

Part I: Answer any THREE questions from this part. Each is worth 10 points.

1. Discuss the efficiency consequences of the following legal rule: "For any contracts concluded after 1:00 a.m., January 1, 2001, the innocent party, in the event of a breach of contract, will be entitled to recover in money damages three times the benefit that she reasonably expected from the performance of the contract by the breaching party."
2. Explain why setting expectation damages at the level that leaves the promisee indifferent between performance and breach of a contract is economically efficient. Assume that the promisee has invested in the optimal level of reliance. How should this be factored into the calculation of perfect expectation damages? Why?
3. Compare and contrast the case for damages versus specific performance as an efficient remedy for breach of contract in the case of an unfortunate contingency. Under what conditions would you argue for specific performance in place of damages?
4. In what circumstances is mistake a valid (i.e., economically efficient) formation defense for breach of contract? In your answer, distinguish between productive facts and redistributive facts and explain why this approach to addressing the question of mistake is more fruitful than trying to determine whether mistake was mutual or unilateral

More questions on the back!

Part II: Answer BOTH questions from this part.

5. *Silicon Inc. is a manufacturer of computer microprocessor chips. Peachware Co. is a desktop computer manufacturer. On Monday, Peachware and Silicon enter a contract in which Silicon agrees to deliver 1000 chips to Peachware on Friday; Peachware agrees to pay Silicon \$200 per chip.*

Silicon's cost of manufacturing and delivering 1000 chips is \$150,000.

Peachware's cost of manufacturing 1000 computers is \$150,000. Of this amount, \$50,000 must be spent on Friday morning before the chips are delivered and which cannot be recovered if no chips arrive.

If no chips arrive on Friday, Peachware must wait until Monday to call around to alternative suppliers to purchase chips. The price of chips on this "spot" market is \$300 per chip.

The market price for the finished Peachware computers is \$900 per computer.

Now, assume that Peachware paid for the chips at the time the contract was signed. Just before delivering the chips to Peachware at noon on Friday, Silicon receives a frantic call from IBN, another computer manufacturer. IBN has discovered that the chips they purchased from another supplier are defective and they need 1000 chips to fulfill an order for new computers. IBN is willing to pay \$600 per chip, as they cannot wait till Monday to buy chips on the spot market.

- a) Calculate the profits that Silicon and Peachware earn if Silicon performs the contract and if Silicon breaches the contract. For this part of the question, do not include any damage awards in your calculations. Put your answers in the Blue Book in the form of the following (show your computations) [8 points]:

Perform:

Silicon's Profit =

Peachware's Profit =

Breach:

Silicon's Profit =

Peachware's Profit =

- b) Calculate the following damage awards based on the above information [6 points]:

- i) Expectation Damages
- ii) Reliance Damages
- iii) Opportunity Cost Damages

- c) Is breach efficient? Under what measures of damages will efficient breach be achieved? Explain. [6 points]

6. *In January 1997, Biggs entered into a contract with Franks, a builder, for the construction of a home. The contract price was set at \$350,000. Construction was scheduled to begin on August 1, 1997. In anticipation of his new home, which was to be located on 5 acres of land in the country, Biggs contracted with a pool company to install an in-ground Olympic-sized swimming pool. Because the pool was to be located approximately 50 yards from the house, construction on the pool was able to proceed prior to the starting date for construction of the house. However, in the spring of 1997, several natural disasters in other parts of the country caused extensive property damage, driving up the costs of building materials by almost 25 percent. Because this would have raised the cost of building the house to \$370,000, Franks breached the contract.*

- a) In this case is there a gap in the contract? If so, in your opinion was it efficient for the parties to leave the gap? What condition must be satisfied for this to be the case? [7 points]
- b) Considering economic efficiency, how should the court rule, i.e., should the court excuse Franks, impose legal relief (damages), or require specific performance? Why? [7 points]
- c) Finally, should Biggs' reliance be figured into the efficient resolution of this dispute? Why or why not? If so, to what extent? [7 points]