IN THE SUPERIOR COURT OF THE STATE OF DELAWARE

CRS PROPPANTS LLC d/b/a NORTHERN WHITE SAND LLC, a Delaware limited liability company,	)	
Plaintiff and Counterclaim Defendant,	)	
v.	)	C.A. No. N15C-08-111 MMJ CCLD
PREFERRED RESIN HOLDING COMPANY, LLC, a Delaware limited liability corporation,	)	
Defendant and Counterclaim Plaintiff.	)	

Submitted: August 17, 2016
Decided: September 27, 2016

Upon Plaintiff and Counterclaim Defendant's Motion for Summary Judgment
GRANTED IN PART
DENIED IN PART

OPINION

Peter J. Walsh, Jr., Esq. (Argued), Jennifer C. Wasson, Esq., Jesse L. Noa, Esq., Potter Anderson & Corroon LLP, Attorneys for Plaintiff and Counterclaim Defendant CRS Proppants LLC d/b/a Northern White Sand LLC

Oderah C. Nwaeze, Esq., Robert M. Palumbos, Esq. (Argued), Duane Morris LLP, Attorneys for Defendant and Counterclaim Plaintiff Preferred Resin Holding Company, LLC

JOHNSTON, J.

PROCEDURAL CONTEXT

This dispute is over an admitted breach of contract to buy certain quantities of sand used in the oil and gas industry. On August 27, 2015, Plaintiff CRS Proppants d/b/a Northern White Sand LLC ("CRS") sued Defendant Preferred Resin Holding Company, LLC ("Preferred"). CRS alleged Preferred breached several provisions of the parties' heavily-negotiated Purchase and Sale Agreement ("PSA"). On September 30, 2015, Preferred answered and filed counterclaims, alleging that the PSA's liquidated damages provision is unenforceable, and that there are material questions of fact regarding the parties' proposed dry/wet plant expansion.

On June 10, 2016, CRS filed its motion for summary judgment. CRS argues it is entitled to summary judgment because Preferred admitted it did not make two consecutive quarterly purchases. CRS also contends that the liquidated damages provision is unambiguous and enforceable. Finally, CRS asserts that Preferred has no valid defense to its failure to perform pursuant to the PSA.

STATEMENT OF FACTS

CRS is a supplier of northern white sand, which is typically used in the process of hydraulic fracturing. Preferred uses dry sand for its resin-coated products business, and ships dry sand to its customers who are directly involved in hydraulic fracturing.

Preferred entered into the PSA, dated July 3, 2014, to purchase sand from CRS. CRS was acquired by plaintiff Northern White Sand LLC.

In early 2014, CRS informed Preferred that it was preparing to expand its "Plant" in order to increase sand producing capacity. Section 2.1(g) in the PSA allowed for an automatic reduction in the Quarterly Quantities if CRS did not complete its "Plant" expansion by April 1, 2015.

CRS produces two types of sand – dry and wet – that are used in the hydraulic fracturing process. CRS maintains two sand-producing facilities, a Dry Sand Plant ("Dry Plant") and a Wet Sand Plant ("Wet Plant"). CRS completed expansion of its dry plant on March 12, 2015. On March 26, 2015, Preferred notified CRS of the completion. CRS did not complete expansion of its wet plant until after June 1, 2015.

The PSA provides for certain "Quarterly Quantities" that Preferred was obligated to purchase from CRS on a quarterly basis. Section 2.2(a) of the PSA set forth a "Buyer Deficiency Payment" ("BDP"), that Preferred was required to pay to CRS if Preferred defaulted on the contract. The parties negotiated the BDP at a rate of $25 per ton of unpurchased Quarterly Quantity sand.

On April 15, 2015, Preferred failed to purchase a required Quarterly Quantity of sand. Preferred also failed to purchase the Quarterly Quantity for the second

quarter of 2015. Section 9.1 of the PSA provides that Preferred is in default of the PSA upon failure to purchase the Quarterly Quantity in a given quarter. Section 9.2 requires CRS to notify Preferred in writing of any breach in order to initiate default proceedings. CRS notified Preferred and invoked Section 9.3 of the PSA. CRS demanded payment of the BDP within 30 days pursuant to Section 2.2(a).

Section 3.1 of the PSA provides the price terms for the quarterly purchase quantities until the third quarter of 2015 ("Q3 2015"). Section 3.2 of the PSA states that all payments beyond, and including, Q3 2015 would be adjusted for local economic conditions.

