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COMMENTS

AN EXERCISE IN CONTRACT DAMAGES: *CITY OF MEMPHIS v. FORD MOTOR COMPANY*

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When the court tangled with difficult problems of contract damages in *City of Memphis v. Ford Motor Co.*,[1] certain salutary rules of damages emerged somewhat the worse for wear. Although the case itself can in no sense be considered a landmark in the law, nevertheless, certain aspects, because they are found only in the record and thus generally unavailable in the future to the profession, require comment.

For many years Ford had an assembly plant in Memphis in which it used substantial amounts of electricity, supplied by Memphis Light, Gas and Water Division, a branch of the city government engaged in the electric utility business.[2] In 1955 Memphis hired consulting engineers to consider the feasibility of building a steam generating plant. Memphis at that time had no generating capacity, purchasing all of its energy. Early in 1956 Memphis awarded contracts for the building of three 250,000 KW[3] units. According to the President of the Division this was one of the largest steam generating plants ever to be built at one time.[4] By November 19, 1956 Memphis had made commitments for over $45,000,000. Less than a month later it issued $163,000,000 in bonds to finance the generating plant and related facilities.

On November 19, 1956 Ford entered a contract with Memphis, under the terms of which Memphis agreed to supply and Ford agreed to buy electrical energy to be used for the operation of Ford's plant. The life of the contract was five years from the effective date, December 1, 1956. Under the terms of the contract "The minimum monthly bill for demand and energy . . . shall in no case be less then $1.20 per

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1 304 F.2d 845 (6th Cir. 1962).

2 This statement of facts is from the appendices filed in the Court of Appeals. Reference is made to particular pages only when the fact referred to was or might be subject to substantial controversy.

3 A brief explanation of some of the terms and abbreviations used may be helpful. KW (kilowatt) is a measure of the rate of delivery of electric energy. Demand, which is measured in KW, is the rate at which the customer calls for energy. The maximum rate to which the customer has a contract right is the contract demand. KWH (kilowatt hours) is the total amount of energy delivered during any given period.

4 For comparison: The Grand Coulee hydroelectric plant has a capacity of 1,974,000 KW; Hoover hydroelectric plant has a capacity of 1,249,800 KW. The World Almanac and Book of Facts, 1962, p. 220.

kilowatt, times the highest demand established during the preceding twelve months or contract demand, whichever is greater." Contract demand was 5300 KW. Another clause provided a surcharge of fifteen per cent on demand and energy charges and on minimum bills. In addition the contract contained the following provision:

> In the event of cancellation of this agreement by Division for any breach or default on the part of Customer, . . . there shall immediately become due and payable to Division as liquidated damages, and not as a penalty, on account of the 'special investment'[5] of Division made for the benefit of Customer, a further amount equal to the sum of the minimum amounts or minimum monthly bills computed for the entire period of the unexpired term thereof. (Footnote added.)

In the middle of January 1959 Ford sold its plant, and moved out of Memphis. The Division thereupon sent Ford a bill of $3,413.22 for the first part of January and for $252,576.78, the amount of the minimum charge for the remaining thirty-four and one-half months of the contract.[6] Ford paid the bill for the service rendered during the first part of January, but refused to pay any of the balance. The Division sued Ford in the United States District Court for the Western District of Tennessee where it secured judgment for $252,576.78 with interest from the date of the filing of the complaint. In the Court of Appeals Ford argued, among other things,[7] that the acceleration clause was a penalty. However, the court rejected Ford's arguments and affirmed the judgment below.

Two aspects of the case deserve particular consideration: (1) whether the acceleration clause was valid and (2) what the measure of damages would be in a case like this in the absence of the acceleration clause. Since the answer to the first question depends in part on the second, they will be considered in reverse order.

Measure of damages in absence of acceleration clause. One of the fundamental assumptions of contract law is that generally a party to

[5] The meaning of the words "special investment" which were also used elsewhere in the agreement were complicated in the case by facts which need not concern us in analyzing the problems raised here.

