

Exam Number _____
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UNIVERSITY OF CALIFORNIA
HASTINGS COLLEGE OF THE LAW

FINAL EXAMINATION: CONTRACTS
(Course # 11044)

PROFESSOR WILLIAM S. DODGE

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SPRING SEMESTER 2003

TUESDAY, MAY 13, 2003

TIME: THREE HOURS

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LIMITED OPEN NOTES EXAMINATION

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INSTRUCTIONS

1. This is a limited open notes examination. You may bring with you and consult one 8½ by 11 sheet of notes (both sides) in print that can be read without magnification. You may not use or consult any other materials. If you use a sheet of notes, you must turn that sheet in, separately from the examination, before you leave the examination room. Please do not put your name or examination number on the sheet of notes.
2. The allotted time for the examination is three hours. There are three questions. Question one is worth 75 points, question two is worth 60 points, and question three is worth 45 points. I recommend that you spend one hour and 15 minutes on question one, one hour on question two, and 45 minutes on question three.
3. Read each question carefully, including the instructions at the end of the question. Within the limits of those instructions, discuss each issue reasonably raised by the facts, including issues that might be rendered moot by your resolution of another issue.
4. Think about and organize your answers before starting to write.
5. To the extent possible, write on every other line of the bluebooks and on only one side of the page. This will give you room to revise your answers if necessary.
6. Please write as neatly as you can.

Good luck and enjoy your summer!

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QUESTION ONE
(75 points)

Flyfuel, Inc., is a large, multinational corporation with its place of business in Chicago, Illinois. Flyfuel is in the business of distributing and selling jet fuel for commercial aircraft. Jet fuel is made from petroleum, and is manufactured almost exclusively by the major oil companies. Flyfuel is not itself a manufacturer of jet fuel (because it is not an oil company and so has no access to petroleum). Instead, Flyfuel purchases jet fuel from oil companies and then supplies the fuel to its customers, who are all commercial airlines, at specified airports throughout the world. Flyfuel purchases its jet fuel both on the open market and pursuant to long term contracts. In both cases, however, the price that Flyfuel must pay for jet fuel is directly linked to the world price for oil.

California Airlines, or "CalAir," is a regional airline which operates flights in and out of twelve airports, all located in the western United States. For many years, Flyfuel has had contracts with CalAir to provide CalAir with its jet fuel needs at all twelve of those airports. In the past three years, Flyfuel has supplied CalAir with an average of 12 million gallons of jet fuel each month pursuant to these contracts, though the actual amount of fuel supplied each month has varied by as much as 1 million gallons from that average.

Because the existing contract between Flyfuel and CalAir was due to expire on February 28, 2003, on February 1, 2003, CalAir and Flyfuel enter into a new, one-year, written contract, signed by both parties. That contract requires Flyfuel to supply to CalAir its requirements for jet fuel at the twelve airports at which CalAir operates for one year beginning on March 1, 2003. The contract further provides that CalAir shall pay a price of 50 cents per gallon of jet fuel throughout the term of the contract. (In setting this price, Flyfuel calculated that it could make a profit so long as the world price for oil remained below \$35 per barrel, which it had done quite consistently for the past several years).

On March 1, 2003 the parties began performing their new contract. At that time, the world price for oil was approximately \$25 per barrel. About two weeks later, however, in the middle of

(Question One Continues on Next Page)

QUESTION ONE: Continued

March, the United States launched a military invasion of Iraq. This event had two important effects for the parties:

First, domestic air travel in the United States declined by approximately twenty percent, and CalAir saw a similar fall in its passenger traffic. As a result, CalAir immediately canceled approximately ten percent of its flights in order to reduce its losses, and also reduced the amount of jet fuel it was purchasing from Flyfuel to 10 million gallons per month.

Second, the world price for oil jumped from approximately \$25 per barrel to approximately \$50 per barrel, where the price remained for the next several months because of the continuing political uncertainty in Iraq. As a consequence of this, Flyfuel's own cost for acquiring jet fuel immediately rose from 35 cents per gallon to 70 cents per gallon.

