



UNC
SCHOOL OF LAW

NORTH CAROLINA JOURNAL OF
INTERNATIONAL LAW

Volume 8 | Number 1

Article 7

Winter 1982

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Recommended Citation

Laura S. Conrad, *Bernina Distributors, Inc. v. Bernina Sewing Machine Co.: New Grounds for Commercial Impracticability Based on Currency Exchange Rates under Uniform Commercial Code Section 2-615*, 8 N.C. J. INT'L L. 117 (1982).

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***Bernina Distributors, Inc. v. Bernina Sewing Machine Co.:* New Grounds for Commercial Impracticability Based on Currency Exchange Rates under Uniform Commercial Code Section 2-615**

In contracts involving two or more currencies, fluctuations in exchange rates may adversely affect the profitability of business transactions. Price terms which are based on the exchange rates prevailing when a contract is written may threaten ruin to one party if subsequent shifts in the exchange rate produce a divergence in nominal and effective prices. For example, if a domestic purchaser is required to pay a fixed price in the currency of a foreign seller and the relative value of the domestic currency declines, the purchaser will find it necessary to convert more of his assets into the foreign currency in order to obtain the goods. Although the nominal price remains the same, the purchaser's effective cost has increased, perhaps substantially. Consideration of potential exchange rate problems is a critical factor in contract negotiations because United States courts generally have refused to alter contract prices which have become financially oppressive to one party after a contract has been signed.

The holding in *Bernina Distributors, Inc. v. Bernina Sewing Machine Co.*¹ is illustrative of the restrictive approach utilized by the courts in applying the doctrine of commercial impracticability,² as formulated in section 2-615 of the Uniform Commercial Code.³ The *Bernina* decision was

¹ 646 F.2d 434 (10th Cir. 1981).

² See *Eastern Air Lines, Inc. v. Gulf Oil Corp.*, 415 F. Supp. 429 (S.D. Fla. 1975), and Huffmire, *Section 2-615 and Corporate Accountability*, 13 U.C.C.L.J. 256, 256 (1980). In the *Eastern Air Lines* case, the court commented that "recent American cases . . . strictly construe the doctrine of commercial impracticability." 415 F. Supp. at 438. The *Eastern Air Lines* court rejected a commercial impracticability defense on grounds that the seller had not incurred significant hardship and that the energy crisis of the early 1970's, and the ensuing adverse effect on the oil market, was foreseeable. The court reached this conclusion even though the implementation of a two-tier price control system for oil by the U.S. government, which was a major cause of the failure of the contract terms to reflect increased oil prices, was "completely without precedent in the history of government price control action." *Id.* at 434.

³ UTAH CODE ANN. § 70A-2-615 (1980), "Excuse by Failure of Presupposed Conditions":

Except so far as a seller may have assumed a greater obligation and subject to the preceding section on substituted performance:

(a) Delay in delivery or non-delivery in whole or in part by a seller who complies with paragraphs (b) and (c) is not a breach of his duty under a contract for sale if performance as agreed has been made impracticable by the occurrence of a con-

the first United States case in which the claim of commercial impracticability was based on increased costs caused by fluctuations in exchange rates. While the *Bernina* court rejected the impracticability defense, a growing willingness by the judiciary to broaden the commercial impracticability concept coupled with a more incisive presentation of the exchange rate problem⁴ may eventually result in the recognition of extreme exchange rate fluctuations as a viable ground for a section 2-615 argument.

Bernina involved a dispute between an importer of Swiss-manufactured sewing machines (defendant) and a retail distributor (plaintiff). The importer paid his supplier, the manufacturer, in Swiss francs.⁵ Under the terms of a seven-year contract executed in 1971, increases in the importer's invoice costs, which included changes in the exchange rate between Swiss francs and United States dollars, were passed on in the same amount to the distributor.⁶ In 1973, unusual fluctuations in the exchange rate had doubled the importer's effective costs, which prompted him to charge higher prices than permitted by the pricing formula contained in the contract.⁷ The distributor brought suit to enjoin the importer from charging the excessive prices. The importer claimed that his performance should be excused because his effective rate of return had been reduced by one-half.⁸

The difficulty encountered by the importer resulted from a contractual agreement to base prices upon a fixed profit system. As described in *Bernina*, the fixed profit device allowed no additional profit for cost increases to the importer, who was the middleman in the transaction.

tingency the non-occurrence of which was a basic assumption on which the contract was made or by compliance in good faith with any applicable foreign or domestic governmental regulation or order whether or not it later proves to be invalid.

(b) Where the causes mentioned in paragraph (a) affect only a part of the seller's capacity to perform, he must allocate production and deliveries among his customers but may at his option include regular customers not then under the contract as well as his own requirements for further manufacture. He may so allocate in any manner which is fair and reasonable.

