C. Rep. Serv. (Callaghan) 254, 262-64 (6th Cir. 1977) (applying Tennessee law); *Great W. Sugar Co. v. Mrs. Alison's*



recover pre-judgment interest at competitive market rates,<sup>81</sup> and cannot

Cookie Co., 36 U.C.C. Rep. Serv. (Callaghan) 164, 166 (E.D. Mo. 1983) (applying Missouri law); *Decor by Nikkei Int'l v. Federal Republic of Nigeria*, 497 F. Supp. 893, 911 (S.D.N.Y. 1980) (applying New York law), *aff'd*, 647 F.2d 300 (2d Cir. 1981), *cert. denied*, 454 U.S. 1148 (1982); *Jelen & Son, Inc. v. Bandimere*, 801 P.2d 1182, 1185 (Colo. 1990); *Florida Nat'l Bank v. Alfred & Ann Goldstein Found.*, 18 U.C.C. Rep. Serv. (Callaghan) 850, 851 (Fla. Dist. Ct. App. 1976); *Neri v. Retail Marine Corp.*, 10 U.C.C. Rep. Serv. (Callaghan) 950, 956 (N.Y. 1972). Similarly, buyers generally may not recover attorney's fees as incidental or consequential damages under § 2-715. *See* *Nick's Auto Sales v. Radcliff Auto Sales*, 591 S.W.2d 709, 710-11 (Ky. Ct. App. 1979); *Jacobs v. Rosemount Dodge-Winnebago S.*, 310 N.W.2d 71, 79 (Minn. 1981); *Hardwick v. Dravo Equip. Co.*, 569 P.2d 588, 592 (Or. 1977); *Modine Mfg. Co. v. North East Indep. Sch. Dist.*, 503 S.W.2d 833, 844 (Tex. Civ. App. 1973); *Devore v. Bostrom*, 31 U.C.C. Rep. Serv. (Callaghan) 984, 988-90 (Utah 1981); *Murray v. Holiday Rambler, Inc.*, 265 N.W.2d 513, 527 (Wis. 1978). *Contra* *Cady v. Dick Loehr's, Inc.*, 299 N.W.2d 69, 72 (Mich. Ct. App. 1980) ("[Sections 2-714 and 2-715] confer[] on the trial court discretion to award attorney's fees as an element of damages incurred as a result of a breach of warranty.")

There are, however, important exceptions to these general rules. First, parties may provide for the payment of attorney's fees. *See, e.g.*, *Great W. Sugar Co. v. Mrs. Alison's Cookie Co.*, 36 U.C.C. Rep. Serv. (Callaghan) 164, 166 (E.D. Mo. 1983) (applying Missouri law); *Sellinger v. Freeway Mobile Home Sales*, 14 U.C.C. Rep. Serv. (Callaghan) 958, 962 (Ariz. 1974); *Nick's Auto Sales v. Radcliff Auto Sales*, 591 S.W.2d 709, 711 (Ky. Ct. App. 1979); *Universal C.I.T. Credit Corp. v. State Farm Mut. Auto. Ins. Co.*, 493 S.W.2d 385, 393 (Mo. Ct. App. 1973); *Equitable Lumber Corp. v. I.P.A. Land Dev. Corp.*, 18 U.C.C. Rep. Serv. (Callaghan) 273, 276 (N.Y. 1976). Second, there are federal and state statutes, notably in the area of consumer protection, that provide for the recovery of attorney's fees. *See, e.g.*, 15 U.S.C. § 2310(d)(2) (1988) (giving trial courts discretion to award attorney's fees to consumers prevailing in actions brought for breach of warranty); CAL. CIV. CODE § 1717(a) (West Supp. 1994) (providing that where contract provides for attorney's fees for one party should that party prevail in action to enforce contract, other party is likewise entitled to attorney's fees should it prevail, whether or not fees for second party are specified in contract); ILL. ANN. STAT. ch. 815, para. 505/10a(c) (Smith-Hurd 1993) (providing for award of reasonable attorney's fees to prevailing party in actions for damages brought under Consumer Fraud and Deceptive Business Practices Act); KAN. STAT. ANN. § 50-639(e) (1993) (providing for award of reasonable attorney's fees to prevailing consumer in action based on breach of warranty where supplier illegally disclaimed or limited warranties); MINN. STAT. ANN. § 8.31 subd. 3a (West Supp. 1994) (providing for award of reasonable attorney's fees to persons injured in violation of Prevention of Consumer Fraud Act); N.Y. GEN. OBLIG. LAW § 5-327 (McKinney 1989) (providing that where consumer contract provides for recovery of attorney's fees incurred by seller in enforcing contract, seller shall pay attorney's fees incurred by buyer as result of seller's breach or in successfully defending against suit brought by seller); OKLA. STAT. ANN. tit. 12, § 936 (West 1988) (providing for award of reasonable attorney's fees to prevailing party in action to recover on contract relating to purchase or sale of goods, wares, or merchandise); TEX. CIV. PRAC. & REM. CODE ANN. § 38.001 (West 1986) (providing for recovery of reasonable attorney's fees in action on contract). Finally, a buyer may recover attorney's fees incurred in third-party litigation resulting from the seller's breach of warranty. *See* *Chemco Indus. Applicators Co. v. E.I. du Pont de Nemours & Co.*, 366 F. Supp. 278 (E.D. Mo. 1973) (applying Arkansas law); *De La Hoya v. Slim's Gun Shop*, 24 U.C.C. Rep. Serv. (Callaghan) 45 (Cal. App. Dep't Super. Ct. 1978); *Universal C.I.T. Credit Corp. v. State Farm Mut. Auto. Ins. Co.*, 493 S.W.2d 385, 391-92 (Mo. Ct. App. 1973); *Hartwig Farms v. Pacific Gamble Robinson Co.*, 30 U.C.C. Rep. Serv. (Callaghan) 1552, 1559 (Wash. Ct. App. 1981).

81. The rate of prejudgment interest is generally set by statute. *See, e.g.*, CAL. CIV. CODE § 3289(b) (West Supp. 1994) (providing for 10% rate of interest after breach when none is specified in contract); COLO. REV. STAT. § 5-12-102(1) (1989) (providing that when there is no agreement as to rate, and money or property has been wrongly withheld, interest shall be either amount which fully recognizes gain realized by party wrongfully withholding or 8%); ILL. ANN. STAT. ch. 815, para. 205/2 (Smith-Hurd 1993) (providing for receipt of 5% on, *inter alia*, money withheld by "unreasonable and vexatious delay of payment"); MICH. COMP. LAWS § 600.6013(6) (West Supp. 1994) (providing that except for judgments on written instruments, "interest on a money judgment recovered in a civil action shall be calculated at 6-month intervals from the date of filing the complaint at a rate of interest that is equal to 1% plus the average interest rate paid at auctions of 5-year United States treasury notes during the 6 months immediately preceding July 1 and January 1"); N.J. CT. R. ANN. § 4:42-11(b) (West 1993) (requiring prejudgment interest in tort and product liability cases at rate equal to average rate of return of State of New Jersey Cash Management Fund in preceding fiscal year; statute also has been interpreted as allowing prejudgment interest in contracts cases when equitable principles call for it, *see* *McAdam v. Dean Witter*

recover losses that are too difficult to measure.<sup>82</sup> These facts suggest that nonbreachers risk systematic undercompensation.<sup>83</sup> In most cases, contract remedies that are predictably undercompensatory are likely to lead to suboptimal remedies that in turn create deadweight losses.<sup>84</sup>

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Reynolds, Inc., 896 F.2d 750, 773 (3d Cir. 1990); *George H. Swatek, Inc. v. North Star Graphics, Inc.*, 587 A.2d 629, 632 (N.J. Super. Ct. App. Div. 1991); N.Y. CIV. PRAC. L. & R. 5001, 5004 (McKinney 1992 & Supp. 1993) (requiring preverdict interest of 9% in contracts cases, except in cases of equitable nature, where rate is in court's discretion); OHIO REV. CODE ANN. § 1343.03(A) (Anderson 1993) (providing for 10% interest in contracts cases unless contract provides for different rate); PA. STAT. ANN. tit. 41, § 202 (1992) (establishing 6% as "legal rate of interest," which has been interpreted as providing rate of prejudgment interest in contracts cases, see *Security Pac. Int'l Bank v. National Bank of Western Pa.*, 772 F. Supp. 874, 878 (W.D. Pa. 1991)); TEX. REV. CIV. STAT. ANN. art. 5069-1.05 §§ 2, 6(g) (West Supp. 1994) (requiring prejudgment interest of no less than 10% and no greater than 20% and equal to auction rate quoted on discount basis for 52-week treasury bills if that is between 10 and 20%)

Currently, all of these statutory rates are at or above the one year Treasury bill interest rate. WALL ST. J., Sept. 27, 1994, at C21. In Texas, prevailing parties receive prejudgment interest as a matter of course, see, e.g., *Richter, S.A. v. Bank of America Nat'l Trust & Sav. Ass'n*, 939 F.2d 1176, 1197 (5th Cir. 1991), *reh'g denied*, 962 F.2d 9 (1992), and in New York, prevailing plaintiffs in contract cases receive prejudgment interest as a matter of right, see, e.g., *Bausch & Lomb Inc. v. Sonomed Tech., Inc.*, 780 F. Supp. 943, 973 (E.D.N.Y. 1992), *aff'd in part and vacated in part on other grounds sub nom. Bausch & Lomb, Inc. v. Bressler*, 977 F.2d 720 (2d Cir. 1992). In many other states, however, recovery of prejudgment interest is limited. See, e.g., *United States ex rel. Bartec Indus. v. United Pac. Co.*, 976 F.2d 1274, 1279 (9th Cir. 1992) (applying California law) ("Where the parties dispute *only* the question of ultimate liability and not the amount of damages that may be awarded, prejudgment interest can be obtained; otherwise, it is not available.") (alteration in original); *H & W Indus. v. Occidental Chem. Corp.*, 911 F.2d 1118, 1123 (5th Cir. 1990) (applying Mississippi law) ("Although not foreclosed, prejudgment interest awards are generally denied in a breach of contract action where the claim is unliquidated."); *Ciba-Geigy Corp. v. Alter*, 834 S.W.2d 136, 148 (Ark. 1992) ("In cases where damages cannot be ascertained at the time of the loss, prejudgment interest should not be allowed."); *Meldco, Inc. v. Hollytex Carpet Mills*, 796 P.2d 142, 147 (Idaho Ct. App. 1990) ("[A]n award of prejudgment interest should run from the date the damages amount first becomes 'fixed' or 'ascertainable.'"); *Ouwenga v. Nu-Way Ag, Inc.*, 604 N.E.2d 1085, 1091 (Ill. App. Ct. 1992) ("Absent an agreement between the parties, prejudgment interest is properly awarded only when specifically provided for by statute, and only if the damages are liquidated or subject to exact computation.") (citations omitted); *Trienco, Inc. v. Applied Theory, Inc.*, 794 P.2d 1239, 1243 (Or. Ct. App. 1990) ("Prejudgment interest is allowable where the exact amount owed is ascertained or ascertainable by simple computation or by reference to generally accepted standards and where the time from which the interest runs can be ascertained."); *D'Huyvetter v. A.O. Smith Harvestore Prod.*, 475 N.W.2d 587, 594 (Wis. Ct. App. 1991) ("An award of prejudgment interest is inappropriate where there is a genuine dispute as to the amount of damages throughout the trial.") (citation omitted)

82. Losses that are too difficult to measure because they are vague or speculative are not compensated under the common law of contract. See E. ALLAN FARNSWORTH, *CONTRACTS* § 12.15 (1990). This common law rule is incorporated into the Code under § 1-103.

83. In some cases, contract remedies may also lead to overcompensation. The discussion in the text is confined to the problem of undercompensation because, unlike the problem of overcompensation, undercompensation seems to be systematic. The argument advanced in this Part is that the Code's rules governing salvage can be understood as implicitly providing a counterweight to systematic undercompensation by deliberately, or foreseeably, permitting the more efficient salvor to avoid salvaging in order to avoid exacerbating his risk of systematic undercompensation. If expected overcompensation were systematic, and equivalent in average amount to the systematic undercompensation, the two phenomena would cancel each other out, and contract remedies would be systematically compensatory. Although there are classes of cases in which an overcompensatory remedy might result (e.g., the case of the losing contract, overvaluation of personal losses, etc.), these cases are not generally regarded as likely enough *ex ante* to create a systematic risk of overcompensation, at least not on the order of magnitude comparable to the risk of systematic undercompensation created by attorney's fee and prejudgment interest rules, as well as measurement rules that favor the breacher.

84. Suboptimal remedies, including those that are suboptimal because they are undercompensatory, potentially undermine (1) the incentive to make the proper *ex post* choice between performing and not performing the contract; (2) the incentive to take the optimal level of precautions against accidents that

Rules that impose positive duties on nonbreachers following breach potentially exacerbate the problem of systematic undercompensation for three reasons. First, if those rules require nonbreachers to incur incidental expenses, those expenses are subject to the same expected undercompensation as the direct and consequential losses the nonbreacher incurs. Thus, requiring incidental expenditures increases the nonbreacher's net expected loss due to undercompensation. Second, such rules expose the nonbreacher to strategic claims by the breacher that the nonbreacher failed to discharge the post-breach duty. Litigating these claims increases the nonbreacher's costs of litigation and thus his expected undercompensation. Moreover, the possibility that the breacher will prevail in such litigation further increases expected undercompensation.

Third, the nonbreacher may face what Goetz and Scott have called "the breacher-status problem."<sup>85</sup> The anticipatory repudiation doctrine illustrates the problem well. If one party incorrectly interprets the other party's behavior as a repudiation and therefore mitigates before the time for the other party to perform under the contract has expired, any mitigating activity may itself constitute a breach. For example, if the nonbreaching seller believes the buyer has repudiated, he might engage in a resale of the goods identified to the initial contract. If a court subsequently determines that the buyer did not repudiate, the seller's resale will constitute a breach. Given this possibility, buyers might send ambiguous signals to preserve the right to both seller's performance and seller's mitigation. If the seller mitigates, he risks the buyer alleging that she never repudiated. If the seller does not mitigate, he risks the buyer alleging that he repudiated. In the former case, the seller might be found to be the breacher;

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might leave the breacher unable to perform; and (3) the parties' attempt to provide the more risk averse party with 100% insurance against breach. For an extended discussion of the benefits of exact compensation, see Richard Craswell, *Contract Remedies, Renegotiation, and the Theory of Efficient Breach*, 61 S. CAL. L. REV. 629 (1988). However, perfectly compensatory remedies may also cause inefficiencies. For an example of the potential inefficiencies of compensatory damages, see Lucan Ayre Bebhuk & Steven Shavell, *Information and the Scope of Liability for Breach of Contract: The Rule of Hadley v. Baxendale*, 7 J.L. ECON. & ORG. 284 (1991) (analyzing inefficiency in awarding unforeseeable damages); Goetz & Scott, *The Mitigation Principle*, *supra* note 9; Alan Schwartz, *Proposals for Products Liability Reform: A Theoretical Analysis*, 97 YALE L.J. 353, 362-67 (1988) (arguing that 100% insurance for certain non-pecuniary losses may be inefficient even if nonbreachers are risk-averse); Gwyn D. Quillen, Note, *Contract Damages and Cross-Subsidization*, 61 S. CAL. L. REV. 1125 (1988) (arguing that compensatory damages may lead to cross-subsidization among different classes of nonbreachers with different amounts of risk). Where perfect compensation is likely to lead to inefficiencies, the Code and the common law often limit the nonbreacher's recovery accordingly. For example, the *Hadley* rule limits nonbreachers to foreseeable damages. See *Hadley v. Baxendale*, 156 Eng. Rep. 145 (Ex. 1854). Thus, this Article's concern with undercompensation is limited to the large group of cases in which perfect compensation would be efficient and in which undercompensation therefore causes deadweight losses. The argument in the text is that the goal of reducing the risk of undercompensation can provide a plausible explanation for those instances in which the Code allows one party to avoid efficiently reducing the costs of breach. The implicit presupposition of this analysis is that in these instances, undercompensatory remedies would lead to deadweight losses.

85. "A party who contests the interpretation of his obligation by withholding any part of the disputed performance risks being characterized as a breacher." Goetz & Scott, *The Mitigation Principle*, *supra* note 9, at 983.

in the latter case, the seller might be found to have failed to mitigate and therefore might be barred from recovering mitigable losses. Both of these possibilities exacerbate the nonbreacher's exposure to undercompensation.

The problem of undercompensation is ameliorated to a considerable degree by the parties' extralegal incentives, most notably their desire to preserve their commercial reputation for cooperation. In many cases, breachers will fully compensate the nonbreacher simply by paying the nonbreacher's damage bill, and the nonbreacher can be expected to undertake mitigation and salvage activity when it is cost-effective to do so. In some cases, however, these extralegal incentives are outweighed by the prospect of significant losses or gains. As a result, terms that maximize the joint value of a contract must provide mitigation and salvage duties for the nonbreacher and yet prevent those duties from increasing the nonbreacher's exposure to undercompensation. One approach to accomplishing these two goals is to build a compromise directly into the rules requiring joint minimization of the costs of failed transactions. Goetz and Scott's account of the logic of the common law time-of-performance rule in the doctrine of anticipatory repudiation illustrates this approach.

