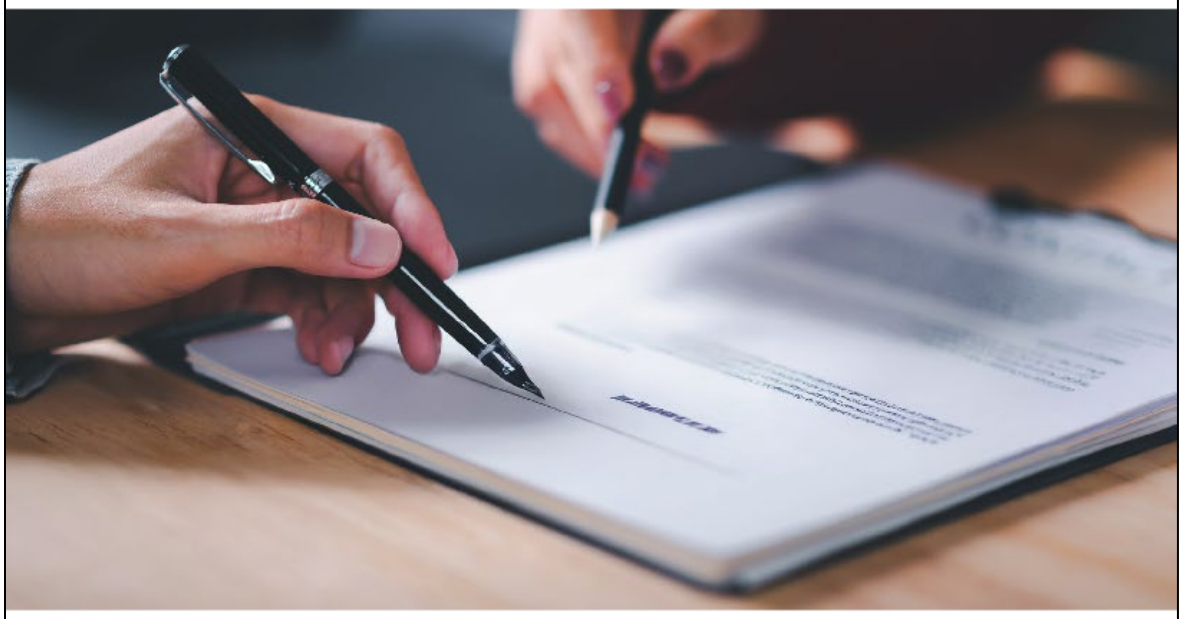
Contract Law: Application and Logic



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Professor of Law
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Contract Law: Application and Logic

First Edition (2026)

by Val Ricks

Professor of Law

South Texas College of Law Houston

Contract Law: Application and Logic

First Edition

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About the Author

Val Ricks has taught Contracts since 1996. His scholarship on contract law appears in the Georgetown LJ, Indiana LJ, BYU LR, George Mason LR, Baylor LR, Florida St U LR, Texas A&M LR, U. Kan. LR, American U. LR, and South Texas LR. He claims the original discovery that Isaac Kirksey actually made a bargain with Antillico. Professor Ricks also teaches, and writes about, business associations and other intersections of law and business. Before teaching, he clerked for Judge Charles Wiggins of the 9th Circuit U.S. Court of Appeals and practiced transactional and appellate law in Salt Lake City. Professor Ricks received a B.A. summa cum laude in Philosophy and a J.D. summa cum laude, both from BYU. He and his bride are the parents of seven beautiful children.

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VR, 2026

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Preface: Why This Casebook?

This casebook is different from other Contracts casebooks in important ways. Decades ago, I tried an experiment: teach the doctrines of contract law in the order they developed. The doctrines of contract law came to exist slowly between the 1500s and the late 1900s. What I discovered is that my students and I understood the doctrines better this way. Contract law has been famously derided for lacking coherence, but the doctrines themselves are logically put together to enforce and regulate exchanges involving promises. Studying the doctrines in the order they developed shows this better than any other method I know.

Second, the materials in this book focus not just on the doctrines of contract law but also on the transactions that are governed by the common law of contract. While you learn the doctrines, you will also learn the structures that certain transactions take: real property sales, leases, employment, contracts for services, loans, guarantees, settlement agreements, and (to some extent) sales of goods and licenses (thought time is limited for these last two). Among these transactional structures, you will see various contractual devices, including demand provisions, satisfaction clauses, cancellation clauses, earnest money, subject-to-financing clauses, options, non-competes, prenuptial agreements, bidding, continuing guarantees, lease renewals, negotiations and letters of intent signed during negotiations, insurance policy claims notices, arbitration clauses, assignment of debts, and mortgage assumptions. These and many others found in the book are common agreements and devices that all lawyers understand, and the materials were designed to teach you the ins and outs of these—while you learn the doctrines of contract law. The doctrines themselves influence how these types of agreements are formalized and how these devices are used.

Third, the book is repetitive. The doctrines—especially the difficult ones—are often

(i) introduced in part before they are taught in full, often in a prior case;

(ii) covered formally in a chapter, where they appear in the table of contents; and

(iii) reiterated in later cases.

Returning to them several times should help you both understand the doctrines (in context of the fact patterns in which they arise and are applied) and integrate them together. Understanding the transactions requires understanding the doctrine, and vice versa. Immersion in both the doctrines and in the transactions themselves allows this more practical understanding.

My hope is that students who see these and similar transactions soon after the class—in the summer after they take Contracts, for example—will say to themselves, yes, I have seen that before and can figure this out. Odds are that the transactions you see will be like one we have studied. If you see this, and find the casebook useful in handling it, I'd love to hear about it!

Best regards,

VR

Introduction

A. The Law's Logic

"A contract is a promise or set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty." *Restatement (Second) of Contracts* § 1 (Am. Law Inst. 1981). Contract law is the set of rules dictating when the law confers such remedy or recognition.

Contract law's logic is determined in part by its history, specifically, the order in which its doctrines were adopted. Aside from recognizing promises (including all various ways of committing) as promises, the next rule was consideration. The law's logic hangs on promise and consideration. In fact, in the late 1500s, Thomas Egerton, Queen Elizabeth's Solicitor General, argued that contract law had just three issues: "In every action on the case [upon an assumpsit], there are three things considerable: consideration, promise and breach of promise." *Golding's Case* (1586), 2 Leon. 72, 74 ER 367. All the later rules developed on the assumption that these three things were already in place.

Though the world has changed a great deal since 1539, when the consideration doctrine was invented, and since the reign of Elizabeth I in which the doctrine was settled largely into its present form, the problems that contract law must solve have not changed enough to prompt a wholesale change in contract law's structure. In part, this is because the rules are formed by the needs of litigation, and litigation in the Anglo-American system retains basically the same structure it had in the 1500s: a plaintiff complains, a defendant answers, the facts are discovered, and a trial occurs to resolve factual disputes so that a judge can apply the law.

In this structure, the plaintiff makes a case for a binding promise and remedy, the defendant responds with proposed defenses, a trial occurs if necessary, and then the judge imposes a remedy or not—that is what the law is established to do. (Of course, almost all cases settle or go to private arbitration, but the law strongly influences settlement value and is applied by arbitrators much as it would be in court.) The rules of contract law are designed for this litigation process, and you will understand them much better if you learn them that way.

If you poke about in the literature, you will find moralists, Kantians, law and economics scholars, and others who try to rationalize contract law in other ways. These theories can be helpful in understanding various doctrines and can influence how they are applied. But the doctrines of contract law at the nut and bolt level only hang together logically as a practical method of resolving disputes about promise enforcement.

B. Sources of Contract Law

Before the American Revolution, the American states were British colonies. English law, including English contract law, applied in each of the thirteen colonies. The Revolutionary War freed the colonies from the British crown, but each of the new states continued to apply primarily English contract law. The federal government came into existence in the 1780s as a government of limited powers. Various attempts have since been made to promulgate a federal contract law, but none have as yet succeeded.

That means that states control contract law. Contract law is fashioned by state courts and state legislatures. The English law of contracts was created one case at a time in England's courts, and our states have generally carried on that tradition. Court-created law is usually called "common law" because English medieval royal courts supposedly adopted as law the common customs of the people, and also because that law applied nationally. The name stuck several hundred years ago. Now, our court-made law is called "common law" even if it is contrary to the customs of the people and applies only in a single jurisdiction within the United States. State legislatures also get in the act by passing statutes that codify or change the common law. Law promulgated by legislatures is called "statutory" law as opposed to "common law." Most of the law we study will be common or statutory law, adopted or promulgated by state courts or state legislatures. In fact, most of it is common law. Here and there a statute or regulation will intrude.

In the last hundred years, two groups of lawyers have somewhat successfully influenced the process of contract law making in America. The first is the Uniform Law Commission (ULC, formerly known as the National Conference of Commissioners on Uniform State Laws (NCCUSL)). The Conference includes 50 state-appointed commissioners who draft and recommend legislation to state legislatures. Please look over ULC's website at http://www.uniformlaws.org/.

The second group is the American Law Institute (ALI). The ALI is an organization of lawyers, judges, and legal academics dedicated to clarifying, simplifying, and reforming law. Please look at the ALI website also, at http://www.ali.org/. (The "About ALI" link is especially helpful.) The ALI's primary vehicle for accomplishing its mission is to "restate" the common law; that is, to boil down all the common law from court opinions into black letter rules that lawyers can better understand. The first Restatement of Contracts was published in 1932. The Restatement (Second) of Contracts was published in 1981. Sometimes the ALI merely restates the common law. The first Restatement of Contracts tried to do that. But often the ALI "restates"(?) as law what isn't yet law, in the hope that courts will adopt the ALI position. The Restatement (Second) (affectionately referred to as "R2K") proposed more of this reforming than did the first Restatement. But courts have drawn (and will draw) on the wisdom of both documents. The Restatement and Restatement (Second) are not law but only commentary, unless something in them has been adopted by courts. The common law comes from decided cases, as it always has.

Between 1940 and 1952, ULC (then NCCUSL) and the ALI teamed up to draft the Uniform Commercial Code (UCC), which they then proposed to state legislatures. This statute has been wildly successful: eventually all fifty state legislatures passed it, with only some local variation (though Louisiana did not pass Article 2). The result is that for certain kinds of commercial transactions, the law of all fifty states is uniform. The UCC governs such things as sales of goods (Article 2), negotiable instruments (Article 3), and secured transactions (Article 9). Excerpts from the UCC are included in your statutory supplement, if one is assigned. You may study Articles 2, 3, 4, and 9 in later courses.

The rest of contract law is unspoken. It exists in the practices, morals, prejudices, theories, and goals of the lawyers, judges, litigants, and facts involved in its making and application. In this course you will study not only the rules themselves, which make up the body of contract law proper, but also the culture in which contract law exists, is applied, and is a part.

C. How this Book Is Organized

To understand the materials that follow, you must first know something about the history of American contract law. Our law of contracts includes (1) several hundred rules, formulated in both case law and statutes (we will study roughly 500 in this book, depending on what one counts as a rule); (2) the application of those rules in many thousands of cases (of course we won't read all of them, just those in the Table of Contents); and (3) a good deal of theory and culture.

The rules, applications, theory, and culture of contract law have developed over almost five centuries. Some of the authorities we study will be reports of cases from the 1500s—these are the authorities that created the rules, and they still give the best descriptions of those rules and the reasons the rules exist. Most of our common law of contract is traceable to one of two sources: (1) English common law developed from the practices of the English royal courts between 1500 and 1800, and (2) the combination of Roman law and Aristotelian personality theory worked out by sixteenth century scholars in Spain and later adopted as an overarching legal theory by European scholars in the 1600s and 1700s. These two sets of authority were then combined in the 1800s as judges in the new American republic gathered what they thought was the best in legal wisdom from around the world.

You must read carefully what is here. Most of it is case law. You will be unable to understand the materials adequately unless you ask and answer questions of the material. For instance, for both cases and statutes you will have to ask such questions as "What is the issue here?" "What rule is the court following?" "Which facts determine the result under this rule?" "How can I change the facts so that the rule does not (or does) apply?" These kinds of questions will guide your learning so that the knowledge you take from the materials will be useful to you on the class exam, on the bar exam, and in practice.

Questions are set forth below many items in the reading, also. These are questions your professor will probably expect you to be able to answer; they are the kinds of questions that a lawyer should be able to answer from the materials. Near the beginning of the semester, some of you may need help answering some of them. As the semester progresses, however, you should become able to answer these questions from the materials yourself. If you cannot, you have missed something and you should study harder (or smarter?) for the next assignment so that you can.

The organization of the casebook reflects the way that contract law developed. Studying chronological development helps you make sense of contract law and see how litigations' needs drive the development of doctrine. But the law of contract formation breaks down into different but easy (though slightly false) categories around which you can begin to build an outline of the law. (These categories did not develop chronologically, so your outline of the law *should not* follow the Table of Contents exactly.) First, three

different theories of liability exist: I. Consensual Contract (often called simply “Contract”), II. Promissory Estoppel, and III. Unjust Enrichment. You should begin your outline of the course as soon as possible and include these three categories.

Second, might include in your outline two main categories under Consensual Contract: Elements and Defenses. A consensual contract has at least five elements, all of which are necessary for a binding contract. Four of these regularly appear in lists in judicial opinions. For example: “The fundamentals of a legal contract are *competent parties, legal subject-matter, valuable consideration, and mutual assent*. There can be no contract if any of these elements [is] lacking.” *Virginian Export Coal Co. v. Rowland Land Co.*, 131 S.E. 253, 262 (W.Va. 1926) (italics added). To these four, add *definiteness* (or *specificity*), a topic we will study near the middle of the semester. You also need to fit defenses in your outline. Sometimes things happen to unwind contract formation even when the elements of a contract exist, and rules that capture these facts are called defenses to formation. We will talk more about outlining in Chapter 2.

D. How to Study or, at Least, How Your Casebook Author Thinks You Will Study

Law, as hinted above, is a method of solving problems even more than it is a body of knowledge. The method requires the lawyer to know quite a lot of things, but more importantly, most importantly, the method requires the lawyer to do certain things with that knowledge. What you are trying to learn to do is resolve the legal issues presented by a fact pattern, a case you have never seen before. Stated in another way, you are trying to apply legal rules you have learned to fact patterns you have never seen.

In order to do this, you will first have to learn the words of the law, including how the law has been applied in the past. Law is words, for the most part. The cases you study are law, the statutes are law, the constitution is law, all are words. Lawyers use the words to resolve new problems as they arise. Contract law has been developing for a long time, and new problems do not arise often, but they will often be new to you, to opposing counsel, and to the judge.

Because law is words, you will have to learn many. Successful law students become expert at identifying the words that solve issues: the legally operative language in the cases and statutes. Each case and statute was written to solve a problem, and learning the rule from the case and the statute requires that you learn that legally operative language and how it solves the problem in the fact pattern.

Because, in the common law system, cases are law, one of the first skills you must learn is how to glean law from judicial opinions. To help you learn how to do this, we ask you to brief cases. Your brief should have the following entries:

(1) facts (we only need the relevant facts, though which are relevant is very difficult to tell at this stage of your education, so perhaps you should just include all of them (hint: some of them (probably the most important) are in the analysis later in the opinion)),
(2) procedure (the current status of the lawsuit that is on appeal, including where the case is in the process of preparation for trial or trial or after trial, and what the relationship is between the trial court and the court that wrote the opinion),

(3) issues (the legal issues addressed by the court),
(4) holdings (the legal rules employed by the court to resolve the issues),
(5) analysis and rulings (how the legal rules are applied to the facts or how the facts and policy are used by the court to determine whether a rule applies or how it applies).

Your professor might ask about any of these. As you write your brief, it will help you to write down as you go where you found these things. Your professor may ask that, too. The paragraphs in the cases are numbered so that you can easily write down your sources.

After the cases, you will find questions, notes with questions, and hypotheticals with questions. You should prepare to answer each question in class. If a sentence has a question mark after it, your professor might ask you the answer in class.

We will learn so many rules in class. How will you keep them all straight and learn to use them effectively and efficiently? We will talk about this in class in a couple of days, and there will be reading about it in Chapter 2. Basically, you will make an outline. This is an organized statement of all the rules you need to know to prepare for the exam. It might helpfully include analyses of fact patterns that help you understand how the rules apply. It might also include brief policy notes.

For the exam, you will have to have the rules memorized (the bar exam is closed book, too). So, the outline should write the rules in a form that is (i) workable, meaning that it (a) contains the words that do the legal work and (b) sets those words out in memorizable form (lists are *very* helpful), (ii) organized into the law's categories, so that you can see how the law regulates promising activity and so that you can practice applying the rules.

Making your outline is how you first prep for the exam. After you have made it, studying from it and practicing applying the rules in it is how you next prep for the exam. You should probably begin outlining no later than the first couple of weeks of class. This is why we will talk more about this when we reach Chapter 2.

Ready, set, go!

Chapter 1. Consideration: Contract & Bargain

Learning law is like learning a language. Here is some vocabulary.

Contract: "A contract is a promise or set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty." R2K § 1.

Promise: (a) A manifestation of intent to commit to a future act or refrain from some future act (b) made so as to justify the promisee's reasonable belief that a commitment has been made.

Promisor: The person who makes the promise we are talking about. Usually, this is the defendant. Contract is constructed around determining whether the defendant's (the breaching party's) promise is enforceable, so usually *promisor* is a reference to the defendant.

Promisee: The person to whom the promise is made. Usually, this is the plaintiff, but it need not be.

These are law words, though two of them also have non-law uses. Lawyers deal in words, so expect your general vocabulary to expand. A dictionary will help, both an English dictionary and a law dictionary (and sometimes you may get to translate Latin or French!).

A. The General Test

An opinion of the court is itself law. That's how the common law works. If the case is not published, the opinion is law only between the parties. If the case is published, then, generally speaking, it is law for the court in all of its cases.

But the opinion has many parts, and they are not all equal with regard to the law that the opinion follows or creates. For instance, the opinion has facts, procedure, rule statements (one or some of which might be law the court follows), application of the rule/s to the facts of the case, policy, or other jurisprudential arguments. Lawyers know how to read a case and then report the law the case stands for; often, the lawyer will say it in a single rule statement (e.g., "*Vian v. Carey* followed the rule that . . . ."). This rule statement is often called the "holding" or the "law established by the case." Courts usually help lawyers and the parties know what the court thinks is law by including a rule statement or statements that the court then applies to reach a result. But courts do not always do this, and sometimes the lawyer must formulate the rule statement.