In response to these events, on March 24, 2003 Flyfuel sends a letter to CalAir, which CalAir receives on March 27, 2003. The letter reads as follows:

"Due to recent world events, effective April 1, 2003, we are forced to increase the price of jet fuel provided to CalAir pursuant to our contract of February 1, 2003 to \$1 per gallon. Given the recent rise in the market prices of petroleum and jet fuel, we simply cannot continue to provide jet fuel at a lower price than this. You will therefore be billed at this rate for all supplies made after April 1, 2003. Any failure to pay such bills promptly when due will be considered a breach of your obligations, and grounds for termination of our contract. Please sign and return this letter immediately to indicate your acceptance of this price change, or we will be forced to terminate our supplies of jet fuel effective April 1.

Sincerely,
Fiona Fickle,
Regional Manager for the West

(Question One Continues on Next Page)

QUESTION ONE: Continued

Flyfuel, Inc."

In response to this letter, on March 28 the President of CalAir, Cal Cool, telephones Fiona Fickle. Cal complains, "Fiona, this price change is outrageous. It is completely unjustified under our contract. Furthermore, given the difficulties the airline industry is facing because of 9/11 and the Iraq War, I just don't think our company can absorb these extra costs."

Fiona responds, "Sorry Cal, but there is nothing I can do. The people in the front office have informed us that we are not permitted to make any more sales of jet fuel for less than \$1 per gallon. They are concerned that Flyfuel itself might be driven into bankruptcy if it doesn't raise prices."

Cal concludes the conversation by saying, "I guess we have no choice then. I've already looked around and no one else can even supply us with jet fuel right now given the supply shortage, much less for 50 cents per gallon." After he hangs up the telephone Cal signs the letter from Flyfuel and mails it to Fiona.

During the month of April, Flyfuel supplies the 10 million gallons of jet fuel which CalAir orders, and CalAir pays for the jet fuel at the new price of \$1 per gallon. By the end of the month, however, it becomes clear to Cal Cool that CalAir cannot remain in business if something does not change. The combination of reduced air traffic and vastly increased fuel costs is imposing enormous losses on the company, so that it faces bankruptcy within a few weeks if current losses continue.

You are the General Counsel of CalAir. At the end of April President Cool comes to your office and explains all of the above circumstances. He also tells you that he has spent the past month searching for a new supplier of jet fuel, but with little luck. No other company is currently able to supply the 10 million gallons per month of jet fuel that CalAir needs. One of Flyfuel's competitors has offered to supply CalAir with its jet fuel needs beginning on July 1, two months from now, but only at a price of \$1 per gallon, which is the same price that CalAir is paying Flyfuel now.

President Cool has several questions for you. First, he wants to know if there are any grounds upon which Flyfuel might claim that

(Question One Continues on Next Page)

QUESTION ONE: Continued

the February 1 contract between Flyfuel and CalAir is no longer binding on the parties. Second, he wants to know if the price increase that he agreed to in late March is binding on CalAir. Third, he wants to know if CalAir can force Flyfuel to specifically perform its original contractual obligation to supply CalAir with its fuel requirements at a price of 50 cents per gallon. Finally, President Cool wants to know what other remedies, if any, CalAir might be entitled to because of Flyfuel's conduct.

Advise President Cool.

(End of Question One)

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QUESTION TWO
(60 points)

Walter Williams is a history professor, who lives in Oakland, California with his spouse and three small children. Walter's mother Maggie recently retired from her job as an elementary school teacher in Oregon. She wanted to see more of her grandchildren, but did not want to move permanently from her home in Oregon. Walter was able to get her to agree, however, to come and visit him and his family several times a year for a few weeks at a time. To accommodate his mother, Walter remodeled a basement room in his home and purchased a used car for her to drive during her visits, so that she would not feel completely dependent on him and his spouse to get around.

