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Solidifying Arkansas's Liquidated Damage Law after S.O.G.-San-Ore-Gardner v. Missouri Pacific Railroad Co.: It's Not All Water Under the Bridge

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SOLIDIFYING ARKANSAS'S LIQUIDATED DAMAGE LAW AFTER *S.O.G.-SAN ORE-GARDNER V. MISSOURI PACIFIC RAILROAD CO.*: IT'S NOT ALL WATER UNDER THE BRIDGE

I. INTRODUCTION

Railroads once symbolized wealth, political power, and the industrialization of the United States. During the late nineteenth century, many states' economic structures began to change as a result of railroad construction and industrial development.[1] Railroad growth into new geographic areas helped revolutionize agriculture, manufacturing, and transportation.[2] As part of that growth, expanding railroad infrastructure played a significant role in the economic development of the United States. Around 1900, more miles of rail were laid down in a ten-year span than the preceding one hundred years combined.[3] That grand effort necessarily kept contractors busy building bridges, tunnels, and other forms of infrastructure ancillary to actual rail installation.

Even as passenger travel via rail waned in the twentieth century, by 1970, rail freight was consistently setting usage records; "[b]etween 1970 and 2000, rail freight [usage] doubled."[4] Just like the boom at turn of the twentieth century, this increase in rail freight also led to increased infrastructure construction—some of which took place in Arkansas. Looking at the Benzal Bridge over the White River, it is easy to imagine the positive financial impact building the bridge had on that part of rural Arkansas. The image of this economic blessing makes it hard to believe that constructing that bridge would result in years of litigation.[5] The most damaging aspect of this litigation is that it yielded a rule of law that was one of the worst things to happen to Arkansas construction law in the past three decades.

Rooted in the "fundamental principal of freedom of contract," parties have been free to negotiate specific or liquidated sums and contractually bind themselves to those sums as a basis of damages for breach of contract actions.[6] Typically, these liquidated damage provisions are included where

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1. *See* James Logan Hunt, *Private Law and Public Policy: Negligence Law and Political Change in Nineteenth-Century North Carolina*, 66 N.C. L. REV. 421, 434 (1988).

2. *Id.*

3. *See id.*

4. *American Railroads in the 20th Century*, NAT'L MUSEUM AM. HISTORY, http://americanhistory.si.edu/onthemove/themes/story_42_1.html (last visited Mar. 10, 2012).

5. *See infra* Part IV.A.

6. 24 SAMUEL WILLISTON & RICHARD A. LORD, A TREATISE ON THE LAW OF CONTRACTS § 65.1, at 213 (4th ed. 1993).

actual damages "are by their nature uncertain and difficult to determine."[7] From a court's standpoint, actual cost information is always preferable to estimates when establishing damages.[8] Courts will uphold liquidated damage provisions only if they pass the most exacting judicial scrutiny.[9]

Judicial scrutiny is not limited to an inquiry of whether a liquidated damage provision bears some relationship to the actual damages that may flow from a breach. A second potential issue comes to life where one party has contributed to a breach yet still seeks to enforce a damage provision against the other party. State laws vary on this issue.[10] The traditional view leads courts to opt against enforcement, whereas the modern view will apportion fault and enforce the provision accordingly.[11] This approach of dividing the fault is commonly known as the apportionment rule.[12]

Jurisdictions opposing the apportionment rule must face problems with which their counterparts need not be concerned. First, refusing to apportion damages contravenes public policy. Nearly all state legislatures have en-

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7. 1 HOWARD W. BRILL, ARKANSAS PRACTICE SERIES: LAW OF DAMAGES § 8.1, at 99 (5th ed. 2004). Though the language of liquidated damage provisions often varies from contract to contract, the spirit of them remains the same. In the internet age we live in, parties to construction contracts are increasingly using electronic versions of American Institute of Architects (AIA) contract documents. *See* WERNER SABO, LEGAL GUIDE TO AIA DOCUMENTS, at vii (5th ed. 2008). A variation on an AIA liquidated damage provision may read as follows:

> 8.3.1.1 Failure to Complete the Work on Time. It is mutually agreed by and between the parties hereto that time shall be an essential part of this contract and that if the Contractor fails to complete its contract within the time specified and agreed upon, the Owner will be damaged thereby; and because the amount of said damages, inclusive of expenses for inspection, superintendence, and necessary traveling expenses, is difficult if not impossible to definitely ascertain and prove, it is hereby agreed that the amount of such damages shall be the appropriate sum set forth below in the Schedule of Liquidated Damages as liquidated damages for every working day's delay in finishing the work in excess of the number of working days prescribed; and the Contractor hereby agrees that said sum shall be deducted from monies due the Contractor under the contract or, if no money is due the Contractor, the Contractor hereby agrees to pay to the Owner as liquidated damages, and not by way of penalty, such total sum as shall be due for such delay, computed aforesaid.

Id. § 5.47, at 619 (adapting a liquidated damage provision in a case before the Hawaii Supreme Court) (citing Associated Eng'rs & Contractors, Inc. v. State, 567 P.2d 397 (Haw. 1977)).

8. *See* LYNN R. AXELROTH ET AL., FUNDAMENTALS OF CONSTRUCTION LAW 250–51 (Carina Y. Enhada et al. eds., 2001).

9. *See* 1 BRILL, *supra* note 7, § 8.1, at 99–100.

10. *See infra* Part II.B.

11. *See infra* Part II.B.

12. *E.g.*, PCL Constr. Servs., Inc. v. United States, 53 Fed. Cl. 479, 487 (2002).

acted portions of the Uniform Commercial Code and comparative fault statutes that operate analogously to the apportionment theory.[13] Second, refusing to apportion damages creates a conflict with the fundamental freedom to contract. Sophisticated parties to a commercial contract allocate risk using various contract provisions—including liquidated damages.[14] Third, refusing to apportion merely prolongs litigation. Courts falsely cite undue hardship and judicial inefficiency as reasons against apportioning liquidated damages. However, when courts refuse to apportion, parties continue to pursue litigation—then, the fact-finder shoulders the entire burden of ascertaining damages due without the benefit of using a contractually agreed-upon basis.[15]

This note argues that the Eighth Circuit's holding in *S.O.G.-San Ore-Gardner v. Missouri Pacific Railroad Co.*[16] is bad law because the court concluded that any act contributing to the failure to meet contractual deadlines, notwithstanding a disproportionate level of corresponding fault, bars parties from enforcing a liquidated damage provision. First, this note will discuss the development of liquidated damage law in the United States, including the apportionment rule. Next, it will illustrate problems that arise when a court rejects the apportionment rule. Finally, it will propose that Arkansas adopt the apportionment rule and provides justifications for that adoption.

II. BACKGROUND

A. Development of Liquidated Damage Law

Distinguishing the differences in liquidated damages and penalties is critical, for these differences help highlight the underlying policies and controversies surrounding liquidated damage law. Liquidated damages are fixed sums that contracting parties agree to pay if they later break a contractual obligation.[17] Those agreed-upon sums must have been determined as a result of a good faith effort to estimate actual damages that were likely to follow a breach.[18] When parties do not estimate actual damages and instead designate a sum likely to prevent a breach, that sum will be deemed a penalty.[19]

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13. *See infra* Part III.A.1–2.
14. *See infra* Part III.B.
15. *See infra* Part III.C.
16. 658 F.2d 562, 564 (8th Cir. 1981).
17. BLACK'S LAW DICTIONARY 447 (9th ed. 2009). Liquidated damages are also referred to as stipulated damages. *Id.*
18. *See, e.g.*, RESTATEMENT (SECOND) OF CONTRACTS § 356 (1981).
19. *Id.*

1. *Historical Background*

Litigating to determine damages is an expensive and cumbersome process.[20] As a result, contracting parties have long stated remedies for breaching their agreement prior to contract formation rather than vesting the responsibility with a judge or, perhaps even less reassuring for some parties, a jury.[21] In England, until the late eighteenth century, courts of law and equity freely conceded the "power of binding oneself to pay any sum one was willing to assume" for failing to perform an obligation.[22] Near the turn of that century, the judiciary began disfavoring such agreements.[23] Courts became wary of "the unusual danger of oppressive and extortionate bargains."[24] As time progressed, however, the concept of allowing parties to allocate risk by stipulating damages for breach took hold, albeit in a very small way, in English common law tradition.[25] "[I]t came to be recognized that promises to pay money as recompense for future defaults which could not be exactly valued were legitimate expedients for avoiding the uncertainty of a jury's finding and should be enforced."[26]

Around 1835, English and American courts began selectively enforcing liquidated damage provisions where they clearly bore some rational relationship to actual damages that might flow as a result of a breach.[27] When any uncertainty arose as to whether the breach was meant to be addressed by the provision, those early courts tended to hold the provision to be an unenforceable penalty.[28] If the parties limited the scope of the liquidated damage

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20. *See* Daniel D. Barnhizer, Foreword, *Power, Inequality, and the Bargain: The Role of Bargaining Power in the Law of Contract—Symposium Introduction*, 2006 MICH. ST. L. REV. 841, 845 (2006).

