STATE OF MICHIGAN

COURT OF APPEALS

WEST BRANCH TANK & TRAILER, INC.,

Plaintiff-Appellee,

v

TIMOTHY K. SEARFOSS,

Defendant-Appellant.

UNPUBLISHED
March 10, 1998

No. 194399
Ogemaw Circuit Court
LC No. 94-000606-CK

Before: MacKenzie, P.J., and Holbrook, Jr., and Saad, JJ.

PER CURIAM.

Defendant appeals as of right from a bench trial judgment in favor of plaintiff in this breach of contract action. Specifically, defendant appeals the trial court's ruling that defendant breached an exclusive licensing agreement by failing to repurchase plaintiff's inventory when he terminated the contract. We affirm.

I

Defendant first argues that the trial court erred when it found that plaintiff did not materially breach the contract before defendant terminated the contract. We conclude that the trial court's finding was erroneous, but because plaintiff's material breach was waived by defendant, the trial court's ultimate conclusion on this issue was correct (i.e. defendant may still be liable for damages).

There was no dispute that plaintiff was having difficulty selling defendant's product and failed to meet the minimum sales quotas. As seen from plaintiff's invoices, its annual purchases were far short of the annual purchase quotas. Therefore, it appears that plaintiff did materially breach the contract before defendant terminated the contract. However, a waiver of a material breach may be shown by either express language of agreement, or implicitly by a declaration, act, or by conduct that is inconsistent with exacting strict performance. See *Fitzgerald v Hubert Herman, Inc*, 23 Mich App 716, 718; 179 NW2d 252 (1970). Put another way, if a material breach of contract occurs that does not indicate an intention to repudiate the remainder of the contract, the injured party must elect to either continue performance or cease performance and seek damages. *Schnepf v Thomas L McNamara Inc*, 354 Mich 393, 397; 93 NW2d 230 (1958). Consequently, any act by the injured party that indicates an

intent to continue will operate as a conclusive election to waive the breach. *Id.* Moreover, once the injured party has waived the breach, it may then be held liable for its subsequent breach of the contract. *Id.* at 397-398.

Here, defendant waived plaintiff's prior breaches of the contract between the parties. The language of clause five states: "if the licensee fails to purchase the minimum number required. . . ." This clause as a whole implicitly assumes that if defendant exercises its option to afford plaintiff additional time, defendant will waive a breach in order to continue the contractual relationship. Moreover, after plaintiff failed to meet its quota, instead of claiming breach and requesting damages, defendant complied with plaintiff's request to slow production and continued the contractual relationship.

As part of this issue on appeal, defendant also argues that although there was no mention of specific marketing obligations in the contract, plaintiff breached its implied duty of good faith and fair dealing by not adequately marketing the product during the duration of the contract. In the context of commercial transactions, "good faith" is defined as "honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade." MCL 440.2103(1)(b); MSA 19.2103(1)(b). "Good faith" therefore has both a subjective component i.e., "honesty in fact" and an objective component i.e., "reasonable commercial standards." Here, defendant offered no evidence of plaintiff's dishonesty or bad faith omissions in execution of its duties under the contract. Defendant merely expressed an opinion that more marketing could have been done to increase sales. Moreover, plaintiff did attempt to market the products by: (1) employing a full time salesman to work exclusively with defendant to sell his products; (2) conducting local demonstrations of the products; (3) attending national trade shows; (4) advertising locally; (5) creating flyers and sales brochures; and (6) advertising in trade publications. This evidence suggests that plaintiff attempted in a commercially reasonable manner to market defendant's products. Therefore, there was no breach of the implied covenant of good faith and fair dealing.

II

Defendant contends that the remedy provision of clause five was not intended to be the exclusive remedy in the event of breach or, alternatively, that it "failed of its essential purpose" when the inventory became obsolete. We disagree. Under MCL 440.2719; MSA 19.2719, the parties to a contract may limit their potential damages or modify the remedies for breach. Clause five set forth a procedure for the parties to follow in the event plaintiff became unable to purchase the minimum number of systems designated in the contract. This remedy clause, by its very language, could be triggered at the option of defendant who upon termination of the contract was required to repurchase unsold inventory. Although the express language of the contract did not state that this remedy was exclusive, if triggered by the affirmative actions of defendant, it appears from the language of the clause that the remedy did become the intended sole remedy. The clause states that "the LICENSOR may terminate this Agreement . . . [and then defendant] will repurchase all unsold inventory." Moreover, defendant did not seek traditional contract damages or even plead a counterclaim for such damages. Therefore, although the clause five remedy was optional, the repurchase of plaintiff's inventory became mandatory upon defendant's decision to waive prior breaches of the contract and comply with the procedure set forth in clause five.