[6] It is interesting to note that the record is lacking in evidence that there had *at this point been* any clear repudiation by Ford which would justify the acceleration of the subsequent bills. The Division did, however, know informally (Appellant's Appendix, 47a) what Ford's position was, and it was not unreasonable for it to assume that Ford would repudiate the contract, as Ford in fact did.

[7] Ford's primary position was that the contract was a requirements contract and that when its need for electricity terminated it was no longer obligated by the minimum bill provision. However, the Court of Appeals agreed with the District Court's findings that, in effect, "the contract was not a 'requirements contract' but was a contract for a five-year term, under which Ford was obligated to pay the minimum monthly bills specified in the contract during that period. . . ." 304 F.2d at 848.

a contract injured by breach is entitled to damages sufficient to put him in the position that he would have been in if the performance had been rendered as promised.[8] In short he receives protection of what has been called the expectation interest.[9] Had Ford not breached the contract Memphis would have been entitled to receive $7,314 the middle of each month from February 1959 through December 1961, for service during the months of January 1959 through November 1961. Under the decision in this case Memphis received judgment for the total of those amounts, less the $3,413.22 already received for service in January. Such an award in two ways puts Memphis in a better position than it would have been in if the contract had been performed. First, Memphis would have had expenses which it was saved by the breach. These savings were not deducted from its recovery. Second, under the contract Memphis would have received payment of the minimum bills only in installments and not in a lump sum. The judgment does not transform those installments into their present value at the time of judgment.

Expenses saved. The contract incorporated a rate schedule which provided for a monthly demand charge[10] of one dollar per KW of demand and an energy charge[11] of 2.75 mills per KWH, plus a fifteen per cent surcharge on each.[12] If Ford had fully performed its contract obligations it would have paid Memphis $7,314 per month through the end of November 1961, the "minimum monthly bill for demand

[8] The purposes underlying this assumption are explored in the classic article, Fuller & Perdue, The Reliance Interest in Contract Damages, 46 Yale L.J. 52, 373 (1936-1937). See also Dawson, Restitution or Damages?, 20 Ohio St. L.J. 175, 187 (1954). An even more basic principle is that plaintiff can recover only compensation for losses. McCormick, Damages § 81 (1935). Thus the plaintiff should recover no more than the amount necessary to place him in the same position that he would have been in, had there been no breach, unless, of course, he can show some other losses to be compensated. A possible exception even to the compensation principle is the notion that one who breaches may be deprived of his enrichment even though plaintiff's losses of any kind are less than defendant's enrichment. See Dawson, supra, especially 185-89.

[9] Fuller & Perdue, supra note 8, at 54.

[10] As the rate schedule implies, a demand charge is a charge determined by the maximum rate of delivery of energy to which the customer is entitled during a specified period. It is designed to reimburse the utility for its demand costs, "those which are imposed upon the utility by the capacity—in terms of plant, equipment, and personnel —which it must hold in readiness to serve its customers." Barnes, The Economics of Public Utility Regulation 325 (1942).

[11] Energy charges are determined by the total amount of energy used by the customer. They are designed to reimburse the utility for its output costs, "those which are a function of the volume of production and sale. These are the costs which relate to the utilization of the existing capacity rather than to the amount of the capacity itself." Barnes, op. cit. supra note 10, at 331. A third type of cost, customer costs (". . . those which can be directly assigned to the individual customer." Barnes, ibid.) need not concern us here.

[12] There were other charges which are not pertinent to the issues here. There also was an adjustment for variations in the cost of coal, the effect of which was not brought into the case by testimony at trial, and which can therefore be ignored.

and energy." Ford would have had the right under the contract to use as much energy as it wished so long as its demand never exceeded 5300 KW.[13] Moreover, if the demand charge and energy charge for the month did not exceed the minimum bill, Ford would have to pay no more than $7,314. For example, during each of the months from May through December of 1958 Ford paid only the minimum bill, although it used from 90,000 to 540,000 KWH of energy. Thus in those months its energy charge ranged from $284.63 to $1,707.75. It is not possible to tell from the record exactly how much the demand charge was in those months. But it could not have been over $5,607.25[14] in the month in which the energy charge was $1,706.75. Nor could it have exceeded $6,095[15] in any of the months since in none of those months did Ford have a demand in excess of its contract demand.