21. *See* 11 JOSEPH M. PERILLO, CORBIN ON CONTRACTS § 58.1, at 395–96 (rev. ed. 2005).

22. CHARLES T. MCCORMICK, HANDBOOK ON THE LAW OF DAMAGES § 147, at 601 (1935).

23. *See id*. Disfavor from United States courts can be seen from decisions as early as the mid-nineteenth century. *See* 11 PERILLO, *supra* note 21, § 58.4, at 413.

24. *See* MCCORMICK, *supra* note 22, § 147, at 600. These oppressive tactics largely resulted from the enforcement of creditors' penal bonds against vulnerable debtors beguiled by illusions of hope. *See, e.g.*, 24 WILLISTON & LORD, *supra* note 6, § 65:4, at 253–55.

25. *See* Kemble v. Farren, (1829) 130 Eng. Rep. 1234, 1236–37 (C.P.); 6 Bing. 140, 147–49 (discussing a liquidated damage provision in an employment contract). The court illustrated the limited nature of enforceable liquidated damage clauses by approving enforcement where "an agreement fixes that which is almost impossible to be accurately ascertained," but declining to do so when the clause "extends to the breach of *any* stipulation by either party." *Id.* at 1237; 6 Bing. at 148 (emphasis added).

26. MCCORMICK, *supra* note 22, § 147, at 602.

27. *See id.* at 603.

28. United States v. Bethlehem Steel Co., 205 U.S. 105, 119 (1907).

provision to a genuinely unascertainable injury, however, courts were much more likely to enforce those provisions.[29]

2. *Current State of the Law*

In Arkansas, before a court will uphold a liquidated damage provision, it will determine whether the contracting parties contemplated that damages would result from nonperformance, the damages would otherwise be difficult or impossible to calculate with precision, and the agreed-upon sum is proportional to the non-performance damages originally contemplated.[30] Failing to meet all three conditions precludes enforcement.[31] Although outside the construction context, an opinion issued by the Arkansas Supreme Court illustrates a detailed application of the three-pronged rule.[32]

Identifying whether contracting parties contemplated damages flowing from a breach is generally self-explanatory. In *Alley v. Rodgers*, sellers brought an action against the estate of a deceased buyer, seeking to enforce a provision in a contract for sale of three mobile homes.[33] On appeal from a jury verdict for the sellers, the Arkansas Supreme Court analyzed the validity of the liquidated damage provision.[34] In the first prong of the analysis, the court plainly stated that "here the parties recognized damages would flow from a breach of the contract."[35] The only language available for the court to infer contemplation of damages in the event of a failure to perform came from the contract itself: "[Buyer] agrees that down payment is to be considered as earnest money and liquidated damages should [Buyer] not complete the terms of the contract."[36] Satisfied that the parties contemplated damages, the court next moved to the second prong.[37]

Determining the difficulty of ascertaining damages flowing from a breach of contract requires more analysis than the first prong of the enforceable liquidated damage test. The *Alley* court answered this question using facts outside the contract language.[38] Prior to entering into the contract for sale, the sellers rented two of the mobile homes that were to be sold.[39] Once

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29. *See, e.g.*, *Kemble*, 130 Eng. Rep. at 1237; 6 Bing. at 148 (declining to enforce a liquidated damage clause that purported to apply to all breaches).

30. Alley v. Rodgers, 269 Ark. 262, 264, 599 S.W.2d 739, 741 (1980); *see also* Welbourn v. Kee, 134 Ark. 361, 204 S.W. 220 (1918); AXELROTH ET AL., *supra* note 8, at 261.

31. *See, e.g.*, *Welbourn*, 134 Ark. at 361, 204 S.W. at 220.

32. *See Alley*, 269 Ark. at 262, 599 S.W.2d at 739.

33. *Id.* at 263–64, 599 S.W.2d at 740.

34. *Id.*, 599 S.W.2d at 740.

35. *Id.* at 264, 599 S.W.2d at 741.

36. *Id.* at 263, 599 S.W.2d at 740.

37. *See id.* at 264–65, 599 S.W.2d at 741.

38. *See Alley*, 269 Ark. at 264–65, 599 S.W.2d at 741.

39. *Id.*, 599 S.W.2d at 741.

the sellers executed the contract, they ordered the tenants to vacate,[40] discontinued all advertising, and turned away other prospective buyers.[41] Predicting the exact amount of damages flowing from a breach would have been difficult to determine. Neither the buyer nor the sellers could accurately predict how long it would take to sell the mobile homes in the event of a breach.[42] How could "the parties . . . estimate without some difficulty the potential loss of rental income?"[43] This difficulty in estimation sufficiently warranted the court's enforcement of the liquidated damage provision—so long as the sellers were able to meet one last condition.

The final step in determining whether a liquidated damage provision is enforceable hinges on the provision's sum bearing a reasonable proportion to what the parties contemplated might flow from a breach.[44] The *Alley* court reached a conclusion by merely interjecting figures into its previous second prong analysis.[45] Here, the sellers had rented two of the trailers for $140 each per month.[46] "At a combined rental income of $280 per month, seven months' vacancy would have resulted in an approximate loss of $2000," which was the liquidated damage sum.[47] On these facts, the court found a connection between the provision and the actual damages that could flow from breaching the contract for sale.

Failing to satisfy any of the three prongs of the enforceable liquidated damage test will deem the provision a penalty—rendering it unenforceable. This test is designed to ferret out the true intent of the parties' purpose for including a provision. The courts' process of determining intent in this context is similar to applying contract interpretation principles. If at all possible, courts will effectuate the mutual intent of the parties.[48] Though form and language of the contract will also be considered, language alone is not dis-

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40. *Id.*, 599 S.W.2d at 741.

41. *See id.* at 265, 599 S.W.2d at 741.

42. *Id.*, 599 S.W.2d at 741. The court also considered it likely that the number of potential offers would be reduced based on the sellers' attempts to bundle three mobile homes in one sale. *Id.*, 599 S.W.2d at 741.

43. *Id.* at 265, 599 S.W.2d at 741.

44. Note that

> [t]his last qualification is important, since in many cases at the time of the breach it is apparent that the liquidated damages rate is too high or too low in relation to the owner's actual damages. The owner in fact may have no actual damages at all stemming from the delayed completion.

AXELROTH ET AL., *supra* note 8, at 263.

45. *See Alley*, 269 Ark. at 265, 599 S.W.2d at 741.

46. *Id.*, 599 S.W.2d at 741.

47. *Id.*, 599 S.W.2d at 741.

48. *See* McIlvenny v. Horton, 227 Ark. 826, 829, 302 S.W.2d 70, 72 (1957); Reed v. Wright, 270 Ark. 45, 51, 603 S.W.2d 422, 426 (Ark. Ct. App. 1980).

positive.[49] Inclusion of the words *liquidated damages* or *penal sum* are not controlling.[50] Additionally, any ambiguity "will be resolved against the [party] whose form was used."[51] If a liquidated damage provision is deemed enforceable, it is necessary to inquire into each individual party's fault.

B. Development of the Apportionment Rule

Apportionment is the idea that a party seeking to enforce a liquidated damage provision may only recover such damages for which it is not proportionally responsible.[52] As early as 1883, United States courts recognized apportionment as an appropriate means of addressing liability for parties' mutual construction delay.[53] At the time, however, the idea was a significant departure from English common law and only adopted by a few jurisdictions.[54]

Historically, courts resisted apportionment because of "early judicial hostility to the use of privately agreed upon contract damage remedies."[55] This and other underlying policies have eroded over time, resulting in widespread acceptance of apportionment in many jurisdictions.[56] Today, nearly

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49. *See* Robbins v. Plant, 174 Ark. 639, 297 S.W. 1027 (1927); Johnson v. Jones, 33 Ark. App. 149, 152, 807 S.W.2d 39, 42 (1991).

50. *See In re* Lammers, 211 F. Supp. 448, 449 (E.D. Ark. 1962) (use of "liquidated damages" not controlling); Lasater v. W. Clay Drainage Dist., 177 Ark. 997, 8 S.W.2d 502, 503 (1928) (parties' intention is controlling); Montague v. Robinson, 122 Ark. 163, 163, 182 S.W. 558, 559 (1916) (use of "penal sum" not controlling).

51. Hall v. Weeks, 214 Ark. 703, 707, 217 S.W.2d 828, 830 (1949).

52. *See* BLACK'S LAW DICTIONARY, *supra* note 17, at 116.