(c) The seller must notify the buyer seasonably that there will be delay or non-delivery and, when allocation is required under paragraph (b), of the estimated quota thus made available for the buyer.

The Utah version of section 2-615 is identical to the Official Text—1978, of the Uniform Commercial Code adopted by The American Law Institute.

For discussions of the United Nations recent adoption of the draft of the proposed codification of international commercial law, see Lansing & Hauserman, *A Comparison of the Uniform Commercial Code to UNCITRAL's Convention on Contracts for the International Sale of Goods*, 6 N.C.J. INT'L L. & COM. REG. 63 (1980), and Note, *International Trade: Uniform Law of Sales*, 22 HARV. INT'L L.J. 473 (1981).

⁴ The exchange rate problem may be analogized to inflation in order to draw support from recent decisions involving section 2-615 and inflation. See, e.g., *Aluminum Co. of America v. Essex Group, Inc.*, 499 F. Supp. 53 (W.D. Pa. 1980).

⁵ 646 F.2d at 437.

⁶ *Id.* at 437-38.

⁷ *Id.*

⁸ *Id.*

Rather, cost variations passed through to the distributor, without any adjustment in the importer's gross profit margins.⁹ As a consequence, the nominal amount of gross profit per unit remained constant, but the actual rate of profit earnings was inversely related to cost increases or decreases. Therefore, once a price for a specified good was established, the importer, who had elected the fixed profit method, assumed the risk of a diminishing profit rate.¹⁰ Conversely, if the importer's cost decreased, the importer benefited from a higher profit rate.

The *Bernina* court noted that the distributor had urged the importer to utilize a cost-plus price formula to protect against the contingency of exchange rate vacillations.¹¹ Under the cost-plus method, the purchase price is derived "by providing for the payment of an amount equal to the costs of the seller or contractor to which is added a stated percentage as his profit."¹² Thus, cost-plus pricing provides for a target rate of return and eliminates risks due to changes in costs of the seller. However, the seller must forego the opportunity to receive higher profits which are afforded upon decreases in costs when using a fixed profit system.¹³

⁹ *Id.* at 439. See *infra* text accompanying note 13. The importer's profit per unit remained constant, however, the percentage of profit per unit cost gradually decreased due to movements in the exchange rates.

¹⁰ 646 F.2d at 440.

¹¹ *Id.* at 440, 442.

¹² A. KUMPH, BUSINESS LAW 7 of the glossary (9th ed. 1972).

¹³ The difference in the impact of the fixed profit and cost-plus formulas is compared in the following illustration. Assume that the initial exchange rate is \$1.00=1f., the initial cost to wholesaler is \$2.00, and the agreed rate of return is fifteen percent.

Cost-Plus	Fixed Profit
Then \$2.00 + 15% of \$2 = \$2.30 price -2.00 cost .30 profit + 2.00 cost Recheck .15 or 15%	\$2.00 + .30* = \$2.30 price -2.00 cost .30 profit + 2.00 cost .15 or 15%

*30¢ is the nominal money amount required to produce a fifteen percent rate of return on goods costing \$2.00 each at the time of contracting; therefore, initial price is established at \$2.30.

Suppose the exchange rate becomes unfavorable to wholesaler and changes to \$1.10 = 1f., representing a ten percent devaluation of the dollar, which increases costs by 20¢.

Then \$2.20 + 15% of \$2.20 = \$2.53 price -2.20 cost .33 profit + 2.20 cost Impact .15 or 15%	\$2.30 + .20 = \$2.50 price -2.20 cost .30 profit + 2.20 cost .136 or 14%
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Suppose the exchange rate becomes more unfavorable to wholesaler and changes to \$2.00 = 1f., a 100 percent devaluation of the dollar which increases costs by \$2.00.

Then \$4.00 + 15% of \$4.00 = \$4.60 price -4.00 cost .60 profit + 4.00 cost Impact .15 or 15%	\$2.30 + \$2.00 = \$4.30 price -4.00 cost .30 profit + 4.00 cost .075 or 8%
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The distributor refused to absorb the importer's higher costs which resulted from using the fixed profit method of pricing and brought suit to enforce the sales agreement. The Tenth Circuit affirmed the trial court's denial of the defense of impracticability.¹⁴ In its analysis of section 2-615 of the Uniform Commercial Code, the court focused on two factors; foreseeability and the extent of the hardship incurred.

In examining foreseeability, the Tenth Circuit discussed the assignment of the risk of loss between the parties. The court found that the contractual fixed gross profit provision implied that the importer had assumed the risk that the return on his capital investment might be reduced by devaluations of the dollar.¹⁵ In addition to objective evidence of the foreseeability factor, the court considered a letter written during the contract negotiations by the importer to the distributor in which the importer expressed concerns about a recent seven percent devaluation of the dollar in relation to the Swiss franc. The court found, relying heavily upon the letter, that the importer had actual foreknowledge of the instability of exchange rates.¹⁶ Based on the finding that exchange rate fluctu-

Suppose the exchange rate becomes favorable to wholesaler and changes to 80¢ = 1f., a twenty percent appreciation of the dollar which decreases costs by 40¢.

