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Lost Profits for the Lost Volume Seller: A Businessperson's Pipe Dream or Entitlement?

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LOST PROFITS FOR THE LOST VOLUME SELLER: A BUSINESSPERSON’S PIPE DREAM OR ENTITLEMENT?

Sellers seeking to recover lost profits under the Uniform Commercial Code generally must mitigate their damages by giving "due credit for proceeds of resale." Unfortunately, for one class of sellers, the lost volume seller, a unit of profit is lost when a buyer breaches a contract. A resale, therefore, benefits the breaching buyer and deprives the seller of a unit of profit. This Note discusses why, under the Code, a lost volume seller need not mitigate damages and recommends a method for determining when a seller is really a lost volume seller. In doing so, the opinions of several commentators are discussed, case law is reviewed and an economic analysis is completed.

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I. INTRODUCTION

Common law damages for breach of sales contracts are founded on concepts of reliance and expectation damages.1 A person breaching a contract is liable for its value and any reasonably foreseeable reliance and expectation damages,2 unless the non-breaching party could have

1. See J. CALAMARI & J. PERILLO, THE LAW OF CONTRACTS § 14-4 (2d ed. 1977). The authors state:
   The reliance interest represents the detriment he may have incurred by changing his position. The expectation interest represents the prospect of gain from the contract. This analysis does not conflict with the gains prevented and losses sustained analysis; it merely represents a different breakdown of the same economic harm suffered. The use of this newer analysis is gaining acceptance as it often permits a clearer way of determining the actual economic harm.

Id. at 522.

2. See infra note 7 and accompanying text. Any discussion of damages must include their purpose. Damages are considered compensatory, a deterrent to future breaches, or
mitigated his losses.3 Proof of loss varies with each set of facts. Courts allow recovery of lost profits for breach of contract if such loss is not too remote or speculative. Unfortunately, recovery of common law damages economically efficient. Each of these three approaches is adopted by different authors as the primary motive behind granting damages. See 5 A. CORBIN, CORBIN ON CONTRACTS § 1002, at 33-34 (1964 & Supp. 1971) (espouses general deterrence theory); Birmingham, Breach of Contract, Damage Measures, and Economic Efficiency, 24 RUTGERS L. REV. 273, 284-86 (1970) (economic efficiency); Farnsworth, Legal Remedies for Breach of Contract, 70 COLUM. L. REV. 1145, 1147 (1970) (compensatory). All but the economic efficiency approach results in the security of business transactions.

Professor Corbin suggests that the purpose of damages is one of general deterrence. See 5 A. CORBIN, supra, § 1002, at 33, 34. Corbin states: “The fact that damages must be paid tends directly to the prevention of breaches of contract. It makes, therefore, for the security of business transactions and helps to make possible the vast structure of credit, upon which so large a part of our modern prosperity depends.” Id. at 34.

Professor Farnsworth believes the purpose of damages is to compensate the aggrieved party. Farnsworth, supra, at 1147. This approach does not emphasize Corbin’s deterrence rationale which admonishes parties of the serious consequences of a breach. Instead it encourages contractual relationships with the understanding that a breach by one party will mean an adequate remedy at law for the other. “By protecting their expectations in the event of a breach,” people are encouraged to keep their promises. Id. This also results in security of business transactions.

Finally, Professor Robert Birmingham, a lawyer-economist, observes that breaches should be encouraged when the defendant can gain from the reallocation of resources and the plaintiff is fully remunerated for his lost bargain and any transaction costs incurred. See Birmingham, supra, at 292. This philosophy repudiates notions of morality in keeping promises or the security in transactions and utilizes a sterile economic analysis. If a party bound by a contract can prosper by breaching, inclusive of costs paid to the non-breaching party, then he should be encouraged to do so. As the author states, this would foster the “optimal reallocation of factors of production and goods without causing material instability of expectations.” Id.

Comment 1 to § 2-609 of the Uniform Commercial Code indicates that the policy behind the Code is transactional security, the same policy that Professor Farnsworth supports. Comment 1 to § 2-609 states:

The section rests on the recognition of the fact that the essential purpose of a contract between commercial men is actual performance and they do not bargain merely for a promise, or for a promise plus the right to win a lawsuit and that a continuing sense of reliance and security that the promised performance will be forthcoming when due, is an important feature of the bargain. If either the willingness or the ability of a party to perform declines materially between the time of contracting and the time for performance, the other party is threatened with the loss of a substantial part of what he has bargained for.

U.C.C. § 2-609, comment 1 (1978) (emphasis added) (hereinafter all references to the UCC will be to the 1978 version).

3. See J. CALAMARI & J. PERILLO, supra note 1, § 14-15. Regarding mitigation, the authors believe that:

As an almost inflexible proposition a party who has been wronged by a breach of contract may not unreasonably sit idly by and allow damages to accumulate. The law does not permit him to recover from the wrongdoer those damages which he “should have foreseen and could have avoided by reasonable effort without undue risk, expense, or humiliation.”

See id. at 538.
for breach of contract does not always proceed in a uniform fashion and no specific guidelines for recovery of lost profits exist.

Article Two of the Uniform Commercial Code (UCC) brings clarity and uniformity to the issue of damages in sales law. The Code provides a framework for determining damages that result from a breached contract. Article Two organizes its remedies provisions into a schedule of well-delineated alternative actions. To preserve continuity and eliminate disparate treatment of parties, the Code employs various objective measures of damages. Among the objective measures used to determine loss are market price, contract price, and the value received on a resale. These measures provide fairly accurate estimates in forecasting loss. They are more certain indicators of loss than such imprecise, subjective


6. See Childres & Burgess, Seller's Remedies: The Primacy of UCC 2-708(2), 48 N.Y.U. L. Rev. 833, 833-36 (1973); Peters, supra note 4, at 253-54, 267-68. The three major objective measures employed by the Code are: 1) section 2-706 which allows the seller to recover the difference between the contract price and the resale price; 2) section 2-708(1) which allows the seller to recover the difference between the market price and the contract price; and 3) section 2-709 which allows recovery of the contract price. These measures do not allow the court much latitude in arriving at losses. Each is a fairly stable indicator of losses. All rely on something other than the seller's particularized measures of lost profit, lost goodwill, and other intangibles. The objective measures determine what a plaintiff normally loses in similar situations with no attempt to remunerate the plaintiff for his actual losses.

Incidental damages also fill the interstices the more rigid objective measures do not reach. Section 2-710 of the Code allows the assessment of incidental damages against the buyer. Incidental damages include "any commercially reasonable charges, expenses or commissions incurred in stopping delivery, in the transportation, care and custody of goods after the buyer's breach, in connection with return or resale of the goods or otherwise resulting from the breach." U.C.C. § 2-710 (1978). By supplementing the objective measures, incidental damages make the seller whole.

Professor Peters, a leading authority in Code damages, has commented on the purpose of "personalized" damages as reflected by § 2-708(2). See Peters, supra note 4, at 268. She begins with a discussion of market-based damages (i.e., objective measures):

For its principal remedy, damages, the Code then has a favored method of calculating losses. If the injured party is willing to go out into the market to find a reasonable substitute, damages measured by the cost of such a substitute transaction are readily recoverable, whether the breach be past, present or future. The Code goes out of its way to protect under all circumstances reasonable investments actually made in the market.

See id. at 267.

Professor Peters, after discussing the Code's preferences for market-based remedies, goes on to describe the importance of "personalized" damages:

There are many cases in which the party aggrieved by nonperformance would prefer to measure damages by his own economic circumstances, rather than by the market. If remedies are thus "personalized" they hold out the promise of more adequate relief for the injured party. The Code provides various guidelines for the recovery of non-market based remedies, for profitable and for losing contracts, principally in its section on consequential damages.

Id. at 268 (footnote omitted).
damages as lost profits, lost goodwill, and the like.  

7. The normal rule of contract damages, as established in Hadley v. Baxendale, 9 Ex. Ch. 341, 156 Eng. Rep. 145 (1854), did not allow recovery for damages that were remote and speculative and not within the contemplation of the parties at the time of contracting. The text of § 2-715 embodies this language. See U.C.C. § 2-715 (1978). Section 2-715 is a buyer's remedy that allows consequential damages. Section 2-715 states in pertinent part:

(2) Consequential damages resulting from the seller's breach include
(a) any loss resulting from general or particular requirements and needs of which the seller at the time of contracting had reason to know and which could not reasonably be prevented by cover or otherwise; and
(b) injury to person or property proximately resulting from any breach of warranty.

U.C.C. § 2-715(2).

Section 2-708(2) is similar to § 2-715 because it is designed to give lost profits that are reasonably discernable, and therefore, awards damages outside the normal measure of damages. Section 2-715 awards those damages proximately arising from the breach as a natural and probable consequence of the breach. As a result, damages awarded under § 2-715 may exceed the contract amount. Conversely, § 2-708(1) limits damages to the contract price and any incidental damages reasonably incurred.

Pre-Code cases generally followed the Hadley v. Baxendale rule in which lost profits were not allowed where they could not be measured with reasonable certainty. See L. Simpton, Contracts § 196, at 396 (2d ed. 1965). For example, a new business venture not having an established cash flow or patrons, could not recover lost profit. Id. § 197, at 397. Therefore, pre-Code profits might not be determinable in such a situation. For a situation in which a buyer with an unestablished business was allowed to recover lost profits, see Leoni v. Bemis Co., 255 N.W.2d 824, 826 (Minn. 1977). See generally 5 Wm. Mitchell L. Rev. 280 (1979).

Subsection 2 of § 2-708 allows the recovery of lost profits and as such departs from the common law. Comment 2 states that “[i]t is not necessary to a recovery of ‘profit’ to show a history of earnings, especially if a new venture is involved.” U.C.C. § 2-708, comment 2. Additionally, comment 1 of § 1-106 states that the purpose of the Code is to “reject any doctrine that damages must be calculable with mathematical accuracy.” U.C.C. § 1-106, comment 1. It continues by stating, “[c]ompensatory damages are often at best approximate: they have to be proved with whatever definiteness and accuracy the facts permit, but no more.” Id.