53. *See* Tex. & St. L. Ry. Co. v. Rust, 19 F. 239 (E.D. Ark. 1883). Interestingly enough, *Rust* bore a strong resemblance to *San Ore-Gardner*. In *Rust*, a railroad sued a contractor for breaching a contract to construct a railroad bridge across the Arkansas River. *Id.* at 239. After completing the enforceable liquidated damage provision analysis, the court held that "[i]f the plaintiff directed the defendants to . . . do work on the bridge not covered by the contract, . . . then it must be implied that both parties consented to such an extension of time as was necessary or reasonable for making such . . . changes." *Id.* at 245 (citing Mfg. Co. v. United States, 84 U.S. 592 (1873)). In *Rust*, "the time at which the [stipulated sum] was to commence to accrue under the contract would be postponed" by whatever additional duration the agreed to change would have taken to complete. *Id.*

54. *See* J.E. Macy, Annotation, *Liability of Building or Construction Contractor for Liquidated Damages for Breach of Time Limit Where Work Is Delayed by Contractee or Third Person*, 152 A.L.R. 1349 (1944).

55. E.C. Ernst, Inc. v. Manhattan Constr. Co. of Tex., 551 F.2d 1026, 1038–39 (5th Cir. 1977) (citing Mosler Safe Co. v. Maiden Lane Safe Deposit Co., 93 N.E. 81, 83 (N.Y. 1910)) ("While such an agreement has not the harshness of a penalty, it is, nevertheless, in its nature, such that its enforcement, where the party claiming the right to enforce has, in part, been the cause of delay, would be unjust.").

56. *See* Macy, *supra* note 54, at 1349. Though the differences in the effects of all apportionment theories appear to be negligible, upon closer review, the subtle nuances of each variation may seem confusing. One approach may be to extend the term of the contract based

all jurisdictions adhere to one of three prevailing rules that address apportionment.

The traditional view is one of no-apportionment. Jurisdictions following this rule will not enforce a liquidated damage provision when the party seeking enforcement has contributed to the delay.[57] An early line of cases illustrating the rule's development begins with *Weeks v. Little*,[58] an 1882 New York case. In *Weeks*, the New York Court of Appeals found no merit in a contractor's argument that its delay was caused by the delay of another contractor working for the same owner.[59] The court refused to enforce the provision, stating that it could not divide and apportion the fault.[60] The New York line continued to develop, with *Mosler Safe Co. v. Maiden Lane Safe Deposit Co.*[61] marking the significant shift into twentieth century jurisprudence. In *Mosler*, the same New York court reiterated its previous holding in *Weeks* by refusing to apportion liquidated damages.[62] However, the court left open the possibility of apportionment when expressly stated within the contract.[63]

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on the delay by the contractee whereas another may be to divide them more traditionally based on the exact number of days of delay attributable to each party. *See* 2 STEVEN G.M. STEIN, CONSTRUCTION LAW ¶ 6.10[3], at 6-41 to -42 (Lexis Nexis Matthew Bender 2010).

57. *See* United States v. United Eng'g & Constructing Co., 234 U.S. 236 (1914); United States v. Kanter, 137 F.2d 828 (8th Cir. 1943); San Ore-Gardner v. Mo. Pac. R.R. Co., 496 F. Supp. 1337 (E.D. Ark. 1980), *aff'd*, 658 F.2d 562 (8th Cir. 1981); Glassman Constr. Co. v. Md. City Plaza, Inc., 371 F. Supp. 1154 (D. Md. 1974); Peter Kiewit Sons' Co. v. Pasadena City Junior Coll. Dist. of L.A. Cnty., 379 P.2d 18 (Cal. 1963); State *ex rel.* Smith v. Jack B. Parson Constr. 456 P.2d 762 (Idaho 1969); City of Houma v. C-Well Ltd., 515 So. 2d 646 (La. Ct. App. 1987); Peabody N.E., Inc. v. Town of Marshfield, 689 N.E.2d 774 (Mass. 1998); Intertherm, Inc. v. Structural Sys., Inc., 504 S.W.2d 64 (Mo. 1974); Haggerty v. Selsco, 534 P.2d 874 (Mont. 1975); Utica Mut. Ins. Co. v. DiDonato, 453 A.2d 559 (N.J. Super. Ct. App. Div. 1982); Corinno Civetta Constr. Corp. v. City of New York, 493 N.E.2d 905 (N.Y. 1986); L.A. Reynolds Co. v. State Highway Comm'n, 155 S.E.2d 473 (N.C. 1967); Lee Turzillo Contracting Co. v. Frank Messer & Sons, Inc., 261 N.E.2d 675 (Ohio Ct. App. 1969); V.L. Nicholson Co. v. Transcon Inv. & Fin. Ltd., 595 S.W.2d 474 (Tenn. 1980); Shintech, Inc. v. Grp. Constructors, Inc., 688 S.W.2d 144 (Tex. Ct. App. 1985); Higgins v. City of Fillmore, 639 P.2d 192 (Utah 1981).

58. Weeks v. Little, 89 N.Y. 566 (1882).

59. *Id.* at 569–70.

60. *Id.* at 570.

61. Mosler Safe Co. v. Maiden Lane Safe Deposit Co., 93 N.E. 81 (N.Y. 1910).

62. *Id.* at 82–84.

63. Specifically, the court stated,

> It was competent for the parties, anticipating mutations of mind and conditions, to have provided against forfeiture of the right to liquidated damages by further agreeing that . . . if the contractor was delayed in his work in certain specified events, or by causes specified. With such a provision, the obligation to pay liquidated damages might be preserved and its commencement deferred to a substituted date. Without such a provision, where, by the mutual fault of the parties,

Unlike the traditional view, the modern view supports apportioning liquidated damages for mutual delay in construction contracts. Some jurisdictions have flatly rejected the traditional view.[64] In *E.C. Ernst, Inc. v. Manhattan Construction Co.*, the Fifth Circuit Court of Appeals concluded that Alabama courts would permit apportionment by using the *Mosler* court's policy justifications against the application of the no-apportionment rule: "The opposing rule is an old one whose underlying policies do not remain in full force."[65] In between the two extremes lies a third approach. This approach enforces a liquidated damage provision if a court is able to determine a basis for apportionment.[66]

III. PROBLEMS

Courts rejecting the apportionment rule must deal with numerous problems that may arise as a result of that rejection. Some of those problems may stem from inherent problems in justifying the application of the no-apportionment rule rather than the repercussions of applying the rule itself. Three primary problems that courts rejecting apportionment face include contravening public policy of the forum state, conflicting with the freedom of contract, and hampering judicial efficiency.

> the contractor's original obligation has been put alend to, how could he come under a new obligation to pay the liquidated damages from some subsequent date? *Such an obligation could not be renewed except by some express agreement*.

Id. at 83–84 (emphasis added).

64. *See* E.C. Ernst, Inc. v. Manhattan Constr. Co. of Tex., 551 F.2d 1026, 1038 (5th Cir. 1977); Aetna Cas. & Sur. Co. v. Butte-Meade Sanitary Water Dist., 500 F. Supp. 193 (D.S.D. 1980).

65. *E.C. Ernst, Inc.*, 551 F.2d at 1038. The court continued on to say, "[G]iven the increasing complexity of contractual relationships, liquidated damage provisions have obtained firm judicial and legislative support." *Id.* at 1039.

66. *See* United States *ex rel.* Thorleif Larsen & Son, Inc. v. B.R. Abbot Constr. Co., 466 F.2d 712 (7th Cir. 1972); Sw. Eng'g Co. v. United States, 341 F.2d 998 (8th Cir. 1965); Nomellini Constr. Co. v. California *ex rel* Dep't of Water Res., 96 Cal. Rptr. 682 (Ct. App. 1971); Wallis v. Inhabitants of Wenham, 90 N.E. 396 (Mass. 1910); Bedford-Carthage Stone Co. v. Ramey, 34 S.W.2d 387 (Tex. Civ. App. 1930); Alcan Elec. & Eng'g Co. v. Samaritan Hosp., 109 Wash. App. 1072 (2002) (unpublished opinion); Brashear v. Richardson Constr., Inc., 10 P.3d 1115 (Wyo. 2000); Keith v. Burzynski, 621 P.2d 247 (Wyo. 1980).

A. Public Policy

The public policy of a state is found in its constitution, statutes, and case law.[67] Revised Article 3 of the Uniform Commercial Code exemplifies the policy goal of achieving equitable results by apportioning loss between parties.[68] Additionally, comparative fault statutes reflect a policy goal of trying to achieve an equitable result by eliminating the "'all or nothing' rule[] of recovery . . . [of] contributory negligence" and instead apportioning fault by each party's own degree of liability.[69] States that have codified Revised Article 3 or comparative fault laws express a public policy that is at odds with a rule against apportioning liquidated damages. But because the Uniform Commercial Code is essentially a subset of contract law, bearing a closer relationship to liquidated damage law, the policy exemplified by Revised Article 3 will be discussed first.