The goal of reducing the joint costs of a failed transaction requires that the nonbreaching party mitigate his damages as soon as he receives effective notice of the other party's anticipatory repudiation. Goetz and Scott argue, however, that a rule that permits the nonbreacher to wait until the time of performance to mitigate might be justified so as to countervail the nonbreacher's risk of undercompensation.<sup>86</sup> A rule that allows the nonbreacher to wait until the time of performance in effect provides the nonbreacher with the option to speculate at the breacher's expense.<sup>87</sup> For example, a nonbreaching buyer who receives notice of repudiation from her seller can ignore loss-reducing cover transactions and gamble that the market price will fall below the contract price by the time for performance. The gamble, of course, is at the seller's expense: the buyer will be awarded the difference between the contract price and the cover price and thus will be protected from any market price increase between the time of repudiation and the time of performance. The justification for the time-of-performance rule is that this benefit to the nonbreacher at the breacher's expense helps to counterbalance the nonbreacher's expected undercompensation. As Goetz and Scott put it,

[t]he common-law time-of-performance rule encourages an obligee to extort a side payment from the obligor in exchange for his agreement to cover promptly in a rising market. On the other hand, to require mitigation at the time of repudiation would enhance the potency of

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86. See *id.* at 993-95.

87. See SCHWARTZ & SCOTT, *supra* note 19, at 337-39, which argues that the time-of-performance rule is equivalent to an option contract benefiting the nonbreacher.

any threats of evasive acts. Thus, the common-law time-of-performance rule is also an implicit security against evasion, particularly the threat of nonsatisfactory breach.<sup>88</sup>

This rationale for the time-of-performance rule suggests that a rule that not only permits but encourages inefficient mitigation might be justified because it has the effect of reducing the extent to which mitigation rules exacerbate the nonbreacher's risk of undercompensation. The rule is justified if the efficiency losses anticipated from the suboptimal mitigation rules are exceeded by the expected gains from the concomitant reduction in expected undercompensation. Under these conditions, there is an overall net gain in efficiency. At bottom, Goetz and Scott purport to explain and justify the common law time-of-performance rule by arguing that two "efficiency wrongs" sometimes make an "efficiency right." This is the essence of the efficiency trade-off story.

The central claim of the next two sections is that the best explanation and justification of the Code's salvage rules depend on the same kind of efficiency trade-off story that Goetz and Scott provide for the time-of-performance rule. I present the best case scenario for believing that the Code's salvage regime can be explained and justified as an attempt to allocate the salvage duty to the party most likely to be able to salvage them efficiently, unless the efficiency gains of such an allocation are likely to be outweighed by efficiency losses due to the increase in expected undercompensation. This analysis of the Code's salvage regime begins by assuming that the parties have what I will call "perfect legal information": At the time they make their salvage decisions, the parties know the answers to the legal questions of whether acceptance, rejection, or revocation has taken place and which party is the breacher. In the final section of this Part, I argue that the perfect legal information assumption is unrealistic in many cases. I then demonstrate how the introduction of legal uncertainty will lead to a significant reduction in the efficiency of the Code's salvage regime.

The analysis of the Code's salvage regime will depend upon several empirical assumptions about the conditions under which buyers and sellers are likely to have comparative advantages in salvaging the goods. The first assumption is that if one party has an inherent advantage in reselling goods, that party is most likely to be the seller. This assumption is based on the empirical generalization that sellers more often than buyers will have, among other things, more experience at selling, better access to relevant markets, and greater benefits from economies of scale in advertising, marketing, and distribution.<sup>89</sup>

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88. Goetz & Scott, *The Mitigation Principle*, *supra* note 9, at 995.

89. *See id.* at 984-86 (discussing nature of resale market). Further development of Goetz and Scott's analysis reveals that the difference between the parties' resale abilities is likely to be greatest in what I call "medium" markets. If the market is either "thick" or very "thin," neither party is likely to have an

The second empirical assumption is that, all other things being equal, the party in possession or control of the goods is the superior reseller. The comparative advantage of a reseller in possession and control of the goods consists in his superior ability to provide potential buyers with access to the goods, to vouch for their current condition, and to effect their immediate delivery without going through an intermediary. The comparative advantage of a reseller in possession or control of the goods consists at a minimum in his saving the cost of conducting the resale through a third party who has possession or control of the goods.<sup>90</sup>

The third empirical assumption is that the value generated by the buyer's use of nonconforming goods is likely to exceed the value of the seller's use of nonconforming goods. Recall that determining the most efficient salvage of the goods requires a comparison between the maximum net resale value and the maximum net use value of the goods.<sup>91</sup> The current assumption holds that the maximum net use value can be identified with the buyer's use value of the goods in most cases. If one party's adjusting to the nonconforming goods is the highest valued use of the goods, it is likely to be the buyer's use that generates the greatest value. The rationale for this assumption is analogous to the rationale for presuming that a merchant buyer will have a comparative advantage in reselling goods with respect to which she is a merchant seller. As long as the goods are not inherently defective, a buyer is more likely to be

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advantage at resale. The paradigmatic examples of a thick market are commodities, futures, or stock markets. A typical example of a thick resale market governed by sales law is the market for wholesale corn or wheat. Parties have access to such thick markets at roughly equal cost and face the same price structure for their purchases or sales. There is little reason to suppose that a seller would have a comparative advantage over a buyer in reselling goods in a thick market. The limiting case of a "thin market" is a non-existent market. If there is no resale market for goods, neither a seller nor a buyer will have a comparative advantage in reselling the goods. Thus, if one party ever has a significant comparative advantage in reselling rejected goods, the market of resale is likely to be neither thick nor thin, but "medium." In medium markets, where resale is possible but access to the resale market is limited, the experience and expertise of sellers will give them a comparative advantage in reselling rejected goods. Sellers are likely to have established connections and procedures for accessing difficult markets and conducting sales, whereas buyers may have no experience in selling in that market. A seller, therefore, is likely to be able to resell goods for a higher price and at less expense than a buyer. However, it is unlikely that a seller of new goods will have a comparative advantage in reselling defective or damaged goods, even if the market for such goods is a medium market. In other words, a seller's comparative advantage may be closely tied to the particular kind of goods that he, as a merchant, sells. Thus, the assumption that sellers are more likely than buyers to have a comparative advantage in resale amounts to the claim that whenever markets are neither thick nor thin, but medium, sellers are likely to have the comparative advantage in resale. And even in medium markets, a seller's comparative advantage is likely to be diminished if the goods to be resold fall outside the category of goods the seller ordinarily sells, as they might if the seller is a retailer of new goods and the rejected goods are defective or damaged. In thick and thin markets, however, neither party is likely to have an appreciable advantage at resale.

90. Note that when the buyer has possession of the goods, the assumption that the party in possession is, all things being equal, the superior reseller will be in tension with the first empirical assumption, which presumes that the seller typically will have an advantage in resale. For example, these assumptions lead to opposing conclusions in the analysis of the salvage responsibilities of (1) the rightfully rejecting merchant buyer in possession of the goods when the seller has no presence in the market of rejection, see *infra* part II.C.2, and (2) the accepting buyer, see *infra* text following note 122.

91. See *supra* text following note 67.

able to put them to use than is a seller. Buyers are in the business of using goods. Sellers typically never use the goods they sell and therefore would not be expected to have any (non-resale) use even for conforming goods. Of course, the greater the difference between the nonconforming goods tendered and the goods described in the contract, the less reason there is to suppose that buyers will be better able to adjust to and make use of the goods. However, the plausibility of this empirical assumption depends only on the claim that if one party has a comparative advantage in putting nonconforming goods to use, it is more likely to be the buyer than the seller.

C. *The Analysis of the Duty of the Rightfully Rejecting Buyer To Salvage the Goods Assuming Perfect Legal Information*

If the Code did not provide an independent basis for requiring the rightfully rejecting buyer<sup>92</sup> to salvage goods when doing so is efficient, the common law would at least provide her in some cases with the duty to undertake minimal, if insufficient, salvage activity. Under the common law and the Sales Act, a buyer who has rightfully rejected goods in her possession is an involuntary bailee<sup>93</sup> and therefore would be liable at least for gross negligence in her care of the goods. But Article 2 of the Code provides the buyer with specific rights and greater responsibilities to care for or dispose of rejected goods. A rejecting buyer without a security interest in goods is at least under the express obligation to hold the goods "with reasonable care at the seller's disposition for a time sufficient to permit the seller to remove them."<sup>94</sup> The nonmerchant buyer is expressly exempted from any further responsibilities for rightfully rejected goods.<sup>95</sup> When the seller has no agent

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92. As noted earlier, the analysis of the rightfully rejecting buyer's salvage duties is unaffected by the Code's provision granting the seller a right to cure under § 2-508. See *supra* note 72. For a discussion of the role of cure in the alternative salvage regime I propose, see *infra* note 173.

93. Under the U.S.A.,

[s]ince the seller, in delivering improper goods, is not carrying out his contract, he cannot thereby impose any obligation upon the buyer to return those improper goods or go to any expenses for them. In shipping the goods, the seller has forced upon the buyer something for which he never contracted. There can therefore arise no obligation to deal with those goods at all, even to the extent of returning them. The buyer becomes an involuntary bailee, and he need do nothing with respect to the goods to his inconvenience, except exercise such reasonable care of them as would be expected of any involuntary bailee.

MARIASH, *supra* note 5, § 288, at 587. Note that the U.S.A. rule limiting the obligation to salvage rightfully rejected goods to the duties of an involuntary bailee is rejected by the U.C.C., which replaced the U.S.A. As I explain below, the U.C.C. places greater duties on a rightfully rejecting buyer. This rejection of the U.S.A.'s treatment of the rightfully rejecting buyer's duties to salvage goods in her possession supports the view that parties seeking to maximize the joint value of their contract *ex ante* would agree to a term requiring rightfully rejecting buyers to take greater responsibility for salvaging rejected goods in their possession.

94. U.C.C. § 2-602(2)(b).

95. *Id.* § 2-602(2)(c).

or place of business at the market of rejection, a merchant buyer without a security interest in goods rightfully rejected is

under a duty after rejection of goods in his possession or control to follow any reasonable instructions received from the seller with respect to the goods and in the absence of such instructions to make reasonable efforts to sell them for the seller's account if they are perishable or threaten to decline in value speedily.<sup>96</sup>

If the seller fails to provide reasonable instructions following notice of rejection, the nonmerchant buyer has the option to "store the rejected goods for the seller's account or reship them to him or resell them for the seller's account . . . ."<sup>97</sup> So long as the goods are not perishable and do not threaten to decline in value speedily, and the seller does not provide reasonable instructions inconsistent with these options, the rightfully rejecting merchant buyer has these options as well. Given these rules, the salvage duties imposed upon rightfully rejecting buyers depend upon whether the seller or buyer is in possession or control of the goods.

#### 1. *Seller in Possession or Control of Rightfully Rejected Goods*

Suppose the seller retains possession or control of rightfully rejected goods. Under the Code, the buyer will be free of any duty to salvage them. If the goods' nonconformity constitutes a defect, and thus distinguishes them from those the seller is ordinarily in the business of selling, he is unlikely to have any inherent comparative advantage in reselling them. But the buyer is also unlikely to have an advantage, no matter what kind of market exists for the goods. If the nonconformity does not constitute a defect in the goods, and thus they remain the kind of goods with respect to which the seller is a merchant, the seller is likely to have an inherent comparative advantage in reselling them if the resale market is neither very thick nor very thin.<sup>98</sup> Thus, either the seller will have an inherent comparative advantage in reselling the goods or neither party will have an inherent comparative advantage. In either case, given that the goods are in the seller's possession or control, the seller is likely to be the superior reseller. Thus, if the most efficient salvage of the goods is to resell them, the Code's salvage regime is likely to be efficient. If, however, the most efficient salvage of the goods is for one party to use them, the third assumption predicts that the buyer will be the superior user of the goods. By allowing the buyer to reject the goods in the seller's possession, the

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96. *Id.* § 2-603(1).

97. *Id.* § 2-604.

98. For the distinctions between thick, thin, and medium resale markets and their relevance to determining the parties' comparative resale abilities, see *supra* note 89



buyer can avoid adjusting to nonconforming goods even if doing so would constitute the most efficient salvage of the goods. Thus, the doctrine of rejection, when combined with the Code's salvage rules, allows the rightfully rejecting buyer in some cases to avoid undertaking the most cost-effective salvage of nonconforming goods.

The Code's failure to require the rightfully rejecting buyer to adjust to and use goods might be justified by the assumption that in the majority of cases, adjustment and use will not constitute the most efficient salvage option. The Code's salvage rules governing rightfully rejecting buyers would, on this view, place the incentive to salvage on the party who in most cases is likely to be the most efficient salvor. This is precisely what majoritarian default rule analysis<sup>99</sup> recommends. In the minority of cases in which the rightfully rejecting buyer is the most efficient salvor, the seller will often be able to bargain *ex post* for the buyer to keep and adjust to the goods. But there is no basis for asserting that in the majority of sales cases in which nonconforming goods are tendered, the buyer's adjustment and use does not constitute the most efficient salvage of the goods. Moreover, even if there were, we might want to design a more fine-tuned default rule that requires buyers to adjust to and use goods whenever doing so would constitute the most efficient salvage of the goods. Even though *ex post* bargains leading to an efficient salvage of the goods in the minority cases might sometimes result, they will require the parties to incur positive transaction costs which constitute a deadweight loss.<sup>100</sup> Those costs could be avoided if the salvage duties were allocated to the most efficient salvor directly. Moreover, insuperable transaction costs sometimes will prevent post-breach bargains. A default rule that allocated the salvage duties to the party expected to be the most efficient salvor in almost every case would be superior to one that allocated those duties efficiently in a smaller majority of cases. Thus, it appears that a defense of the Code must hold either that the rightfully rejecting buyer's adjustment and use is the most efficient salvage option only in a minority of cases, or that it is undesirable or impossible to design a more fine-tuned default rule. Even if the former claim is true, the latter must be specifically defended in order to defend the Code's regime on the whole. A more fine-tuned default rule would in principle increase the Code's efficiency, either by facilitating gains from more efficient salvage of goods or by eliminating the transaction costs attending *ex post* bargains in the minority cases under the Code's current rules.

In practice, however, it may be that such a fine-tuned default rule is likely to exacerbate both the buyer's exposure to undercompensation and the seller's strategic behavior. It would require that the parties determine at the time of their salvage decision whether the rightfully rejecting buyer's adjustment and

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99. See *supra* note 19.

100. See *supra* note 78 for a discussion of the transaction costs defense of efficient default rules.

use of the goods was the most efficient salvage option. Courts would have to make the same determination at the time of adjudication. These determinations will often be difficult for the parties and the courts to make. Thus, the fine-tuned default rule requiring the rightfully rejecting buyer to adjust and use goods when doing so provides the most efficient salvage of the goods subjects her to litigation over the question of whether the buyer's adjustment and use was the most efficient salvage option and whether her bill for adjustment and use is reasonable.<sup>101</sup> The Code's default rule allowing the rightfully rejecting buyer to avoid adjustment and use, except as she might agree under an *ex post* bargain with the seller, might therefore be justified because it avoids exacerbating the rightfully rejecting buyer's risk of undercompensation.

## 2. *Buyer in Possession or Control of Rightfully Rejected Goods*

Suppose the buyer is in possession or control of rightfully rejected goods. There are three possible Code rules that might apply.<sup>102</sup> To determine whether these rules require the efficient salvor to salvage the goods, consider how the parties' salvage duties are affected when the resale and adjust-and-use salvage options, respectively, provide the most efficient salvage of the goods.

First, suppose that resale provides the most efficient salvage of the goods. The first rule relieves merchant buyers from resale obligations when the seller has a presence in the market of rejection. This rule would be efficient if we assume that the ordinary comparative resale advantage of the buyer in possession or control of the goods will be outweighed by the seller's presence in the market of rejection. Since such a seller presumably could at little expense regain possession and control of the goods, he could just as easily resell the goods as the buyer. Moreover, if one party has an inherent comparative advantage in resale, it is likely to be the seller and not the buyer. So if the seller has a presence in the market of rejection, relieving the buyer in possession of rightfully rejected goods of any major salvage responsibilities is either consistent with or necessary for achieving the most efficient salvage of the goods.

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101. Note, however, that the rule requiring the buyer to adjust to and use nonconforming goods, when doing so provides the most efficient salvage of the goods, will not be subject to the breacher-status problem. In the case of anticipatory repudiation, the breacher-status problem arises because the nonbreaching buyer, for example, is required by a time-of-repudiation rule to cover at the time the seller repudiates. Once the buyer covers, however, the seller can accuse the buyer of breach and will be upheld if the court believes the seller never repudiated. The potential ambiguity of the repudiation signal thus exposes the buyer both to the possibility of inadvertent breach and to the possibility of the seller's deliberate use of an ambiguous repudiation signal to preserve the option of performing or the option of breaching and alleging the buyer's failure to mitigate. But these possibilities are not presented by a rule requiring the buyer to adjust to and use nonconforming goods when doing so is efficient, for a buyer who decides to adjust to and use nonconforming goods tendered by the seller is thereby performing the contract. The buyer's mitigation, in this case, requires her to accept the goods and is therefore consistent with performing the contract.