Common law damages are given for the net amount of losses caused and gains prevented by defendant's breach in excess of the savings made possible. 5 A. Corbin, supra note 2, § 1029, at 177 (1964 & Supp. 1971). This means that plaintiff may recover what he invested in the bargain (reliance damages) and the net gain prevented by the breach (expectation damages). There are, however, a few limitations on recovery of these damages. First, any reliance must be reasonable. See 1A A. Corbin, supra note 2, § 200, at 218-19. For instance, any decision by a seller to complete unfinished goods must be commercially reasonable under § 2-704. See U.C.C. § 2-704(2) (1978). If the seller does not make a resale after completing the goods or is unable to do so, it will be difficult for the seller to show that his decision to complete the goods was reasonable.

Second, the plaintiff cannot recover any loss which was not reasonably foreseeable by the defendant as a probable result of the breach at the time of contracting. See 5 A. Corbin, supra note 2, § 1007, at 70-71. Third, the plaintiff has a duty to mitigate his damages. Id. § 1039, at 241-43. Finally, problems of proof in relation to proximate cause, certainty of losses, and formulas measuring loss must be encountered. Id. at § 1021, at 127-35; see 11 S. Williston, A Treatise on the Law of Contracts § 1346A, at 245-51 (3d ed. 1968 & Supp. 1983).

The aggregate effect of these limitations upon recovery favors the breaching party.
The objective measures resolve the issue of damages in the majority of standard breach of contract actions. In some cases, however, objective measures inadequately approximate a seller’s true loss. Subjective measures of damages add flexibility to the Code and apply in situations where the objective measures are inadequate. Subjective measures allow the seller to recover his actual losses rather than the predetermined objective damages.

Subsection two of UCC 2-708 is one of the subjective measures. Section 2-708 provides two formulas for computing a seller’s damages when a buyer repudiates or refuses to accept goods. One formula, subsection one, is characterized as an objective measure while the other, subsection two, is subjective. Subsection one offers sellers the traditional contract remedy of the difference between the market price and the unpaid contract price at the time and place of tender. Should that be inadequate, subsection two, the focus of this Note, allows the aggrieved seller his lost profits, including reasonable overhead, together with any incidental damages less any proceeds arising from resale. The express purpose of

"All in all, our system of legal remedies for breach of contract, heavily influenced by the economic philosophy of free enterprise, has shown a marked solicitude for men who do not keep their promises." Farnsworth, supra note 2, at 1216; Speidel & Clay, Seller’s Recovery of Overhead Under UCC Section 2-708(2): Economic Cost Theory and Contract Remedial Policy, 57 CORNELL L. REV. 681, 686 (1972) (quoting Farnsworth).

8. See Peters, supra note 4, at 268; supra note 6 and accompanying text.
10. Section 2-708 provides that:
   1) Subject to subsection (2) and to the provisions of this Article with respect to proof of market price (Section 2-723), the measure of damages for non-acceptance or repudiation by the buyer is the difference between the market price at the time and place for tender and the unpaid contract price together with any incidental damages provided in this Article (Section 2-710), but less expenses saved in consequence of the buyer’s breach.
   2) If the measure of damages provided in subsection (1) is inadequate to put the seller in as good a position as performance would have done then the measure of damages is the profit (including reasonable overhead) which the seller would have made from full performance by the buyer, together with any incidental damages provided in this Article (Section 2-710), due allowance for costs reasonably incurred and due credit for payments or proceeds of resale.

U.C.C. § 2-708.

For a discussion behind the history of § 2-708(2), see infra notes 46-56 and accompanying text.

11. For excellent discussions on the import of U.C.C. § 2-708(2), see generally J. WHITE & R. SUMMERS, UNIFORM COMMERCIAL CODE §§ 7-8 through 7-13 (2d ed. 1980); Childers & Burgess, supra note 6; Goetz & Scott, Measuring the Sellers’ Damages: The Lost Profits Puzzle, 31 STAN. L. REV. 323 (1979); Harris, A Radical Restatement of the Law of Seller’s Damages: Sales Act and Commercial Code Results Compared, 18 STAN. L. REV. 66 (1965); Peters, supra note 4; Schlosser, Construing UCC Section 2-708(2) to Apply to the Lost-Volume Seller, 24 CASE W. RES. L. REV. 686 (1973); Shanker, The Case for a Literal Reading of UCC Section 2-708(2) (One Profit for the Reseller), 24 CASE W. RES. L. REV. 697 (1973); Speidel & Clay, supra note 7.

12. U.C.C. § 2-708(1).
subsection two of 2-708 is to put the seller in as good a position as performance would have done. Subsection 2 more accurately reflects the losses of sellers whose damages would be undervalued by the objective measures of damages. While subsection two aims at remunerating sellers whose damages cannot be measured by objective means, it is potentially ineffective for one group of sellers for whom it was drafted, the lost volume seller.

Subsection 2 of 2-708 covers at least three types of sellers who lose profits and volume on a breached contract and cannot recoup their losses by resort to objective measures of damages: jobbers, manufacturers, and lost volume sellers. A jobber is one who solicits orders from a third party and then arranges with suppliers to fill the orders. If a breach occurs before the goods are in the jobber's hand and the goods are subsequently sold to another buyer, the jobber loses profits and volume. A manufacturer is one who acquires raw materials from which he assembles goods for the buyer. When notified of a breach, this seller stops fabrication and is left with unfinished goods.

14. Id. There is apparently some dispute regarding into what position a lost volume seller can reasonably expect to be placed. In that regard, compare Harris, supra note 11, at 80-83, 99-101, and Schlosser, supra note 11, at 689-91, with Shanker, supra note 11, at 704-07.

15. See supra note 6 and accompanying text. Any discussion of when 2-708(2) will be applied must include how lost profits can be proved. An attempt is made, in notes 33-34 infra and the accompanying text, to proffer some guidelines for determining when a seller has lost volume.


17. Professor Harris is the original creator of these classifications. See Harris, supra note 11, at 68-73, 97-99, 101-07; J. WHITE & R. SUMMERS, supra note 11, § 7-9 through 7-11.

18. J. WHITE & R. SUMMERS, supra note 11, § 7-10, at 278. A jobber also looks to § 2-708(2) to recover lost profits. White and Summers suggest that a jobber must satisfy two conditions before recovering lost profits. First, he must never have acquired the contract goods. Second, his decision not to acquire those goods after learning of the breach must be commercially reasonable under § 2-704. See id. A jobber with no goods to resell cannot avail himself of a § 2-706 resale, a § 2-709 price action, or a § 2-708(1) action for the contract less market price. The reason is that the jobber does not have completed goods to resell because the breach has occurred before performance of the contract. Instead, he must pursue his remedy under § 2-708(2) because his loss is entire. The "due credit" provision does not affect a jobber because he has nothing to resell.

19. Id. § 7-10, at 276. Professor Harris noted that a jobber is not functionally different from a manufacturer (he uses the word "components" seller) in attempting to assess the amount of damages:

These two types of cases should be distinguished from those cases in which breach occurs before plaintiff (in this case typically a retailer or wholesaler) has acquired the goods he is to deliver to defendant. In this situation a components approach is more appropriate—that is, plaintiff should abandon efforts to acquire the goods. Valuation of the yet-to-be-acquired goods should be at cost of acquisition ("components valuation") even if there is only a single component to be valued—the goods themselves.

Harris, supra note 11, at 77 (footnotes omitted).
Both sellers lose volume not because they have sold completed goods, but because they have sold uncompleted goods or never-purchased goods needed to fill a contract.20 Because these sellers do not have completed goods they cannot pursue an action for recovery of price under 2-709.21 As well, subsection 2-708(1) and 2-706 which utilize the market price in assessing damages imply that completed goods must be involved.22 Consequently, these sellers must, out of necessity, pursue an action under subsection 2-708(2).

The last seller apparently covered by subsection two of section 2-708 is the lost volume seller.23 This seller differs from a jobber or manufacturer in that he has completed goods which could be sold to mitigate his damages. A lost volume seller, however, will still lose profits if he resells goods left behind by a breach. A lost volume seller must also be distinguished from a seller who also resells completed goods after a breach, but who cannot show that he could have supplied every willing buyer.

A lost volume seller has an unlimited capacity to produce goods and a

20. J. WHITE & R. SUMMERS, supra note 11, § 7-10, at 276. Any decision to cease manufacture or work must be commercially reasonable. See U.C.C. § 2-704(2). The comments to § 2-704 indicate that the burden is on the buyer to show that the seller's decision to cease manufacture to complete the unfinished goods is commercially unreasonable. Two questions may be posited to determine whether a seller should complete the product or cease manufacture. First, what damages could the seller claim from the buyer if he ceases manufacture and sues under § 2-708(2) for lost profits? See J. WHITE & R. SUMMERS, supra note 11, § 7-14, at 290. Second, how do these "damages compare with the damages the seller is likely to recover under 2-706 upon completion of the manufacture and resale of the goods?" See id.

It seems evident that § 2-704 is consistent with the general rule of mitigation which is incorporated into the Code by way of § 1-103. See U.C.C. § 1-103. This means any decision not to complete goods must be reasonable as well as any decision to complete goods.

In the case of a lost volume seller, § 2-704(2) is theoretically of no consequence. Any decision to complete or cease manufacture does not affect a recovery under § 2-708(2) because the due credit for proceeds of a resale should not be given in either event. The seller should be allowed to recover his lost profit without any corresponding set-off for the resale of completed goods or the scrap value of uncompleted goods. See J. WHITE & R. SUMMERS, supra note 11, §§ 7-10 to 7-11, for an explanation of how manufacturers and sellers may also be lost volume sellers. The distinctions between them must be recognized. A manufacturer or jobber may also be considered a lost volume seller, but only if lost volume is proven. See also R. DUNN, RECOVERY OF DAMAGES FOR LOST PROFITS § 2.8 (2d ed. 1981) (author discusses "middleman" exception to § 2-708(2) which allows recovery when the seller is a middleman).