STANDARD OF REVIEW

Summary judgment is granted only if the moving party establishes that there are no genuine issues of material fact in dispute and judgment may be granted as a matter of law.[1] All facts are viewed in a light most favorable to the non-moving party.[2] Summary judgment may not be granted if the record indicates that a material fact is in dispute, or if there is a need to clarify the application of law to the specific circumstances.[3] When the facts permit a reasonable person to draw only one inference, the question becomes one for decision as a matter of law.[4] If the

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[1] Super. Ct. Civ. R. 56(c).
[2] *Burkhart v. Davies*, 602 A.2d 56, 58–59 (Del. 1991).
[3] Super. Ct. Civ. R. 56(c).
[4] *Wooten v. Kiger*, 226 A.2d 238, 239 (Del. 1967).

non-moving party bears the burden of proof at trial, yet "fails to make a showing sufficient to establish the existence of an element essential to that party's case," then summary judgment may be granted against that party.[5]

ANALYSIS

Liquidated Damages Provision

The PSA was heavily negotiated by sophisticated parties. Mr. Cobb, CRS' president, negotiated on CRS' behalf. Preferred's Chief Operating Officer negotiated on Preferred's behalf. Outside counsel assisted both parties in drafting and negotiation. Preferred's in-house also counsel actively participated.

Section 2.1 of the PSA outlined the quarterly quantities Preferred was required to buy from CRS. Section 2.2(a) provides in part:

> Subject to Section 2.2(c), if Buyer fails for any reason (other than due to Seller's failure to make sufficient Material available to Buyer pursuant to and in accordance with any Valid Purchase Order or any other breach by Seller of its obligations to supply such Material under this Agreement) to purchase any Quarterly Quantity during the Term, then Buyer shall, no later than thirty (30) days after the end of such calendar quarter, pay a Seller a **"Buyer Deficiency Payment"** equal to: Buyer Shortfall Quantity *multiplied by* the Buyer Deficiency Fee *where* . . . **"Buyer Deficiency Fee"** = $25.00/ton.

Section 2.5(a) provides in part:

> Subject to Section 2.5(d), in the event that Seller fails (other than due to a breach by Buyer of its obligations under this Agreement) to deliver

[5] *Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986).

> any of the Quarterly Quantity in accordance with Buyer's Valid Purchase Orders in any calendar quarter during the term (the "**Seller Delivery Shortfall**"), Seller shall, no later than thirty (30) days after the end of such calendar quarter, pay Buyer a "**Seller Deficiency Payment**" equal to: Seller Delivery Shortfall Quantity *multiplied by* the Seller Deficiency Fee *where* . . . **"Seller Deficiency Fee"** = $25.00/ton.

Sections 2.2(a) and 2.5(a) are nearly identical, reciprocal deficiency fee provisions.

Section 9.1(c) states that it shall be an "Event of Default" if either Party fails to make any payment when due in accordance with the PSA.

Section 9.3 provides, in pertinent part:

> Upon termination of the Agreement by Seller as a result of the occurrence of an Event of Default by Buyer which remains uncured after expiration of all applicable cure periods in Section 9.2, Seller may, at its sole option, upon notice to Buyer . . ., accelerate and declare due and payable an amount equal to the aggregate Quarterly Quantity (*i.e.*, the amount of Material that should have been purchased) for the remaining Term of the Agreement (as if the Agreement had continued to the expiration of the Initial Term) multiplied by the Buyer Deficiency Fee[.]

Section 9.3 is the parties' liquidated damages clause for Preferred's potential breach.

Section 9.4 states, in pertinent part:

> Upon termination of the Agreement by Buyer as a result of the occurrence of an Event of Default by Seller which remains uncured after expiration of all applicable cure periods in Section 9.2, Buyer may, at its sole option, upon notice to Seller . . ., accelerate and declare due and payable an amount equal to the aggregate Quarterly Quantity (*i.e.*, the amount of Material that should have been supplied) for the remaining Term of the Agreement (as if this Agreement had continued to the expiration of the Initial Term) multiplied by the Seller Deficiency

Fee.

Section 9.4 mirrors Section 9.3, and is the parties' liquidated damages clause for CRS' potential breach.

Preferred contracted to buy 39,000 tons of sand in the first quarter ("Q1") of 2015, and 48,000 tons of sand in the second quarter ("Q2") of 2015. The parties do not dispute that Preferred failed to buy the contracted-for amounts in Q1 and Q2. Preferred's failures to buy the required Quarterly Quantity each constitute an Event of Default pursuant to the PSA. CRS provided Preferred a written notice of default on July 10, 2015. Preferred failed to cure the Events of Default within the required timeframe. On August 14, 2015, CRS terminated the PSA pursuant to Section 9.2. CRS also invoked the liquidated damages clause under Section 9.3.