102. See *supra* text accompanying notes 94-97

Next, consider the rule that places the merchant buyer under a more extensive duty to salvage the goods when the seller has no presence in the market of rejection. This rule achieves the efficient allocation of the salvage duty if whatever inherent comparative advantage the seller may have in resale is outweighed by his disadvantage of not having possession and control of the goods. Given that the seller has no presence in the market of rejection, regaining possession of the goods is likely to be costly, and conducting resale long-distance with the buyer as intermediary will create costs a buyer's resale would avoid. Moreover, if the resale market is thick, the seller is unlikely to have a significant inherent advantage in resale anyway. This rule does presuppose, however, that the expected benefits from the buyer's comparative advantage in resale outweigh the expected losses due to the increase in her risk of undercompensation from litigation over the timeliness and reasonableness of her incidental expenses.

Finally, consider the rule that exempts the nonmerchant buyer from any salvage duty except holding the goods with reasonable care at the seller's disposal. According to the first empirical assumption, any inherent advantage in resale will be the seller's. The ordinary advantages in resale due to possession and control under the second assumption are somewhat counterbalanced by the inexperience of nonmerchant buyers.<sup>103</sup> This rule, then, might reflect the belief that the expected benefits of having the resale of goods conducted by the seller instead of an inexperienced nonmerchant buyer are likely to outweigh the expected costs of a seller retrieving rightfully rejected goods. And if the expected net benefits of resale are equal whether the buyer resells directly or the seller retrieves the goods and resells, placing the resale duty on the seller will avoid exposing the buyer to the risks of undercompensation attending a buyer resale requirement.

Now suppose that the efficient salvage of the goods requires their use instead of their resale. According to the third empirical assumption, buyers are more likely than sellers to be able to maximize the net use value of rejected goods. Under the Code, if the buyer is in possession or control of rightfully rejected goods and the seller has a presence in the market of rejection, the seller must salvage the goods. By rejecting the goods, the buyer can avoid adjusting to the goods even if that would constitute the most efficient salvage of the goods. Moreover, even if the seller does not have a presence in the market of rejection, the merchant buyer's duties are restricted to following the seller's reasonable instruction to salvage the goods, or in the absence of such instructions, to resell goods likely to diminish in value quickly. But none of these duties requires even the merchant buyer in possession of rightfully rejected goods to adjust to the goods' nonconformity and use them. Such a

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103. In addition, a rule imposing a greater duty on nonmerchants might be ineffective because nonmerchants are more likely than merchants to be unaware of the rule.

requirement would be tantamount to requiring a buyer to accept nonconforming goods, a requirement contradicted by the buyer's unconditional right to reject them.<sup>104</sup> And of course, if the buyer is a nonmerchant, he does not even have the duty to resell the goods, much less to adjust and use them. The Code rules governing the salvage of goods give the merchant and nonmerchant buyer the unilateral right to reject nonconforming goods, and thus sometimes allow the buyer to forgo salvage of the goods even when she is the most efficient salvor. Although a buyer's decision whether to use or resell accepted nonconforming goods is disciplined, at least in theory, by the Code's mitigation requirement,<sup>105</sup> her initial decision whether to reject or accept nonconforming goods is entirely within her discretion<sup>106</sup> and may contravene the goal of allocating the duty to salvage to the most efficient salvor.

Once again, however, the possibility of *ex post* bargains and the problem of exacerbating the nonbreacher's exposure to undercompensation provide possible rationales for the Code's rule exempting rightfully rejecting buyers in possession of goods from adjusting to and using the goods. A more fine-tuned default rule might require the buyer to adjust to and use nonconforming goods when doing so would maximize the value of the goods. Such a rule, however, increases the buyer's exposure to undercompensation resulting from litigation over the questions of whether the buyer's adjustment and use was the most efficient salvage option and whether her bill for adjustment and use is reasonable.

### 3. *Summary of the Analysis of the Rightfully Rejecting Buyer's Duty To Salvage Goods Assuming Perfect Legal Information*

I have argued that given the three empirical assumptions, the Code's express salvage requirements for the rightfully rejecting buyer could reasonably be expected to result in the most efficient resale of rejected goods in most cases. But because the rules presuppose the buyer's right to reject nonconforming goods, the rules do not require her to adjust to and use nonconforming goods even when doing so is the most efficient salvage of rejected goods. This feature of the Code's salvage rules might be justified under standard majoritarian default analysis if, in most cases, maximum net

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104. Note that the Code's cure provision, § 2-508, does not make the buyer's right of rejection conditional. Under § 2-601, the buyer is allowed to reject "if the goods . . . fail in any respect to conform to the contract." U.C.C. § 2-601. Section 2-508 provides that the seller may tender with conforming goods if the time for performance has not expired or if the seller had reasonable grounds for believing the nonconforming tender would be acceptable to the buyer with or without a money allowance. The cure provision thus never forces a buyer to accept nonconforming goods.

105. Section 2-715 limits the buyer's recovery of consequential damages that she could have avoided through cover or otherwise.

106. It might be argued that § 2-715 prevents a rejecting buyer from recovering consequential damages that could have been avoided had she accepted the goods. See *supra* note 72 for the argument against this interpretation of § 2-715.

resale value will exceed maximum net use value in salvaging goods in a failed transaction. Moreover, the likelihood of *ex post* bargains that will lead to the efficient salvage of the goods will ameliorate, to some extent, the inefficient allocation of the salvage duty in this minority of cases. It is difficult, however, to determine whether resale or adjustment will be the most efficient salvage option in most failed transactions. More important, even if resale more frequently provides the most efficient salvage of the goods, it would be ideal if a more refined default rule could effectively allocate the duty to adjust to and use rejected goods to the buyer when that option maximizes the value of the goods. Yet, because such a default rule would likely exacerbate the buyer's exposure to undercompensation, the Code's default rules might represent an acceptable balance between the competing goals of efficiently salvaging the goods and reducing the nonbreacher's exposure to undercompensation.

*D. The Analysis of the Seller's Duty To Salvage Accepted Goods Assuming Perfect Legal Information*

In this Section, I consider the Code's regulation of the salvage of accepted goods. The seller's duty to salvage accepted goods turns on the construction of the seller's action for the price. According to the standard interpretation, the Code grants a nonbreaching seller the right to be paid the price by a breaching buyer only in the three cases provided for under § 2-709(1). The first is when the breaching buyer has accepted the goods.<sup>107</sup> The second is when conforming goods are lost or damaged within a commercially reasonable time after risk of their loss has passed to the buyer. The third is when the goods have been identified to the contract, so long as the seller cannot, with reasonable effort, resell the goods himself at a reasonable price.<sup>108</sup> This interpretation of § 2-709 has been adopted in virtually all of the cases decided under that section to date.

One important question raised by § 2-709 is whether the general common law mitigation rule is displaced by the action for the price. Section 1-103 states that "[u]nless displaced by the particular provisions of this Act, the principles of law and equity . . . shall supplement its provisions."<sup>109</sup> Unless displaced by the Code, the common law mitigation requirement is incorporated into the

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107. U.C.C. § 2-709(1)(a). A seller is not entitled to the price from an accepting buyer in a credit transaction, however. The seller must wait until the buyer defaults under the credit agreement before maintaining an action for the price. See 3 WILLIAM D. HAWKLAND, UNIFORM COMMERCIAL CODE SERIES § 2-709:01 (1984).

108. A buyer who anticipatorily repudiates can be forced to pay the price under the same conditions as a rejecting or revoking buyer: the seller can "resort to any remedy for breach (Section 2-703 or Section 2-711)." U.C.C. § 2-610. But presumably, the conditions for availability of those remedies still apply, so that a seller cannot get the price from a repudiating buyer unless (1) the buyer accepted, which is inconsistent with revocation, (2) the goods are lost or destroyed after risk of loss passed to the buyer, or (3) the goods are identified to the contract and the seller cannot resell at a reasonable price.

109. *Id.* § 1-103.

Code. Thus, although the action for the price, according to the above interpretation, does not require a seller of accepted goods to attempt any reasonable resale in order to be entitled to the price, the common law mitigation rule might nonetheless require that that seller attempt a reasonable resale notwithstanding his entitlement to the price.

The effect of imputing this mitigation requirement is unclear. One effect might be to force the return of the goods to the seller and to reduce the price to which he is entitled under § 2-709 by the difference between the price the seller realizes upon resale (or the price expected upon resale) and the contract price, less the seller's costs of resale. That result was sought but denied in *F & P Builders v. Lowe's of Texas*.<sup>110</sup> The buyer, F & P Builders, accepted "construction products" upon delivery from the seller, Lowe's, but refused to pay the price due under the contract. F & P argued that Lowe's duty to mitigate damages required it to pick up the delivered goods and attempt a resale. The court held that § 2-709(1)(a), which entitles a seller of accepted goods to the price, "supplants any duty upon the seller to mitigate damages for goods delivered and accepted."<sup>111</sup> F & P evidently claimed that Lowe's should be forced to take back the goods and should be awarded only the difference between their resale value and the contract price plus incidental damages incurred in retrieving and reselling the goods.<sup>112</sup> Since Lowe's was in the business of retailing construction products, it is reasonable to assume that Lowe's would have been able to resell the goods at the contract price in the ordinary course of business simply by returning them to inventory. Nonetheless, the court viewed acceptance as sufficient to relieve the seller of this burden. The court's claim that § 2-709(1)(a) supplants the seller's duty to resell the goods under the common law mitigation requirement clearly gains support from the commentary accompanying § 2-709: "[t]he action for the price is now generally limited to those cases where resale of the goods is impracticable *except where the buyer has accepted the goods . . .*"<sup>113</sup> If § 2-709(1)(a) did not supplant the common law mitigation rule and thus nullify any requirement that the seller undertake resale when practicable, there would be no point to that provision. The seller's rights under the acceptance clause of § 2-709(1)(a) would duplicate his rights under § 2-709(1)(b), which grants the seller the price of conforming goods, accepted or not, "if the seller is

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110. 786 S.W.2d 502 (Tex. Ct. App. 1990).

111. *Id.* at 503 (interpreting TEX. BUS. & COM. CODE ANN. § 2-709(a)(1) (West 1968), which is identical to U.C.C. § 2-709(1)(a)).

112. The decision states, "F & P argues that the common law duty that a claimant mitigate damages creates a fact question of whether, under the circumstances of this case, the seller should have picked up the goods." *Id.*

113. U.C.C. § 2-709 cmt. 2 (emphasis added).

unable after reasonable effort to resell them at a reasonable price or the circumstances reasonably indicate that such effort will be unavailing.”<sup>114</sup>

We are now in a position to assess the effect of the action for the price in regulating the salvage of accepted goods. Section 2-709(1)(a) provides for two circumstances in which the seller can receive the price of conforming goods without first attempting a feasible and reasonable resale. A seller's right to the price is unqualified if the goods have been accepted or are identified to the contract and damaged. Both of these provisions constitute an exception to the common law rule requiring sellers to mitigate by effecting a reasonable resale if feasible. If the common law rule is efficient, we might doubt the efficiency of the Code's exceptions to it. The claim that the common law rule is efficient is supported by the first empirical assumption, which holds that sellers are generally more efficient resellers than buyers. The Code implicitly endorses this assumption in § 2-709(1)(b), which requires a seller to resell conforming goods that his buyer no longer desires, unless the seller has no comparative advantage over the buyer in reselling the goods.<sup>115</sup> Thus, the exceptions to the common law rule provided under § 2-709(1)(a) are efficient only if sellers do not have their typical comparative advantage in resale when reselling

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114. *Id.* § 2-709(1)(b). However, § 2-709(1)(a) can be distinguished from § 2-709(1)(b) without completely eviscerating the common law mitigation rule. Even if that rule cannot operate to bar a seller from recovering the price of accepted goods, it might nonetheless prevent the seller who forgoes a reasonable resale of accepted goods from recovering consequential damages. There is some question as to whether the Code entitles sellers to consequential damages under any circumstances. According to White and Summers, the courts that have considered the question so far have denied sellers consequential damages because of their reading of § 1-106(1) and the presence of § 2-715:

Consequential damages are specifically granted to the buyer under section 2-715. Section 1-106(1) states that consequential or other such damages are not available unless they are specifically provided for “in this Act or by other rule of law.” Reading the explicit grant in 2-715 together with the restriction in 1-106, courts have concluded that the drafters did not intend to give the seller consequential damages. The courts seem also to have concluded that the words “or otherwise resulting from the breach” in 2-710 itself do not authorize recovery of consequential damages.

WHITE & SUMMERS, *supra* note 6, § 7-16, at 338.

Notwithstanding the apparent judicial consensus denying the seller's consequential damages under the Code, however, there are compelling reasons to adopt the available interpretation of the Code that would allow sellers consequential damages. *Id.* § 7-16, at 338-40. Assuming the latter interpretation, a seller who is entitled to the price under § 2-709(1)(a) may not recover consequential damages that could have been avoided had he resold the goods. Typical examples of the seller's consequential damages in an action for the price might be losses due to interest payments on loans required by the buyer's delay in payment or loss of earned interest due to late payment. The common law mitigation rule could operate to bar the seller's recovery of these damages without also barring his recovery of the price. Because no appellate court to date has held that sellers are entitled to consequential damages, this possibility has never been raised. Thus, analysis of the action for price demonstrates that sellers have an unqualified right to the price of accepted goods, although in the event that sellers are entitled to consequential damages, the common law mitigation rule might exclude consequential damages avoidable by the seller's resale of accepted goods where the buyer requested such a resale.

115. Section 2-709(1)(b) implicitly endorses the assumption that sellers are typically better resellers than buyers because it requires sellers to prove that they could not effect a reasonable resale in order to compel the buyer to take (and presumably resell) the goods. If the Code were implicitly to endorse the opposite assumption, that buyers are typically better resellers than sellers, § 2-709(1)(b) would have reflected that assumption by requiring the buyer to prove that she could not effect a reasonable resale in order to compel the seller to take (and presumably resell) the goods.

damaged or accepted goods. Consider the clause of § 2-709(1)(a) that entitles the seller to the price of damaged goods after risk of their loss has passed to the buyer. As I argued above, there is certainly less reason to credit a seller of new goods with an advantage in reselling damaged goods than to credit him with an advantage in reselling used goods. Whatever advantages sellers generally have over buyers in reselling undamaged goods are likely to be reduced when goods are damaged. Whether the reduction in the cost-effectiveness of sellers' resale of damaged goods is likely to eliminate rather than merely reduce sellers' resale advantage is unclear. The exception to the rule requiring the seller to undertake any reasonable resale might be justified, then, if it is true that sellers' comparative advantage over buyers in resale is unlikely to obtain when reselling damaged goods. In the absence of the seller's inherently superior resale capacity, the empirical assumption that the party in possession or control of the goods is the superior reseller should guide the assignment of the salvage duty. And since the seller loses at least possession of the goods once risk of their loss passes to the buyer,<sup>116</sup> the damage clause of § 2-709(1)(a) is likely to be efficient.

Now consider the acceptance clause of § 2-709(1)(a). Given that the common law mitigation principle does not apply to the seller of accepted goods, the acceptance clause of § 2-709(1)(a) appears to exempt the seller from the duty to resell accepted goods. If the buyer could reject goods following acceptance, she could escape § 2-709(1)(a) and force the seller to make a reasonable resale if possible. But once a buyer has accepted goods, she no longer has the option of rejecting them.<sup>117</sup> Therefore, an accepting buyer will be able to compel the seller to resell goods only if she can revoke her acceptance. There is some question as to whether a revocation, like a rejection, can be procedurally effective but substantively wrongful. If it can be, then the acceptance clause of 2-709(1)(a) does not prevent the buyer of conforming goods from forcing the seller to resell the goods when the seller's resale is feasible.<sup>118</sup> On this interpretation of the revocation doctrine, the acceptance clause would appear to be consistent with the goal of facilitating the most efficient salvage of the goods. According to the first empirical assumption, the

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116. Under a contract that does not require carriage of goods, the risk of loss passes from a merchant seller to a buyer on the buyer's receipt of the goods, and from a nonmerchant seller on tender of goods. See U.C.C. § 2-509(3). When sellers tender goods, they are typically relieved of possession. Under a contract that requires carriage of goods, the risk of loss passes to the buyer when goods are duly delivered to the carrier by the seller or duly tendered at a given destination while in possession of the carrier, depending on whether it is a shipment or destination contract, respectively. See *id.* § 2-509(1). In both cases of carriage contracts, the risk of loss passes from the seller to the buyer after the seller has lost possession of the goods.

117. "Acceptance of goods by the buyer precludes rejection of the goods accepted." *Id.* § 2-607(2).