22. Id. at § 7-10.

23. Id. at §§ 7-8 to 7-11. White and Summers explain that there are "other" lost volume sellers who must be allowed to recover lost profits without a resale. The first occurs when a seller resells a completed project but cannot prove he lost volume as a result of the breach. The second is the seller who holds completed goods in stock and unsold at the time of trial. Clearly, these sellers are not to be compensated only by receiving as damages the difference between the market price and the contract price. See id. § 7-10, at 280-81.
finite number of buyers.24 If one buyer breaches, although the next buyer in line purchases those goods, the seller ultimately loses one sale that he normally would have captured.25 The seller expects two sales, but when the first buyer breaches, he is left with only one.26 When the lost volume seller loses the profit from a sale, he loses that portion of the profit allocated to his fixed costs and a reasonable rate of return on his investment.27

The nature of a lost volume seller’s damages is obvious: lost profits.28 Since section 2-708 provides that “due credit for proceeds of resale” must be subtracted from any recovery, this section is useless as a remedy for lost volume sellers.29 Only the award of lost profits makes recovery total for the lost volume seller.30 A lost volume seller should not be required

24. See 1 W. HAWKLAND, A TRANSACTIONAL GUIDE TO THE UNIFORM COMMERCIAL CODE § 1.5505 (1964); Comment, The Measure of Damages Due the Lost-Volume Seller Under UCC Section 2-708(2): Two Points of View, 24 CASE W. RES. L. REV. 684, 684 (1973). Professor Corbin used different terminology for a lost volume seller. He coined the word “expansive” seller. Both terms mean essentially the same thing. Corbin explained the problem of the “expansive” seller as follows:

If the seller is a manufacturer or producer of the subject of the sale, with capacity to produce enough such articles to supply all probable customers, the buyer’s rejection does not make possible a second sale that the seller could not otherwise have made. Every new customer would have been supplied even if the buyer had kept the goods and performed his contract. The same is true if the seller, though not himself a producer of the goods, is an intermediate dealer whose relations with a producer enable him to supply all obtainable customers. In these cases, the buyer’s breach does not make possible a new sale in which the profit lost by the buyer’s breach would be replaced.

5 A. CORBIN, supra note 2, § 1100, at 541-42 (1964) (footnotes omitted).

It follows that the lost volume seller is an “expansive” seller within Corbin’s definition. This seller can manufacture (or obtain through a middleman) as many units as he has buyers. Accordingly, this seller loses a sale when the buyer breaches. Corbin concludes that the seller is entitled to recover the profit he would have earned had the sale been consummated:

The only “saving” that the buyer’s breach makes possible in [the case of a lost volume seller] is the “cost” of producing or procuring the subject of the sale; the seller is enabled to make one new sale without incurring the cost of a second article of the kind. In order to put the seller in as good a position as that in which performance would have put him, he must now be awarded the contract price diminished only by his cost of procurement. Normally, this “cost of procurement” by an intermediate dealer is the “wholesale price” to dealers, not the market value at retail, the difference being the dealer’s profit.

Id. at 542 (footnote omitted).

One article persuasively challenges the economic foundations upon which Corbin and other authors use to explain the plight of the lost volume seller. See Comment, A Theoretical Postscript: Microeconomics and the Lost-Volume Seller, 24 CASE W. RES. L. REV. 712, 712-19 (1973) [hereinafter cited as Comment, Theoretical Postscript].


26. See W. HAWKLAND, supra note 24, § 1.5505.

27. See id.


29. U.C.C. § 2-708(2).

30. See Schlosser, supra note 11, at 688-91. But see Shanker, supra note 11, at 700-03.
to give due credit for the proceeds of a resale because his loss is a whole one.\textsuperscript{31} When the seller has the capacity to supply all buyers and loses an entire sale, then the second sale to another buyer does not mitigate his loss.\textsuperscript{32} If a sale to a second buyer relieves the obligation of the first buyer, the lost volume seller has lost profit on the unrealized sale to the first buyer.

This Note will examine how volume sellers are identified and whether UCC 2-708(2) should be applied to lost volume sellers. Additionally, the judicial treatment of UCC 2-708(2) will be reviewed. The Note concludes its discussion of the lost volume phenomenon by subjecting it to an economic analysis and suggests future courses of action for courts dealing with the lost volume problem.

II. IDENTIFYING LOST VOLUME SELLERS

Since many sellers appear to be lost volume sellers when in fact they are not, courts must scrutinize the seller's position to determine whether a seller indeed has lost volume. The consequences of incorrectly assum-

Professor Shanker is disturbed by the consequences of ignoring the due credit language of § 2-708(2). He believes such a reading makes mitigation of damages inapplicable or useless to sales contract litigation. Applying the principle of mitigation, the buyer's default makes the second sale possible and the second sale mitigates any profits from the first sale. Cf. R. Nordstrom, Handbook of the Law of Sales § 177, at 536 (1970) (the lost volume seller does not mitigate his profit when he makes a second sale).


32. \textit{See id. at} § 7-13. Professors White and Summers have created a useful hypothetical to illustrate why this phrase causes difficulties in a lost volume situation. In their hypothetical, Boeing contracts with a number of airlines for the sale of 100 747's for the year. One of the buyers, TWA, breaches and refuses to buy the third 747 off the line. Pan Am accepts plane number three in TWA's stead.

For the year Boeing only sells 99 747's as opposed to the projected sales of 100 planes. This lost sale results in a loss of profit and an amount allocable to fixed costs of overhead. Boeing's calculation of damages appears as follows:

\begin{align*}
\$2 \text{ million (profit)} \\
\text{plus } \$1 \text{ million (overhead)} \\
\text{plus 0 (incidental)} \\
\text{plus 0 (costs reasonably incurred [all allocated to Pan Am and so saved])} \\
\text{minus 0 (credit for resale)} \\
\$3 \text{ million damages}
\end{align*}

Although this appears to be the correct result for a lost volume seller, TWA argues that it fails to take account of the resale Boeing is able to make because of TWA's breach. This resale figures prominently in TWA's calculation:

\begin{align*}
\$2 \text{ million (profit)} \\
\text{plus } \$1 \text{ million (overhead)} \\
\text{plus 0 (incidental)} \\
\text{plus } \$17 \text{ million (cost reasonably incurred)} \\
\text{minus } \$20 \text{ million (credit for resale)} \\
0 \text{ damages}
\end{align*}

Assuming Boeing indeed loses volume, the latter calculation is untenable because it fails to give the seller his lost unit of profit. For different solutions posed by several authors dealing with this controversy, see infra notes 64-94 and accompanying text.
ing a seller has lost volume are significant. Plaintiff-sellers not entitled to lost profits will receive two units of profit from one sale. In addition, allowing recovery for lost profits without the corresponding set-off for resale creates indirect access to the 2-709 action for recovery of contract price,\textsuperscript{33} the Code’s equivalent to specific performance.\textsuperscript{34} Section 2-709 provides an extraordinary remedy for the seller applicable only when completed goods have been either accepted by the buyer, identified to the contract, or risk of loss has passed to the buyer.\textsuperscript{35} Under 2-709 a seller could improperly recover the price of a breached contract without demonstrating lost volume.

Professor Harris\textsuperscript{36} suggests three criteria for determining which sellers

\begin{itemize}
  \item Section 2-709 provides:
    \begin{enumerate}
      \item When the buyer fails to pay the price as it becomes due the seller may recover, together with any incidental damages under the next section, the price
          \begin{enumerate}
            \item of goods accepted or of conforming goods lost or damaged within a commercially reasonable time after risk of their loss has passed to the buyer; and
            \item of goods identified to the contract if the seller is unable after reasonable effort to resell them at a reasonable price or the circumstances reasonably indicate that such effort will be unavailing.
          \end{enumerate}
      \item Where the seller sues for the price he must hold for the buyer any goods which have been identified to the contract and are still in his control except that if resale becomes possible he may resell them at any time prior to the collection of the judgment. The net proceeds of any such resale must be credited to the buyer and payment of the judgment entitles him to any goods not resold.
      \item After the buyer has wrongfully rejected or revoked acceptance of the goods or has failed to make a payment due or has repudiated (Section 2-610), a seller who is held not entitled to the price under this section shall nevertheless be awarded damages for non-acceptance under the preceding section.
    \end{enumerate}
  \item See J. White & R. Summers, supra note 11, § 7-2, at 254 n.3, supra note 19 and accompanying text. For example, suppose a seller cannot prove he has lost volume, but his situation closely resembles the characteristics of a lost volume seller. If the court awards this seller lost profits on a breached contract without subcontracting due credit for a resale, the seller uses § 2-708(2) to effect a recovery normally given only under extraordinary circumstances by § 2-709. Thus, the seller circumvents § 2-709 entirely. J. White & R. Summers, supra note 11, at § 7-2. Again, this demonstrates the need for the three coherent criteria laid down by Professor Harris.
  \item See J. White & R. Summers, supra note 11, § 7-11, at 280. The authors state: The art comes in establishing the figure which the court will allow as “due credit for payments or proceeds of resale.” If the seller has resold, the due credit should never be less than the amount for which he has resold (remember he is not a lost volume seller), but conceivably it should be more than that figure if the court finds, for example, that the seller lacked commercial reasonability in waiting as long as he did in the falling market. If the seller still holds the goods at the time of trial, the court will still have to determine a figure to include as due credit for a putative resale even though the seller has not yet resold. If the court does not deduct some amount for due credit for resale, 2-708(2) will simply become a backdoor action for the price, and quite clearly the draftsmen did not intend that result.
  \item Id. (emphasis added).
  \item See Harris, supra note 11. Professor Harris is a leading authority on lost sales volume. His works are cited by most authors dealing with this topic.
\end{itemize}
are lost volume sellers.37 According to Professor Harris, resale will result in a loss of volume if three criteria are met: (1) the person who bought the resold goods would have been solicited by the plaintiff had there been no breach and resale;38 (2) the solicitation by the plaintiff would have been successful; and (3) the plaintiff could have performed the additional contract.39 Once these criteria are proven, a seller is entitled to lost volume profits.

