New York Court of Appeals Holds that Seller's Express Warranties in Nongoods Sales Are Bargained-for Contractual Terms, and Buyer Need Not Rely on Truth of Warranted Information to Seek Damages for Breach of Such Warranties

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New York Court of Appeals holds that seller's express warranties in nongoods sales are bargained-for contractual terms, and buyer need not rely on truth of warranted information to seek damages for breach of such warranties

Express warranty liability in a contract for the sale of goods in New York is governed by the Uniform Commercial Code ("Code" or "UCC"). Under the UCC, to bring an action for breach of express warranty, a buyer must show that the seller did not comply with an affirmation, promise, or description considered to be "part of the basis of the bargain." In nongoods sales, however, recovery

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1 See N.Y. U.C.C. LAW § 2-313 (McKinney 1964). Sales subject to the UCC are governed by article two, the scope of which is limited to "transactions in goods." See id. § 2-102. Goods are defined as "all things . . . which are movable at the time of identification to the contract for sale other than the money in which the price is to be paid, investment securities . . . and things in action." Id. § 2-105(1).

2 Id. § 2-313(1)(a). Replacement of the reliance requirement with the "basis of the bargain" provision was made deliberately by Karl Llewellyn, a principal drafter of the UCC. See Heckman, "Reliance" or "Common Honesty of Speech": The History and Interpretation of Section 2-313 of the Uniform Commercial Code, 38 CASE W. RES. L. REV. 1, 14 (1987). "Part of" was added to the "basis of the bargain" language at the insistence of the New York Law Revision Commission. See id. at 25-26.

At common law, a buyer of goods was required to rely on the seller's affirmations or representations to recover for breach of express warranty. See 1 S. WILLISTON, THE LAW GOVERNING SALES OF GOODS AT COMMON LAW AND UNDER THE UNIFORM SALES ACT § 206, at 397 (2d ed. 1924). The reliance requirement was codified in the express warranty provision
for breach of express warranty is subject to the common-law rule, established nearly a century ago, that requires a buyer to prove reliance on the seller's affirmation or promise.\(^3\) This reliance requirement has been challenged by a seemingly contrary line of cases, resulting in a lack of consensus as to its validity and application.\(^4\) Recently, in *CBS Inc. v. Ziff-Davis Publishing Co.*,\(^5\) the New


The ambiguity of the new language in the Code created confusion. See 1955 N.Y. Law Rev. Comm'n, *supra* (since "basis of the bargain" does not convey a definite meaning," courts cannot assume Code's language incorporates reliance requirement); 1 O. Harris \& A. Squillante, *Warranty Law in Tort and Contract Actions* § 6.18, at 192 (1989) (discussing abundance of contradictory authority surrounding UCC's "basis of the bargain" requirement as unspoken test for reasonable reliance); Special Project, *Article Two Warranties in Commercial Transactions: An Update*, 72 Cornell L. Rev. 1159, 1173-84 (1987) (discussing various interpretations of section 2-313's reliance requirement). Consequently, some courts have persisted in interpreting the new language as tantamount to a reliance requirement. See, e.g., *Overstreet v. Norden Labs.*, 669 F.2d 1286, 1290-91 (6th Cir. 1982) (reliance as element of recovery under UCC express warranty erroneously excluded from jury instruction); *Speed Fastners, Inc. v. Newsom*, 382 F.2d 395, 397 (10th Cir. 1967) (no express warranty created in sale of stud fasteners because buyer did not rely on promises or descriptions in seller's pamphlet); *In re Bob Rigby, Inc.*, 62 Bankr. 900, 906 (Bankr. M.D. Fla. 1986) (no express warranty created by seller's affirmations about rock-crushing machine because buyer not entitled to rely on them). Other jurisdictions have held that the reliance requirement has been eliminated altogether. See, e.g., *Keith v. Buchanan*, 173 Cal. App. 3d 13, 23, 220 Cal. Rptr. 392, 397-98 (1985) ("new language of this code section" illustrates that "reliance has been purposefully abandoned").

The official comments to the UCC support the elimination of reliance as an element of express warranty. See N.Y. U.C.C. Law § 2-313 comment 3 (McKinney 1964) ("no particular reliance on [seller's affirmations of fact, descriptions of goods, or exhibitions of samples] need be shown . . . to weave them into the fabric of the agreement").