Ford's breach and consequent relief of Memphis from its obligation to perform thus saved Memphis considerable expense in fuel costs alone. Even though the District Court found that Memphis was ready, able and willing to carry out its obligations to supply electrical power as specified in the contract, this does not alter the fact that Memphis did not have to spend money for coal, etc.; a necessity if Ford was using energy. Therefore, in order to put Memphis *only* in the same position that performance would have done, this saving should have been deducted from its recovery. This, however, was not argued on appeal, and thus the Court of Appeals could only have considered the point on its own.

Even apart from proper judicial reluctance to consider unargued questions, it would have been difficult on the record for the court to apply the "savings of expense" doctrine (or for counsel to argue it). While plaintiff would hardly complain if the court considered all the unpaid *demand charge* to represent a loss, it might properly complain if, on the record before it, the court had held that Ford's breach saved Memphis the full amount of the *energy charge* (which charge, as we have seen, is generally predicated on the actual output costs). There was nothing in the record to show that there were no fixed costs covered by the energy charges.[16] Nor was there any indication that

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13 Memphis had no obligation to supply electricity at a rate in excess of the contract demand of 5300 KW. Of course, if such a demand were made, Memphis would naturally meet it if it had the energy readily available, which was probably generally the case. In fact in two months, April 1957 and April 1958, Ford did have loads in excess of 5300 KW.

14 The record, Appellant's Appendix, 36a, is not altogether clear on this point. It shows a demand during each of the months from May through December 1958 of 5300 KW. But this must mean the contract limit on demand rather than Ford's actual demand, since in May the energy charge plus a demand charge for 5300 KW would have exceeded the $7,314 which Ford was billed. Therefore, $7,314 less $1,706.75, the stated energy charge, equals $5,607.25, the maximum demand charge for this particular month.

15 [5300 KW (contract demand) × $1.00 per KW] 115% = $6,095.

16 One of plaintiff's witnesses testified that "the fixed charges are considerably above

there was no profit element in the energy charge to which Memphis would be entitled. Certainly then the court is not to be criticized for failure to examine this contention, but, on the other hand, the case should not be used as authority in similar cases where the utility's savings due to the breach are shown.

In the present case, if the energy charges had been shown not to include any fixed costs, Ford could have argued savings to Memphis on the following basis: Ford was entitled under the contract to use electricity any way it wished (except for resale). It could have set up a unit using electricity at a constant rate of about 2136 KW. This would have caused energy usage of about 1,538,000 KWH per month. The demand charge would have been about $2,556 per month, and the energy charge about $4,758 per month. This argument carries the "saving of expense" notion to an extreme. The court could, however, in a case with the facts properly established, stop short of such an extreme position. It could deduct the saving of energy costs which would result from Ford's using no energy rather than its using an amount at a peak demand more reasonably anticipated at the time of the contract. If the court accepted the argument in principle, and if in fact none of the energy charges represented fixed costs or profits, Ford would have been entitled to deduct at least $1,219 from the minimum monthly bills of $7,314, since the parties contemplated that the peak demand would not exceed 5300 KW and hence that the demand charge would not exceed $6,095 per month.

One caveat should perhaps be added since the contract in *Memphis* provided for a minimum charge designed to cover more than fixed costs. Where, however, the minimum bill is $X per KW of demand and all energy consumed is to be paid for in addition to the minimum bill, the utility should not suffer the reduction on breach which is suggested here. At least, it should not suffer such reduction in the absence of a clear showing by defendant that its breach saved the utility some expense.