Under Professor Harris' first criterion, a seller who does not seek out another buyer does not lose volume because a subsequent sale would not have been expected.40 Additionally, if the seller reaches his peak in volume so that production of another unit is not profitable for him, there is no lost volume because the seller does not want the additional sales volume.41 The seller will only want to produce the quantity of goods that maximizes his profits.42

Criterion number two requires the seller to prove that the second purchaser would have purchased the resale goods if the goods actually sold were not available. The seller must show that the resale purchaser would have purchased the goods even if there had not been a breach.43 Evidence of actual resale would partially satisfy the requirement of successful solicitation. Difficulties arise when the resold goods are not fungible. If the goods that would have been sold to the initial purchaser differ in any way from the resold goods, the seller must establish that the second purchaser would have bought the resale goods if the goods actually sold had not been available.44 For example, suppose a second purchaser bought a green Model X car but the car left behind by the breaching buyer was a red Model X. The seller must show that the second purchaser would have purchased the red car had the green one not been available.

Finally, the third criterion denies the seller lost profit if he cannot show that he could have supplied the goods for the lost sale.45 If the seller

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37. Id. at 82.
38. Id. Professor Harris indicates that unless the plaintiff is a commercial seller, he probably would not have solicited another buyer. Id. The other possibility is that the seller solicited one buyer, but the sale actually is made to another buyer. The first criterion would not be met in this circumstance. See id. at 82-83.
39. Id. at 82. For an economic discussion regarding economies of volume, see infra notes 130-39 and accompanying text. Cf. infra notes 147-49 and accompanying text (explaining why the principle of profit maximization probably is not a foremost consideration of most businesses in the short run).
40. See Harris, supra note 11, at 82; infra text at notes 131 & 135 (lost volume seller is one who has an unlimited capacity to produce goods for finite number of buyers; a lost profit seller must show he can meet an existing demand).
41. See Harris, supra note 11, at 83; infra notes 134-39 and accompanying text.
42. See Harris, supra note 11, at 83.
43. Id. at 82-83.
44. Id. at 83.
45. Id. at 83 n.85.
could not have accommodated the "lost" sale, there is no lost profit to recoup.

III. SHOULD 2-708(2) BE APPLIED TO A LOST VOLUME SELLER?

The official comments to the Code provide insight in determining the purpose of subsection 2-708(2).46 Comment two to section 2-708 envisages a lost volume seller in its reference to the "unfair . . . results . . . when fixed price articles [are] involved."47 Although an explicit reference to lost volume sellers is not made, most commentators agree that the drafters were addressing this problem.48 The drafters believed that sellers of fixed price articles could recover only the 2-708(1) contract/market differential except where such damages were inadequate. In that case some other measure was needed to allow these sellers a recovery reflecting their true losses.49 The proposed revisions to the Uniform Sales Act, the precursor of the UCC, clearly applied to lost volume sellers because recovery of lost profits was allowed without subtracting resale proceeds.50 These revisions were later incorporated into the original version of section 2-708.51

By adding the resale credit provision in 1955, the drafters attempted to make subsection 2-708(2) applicable to manufacturer cases.52 The provision clarified the privilege of the seller to realize junk value when completion of manufacture was manifestly useless.53 This allowed the manufacturer to recover his lost profits, but made him subtract any amounts received from the resale of uncompleted goods.

46. U.C.C. § 2-708(2), comment 2.
47. See id.; Harris, supra note 11, at 98-99.
48. See R. Nordstrom, supra note 30, § 177, at 541; J. White & R. Summers, supra note 11, § 7-9, at 275 n.64; Harris, supra note 11, at 94-96; Schlosser, supra note 11, at 688.
49. See Harris, supra note 11, at 98. At that time the Enlarged Editorial Board recommended that § 2-708 in Supplement No. 1 to the 1952 Official Draft be amended to read:

Unless a lesser measure is agreed, the measure of damages for non-acceptance or repudiation is the difference between the price current at the time and place for tender and the unpaid contract price together with any incidental damages provided in this Article (section 2-710), but less any expense saved in consequence of the buyer's breach, except that if the foregoing measure of damages is inadequate to put the seller in as good a position as performance would have done then the measure of damages is the profit (including reasonable overhead), which the seller would have made from full performance by the buyer with due allowance for costs reasonably incurred and due credit for any resale.


50. See Harris, supra note 11, at 97-98.
51. See J. White & R. Summers, supra note 11, § 7-9, at 275 n.64; Harris, supra note 11, at 97-98.
52. See J. White & R. Summers, supra note 11, § 7-10, at 277; Harris, supra note 11, at 98.
While the text of the Code makes it clear that the resale credit provision applies to manufacturer cases, some commentators assert it should be equally applicable to lost volume sellers. It is uncertain whether this was the intention of the drafters. Comment two to 2-708, which originated with the 1949 draft of the Code, however, indicates by its reference to standard priced articles that subsection two governs lost volume cases:

The provision of [section 2-708(2)] permitting recovery of expected profit where the standard measure of damages is inadequate, ... [is] designed to eliminate the unfair and economically wasteful results arising under the older law when fixed priced articles were involved. This section permits the recovery of lost profits in all appropriate cases, which would include all standard priced goods.

Any interpretation of 2-708(2) must reconcile the original intent of this subsection and the resale credit provision. The text does not seem to allow recovery for lost volume sellers but comment two makes it clear that subsection 2-708(2) is aimed at giving the lost volume seller his full measure of damages. As a result, the history of 2-708(2) provides little guidance in deciding whether the resale credit provision applies to lost volume sellers.

An interpretation of 2-708(2) must also consider the general philosophy behind the damage provisions of the Code, as reflected in subsection 1-106(1). Subsection 1-106(1), which applies to all provisions of the Code, states that the “aggrieved party” should be put “in as good a position as if the other party had fully performed but neither consequential or special nor penal damages may be had except as specifically provided in this Act or by other rule of law.

54. See J. WHITE & R. SUMMERS, supra note 11, § 7-13, at 284-85; Harris, supra note 11, at 99. White and Summers state:

Since the statutory history of the Code and in particular Comment 2 to 2-708 indicate that the current 2-708(2) was intended to provide an adequate remedy for the lost volume seller, it is most surprising to find that the 2-708(2) formula strictly applied will not yield the correct recovery to a lost volume seller. ... We agree with Professor Harris: courts should simply ignore the “due credit” language in lost volume cases.

Id. (footnotes omitted).

55. See 1949 Draft of the Uniform Commercial Code § 2-708, Comment 2, quoted in J. WHITE & R. SUMMERS, supra note 11, § 7-9, at 275 n.64 (emphasis added by White & Summers).

56. See Harris, supra note 11, at 99.

57. U.C.C. 1-106(1) states:

(1) The remedies provided by this Act shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed but neither consequential or special nor penal damages may be had except as specifically provided in this Act or by other rule of law.

Id.

58. An “aggrieved party” is defined as “a party entitled to resort to a remedy.” See U.C.C. § 1-201(2).
position as if the other party had fully performed." 59 Section 1-106 also
commands "liberal" administration of the Code's damages provisions. 60
If, as section 1-106 states, a lost volume seller is to be put in as good a
position as if buyer performed, and subsection one of 2-708 is an inade-
quate remedy, then the resale credit provision of subsection two should
not be applied. The damages of a lost volume seller are not recouped on
a resale. The resale credit provision should apply only where the non-
volume seller captures through resale the scrap value of the goods of the
breached contract.

Undaunted by the literal "due credit for proceeds of resale" language
of 2-708(2), some courts have allowed lost volume sellers their lost profits
without deduction of resale proceeds. 61 Three divergent approaches to
the lost volume seller/resale credit dilemma have developed. Professor
Harris suggests the "traditional approach" that courts simply must ig-
nore the resale credit clause of 2-708(2) if they intend to let lost volume
sellers recover their entire loss. 62 The double profit approach suggests
stretching the language of 2-708(2) to reach the "right" result. This ap-
proach uses an alternative construction of 2-708(2) that allows the lost
volume seller to recover lost profits and still gives meaning to the resale
credit provision. Finally, a third approach vehemently rebukes attempts
to ignore or misconstrue the plain meaning of the words in 2-708(2) and
suggests that the drafters intended to allow mitigation by resale to reduce
the amount recoverable by a lost volume seller. 63 Each of these three
views is considered in greater detail below.

A. The Traditional Approach

The traditional approach ignores the resale credit language of subsec-
tion 2-708(2). 64 Most jurisdictions analyzing lost volume cases have

59. U.C.C. § 1-106(1).
60. Id.
61. See, e.g., Teradyne, Inc. v. Teledyne Indus., Inc., 676 F.2d 865, 868-70 (1st Cir.
1982); Famous Knitwear Corp. v. Drug Fair, Inc., 493 F.2d 251, 253-54 (4th Cir.
1974); Nederlandse Draadindustrie NDI B.V. v. Grand Pre-Stressed Corp., 466
F. Supp. 846, 853-54 (E.D.N.Y. 1979); Distribu-Dor., Inc. v. Karadanis, 11 Cal.
App. 3d 463, 470, 90 Cal. Rptr. 231, 235-36 (1970); Snyder v. Herbert
Greenbaum & Assocs., 38 Md. App. 144, 156, 380 A.2d 618, 625 (1977);
Neri v. Retail Marine Corp., 30 N.Y.2d 393, 400-01, 285 N.E.2d 311, 314,

In one case, the Arkansas Supreme Court intimated without holding that the plaintiff
was a lost volume seller. Combining the court's discussion with respect to inventories, the
plaintiff's capability of supplying all buyers, and a citation to one of Professor Harris'
articles, it is evident that the court was referring to a lost volume situation. See Capitol
Steel Co. v. Foster & Creighton Co., 264 Ark. 683, 688-90, 574 S.W.2d 256, 259-60
(1978).
62. See Harris, supra note 11, at 94-99.
63. See Shanker, supra note 11, at 700-04; infra notes 76-94 and accompanying text.
64. See J. WHITE & R. SUMMERS, supra note 11, at 285; Harris, supra note 11, at 94-
99.
adopted this approach. This approach relies on the Code’s policy of placing the seller in as good a position as full performance. Accordingly, the traditional approach acknowledges that loss of volume is economically possible and that such loss must be compensated because it cannot be replaced.