Can you pick out the rule statement from this case? If you are called on in class to recite the case, your professor will always (or nearly always) ask you for the holding, meaning the rule the court relied on or established to reach the result. The professor may also ask why you think the statement you give me is the holding. Learning to read legal sources to find and articulate the rule is the first task of law students.

Joseph VIAN v. Mariah CAREY (1993)

Not Reported in F. Supp.

United States District Court, S.D. New York

No. 92 Civ. 0485 (MBM

OPINION AND ORDER

[¶1] Defendant Mariah Carey is a famous, successful and apparently wealthy entertainer. Plaintiff Joseph Vian was her stepfather before she achieved stardom, but at the start of this litigation was in the process of becoming divorced from defendant's mother. He claims defendant agreed orally that he would have a license to market singing dolls in her likeness, and sues for breach of that agreement. Defendant moves for summary judgment pursuant to Fed.R.Civ.P. 56, claiming that no contract existed and that the damages plaintiff seeks are not recoverable as a matter of law. For the reasons discussed below, defendant's motion is granted.

I.

[¶2] Plaintiff claims that he and Carey had an oral contract for him to receive a license to market "Mariah dolls." These dolls would be statuettes of the singer and would play her most popular songs. Plaintiff claims that the contract was in consideration of his financial and emotional support of defendant, including picking her up from late-night recording sessions, providing her with the use of a car, paying for dental care, allowing her to use his boat for business meetings and rehearsals, and giving her various items, including unused wedding gifts from his marriage to her mother, to help furnish her apartment. (Complaint ¶ 6)

[¶3] The alleged basis of the oral contract is that on at least three occasions, twice in the family car and once on Vian's boat, Vian told Carey "Don't forget the Mariah dolls," and "I get the Mariah dolls." (Liebman Aff. Exhs 2, 4, 5, 6.) According to Vian, on one occasion Carey responded "okay" and on other occasions she merely smiled and nodded. (*Id*.) Although Carey admits Vian mentioned the dolls two or three times, she testified that she thought it was a joke. (Carey Depo., Liebman Aff. Exh. 7.) For 30 years plaintiff has been in the business of designing, producing, and marketing gift and novelty items. (Pre-Trial Order at 3.)

II.

[¶4] Summary judgment will be granted if "there is no genuine issue as to any material fact and the moving party is entitled to judgment as a matter of law." *Anderson v. Liberty Lobby, Inc*. 477 U.S. 242, 250 (1986). "Summary judgment is properly regarded not as a disfavored procedural shortcut, but rather as an integral part of the Federal Rules as a whole, which are designed to 'secure the just, speedy and inexpensive determination of every action.'" *Celotex Corp. v. Catrett*, 477 U.S. 317, 327 (1986) (quoting Fed.R.Civ.P. 1).

[¶5] In determining whether there is a genuine issue of material fact, a court must resolve all ambiguities, and draw all inferences, against the moving party. *See United States v. Diebold, Inc*., 369 U.S. 654, 655 (1962) (per curiam). * * * *

[¶6] [Here], the necessary consideration for the contract is wholly lacking. Consideration is a bargained for exchange. "In other words, the promise and the consideration must purport to be motive each for the other, in whole or at least in part; it is not enough that the promise induces the detriment or that the detriment induces the promise if the other half is wanting." *Banque Arabe et Internationale D'Investissement v. Bulk Oil (USA), Inc*., 726 F. Supp. 1411, 1419 (S.D.N.Y. 1989) (citations omitted) (emphasis in original). Plaintiff admits that he did not express to defendant that his help to her was a quid pro quo for a license. (Liebman Aff. Exhs 13 & 14.) Plaintiff specifically acknowledged that the household gifts and permission to use the car plaintiff purchased for defendant's mother were bestowed out of affection, not in consideration for a vague share in defendant's financial success or a more specific license for "Mariah dolls." (Liebman Aff. Exhs 16 & 20.) Nor did plaintiff ever tell defendant that her use of the boat was in consideration for a contract. (Liebman Aff. Exh. 22.) As to the dental care, plaintiff does not claim that he told defendant he expected anything in return for the money he gave her through her mother to go to a dentist. (Liebman Aff. Exh. 24.) Plaintiff further concedes that defendant may have repaid her mother. (Liebman Aff. Exh. 23.) Particularly when plaintiff was acting in a quasi-parental relationship to defendant, it is impossible to interpret plaintiff's gifts and acts as consideration for a contract.

[¶7] In sum, plaintiff has not raised a triable issue of fact as to the existence of a contract. * * * * [Among other objections,] consideration is lacking * * * *

[¶8] [D]efendant's motion for summary judgment is granted.

SO ORDERED.

Questions:

1. Is there consideration for Carey's promise?

2. What is the rule of law the court followed or relied on? Please write it out or mark it clearly in your book. You will find as you work with legal rule statements that they seldom contain a single legal standard; most contain several. These can helpfully be made into a list of elements or factors that must be analyzed separately.

3. Legal analysis primarily consists of showing how the facts prove or disprove each element or factor of a legal rule. (It also includes policy or jurisprudential argument in support.)

4. How many elements or factors are in the consideration test? What are they? We will talk about this at length in class.

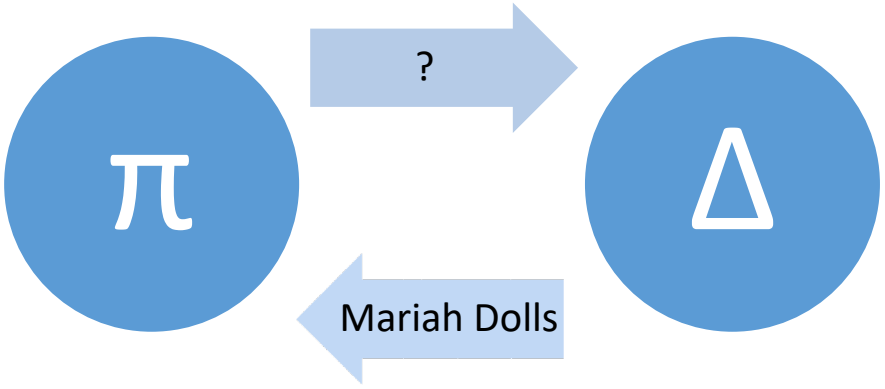
5. One of the most confusing parts of the Vian v. Carey opinion is the phrase "purport to be motive." The case does not explain this phrase, though it does analyze it. When we talk about motive in non-law settings, we are often talking about the desires and hopes of a person. It would be nice or horrible if the law could look into the hearts of humans and see what actually motivates them, but the law cannot do this. What counts as evidence of Vian's motive? Carey's motive? The R2K contains some helpful language on the relationship between motives (what is sought) and evidence: "[T]he law is concerned with the external

manifestation rather than the undisclosed mental state . . . .” R2K § 71 cmt. b. Is Vian consistent with this standard?

6. Did the court discuss why it requires a consideration—the policies underlying the consideration requirement?

7. The first common law decision adopting something like a consideration doctrine happened in 1539.* Does the court note that the consideration requirement was then 454 years old, and that times have changed?

8. Do you think this court reached the wrong result? Vian v. Carey is a very typical example of a modern consideration decision. In another part of the decision, the court held that Carey also failed to assent and that the contract as described here did not have the required definiteness.



Ways to write the rule: Because the consideration doctrine is so old and each state, the federal government, and the United Kingdom are all different jurisdictions, each of which writes contract law, several ways to write the consideration rule exist.

Here is a very traditional way to write the rule: “Consideration is a present exchange bargained for in return for a promise. It consists of either a benefit to the promisor or a detriment to the promisee. The detriment must induce the making of the promise, and the promise must induce the incurring of the detriment.” *Plains Builders, Inc. v. Steel Source, Inc.* 408 S.W.3d 596, 602 (Tex. App.—Amarillo 2013). This method is somewhat incomplete because a promise of a detriment to the promisee is another acceptable form.

The R2K also writes an acceptable form for the rule: “(1) To constitute consideration, a performance or a return promise must be bargained for. (2) A performance or return promise is bargained for if it is sought by

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* *Marler v. Wilmer* (King’s Bench 1539). See David J. Ibbetson, Assumpsit and Debt in the Early Sixteenth Century: The Origins of the Indebitatus Count, 1982 CAMBRIDGE L.J. 142.

the promisor in exchange for his promise and is given by the promisee in exchange for that promise." R2k § 71(1)–(2). The R2K version also leaves out parts of the rule, namely the "purport" part.

You were introduced to the rule to you using *Vian* because the case captures the most important parts of the rule to learn from, but you could use *Vian* or *Plains Builders* or § 71. They are more or less all used the same way in court.

1. Note: What Policy Supports Consideration Doctrine?

Why do we have this rule focused on exchange? The theory is ancient and predates the consideration doctrine. Here are some possibilities we will discuss in class:

a. Christopher St. German, writing in 1531 in *Doctor and Student*, said,

> [A] nude contract is where a man [promises] his goods or lands without any recompense appointed for it. As, if I say to another, "I sell thee all my land (or all my goods)," and nothing is assigned that the other shall give or pay for it, that is a nude contract, and (as I take it) it is void in the law . . . . And a nude or a naked promise is where a man promiseth another to give him certain money such a day or to build him a house or to do him such certain service and nothing is assigned for the money, for the building, or for the service. These be called naked promises because there is nothing assigned why they should be made. And I think no action lies in those cases, though they be not performed.

You get some extra fact patterns out of this passage. What does St. German mean when he says "there is nothing assigned why they should be made"? Why would that stop a court from enforcing them?

What St. German said still resonates. US federal district court judge Philip Simon opined, "There is no socially useful reason for a legal system to enforce agreements that are not supported by consideration." *Yessenow v. Hudson, Opinion and Order*, 2012 WL 2990643 *10 (N.D. Ind., July 18, 2012). Of course, if Judge Simon is correct, we should think about what socially useful reasons exists to enforce promises supported by consideration.

b. In *Sharington v. Strotton*, (Queen's Bench 1565), Plowden 301, 75 ER 454, two famous lawyers, Fletewood and Wray, argued there was no consideration. Their argument helpfully suggests some other ways to describe the consideration doctrine, so note how they say it:

> [N]othing new is here done on one side or the other, as is requisite in contracts and also in a covenant upon consideration. For instance, if I sell my horse to someone for money, or for some other recompense, here is a thing given on both sides (namely, one gives the horse and the other the money or other recompense), and therefore it is a good contract. Likewise in the case of the covenant upon consideration: for instance, if I covenant with you that if you marry my daughter you will have my land, . . . here is an act on each side (namely, you shall marry my daughter, and in return for that I grant you the use). Thus there is an act done and a fresh cause arising from each side. . . . The common law . . . requires

> a new cause, whereof the country may have intelligence or knowledge for trial if need be; and thus it is necessary for the public good . . . .

The last sentence is the policy rationale, but the words are tricky. Who is "the country" that needs intelligence or knowledge for trial?

To understand "the country" fully, you need to know how lawsuits worked in England. Mostly, they happened at Westminster Hall,[*] a big building built originally in 1097 but changed much in the millennium since. The Magna Carta supposedly required that English judges sit continuously at Westminster, so that's where they were. In the English legal system of the 1500s, the Chancery sat on the right side of the end of the Hall. Plaintiffs lawyers first went to the Chancery to buy a writ, a form they could fill in that allowed them to sue. Then the plaintiff's lawyer would walk across the Hall to one of the courts. The Queen's Bench sat on the left side of the end of the Hall. Lawyers would wait in line to plead their writ in Latin, filling in the blanks in the form as they spoke. The court would at some later time summon the defendant, who would enter a plea (which we would now call an answer). If the defendant disputed the facts of certain writs, then the courts sent the case to "the country," basically back out to the county where the facts happened, for trial by jury. So, "the country" meant the jury. Why would a jury more likely know of or understand a "fresh cause arising from each side" than a naked promise? Do you suppose the public good is the jury's knowledge or the good of encouraging exchanges or something else?

Fletewood and Wray's rationale for consideration is still with us. In 1941, Lon Fuller in *Consideration and Form*, 41 Columb. L. Rev. 799, 799 (1941), cited the discussion in the first footnote.

c. In *Sharington*, the lawyer on the other side, Plowden, wrote this:

> [T]he law of the land has two ways of making contracts or agreements for land or chattels. One is by words, which is the lower, and the other is by [sealed] writing, which is the higher. And because words are often spoken or uttered by a man without great advisement or deliberation, the law has provided that a contract by words shall not bind without consideration. Thus, if I promise to give you £20 to rebuild your hall, here you shall not have an action against me for the £20 ..., for it is a naked pact, *et nudo pacto non oritur actio*. And the reason is because the agreement is by words, which pass from men lightly. But where the agreement is made by deed [that is, by sealed writing,] there is more stay. .... [T]here is great thought and deliberation in the making of deeds [that is, sealed writings], and therefore we receive them as a final tie of the party and adjudge them to bind the party without thinking what cause or consideration there was for making it.

Fuller cited this passage, too. What is the policy argument for consideration here? If you are exchanging something, do you think about it more carefully than if you giving a gift? More carefully than when you are receiving a gift? Why do you suppose that is? If you had to seal a writing (meaning stamp your unique seal

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[*] Parliament has a helpful website: https://www.parliament.uk/about/living-heritage/building/palace/westminsterhall/.

on melted wax on a piece of paper), would you think about it carefully before you did it? Which act would cause you to deliberate more—exchange or seal?

St. German said the plaintiff needed to show a reason for a promise, and Plowden said the promise merely had to be made with deliberation. Which rationale trusts promisor's more? (Which question by a parent trusts a child more: (i) "Why did you do that?" ("What were you thinking?") or (ii) "Did you think about that carefully before you did it?")

2. A HISTORICAL NOTE

Because contract law is so old and developed so slowly, the law retains quite a few old terms. The most important bits of our contract law began to develop in the 16th century, so usage begins to be established then. When plaintiffs lawyers in 16th century England went to Westminster Hall to start a promise breach case, they had a choice of which writ to buy. They could buy a writ of *covenant*, a writ of *debt*, or a writ of *assumpsit*.

Covenant is an English translation of the Latin *conventiones*, which means literally agreements. If the plaintiff alleged a breached agreement (that included a promise), this writ was available. On a writ of covenant, the justices applied the following rules: (i) Trial of factual issues was by jury in the county where people would know something related to the transaction. The jury could be counted on to know the customs of the country. (ii) The plaintiff's case failed unless the promise or agreement was in a sealed writing. (Other courts might grant relief on an unwritten promise, but not the king's courts.) (iii) The jury would set damages for the breach. (iv) The justices would not order the defendant to perform the promise.

Debt was a property-related writ. The plaintiff got a writ of debt to sue for property owed. Various transactions would cause the defendant to be in debt, and these had to be alleged before the court in pleading. Most involved some sort of breach of promise: i.e., an informal sales contract in which the goods had been delivered, a loan, a service agreement already performed, a lease. But if these transactions involved breach of promise, why were they not cases of covenant? Because they also involved one other element: a *quid pro quo*, a "something for which" the defendant's promise was made, the plaintiff's action was appropriate. In the case of a loan, for example, the lender had already lent the money, and coupled with the agreement to pay, this *quid pro quo* justified the lender's suing for the property owed. The *quid pro quo* separated debt from covenant.

When a plaintiff alleged a debt, the justices applied the following rules: (i) The plaintiff could not proceed unless the amount of damages was certain. (ii) Trial of factual issues was by jury or by "wager of law," as the defendant may elect. A defendant waged his law by (a) swearing an oath that he was not indebted to the plaintiff and (b) producing eleven other "compurgators" or oath-helpers to swear that the defendant's oath was credible. If the defendant could swear and find eleven others to swear with him, he could go free and never pay. It was possible to lie one's way out of a debt, though in practice this probably did not happen often because fear of God and loss of reputation kept defendants from lying. The common law courts did not punish perjury until 1563. Naturally, plaintiffs would have preferred another method of recovery to debt had one been available.

You would think that, given the uncertainty of debt actions, potential plaintiffs would have been wise to put their transactions in writing and under seal. In fact, many transactions were put in writing and under seal. Cautious people even went one step further and, instead of having the person promising (the "promisor") merely promise something in the writing, they would have the promisor promise to pay a penalty if the promisor did not do the desired act. For instance, if the cautious plaintiff had sold the defendant a house for 40£, the cautious plaintiff would have the defendant promise to pay 80£ if the defendant had not paid 40£ by a certain date. The defendant's writing, called a "penal bond," was enforceable in a special debt action called *debt sur obligacion*. No wager of law was available in a case of *debt sur obligacion*, and the defendant had very few defenses. Factual issues went to the jury, but the bond itself set the damages.

For a long time, covenant and debt writs handled all the contract litigation, and as a consequence, contract law hardly developed. In covenant actions, the sealed document answered all the hard questions about whether a promise was made and made fairly, and the jury answered all the difficult questions about damages. In debt actions on a penal bond, the bond itself set both the obligation and the damages, and occasionally a jury was allowed to step in to grant a defense. In other debt actions, all factual disputes either went to the jury or disappeared when the defendant waged law. Judges took these easier, procedural routes to resolution rather than make rules for parties to follow. Nearly all questions were settled by the parties, the jury, or by wager of law. If a defendant waged law unfairly, God punished. Agreement, custom, and God were in the end arbiters of nearly all disputed cases. No one either asked or answered many of the questions we will ask for the rest of this semester.

This changed in the early 1500s, when the royal courts settled on another means for remedying a breached promise. The common law had long given a remedy for a trespass. You know what *trespass* means: it's when you walk on someone else's property against that person's express will. But *trespass* also means more generally to commit some other wrong against another personally (as in "For if ye forgive men their trespasses, your heavenly Father will also forgive you: But if ye forgive not men their trespasses, neither will your Father forgive your trespasses."—Matt. 6:14-15, KJV). The English lawyers came to think of a breach of promise as a trespass in the sense used in the KJV of Matthew. When plaintiffs alleged a trespass in the royal courts, a jury resolved the factual disputes and set the damages. The trespass action was very broad, and the royal courts purposefully allowed one strand of it, called trespass on the case, to expand to cover pleas warranting relief not covered by any other action. It is this strand of trespass on the case that came to cover breaches of promise.