1. *Article 3 of the Uniform Commercial Code*

Negotiable instruments are specialized or formal types of contracts.[70] Specific types of negotiable instruments include checks, notes, and bank drafts.[71] The drafters of the original Article 3 set out laws to govern transactions involving negotiable instruments.[72]

When the original Article 3 was promulgated in 1952, it was based upon a paper payment system.[73] Around that time, approximately seven billion checks were processed annually.[74] By the late 1980s, the volume increased to forty-eight billion annually.[75] The American Law Institute revised Article 3 in 1990 to accommodate changing business practices and modern technologies, as well as to address problems with lack of clarity and certainty that resulted from an evolving business landscape.[76] The drafters

67. *See* Vincent v. Prudential Ins. Brokerage, 333 Ark. 414, 417–18, 970 S.W.2d 215, 217 (1998) (citing Wal-Mart Stores, Inc. v. Baysinger, 306 Ark. 239, 812 S.W.2d 463 (1991)).

68. *See* discussion *infra* Part III.A.1.

69. *See* Michael B. Gallub, Note, *A Compromise Between Mitigation and Comparative Fault?: A Critical Assessment of the Seat Belt Controversy and a Proposal for Reform*, 14 HOFSTRA L. REV. 319, 334 (1986).

70. 24 WILLISTON & LORD, *supra* note 6, § 2.21, at 224; *see also* RESTATEMENT (SECOND) OF CONTRACTS, *supra* note 18, § 6.

71. U.C.C. § 3-104 (12th ed. 1990); BLACK'S LAW DICTIONARY, *supra* note 17, at 1136.

72. *See* U.C.C., *supra* note 71, § 3-102.

73. *Id.* art. 3 Prefatory Note, at 325.

74. *Id.*

75. *Id.*

76. *Id.*

sought to benefit public interest by attempting to reduce litigation involving negotiable instruments.[77]

The drafters revised sections 3-404 through 3-406 so that fault could be allocated based on each party's respective fault.[78] Generally, in instances of fraud involving negotiable instruments, "the person bearing the loss may recover from the person failing to exercise ordinary care *to the extent* the failure to exercise ordinary care contributed to the loss."[79] Prior to the 1990 revision, original Article 3 did not allocate fault.[80] In addition to the text itself, the states that adopted revised Article 3 also adopted the policy behind those revisions—courts should allocate fault when multiple parties are responsible for breaking a contract.

2. *Comparative Fault*

Traditionally, tort and contract law are considered completely distinct bodies of substantive law. Some would say blending principles from tort into contract, or vice versa, is impossible based on the traditional premise alone.[81] Today, however, courts consistently cross historical boundaries between the bodies of law, blurring lines that were once clearly defined. For instance, a plaintiff's own negligence can substantially impact damages recoverable for breach of contract.[82] A second application of tort principles to contract law is courts allowing emotional distress claims to be considered contemporaneously with damages for breach.[83] Yet another is when fraud induces breach of contract and courts award punitive damages.[84] Although many critics will continue to resist the application of tort principles to contract law, evidence of modern American courts applying such principles cuts away at that resistance.

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77. *Id.* at 328. "By clarification of troublesome issues, and by the provisions of Sections 3-404 through 3-406[,] which reform rules for allocation of loss from forgeries and alterations, the Revision should significantly reduce litigation." *Id.*

78. *See* U.C.C., *supra* note 71, §§ 3-404 to -406.

79. *Id.* § 3-404(d) (emphasis added). Slightly different language is used in section 3-406: "[T]he loss is allocated between the person precluded and the person asserting the preclusion according *to the extent* to which the failure of each to exercise ordinary care contributed to the loss." *Id.* § 3-406(b) (emphasis added).

80. *See id.* app. VII, §§ 3-404 to -406, at 1231–42.

81. *See* Lesmeister v. Dilly, 330 N.W.2d 95, 101–02 (Minn. 1983).

82. 57B AM. JUR. 2D *Negligence* § 913 (1989).

83. *See* Volkswagen of Am., Inc. v. Dillard, 579 So. 2d 1301 (Ala. 1991); *see also* Salka v. Dean Homes of Beverly Hills, Inc., 22 Cal. Rptr. 2d 902 (Ct. App. 1993), *superseded by* 864 P.2d 1037 (Cal. 1993).

84. Edens v. Goodyear Tire & Rubber Co., 858 F.2d 198 (4th Cir. 1988); Welborn v. Dixon, 49 S.E. 232 (S.C. 1904) (representing one of the earliest applications of punitive damages for breach of contract).

The concept of negligence first appeared in the early nineteenth century.[85] This relatively recent addition of a means of establishing liability in tort took hundreds of years to develop, the major hurdle being the unwillingness of old English courts to depart from the intentional-unintentional standard.[86] The unwillingness eroded over time.[87]

Once the doctrine of negligence became established as more than a passing fad, common law defenses to such claims began to arise. In *Butterfield v. Forrester*,[88] a man riding his horse on a public road collided with a pole that had been left there by another.[89] The rider sustained significant injuries and brought suit against the man who left the pole in the road.[90] At the end of the trial, the judge instructed the jury, "[I]f a person riding with reasonable and ordinary care could have seen and avoided the obstruction; and if . . . the plaintiff was riding along the street extremely hard, and without ordinary care, [you] should find a verdict for the defendant."[91] After the jury returned a verdict in favor of the defendant, the plaintiff appealed.[92] On appeal, Lord Ellenborough authored the unanimous affirming opinion of the court that would become known as the first exposition of the concept of contributory negligence in modern era tort law: "One person being in fault will not dispense with another's using ordinary care for himself. Two things must concur to support this action, an obstruction in the road by the fault of the defendant, and no want of ordinary care to avoid it on the part of the plaintiff."[93]

Contributory negligence quickly gained enduring popularity in the United States.[94] However, strict application yielding harsh results chipped away at the traditional contributory negligence doctrine, which barred all claims for any fault.[95] The next chapter in this era gave rise to limitations like last clear chance and assumption of risk.[96] This law evolved with the help of railroad cases.[97] The deep pockets of railroads made them vulnerable

85. W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 28, at 160–61 (5th ed. 1984).

86. *See* Ernest A. Turk, *Comparative Negligence on the March*, 28 CHI.-KENT L. REV. 189 (1950).

87. "Action upon the case for negligence" and "case for negligence" became common expressions in mid-eighteenth century cases. *See, e.g.*, Aston v. Heaven, (1797) 170 Eng. Rep. 445 (C.P.) 446; 2 Esp. 533, 535.

88. Butterfield v. Forrester, (1809) 103 Eng. Rep. 926 (K.B.); 11 East 60.

89. *Id.* at 926; 11 East at 60.

90. *Id.*; 11 East at 60.

91. *Id.* at 927; 11 East at 60.

92. *See id.* at 926–27; 11 East at 60–61.

93. *Id.* at 927; 11 East at 61.

94. HENRY WOODS & BETH DEERE, COMPARATIVE FAULT § 1:4 (3d ed. 1996).

95. *See, e.g.*, Smithwick v. Hall & Upson Co., 21 A. 924 (Conn. 1890).

96. WOODS & DEERE, *supra* note 94, §§ 1:6–1:8, at 9–13.

97. *See, e.g.*, Herbert v. S. Pac. Co., 53 P. 651 (Cal. 1898).

to sympathetic juries in personal injury actions; applying the rigid doctrine would oftentimes require courts to overturn jury verdicts for plaintiffs.[98] This gave rise to Congress's codification of a comparative fault statute in 1908.[99]

Early, or pure, forms of comparative fault allowed plaintiffs to recover from negligent tortfeasors, regardless of their own degree of negligence.[100] Eventually, this pure form developed into what is now commonly known as modified comparative fault.[101] Under this system, a plaintiff can only recover when his level of negligence is less than the defendant's.[102] Today, all but four states have adopted some type of comparative fault doctrine, evidencing the public preference for equitable results.[103]

Forty-six states recognize the comparative fault doctrine.[104] For those states, the idea that inadvertent fault, no matter how little, can preclude just recovery for an aggrieved party is gone. Everyone can recover their fair share; that is, fault can be apportioned to achieve the most equitable result for all involved.

B. Freedom of Contract

"There is no reason why parties competent to contract may not agree that certain elements of damage difficult to estimate shall be covered by a provision for liquidated damages and that other elements shall be ascertained in the usual manner."[105] Recognizing that freedom of contract represents a pillar of contract remedies,[106] judicial encouragement of that principle has held a hallowed status throughout American legal history.[107] With respect to liquidated damages, this status has resulted in widespread enforcement of such provisions, so long as they were not deemed to be a penalty.[108] "The [judiciary's] emphasis on the parties' freedom of contract often

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98. *Id.*

99. *See* 46 U.S.C. § 766 (1920) (current version at 46 U.S.C. § 30304 (2006)).