118. Similarly, if effective but wrongful revocations are possible, a buyer who accepts nonconforming goods whose nonconformity does not justify revocation nonetheless would potentially be able to compel a seller to resell the goods by improperly but effectively revoking her acceptance.



seller typically will be the superior reseller of goods in a failed transaction. The fact that the buyer accepted goods would not prevent her from compelling the seller to resell conforming goods, for she would still be free to make an effective, though wrongful, revocation. Yet commentators<sup>119</sup> and courts<sup>120</sup>

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119. Although they ultimately reject it, White and Summers identify the strongest textual argument in favor of interpreting the Code as allowing effective but wrongful rejections. They observe that 2-709(3) seems to contemplate at least some circumstances in which a buyer who has "wrongfully . . . revoked" will *not* be liable for the price. If only justified revocations free the buyer from his liability under 2-709(1)(a), then there would be no need to mention wrongful revocations in 2-709(3), for one who wrongfully revoked would always be liable for the price as one who "accepted" the goods. Moreover, 2-703 refers to wrongful revocation and rejection in tandem without apparent distinction.

WHITE & SUMMERS, *supra* note 6, § 7-3, at 296 (ellipsis in original). Although § 2-709(3) provides a significant textual argument for allowing effective but wrongful revocations, § 2-703 does not. That provision only provides that the seller has the right to take the goods back from a wrongfully revoking buyer and to sue for § 2-706 or § 2-708 remedies rather than suing for the price. *See* Roy R. Anderson, *The Code's Action for the Price: A Survey*, 1 GA. ST. U. L. REV. 27, 40 (1984).

White and Summers ultimately agree with the argument that follows from a straightforward interpretation of §§ 2-607(2) and 2-608:

2-607(2) states that buyer cannot revoke an acceptance he made with knowledge of a nonconformity unless he accepted on the reasonable assumption that the nonconformity would be seasonably cured. It would seem to follow *a fortiori* from this and from the grounds for revocation of acceptance stated in 2-608 that a buyer cannot revoke acceptance of conforming goods.

WHITE & SUMMERS, *supra* note 6, § 7-3, at 296. After rejecting an argument for allowing effective but wrongful revocation based on parallel construction with wrongful but effective rejection, White and Summers conclude that "any buyer who accepts goods is liable for the price unless he makes a procedurally effective *and* substantively *rightful* revocation of acceptance; we believe that a procedurally effective but substantively wrongful revocation should not free him from price liability under 2-709(1)(a)." *Id.* at 297.

Richard Alderman argues:

The term "wrongful revocation," as employed in Section 2-703, simply means that the buyer has failed to meet the requirements of Section 2-608. In other words, if the defect did not substantially impair the value of the goods or if they were accepted after inspection and without assurances that they would be repaired or if the defect was not discovered until after a reasonable time, then any attempt to revoke the acceptance is ineffective and wrongful. Under these circumstances, the seller is entitled to relief under Section 2-703.

1 RICHARD M. ALDERMAN, A TRANSACTIONAL GUIDE TO THE UNIFORM COMMERCIAL CODE § 1.68-20, at 368 (2d ed. 1983). Roy Anderson argues:

Can the buyer make a procedurally effective, wrongful revocation of acceptance, throw the goods back on the seller, and thereby avoid an action for the price? The answer is no. In fact, an effective but wrongful revocation is a misnomer; if it is wrongful, it is not effective. . . . Accordingly, it is a bit inelegant to distinguish between ineffective and wrongful revocations. However, there are cases in which the buyer did everything right (procedurally) to revoke, but he did not have a substantive basis for doing so. The buyer's revocation was thus wrongful and, accordingly, ineffective; the seller was entitled to the action for the price.

Anderson, *supra*, at 39-43.

120. The majority of courts that have considered the question directly argue that only a justified revocation of acceptance bars the seller from the price of accepted goods that he might feasibly resell. *See, e.g.,* Atlas Concrete Pipe, Inc. v. Roger J. Au & Son, 467 F. Supp. 830, 835 (E.D. Mich. 1979) (holding that despite fact that return of goods placed seller on notice of revocation, buyer cannot receive "credit" for returned goods against judgment for price because buyer did not meet requirements of § 2-608, and concluding that "[a]s Au had the burden of proving the acceptance of the pipe was properly revoked, Au's claim for credit in this regard is accordingly rejected, and Atlas is entitled to recover its price"); Plateq Corp. v. Machlett Lab., Inc., 456 A.2d 787, 790-91 (Conn. 1983) (upholding granting of price to seller on ground that, because buyer had failed to prove that goods were substantially nonconforming, "we can find no error in the conclusion that the defendant's cancellation constituted an unauthorized and hence wrongful revocation of acceptance"); Axion Corp. v. G.D.C. Leasing Corp., 269 N.E.2d 664, 667 (Mass. 1971) (upholding seller's action for price because buyer failed to establish substantial impairment of value, and

generally agree that only rightful revocations can be effective. As a textual matter, the language in the provision defining revocation as well as the comments in the Code support this view.<sup>121</sup>

It is possible simply to dismiss the judicial construction of the revocation doctrine and argue for the interpretation that allows the buyer to compel the seller to resell even conforming accepted goods when feasible. But if we take the received interpretation as controlling, we face the difficulty of explaining why it makes sense to exempt a seller from the duty to resell conforming goods following acceptance in a failed transaction.<sup>122</sup> Given this interpretation of revocation, the acceptance clause of § 2-709(1)(a) has the effect of entitling the seller to the price of all conforming goods accepted. The buyer who accepts conforming goods but then regrets her acceptance will lack the power to revoke and compel the seller's resale and will instead be liable for the price under § 2-709(1)(a). This result might be justified if sellers are not likely to be the most efficient resellers of accepted goods, which in turn might be the case if the assumption that sellers are better resellers is canceled or trumped by the assumption that the party in possession or control of the goods is likely to be the superior reseller. Acceptance serves as a good proxy for possession: Buyers who have accepted goods are likely to have those goods in their possession. Thus, one justification for interpreting the revocation doctrine to prohibit effective but wrongful revocations is that § 2-709(1)(a) prohibits the buyer from forcing the seller to resell goods when the seller has no comparative advantage in resale because buyer has possession of the goods.

But why would a breaching buyer intentionally force a seller to resell goods unless she believed the seller could resell more efficiently?<sup>123</sup> If the

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thus failed to meet its burden of establishing seller's breach: "If it met that burden, however, it *could* in proper circumstances revoke its acceptance . . ." (emphasis added); *Connor v. Bogrett*, 596 P.2d 683, 686 (Wyo. 1979) (upholding action for price on ground that since no express warranty regarding fitness of dog was granted by seller and buyer had accepted dog, "[the buyer] had no right to revoke his acceptance") *But see Dehahn v. Innes*, 356 A.2d 711, 720 (Me. 1976) ("[W]hen the buyer unjustifiably revokes his acceptance of the goods which he contracted to buy, as well as when he fails to receive and pay for the goods, the seller may recover the difference between the contract price and the fair market value of the goods at the time of the breach.").

121. Section 2-608(1) begins, "[t]he buyer may revoke his acceptance of a . . . unit whose non-conformity substantially impairs its value to him . . ." U.C.C. § 2-608(1). It is difficult to interpret this clause as allowing for the possibility of a revocation of goods that are conforming. Indeed, "[r]evocation of acceptance is possible only where the non-conformity substantially impairs the value of the goods to the buyer." *Id.* § 2-608 cmt. 2. This seems to entail that revocation is not possible unless the goods accepted are nonconforming. In addition, comment 5 to § 2-709 states that "'[g]oods accepted' by the buyer under subsection (1)(a) include only goods as to which there has been no *justified* revocation of acceptance, for such a revocation means that there has been a default by the seller which bars his rights under this section" *Id.* § 2-709 cmt. 5 (emphasis added).

122. Similarly, an explanation is needed for why the seller should be exempted from the duty to resell nonconforming goods whose acceptance the buyer cannot rightfully revoke.

123. If the buyer is the nonbreacher, and has accepted nonconforming goods, then the explanation for why she would want to force the seller to resell the goods, even though she is the more efficient reseller, is straightforward. She might want to avoid the risk of being undercompensated for her resale expenses. Thus, by preventing the nonbreaching buyer from revoking her acceptance, because of her failure to satisfy all of the requirements of § 2-608, the Code exacerbates rather than reduces the nonbreacher's risk of

buyer intends to pay the seller's damage bill, wouldn't she have the incentive to reduce rather than increase the costs of breach? The answer is that the buyer might be breaching strategically, hoping to exploit the possibility of undercompensating the seller's incidental and other damages. If the seller is prohibited from suing the buyer for the price, all of the seller's alternative remedies in effect require him, in most cases, to resell the goods in order to recoup his losses.<sup>124</sup> Theoretically, these costs are recoverable under § 2-710 as incidental damages. But in practice, it is difficult for a seller to recover his true resale costs. For these include not only tangible expenses for shipping, telephone calls, transportation and the like, but intangible opportunity costs as well. These remedies thus expose the seller to a significant risk of undercompensation in addition to the risk of systematic undercompensation that all nonbreachers face. In addition, the seller's price remedy under § 2-709(1)(b) and his resale remedy under § 2-706 expose him to the risk of protracted litigation over the respective questions of whether a reasonable resale was possible and whether the resale he conducted was reasonable. The risk of such litigation entails not only the risk of incurring attorney's expenses and the like, but also the risk of being denied full recovery should the court find either that a reasonable resale was feasible or that the resale conducted was not reasonable.<sup>125</sup>

By prohibiting the breaching buyer of accepted goods from imposing further incidental costs on the nonbreaching seller, § 2-709(1)(a) can be defended as a prophylactic against the seller's risk of undercompensation. This is because the action for the price, unlike the seller's other remedies, allows

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undercompensation.

124. The seller's first alternative remedy is § 2-706(1), which simply entitles him to resell the goods and sue for the difference between the resale price and the contract price. The seller's second alternative remedy is § 2-708(1), which entitles him to the difference between the market price and the contract price at the time of tender. This remedy is designed to mirror the § 2-706(1) remedy without requiring an actual resale. In some cases, the buyer breaches before goods are identified or identifiable to the contract and resale is therefore not possible. Section 2-708(1) provides the seller with a remedy in that event. In other cases, goods are identified or identifiable to the contract, and § 2-708(1) preserves the seller's right to retain the goods and either use them or sell them at a later time. In most cases, a seller receiving § 2-708(1) damages will have to recoup his loss from the breached contract by reselling the goods. The third alternative remedy for the seller is provided by § 2-708(2) and entitles him to the profit he lost as a result of the breach. In theory, § 2-708(2) is designed to compensate the "lost volume" seller whose resale of the goods would not compensate him for the lost sale to the breaching buyer. Even the lost volume seller, however, must resell the goods in addition to suing for his lost profit in order to recoup his losses from the buyer's breach. The only cases in which resale is not necessary for the seller to recoup his losses are those in which the seller's use value of the goods exceeds their resale value.

125. As explained in the discussion of undercompensation, these latter risks are analogous to the risks Goetz and Scott subsume under the "breacher-status" problem. See *supra* note 85 and accompanying text. Recall that the breacher-status problem is that the nonbreacher takes the risk of subsequently being held to have breached himself should he attempt to mitigate following a perceived anticipatory repudiation by the other party. In the present context, the problem is that the seller, (1) by failing to resell and suing for the price under § 2-709(1)(b), takes the risk of subsequently being held to have failed to undertake a feasible resale, or (2) by reselling following buyer's breach, takes the risk of being held to have failed the standard of reasonableness for a resale. In either event, the buyer's breach subjects the seller to the risk of undercompensation due to an improper mitigation decision.

him to recover at least direct damages<sup>126</sup> without reselling the goods. Thus, by interpreting the revocation doctrine as barring wrongful but effective revocations, § 2-709(1)(a) then might provide the seller with a hedge against systematic undercompensation and the strategic behavior it makes possible. By permitting the seller to recover the price without attempting a reasonable resale, § 2-709(1)(a) allows the seller to eliminate his risk of undercompensation of incidental resale damages. Of course, § 2-709(1)(b) also allows the seller to reduce this risk of undercompensation, but only if a reasonable resale is not feasible.<sup>127</sup> Section 2-709(1)(a) eliminates the seller's risk of litigation over whether a reasonable resale was feasible. And by assuring an award of the price to a seller of accepted goods, § 2-709(1)(a) eliminates the possibility that the seller will have to resell even when feasible and thereby eliminates the possibility of litigation over whether an actual resale was reasonable. Finally, § 2-709(1)(a) provides the seller with the same protection from undercompensation that a § 2-709(1)(b) award provides: it reduces the seller's risk of undercompensation by eliminating the possibility of valuation errors that attends the calculation of a market price/contract price differential under § 2-708(1) or lost profits under § 2-708(2). The action for the price is the seller's specific performance; it guarantees him the benefit of his bargain.<sup>128</sup>

Even though the Code forbids the buyer to revoke wrongfully but effectively, however, it permits her to reject wrongfully but effectively. Thus, the Code forces the seller to undertake resale of the goods when feasible, despite the possibility that the wrongfully rejecting buyer might be breaching strategically. Why should the concern about protecting the seller against the possibility of the buyer's strategic breach be more compelling once goods have been accepted? One reason is that acceptance might serve as a device for sorting strategic from nonstrategic buyers. The buyer who wrongfully rejects conforming goods may be less likely to be strategically breaching than a wrongfully revoking buyer. The fact that a buyer initially (1) explicitly accepted the goods, (2) accepted the goods constructively by retaining possession of the goods for a period exceeding the time for a reasonable inspection, or (3) accepted the goods constructively by acting inconsistently with the seller's ownership of the goods, might indicate that the wrongfully

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126. As noted earlier, the action for the price arguably does not allow the seller to recover consequential damages, either because the Code bars the seller from recovering any consequential damages, or because the seller is barred from recovering consequential damages that he could have mitigated, for example, by executing a feasible resale. *See supra* note 114.

127. As noted above, a seller's decision not to resell unaccepted goods exposes him to the risk that a court will disagree with him that resale was not feasible.

128. Section 2-709(1)(a) might not, however, thereby guarantee the seller his full expectation measure because his consequential damages might be limited (1) if the Code bars such recovery, or (2) if the common law mitigation rule bars the seller's recovery of foreseeable losses that could be mitigated, for example, by resale. *See supra* note 114.

revoking buyer is less likely to concede breach and pay the seller's incidental damage bill for reselling the conforming goods and more likely to contest the goods' conformity as well as the reasonableness of the seller's incidental damage bill. Thus, acceptance might indicate that the buyer is likely to attempt to exploit the potential of undercompensating the nonbreacher through real or threatened litigation.

But why should we believe that buyers who breach following acceptance would be more likely to be strategic breachers than buyers who breach by wrongfully rejecting goods? Absent a persuasive answer to this question, the interpretation of the Code as prohibiting effective but wrongful revocations appears to be inconsistent with the Code's rule permitting effective but wrongful rejections.

Perhaps the key to justifying the view that wrongful revocations are ineffective is that § 2-709(1)(a) would then function as a temporal limitation on the seller's vulnerability to undercompensation. Just as the Code shifts the burden of proof to the buyer upon acceptance, thus greatly reducing the seller's risk of being found to have breached, it similarly shifts upon acceptance the risks of the seller's undercompensation attending the resale requirement of § 2-709(1)(b). Perhaps the Code's response to the seller's and buyer's risk of systematic undercompensation is to provide a temporal cap or limit on a portion of that risk. Once a transaction reaches the stage of acceptance, the seller's risk of undercompensation is reduced and the buyer's is increased. The buyer is therefore able to control her risk exposure by rejecting goods, and the seller limits his risk exposure by insuring for certain kinds of undercompensation up until the point of acceptance but not beyond. Acceptance might be thought of as a quasi-statute-of-limitations for the seller's risk of undercompensation of incidental resale expenses and for the risks attending litigation over the feasibility or reasonableness of resale.

This rationale for interpreting the revocation doctrine as prohibiting effective but wrongful revocations is the same as the rationale underlying the efficiency trade-off story: it seeks to offset systematic undercompensation by permitting suboptimal mitigation. Given this interpretation, the acceptance clause of § 2-709(1)(a) reduces the seller's exposure to undercompensation by exempting him from the responsibility to mitigate efficiently. This doctrine makes sense only if the expected benefits of reduced undercompensation and strategic buyer behavior outweigh the expected costs of inefficient mitigation.

#### E. *The Analysis of the Code's Regulation of the Salvage of Goods Assuming Imperfect Legal Information*

So far, the analysis of the Code's rules governing the salvage of goods in failed transactions has presupposed that at the time the parties make their salvage decisions, they know whether rejection or acceptance has occurred and

whether the tendered goods are conforming. Given this assumption of perfect legal information, the salvage of rightfully rejected goods is likely to be efficient, except when the buyer's use of the goods is the most efficient salvage of the goods. But given that the risk of undercompensation for the buyer is arguably at its highest in this case, freeing the buyer from the duty to adjust to the goods might be defended as the lesser of two efficiency evils. The salvage of accepted goods, however, is unlikely to be efficient, except on the view that freeing the seller from the duty to resell goods is necessary to avoid exposing the seller to an unacceptably high risk of undercompensation, even when seller's resale constitutes the most efficient salvage of the goods.