Present valuation. The second failure (again ignoring the acceleration clause) to put plaintiff only in the position it would have been in if the contract had been performed involves the fact that Memphis would have received payment of its minimum bills *only* in installments, and not in a lump sum, as it demanded in this case.[17] The Court of Appeals disposed of this problem in the following short paragraph:

production charges. In our case, they are almost double." Appellant's Appendix, 60a. This probably referred to system wide costs, and is not very informative on the point involved here. Fixed costs are often covered in energy charges to many domestic users of electricity who pay on the basis of the number of KWH used without a separate demand charge.

[17] Ford did not make the "present value" argument on appeal in the manner referred to. It did, however, raise the point in its argument on acceleration under the agreed damage clause.

> Under the doctrine of anticipatory breach, upon the default of Ford, this total amount became due prior to the filing of the suit; and the district court was not in error in holding that the City of Memphis was entitled to recover all amounts due for minimum bills for the remainder of the contract term.[18]

This conclusion of the court confuses the right of a party to sue immediately for all that is or will be due him upon an anticipatory breach, with the valuation of that right. In short, if the purpose of the court is to put the plaintiff in the position he would have been in if the contract had been performed, the court cannot ignore the fact that money paid today is worth more than money paid a year from now. If the court gives the plaintiff more than the *present* value of the payments due in the future, it is placing plaintiff in a better position than he would have found himself had the contract been performed. There is abundant authority for requiring the *present* valuing of plaintiff's recovery in cases such as this one.[19] While it is unfortunate that the Court of Appeals leaves to posterity the language quoted above, the result in the case belies the language. The decision does not in fact allow Memphis to recover even the full amount of the unpaid installments effective as of the time of the breach. The District Court had allowed interest only since the filing of the complaint on August 19, 1960, $10,296.83.[20] Had an effort been made to transmute the payments into their present value at the time of judgment[21] the net

18 304 F.2d at 853.

19 4 Corbin, Contracts §§ 965-66 (1951); McCormick, Damages § 144 (1935).

20 This limited allowance is probably not in accordance with Tennessee practice. In Brady v. Oliver, 125 Tenn. 595, 147 S.W. 1135 (1911), the court refused to allow interest in an action for breach of contract from the date of breach, and instead allowed it from the time of the bill. But the damages were not liquidated. In such a case the Tennessee Court of Appeals has allowed interest from the date performance was due, City of Lawrenceburg v. Maryland Casualty Co., 16 Tenn. App. 238, 64 S.W.2d 69 (1933). Even if it were held that demand was required to start interest running, as was held in a case on an implied in law contract, Robertsen v. Inglewood, 174 Tenn. 92, 123 S.W.2d 1090 (1939), Memphis did make such demand in February 1959. Of course, the argument in the text accompanying note 10 et. seq., supra, if accepted would make the claim of Memphis unliquidated. But the way both the District Court and the Court of Appeals handled the case the claim was a liquidated one. Until judgment, interest would be determined in accordance with Tennessee law in this diversity of citizenship case. Massachusetts Benevolent Ass'n v. Miles, 137 U.S. 689 (1891), cited with approval in Klaxon Co. v. Stentor Elec. Mfg. Co., 313 U.S. 487, 497 (1941); Hobart v. O'Brien, 243 F.2d 735 (1st Cir. 1957); Midstates Oil Corp. v. Waller, 207 F.2d 127 (5th Cir. 1953); New Amsterdam Cas. Co. v. Soileau, 167 F.2d 767 (5th Cir. 1948); see T. & M. Trans. Co. v. S. W. Shattuck Chem. Co., 158 F.2d 909 (10th Cir. 1947).

