Chapter 21 #2: What is a complete contingent contract? Why don't we see any?

A complete contingent contract is a contract that contains provisions for all possible contingencies that might arise in the course of the contract's performance. It is a contract that is written by supernatural creatures that can foresee all possible occurrences in the future and regulate what rights the parties will have in case any of those come up. We don't observe such contracts because such creatures are not around. Instead we rely on the provisions of the law which are generic and comprehensive.

Chapter 21 #3: Define default rule.

This is the ruling that automatically takes place unless other regulation or court decision indicates otherwise.

Chapter 21 #4: In the United States, the default rule is that organs cannot be harvested from a dead body; in many states, the default rule can be overridden when you apply for a driver's license by signing a declaration that you will allow your organs to be donated in case of death. In Austria, the default rule is the opposite – unless you have signed a document stating the contrary, you are assumed to have consented to having your organs harvested. How do you think that these rules influence the number of organs harvested?

Since the default rule in Austria is unless otherwise provided your organs can be taken, we can expect that more organs will be taken there compared to the US where the default rule is the opposite. In a world of zero transaction costs it wouldn't make a difference. But since people may be lazy or don't take the time to think about it or just randomly fill out application forms, we can expect that the default rule of the US will not be overridden by private parties sufficiently.

Chapter 21 #6: In California, surrogate mother contracts are upheld. If the surrogate mother refuses to give up the baby, the law requires specific performance rather than having the surrogate mother pay damages to the people who contracted her. Why?

Because in that case only <u>one transfer</u> is involved and therefore specific performance is the optimal remedy. Damages hardly make up for the damage suffered due to the breach of contract.

Chapter 21 #8: In 1999 France passed legislation (since rescinded) requiring employers to reduce the workweek for their full-time employees by four hours – from 39 hours to 35 hours – but to

keep the total weekly pay per worker unchanged. The reasoning behind the legislation was that this would reduce unemployment. What do you think happened?

The market usually finds a way around this kind of measures. Usually, it might resort to part time employment or change the legal form of employment for their employees, e.g. from employees in the strict sense to hired private contractors etc. We would therefore expect unemployment to rise.

Chapter 21 #9: What is a relational contract? When and why would we expect to see contract terms to be relational rather than substantive?

A relational contract is a contract that specifies which side has the right to make a decision without specifying what the decision should be. For example, if the contract says that if it rains, the manager can decide if the business is going to stay open or not.

We would expect to see this kind of contracts in legal relationships that are long term and complex. An example is the articles of association of a corporation that provide for which body of the company has the right to make which decisions.

Unless otherwise provided in the law, a court would not enter into the relationship trying to second guess what the decision of the competent party should be.

Chapter 21 #10: Korean Steel Works promises to deliver steel springs for rabbit dolls to Los Angeles Rabbit Works on November 1. A wildcat strike takes place at the steel works and the springs cannot be delivered in time to the Rabbit Works. The rabbits cannot be made for the Christmas season and Rabbit Works loses $3 million in profits. In this situation, both sides can undertake precaution in case there is a wildcat strike (provide some examples). But only Korean Steel Works can reduce the probability of a strike. Who should be liable for these lost profits?

Contracts must be performed. We start from there. Non-performance with impunity should be a rare exception. In that case the factory did not deliver and could not possibly deliver due to the strike. The reason is a strike. The question is whether <u>consequential damages</u> are owed. The strike falls in the sphere of interests of the factory so it should bear the costs from it as it also earns the profits from its employees' work. However, if the strike is totally unforeseen, has never occurred before, is not the result of tough management etc., maybe the factory could claim the doctrine of frustration and ask for a readjustment or rescission of the contract.

<u>What would the parties have agreed in advance if they could have provided for such an occurrence</u>: probably they would have said that the factory is relieved and that it has to compensate the buyer for any difference in price since he now must purchase the goods from

another seller. This should be the decision of the court. If there is room for mitigation (by buying from another seller) it should be applied and the seller should be liable for the price difference, as we said before and not for the forgone profits (consequential damages).

Chapter 21 #11: A basketball player for the Los Angeles Lakers orders a size 24 basketball shoe for a game against the Miami Heat. When the shoes arrive, they are only a size 23 and too tight. As a result, the player underperforms and the Lakers lose. Should the shoe store be held liable for the loss of the game?

Consequential damages are an issue again here but there is no case for frustration. If the underperformance is due to the shoe size and also the defeat is due to the underperformance, then there is an issue for liability. Mitigation plays an important role here too. The player should not play, or should play barefoot etc. What would the parties have agreed in advance if they could have provided for such an occurrence: here there is no unforeseen event; just a breach of contract. It seems though that the seller wouldn't have agreed to such a liability in case of breach so he wouldn't have entered into the contract. It looks like the victim here can protect itself at a relatively low cost (order well in advance etc.) while the seller wouldn't know the extent of consequential damages he might be held liable for.

Chapter 21 #13: Westinghouse had a fixed-price contract to sell uranium to electrical utilities at $10 a pound. Westinghouse was a "middleman." It purchased uranium from producers and then sold it to the electrical utilities. In 1975, the price on world markets was $40 a pound. Only a small proportion of Westinghouse's obligations were covered by fixed-price contracts with uranium producers. It appears that Westinghouse had bet that the price of uranium would go down (which it did but not until 1982 when the price was $8 a pound). If Westinghouse honored the contracts, Westinghouse would have incurred over $2 billion in losses. It claimed it did not have to honor the contracts with the utilities because of commercial impracticability. Should Westinghouse have had its way? Postscript, the case was settled out of court with the utilities absorbing a lot of the cost.

It seems that the selling firm lost a bet and it should honor its promise. This is a classic example of hedging risk on the part of the buyers and they won the bet. The contract should be honored as there is double way speculation involved here.