However, even if the Code's salvage regime constitutes a reasonably efficient compromise between the competing goals of efficient salvage and minimized undercompensation given the assumption of perfect legal information, the analysis changes significantly when that assumption is relaxed. The efficiency of the Code's rules depends on the ability of the parties, at the time they make their salvage decisions, to predict a court's *ex post* determination of whether acceptance, rejection, or revocation has occurred and whether the tendered goods were conforming. A realistic analysis of the Code's regulation of the salvage of goods must take the perspective of the parties at the time of their salvage decision. If the parties are uncertain as to whether acceptance, rejection, or revocation has occurred and whether the goods tendered were conforming or nonconforming, the Code's salvage rules will be unlikely to lead to efficient salvage decisions. Both of these determinations are matters for judicial determination *ex post*. In those cases in which the parties cannot predict judicial outcomes with reasonable certainty at the time they must decide whether and how to salvage the goods, the parties will be unable to determine their salvage obligations. As a result, the *ex ante* salvage decisions the parties must make may not lead to the *ex post* results desired.

### 1. *The Cause of Imperfect Legal Information at the Time of Salvage*

It is reasonable to suppose that in the run-of-the-mill case, judicial determinations of acceptance, rejection, and revocation will be easy for the parties to predict at the time they make their salvage decisions. There are certainly many cases that are never litigated because the buyer's express rejection is unambiguous and unquestionably timely, or her acceptance is either clear and explicit or created by an obviously inordinate lapse of time following delivery. Similarly, in many cases a buyer's revocation will not be in doubt because it is clearly based on the seller's promise of cure<sup>129</sup> or on the

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129. The buyer may revoke her acceptance if the nonconformity of the goods substantially impairs the goods' value to the buyer and the buyer accepted the goods "on the reasonable assumption that [their]

discovery of an obviously substantial and latent defect, and the buyer's notice of revocation is unquestionably timely.

There are, however, a significant number of cases in which the judicial determination of acceptance, rejection, and revocation is more difficult for the parties to predict. One reason parties might have difficulty predicting the result of such a judicial determination is the crucial role played by undefined temporal elements in the definitions of acceptance, rejection, and revocation.<sup>130</sup> Acceptance and rejection require a "reasonable opportunity" to inspect.<sup>131</sup> Rejection must be within a "reasonable time" after delivery or tender and requires "seasonable notification" to the seller. A buyer can revoke only if the seller failed "seasonably" to cure and the attempted revocation occurs within a "reasonable time" after the buyer discovers or should have discovered the defect. What constitutes a "reasonable time" is a matter of usage of trade, course of dealing, or course of performance as well as judicial policy. As a result, the judicial construction of a "reasonable time" varies considerably from case to case.<sup>132</sup>

For example, in *Miron* the buyer was barred from rejection by waiting less than twenty-four hours after delivery to inspect and notify the seller of rejection;<sup>133</sup> in another case, in which boxed wrench sets were sold, the buyer's rejection more than six weeks following delivery was held to be effective.<sup>134</sup> To be sure, relevant distinctions between the goods in different contracts help explain these variances, such as the differences between the likelihood of a buyer causing injury to a horse and a buyer causing a defect in wrench sets as the time following delivery increases. Yet differences between cases are not always obvious. In a case involving the sale of sheets of high tensile steel, the court held that rejection seven weeks after delivery was

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non-conformity would be cured and it has not been seasonably cured." U.C.C. § 2-608(1)(a).

130. Another source of uncertainty surrounding a determination of rejection and revocation is that the buyer might send the seller an ambiguous sign of rejection or revocation, for example, by complaining that she "has some trouble with the goods." Such ambiguous signals subject the nonbreaching seller to the breacher-status problem discussed earlier. See *supra* text accompanying note 85. Although the alternative salvage regime I sketch below does not purport to solve this problem, I do suggest an approach for reducing it. See *infra* part III.

131. The U.C.C. independently provides the buyer's right to inspect within a reasonable time before payment or acceptance: "Unless otherwise agreed . . . where goods are tendered or delivered or identified to the contract for sale, the buyer has a right before payment or acceptance to inspect them at any reasonable place and time and in any reasonable manner." U.C.C. § 2-513(1).

132. The Code's explicit attempt to reduce uncertainty and subjectivity in the administration of these temporal requirements is entirely unhelpful. U.C.C. § 1-204(1) states that "[w]henver this Act requires any action to be taken within a reasonable time, any time which is not manifestly unreasonable may be fixed by agreement." Section 1-204(2) states that "[w]hat is a reasonable time for taking any action depends on the nature, purpose and circumstances of such action." Section 1-204(3) states that "[a]n action is taken 'seasonably' when it is taken at or within the time agreed or if no time is agreed at or within a reasonable time."

133. *Miron v. Yonkers Raceway, Inc.*, 400 F.2d 112 (2d Cir. 1968).

134. *Zimmerman v. Bass & Sons, Inc. (In re H.P. Tool Mfg. Corp.)*, 37 B.R. 885, 888 (Bankr. E.D. Pa. 1984).

ineffective.<sup>135</sup> Although courts and scholars have attempted to explain why the reasonable time in which to reject steel wrench sets should be greater than the reasonable time in which to reject sheets of steel,<sup>136</sup> it is doubtful that contracting parties will always be able to discern these rationales and predict with precision the period of time beyond which a court will hold that rejection can no longer be effective.

In addition to these loosely defined temporal elements, acceptance and revocation rely on other imprecisely defined notions. The subtleties of the judicial determination of what constitutes a wrongful "exercise of ownership by the buyer" following rejection<sup>137</sup> or "any act inconsistent with seller's ownership"<sup>138</sup> are sometimes difficult for contracting parties to discern.<sup>139</sup> Similarly, it is difficult in some cases to predict whether a court will find that a good's nonconformity "substantially impairs its value" to the buyer,<sup>140</sup>

135. *Michael M. Berlin & Co. v. T. Whiting Mfg., Inc.*, 5 U.C.C. Rep. Serv. (Callaghan) 357, 360-61 (N.Y. Sup. Ct. 1968).

136. The court in *Berlin* argued that inspection of the thickness of the sheets of steel would have been easy and free of significant costs, *id.* at 360; the court in *Zimmerman* held that inspection of the wrench sets would have been difficult and costly. But the court's rationale in *Zimmerman* was that "the only way that [the buyer] could have discovered the non-conformity was to have opened each carton and then unfold the wrench kits which were individually rolled up in a vinyl-like pouch." 37 B.R. at 887. An effective inspection, however, does not require that the buyer inspect *each* of the wrench sets delivered. The court in *Zimmerman* could have easily seized upon the fact that the buyer never even attempted an inspection of the wrench sets but could have inspected at least a sample of them at little cost.

137. U.C.C. § 2-602(2)(a). This provision and § 2-606(1)(c) together provide that a buyer's exercise of ownership following rejection is wrongful and constitutes an acceptance that overrides the previous, effective rejection.

138. *Id.* § 2-606(1)(c).

139. For example, one court has interpreted a wrongful "exercise of ownership by the buyer" following rejection, under U.C.C. § 2-602(2)(a), to sustain an effective rejection, even though the buyers continued for six weeks to live in the mobile home they purchased. See *Minsel v. Rancho Mobile Home Ctr., Inc.*, 188 N.W.2d 9, 12 (Mich. Ct. App. 1971). Another court interpreted "any act inconsistent with the seller's ownership," under § 2-606(1)(c), to permit a buyer of a mobile home to live in the mobile home for 10 months following his revocation of acceptance without transforming the revocation into an acceptance. See *Jorgensen v. Pressnall*, 545 P.2d 1382, 1386 (Or. 1976). Yet in another case, a court barred a buyer from revoking acceptance because, *inter alia*, he lived in it for over a year following his attempted cancellation and prior to returning it to the seller. See *Bowen v. Young*, 507 S.W.2d 600, 605 (Tex. Civ. App. 1974). Although there may be sound judicial policies underlying each of these cases, parties may not always be able to discern these policies and their implications for their case at the time of their salvage decision. Moreover, the decisions interpreting "exercise of ownership by the buyer" and "any act inconsistent with the seller's ownership" vary more considerably among cases regarding different kinds of goods and different sorts of uses. For example, a court found that a buyer who discovered defects after partially installing kitchen units had thereby accepted the units. See *Cervitor Kitchens, Inc. v. Chapman*, 513 P.2d 25, 28 (Wash. 1973). Although variance between industries could in principle provide for more consistency and predictability *within* industries, the variance in Code interpretation in the mobile home cases suggests otherwise.

140. The Code and courts clearly interpret the requirement in § 2-608(1) that the goods' "non-conformity substantially impairs its value to [the buyer]" as a question of subjective impairment. Thus, the test is not what the seller had reason to know at the time of contracting, the question is whether the non-conformity is such as will in fact cause a substantial impairment of value to the buyer though the seller had no advance knowledge as to the buyer's particular circumstances.

U.C.C. § 2-608 cmt. 2. The court in *Jorgensen* stated that the question of substantial impairment "is a subjective question in the sense that it calls for a consideration of the needs and circumstances of the plaintiff who seeks to revoke; not the needs and circumstances of the average buyer. The existence of



whether it will find that acceptance "was reasonably induced" by the difficulty of discovery of the defect<sup>141</sup> or by the seller's assurances,<sup>142</sup> or whether there was "any substantial change in condition of the goods which is not caused by their own defects."<sup>143</sup> The fact that acceptance, rejection, and revocation are determined by the trier of fact and that therefore juries will often be making that determination also potentially increases the likelihood that the parties will have difficulty predicting whether acceptance, rejection, and revocation have occurred. Even if judges rule on these questions consistently and predictably by advertent to policy-based distinctions between different cases, juries are less likely to understand these policies and thus are less likely to make decisions resulting in a coherent, predictable interpretation of these doctrines.<sup>144</sup>

Finally, in a significant number of cases the parties will be uncertain how a court will rule on the question of conformity. There are two reasons for this uncertainty. First, whether the seller has tendered conforming goods might turn on the interpretation of the contract's performance standards over which the

substantial impairment depends upon the facts and circumstances in each case." 545 P.2d at 1384-85 (footnotes omitted). Given the subjective nature of the inquiry, whether a court, much less a jury, will find substantial impairment so understood may be difficult to predict in some cases. For example, one court held that a buyer could revoke his acceptance of a new car on the ground that the car was missing its spare tire and the car dealer could not immediately provide it. *See Colonial Dodge, Inc. v. Miller*, 362 N.W.2d 704, 707 (Mich. 1984).

141. For example, consider the finding in *Zimmerman v. Bass & Sons, Inc. (In re H.P. Tool Mfg. Corp.)*, 37 B.R. 885, 887 (Bankr. E.D. Pa. 1984), that the acceptance of packaged wrench sets by a buyer "was reasonably induced because of the difficulty of discovering the non-conformity." In that case, the defect was that the wrenches delivered "which were unpolished, did not conform to the type ordered which had a highly polished finish with the 'Blue Line' label inscribed thereon." *Id.* The court found this defect difficult to discover even though merely opening one box of wrenches at the time of delivery presumably would have revealed it. It certainly is not a paradigm case of a latent defect only discoverable long after an initial inspection.

142. *Compare Morrisville Comm'n Sales Inc. v. Harris*, 34 U.C.C. Rep. Serv. (Callaghan) 1190 (Vt. 1982) (buyer purchases cow without inspecting its mouth upon seller's representation that cow is "clean, good, healthy, ready to be a milker"; cow is in fact toothless; buyer may revoke) with *Scaringe v. Holstein*, 38 U.C.C. Rep. Serv. (Callaghan) 1595, 1596 (N.Y. App. Div. 1984) (buyer purchases automobile in reliance on seller's newspaper advertisement of car as in "excellent condition"; despite fact that seller's representations were false, they were "puffery" and buyer may not revoke).

143. *Compare Intervale Steel Corp. v. Borg & Beck Div.*, 578 F. Supp. 1081, 1087 (E.D. Mich. 1984) (holding that stamping out of steel into parts constitutes substantial change in condition) with *Alimenta v. Anheuser-Busch*, 803 F.2d 1160, 1164 (11th Cir. 1986) (holding that blanching of peanuts does not constitute substantial change in condition of goods) and *Lackawanna Leather Co. v. Martin & Stewart Ltd.*, 38 U.C.C. Rep. Serv. (Callaghan) 475, 481-82 (8th Cir. 1984) (holding that processing of hides to remove hair and salt and splitting them does not constitute substantial change in condition); *compare Roy Burt Enter. v. Marsh*, 400 S.E.2d 425, 427 (N.C. 1991) (holding that spreading and absorption of contaminated fertilizer by soil does not constitute substantial change in condition of goods) with *Ace Chem. Corp. v. Atomic Paint Co.*, 229 S.E.2d 55, 57 (N.C. Ct. App. 1976) (holding that use of nonconforming acetone in manufacturing process constitutes substantial change) and *Western Paper Co. v. Bilby*, 783 P.2d 980, 982 (Okla. Ct. App. 1989) (holding that processing and printing of nonconforming labels constitutes substantial change).

144. The fact that juries often decide questions about acceptance, rejection, and revocation also undermines the argument that courts can consistently effect rational policy through the use of vague and manipulable doctrines. *See* discussion of courts' ability to allocate the burden of proof efficiently, *supra* text accompanying note 39.

parties disagree. Such was the case in *Frigalment Importing Co. v. B.N.S. International Sales Corp.*<sup>145</sup> In that case, the buyer claimed the contract term “chicken” meant a “young chicken, suitable for broiling and frying,” while the seller contended it meant “any bird of that genus that meets contract specifications on weight and quality, including what it calls ‘stewing chicken’ and [the buyer] pejoratively terms ‘fowl.’”<sup>146</sup> After a lengthy analysis, Judge Friendly found in favor of the seller’s interpretation, but the opinion was not based on facts and reasoning so evident and controlling that the parties could or should have known at the time that their dispute arose that the seller’s claim would prevail. Had a salvage issue arisen in the case, the buyer and seller arguably would have been quite uncertain about the court’s likely ruling, and so, as I argue below, would be uncertain about their respective rights and duties to salvage the goods.

The second reason the parties might be in doubt as to whether a court will find that the goods tendered were conforming is that they might disagree about the condition of the goods when tendered. The parties’ ability to prove conformity at tender will depend on whether and when an inspection occurred, who conducted it, and how thorough it was.<sup>147</sup> In addition, the difficulty of discovering the defect at tender as well as the likelihood the defect was caused by the buyer’s post-tender activity will be relevant.<sup>148</sup>

## 2. *The Effects of Imperfect Legal Information on the Code’s Salvage Regime*

In this Subsection, I illustrate the possible disparity between the *ex post* ideal and the *ex ante* reality of the Code’s salvage rules by isolating the effects on the parties’ salvage decisions when they cannot predict with reasonable

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145. 190 F. Supp. 116 (S.D.N.Y. 1960).

146. *Id.* at 117.

147. Thus, in *Miron v. Yonkers Raceway, Inc.*, 400 F.2d 112 (2d Cir. 1968), the court held that the buyer of a horse who discovered a defect the day after delivery could not carry his burden of proving the defect existed at the time of delivery. Had the court found that one day was a reasonable amount of time to inspect the horse, the buyer may have carried his burden as an accepting buyer, or may have been held to have rejected, thus placing the burden on the seller. In this case, the placement of the burden of proof, itself a function of whether acceptance or rejection occurred, is dispositive of the question of conformity at the time of tender.

148. In many cases, even if the parties are certain about which party will bear the burden of proving conformity, they will be unable to predict whether that party will be able to carry the burden. The facts are often ambiguous. *See, e.g.*, *Bickett v. W. R. Grace & Co.*, 12 U.C.C. Rep. Serv. (Callaghan) 629 (W.D. Ky., 1972) (holding that plaintiff-buyers who showed only poor results from their planting of seed without any specific proof as to how seed was defective or how defect caused loss claimed did not meet their burden of establishing defect); *Latham & Assocs. v. William Ravets Real Estate, Inc.*, 218 Conn. 297 (1991) (placing burden of proof on seller to show that computer system malfunction was due to buyer’s operator error and not system hardware or software); *Alliance Wall Corp. v. Ampat Midwest Corp.*, 477 N.E.2d 1206 (Ohio Ct. App. 1984) (holding that buyer alleging tender of defective aluminum panels presented no persuasive evidence that seller was responsible for defects or that goods were damaged while risk of loss was on seller).

certainty at the time of their decision the court's determination of acceptance, rejection, revocation, or conformity of tender. I begin by assuming that the parties know whether the goods tendered in a failed transaction were conforming.

a. *Analysis Assuming Perfect Knowledge of Conformity and Imperfect Knowledge of Acceptance, Rejection, and Revocation*

Even if the parties know whether the goods in a failed transaction are conforming, their salvage decisions still depend upon whether the buyer has accepted, rejected, or revoked acceptance. Consider, for example, how the parties would make their salvage decisions if they knew the goods tendered were nonconforming and were in the possession or control of the buyer.<sup>149</sup> If rejection or revocation has occurred, the merchant buyer must resell perishables in the absence of the seller's instructions and follow the seller's instructions to salvage nonperishables.<sup>150</sup> If after a reasonable time the seller offers no instructions, the merchant buyer has the option of storing, reselling, or returning nonperishable goods to the seller.<sup>151</sup> In the event the seller directs the merchant buyer to resell the goods, the buyer's duty to carry out the resale is conditional upon the seller immediately meeting the buyer's demand for indemnity of the expenses she will incur in reselling the goods.<sup>152</sup> On pain of giving the merchant buyer unfettered discretion to salvage the goods by reselling them, storing them, or returning them, the seller must take care to direct the buyer to salvage nonperishables and to indemnify her for the salvage expenses if requested.<sup>153</sup> A nonmerchant buyer has no duty to salvage the goods other than merely to hold them for the seller's disposition.<sup>154</sup> And the seller must take care to retrieve goods from the nonmerchant buyer if the

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149. For purposes of illustrating the gap between the *ex post* ideal and the *ex ante* reality of the Code's salvage system, I will restrict the analysis in the text to the salvage decisions of the parties when the buyer is in possession or control of the goods when the transaction fails. The same point can be made, however, by taking an *ex ante* perspective on the parties' salvage decisions when the seller is in possession or control of the goods.