This occurred in some cases by 1500. The resulting sub-category of trespass on the case was called "trespass on the case in assumpsit," or simply "assumpsit," which means in Latin literally "he has undertaken." The gist of the assumpsit action was that the defendant undertook to do something and had not done it, to the plaintiff's damage. The defendant could undertake a task by promising to do it. Thus, to promise a performance and then later not perform it warranted relief in assumpsit—that could be a trespass. By 1500, the king's courts had approved this kind of action in cases of breach by a building contractor, and other kinds of cases soon followed. Assumpsit cases involving breach of promise became commonplace by the late 1530s. Assumpsit proved a great boon to plaintiffs. In the assumpsit action, the defendant was not allowed to wage law, no sealed writing was required, oral promises were routinely actionable, and the jury set the damages according to the plaintiff's proof of injury. (Assumpsit grew to cover other actions as well, including many now called unjust enrichment.)

Soon after, the requirement of a consideration arose. At first, the problem was rather formal. Plaintiffs' lawyers wanted to make sure that the covenant and debt rules did not apply to their cases, because they

preferred the assumpsit rules. At the time, the writs were not supposed to overlap; plaintiffs were not supposed to be able to pick and choose. How were courts to tell whether the action arose in covenant, debt, or trespass when each of those involved an allegation that a promise had been breached? The assumpsit action could not rest on mere agreement, for then the action was based on a covenant and covenant rules should apply. Lawyers resolved this problem by omitting any reference to agreement in their pleadings in assumpsit. But this raised another difficulty. A bare promise did not overlap with any other action, but why should the court enforce a bare promise? The common law courts had for centuries been claiming that on a *nudum pactum* (a bare promise) no action would lie. To allege a wrong worth remedying, the plaintiff had to allege something besides the promise or undertaking that would make the promise worth enforcing. At first, plaintiffs alleged *quid pro quo* or *consideration* or just *for* (*pro*) or *causa* (cause), but eventually (in the 1550s and 60s), judges reasoned that *quid pro quo* should be off limits because that was the requirement for a valid debt action when no sealed writing existed. *For* (or *pro*) may not have been specific enough, and it was part of *quid pro quo*. Courts instead required that a consideration be alleged.

The word *consideration* initially meant something like “any good reason for an act that had legal consequences,” but that is not its meaning today. The word as used by the courts in breach of promise cases in assumpsit quickly developed the more specialized, complicated meaning explained by Fulbecke in 1602 (see problem 3 below) and *Vian v. Carey* in 1993. Today, still, a promise, to be enforceable, must be given for a consideration. The following statement is common: “Consideration is indeed a necessary element to the formation of a legal contract, and in general a contract that is unsupported by consideration is unenforceable.” *Regions Bank v. Bric Constr., LLC*, 380 S.W.3d 740, 761 (Tenn. App. 2011).

The word *assumpsit* is also still current usage. The common law writ system was abolished (mostly in the 1800s), but the word *assumpsit* still means a cause of action or suit for breach of promise or for unjust enrichment. *See, e.g.*, *Nevarez v. USAA Federal Savings Bank*, No. 08-19-00120-CV, 2021 WL 837624 at *4 (Tex. App.—El Paso Mar. 5, 2021) (“Money had and received is a category of general assumpsit.”).]

a. Example Cases: Testing the Bargain Principle

Now that you have a rule for consideration, you can practice applying it. *Everyone is bound by the law*, including the parties to disputes, the lawyers who argue for the parties, the judge who hears the legal arguments, the jury who decides factual issues, the intermediate court of appeals that decides whether everyone in the trial court (including the trial judge) followed the law, and the ultimate, higher court of appeals that has to decide if the intermediate court of appeals followed the law.

The result is that, when the law (its words and its meaning in application) is clear and you understand it, you should be able to apply it to fact patterns you have never seen before. In the following problems 1–7, apply the law you learned from *Vian v. Carey* to reach the result that the courts actually reached in the cases. There should be no need to look up any of the cases.

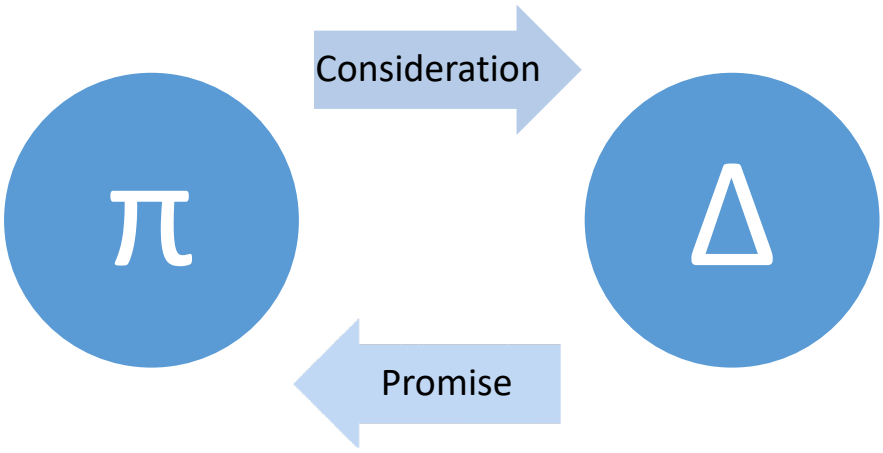
PROBLEM 1. *Mona v. Harry*: Harry and Mona, both widowed and elderly, met, dated, and married. One year later, Harry contracted Alzheimer’s disease. He steadily went downhill until he died eleven years later.

Mona cared for him during all his years of illness and gave him some financial assistance. Two years after he contracted the disease, Harry signed a promissory note in which he promised to pay Mona $2 million. Six months later, Harry was declared incompetent and Mona was appointed as his guardian. After Harry died, his children, who controlled his estate, refused to pay Mona the $2 million, so Mona sued Harry's estate. When the estate's lawyer deposed Mona, he asked her why Harry gave her the note. Mona replied, "I was his wife. He wanted to take care of me." When asked whether she took care of Harry because of the note, Mona said, "No. I gave him my life, my love, my devotion, taking care of him because I loved him and he loved me." Is there any consideration for Harry's promise? *See Wagner v. Golden*, 1993 WL 350027 (Ct. App. Ohio 1993). Please formulate your answer in the language of the rule from *Vian*.

PROBLEM 2. *Leah v. Samuel*: Leah, the plaintiff, alleged that Samuel, a married man, promised in writing to purchase an apartment for Leah, his female companion, in return for the "love and affection" that she provided him during the prior three years. Is there consideration for Samuel's promise? *See Rose v. Elias*, 576 N.Y.S.2d 257 (N.Y. Supr. App. 1991). Whether Samuel's promise formed a contract or not, why might the court have frowned on this agreement?

PROBLEM 3. *Hunt v. Bate I*: Employee was arrested and placed in debtor's prison (an institution we no longer have; it was replaced by the much more merciful bankruptcy proceeding). Under debtor's prison rules, another person could take the debtor's place in the prison for a time, but if the person did, the person could only get out of the prison by paying the debt. Another person, let's call him Pledge, took Employee's place in the jail. Pledge said he did this so that Employer's work would not go undone. When Employer heard that Pledge had done this, Employer visited Pledge in the prison and promised to reimburse Pledge if Pledge had to pay Employee's debt in order to get out. Pledge later paid the debt and got out of jail and then sued Employer for reimbursement. Was there consideration for Employer's promise? The court in the case said that Employer "did never make request of the plaintiff for to do so much, but he [Pledge] did it of his own head." *Hunt v. Bate I*, Dyer 272a, 73 ER 605 (Common Pleas 1568).

William Fulbecke, in THE SECOND PART OF THE PARALLELE, OR CONFERENCE OF THE CIVILL LAW, THE CANON LAW, AND THE COMMON LAW OF THIS REALME OF ENGLAND 18b (Thomas Wight 1602), reported that "our Law requireth in all contractes a mutuall consideration, and one part of the contract challengeth and begetteth the other." His first illustration for this principle was *Hunt v. Bate I*.



PROBLEM 4. Abe v. Juanita: Abe is a police officer. Juanita owns a jewelry store in Abe's jurisdiction, where Abe patrols. Juanita's store was burglarized, and Juanita offered a $5,000 reward to anyone with information leading to the arrest and conviction of the burglars. Abe, while working part-time as a security guard at a nearby store, found evidence that led to the arrest and conviction of the burglars. Police officers are considered by law to be police officers, even when they are not actively on the clock. For example, Tex. Code of Crim. Proc. Art. 2A.051 says, "Each peace officer shall: (1) preserve the peace within the officer's jurisdiction using all lawful means; . . . (5) when authorized by law, arrest an offender . . . ." Can Abe claim Juanita's reward? The answer is "no." Can you formulate a legal reason for denying Abe's claim using the language of the consideration rule in *Vian*? Is there some other public policy that counsels against Abe's recovering the reward?

This last question, "Is there some other public policy . . . ," can overwhelm the analysis of consideration in fact patterns like this. In these cases, it is often not clear whether the court is ruling on the consideration question or the duty.

Here are a couple of other problems like *Abe v. Juanita* to try.

PROBLEM 5. Hildegard v. Grace, Executor for Michael. Michael married Hildegard when he was old and wealthy. They signed a pre-nuptial agreement the day before the wedding that preserved each of their separate property as their own. Beginning three years later, Michael began to have heart problems. Over the next four years, he was admitted to the hospital three times. He became frightened and worried that he would be incapacitated and institutionalized. He told Hildegard (orally) that he intended to leave to her a list of nine items, including a life estate for the use of a condo in Hawaii, a 25% stake in a company he founded, and the cost of educating Hildegard's daughter from another marriage. The last time Michael was hospitalized, said Hildegard, he and she agreed that he would leave to her this list of nine items in exchange for Hildegard's promise to care for Michael in his own home for the duration of his illness. She performed

her promise until Michael died a few months later. Michael did not perform his promise, however. Hildegard sued Michael's estate for breach.

You have to learn a bit of estate law, here. Generally speaking, at death, a person's property becomes the property of their estate and their liabilities become the liabilities of their estate. If Michael was legally bound when he died to perform his promise, then his failure at death to leave the nine things to Hildegard was breach, and his estate would be liable. In response to Hildegard's suit, Michael's estate argued that Hildegard's care for Michael in his home was not given in exchange for the promise. If Hildegard did not care for Michael in exchange for Michael's promise, why did she care for Michael? *See Borelli v. Brusseau*, 16 Cal. Rptr. 2d 16 (Cal. App. 1993) (ruling for the estate). Judicial rulings on this specific fact pattern (and those very close to it involving married couples) vary from state to state, meaning that some courts in some states would have ruled for Hildegard.

For the record, courts are very hesitant to allow contract law to govern relationships between spouses in an intact marriage. Courts are not going to hear contract breach cases over promises involving intimacy, child-rearing, or housecleaning. If the parties are not married, however, they have more freedom of contract. For an interesting summary of both marital limits on contract and contracts between non-married couples, see Albertina Antognini, *Nonmarital Contracts*, 73 Stanford L. Rev. 67 (2021).

PROBLEM 6. Duane II's rich uncle Duane I, for whom Duane II was named, promises him in private at a family dinner at which Duane II's parents are the only other guests, that if Duane II will refrain from recreational use of harder drugs—heroin, LSD, cocaine, methamphetamine—until the age of 21, Duane I will pay him $10,000. Enforceable?

Question: Suppose a debtor is sued by a lender for a debt due and the lender obtains a judgment against the debtor in court for 100% of the debt. But the debtor does not have the money to pay 100% of the debt. If the debtor and lender agree that the debtor will pay 80% of the debt in exchange for the lender's forgiving the whole debt, is there consideration for the lender's promise?

A similar question: Suppose a debtor owes money by contract to a lender but can't pay it. If the debtor and lender agree that the debtor will pay 80% of the debt in exchange for the lender's forgiving the whole debt, is there consideration for the lender's promise?

As noted earlier, in these types of cases, the public policy supporting the duty may be more important than the consideration rule. In this last case, oddly, the two policies sort of equal each other or cancel out: In favor of the duty is contract law, and in favor of the compromise is contract law. Which should win? There is controversy about this fact pattern that we will return to later.

*PROBLEM 7***.** Bill Simmons enjoyed fishing and lived on the Maryland shores of Chesapeake Bay. One spring morning while fishing the Bay on a planned trip with two fishing buddies, Bill caught a 2-foot-long rock fish. After picking up the fish in a net and dropping it in the boat, Bill noticed a tag attached to its tail. The tag said, "Congratulations! This fish is 'Diamond Jim III.' If you caught Jim on hook and line, you have won the Third Annual American Beer Fishing Derby. If you text this number (XXXXX) and appear at the American Brewery company offices with Diamond Jim to sign an affidavit that you caught Jim on Hook and

line, you will receive $25,000!" Bill had heard of this contest before and even knew the fish's name, but there are probably 2 million adult rock fish in the Bay during the spring. The chances of catching this fish are miniscule, and Bill fished because he loved fishing, not in an attempt to catch this fish. Was Bill induced by the contest's promise? What language in the *Vian v. Carey* rule answers this question?

In *De Cicco v. Schweizer*, 117 N.E. 807 (N.Y. 1917), Justice Cardozo addressed a similar fact pattern this way (probably, he says the same thing twice): "It is enough that the natural consequence of the [promisor's] promise was to induce [the promisee] to put the thought of . . . delay aside. . . . If the tendency of the promise is to induce them to persevere, reliance and detriment may be inferred from the mere fact of performance."

B. Consideration's Form

The *Plains Builders* formulation of the consideration rule reflects the earliest form. Courts have talked that way since the 1500s: "The consideration is the ground of every action on the case, and it ought to be either a charge to the plaintiff or a benefit to the defendant . . . ." *Stone v. Withepoole* (Queen's Bench 1588), 1 Leon. 113, 74 ER 106, Cro. Eliz. 126, 78 ER 383, Owen 94, 74 ER 924, Latch, 82 ER 254. Because the test was written either charge (detriment) to the plaintiff (promisee) *or* benefit to the defendant (promisor), quite a few cases address what counts as benefit or detriment. Analytically, detriment is easiest, so let's take that first.

1. Detriment

WEBBS CASE (1576)

4 Leonard 110, 74 ER 763

[In this case, the plaintiff alleged as follows: Cobham was indebted to John of Style and John of Style was indebted to the defendant. John of Style apparently did not have enough money to pay defendant because Cobham had not paid John of Style. So, defendant hired plaintiff to obtain from John of Style a power of attorney authorizing defendant to sue Cobham on John of Style's behalf, and in exchange for this, defendant promised plaintiff 10£. A power of attorney is a document in which one person, called a principal, appoints another to be her agent, usually for a certain purpose(s) named in the document. In this power of attorney, John of Style would have authorized defendant to sue Cobham. Plaintiff obtained the power of attorney from John of Style, but defendant refused to pay plaintiff the 10£, so plaintiff sued. The defendant objected that there was no consideration because the defendant obtained no benefit from the power of attorney. We don't know why defendant said this. Perhaps Cobham was broke. Anyway, here is what the court said:]

But the exception was not allowed of. For in this case not so much the profit which redounds to the defendant, as the labour of the plaintiff in procuring of the letter of attorney, is to be respected.

Questions:

1. Was there a detriment here?

2. Was there a "purported" bargain here?

3. Your casebook author thinks about this case every time he feels he has worked all day and done nothing worthwhile for his employer. We all have days like that. If the worker was doing what was asked of the worker, is there consideration for the employer's promise to pay wages for that day?

4. Christopher St. German write in *Doctor and Student* another passage about, essentially, detriment as consideration for a promise: "As, if a man say to another, 'Heal such a poor man of his disease', or 'Make such a highway, and I shall give thee thus much', and if he do it I think an action lieth at the common law." 91 Selden Soc. 230–31. In the first promise, to the doctor, does the promisor get the benefit? Does the promisee have a detriment? What about in the second? Is there a "purported" bargain in these two examples?

2. Benefit

GAME v. HARVIE (1605)

King's Bench

Yelverton 50, 80 ER 36

[Plaintiffs loaned defendant money, to be paid back on request. Defendant refused to pay when requested, so plaintiffs sued in assumpsit, winning a judgment. On appeal, defendant's lawyer (Yelverton) argued that there was no benefit to the promisor from the promise because the promisor had to have the money ready to give back at any time, it being due on request, and therefore the promisor could not use the money at all. All the judges on the King's Bench had the same reaction to this argument, but their language may seem obscure, and you will have to think about why they reacted this way:]

[W]hen the intent of the parties may stand with the law, it shall be expounded accordingly; ... and ... here ... (as Popham [J.] said) the promise is grounded upon an accommodation, viz. a loan, which implies an use of the [money] by the defendant. .... But if a man delivers to J.S. a bag sealed with money, and the defendant promises to redeliver it upon request, no *assumpsit* lies upon this; for the defendant has not any benefit by it, for the money being in a bag has only a charge imposed by the keeping, *vide* P. 44 Eliz. before, the case

of *Riches* [*v. Bridges*], which Yelverton cited to be reversed, and . . . the Court [the King's Bench] said it was erroneously reversed.

Questions:

1. As a young associate, your casebook author used to examine loan documents to determine their enforceability. Many loans he examined were based on demand notes, promissory notes that required the borrower to pay the money back whenever it was demanded by the creditor. "What a silly provision," he thought, "The borrower could have the money tied up in a building project and have no means to pay it back! If we took this demand provision literally, the borrower would be unable to use the money, and the loan would be of no use to her." That is exactly Yelverton's objection. What is Popham's response?

2. The defendant possessed the money. Where did the defendant get it? Even if there was not a bargained-for benefit here, was there a bargained-for detriment? Why do you suppose the court goes to such lengths to find a benefit when there is quite clearly a detriment to the promisee?

3. What does "intent of the parties may stand with the law" mean? Why would the court want to say that when ruling on these particular facts?

RICHES v. BRIDGES (1602)

Queen's Bench & Exchequer Chamber

[The plaintiff owed John of Style about 80 bushels of grain, to be delivered on a certain day. For some reason, the plaintiff wanted the defendant to deliver the grain. In court, the plaintiff alleged that, in consideration that the plaintiff would deliver the grain to the defendant before that day, the defendant promised to re-deliver it to John of Style on the day it was due. Plaintiff delivered the grain to defendant, but the defendant breached the promise to re-deliver the grain. Plaintiff sued defendant, winning a judgment. The defendant appealed, arguing that, because the defendant was to deliver the exact "same corn which he had received, he cannot have any use of it, nor any benefit by it."

