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***Chernick v. Fasig-Tipton:***  
**A Caveat to the Horse Trader**

by

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# *Chernick v. Fasig-Tipton:* A Caveat to the Horse Trader

## INTRODUCTION

As late as 1978, Kentucky courts have asserted that “caveat emptor,” or let the buyer beware,<sup>1</sup> is “commercial reality” in the sale of personal property or goods.<sup>2</sup> In 1986, however, the court of appeals, in *Chernick v. Fasig-Tipton Kentucky, Inc.*,<sup>3</sup> substantially eroded that doctrine. The decision warns thoroughbred sellers and auctioneers to deal in a manner befitting one of Kentucky’s leading industries or face what one commentator has termed “caveat vendor,” or “let the seller beware.”<sup>4</sup>

Kentucky has long held a position of integrity in the horse industry, and the *Chernick* holding aims at enhancing that position.<sup>5</sup> The *Chernick* court purports to advance Kentucky’s reputation in the equine business by two means—(1) by awarding punitive damages to a buyer damaged by a seller’s breach of contract<sup>6</sup> and (2) by suggesting that an auctioneer may be jointly

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<sup>1</sup> BLACK’S LAW DICTIONARY 202 (5th ed. 1979).

<sup>2</sup> *Greg Coats Cars, Inc. v. Kasey*, 576 S.W.2d 251, 253 (Ky. Ct. App. 1978).

<sup>3</sup> 703 S.W.2d 885 (Ky. Ct. App. 1986).

<sup>4</sup> Hollingsworth, *What’s Going on Here*, THE BLOODHORSE 5057, 5147 (July 27, 1985). The actual term is *caveat venditor*, which is defined as: “A maxim, or rule, casting the responsibility for defects or deficiencies upon the *seller* of goods.” BLACK’S LAW DICTIONARY 281 (Rev. 4th ed. 1968).

<sup>5</sup> “We agree with the trial court that the Commonwealth of Kentucky maintains an international reputation for excellence in the equine industry. The conduct of one of the Commonwealth’s foremost consignors of breeding stock is not to be reviewed at a level lower than that of strict scrutiny.” 703 S.W.2d at 890. Fasig-Tipton’s identity as “one of the foremost consignors” of breeding stock extends to other jurisdictions where thoroughbreds are an important industry. For example, Fasig-Tipton also controls sales companies in Florida, Louisiana and California. See Hollingsworth, *supra* note 4, at 5146.

<sup>6</sup> For a discussion of the customary elements and measure of damages for breach of warranty in a horse sale, see Annot., 91 A.L.R.3d 415 (1979). See also *Schleicher v. Gentry*, 554 S.W.2d 884 (Ky. Ct. App. 1977) (buyer’s remedies, in affirming contract, limited to difference between value of mare as represented and actual value plus stud fees).

liable with the seller for the breach. This Note first focuses on these approaches, then examines the future application of *Chernick* and how the seller and auctioneer may avoid its consequences.

Although equine law combines principles from various areas of the law, many of its applications are unique.<sup>7</sup> *Chernick* involved facts clearly unique to the horse industry, and the decision reflects that the sale involved a horse rather than some other good.<sup>8</sup> For this reason, this Note focuses on the implications of *Chernick* to the horse trader.<sup>9</sup>

### I. THE FACTS OF *Chernick v. Fasig-Tipton*

The Chernicks purchased a bay mare<sup>10</sup> named Fiddler's Colleen at the Keeneland breeding stock sale in November, 1981.<sup>11</sup>

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<sup>7</sup> It is questionable whether there is actually a body of law that may be designated as "equine law." See Miller, *America Singing: The Role of Custom and Usage in the Thoroughbred Horse Industry*, 74 Ky. L.J. 781 (1985-86). If indeed there is such a body of law, its application in *Chernick* and similar cases is merely a combination of the Uniform Commercial Code (U.C.C.), contract, tort and agency law. Case law and the U.C.C. itself clearly establish that the U.C.C.'s rules apply to transactions in thoroughbred horses. See U.C.C. § 2-105(1) (1972). See also *Keck v. Wacker*, 413 F. Supp. 1377, 1381 (E.D. Ky. 1976); *Grandi v. LeSage*, 399 P.2d 285, 290 (N.M. 1965) (Both cases apply the U.C.C. without addressing its scope.). The U.C.C., in turn, incorporates other legal principles: "Unless displaced by the particular provisions of this Act, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake . . . or other validating or invalidating cause shall supplement its provisions." U.C.C. § 1-103 (1972).

<sup>8</sup> See notes 163-69 *infra* and accompanying text.

<sup>9</sup> The dictionary definition of a horse trader is "one who engages in horse trading." WEBSTER'S THIRD INTERNATIONAL DICTIONARY 1093 (unabridged 1966). Since *Chernick* involved fraudulent acts of a seller, an ordinary "horse trader" would not be affected. The colloquial definition as one who engages in "sharp practices" that are "in conflict with fairness and openness," Kershen, *Horse-Tradin': Legal Implications of Livestock Auction Bidding Practices*, 37 ARK. L. REV. 119, 120 (1983), is more applicable in this context.

<sup>10</sup> A bay mare is a mare with reddish-brown coloration. See WEBSTER'S THIRD INTERNATIONAL DICTIONARY 188 (unabridged 1966).

<sup>11</sup> The November sales are the premier mare sales. Although the sale of mares for breeding does not generate the level of sales volume or gross receipts that is generated by the yearling sales, the sale of brood mares did rank second to yearlings in 1983. "7,023 were sold for gross receipts of \$240,244,133 an average of \$34,208." J. LOHMAN & A. KIRKPATRICK, *SUCCESSFUL THOROUGHBRED INVESTMENT IN A CHANGING MARKET* 81 (1984). The Chernicks paid \$175,000 for Fiddler's Colleen in 1981. *Chernick v. Fasig-Tipton Ky., Inc.*, 703 S.W.2d 885, 887 (Ky. Ct. App. 1986).

In February, 1982, the mare aborted twin fetuses while at the Chernick's New York farm.<sup>12</sup> After being pronounced ready to breed again in March, 1982, the mare was booked<sup>13</sup> to a stallion whose efforts did not result in conception. She was then bred to a less valuable stallion in July, 1982.<sup>14</sup>

On August 4, 1982, the Chernicks' veterinarian found Fiddler's Colleen to be in foal.<sup>15</sup> That finding was confirmed on September 9, 1982.<sup>16</sup> After the first veterinary examination, the Chernicks entered the mare in Fasig-Tipton's 1982 November sales. The Chernicks completed a form consignment contract requiring that the consignors (Chernicks) provide information regarding broodmares<sup>17</sup> only as to "this year's produce" and "last year's produce." Fasig-Tipton ordinarily obtained information about prior years from a pedigree statistics corporation whose statistical information normally ran about two years behind.<sup>18</sup>

On the consignment contract the Chernicks listed Fiddler's Colleen's 1981 produce as a colt and her 1982 produce as "slip."<sup>19</sup> In accordance with the conditions of sale, the Chernick's veter-

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<sup>12</sup> The Chernick's veterinarian, Dr. William Bradley, observed and verified this abortion. 703 S.W.2d at 887. Twins are undesirable in a mare because they may endanger the mare and are often of little racing value. See *Taylor v. Johnston*, 539 P.2d 425, 428 (Cal. 1975). Likewise, the abortion of twin fetuses increases "the mare's propensity for such an occurrence" later and may make the mare "unfit for breeding purposes." 703 S.W.2d at 890.

<sup>13</sup> A book is "[t]he group of mares being bred to a stallion in one given year." J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 210.

<sup>14</sup> 703 S.W.2d at 887.

<sup>15</sup> This was the 25-day examination and is generally not as reliable as a 60-day examination. *Chernick v. Fasig-Tipton*, No. 83-CI-1365, slip op. at 2, 3 (Fayette Cir. Ct. Apr. 5, 1984).

<sup>16</sup> This was the 60-day examination and is generally considered reliable in determining pregnancy status. *Id.*, slip op. at 3.

<sup>17</sup> A broodmare is simply a "[f]emale thoroughbred used for breeding." J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 211.

<sup>18</sup> Fasig-Tipton relied on Pedigree Associates, Inc., which accesses Jockey Club statistical information. This information normally was two years behind but in this case was four years delinquent. 703 S.W.2d at 885. For a discussion of the Jockey Club's role in the horse industry, see note 174 *infra*.

<sup>19</sup> 703 S.W.2d at 887. The word slip is used interchangeably with the word aborted. This is consistent with the definition of "slipped" as, "A pregnancy aborted or resorbed spontaneously." J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 219. The correct listing for her 1982 produce was "slipped twins." 703 S.W.2d at 887.

inarian conducted an examination of the mare within ten days of the sale. The veterinarian completed an examination form that provided him with five options relating to the mare's breeding status.<sup>20</sup> The veterinarian checked the second option, thus representing that the mare was "barren and free from infection."<sup>21</sup>

As a result of this examination, Fasig-Tipton officials corrected the official form, marking it "B-okay." That listing was intended to direct the announcer at the sale that the mare was not in foal but was barren, apparently free of genital disease and in sound breeding condition.<sup>22</sup>

Cloverfield Farm purchased the mare for \$85,000.00. Immediately after the fall of the hammer,<sup>23</sup> Cloverfield Farm had the mare examined by a veterinarian recommended by Fasig-Tipton. Using the same form used by the Chernick's veterinarian in the pre-sale exam, this veterinarian checked the box for barren and not in sound breeding condition.<sup>24</sup> Based on this examination, the buyers declined to accept the mare.<sup>25</sup> Following this

<sup>20</sup> The five options included on the form were:

- (1) In foal;
- (2) Barren and free from infection;
- (3) Maiden, free from infection;
- (4) Barren and not in sound breeding condition; and
- (5) Maiden and not in sound breeding condition.

703 S.W.2d at 887.

<sup>21</sup> *Id.*

<sup>22</sup> The announcement actually made was: "'She is not in foal, she is barren. The mare is not in foal.'" 83-CI-1365, slip op. at 7. The sale announcement takes precedence over the status published in the sales catalog. J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 84. Furthermore, an auctioneer's announcement may create an express warranty when none existed previously. See *Miron v. Yonkers Raceway, Inc.*, 400 F.2d 112, 114 (2d Cir. 1968). See also U.C.C. § 2-313 (1972), which governs the formation of an express warranty.

<sup>23</sup> The "fall of the hammer" has been clearly established to indicate the finality of the sale. 703 S.W.2d at 887. See also 400 F.2d at 115; J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 84-85. "Only upon precisely described circumstances can the drop of the hammer be held in abeyance or suspended." 703 S.W.2d at 887-88.

<sup>24</sup> See note 20 *supra*.

<sup>25</sup> Although the hammer had fallen, the conditions of sale allowed the buyers to reject the mare if it did not conform to the warranties made at the sale. See note 123 *infra* and accompanying text. Likewise, the Code grants the right to reject:

Subject to the provisions of this Article on breach in installment contracts (Section 2-612) and unless otherwise agreed under the sections on contrac-

rejection, Fasig-Tipton appointed two other veterinarians whose examinations conflicted somewhat with the examination of the first veterinarian following the sale.<sup>26</sup>

The Chernicks refused return of the mare and Fasig-Tipton refused to return the purchase price, so the buyers shipped Fiddler's Colleen to their Maryland farm. In Maryland, a final veterinarian examined the mare and found that her chances of ever carrying a foal to term were slim.<sup>27</sup> The Chernicks filed suit against Fasig-Tipton in the Fayette Circuit Court to recover the purchase price that Cloverfield Farm had paid to Fasig-Tipton. Cloverfield Farm intervened and demanded rescission,<sup>28</sup> return

tual limitations of remedy (Sections 2-718 and 2-719), if the goods or tender of delivery fail in any respect to conform to the contract, the buyer may

- (a) reject the whole; or
- (b) accept the whole; or
- (c) accept any commercial unit or units and reject the rest.

