



Business 231 Mid-Term Exam-AID Review Package

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Sample Question:

Jennifer has developed a new method for manufacturing cell phone cases. Her method allows the plastic to be molded to the shape of the desired phone and hardens permanently to the new shape within 5 seconds. This allows for her to make more cell phone cases faster and cheaper than her competitors. Jennifer hires Mark to be her sales manager.

Jencell is progressing slowly as a company. Jennifer works hard on improving her molding technique. She has two large cell phone manufacturers as regular clients for their phone cases and is just able to keep up with orders, manufacturing 10,000 cases per week (5,000 each). Mark thinks it is time to expand business so that they can see a better profit. Mark solicits five more cell phone companies and enters contracts with them to fill orders of 1,000 cases per week each (for 5,000 cases). He tells the factory staff to increase the speed of the process by half again.

For the first 2 weeks the machinery is able to pump out the 15,000 cases, but during the 3rd week after only 8,000 cases are made before the machines break down. Jennifer is called in to check the machines. She forwards 4,000 cases each to her first two clients and calls them to let them know that she will be delayed in delivering the remaining cases to them. She then repairs the machines and sets them to running again. The company then produces another 5,000 cases which are shipped out to Mark's clients.

During the 4th week, the machines break down again, but this time after only 4,000 cases are made. Jennifer has her staff ship 2,000 cases each to her two clients and once again advises them of the shortfall. She examines her machine and discovers that major parts have been burned out. She will need to get replacement pieces and that will take 4 weeks to be delivered.

Shortly thereafter, Jennifer's two clients both return the last shipment of cases and tell her that she is in breach of her contract. Likewise, she receives notice that the five other cell phone companies are likewise suing her for breach of contract.

- a. What is the type of breach of contract experienced by the two big cell companies and what are their legal rights? What remedies are available to them?
- b. What is the nature of the relationship between Jennifer and the other 5 cell phone companies, and what legal action is available to them?

ANSWERS

A:

The second breach is a major breach of the contract. It is a breach of a condition. A condition is an essential term of the contract. The number of cell phone cases to be delivered and the date they are due are both essential terms of the contract in this instance.

The type of breach is either an express repudiation or a failure of performance, or more particularly in this instance, grossly inadequate performance. As Jennifer called the cell phone companies to advise them that the delivery was short, she has expressly informed them of the breach. Repudiation can occur after performance has been rendered in situations where there is ongoing or continuous performance, as in this case. However, failure of performance can only occur at the time performance is due and in this case Jencell performed the contract, but failed to meet the required number of cases and therefore did not perform adequately.

The second occasion where only 2000 cases are sent is a major breach in the contract. The cell phone companies have the option to discharge the contract and not perform or to affirm the contract and continue to bind themselves to the contract, but sue for any damages arising from the breach. In order to make this decision, the cell phone companies would need to ask themselves if they believed that future performance by Jencell would also likely be defective and if the actual or expected future deficiency is important relative to the entire performance under the contract. If they are unsure, they should seek legal advice, particularly if there is a concern as to whether the breach is a major breach or a minor breach.

The fact that the cell phone companies have refused to accept the last shipment is an indication of their option to discharge the contract and free themselves from performance in order to contract with another cell phone case provider. They still retain the right to sue Jencell for damages.

They would be entitled to sue for damages, most particularly any expectation damages arising out of lost profits. They would also be able to sue for opportunity costs as by relying on their contract with Jencell, they were unable to enter a contract with another cell phone case provider. Further, they would be entitled to sue for consequential damages arising from any contracts they had entered into on reliance of this contract with Jencell, where they are now unable to fulfill those other obligations as a result of Jencell's breach. As long as the damages are reasonably foreseeable as flowing naturally from the breach, the cell phone companies would be able to recover these damages. The cell phone companies however, would be required to mitigate their losses by contracting with other parties in order to reduce the losses where it is possible and reasonable to do so. If they fail to mitigate their losses, Jencell may not be required to pay the full amount of the damages. Equitable remedies, particularly specific performance would not be available to the cell phone companies in this instance, as the cell phone cases would not be considered a unique item and in order to request specific

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performance, a chattel must be considered unique. Likewise, rescission would not be possible, because it would not be possible to return the parties to their precontractual positions.

NB. The first breach of the contract in only delivering 4000 of the required 5000 cases may be considered a minor breach of a condition. If it is considered a minor breach of an essential term, then Jencell has performed its part of the contract substantially and is entitled to expect performance on the part of the cell phone companies under the Doctrine of Substantial Performance. The cell phone companies would have to perform their end of the contract but would be entitled to a reduction in price due to damages arising from the breach.

B:

Jennifer, as the owner of Jencell, is also the employer of Mark. Mark was acting in the course of his employment when he entered the contracts with the 5 other cell phone companies and was performing vicariously. Under vicarious performance, a third party performs on behalf of the promisor who remains responsible for proper performance. Jennifer as the employer is also the promisor and would remain liable under the contracts with the 5 cell phone companies for proper performance. So, in spite of the fact that the 5 cell phone companies dealt with Mark, they have no privity of contract with him. Their contractual relationship is with Jennifer/Jencell.

In this case, the breach of contract is a breach of a condition of the contract, however it is the first breach for the 5 cell phone companies. The companies would have a choice of opting for discharge of the contract to free themselves from performance or they could affirm the contract continuing to bind themselves with a reduction in the payment due to the damages arising from the breach. They would have to consider whether future performance by Jencell would also likely be defective and if the actual or expected future deficiency is important relative to the entire performance under the contract. If the contracts are for a long duration and this was the only shipment that failed, they may choose the second option to maintain their ongoing relationship with Jencell. They would sue for expectation damages, opportunity costs and consequential damages arising from the breach. They too would be expected to mitigate their losses.