MCL 440.2719(2); MSA 19.2717(2) provides that if an exclusive remedy provided for in the contract "fails of its essential purpose," then alternative remedies may be provided in accordance with the Code. An agreed upon remedy "fails of its essential purpose" when unanticipated circumstances cause the seller to be unable to provide the buyer with the remedy to which the parties agreed. *Price Bros Co v Charles J Rogers Construction Co*, 104 Mich App 369, 374; 304 NW2d 584 (1981). It is a well established principle of contract law that changes in economic conditions do not alter contractual obligations. See *Chase v Clinton Co*, 241 Mich 478, 484; 217 NW 565 (1928). Defendant, regardless of his initial economic reasons for such a remedy, agreed to carry the market risk of obsolescence in this contractual relationship. More importantly, defendant is capable of providing the remedy agreed upon, namely repurchasing the inventory. Therefore, the trial court did not err when it held that defendant was required to repurchase the inventory pursuant to clause five of the contract.

III

Next, defendant claims that the remedy provision of clause five was unconscionable and unenforceable. The examination of a contract or a specific provision for unconscionability involves a procedural inquiry and a substantive inquiry. *Northwest Acceptance Corp v Almont Gravel Inc*, 162 Mich App 294, 302; 412 NW2d 719 (1987). Procedural unconscionability examines the "real and voluntary meeting of the minds" of the parties at the time the contract was executed and considers factors such as: (1) relative bargaining power; (2) age; (3) education; (4) intelligence; (5) business savvy and experience; (6) the drafter of the contract; and (7) whether the terms were explained to the "weaker" party. *Johnson v Mobil Oil Corp*, 415 F Supp 264, 266-268 (ED MI, 1976). Substantive unconscionability inquires whether the disputed term is commercially reasonable. *Id.*

Defendant identifies no evidence to suggest that he did not understand the ramifications of clause five at the time the contract was executed. Defendant admitted that he had an attorney draft a version of the contract. Moreover, testimony suggests that defendant requested the insertion of clause five and aided in its drafting. Defendant is a fifty percent owner of a Michigan corporation and presumably competent in matters concerning his business. Notably, the parties had done business in the past. Finally, defendant testified that he fully understood and personally executed the contract. This contract was executed by two businessmen with comparable business savvy and experience. Moreover, there was not a great disparity in bargaining power between the parties. In fact, it was defendant who held a patent on the tarp systems, thereby giving him the power to choose any distributorship agreement which met his business requirements. In light of these factors, it appears that the parties at the time of the execution of the contract had a "real and voluntary meeting of the minds," and therefore procedural unconscionability did not exist. Nor was the provision substantively unconscionable. Defendant may have wished to repurchase all outstanding devices in order to strictly control the distribution of the tarp systems or have an intact and ready to sell inventory to transfer to another distributor in the event the present agreement did not result in the acceptable number of sales. Therefore, the clause was commercially reasonable.

IV

Next, defendant says that the term "all unsold inventory" in clause five of the contract was ambiguous because it is unclear whether this term included: (1) all inventory held by plaintiff, including other items not manufactured from defendant, or merely defendant's goods; (2) items designed and manufactured after the execution of the contract and items purchased before execution; or (3) obsolete items in the inventory. The principal aim in the interpretation of contracts is to ascertain the intention of the parties. *D'Anvanzo v Wise & Marsac, PC*, 223 Mich App 314, 319; 565 NW2d 915 (1997). A contract is ambiguous if it is: (1) susceptible to two or more reasonable interpretations (a latent ambiguity); or (2) inconsistent on its face (a patent ambiguity). *Petovello v Murray*, 139 Mich App 639, 642-645; 362 NW2d 857 (1984).

"Inventory" has been defined in the context of commercial transactions as goods "held by a person who holds them for sale or lease or to be furnished under contracts of service or if he has so furnished them, or if they are raw materials, work in process or materials used or consumed in a business." MCL 440.9109; MSA 19.9109; *Litwiller Machine & Mfg Inc v NBD Alpena*, 184 Mich App 369, 373-374; 457 NW2d 163 (1990) (component parts of boom assemblies constituted inventory). Plaintiff was holding these units to resell at the retail level and therefore, they were inventory. The word "unsold" is also unambiguous. It is defined as not "to give up, deliver, or exchange goods or services for money or its equivalent; to part with for a price." Webster's New Twentieth Century Dictionary of the English Language 2d ed, 1983. Therefore, plaintiff's unsold inventory would include all inventory for which plaintiff had not yet transferred title to a purchaser. Finally, the word "all" is unambiguous. This Court has held in the context of interpreting a contractual release of liability that the word "all" should be given its ordinary and natural meaning and connote the broadest possible classification leaving no room for exceptions. *Skotak v Vic Tanny Int'l, Inc*, 203 Mich App 616, 619; 513 NW2d 428 (1994). This would suggest that defendant was required to repurchase every unit in plaintiff's inventory.