U.C.C. § 2-601 (1972).

<sup>26</sup> The first of these post-rejection veterinarians "expressed no opinion as to the mare's breeding status but penciled in 'no gross signs of exudate . . . infection cannot be ruled out.'" The second post-rejection veterinarian "orally indicated the mare was sound for breeding but that it would be necessary to suture the horse before she could carry a foal." 703 S.W.2d at 888.

<sup>27</sup> There was, therefore, a total of five examinations of Fiddler's Colleen: (1) The pre-sale examination by Dr. Bradley for the sellers, finding her to be barren and sound for breeding; (2) The first post-sale exam by Dr. McKee for the purchasers, finding her barren and not sound for breeding due to infection; (3) The second post-sale exam by Dr. Cash, hired by the sellers, finding no signs of infection but not ruling out infection (Dr. McKee had removed the infectious exudate); (4) The third post-sale exam by Dr. Fishback, hired by Fasig-Tipton, finding that the mare was sound for breeding if sutured; (5) The final exam by Dr. Brown after the horse had been removed to Maryland. He found that the chances of the mare carrying a foal to term were slim. *Id.* As we shall see, the chronology and findings of these exams are critical to determining the liability of the sellers and the auctioneer. See notes 134-36 *infra* and accompanying text.

<sup>28</sup> The word rescission is not used in any of the sections of the U.C.C.. The comment to U.C.C. § 2-608, however, states:

"The section no longer speaks of 'rescission,' a term capable of ambiguous application either to transfer of title to the goods or to the contract of sale and susceptible also of confusion with cancellation for cause of an executed or executory portion of the contract."

U.C.C. § 2-608 comment 1 (1972). Rescission may be the proper term to be applied in these circumstances. The U.C.C. clearly allows rejection, see § 2-601(a) (1972), and revocation of acceptance, see § 2-608 (1972). "It is the apparent intention of the drafters to restrict the word rescission to a rather limited number of cases, those involving a mistake or in which the seller has committed fraud, duress, or the like." J. WHITE & R. SUMMERS, HANDBOOK OF THE LAW UNDER THE UNIFORM COMMERCIAL CODE § 8-1, at 295 (2d ed. 1980).

of the purchase price and compensatory and punitive damages.

## II. PUNITIVE DAMAGES: PUNISHING THE SELLER?

This Note does not undertake to trace the history or development of punitive damages.<sup>29</sup> For our purposes, it is sufficient to have a basic understanding of the theory behind punitive damages awards. Popular wisdom holds that punitive or exemplary damages are a means of punishing a defendant for a wrong committed against the plaintiff and society in general.<sup>30</sup> As a corollary, punitive damages are permitted in tort actions due to the common origins of tort and criminal law and the belief that the tortfeasor deserves punishment.<sup>31</sup>

In contrast, the general theory of contract damages is "compensation for pecuniary loss."<sup>32</sup> Thus, it is generally held that punitive damages are not awardable in contract actions.<sup>33</sup> Courts and commentators have set forth several exceptions to this clearly

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<sup>29</sup> For a general discussion of the history and development of punitive damages, see I T. SEDGWICK, *A TREATISE OF THE MEASURE OF DAMAGES* § 347-55 (9th ed. 1920); Sullivan, *Punitive Damages in the Law of Contract: The Reality and the Illusion of Legal Change*, 61 MINN. L. REV. 207, 208-16 (1976-77); Comment, *Punitive Damages in Ordinary Contracts*, 42 MONT. L. REV. 93, 93-96 (1981).

<sup>30</sup> See C. McCORMICK, *THE LAW OF DAMAGES* § 77 (1935); Coleman, *Punitive Damages for Breach of Contract: A New Approach*, 11 STETSON L. REV. 250, 277-78 (1981-82); Sullivan, *supra* note 29, at 217; Comment, *supra* note 29, at 93-94. See also Comment, *Zen and the Art of Exemplary Damages Assessment*, 72 KY. L.J. 897, 903 (1983-84), in which the author recognizes that recent Kentucky opinions reflect this punitive purpose. The author also recognizes, however, that Kentucky has not abandoned the compensatory justification for punitive or exemplary damages. Both of these purposes seem to underlie the *Chernick* court's punitive damage award. See Jones, *Survey—Remedies*, 74 KY. L.J. 441, 441 n.4 (1985-86).

<sup>31</sup> See Sullivan, *supra* note 29, at 217 (quoting RESTATEMENT OF TORTS, Explanatory Notes § 901, comment a, at 538 (1939)). See also Coleman, *supra* note 30, at 278; Comment, *supra* note 29, at 93-94.

<sup>32</sup> Sullivan, *supra* note 29, at 218.

<sup>33</sup> See *General Accident Fire & Life Assurance Corp. v. Judd*, 400 S.W.2d 685, 688 (Ky. 1966); *Wahba v. Don Corlett Motors, Inc.*, 573 S.W.2d 357, 360 (Ky. Ct. App. 1978); *Louisville Bear Safety Serv., Inc. v. South Cent. Bell Tel. Co.*, 571 S.W.2d 438, 439 (Ky. Ct. App. 1978); *Ford Motor Co. v. Mayes*, 575 S.W.2d 480, 486 (Ky. Ct. App. 1978). See also Sullivan, *supra* note 29, at 207; Note, *Exemplary Damages in Contract Cases*, 7 WILLAMETTE L.J. 137 (1971); Comment, *supra* note 29, at 93. *But see* Note, *In Defense of Punitive Damages*, 55 N.Y.U. L. REV. 303 (1980).

stated and widely recognized rule.<sup>34</sup> These exceptions fall into four categories: (1) a contract breach accompanied by an independent tort, (2) a contract breach accompanied by fraudulent conduct, (3) a breach of a fiduciary duty, and (4) a breach of a special contract.<sup>35</sup> Any of the first three exceptions could apply in the context of our discussion. The courts, however, have generally applied only the first two exceptions to horse sales.<sup>36</sup>

#### A. *Applying the Uniform Commercial Code Damage Provisions*

The New Mexico Supreme Court, in *Grandi v. LeSage*,<sup>37</sup> combined the Uniform Commercial Code (U.C.C.) damage provisions with the concept of contemporaneous fraudulent conduct. In *Grandi*, the buyers of a thoroughbred brought suit against the seller and his trainer for rescission as well as compensatory and punitive damages.<sup>38</sup> The horse trainer had entered the seller's horse in a claiming race<sup>39</sup> and registered the horse as

<sup>34</sup> See, e.g., *Brown v. Coates*, 253 F.2d 36, 39 (D.C. Cir. 1958); *Gruenberg v. Aetna Ins. Co.*, 510 P.2d 1032, 1042 (Cal. 1973); *Hibschman Pontiac Inc. v. Batchelor*, 362 N.E.2d 845, 847 (Ind. 1977); 575 S.W.2d at 486; *Stanard v. Bolin*, 565 P.2d 94, 98 (Wash. 1977); D. DOBBS, *LAW OF REMEDIES* 818 (1973); *Coleman*, *supra* note 30, at 250-51; *Sullivan*, *supra* note 29, at 223-51; Comment, *supra* note 29, at 94-95.

<sup>35</sup> These special contracts include: A breach of a contract owed to the general public by a public service company, a breach of a promise to marry, and insurance contracts. See *Coleman*, *supra* note 30, at 251, & n.11; *Sullivan*, *supra* note 29, at 220-51; Comment, *supra* note 29, at 93.

<sup>36</sup> See *Keck v. Wacker*, 413 F. Supp. 1377, 1383 (E.D. Ky. 1976); *Chernick v. Fasig-Tipton Ky., Inc.*, 703 S.W.2d 885 (Ky. Ct. App. 1986); *Grandi v. LeSage*, 399 P.2d 285, 293 (N.M. 1965). These cases have applied the independent tort and contemporaneous fraudulent conduct approaches. If the court takes the fiduciary duty approach similar to the *Chernick* circuit court decision, then arguably a breach of this duty could justify punitive damages. See notes 121-43 *infra* and accompanying text.

<sup>37</sup> 399 P.2d 285 (N.M. 1965).

<sup>38</sup> *Id.* at 287.

<sup>39</sup> A claiming race is:

An event in which each horse entered is eligible to be purchased at a set price. Claims must be made before the race and can be made only by persons who have had a horse claimed at that same meeting or who have received a claim certificate from the stewards. Claiming races are generally of a lower class than allowance races; also, the lower the claiming price, the lower the class.

J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 211. See generally *id.* at 45-49.



a chestnut colt when, in fact, the horse was a gelding.<sup>40</sup> After claiming the horse and finding it useless for either breeding or racing, the plaintiff revoked acceptance under U.C.C. section 2-608.<sup>41</sup> The court granted the plaintiff judgment against the seller for \$3,500.00 representing the purchase price of the gelding, the

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<sup>40</sup> A gelding is a "male horse who has been castrated." *Id.* at 214. Because the buyer in *Grandi* took possession of the horse following the race, one could argue that such an obvious defect would preclude the buyer's revocation of acceptance under U.C.C. § 2-608(1)(b) (1972). See note 41 *infra* for the text of section 2-608. A failure to make a customary examination of a thoroughbred and discover obvious defects may constitute a waiver of the buyer's right to revoke acceptance. See *Miron v. Yonkers Raceway, Inc.*, 400 F.2d 112, 119-20 (2d Cir. 1968).

The *Grandi* court found that custom did not require the buyer of the gelding to inspect and report defects in the horse before acceptance. First, the court found it to be established custom that a claimant in a claiming race is prohibited from making a prior inspection of the horse other than a quick glimpse of the horse as it moves from the paddock to the starting gate. 399 P.2d at 289. Second, the court found that in New Mexico it was an accepted practice to use medication and to freeze the scrotum. This draws the organs up so that a horse's running will not be hindered. *Id.* Therefore it is nearly impossible even for a careful buyer to determine whether a horse is a colt or a gelding. *Id.*

The court in *Brodsky v. Nerud*, 414 N.Y.S.2d 38 (N.Y. App. Div. 1979), addressed this distinction between the *Miron* and *Grandi* cases. The *Brodsky* court distinguished the claiming race-gelding situation because, unlike *Miron*, the condition could not have occurred after the sale. *Id.* at 41. Therefore, the customary lack of a pre-race examination was of no consequence. *Id.*

<sup>41</sup> U.C.C. § 2-608 provides:

- (1) The buyer may revoke his acceptance of a lot or commercial unit whose non-conformity substantially impairs its value to him if he has accepted it.
  - (a) on the reasonable assumption that its non-conformity would be cured and it has not been seasonably cured; or
  - (b) without discovery of such non-conformity if his acceptance was reasonably induced either by the difficulty of discovery before acceptance or by the seller's assurances.
- (2) Revocation of acceptance must occur within a reasonable time after the buyer discovers or should have discovered the ground for it and before any substantial change in condition of the goods which is not caused by their own defects. It is not effective until the buyer notifies the seller of it.
- (3) A buyer who so revokes has the same rights and duties with regard to the goods involved as if he had rejected them.