The traditional approach is justified by more than broad policy considerations; official comment two to 2-708 also supports this approach. Comment two contemplates full recovery when fixed priced articles are involved. By ignoring the resale credit language, the lost volume seller’s inability to replace the lost sale is acknowledged and the “proper” result is achieved.

B. The Double Profit Approach

Under the double profit approach the lost volume seller receives one “unit of profit” for the breached contract and an additional unit of profit for the resale of the same item. Subtracting one unit as due credit for proceeds of a resale from the two units of profit leaves one unit of profit to which the seller is entitled for his loss of a sale from the breaching buyer. The breaching buyer thereby obtains the benefit of the 2-708(2) resale credit provision, but remains liable for the profit lost as a result of this breach. This construction, rather than ignoring the language of 2-708(2), expands the subsection to accommodate the drafters’ intent of

65. See supra note 61.
66. See U.C.C. § 1-106.
67. See U.C.C. § 2-708, comment 2. The comment states that it applies to standard priced goods and that the normal measure of damages in such a case would be the “list price less cost to the dealer or list price less manufacturing cost to the manufacturer.” This is precisely the recovery to which a lost volume seller is entitled.
68. Id.
69. See Schlosser, supra note 11, at 692-93.
70. Id.
71. Id.
72. Id. Schlosser distinguishes the application of § 2-708(2) to jobber and component sellers in this way:

This interpretation does not interfere with the application of the subsection 2-708(2) formula to jobber and component sellers, the two other cases to which the subsection applies. In those cases the reasoning discussed in relation to lost-volume sellers does not apply, and “profit . . . which the seller would have made from full performance by the buyer” refers only to the unit profit, that is, the “profit which the seller would have made on the sale to the buyer.” There is a distinction between these two cases and the lost-volume case which makes this outcome possible. If there is no completed unit available for sale, as is the case with the jobber and component sellers, the critical assumption that there is another buyer who would perform fully cannot be made. If there had been an additional buyer, the components seller would have completed manufacture of the unit or the jobber seller would have purchased the unit from the manufacturer, and a resale would have occurred. But since there is no buyer for an additional unit, even full performance by the defaulting buyer would not have resulted in two unit profits. By way of contrast, in the case of the lost-volume seller, there was an additional buyer willing and able to purchase the extra unit,
recovery of lost profits without credit for resale. In this way, the double profit approach reaches the same result as the traditional approach.

In addition to the drafters' comments, the double profit approach relies on the substantive language of 2-708(2). The drafters' choice of the words "profits made from full performance" instead of "profit made on the sale" indicates that full compensation, which results from full performance, is the desired result. When the seller subtracts a resale from the "profit made on a sale" he might end up with little or no profit. When a resale is subtracted from the "profit made from full performance," however, something must be left over to fulfill the meaning of the words "full performance." This construction avoids the candid disregard of the resale credit language endorsed by the traditional approach and achieves the "right" result.

C. The Literal Approach

The literal approach demands an exact reading of 2-708(2); the seller must subtract income received from resale. This approach relies on an overall view of the Code's remedies scheme. Two other seller's reme-
dies, sections 2-706 and 2-709, require that the proceeds of a resale mitigate the breaching buyer's liability to the seller. The duty to mitigate damages under these sections seems to coincide with the same duty under subsection 2-708(2). Following a literal interpretation, a resale must be subtracted from a seller's damages. If 2-708(2) requires the same treatment as sections 2-706 (resale) and 2-709 (price), then a lost volume seller should not receive lost profits because his subsequent resale mitigates his damages.

Similarly, the literal approach maintains that nothing in the text or comments suggests 2-708(2) is superior to 2-706. In fact, 2-708(2) by its own terms operates only when 2-708(1) proves inadequate. A seller may utilize subsection 2-708(1) when no resale is made or when resale is support in comment 1 to § 2-704 of the Code. The comment discusses § 2-706 in its reference to the "resale section." Comment 1 reads in pertinent part:

[Section 2-704] thus makes the goods available for resale under the resale section, the seller's primary remedy, and in the special case in which resale is not practicable, allows the action for the price which would then be necessary to give the seller the value of his contract.

U.C.C. § 2-704, comment 1 (emphasis added). See Childres & Burgess, supra note 6, at 864. Likewise, comment 2 to § 2-706 reads in relevant part: "Failure to act properly under this section deprives the seller of the measure of damages here provided and relegates him to that provided in section 2-708." U.C.C. § 2-706, comment 2 (emphasis added). Both comments suggest that § 2-708 is to be subordinated to § 2-706 in the Code's scenario of damage remedies.

78. U.C.C. §§ 2-706 & 2-709. The measure of damages under § 2-708(1) in the vast majority of cases allows the seller to recover only a small fluctuation in the market price. For instance, assume the contract price for a quantity of goods is $1000. After breach, the seller calculates the market price at the time and place for tender as $950. The difference (excluding incidental damages for ease of computation) is $50; recoverable as damages under § 2-708(1). If the profit lost is $400, however, that is the amount recoverable under § 2-708(2). See J. White & R. Summers, supra note 11, § 7-7, at 269. In most cases it is not economically feasible to hire an attorney to collect contract-market price differentials.

Some § 2-708(1) situations may afford the seller a windfall. Assume a seller resells goods for $5000 on a $6000 contract. Further assume that under § 2-708(1) the difference between the market price and the contract price is $3000. In this case, the seller apparently could recover $8000 on a $6000 contract. The seller gets $5000 on a resale plus the $3000 damages, $2000 in excess of the original contract price. By way of contrast, § 2-706 limits the recovery to $1000, the difference between the resale price and the contract price. See J. White & R. Summers, supra note 11, § 7-7, at 269-71.

In connection with this discussion, see the court's analysis of the problem in Detroit Power Screwdriver Co. v. Ladney, 25 Mich. App. 478, 485-89, 181 N.W.2d 828, 832-34 (1970). The Ladney court found the plaintiff had proved his damages under § 2-708(2), but had not shown § 2-708(1) to be inadequate. Therefore, the court remanded the case to the lower court to make that determination. Id. at 489, 181 N.W.2d at 834.

79. See Shanker, supra note 11, at 699-700.
80. See supra note 77.
81. U.C.C. § 2-708(2). For a discussion of the relationship of §§ 2-708(2) to 2-706, 2-708(1) and 2-709, see Childres & Burgess, supra note 6, at 860-80. Although § 2-708(2) ostensibly operates only when § 2-708(1) is inadequate, many commentators believe that § 2-708(1) is almost never an adequate measure of damages. See id. at 834, 874-85.
improper under 2-706. Further, 2-706, which specifically defines the
damage rights of aggrieved sellers who resell, is the seller’s primary rem-
edy. If 2-706, as the “primary” remedy, denies recovery to an ag-
grieved seller, he should not be placed in a better position through the
secondary 2-708(2) remedy. This approach not only depends on a literal reading of 2-708(2) and its
place in the Code’s damages scheme, it also depends on a denial that lost
volume sellers exist. Criticism of the economic theories espoused under
the traditional approach is rebutted by countervailing economic consid-
erations advanced by the literal approach. The traditional approach
accepts the existence of sellers who have an unlimited capacity to pro-
duce goods and a finite number of buyers. The traditional approach
also agrees that in a lost volume situation each buyer in line can be sup-
plied and a breach results in loss of a sale that cannot be replaced.
Breaches in this context decrease total sales and profit that would have
been realized from those sales.

The literal approach attacks the underlying economic theory of the
traditional approach. It suggests that all sellers claim to operate in a

82. U.C.C. § 2-706, comment 2. See Childres & Burgess, supra note 6, at 872; Shanker, supra note 11, at 699.
83. See supra note 77.
84. See Shanker, supra note 11, at 704; supra note 77. Professors Childres and Burgess
concede that § 2-706 occupies a principal position in its domain, that being, a proper
resale. They feel that § 2-706, however, is of limited application. The authors state their
case:

The fact is that 2-706 has virtually no range of transactions to which it is
both properly applicable and of any significance. It is applicable only to finished
goods and only if the seller has resold. A much more important limitation, how-
ever, especially since the UCC does not tell us about it, is that the act of resale
should lock the seller into the resale formula only if he has more customers than
he can supply at the prevailing price during the contract period. Such situations
are precisely those in which there will be little, if any, general damages, because
in such situations the seller’s resale price is apt to meet, or even to exceed, the
contract price. This probability can only mean that the seller’s remedy which
the draftsmen thought primary is largely irrelevant to seller’s damages law.
Childres & Burgess, supra note 6, at 873-74 (authors’ emphasis).
85. See Shanker, supra note 11, at 704-05. Shanker states:

The error of the commentator’s analysis may be that it is based on the erro-
neous assumption that sellers operate in some theoretically perfect “buyer’s mar-
ket;” that is, a situation where it can be shown that the seller has and will in the
future have (1) only a predictable and finite number of customers, and (2) an
unlimited capacity continually to sell to all new buyers that may appear on the
scene. Under these assumptions, it is true that every buyer who reneges on a sale
contract theoretically has deprived his seller of a sale and a profit.

However, it is unlikely that any individual seller in the real business world
fits into this theoretical model. Few, if any, could prove with any certainty the
specific number of customers they will have in the future, and probably none
ever have the unlimited capacity to sell to all those who may appear.