Defendant's post-termination conduct further evidences his original intent to repurchase all of the unsold Roll Rite inventory. In the letter in which defendant terminated the contract pursuant to clause five, defendant stated that "since my inventory of finished product is small and I am limited by time and money I should be able to start repurchasing your inventory fairly soon, as sales dictate." This letter appears to comply with the procedure in clause five and explicitly states that defendant intended to repurchase plaintiff's inventory. Moreover, defendant actually did begin to repurchase plaintiff's inventory and even added the five percent handling fee as required by clause five of the contract. This course of conduct exhibited defendant's understanding of the contract.

V

Defendant claims that at the behest of plaintiff, he developed an alternative semi-automatic design that sold poorly and remained in plaintiff's inventory until the trial court ordered defendant to repurchase the inventory. He argues that the trial court's inclusion of these alternative designs into the repurchase inventory was erroneous because the contract contained no provision addressing these manual systems. We disagree. This agreement was an exclusive distributorship that by its terms

granted plaintiff the exclusive authority to "sell tarp reel apparatus or any improved or revised versions thereof within the continental United States, Alaska and Hawaii, to any other person, firm or corporation." The scope of the contract expressly included revisions and modifications of the original product subsequent to the time of execution, including a semi-automatic version. It would be an unreasonable interpretation of clause five if the scope of the contract included all versions of defendant's product but the remedy clause included only "electric tarp systems." Moreover, the contractual language was "all unsold inventory." The word "all" is unqualified and its qualification to include only electric tarp systems would be inconsistent with the scope of the contract. Also, defendant testified in a deposition that he intended to repurchase everything produced within the dates of the contract. This testimony exhibits defendant's understanding of the clause as meaning electric as well as other versions of the tarp systems. In light of the overall scope of the contract, the generally unqualified meaning of the word "all," and defendant's apparent understanding of the contractual language, the trial court was correct to interpret "all unsold inventory" as including the semi-automatic systems.

With regard to defendant's objection to the inclusion of damaged inventory in the term "all unsold inventory," testimony at trial indicated that there were seventeen units that suffered water damage because of substandard warehousing. However, the extent of this damage was to the packaging of the items and not to the actual products. The trial court's finding that these products were undamaged was not clearly erroneous, especially in light of plaintiff's general practice of removing the packaging to install the product for the purchaser. With regard to defendant's objection to the inclusion of obsolete inventory items, the contract clearly apportioned the risk of obsolescence upon him and changes in economic or market conditions do not alter contractual obligations.

Defendant also argues that the obsolete goods should not be included in the inventory to be repurchased because, as "goods" under the Uniform Commercial Code, they are covered by an implied warranty of merchantability which obsolete goods could not meet. MCL 440.2314; MSA 19.2314 provides a warranty that goods shall be merchantable in a contract for their sale if the seller is a merchant with respect to goods of that kind. Defendant's repurchase of plaintiff's inventory is not a "contract for the sale of goods." Title to the inventory is being transferred back to defendant but not pursuant to a sale.

VI

Defendant also contends that the trial court erred in awarding plaintiff its specified damages because plaintiff failed to establish its burden of proof as to which products were produced during the contract period. With regard to damages, the party asserting a breach of contract bears the burden of proving its damages with reasonable certainty. *Walter Toebe & Co v Dep't of Highways*, 144 Mich App 21, 38; 373 NW2d 233 (1985). According to trial testimony from both parties, the sole item category that had both pre- and post-contract production was RR 525. Plaintiff's president testified that fifty-six percent of this category was produced during the contract period and substantiated this allegation with purchase invoices. Defendant's own testimony suggested that approximately fifty percent was produced during this period. The trial court's damage computation required defendant to repurchase only fifty-six percent. Although not exactly mathematically in accord with defendant's testimony, this is a reasonable computation. Further, defendant offered no objection to the inventory

data that was admitted by plaintiff. Therefore, in light of plaintiff's undisputed inventory data and the reasonableness of the damages computation as compared with defendant's own testimony, the trial court was correct in finding that plaintiff had met its burden of proof with regard to damages.

VII

Finally, defendant argues that he was denied a fair trial as a result of prior deposition testimony taken out of context and used to impeach him, giving the impression that he would repurchase all inventory purchased after the execution of the contract. Defendant did not offer a specific ground for objecting to the nature of the cross-examination at trial and did not object to references made to it in closing argument. Therefore, this issue was not preserved for review. *Tringali v Lal*, 164 Mich App 299, 306; 416 NW2d 117 (1987).

Affirmed.

/s/ Barbara B. MacKenzie
/s/ Donald L. Holbrook, Jr.
/s/ Henry William Saad