U.C.C. § 2-608 (1972). This section is of particular importance if the property involved is a live animal with defects that are difficult to discover. See note 40 *supra*. See also 400 F.2d at 118; J. WHITE & R. SUMMERS, *supra* note 28, § 8-3, at 311. Other factors affecting a reasonable time to inspect and revoke are the buyer's sophistication and the contract of sale. See *id.* at 310-11. See also 400 F.2d at 120 (interpreting the auction's conditions of sale).

expenses incurred in maintaining the horse and \$2,500.00 in punitive damages.<sup>42</sup>

The awards of maintenance and punitive damages are so-called incidental damages awarded pursuant to U.C.C. section 2-715(1).<sup>43</sup> This section allows recovery of damages resulting from the seller's breach and any other expenses "incident to the delay or other breach."<sup>44</sup> The *Grandi* court believed that section 2-715(1) permitted a recovery of punitive damages "where the breach is accompanied by fraudulent acts which are wanton, malicious and intentional."<sup>45</sup> The court awarded damages against the seller, although the trainer had actually entered the horse in the race and listed it as a colt.<sup>46</sup> Justifying its decision, the court recognized that the seller ratified his agent's actions in two ways. First, the seller had seen the track program listing the horse as a colt<sup>47</sup> when he knew the horse was a gelding. Further, the seller failed to advise race officials of the error.<sup>48</sup> Second, he failed to return the sales price following the buyer's rejection and continued to employ the trainer.<sup>49</sup> Thus, the seller "received the benefits of the sale by his acceptance and retention of the

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<sup>42</sup> 399 P.2d at 288.

<sup>43</sup> U.C.C. § 2-715(1) provides, "(1) incidental damages resulting from the seller's breach include expenses reasonably incurred in inspection, receipt, transportation and care and custody of goods rightfully rejected, any commercially reasonable charges, expenses or commissions in connection with effecting cover and any other reasonable expense incident to the delay or other breach." U.C.C. § 2-715(1) (1972). These damages also apply when acceptance is "justifiably revoked." *Id.* at official comment 1.

<sup>44</sup> *Id.*

<sup>45</sup> 399 P.2d at 293. The *Grandi* court did not directly apply section 2-715, but applied section 2-711, which provides the buyer's general remedies if acceptance of goods is justifiably revoked. That section allows recovery of damages under Section 2-712. *See* U.C.C. § 2-711(1)(a) (1972). Section 2-712 allows recovery of the incidental damages of section 2-715(1). *See* U.C.C. § 2-712(2). The leading commentators on the U.C.C. believe section 2-715 ultimately justified the *Grandi* court's award. *See* J. WHITE & R. SUMMERS, *supra* note 28, § 10-3, at 384 & n.37.

<sup>46</sup> The defendant argued that he did not ratify his agent's acts and thus should not be held liable for the misrepresentations. 399 P.2d at 293.

<sup>47</sup> The program in this claiming race showed the entries, their names, age, color and sex. *Id.* at 289. The program in a claiming race is relied upon by persons qualified to make a claim. *Id.* Therefore, a buyer may rely on this data in the same way an auction purchaser may rely on the data contained in an auction catalog. *See* note 72 *infra* and accompanying text.

<sup>48</sup> 399 P.2d at 293.

<sup>49</sup> *Id.*

consideration [and could not] reject the burdens incident thereto,"<sup>50</sup> specifically the liability for punitive damages.

It is usually difficult to discern which punitive damage exception a court has applied because of the similar language of the two exceptions.<sup>51</sup> One method of distinguishing which exception has been applied is to ascertain the U.C.C. section used to justify the award. Because the *Grandi* court applied section 2-715, it is clear that the court believed the punitive damages were "incident to the delay or other breach."<sup>52</sup> If so, then the damages resulted from the contract breach coupled with fraudulent acts rather than the independent tort of fraud.

If an independent tort warrants recovery of punitive damages, the recovery springs not from the "contractual duty" but from "a duty separate from the contract."<sup>53</sup> In this vein, section 2-721 allows recovery of contract damages in an action for fraud.<sup>54</sup> Therefore, through application of the U.C.C., one can reach the same result whether the action is based primarily on a contract breach accompanied by fraudulent conduct, or on an independent tort accompanied by contract damages.<sup>55</sup>

The two approaches differ in the burden of proof. Application of the independent tort approach is difficult at best con-

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<sup>50</sup> *Id.* at 294.

<sup>51</sup> It is very difficult to distinguish between "fraudulent acts" and acts that would constitute the "independent tort" of fraud. This is especially true if courts applying both methods use the terms willful, wanton, malicious and oppressive. See *Keck v. Wacker*, 413 F. Supp. at 1383; *Chernick v. Fasig-Tipton Ky., Inc.*, 83-CI-1365, slip op. at 19 (Fayette Cir. Ct. Apr. 5, 1984); 399 P.2d at 293.

<sup>52</sup> U.C.C. § 2-715(1) (1972). See also note 43 *supra*.

<sup>53</sup> Comment, *supra* note 29, at 95.

<sup>54</sup> U.C.C. § 2-721 provides:

Remedies for material misrepresentation or fraud include all remedies available under this Article for non-fraudulent breach. Neither rescission or a claim for rescission of the contract for sale nor rejection or return of the goods shall bar or be deemed inconsistent with a claim for damages or other remedy.

UCC § 2-721 (1972).

<sup>55</sup> Arguably, if the damages result from the independent tort then this is not truly an exception to the general rule that punitive damages are unavailable for breach of contract. See Comment, *supra* note 29, at 95. Courts and commentators, however, treat it as an exception. See *Ford Motor Co. v. Mayes*, 575 S.W.2d 480, 486 n.3 (Ky. Ct. App. 1978); Sullivan, *supra* note 29, at 236-37.

sidering the indistinct line between the law of tort and contract.<sup>56</sup> This may reduce one's chances of recovery in such an action.<sup>57</sup> The contemporaneous conduct approach bears an easier burden of proof for the plaintiff. As one commentator stated, "[F]raudulent conduct [may cut] across the whole range of contractual relations."<sup>58</sup> For example, in *Grandi* the conduct supporting the punitive award was evident in the contract formation as well as the attempted revocation.<sup>59</sup> Arguably, fraudulent conduct in only one of these areas would support a punitive damages award when mere fraudulent conduct is required.

### B. Kentucky's Approach to Punitive Damages on Contract

Kentucky has followed the general rule that punitive damages are not recoverable for a breach of contract action.<sup>60</sup> Kentucky does recognize an exception when the elements of actionable fraud accompany a breach.<sup>61</sup> Such a standard requires that the defendant make a willful, malicious, wanton or oppressive misrepresentation.<sup>62</sup> Therefore, Kentucky has clearly adopted the independent tort exception to the general rule.<sup>63</sup>

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<sup>56</sup> "It assumes too casually that the line between contract and tort may be precisely drawn; yet marking that boundary line has been acknowledged by some of our ablest scholars to be among the most perplexing challenges in the law." Sullivan, *supra* note 29, at 229-30. See Comment, *supra* note 29, at 95.

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If [this exception] is applied correctly, no amount of fraud in the contract transaction will warrant punitive damages if there is no tort present arising from breach of a duty separate from the ordinary contractual duty. Such a separate duty can be present between parties although their relationship is originally created by the contract.

Comment, *supra* note 29, at 95. For a discussion of the duty in thoroughbred horse cases, see notes 165-69 *infra* and accompanying text.

<sup>58</sup> Comment, *supra* note 29, at 95.

<sup>59</sup> See text accompanying notes 47-50 *supra*.

<sup>60</sup> See *General Accident Fire & Life Assurance Corp. v. Judd*, 400 S.W.2d at 688; *Cumberland Tel. & Tel. Co. v. Cartwright Creek Tel. Co.*, 108 S.W. 875, 878 (Ky. 1908); *Wahba v. Don Corbett Motors, Inc.*, 573 S.W.2d at 360; *Ford Motor Co. v. Mayes*, 575 S.W.2d at 486; *Louisville Bear Safety Serv., Inc. v. South Cent. Bell Tel. Co.*, 571 S.W.2d at 439.

<sup>61</sup> 575 S.W.2d at 486 n.3.

<sup>62</sup> See *Keck v. Wacker*, 413 F. Supp. at 1383.

<sup>63</sup> The Kentucky Court of Appeals expressly rejected the contemporaneous fraudulent conduct exception. "We recognize that some courts have awarded punitive damages

The relatively few Kentucky cases in which the plaintiff has successfully recovered punitive damages in an action stemming from a contract breach evidence the implications of the independent tort approach (i.e., the difficulty of the plaintiff's burden of proof).<sup>64</sup> Although this may be explained by the Kentucky courts' aversion to punitive damages,<sup>65</sup> the better explanation seems to be the inability of plaintiffs to meet their burden of proving the independent tort.<sup>66</sup>

### C. *A Prologue: Keck v. Wacker*

Although the plaintiff in *Keck v. Wacker*<sup>67</sup> failed to establish the existence of an independent tort, no discussion of *Chernick* would be complete without an analysis of *Keck*. *Keck* planted the seed for the *Chernick* court's analysis of the punitive damages issue<sup>68</sup> and the plaintiff's ability to prove the existence of an independent tort.<sup>69</sup>

#### 1. *The Facts of Keck*

The facts of *Keck* and *Chernick* are strikingly similar. In *Keck*, a mare named Plage was listed in the Keeneland sales catalog as "Produce record: 1973 Barren."<sup>70</sup> This information had been provided by Claiborne Farm, the seller's agent. When sold at the Keeneland January sales, the mare was in foal.<sup>71</sup>

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in contract actions without finding a separate tort. . . . However, this court has no authority to disregard the opinions of the Supreme Court of Kentucky or its predecessor court even if we desired to do so." 575 S.W.2d at 486 n.3. See also *Feathers v. State Farm Fire & Casualty*, 667 S.W.2d 693 (Ky. Ct. App. 1983) (recognizing an independent tort action for breach of insurer's covenant to act in good faith).

<sup>64</sup> In most cases recognizing the exception of an independent tort, the plaintiff has been limited to contract damages. See, e.g., 413 F. Supp. at 1383-84; 573 S.W.2d at 360; 575 S.W.2d at 487; 571 S.W.2d at 439.

<sup>65</sup> See *Hensley v. Paul Miller Ford, Inc.*, 508 S.W.2d 759, 764 (Ky. 1974) (Reed, J., concurring) (suggesting that punitive damages should be abolished in Kentucky). See also 575 S.W.2d at 486 n.3.

<sup>66</sup> See cases cited *supra* note 64.

<sup>67</sup> 413 F. Supp. 1377 (E.D. Ky. 1976).

<sup>68</sup> See notes 79-88, 99-103 *infra* and accompanying text.

<sup>69</sup> See notes 89-94, 104-08 *infra* and accompanying text.

<sup>70</sup> 413 F. Supp. at 1380.

<sup>71</sup> *Id.*

Relying on the catalog data,<sup>72</sup> Mrs. Wacker, through her son and a bloodstock agent,<sup>73</sup> was the successful bidder at \$117,000.00. Shortly thereafter the mare slipped the foal that she was carrying when sold.<sup>74</sup> Mrs. Wacker's son subsequently discovered that the mare had slipped in 1972,<sup>75</sup> contrary to the produce record as represented in the sales catalog. Wacker's son was unable to contact the seller or Keeneland's sales director by telephone, so he wrote letters to both parties indicating that the sale should be "null and void."<sup>76</sup> Keck, the seller, refused to nullify the sale and demanded payment. Wacker refused to tender the purchase price, and Keck instituted a suit for a judgment on the sales price.<sup>77</sup> Wacker counterclaimed seeking rescission<sup>78</sup> as well as punitive damages.