Liquidated damages is the amount the parties to a contract have agreed, at the time of entering into the contract, will satisfy any loss or injury flowing from a breach of their contract.[6] Delaware's contract law allows parties to agree to a good faith estimate of actual damages which may result from termination of a contract.[7] Liquidated damages clauses are presumed valid.[8] In contrast, a penalty is a contractual sum that serves as a punishment for default, rather than as a measure of

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[6] *S.H. Deliveries, Inc. v. TriState Courier & Carriage, Inc.*, 1997 WL 817883, at *2 (Del. Super.).
[7] *Delaware Bay Surgical Servs., P.C. v. Swier*, 900 A.2d 646, 650 (Del. 2006).
[8] *S.H. Deliveries, Inc.*, 1997 WL 817883, at *2.

compensation for breach.[9] An agreement to pay a stipulated sum upon breach, irrespective of the damages sustained, constitutes a penalty.[10] A penalty provision is void as a matter of public policy.[11] Preferred bears the burden to show that the liquidated damages clause in the PSA is a penalty.[12]

Determining whether a stipulated sum is a liquidated damages provision is a two-part test.[13] First, are the reasonably-anticipated damages difficult to ascertain at the time of contracting because of indefiniteness or uncertainty?[14] Second, is the amount stipulated either a reasonable estimate of the future damages, or reasonably proportionate to the damages that actually have been caused by the breach?[15]

Damages are Difficult to Ascertain

The parties extensively negotiated the PSA. Only the first four quarters had explicit pricing. The parties included several price adjustments to reflect future uncertainty. For example, Section 3.2 called for a bi-annual price adjustment based on several factors. These factors included the Produced Price Index and the price of natural gas. At the time of contracting, the parties did not know the exact purchase price for the subsequent 16 quarters due to these price adjustments.

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9 *Id.*
10 *Id.*
11 *Id.*
12 *Id.*
13 *Id.*
14 *Id.*
15 *Id.*

The parties also considered a "macro-economic" shock provision. CRS proposed a provision to protect the parties against extraordinary macro-economic fluctuations in the industry. CRS' proposed language stated: "In the event of an extraordinary economic condition such as a major macro-economic shock (i.e., high inflation, high interest rates, etc.), threshold barometers will be determined under which the normal governance of the indexing function will be modified to account for the existing extraordinary economic condition." Preferred rejected the provision.

These provisions reflect the parties' recognition that damages were difficult to ascertain at the time of contracting. Prices consistently fluctuated. The industry was well aware of the realistic possibility of catastrophic economic conditions.

Liquidated Damages are a Reasonable Estimate of Actual Damages

The second prong is whether the stipulated-for damages are either a reasonable estimate, or reasonably proportionate to, actual damages. CRS has alleged that liquidated damages are approximately $24 million. Preferred contends that the liquidated damages provision is neither a reasonable estimate nor reasonably proportionate to the admitted approximately $1.5 million in damages.

During negotiation of the PSA, the parties considered both advanced pre-payments and liquidated damages. In the end, the parties agreed to a lower

pre-payment in exchange for higher liquidated damages.

Section 9.3 allows CRS to accelerate and declare due and payable an amount equal to the aggregate Quarterly Quantity for the remaining Term of the Agreement multiplied by the $25/ton Buyer Deficiency Fee. Thus, the later during the course of the PSA a breach occurred, the lower the damages. Because Preferred breached the contract early, the damages are proportionately higher. The $25.00/ton fee is approximately half of the parties' contracted-for pricing.

The parties also provided expert damages calculations. Preferred's expert calculated damages at $17,957,946.00. CRS' expert calculated damages at $31,927,566.00.

The Court finds that the PSA formula for determining liquidated damages is a reasonable estimate of future damages when the breach occurs near the beginning of the contract term. Additionally, CRS' proffered liquidated damages amount is between the parties' experts' calculations. Therefore, The Court finds that liquidated damages are reasonably proportionate to actual damages.

Parties Intended Section 9.3 to be a Liquidated Damages Clause

Preferred has the burden to show that the liquidated damages clause is invalid. Preferred argues that Section 9.3 is an unenforceable penalty because CRS' negotiator, Mr. Cobb, intended it to be a penalty for Preferred's non-performance.

Mr. Cobb testified at deposition that the purpose of Sections 9.3 and 9.4 was "ultimately, what you want as a businessperson is to have a contract perform. And if the contract does not have any penalties associated with it, the counterparty is less likely to perform. So the purpose of those provisions [Sections 9.3 and 9.4] is really to try and keep both parties performing."