150. U.C.C. § 2-603(1).

151. *Id.* § 2-604.

152. *Id.* § 2-603(1).

153. *Id.*

154. *Id.* § 2-604 & cmt.

goods are to be salvaged at all.<sup>155</sup> On the other hand, after acceptance, both merchant and nonmerchant buyers are required by the common law mitigation rule to mitigate their damages by salvaging the goods. If the seller does nothing, the buyer is still under an obligation to maximize the value of the goods either by reselling them or by using them. The seller has no right to direct the salvage of the goods and the buyer has no right to demand indemnity for any resale she might undertake.

Thus, the buyer's salvage decision depends crucially on whether acceptance, rejection, or revocation has occurred. For example, a buyer might have to decide whether, in the absence of the seller's instructions, her interests are protected by storing nonperishable goods for the seller's account. If the buyer wrongly believes she has rejected, she might store the seller's goods and bypass a resale opportunity required of accepting buyers under the mitigation rule. Similarly, a seller might need to decide whether he must direct the salvage of the goods or salvage them himself, or whether he can instead rely on the buyer to salvage the goods. If the seller wrongly believes that a merchant buyer has accepted, he might fail to direct the salvage of the goods and the merchant buyer may exercise her right, as determined *ex post*, simply to store goods whose value might have been maximized through resale. If the seller wrongly believes that a nonmerchant buyer has accepted, the nonmerchant buyer may exercise her right, as determined *ex post*, simply to hold the goods at the seller's disposition and the seller might bypass a superior opportunity to resell the goods.

Now suppose the parties knew the goods were conforming and the buyer had possession or control of them. If rejection has taken place, the buyer can leave resale to the seller unless the seller is unable to resell the goods. If acceptance has taken place, the seller has no duty or incentive to resell. If the buyer wants the goods resold, she must resell them herself. If the buyer wrongly believes she has rejected the goods, she may fail to resell them, wrongly believing that the seller will bear the loss of the forgone resale opportunity. If the seller incorrectly believes that the buyer has accepted, he might forgo a resale opportunity wrongly believing that the buyer will bear that loss.

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155. Section 2-604 allows the merchant and nonmerchant buyer to store nonperishable goods in the absence of the seller's instructions. Although the merchant buyer has a duty to resell perishable goods even without the seller's instructions under § 2-603, the nonmerchant buyer does not. Moreover, even though the buyer's options under § 2-604 are conditional upon her not receiving reasonable instructions from the seller, and this condition might appear to apply to both merchant and nonmerchant buyers, only merchant buyers are required to follow the seller's instructions. There is no provision that requires a nonmerchant buyer to follow seller's instructions. The comment to § 2-604 explicitly limits the requirement to follow seller's instructions to the merchant buyer: "[T]he buyer's right to act under [§ 2-604] is conditioned upon . . . the absence of any instructions from the seller which the *merchant-buyer* has a duty to follow under [§ 2-603]." *Id.* § 2-604 cmt. (emphasis added).

Whenever salvage decisions are based on incorrect or considerably uncertain predictions of the outcome of a subsequent finding of acceptance, rejection, or revocation, the resulting salvage of goods is more likely to be inefficient. No system of rules can ensure predictable, much less optimal, results when the parties governed by those rules have difficulty determining which rules apply at the time of their decision to act. Even if following the rules would lead to optimal results, any difficulty the parties have in determining which rule applies to them will undermine their ability to follow the rules. Moreover, because the Code's salvage system is based on rough empirical generalizations, even following the rules will sometimes lead to suboptimal results. In cases where the Code's salvage rules fail to assign the salvage duty to the most efficient salvor, the parties sometimes will be able to make *ex post* bargains in which one party pays the other to undertake the most efficient salvage. But these *ex post* bargains themselves are less likely to take place if the parties are uncertain about their legal salvage rights and duties. Thus, if the parties cannot reliably determine which rules apply at the time of their salvage decision, they will not only have difficulty following the rules and effecting the salvage decision the Code contemplates, but may also have difficulty bargaining around the Code's rules when the rules allocate salvage duties to the less efficient salvor.

If the parties are uncertain about their salvage duties at the time they make their salvage decisions, that uncertainty will decrease the probability that they will act in accordance with the Code's salvage regime. Such uncertainty is therefore likely to undermine the claim that the Code's regime in fact achieves the optimal trade-off between efficient salvage and reduced undercompensation contemplated by the efficiency trade-off story. To illustrate, I will consider how the parties' uncertainty could undermine the salutary effects of those Code rules exempting the nonbreacher from salvage duties.

First, consider the undercompensation rationale for the rule allowing the buyer to reject nonconforming goods and thus to avoid a potential mitigation requirement that she adjust to the goods and use them. The rationale might be that the rule allows the buyer to avoid suing for damages that are difficult to prove, and instead permits her to purchase conforming goods on the market. As a result, the buyer can sue for the difference between her cover price and contract price, plus her incidental expenses. She need not prove that adjusting to the seller's nonconforming goods constituted a reasonable mitigation of her damages; nor need she demonstrate the extent of her damages due to the costs of adjustment. Because the costs of adjustment are likely to be difficult to prove, permitting the buyer to reject nonconforming goods—even when her use of the goods might constitute the most efficient salvage of them—might be justified in order to protect her from undercompensation. The buyer can rely on the protection of the Code's salvage rules, however, only to the extent that she can predict whether a court will find she has rejected the goods. If at the

time of her salvage decision, she knew a court would find she had effectively rejected, she could then decide to minimize her exposure to undercompensation by ignoring the option of using the goods while suing for damages. But if she is uncertain whether a court might instead determine that her rejection was ineffective—for example, because it was too late—a decision to forgo using the goods might constitute a failure to mitigate and result in a reduction of her compensable damages. Similarly, in the absence of the seller's instructions, she might choose simply to store the seller's goods instead of reselling them herself, in order to avoid exacerbating her risk of undercompensation. However, that choice is predicated on her having the rights of a rejecting buyer. Thus, if she makes that choice and is subsequently determined to have accepted the goods, her decision might constitute a failure to mitigate.

Second, consider the undercompensation rationale for the rule allowing the seller to avoid resale of conforming goods once the buyer accepts the goods. The efficiency trade-off story suggests that acceptance might be thought of as a quasi-statute-of-limitations for the seller's risk of undercompensation, both with respect to incidental resale expenses and due to the risks attending litigation over the feasibility or reasonableness of resale. The efficiency trade-off story rationalizes the seller's entitlement to the price under § 2-709(1)(a) as an effort to protect him from these sources of undercompensation. But a seller will be able to benefit from this protection only to the extent that at the time of the salvage decision he can determine whether a court will later find that acceptance has occurred. If he cannot make this determination with reasonable certainty, such a benefit will be unavailable to him.

b. *Analysis Assuming Imperfect Knowledge of Conformity and Perfect Knowledge of Acceptance, Rejection, and Revocation*

Now consider how the buyer's and seller's duties to salvage depend on which party has breached. Assume that the buyer has possession or control of the goods and that the parties know that rejection has taken place. If the goods are conforming, the buyer need not resell the goods unless resale is not feasible for the seller. If the goods are not conforming, a merchant buyer must follow the seller's reasonable instructions to salvage nonperishables and must resell perishables in the absence of the seller's instructions.<sup>156</sup> A nonmerchant buyer need only hold conforming goods at the seller's disposal, but will suffer a loss if she bypasses an opportunity to salvage conforming goods the seller could not feasibly resell.<sup>157</sup> A seller of (rejected) conforming goods must

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156. *Id.* § 2-603.

157. See discussion of § 2-604, *supra* note 155.

resell them if feasible<sup>158</sup> but can direct a merchant buyer in possession or control of the goods to resell them if they are nonconforming.<sup>159</sup>

Assume now that the buyer has possession or control of the goods and that the parties know acceptance has taken place. Whether or not the goods are conforming, the buyer must undertake any salvage of the goods herself. Salvage is required to mitigate her damages if the accepted goods are nonconforming, and if they are conforming, the seller is entitled to the price. But a seller of accepted goods has different incentives depending on whether or not the goods are conforming. If they are conforming, he is free from any duty or incentive to salvage. If they are nonconforming, he can rely on the buyer's mitigation-based duty to salvage the goods. However, if the seller's resale is the superior salvage option, he might volunteer to resell the nonconforming accepted goods to reduce the damages he would have to pay the buyer.<sup>160</sup>

Given that the parties' rights, duties, and incentives to salvage turn in important respects on which one of them has breached, their abilities to make efficient salvage decisions will be seriously impaired when they are in doubt as to which party a court will find to be the breacher. As a result, the parties may make decisions contrary to their duties and interests, and the resulting salvage may be inefficient.

#### F. *Summary of the Analysis of the Code's Regulation of the Salvage of Goods*

The Code regulates the salvage of goods by relying either on the mitigation requirement or on specific salvage provisions requiring the parties to resell or adjust to the goods. Because the mitigation requirement fails to impose a duty to salvage goods on rightfully rejecting buyers, even if doing so would be efficient, the Code imposes express salvage duties on them. Given our three empirical assumptions, the analysis assuming perfect legal information suggests these duties will yield the most efficient salvage of the goods, except in some cases in which the buyer's use is the most efficient salvage. By rejecting nonconforming goods, the buyer avoids the responsibility for salvaging the goods by using them.

In addition, although the Code generally requires the seller to resell conforming goods when feasible, it exempts him from this duty when the buyer has accepted the goods. However, this inefficient allocation of duties can

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158. Strictly speaking, the seller of rejected conforming goods is never per se required to salvage the goods. But under § 2-709(1)(b), he will be barred from recovering the price if he can resell the goods at a reasonable price. And under the common law mitigation principle, he will be barred from recovering losses avoidable by salvage.

159. U.C.C. § 2-603(1).

160. Of course, the seller might deliberately forgo an opportunity to resell the goods for greater profit than the buyer's resale in order to benefit from expected undercompensation of the buyer's incidental resale expenses.

be defended. To the extent *ex post* bargains reallocate inefficient salvage duties, the ultimate salvage of the goods will be efficient. According to the efficiency trade-off story, the costs created by these bargains and by the inefficient salvage of goods when these bargains do not occur are justified because they are less than those that would result from a per se rule requiring the efficient salvor to salvage. Such a rule would exacerbate the nonbreacher's risk of undercompensation.

Once the perfect legal information assumption is relaxed, however, this story becomes less plausible. The Code's salvage regime will achieve the desired balance between efficient salvage and reduced undercompensation only to the extent that the parties can determine with reasonable probability how a court will rule on acceptance, rejection, revocation, and conformity. In those cases in which such a determination is not possible, the Code's rules are unlikely to lead to the results contemplated by the efficiency trade-off story. Although I provided a number of reasons for believing that the perfect legal information assumption is unrealistic, the actual extent and significance of legal uncertainty affecting the Code's salvage regime is, of course, an empirical question. There is no doubt, however, that at least in some cases, the parties' uncertainty about their salvage duties undermines the Code's regime.

### III. DECOUPLING THE REGULATION OF SALVAGE FROM UNDERCOMPENSATION

The goal of minimizing the joint expected costs of salvaging goods in a failed transaction is difficult to achieve. The challenge is to design salvage rules that reduce the expected costs of salvaging the goods without creating additional costs that outweigh these benefits. Rules that reduce the expected costs of salvaging the goods create three kinds of costs. First, the rules can create uncertainty. When rules are uncertain, parties cannot reliably regulate their behavior and plan to conform with their obligations. If the parties are uncertain of which salvage rule applies at the time they make their salvage decision, the most efficient salvor mistakenly might not undertake the efficient salvage even if the rules were perfectly designed to ensure efficient salvage. Second, as I argued above, salvage rules potentially exacerbate the nonbreacher's risk of undercompensation. Third, they require the parties to "stand ready" to assist in salvage following performance. Both parties must pay the costs of bearing the risk that they will have to participate in salvaging the goods following performance. The longer their exposure to this risk, the greater the cost. Thus, an efficient salvage regime is one that decreases the actual costs of salvage without creating a greater increase in the parties' uncertainty, risk of undercompensation, and standing-ready costs.

In this Part, I sketch an alternative salvage regime that not only eliminates the Code's sources of uncertainty, but also eliminates the trade-off between



efficient salvage and reduced undercompensation. Of course, the problems of uncertainty and efficiency trade-offs will to some extent confront any salvage regime. But by decoupling the salvage regime from undercompensation rules, and by virtually eliminating the role of the acceptance-rejection fulcrum in both, the alternative regime is likely to minimize both effects.<sup>161</sup> By charging the party in possession with the duty to direct the salvage of goods, the alternative regime minimizes the incidence of uncertainty by replacing the relatively difficult determinations of rejection, acceptance, revocation, and breach with the relatively clear and simple determination of which party is in possession. Although the regime also requires the parties to exchange estimates of salvage costs, I argue that this uncertainty is unavoidable in any efficient salvage regime and over time will be far less than the uncertainty under the Code. The alternative regime also uses independent procedural rules tailor-made for reducing the potential increase in the risk of undercompensation created by otherwise efficient salvage rules. Thus, by protecting the mitigating nonbreacher with procedural rules at the time of litigation, the alternative regime decreases the breacher's opportunity for strategic behavior. As a result, the regime can require the efficient salvor to salvage in every case without fear of increasing the risk of undercompensation. Although the alternative regime increases the risk of overcompensation, I argue that the expected losses due to the efficiency trade-off in the Code's regime will far exceed the marginal expected costs due to possible overcompensation under the alternative regime.

A. *An Illustration of the Code's Regime: The Possibility for Improvement*

Before considering potential improvements on the design of the Code's salvage regime, I begin with simple illustrations of the two kinds of cases in which the Code's salvage regime might result in an inefficient salvage of the goods, even when the parties are certain about whether acceptance, rejection,

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161. The Code's trade-off results from the fact that the Code addresses the goals of efficient salvage and reduced undercompensation with the same set of rules. I claim that if salvage and reduced undercompensation are treated independently, separate rules can be designed to achieve the same reduction in undercompensation without sacrificing efficient salvage. The case for the alternative regime I propose ultimately turns on the empirical question of whether the net benefits achieved by the efficiency trade-off in the Code's regime are less than those achieved by the alternative regime. Although empirical data cannot be adduced to settle the question, the defense of the alternative regime relies on two intuitive claims. The first is that the alternative regime fares better when compared to the more realistic view of the Code's regime. Given that the parties will be uncertain of their salvage duties at least in some cases, and given that in those cases the Code's regime will not function as the efficiency trade-off story predicts, the alternative regime, which avoids these uncertainties, is likely to be more efficient. According to this perspective, the Code's regime is inferior to the alternative regime, even in light of the underlying approach of the efficiency trade-off story. The second claim is that the net benefits of the alternative regime are likely to be greater than those one would expect under the Code's regime, even assuming the Code's regime functions precisely as the efficiency trade-off story would have it. The alternative regime fares better in a side-by-side comparison between the results it would be expected to produce and the results described in the analysis of the best case scenario of the Code's regime in Parts II.C and II.D. The argument for the alternative regime succeeds if either of these empirical claims can be sustained.

or revocation has taken place and whether the goods are conforming. The gaps in the Code's salvage rules allow the rightfully rejecting buyer to avoid adjusting to and using nonconforming goods<sup>162</sup> and the seller of accepted goods to avoid reselling them,<sup>163</sup> even when doing so constitutes the most efficient salvage. The inefficiencies created by these gaps are exacerbated by any uncertainties surrounding the parties' salvage responsibilities.

