**UNITED STATES BANKRUPTCY COURT**
**WESTERN DISTRICT OF NEW YORK**

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**In Re:**

**ALP Freddy's Limited Partnership,**

**Debtor(s).**

**CASE NO. 93-20542**

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**ALP Freddy's Limited Partnership,**

**Plaintiff(s),**

**A.P. NO. 95-2334**

**vs.**

**Wally Packaging, Inc.,**

**Defendant(s).**

**DECISION & ORDER**

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## BACKGROUND

On March 12, 1993, ALP Freddy's Limited Partnership, d/b/a Freddy's ("Freddy's") filed a petition initiating a Chapter 11 case. Both prior to and for a time after the filing of the petition, Freddy's operated a number of deep-discount health and beauty aid/pharmacy outlets in New York and Florida. After determining that it could not effectively reorganize, Freddy's ceased operations in late 1993 and early 1994 after it had conducted a series of "going-out-of-business sales" and otherwise disposed of its operating assets.

At a hearing conducted on February 23, 1995, the Court confirmed a First Amended Joint Plan of Liquidation (The "Plan") which had been proposed by Freddy's and the unsecured creditors' committee. On March 9, 1995, an Order Confirming the Plan was entered.

On February 22, 1995, Freddy's commenced an adversary proceeding against Wally Packaging, Inc. ("Wally") wherein it: (1) objected to the unsecured proof of claim filed by Wally in the amount of $340,730.00 (The "Wally Claim"); and (2) requested that the Court grant Freddy's a judgment against Wally for the damages which it alleged Freddy's had sustained because the goods (front-end plastic shopping bags) which Wally had supplied to Freddy's were defective.

In its Complaint in the adversary proceeding, Freddy's alleged that: (1) the Wally Claim should be reduced by $130,158.20, representing uncredited payments on account made by Freddy's, and the additional amount of $5,500, representing a distribution which Wally had received in the bankruptcy proceeding of ALP Acquisition Limited Partnership, d/b/a A.L. Price ("A.L. Price")"; (2) the Wally Claim incorrectly included the amount of $32,902, representing bags delivered to A.L. Price, and the additional amount of $41,499.50, representing bags which A.L. Price had refused delivery on; (3) Freddy's books and records indicated that $68,828.78 was the maximum amount due from Freddy's to Wally for bags which it had received; (4) Freddy's believed that it had no obligation to pay for bags received from Wally because Wally had breached its contract with Freddy's in that it delivered bags that were not fit for the purpose intended and which failed of their essential purpose; (5) pursuant to New York Uniform Commercial Code Section 2-714, Freddy's was entitled to damages resulting from the delivery of defective goods[1]; (6) because the bags

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[1] New York Uniform Commercial Code Section 2-714 provides:

(1) Where the buyer has accepted goods and given notification (subsection (3) of Section 2-607) he may recover as damages for any non-conformity of tender the loss resulting in the ordinary course of events from the seller's breach as

delivered by Wally were defective, Freddy's employees had to double or triple the bags when completing customer purchases, so Freddy's was entitled to a one-third credit against the amount alleged to be due for bags delivered and received, as well as an additional credit, representing the time value of the employees having to double or triple-bag customer orders; and (7) Freddy's damages under UCC Section 2-714 exceeded the amounts claimed to be due to Wally by $20,000.

Wally interposed an Answer in the adversary proceeding which alleged that: (1) Freddy's and A.L. Price were jointly liable for the amounts due for the bags delivered by Wally to Freddy's and A.L. Price pursuant to an April 15, 1992 agreement (The "Purchase Contract"); (2) Freddy's had waived the right to assert that the bags delivered by Wally were defective; (3) Freddy's should be found to be estopped from raising any claim that the bags delivered by Wally were defective; and (4) Freddy's was liable for the full amounts due for the bags delivered by reason of an account stated between the parties.

After a number of motions were heard and decided by the Court, extensive discovery was conducted by the parties and several pre-trials were conducted by the Court, the matter was tried on May 2, 1996 at which time the parties were given until June 14, 1996 to file post-trial submissions.

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determined in any manner which is reasonable.