\(^2\) *Crocker-Wheeler Elec. Co. v. Johns-Pratt Co.*, 29 A.D. 300, 302, 51 N.Y.S. 793 (1st Dep't 1898), aff'd, 164 N.Y. 593, 58 N.E. 1086 (1900). In *Crocker-Wheeler*, the seller was held to have warranted the quality, but not fitness for use, of an insulating material for electrical machinery because the buyer had conducted its own precontractual test of the material and therefore had not relied on the defendant's warranty of fitness for a particular purpose. *See id.* The *Crocker-Wheeler* court stated the following rule: "It is elementary that, in order to entitle the plaintiff to maintain an action for breach of an express warranty, it must be established that the warranty was relied on." *Id.*; see *Randy Knitwear, Inc. v. American Cyanamid Co.*, 11 N.Y.2d 5, 11-12, 181 N.E.2d 399, 401-02, 226 N.Y.S.2d 363, 366-67 (1962) (remote buyer of treated fabric rightfully relied on seller's express warranties of nonshrinkage).

York Court of Appeals held that a buyer's acknowledged disbelief in and lack of reliance on the truth of the seller's express warranties at the time it closed on a contract for the sale of businesses did not relieve the seller of its warranty obligations.8

In CBS, the plaintiff, CBS Inc. ("CBS"), contracted to purchase twelve consumer magazine businesses from the defendant, Ziff-Davis Publishing Co. ("Ziff-Davis"), on the basis of financial data supplied by the seller, Ziff-Davis.7 In the written purchase agreement, Ziff-Davis warranted to CBS that the audited income and expense reports of the businesses had been prepared in compliance with generally accepted accounting principles ("GAAP") and that the profitability of the publications had not changed substantially from the time the reports were prepared until the time of closing.8 Pursuant to the written purchase agreement, CBS performed its own "due diligence" audit of Ziff-Davis's financial statements, the results of which suggested that they "were not prepared according to GAAP and did not fairly depict Ziff-Davis's financial condition."9 Ziff-Davis maintained otherwise,10 and, despite its doubts, CBS closed on the contract.11 CBS's subsequent action for breach of express warranty against Ziff-Davis was dismissed in the lower courts on the ground that CBS had not relied on the truth of

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9 See id. at 500, 553 N.E.2d at 999, 554 N.Y.S.2d at 451. CBS's letter of notification to Ziff-Davis stated that "[b]ased on the information and analysis provided [to it, CBS was] of the view that there [were] material misrepresentations in the financial statements provided [to CBS]." Id.

10 See id. Ziff-Davis insisted that the accusation had "no merit." Id.

11 See id. at 501, 553 N.E.2d at 999, 554 N.Y.S.2d at 451. Although CBS acknowledged the existence of a "clear dispute" in a letter to Ziff-Davis, CBS decided to proceed with the closing the same day because of the "considerable time, effort and money [CBS had spent] in complying with [its] obligations." Id.
the financial statements supplied by Ziff-Davis.\textsuperscript{12} However, upon review, the Court of Appeals modified the order of dismissal, giving CBS the right to seek damages for breach of express warranty.\textsuperscript{15}

Writing for the court, Judge Hancock cited with approval the contractual characterization of reliance adopted by the District Court for the Southern District of New York in Ainger v. Michigan General Corp.\textsuperscript{14} The critical question, he stated, was “not whether the buyer believed in the truth of the warranted information . . . but ‘whether [the buyer] believed [it] was purchasing the [seller’s] promise [as to its truth].’”\textsuperscript{16} The court agreed with CBS, holding that the only reliance needed was on the warranties as bargained-for contractual terms.\textsuperscript{18} Further, the court described Ziff-Davis’s argument, that CBS’s lack of reliance at closing negated the effect of the warranties, as based on a “tort-action type of reliance” that would necessitate belief in the truth of the representations and a subsequent change of position in reliance thereon.\textsuperscript{17} Finally, the court distinguished cases cited by Ziff-Davis in support of the proposition that the weight of precedent required buyer reliance.\textsuperscript{16}

Dissenting, Judge Bellacosa regretted the court’s “discarding” of reliance and its “sacrifice” of precedent in the field of common-law commercial transactions.\textsuperscript{19} Next, he criticized Ainger as inferior authority because the issue of reliance in express warranty was only discussed as dicta.\textsuperscript{20} Without addressing the tort-contract di-