21 Since the judgment starts drawing interest immediately, 62 Stat. 957 (1948), 28 U.S.C. § 1961 (1958), the judgment is the time at which the present valuation should take place. 4 Corbin, Contracts § 965 (1951). It is, however, perfectly consistent with the purpose of putting plaintiff in the same position as performance to use some earlier time, provided further interest on the amount then calculated is allowed from that time

increase would have been $11,707.27.[22] The record thus shows that the language above was in effect a somewhat ambiguous dictum inconsistent with the actual results of the case.

Acceleration clause. The opinion of the Court of Appeals does not contain the acceleration clause[23] which Ford attacked as constituting a penalty. Thus it appears that the clause attacked as a penalty is the minimum bill provision. This greatly eased the court's route to the result it reached since it could easily justify the minimum bill provision as being a proper liquidation of damages. Also it is much easier to ignore the problems of present valuation and of savings of expenses by breach, discussed above, if one firmly fixes in one's mind that the minimum bill provision is designed for the post-breach situation. The only trouble with this is that it totally ignores the facts of the case. The minimum bill provision was a part of the operating relationship of the parties,[24] looking not toward breach, but toward performance.[25]

If the same rate and method of calculation are used throughout, the result will be the same save for the effect of compounding.

[22] The legal rate of interest in Tennessee is 6%, Tenn. Code Ann. § 47-1604 (1956). Applying that legal rate and adding it to installments overdue at the time of judgment (April 26, 1961, approximately 26½ months after the first unpaid installment was due) and subtracting it from installments not yet due at the time of judgment, Memphis was entitled to a judgment of $252,576.78 plus a net increase due to interest of $11,707.27. These calculations were made by simple interest. While compounding would be more accurate, there is relatively little difference over the time involved. And, of course, compounding always raises serious legal questions. McCormick, Damages § 53 (1935). The figures, of course, show the wisdom of Ford's not directly raising this point in its appeal.

Professor McCormick suggests that the legal rate is inappropriate for these purposes, and that computation should be "on the basis of the net yield, duly compounded, of investments available to plaintiff at a minimum of risk." Id. § 144 (1935). His suggestion is an excellent one, but involves certain legal difficulties which are illustrated by the *Memphis* case. Under Tenn. Code Ann. § 47-1608 (1956) Memphis was entitled to interest at the legal rate on the overdue installments. If it is also permitted under Professor McCormick's view to discount future installments at an effective lower rate of interest, Memphis gets the best of two worlds. This problem is not insuperable. A court could perhaps dodge the interest statute as to the overdue installments by holding that, since plaintiff was bringing a suit for breach of the whole contract, not for installments due, the question is one of damages to which the interest statute is inapplicable. See also Note, Present Worth of Future Damages, 5 So. Cal. L. Rev. 330 (1932). Both the question of the rate of interest and of compounding illustrate the failure of the law to be very sophisticated about the value of the use of money (or other property) during a period of time. See, e.g., Comment, Interest as Damages in California, 5 U.C.L.A.L. Rev. 262 (1958); and see generally, McCormick, Damages §§ 50-59 (1935). See also Gregorius v. Safeway Steel Scaffolds Co., 31 U.S.L. Week 2369 (Pa. 1963); Note, Prejudgment Interest as Damages: New Application of an Old Theory, 15 Stan. L. Rev. 107 (1962).

[23] See text between notes 4 & 5, supra.

[24] It is interesting to note at this point that Memphis did not attempt to use in the case the following provision in the contract:

> The above rates and all charges are net, the gross rate being 10% higher. In the event the current monthly bill is not paid on or before delinquent date shown on the bill, the gross rate shall apply.

This was a sensible bit of advocacy since the court might very well have held this a penalty, and its whole outlook in the case might have been colored.

