MEMORANDUM

The memorandum analyzes the liability of Yo-Go in a breach of the installment contract with ADC. Yo-Go's primary defense is that ADC was in material breach and that no notice for termination was required. Our strategy is to emphasize that even a single delivery of bad milk may substantially impair the value of the entire installment contract. A broader theory of breach involves ADC's failure to deliver quality product over time. The biggest threat to our claim is that Yo-Go reinstated the contract.

1. A Single Shipment of Bad Milk can Substantially Impair the Contract

California's Commercial Code expressly states that even a single non-conforming installment in an installment contract can amount to a breach of the entire contract if it impairs the value of the entire contract.[1] ADC's delivery of milk that was unfit for human consumption is such a significant breach that the single shipment substantially impaired the value of the entire contract. Selling bad milk can cause illness or death. It can degrade consumer confidence and cripple a business. Both the state's standards for milk products and industry practice support this argument.

California Food and Agriculture statutes emphasize the extreme importance of safe milk products. *Cal. Food & Agr. Code 32906* provides: "It is unlawful for any person to sell, give away, deliver, or to knowingly purchase or receive any impure, polluted, tainted, unclean, unwholesome, stale or adulterated milk or cream, or any product which is manufactured wholly or in part from such milk or cream." *§35281* of the same code classifies any such violation as a misdemeanor and is punishable by both jail time and fines. With strong evidence that ADC's milk was tainted, its actions amounted to criminal activity. No reasonable interpretation of the parties' intent, as expressed in the 1993 agreement, would disallow immediate termination under these circumstances. This is especially true given that Yo-Go could also find itself criminally responsible for selling milk products manufactured with tainted milk because of ADC's actions.

Furthermore, industry practices also indicate that the provision of milk that meets health standards is essential to supply contracts. ADC itself enters contracts with other milk buyers that allow for immediate termination of a long-term contract upon "discovery and confirmation by credible evidence of a breach related to the safety or health aspects of the milk being purchased." (p. 7). This language indicates that a single shipment of unhealthy milk justifies terminating an entire installment contract.

ADC will argue that it had a termination clause in place from the 1993 MPA did not include a right to immediate termination for health risks. ADC will likely point to its other contracts to show that that parties would have included an express term if they intended to allow for an immediate termination. Moreover, they will also point out that Yo-Go continued to accept shipments for eighteen months after the sub-par shipment. ADC may argue that there is no "credible evidence" that the tainted milk originated with them. ADC will also argue, as it does in proposed jury instruction 28, that one bad shipment is relatively minor compared to the fourteen years and 5000 shipments that have been covered by this contract.

Although ADC's counter-argument may be persuasive at first blush, it can be countered. ADC has not supplied safe milk for fourteen years and 5000 shipments with only one bad shipment, as it claims. In fact, ADC has supplied two bad shipments in two years. Furthermore, Yo-Go has only recently learned that ADC knew the source of the unsafe milk (p. 3). Given these circumstances, the importance of safe milk, and the standard industry practice of terminating contracts with unsafe providers, the court should find that a single unsafe shipment did substantially impair the entire contract.

The benefit of using this argument is that is consistent with the judge's existing interpretation of the case. It will not require an additional procedural maneuver. However, it may be worthwhile to explore the options below, which place more emphasis on ADC's cover-up of the origin of the unhealthy milk.

[1] *Cal U Com Code §2612(3)*

Comment [GH1]: Nice succinct opener, with good attention to downsides.

Comment [GH2]: I think bringing in this context is excellent.

Comment [GH3]:

Comment [GH4R3]: Good attention to counterarguments. Note also their direct counterargument to 'criminal' above which is—this wasn't a 'knowing' delivery of bad milk and it was never repeated, making the risk of criminal prosecution effectively zero. But what is important about this line of analysis is how it can be leveraged into the critical importance of working together to discover the source of contamination and eliminate it.

Comment [GH5]: Good

Comment [GH6]: Good--more

Comment [GH7]: Nice attention to strategic considerations.

2. ADC Further Substantially Impaired the Contract by Covering-up the Origin of the Bad Milk

ADC may have breached more than a single installment of a recurring milk-for-money contract. The 1993 Milk Purchase Agreement ("MPA") was between two trusted parties—MAM and Yo-Go. The contract involved cooperation over time, delivery of healthful milk over time, third party testing over time, plus ADC's best efforts to deliver the expressly warrantied product and Yo-Go's exclusive buying of ADC Grade A milk—fit for human consumption.