$\begin{array}{r} \text{Then } \$1.60 + 15\% \text{ of } \$1.60 = \\ \underline{-1.60} \text{ price} \\ \text{cost} \\ \text{.24 profit} \\ \underline{+ 1.60} \text{ cost} \\ \text{Impact} \end{array}$	$\begin{array}{r} \$2.30 - .40 = \\ \underline{-1.60} \text{ price} \\ \text{cost} \\ \text{.30 profit} \\ \underline{+ 1.60} \text{ cost} \\ \text{Impact} \end{array}$
.15 or 15%	.1875 or 19%

¹⁴ 646 F.2d at 444. The *Bernina* decision also dealt with the issues of open price term, Utah Code Ann. § 70A-2-305(1) (1980), and unconscionability, Utah Code Ann. § 70A-2-302 (1980). The court found that a method of determining the price was provided for in the contract, and therefore the court was not called upon to supply a reasonable price term. 646 F.2d at 439. The claim of unconscionability was also dismissed due to the absence of oppression in the contract terms under the circumstances existing at the time the contract was made and the lack of a significant imbalance in the relative bargaining strengths of the parties. *Id.* at 440.

In interpreting some of the collateral terms of the contract, the trial court heard parol evidence as to the parties' intentions at the time of contracting; however, the *Bernina* court found that the trial court did not rely on the extrinsic evidence and furthermore, that the parties' intentions had been put in issue by the importer. *Id.* at 441. The *Bernina* court, in construing the details of the contract, did find that the adjustment in price of new models introduced during the contract period was to be computed according to exchange rates prevailing at the time of introduction, and not as of the time of contracting. Otherwise, cost changes after introduction of a new model were not to affect the margins. *Id.* at 443.

Finally, the distributor was found not to be in breach of contract for failing to take delivery of sewing machines from the importer's warehouse within the requisite six-month period because the importer did not give the distributor proper notice and an opportunity to withdraw the machines. Accordingly, the distributor was not liable to the importer for interest on the unclaimed machines. *Id.* at 444.

¹⁵ *Id.* at 439. Risk may be expressly or tacitly assigned; a finding of actual risk allocation presupposes foreseeability of the risk. *Robberson Steel, Inc. v. J.D. Abrams, Inc.*, 582 S.W.2d 558, 562 (Tex. Civ. App. 1979). Furthermore, the promisor, seller, is presumed to bear the loss of any foreseeable risk, unless there is evidence to the contrary, because the promisor is believed to be in a position to protect himself from risks which he should have been aware of at the time of contracting, by an express term in the agreement. *Eastern Air Lines, Inc. v. McDonnell Douglas Corp.*, 532 F.2d 957, 991-92 (5th Cir. 1976).

¹⁶ 646 F.2d at 439.

tuations were foreseeable, the court concluded that Comment 8 of section 2-615,¹⁷ as adopted by the controlling state law, supported the denial of relief to the importer.¹⁸

With regard to the hardship incurred by the importer, the *Bernina* court relied on Comment 4 of section 2-615 of the Uniform Commercial Code,¹⁹ in determining that "cost increases alone, though great in extent, do not render a contract impracticable."²⁰ Accordingly, the Tenth Circuit would not excuse performance under section 2-615 unless the party requesting relief could demonstrate that he could not perform under the contract without realizing a "severe and unreasonable" loss.²¹ Since the importer had not sustained a loss, but merely a lower rate of profit, the court refused to excuse the importer from performance under the contract terms.

The importance of risk allocation and foreseeability in applying section 2-615 became apparent in the earlier case of *Transatlantic Financing Corp. v. United States*.²² In *Transatlantic*, the Court of Appeals for the District of Columbia found that the risk of increased costs caused by the closing of the Suez Canal was assumed by the shipper. Facts indicating that the contract was silent as to such risks and that the canal closing itself was an unexpected contingency did not alter the assumption of risk.²³ The *Transatlantic* court did not find an allocation of the risk of shipping by way of the Cape of Good Hope, the alternate route, from the express or implied terms of the contract. However, the foreseeability of some nonspecific risk did have probative value in assigning the actual risk incurred. Thus, by defining foreseeability to include risks generally

¹⁷ U.C.C. § 2-615 (1978), Official Comment 8:

The provisions of this section are made subject to assumption of greater liability by agreement and such agreement is to be found not only in the expressed terms of the contract but in the circumstances surrounding the contracting, in trade usage and the like. Thus the exemptions of this section do not apply when the contingency in question is sufficiently foreshadowed at the time of contracting to be included among the business risks which are fairly to be regarded as part of the dickered terms, either consciously or as a matter of reasonable, commercial interpretation from the circumstances.

