

The Importance of Complying with the Uniform Commercial Code's "Notice" Requirement When a Supplier Provides Defective Goods

by John J. Bursch

Introduction

In late 1993, Ford Motor Company notified American Bumper & Manufacturing Company that its bumpers were falling off Ford's trucks. American Bumper immediately notified its fastener supplier of the problem and, a short while later, canceled the supply contract. In 1995 American Bumper settled with Ford for payments and price reductions totaling nearly \$10 million. However, when American Bumper tried to sue the supplier for breach of warranty and indemnification, the lawsuit was dismissed because American Bumper had failed to give the supplier notice of breach as Section 2-607 of the Uniform Commercial Code (UCC) requires.

The notice requirement of UCC 2-607 is an often overlooked provision that rarely receives attention in published cases, but it can operate as a complete liability shield in cases involving alleged defective goods. The Michigan Court of Appeals recently reiterated UCC 2-607's importance when it affirmed the dismissal of American Bumper's nearly \$10 million lawsuit against its parts supplier.¹ This article provides an overview of the UCC 2-607 notice requirement. It then analyzes the Michigan Court of Appeals' decision in *American Bumper & Mfg Co.* The article concludes with practical tips for purchasers when dealing with notice situations.

Section 2-607'S Notice Requirement

Section 2-607(3)(a) of the Uniform Commercial Code states:

Where a tender has been accepted . . . the buyer must *within a reasonable time* after he discovers or should have discovered any breach *notify the seller of breach* or be barred from *any remedy*. . . .²

The italicized portions of the above text highlight three important points. First, a

buyer must give notice "within a reasonable time" after he or she discovers or should have discovered any breach. What is "reasonable" in a given case depends on the facts and circumstances. For example, if a buyer determines that a shipment of goods is defective and then destroys the goods before the seller has a chance to inspect them, any subsequent notice is likely to be deemed too late to be effective. The same is true if the buyer immediately buys replacement parts without giving the seller an opportunity to cure. The sooner a buyer gives notice, the more likely a court will conclude that the notice was given "within a reasonable time."

Second, the buyer must notify the seller "of breach," although it is unclear what kind of notice satisfies this requirement. The section does not say specifically what form this notice should take, and two different approaches have developed. The third sentence of Official Comment 4 to Section 2-607 states: "The content of the notification need merely be sufficient to let the seller know that the transaction is still troublesome and must be watched." Some courts have used this language to support application of a "lenient standard" of notice, i.e., notification that a transaction is merely "troublesome."³ Three sentences later, however, the Comment states that the notice must inform the seller "that the transaction is claimed to involve a breach." This language is consistent with the text of UCC 2-607 and has been used to support application of a "strict standard" of notice, i.e., the buyer must notify the seller not only of a problem with the goods, but that the buyer holds the seller accountable for the problem and considers the delivery to be a "breach."⁴

Two Michigan Court of Appeal cases from the 1970s apply what appears to be the lenient standard.⁵ But the opinions do not even mention the strict standard, much less discuss which notice standard is preferable. The *American Bumper* court noted the split in authority between the "lenient" and

"strict" standards, but it did not decide which standard applies as a matter of Michigan law because the court concluded that American Bumper's notice to its supplier did not satisfy either standard.⁶ As a result, it is unclear which standard will apply to future Michigan transactions.

Third, a buyer's failure to give notice bars the pursuit of "any remedy." UCC 1-201(34) broadly defines remedy as "any remedial right to which an aggrieved party is entitled with or without resort to a tribunal."⁷ The *American Bumper* court relied on UCC 1-201(34) and interpreted UCC 2-607 to bar literally "any remedy," including American Bumper's claims for express and implied indemnity.⁸ Thus, if a buyer fails to notify a seller of breach within a reasonable time, it may lose not only its UCC claims but also other claims, including bargained-for contract remedies such as indemnity.

The American Bumper Decision

Until last year's *American Bumper* decision, Michigan appellate courts had not written an opinion squarely addressing the UCC 2-607 notice issue in over two decades. The *American Bumper* dispute began in late 1993 when American Bumper's bumper assemblies began falling off Ford trucks. American Bumper notified its fastener supplier of the problem and canceled the supply contract. Early in the investigation into the cause of the problem, Ford issued a report stating its belief that American Bumper and its fastener supplier were at fault and that American Bumper "should bear the financial responsibility because it was the end item supplier."⁹

American Bumper and its supplier did an independent investigation and found that the cause of the failure was a change in the coating used on the fasteners. American Bumper presented its response to Ford in June 1994. Critically, for purposes of the notice issue, American Bumper "dismissed each charge against it and [the supplier] and . . . clearly stated that the fault was with Ford and Metal Coatings International because Ford directed [the supplier] and all the approved fastener suppliers" to make the coating change.¹⁰