We would argue that Yo-Go, after the January 2007 contamination, reasonably requested that ADC investigate in order to uphold its contractual obligation to provide best efforts to supply the product it warrants as safe and of-Grade. ADC gave Yo-Go repeated assured ADC that it was investigating the matter. Yo-Go relied on these promises, rather than cancelling the contract or bringing an immediate action against ADC. Yo-Go later learned from two different sources that ADC had known for a long time that the January 2007 delivery of bad milk was caused by its unclean tankers. (p. 3 & 4). Upon learning this fact, Yo-Go sought immediate termination, because it was clear that ADC was ignoring it duties with regards to its provision of safe milk. Although the 1993 MPA is an installment contract where goods are delivered in separate lots and accepted separately[2], there is evidence that the provision of safe milk required ADC to cooperate in investigating the origin of the unsafe milk. While there is no contract term explicitly requiring investigation into bad milk, ADC's 2006 submission to third-party testing suggests that such an investigation is part of the normal course of business. Given that Yo-Go originally entered the existing contract with a smaller, trusted supplier, the value of its bargain has been substantially impaired because it cannot trust ADC to supply safe milk.

The advantage of this argument is that it includes the facts that would have been argued in the rejected good faith and fair dealing claim. The problem with this argument is that there is no express duty for the supplier to cooperate in any investigation. Instead, we are relying on Yo-Go's relationship with ADC's predecessor company, which may be too weak.

3. ADC may have Violated its Duty of Good Faith and Fair Dealing in Performance of the Contract

Every contract or duty imposes an obligation of good faith in its performance and enforcement.[3] In the case of merchants defined in *§ 2104(1)*, "good faith" broadens the definition contained in former *Civil Code § 1796*, in that it additionally requires "the observance of reasonable commercial standards of fair dealing in the trade."

Judge Marshall has already stated that the case before him appears to be a UCC case. He reduced our prior good faith claim to an ill-formed claim for legal remedy to a single installment. It may be difficult to re-characterize our good argument so that it will pass his muster. Nonetheless, for appeal if nothing else, it is worth making the argument that ADC violated the commercial code's good faith requirement. The consideration of the 1993 MPA went far beyond a simple exchange of milk for money. It was a long-term exclusive agreement that required cooperation to deliver healthful, third-party-inspected product over time. Thus, ADC's failure to commit to delivering this product—in an industry where a health hazard could bring ruin—was a violation of good faith performance of the contract. In addition, we argue any delays in recognizing the source of the problem were caused by ADC's failure to cooperate—a breach in itself.

Using this strategy may require filing a motion for reconsideration or an appeal. A motion for reconsideration would be before the same judge, and he may not be receptive given his rejection of our first good faith and fair dealing argument. An appeal would also take more time and money. Given these costs, it is likely better to pursue another strategy.

[2] *Cal U Com Code § 2612(1)*
[3] *Cal U Com Code § 1304*

Comment [GH8]: This is exactly the line of reasoning we need to pursue—but it's not evidence we're looking for, it's an obligation to cooperate in investigating. That would be an implied contract term so the issue is: can we argue these terms are implied?

Comment [GH9]: So close—not whether it's normal course of business but whether it's an implied contractual obligation—a reasonable interpretation of the parties' intent!

Comment [GH10]: Yes---more on this!

Comment [GH11]: Good attention to particular context here.

Comment [GH12]: Good

Comment [GH13]: Excellent

Comment [GH14]: As we discussed in class—you need to connect the good faith argument here to a specific obligation in the contract—so connect directly to the implied term of a duty to cooperate in investigating the potential sources of contaminated milk.

Comment [GH15]: Yes, they always do….But we're not at this point in decisionmaking; we only have to appeal if we lose and all we need to do now is make sure we've made the argument so as to preserve the right of appeal if we decide, later, to take it.

4. Yo-Go Did Not Likely Reinstate the Contract by Accepting Further Shipments Before it was Clear that ADC was Responsible for the Bad Milk

An "aggrieved party reinstates the contract if he accepts a non-conforming installment without seasonably notifying of cancellation or if he brings an action with respect only to past installments or demands performance as to future installments."[3] However, "a reasonable time for notifying of cancellation, judged by commercial standards under the section on good faith, extends of course to include the time covered by any reasonable negotiation in good faith." *Gantry Constr. Co. v. American Pipe & Constr. Co.* (this language noted by the court as borrowed from legislative history for Commercial Code).[4]