Suppose that the seller and buyer contract for the sale of 100,000 #1 ball bearings for \$10,000 and the buyer plans to use the bearings to manufacture hub assemblies for retail. Suppose further that when performance is due under the contract, the seller tenders #2 ball bearings even though he had no reasonable expectation that the buyer would accept them despite their nonconformity.<sup>164</sup> Finally, suppose that the buyer can use those bearings to make the hub assemblies of equivalent market value by increasing the width of the bearing sockets in the hubs, but that in order to produce these equivalent hubs on schedule, the buyer must expend \$500 to adjust the factory to drill wider bearing sockets. Alternatively, the buyer could resell the #2 bearings at a cost of \$700 and the seller could resell them at a cost of \$600. In this example, the most efficient salvage of the goods is for the buyer to adjust her factory and use the #2 bearings. But under the Code's salvage regime, the buyer has the option of rejecting the #2 bearings and thus forcing their resale at a minimum cost of \$600.<sup>165</sup> If the buyer exercises her right of rejection, she will increase the joint costs of the seller's breach by at least \$100.<sup>166</sup>

One justification for permitting the buyer to reject the goods in this case is that the parties will have difficulty determining whether, in any given case, the expected cost of the adjust-and-use option is less than the resale option. The parties might have difficulty making this determination for two reasons. First, the buyer and seller do not know each other's salvage costs. Under the Code regime, the buyer stands to gain by bargaining *ex post* with the seller for the buyer's adjustment and use of nonconforming goods. Since each party's reservation price in an *ex post* bargain equals his or her cost of salvage, neither

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162. See *supra* part II.C.

163. See *supra* part II.D.

164. If performance were not yet due under the contract, or if seller had reasonable grounds for believing the #2 ball bearings would be acceptable with or without a money allowance, then the seller would have the right to cure the nonconforming tender under § 2-508(1) or (2), respectively. In this case, however, the seller has no right of cure.

165. If the bearings are in the buyer's possession and the seller has no agent in the buyer's city, then the seller's resale costs will include not only the \$600 but also the costs of retrieving the bearings or selling them long distance. If these costs exceed \$100, the seller will direct the buyer to resell the bearings for him despite the seller's lower internal resale costs.

166. Note that even if the seller did have the right to cure in this case, that right has no effect on the problem created by the buyer's right to reject the nonconforming goods in the example. The buyer is free to reject the nonconforming goods even though the most efficient salvage of these goods would require her to adjust to and use them. The seller's right to cure only affects the question of whether the seller's tender of the nonconforming goods constitutes breach, not whether the buyer has a right to reject them when tendered.

party has an incentive to reveal that information. One party can use such information strategically in negotiating a larger share of the gains from the bargain. Second, even if both parties revealed their expected salvage costs, the buyer's estimate of the full expected costs of the adjust-and-use option will sometimes be too speculative to be reliable. In addition to the difficulty of determining when the buyer's adjust-and-use option provides the most efficient salvage of the goods, however, the chief justification for not requiring the buyer to adjust even when doing so is clearly efficient is that such a requirement exacerbates her exposure to undercompensation. The seller can now contest the reasonableness of the buyer's incidental damage bill for adjustments. Once the buyer is forced to adjust to nonconforming goods, the seller can threaten to impose on her further costly and undercompensated litigation expenses.

Now consider a variant on the above example. Suppose that the seller tenders conforming #1 bearings to the buyer who accepts them. But one month later, the buyer realizes that by using #2 bearings she can reduce her total manufacturing costs by more than \$10,000. Suppose that she can resell the #1 bearings for \$9000 at a cost of \$700, but the seller could resell them for the same price at a cost \$500. In this example, assuming the buyer cannot wrongfully but effectively revoke her acceptance,<sup>167</sup> the seller will have a right to the \$10,000 contract price from the buyer who will be unable to compel the seller to resell the bearings for her. She may be able to strike an *ex post* bargain with the seller to resell the bearings for her, but if the expected cost of negotiating such a bargain exceeds \$200, the bargain will not be rational.

There are two reasons for not requiring the seller to resell the bearings in this case. The first reason is that such a requirement will exacerbate his risk of undercompensation.<sup>168</sup> That requirement enables the buyer to contest both the timeliness of the seller's resale and the reasonableness of the resulting incidental expenses. The seller will thus face increased expected undercompensation of litigation expenses. The second reason is that requiring a seller to stand ready to participate in salvaging conforming goods tendered, accepted, and paid for imposes costs on him. At some point, the costs of bearing this risk exceed the expected joint benefits from any agreement that requires the seller to salvage the goods when he can do so at less cost than the buyer.<sup>169</sup> It is worth noting, however, that the Code does require a seller to

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167. For the argument that wrongful revocations are ineffective, see *supra* notes 119–28 and accompanying text.

168. If in most cases the buyer's costs of resale will be no greater than the seller's costs of resale, then a majoritarian default rule might not require the seller's resale in this case. But the empirical assumption I proposed earlier suggests that the opposite is true. Moreover, if we could determine accurately in each case which party had the least cost salvage option, there would be no need to use majoritarian default rules.

169. Note that under the Code's default rules, a seller cannot under any circumstances require the buyer to stand ready to return the goods to the seller in the event the seller regrets a successfully completed

stand ready to participate in the salvage of nonconforming goods paid for and accepted by the buyer. A buyer is allowed, under certain circumstances, to revoke her acceptance of nonconforming goods, and revocation requires the seller to participate in the salvage of the goods rather than simply paying damages.<sup>170</sup>

There are, then, four possibilities for improving the Code's salvage regime. The first is to create incentives for the parties to determine and reveal their expected costs of salvage. If the Code does not require the parties to make and share this determination when any transaction fails, its rules can be based only on rough approximations of the efficient allocation of salvage costs.<sup>171</sup> The second is to take additional measures to prevent salvage duties from exacerbating the nonbreacher's risk of undercompensation. The third is either to lengthen or to shorten the period of time the parties must stand ready to participate in salvaging goods following the buyer's acceptance and payment for the goods, depending on which option is expected to result in a net increase of the efficiency. The fourth is to reduce the uncertainties in the Code's salvage regime by reducing or eliminating the role of acceptance, rejection, revocation, and conformity in allocating parties' salvage duties. The following alternative salvage regime explores these possibilities.

#### B. *An Alternative Salvage Regime: A Sketch*

Any salvage regime must begin by creating some mechanism to enable the parties to determine that a transaction has failed and is therefore in need of salvage. Under the Code's regime, the seller's anticipatory repudiation and the buyer's rejection or revocation signal a failed transaction. The seller's anticipatory repudiation signals his breach and triggers the buyer's salvage responsibilities. The buyer's anticipatory repudiation signals her breach and triggers the seller's salvage responsibilities. The buyer's rejection signals her dissatisfaction with the seller's tender, and although it does not establish that

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transaction. Once the buyer accepts and pays for the goods, the seller has no remedies available to compel the buyer to return the goods. Section 2-703 lists all of the seller's remedies, *see* § 2-703 cmt 1, none of which are available against an accepting buyer who has paid the price. In theory, the joint maximization principle, and its attendant joint loss reduction requirement, would support a rule requiring the buyer to return goods accepted and paid for if the seller regrets the transaction and could put the goods to a higher valued use. The seller should be able to reclaim the goods and pay the buyer damages. But the buyer's risk of undercompensation increases dramatically if she is required to return such goods and sue for damages. Her reliance damages would presumably be quite extensive and difficult to prove as time increases following acceptance. Thus, though joint maximization may require the parties to undertake joint loss reduction following a completed transaction, the costs of implementing that principle outweigh the efficiency gains.

170. "A buyer who . . . revokes has the same rights and duties with regard to the goods involved as if he had rejected them." U.C.C. § 2-608(3). These rights and duties often require the seller's active participation in salvage. *See id.* §§ 2-603 to 2-604.

171. The three empirical assumptions made earlier provide the basis for such approximations under the Code's salvage regime. *See supra* text accompanying notes 89-91

the seller has breached, it does establish that someone has breached. In the event a court determines that the seller's tender was conforming, the buyer's rejection itself will constitute breach. In either case, rejection signifies that a breach has occurred and triggers the parties' salvage duties. Similarly, the buyer's justified revocation signifies the seller's breach and triggers the buyer's salvage duties.<sup>172</sup>

The alternative I propose would leave the Code's anticipatory repudiation regime in place. It would also preserve the rejection, acceptance, and revocation doctrines, but only as devices to signal the failure of a transaction.<sup>173</sup> The buyer would signal to the seller that she believes his tender is nonconforming by rejecting or revoking. The doctrine of revocation would be modified to become effective once the seller is given notice of revocation. The salvage obligations of the parties following notice of rejection or revocation would be determined by new salvage rules according to which the parties' obligations to salvage goods do not depend on whether the goods tendered are conforming and thus whether the buyer's rejection or revocation is rightful.<sup>174</sup> These rules would require that the party in possession of the goods at the time of rejection or revocation take responsibility for directing the salvage of the goods. The principal virtue of this rule is that the party responsible for directing salvage can be readily determined initially by the parties at the time of rejection or revocation, and later by a court should the case be litigated.<sup>175</sup> That party would be charged with deciding whose resale

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172. The buyer's unjustified revocation will constitute breach only if accompanied by her refusal to pay or otherwise perform under the contract.

173. The alternative salvage regime also leaves in place § 2-508, the Code's cure provision. Under the Code, a buyer has a right to reject nonconforming goods and the seller has the right to cure a nonconforming tender if the time for performance has not elapsed, or if the seller had reasonable grounds to expect the buyer would find the tender acceptable with or without a money allowance. *See* U.C.C. § 2-508. Under the alternative regime, a buyer has a right to reject nonconforming goods and the seller has the right to cure in the same circumstances as under the Code. If the buyer rejects an offer to cure to which the seller is entitled, the buyer is in breach, just as she is under the Code. Similarly, the seller's right to cure has no effect on the parties' salvage duties. The difference between the two regimes lies in the salvage duties of the parties following buyer's rejection, irrespective of whether cure was attempted. Under the Code, a buyer who rejects a cure, whether improperly or not, has no duty to use the goods, even if that option clearly maximizes the salvage value of the goods. If she is a nonmerchant, she has no duty to resell them, even if that is the most efficient salvage option. If the seller is in possession, the buyer has no duty to resell them, even if that is the most efficient option. As I present the alternative regime below, a buyer who rejects a cure, whether improperly or not, will have the duty to undertake the most efficient salvage of the goods as determined by the parties' salvage estimates. The party in possession makes that determination. Thus, because the cure rule in the Code affects only the underlying contractual liability and not the parties' salvage duties, it has no effect on the alternative salvage regime. Cure is simply an option that allows a seller to avoid breach by retendering conforming goods. It does not determine which party should salvage nonconforming goods.

174. As a result, §§ 2-602(2), 2-602(3), and 2-604 would be unnecessary. These provisions specify the parties' salvage rights and duties depending on whether the buyer has rejected or accepted the goods.

175. Another virtue of this rule is the intuitive appeal of assigning the salvage directorship to the party most likely to be the most efficient salvor. However, nothing more than intuition supports this rule over any number of other clear and easily administered rules for assigning the salvage directorship. Even if the party in possession or control of the goods is most likely to be the more efficient salvor of the goods, that fact alone does not provide a reason for assigning the salvage directorship to that party. For once the parties

or adjustment and use would be more efficient. In order to make this decision, the party directing the salvage would have the right to request that the other party reveal its expected costs of salvage, and that party would be under an obligation to provide a reasonable estimate of its salvage expenses in good faith. Both the fact of the other party's refusal to provide this estimate and the fact of deliberate misrepresentation in providing salvage estimates would be admissible in court as evidence of that party's bad faith. In the event that such a party turns out to be the breacher, a showing of his bad faith would provide the basis for estopping him from alleging that the party directing the salvage failed to mitigate adequately. In the event the party directing the salvage is determined to be the breacher, a showing of the other's bad faith would provide the basis for a conclusive presumption of the nonbreacher's failure to mitigate. In addition, the information the other party provides to the party directing salvage can be used by the former to carry his burden of proving the reasonableness of his salvage decision.

The party who actually undertakes the salvage of the goods, then, will do so either by exercising his own power to undertake salvage if he is in possession of the goods at the time of rejection or revocation, or by following the directions of the other party if he is not in possession. If the former turns out to be the nonbreacher, he can submit any incidental damage bill in good faith. He would bear the burden of production to establish the reasonableness of his bill, but the breacher would bear the risk of nonpersuasion on the question of whether the bill is unreasonable.<sup>176</sup> If the party undertaking the salvage of the goods turns out to be the breacher, and that party was also in possession of the goods and thus directing the salvage, he internalizes the cost of his salvage decision. However, if he was not in possession of the goods, and therefore salvaged at the nonbreacher's direction, he can object subsequently in court that the nonbreacher's decision to assign to him the duty of salvaging the goods was unreasonable and therefore constituted a failure to mitigate damages. Although the breacher would bear the risk of nonpersuasion on the question of the reasonableness of his salvage decision, the nonbreacher would

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signal each other that the transaction has failed, both parties ordinarily will participate in the salvage decision process, and the salvage director will be free to conclude that the non-director is the superior salvor because he is in possession or control of the goods. There is no obvious gain from assigning the salvage directorship to the party most likely to be the more efficient salvor. Moreover, if there were, the party in possession might not be that party, for the assumptions of the seller's comparative resale advantage and the buyer's comparative use advantage suggest that the most efficient salvor will vary from case to case.

176. For the difference between the burden of production and the risk of nonpersuasion, see *supra* discussion and sources in note 22. Under the Code, the buyer bears the burden of proving her incidental damages. See 4 RONALD A. ANDERSON, *ANDERSON ON THE UNIFORM COMMERCIAL CODE* § 2-715:14, at 507 (3d ed. 1983); WHITE & SUMMERS, *supra* note 6, § 6-5, at 266, § 10-3, at 439; see also *In re Repco Prods. Corp. v. Reliance Elec. Co.*, 8 U.C.C. Rep. Serv. 2d (Callaghan) 950, 969 (Bankr. E.D. Pa. 1989); *Skyline Steel v. A.J. Dupuis Co.*, 648 F. Supp. 360, 374 (E.D. Mich. 1986); *Traynor v. Walters*, 10 U.C.C. Rep. Serv. (Callaghan) 965, 975-77 (M.D. Pa. 1972); *Bob Anderson Pontiac v. Davison*, 293 N.E.2d 232, 237 (Ind. Ct. App. 1973).

bear the burden of production.<sup>177</sup> But the nonbreacher will have had the opportunity to create a record vindicating her decision. That record should include estimated salvage figures from the breacher and comparisons to his own estimated salvage costs.

To see how this salvage regime would work, consider the two examples of ball bearing contracts discussed above. In the first example, the seller and buyer contract for the sale of 100,000 #1 ball bearings that the buyer plans to use to manufacture hub assemblies for retail. Assume that the seller tenders #2 ball bearings at the buyer's place of business and that the buyer takes possession. Upon the buyer's determination that the seller's tender is nonconforming, she could give the seller notice of her rejection of his tender. Since she is in possession of the goods, she would have the responsibility to direct the salvage of the goods. She would have the right to request the seller's estimated costs of using or reselling the #2 ball bearings, and the seller would have the obligation to comply with her request.

Assume next that the seller attaches no use value to the bearings but can resell them at a cost of \$600. Given that the buyer's cost of resale is \$700, she should direct the seller to resell if resale maximizes the value of the goods; but since the buyer can adjust and use the #2 bearings at a cost of only \$500, she should do so. If, however, the buyer still directs the seller to resell the goods, the seller can allege in court that the buyer's salvage decision was unreasonable. The buyer would bear the burden of production: She would have to establish the evidence of the reasonableness of her decision to direct the seller to resell the goods and that evidence would have to reveal comparisons of the parties' respective costs of salvage, including their estimated costs of

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177. Courts are divided on the question of who bears the burden of proving the reasonableness of a buyer's mitigation under the Code. A number of courts have held that this burden is on the seller. *See, e.g.,* John S. Herbrand, Annotation, *Buyer's Incidental And Consequential Damages From Seller's Breach Under U.C.C. § 2-715*, 96 A.L.R. 3d 299, 341-42 (1980) (listing cases in Arkansas, Minnesota, Nebraska, Oregon, and Pennsylvania (federal district court applying Pennsylvania law)); *see also* Cates v. Morgan Portable Bldg., 42 U.C.C. Rep. Serv. (Callaghan) 451 (7th Cir. 1985) (applying Illinois law); *Skyline Steel*, 648 F. Supp. at 377 (applying Michigan law); *Harper & Assocs. v. Printers, Inc.*, 730 P.2d 733, 736-37 (Wash. Ct. App. 1986) (applying Washington law). A number of courts have also held that this burden is on the buyer. *See, e.g.,* Herbrand, *supra*, at 342-43 (listing cases in Iowa, Nebraska, New York, and Texas).

Courts allocating the burden of proof to the seller reason that failure to mitigate is a defense to a damages claim, and so must be pleaded by the seller. *See, e.g., Skyline Steel*, 648 F. Supp. at 377. Nebraska places the burden on the seller to prove mitigation by means other than cover, but places the burden on the buyer to prove mitigation by cover. *See, e.g., National Farmers Org. v. McCook Feed & Supply*, 243 N.W.2d 335, 340 (Neb. 1976). Courts placing the burden on the buyer make proof of appropriate mitigation an element of the damages claim. There is no apparent trend, temporal or otherwise, in this allocation of burdens. As Judge Posner noted in *Cates*, given the Code's regime, the issue is not easy to resolve on policy grounds:

On the one hand the plaintiff has easier access to information about his own efforts to mitigate damages. On the other hand he is more likely to mitigate his damages than to trust entirely to his legal remedies for breach of contract, and on this ground similar disputes over burden of proof in tort cases have been resolved in favor of placing the burden of proof on the defendant . . .