¹⁸ 646 F.2d at 439.

¹⁹ U.C.C. § 2-615 (1978), Official Comment 4:

Increased cost alone does not excuse performance unless the rise in cost is due to some unforeseen contingency which alters the essential nature of the performance. Neither is a rise or a collapse in the market in itself a justification, for that is exactly the type of business risk which business contracts made at fixed prices are intended to cover. But a severe shortage of raw materials or of supplies due to a contingency such as war, embargo, local crop failure, unforeseen shutdown of major sources of supply or the like, which either causes a marked increase in cost or altogether prevents the seller from securing supplies necessary to his performance, is within the contemplation of this section.

²⁰ 646 F.2d at 439.

²¹ *Id.* at 440 (citing *Gulf Oil Corp. v. F.P.C.*, 563 F.2d 588, 600 (3d Cir. 1977)).

²² 363 F.2d 312 (D.C. Cir. 1966).

²³ *Id.* at 315-19. The *Transatlantic* court, in its preliminary discussion of the issues, postulated that even the expectations of the parties as implied from the contract terms may not be controlling if the risk was foreseeable. *Id.* at 317.

related to the circumstances surrounding the contract negotiations, the court was able to find an assignment of the particular risk of the canal closure to the shipper. Furthermore, the court required a strict standard of proof in determining the degree of impracticability or hardship necessary to excuse performance in those cases in which risk had been allocated to the party asserting impracticability, either on the basis of the contract terms or foreseeability.²⁴ In *Transatlantic*, an increase in costs of \$43,972 above the contract price of \$305,843 was held insufficient to invoke relief because of the foreseeability of abnormal risks flowing from the turbulent political conditions prevailing in the Middle East at the time of contracting.²⁵

The broad definition of foreseeability invoked by the *Transatlantic* court, together with the utilization of foreseeability to assign risk, has made it a virtual certainty that risk will be assigned to the seller in actual practice.²⁶ In addition, whenever risk is allocated, a higher burden of proof is necessary to satisfy the hardship requirement. The stricter burden of proof raises the difficulty of establishing commercial impracticability to a level commensurate with the pre-Code impossibility standard.²⁷ As a consequence, the *Transatlantic* opinion has been criticized for injecting the common law doctrine of impossibility into section 2-615.²⁸ In addition, *Transatlantic's* analysis of foreseeability has met with disapproval because it merged the elements of "the parties' basic assumptions, impracticability, and the causal nexus between these two elements."²⁹ However, the manner in which section 2-615 is drafted does

²⁴ *Id.* at 319.

²⁵ *Id.*

²⁶ *See, e.g., Eastern Air Lines, Inc. v. McDonnell Douglas Corp.*, 532 F.2d 987, 991-92 (5th Cir. 1976).

²⁷ Black's Law Dictionary 680 (rev. 5th ed. 1979) offers this definition of impossibility:

As absolving party from liability for nonperformance, means not only strict impossibility, but impracticability because of extreme and unreasonable difficulty, expense, injury or loss involved. Total inability of party to perform for either subjective or objective reasons and under certain circumstances, though not all, such impossibility may be a defense.

²⁸ *See* Comment, *Contractual Flexibility in a Volatile Economy: Saving U.C.C. § 2-615 from the Common Law*, 72 NW. U.L. REV. 1032 (1978). The *Transatlantic* approach contravenes "the Code's express reason for adopting the test of commercial impracticability: that is 'in order to call attention to the commercial character of the criterion chosen by this Article.'" *Id.* at 1044 (quoting U.C.C. 2-615, Comment 3). The author proposes that foreseeability should be discarded altogether in determining the actual assumptions of the parties. *Id.* at 1038 n.35. *Cf.* Hurst, *Freedom of Contract in an Unstable Economy*, 54 N.C.L. REV. 545, 575 (1976) (calling for replacement of the impracticability standard with impossibility and establishment of a rebuttable presumption that the seller assumed the risk of the occurrence of all contingencies affecting performance).

See also, e.g., Florida Power & Light Co. v. Westinghouse Electric Corp., 517 F. Supp. 440, 450 (E.D. Va. 1981) ("Commercial impracticability under the UCC is basically a codification of the common law doctrine of impossibility of performance . . .") However, note the statement in the opinion that "Common law impossibility, formerly a very harsh doctrine which purported to require a showing of objective or scientific impossibility, has been moderated by case law to the point where it is equivalent to impracticability under the Code." *Id.* at 451.