There is a great risk that Yo-Go's conduct will be interpreted as reinstating the installment contract. Yo-Go has already accepted over 1 1/2 year's worth of milk deliveries from ADC with no further problems that we know of. In the good faith and fair dealing complaint brought before Judge Marshall, Yo-Go's claim has already been (mis-)characterized as seeking legal remedy for a past installment. Our task is to frame the time-lag between the initial breach and cancellation as reasonable. We argue that the initial breach, although a single installment breach, causes substantial impairment to the entire contract. Yo-Go took part in good faith discussions with ADC to investigate the harm. Lilly Bach states that it is industry practice to cooperate when trying to discover the source or reason for a contamination. (p. 5). Yo-Go should also argue that it was not commercially reasonable to suspend performance until they had reason to believe that ADC was acting improperly and not taking measures to rectify the situation, as they had in 2006 when they replaced an entire silo full of milk after delivering contaminated milk. ADC's other contracts and industry standards typically allow for cancellation upon "confirmation" of evidence of a safety violation. (p. 7). Thus, it is a compelling argument to say that the cancellation of the contract was not delayed at all. In fact, Yo-Go did not accept any shipments of milk following its confirmation that the material breach had occurred.

Furthermore, *Gantry* notes that any time spent in "reasonably negotiation in good faith" is included in the assessment of "reasonable time" for notification. Even if Yo-Go had reason to cancel the contract at the time of bad shipment, we can argue that the delay was in part for good-faith negotiations. In the past, ADC willingly replaced an entire silo of milk after making a contaminated delivery. We expected them to take similar, good-faith steps in the present case after they repeatedly re-assured us that they were looking in to the origin the bad milk. Given their past behavior and their current assurances, it was reasonable for Yo-Go to expect ADC to investigate and cover damages if it was at fault. When it became clear that good faith negotiations were not in fact happening, Yo-Go immediately terminated, which was reasonable given ADC's bad faith actions.

Great work on this—be more consistent in addressing counterarguments. But very good judgment in general and a sharp focus on key arguments. Keep the good faith and 'implied' duty to cooperate arguments, however, closely tied to contractual obligations—find them/imply them.

Comment [GH16]: Yes---good attention to realities of strength of position here.

Comment [GH17]: Excellent.

Comment [GH18]: Excellent way to frame this.

Comment [GH19]: Good—but what's the counterargument? How strong is this line of reasoning?

Comment [GH20]: You shifted into brief-writing here.

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[4] *49 Cal.App.3d 186, 122 (FN5)*

Client Comments Re: YoGo I

The major issue facing YoGo is whether or not we breached our contract with ADC by only giving them 10 days notice prior to cancellation. When we decided to end our relationship with YoGo and switch over to a new supplier, we felt that we had every right to do so based on ADC's failure in compensating us for the defective milk they delivered to us in 2007.

All of the attorney groups based their main argument on the assumption that the contract between YoGo and ADC was an installment contract. It was explained that under the UCC, one defective installment gives the other party the right to void the contract only if that installment substantially impairs the value of the entire contract. A few groups seemed to believe that the mixing of shipments into huge silos combined with the fact that this is the second time that ADC has delivered a defective shipment, would be enough to substantially impair the entire contract. However, in 2006 when it was clearly found that ADC was responsible for the contamination, they quickly cured the defect at their own expense. We are a little worried that this works in their favor showing that we should have faith in them to cure when they do discover that defect was completely their fault. Furthermore, if we are then only left with the one defective shipment in 2007, we are not very sure how this one shipment even if mixed into huge silos lines up with the judge's prior statements that he doesn't feel that one bad shipment can truly substantially impair an entire contract when there has been a long history of good shipments.

After reading all of the memos and sitting in on both meetings, we came to the understanding that a breach could only take place if there was a specific obligation set forth in the contract that ADC failed to meet. The judge stated that there was no obligation stated in the agreement that required ADC to automatically pay damages if YoGo claims ADC delivered defective milk. Two of the attorney groups seemed to believe that this failure to pay us the one million dollars would qualify as anticipatory repudiation because ADC stated that they would not pay us this money unless we agreed to sign a renewal contract. However, we don't understand what obligation would be violated in that situation when the judge has already made it clear that the failure to pay damages is not an obligation set forth in the MPA.

Lastly, all of the attorney groups based their memos on the assumption that ADC would be found to be at fault for the contamination in 2007. Based on this assumption, all of the groups felt that ADC had the right to cure their defect within a reasonable amount of time. Group six seemed to believe that a possible contract by conduct had been created that would allow us out of the contract whether or not the defect was their fault or ours, but outside of that possibility it appeared that we would have no defense to breaking the contract if it is found that ADC wasn't at fault. We would like to know if there are any other options available to us to avoid the costly damages we are at risk of paying if it is found that ADC isn't at fault.