Here is the report of the case from Croke (pronounced "Crook") (Cro. Eliz. 883, 78 ER 1108):]

But the whole Court [the Queen's Bench] held it to be a good consideration; for in regard he received it, and made such a promise, it shall be intended that he had some benefit thereby, viz. that he had the better credit to retain it in his hands; or otherwise he would not make such a promise: and if by any intendment it can be, the law will well intend it. Wherefore it was adjudged for the plaintiff.

Note, afterwards upon a writ of error in the Exchequer Chamber, it was reversed for this cause; for that there was not any sufficient consideration whereof the law takes any regard.

[The report from Yelverton (4 Yelv., 80 ER 4) is even odder:]

[From the Queen's Bench:] The very possession of the wheat might be a credit and good countenance to the defendant to be esteemed a rich farmer in the country, as in case of the delivery of the 1000*l*. in money to deliver again upon request; for by having so much money in his possession he may happen to be preferr'd in marriage. *Quaere*, for it seems a hard judgment; for the defendant has not any manner of profit to receive but only a bare possession. .... But [note], the judgment was reversed in the Exchequer, ... as Hitcham told Yelverton.

Questions:

1. The Queen's Bench found consideration in this case. Do we know for what reason the defendant made this promise? Why would the defendant make such a promise (you may speculate on this one; after all, the court seems to)?

2. What does "shall be intended" mean, do you suppose? How does a court "intend" something?

3. What happened to this case in the Exchequer Chamber, which was the court of appeals that in 1602 reviewed cases from the Queen's Bench?

4. There may not have been a benefit here, perhaps, but was there a detriment? Was the detriment bargained for?

5. Courts still make this sort of move, but it sort of bothers lawyers when courts start making things up. That is one reason that the R2K's consideration test does not talk in terms of benefit and detriment but rather "performance or return promise." Was defendant's promise given in exchange for a performance, at least purportedly?

PROBLEM 8. A tractor dealer sells a tractor to a farmer, meaning that the farmer takes immediate possession of the tractor and in return promises to pay for the tractor over the next five years. Is there consideration?

3. The Mutual Promise

The courts came around quickly to holding that a promise could be consideration for another promise. There were hints of this in the early 1560s. By 1589, the Queen's Bench could say in *Strangborough v. Warner*, "[A] promise against a promise will maintain an action [in assumpsit], as in consideration that you do [promise to] give me £10 on such a day, I promise to give you £10 the day after." 4 Leonard 3, 74 ER 686. How is that case different from the facts of *Game v. Harvie*?

The following case, *Nicholas*, includes some results that are no longer *entirely* good law. We will study later in the course how and when parts of *Nicholas* were overruled. But *Nicholas* played an important role in contract law's development. First, the case illustrates the mutual promise rule in action. Second, two aspects of the opinion have been rejected by courts at key moments in contract law's development. *Nicholas*'s supersession by the mailbox rule is when assent doctrines made their way into the law of contract. And *Nicholas*'s outright partial overruling was required by the doctrine of "constructive conditions." Only the mutual promise rule is left of *Nicholas* now, but that rule's operation is most striking in its original application.

NICHOLAS v. RAYNBRED (1615)

King's Bench and Exchequer Chamber

Jenk. 296, 145 ER 215, Hob. 88, 80 ER 238

[¶1] A sells a cow to B for 5l. and [promises] to deliver her to him at a certain day; at the same time B [promises] to A to pay him 5l. for the said cow, at the said day. A brings an assumpsit for the 5l. not paid, and does not [allege] delivery of the cow: [Now, here's the court's ruling:] it need not be [alleged]; but the writ [the complaint] ought to [allege] the mutual assumpsit; for they are reciprocal assumpsits: and such mutual assumpsits are a good consideration, and each of them has a remedy against the other; one for the cow, and other for the 5l.

[¶2] Judged in both courts [the King's Bench and the Exchequer].

[¶3] ... [B]ut such mutual assumpsits ought to be made at the same time; for they make the consideration, and the consideration and the promise always ought to be together: otherwise it is nudum pactum.

Questions:

1. This opinion always throws students, and not just because *assumpsit* has two meanings. This result is counter-intuitive. Does A have to deliver the cow before he sues for the money? The answer the court gives

to this question is “no,” but that seems strange. Answer this, though: What is consideration here: delivery of the cow or the promise to deliver the cow?

2. If A does not have to deliver the cow before suing B for the money, how will B get the cow?

3. Is there a bargain here?

4. Why must the promises be made at the same time, do you think? That rule is also no longer good law, but we will pinpoint later in the semester the exact date on which this rule was changed. The reason for the rule is still with us, though, but that reason is enforced through another rule, one we have already studied.

5. While the mutual promise form of consideration is now the most common kind, by far, the holding of this case that the plaintiff categorically need not perform before suing is no longer good law. It was modified in the early 1700s in a case we will read later. This part of *Nicholas* is important, though, because every student of contract law must understand that, in its simplest form, contract law is logically focused only on the enforcement of one promise, not the enforcement of an agreement.

PROBLEM 9. Harry promises to give $2,000,000 to Mona, and Mona promises to accept it. Is this consideration? In other words, is a promise to accept a gift consideration for a promise to give the gift?

The answer to Problem 9 is no. It may help you to know the additional rule of law, here stated somewhat roughly, that the thing promised as consideration must itself be adequate consideration if exchanged for the promise at the time the promise was made. *E.g.*, Restatement (Second) of Contracts § 75 (1981).

PROBLEM 10. Farmer promises to buy a tractor and seller promises to sell that tractor. Is there consideration here?

C. Special Consideration Problems

1. Detriment Without Exchange?

If the rule is phrased the *Stone v. Withepoole* way (“charge to the plaintiff or a benefit to the defendant”), then the court may forget that a plausible exchange is required. Did that happen here?

STORER'S CASE (1615)

Dyer 272a, 272b n.32, 73 ER 605, 607

In an action upon the case, on assumpsit against one Storer, an agreement was between A. and B. that A. should have a lease of B. with [various] covenants; at the day of sealing A. refused, on account of the insertion of a new covenant concerning repairs, whereupon [Storer], standing by, took upon himself, if A. would seal it, to make the repairs; and it was adjudged for the plaintiff a good consideration, although the sealing of the deed was of no consequence to [Storer].

Questions:

1. This is a very brief report, just one sentence long. I'm pretty sure that B is the plaintiff, but it could be A. What about the application of consideration doctrine would make A or B a proper plaintiff?

2. Can you be sure there was a bargain here? Did Storer's promise induce A to sign the lease? Did the prospect of A's signing the lease induce Storer to promise? Why would Storer care?

We will study non-bargained-for detriment cases later when we study promissory estoppel.

2. Benefit Without Exchange?

EDMONDS CASE (1587)

3 Leon. 164

In an action [in assumpsit] against Edmonds, the case was, that the defendant being [a minor], requested the plaintiff to be bounden for him to another [essentially guarantee a debt], for the payment of 30l., which he [Edmonds] was to borrow for his own use; to which the plaintiff agreed, and was bounden [as guarantor], [as requested]; afterwards, the plaintiff was sued for the said debt [of Edmonds], and paid it; and afterwards, when the defendant [Edmonds] came of full age the plaintiff put him in mind of the matter aforesaid, and prayed him that he might not be damnified so to pay 30l., it being the defendant's debt: whereupon the defendant promised to pay the debt again to the plaintiff; upon which promise, the action was brought. And it was holden by the Court, that although here was no present consideration upon which the assumpsit could arise; yet the Court was clear, that upon the whole matter the action did lie, and judgment was given for the plaintiff.

Questions:

1. Was there consideration for the second promise?

2. Do you think it was fair to hold Edmonds bound to pay his guarantor even without present consideration? Why?

This next case is an aside. It deals with a problem of capacity. Can a minor contract? Or, why did the infant in *Edmonds Case* need to promise again? *Ex Parte Odem* discusses the capacity of infants.

Ex parte: Iris ODEM

(Re: The CHILDREN'S HOSPITAL OF BIRMINGHAM v.

Vincent KELLEY and Iris Odem) (1988)

Supreme Court of Alabama

537 So.2d 919

[¶1] We granted this petition for writ of certiorari in order to review the limited issue of whether a minor who executes a contract for a "necessary" is obligated to comply with the express terms of the entire contract, including those provisions regarding attorney fees and waiver of personal exemptions.

[¶2] The facts of this case are set forth in the opinion by the Court of Civil Appeals, 537 So.2d 917, and we agree that medical services provided to an infant child of a minor are "necessaries" for which the minor parent may be obligated to pay, but we hold that the attorney fees for enforcing the contract are not "necessaries" for which the minor is legally obligated to pay.

[¶3] The general rule of law is that contracts of minors are voidable. That is, the contract may be avoided or ratified at the election of the minor. *Flexner v. Dickerson*, 72 Ala. 318 (1882). In the instant case, Iris Odem disaffirmed, or avoided, the contract she had executed with Children's Hospital. Consequently, Iris Odem's obligation to pay for necessaries, i.e., the medical services rendered to her infant son, is not the result of the express contract between the parties, but arises from a quasi-contractual relationship created by operation of law which enforces the implied contract to pay. 43 C.J.S. Infants § 180 (1978). Therefore, a minor is not liable on any portion of the contract, or for what was agreed to be paid, except that the minor is liable for the just value of the necessaries.

[¶4] In *Wiggins Estate Co. v. Jeffery*, 246 Ala. 183, 19 So.2d 769 (1944), this Court, with approval, quoted the following from 18 Am.St.Rep. p. 650 et seq.:

> "It is for the court to determine, as a matter of law, in the first place, whether the things supplied may fall within the general classes of necessaries, and if so, whether there is sufficient evidence to warrant the jury in finding that they are necessary. If either of these

> preliminary inquiries be decided in the negative, it is the duty of the court to nonsuit the plaintiff who seeks to recover from the [minor]. If they be decided in the affirmative, it is then for the jury to determine whether, under all the circumstances, the things furnished were actually necessary to the position and condition of the [minor], as well as their reasonable value, and whether the [minor] was already sufficiently supplied...."

Therefore, the class and character of articles that are necessaries are issues of law. *Wiggins Estate Co*., *supra*.

[¶5] Do the attorney fees in this case fall within the general classes of necessaries? Stated differently, are the attorney fees necessary to the position and condition of the minor?

[¶6] Under Alabama law, attorney fees are recoverable from an opposing party only when provided for by contract or by statute. * * * * Thus, any contractual provision regarding the recovery of attorney fees in this case is for the benefit of Children's Hospital, because the attorney fees would not otherwise be recoverable. Accordingly, attorney fees are not necessary to the position and condition of the minor and are not recoverable from Iris Odem.

> "It is the policy of the law to protect infants against their own mistakes or improvidence, and from designs of others, and to discourage adults from contracting with an infant." 43 C.J.S. Infants § 180 (1978).

Accordingly, when an infant executes a contract, the infant is liable only on his implied promise to pay for necessaries, and all other provisions of the contract are voidable at the election of the infant. Further, attorney fees are not necessaries, because they are not necessary for the position and condition of the infant. We reverse the judgment of the Court of Civil Appeals to the extent that it holds that Iris Odem is obligated under all of the terms of the contract, and we affirm that portion of the judgment that holds that she is obligated for the reasonable value of the medical services rendered to her infant son.

AFFIRMED IN PART; REVERSED IN PART; AND REMANDED.

TORBERT, C.J., and MADDOX, JONES, BEATTY, ADAMS, HOUSTON and STEAGALL, JJ., concur.

Questions:

1. Is a contract by a minor void?

2. Is medical care for a minor a necessary?

3. Are attorney's fees specified in the contract for medical care necessaries?

4. Are clothes necessaries?

5. Is an apartment a necessary?

6. Infancy and intoxication (the rule for which is described later) are actually as close as we will get to incapacity. Other than in these cases, you should presume capacity to contract. The age of majority for contract is 18 for most states. Every individual of the age of majority and over is presumed competent to contract unless they are proved incompetent in court. Business entities (corporations, limited liability companies, limited partnerships, etc.) in good standing with the state have capacity to contract. Also, please note: If a contract is voided for infancy, normally the infant or new adult must return the item purchased, if possible; exact rules for restitution of benefits received by infants under avoided contracts differ state to state.

Aside over—now we are going back to benefit without exchange cases, which are often called cases of "moral obligation."

The next source, from the U.S. Bankruptcy Code, addresses the status of promises to pay debts that have previously been discharged in bankruptcy.

PROBLEM 11. J.S. takes possession of a truck and promises in return to pay for it in installments. Then J.S. is laid off from work, abandons his $400,000 home (on which he owes $390,000), and drinks heavily. He fails to make his truck payments. He also does not pay his credit card bills. The bank takes the house back. The truck dealer takes the truck back, but J.S. owes more for the truck than the truck is worth. J.S.'s creditors, including the truck note claim holder, file suits against him. To escape liability to them, J.S. files for bankruptcy. Soon after J.S. files a bankruptcy case, the bankruptcy court grants him a discharge (http://cca.li/QL). This means that J.S. is no longer liable to pay for the truck or the credit cards. But, J.S. is plagued by guilt and wants to live an honorable life. He also wants to drive a truck again, and he hopes that paying off the truck debt, even though it is discharged, will influence someone to lend to him again. J.S. writes to the truck note claim holder and promises to pay the debt for the truck. Is this promise enforceable? See the following statute.

11 U.S.C. § 524. Effect of discharge

(a) A discharge in a case under this title—

> (1) voids any judgment at any time obtained, to the extent that such judgment is a determination of the personal liability of the debtor with respect to any debt discharged under section 727, 944, 1141, 1192, 1228, or 1328 of this title, whether or not discharge of such debt is waived;
>
> (2) operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover or offset any such debt as a personal liability of the debtor, whether or not discharge of such debt is waived . . . . * * * *

(c) An agreement between a holder of a claim and the debtor, the consideration for which, in whole or in part, is based on a debt that is dischargeable in a case under this title is enforceable only to any extent enforceable under applicable nonbankruptcy law, whether or not discharge of such debt is waived, only if—

(1) such agreement was made before the granting of the discharge under section 727, 1141, 1192, 1228, or 1328 of this title;

(2) the debtor received the disclosures described in subsection (k) at or before the time at which the debtor signed the agreement;

(3) such agreement has been filed with the court and, if applicable, accompanied by a declaration or an affidavit of the attorney that represented the debtor during the course of negotiating an agreement under this subsection, which states that—

(A) such agreement represents a fully informed and voluntary agreement by the debtor;

(B) such agreement does not impose an undue hardship on the debtor or a dependent of the debtor; and

(C) the attorney fully advised the debtor of the legal effect and consequences of—

(i) an agreement of the kind specified in this subsection; and

(ii) any default under such an agreement;

(4) the debtor has not rescinded such agreement at any time prior to discharge or within sixty days after such agreement is filed with the court, whichever occurs later, by giving notice of rescission to the holder of such claim;

(5) the provisions of subsection (d) of this section have been complied with; and

(6)

(A) in a case concerning an individual who was not represented by an attorney during the course of negotiating an agreement under this subsection, the court approves such agreement as—

(i) not imposing an undue hardship on the debtor or a dependent of the debtor; and

(ii) in the best interest of the debtor.

(B) Subparagraph (A) shall not apply to the extent that such debt is a consumer debt secured by real property.

(d) In a case concerning an individual, when the court has determined whether to grant or not to grant a discharge under section 727, 1141, 1192, 1228, or 1328 of this title, the court may hold a hearing at which

the debtor shall appear in person. At any such hearing, the court shall inform the debtor that a discharge has been granted or the reason why a discharge has not been granted. If a discharge has been granted and if the debtor desires to make an agreement of the kind specified in subsection (c) of this section and was not represented by an attorney during the course of negotiating such agreement, then the court shall hold a hearing at which the debtor shall appear in person and at such hearing the court shall—

> (1) inform the debtor—
>
> > (A) that such an agreement is not required under this title, under nonbankruptcy law, or under any agreement not made in accordance with the provisions of subsection (c) of this section; and
> >
> > (B) of the legal effect and consequences of—
> >
> > > (i) an agreement of the kind specified in subsection (c) of this section; and
> > >
> > > (ii) a default under such an agreement; and
>
> (2) determine whether the agreement that the debtor desires to make complies with the requirements of subsection (c)(6) of this section, if the consideration for such agreement is based in whole or in part on a consumer debt that is not secured by real property of the debtor. * * * *

(f) Nothing contained in subsection (c) or (d) of this section prevents a debtor from voluntarily repaying any debt. * * * *

(k) [Subsection (k) explains in detail what disclosures are required by subsection (c)(2). These include the amount reaffirmed, the annual percentage rate (mostly interest rate) of the amount reaffirmed, the actual amounts of payments to be made, and the following additional statements:]

> Reaffirming a debt is a serious financial decision. The law requires you to take certain steps to make sure the decision is in your best interest. If these steps are not completed, the reaffirmation agreement is not effective, even though you have signed it.
>
> 1. Read the disclosures in this Part A carefully. Consider the decision to reaffirm carefully. Then, if you want to reaffirm, sign the reaffirmation agreement in Part B (or you may use a separate agreement you and your creditor agree on).
>
> 2. Complete and sign Part D and be sure you can afford to make the payments you are agreeing to make and have received a copy of the disclosure statement and a completed and signed reaffirmation agreement.
>
> 3. If you were represented by an attorney during the negotiation of your reaffirmation agreement, the attorney must have signed the certification in Part C.
>
> 4. If you were not represented by an attorney during the negotiation of your reaffirmation agreement, you must have completed and signed Part E.

5. The original of this disclosure must be filed with the court by you or your creditor. If a separate reaffirmation agreement (other than the one in Part B) has been signed, it must be attached.

6. If you were represented by an attorney during the negotiation of your reaffirmation agreement, your reaffirmation agreement becomes effective upon filing with the court unless the reaffirmation is presumed to be an undue hardship as explained in Part D.