(2) The measure of damages for breach of warranty is the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been warranted, unless special circumstances show proximate damages of a different amount.

(3) In a proper case any incidental and consequential damages under the next section may also be recovered.

## DISCUSSION

### I. Overview of the Facts Developed at Trial

Wally had supplied front-end bags to F&S Sales, Inc. which operated New York and Florida outlets under the trade name Freddy's until approximately 1991 when the chain was acquired by ALP Freddy's Limited Partnership. Prior to or at the same time as that acquisition, ALP Acquisition Limited Partnership, d/b/a A.L. Price, whose principals were identical or substantially identical, acquired the A.L. Price health and beauty aid chain which operated in Michigan. That chain, which continued to do business as A.L. Price, was proceeding in a Chapter 11 case in the Eastern District of Michigan at the same time that the Freddy's Chapter 11 Case was proceeding in the Western District of New York. In the Spring of 1992 the upper management of Freddy's and A.L. Price, including their chief financial and operating officers, was identical and was based at offices located at 90 Commerce Drive, Rochester, New York.

Shortly before April 15, 1992, Curt C. Edwards ("Edwards"), the then 24-year-old son of the president of the corporate general partner of Freddy's, was: (1) employed by Freddy's and A.L. Price; (2) located at the Commerce Drive office; and (3) responsible for buying front-end bags for both Freddy's and A.L. Price. Edwards was contacted by Mr. Gary Greenberg ("Greenberg") the Wally sales representative, which resulted in Wally participating in a bidding process to supply front-end bags to Freddy's and A.L. Price. Wally was the successful bidder, and on or about April 15, 1992, the Purchase Contract was executed by Greenberg, on behalf of Wally, and Edwards, on behalf

of A.L. Price and Freddy's (Edwards signed his name above a signature line which read "A.L. Price/Freddy's"). The Purchase Contract (Exhibit No. 1 at Trial): (1) was typed on Wally letterhead; (2) was addressed to A.L. Price/Freddy's at Commerce Drive; (3) set forth separately the specifications and annual usage for both large and small shopping bags for Freddy's and A.L. Price; (4) indicated that "[b]ased on a one year contract, Wally Packaging will immediately forward a five thousand dollar rebate check and an additional ten thousand dollar rebate check in December 1992"; (5) indicated that 3% should be added to the bags to be shipped to the Florida stores because of a photo-degradable requirement; and (6) indicated that freight would be prepaid full containers to Florida and Michigan warehouse.

By a check (Exhibit No. 31 at Trial), dated June 9, 1992, and made payable to ALP/Freddy's in the amount of $5,000.00, which was deposited on June 19, 1992 into an account maintained by ALP Freddy's, and a check (Exhibit No. 31 at Trial), dated February 2, 1993, and made payable to ALP Freddy's in the amount of $10,000.00, which was deposited on February 9, 1993 into an account maintained by ALP Freddy's, Wally paid the $15,000.00 rebate required by the Purchase Contract.

Between April, 1992 and approximately September, 1992, Freddy's and A.L. Price continued to use front-end bags supplied to them under prior contracts.

Admitted into evidence at trial (Exhibit No. 34 at Trial) were copies of September 1, 1992, November 6, 1992 and January 15, 1993 purchase orders addressed to Wally. The September 1, 1992 and November 6, 1992 purchase orders indicated that the goods covered were to be billed to

A.L. Price in Melvindale, Michigan and shipped to Freddy's Warehouse, c/o Art's Warehouse, Melvindale, Michigan. The January 15, 1993 purchase order indicated that the goods covered were to be billed to ALP Freddy's Ltd Partnership and shipped to Freddy's New York Warehouse. On all three of the purchase orders there are set forth the logos of both A.L. Price and Freddy's Rx.

Also admitted into evidence at trial was a photocopy of a September 10, 1992 Wally invoice (No. 6228) in the amount of $24,590.40 (Exhibit No. 32 at Trial), which was typed up to indicate that the goods covered were sold to A.L. Price and shipped to ALP/Freddy's Warehouse. (This invoice appears to match up generally with the September 1, 1992 purchase order referred to in the proceeding paragraph). This Wally invoice covered 768 cases of A.L. Price large bags and 1008 cases of Freddy's New York large bags. Exhibit No. 32 at Trial also included a photocopy of an A.L.P. Freddy's check, dated December 2, 1994, in the amount of $24,098.09, which indicates that it was in payment of Wally Invoice No. 6228.