[25] Of course, any clause establishing the operating relationship may be of moment

The clause Ford alleged to be a penalty was the acceleration clause.[26]

It is difficult to uphold the acceleration clause as a liquidated damage clause on the basis that it liquidated Memphis' expectation. Memphis' maximum legally enforceable expectation under the contract was the receipt of the minimum charges at the proper time each month. In the absence of the suggested justification below, to permit it to accelerate such payments without reduction to present value would be to allow it to impose a penalty for two reasons. First, the harm from breach was very certain.[27] Second, the amount of damages fixed is unreasonably large in relation to either the expected or actual harm which would flow from the breach. As pointed out previously, in an action for damages for an anticipatory breach the amounts due the plaintiff are to be reduced to their present value. An acceleration clause which ignores the interest factor thus fixes unreasonably large damages and hence is a penalty.[28]

It can, however, be argued that Memphis has suffered an expectation loss in addition to the present value of the $7,314 due it each month under the contract. Expectation has been used thus far to refer to the amount to which Memphis was entitled by law under the contract. But parties often enter contracts with expectations beyond the bare minimum of the other party's promises. That was certainly true of the contract in this case, where Memphis doubtlessly hoped to,[29] and in fact did, sell much more energy to Ford than that covered by the minimum bills. Prior to the 1956 agreement, Ford's monthly bills had been substantially in excess of $7,314 for many years, and continued in the $9,000 and $10,000 range until the Spring of 1958 when Ford began serious cutbacks at the plant. By Ford's breach Memphis lost the hope of such sales. While Memphis could not in the absence of a liquidated damage clause have recovered damages for the demise of such hopes, there seems to be no reason why the parties could not bring those hopes within the scope of contract

in defining plaintiff's rights upon defendant's breach. This fact is built into the formula which allows plaintiff to recover the monetary equivalent of performance.

26 Ford also argued that the interpretation put on the agreement by the District Court led to harsh and unreasonable results and hence was an improper interpretation. But this was separate from its argument concerning the acceleration clause.

27 The certainty requirement has been criticized in McCormick, Damages § 148 (1935).

28 See 5 Corbin, Contracts §§ 1065, 1072 (1951). Ford also argued that the clause was a penalty since it applied to "any breach or default" and hence violated the "other breaches" rule, i.e., since it applied to some breaches as to which it would be a penalty, it was a penalty in all circumstances. For criticism of this rule, see id. § 1066 (1951) and McCormick, Damages § 151 (1935).

29 Both the President of the Division, Appellant's Appendix 58a, and a witness from TVA, Appellee's Appendix 10b-12b, indicated that the minimum charges shifted only some of the risks of non-use of capacity to the customer.

protection through a reasonable liquidated damage provision.[30] Just such a provision existed here since the amount of gain to Memphis through the application of the acceleration clause was not unreasonably large in relation to the loss of the unpromised but hoped for gains.

It might further be argued that the clause was valid as a reasonable liquidation of the investment and construction costs which Memphis expected to incur in reliance on the contract.[31] The President of the Division testified that the annual fixed charges for the generating and transmission capacity necessary to meet Ford's demand of 5300 KW were $140,000.[32] Such an argument is not too far afield

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30 Support for this argument is found in legions of cases which have allowed a reasonable liquidation of damages where, for reasons of difficulty of proof, no legal protection of the expectancy in the form of damages would otherwise be available, e.g., covenants not to compete in business. See 5 Corbin, Contracts § 1071 (1951). If we take Holmes' "bad man" approach those cases in the eyes of the law involve exactly the same issue as the hoped for but unpromised expectation, since the law will effectuate neither (at least in those cases where specific performance is unavailable).

31 The District Court made the following finding of fact, Appellant's Appendix, 92a:

> In determining the size of the generating station and the related financial requirements, the Division gave specific consideration to the contracted power requirements of each of its major industrial customers, including Ford, which was one of the nine largest customers on plaintiff's system. It is impossible to determine whether plaintiff would have been able to reduce the size of the generating plant and the corresponding investment had it known that Ford would abandon its operations in Memphis, but Ford's load was sufficiently large so that it could have affected the size of the generating units and the amount of investment required therefor.