Id. (footnotes omitted).
86. See id.
87. Compare id. with Harris, supra note 11, at 80-84.
"buyer's market" where they have more goods to sell than customers to buy them. Almost all sellers, in effect, would constitute lost volume sellers and therefore be entitled to lost profits under 2-708(2) without any possibility of mitigation. The literal approach believes it is important to preserve the concept of mitigation. This approach also posits that many potential lost volume sellers can prove they lost volume. In fact, few if any sellers have an unlimited capacity to produce enough goods to meet the demands of all willing buyers. Most sellers face situations where they cannot provide goods to all customers. Material shortages, mechanical breakdowns, strikes, and other contingencies substantially decrease a business' productive capacity and ability to supply all willing customers.

Finally, the literal approach has no difficulty with the unusual situation in which a seller loses volume sales even though the buyer fully performs the contract. This phenomenon occurs when a buyer, realizing it no longer needs the goods from the seller, buys them anyway in contemplation of reselling or assigning them to another buyer. This procedure undermines the traditional and double profit approaches since the first buyer escapes liability by complying with the contract. Yet under the lost sale theory the first buyer, by selling the goods he purchases, takes a sale away from the seller who would have sold those goods to the second buyer. If a buyer can do this without liability, then a seller reselling under 2-708(2) should mitigate his lost volume damages with his resale proceeds because the effect is the same—the seller loses a sale.

IV. JUDICIAL TREATMENT OF 2-708(2)

The traditional, double profit, and literal approaches must be examined in light of the courts' treatment of 2-708(2) and the lost volume seller. The rationales used by the courts clarify the interpretation of subsection 2-708(2) in the lost volume context. While there are numer-

88. See Shanker, supra note 11, at 700-01.
89. Id.
90. See id. at 704-07.
91. See id. at 705.
92. See id. at 701-03.
93. See id.
94. See id. at 702-03.
ous decisions in this area, only a few need be discussed to illustrate the various rationales used by courts in interpreting 2-708(2).

One of the first reported cases on lost profits for a lost volume seller is the case of *Neri v. Retail Marine Corp.* In that case, Neri contracted to purchase a new boat from the defendant Retail Marine Corporation. Following receipt of a down payment, Retail Marine ordered the boat from its supplier. Neri later repudiated the contract and sued for restitution of the down payment pursuant to UCC 2-718. Retail Marine counterclaimed for lost profits on the lost sale. The same boat was sold four months later to another buyer for the original price. Neri claimed that as a result, Retail Marine had regained its lost profits and the resale proceeds should be credited pursuant to 2-708(2). Retail Marine successfully alleged that it had lost profits as a result of Neri’s repudiation notwithstanding the resale of the goods.

The *Neri* court held that had it not been for the breach, Retail Marine would have sold two boats instead of one. The *Neri* court analogized the situation to a car dealer with an unlimited supply of standard-priced goods. If one buyer breaches, “the resale to replace the breaching buyer costs the dealer a sale, because, had the breaching buyer performed, the dealer would have made two sales instead of one.” Had the original sale been consummated and a second sale made, Retail Marine would have sold two boats, and earned two profits instead of one. The court relied on the Code’s overriding policy in section 1-106 that the seller should be put in as good a position as performance would have done.

The Maryland Court of Special Appeals made a convincing argument for ignoring the due credit language for lost volume sellers in *Snyder v. Herbert Greenbaum & Associates.* In *Snyder*, plaintiff Herbert Greenbaum

96. See infra notes 97-111 and accompanying text.
98. Id. at 397-98, 285 N.E.2d at 312-13, 334 N.Y.S.2d at 167-68. Restitution under § 2-718 operates where the seller justifiably withholds delivery of goods because of the buyer’s breach. See U.C.C. § 2-718. It allows the buyer to seek restitution of any amounts paid in excess of what the seller is entitled to in a liquidated damages clause. In the absence of a liquidated damages clause, the seller may keep twenty percent of the value of total performance or $500, whichever is smaller.

Because Neri counterclaimed for and proved lost profits on lost volume, restitution was not applicable. Therefore, Retail Marine received the profit lost on the sale of the boat. For the court’s discussion of § 2-718 and its relation to § 2-708, see 30 N.Y.2d at 397, 285 N.E.2d at 313, 334 N.Y.S.2d at 167.
99. Id. at 397-98, 285 N.E.2d at 312-13, 334 N.Y.S.2d at 167.
100. Id.
101. Id.
102. Id.
103. Id.
104. 38 Md. App. 144, 380 A.2d 618 (1977). For a discussion of these arguments, see supra notes 64-75 and accompanying text.
& Associates contracted to supply and install carpeting for appellants' apartments. Appellants later cancelled the contract and plaintiff sued for lost profits. The court held:

Logically, lost volume status, which entitles the seller to the § 2-708 formula rather than the formula found on § 2-708(1), is inconsistent with a credit for the proceeds of resale. The whole concept of lost volume status is that the sale of the goods to the resale purchaser could have been made with other goods had there been no breach. In essence, the original sale and the second sale are independent events, becoming related only after breach, as the original sale goods are applied to the second sale. To require a credit for the proceeds of resale is to deny the essential element that entitles the lost volume seller to § 2-708(2) in the first place—the mutual independence of the contract and the resale.

The Snyder court determined that the practical effect of applying the resale credit provision was to make a seller's recovery under subsection 2-708(2) almost identical to the recovery received by the contract-market differential of subsection 2-708(1). Applying the resale credit provision, the seller recovers the difference between the resale price and the contract price, which is no different from his recovery under subsection 2-708(1). This restricts the useful application of 2-708(2) to jobbers and manufacturers and unreasonably limits recovery by lost volume sellers of "standard priced" goods. The court added that the subsection 2-

105. Id. at 146-47, 380 A.2d at 620. The Uniform Commercial Code only applies to the sale of goods. U.C.C. § 2-102. The contract in Snyder involved the performance of services, as well as the sale of carpeting. Before the court could decide the merits of the case, it had to determine whether the UCC applied to a transaction that involved both sales and service. The court held that the sale of goods was the predominant factor in this contract, and therefore, the transaction was governed by the UCC. Id. at 147, 380 A.2d at 621 (citing Bonebrake v. Cox, 499 F.2d 951 (8th Cir. 1974) (establishing the predominate factor test in determining whether a transaction is the sale of services or goods)). The Bonebrake test is:

[Not whether they are mixed, but, granting that they are mixed, whether their predominant factor, their thrust, their purpose, reasonably stated, is the rendition of service, with goods incidentally involved (e.g., contract with artist for painting) or is a transaction of a sale, with labor incidentally involved (e.g., installation of a water heater in a bathroom).

Id. at 960 (footnotes omitted).

106. 38 Md. App. at 156, 380 A.2d at 625.

107. Id.

108. Id. at 156-57, 380 A.2d at 625-26. The Snyder court adopted familiar language when it stated:

The statutory history of the "due allowance-due credit" provision of § 2-708(2) indicates that it was added to § 2-708(2) to cover a particular class of sellers. . . . The "due credit" provision was intended to "clarify the privilege of the seller to realize junk value when it is manifestly useless to complete the operation of manufacture." Apparently, then, the "due credit" provision was intended to affect the rights of a particular class of sellers, which class does not include the "lost volume seller."

Id. (emphasis added) (footnotes omitted). In holding that the due credit clause does not apply to the circumstances of a lost volume seller, the court stated that such an interpreta-
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708(1) recovery failed to put the seller in the same position he would have enjoyed had there been full performance.109

Other courts resorting to 2-708(2) in lost volume situations take an approach similar to that of the Neri and Snyder courts.110 Courts seem to ignore the due credit language and justify doing so by relying on the history of 2-708(2) and the general philosophy of the Code to put the seller in as good a position as performance would have. Courts confronted with this question in the future will have well-founded precedent to follow. Unless courts begin to adopt the literal approach and apply the due credit language, lost volume sellers will continue to recover their lost profits in most jurisdictions.111

No Minnesota cases deal with lost volume sellers under 2-708(2),112 but Minnesota's pre-Code common law is instructive. The case of Wilhelm Lubrication Co. v. Brattrud113 appears to be the only Minnesota case addressing this issue. In Wilhelm, defendant contracted to purchase substantial amounts of lubricating oil and transmission grease from the plaintiff. Shortly after the formation of the contract, defendant repudiated.114 Plaintiff sued and the Minnesota Supreme Court determined damages as "the difference between the contract price and the cost of the merchandise to plaintiff, including all expenses, overhead, and cost of

109. Id. at 156, 380 A.2d at 625.
111. See cases cited id.
112. A computer check was run and the Uniform Commercial Code Reporting Service Findex (1978 & Supp. 1981) was used to locate Minnesota cases citing U.C.C. § 2-708. Of the cases discovered, none referred to lost volume sellers. One recent Minnesota case, however, dealt with lost profits. See Cardinal Consulting Co. v. Circo Resorts, Inc., 297 N.W.2d 260 (Minn. 1980).
113. 197 Minn. 626, 268 N.W. 634 (1936).
114. Id. at 627, 268 N.W. at 635.
delivery."  

The court added that "full performance by the defendant as agreed would usually result in a gain by the plaintiff, and the breach by defendant is a prevention of this gain, as defendant has reason to know." The court stated that the usual measure of damages was the difference between the contract price and the market price at the time and place for performance. Nevertheless, if that measure was inadequate, then the measure of damages was the seller's lost profits. The court arrived at the appropriate measure of damages after determining which measure accomplished the purpose of putting plaintiff in as good a position as complete performance.

In constructing its remedy, the court described why a resale would not mitigate this particular seller's damages:

Plaintiff herein is a company that compounds and sells at wholesale in a highly competitive market large quantities of oil and grease. It is not in the position of one who has obtained or prepared specific goods for the sole purpose of appropriation to one certain and specific contract. It has many contracts such as the one involved in this case. The breach of one such contract does not mean plaintiff must dispose of the quantity of goods specified therein in order to prevent serious loss. It merely means the loss of one sale and the profit that plaintiff would have received thereby.