A similar exhibit, Exhibit No. 33 at Trial, was a photocopy of a November 4, 1992 Wally invoice (No. 6239) in the amount of $12,684.30. This invoice indicated that these goods were sold to ALP/Freddy's and shipped to Art's Warehouse, Melvindale, Michigan. This Wally invoice covered 220 cases of A.L. Price bags, 350 cases of Freddy's NY bags and 173 cases of Freddy's Florida bags, for a total amount due of $12,684.30. Exhibit No. 33 at Trial also included a photocopy of an A.L.P. Freddy's check, dated December 4, 1992, in the amount of $3,814.61 in payment of Wally invoice No. 6239. The accompanying check stub indicated that it was for bags for the Michigan, New York and Florida stores.

The first shipment of Freddy's and A.L. Price bags was made in approximately September, 1992 and was manufactured by Sack Corporation ("Sack") which was located in New Jersey. The total amount originally due Wally on that first shipment of Freddy's and A.L. Price bags was $130,158.70.

When Freddy's began to use the bags from the first shipment it determined that there were defects in a substantial number of the bags. The store employees found that the bottoms of a substantial number of the bags were separating, forcing them to double-bag and in some cases triple-bag customer purchases to insure that there was no breakage as the customers left the store. Wally was advised of the defects and thereafter: (1) representatives of Wally and Sack met with Edwards in Rochester; (2) 97 cases of bags were returned to Sack from Freddy's New York stores and 96 cases of bags were returned to Sack from Freddy's Florida stores; (3) a 33% discount, amounting to $8,114.80, was allowed to Freddy's on the September 10, 1992 Invoice No. 6228 (the invoice which indicated that the goods, which included A.L. Price and Freddy's New York bags, were sold to A.L. Price and shipped to ALP/Freddy's warehouse c/o Arts Warehouse in Michigan).

In January and February of 1993, a second shipment of bags, manufactured for Wally in the Orient, was delivered. This second shipment included bags with a total original dollar value pursuant to the Purchase Contact of $68,828.75 bearing the Freddy's logo, and $32,855.70, bearing the A.L. Price logo.

Freddy's alleged that it experienced even worse problems with the second shipment of bags than it had experienced with the first shipment, but only with respect to the larger bags (the bags

designated in the Purchase Contract as 1/6th T-Shirt bags). Employees of Freddy's at the stores complained that the bags not only were breaking apart at the seams, but in many cases had defective and unusable handles.

By a March 30, 1993 letter (The "Notice") (typed on letterhead which at the top indicated that it was being sent by ALP Freddy's Limited Partnership, but on the bottom bore the A.L. Price and Freddy's logos), Edwards advised Wally that there were numerous store and customer complaints regarding the construction and integrity of the bags in the latest shipment (handles falling off regardless of weight and the bottoms are giving out). The Notice (Exhibit No. 8 at Trial) also indicated that, "these constructional deficiencies are monumental issues that need resolution immediately. Until these problems are worked out, all payments due to Wally Packaging are considered frozen."

In April, 1993, Ray Wallerstein ("Wallerstein"), the President of Wally, Greenberg and Edwards met in Rochester to discuss the concerns raised by Edwards in the Notice.

There does not appear to be any dispute that at the April, 1993 meeting, Wallerstein proposed to resolve the problem Freddy's alleged it was experiencing by "swapping-out" any defective bags for new bags on a per-case basis after inspecting and confirming defects. The swap-out would be accomplished by using other bags which Wally had already had manufactured with the A.L. Price and Freddy's logos, and were being warehoused by Wally. It appears that Edwards advised Wallerstein at the April, 1993 meeting that he would discuss the swap-out proposal with Freddy's

attorneys, since the company was now in a Chapter 11 proceeding and Edwards was not sure as to his authority to agree to a resolution of the matter.