## 2. "Slipped" Versus "Barren" and the Usage of Trade

To understand the *Keck* court's decision regarding punitive damages, one must analyze the court's approach to settling what

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<sup>72</sup> "It is customary for buyers to rely entirely upon the catalog data when purchasing a horse at these auctions." *Id.* See also *Overstreet v. Norden Laboratories, Inc.*, 669 F.2d 1286, 1290 (6th Cir. 1982) (catalog description may create an express warranty); *Chernick v. Fasig-Tipton Ky., Inc.*, 703 S.W.2d at 887 (recognizing the high degree of reliance placed upon the catalog by buyers). For a discussion concerning the various portions of the thoroughbred sales catalog, see J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 83-102.

<sup>73</sup> A bloodstock agent is an agent "who represents the purchaser or seller (or both) of thoroughbreds at public or private sale, generally in exchange for a commission." J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 210. See also *id.* at 36 (discussing the pros and cons of hiring a bloodstock agent).

<sup>74</sup> 413 F. Supp. at 1380. The mare slipped the foal shortly after being shipped to Spendthrift Farm in Lexington. The slip was caused by a viral infection, not by any mishandling after the sale. *Id.*

<sup>75</sup> *Id.* Mr. Wacker was informed that the mare had slipped in 1972. Wacker attempted to verify this by calling Claiborne Farm, where the horse had been boarded prior to sale. Claiborne's veterinarian informed Wacker that the farm's records indicated "that the mare had been declared in foal and then was declared barren." *Id.*

<sup>76</sup> *Id.* This was an effective revocation because it was made shortly after discovery of the defect. See *id.* For the text of U.C.C. § 2-608 on revocation of acceptance, see note 41 *supra*.

<sup>77</sup> This action is permitted in U.C.C. § 2-709, which 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 (a) of goods accepted . . ." U.C.C. § 2-709 (1972).

<sup>78</sup> For a discussion of the word rescission, see note 28 *supra*.

may be termed the "slipped" versus "barren" controversy.<sup>79</sup> As mentioned, Keck had reported the mare's produce record as "barren" rather than "slipped."<sup>80</sup> The court and the parties agreed that "barren" meant "bred and did not conceive," while "slipped" meant "bred, conceived and then aborts its foal."<sup>81</sup> The disagreement centered around the application of these definitions. More precisely, the disagreement concerned the proper listing of a mare that is bred and found to be in foal, but on a subsequent examination is found to be "empty" with no sign of a fetus.<sup>82</sup> Keck asserted that such a mare should be listed as "barren," while Wacker argued that such a mare should be listed as "slipped."<sup>83</sup>

Both parties offered experts supporting their side of the controversy.<sup>84</sup> The court applied the definition of usage of trade embodied within U.C.C. section 1-205(2)<sup>85</sup> and held that listing the mare as barren "was not in accordance with a usage of trade in the thoroughbred horse industry."<sup>86</sup> The mare thereby failed

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<sup>79</sup> The primary controversy in *Keck* centered around the use of these terms. See 413 F. Supp. at 1380-81. See also Cohan, *The Uniform Commercial Code as Applied to Implied Warranties of "Merchantability" and "Fitness" in the Sale of Horses*, 73 Ky. L.J. 665, 691-92 (1984-85).

<sup>80</sup> See note 70 *supra* and accompanying text.

<sup>81</sup> 413 F. Supp. at 1381.

<sup>82</sup> *Id.*

<sup>83</sup> *Id.*

<sup>84</sup> Keck's assertion that such a mare should be listed as barren was supported by Claiborne Farm and C.V. Whitney Farm. According to the court, this was also approved, "to some degree," by the Executive Secretary of the Jockey Club, which is the record-keeping authority for the thoroughbred horse pedigrees. *Id.* See also note 174 *infra*.

Wacker's assertion was supported by veterinarians, the general manager of the California Thoroughbred Breeders Association, the owner of Normandy Farm, and John A. Bell, who is the owner of a horse farm and bloodstock agency and former member of the Kentucky Racing Commission. 413 F. Supp. at 1381.

<sup>85</sup> U.C.C. § 1-205(2) provides:

(2) A usage of trade is any practice or method of dealing having such regularity of observance in a place, vocation or trade as to justify an expectation that it will be observed with respect to the transaction in question. The existence and scope of such a usage are to be proved as facts. If it is established that such a usage is embodied in a written trade code or similar writing the interpretation of the writing is for the court.

U.C.C. § 1-205(2) (1972). For a general discussion of usage of trade in the thoroughbred horse industry, see Miller, *supra* note 7.

<sup>86</sup> 413 F. Supp. at 1381. Because there is no trade code for the thoroughbred horse industry, the usage of trade was determined by weighing the conflicting testimony on the issue. See note 84 *supra* and accompanying text.

to conform to the contract description,<sup>87</sup> and her value to Mrs. Wacker was substantially impaired.<sup>88</sup> Because a material misrepresentation existed, the court addressed the propriety of punitive damages.

### 3. *The Tortious Requirements: Willful and Wanton*

The *Keck* court recognized that punitive damages were recoverable but that “the defendants [buyers] have the burden of proving fraud by clear and convincing proof.”<sup>89</sup> To meet this burden, the defrauded buyer must prove six essential elements:

- (1) That [the seller] made a material representation;
- (2) that it was false;
- (3) that when he made it he knew it was false, or made it recklessly, without any knowledge of its truth and as a positive assertion;
- (4) that he made it with intention of inducing [the buyer] to act, or that it should be acted upon by [the buyer];
- (5) that [the buyer] acted in reliance upon it, and
- (6) that [the buyer] thereby suffered injury.<sup>90</sup>

Applying this list of essential elements to the facts in *Keck*,<sup>91</sup> the court held that the catalog description was not done “willfully, maliciously, wantonly or oppressively.”<sup>92</sup> Two facts supported this holding. First, *Keck* had relied upon Claiborne Farm to list the mare in the sales catalog, an act in accordance with the practice in the industry.<sup>93</sup> Second, and most important, Clai-

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<sup>87</sup> 413 F. Supp. at 1381.

<sup>88</sup> Mrs. Wacker's son testified that the mare would have been worth about \$40,000 if it had been listed as “slipped.” In comparison, Mrs. Wacker paid \$117,000 for a “barren” mare. *Id.* at 1382.

<sup>89</sup> 413 F. Supp. at 1383 (citing *Terrill v. Carpenter*, 143 F. Supp. 747 (E.D. Ky. 1956), *aff'd*, 249 F.2d 142 (6th Cir. 1957); *Sanford Constr. Co. v. S & H Contractors, Inc.*, 443 S.W.2d 227 (Ky. 1969)).

<sup>90</sup> *Id.* (citing 443 S.W.2d at 231).

<sup>91</sup> See notes 70-78 *supra* and accompanying text.

<sup>92</sup> 413 F. Supp. at 1383.

<sup>93</sup> *Id.* at 1382.



borne Farms properly relied on a Jockey Club interpretation as to the listing of the mare and "acted upon an honest belief in what it did."<sup>94</sup> As a result, the catalog misdescription was an innocent misrepresentation rather than actionable fraud.

*D. Chernick: Picking Up Where Keck Left Off*

At first glance, *Chernick* and *Keck* appear identical. *Chernick*, however, is "precisely the opposite of *Keck*."<sup>95</sup> Yet, it is quite possible that *Chernick* may have been decided differently had *Keck* not preceded it. A state court is not necessarily bound by federal district court precedent. Nevertheless, *Keck* made two important pronouncements for the *Chernick* court. First, *Keck* established the proper labeling of a mare determined to be in foal and later found to be empty with no evidence of a fetus.<sup>96</sup> Second, it set definite criteria for determining what actions would support a punitive damages award.<sup>97</sup>

Clearly, mares of the type involved in *Keck* must be listed as "slipped" rather than "barren."<sup>98</sup> According to *Keck*, this was "the logical and legal inference to be made."<sup>99</sup> A seller could no longer argue that usage of trade allowed him to list the horse as "barren" rather than "slipped." In effect, case law had determined usage of trade.<sup>100</sup> What had once been a question of fact, open to debate,<sup>101</sup> became a matter of law determined by reference to prior case law, in this instance the *Keck* decision.<sup>102</sup>

<sup>94</sup> *Id.*

<sup>95</sup> Appellee's Reply Brief at 15, *Chernick v. Fasig-Tipton Ky., Inc.*, 703 S.W.2d 885. This difference lies in the presence of evil intent in *Chernick* that was lacking in *Keck*. *Id.* at 15-16. See also notes 105-08 *infra* and accompanying text (listing the specific elements of the seller's fraud in *Chernick*).

<sup>96</sup> *Keck v. Wacker*, 413 F. Supp. at 1381.

<sup>97</sup> See 413 F. Supp. at 1383-84. See also notes 103-08 *infra* and accompanying text (application of the *Keck* criteria to the facts of *Chernick*).

<sup>98</sup> 413 F. Supp. at 1381.

<sup>99</sup> *Chernick v. Fasig-Tipton Kentucky, Inc.*, No. 83-CI-1365, slip op. at 5.

<sup>100</sup> It is questionable whether *Keck* actually determined usage of trade or whether *Keck* merely reported what the usage of trade should be. In any event, the industry usage has conformed to the *Keck* decision. See, e.g., J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 84 (discussing the definition and implication of "slipped").

<sup>101</sup> See note 84 *supra*.

<sup>102</sup> The *Chernick* court did not ponder the question of the proper listing of Fiddler's Colleen. The circuit court merely relied on the *Keck* court's decision as to the proper listing. See No. 83-CI-1365, slip op. at 5-6.

Because the facts established that the sellers in *Chernick* had listed the mare contrary to established law, the court turned its attention to the fraud question. Applying the *Keck* requirements<sup>103</sup> and holding that the sellers acted fraudulently, the court awarded punitive damages.<sup>104</sup> Supporting this decision, the court designated four crucial aspects of the seller's actions: (1) the knowledge of critical facts,<sup>105</sup> (2) the duty to review the catalog descriptions and report mistakes,<sup>106</sup> (3) a reckless or wanton disregard for the rights of others,<sup>107</sup> and (4) a breach of good faith following notice of rejection by the buyer.<sup>108</sup>

Under the *Keck* standard all four of these elements, in one form or another, must be present.<sup>109</sup> In a *Grandi v. LeSage*<sup>110</sup> jurisdiction, where punitive damages require only fraudulent acts accompanying the breach of contract,<sup>111</sup> the buyer need only show acts that are "wanton in character and maliciously intentional."<sup>112</sup> The *Keck-Chernick* standard is clearly the better rule. A seller can be more sure of exactly what his or her liability may be. Under a *Grandi* approach, acts that alone do not constitute fraud may impose punitive liability on an unsuspecting seller. For example, the seller in *Grandi* was not permitted the

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<sup>103</sup> See text accompanying note 90 *supra*.

<sup>104</sup> The *Chernick* court granted the buyers \$40,000 in punitive damages. 703 S.W.2d at 888.

<sup>105</sup> Although the Chernicks were "relative novices in the thoroughbred industry," the court found that they were aware of the importance of disclosing all of the facts of a mare's breeding history. Mr. Chernick was admittedly aware that Fiddler's Colleen was a "problem mare," yet these facts were "deliberately and consciously suppressed." This "suppression" amounted to "conscious wrongdoing," 703 S.W.2d at 889 (citing *Fowler v. Mantooth*, 683 S.W.2d 250 (Ky. 1984)). It also demonstrated the Chernicks' "wanton disregard for the rights of others," 703 S.W.2d at 889 (quoting the trial court and citing *Hensley v. Paul Miller Ford, Inc.*, 508 S.W.2d 759 (Ky. 1974); *Island Creek Coal Co. v. Rodgers*, 664 S.W.2d 339 (Ky. Ct. App. 1982)).

