# UCC Risk of Loss and Contract Performance



The UCC has special provisions to determine who bears the risk of loss when goods are destroyed and the contract is silent about who bears the risk. To understand these principles, it is important to identify the goods, understand which party has title to the goods, and determine when the risk transfers from the seller to the buyer.

## Identification

Before ownership in goods can pass from one seller to a buyer, the goods must exist and and be identified. In a sale of goods, identification occurs when specific goods are designated as the subject matter of a sales contract. Identification is a prerequisite for the title to pass from the seller to buyer. This is important because it also allows risk of loss to pass from the seller to the buyer.

Of course, the parties can agree as to when identification occurs; but if they don't, the UCC comes to the rescue to add clarity. For our purposes, if the contract involves the sale of goods that are already in existence, identification occurs when the contract is formed.

## Passage of Title

Again, the parties can agree as to when title (ownership) passes from the seller to buyer.  In the absence of such an agreement, the UCC steps in to fill the gaps of contracts. In general, the UCC indicates that title passes to the buyer when the seller delivers the goods. However, when title passes may depend on which kind delivery is involved.

In a **shipment contract**, the seller is permitted to ship goods by carrier (e.g., UPS, FedEx, DHL). In a shipment contract, the seller delivers the conforming goods to the carrier, at which time title passes to the buyer. All contracts involving delivery are assumed to be shipment contracts unless something to the contrary is stated in the agreement.

A **destination contract** involves a delivery agreement where the seller must deliver the goods to a specific place, usually directly to the buyer. Title passes when delivered according to the terms of the agreement.

A third option occurs when the buyer picks up the goods. In these cases, there are no shipment terms, but rather title passes when the buyer takes possession and the seller gives the buyer a receipt (if applicable). If the goods do not move, title passes when the appropriate documents are delivered to the buyer.

## Risk of Loss

If the contract is silent, the UCC adds clarity as to when the risk of loss (i.e., liability) transfers from the seller to the buyer. When the contract involves the movement of goods via a carrier, courts will look at the terms used in the contract. The most common shipping terms are known as Free On Board (FOB). This indicates that the selling price of the goods includes transportation costs to the specific FOB location. The seller carries the risk of loss to the FOB. location. If the location is the seller's location (i.e., the seller's city), the contract is a shipment contract. If the FOB location is the place to which the goods are being shipped (i.e., the buyer's city), the contract is a destination contract.

In a shipment contract, the seller can ship goods by carrier. The risk of loss in a shipment contract passes to the buyer when the goods are delivered to the carrier. Hence, if the goods are lost, stolen, or destroyed in transit, the buyer bears the risk of loss. In a destination contract, the risk of loss passes to the buyer when the goods are delivered to the buyer at the location specified in the contract. If the goods are lost, stolen, or destroyed in transit as before, the seller bears the risk of loss.

The UCC also addresses risk of loss when the goods are not moved. In these cases, the buyer picks up the goods from the seller. When the seller keeps the goods for pickup, it's important to know whether or not the seller is a merchant. If the seller is a merchant, risk of loss passes to the buyer when the buyer actually takes physical possession of the goods. If the seller is not a merchant, the risk of loss passes to the buyer upon tender of delivery. Tender of delivery occurs when the seller makes the goods available to the buyer and notifies the buyer that the goods are ready for pick up.

These rules may be modified if the contract is breached. For example, if the seller breaches by sending nonconforming goods, the risk of loss does not pass to the buyer when delivered to a carrier. As a result, if the goods are damaged en-route, it is the seller that must seek redress from the carrier.

This is a good time to clarify that risk of loss does not mean that a party is liable for the damage. Should you place  goods with a carrier and they are damaged in transit, the carrier is going to bear responsibility and carry insurance to cover claims. Risk of loss determines whether the buyer or seller will have to file that claim with the carrier.

## Performance

Performance under the UCC requires (1) that the seller delivers goods that measure up to the contract and (2) that the buyer pays for those goods. When one or both parties breach these duties, the UCC provides remedies. Underlying every UCC contract is the duty of good faith, meaning that the parties act honestly in the performance of the contract.

### Buyer's Duties and Rights

If the seller breaches the contract, the buyer has a number of options to seek redress. These involve:

1. **The right to inspect the goods**. Prior to accepting and paying for the goods, the buyer has the right to inspect the goods to ensure that they conform to the contract. The UCC is a bit vague here, giving the buyer a "reasonable" time to inspect the goods. If the inspection finds that the goods are non-conforming, the buyer may reject them.
2. **The right to reject**. If the goods or delivery fails to conform to the contract (e.g., the seller sends the wrong goods or delivers them too late), the buyer may reject them if done in a “reasonable” time. If properly rejected, the buyer will not have to pay. If payment was already tendered, the buyer is entitled to a refund.
3. **The right to revoke acceptance**. In some circumstances, the defect in the goods can't immediately be determined. For example, if I purchase 500,000 toy boats and upon receipt check one to ensure it floats (it does), I would reasonably accept them. However, if I later find that 200,000 of the boats sink in the water, the UCC permits me to revoke my acceptance.
4. **The right to damages**. If a buyer does not receive the goods bargained for, the buyer may have to purchase the goods elsewhere, often for a higher price. If the buyer is required to pay more for these substitute goods than per the contract, the buyer has a right to receive the difference as damages. The buyer is, however, required to mitigate damages and reasonably seek out the best deal rather than simply purchase the most expensive substitute goods.

### Seller's Duties and Rights

The UCC also provides rights and remedies for sellers. These include:

1. **The right to cure**. If the buyer rejects the goods for nonconformity, the UCC allows the seller to cure the defective performance assuming the defect is relatively minor. Remember that this differs from common law where any deviation was considered breach, terminating the contract. The right to cure only applies if the time for performance has not expired or if the seller has reasonable grounds to believe that the goods were acceptable.
2. **The right to reclaim goods**. If the seller finds that the goods have been delivered to an insolvent buyer or to a solvent buyer who has acted wrongfully (e.g., failed to pay or otherwise breached the contract), the seller is given the right to reclaim the goods. If the goods are in transit, the seller may intercept the goods to reclaim them. Even if the goods have been delivered, the seller may make a demand that the goods be returned and enforce that demand in court.
3. **Right to resell the goods**. If the buyer has breached and the seller is still in possession of the goods, the seller may resell the goods to another.
4. **The right to damages**. If the goods are sold for less than the contract price with the breaching buyer, the seller has a right to damages for the difference.

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