²⁹ *See* Note, *U.C.C. § 2-615: Defining Impracticability Due to Increased Expense*, 32 U. FLA. L. REV. 516 (1980). The author concludes that "[i]f foreseeability and impracticability are corre-

not support the judicial practice of compounding the factors of impracticability and foreseeability.³⁰ Instead, the determination that performance is impractical appears independent of the inquiry into the basic assumptions of the parties at the time the contract was made. The comments to section 2-615 discuss foreseeability and allocation of risks in relation to the parties' basic assumptions; however, the text of the statute requires only that the impracticability be caused by a "contingency the non-occurrence of which was a basic assumption"³¹ of the contract. Thus, while consideration of foreseeability and risk allocation may be called for under the circumstances of a particular case, the use of these factors to increase the burden of proving hardship defeats the original purpose of section 2-615, which was to replace the doctrine of impossibility with a sensible commercial standard.³² It has been suggested that the body of case law following *Transatlantic* has excessively utilized foreseeability, producing holdings "as harsh as the most technical of the early absolute impossibility cases."³³

The *Bernina* court relied on *Iowa Electric Light & Power Co. v. Atlas Corp.*³⁴ in concluding that the importer had not sustained the burden of proof for a section 2-615 action. Interestingly, the opinion in *Iowa Electric* emphasized "the difference between commercial impracticability and physical impossibility in *Transatlantic*."³⁵ By listing the elements of section 2-615 separately,³⁶ the *Iowa Electric* court seemed prepared to analyze commercial impracticability under a less demanding standard than

lated [in judicial interpretation], increased costs may never constitute impracticability regardless of the essential nature of performance." *Id.* at 537.

And see, e.g., *Florida Power & Light Co.*, 517 F. Supp. at 451:

[C]ommercial impracticability raises four issues: (1) Was performance as agreed rendered impracticable? (2) Did the claimed impracticability arise from an unforeseen contingency? (3) Was the non-occurrence of the contingency a basic assumption on which the contract was made? (4) Did the parties, explicitly or implicitly, allocate the risk that the contingency would occur?

The court then says that these four questions are not elements of proof, and furthermore, that the issues are "interrelated: the 'answer' to each depends in part on the 'answers' to the other three." *Id.*

³⁰ See Note, *supra* note 29, at 537, and Comment, *supra* note 28, at 1038.

³¹ U.C.C. § 2-615(a) (1978), "Excuse by Failure of Presupposed Conditions."

³² See Comment, *supra* note 28, at 1044.

³³ Huffmire, *supra* note 2, at 259-60. The author contends that "[j]udicial resistance to the application of the principles of risk allocation which are central to excuse for nonperformance continues in the form of reluctance to give effect to the doctrine of commercial impracticability. . . ." *Id.*

For a discussion of risk distribution between parties and relational patterns in the context of the neoclassical micro-economic model, see Macneil, *Economic Analysis of Contractual Relations: Its Shortfalls and the Need for a 'Rich Classificatory Apparatus'*, 75 NW. U.L. REV. 1018 (1981).

³⁴ 467 F. Supp. 129 (N.D. Iowa 1978), *vacated*, 603 F.2d 1301 (8th Cir. 1979) (lack of personal jurisdiction).

³⁵ *Id.* at 134 n.7 (quoting *Transatlantic*, "The doctrine [of impracticability] ultimately represents the evershifting line, drawn by courts hopefully responsive to commercial practices and mores, at which the community's interest in having contracts enforced according to their terms is outweighed by the commercial senselessness of requiring performance." 363 F.2d at 315).

³⁶ 467 F. Supp. at 134: "(1) the seller must not have assumed the risk of some unknown contingency; (2) the nonoccurrence of the contingency must have been a basic assumption un-

the common law impossibility standard. However, the court adhered to the conventional approach of combining foreseeability, risk allocation, and hardship in holding that inflation and expenditures required by federal environmental and occupational safety regulations, which increased overall costs by fifty to fifty-eight percent, were foreseeable, and that therefore the risk should be borne by the seller.³⁷ Although the *Iowa Electric* decision denied any excuse on grounds of impracticability under section 2-615, it indicated that a change in policy toward application of the section might be appropriate:

The doctrine of impracticability has been narrowly construed [F]ew courts have excused performance on [the basis of excessive and unreasonable costs] alone

However the magnitude and impact of drastic cost increases in the modern commercial context may call for a liberalization of the way courts read § 2-615 where performance makes little commercial sense and there is adequate proof of actual costs brought about by the unforeseen contingency.³⁸

Comment 6 of the Uniform Commercial Code, section 2-615,³⁹ supports the *Iowa Electric* court's advancement of equitable principles in resolving impracticability cases. Alternatively, in situations of unforeseen difficulties which do not rise to the level of impracticability under section 2-615, the *Iowa Electric* opinion intimated that equitable adjustment may be available under section 2-209.⁴⁰

In an unusual departure from the characteristic judicial restraint regarding section 2-615, the court in *Aluminum Co. of America v. Essex Group, Inc.*⁴¹ permitted modification of a contract price term. The *ALCOA* court purportedly based its decision on prior case law; however, it was able to distinguish the factual situation at issue from those of past holdings which had denied relief.

derlying the contract; and (3) the occurrence of that contingency must have made performance commercially impracticable."