<sup>106</sup> 83-CI-1365, slip op. at 18.

<sup>107</sup> *Id.*, slip op. at 19.

<sup>108</sup> "[T]he Plaintiffs knew they had misrepresented the mare and good faith would have required them to have taken her back." *Id.* at 20.

<sup>109</sup> See 413 F. Supp. at 1383. See also text accompanying note 90 *supra*. The four elements present in *Chernick* fulfilled the six requirements of fraud enunciated in *Keck*. Therefore, these four aspects supported a punitive damages award. 703 S.W.2d at 889.

<sup>110</sup> 399 P.2d 285 (N.M. 1965).

<sup>111</sup> See notes 43-52 *supra* and accompanying text. *But cf.* Comment, *supra* note 29, at 95 (Some jurisdictions require the existence of a tort independent of the contract.).

<sup>112</sup> 399 P.2d at 293.

same type of reliance on his agent's actions as was the seller in *Keck*.<sup>113</sup> Those disagreeing with the *Chernick* decision because of its possible detrimental effect on the horse industry should feel heartened by the court's acceptance of this tougher standard.

Coming full circle, we return to the purpose for awarding punitive damages. If Kentucky continues to apply the independent tort exception to the general rule, a breach of duty "separate from the ordinary contractual duty"<sup>114</sup> will be required. In other words, Kentucky courts should award punitive damages only when the defendant's actions evidence "a spirit of mischief or criminal indifference to civil obligations."<sup>115</sup> As we shall see, the nature of the industry under scrutiny may affect this determination.<sup>116</sup> If this is true, then obviously punitive damages are not available for every contract breach. Because of the prominence of the horse industry in Kentucky, however, the court may have an easier time finding an independent tort.

### III. LIABILITY OF THE AUCTIONEER

The second important holding of *Chernick* is that an auctioneer may be jointly liable for a seller's fraudulent acts.<sup>117</sup> There are two approaches to making such a determination, and a comparison of the circuit and appellate court decisions in *Chernick* illustrates these variant theories. The Fayette Circuit Court found that Fasig-Tipton, as auctioneer, breached a fiduciary duty owed to both the buyer and the seller.<sup>118</sup> The second theory, adopted by the Kentucky Court of Appeals, was that Fasig-Tipton negligently dictated the terms of the sale and conducted

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<sup>113</sup> Compare 399 P.2d at 293 (quoting *Adrian v. Elmer*, 284 P.2d 599, 603 (Kan. 1955)) (principal's failure to promptly repudiate his agent's acts resulted in ratification) with 413 F. Supp. at 1382 (seller's reliance on her agent's actions resulted in innocent misrepresentation by the seller).

<sup>114</sup> Comment, *supra* note 29, at 95.

<sup>115</sup> *Wahba v. Don Corlett Motors*, 573 S.W.2d 357, 360 (Ky. Ct. App. 1978) (quoting *Bisset v. Goss*, 481 S.W.2d 71, 73 (Ky. 1972)); *Louisville & N. R.R. v. Jones Adm'r*, 180 S.W.2d 555, 588 (Ky. 1944).

<sup>116</sup> See notes 163-69 *infra* and accompanying text.

<sup>117</sup> See *Chernick v. Fasig-Tipton Ky., Inc.*, 703 S.W.2d 885, 887-90 (Ky. Ct. App. 1986).

<sup>118</sup> *Chernick v. Fasig-Tipton Ky., Inc.*, No. 83-CI-1365, slip op. at 23-24 (Fayette Cir. Ct. Apr. 5, 1984).

the sale according to those terms.<sup>119</sup> In addition to these theories, both courts agreed that the auctioneer's attempts to limit liability and the public policy surrounding Kentucky's thoroughbred industry supported a finding that Fasig-Tipton should be jointly and severally liable for compensatory damages.<sup>120</sup>

#### A. Breach of Fiduciary Duty

The Fayette Circuit Court clearly stated that "an auctioneer, while primarily the agent of the seller in making the sale, is for some purposes the agent of both parties."<sup>121</sup> Clarifying this initial finding, the court determined that Fasig-Tipton had failed to properly conduct the sale according to the conditions embodied in the consignment contract.<sup>122</sup> Specifically, the court emphasized Fasig-Tipton's breach of a fiduciary duty in the enforcement of the tenth condition of sale, which stated in pertinent part:

Any brood mare so examined whose pregnancy status and/or breeding is found not to be as represented in the veterinarian's certificate provided by consignor . . . may be returned to consignor as unsold. . . . In the event of a material difference in findings between the veterinarians acting for consignor and buyer . . . a third veterinarian shall be designated by the auctioneer . . . who shall examine the mare to determine whether or not she may be returned under this *CONDITION*. . . .<sup>123</sup>

An understanding of this condition is critical because it is nearly identical to conditions that exist in all thoroughbred auction sales.<sup>124</sup> Regardless of the theory used, the interpretation of this

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<sup>119</sup> See 703 S.W.2d at 890.

<sup>120</sup> See *id.* at 890 (In this case, Fasig-Tipton was not liable to Cloverfield Farm for compensatory damages solely because no claim was asserted against Fasig-Tipton for such damages.); No. 83-CI-1365, slip op. at 22-24.

<sup>121</sup> Chernick v. Fasig-Tipton Ky., Inc., No. 83-CI-1365, slip op. at 23 (citing 7A C.J.S. *Auctions and Auctioneers* § 5, at 860 (1980); Parke v. Spurlin, 268 S.W.2d 33, 35 (Ky. 1954)).

<sup>122</sup> *Id.*

<sup>123</sup> Chernick v. Fasig-Tipton Ky., Inc., 703 S.W.2d at 888. The circuit court quoted the condition much more extensively. See No. 83-CI-1365, slip op. at 7-8. The appellate court quoted only that part of the condition emphasized by the circuit court.

<sup>124</sup> See J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 83-84. There has been some effort to standardize these conditions throughout the industry. There remain, however, minor differences that require a prudent buyer to examine closely the conditions. *Id.* at 85.

condition is crucial to a determination of the auctioneer’s liability.<sup>125</sup>

Although the circuit and appellate courts believed that Fasig-Tipton was negligent in its enforcement of this provision,<sup>126</sup> the circuit court also found that Fasig-Tipton failed to apply this condition impartially, in derogation of its fiduciary duty to both parties.<sup>127</sup> While the court’s fiduciary relationship approach was almost indistinguishable from the court’s negligence theory,<sup>128</sup> there are apparently two instances in which a breach of a dual fiduciary duty may occur.

The first possible breach in *Chernick* was Fasig-Tipton’s appointment of a “referee” veterinarian.<sup>129</sup> Rather than accepting the opinion of the first veterinarian it suggested immediately following the sale,<sup>130</sup> Fasig-Tipton appointed a second veterinarian to examine Fiddler’s Colleen.<sup>131</sup> This suggests that Fasig-Tipton may have been engaging in opinion shopping to assure that it received its commission at all costs, clearly short of the fair dealing required of an agent.<sup>132</sup> The vulnerability of Fasig-

<sup>125</sup> Although the appellate and circuit courts implemented different theories, both relied upon Fasig-Tipton’s interpretation and application of this condition. See 703 S.W.2d at 888; No. 83-CI-1365, slip op. at 7-8. A court must consider such a condition when addressing an auctioneer’s liability since “this section of the catalog is written primarily for the protection of the sales company. . . .” J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 83.

<sup>126</sup> See notes 173-210 *infra* and accompanying text.

<sup>127</sup> See notes 121-22 *supra* and accompanying text.

<sup>128</sup> This can be attributed to the necessity of interpreting the tenth condition of sale. See notes 123-25 *supra* and accompanying text.

<sup>129</sup> The “referee” veterinarian is the third veterinarian and is to be designated by the auctioneer. See text accompanying note 123 *supra*.

<sup>130</sup> This second post-sale examination did not rule out the infection found by the buyer’s veterinarian. See note 27 *supra*.

<sup>131</sup> *Id.*

<sup>132</sup> If the auctioneer is an agent of both parties, the *Restatement (Second) of Agency* imposes specific duties:

An agent who, to the knowledge of two principals, acts for both of them in a transaction between them, has a duty to act with fairness to each and to disclose to each all facts which he knows or should know would reasonably affect the judgment of each in permitting such dual agency, except as to a principal who has manifested that he knows such facts or does not care to know them.

RESTATEMENT (SECOND) OF AGENCY § 392 (1958). A failure to appoint veterinarians in accordance with the contract terms is not fair to both parties if the additional veterinarians can only harm the buyer’s position.

Tipton to this argument was compounded by Fasig-Tipton's insistence that the parties abide by the conditions of the sale,<sup>133</sup> conditions that Fasig-Tipton failed to carry out properly.

The second possible breach of a dual fiduciary duty was Fasig-Tipton's improper enforcement of the tenth condition. Regardless of the number of veterinarians appointed to examine Fiddler's Colleen, she remained unsound for breeding purposes.<sup>134</sup> Once this was discovered, Fasig-Tipton had a duty to accept the buyer's rejection or revocation of acceptance.<sup>135</sup> Like the failure to accept the first veterinarian's opinion, the failure to void the sale increased the seller's chances of prevailing because the buyer would have to bring suit to recover the purchase price paid. Assuming the auction company owed a fiduciary duty to the buyer, failure to void the sale would violate that duty.<sup>136</sup>

That an auctioneer is a buyer's agent is indeed an assumption, despite the circuit court's holding to the contrary.<sup>137</sup> Although courts have held that an auctioneer is for some purposes an agent of both the seller and buyer,<sup>138</sup> those holdings have been limited to specific types of auctioneers<sup>139</sup> or

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<sup>133</sup> Following the two post-sale examinations, see note 27 *supra*, the buyer and sellers were discussing an alternative course of action (a 30-day trial of the mare) when the vice president and general manager of Fasig-Tipton interjected. "That is an extraneous warranty which Fasig-Tipton cannot be a part of. It is not part of the conditions of sale. We must get a third veterinarian, a referee veterinarian, and must make that decision now as to who that vet is going to be." No. 83-CI-1365, slip op. at 11. Therefore, the buyer and seller were denied the "freedom to negotiate." *Id.*

<sup>134</sup> This was evidenced by the testimony of the final veterinarian to examine Fiddler's Colleen. See note 27 *supra*. That veterinarian found that the mare had serious "confirmation defects" and a chronic infection "of long standing [that] clearly existed at the time Fiddler's Colleen was sold." No. 83-CI-1365, slip op. at 13. Based on this testimony, the court found that the mare was "not in sound breeding condition at the fall of the hammer." *Id.*

<sup>135</sup> No. 83-CI-1365, slip op. at 16.

<sup>136</sup> *Id.*

<sup>137</sup> See *id.*, slip op. at 23 (citing 7A C.J.S. *Auctions and Auctioneers* § 5 (1980); 268 S.W.2d at 5).

<sup>138</sup> See *Melheiser v. Central Trust Co.*, 36 S.W.2d 377, 379 (Ky. 1931); *Mathis v. Martin*, 228 S.W. 431, 432 (Ky. 1921); *Garth v. Davis & Johnson*, 85 S.W. 692, 693 (Ky. 1905).

<sup>139</sup> For example, all Kentucky cases holding that an auctioneer is an agent of both

duties.<sup>140</sup> This concept should not be expanded automatically to the realm of the thoroughbred auctioneer. Fasig-Tipton and the other thoroughbred auction companies are independent corporations with interests in earning a commission from the seller.<sup>141</sup> The auctioneer should not be required to jeopardize that commission by telling the purchaser that the mare is not worth the price paid even though the mare has no physical defects. Clearly such a statement would "affect the judgment" of the buyer in deciding whether to bid on the mare.<sup>142</sup> This, however, is the function of the buyer's independent agent,<sup>143</sup> and there is no need to impose such a duty on the auctioneer.