Wallerstein testified at trial that at the April, 1993 meeting: (1) he requested that Edwards instruct all stores not to use but to collect any bags which were found to be defective so that Wally could return them to its supplier for full credit; and (2) he advised Edwards that he needed instructions with respect to the remainder of the bags identified in the Purchase Contract which were being stored in warehouses by Wally. Edwards in his deposition testimony did not confirm that these additional requests were made by Wallerstein at the April, 1993 meeting.

There is no evidence before the Court, including Edwards' testimony, that indicates that prior to Freddy's ceasing operations either Edwards or any other representative of Freddy's ever followed up on Wallerstein's swap-out proposal or ever conveyed to Wally any other proposal, counter-proposal or demand in connection with the bags in the second shipment which Freddy's alleged were defective .

Exhibit No. 9 at Trial, a May 1, 1993 letter from Wally to Freddy's, and further addressed "Dear Mr. Edwards",[2] essentially stated that: (1) Wally would always exchange and replace bags which had not satisfied the customer; (2) Wally could not exchange and give credit on bags that had already been distributed to customers and therefore could not be returned; (3) Wally was holding approximately 8,000 cases of Freddy's bags in warehouses which could be used to replace any cases that upon inspection were not satisfactory; (4) at the April meeting the parties had discussed

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[2] There was argument at trial that the words "Dear Mr. Edwards" were added later.

requesting that the stores ship to Wally any bags not 100% satisfactory; (5) Wally continued to be willing to replace and exchange all unsatisfactory bags; (6) Wally would not be liable for any liability (to customers) caused in connection with the bags, but would be willing to exchange bags; and (7) Wally understands that all agreements made prior to the bankruptcy were canceled.

Freddy's, and apparently A.L. Price, continued to use the bags supplied to it by Wally in the second shipment, and Freddy's continued to use its bags until it ceased operations in December, 1993 and January, 1994.

## II. Freddy's Alleged Liability on the Amounts Due to Wally for Bags Delivered to and Used by A.L. Price

Based upon the evidence presented, I find that Freddy's is liable for the amounts found in this Decision & Order to be due to Wally for bags delivered to and used by A.L. Price.

None of the documentary evidence introduced and admitted at trial clearly indicated that Wally knew or should have known that Freddy's and A.L. Price were separate legal entities which would be severally liable to Wally for the front-end bags manufactured, delivered, received and/or used pursuant to the Purchase Contract which was signed by Freddy's. The Purchase Contract, Exhibit No. 1 at Trial, was addressed to A.L. Price/Freddy's and signed by Edwards on behalf of A.L. Price/Freddy's.

Although there are different amounts and prices for the bags identified for use by Freddy's and A.L. Price stores, the evidence at trial indicated that this was because the different bags were printed on either one (Freddy's) or two (A.L. Price) sides, not because Freddy's and A.L. Price were

separate legal entities. There is no testimony in the record by anyone at Freddy's, including Edwards, which clearly indicated that before the delivery of the second shipment, Edwards or any representative of Freddy's or A.L. Price ever made it clear to any representative of Wally that Freddy's and A.L. Price were two separate legal entities, severally responsible to pay Wally for their own front-end bags.

Moreover, the purchase orders, Exhibit No. 34 at Trial, did not clearly indicate that Freddy's and A.L. Price were separate legal entities. To the contrary, the purchase orders each bear the logos of both Freddy's and A.L. Price, notwithstanding the particular billing and shipping information set forth, making the purchase orders, at best, ambiguous. The September 1, 1992 purchase order included both Freddy's and A.L. Price bags and indicated that the bags were to be billed to A.L. Price but shipped to Freddy's warehouse in Michigan (Why would Freddy's have a Michigan warehouse?).

Furthermore, the payments by Freddy's of the Wally invoices indicated that Freddy's was responsible for the payment of bags delivered pursuant to the Purchase Contract. Wally Invoice No. 6228 (Exhibit No. 32 at Trial), forwarded to Michigan, seemingly in accordance with the instructions on the September 1, 1992 purchase order, included both A.L. Price and Freddy's bags, but was ultimately paid by an A.L.P. Freddy's check. Similarly, Wally Invoice No. 6239 (Exhibit No. 33 at Trial), which included both Freddy's New York and Florida bags and A.L. Price bags, all of which were designated to be shipped to a Michigan warehouse, was paid by an A.L.P. Freddy's check.