CRS asserts that the parties intended Section 9.3 to be a liquidated damages provision in case Preferred breached. CRS also argues that the parties included a reciprocal provision, Section 9.4, in case CRS breached the PSA. CRS contends these provisions are incentive clauses, and an incentivizing clause is not tantamount to a penalty.

The Court will enforce a liquidated damages clause if the parties unambiguously intended to create one.[16] Generally, a fixed amount regardless of the breach is considered intent to impose a penalty.[17]

In *Delaware Bay Surgical Services, P.C. v. Swier* ("*Swier*"),[18] the Delaware Supreme Court upheld a liquidated damages provision that explicitly used the word "penalty." In *Swier*, Dr. Swier contracted to work with Delaware Bay Surgical Services for two years.[19] His employment contract included a $25,000 payment for

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[16] *Ballenger v. Applied Digital Solutions, Inc.*, 2002 WL 749162, at *12 (Del. Ch.).
[17] *S.H. Deliveries, Inc*, 1997 WL 817883, at *2.
[18] 900 A.2d 646 (Del. 2006).
[19] *Id.* at 649.

early termination.[20] The clause stated:

> TERMINATION WITHOUT CAUSE. This agreement may be terminated by either party upon one (1) month's prior written notice.
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> In recognition of the expenses incurred by Employer in employing Employee and introducing Employee to the medical community, and aiding the procurement by Beebe Medical Center, of certain equipment needed by Employee to perform certain procedures at the hospital, if Employee terminates this agreement prior to the end of its term, Employed agrees to pay Employer an early termination penalty equal to $25,000.00.[21]

Dr. Swier terminated his contract early.[22] Delaware Bay Surgical Services sought payment of the $25,000.[23] This Court found that Dr. Swier owed Delaware Bay Surgical Services $25,000 in liquidated damages.[24]

On appeal, the Delaware Supreme Court analyzed the liquidated damages provision under Delaware's two-prong test.[25] The Court found that there was sufficient evidence that at the time of contracting, calculating the damages was uncertain and that $25,000 was a reasonable estimate and not unconscionable. The Court disregarded the use of the term "penalty."

In *Piccotti's Restaurant v. Gracie's, Inc.*,[26] this Court found that the

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[20] *Id.*
[21] *Id.*
[22] *Id.*
[23] *Id.*
[24] *Id.*
[25] *See id.* at 650–51.
[26] 1988 WL 15338 (Del. Super.).

contracting parties intended to create a liquidated damages clause, not a penalty. In *Piccotti's,* plaintiffs agreed to sell restaurant business assets to defendants.[27] Defendants promised not to use the "Piccotti's" name in new ventures. The sale contract provided:

> Sellers and Buyers agree that since it is exceptionally difficult to assess damages in the event that the Buyers violate all or part of this agreement, it is hereby mutually agreed that in the event that Buyers do in fact violate one or more of the terms of this agreement that Buyers shall be liable to pay damages to Sellers in the amount of $15,000.00 plus costs and reasonable attorney's fees involved in any litigation or court action needed to enforce this agreement . . . .[28]

Defendants used the Picotti's name, and plaintiffs sued to recover $15,000 in liquidated damages.[29] Defendants contended the liquidated damages provision was an unenforceable penalty because actual damages could not be proven.[30]

The *Piccotti's* Court found the parties intended the contract provision to be a liquidated damages clause. The Court determined that the language itself was evidence that damages resulting from a breach would be difficult to calculate.[31] Additionally, this language did not "operate so as to exact a stipulated sum from the defendants irrespective of harm."[32]

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[27] *Id.* at *1.
[28] *Id.*
[29] *Id.*
[30] *Id.* at *1–2.
[31] *Id.* at *2.
[32] *Id.*

Preferred relies on certain cases (not involving Delaware law), in which the courts invalidated liquidated damages clauses as penalties.

In *In re Trans World Airlines, Inc. ("TWA")*,[33] the United States Court of Appeals for the Third Circuit found, under New York law, that a liquidated damages provision was intended to be a penalty. In *TWA*, TWA leased two planes from Interface Group-Nevada.[34]

TWA filed for bankruptcy and repudiated its lease.[35] Interface claimed entitlement to liquidated damages.[36] TWA argued that the liquidated damages provision was void.[37] The United States Bankruptcy Court for the District of Delaware and the United States District Court for the District of Delaware held that the liquidated damages provision was void as an unenforceable penalty because there was no reasonable relationship to actual damages.[38]

On appeal, the Court of Appeals affirmed. The Court found that the clause unduly shifted the burden of making Interface whole onto TWA. The Court hypothesized that, if TWA breached with one month left in the contract, Interface's

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[33] 145 F.3d 124 (3d Cir. 1998).
[34] *Id.* at 128.
[35] *Id.* at 129.
[36] *Id.*
[37] *Id.*
[38] *Id.* at 134.

actual damages only would be one month's rent.[39] Nonetheless, the Court stated that the liquidated damages provision would require TWA to pay either the difference between termination value and resale value **or** the difference between termination value and the monthly rent.[40] The Court found this was grossly disproportionate to Interface's actual damages.