100. *See* Carol A. Mutter, *Moving to Comparative Negligence in an Era of Tort Reform: Decisions for Tennessee*, 57 TENN. L. REV. 199, 245–50 (1990). Mississippi was one of two southern states that pioneered comparative fault, adopting a pure comparative fault statute in 1910. *See* MISS. CODE ANN. § 11-7-15 (Supp. 2011).

101. *See* Mutter, *supra* note 100, at 245–50.

102. *See id.*

103. WOODS & DEERE, *supra* note 94, § 1:11, at 19–25.

104. *Id.*

105. J.E. Hathaway & Co. v. United States, 249 U.S. 460, 464 (1919).

106. Larry A. Dimatteo, *A Theory of Efficient Penalty: Eliminating the Law of Liquidated Damages*, 38 AM. BUS. L.J. 633, 639 (2001).

107. Susan V. Ferris, Note, *Liquidated Damages Recovery Under the Restatement (Second) of Contracts*, 67 CORNELL L. REV. 862, 863 (1982).

108. *Id.*

resulted in upholding liquidated damage clauses where little or no damage actually occurred."[109]

In *United States v. Bethlehem Steel Co*.,[110] the Supreme Court upheld a liquidated damages clause on the basis of freedom of contract. Pursuant to a wartime contract, Bethlehem Steel agreed to manufacture and sell gun carriages to the United States over a limited amount of time.[111] Since the gun carriages were vital to aid the government in its war efforts, the parties contracted to give effect to a liquidated damage provision.[112] Despite the war's end, the government sought to enforce the liquidated damage clause when Bethlehem Steel failed to deliver the guns on time.[113]

The Supreme Court examined the government's and Bethlehem Steel's intent at the time of contracting and determined that the clause was a fair estimate of the harm that might have resulted from the failure to deliver in a timely manner.[114] Accordingly, the Court held that the clause was valid and enforceable despite the lack of actual damage.[115] This holding evidenced the importance of freedom to contract.

Despite the Supreme Court's enforcement of liquidated damage provisions, many other state courts continued to express hostility towards those provisions during the early twentieth century. Most of the hostility stemmed from a disparity in contracting parties' bargaining power.[116] Powerful parties often abused that imbalance to their advantage.[117] But as contract law continued to develop, obligations of good faith and fair dealing became facets of American common law jurisprudence.[118] With these doctrines as the backdrop of modern contract law, critics no longer need to be overly concerned with zealously protecting the rights of the vulnerable when considering whether to apportion liquidated damages. Courts may still address infirmity in a party's bargaining power when choosing to enforce a liquidated damage provision; however, once that provision passes judicial muster, refusing to apportion those damages where mutual fault is encountered conflicts with the freedom of contract.

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109. *Id.* at 864 (citing Ellicott Mach. Co. v. United States, 43 Ct. Cl. 232 (1908); Byron Jackson Co. v. United States, 35 F. Supp. 665, 667 (S.D. Cal. 1940)).
110. 205 U.S. 105 (1907).
111. *Id.* at 119.
112. *Id.* at 119–20.
113. *See id.*
114. *Id.*
115. *Id.* at 121–22.
116. *See* 11 PERILLO, *supra* note 21, § 58.3, at 402–03.
117. *See id.*
118. *See* 17A AM. JUR. 2D *Contracts* § 370 (1989).

C. Judicial Efficiency

Numerous judicial justifications support the apportionment rule of liquidated damages, including preserving valuable judicial resources:

> The modern trend is to look with candor, if not with favor, upon a contract provision for liquidated damages when entered into deliberately between parties who have equality of opportunity for understanding and insisting upon their rights, since an amicable adjustment in advance of difficult issues saves the time of courts, juries, parties, and witnesses and reduces the delay, uncertainty, and expense of litigation.[119]

These notions of judicial efficiency are further supported by the no-apportionment rule's already existing effects. "[C]ourts have held that the rule against apportionment bars only the owner's right to rely upon a liquidated damage provision, but does not prevent the owner from proving and recovering actual damages resulting from contractor-caused delays."[120] So, the courts rejecting apportionment still have to endure the tedious, lengthy, and costly process of parties proving actual damages anyway.

The idea that determining actual damages is somehow easier than apportioning liability is a fiction. In the construction context, the sheer number of parties that may affect timely performance—owner, architect, engineer, government regulators, permitting agencies, prime and subcontractors, suppliers, etc.—shows the inadequacy of a rule that refuses to apportion fault. As difficult as it may be to apportion delay, the time and expense of litigation justifies courts' attempts to do so.

IV. PROPOSAL

Arkansas courts should adopt the apportionment rule of liquidated damages, especially when dealing with mutual delay in construction litigation, to remedy the potential problems they face as a result of the current state of the law. What many practitioners consider to be the seminal Arkansas case that stands for the rule against apportionment is non-binding federal authority.[121] Furthermore, the analysis that was used to arrive at that conclusion is flawed—the legal bases are infirm.[122]

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119. Gorco Constr. Co. v. Stein, 99 N.W.2d 69, 74 (Minn. 1959) (citing Wise v. United States, 249 U.S. 361 (1919); Meuwissen v. H.E. Westerman Lumber Co., 16 N.W.2d 546 (Minn. 1944); RESTATEMENT (FIRST) OF CONTRACTS § 339 cmt. c (1932)).

120. *See* 2 STEIN, *supra* note 56, ¶ 6.10[3], at 6-42; *see also supra* Part III.A.1.

121. *See* San Ore-Gardner v. Mo. Pac. R.R. Co., 496 F. Supp. 1337 (E.D. Ark. 1980), *aff'd*, 658 F.2d 562 (8th Cir. 1981).

122. *See infra* Part IV.B.1.

Arkansas courts can rest assured that adopting the apportionment rule is supported by ample case law from other jurisdictions that follow the modern view of apportionment.[123] Furthermore, Arkansas public policy supports apportionment. The following case analysis demonstrates the suitability of the doctrine in Arkansas law.

A. *S.O.G.-San Ore-Gardner v. Missouri Pacific Railroad Co.*

On June 19, 1967, the United States government entered into a contract with Missouri Pacific Railroad Company ("Missouri Pacific") to modify the Benzal Bridge.[124] Pursuant to the terms of that contract, Missouri Pacific issued invitations to bid on the construction project to numerous contractors, and ultimately accepted San Ore-Gardner's (S.O.G.) bid on November 5, 1968.[125]

The Missouri Pacific/S.O.G. contract called for separating construction into three separate stages.[126] Two new piers were to be constructed during the substructure stage, a portion of the existing bridge was to be replaced during the changeover stage, and final adjustments to the replacement section of the bridge along with removal of an old pier were to be completed during the superstructure phase.[127] Among other material terms, "[t]he contract contained . . . a provision for liquidated damages of $600 per day if performance of the contract was not completed within the time period specified."[128]

Originally, the term for completion was set at 660 days.[129] Later, it was extended to 1122 days—equating to a completion date of March 5, 1972.[130] S.O.G. actually completed the bridge modifications on July 18, 1974—over two years beyond the contractual deadline.[131]

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123. *See infra* Part IV.B.2.

124. *San Ore-Gardner*, 496 F. Supp. at 1339.

125. *Id.*

126. *Id.* at 1340–41.

127. *Id.* The existing bridge was one that had a central portion that would rotate ninety degrees to allow boat traffic to pass. *Delta Heritage Trail: Arkansas State Parks*, ARK. DEP'T OF PARKS & TOURISM, http://www.arkansasstateparks.com/photo-gallery (select "Delta Heritage Trail State Park" from drop-down list) (last visited, Apr. 4, 2013) (though not the Benzal Bridge, this bridge is a swing bridge, rotating on the central pier pictured). That rotating portion was to be replaced with a section that would elevate instead. *San Ore-Gardner*, 496 F. Supp. at 1341; *see also* Pat Rawls, *Capture Arkansas Photo Contest*, ARK. DEMOCRAT-GAZETTE (July 3, 2010, 8:21 AM), http://www.capturearkansas.com/photos/53029 (recent photograph of Benzal Bridge).

128. S.O.G.-San Ore-Gardner v. Mo. Pac. R.R. Co., 658 F.2d 562, 564 (8th Cir. 1981).

129. *San Ore-Gardner*, 496 F. Supp. at 1344.

130. *Id.*

131. *S.O.G.-San Ore-Gardner*, 658 F.2d at 564.