42 U.C.C. Rep. Serv. (Callaghan) at 455-56 (citing *W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS* § 451, at 458 (5th ed. 1984)).

adjustment. The seller, however, would bear the risk of nonpersuasion on the question of the reasonableness of the buyer's salvage decision.

If the seller retained possession of the #2 ball bearings following the buyer's rejection, then the seller would have the power to direct the salvage of the goods. After requesting the buyer's estimated costs of salvage, the seller could either resell or direct the buyer to resell or adjust to and use the goods. If the buyer submitted a good faith estimate stating her \$500 cost of adjustment, the seller would direct her to adjust and use the goods. The buyer would then be entitled to reimbursement of the expenses she incurred and the seller would bear the burden of proving her incidental damage bill unreasonable. This proof would be particularly difficult if her incidental damage bill corresponded to her estimated cost of adjustment.<sup>178</sup>

Now consider the second example. In that case, the seller tenders conforming #1 bearings to the buyer who accepts them. One month later, the buyer realizes that by using #2 bearings, she can reduce her manufacturing costs by more than \$10,000. She would then notify the seller that she is revoking her acceptance. Since she is in possession of the bearings, she would have the right to direct the salvage of the goods. She would ask the seller to estimate his costs of resale. Since his expected cost of resale is \$500 and hers is \$700, she would direct the seller to resell the bearings. The seller in turn would be entitled to reimbursement for his incidental resale costs and the buyer would bear the burden of proving them unreasonable.

As these examples demonstrate, this alternative salvage regime eliminates many of the sources of uncertainty that potentially undermine the efficiency of the Code's salvage regime. As I have demonstrated, the efficiency of the Code's salvage regime requires that acceptance, rejection, revocation, and conformity can be determined with reasonable certainty at the time the parties make their salvage decision. Under the alternative salvage regime, the buyer can trigger the parties' salvage obligations simply by giving the seller notice of rejection or revocation. The parties do not need to know if the buyer has accepted because whether the buyer's objection constitutes a rejection or revocation has no effect on the parties' salvage duties. In either case, the party in possession of the goods has the responsibility of directing the salvage of the goods. Similarly, whether the seller's tender was conforming has no effect on the party's salvage duties. Even if the parties are quite uncertain as to who will prevail on the question of conformity, they will be able to determine their salvage responsibilities with certainty following rejection or revocation.

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178. If the actual damage bill is less than the estimate, the breaching party would be required to pay only the actual damage bill. If the actual damage bill is greater than the estimate, then a court would determine whether the excess (1) was within the industry's acceptable margin of error for such estimates, (2) resulted from unanticipated and therefore excusing circumstances, or (3) resulted from the nonbreacher's bad faith. In the first two cases, the breacher must pay the actual damage bill. In the third case, the nonbreacher will be barred from recovery.



These examples also illustrate that this regime relies substantially upon the parties submitting good faith estimates of their salvage costs. But the rules are designed to reduce the nonbreacher's incentives to provide inaccurate salvage estimates. One reason the nonbreacher might overestimate her costs of salvage at the time of the salvage decision is that doing so will reduce the likelihood of her having to undertake salvage of the goods. The only reason a nonstrategic nonbreacher would want to avoid undertaking salvage is that doing so exacerbates her risk of undercompensation. But under the proposed burden-of-proof rules, the nonbreacher's risk of undercompensation is minimal as long as she has evidence of a good faith estimate of her costs. The breacher bears the risk of nonpersuasion on the question of the reasonableness of the nonbreacher's salvage decision and incidental damage bill. A fear of undercompensation, therefore, is unlikely to lead the nonbreacher to overestimate her expenses so that she avoids incurring incidental expenses. The strategic nonbreacher, however, might overestimate her salvage expenses to preserve her option of submitting, or threatening to submit, an inflated incidental expense bill if she undertakes the salvage of the goods. The principal deterrent to this behavior is the rule that presumes the nonbreacher's failure to mitigate if the breacher can establish that the nonbreacher's estimates or actual expenses were submitted in bad faith.

Thus, in both of these examples, the risk of undercompensation to the nonbreacher has been transformed into a risk of overcompensation to the breacher. In the first case, the breaching seller risks that the buyer will purposefully overestimate her costs of adjustment; in the second case, the breaching buyer risks that the seller will purposefully overestimate his costs of resale. In both cases, the breacher bears the risk of nonpersuasion on the question of the reasonableness of both the salvage decision and the incidental damage bill. This regime is therefore likely to reduce expected undercompensation only by increasing expected overcompensation.

In this sense, the alternative regime relies on the rationale of counterbalancing inefficient undercompensation with an inefficient mitigation rule. But the inefficiency is confined to the rule regulating the adjudication of the nonbreacher's incidental damages bill. The underlying duty to mitigate damages is not eliminated in order to reduce the nonbreacher's exposure to undercompensation. Rather, the nonbreacher is required to undertake efficient salvage and is protected by a procedural rule that may systematically overcompensate her. Although the alternative regime therefore creates a risk of overcompensating the nonbreacher's incidental expenses, it does not allow her to avoid the duty to salvage the goods if she is the most efficient salvor, as the Code does.<sup>179</sup>

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179. Of course, if the breacher anticipates that the nonbreacher will receive an overcompensatory award of incidental damages, then the breacher may forgo the opportunity to require the nonbreacher to

Even though the alternative regime eliminates most of the uncertainties in the Code's salvage regime, it does retain some of the Code's uncertain elements and introduces another source of uncertainty that the Code's regime avoids. First, the alternative salvage regime does not, as I have described it, reduce the uncertainty inherent in the rules governing the parties' communication of the failure of a transaction. In both the Code's regime and the alternative regime, the parties and the courts must determine whether the buyer has given effective notice of rejection or revocation. Just as the parties might strategically send an ambiguous rejection or revocation signal under the Code regime, so they might under the alternative regime. Although I do not propose to solve this problem here, it might be possible to reduce this uncertainty by designing boilerplate language for rejection and revocation and creating a rebuttable presumption against a finding of effective rejection or effective revocation when parties fail to use such language. Second, unlike the Code, the alternative regime relies upon the exchange of salvage estimates, a process that introduces other uncertainties into the parties' salvage decisions. The parties and courts must be able to determine the effort and expense required to comply with their duty to exchange salvage cost estimates. The alternative regime requires that salvage estimates be reasonable, but parties and courts might find it difficult to determine what constitutes a reasonable salvage estimate. Given that the task of estimating salvage costs is itself costly, a system that depends on the exchange of estimates must confront the trade-off between the benefits from increased accuracy of estimates and the additional costs of providing more accurate estimates. Obviously, it would be inefficient to require parties to generate estimates whose expected cost outweighs their expected benefits from increased salvage efficiency. Likewise, it would be inefficient to allow parties to forgo the possibility of increasing the accuracy of an estimate when the expected increase in the efficiency of salvage created by the marginal increase in the estimate's accuracy exceeds the expected cost of the measures required to increase the estimate's accuracy.

Merely defining a "reasonable salvage cost estimate" as one whose marginal cost equals its marginal benefit hardly provides a practical rule for the parties or the courts. Instead, the reasonableness of salvage estimates must be determined according to the Code's standard approach to all questions of interpretation: by using course of performance, course of dealing, and usage of trade.<sup>180</sup> Under the alternative salvage regime, the question of the reasonableness of salvage estimates would be determined by looking to the parties' previous estimates under the contract, their past practices in providing estimates in previous contracts, and the practices of other parties in the

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salvage the goods, even if the nonbreacher is the most efficient salvor

180. U.C.C. § 1-205 defines "course of dealing" and "usage of trade." U.C.C. § 2-208 defines "course of performance."

relevant industry that will develop under the alternative regime.<sup>181</sup> The ability of the parties and courts to determine the level of effort required to produce salvage estimates will depend upon the development of industry-wide practices and the corresponding development of case law adjudicating the reasonableness of salvage estimates. Over time, the uncertainty surrounding this question presumably would diminish significantly.

Thus, notwithstanding these sources of uncertainty in the alternative regime, it will considerably reduce, as compared to the Code's regime, the likelihood that the parties will be uncertain of their salvage responsibilities at the time of their salvage decision.<sup>182</sup> The parties' salvage decisions under the Code's regime turn, among other things, on whether a court will hold that a reasonable time has elapsed since tender, whether notice of rejection or revocation was seasonable, whether the buyer's use was inconsistent with the seller's ownership, and whether the buyer or seller is the breacher. As I have shown, whatever industry practices and judicial interpretations come to guide parties and courts in answering these questions bear at best an indirect relationship to the goal of efficiently salvaging goods. Under the alternative regime, the uncertainty is reduced to the question of what constitutes a reasonable salvage estimate. This is the one question that must be answered in any regime that seeks to achieve an efficient exchange of information necessary to effect efficient salvage.<sup>183</sup> The multiple and irrelevant questions generating uncertainty under the Code's regime are eliminated and replaced with the sole question that is relevant: Who can most efficiently salvage the goods?

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181. Under the Code, the nonbreacher's salvage decision is almost presumed to be reasonable and in good faith. *See, e.g.*, *Samarar Aluminum Co. v. Horizon Skylight Sys., Inc.*, 10 U.C.C. Rep. Serv. 2d (Callaghan) 383, 386 (Bankr. N.D. Ohio 1989); *Sullivans Island Seafood Co. v. Island Seafood Co.*, 390 So. 2d 113, 114 (Fla. Dist. Ct. App. 1980); *Buckeye Trophy, Inc., v. Southern Bowling & Billiard Supply Co.*, 3 Ohio App. 3d 32, 34 (1982) (holding buyer's actions in ignoring seller's instructions to reshipe to be reasonable and in good faith) ("[Section 2-603:6] was not enacted to make buyers liable for errors of judgment."). One reason for this presumption is that the Code does not require, and therefore case law has not developed, any process for verifying the parties' estimated salvage expenses at the time of salvage. In the absence of any evidence to the contrary, courts presume the nonbreacher's salvage decision to be reasonable and in good faith in order to protect the nonbreacher from an increase in expected undercompensation. The alternative salvage regime would require the parties to produce evidence of the reasonableness of their salvage decisions and would lead to case law defining the standards of reasonable salvage in various industries.

182. At the very least, the usage of trade and judicial decisions that will provide the content for the legal standards of "reasonable" and "good faith" salvage estimates will be no less clear than, for example, those that now provide the content for the legal standard, under § 2-606(1)(a), of a "reasonable opportunity to inspect."

183. As Goetz and Scott argue,

One can . . . derive a broad principle of mitigation by predicting how contractors would agree to cooperate if charged explicitly with designing a policy to cope with readjustment contingencies. The resulting mitigation principle would require each contractor to extend whatever efforts in sharing information and undertaking subsequent adaptations that are necessary to minimize the joint costs of all readjustment contingencies.

Goetz & Scott, *The Mitigation Principle*, *supra* note 9, at 973 (emphasis added).

In order to eliminate the uncertainty created by a salvage rule that requires the parties to determine whether a rightful revocation has occurred, the alternative salvage regime allows for wrongful but effective revocations. Once the buyer gives the seller notice of revocation, the seller can be required to participate in the salvage of the goods. By allowing a wrongful but effective revocation, the alternative regime thus reduces the uncertainty of the parties' salvage duties, but increases the seller's costs of standing ready. Although it may be possible to design a more subtle revocation rule that leaves greater uncertainty but creates smaller costs of standing ready,<sup>184</sup> the revocation rule I propose is supported by three considerations.

First, the rule has the virtue of simplicity and clarity. To determine the parties' salvage responsibilities, the only question the parties and courts must answer is whether there was notice of revocation. Second, the alternative regime considerably reduces the standing-ready costs. The seller's standing-ready costs stem from the risk that he will be undercompensated for his true incidental expenses of participating in salvage. The burden-of-proof rules governing these expenses favor the nonbreacher. If those rules adequately protect the nonbreacher from undercompensation, there is less reason to be concerned that this increase in the seller's exposure to participating in the salvage of conforming goods will be unduly costly for the seller. Third, the alternative regime's revocation rule creates expected joint gains absent from the Code's regime. Instead of permitting the seller to refuse to provide cost-effective salvage assistance following the completion of a successful transaction, it requires the seller to reduce the joint costs of a regret contingency whenever such assistance would be cost-effective.<sup>185</sup> Thus, the increase in standing-ready costs arguably will be outweighed by both the decrease in uncertainty costs and the decrease in the expected costs of any regret contingency following the completion of the transaction.

### C. *Summary of the Alternative Salvage Regime*

The alternative salvage regime is designed to improve upon the Code's salvage regime. It purports to do so by (1) eliminating both the buyer's ability to avoid adjusting to nonconforming goods that are rejected and the seller's

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184. For example, a wrongful but effective revocation might be allowed only when the seller is liable for the defect. Thus, if a seller properly disclaimed any warranty for defects after five years following acceptance, a buyer's wrongful revocation for a defect alleged in the third year following acceptance would be effective. But a buyer's revocation in the sixth year following acceptance would not be effective. Such a rule enables sellers to limit not only their underlying contractual liability, but the temporal duration of their salvage responsibilities as well. It also requires the parties to determine the nature and extent of their underlying contractual obligations, however, in order to determine their salvage responsibilities. The rule therefore increases the parties' expected uncertainty about their salvage responsibilities at the time of their salvage decision.

185. See *supra* note 64.

ability to avoid reselling conforming goods that are accepted when those activities are expected to provide the most efficient salvage of goods in failed transactions, (2) facilitating the exchange of information at the time of the parties' salvage decisions in order to ensure that the most efficient salvor salvages the goods, (3) eliminating the role of acceptance, rejection, revocation, and nonconformity in determining the parties' salvage responsibilities, thereby eliminating the major source of uncertainty in the Code's regime, and (4) extending the seller's responsibility to participate in the salvage of conforming goods accepted by the buyer. The alternative salvage regime does create other potential sources of inefficiency that the Code's regime avoids. The salvage-exchange process introduces uncertainty into the alternative regime, and thus may counterbalance the greater certainty achieved by eliminating acceptance, rejection, revocation, and nonconformity from the Code's salvage rules. I have argued, however, that course of performance, course of dealing, and usage of trade will facilitate adjudication of uncertainties in the salvage-exchange process and that the alternative regime will evolve into more certain rules for determining salvage duties than those created by the adjudication of the Code's rules. Although the seller's risk of undercompensation under the alternative regime's revocation rule is greater than his risk under the Code's regime, I have argued that the alternative regime's burden-of-proof rules reduce the seller's expected undercompensation so as to yield a net gain from the increased efficiency of salvage that that rule facilitates.

It is difficult to demonstrate that this regime is more efficient than the Code's regime. Any salvage regime has costs and benefits that turn on complex empirical effects that are difficult to verify. My purpose in sketching this alternative regime is to illustrate the likely benefits of decoupling salvage and undercompensation rules from each other and from the acceptance-rejection fulcrum. Once we decouple these rules, we can design more efficient default rules than the common law and law-revision processes have produced. The most efficient regime is likely to be one explicitly designed to be efficient, rather than one that has simply evolved from processes not directly or exclusively concerned with promoting efficiency. Abandoning the acceptance-rejection fulcrum and using separate doctrines to allocate salvage duties and to reduce undercompensation would be a crucial step toward creating a more efficient salvage regime.

#### IV. CONCLUSION

A great deal has been learned from traditional economic analyses of contract and sales rules. Those analyses have uncovered the fundamental tensions between competing efficiency goals and have produced illuminating accounts of how contract and sales rules can be understood as striking an acceptable balance between them. But these rules have evolved through

common law adjudication and legal revision processes, neither of which explicitly sought to tailor or design rules to pursue economic efficiency. It would therefore be surprising if we couldn't do better if we tried. If our objective is to design optimal default rules rather than to rationalize existing default rules, a number of possible improvements come to mind. Each of these improvements is made possible simply by decoupling independent goals. By decoupling burden-of-proof from salvage rules, we are free to design an optimal burden-of-proof rule without trading off the efficiency of a salvage regime. By decoupling the rules governing the salvage of goods in failed transactions from those protecting the nonbreacher from undercompensation, we can design separate rules to achieve both more efficiently. And by decoupling all of these rules from the acceptance-rejection fulcrum, we not only avoid significant efficiency trade-offs, but we can replace the acceptance-rejection fulcrum itself with rules that are independently more efficient. Whether or not my arguments for the burden-of-proof rule and the salvage regime I propose are ultimately persuasive, I hope at least to have shown that there is considerable room to improve upon the Code's approach. In balancing proof, salvage, and undercompensation on the acceptance-rejection fulcrum, the Code unnecessarily reaches "for a single lump to solve all or most of the problems between seller and buyer . . ." <sup>186</sup> We can do better by following Llewellyn's lead and designing independent rules to achieve each goal more efficiently.

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186. Llewellyn, *supra* note 1, at 84.