The better approach begins with the proposition that the auctioneer is the seller's agent. This is the traditional view of the courts addressing auctioneer agency in general<sup>144</sup> and in the

parties involve the sale of realty. See cases cited *supra* note 138. See also Parke v. Spurlin, 268 S.W.2d 33.

<sup>140</sup> The general rule is that "the auctioneer is also treated as the agent of the purchaser for the purpose of making the written evidence at the time of the sale, but his authority to represent the purchaser is thus limited." Johnson v. Haynes, 532 S.W.2d 561, 564-65 (Tenn. Ct. App. 1975) (citing Green v. Crye, 11 S.W.2d 869, 870 (Tenn. 1928)). See also Schwinn v. Griffith, 303 N.W.2d 258, 262 (Minn. 1981) (auctioneer is an agent of the buyer to the extent he binds the buyer through the memorandum of sale.); Tulsa Auto Dealers Auction v. North Side State Bank, 431 P.2d 408, 412 (Okla. 1966) (auctioneer is an agent of the buyer only after the hammer falls). The nature of the double agency may be explained as follows:

While an auctioneer is an agent of both seller and purchaser for signing a contract of sale, it does not follow that his agency for the one is coextensive in its nature and duration with that for the other; his agency for the purchaser is usually conferred when the bid is accepted and begins at the fall of the hammer. Such an authority must be exercised contemporaneously with the sale; but his agency for the seller is generally more extensive, and may cover time both before and after the sale.

7A C.J.S. *Auctions and Auctioneers* § 5, at 860-61 n.75 (1980). This is a crucial distinction in a case such as *Chernick* in which misrepresentations exist before the sale and the auctioneer's negligence appears following the sale.

<sup>141</sup> They are, however, "affected with a public interest and therefore should be held to a higher standard of honesty, integrity and performance than an ordinary private corporation." 83-CI-1365, slip op. at 23.

<sup>142</sup> An agent must disclose any facts that "affect the judgment" of the buyer. RESTATEMENT (SECOND) OF AGENCY § 392 (1958). See note 132 *supra* for the text of section 392.

<sup>143</sup> See J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 31-40.

<sup>144</sup> See, e.g., Becker v. Crabb, 4 S.W.2d 370, 371 (Ky. 1928); *In re Premier Container Corp.*, 408 N.Y.S.2d 725, 729 (N.Y. Sup. Ct. 1978). See also 7A C.J.S. *Auctions and Auctioneers* § 5 (1980).

context of a thoroughbred auction sale.<sup>145</sup> This approach may, once again, require that a distinction be made between contract and fraud actions.

Just as in the punitive damages issue, *Grandi v. LeSage*<sup>146</sup> presents both the U.C.C. and the breach of contract approaches to discerning an agent's liability. *Grandi* did not involve an auctioneer but did consider the liability of the seller's agent, in that case the trainer.<sup>147</sup> Recall that the trainer had entered the horse in a claiming race and registered the horse as a colt when, in fact, the trainer knew that the horse was a gelding.<sup>148</sup> The New Mexico Supreme Court held the trainer not liable for any damages resulting from the seller's breach.<sup>149</sup> Relying on the U.C.C.'s lack of authority, the court found "nothing therein evidencing an intent that an agent of the seller shall be held liable along with the seller."<sup>150</sup> Thus, in an action in which only U.C.C. damages are sought, the seller's agent is not liable.<sup>151</sup>

The Louisiana decision of *Castille v. Folck*<sup>152</sup> supports this proposition. The *Castille* court agreed that an action based on contract, seeking rescission and damages, was unavailable against the seller's agent, in that case, the auctioneer.<sup>153</sup> The court did

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<sup>145</sup> See *Miron & Yonkers Raceway, Inc.*, 400 F.2d 112, 113 (2d Cir. 1968); *Castille v. Folck*, 338 So. 2d 328, 331 (La. Ct. App. 1976).

<sup>146</sup> 399 P.2d at 285.

<sup>147</sup> *Id.* at 290-91.

<sup>148</sup> *Id.* at 288-89. See also notes 39-40 *supra* and accompanying text.

<sup>149</sup> The court held the trainer not liable for return of the purchase price because he did not receive any of the purchase price from the buyer. *Id.* at 290. As a corollary to this holding, the trainer was also held not liable for incidental damages incurred "in the care and custody of the goods." *Id.* Finally, punitive damages were not recoverable because there had been no recovery of compensatory damages against the trainer. *Id.* at 291.

<sup>150</sup> *Id.* at 290. Although the court was referring to expenses related to the upkeep of the gelding, it was this failure to award incidental damages that also limited the recovery of punitive damages against the agent. See note 149 *supra*.

<sup>151</sup> This is assuming that the agent did not receive any of the buyer's purchase price. If the auctioneer holds the sales proceeds, as in the ordinary thoroughbred consignment situation, that auctioneer may be liable to the buyer for the purchase price held. See U.C.C. § 2-711(1) (1972) (buyer may recover purchase price paid); RESTATEMENT (SECOND) OF AGENCY § 339 (1958) (agent's duty to return items received if the transaction is rescinded for a cause existing at the time of receipt by the agent).

<sup>152</sup> 338 So. 2d 328 (La. Ct. App. 1976).

<sup>153</sup> *Id.* at 332. Specifically, the *Castille* court held, "We know of no authority . . . which would authorize a suit for rescission of sale being brought against the agent of



hold, however, that the plaintiff-buyer's allegations did support an action *ex delicto*<sup>154</sup> based on the misrepresentations of the seller and auctioneer.<sup>155</sup> The *Castille* court found the auctioneer personally liable because he had "pledge[d] his own responsibility" by making "the rules of the game."<sup>156</sup> Thus, under *Castille*, once an auctioneer dictates the terms defining the relationship of the parties, he assumes an additional responsibility to the buyer.<sup>157</sup> This is the same approach that the circuit court in *Chernick* used to determine agency liability,<sup>158</sup> and it was also the crux of the appellate court's negligence theory.<sup>159</sup>

### B. *Negligence of the Auctioneer*

The Kentucky Court of Appeals in *Chernick* did not use the word "agent" in its opinion. It is unclear whether this omission

the seller. A suit for rescission of sale, be it for error of fact or redhibition, must be brought against the seller." *Id.* This holding is in line with the approach taken by the *Restatement*: "Unless otherwise agreed, a person making or purporting to make a contract with another as agent for a disclosed principal does not become a party to the contract." RESTATEMENT (SECOND) OF AGENCY § 320 (1958). *See also* RESTATEMENT (SECOND) OF AGENCY § 328 (1958) (An agent is not liable for nonperformance of a contract to which he is not a party.).

<sup>154</sup> 338 So. 2d at 332. An action *ex delicto* in this case is an action in tort. *See* BLACKS LAW DICTIONARY 509 (5th ed. 1979). *See also* Sayers & Muir Service Station v. Indian Refining Co., 100 S.W.2d 687, 689 (Ky. 1936).

<sup>155</sup> 338 So. 2d at 332. The auctioneer had sold a broodmare named Flying Cobre and misrepresented that the mare had been Coggins tested and that a Coggins certificate would be furnished to the purchaser. *Id.* at 330-32.

A Coggins test is a test used to determine whether a horse is a carrier of "Equine Infections Anemia," a malady more commonly known as swamp fever. *Id.* at 331 n.1. *See also* J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 212. A Coggins certificate is merely proof that the test was negative. 338 So. 2d at 331 n.1.

<sup>156</sup> 338 So. 2d at 333 (quoting the trial court). This brought the situation in *Castille* outside the realm of the general rule that "an agent is not responsible to third persons where his principal is disclosed." *Id.* *See also* note 153 *supra*.

<sup>157</sup> 338 So. 2d 333. Specifically, in the thoroughbred consignment industry:

It is the agent who, in effect, says to the principal, "I will sell your horses for you if you meet the standard and representations I make to prospective purchasers." There can be little doubt that under these circumstances, [the auctioneer] obligated himself to make sure all horses met the requirements as advertised.

*Id.* (quoting the trial court).

<sup>158</sup> The Fayette County Circuit Court held that thoroughbred auction companies have the duty to provide the rules and regulations governing the sale of thoroughbreds at auction. "In this case the Defendant, Fasig-Tipton, ha[d] undertaken to perform that duty by unilaterally dictating the terms and conditions of sale." No. 83-CI-1365, slip op. at 22.

<sup>159</sup> *See* 703 S.W.2d at 889-90.

was intentional. The court did adopt the circuit court opinion in two specific areas: The awarding of punitive damages<sup>160</sup> and Fasig-Tipton's public responsibility.<sup>161</sup> The opinion, however, did not specifically adopt the circuit court's agency theory. The court of appeals decision recognized that a judicial admission rendered the sellers liable for the entire compensatory damage award.<sup>162</sup> The court felt compelled, however, to opine what damages an auctioneer in Fasig-Tipton's position *should* pay. Therefore, the court's dictum imposes a liability on the auctioneer worth examination.

Whether a defendant is negligent in any given situation depends on the standard of conduct applied. The *Chernick* court held that Fasig-Tipton's actions were not to be "reviewed at a level lower than that of strict scrutiny."<sup>163</sup> This is consistent with the idea that auction sales companies, by dictating the terms of the sale,<sup>164</sup> have assumed the duty of "fostering" and "encouraging" the "thoroughbred horse industry within the Commonwealth" of Kentucky.<sup>165</sup> Kentucky legislative policy aims at promoting the thoroughbred industry.<sup>166</sup> Kentucky statutes, how-

<sup>160</sup> "This court is in complete agreement with the Fayette Circuit Court's findings and conclusions and will not disturb the award of punitive damages." *Chernick v. Fasig-Tipton Ky., Inc., id.* at 888.

<sup>161</sup> *Id.* at 890.

<sup>162</sup> *Id.* at 889. Counsel for the buyers stated in court: "'We don't make any claim for any other damages, or any damages, other than the return of our money against Fasig-Tipton'" *Id.* The court held that this statement fell within the definition of a judicial admission. *Id.* See also *Arnett v. Thompson*, 433 S.W.2d 109, 114 (Ky. 1968) (quoting *Sutherland v. Davis*, 151 S.W.2d 1021, 1024 (Ky. 1941)) (A judicial admission is a "formal act done in the course of judicial proceedings."); *George M. Eady v. Stevenson*, 550 S.W.2d 473, 473-74 (Ky. 1977) ("The doctrine of judicial admissions should be applied only when the statements are unequivocal and must be considered to be deliberately true or false.") Therefore, the court held that Fasig-Tipton was absolved of liability. 703 S.W.2d at 889.

<sup>163</sup> 703 S.W.2d at 890.

<sup>164</sup> See note 158 *supra*.

<sup>165</sup> *Chernick v. Fasig-Tipton Ky., Inc.*, No. 83-CI-1365, slip op. at 22.

<sup>166</sup> Kentucky Revised Statutes § 230.215 provides in pertinent part:

It is the policy of the commonwealth of Kentucky, in furtherance of its responsibility to foster and to encourage legitimate occupations and industries in the commonwealth and to promote and to conserve the public health safety, and welfare, and it is hereby declared the intent of the commonwealth to foster and to encourage the thoroughbred horse breeding industry within the commonwealth and to encourage the improvement of the breed of thoroughbred horses. . . .