The reasons for the two-plus year delay were not attributable to any single act or omission by one party. However, the significant sources of delay were easily ascertainable. S.O.G. admitted to a year's delay in completing the substructure stage alone, and evidence also suggests that it probably was responsible for more.[132] But Missouri Pacific was not without fault. The district court found that Missouri Pacific offered "[n]o satisfactory explanation . . . for its failure to promptly transmit" reports that S.O.G. submitted for approval to the Army Corps of Engineers.[133] Despite contributing to the delay, the proportion for which Missouri Pacific was responsible was far less than S.O.G.'s fault.[134]

As the construction process came to a close, Missouri Pacific retained funds that were due to S.O.G. because of S.O.G.'s delay and defective work.[135] Additionally, $70,000 was withheld "for noise in the bearings of the lift mechanism" of the new railroad bridge.[136] These and other difficulties led to litigation.[137]

Although S.O.G. alleged multiple claims against Missouri Pacific,[138] at the crux of the parties' dispute was whether the liquidated damage provision of the contract was enforceable.[139] In June 1980, after a week-long trial in the United States District Court for the Eastern District of Arkansas, Judge Elsijane Trimble Roy concluded "that both sides were at fault to some extent."[140]

After a lengthy and detailed discussion of the facts, Judge Roy held that the liquidated damage provision of the contract was unenforceable, not because both parties were at fault, but because the $600 per day figure "was not the subject of negotiation" and Missouri Pacific offered no "rational

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132. *San Ore-Gardner*, 496 F. Supp. at 1346.

133. *Id.* at 1347. S.O.G. "discovered that [Missouri Pacific] had not mailed the . . . report to the Corps of Engineers until . . . over three months after receipt from S.O.G." *S.O.G.-San Ore-Gardner*, 658 F.2d at 568–69. This left S.O.G. at a veritable standstill until the Corps of Engineers responded to the forwarded report. *See id.*

134. The district court highlighted several of S.O.G.'s defects that were "clearly reflected in the record." *San Ore-Gardner*, 496 F. Supp. at 1347–48 (failing to install an adequate emergency power system after being directed to do so; failing to address operations of the bridge during construction, which were caused by movement of the piers; taking twice the time to complete construction of the cofferdams).

135. *Id.* at 1350.

136. *Id.*

137. *See id.* at 1339 (S.O.G. filed its amended complaint on January 8, 1975, and Missouri Pacific filed a third party complaint against S.O.G.'s insurer on February 17, 1977).

138. Most of these claims could be characterized as breach of contract claims or declaratory judgments. *See id.* at 1340.

139. *Id.* (S.O.G. contended that the provision was unenforceable, while Missouri Pacific sought enforcement of the $600 per day clause).

140. *San Ore-Gardner*, 496 F. Supp. at 1340.

basis for its choice of [that figure] . . . as damages for delay."[141] Instead of stopping there, arguably in dicta, the court delved into an analysis of liquidated damage law:

> Where the party who is seeking to enforce a liquidated damages provision of a contract is responsible for the failure to perform or *has contributed in part to it*, the liquidated damages provision will not be enforced. We recognize that some jurisdictions allow apportionment but the better rule seems to be that where delays are occasioned by the mutual fault of the parties, the Court will not attempt to apportion but will refuse to enforce the provision for liquidated damages.[142]

The court refused to enforce the provision for either party because, in its view, doing so would result in an injustice.[143]

S.O.G. appealed the "portion of the judgment denying it damages from the delay caused by" factors allegedly beyond its control.[144] The United States Court of Appeals for the Eighth Circuit affirmed the district court's holding, but not before it too expounded upon the district court's discussion of Arkansas liquidated damage law.[145]

Just as the district court did, the court provided a comprehensive list of authorities on both sides of the issue while addressing Missouri Pacific's pro-apportionment argument.[146] Unlike the district court, however, the Eighth Circuit cited *City of Whitehall v. Southern Mechanical Contracting, Inc.*,[147] an Arkansas Court of Appeals opinion issued in 1980, for the proposition that "Arkansas ha[d] *apparently* retained the rule against apportionment."[148] Recognizing the import of the district court's decision, the Eighth Circuit attempted to clarify that court's basis of denying apportionment: "The district court denied apportionment based more upon the interrelatedness of the parties' delays than upon its reading of Arkansas law."[149] Lending its support to this apparent foundation of Arkansas law, the court af-

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141. *Id.* at 1348–49.

142. *Id.* at 1349 (emphasis added) (internal citations omitted). The court continued its analysis, recognizing that some jurisdictions that allow apportionment apply the rule only where "apportionment could feasibly be made." *Id.* The court did not cite to any Arkansas state court opinions throughout any of this analysis.

143. *Id.* at 1350. The court also awarded S.O.G. the $70,000 payment retained by Missouri Pacific and ordered Missouri Pacific to return all sums wrongfully withheld for S.O.G.'s delays. *Id.*

144. S.O.G.-San Ore-Gardner v. Mo. Pac. R.R. Co., 658 F.2d 562, 565 (8th Cir. 1981).

145. *Id.* at 569–70 (agreeing "that the Railroad should be precluded from recovering the liquidated damages for delay of performance").

146. *See id.* at 570–71.

147. 269 Ark. 563, 599 S.W.2d 430 (Ct. App. 1980).

148. *S.O.G.-San Ore-Gardner*, 658 F.2d at 571 (emphasis added) (citing *City of Whitehall*, 269 Ark. at 571, 599 S.W.2d at 435).

149. *Id.*

firmed not only the district court's judgment, but also its "conclusion to deny apportionment of liquidated damages."[150]

B. All Factors Point Toward Adoption of the Apportionment Rule

The Eighth Circuit decided *S.O.G.-San Ore-Gardner v. Missouri Pacific Railroad Co.* without any on-point Arkansas authority to support its holding.[151] In what should have been limited to a clear question and answer of whether a liquidated damage provision was an unenforceable penalty,[152] the court affirmed the district court's holding in its entirety.[153] The Eighth Circuit's decision rejected established Arkansas liquidated damage law and contradicted the state's public policy.

1. *The Federal Court's Dicta Rejecting Apportionment Is Not Supported by Arkansas Law*

In *S.O.G.-San-Ore Gardner*, the Eighth Circuit's contention that an Arkansas court had "apparently retained the rule against apportionment" is unfounded.[154] In *City of Whitehall v. Southern Mechanical Contracting, Inc.*, a municipality appealed a judgment in favor of a contractor who had brought suit against the city for unpaid funds under a construction contract.[155] The city, in turn, counter-claimed for liquidated damages.[156] Pursuant to the contract, the contractor was to install a new "sewer treatment pond and five sewage pump stations."[157] Before construction was completed, the city fired the contractor and sought to enforce the liquidated damage provision after a replacement contractor finished the work.[158] After analyzing the circumstances of the case, the Arkansas Court of Appeals determined that the city could not enforce the liquidated damage provision against the contractor because the city waived its right to do so when it fired the contractor before making the construction site available.[159]

Nothing in the opinion indicated that the contractor contributed to the city's delay in making the construction site available. The only delays were

150. *Id.*
151. *See id.* at 570–71.
152. Obviously, S.O.G. would have prevailed even if the holding was limited to this alone. No reasonable argument could be made to show that the clause was not a penalty.
153. *S.O.G.-San Ore-Gardner*, 658 F.2d at 571.
154. *Id.* (citing City of Whitehall v. S. Mech. Contracting, Inc., 269 Ark. 563, 599 S.W.2d 430 (Ct. App. 1980)).
155. *City of Whitehall*, 269 Ark. at 564, 599 S.W.2d at 431.
156. *Id.* at 564–65, 599 S.W.2d at 431.
157. *Id.*, 599 S.W.2d at 432.
158. *Id.* at 565–68, 599 S.W.2d at 431–34.
159. *Id.* at 571, 599 S.W.2d at 435.

no fault of the contractor—primarily, bad weather and an oil embargo.[160] In fact, the city was responsible for the very delays it was attributing to the contractor.[161] Thus, *City of Whitehall* does not support the Eighth Circuit's contention that Arkansas had adopted the no-apportionment rule.

2. *Apportionment Was and Still Is the Prevailing View*

In its opinion, the *S.O.G.-San Ore-Gardner* district court quickly endorsed the no-apportionment rule and cited numerous cases for support.[162] Arkansas state court cases were missing from this list entirely.[163] Nevertheless, the court stated that "[w]here the party who is seeking to enforce a liquidated damages provision of a contract is responsible for the failure to perform or has contributed [to] part [of] it, the liquidated damages provision will not be enforced."[164] But what seemed like a conclusive holding was put in doubt by the court's ensuing discussion of jurisdictions allowing apportionment along with applying facts of the instant case to that model.[165] Although the district court could have stopped its analysis after holding that the liquidated damage provision could not be enforced because it was a penalty, in the end, the lukewarm dismissal of the apportionment rule followed by an analysis of the rule anyway did not completely close the door on this issue.