In addition, the $15,000 rebate required by the Purchase Contract was paid to ALP Freddy's by two checks which were deposited into an ALP Freddy's bank account.

Clearly, it was reasonable for Wally, based upon the documentary evidence discussed above, to conclude that Freddy's was either operating the A.L. Price and Freddy's stores under one legal entity, or, that Freddy's, which received the full rebate, paid invoices for bags used by the A.L. Price and Freddy's stores that were delivered pursuant to purchase orders which included both the A.L. Price and Freddy's logos, and received the discount for the defective first shipment, was financially responsible to Wally for the amounts due for all of the bags delivered pursuant to the Purchase Contract.

## III. Liability to Pay for Second Shipment Bags Where Delivery Was Made by Wally to Freddy's or A.L. Price

### A. Overview

Apart from the analysis that follows under Article 2 of the New York Uniform Commercial Code as it relates to the facts and circumstances of this case, it is clear that Freddy's never followed through on arriving at a negotiated business resolution with Wally of the problems it was experiencing with the bags delivered in the second shipment. The Notice which Edwards sent Freddy's indicated that this was a problem which needed resolution immediately. The parties had previously worked with each other and achieved an acceptable business resolution to the problems encountered with the first shipment, but they never achieved a business or legal resolution of the problems encountered with the second shipment. Although the parties met and Wally made a

reasonable proposal to resolve the matter, the swap-out proposal, Freddy's simply never followed up with Wally on either the proposal or the problem so that the parties could come to a final business or legal resolution. The evidence indicates that Freddy's never responded to the Wally proposal, never made a counter proposal or gave Wally a further opportunity to satisfactorily resolve the matter. Freddy's did, however, unilaterally determine that it would continue to use the bags which had been delivered to it by Wally in a manner inconsistent with the swap-out proposal, even though Freddy's usage might have been substantially prejudicial to Wally if it is true that Wally could have received full credit from its supplier for any bags proven to be defective and returned to the supplier. Whether Freddy's failed to follow up on achieving a final resolution to the problems encountered with the second shipment because its personnel were involved in other higher priority matters in the company's bankruptcy proceeding, or, if and when they were consulted regarding the Wally swap-out proposal, the attorneys for Freddy's advised the responsible Freddy's employees to simply drop the matter and pursue the course of action which they pursued (unilaterally using the bags), is not in evidence. All the evidence indicates is that Freddy's did not respond to the Wally proposal and did not return the bags, but it did, without Wally agreeing, continue to use the bags delivered to it in the operation of its business.

**B. Article 2 of the New York Uniform Commercial Code**

At trial and in its post-trial Findings of Fact and Conclusions of Law, Freddy's asserted that, apparently admitting that it had not rejected the bags delivered by Wally in the second shipment in

accordance with UCC Section 2-602, it had revoked its acceptance of the bags in accordance with UCC Section 2-608(b)(3).

Wally at trial and in its Post-Trial Memorandum contended that: (1) Freddy's should be deemed to have accepted the bags delivered to it by Wally in the second shipment in accordance with UCC Section 2-606(1) because Freddy's: (a) had failed to properly and effectively reject the goods under UCC Section 2-602 (which Freddy's does not appear to dispute); (b) had failed to effectively revoke acceptance under UCC Section 2-608, in that the May 30, 1993 Notice was not a clear and unambiguous notice of rejection or revocation, but was more in the nature of a statement designed to open negotiations; (c) never held the bags which it alleged were defective for Wally's disposition, as required by UCC Section 2-602(b) and UCC Section 2-608(b)(3), including affording Wally the ability to remove them, even though Wally had made the swap-out proposal; and (d) used the bags which it alleged were defective, contrary to UCC Section 2-602 and UCC Section 2-608; (2) in the absence of an effective rejection or a revocation of acceptance, UCC Section 2-607 requires that Freddy's and A.L. Price be deemed to have accepted the second shipment, and pursuant to UCC Section 2-607(1), Wally must be paid the contract price for the accepted goods; and (3) even if the bags in the second shipment were defective in whole or in part, Freddy's failed to properly mitigate its damages by failing to allow Wally to implement its swap-out proposal or otherwise cure the problems.