32 Appellant's Appendix, 49a-50a. This rather astounding testimony apparently went unchallenged on cross-examination. It was evidently accepted by the District Court in its findings of fact, Appellant's Appendix, 92a. For the purpose of commenting on the legal rules emanating from the case, therefore, the figures must, of course, be accepted as accurate. Nevertheless, the fact that at no time had the total charges for both demand and energy paid by Ford ever reached $140,000 per year causes one to question the testimony. The figure was reached by the following route: the transmission and generating capacity cost Memphis about $200 per KW. To meet a demand of 5300 KW it is necessary to have about 7000 KW generating capacity, the difference being for necessary reserves and for capacity for use of energy by the utility itself. The annual fixed charges run about ten per cent. Thus $200 × 7000 KW × 10% = $140,000.

Such testimony introduces a brand new method of electric rate fixing which should bring delight to all utilities. In computing a unit fixed cost per KW to be charged each customer the utility divides the total customer fixed costs (which under this method are based on contract demands) by the actual capacity. This unit cost would then be charged each customer for each KW of his contract demand. But since the utility knows that it will not have to meet all the contract demands of its customers at the same time, it builds a good deal less capacity than the total of those contract demands. With unit fixed cost being predicated on contract demand, the effect of the utility operating at less than total contract demand results in a reimbursement for costs which the utility is not incurring. It would be amusing to see the cross-examination if a witness made this suggestion in a rate proceeding before a regulatory agency.

The testimony, however, might possibly have been justified by the Peak Responsibility method of allocating total system demand costs among customers. Under this method, however, it was proper to attribute the whole 7000 KW to Ford only if Ford's demand for 5300 KW came or was expected to come at the time the Division was subject to peak demand of all customers. Otherwise Ford's share of total system demand costs from what the Court of Appeals seems to be doing with the minimum bill provision (not the acceleration clause, which the court ignores) when referring to Memphis' change of position in reliance on the contract:

> The large expenditures aggregating more than $163,000,000 incurred by the City in order to supply the contractual requirements of Ford, and other users of electric power, make the damages in this case uncertain in amount and difficult of ascertainment. Ford is not being penalized by being held liable for the payments it agreed to make, even though it does not take the electricity, which it agreed to purchase. The large sums of money, representing the accumulated minimum monthly bills for which Ford was indebted, according to the holding of the court, are attributable to the great amount of money invested by the City of Memphis in planning and building for Ford's needs, and in reliance upon Ford's agreement to purchase electricity at the specified rate over a five year period.[33]

The question then is, can the parties provide that the reliance interest will be more fully protected after a breach than it would be by performance? At first blush the answer would seem to be "yes." After all, the reliance interest is one of the key interests to be protected by the law of contract. Nor can the argument be refuted by merely noting that, absent the clause, reliance damages could not be recovered without reduction by the loss which the plaintiff would have had if there had been performance.[34] It is precisely here, where the law gives inadequate protection to appropriate contract interests, that agreed damage clauses are enforced.[35] But first impressions are some-

was only the percentage of those costs which Ford contributed to the system wide peak. Thus, if the total system peak was, say 600,000 KW, and Ford's demand at that time was 3000 KW, its share of demand costs would be 5% of the total demand costs of the system. Using the President's figure, annual total system demand costs were $1,500,000 to $1,600,000, and Ford's share in the hypothetical situation under the Peak Responsibility method would have been $75,000 to $80,000 annually. The Peak Responsibility method and other more sophisticated and widely used methods are described in Barnes, The Economics of Public Utility Regulation 327-31 (1942) and Caywood, Electric Utility Rate Economics 156-72 (1956).

[33] 304 F.2d at 853.

[34] L. Albert & Son v. Armstrong Rubber Co., 178 F.2d 182 (2d Cir. 1949); Gruber v. S-M News Co., 126 F. Supp. 442 (S.D.N.Y. 1954); Stolper Steel Prod. Co. v. Behrens Mfg. Co., 10 Wis. 2d 478, 103 N.W.2d 683 (1960); see Security Stove & Mfg. Co. v. American Ry. Express Co., 227 Mo. App. 175, 51 S.W.2d 572 (1932); Restatement, Contracts § 333(d) (1932); Fuller & Perdue, supra note 8, at 75; 5 Corbin, Contracts § 1033 (1951); McCormick, Damages § 142 (1935).