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\item Id. The order of dismissal for the breach of express warranty claim was affirmed without comment by the Appellate Division, First Department in a unanimous decision. Id.
\item See id.
\item 476 F. Supp. 1209, 1225 (S.D.N.Y. 1979).
\item CBS, 75 N.Y.2d at 503, 553 N.E.2d at 1000-01, 554 N.Y.S.2d at 452-53 (quoting Ainger, 476 F. Supp. at 1225 (citations omitted)).
\item CBS, 75 N.Y.2d at 504-05, 553 N.E.2d at 1001-02, 554 N.Y.S.2d at 453-54.
\item See id.
\item Id. at 506, 553 N.E.2d at 1003, 554 N.Y.S.2d at 455 (Bellacosa, J., dissenting). The precedent referred to was Crocker-Wheeler Elec. Co. v. Johns-Pratt Co., 29 A.D. 300, 51 N.Y.S. 793 (1st Dep’t 1898), aff’d, 164 N.Y. 593, 58 N.E. 1086 (1900). See CBS, 75 N.Y.2d at 506, 553 N.E.2d at 1003, 554 N.Y.S.2d at 455 (Bellacosa, J., dissenting); see also note 3 and accompanying text (discussion of Crocker-Wheeler).
\item See CBS, 75 N.Y.2d at 508-09, 553 N.E.2d at 1004, 554 N.Y.S.2d at 456 (Bellacosa, J., dissenting). Judge Bellacosa noted that “[lack of reliance . . . was not part of the holdings in Ainger or CPC, even at their trial level citations by the majority.” Id. at 509, 553
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chotomy raised by the majority, Judge Bellacosa also noted that CBS, by choosing to close on the contract after acquiring reason to doubt the truth of the warranted information, took a business risk with its "cyclopean eye wide open."22

It is asserted that CBS was correctly decided because the parties' acknowledgement of the express warranties as bargained-for contractual terms made a consideration of reliance unnecessary. It should, though, be noted that the court did not address the question of whether reliance would be required when the parties do not agree that an express warranty exists. However, the principles set forth in the UCC would provide a functional framework with which to analyze the issues of reliance and express warranty liability in nongoods sales.23 Furthermore, application of the UCC by analogy to the facts in CBS provides a way to harmonize the divergent philosophies voiced therein. Both the CBS court24 and its dissent25 explicitly and implicitly drew from the Code to support their rationale. They also agreed that "analogy to the UCC is 'instructive,'"26 and cited with approval sales actions governed by statute.27

N.E.2d at 1004, 554 N.Y.S.2d at 456 (Bellacosa, J., dissenting).

See id. at 507, 553 N.E.2d at 1003, 554 N.Y.S.2d at 455 (Bellacosa, J., dissenting).

CBS had a contractual right not to close if the warranted information proved to be untrue. Id. (Bellacosa, J., dissenting).

See id. at 510, 553 N.E.2d at 1005, 554 N.Y.S.2d at 457 (Bellacosa, J., dissenting).

See N.Y. U.C.C. LAW § 1-102 (McKinney 1964). Extension of the precepts embodied in the UCC to non-Code commercial transactions is supported by article one, which establishes the purposes and rules of construction. See id.

See CBS, 75 N.Y.2d at 506 n.4, 553 N.E.2d at 1002 n.4, 554 N.Y.S.2d at 454 n.4.

See id. at 509, 553 N.E.2d at 1004, 554 N.Y.S.2d at 455 (Bellacosa, J., dissenting).

Id. at 506 n.4, 553 N.E.2d at 1002 n.4, 554 N.Y.S.2d at 454 n.4; see id. at 509, 553 N.E.2d at 1004, 554 N.Y.S.2d at 455 (Bellacosa, J., dissenting). The court invoked UCC sections 2-607(2) and 2-714 to support its theory that the Ziff-Davis warranties were promises of indemnification. Id.; see also N.Y. U.C.C. LAW §§ 2-607(2), 2-714 (McKinney 1964). It is submitted that the court's reliance on these Code provisions was misplaced. The dissent cited the language in official comment 3 of the express warranty provision of the UCC (§ 2-313) to support its position on reliance. See CBS, 75 N.Y.2d at 509, 553 N.E.2d at 1004, 554 N.Y.S.2d at 455 (Bellacosa, J., dissenting); see also N.Y. U.C.C. LAW § 2-313 comment 3 (McKinney 1964).

Viewing the transaction in CBS from the perspective of the UCC express warranty provisions suggests that the financial statements circulated to CBS constituted part of the basis of the bargain, as they related to the "goods" and induced the contract of sale. Moreover, by engaging its own experts to audit the information, it is asserted that CBS placed itself in the position of an inspecting buyer who discovered a defect prior to closing. By proceeding with the sale under these circumstances, CBS should have been precluded from claiming that the financial data was part of the basis of the bargain and, therefore, no effect could have been given to the warranted information. A seller’s affirmations, however, need not be part of the basis of the bargain when an express warranty is already in place and undisputed, as was the situation in CBS.


See supra note 2 and accompanying text (discussion of UCC express warranty provision).