In *Lake River Corp. v. Carborundum*,[41] the United States Court of Appeals for the Seventh Circuit found that a contract's liquidated damages provision was an unenforceable penalty under Illinois law. The defendant, a manufacturer of a steel precursor, contracted with plaintiff to provide distribution services.[42] The contract included a liquidated damages clause.

Defendant failed to ship the guaranteed amount. Defendant owed plaintiff $241,000 – the full $533,000 contract amount minus what defendant already paid for plaintiff's bagging of the supplied quantity.[43] Plaintiff sought $241,000 as liquidated damages. The United States District Court for the Northern District of Illinois awarded plaintiff its liquidated damages.

On appeal, the Court of Appeals reversed the liquidated damages ruling. The Court ruled that the parties' damage formula was a penalty "because it is designed

[39] *Id.* at 135.
[40] *Id.*
[41] 769 F.2d 1284 (7th Cir. 1985)
[42] *Id.* at 1286.
[43] *Id.*

always to assure [plaintiff] more than its actual damages. The formula – full contract price minus the amount already invoiced to [defendant] – is invariant to the gravity of the breach."[44]

Both *TWA* and *Lake River Corp.* are distinguishable. In this case the liquidated damages clause is not a set fee, which would disregard the timing and gravity of the breach. Instead, the forecast damages bear a reasonable relationship to actual damages. Preferred has provided no evidence, other than Cobb's deposition reference, to show that the parties intended that Section 9.3 be a penalty. The parties negotiated identical, reciprocal liquidated damages provisions: Section 9.3 was for Preferred's breach, Section 9.4 was for CRS' breach. The provisions calculated liquidated damages on a sliding scale proportionate to the timing of the breach: the Buyer (or Seller) Deficiency Quantity multiplied by the $25.00/ton Buyer (or Seller) Deficiency Fee. Section 9.3 is not a rigid calculation irrespective of the gravity of the breach. Rather, the parties "intended to fix an amount compensable in contemplation of the potential loss that might flow from a breach."[45]

Commercial Impracticability and Frustration of Purpose Defenses

Preferred admits it did not purchase the Quarterly Quantities for the first and second quarters of 2015. Preferred contends that its failure was excused by two

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[44] *Id.* at 1290.
[45] *See S.H. Deliveries, Inc,* 1997 WL 817883, at *2.

defenses. First, it contends commercial impracticability excuses its performance. Commercial impracticability applies when: (1) an event occurs that the parties assumed would not happen; (2) continued performance is not commercially practicable; and (3) the party asserting the defense (*i.e.,* Preferred) did not expressly or impliedly agree to performance in spite of impracticability.[46] Performance may be impracticable because of extreme and unreasonable difficulty, expense, injury, or loss to one of the parties involved.[47]

Alternatively, Preferred contends that the market downturn frustrated the contract's purposes. A frustration of purpose defense is available when: (1) there is substantial frustration of the principal purpose of the contract; (2) the parties assumed that the frustrating event would not occur; and (3) the Defendant is not at fault.[48] Performance may remain possible, but is excused because it "would make little sense" to continue where the object frustrated was the basis of the contract.[49]

Preferred contends there is ample evidence that the fracking sand market experienced an extraordinary downturn beginning in early 2015. The decline was unprecedented and unforeseeable in its magnitude and duration. Preferred argues that market participants sought cheaper proppants (fracking sand is a proppant) due

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[46] *Mountaire Farms, Inc. v. Williams,* 2005 WL 1177569, at *5 (Del. Super.).
[47] RESTATEMENT (SECOND) OF CONTRACTS § 261 cmt. d.
[48] *Chase Manhattan Bank v. Iridium Africa Corp.,* 474 F.Supp.2d 613, 620 (D.Del. 2007).
[49] RESTATEMENT (SECOND) OF CONTRACTS § 265 cmt. a (1981).

to this downturn. Market-wide demand for resin-coated sand fell by 50%; prices dropped 40%. This left Preferred with an expensive, unsellable product. Preferred argues that purchasing the quarterly quantities at the prices in the PSA would have resulted in devastating out-of-pocket losses for Preferred. Preferred would have incurred a $6 million loss each quarter had it continued to perform. Preferred also contends it would have incurred a $137/ton operating loss for each ton it may have sold by the first quarter of 2016. Continued performance would have been catastrophic. The commercial impracticability and frustration of purpose defenses obviated Preferred's duty to honor the PSA.