7. If you were not represented by an attorney during the negotiation of your reaffirmation agreement, it will not be effective unless the court approves it. The court will notify you of the hearing on your reaffirmation agreement. You must attend this hearing in bankruptcy court where the judge will review your reaffirmation agreement. The bankruptcy court must approve your reaffirmation agreement as consistent with your best interests, except that no court approval is required if your reaffirmation agreement is for a consumer debt secured by a mortgage, deed of trust, security deed, or other lien on your real property, like your home.

Your right to rescind (cancel) your reaffirmation agreement. You may rescind (cancel) your reaffirmation agreement at any time before the bankruptcy court enters a discharge order, or before the expiration of the 60-day period that begins on the date your reaffirmation agreement is filed with the court, whichever occurs later. To rescind (cancel) your reaffirmation agreement, you must notify the creditor that your reaffirmation agreement is rescinded (or canceled).

What are your obligations if you reaffirm the debt? A reaffirmed debt remains your personal legal obligation. It is not discharged in your bankruptcy case. That means that if you default on your reaffirmed debt after your bankruptcy case is over, your creditor may be able to take your property or your wages. Otherwise, your obligations will be determined by the reaffirmation agreement which may have changed the terms of the original agreement. For example, if you are reaffirming an open end credit agreement, the creditor may be permitted by that agreement or applicable law to change the terms of that agreement in the future under certain conditions.

Are you required to enter into a reaffirmation agreement by any law? No, you are not required to reaffirm a debt by any law. Only agree to reaffirm a debt if it is in your best interest. Be sure you can afford the payments you agree to make.

What if your creditor has a security interest or lien? Your bankruptcy discharge does not eliminate any lien on your property. A ‘lien’ is often referred to as a security interest, deed of trust, mortgage or security deed. Even if you do not reaffirm and your personal liability on the debt is discharged, because of the lien your creditor may still have the right to take the property securing the lien if you do not pay the debt or default on it. If the lien is on an item of personal property that is exempt under your State’s law or that the trustee has abandoned, you may be able to redeem the item rather than reaffirm the debt. To redeem, you must make a single payment to the creditor equal to the amount of the allowed secured claim, as agreed by the parties or determined by the court.

There is much more. Reaffirmation agreements are hard to form in a legally binding way. You can read the whole regulation at https://www.govinfo.gov/content/pkg/USCODE-2023-title11/html/USCODE-2023-title11-chap5-subchapII-sec524.htm

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Questions:

1. What is the consideration for the agreement mentioned in subsection 524(c)?

2. May J.S. rescind the agreement? Why?

3. Must the debtor have an agreement in order to repay a debt that has been discharged in bankruptcy?

4. The following excerpt from *In re Ray*, 26 B.R. 534, 537 (Bankr. D. Kan. 1983), details why § 524 was passed. Bankruptcy was thought to bar only collection of the debt, but the moral obligation to pay it remained. Note that the court names a third exception to the moral-obligation-is-no-consideration rule, besides the two we have studied. What is it?

> [¶1] At common law, it was generally believed "that a promise made in recognition of a moral obligation, arising out of a benefit previously received, was not enforceable." Comment, *Reaffirmation Agreements: A Fight for Enforceability Under the New Bankruptcy Code*, 12 Cumberland L. Rev. 431, 433-34 (1982) (hereinafter cited: Comment, *Reaffirmation Agreements*). Exceptions, however, were developed. In *Ball v. Hesketh*, 90 Eng.Rep. 541 (K.B.1697), a promise to pay a debt contracted during infancy was enforced. In *Hyleing v. Hastings*, 91 Eng.Rep. 1157 (K.B.1699), a promise to pay a debt barred by the statute of limitations was enforced. English attorneys then began arguing that a bankrupt had a moral obligation to repay discharged debts. See generally, Boshkoff, *The Bankrupt's Moral Obligation to Pay His Discharged Debts: A Conflict Between Contract Theory and Bankruptcy Policy*, 47 Ind. L.J. 36, 39-44 (1971) (hereinafter cited: Boshkoff, *Moral Obligation*). In *Truemon v. Fenton*, 98 Eng.Rep. 1232 (K.B.1777), Lord Mansfield declared that a bankrupt was morally obligated to pay discharged debts, and a new promise to pay a discharged debt was sufficient consideration to revive the enforceability of the debt.
>
> [¶2] After *Truemon*, "creditors began to use reaffirmations to escape [the effect of] the bankruptcy discharge. . . ." Comment, *Reaffirmation Agreements*, *supra* at 435. In an effort to control the problem, Parliament first required that the reaffirmation agreement must be in writing, 5 Geo. 4, c. 98, § 128 (1824), and later declared unenforceable all such reaffirmation agreements. 12 & 13 Vict. c. 106, § 204 (1849). Comment, *Reaffirmation Agreements*, *supra* at 435, n.21-23.
>
> [¶3] Just before reaffirmations were banned in England, their use began to grow in the United States, helped by *Scoutland v. Eislord*, 4 N.Y.Com.L.Rep. 241, 7 Johns. 36 (1810), in which Lord Mansfield's doctrine of moral obligation was followed. Even after Congress

passed the Bankruptcy Act of 1898, most states, “by statute or case law, recognized the theory that a discharge did not prohibit collection of the debt or erase the debt.” Comment, *Reaffirmation Agreements*, *supra* at 436.

[¶4] Often, creditors harassed debtors by using the doctrine of moral obligation and the theory that discharged debts were not erased. Sometimes, creditors would sue debtors on the discharged debt in state court “in the hope that the debtor would rely upon the discharge and fail to appear in the subsequent action.” Comment, *Reaffirmation Agreements*, *supra* at 437. Other times, secured creditors would obtain a reaffirmation agreement from the debtor under threat of repossession of collateral. H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 164 (1977), U.S. Code Cong. & Admin. News 1978, p. 5787. Thus,

> (t)he resulting practices under the 1898 Act were similar to those experienced by the English courts in the eighteenth century. Reaffirmations tended to frustrate severely the debtor’s purpose for seeking a discharge from the bankruptcy court.

Comment, *Reaffirmation Agreements*, *supra* at 437. Where the secured creditor used the threat of repossession as leverage to coerce the discharged debtor into reviving and reaffirming his entire personal liability to the creditor, the collateral was generally worth only a portion of the amount owed. The secured creditor did not want to enforce its in rem rights against the collateral. Rather, the secured creditor desired to use the threat of enforcing its in rem rights as a means of coercing the debtor into reviving his in personam obligation which had been discharged. See Boshkoff, *Moral Obligation*, *supra* at 37, n.5.

[¶5] Consider, for example, *In Re Thompson*, 416 F. Supp. 991 (S.D.Tex.1976). A secured creditor was scheduled by the bankrupt in his bankruptcy petition, and filed a proof of claim. The bankrupt was discharged, and was purportedly relieved of any personal liability to the secured creditor. After discharge, the secured creditor began sending letters to the debtor, threatening civil and criminal action if the discharged debt was not paid. *Id.* at 993. The simple fact is that such coercion by creditors has always been built into the system of debtor-creditor relations, and non-judicial coercion has always been viewed by creditors as an effective and certainly inexpensive method of enforcing and reviving a debtor’s in personam obligations. See Leff, *Coercive Collection*, *supra* at 5-9.

[¶6] In 1970, Congress attempted to curtail creditor abuse. Under the Act of Oct. 19, 1970, Pub.L. No. 91-467, sec. 2, 14, 15, 17, 38, 58, 84 Stat. 990 (amending 11 U.S.C. sec. 11, 32, 33, 35, 66, 94 (1964)), bankruptcy courts were given exclusive jurisdiction to determine the right to and effect of a discharge, removing jurisdiction from state courts. No longer could creditors sue debtors in state court on discharged obligations hoping for default judgments. But reaffirmations by non-judicial leverage or coercion were not controlled. See, e.g., *In Re Thompson*, *supra*.

[¶7] It is with this history of creditor coercion and abuse in mind that Congress sat down to draft § 524 of the Code. See H.R. Rep. 95-595, *supra* at 164.

So, there are three circumstances in which a supposed moral obligation (literally a benefit without a present exchange) counts as consideration. What are those three circumstances?

Many lawyers have rationalized these moral obligation cases on a ground other than moral obligation. They claim that moral obligation is not the true ground of these decisions. What is their argument? Well, these lawyers take note that infancy, discharge in bankruptcy, and the statute of limitations are legal defenses to a creditor's breach of contract case against the promisor. These lawyers then argue that something happened to the defense when the second promise was made by the promisor to pay the prior debt: They claim that the defenses were waived. This is not a bad argument. We have not studied waiver yet, but we soon will, and when we do, you can test the theory.

Now here is one more possible moral obligation exception, from the rest of the *Hunt v. Bate* report:

HUNT v. BATE II(1568)

Common Pleas

3 Dyer 272a

* * * * But in [an] action on the case brought upon a promise of twenty pounds made to the plaintiff by the defendant in consideration that the plaintiff, at the special instance [meaning, special request] of the said defendant, had taken to wife the cousin of the defendant, that was good cause, although the marriage was executed and past before the undertaking and promise, because the marriage ensued at the request of the defendant. * * * * And therefore the opinion of the Court in this case this Term was, that the plaintiff should recover upon the verdict, &c.

Questions:

1. What was consideration for the promise?

2. Was there a bargain?

And then there are courts who just disagree:

WEBB v. McGOWIN (1935)

Court of Appeals of Alabama

168 So. 196

BRICKEN, Presiding Judge.

[¶1] This action is in assumpsit. The complaint as originally filed was amended. The demurrers to the complaint as amended were sustained, and because of this adverse ruling by the court the plaintiff took a nonsuit, and the assignment of errors on this appeal are predicated upon said action or ruling of the court.

[¶2] A fair statement of the case presenting the questions for decision is set out in appellant's brief, which we adopt.

> [¶a] "On the 3d day of August, 1925, appellant while in the employ of the W.T. Smith Lumber Company, a corporation, and acting within the scope of his employment, was engaged in clearing the upper floor of Mill No.2 of the company. While so engaged he was in the act of dropping a pine block from the upper floor of the mill to the ground below; this being the usual and ordinary way of clearing the floor, and it being the duty of the plaintiff in the course of his employment to so drop it. The block weighed about 75 pounds.
>
> [¶b] "As appellant was in the act of dropping the block to the ground below, he was on the edge of the upper floor of the mill. As he started to turn the block loose so that it would drop to the ground, he saw J. Greeley McGowin, testator of the defendants, on the ground below and directly under where the block would have fallen had appellant turned it loose. Had he turned it loose it would have struck McGowin with such force as to have caused him serious bodily harm or death. Appellant could have remained safely on the upper floor of the mill by turning the block loose and allowing it to drop, but had he done this the block would have fallen on McGowin and caused him serious injuries or death. The only safe and reasonable way to prevent this was for appellant to hold to the block and divert its direction in falling from the place where McGowin was standing and the only safe way to divert it so as to prevent its coming into contact with McGowin was for appellant to fall with it to the ground below. Appellant did this, and by holding to the block and falling with it to the ground below, he diverted the course of its fall in such way that McGowin was not injured. In thus preventing the injuries to McGowin appellant himself received serious bodily injuries, resulting in his right leg being broken, the heel of his right foot torn off and his right arm broken. He was badly crippled for life and rendered unable to do physical or mental labor.
>
> [¶c] "On September 1, 1925, in consideration of appellant having prevented him from sustaining death or serious bodily harm and in consideration of the injuries appellant had received, McGowin agreed with him to care for and maintain him for the remainder of appellant's life at the rate of $15 every two weeks from the time he sustained his injuries to and during the remainder of appellant's life; it being agreed that McGowin would pay this

> sum to appellant for his maintenance. Under the agreement McGowin paid or caused to be paid to appellant the sum so agreed on up until McGowin's death on January 1, 1934. After his death the payments were continued to and including January 27, 1934, at which time they were discontinued. Thereupon plaintiff brought suit to recover the unpaid installments accruing up to the time of the bringing of the suit.
>
> [¶d] "The material averments of the different counts of the original complaint and the amended complaint are predicated upon the foregoing statement of facts."

[¶3] In other words, the complaint as amended averred in substance: (1) That on August 3, 1925, appellant saved J. Greeley McGowin, appellee's testator, from death or grievous bodily harm; (2) that in doing so appellant sustained bodily injury crippling him for 'life; (3) that in consideration of the services rendered and the injuries received by appellant, McGowin agreed to care for him the remainder of appellant's life, the amount to be paid being $15 every two weeks; (4) that McGowin complied with this agreement until he died on January 1, 1934, and the payments were kept up to January 27, 1934, after which they were discontinued.

[¶4] The action was for the unpaid installments accruing after January 27, 1934, to the time of the suit.

[¶5] The principal grounds of demurrer to the original and amended complaint are: (1) It states no cause of action; (2) its averments show the contract was without consideration; (3) it fails to allege that McGowin had, at or before the services were rendered, agreed to pay appellant for them; (4) the contract declared on is void under the statute of frauds.

[¶6] 1. The averments of the complaint show that appellant saved McGowin from death or grievous bodily harm. This was a material benefit to him of infinitely more value than any financial aid he could have received. Receiving this benefit, McGowin became morally bound to compensate appellant for the services rendered. Recognizing his moral obligation, he expressly agreed to pay appellant as alleged in the complaint and complied with this agreement up to the time of his death; a period of more than 8 years.

[¶7] Had McGowin been accidentally poisoned and a physician, without his knowledge or request, had administered an antidote, thus saving his life, a subsequent promise by McGowin to pay the physician would have been valid. Likewise, McGowin's agreement as disclosed by the complaint to compensate appellant for saving him from death or grievous bodily injury is valid and enforceable.

[¶8] * * * * Any holding that saving a man from death or grievous bodily harm is not a material benefit sufficient to uphold a subsequent promise to pay for the service, necessarily rests on the assumption that saving life and preservation of the body from harm have only a sentimental value. The converse of this is true. Life and preservation of the body have material, pecuniary values, measurable in dollars and cents. Because of this, physicians practice their profession charging for services rendered in saving life and curing the body of its ills, and surgeons perform operations. The same is true as to the law of negligence, authorizing the assessment of damages in personal injury cases based upon the extent of the injuries, earnings, and life expectancies of those injured.

[¶9] In the business of life insurance, the value of a man's life is measured in dollars and cents according to his expectancy, the soundness of his body, and his ability to pay premiums. The same is true as to health and accident insurance.

[¶10] It follows that if, as alleged in the complaint, appellant saved J. Greeley McGowin from death or grievous bodily harm, and McGowin subsequently agreed to pay him for the service rendered, it became a valid and enforceable contract.

[¶11] 2. It is well settled that a moral obligation is a sufficient consideration to support a subsequent promise to pay where the promisor has received a material benefit, although there was no original duty or liability resting on the promisor. * * * *

[¶12] 3. Some authorities hold that, for a moral obligation to support a subsequent promise to pay, there must have existed a prior legal or equitable obligation, which for some reason had become unenforceable, but for which the promisor was still morally bound. This rule, however, is subject to qualification in those cases where the promisor having received a material benefit from the promisee, is morally bound to compensate him for the services rendered and in consideration of this obligation promises to pay. In such cases the subsequent promise to pay is an affirmance or ratification of the services rendered carrying with it the presumption that a previous request for the service was made *McMorris v. Herndon*, 2 Bai1ey (S.c.) 56, 21 Am.Dec. 515; *Chadwick v. Knox*, 31 N.H. 226, 64 Am.Dec. 329; *Kenan v. Holloway*, 16 Ala. 53, 50 Am.Dec. 162; *Ross v. Pearson*, 21 Ala. 473.

[¶13] Under the decisions above cited, McGowin's express promise to pay appellant for the services rendered was an affirmance or ratification of what appellant had done raising the presumption that the services had been rendered at McGowin's request.

[¶14] 4. The averments of the complaint show that in saving McGowin from death or grievous bodily harm, appellant was crippled for life. This was part of the consideration of the contract declared on. McGowin was benefited. Appellant was injured. Benefit to the promisor or injury to the promisee is a sufficient legal consideration for the promisor's agreement to pay. *Fisher v. Bartlett*, 8 Greenl. (Me.) 122, 22 Am.Dec. 225; *State ex rel. Bayer v. Funk, supra*.

[¶15] 5. Under the averments of the complaint the services rendered by appellant were not gratuitous. The agreement of McGowin to pay and the acceptance of payment by appellant conclusively shows the contrary. * * * *

[¶16] From what has been said, we are of the opinion that the court below erred in the ruling complained of; that is to say in sustaining the demurrer, and for this error the case is reversed and remanded.

Reversed and remanded.

SAMFORD, Judge (concurring).

The questions involved in this case are not free from doubt, and perhaps the strict letter of the rule, as stated by judges, though not always in accord, would bar a recovery by plaintiff, but following the principle announced by Chief Justice Marshall in *Hoffman v. Porter*, Fed. Cas. No. 6,577, 2 Brock. 156, 159, where he says, "I do not think that law ought to be separated from justice, where it is at most doubtful," I concur in the conclusions reached by the court.

WEBB v. McGOWIN (1936)

Supreme Court of Alabama

168 So. 199

FOSTER, Justice.

[¶1] We do not in all cases in which we deny a petition for certiorari to the Court of Appeals approve the reasoning and principles declared in the opinion, even though no opinion is rendered by us. It does not always seem to be important that they be discussed, and we exercise a discretion in that respect. But when the opinion of the Court of Appeals asserts important principles or their application to new situations, and it may be uncertain whether this court agrees with it in all respects, we think it advisable to be specific in that respect when the certiorari is denied. We think such a situation here exists.

[¶2] Neither this court nor the Court of Appeals has had before it questions similar to those here presented * * * *. * * * *

[¶3] The opinion of the Court of Appeals here under consideration recognizes and applies the distinction between a supposed moral obligation of the promisor, based upon some refined sense of ethical duty, without material benefit to him, and one in which such a benefit did in fact occur. We agree with that court that if the benefit be material and substantial and was to the person of the promisor rather than to his estate, it is within the class of material benefits which he has the privilege of recognizing and compensating either by an executed payment or an executory promise to pay. The cases are cited in that opinion. The reason is emphasized when the compensation is not only for the benefits which the promisor received, but also for the injuries either to the property or person of the promisee by reason of the service rendered.

Writ denied.

ANDERSON, C.J., and GARDNER and BOULDIN, JJ., concur.