I agree with the contentions of Wally that Freddy's failed to effectively reject or revoke acceptance of the bags delivered in the second shipment pursuant to the purchase contract. Freddy's

conduct before the Notice was sent, the wording of the Notice, and Freddy's conduct after the Notice in dealing with Wally and the problems encountered in the second shipment did not constitute a clear rejection of the shipment or a revocation of acceptance. The following specific facts and circumstances support the conclusion that there was not an effective rejection or revocation of acceptance: (a) the parties' prior good faith dealings in resolving the problems encountered in the first shipment; (b) the language of the Notice; (c) the discussions at the follow-up meeting, including the swap-out proposal; (d) the response of Edwards to the swap-out proposal at the follow-up meeting; and (e) the failure of Freddy's to comply with UCC Section 2-602 by holding the goods for Wally or allowing it to take them back.

Article 2 of the UCC, as does the UCC for parties in general, imposes on the buyer and seller the requirement that they act reasonably and in good faith. Freddy's and Wally acted reasonably and in good faith with respect to the problems encountered in the first shipment and then were able to arrive at a negotiated business resolution. With respect to the second shipment, even though the problems which Freddy's alleged were more serious than those encountered in the first shipment, Freddy's, as required, attempted to work with Wally reasonably and in good faith up through the April, 1993 follow-up meeting, after which Freddy's simply "dropped the ball". From the evidence it appears that Wally was also acting reasonably and in good faith towards Freddy's through the April, 1993 meeting when it made the swap-out proposal, which, given the facts and circumstances presented and the framework of Article 2 of the UCC, seems to have been reasonable and appropriate. Had Freddy's not "dropped the ball" and followed up on the swap-out proposal or

otherwise addressed the problem after the April 1993 meeting, there may have been an acceptable business resolution, or, after Freddy's consulted with its attorneys, the parties may have clarified their legal positions or otherwise complied with the technical requirements of Article 2 of the UCC. Freddy's failed to continue to operate reasonably and in good faith to arrive at a negotiated or acceptable business resolution, and, not having otherwise focused on its rights and duties under Article 2 of the UCC, has left the Court with a somewhat unclear pattern of behavior which it must judge under the technical provisions of Article 2.

I believe that it would be unjust, inequitable and not in accordance with the provisions of Article 2 of the UCC for the Court to find that Freddy's actions: (1) constituted an effective rejection or a revocation of acceptance[3]; (2) fulfilled Freddy's duties or excused it from its duties under Section 2-602 of the UCC, if there otherwise was an effective rejection or revocation of acceptance; (3) excused Freddy's from failing to operate in good faith by responding to Wally's swap-out proposal or otherwise allowing Wally the opportunity to cure, mitigate damages or achieve an acceptable business settlement; (4) excused Freddy's use of the bags which it alleged were defective, when it was inconsistent with the swap-out proposal and Wally's ownership of the goods, and when Freddy's had been advised that such usage may have directly prejudiced Wally because it prevented Wally from obtaining full credit from its supplier[4]; and (5) justify a finding that Freddy's is not

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[3] *See* UCC Section 2-606 and Section 2-602 and *Maggio Importato, Inc. v. Cimitron, Inc.*, 189 A.D.2d 654 (1st Dept. 1993).

[4] *See Sears Roebuck & Company vs. Galloway*, 195 A.D.2d 825 (3rd Dept. 1993).

obligated for the contract price of the bags delivered to it and A.L. Price in the second shipment.

## IV. Liability of Freddy's to Pay for Bags Which Wally's had Manufactured Pursuant to Specifications in the Purchase Contract Which Were Not Delivered in the First or Second Shipment

At trial and in its Post-Trial Memorandum, Wally alleged that Freddy's was liable in the amount of $59,910.95 for bags bearing Freddy's logo which Wally had had manufactured pursuant to the Purchase Contract, but which had not been delivered to Freddy's. Wally relied on the provisions of UCC Section 2-709(1)[5] for this contention.