The rule permitting recovery of expenditures made in reliance on the contract is recognized in Tennessee. Brady v. Oliver, 125 Tenn. 595, 147 S.W. 1135 (1911); Allen v. Elliott Reynolds Motor Co., 33 Tenn. App. 179, 230 S.W.2d 418 (1950).

[35] Macneil, Power of Contract and Agreed Remedies, 47 Cornell L.Q. 495, 501-03 (1962).

times wrong. Any simple affirmative or negative answer should be hedged with caution, since one cannot foresee the circumstances in which the question may be raised.[36] Certainly, in a great many cases the argument should be rejected in sheer disbelief of the alleged facts. For example, if a seller delivers 100 widgets to a buyer, the price promised being $10,000, an agreed damage clause of $12,000 should not be upheld as a reasonable liquidation of his uncertain reliance loss in delivering the widgets,[37] even though $12,000 might otherwise be upheld as a reasonable valuation of the widgets.[38] The *Memphis* case itself is perhaps just such a situation. One cannot compare the annual minimum bills of $87,768 (the annual demand charge was even less) with the testimony that annual fixed costs were $140,000 without wondering why a utility would enter such a disastrously losing contract. One may be forgiven for simply refusing to believe that it did. Acceptance of plaintiff's argument in such a case would tend to cut down flexibility and cooperation in contract relations, since it would pay the beneficiaries of such clauses to be as rigid as possible in their demands in the hope that the other party would breach.[39] Moreover, it is difficult to see how refusal to uphold the plaintiff's argument in the foregoing hypothetical situation would inhibit reliance on contracts in the future. Since the beneficiary of the clause is willing to rely on the performance, which is definite in amount, his only reliance on the clause would be on the gamble of non-performance. Where this element becomes substantial the contract becomes an alternative one and we are no longer concerned with an agreed remedy clause.[40] Thus more reflection suggests that clauses which do not meet the tests of reasonableness and uncertainty of damages as applied to expectation losses are not an appropriate protection of the reliance interest.

Where a party has a bona fide desire that his reliance losses in

[36] Traditional structuring of indices and digests does not make possible a thorough search for cases or other authorities which may have advanced this point without reading substantially everything written on liquidated damages. I have not undertaken this forbidding task. The research which has been done in preparation of this comment, and other work, has, however, revealed no such case or authority.

[37] This example illustrates that the same problem arises if the innocent party tries to justify an agreed damage clause on the ground that it is a reasonable liquidation of the amount of the breacher's unjust enrichment.

[38] Of course, the additional $2,000 might be upheld on other grounds, namely that the breach caused additional losses, such as court costs, attorneys fees, etc.

[39] A similar possibility flowing from a right to restitution of benefits in excess of the expectancy has not prevented the effectuation of such a right in the courts. See generally, Palmer, The Contract Price as a Limit on Restitution for Defendant's Breach, 20 Ohio St. L.J. 264 (1959). But the right to restitution in excess of the expectancy involves risks of valuation not likely to be present in the liquidated damage cases which are being considered here. Thus one party can not usually be sure that it would really benefit him if the other party breaches. This is especially true in view of the availability of the contract price as evidence of value for restitution. See Palmer, id. at 271.

[40] See 5 Corbin, Contracts § 1070 (1951).

event of breach be reimbursed through a liquidated damage clause, which could not be upheld by the traditional references to the legally enforceable expectation loss, it seems very likely that the legally enforceable expectation was not all that he hoped for under the contract. It has already been suggested that such hopes might properly be protected by a liquidated damage clause.[41] Certainly the occurrence of large reliance losses should reinforce any such claim.

[41] See text accompanying notes 29 & 30, supra.