Questions:

1. What is the law in Alabama after these two opinions?

2. How is this case different from *Hunt v. Bate* 1? Is Webb like the physician the court mentions in ¶ 7? Can you make sense of the court's reasoning in ¶ 12? The first sentence says, some courts say X is required, and the next sentence says that these cases are "subject to the qualification" that X is not required, yes? Then the court says that, actually, moral obligation cases are equivalent to prior request cases. Are they? Is that even related to the first two sentences?

3. Most serious promises are made because the promisor feels (i) an obligation to make a promise or (ii) or a need to create an obligation (promises create obligations). Both situations can be described as moral obligations. In an exchange, the trade itself creates the moral obligation to promise or the need to create

the obligation. In fact, McGowin owned the mill. Do the facts of *Webb v. McGowin* make more sense if you know that? Is compensating employees for work injuries part of the exchange that is employment? If it is, then McGowin's promise was merely evidence of the exchange. That approach to the case would require no legal innovation, only good use of evidence. One wonders if McGowin compensated other workers who were injured on the job at the mill. Some courts, then, might handle the case solely as an implied-in-fact exchange (with McGowin's promise being a recognition of the amount owed and Webb's acceptance of it as acquiescence of that settlement). Many cases purporting to follow a rule like *Webb*'s make more sense as recognizing, in their times and circumstances, an implied-in-fact exchange: e.g., a real estate agent who has never spoken with the seller finds a buyer, a passerby takes an apple from the cart and winks at the apple seller. Outside of exchange (express or implied), what constitutes a moral obligation worthy of legal recognition for making a promise binding? The difficulty of answering this question has mostly stopped courts from expanding this line of precedent further. Recent cases are obscure and rare (*Webb* itself has only been cited eight times, and not in any case since 1982). Only a minority of jurisdictions support a "material benefit" rule, and cases outside the exchange context are a subset.

HARRINGTON v. TAYLOR

Supreme Court of North Carolina

36 S.E.2d 227 (1945)

PER CURIAM.

[¶1] The plaintiff in this case sought to recover of the defendant upon a promise made by him under the following peculiar circumstances:

[¶2] The defendant had assaulted his wife, who took refuge in plaintiff's house. The next day the defendant gained access to the house and began another assault upon his wife. The defendant's wife knocked him down with an axe, and was on the point of cutting his head open or decapitating him while he was laying on the floor, and the plaintiff intervened, caught the axe as it was descending, and the blow intended for defendant fell upon her hand, mutilating it badly, but saving defendant's life.

[¶3] Subsequently, defendant orally promised to pay the plaintiff her damages; but, after paying a small sum, failed to pay anything more. So, substantially, states the complaint.

[¶4] The defendant demurred to the complaint as not stating a cause of action, and the demurrer was sustained. Plaintiff appealed.

[¶5] The question presented is whether there was a consideration recognized by our law as sufficient to support the promise. The Court is of the opinion that, however much the defendant should be impelled by common gratitude to alleviate the plaintiff's misfortune, a humanitarian act of this kind, voluntarily performed, is not such consideration as would entitle her to recover at law.

[¶6] The judgment sustaining the demurrer is

Affirmed.

Question: Is this result consistent with *Hunt v. Bate* I? *Harrington* is the majority rule.

3. The Special Problem of Settlement

This case and the next are somewhat difficult, but only because their analyses depend on non-contract law that we have not studied. The non-contract law in both cases is extremely clear and not in dispute. The first case, *Kim v. Son*, relies on rules from corporate law. A corporation is, in the law, a person or entity separate from and not dependent for its existence on any real person, including its shareholders, directors, officers, or employees. So a shareholder of that corporation is no more liable for the debts of the corporation than you are for your neighbor's debts, absent special circumstances not relevant here. In *Kim v. Son*, a party with no right thought it had a right and proceeded to bargain away what it thought it had. Whether this activity has any legal effect is the issue.

The second case is more straightforward, and you should be able to determine the validity of the plaintiff's claims from the case's context. Did the plaintiff in the second case have anything to bargain with?

Jinsoo KIM v. Stephen SON

2009 WL 597232

Court of Appeal, Fourth District, Division 3, California

No. G039818

(Super. Ct. No. 06CC02419).

March 9, 2009

OPINION

O'LEARY, J.

[¶1] Jinsoo Kim begins his opening brief by stating, "Blood may be thicker than water, but here it's far weightier than a peppercorn."[*] Kim appeals from the trial court's refusal to enforce a gratuitous promise, handwritten in his friend's own blood, to repay money Kim loaned and lost in two failed business ventures. He faults the trial court for not discussing or deciding in its statement of decision the issue of whether Kim's forbearance (waiting over a year to file a meritless lawsuit against his friend, Stephen Son), supplied adequate consideration for Son's blood-written document. We conclude the trial court's statement of decision sufficiently set forth the facts and law supporting its ultimate conclusion Son's promise to repay the money was entirely gratuitous and unenforceable, even when reduced to blood. Forbearance to sue cannot supply consideration to what the trial court determined was an invalid claim. In the context of this contract dispute, Son's blood was not weightier than a peppercorn.

I

[¶2] Son was the majority shareholder (70 percent owner) and operated a South Korean company, MJ, Inc. (MJ). He was also the sole owner of a California corporation, Netouch International Inc. (Netouch). After several months of investigation, Kim loaned money and invested in these companies. It was undisputed he wired the money directly to the corporate bank accounts. Son did not personally receive any of the funds. Kim invested 100 million won,[†] and later loaned 30 million won to MJ. He loaned $40,000 to Netouch. There was no evidence these investments or loans were personally guaranteed by Son.

---

[*] [1] The obscure peppercorn reference can be found in Hobbs v. Duff (1863) 23 Cal. 596, 602-603 ["'What is a valuable consideration? A peppercorn; and for aught that appears by the pleadings in this case, there was no greater consideration than that for the supposed assignment,' etc."].

[†] [2] The won (원) (sign: ₩; code: KRW) is the currency of South Korea.

[¶3] Unfortunately, these businesses failed and Kim lost his money. In October 2004, Son and Kim met in a sushi bar where they consumed a great deal of alcohol. When they were at the bar, Son asked the waiter for a safety pin, used it to prick his finger, and then wrote a "promissory note" with his blood. The document, translated from Korean to English, reads, "Sir, please forgive me. Because of my deeds you have suffered financially. I will repay you to the best of my ability." At some point that same day, Son also wrote in ink "I hereby swear [promise] that I will pay back, to the best of my ability, the estimated amount of 170,000,000 [w]ons to [Kim]."

[¶4] Well over a year later, in June 2006, this blood-written note became the basis for Kim's lawsuit against Son alleging: (1) default of promissory note; (2) money had and received; and (3) fraud. He claimed Son agreed in the "promissory note" to pay Kim 170 million won, which is approximately equivalent to $170,000.

See copies of the promises at http://cca.li/QC.

[¶5] After holding a bench trial, the court ruled in Son's favor. In its statement of decision, the court determined the "blood agreement" was not an enforceable contract. The court made the following findings: There was no evidence Son agreed to personally guarantee the loan or investment money. Son wrote the note in his own blood "while extremely intoxicated and feeling sorry for [Kim's] losses." The blood agreement lacked sufficient consideration because it "was not a result of a bargained-for-exchange, but rather a gratuitous promise by [Son] who took personally that [Kim], his good friend, had a failure in his investments that [Son] had initially brought him into." The court reasoned the agreement lacked consideration because Son "was not required to and did not guarantee these investments and loans. The [c]ourt refuses to enforce a gratuitous promise even when it is reduced to blood." The court also rejected the fraud claim, relying on "credible evidence" Son intended for the businesses to succeed, and he never made any promises to Kim without the intent of performing them.

[¶6] Kim filed objections to the statement of decision, claiming inter alia, the court failed to address whether Kim's forbearance from suing Son in 2003 and 2004 was consideration for the blood written promissory note. The court did not modify its statement of decision and entered the final judgment in July 2007. Kim appealed.

II

[¶7] Kim raises two issues on appeal: (1) Did the trial court erroneously fail to consider or apply Kim's forbearance as consideration of Son's blood agreement? and (2) Did the statement of decision adequately address the forbearance issue?

(1) Forbearance

[¶8] "Consideration may be forbearance to sue on a claim, extension of time, or any other giving up of a legal right, in consideration of some promise. [Citations.]" (1 Witkin, Summary of Cal. Law (10th ed. 2005) Contracts, § 211, p. 246.) "The slightest forbearance will suffice: 'Even though the forbearance is for one day only, there is sufficient consideration as the law does not weigh the quantum.' [Citations.]" (*Id*. at pp. 246-247.) Moreover, "The compromise of a claim, either valid, doubtful, or disputed (but not void) is good consideration, the claimant giving up his or her asserted right to recover the whole amount as consideration for a promise to pay a lesser amount. [Citations.]" (*Ibid*.)

[¶9] "However, if the forbearance has no value, it will not suffice. [Citation.]" (1 Witkin, Summary of Cal. Law, *supra*, Contracts, § 211, p. 247.) And relevant to this case, "If a claim is wholly invalid, neither forbearance to sue nor a compromise thereof can be good consideration. (*Union Collection Co. v. Buckman* (1907) 150 C[al]. 159, 164 . . . .) *City Street Imp. Co. v. Pearson* (1919) 181 C[al]. 640, [649] . . . applied this doctrine with great strictness. A promissory note was given in consideration of forbearance to foreclose a lien upon a street assessment, which both parties believed was valid. However, the assessment was void for technical reasons that were ascertainable from the public record. Held, the note was unsupported by consideration. . . . (*See Orange County Foundation v. Irvine Co.* (1983) 139 [Cal. App.]3d 195 . . . [promise to compromise wholly unfounded claim is not valuable consideration . . .] . . . .)" (1 Witkin, Summary of Cal. Law, *supra*, § 220, pp. 253-254.)

[¶10] Here, the purported forbearance to sue cannot be good consideration because Kim's claims against Son were wholly invalid. As determined by the trial court, any claim Son personally owed Kim money was invalid. The statement of decision noted it was undisputed the corporations (MJ and Netouch) were valid separate corporate entities and those businesses received Kim's loans and investment money. The court concluded Son did not guarantee the money on behalf of the two corporations. He did not personally receive any of Kim's money. And, Kim does not dispute a shareholder/owner generally is not personally liable for the debts of a corporation. (*See Mesler v. Bragg Management Co*. (1985) 39 Cal.3d 290, 301 [society legally recognizes the benefits of individual limitation of business liability through incorporation, so "the corporate form will be disregarded only in narrowly defined circumstances," and only when justice so requires]; *Pacific Landmark Hotel, Ltd. v. Marriott Hotels, Inc.* (1993) 19 Cal.App.4th 615, 628.) Consequently, any debt collection or breach of contract claim Kim may have had against the corporations, could not be legally imputed to Son, individually. In other words, Kim's forbearance in filing a meritless lawsuit cannot supply adequate consideration for Son's gratuitous promise.

[¶11] Moreover, Kim does not dispute the trial court's conclusion credible evidence established Son was not liable for fraud. Accordingly, his alleged forbearance to sue on the clearly unfounded tort claim would not constitute valuable consideration. We conclude the trial court properly decided Kim's lawsuit was based entirely on a gratuitous unenforceable promise, and as such, the court did not need to address the immaterial issue of forbearance.

(2) Statement of Decision

[The court determined that the trial court's opinion adequately addressed the forbearance issue.]

III

The judgment is affirmed. Respondent shall recover his costs on appeal.

WE CONCUR: SILLS, P.J., and RYLAARSDAM, J.

Questions:

1. Did the court ask whether Kim believed in good faith that Son was liable for the debts at and after the time the money was invested and lent? Did the court ask whether Kim believed in good faith, before Son signed the document in the bar, that Kim had valid grounds to sue Son with regard to the investments and the loan?

2. The court addressed whether forbearance to sue was consideration, but Kim provided Son's companies with $170,000 in financing. Why wasn't Kim's making the investment and loan consideration?

3. Did it matter that the contract was in writing?

4. Son was drunk when he wrote this document, but is there any doubt that, at the time he wrote the document, he intended to create a binding legal document? Did that matter?

Fannie B. KALIS v. COLGATE-PALMOLIVE COMPANY

Ill. App., 1st District

787 N.E.2d 182

March 10, 2003

JUSTICE McNULTY delivered the opinion of the court:

[¶1] The instant appeal arises from a simple set of undisputed facts: a plaintiff in a products liability action received an offer of settlement from the defendant manufacturer, but did not respond before the defendant prevailed in its motion for summary judgment. Since the settlement proposal had contained no time limit or other conditions for acceptance, the plaintiff notified the defendant that she would take the offer and was promptly informed that the offer was no longer open. While the products liability litigation continued, the plaintiff filed the action underlying this matter: a claim against the defendant for breach of the settlement agreement. The question presented for our review is whether the plaintiff's promise to settle her lawsuit lost its value, and thus its ability to serve as consideration for a settlement payment, once the defendant prevailed in its motion for summary judgment. The trial court answered this question affirmatively. We disagree and reverse the grant of summary judgment in favor of the defendant on the breach of contract claim.

[¶2] Plaintiff Fannie Kalis was injured by the explosion of a container of fuel and in December 1995 filed an action in the United States District Court which sought damages from the alleged manufacturer, defendant Colgate-Palmolive Company (Colgate). On March 13, 1998, Colgate moved for summary judgment. On April 27, 1999, while that motion was pending, Colgate, via letter from its counsel to Kalis's counsel, offered $100,000 to settle the claim. The offer contained no conditions, did not refer to the pending summary judgment motion in any way, and did not purport to expire at any specific time.

[¶3] On May 10, 1999, the district court granted Colgate's motion, and on May 14, Kalis's attorney sent defense counsel a letter accepting Colgate's offer. Colgate's May 18 response advised Kalis that "the

moment the judge ruled summary judgment in our favor and against the plaintiff, the offer of $100,000 was no longer valid."

[¶4] Kalis sought reconsideration of the summary judgment ruling, and when that motion was denied, she appealed. The United States Court of Appeals for the Seventh Circuit heard arguments on the case in April 2000 and affirmed the judgment in Colgate's favor on November 3, 2000.

[¶5] On the same date she filed notice of her appeal of the summary judgment on her products liability claim, Kalis also filed in the circuit court of Cook County the action underlying the instant case: she alleged that Colgate's offer and her acceptance combined to create a binding agreement to settle her claim for $100,000.

[¶6] Kalis and Colgate both moved for summary judgment: Kalis alleging that the formation of a contract and Colgate's subsequent breach were undisputed; Colgate contending that she had no consideration to offer for a settlement agreement after the summary judgment ruling and that an implied condition of its offer was that it be accepted before the motion was decided. The trial court agreed with Colgate, ruled that there was no consideration for the settlement agreement, and granted summary judgment in favor of the company. In our view, established principles of contract law dictate the opposite conclusion.

[¶7] Any act or promise that benefits one party or disadvantages the other is sufficient consideration to support the formation of a contract. *Steinberg v. Chicago Medical School*, 69 Ill. 2d 320, 330 (1977). A promise to forego pursuit of a legal claim will be determined to be adequate consideration to support formation of a contract even if the claim is invalid, provided that it is asserted in good faith. *Keller v. State Farm Insurance Co*., 180 Ill. App. 3d 539, 546 (1989).

[¶8] Such forbearance provides consideration sufficient to support the formation of a contract even if, at the time of the promise, a court has already found the claim to be without merit. "The fact that a lower court has decided against the claim, or that a court has held adversely to it in a suit to which the claimant was not a party, does not prevent the forbearance to press a claim from being consideration." 2 J. Perillo & H. Bender, Corbin on Contracts, §7.17, at 436 (1995).

[¶9] Accordingly, a promise to relinquish a right to appeal has also been recognized as providing consideration sufficient to support contract formation. "Forbearance to appeal or to litigate the question anew, as the claimant is privileged to do, is consideration if the claim was such that forbearance to press it by suit would originally have been consideration." 2 J. Perillo & H. Bender, Corbin on Contracts, §7.17, at 436-37 (1995). In *Kerns v. Engelke*, * * * this court, though ultimately declaring an agreement void on public policy grounds, found that sufficient consideration to form the agreement had been provided by a party's promise to abandon an appeal. * * * *

[¶10] In *F.H. Prince & Co. v. Towers Financial Corp*., 275 Ill. App. 3d 792 (1995), we held that the release of an arguably uncollectible debt provided consideration to support a settlement agreement and highlighted an additional element of value provided by settlement of even a questionable claim: "Settlement of the [plaintiff's] litigation also relieved [defendants] of the need to continue to defend against that claim and to incur additional defense costs related thereto." 275 Ill. App. 3d at 802.

[¶11] In our view, the foregoing principles are readily applicable to the facts presented in the instant case. Though her claim failed to survive Colgate's summary judgment motion, Kalis retained the right to seek

reconsideration of that ruling in the district court as well as the right to seek appellate review, and her promise to compromise these rights provided consideration for the offer of settlement as long as they were asserted in good faith. We believe that the good-faith basis for continued pursuit of her claims at these stages was demonstrated by each court's need for extensive analysis of the merits of those claims. Given that fact, and the fact that the expense of months of additional active litigation of the reconsideration motion and appeal would have been avoided with a settlement, we have little difficulty concluding that Kalis's promise to abandon her claims offered a compromise of her own legal rights, a benefit to Colgate, and thus, consideration. We are therefore unable to share the trial court's view that the summary judgment motion ruling left Kalis with nothing to offer as consideration for the settlement payment. * * * *

[¶12] Finally, although Kalis invites us to direct the trial court to grant her summary judgment motion, she has not demonstrated the absence of issues of fact material to disposition of her claim, and indeed concedes the existence of at least one triable issue of material fact on the record assembled to date. Accordingly, we decline the invitation to order entry of summary judgment in her favor, reverse the entry of summary judgment for Colgate, and remand the cause to the circuit court for further proceedings consistent with this order.

Reversed and remanded.

Questions:

1. How do you distinguish this case from *Kim v. Son*?

2. When the court says "provided that it is asserted in good faith," does the court mean merely that the person asserting the claim must be asserting it honestly? Or must the claim have some objective basis?