To find that the undelivered bags were identified to the Purchase Contract within the meaning and intent of UCC Section 2-709(1)(b), the parties have agreed that it is necessary for the Court to determine whether the Purchase Contract was, as Freddy's alleges, a "requirements contract", or as Wally alleges, an "installment contract".

Unfortunately, neither the Purchase Contract itself, typed up by Greenberg of Wally, nor the testimony at trial, makes it clear what the intended agreement was.

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[5] Section 2-709 provides in pertinent part:

(1) When the buyer fails to pay the price as it becomes due the seller may recover, together with any incidental damages under the next section, the price

(b) of goods identified to the contract if the seller is unable after reasonable effort to resell them at a reasonable price or the circumstances reasonably indicate that such effort will be unavailing.

I find that Freddy's is not obligated to pay for bags beyond the second shipment for the following reasons: (1) the testimony of those Freddy's store managers who appeared at trial makes it clear that there were substantial defects with the bags delivered in the second shipment; (2) Wally had alleged that it could get credit from its supplier for defective bags which it could return to the supplier, yet it did not return any undelivered bags to its supplier for full credit or establish that it attempted to identify any of them as defective bags (and there must have been some), it simply elected to resell the undelivered bags for $7,500.00, leaving a net balance of $52,410.95; (3) even with double and triple bagging, Freddy's needs for bags was met with the first and second shipments made pursuant to the Purchase Contract and purchase orders (or release orders), so that more than a full year of Freddy's needs (September 1992 through December 1993) were met by the first and second shipments; (4) it is unclear, but it may be that Wally, at its own business risk, had the estimated annual usage of Freddy's and A.L. Price bags prematurely manufactured, not pursuant to proper purchase or release orders, but in an attempt to achieve a larger margin or obtain a greater discount from its supplier, with the assumption that Freddy's and A.L. Price would eventually request and take delivery of all of the bags up to the amounts set forth on the Purchase Contract.

In addition, the testimony of Wallerstein and Freddy's Chief Financial Officer, Ken Koester, regarding their discussions about Wally finding a buyer for the undelivered bags, discussions which occurred after Freddy's had ceased operations, did not indicate that Wallerstein ever asserted that the parties needed to achieve the maximum return on a disposition of those bags because Freddy's was otherwise liable to pay for those bags. The testimony indicated that there was a mere request by

Wallerstein that Freddy's assist him in any way possible in obtaining a favorable disposition of the bags. Furthermore, it is not clear why if Wally already believed that the bags which it had warehoused were identified to the Purchase Contract within the meaning of UCC Section 2-709(1)(b), it proposed to use some or all of those bags to effectuate the swap-out proposal.

Based on the foregoing, the Court finds that the Purchase Contract was a "requirements contract".

## V. Return of the Rebate

At trial and in its Post-Trial Memorandum Wally asserted that since Freddy's did not take and pay for a full year's supply of bags pursuant to the Purchase Contract, Freddy's should be required to refund all or a portion of the rebate. Since it appears that Freddy's and A.L. Price did receive in the first and second shipments bags sufficient to meet their requirements for more than one year, and, in accordance with this Decision & Order, Wally will have an allowed claim for all unpaid amounts due for bags delivered in the first and second shipments, there is no reason for Freddy's to return all or a portion of the rebate.

In addition, Wally's May 1, 1993 letter (Exhibit No. 9 at Trial) states that, "In order for us to keep the account out of our competitors hands we agreed to pay Freddy's $15,000 in advance to receive this years contract". That statement clearly discloses the reason for the rebate payment; to keep competitors from getting a foot in the door.

## CONCLUSION

The Wally claim is allowed for the unpaid amounts due for the second shipment of bags to both Freddy's and A.L. Price. The Wally claim is disallowed to the extent that it represents amounts for bags not delivered to Freddy's or A.L. Price as part of the first or second shipment, and to the extent that it represents a request for the return of all or a portion of the rebate.

**IT IS SO ORDERED.**

**_____/s/_____**
**HON. JOHN C. NINFO, II**
**U.S. BANKRUPTCY JUDGE**

**Dated: September 5, 1996**