CBS, 75 N.Y.2d at 498-99, 553 N.E.2d at 998, 554 N.Y.S.2d at 450.

Pre-Code law generally held that a buyer’s inspection of the goods vitiated an express warranty unless a hidden defect was present. See, e.g., Turner v. Central Hardware Co., 353 Mo. 1182, 1190, 186 S.W.2d 603, 607 (1945) (inspection failing to detect latent defect in ladder did not negate seller’s express warranty). The Code is silent on the effect of a buyer’s inspection of goods with regard to a seller’s express warranty. See N.Y. U.C.C. Law § 2-313 (McKinney 1964). Case law interpreting the Code has suggested, however, that a presale detection of a defect would preclude an express warranty from taking effect. See, e.g., Janssen v. Hook, 1 Ill. App. 3d 318, 321, 272 N.E.2d 385, 388 (1971) (no express warranty created by seller’s affirmation that milk truck “in good condition” when presale inspection by buyer revealed need for repair). Additionally, opportunity to learn of a falsity in the seller’s affirmation of a fact over the course of the parties’ commercial relationship and experience gained similarly has been held to be fatal to a breach of express warranty claim. See, e.g., Royal Business Mach. v. Lorraine Corp., 633 F.2d 34, 44 (7th Cir. 1980) (discovery of falsity of seller’s affirmations during commercial transactions spanning 18 months removed them from consideration as “part of the basis of the bargain”).

See CBS, 75 N.Y.2d at 506 n.4, 553 N.E.2d at 1002 n.4, 554 N.Y.S.2d at 454 n.4. The CBS court interpreted UCC sections 2-607(2) and 2-714 to mean that CBS could accept the nonconforming “goods,” then sue for damages. Id.; see also N.Y. U.C.C. Law §§ 2-607(2), 2-714 (McKinney 1964). It is submitted that the court’s interpretation would defeat the “part of the basis of the bargain” language in section 2-313. Whereas section 2-607(2) guarantees the buyer remedial rights despite acceptance of the goods, see id. § 2-607(2), and section 2-714(1) provides for recovery when tender is nonconforming, see id. § 2-714, it is submitted that the latter section applies to a breach of express warranty action only when the nonconformity is detected after the sale.
The issue of whether a buyer’s nonreliance on a seller’s representations effectively removes them from the contract of sale was sidestepped by the New York Court of Appeals in CBS. Application of the UCC as an analogical tool to nongoods sales suggests that when a buyer acquires reason to disbelieve a seller’s representations in the course of their commercial relationship, the representations cannot remain a part of the basis of the bargain. Unless an express warranty is acknowledged by both parties, one does not come into existence. To allow otherwise would permit a nonrelying party to “have its cake and eat it, too.”

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Absent showing of prejudice, indictment and conviction of criminal defendant by unlicensed prosecutor may stand

The due process clause of the fifth amendment, and the sixth amendment right “to be informed of the nature and cause of accusation,” are vital components of a fair trial. If a criminal defendant is convicted, any infringement upon the fairness guaranteed at trial may warrant reversal unless the evidence of guilt is strong enough to render the resulting prejudice harmless. However, if the

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1 See U.S. Const. amend. V. The fifth amendment provides, in pertinent part: “No person shall . . . be deprived of life, liberty, or property, without due process of law.” Id. The United States Supreme Court has proclaimed that “fair play” is the essence of due process. Galvan v. Press, 347 U.S. 522, 530 (1954). Although many jurisdictions have held that the fifth amendment does not restrict state action, see Pitt v. Pine Valley Golf Club, 695 F. Supp. 778, 781 (D.N.J. 1988), the Southern District of New York has intimated that the right to a fair trial exists in the states through the fourteenth amendment’s due process clause. See Mishkin v. Thomas, 282 F. Supp. 729, 737 (S.D.N.Y. 1968).

2 See U.S. Const. amend. VI. The sixth amendment states that “[i]n all criminal prosecutions, the accused shall enjoy the right . . . to be informed of the nature and cause of the accusation.” Id.

3 See 2 R. Rotunda, J. Nowak, & J. Young, TREATISE ON CONSTITUTIONAL LAW: SUBSTANCE AND PROCEDURE § 17.4(b) (1986 & Supp. 1989). “The essential guarantee of the due process clause is that the government may not imprison or otherwise physically restrain a person except in accordance with fair procedures.” Id. The defendant’s physical liberty is protected in a number of ways: the fourth amendment requires that an arrest be based on probable cause; the eighth amendment prohibits excessive bail; the sixth amendment guarantees a speedy trial; and the fifth amendment places the burden upon the prosecution to prove guilt beyond a reasonable doubt. See id.