3. When do we judge that "good faith"—at the time of the promise or later after all appeals are exhausted?

4. In *Atlantic Trust Co. v. Graver*, No. 2-09-0589, 2011 WL 10109585 at *7 (Ill. App. Jan. 31, 2011), the court said,

In *Kalis*, the plaintiff *retained the right* to seek reconsideration of the summary judgment ruling in the trial court as well as the right to seek appellate review, and her *promise to compromise these rights* constituted consideration for the offer of settlement as long as they were asserted in good faith. * * * * In other words, the plaintiff's promise to abandon her claims offered a compromise of her legal rights, a benefit to the other party, and thus consideration.

If consideration exists in a compromise of rights case, will the compromise of rights be both benefit and detriment?

5. Would the settlement agreement have been binding if Kalis had waited to accept it until Nov. 4, 2000?

_____

Here is an example of a contract form that settlement often takes, an accord and satisfaction:

ASSOCIATED BUILDERS, INC. v. William M. COGGINS et al. (1999)

Supreme Judicial Court of Maine

722 A.2d 1278

DANA, J.

[¶1] Associated Builders, Inc. appeals from a grant of a summary judgment entered in the Superior Court * * * * in favor of the defendants William M. Coggins and Benjamin W. Coggins, d/b/a Ben & Bill's Chocolate Emporium. Associated contends that the court erred when it held that despite a late payment by the Cogginses, an accord and satisfaction relieved the Cogginses of a contractual liability. The Cogginses argue that the three-day delay in payment was not a material breach of the accord and, even if the breach was material, Associated waived its right to enforce the forfeiture. We agree with the Cogginses and affirm the judgment.

[¶2] Associated provided labor and materials to the Cogginses to complete a structure on Main Street in Bar Harbor. After a dispute arose regarding compensation, Associated and the Cogginses executed an agreement stating that there existed an outstanding balance of $70,005.54 and setting forth the following terms of repayment:

> It is agreed that, two payments will be made by [the Cogginses] to [Associated] as follows: Twenty Five Thousand Dollars ($25,000.00) on or before June 1, 1996 and Twenty Five Thousand Dollars ($25,000.00) on or before June 1, 1997. No interest will be charged or paid providing payments are made as agreed. If the payments are not made as agreed then interest shall accrue at 10% [ ] per annum figured from the date of default. There will be no prepayment penalties applied. It is further agreed that Associated Builders will forfeit the balance of Twenty Thousand and Five Dollars and Fifty Four Cents ($20,005.54) providing the above payments are made as agreed.

The Cogginses made their first payment in accordance with the agreement. The second payment, however, was delivered three days late on June 4, 1997. Claiming a breach of the contract, Associated filed a complaint demanding the balance of $20,005.54, plus interest and cost. The Cogginses answered the complaint raising the affirmative defense of an accord and satisfaction and waiver. Both parties moved for a summary judgment. The court granted the Cogginses' motion and Associated appealed.

[¶3] The trial court must enter a summary judgment "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, referred to in the statements

required by [M.R. Civ. P.] 7(d) show that there is no genuine issue as to any material fact set forth in those statements and that any party is entitled to a judgment as a matter of law." M.R. Civ. P. 56(c). "On appeal from a grant of summary judgment, we view the evidence in the light most favorable to the nonprevailing party, and review the trial court decision for errors of law." * * * *

[¶4] "An accord 'is a contract under which an obligee promises to accept a substituted performance in future satisfaction of the obligor's duty.'" * * * * Settlement of a disputed claim is sufficient consideration for an accord and satisfaction. * * * * Here, the court correctly found the June 15, 1995 agreement to be an accord.

[¶5] Satisfaction is the execution or performance of the accord. See Restatement (Second) of Contracts § 281(1) (1981). If the obligor breaches the accord, the obligee may enforce either the original duty or any duty pursuant to the accord. See *id.* § 281(2) (1981); *see also* Arthur L. Corbin, 6 Corbin on Contracts § 1271, at 93-94 (1961). * * * *

[¶8] Even if the [Cogginses breached and Associated had a right to disregard the accord and enforce the original obligation (—Ricks)], Associated waived that right when it accepted the late payment. A waiver is a voluntary or intentional relinquishment of a known right. * * * * If a party in knowing possession of a right does something inconsistent with the right or that party's intention to rely on it, the party is deemed to have waived that right. * * * * A party waives a contractual right arising from a breach because of a late payment when that party accepts tender of the late payment. * * * * Here, because Associated accepted the final $25,000 payment, it waived its right to enforce the forfeiture.

[¶9] The trial court, therefore, did not err when it held that a satisfaction of the accord occurred when Associated accepted the final payment.

The entry is:

Judgment affirmed.

Questions:

1. What is an accord?

2. Paragraph 4 probably contains an implied ruling on consideration. What is probably consideration for the accord in this case? If the accord settled the dispute, do we know what amount Associated Builders initially claimed was owed by the Cogginses?

3. Was consideration here a performance or a promise?

4. If the obligor breaches the accord, what remedies does the obligee have?

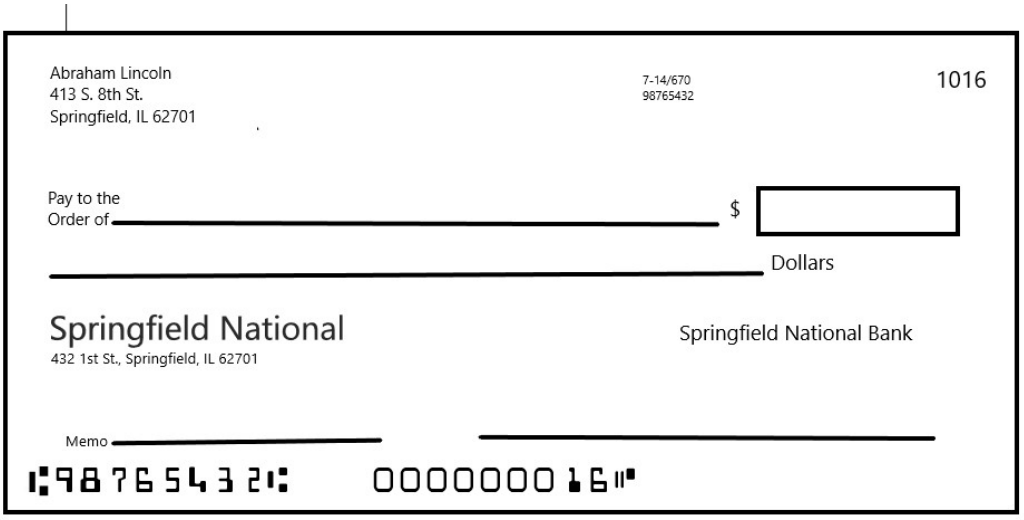
5. What act constituted waiver?

6. What should Associated have done after it received the check if it wanted to sue for the other $20,005.54?

_____

Another accord and satisfaction problem is presented by the mechanism of the “full payment check.” What’s a check?

This is a common bank check. A number is written in the box, e.g., “644.72.” Before “Dollars,” the same number should be written out in words, e.g., “*Six hundred forty-four and 72/100s* Dollars.” After Memo, the line is typically left blank. The line on the bottom right is for the check-writer’s signature.



A check may be a negotiable instrument under UCC Article 3. Will Mr. Lincoln’s check filled out as described above likely be one? Here is the definition:

> Sec. 3.104. NEGOTIABLE INSTRUMENT. (a) Except as provided in Subsections (c) and (d), “negotiable instrument” means an unconditional promise or order to pay a fixed amount of money, with or without interest or other charges described in the promise or order, if it:
>
> (1) is payable to bearer or to order at the time it is issued or first comes into possession of a holder;
>
> (2) is payable on demand or at a definite time; and
>
> (3) does not state any other undertaking or instruction by the person promising or ordering payment to do any act in addition to the payment of money, but the promise or order may contain:

(A) an undertaking or power to give, maintain, or protect collateral to secure payment;

(B) an authorization or power to the holder to confess judgment or realize on or dispose of collateral; or

(C) a waiver of the benefit of any law intended for the advantage or protection of an obligor.

(b) “Instrument” means a negotiable instrument.

(c) An order that meets all of the requirements of Subsection (a), except Subdivision (1), and otherwise falls within the definition of “check” in Subsection (f) is a negotiable instrument and a check.

The fact patterns presenting the problem arise when a person receiving an offer of settlement in the form of a full-payment check attempts to cash the check even while disagreeing with the settlement. The right to disagree seemed to be implied by UCC § 1-308(a), at least while 308 lacked subsection (b). Here is the Texas version of the section:

Sec. 1.308. PERFORMANCE OR ACCEPTANCE UNDER RESERVATION OF RIGHTS.

(a) A party that with explicit reservation of rights performs or promises performance or assents to performance in a manner demanded or offered by the other party does not thereby prejudice the rights reserved. Such words as “without prejudice,” “under protest,” or the like are sufficient.

(b) Subsection (a) does not apply to an accord and satisfaction.

The resolution of these fact patterns depends on this and another statute, UCC 3-311, which is recited in the case itself.

Steven D. HAVARD and Judy A. Havard v. KEMPER NATIONAL INSURANCE COMPANIES et al. (1995)

S.D. Miss., 945 F. Supp. 953, ***aff’d***, 71 F.3d 876 (5th Cir. 1995)

MEMORANDUM OPINION AND ORDER

WINGATE, District Judge.

[¶1] Before the court is the defendants’ motion for summary judgment pursuant to Rule 56(b), Federal Rules of Civil Procedure. Plaintiffs Steven D. Havard and Judy A. Havard filed a complaint in the instant lawsuit seeking actual and compensatory damages and punitive damages against the defendants, Kemper National Insurance Companies d/b/a American Manufacturers Mutual Insurance Company (“Kemper”), Brown & Haynes Insurance, Inc., (“Haynes”), Hatch, Jones & Associates, Inc., (“Hatch”), and Midsouth

Home Service, Inc., ("Midsouth"), for bad faith, fraud, gross negligence, negligent misrepresentation, deceit and other wrongful conduct. The genesis of this dispute began when plaintiffs' home, insured by Kemper, was damaged by an accidental fire. Plaintiffs are unhappy with Kemper's response to their claim under their fire policy and unhappy with the alleged activities of Hatch and Midsouth whose employees acted as appraisers in this matter. All defendants move for summary judgment on the ground that by cashing Kemper's check tendered to plaintiffs in full satisfaction of their policy claim for fire damage to their home, plaintiffs now have fully discharged their claims under the doctrine of accord and satisfaction codified by Miss. Code Ann. § 75-3-311 (Supp.1994). * * * *

FINDINGS OF FACT

[¶2] A fire damaged the home of the Havards, plaintiffs in this suit. The Havards had a homeowners' policy of insurance with Kemper, so following the fire, they submitted an insurance claim with Kemper. Kemper processed the Havards' claim and tendered a check for $5,374.45 for the claim on the damage to the dwelling. An accompanying letter dated June 25, 1993, informed the Havards:

Please find enclosed a check in the amount of $5,374.45 for the repairs to your house. We stand by our letter dated April 30, 1993, which stated the loss settlement and appraisal provisions of your policy. We have reviewed the repair estimates you sent and feel the damage repairs can be properly repaired in accordance with Mr. Meadows' appraisal of $5,874.45.

Later, an attorney for Kemper, Larry Gunn, wrote a letter to plaintiffs' attorney, stating the following:

A check was previously tendered to Mr. and Mrs. Havard in the sum of $5,374.45. The check has not been cashed.

The Havards are not happy with this check. Thus Kemper has elected to rely upon the appraisal provision of the policy. I enclose a copy of the page from the policy showing the terms and provisions of the appraisal provision of the policy. I also enclose a copy of *Hartford Fire Insurance Company v. Conner*, 79 So.2d 236 (Miss. S. Ct.1955) holding the appraisal provision of homeowner's insurance policies to be valid and enforceable.

Please let me know if your clients would like to cash the check for $5,374.45 or if they would like to enter into an appraisal proceeding.

[¶3] After receiving the check, the June 25, 1993, letter from Kemper, and the following letter from Larry Gunn, the Havards cashed the Kemper check. The Havards apparently attempted to reserve their rights to sue by marking on the back of the check "in partial payment and accepted with reservation."

[¶4] Later, after the check had been cashed, plaintiffs sued all parties connected with the insurance claim for bad faith, fraud, gross negligence, negligent misrepresentation, deceit and other wrongful conduct. In short, the plaintiffs claim that Kemper did not properly evaluate their claim and that the other defendants acted with Kemper to undervalue plaintiffs' loss.

PROCEDURE FOR SUMMARY JUDGMENT

[¶5] In response to a motion for summary judgment, the non-moving party is required to respond with proof of a prima facie case, sufficient for a jury to enter a verdict in their favor. * * * *

[¶6] Rule 56(c) of the Federal Rules of Civil Procedure mandates summary judgment in any case where a party fails to establish the existence of an element essential to the case and on which that party has the burden of proof. * * * * Rule 56(c) further requires that the court enter summary judgment if the evidence favoring the non-moving party is not sufficient for the jury to enter a verdict in the non-moving party's favor. * * * * When the moving party has carried the Rule 56(c) burden, the opposing party must present more than a metaphysical doubt about the material facts in order to preclude the grant of summary judgment. * * * *

CONCLUSIONS OF LAW

[¶7] The doctrine of accord and satisfaction recently has been codified in Mississippi, Miss. Code Ann. § 75-3-311 (Supp.1994). The new statute effective after January 1, 1993, provides:

> (a) If a person against whom a claim is asserted proves that (i) that person in good faith tendered an instrument to the claimant as full satisfaction of the claim, (ii) the amount of the claim was unliquidated or subject to a bona fide dispute, and (iii) the claimant obtained payment of the instrument, the following subsections apply.
>
> (b) ... the claim is discharged if the person against whom the claim is asserted proves that the instrument or an accompanying written communication contained a conspicuous statement to the effect that the instrument was tendered as full satisfaction of the claim.

[¶8] The evidence received by this court convincingly establishes that plaintiffs' claim has been discharged under an accord and satisfaction. Here, there was a bona fide dispute, a good faith tender of a check in full satisfaction of the plaintiffs' claim, and the plaintiffs accepted payment of the check. A letter, accompanying the check, contained a conspicuous[**] statement to the effect that the check was tendered in full satisfaction of the claim.

[¶9] Not only did the letter accompanying the check inform the Havards that Kemper was paying no more money on the claim, a subsequent letter written by Kemper's attorney, Larry Gunn, informed the Havards' attorney that the Havards should either cash the check or enter into an appraisal proceeding in accordance with the provisions of the insurance policy.[††] Moreover, the check itself stated on its face that it was "Payment for Fire Damage—Building."

[**] [5] Mississippi Code Annotated § 75-1-201(10) provides:

> (10) "Conspicuous": A term or clause is conspicuous when it is so written that a reasonable person against whom it is to operate ought to have noticed it. A printed heading in capitals (as: NONNEGOTIABLE BILL OF LADING) is conspicuous. Language in the body of a form is "conspicuous" if it is in larger or other contrasting type or color. But in a telegram any stated term is "conspicuous." Whether a term or clause is "conspicuous" or not is for decision by the court.

[††] [6] Section I, Condition (6), of the insurance agreement between the parties provides:

> [i]f you and we fail to agree on the amount of loss, either party may demand an appraisal of the loss ... The two appraisers will choose an umpire. If they cannot agree on an umpire within 15

[¶10] Throughout this entire period, when plaintiffs received the Kemper check and accompanying correspondence, plaintiffs were actively represented by counsel. Hence, before cashing the Kemper check they had ready access to a legal opinion on the possible consequences.

[¶11] But, presence of counsel, while important, is not the key point here. The pivotal fact here is that the correspondence accompanying the check and that sent subsequently certainly told the plaintiffs that Kemper had determined their loss to be no more than $5,394.45; that this was Kemper's final offer; and that if plaintiffs refused to accept this amount, Kemper was prepared to submit the matter to an appraisal proceeding. When plaintiffs cashed the check under these circumstances, plaintiffs showed accord and satisfaction as a matter of law.

[¶12] Plaintiffs seemingly knew that by cashing the check they could be compromising their case. When the Havards cashed the check, they attempted to reserve their rights through notations on the back of the check. However, Miss. Code Ann. § 75-1-207(2)7 (Supp.1994)†††† specifically states that accord and satisfaction is an exception to the general rule that a party may reserve its rights on an instrument. So, while the plaintiffs failed to preserve the vitality of their dispute through this means, by these actions in attempting to do so, they showed an appreciation for the operation of the principle of accord and satisfaction. On this issue of accord and satisfaction, then, this court finds that there are no genuine issues of material fact, and all defendants are entitled to summary judgment on the ground of accord and satisfaction. * * * *

IT IS, THEREFORE, ORDERED AND ADJUDGED that all defendants are entitled to summary judgment, and all claims against all of the defendants are dismissed WITH PREJUDICE. A separate judgment shall be entered in accordance with the local rules.

Questions:

1. Did the Havards assent?

2. What is consideration for the accord and satisfaction?

3. Does one have to find consideration in a full payment check case to which § 3-311 applies?

4. What should the Havards have done with the check?

> days, you or we may request that the choice by [sic] made by a judge of a court of record in the state where the resident premises is located ...

†††† [7] Mississippi Code Annotated § 75-1-207(2) provides:

> (2) Subsection (1) does not apply to an accord and satisfaction.

5. The full payment check device is not as useful as it might seem at first. What in section (a) prevents the device from being used to dispute a phone bill that a consumer simply does not want to pay? Also, consider the other two subsections of 3-311, here reported from the Texas Business & Commerce Code:

> c) Subject to Subsection (d), a claim is not discharged under Subsection (b) if either of the following applies:
>
> (1) The claimant, if an organization, proves that:
>
> (A) within a reasonable time before the tender, the claimant sent a conspicuous statement to the person against whom the claim is asserted that communications concerning disputed debts, including an instrument tendered as full satisfaction of a debt, are to be sent to a designated person, office, or place; and
>
> (B) the instrument or accompanying communication was not received by that designated person, office, or place.
>
> (2) The claimant, whether or not an organization, proves that within 90 days after payment of the instrument, the claimant tendered repayment of the amount of the instrument to the person against whom the claim is asserted. This subdivision does not apply if the claimant is an organization that sent a statement complying with Subdivision (1)(A).
>
> (d) A claim is discharged if the person against whom the claim is asserted proves that within a reasonable time before collection of the instrument was initiated, the claimant, or an agent of the claimant having direct responsibility with respect to the disputed obligation, knew that the instrument was tendered in full satisfaction of the claim.