³⁷ *Id.* at 134-35, 140.

³⁸ *Id.* at 134 n.7.

³⁹ U.C.C. § 2-615 (1978), Comment 6:

In situations in which neither sense nor justice is served by either answer when the issue is posed in flat terms of "excuse" or "no excuse," adjustment under the various provisions of this Article is necessary, especially the sections on good faith, on insecurity and assurance and on the reading of all provisions in the light of their purposes, and the general policy of this Act to use equitable principles in furtherance of commercial standards and good faith.

⁴⁰ 467 F. Supp. at 135-36 (quoting U.C.C. § 2-209, Comment 2):

The test of "good faith" between merchants or as against merchants includes "observance of reasonable commercial standards of fair dealing in the trade" (Section 2-103), and may in some situations require an objectively demonstrable reason for seeking a modification. But such matters as a market shift which makes performance come to involve a loss may provide such a reason even though there is no such unforeseen difficulty as would make out a legal excuse from performance under Sections 2-615 and 2-616.

See also Huffmire, *supra* note 2, at 261-64 for a discussion of other courts' use of equitable principles to resolve impracticability cases.

⁴¹ 499 F. Supp. 53 (W.D. Pa. 1980).

In the *ALCOA* case, the contract price was calculated under an escalation clause linking ALCOA's non-labor production costs to the wholesale price index for industrial commodities. Historically, these two figures had moved congruently; however, subsequent acceleration in the general inflation rate caused a deviation between the figures which the *ALCOA* court determined to be so "extreme"⁴² that such a variation could not have been a basic assumption of the parties at the time of contracting. The *ALCOA* court found that there was a limit to the foreseeability of the inflation rate. Rates of inflation which exceeded this limit were "unforeseeable in a commercial sense," and the risk of such inflation was not expressly and could not be impliedly assigned to ALCOA.⁴³ Since the possibility that the escalation clause would fail to serve its function due to exceptional inflation rates was not a basic assumption of the parties, the *ALCOA* court turned to the question of the impracticability requirement under 2-615.

The court referred to *Transatlantic* in evaluating the extent of hardship that ALCOA would be subjected to under the contract. After comparing the approximate \$44,000 additional expense of Transatlantic with the \$60,000,000 projected loss of ALCOA, the court had no difficulty finding that ALCOA's claim constituted impracticability.⁴⁴

The *ALCOA* court also cited *Publicker Industries, Inc. v. Union Carbide Corp.*⁴⁵ for the proposition that a one hundred percent cost increase should be the minimum degree of hardship necessary under section 2-615.⁴⁶ The natural gas supply contract in *Publicker Industries* contained an escalation clause; however, the clause provided for price adjustments based on the previous year's average cost, with the maximum amount of increase specified for each year of the contract.⁴⁷ Due to actual price changes arising from the Middle East war in 1973, Union Carbide's cost of performance had doubled and it faced a potential loss of \$5,800,000,000.⁴⁸ However, the court in *Publicker Industries* did not find commercial impracticability and enforced the contract terms. The *ALCOA* court observed that the contract in *Publicker Industries* was executed after the sharp price increase which occurred in 1971, which supported the *Publicker Industries* finding that the seller had assumed the risk of inflation; however, the contract in *ALCOA* had been entered into prior to

⁴² *Id.* at 72.

⁴³ *Id.* at 76.

⁴⁴ *Id.* at 74-75.

⁴⁵ 17 U.C.C. Rep. Serv. 989 (E.D. Pa. 1975).

⁴⁶ 499 F. Supp. at 74.

⁴⁷ 17 U.C.C. Rep. Serv. at 990. In *Publicker Industries*, the contract price was to be adjusted by \$.004 per gallon for each \$.001 per pound increase or decrease from the base value in the average of the seller's cost for ethylene, the major cost element of ethanol, which was the subject of the contract. However, the increased price was not to exceed a specified price for any given year, as provided in a schedule contained in the contract.

⁴⁸ *Id.* at 992.

1971.⁴⁹

The *ALCOA* court stressed that its application of section 2-615 to the facts in dispute conformed to precedent; however, it is doubtful that other courts will adopt the novel construction of *Transatlantic* contained in the dictum of *ALCOA*.⁵⁰ Although the *ALCOA* court had found that the wide variation between the Wholesale Price Index-Industrial Commodities and *ALCOA*'s labor costs were unforeseeable, the court stated that "foreseeability . . . would not preclude relief under the doctrine of impracticability."⁵¹ The court relied on *Transatlantic* as support for rejecting the requirement that a risk be unforeseeable: "Foreseeability or even recognition of a risk does not necessarily prove its allocation."⁵² The *ALCOA* court, concluding that the *Transatlantic* position was "more in keeping with the spirit and purpose of the Uniform Commercial Code than . . . the strict approach," declared that contracts should not be enforced if it would be "commercially senseless and unjust" to do so.⁵³ Although *Transatlantic* does contain language which militates against assigning risk exclusively upon a finding of foreseeability, the *ALCOA* court's interpretation of *Transatlantic* is questionable because risk was allocated on the basis of foreseeability in *Transatlantic*. However, *ALCOA* illustrates the growing judicial awareness of the restrictive effect of foreseeability upon the application of section 2-615.