In 1995, American Bumper and Ford entered into settlement negotiations, and American Bumper settled all recall issues by absorbing \$900,000 in recall costs that American Bumper had incurred and by giving Ford a one-time price reduction of \$2.2 million. American Bumper did not notify its supplier of the settlement negotiations or

settlement, nor did it seek contribution following the conclusion of negotiations. Later, American Bumper made the one-time price reduction permanent, bringing the price reductions to a total of about \$8 million. Finally, in August 1997, more than three years after American Bumper's response to the Ford report, American Bumper sued its supplier, claiming that the supplier was responsible for the design change and the settlement costs.¹¹

The trial court dismissed American Bumper's lawsuit based on American Bumper's failure to give its parts supplier the UCC 2-607 notice. The Michigan Court of Appeals affirmed, concluding that American Bumper's conduct failed to satisfy either the strict or the lenient standard for notice:

Regardless of whether a strict or lenient standard is applied, we find that the notice was not adequate in this case because the notice did not satisfy the policies underlying the UCC's notice provision and plaintiff's conduct did not satisfy the UCC's standard of commercial good faith.¹²

In so holding, the court first identified four purposes of the UCC's notice requirement:

(1) to prevent surprise and allow the seller the opportunity to cure the nonconformance; (2) to allow the seller the fair opportunity to investigate and prepare for litigation; (3) to open the way for settlement of claims through negotiation; (4) to protect the seller from stale claims and provide certainty in contractual arrangements.¹³

The court then discussed how American Bumper's course of conduct failed to satisfy those purposes:

Here, rather than allowing [the supplier] to attempt to cure the defect, plaintiff recommended purchasing the U-nuts from another manufacturer and simply canceled the contract. Once the parties investigated the problem with the U-nuts, plaintiff determined that [the supplier] was not at fault. Further, *there was no overture to negotiation or settlement between plaintiff and [the supplier]. . . .*

. . . .

. . . [P]laintiff did nothing more than initially notify defendants that there was a problem with the U-

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nuts, but never notified defendants that they were in breach. *Some courts have made clear that it is not enough for the buyer to only notify the seller that it is having difficulty with the goods.* Clearly, plaintiff's conduct after the problem with the U-nuts was discovered is completely contrary to a finding that plaintiff considered defendants to be in breach.¹⁴

The court also specifically noted that an initial and adequate notice may be dissipated by the seller's later conduct and that it is the entire course of conduct that must satisfy UCC 2-607: "[E]ven if adequate notice is given at some point, subsequent actions by the buyer may negate its effect[,] and the buyer's conduct, taken as a whole, must constitute timely notification that the transaction is claimed to involve a breach."¹⁵

How To Counsel Your Client When Dealing With a UCC 2-607 Notice Situation

There are a number of important lessons that can be gleaned from the *American Bumper* opinion. First, a court will evaluate a buyer's entire course of conduct as it relates to notice. This can create a quandary for a mid-tier parts supplier, which may find itself responsible not only for defects in its own product but also defects caused by any of its down-line suppliers. To avoid liability, the mid-tier supplier must shift *all* the blame up-line. In so doing, the mid-tier supplier must be careful to continue communicating privately with a potentially responsible down-line supplier that the down-line still bears responsibility for the problem.

Second, it remains unclear which standard of notice a Michigan court will apply to future UCC actions. It may not be enough to simply notify a supplier that there is a "problem" with a shipment. Counsel therefore *must* be consulted to draft or review "notice" letters when it becomes necessary to contact a supplier about a problematic shipment of goods.

Third, there are other policy purposes underlying a UCC 2-607 notice, including investigation and settlement. In *American Bumper*, for example, the failure to notify deprived the supplier of an opportunity to interview Ford and American Bumper employees about responsibility for the coating change (the theory of liability American Bumper ultimately tried to pin on the supplier). In addition, American Bumper settled its own liability without giving the supplier

notice of or an opportunity to participate in the settlement negotiations. These facts likely influenced the Michigan Court of Appeals' conclusion that American Bumper's notice "did not satisfy the policies underlying the UCC's notice provision."¹⁶

With these lessons in mind, there are a number of points a purchaser should consider when dealing with a notice situation:

- A supplier may try to alter the usual notice rule in its standard terms and conditions (e.g., must give notice of defects within 30 days of receipt). Study the UCC's "Battle of the Forms" rule,¹⁷ and be sure to keep such terms out of the parties' contract.
- When drafting or reviewing a "notice" letter, do not sugarcoat. Use magic words like "breach," "fault," or "we hold you responsible."
- Send "notice" letters early and often. When it is necessary to exonerate your own business *and* down-line suppliers to satisfy an up-line purchaser, continue to notify down-lines privately that they are responsible.
- When entering into settlement negotiations with an up-line purchaser, get potentially responsible down-lines involved in the process. It may not make sense to have all down-line suppliers involved in the actual negotiations because the up-line purchaser will undoubtedly try to leverage the number of participants into a larger final settlement number. But at a minimum, notify the down-line suppliers that settlement discussions are taking place and involve them in presettlement strategy sessions that make it clear they remain potentially responsible.
- When notifying down-line suppliers of problems, try to describe the alleged breach of contract with particularity. Some courts have held that a buyer's specific notice of one breach is *not* sufficient to satisfy the notice requirement for a separate or different alleged breach.¹⁸ The reason is that when the alleged breach changes (as it did in *American Bumper*), the factual investigation and settlement focus likewise change. Thus, while there is some inherent risk in limiting the possible sources for liability, that risk is likely outweighed by the risk of losing all claims for a failure to give proper notice.
- Finally, do not destroy problem goods until the supplier has had a chance to examine them. Similarly, do not buy replacement goods until you have given the supplier an opportunity to cure or replace.

When drafting or reviewing a "notice" letter, do not sugarcoat. Use magic words like "breach," "fault," or "we hold you responsible."

Conclusion

The notice requirement in UCC 2-607 is rife with peril for a purchaser in possession of what it believes to be defective goods. Although notifying the supplier of the defects is often an afterthought, the failure to pay attention to this important requirement may result in the loss of all claims for breach against the supplier. It is critical, therefore, that counsel be involved at every step once a problem develops with a shipment of goods. Conversely, when representing the supplier, be sure to include "failure to give notice" as an affirmative defense to any complaint alleging defective goods.

American Bar Association's Appellate Practice Journal. Mr. Bursch is a summa cum laude graduate of Western Michigan University and a magna cum laude graduate of the University of Minnesota Law School. Before joining Warner Norcross, Mr. Bursch clerked for the Honorable James B. Loken on the U. S. Court of Appeals for the Eighth Circuit.

NOTES

1. *American Bumper & Mfg Co v TransTechnology Corp*, 252 Mich App 340, 652 NW2d 252 (2002). Mr. Bursch represented the parts supplier.

2. MCL 440.2607(3)(a) (emphasis added).

3. See, e.g., *Natron Corp v Hamilton/Avent Elecs*, No 5:90-CV-60, 1991 WL 303604, at *2 (WD Mich 1991); see also James J. White & Robert S. Summers, *Uniform Commercial Code* 425 (2d ed 1980) ("the drafters intended a loose test; a scribbled note on a bit of toilet paper will do").

4. See, e.g., *K&M Joint Venture v Smith Int'l, Inc*, 669 F2d 1106, 1112-1114 (6th Cir 1982); *Allmand Assocs, Inc v Hercules Inc*, 960 F Supp 1216, 1231 (ED Mich 1997).

5. *SC Gray, Inc v Ford Motor Co*, 92 Mich App 789, 803-804, 286 NW2d 34 (1979); *Michigan Sugar Co v Jebavy Sorenson Orchard Co*, 66 Mich App 642, 647, 239 NW2d 693 (1976).

6. 252 Mich App at 345 ("Regardless of whether a strict or lenient standard is applied, we find that the notice was not adequate in this case because the notice did not satisfy the policies underlying the UCC's notice provision and plaintiff's conduct did not satisfy the UCC's standard of commercial good faith").

7. MCL 440.1201(34).

8. 252 Mich App at 348 ("Here, the statute plainly and unambiguously states that notice must be given or the buyer is barred from any remedy").

9. *Id.* at 342-343.

10. *Id.* at 343.

11. *Id.* at 343, 346-347.

12. *Id.* at 345.

13. *Id.* at 346-347 (citing *Aqualon Co v MAC Equip, Inc*, 149 F3d 262, 268-269 (4th Cir 1998)).

14. 252 Mich App at 347-348 (emphasis added).

15. *Id.* at 348 (citing *Eastern Air Lines, Inc v McDonnell Douglas Corp*, 532 F2d 957, 978 (5th Cir 1976)).

16. 252 Mich App at 345.

17. MCL 440.2207.

18. See, e.g., *Standard Alliance Indus v The Black Clawson Co*, 587 F2d 813, 827 (6th Cir 1978); *Eaton Corp v The Magnavox Co*, 581 F Supp 1514, 1531 (ED Mich 1984).

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