Referring to lost volume without using the exact words, the court in *Wilhelm* stated that if it awarded plaintiff the difference between the contract price and market price, the recovery would have been only the difference between the contract price and the market price at the time of the breach. The court concluded, "This clearly would not include the

115. *Id.* at 632, 268 N.W. at 636.
116. *Id.* at 632, 268 N.W. at 637, (quoting Restatement of Contracts § 329, comments a and b (1936)).
117. *Id.* at 633, 268 N.W. at 637.
118. *Id.* (citing Silberstein v. Duluth News-Tribune Co., 68 Minn. 430, 71 N.W. 522 (1897)). *Silberstein* was one of the first Minnesota cases to hold that the plaintiff should be put in as good a position as if the defendant had fully performed. *Id.* at 432, 71 N.W. at 623. *Silberstein* was also a lost profits, but not a lost volume, case.
119. 197 Minn. at 633, 268 N.W. at 637.
120. *Id.* at 633-34, 268 N.W. at 637. The court held:

[The] profit is measured by the difference between the cost of the goods to plaintiff when the same are ready for delivery and the price for which it sells them to the retailer, which undoubtedly conforms closely to the current wholesale market price. If we were to apply the test that the damages are the difference between the contract price and the market price at the time and place of delivery, the only compensation plaintiff would receive would be measured by the amount the price on the market had fluctuated plus what difference there might have been between the price bargained for and the current market price at the time of the making of the contract. This, clearly, would not include the profit to which plaintiff is entitled, which we hold in this case to be properly measured by the difference between the entire cost to plaintiff of the goods contracted for and the price which defendant agreed to pay plaintiff.

*Id.* This language is similar to that used by the Maryland court in Snyder v. Herbert
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profit to which plaintiff is entitled, which we hold in this case to be properly measured by the difference between the entire cost to plaintiff of the goods contracted for and the contract price which defendant agreed to pay plaintiff. 121 This approach is similar to the Code's treatment of the seller under 2-708(2).

The Minnesota Supreme Court has not discussed lost profits for lost volume sellers since Wilhelm. 122 Eventually the court will confront the interpretation of 2-708(2) in the context of lost volume sales. In such a case the court should follow the traditional approach. The traditional approach in Wilhelm and the comments and history behind 2-708(2) compel the court to adopt the traditional approach. Wilhelm, which is in line with Code decisions such as Neri and Snyder, is support for the proposition that a seller can lose volume and consequently profit.

V. AN ECONOMIC ANALYSIS

This portion of the Note combines legal commentary with economic theory in an attempt to provide another perspective on the lost volume problem. Two assumptions are inherent in the lost volume concept. First, that the seller has an unlimited capacity to produce specific goods and second, that the supply of the goods exceeds the demand. 123 These assumptions are analyzed using an economic model of perfect competition. 124 The question that will be addressed is whether it is possible for a business operating in a perfectly competitive market to lose profit from lost sales. Using the model of perfect competition this Note shows that a firm maximizes profits at a defined level of production. Firms producing beyond this level should not recover lost profits. 125 As a rebuttal to the profit maximization argument, it is argued that the condition of profit maximization is not a goal of many firms and is not a foremost consideration when determining how much to produce. Therefore, a lost sale by a firm not interested in maximizing profits is still a loss of profit.

A. The Perfect Competition Model

The model of perfect competition is used in analyzing whether a firm

121. 197 Minn. at 634, 268 N.W. at 637.
122. See supra note 112.
123. The analysis of the perfect competition model is borrowed from E. DOLAN, BASIC ECONOMICS 372-85 (1977).
124. See infra notes 126-29 and accompanying text.
is losing or has lost profit by lost sales. A perfectly competitive firm is defined as one that has no power to alter the price it receives for its products.\textsuperscript{126} Two predominant characteristics identify a perfectly competitive firm.\textsuperscript{127} First, the firm sells a product undifferentiated from that of others produced in the industry. Second, its sales amount to only a small portion of the total market.

Because the product is nearly identical to others produced in the market, consumers do not discriminate between products. Consequently, each firm in the industry must sell its product at the same price as any other. Such firms are labeled price takers.\textsuperscript{128} For example, if firms A, B, C, and D sell their identical widgets for $100, why should buyers pay $120 for the same product from firm E? The market constrains the price a firm may charge. Management need not worry about setting the price because the market sets it. If one firm raises its price it loses sales to the other firms.\textsuperscript{129}

B. The Argument: Choosing a Profit Maximizing Production Level

Assuming a lost volume seller's supply for his product meets and exceeds his demand,\textsuperscript{130} the profit maximization theory introduces a new consideration: Is it desirable, within a firm's profit picture, to produce a quantity that meets all demand? In a perfectly competitive market, a firm's only decision is the amount of its product it should produce; the

\textsuperscript{126} See E. Dolan, \textit{supra} note 123, at 373.

\textsuperscript{127} \textit{Id.}; See E. Mansfield, \textit{supra} note 125, at 249-50; W. Peterson, \textit{Principles of Economics: Micro} 203-204 (3d ed. 1977). Two additional characteristics of perfect competition are one, all market participants are well informed about prices, sources of supply, and other market information; and second, relatively few barriers restrict exit or entry from the market. See E. Dolan, \textit{supra} note 123, at 372-73; E. Mansfield, \textit{supra} note 125, at 249-50.

\textsuperscript{128} See E. Dolan, \textit{supra} note 123, at 372. Dolan describes a price takers method as:

> All decisions that the price taker must make are, by their nature, pure calculative decisions. There is no room . . . for entrepreneurship. All the firm's management need do to earn maximum profits is to look at the given prices, organize internal operations so as to minimize costs, and then to calculate what quantity of output to produce. Such things as advertising, introducing new products, or experimenting with new production techniques have no place.

\textit{Id.}

\textsuperscript{129} See E. Dolan, \textit{supra} note 123, at 372. The amount of goods supplied or demanded in a marketplace corresponds directly to changes in the price of those goods. This concept is known as elasticity of supply or demand. See \textit{id.} at 292. Elasticity of supply is technically defined as "the percentage change in the quantity of a good supplied, divided by the percentage change in the price of the good." \textit{Id.} In simpler terms, elasticity shows how much quantities demanded or supplied change in response to price changes. If the demand for a good is perfectly inelastic, there is no quantity change in response to a price change. Conversely, if, as in perfect competition, the demand is perfectly elastic, the quantity demanded or supplied can vary without a change in the price. For a more thorough discussion, see \textit{id.} at 292-98. The seller is a price taker because in perfect competition the market determines the available price.

\textsuperscript{130} See \textit{supra} notes 23-26 and accompanying text.
price is set by the market. To be profitable, a firm must find a level of production that maximizes revenues and minimizes costs. A firm should produce at the rate where the marginal cost of the last unit produced equals the price.

**FIGURE 1**

_Delination of the short-run supply curve for a price-taking firm_

Marginal cost is defined as the cost of producing one additional unit of output. It is at this point that a lost volume seller maximizes prof-

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131. See E. DOLAN, supra note 123, at 373.

132. Dolan explicates a price-taking firm’s short-run supply curve in Figure 1. Id. at 377. E. DOLAN, supra note 123, at 376-78.

Figure 1 depicts the marginal cost curve. The vertical axis of this illustration measures the cost per unit. The horizontal axis measures quantity of output that will be produced at a given price. The average total cost (ATC) curve portrays the average total sum of fixed costs and variable costs. The average variable costs (AVC) are depicted by the AVC curve. Lastly, the averaged fixed costs (AFC) curve portrays the average fixed costs. This is comprised of costs such as amortization and depreciation of plant and equipment, energy costs to heat and light a building, and a reasonable amount of total profit. It is readily apparent by viewing the downward slope of the AFC that each additional unit reduces the cost allocated to producing that unit by some increment. In effect, the cost of each unit represents a share of the fixed costs. The more units that are produced, the smaller that allocable share becomes. Id. at 375.

At point $E_1$, which is the price of $5, the firm is making pure profit because the price received is in excess of the average total cost of producing a unit. At $E_2$, however, the marginal cost and average total cost are equal. At this price the firm will break even.
As long as producing one more unit adds more to revenue than it does to cost, total profit will rise. Producing the additional unit is inefficient and unwanted when the marginal cost of producing that unit exceeds the profit it would generate. If a firm must produce X number of its product in order to maximize profits and minimize costs, production of X+1 units is beyond peak efficiency. Theoretically, as the literal approach advocates, a lost volume seller attempts to produce at a point where marginal cost equals price. Production of units past this point of peak efficiency results in diminishing marginal returns.

If profits are maximized at the point of peak efficiency, a breached contract does not result in lost volume unless the seller can show that his

**FIGURE 2**

*Maximization of profits where price equals marginal cost*

Breaking even in this context includes a reasonable return on investment (profit). Following the marginal cost curve downward point $E_3$ is reached. Although $E_3$ is a randomly picked point, it is one point where loss minimization occurs. Any firm whose price lies between the ATC and the AVC on the marginal cost curve will have a similar goal in mind. Cutting back production by one unit would save less in costs than revenue that is lost. Producing one point lower, at $E_4$ where marginal cost equals average variable cost, sale of the product would not even cover the cost of labor and raw materials. The firm, at this time, would do just as well to shut down. *Id.* at 375-76.

133. *Id.* at 374-378. See *supra* note 132 and accompanying text.