Some commentators⁵⁴ urge that the impracticability provisions of section 2-615 be given a more relaxed reading in order to allow contract modification in a wider range of circumstances. This was the approach of the *Iowa Electric*⁵⁵ and *ALCOA*⁵⁶ courts. The *Bernina* holding does not represent a reversal in this trend, even though the court upheld the contract in question, because the terms of the contract were not so impracticable as to be within the reach of section 2-615.

In future cases, an attorney may contend that the *Bernina* court recognized that exchange rate variations *may* make a contract commercially impractical. One problem with such an argument is obviously the foreseeability of the rate fluctuations. In *Bernina*, the foreseeability of possible exchange rate movements at the time of contracting was

⁴⁹ 499 F. Supp. at 74.

⁵⁰ See, e.g., *Eastern Air Lines, Inc. v. Gulf Oil Corp.*, 415 F. Supp. 429 (S.D. Fla. 1975). See also Note, *UCC § 2-615: Sharp Inflationary Increases in Cost as Excuse from Performance of Contract*, 50 NOTRE DAME LAW. 297, 305 n.77 (1974): "[T]he court in *Transatlantic* . . . clearly considered [foreseeability] a major factor in determining whether performance should be excused . . . in connection with the assumption of the risk issue . . ." *But see Asphalt Int'l, Inc. v. Enterprise Shipping Corp.*, 514 F. Supp. 1111, 1115 (S.D.N.Y. 1981). The court, in dictum, construed the disputed contract terms under the *Transatlantic* foreseeability requirement and found that risk was not assigned to the seller by the contract or by custom in the trade.

⁵¹ 499 F. Supp. at 76.

⁵² *Id.* (quoting *Transatlantic*, 363 F.2d at 318).

⁵³ *Id.* at 76.

⁵⁴ See *supra* notes 28, 29, 33.

⁵⁵ 467 F. Supp. 129 (N.D. Iowa 1978).

⁵⁶ 499 F. Supp. 53 (W.D. Pa. 1980).

substantiated by the evidence presented. Developments in the case law, however, suggest two ways to offset the damaging effect of such evidence under section 2-615: a policy approach and a direct attack on foreseeability as a question of fact.

The first approach should consist of general policy arguments for liberalization of the commercial impracticability doctrine, stressing the language of the statute and the explanatory official comments. Also, citation of recent cases which reflect a favorable attitude toward deemphasis of foreseeability requirements will add to the persuasiveness and evidentiary weight of the policy arguments.⁵⁷

The second approach to overcoming the difficulty of a section 2-615 defense should address the unforeseeability requirement established in prior case law. Borrowing the distinction regarding inflation made in *ALCOA*, it could be submitted that the "extreme"⁵⁸ variations in exchange rates beyond the normal or predicted range were not foreseeable. The reference by the *ALCOA* court to a case involving an exchange rate problem strengthens the analogy to inflation.⁵⁹ Once an outer limit to foreseeable exchange rate variations is ascertained, then extraordinary exchange rate fluctuations could be viewed as a "contingency the non-occurrence of which was a basic assumption on which the contract was made."⁶⁰ Therefore, the variations in exchange rates could serve as a basis for excuse.

In order to apply the proposed analysis to *Bernina*, examination of the historical context in which the importer and distributor transacted is necessary. During the severe inflation of the 1960's, the U.S. trade payments deficits and the gold shortage caused a fundamental disequilibrium between the actual worth of U.S. currency and the official par value under the two-tier gold price system.⁶¹ In an attempt to relieve the pressure on the dollar, the convertibility feature of U.S. dollars into gold was suspended in 1971,⁶² accompanied by a devaluation of the dollar. In 1972 fixed exchange rates were imposed; however, by 1973 the dollar was devalued again and a system of floating exchange rates was implemented⁶³ in which the relative "cost" of a national currency was determined by supply and demand, with management of sharp movements only by central banks through the International Monetary Fund.⁶⁴ The

⁵⁷ See *supra* note 41 and accompanying text.

⁵⁸ See 499 F. Supp. 72 and *supra* text accompanying note 42.

⁵⁹ 499 F. Supp. at 77 (citing *Anderson v. Equitable Life Assurance Society*, 134 L.T. 557, 42 T.L.R. 302 (1926)).

⁶⁰ U.C.C. § 2-615 (1978).