CRS contends that fracking sand's very nature makes market downturns anticipatory events. Further, Preferred has weathered several market downturns, rendering its argument useless. CRS also contends that Preferred implicitly or expressly agreed to perform in spite of the impracticability by striking the "macro-economic shock" provision from the contract. The provision was to be included to further reflect the fracking sand market's volatility.

In *Friedco of Wilmington, Delaware, Ltd. v. Farmers Bank of the State of Delaware,*[50] Friedco and Farmers negotiated a 35-year lease for office space in

[50] 529 F.Supp. 822 (D. Del. 1981).

1967.[51] Farmers agreed to pay a *pro rata* share of the building's utility costs, not to exceed $1.10/square foot of occupied space.[52]

Friedco filed suit to set aside the *pro rata* cap as commercially impracticable.[53] Friedco argued that the dramatic rise in utility prices cost Friedco $1.43/square foot in utilities.[54] Farmers argued the utility provision was not impracticable.[55]

The United States District Court for the District of Delaware found in Farmers's favor.[56] The *Friedco* Court examined all three commercial impracticability factors, and found none of them favored Friedco. First, the *Friedco* Court found that the parties did not ignore the possibility of changing utility costs in its long-term contract.[57] Farmers' price varied with the rates Friedco paid until that rate reached the $1.10/square foot cap.[58] Further, the cap itself assigned potential burden (*i.e.,* costs greater than $1.10/square foot) to Friedco.[59] The *Friedco* Court stated that "contracting parties may allocate the risks at levels which they recognize as being realistic possibilities during the term of the contract without

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[51] *Id.* at 824.
[52] *Id.*
[53] *Id.*
[54] *Id.* at 828.
[55] *Id.* at 824.
[56] *Id.* at 830.
[57] *Id.* at 826.
[58] *Id.*
[59] *Id.*

assigning risks that are wholly unforeseeable at the time of their negotiations. . . ."[60]

The *Friedco* Court then examined whether an event occurred contrary to a basic assumption of the contract. The *Friedco* Court pointed out that "the parties to any contract to be performed over a term normally assume that the cost of performance may fluctuate during the term, and, as a result, courts ordinarily do not conclude that an increase in the cost of performance is an event the non-occurrence of which was a basic assumption of the contract."[61] Friedco argued that the unforeseen utility rate rise is an event the non-occurrence of which was a basic assumption of the contract because rates at the 1979 level were unforeseen when the parties contracted.[62] The *Friedco* Court disagreed, stating that the parties recognized the possibility of utility costs in excess of $1.10/square foot, and expressly assigned the burden of costs above that level to Friedco.[63] Finally, the *Friedco* Court found that Friedco's paying $1.43/square foot for its utility costs was not "excessive and unreasonable" and the failure to excuse performance would not result in grave injustice.[64]

Similarly, in *Transatlantic Financing Corp. v. U.S.*,[65] the United States Court

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[60] *Id.*
[61] *Id.* at 827.
[62] *Id.*
[63] *Id.* at 828.
[64] *Id.* at 831 (quoting *Gulf Oil Corp. v. F.P.C.*, 563 F.2d 588, 599 (3d Cir. 1977)).
[65] 259 F.Supp. 725 (D.C. 1965), *affirmed*, 362 F.2d 312 (D.C. Cir. 1966).

of Appeals for the District of Columbia Circuit affirmed a United States District Court for the District of Columbia decision finding that commercial impracticability did not occur. In *Transatlantic,* the parties entered into an agreement on October 2, 1956, where Transatlantic agreed to transport wheat from Galveston, Texas to Iran.[66] The agreement did not prescribe the route to take, but the most direct route was through the Suez Canal.[67] Transatlantic's ship left Texas on October 27, 1956.[68] Two days later, Israel invaded Egypt.[69] Two days after that, Great Britain and France invaded the Suez Canal Zone.[70] In response, Egypt closed the Suez Canal to traffic on November 2, 1956.[71] Transatlantic's ship was rerouted around the Cape of Good Hope.[72] Transatlantic sought additional funds from the United States due to commercial impracticability – the Suez's closure forced Transatlantic to take an alternate route.[73] The Court dismissed Transatlantic's claim.[74]

On appeal, the Court of Appeals affirmed. The Court of Appeals found that:

> [T]o justify relief [from a contract based on impracticability], there must be more of a variation between expected cost and the cost of performing by an available alternative than is present in this case,

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[66] *Id.* at 726.
[67] *Id.*
[68] *Id.*
[69] *Id.*
[70] *Id.*
[71] *Id.*
[72] *Id.* at 726–27.
[73] *Id.* at 727.
[74] *Id.* at 728.