KY. REV. STAT. ANN. § 230.215(1) (Bobbs-Merrill 1982) [hereinafter cited as KRS].

ever, center on the racing aspect of the industry<sup>167</sup> and leave largely unregulated the sales aspect.<sup>168</sup> Thus, the *Chernick* court determined that auction companies have assumed "the duty of providing the rules and regulations which govern the sale of thoroughbred horses by auction in Kentucky."<sup>169</sup> Partially based on this civic responsibility, Fasig-Tipton's negligence was evident in three instances: (1) The drafting of the consignment form,<sup>170</sup> (2) the failure to assure the accuracy of the seller's representations in the sales catalog,<sup>171</sup> and (3) the interpretation and enforcement of the contract.<sup>172</sup>

### 1. *The Consignment Form*

The consignment form drafted by Fasig-Tipton required that the seller provide information regarding a broodmare's current and immediately preceding year's produce.<sup>173</sup> Fasig-Tipton was to obtain information on previous years from a private corporation having access to Jockey Club statistical information.<sup>174</sup> Furthermore, the conditions of sale defined "barren" to mean "the mare was bred, was not found to have slipped and failed to produce a foal."<sup>175</sup> This would allow a veterinarian to list a

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<sup>167</sup> See KRS §§ 230.210-.360 (1982 & Cum. Supp. 1984). The intent of these sections is to "vest in the [racing] commission forceful control of thoroughbred racing." KRS § 230.215(2).

<sup>168</sup> No. 83-CI-1365, slip op. at 22.

<sup>169</sup> *Id.*

<sup>170</sup> 703 S.W.2d at 890.

<sup>171</sup> *Id.*

<sup>172</sup> No. 83-CI-1365, slip. op. at 14, 22-23. The court of appeals did not reach this issue because the court found that Fasig-Tipton's negligence in drafting the consignment form was sufficient to impose liability. See 703 S.W.2d at 890.

<sup>173</sup> 703 S.W.2d at 887.

<sup>174</sup> *Id.* The Jockey Club Registration Department "maintains and publishes the American Stud Book, in which breeders can learn the blood lines of every thoroughbred registered in the United States," which is "indispensable to the breeding and racing of thoroughbred horses in the United States." *Jockey Club v. United States*, 137 F. Supp. 419, 421 (Ct. Cl.), *cert. denied*, 352 U.S. 834 (1956).

<sup>175</sup> No. 83-CI-1365, slip op. at 6. This was the definition provided by Fasig-Tipton despite the "well recognized" inference from *Keck v. Wacker*, 413 F. Supp. 1377 (E.D. Ky. 1976), that a mare once found to be in foal had slipped unless there was evidence to the contrary. No. 83-CI-1365, slip op. at 5-6.

mare as barren even though the veterinarian knew that the mare had been in foal.<sup>176</sup>

The form "facilitated" this error by failing to request information on whether the mare was bred and whether a mare so bred had not conceived or had conceived and aborted her foal.<sup>177</sup> Therefore, even assuming that a seller truthfully completed the consignment form, he may have failed to include information material to a "breeder's decision making process."<sup>178</sup> In *Chernick*, the previous slips of Fiddler's Colleen and the slipping of twins was material<sup>179</sup> and would be material to any prudent buyer.<sup>180</sup> Fasig-Tipton has the ability and expertise to draft a proper contract, and failure to fully utilize that expertise was and is negligent.<sup>181</sup>

## 2. *The Accuracy of the Seller's Representations*

Fasig-Tipton was found to have "a fiduciary duty to the purchaser and to the Commonwealth's most prestigious and valued industry to use ordinary care to ensure that its catalog and/or announcements were as accurate and comprehensive as possible."<sup>182</sup> In other words, as in *Castille v. Folck*,<sup>183</sup> the auctioneer has assumed a duty to assure that all horses meet the advertised requirements.<sup>184</sup>

<sup>176</sup> No. 83-CI-1365, slip op. at 6. For example, there may be no direct evidence (i.e., a fetus) that would show that a mare had aborted. Therefore, a mare that had "slipped" would technically fit the definition of "barren" as provided by Fasig-Tipton unless evidence of the slip were present. See *id.*

<sup>177</sup> *Id.*

<sup>178</sup> 703 S.W.2d at 890. "[I]nformation that a mare 'slipped twins' is material to a breeder's decision-making process when the horse is being considered for purchase." *Id.*

<sup>179</sup> *Id.*

<sup>180</sup> If a mare has "slipped" or "slipped twins," it may be indicative of physical damage to the mare, and the mare's propensity for slipping in the future increases. See J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 84.

<sup>181</sup> 703 S.W.2d at 890.

<sup>182</sup> *Id.* The original court of appeals' opinion found that Fasig-Tipton was a "guarantor" for all the information in its catalog. See *Chernick v. Fasig-Tipton Ky., Inc.*, 32 KLS 11, at 1 (Ky. Ct. App. Aug. 16, 1985), *withdrawn and reissued*, 703 S.W.2d 885 (Ky. Ct. App. 1986).

<sup>183</sup> 338 So. 2d at 328 (La. Ct. App. 1975).

<sup>184</sup> *Id.* at 332-33. This is remarkably similar to the *Chernick* court's holding in this context: "In the instant situation [the] delinquency served to place Fasig-Tipton on notice that its sales catalog was incomplete and that it was under a duty to report such ensuing inaccuracies or to correct them." 703 S.W.2d at 890.

The appellate division of the New York Supreme Court, in *Brodsky v. Nerud*,<sup>185</sup> applied this same rule to a claiming race. Just as in *Grandi v. LeSage*,<sup>186</sup> discussed previously,<sup>187</sup> the seller had entered a gelding in a claiming race and incorrectly listed the horse's sex as a colt. Upon learning that the horse's sex was incorrectly listed, the buyer brought suit for rescission and damages against the seller and the New York Racing Association (NYRA). The NYRA argued that it was neither a party to a contract nor a fiduciary, and therefore, "any unintentional mistake or misrepresentation is not actionable."<sup>188</sup>

The court recognized that, although the plaintiff's complaint was one of rescission, it was sufficient "to give the NYRA notice that its representation (for example, in the track program) led to the plaintiff's reliance and ultimate damage."<sup>189</sup> Therefore, the NYRA's failure to discover the improper listing and correct the mistake in the racing program or by announcement "may have constituted actionable negligence."<sup>190</sup>

The New York court did not decide the negligence issue. The court, however, did recognize the cause of action. Like the auctioneer, the racing association conducting a claiming race has a duty to use reasonable care to assure that the representations in its racing program are accurate. More importantly, this duty was found to exist regardless of a fiduciary or contractual relationship.<sup>191</sup> Therefore, an auctioneer or a racing association by conducting the sale could be negligent, and thus liable for damages, even though not an agent of the buyer *or* seller.

To assure that the catalog representations were accurate, Fasig-Tipton relied on two sources: The Jockey Club computer system<sup>192</sup> and the veterinary health certificate required to be filed

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<sup>185</sup> 414 N.Y.S.2d 38 (N.Y. Sup. Ct. 1979).

<sup>186</sup> 399 P.2d 285 (N.M. 1965).

<sup>187</sup> See notes 37-52 *supra* and accompanying text.

<sup>188</sup> 414 N.Y.S.2d at 40. This argument comports with the general rule of *Castille* and *Grandi* that an action for contract rescission is unavailable against the seller's agent because the agent is not a party to the contract. See 338 So. 2d at 332; 399 P.2d at 290.

<sup>189</sup> 414 N.Y.S.2d at 40.

<sup>190</sup> *Id.*

<sup>191</sup> Neither the plaintiff nor the court disputed the NYRA's denial of the agency or contractual relation.

<sup>192</sup> 703 S.W.2d at 890.

with the seller's consignment form.<sup>193</sup> Neither of these sources was sufficient in *Chernick*.

Fasig-Tipton admitted that the Jockey Club information concerning Fiddler's Colleen was delinquent beyond the normal two-year parameters. As a result, Fasig-Tipton should have been on notice that its sales catalog was incomplete or inaccurate and that it had a duty to report or correct any inaccuracies.<sup>194</sup> Once again, Fasig-Tipton was negligent when it failed to report or correct the inaccuracies in its catalog.

### 3. *The Interpretation and Enforcement of the Contract*

Fasig-Tipton's final negligent act surrounded the contract that it had drafted. In drafting its own contract, Fasig-Tipton had given itself and its agents the authority to act and carry out the contract's terms.<sup>195</sup> Fasig-Tipton's agents, however, negligently applied that authority. This is most evident in their negligent enforcement of the examination provisions of the tenth condition of sale.<sup>196</sup> Particularly important was Fasig-Tipton's appointment of the "referee" veterinarian.<sup>197</sup> That veterinarian found Fiddler's Colleen to be "normal."<sup>198</sup> The court considered the previous and subsequent<sup>199</sup> examinations and determined that she had not been sound for breeding purposes at the fall of the hammer. Thus, Fasig-Tipton's "referee" veterinarian was negligent when he found Fiddler's Colleen to be "normal."<sup>200</sup> Fasig-

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<sup>193</sup> *Id.*

<sup>194</sup> *Id.*

<sup>195</sup> 83-CI-1365, slip op. at 10.

<sup>196</sup> See note 123 *supra* and accompanying text. This is indistinguishable from the circuit court's fiduciary duty approach. See notes 121-59 *supra* and accompanying text.

<sup>197</sup> See note 27 *supra*. See also notes 129-32 *supra* and accompanying text.

<sup>198</sup> 83-CI-1365, slip op. at 12.

<sup>199</sup> See note 27 *supra*.

<sup>200</sup> The veterinarian orally reported that

"the mare had problems and she was inflamed inside, but that he did not see any pus (exudate) at the time he examined her and that he felt it was possible to get her in foal, but the only way she would be able to carry a foal would be a deep suture.

No. 83-CI-1365, slip op. at 12. That veterinarian did not sign a certificate, as did the previous veterinarians, but later sent a letter that recited "that he had examined Fiddler's Colleen . . . and found her to be normal on rectal and speculum examination." *Id.*

Tipton was liable for his negligence<sup>201</sup> and for failure to properly interpret the unambiguous terms of Fasig-Tipton's contract. "[I]t was the duty of the Defendant, Fasig-Tipton, to void the sale and declare the mare to be the property of the seller."<sup>202</sup>

#### IV. SUGGESTIONS FOR AVOIDING LIABILITY

A close analysis of *Chernick* is a valuable tool for the seller and auctioneer wishing to avoid liability. By comparing *Chernick* with similar cases, it is possible to devise a framework for avoiding liability. Of course, some problems, such as evil intent, can be corrected only by changing an individual's behavior. But a change in the drafting and enforcement of sale terms may prevent liability absent any actual intent to deceive.

##### A. *The Consignment Form*

The Kentucky Court of Appeals clearly stated how to avoid liability resulting from a faulty consignment form. Specifically, the court noted, "Fasig-Tipton has at its disposal the expertise necessary to ascertain such information and to formulate a questionnaire the responses to which would convey a mare's complete produce record. By so doing Fasig-Tipton would comply with both its contractual and professional duty to fully disclose all material facts."<sup>203</sup> Therefore, the form used must "convey a mare's complete produce record."<sup>204</sup> In 1984, due to the cases discussed previously, most sales companies added "slipped" to their consignment forms and catalogs.<sup>205</sup> In addition, sales companies have changed their bid boards to include a sign reading "not in foal" in addition to the regular "in foal" and "barren" signs.<sup>206</sup>

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<sup>201</sup> *Id.* This conforms to the general rule that a principal is liable for the negligent acts of his agent. *See, e.g.,* RESTATEMENT (SECOND) OF AGENCY § 265 (1958).