Any opportunity to salvage the apportionment rule left by the district court was completely foreclosed on appeal by the Eighth Circuit. Although that court also agreed that the liquidated damage provision was really a pen-

160. *Id.* at 565–67, 599 S.W.2d at 431–33.

161. *City of Whitehall*, 269 Ark. at 565–67, 599 S.W.2d at 431–33 (among other things, instructing the contractor that a pump be moved to another location that had not yet been purchased by the city).

162. San Ore-Gardner v. Mo. Pac. R.R. Co., 496 F. Supp. 1337, 1349 (E.D. Ark. 1980), *aff'd*, 658 F.2d 562 (8th Cir. 1981).

163. *See id.* The court cited to a variety of cases from other jurisdictions, including *Peter Kiewit Sons' Co. v. Summit Construction Co.*, 422 F.2d 242 (8th Cir. 1969); *United States v. John Kerns Construction Co.*, 140 F.2d 792 (8th Cir. 1944); *United States v. Kanter*, 137 F.2d 828 (8th Cir. 1943); *Jefferson Hotel Co. v. Brumbaugh*, 168 F. 867 (4th Cir. 1909); *Investors Thrift Corp. v. Hunt*, 387 F. Supp. 517 (W.D. Ark. 1974), *aff'd*, 511 F.2d 1161 (8th Cir. 1975); *General Insurance Co. of America v. Commerce Hyatt House*, 85 Cal. Rptr. 317 (Ct. App. 1970); *Gogo v. Los Angeles County Flood Control District*, 114 P.2d 65 (Cal. Ct. App. 1941); and *Smith v. City of Tahlequah*, 245 P. 994 (Okla. 1926). Although these cases accurately describe the rule against apportionment, they offer no support for the adoption of that rule in Arkansas.

164. *San Ore-Gardner*, 496 F. Supp. at 1349 (citing *John Kerns Construction Co.*, 140 F.2d at 792; *Kanter*, 137 F.2d at 828). The court continued on to characterize that rule as "the better rule." *Id.*

165. *Id.* The court concluded that "[t]he construction work and delays of each of the parties were so interrelated that it would not be possible for the Court to attempt to break down and determine the number of days' delay for which each party was responsible." *Id.*

alty and therefore unenforceable, it also decided to weigh in on other arguments—only this time, the court purported to reach a definitive conclusion by citing Arkansas case law.[166] The court's holding proposed that Arkansas law rejects all forms of apportioning liquidated damages for delay in construction contracts.[167]

At the time *S.O.G.-San Ore-Gardner* was decided, adopting the apportionment theory of liquidated damages was the obvious next step to be taken in the evolution of the law. The Eighth Circuit minimized apportionment's acceptance by citing to only five jurisdictions that supported the rule.[168] To accurately capture the rule's presence across the United States, the court could have cited to at least thirteen jurisdictions, if not more, that had recognized the apportionment rule; many of those had been doing so since the turn of the century.[169]

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166. S.O.G.-San Ore-Gardner v. Mo. Pac. R.R. Co., 658 F.2d 562, 570–71 (8th Cir. 1981). "Because the Railroad's failure to timely forward the naval architect's report to the Corps of Engineers contributed to the delay in the changeover, we agree that the Railroad should be precluded from recovering the liquidated damages for delay of performance." *Id.* at 570. Unlike the district court's opinion, this court cited to authorities on both sides of the issue. For jurisdictions applying apportionment, the court cited *Dallas-Fort Worth Regional Airport Board v. Combustion Equipment Associates, Inc.*, 623 F.2d 1032 (5th Cir. 1980); *E.C. Ernst, Inc. v. Manhattan Construction Co. of Texas*, 551 F.2d 1026 (5th Cir. 1977), *reh'g denied*, *in part*, *reh'g granted*, *in part*, 559 F.2d 268, *cert. denied sub nom. Providence Hospital v. Manhattan Construction Co.*, 434 U.S. 1067 (1978); *United States ex rel. Thorleif Larsen & Son, Inc. v. B.R. Abbot Construction Co.*, 466 F.2d 712 (7th Cir. 1972); *Barnard-Curtiss Co. v. United States ex rel. D.W. Falls Construction Co.*, 257 F.2d 565 (10th Cir. 1958); and *Brecher v. Laikin*, 430 F. Supp. 103 (S.D.N.Y. 1977). *S.O.G.-San Ore-Gardner*, 658 F.2d at 570–71. For jurisdictions rejecting apportionment, in addition to the cases cited by the district court, the court cited *United States v. United Engineering & Contracting Co.*, 234 U.S. 236 (1914); *State ex rel. Smith v. Jack B. Parson Construction*, 456 P.2d 762 (Idaho 1969); *Haggerty v. Selsco*, 534 P.2d 874 (Mont. 1975); and most importantly, *City of Whitehall v. Southern Mechanical Contracting, Inc.*, 269 Ark. 563, 599 S.W.2d 430 (Ct. App. 1980). *S.O.G.-San Ore-Gardner*, 658 F.2d at 570–71. The court concluded with an attempt to clarify the district court's apparent confusion in Arkansas law:

> Arkansas has apparently retained the rule against apportionment. The district court denied apportionment based more upon the interrelatedness of the parties' delays than upon its reading of Arkansas law. Both the difficulty in delineation of fault and the apparent position of the Arkansas courts support the district court's conclusion to deny apportionment of liquidated damages.

Id. at 571 (citations omitted).

167. *See S.O.G.-San Ore-Gardner*, 658 F.2d at 571.

168. *See id.* at 570–71 (including Alabama, Illinois, New Mexico, Texas, and New York).

169. *See also* Sw. Eng'g Co. v. United States, 341 F.2d 998 (8th Cir. 1965); Aetna Cas. & Sur. Co. v. Butte-Meade Sanitary Water Dist., 500 F. Supp. 193 (D.S.D. 1980) (applying South Dakota law); Am. Eng'g Co. v. United States, 24 F. Supp. 449 (E.D. Pa. 1938) (applying federal common law); Hebert v. Weil, 39 So. 389 (La. 1905); Wallis v. Inhabitants of Wenham, 90 N.E. 396 (Mass. 1910); Jobst v. Hayden Bros., 121 N.W. 957 (Neb. 1909);

Among the jurisdictions recognizing apportionment, there are varied applications of the rule. The most common approach apportions damages when evidence indicating delay and the resultant expenses thereof can be clearly divided amongst all the parties involved in the litigation.[170] In the event a court cannot determine the proportions of responsibility, the provision will not be enforced. A less common approach hinges on the existence of a time extension clause:

> In building contracts, there is often inserted a provision giving the architect power to certify an extension of time in certain cases, by virtue of which the effect of a delay caused by the owner operates merely as an extension of the time for performance, and a new time is substituted for the old. In that event[,] though the owner causes [the] delay the builder is liable in liquidated damages, but the period of delay caused by the owner is deducted from the total delay. Unless the contract contains such a provision[,] the delay due to each party will not generally be apportioned.[171]

Other variations introduce good faith prerequisites.[172] Despite some of the nuanced approaches that some jurisdictions adopt, many still hold that "recovery should not be barred in every case by a rule of law that precludes examination of evidence."[173]

Since the Eighth Circuit decided *S.O.G.-San Ore-Gardner* in 1981, additional jurisdictions have adopted the apportionment rule of liquidated damages.[174] The Fifth Circuit offered several factors that may have served as motivation for both these and previous jurisdictions to adopt the apportionment rule: "[G]iven the increasing complexity of contractual relationships, liquidated damage provisions have obtained firm judicial and legislative support. . . . Generally, owners do not benefit from delays that they incur."[175] Arkansas courts should adopt the apportionment rule because it was the pre-

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Vanderhoof v. Shell, 72 P. 126 (Or. 1903); Pittsburg Iron & Steel Eng'g Co. v. Nat'l Tubeworks Co., 39 A. 76 (Pa. 1898); Williams v. Lewis N. Rosenbaum Co., 106 P. 493 (Wash. 1910).

170. *See* 2 STEIN, *supra* note 56, ¶ 6.10[3], at 6-41 to -42. This is the form the district court attempted to apply. San Ore-Gardner v. Mo. Pac. R.R. Co., 496 F. Supp. 1337, 1349 (E.D. Ark. 1980), *aff'd*, 658 F.2d 562, 564 (8th Cir. 1981).

171. 5 SAMUEL WILLISTON & WALTER H. E. JAEGER, A TREATISE ON THE LAW OF CONTRACTS § 789, at 765–66 (3d ed. 1961) (citations omitted).