> where the promisor can legitimately be presumed to have accepted some degree of abnormal risk, and where impracticability is urged on the basis of added expense alone.[75]

In *Gulf Oil Corp. v. F.P.C.*,[76] the Federal Power Commission ("FPC") ordered Gulf Oil Corporation ("Gulf") to deliver large quantities of natural gas to the Texas Eastern Transmission Company's pipelines.[77] In 1963, Gulf and Texas Eastern entered into a Gas Purchase Contract.[78] Gulf warranted that there would a quantity of gas to meet a volume not less than 125% of the Daily Contract Quantity (500,000 MCF).[79] Gulf overestimated its natural gas reserves to be used in the deal.[80] From 1973 to 1975, Gulf's deliveries fell short of Texas Eastern's demands, and, at times, short of the contract-specified quantities.[81] The FPC issued a show cause order to Gulf.[82]

Gulf contends its performance of the contract was excused by commercial impracticability.[83] Gulf contends unforeseen circumstances rendered performance excessive and unreasonable, and its performance may be excused.[84] The United

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[75] *Transatlantic,* 363 F.2d at 319.
[76] 563 F.2d 588 (3d Cir. 1977).
[77] *Id.* at 593.
[78] *Id.*
[79] *Id.* at 594.
[80] *Id.* at 593.
[81] *Id.*
[82] *Id.* at 596.
[83] *Id.* at 597.
[84] *Id.* at 599.

States Court of Appeals for the Third Circuit disagreed with Gulf's contentions. The *Gulf* Court found that Gulf's express warranty "that there will be provided a quantity of gas sufficient to enable Seller to have available for delivery . . ." is not a mere promise. Gulf assumed the entire risk that future conditions would raise the cost of gas.[85] The *Gulf* Court also found commercial impracticability would not occur even without the warranty. Even if Gulf's costs to deliver the warranted-for gas were exorbitant, Gulf was estimated to make a $190 million profit on the Texas Eastern contract.[86] This rendered the impracticability defense futile.

Restatement (Second) of Contracts Section 261 discusses impracticability.[87] Comment c provides in part:

> A party may, by appropriate language, agree to perform in spite of impracticability that would otherwise justify his non-performance. . . . Even absent an express agreement, a court may decide, after considering all the circumstances, that a party impliedly assumed such a greater obligation. . . . Circumstances relevant in deciding whether a party has assumed a greater obligation include [its] ability to have inserted a provision in the contract expressly shifting the risk of impracticability to the other party.[88]

In this case, Preferred has not demonstrated that either defense applies. The 2014–15 sudden economic downturn was not unknown to Preferred. Its own expert discussed four oil downturns from 1990 to the present. Preferred's expert's report

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[85] *Id.*
[86] *Id.* at 600.
[87] RESTATEMENT (SECOND) OF CONTRACTS § 261.
[88] *Id.* cmt. c.

showed that the crude oil price plummeted from $140/barrel to $30/barrel as recently as the 2008 global crisis. Preferred knew, or should have known, that a downturn in the oil and gas industry was foreseeable. Preferred assumed the risk of performing in spite of any foreseeable potential impracticability.[89] Preferred's performance is not excused by commercial impracticability or frustration of purpose.

Definition of "Plant"

Section 2.1(g) of the PSA provides:

> The Quarterly Quantities have been established in contemplation of Seller's expansion of the Plant, scheduled for start-up in the first calendar quarter of 2015. **In the event that Seller does not complete its contemplated expansion of the Plant so as to be operational by April 1, 2015, the Quarterly Quantities shall be deemed to be automatically adjusted so as to be maintained at the level in effect for the first of quarter of 2015** as set forth in the table in Section 2.1(a) above until such expansion of the Plant is completed. Upon completion of such expansion of the Plant, Seller shall notify Buyer thereof in writing and, if such expansion is completed after June 1, 2015, Buyer shall have the option either to (i) maintain the Quarterly Quantities at the level in effect for the first quarter of 2015 as set forth in the table in Section 2.1(a) above or (ii) increase the Quarterly Quantities to the amounts set forth in the table in Section 2.1(a) above for the applicable calendar quarters for the remainder of the term. (Emphasis added.)