⁶¹ Under the two-tier system, central bankers traded a fixed amount of gold among themselves at the arbitrary price of \$35 an ounce. The significance of this action was that it created a private market for gold which was free to reflect world supply and demand and an official market for gold for the international monetary system which reduced the role of gold to a purely symbolic one. See J. CULBERTSON, *MONEY & BANKING* 409 (1972).

⁶² M. GILBERT, *QUEST FOR WORLD MONETARY ORDER* 122-23 (1980).

⁶³ *Id.* at 220, 223.

⁶⁴ E. MANSFIELD, *ECONOMICS—PRINCIPLES, PROBLEMS, DECISIONS* 638-40, 643 (1974).

"volatility" of exchange rates has been attributed to the general instability of the international economic environment during this period, particularly the oil crisis and OPEC capital flows.⁶⁵

Although not directly mentioned in the *Bernina* opinion, the impact of the transition to free floating exchange rates in 1973 was reflected in the importer's action of raising his prices above that allowable by the contract.⁶⁶ This circumstance is not only significant with respect to the *degree* of change in connection with risk assumption, but it is arguably a *qualitatively*⁶⁷ different risk which was only remotely foreseeable when the contract was executed in 1971. The "collapse"⁶⁸ of the fixed par value order and resort to a floating exchange rate system could not have been envisioned at the time of contracting in *Bernina*. However, the abandonment of the gold standard and depreciation of the dollar in 1971 may fairly be said to have foreshadowed the later changes in economic conditions. Finally, it would constitute a dramatic break with precedent to hold that an increase in costs, even a two hundred percent increase, was sufficient hardship to excuse performance in the absence of any financial loss.⁶⁹

In a future case involving excuse due to variations in the exchange rates, an attorney may use general policy arguments and the direct evidentiary approach to obtain a grant of relief under section 2-615. Signif-

⁶⁵ T. WILLET, FLOATING EXCHANGE RATES AND INTERNATIONAL MONETARY REFORM 32-35 (1977).

For the remainder of the 1970's, the United States experienced continued inflation and increased trade deficits which resulted in a steady decline of the dollar. A retreat from free floating exchange rates occurred in 1978, when the United States announced a policy of intervention that would not permit the dollar to depreciate indefinitely. M. GILBERT, *supra* note 62, at 208-09 and 223-25. Currently, a fixed but adjustable peg system of controlling exchange rates exists, which depends primarily on the United States and the European Monetary System to provide for stabilization. 140 P. KORTEWEG, EXCHANGE-RATE POLICY, MONETARY POLICY, AND REAL EXCHANGE-RATE VARIABILITY 13-17 (1980).

⁶⁶ See 646 F.2d at 437-38 and *supra* text accompanying note 7.

⁶⁷ See Note, *supra* note 29, at 537-38, in which the distinction between quantity of hardship and quality of risk is examined. For example, the normal presumption which flows from long-term contracts that allocation of the risk of inflationary cost increases is borne by the seller should be "irrelevant" when cost increases result from some other cause. The author points out, however, that the reasoning in *Maple Farms, Inc. v. City School District*, 76 Misc. 2d 1080, 352 N.Y.S.2d 784 (Sup. Ct. 1974), that allocation of risk from one contingency includes risks from other contingencies, indicates that judicial recognition of different kinds of risk will not aid the seller. Thus, "[i]n lieu of definitive analysis, courts are inclined to construct a sliding scale between the degree of variance constituting impracticability and the quality of risks conceivably assumed." See Note, *supra* note 29, at 538.

But see Florida Power & Light Co., 517 F. Supp. at 454-55 (rejection of the distinction of risk in kind, based on general foreseeability):

Because the future is by definition unknowable, a rule holding the obligor to performance only where he foresees, but fails to guard against, the *precise* event that renders performance more difficult, would be meaningless. It may be enough that he is (or should be) aware of a certain trend, or that a given state of affairs is in flux, or that an assumption is more than usually uncertain.

(Emphasis in original).

⁶⁸ O. EMMINGER, ON THE WAY TO A NEW INTERNATIONAL MONETARY ORDER 2-3 (1976).

⁶⁹ See 646 F.2d at 440 and *supra* text accompanying notes 21 and 44-46.

icant factors might include differences in the parties' economic acumen and in the information available to them at the time of negotiating. Differences in the particular occurrence which caused the impracticability, and differences in the degree of impracticability could overcome the unforeseeability requirement.

The finding by the *Bernina* court that neither the unforeseeability nor the hardship requirement for commercial impracticability was satisfied would appear justifiable even under the more lenient standards of evaluation. However, despite the lack of success which the excuse of exchange rate fluctuations met in *Bernina*, the theory itself was not discredited. Therefore, if the trend toward affording a wider latitude for impracticability continues, a different factual setting may receive a more favorable determination under section 2-615.

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