Walter had a car insurance policy with United Mutual Insurance Company, though he had never bothered to read its terms. After purchasing the car for his mother, Walter called his insurance agent, Ida Islington, and asked her to add the vehicle to his existing policy. Walter explained that the car would be used by his mother when she was visiting him. Ida said that would be no problem, and Walter gave her the necessary information about his mother's age and driving record. Ida added the new vehicle to Walter's policy and he began paying the additional premium.

Approximately one year later, on one of her trips to visit Walter and his family, Maggie was involved in a bad car accident. According to the police report, Maggie fell asleep at the wheel one evening and swerved into oncoming traffic, striking another car. Fortunately, no one was killed, but two people in the other vehicle were injured, one of them seriously enough to need continuing medical care. The day after the accident, Walter called Ida, his insurance agent, to report the accident. Ida told him not to worry and asked him to send her copies of any legal papers he received from the injured parties. Two weeks later, Walter received a complaint against his mother and himself from an attorney representing the parties injured in the accident seeking \$400,000 in tort damages. Walter forwarded copies of the complaint to Ida, along with a cover letter making a claim under his policy and requesting that United Mutual defend the tort suit.

Walter was understandably shocked when Ida called him a week later to tell him that United Mutual had taken the position that it

(Question Two Continues on Next Page)

QUESTION TWO: Continued

was not obligated to pay under the policy and would not defend the lawsuit against him and his mother. Ida directed his attention to a few provisions of his insurance policy. The first defined those family members covered by the policy as drivers:

``**Family member**' means a person related to the Insured by blood, marriage or adoption who is a resident of your household, including a ward or foster child."

Ida informed Walter that United Mutual had taken the position that his mother was not a "resident" of his household because she was just a temporary visitor and had no intention to remain permanently at his home. Ida confessed that she had thought Walter's mother would be covered and was surprised by United Mutual's interpretation. When Walter objected that Ida had told him adding his mother to the policy would not be a problem, she directed his attention to the policy's merger clause and said, "It's not up to me."

Ida then asked Walter to look at a second provision in the insurance policy that read as follows:

``Notice of Claim or Suit

Upon the Insured's becoming aware of any occurrence which would reasonably be expected to be the basis of a claim or suit covered hereby, written notice shall be given by or on behalf of the Insured to the Company or any of its authorized agents within seven days. If a claim is made or suit is brought against the Insured, the Insured shall immediately forward to the Company every demand, notice, summons or other process received by him or his representative. The Company shall have no obligation whatsoever to make payment on a claim or to defend a suit unless Insured has complied with this provision."

When Walter objected that he had called her the day after the accident, Ida reminded him that the policy said "written" notice and that he hadn't sent them anything in writing until two weeks after the accident. "The company's been hit with a lot of claims recently," she continued, "and they've started seizing on any little reason to deny a claim. I'm sorry, Walter."

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QUESTION TWO: Continued

At his own expense, Walter retained an attorney to defend the tort suit against his mother and himself. After incurring \$10,000 in attorneys fees, and on the advice of his attorney, Walter agreed to settle the suit for \$200,000. Walter then filed suit against his insurer, United Mutual, alleging that it was obligated under his policy to defend the tort suit against him and his mother and seeking to recover: the \$200,000 paid to settle that suit; \$10,000 in attorneys fees for that suit; \$25,000 in attorneys fees for his suit against United Mutual; \$50,000 in damages for emotional distress; and \$200,000 in punitive damages.

It is now the eve of the trial. Based on the facts before you, please analyze whether United Mutual was obligated to defend the tort suit against Walter and his mother, and which of the claimed damages, if any, Walter may be able to recover.

(End of Question Two)

(Question Three Begins on Next Page)

QUESTION THREE
(45 points)

Some commentators have proposed that specific performance be made the standard remedy for breach of contract, available against any defendant who has breached a contract. Please discuss:

1. How this proposal would alter current law; and
2. Whether or not you think that altering the law in this way would be a good idea.

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(End of Examination)

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