It is undisputed that CRS completed the expansion of its dry plant prior to

[89] *See id.* (stating that a party may agree to perform in spite of impracticability that would normally excuse its non-performance).

April 1, 2015. It is also undisputed that Preferred reduced the Quarterly Quantities even though CRS had the capacity to provide the Q2 quantity of 48,000 tons of sand as of April 11, 2015.

CRS argues that it was improper for Preferred to reduce the Quarterly Quantities and to refuse to purchase the Q2 quantity of sand. It asserts that the Plant Expansion Term was included in the PSA to ensure that CRS could meet Preferred's volume demands. It contends that the purpose of the term was to seek flexibility in order to accommodate CRS' substantial volume commitments to Preferred. CRS maintains that the term "Plant" only refers to the dry plant. Therefore, Preferred was contractually bound to purchase the Q2 quantity of sand. CRS argues that a separate "Wet Sand Agreement" governed potential expansions to the wet plant.

Preferred argues that its purchase of the Q2 quantity of material was contingent on CRS' completion of the "Plant." Preferred asserts that CRS approved a planned expansion of its processing facility, or "Plant," in April of 2014. It contends that the term "Plant" included both CRS' dry and wet sand facilities. In support of this contention, Preferred relies on the fact that the state of Wisconsin treated the two sites as a single facility for permitting purposes. Preferred also cites the fact that CRS provided Preferred with information regarding the expansion of ***both*** facilities during a presentation. Preferred further states that it relied on this

presentation information during discussions with CRS.

Preferred asserts that CRS could have exercised an expansion option that would have allowed CRS to pick up an additional 850,000 tons from June 2015 through March 2016. It contends that this option would only have been necessary if CRS had decided not to expand its wet sand plant. Therefore, Preferred argues that CRS knowingly communicated to Preferred that CRS would not be expanding its wet plant by failing to exercise this option.

The Court must determine if it can decide, as a matter of law, whether the "Plant" was completed by April 1, 2015. If so, it must determine whether Preferred was permitted by the PSA to reduce the Quarterly Quantities.

The Court must consider whether the contract term "Plant" is ambiguous. "A contract is not rendered ambiguous simply because the parties do not agree upon its proper construction."[90] "Rather, an ambiguity exists '[w]hen the provisions in controversy are fairly susceptible of different interpretations or different meanings.'"[91] Where a contract is ambiguous, the Court will consider extrinsic evidence in order to ascertain the parties' intentions.[92]

Section 2.1(a) of the PSA defines "Plant" as CRS' "plant located in New

[90] *GMC Capital Invs., LLC v. Athenian Venture Partners I, L.P.*, 36 A.3d 776, 780 (Del. 2012) (citing *Eagle Indus., Inc. v. DeVilbliss Health Care, Inc.*, 702 A.2d 1228, 1232 (Del. 1997)).
[91] *Id.*
[92] *See id.* (explaining the Court's course of action when it determines that a contract term is ambiguous).

Auburn, WI." This definition does not specifically differentiate between the dry and wet plants that exist on CRS' site. Therefore, the contract term "Plant" is ambiguous on its face.

The intent of the Plant Expansion provision can be reasonably interpreted to ensure CRS' capacity to provide the Q2 2015 volume of sand. Nevertheless, the Section 2.1(a) definition of "Plant" renders the term facially ambiguous. Extrinsic evidence is required to address the ambiguity. There is a genuine issue of material fact as to whether the April 1, 2015 completion date applies to both the dry and wet plants, or only to the dry plant. Consequently, there is a genuine issue of material fact as to whether the Quarterly Quantities were properly reduced because the "Plant" was not completed by April 1, 2015.

CONCLUSION

CRS Proppants LLC's Motion for Summary Judgment is **GRANTED IN PART** and **DENIED IN PART.** The Court finds: (1) Plaintiff is entitled to a Quarter 1 of 2015 payment in the amount of $379,846.25; (2) Section 9.3, the liquidated damages provision, is enforceable; (3) Defendant's performance is not excused by commercial impracticability or frustration of purpose; and (4) Section 2.1 is ambiguous, demonstrating genuine issues of material fact. Count IV – attorneys' fees – will be addressed at a later date in these proceedings.

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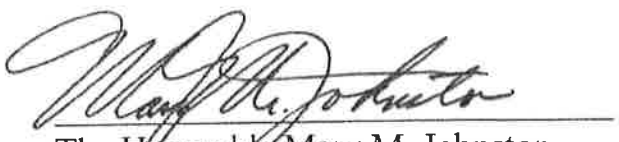
IT IS SO ORDERED.



The Honorable Mary M. Johnston