<sup>202</sup> No. 83-CI-1365, slip op. at 14-16.

<sup>203</sup> *Chernick v. Fasig-Tipton Ky., Inc.*, 703 S.W.2d 885, 90 (Ky. Ct. App. 1986).

<sup>204</sup> *Id.*

<sup>205</sup> *See* J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 84. Prior to 1984, the mares were being offered as "'In Foal,' which means the mare . . . is believed to be in foal . . .;" *Id.* "Barren," which means that the mare is believed to be sound for breeding but failed to conceive when bred; and "Not Bred," which means that the mare is sound for breeding but, for whatever reason, was not bred. *Id.*

<sup>206</sup> *Id.*; Hollingsworth, *supra* note 4, at 5147.

This is a step in the right direction, but there remain some loopholes through which a misrepresentation could pass. For example, a mare might be listed as "slipped" when, in fact, the mare had "slipped twins." Whether a mare had aborted one fetus or twins is a material fact and, if misstated, could lead to a cause of action for breach of warranty or fraud.<sup>207</sup> The auction company must make sure that the consignment form reveals all facts surrounding a slip or other physical defect. This would best be accomplished by requiring that the seller reveal all pertinent facts in textual form. Among these facts should be recent breeding efforts and results.

Finally, in representing the horse's condition, the auction companies cannot rely on outdated statistical information. Auction companies have an affirmative duty, at least in Kentucky, to use reasonable care to assure that all pertinent facts are accurate and to report or correct any inaccuracies. This requires a request that the seller or consignor provide breeding status information for all prior years, not just the last two. Auction companies should then compare this to all available data, to assure that they have fully used their expertise. The auction company must also make all the natural inferences that would result from this knowledge.<sup>208</sup>

To correct the data, auction companies should either note the change in the catalog or in the auctioneer's announcement, because the announcement takes precedence over the catalog.<sup>209</sup> Announcing corrections and videotaping the sale will provide back-up proof as to the exact representation ultimately made to the buyer.<sup>210</sup>

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<sup>207</sup> 703 S.W.2d at 890.

<sup>208</sup> For example, delinquent or missing data should put the auctioneer "on notice" that a problem may exist. *Id.* Furthermore, if the examination ten days before the sale shows that the horse is barren when the horse had been previously found to be in foal, then the auctioneer should realize that the mare has slipped. *Chernick v. Fasig-Tipton Ky., Inc.*, No. 83-CI-1365, slip op. at 5-6 (Fayette Cir. Ct. Apr. 5, 1984).

<sup>209</sup> See J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 84. See also note 22 *supra*.

<sup>210</sup> Two authors give the following advice to the novice horse trader:

If the catalogue says the mare is in foal, and you don't listen to the announcements which say she's barren or has slipped, you're responsible for the price you paid, thinking she was in foal. The sales are videotaped, today, and the sales company will play the videotape of the announcement back to you, and say, "sorry about that."

J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 84.



### B. *Fulfilling Obligations in Conducting the Sale*

In all cases involving thoroughbred auctioneers, the auctioneer's first line of defense is always that he is merely a stakeholder for the parties to the sale.<sup>211</sup> This defense, however, has gained little recognition.<sup>212</sup> Once an auction company dictates the sale terms, U.C.C. section 1-102<sup>213</sup> obligates it to impartially carry out the terms.<sup>214</sup> These terms necessarily address some of the "practicalities and peculiarities of the thoroughbred horse auction business."<sup>215</sup> Therefore, auction companies should properly carry out the contract's terms rather than omit them from the agreement.

Strictly enforcing the agreement will best serve the goal of proper sale conduct. If the agreement calls for three veterinary examinations, then pre-sale examinations should be counted. Alternatively, the condition may be rewritten to include only those veterinary exams occurring after the sale. Such a condition should be acceptable to both the industry and the courts because

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<sup>211</sup> See, e.g., *Chernick v. Fasig Tipton Ky., Inc.*, 703 S.W.2d at 889; *Castille v. Folck*, 338 So. 2d 328, 330 (La. Ct. App. 1976). The New York Racing Association made a similar assertion when it argued that it was not a party to any contract in *Brodsky v. Nerud*, 414 N.Y.S.2d 38, 41 (N.Y. S. Ct. 1979).

<sup>212</sup> The principle reason for the rejection of this argument has been the auctioneer's undertaking to dictate the sale terms and guaranty the accuracy of catalog information. 703 S.W.2d at 890; 338 So. 2d at 333. See also notes 156-58 *supra* and accompanying text.

<sup>213</sup> U.C.C. § 1-102 provides in pertinent part:

(3) The effect of provisions of this Act may be varied by agreement, except as otherwise provided in this Act and *except that the obligations of good faith, diligence, reasonableness and care prescribed by this Act may not be disclaimed by agreement* but the parties may by agreement determine the standards by which the performance of such obligations is to be measured if such standards are not manifestly unreasonable.

U.C.C. § 1-102 (1972) (emphasis added). The tenth condition of Fasig-Tipton's sale clearly falls within this provision. See note 123 *supra* and accompanying text. The emphasized portion of U.C.C. § 1-102 supports the general rule that a party may not contractually disclaim its own negligence under the U.C.C. No. 83-CI-1365, slip op. at 21. This rule must be distinguished from the rule outside the U.C.C. in which one may disclaim his own negligence by express agreement. See PROSSER & KEETON, *THE LAW OF TORTS* 482-84 (5th ed. 1984).

<sup>214</sup> See notes 122-36 *supra* and accompanying text.

<sup>215</sup> No. 83-CI-1365, slip op. at 21.

the critical time for evaluating the horse's soundness is immediately after the fall of the hammer.<sup>216</sup>

Proper interpretation of the sales contract does not end the auction company's duty. The auction company may still be liable if the examinations are conducted improperly. For example, the Fayette Circuit Court held Fasig-Tipton liable for the negligence of the veterinarian that they chose.<sup>217</sup> Thus, it is important to retain a qualified, experienced veterinarian who will give an impartial opinion about the horse's soundness. A veterinarian chosen based on his past record of examinations favorable to the auctioneer may subject even an otherwise prudent auctioneer to liability.

All of these requirements point to two words that sum up the auctioneer's duty: fairness and impartiality. Regardless of whether the auctioneer is an agent of the buyer and the seller, his position as a final adjudicator<sup>218</sup> and holder of the public trust<sup>219</sup> requires that he complete the sale with a view to more than merely recovering his commission.

### CONCLUSION

The end result of *Chernick* was correct. The sellers were or should have been aware that they were misrepresenting the breeding history of Fiddler's Colleen. The auctioneer, although not a party to the sale contract, helped promote the fraud through the auctioneer's negligence and should likewise be liable. The Kentucky Court of Appeals' use of dictum in this case is question-

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<sup>216</sup> The Fayette Circuit Court implied that excluding those exams prior to the sale would be the better approach.

While it may be more logical to exclude the seller's veterinarian's certificate rendered within ten (10) days before sale this is not what is provided in the tenth condition. Perhaps that is what it ought to provide since it is the condition of a mare at the fall of the hammer which is the issue and not her condition either before or after the fall of the hammer. Obviously an examination within twenty-four (24) hours after the fall of the hammer would be best calculated to determine her condition at the time of sale.

No. 83-CI-1365, slip op. at 14.

<sup>217</sup> See note 201 *supra* and accompanying text.

<sup>218</sup> See J. LOHMAN & A. KIRKPATRICK, *supra* note 11, at 85.

<sup>219</sup> See 703 S.W.2d at 890. "Fasig-Tipton had a fiduciary duty to the purchaser, and to the Commonwealth's most prestigious and valued industry." *Id.*

able. Regardless of whether the use of dictum was proper, Kentucky courts have shown their propensity for making such a decision, and their decision should send a warning to the seller and consignor to beware.

The common theme pervading the circuit and appellate court decisions is the importance of the thoroughbred industry to Kentucky. That fact not only imposes a public responsibility on thoroughbred consignment companies, but also justifies punitive damages awards by imposing a duty on the seller separate from his contractual duty to the buyer.

Consignment companies have been charged with the duty of upholding the integrity of Kentucky's thoroughbred sales industry. This blanket statement, however, may be too extreme, for it is clear that although "[a]uction sales are of public concern,"<sup>220</sup> auctioneer's are not "public officer[s],"<sup>221</sup> and any attempt to raise them to such a level should arguably be a legislative function. In any event, the consignor, as the seller's agent, may be liable for fraudulent misrepresentation unless he takes affirmative steps assuring full use of professional resources to determine whether any discrepancies exist in the catalog descriptions.<sup>222</sup> The question then becomes whether the auctioneer's actions as the seller's agent, impose liability on an innocent seller.<sup>223</sup>

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<sup>220</sup> *Robenson v. Yann*, 5 S.W.2d 271, 274 (Ky. 1928).

<sup>221</sup> *Sumuller v. Fuchs*, 1 A. 120, 122 (Md. 1885). That case went on to note that an auctioneer's business "is essentially a private one. He may sell or not, as he pleases, and is not in any respect under the slightest obligations to the public." *Id.*

<sup>222</sup> An agent failing to correct such misrepresentations may be liable to the same extent as if he had made the misrepresentations or "knowingly assist[ed] in the commission of tortious fraud or duress." RESTATEMENT (SECOND) OF AGENCY § 348 (1958). Comment c offers the following hypothetical:

[I]f an agent who has been given misinformation by a principal, on the strength of which he makes statements to a third person, later discovers the untruth and refrains from taking steps to inform the other party, the agent is subject to liability if subsequently the other party completes the transaction with the principal or another agent, relying in part upon the statements of the first agent.

RESTATEMENT (SECOND) OF AGENCY § 348, Comment c (1958).

<sup>223</sup> Address by Robert Miller at the Continuing Legal Education Seminar on equine law (May 2, 1986) (outline of remarks available in University of Kentucky Continuing Legal Education office).

The effect of *Chernick* in other jurisdictions will depend on the emphasis that the jurisdiction places on the thoroughbred industry. In those states in which the promotion of the thoroughbred is embodied in statutes (as in Kentucky),<sup>224</sup> the courts likely will follow the *Chernick* court's reasoning.<sup>225</sup> In states in which the commitment to the industry is not statutorily prescribed, *Chernick's* impact is less clear. Nevertheless, even the dicta in *Chernick* should influence any court considering a similar issue.

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<sup>224</sup> Aside from the Kentucky statutory approach of general promotion of the thoroughbred industry, some states regulate the public sale of thoroughbred horses. For example, Florida requires special licensing of thoroughbred "sales organizations." FLA. STAT. ANN. § 535.01 (West Cum. Supp. 1986). Similarly, California law provides for revocation of an auctioneer's license where the auctioneer misrepresents the nature of the items to be sold. CAL. BUS. & PROF. CODE § 5776(p) (West Cum. Supp. 1986).

Statutes of this nature may become important when an auctioneer misstates the results of a sale or allows agents to buy back their horses. See Hollingsworth, *supra* note 4, at 5146. See also CAL. BUS. & PROF. CODE § 5776(o) (Cum. Supp. 1986).

<sup>225</sup> Public policy interests, however, will not be sufficient merely because the "state regulates the business." *Rutter v. Arlington Park Jockey Club*, 510 F.2d 1065, 1069 (7th Cir. 1975). In *Rutter*, the court would not invalidate on public policy grounds an exculpatory clause that disclaimed negligent performance of a contractual obligation. *Id.* at 1069. When a jurisdiction takes such a view, it may be possible for the auction company to disclaim its negligence.