172. E.C. Ernst, Inc. v. Manhattan Constr. Co., 551 F.2d 1026, 1039 (5th Cir. 1977) (stating that "[a]s long the owner's own delay is not incurred in in bad faith" apportionment would be allowed). Arguably, this is an implicit requirement in all apportionment jurisdictions.

173. *E.g.*, *id.*

174. *See* Airline Constr., Inc. v. Barr, 807 S.W.2d 247 (Tenn. Ct. App. 1990); Brashear v. Richardson Constr., Inc., 10 P.3d 1115 (Wyo. 2000) (extending apportionment rule to cover prime-sub contracts).

175. *E.C. Ernst, Inc.*, 551 F.2d at 1039.

vailing view when the Eighth Circuit affirmed *S.O.G.-San Ore-Gardner v. Missouri Pacific Railroad Co.* and it is still the prevailing view today.

3. *Arkansas's Public Policy Supports the Apportionment Rule*

The Arkansas General Assembly adopted revised Article 3 of the Uniform Commercial Code in 1991.[176] The Act specifically included revisions providing for apportionment of fault where more than one party was responsible—a marked change from the previous statute that completely precluded apportionment.[177] These laws, as originally enacted, continue to exist today. Additionally, Revised Article 3 has been adopted in forty-six states and the District of Columbia, illustrating the widespread consensus that apportionment is the better rule.[178]

Since enactment, courts applying those Arkansas negotiable instrument laws have enforced the provisions consistently—once again giving effect to the policy of equitable apportionment.[179] Any doubt as to whether Arkansas's public policy supports apportionment in contract actions can be cast aside by the Arkansas judiciary's recognition of those policies for over twenty years.

Apart from Arkansas statutory contract law, the public policy showing support for apportionment is evident through statutory tort law. Arkansas is one of the forty-six states that recognize the comparative fault doctrine of liability for negligence.[180] Interestingly, after Georgia, Mississippi, and Wisconsin, Arkansas was the fourth jurisdiction to adopt comparative fault.[181] Originally, Arkansas adopted the pure form of comparative fault.[182] After several years of difficulty applying the doctrine, the legislature amended the statute to reflect the more popular modified form.[183] Since then, the statute has been amended and revised several times but has never lost its main purpose—to ensure that all parties are treated as equitably as possible.[184]

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176. *See* Act of Mar. 15, 1991, No. 572, 1991 Ark. Acts 572 at sec. 9 (codified at ARK. CODE ANN. §§ 4-3-101 to -119 (Repl. 2001 & Supp. 2011)).

177. *See* ARK. CODE ANN. §§ 4-3-404 to -406 (Repl. 2001).

178. 2 PETER A. ALCES ET AL., UNIFORM COMMERCIAL CODE TRANSACTION GUIDE: ANALYSIS AND FORMS § 19:2 (4th ed. 1988).

179. *See, e.g.*, U.S. Fid. & Guar. Co. v. Bank of Bentonville, 29 F. Supp. 2d 553 (W.D. Ark. 1998); A.C.E., Inc. v. Inland Mortg. Co., 333 Ark. 232, 969 S.W.2d 176 (1998); Union Nat'l Bank of Little Rock v. Daneshvar, 33 Ark. App. 171, 803 S.W.2d 567 (1991).

180. WOODS & DEERE, *supra* note 94, § 1:11, at 20–25.

181. *Id.*

182. *See* Act of Mar. 14, 1955, No. 191, 1955 Ark. Acts 191 (repealed by Act of Mar. 27, 1957, No. 296, 1957 Ark. Acts 296).

183. *See* WOODS & DEERE, *supra* note 94, § 1:11, at 19–25 (explaining that through Act of Mar. 27, 1957, No. 296, 1957 Ark. Acts 296, the General Assembly adopted the modified form).

184. *See* WOODS & DEERE, *supra* note 94, § 1:11, at 19–25.

Regardless of Arkansas's comparative fault statute's form, it has embodied that equitable principle for over fifty years.[185] In 1981—the year the Eighth Circuit decided *S.O.G.-San Ore-Gardner v. Missouri Pacific Railroad Co.*—the concept had already been recognized for nearly twenty-five years.[186] The concepts behind comparative fault and apportionment of damages are so similar, many courts that have chosen to adopt the apportionment rule "are apportioning fault . . . by application of rules of comparative [fault]."[187]

Rejecting the apportionment rule of liquidated damages is at odds with Revised Article 3 and comparative fault's unhindered acceptance in Arkansas. Based on the clearly established public policy of the state, the federal courts should have decided to either abstain from deciding the apportionment issue or, alternatively, endorse apportionment as Arkansas law.

V. CONCLUSION

In August 1981, the United States Court of Appeals for the Eighth Circuit issued an opinion that marked an end to nearly ten years of litigation over the alteration of a bridge spanning the White River near Benzal, Arkansas. *S.O.G.-San Ore-Gardner v. Missouri Pacific Railroad Co.* established new precedent that effectively eliminated the possibility of enforcing liquidated damage provisions for delay in Arkansas construction contracts. The evidence at trial clearly indicated S.O.G.'s responsibility for a significant portion of the delay. However, the court precluded Missouri Pacific from enforcing a previously contracted liquidated damage provision because it too contributed to the delay, even though its contribution dwarfed in comparison to S.O.G.'s.[188]

Whether construction involves building the simplest of tract homes or the most complicated power generation plant, delay is both a universal concern and an inevitable reality that must be addressed.[189] The concept of liquidated damages—as it is known today—has been recognized and discussed

185. *See* 1955 Ark. Acts 191.

186. *See id.*

187. E.C. Ernst, Inc. v. Manhattan Constr. Co., 551 F.2d 1026, 1039 n.34 (5th Cir. 1977).

188. The lower court found that Missouri Pacific did not forward a report as quickly as it should have; despite S.O.G.'s self-admitted one-year delay, the court refused to allow Missouri Pacific to enforce, ultimately concluding that the three month delay was too "interwoven" with S.O.G.'s. S.O.G.-San Ore-Gardner v. Mo. Pac. R.R. Co., 658 F.2d 562, 568–69 (8th Cir. 1981).

189. *See, e.g.*, ENERGETICS INC., U.S. DEP'T OF ENERGY OFFICE OF NUCLEAR ENERGY, CONSTRUCTION CODES AND STANDARDS: AVOIDANCE OF NEW NUCLEAR POWER PLANT CONSTRUCTION DELAYS (2008).

by our courts for over one hundred years.[190] Much of the initial discussion centered on making a distinction between penalties and damages, ultimately resulting in the consensus that unless facially unreasonable, liquidated damage provisions would not be subject to judicial intervention and interpretation. From that point on, however, various jurisdictions began adding individual nuances that evolved into several species of liquidated damage law. Nearly fifteen years before the *S.O.G.-San Ore-Gardner v. Missouri Pacific Railroad Co.* decision, a national trend of fault apportionment began developing that could be applied generally without disrupting existing legal precedent.[191] This development helped effectuate the contracting parties' intent while addressing inequities that existed in the then current systems. Unfortunately, the *S.O.G-San Ore-Gardner* court chose not to adopt that trend.

The Eighth Circuit—and Arkansas courts applying the *S.O.G.-San Ore-Gardner* holding since—should not have concluded that any act contributing to the failure to meet contractual deadlines, notwithstanding a disproportionate level of corresponding fault, bars parties from enforcing a liquidated damage provision within a construction contract. Arkansas courts applying a no-apportionment rule to sophisticated commercial parties seeking enforcement of liquidated damage provisions for construction delay contravene the public policy of the state, as evidenced by its statutory negotiable instrument and comparative fault laws. Furthermore, the no-apportionment rule violates the fundamental freedom of contract. Finally, failing to apportion will consume valuable judicial resources, hamper efficiency, and increase costs of litigation for all parties involved.

All is not lost. Although *S.O.G.-San Ore-Gardner*'s no-apportionment rule is considered to be Arkansas law, it is not only non-binding precedent and mere dicta, but its origins are also infirm. In addition to being able to establish law without disturbing any binding authority, Arkansas courts may take comfort in the fact that by adopting an apportionment rule, they will be joining the modern approach that is supported by Arkansas public policy. The point of a liquidated damage provision is to improve certainty by allowing parties to allocate risk. Apportioning agreed-upon damages will give effect to the parties' wishes and avoid needless litigation—significantly reducing the burdens on both the judiciary and parties involved in the construction process.

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190. *See* Sun Printing & Publ'g Ass'n v. Moore, 183 U.S. 642, 660–74 (1902) (making a distinction between an unenforceable penalty and a liquidated damage provision which the parties contemplated while contracting).

191. In fact, the Eighth Circuit itself endorsed the newly developed theory in 1965. Sw. Eng'g Co. v. United States, 341 F.2d 998 (8th Cir. 1965).

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