134. See *E. DOLAN, supra* note 123, at 348.
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firm has not surpassed the point of profit maximization.\textsuperscript{135} If that point has been surpassed, an additional sale is not wanted because it would not promote optimal efficiency and profit. Following this rationale, a court should not award the seller lost profits for volume that surpasses an efficient level of production.\textsuperscript{136}

This problem may be illustrated graphically. In the perfectly competitive market, a business strives to have the price (P) of a unit equal its marginal cost (MC) of producing that unit.\textsuperscript{137} Quantity $Q_0$ in Figure 2 bears a price of $\$4$. If one more unit were produced the additional cost would be $\$4$, but the revenue generated would be $\$6$, leaving a net gain of $\$2$. By spending $\$4$ this firm is getting $\$6$. Based on this information the firm would produce more than $Q_0$ units until it reached equilibrium at $Q_1$ (where MC equals P). The triangle to the lower left of the MC-P intersection ($Q_1$) represents the profits captured by producing $Q_1$ units instead of $Q_0$ units.

Alternatively, the triangle to the upper right of the MC-P intersection ($Q_2$) shows the profits lost by producing $Q_2$ units. At quantity level $Q_2$ the return on a sale of a unit is a loss of $\$2$ because the unit costs $\$8$ to produce but sells for only $\$6$. The optimal level of output is $Q_1$: the intersection of the marginal cost curve with the existing market price.\textsuperscript{138} If the seller’s production passes point $Q_1$ he is not entitled to lost profits for lost volume because he has eclipsed the most desirable level of production. Under the literal approach, recovery of damages for lost profits in such a situation overcompensates the seller.\textsuperscript{139}

\hspace{1cm} \textbf{C. The Rebuttal: The Theory of Profit Maximization is Not Applicable}

As discussed in the previous section, the price-taking firm in a perfectly competitive market attempts to produce that quantity of its product that maximizes profits.\textsuperscript{140} In theory, production beyond this point is not desirable. One theorist believes that a seller who produces beyond this profit maximizing point should not recover lost profits.\textsuperscript{141} To do so rewards the lost volume seller with a sale he does not want. This assumption, though theoretically correct, does not mirror the true image of the everyday business world.\textsuperscript{142}

The profit maximizing theory suffers much criticism from econo-

\begin{itemize}
  \item \textsuperscript{135} See Comment, Theoretical Postscript, at 718-19 & n.10.
  \item \textsuperscript{136} See Shanker, supra note 11, at 704-06.
  \item \textsuperscript{137} See supra note 132 and accompanying text.
  \item \textsuperscript{138} Id. For a further discussion of Figure 2, see W. Nicholson, supra note 125, at 260.
  \item \textsuperscript{139} See Shanker, supra note 11, at 700, 704-07.
  \item \textsuperscript{140} See supra notes 130-39 and accompanying text.
  \item \textsuperscript{141} See Shanker, supra note 11, at 704-07.
  \item \textsuperscript{142} See infra notes 150-59 and accompanying text.
\end{itemize}
mists. While many critics are not particularly enamored with the concept, it has withstood attack primarily because no reasonable alternative has been found. Most economists would agree that profit maximization is not the sole objective of a business. Even if it were, most businesses do not possess adequate information to enable them to maximize profits in an exact sense.

The long run behavior of most firms shows that they strive for profit maximization. In the short run, however, a myriad of other objectives preoccupies the energies of business executives and managers. Among these objectives is the desire to expand clientele and goodwill. To do this a firm may produce and sell goods beyond that quantity known to be profit maximizing, or even profitable. Other important short run objectives include improvement of social conditions in the firm’s community, increased market share, and enhancement of the firm’s image as a good employer and a useful part of the community. Each of these objectives may be important to an individual firm but none can be said to be necessary or even helpful in meeting the goal of profit maximization.

The theoretical construct of profit maximization is not always applied in practice. Because the above goals achieve long run profits, they tend to show that the profit maximization assumption is probably correct. In the short run, day-to-day business world in which breaches of sales contracts occur, however, profit maximization is probably inapplicable. Similarly, in quantifying damages for breach of contract the

143. See W. Nicholson, supra note 125, at 269. Nicholson states:

Over the years a vast amount of evidence has been marshalled against the hypothesis that profit-making firms seek maximum profits, but, primarily because no suitable alternative has been found, the hypothesis has withstood these assaults. The attacks on the marginalist approach can be classed into three general types: that the profit-maximization approach is too simple; that there exist alternative, equally simple hypotheses that can better explain reality; and that real-world firms do not have suitable information to be able to maximize profits, nor would they particularly want to maximize profits if they had such information. Id.

144. Id.

145. See infra notes 152-59 and accompanying text.

146. See W. Nicholson, supra note 125, at 269.

147. See E. Mansfield, supra note 125, at 142.

148. Id.

149. It is suggested that some firms “satisfice” rather than maximize profits. Id. at 167. “Satisficing” occurs when a business firm aims at a satisfactory rate of profit rather than a maximum figure. A firm operating under this principle does not attempt to maximize profits because of the time and expense involved in computing such data on a continuous basis. A firm tries to maintain marginal standards of performance. In essence, a firm operates on a spectrum of operation somewhere between unsatisfactory and satisfactory levels of production. Id. at 167-68. For an extended discussion of the “satisficing” concept and related themes, see id. at 168-69 & n.15.

150. See E. Mansfield, supra note 125, at 142; W. Nicholson, supra note 125, at 270-71.

151. See infra notes 155-59 and accompanying text.
profit maximizing theory may not accurately reflect a seller's true situation.

First, it should be noted that production can be profitably maintained at more than one level. Profit maximization is merely an optimum or ideal level at which to produce. Many firms, in placing other objectives before profit maximization, fail to reach that optimum level in the short run. They are, nevertheless, profitable firms. An illustration may clarify this problem. Assume that firms A and B have differing goals. Firm A wants to maximize profits while firm B seeks to maximize revenue.

Figure 3 illustrates the differences in output levels for both firms A and B. Firm B, the revenue maximizer, chooses to continually increase sales as its goal. Firm B’s production is at point $Q_2$ on the scale. Firm A’s goals are different. It seeks to maximize profits by producing at its point of peak efficiency—$Q_1$, a production level which is below that of firm B at point $Q_2$. Although firm B is receiving a lower rate of return for its product, it is still making a profit.

**FIGURE 3**

*Comparison of Profit Maximization and Revenue Maximization*

152. Compare W. Nicholson, supra 125, at 271-72 with supra notes 130-39 and accompanying text.

153. See W. Nicholson, supra note 125, at 272.

154. Id.

155. Id.

156. Id. Nicholson explains Figure 3 as follows:

For simplicity it has been assumed that each unit of output can always be produced at a cost of $MC$. A profit-maximizing firm will therefore produce output level $Q_1$ for which $MR = MC$. If the firm were devoted to the goal of revenue maximization, however, it would proceed to output level $Q_2$, since at this level of output marginal revenue is 0.
Figure 4(a) shows the actual profitable range. From a price of about $45 and an output of approximately nine widgets, it is profitable to produce more widgets. Figure 4(b) shows the most profitable level at which to produce widgets is where the marginal cost of producing one widget equals the price of that widget. That level of output rests at approximately nineteen widgets. Any range of production between nine and twenty-five widgets, however, is profitable for the firm according to this graph.

This demonstrates that the profit maximizing level is virtually useless in measuring the damages of a lost volume seller. Courts cannot award

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157. See E. DOLAN, supra note 123, at 375.
158. Id. at 376.
159. Id.
damages for certain levels of production and refuse damages to firms that produce beyond the point where marginal cost equals price. A court cannot dictate business policy to a firm. A business may pursue an increase in its market share by continually advertising or increasing the number of retailers it supplies. This business philosophy may not maximize short run profits.

Proof of a firm’s profit maximizing point cannot show whether or not it has lost a sale, and so is irrelevant to a determination of damages. Instead, a court should be concerned with whether there has been a breach and whether the seller has lost volume as delineated by Professor Harris’ three criteria for identifying lost volume sellers. An analysis of lost volume must be suitably rigorous to preclude those improperly seeking to utilize that remedy. If the analysis is too simplistic, too many sellers will be considered lost volume sellers. If the cost and time required to prove lost volume is prohibitive, however, sellers entitled to recover 2-708(2) lost profits will be unable to do so.

VI. CONCLUSION

In applying 2-708(2) to lost volume sellers, one must cope with the frustrating language at the end of that section allowing “due credit . . . for proceeds of resale.”160 Taken at face value the statutory formula provides the seller with only nominal damages. The text of 2-708(2) makes it clear that it governs manufacturing cases. Comment 2 to section 2-708 clearly indicates that subsection 2 is intended to govern lost volume cases as well. Confronted with this evident contradiction, many courts simply have ignored the “due credit” phrase.

Commentators have contested not only the contorted application of section 2-708 to lost volume sellers, but have questioned the existence of the lost volume situation. The economic analysis of perfect competition suggested by the literal approach attempts to show that lost volume sellers do not exist, or if they do exist, they do not deserve lost profits. On the contrary, lost volume sellers do exist and the theoretical constructs of profit maximization are too simplistic and detached from reality to be of any use in analyzing lost volume situations. The more efficacious approach is to determine if a seller meets the three criteria established by Professor Harris.161 If so, a court should award lost profits for lost volume. The Harris criteria provide a useful and feasible guide in finding lost volume.

The text and comments of the Code together with the common law allowance of expectation damages, which represents the prospect of gain from the contract, all militate in favor of rewarding lost profits. The Code’s intent expressed in section 1-106 to liberally administer remedies

160. U.C.C. § 2-708(2).
161. See supra notes 36-45 and accompanying text.
to effectuate complete compensation and subsection 2 of 2-708 which states that the seller should be put in as good a position as performance would have done, should be considered by any court awarding damages.

Finally, the Minnesota Supreme Court's pre-Code decision in *Wilhelm Lubrication Co. v. Bratrud*\(^{162}\) provides a sensible approach for determining lost volume sales and sellers. The *Wilhelm* approach is in keeping with the prevailing interpretation of subsection 2-708(2). Although the Minnesota Supreme Court has not affirmed this decision since the enactment of the Code, Minnesota courts should follow it in assessing the damages of lost volume sellers.

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162. 197 Minn. 626, 268 N.W. 634 (1936).