Before trying the device on your cell phone company, check your phone agreement. What are you likely to find there if your cell phone company has competent legal counsel? If the check went through normal payment processes at the cell phone company, is it likely there will be any evidence satisfying subsection (d)?

4. Mutual Promises

Gaming—

WEST v. STOWELL (1577)

Common Pleas

2 Leonard 154, 74 ER 437, B&M 494

In an action upon the case, by Thomas West against Sir John Stowell, the plaintiff declared, that the defendant, in consideration that the plaintiff promised to the defendant, that if the defendant shall win a certain match at shooting, made between the Lord of Effingham and the defendant, then the plaintiff should pay to the defendant 10£ and promised to the plaintiff, that if the said L. Effingham shall win the same match of the defendant, that then the defendant would pay to the plaintiff 10£ and farther declared that the Lord Effingham won the match, for which the action is brought. It was moved, that here is not any sufficient consideration; for the promise of the plaintiff to the defendant, [is not equally actionable], for there is not any consideration upon which it is conceived, but it [is] only nudum pactum, upon which the defendant could not have an action against the plaintiff. And then here is not any sufficient consideration for the promise of the defendant. Mounsen, Justice, conceived that here the consideration is sufficient, for here this counter promise is a reciprocal promise, and so a good consideration, for all the communication ought to be taken together. Manwood [, J.:] Such a reciprocal promise betwixt the parties themselves at the match is sufficient; for there is consideration good enough to each, as the preparing of the bows and arrows, the riding or coming to the place appointed to shoot, the labour in shooting, the travel in going up and down between the marks: but for the bettors by, there is not any consideration, if the bettor doth not give aim. ....

Questions:

1. Ok, *West* is a little confusing. Perhaps the most confusing part of it is that the reporter, Leonard, doesn't tell you who won. In fact, no one knows. All we have is Leonard's report of the arguments. However, we have evidence from a few years later that gambling cases were being enforced in assumpsit as mutual promises. If the promise was enforced, West won. Do not expect a gambling question on the exam, though; the enforceability of gambling debts could fill a whole semester. Did West and Stowell exchange promises?

2. You have *West* so that you can see (again) that the rule that a promise can be consideration for another promise is quite different than the other consideration forms we have studied. The key to understanding the arguments is that Stowell's counsel is objecting that there is no consideration because there is no detriment to West. That's Manwood's objection, too. But Manwood doesn't think all wagers would be unenforceable. Manwood thinks West could have sued if he had participated in the match. Why would that have made a difference?

3. In this case, if West wins, does he win because otherwise Stowell would get away with a benefit he hadn't paid for? Does he win because otherwise West will have performed a labor Stowell hadn't paid for? What principle(s) of justice supports recovery here?

4. *Nicholas* said that in mutual assumpsit cases, each promisor would have a remedy against the other. Can each have a remedy against the other if the mutual promises were a bet?

5. Who do you think should win this case?

Illusory "Promises"—

RIDGE RUNNER FORESTRY v. VENEMAN (2002)

Fed. Cir.

287 F.3d 1058

[¶1] Ridge Runner Forestry appeals from the decision of the Department of Agriculture Board of Contract Appeals dismissing its cause of action for lack of jurisdiction * * * *. * * * * Because no contract had been formed, we affirm the board's decision.

[¶2] Ridge Runner Forestry is a fire protection company located in the Pacific Northwest. In response to a request for quotations ("RFQ") issued by the Forestry Service, Ridge Runner submitted a proposal and ultimately signed a document entitled Pacific Northwest Interagency Engine Tender Agreement ("Tender Agreement"). The Tender Agreement incorporated the RFQ in its entirety, including the following two provisions in bold faced lettering: (1) "Award of an Interagency Equipment Rental Agreement based on response to this Request for Quotations (RFQ) does not preclude the Government from using any agency or cooperator or local EERA resources"; and (2) "Award of an Interagency Equipment Rental Agreement does not guarantee there will be a need for the equipment offered nor does it guarantee orders will be placed against the awarded agreements." Request for Quotation, No. R6-99-117 (March 29, 1999). Additionally, because the government could not foresee its actual equipment needs, the RFQ contained language that allowed the contractor to decline the government's request for equipment for any reason: "Because the equipment needs of the government and availability of contractor's equipment during an emergency cannot be determined in advance, it is mutually agreed that, upon request of the government, the contractor shall furnish the equipment offered herein to the extent the contractor is willing and able at the time of order." *Id.* (emphasis added). The RFQ also included a clause informing bidders that they would not be reimbursed for any costs incurred in submitting a quotation. Ridge Runner signed Tender Agreements in 1996, 1997, 1998, and 1999. In 1999, it presented a claim for $180,000 to the contracting officer alleging that the Forestry Service had violated an "implied duty of good faith and fair dealing" because Ridge Runner had been "systematically excluded for the past several years from providing services to the Government." In response, the contracting officer told Ridge Runner that she lacked the proper authority to decide the claim. Ridge Runner timely appealed the decision to the Department of Agriculture Board of Contract Appeals. The board granted the government's motion to dismiss concluding that because no

contract had been entered into, it lacked jurisdiction under the Contract Disputes Act ("CDA"), 41 U.S.C. §§ 601-613.

[¶3] We have jurisdiction over an appeal from a decision of an agency board of contract appeals by virtue of 28 U.S.C. § 1295(a)(10). The board's jurisdiction under the CDA requires, at a minimum, a contract between an agency and another party. * * * * Therefore, the threshold matter is whether the Tender Agreements constituted contracts between the parties, which is a question of law that we review de novo. * * * *

[¶4] Ridge Runner argues that the Tender Agreement was a binding contract that placed specific obligations upon the government; namely, the government was obligated to call upon Ridge Runner, and the other winning vendors, for its fire fighting needs, and in return, the vendors were to remain ready with acceptable equipment and trained staff to answer the government's call. This, Ridge Runner argues, places the alleged contract squarely within our holding in *Ace-Federal*, 226 F.3d 1329.

[¶5] *Ace-Federal* involved a requirements contract whereby the government was obligated to use, with limited exceptions, enumerated suppliers. Following a request for proposals, Ace Federal, as well as other vendors, contracted with the government to provide court reporting and transcription services for various federal agencies. Included in each of the contracts was the standard requirements clause found in Federal Acquisition Regulation § 52.216-21(c) which provides "[e]xcept as this contract otherwise provides, the Government shall order from the Contractor all the supplies or services specified in the Schedule that are required to be purchased by the Government activity or activities specified in the Schedule." 48 C.F.R. § 52.216-21(c) (1988). Each contract also included a termination for convenience clause that limited government liability should the General Services Administration ("GSA") choose to cancel any contract. During the relevant term, some of the covered agencies contracted for transcription services from non-contract sources without obtaining the necessary waiver. We held that "each time an agency that did not obtain a GSA waiver arranged for services covered under the contract from a non-contract source, the government did not act within the limited exception and breached the contract." Ace-Federal, 226 F.3d at 1332-33.

[¶6] The contract in *Ace-Federal* is quite distinct from the Tender Agreements at issue in this case. That contract obligated the government to fulfill all of its requirements for transcription services from enumerated vendors or obtain a waiver. The Tender Agreements here are nothing but illusory promises. By the phrase illusory promise is meant words in promissory form that promise nothing; they do not purport to put any limitation on the freedom of the alleged promisor, but leave his future action subject to his own future will, just as it would have been had he said no words at all. *Torncello v. United States*, 231 Ct. Cl. 20, 681 F.2d 756, 769 (1982) (quoting 1 Corbin on Contracts § 145 (1963)). The government had the option of attempting to obtain firefighting services from Ridge Runner or any other source, regardless of whether that source had signed a tender agreement. The Agreements contained no clause limiting the government's options for firefighting services; the government merely "promised" to consider using Ridge Runner for firefighting services. Also, the Tender Agreement placed no obligation upon Ridge Runner. If the government came calling, Ridge Runner "promised" to provide the requested equipment only if it was "willing and able." It is axiomatic that a valid contract cannot be based upon the illusory promise of one party, much less illusory promises of both parties. See Restatement (Second) of Contracts § 71(1).

[¶7] Accordingly, the decision of the Department of Agriculture Board of Contract Appeals is affirmed.

Question: Is this case about the government not promising anything, or about Ridge Runner Forestry not providing any consideration?

The result in *Ridge Runner Forestry* seems acceptable, but consider the following problems. See if you can predict the right result. The answers, taken from real cases, can be found immediately after in excerpts from the cases. A note of caution: Some of these cases are controversial. The rule they cite might be acceptable, but the application may be erroneous, or at least problematic. Some courts myopically look for only a promise when some performance might in fact be the sought-for exchange. Before you look at the court's resolution of these, try to exercise your own judgment regarding whether consideration exists.

PROBLEM 12. Miami Coca-Cola Bottling Co. ("Bottler") agreed with Orange Crush Co. ("Crush") as follows: Crush would give Bottler a perpetual and exclusive license within a designated territory to make, bottle, and distribute Orange Crush under Crush's trademark. Crush would supply concentrate at stated prices and do certain advertising. Bottler agreed to buy a specified quantity of concentrate, maintain the bottling plant, solicit orders for Orange Crush, promote its sale, and "develop an increase in the volume of sales." The license "contained a proviso to the effect that [Bottler] might at any time cancel the contract."

Bottler bought a quantity of concentrate and performed for about a year. Then, Crush gave written notice to Bottler that Crush would no longer be bound. In response to Bottler's suit, Crush claimed that Bottler's promise was illusory and that its own promise was therefore without consideration. What result?

PROBLEM 12 ANSWER: The court in *Miami Coca-Cola Bottling Co. v. Orange Crush Co.*, 296 F. 693 (5th Cir. 1924), ruled for Crush. Here is the court's reasoning:

> We agree with the District Judge that the contract was void for lack of mutuality. It may be conceded that the appellee is liable to the appellant for damages for the period during which the contract was performed; but for such damages the appellant has an adequate remedy at law. So far, however, as the contract remains executory, it is not binding, since it can be terminated at the will of one of the parties to it. The consideration was a promise for a promise. But the appellant did not promise to do anything, and could at any time cancel the contract. According to the great weight of authority such a contract is unenforceable.

Did the court reach the correct result? What did Crush actually want in exchange for their promise?

PROBLEM 13. Ted Mutz became friends with Marshall Hanrahan (H), a lonely and wealthy older man, when Mutz interrupted a vacation to do temp work in H's home. After Mutz went back home, the two traded calls and Christmas cards. Later, on another vacation, Mutz visited and was shocked to find H's health and home

in dire condition. After H's repeated requests, Mutz agreed to stay and help during the vacation, for the same minimal pay as before, thought H's needs made the work more menial, difficult, and longer. Mutz stayed partly out of kindness. When the vacation was over, Mutz returned home, but H phoned him frequently and urged him to return. Mutz did, but he and H decided to put more formality in their relationship. By this time, Mutz was taking care of H 24 hours each day. H suffered a stroke but continued to go out in public, with Mutz's help. Eventually, H called his longtime counsel, Wallace, to draft an employment agreement. The agreement promised Mutz a monthly salary and that H would leave Mutz $10,000 in H's will. The agreement said it might be terminated on thirty days' notice by either party. H ordered Wallace to change H's will to conform, and Wallace started on that, but H never signed the amended will before dying a month later. Mutz performed until H died. Did the termination provision render the promises illusory?

PROBLEM 13 ANSWER: No. The court said this:

> We note also that the decedent's power of revocation in the instrument was exercisable only on notice to the respondent. Thus, the decedent did not have an unlimited power of revocation and the general rule cited by the appellants is not applicable here. It is well established in this state that if a power of arbitrary termination is exercisable only upon notice, the requirement of notice is a sufficient legal detriment to constitute consideration and hence an enforceable obligation . . . .
>
> Furthermore, a lack of mutuality is tantamount to want of consideration and where, as in this case, sufficient consideration is otherwise present, mutuality is not essential. It becomes essential only when its absence would leave a party without a valid or available consideration for his promise . . . .

Mutz v. Wallace, 29 Cal. Rptr. 170, 177 (App. 1963). It is doubtful that anyone bargains for notice, but bargaining for all the performance the other party is willing to give, along with notice of a change of mind, is often worth bargaining for.

Also, what the court says in the second paragraph harmonizes with *Nicholas v. Raynbred*, which is one early (perhaps the most important) source of our phrase "mutuality." What did B really want, the promise of a cow or the cow? If A had delivered the cow, then almost certainly B got what B bargained for; and, in that case, no one would have bothered with a "mutual assumpsit" action for breach of the promise to deliver the cow. The R2K §75 contains this assertion, "[A] promise which is bargained for is consideration if, but only if, the promised performance would be consideration." As a general rule, this is surely true. People who bargain for promises are ultimately seeking the promised performance, so, if they receive that, they have what they bargained for.

The termination provision required thirty days' notice, but what if it required only one day, or no days? What does the rule provide?

If a promise that can be terminated on notice is not illusory, would it make any difference to the enforceability of a contract if only one party had a right to terminate, not both parties? What does the rule provide?

Wallace as H's executor also argued in *Mutz* that H's contract did not survive his death. The court rejected that argument because contractual obligations generally survive a person's death and bind their estate

unless the contract calls only for the promisor to perform them in person (so, if Nikola Jokic dies, his estate cannot finish out his season and should not owe damages for breach). 29 Cal. Rptr. at 176–77.

PROBLEM 14. Scott offered to the Moragues Lumber Co. as follows: "I am thinking of buying an American shipping vessel of about 1,050 tons, due in Chile. If I buy it, I will charter it to you for the transportation of a cargo of lumber from any port in the Gulf of Mexico to Montevideo or Buenos Aires, for the freight of $65 per thousand feet of lumber, freight to be prepaid, free of discount and of insurance, and the vessel to be furnished within a reasonable time after its purchase." Moragues Lumber accepted this offer, meaning it promised to charter the boat as offered. Scott purchased the vessel. Moragues Lumber was ready, willing, and able to charter it, but Scott chartered it to someone else. In response to Moragues Lumber's suit against Scott, Scott argued that his own promise was illusory. Was it?

Along the same line as these facts, consider the common fact scenario of a real estate purchase contract with a financing condition—the purchaser's promise to buy is "subject to" purchaser's obtaining financing. But the purchaser will never obtain financing unless the purchaser applies for financing and cooperates with the lender.[*] Does the financing condition render the promise to buy illusory?

PROBLEM 14 ANSWER: No. Here is the court's language from *Scott v. Moragues Lumber Co.*, 80 So. 394 (Ala. 1918):

> It is said, in the first place, that the alleged contract between the parties was conditioned upon the will of [Scott,] and was therefore void for want of consideration or mutuality of obligation. A valid contract may be conditioned upon the happening of an event, even though the event may depend upon the will of the party who afterwards seeks to avoid its obligation. * * * * [Scott] was not bound to purchase the vessel; but, when he did, the offer—or the contract, if the offer had been accepted—thereafter remained as if this condition had

[*] Nearly all real estate sales transactions occur as follows: The buyer and seller bind themselves to a contract to sell, subject to certain conditions. They then go about seeing if the conditions are met: that the seller owns the property, that the buyer obtains financing, and so on. After a period of time during which the parties can assure that the conditions are met, the parties "close" the transaction by actually trading the real property and the payment given in exchange for it. Often, they will close through a third party who holds the document transferring title to the property (called a "deed," usually) and the money to be paid for the property. We call the holding of these things for a pending transaction an "escrow." These are deposited "in escrow." We often refer to the entity or person holding things in escrow as "escrow agent" even though the person holding things in escrow is not an agent of either party. An escrow is not an agency relationship. (Agents are duty-bound to take directions from a principal, and the escrow is bound by contract, not by either party's directions.)

> never been stipulated, its mutuality or other necessary incidents of obligation depending upon its other provisions and the actions of the parties thereunder.

We will deal with conditions throughout the law of contract, and this holding in *Scott* will come back to help or haunt you (depending on whether you think it is wise).

Does the language from *Scott* also resolve the real estate purchase financing condition problem?

PROBLEM 15. This problem comes from a case written by Justice (then Judge) Cardozo. Best let him tell it in his own words. The case is *Wood v. Lucy, Lady Duff-Gordon*, 118 N.E. 214 (N.Y. 1917):

> The defendant styles herself "a creator of fashions." Her favor helps a sale. Manufacturers of dresses, millinery and like articles are glad to pay for a certificate of her approval. The things which she designs, fabrics, parasols and what not, have a new value in the public mind when issued in her name. She employed the plaintiff to help her to turn this vogue into money. He was to have the exclusive right, subject always to her approval, to place her indorsements on the designs of others. He was also to have the exclusive right to place her own designs on sale, or to license others to market them. In return, she was to have one-half of "all profits and revenues" derived from any contracts he might make. The exclusive right was to last at least one year from April 1, 1915, and thereafter from year to year unless terminated by notice of ninety days. The plaintiff says that he kept the contract on his part, and that the defendant broke it. She placed her indorsement on fabrics, dresses and millinery without his knowledge, and withheld the profits. He sues her for the damages, and the case comes here on demurrer.

Lady Lucy, in demurrer, claimed that Wood never promised to do anything and that the contract was therefore lacking in consideration. True?

PROBLEM 15 ANSWER: Cardozo concluded that Wood actually promised something. Because that is not immediately apparent on the facts, Cardozo spent some time discussing it:

> It is true that he does not promise in so many words that he will use reasonable efforts to place the defendant's indorsements and market her designs. We think, however, that such a promise is fairly to be implied. * * * * A promise may be lacking, and yet the whole writing may be "instinct with an obligation," imperfectly expressed * * * *. If that is so, there is a contract.
>
> The implication of a promise here finds support in many circumstances. The defendant gave an exclusive privilege. She was to have no right for at least a year to place her own indorsements or market her own designs except through the agency of the plaintiff. The acceptance of the exclusive agency was an assumption of its duties * * * *. We are not to suppose that one party was to be placed at the mercy of the other * * * *. Many other terms of the agreement point the same way. We are told at the outset by way of recital that "the

> said Otis F. Wood possesses a business organization adapted to the placing of such indorsements as the said Lucy, Lady Duff-Gordon has approved."
>
> The implication is that the plaintiff's business organization will be used for the purpose for which it is adapted. But the terms of the defendant's compensation are even more significant. Her sole compensation for the grant of an exclusive agency is to be one-half of all the profits resulting from the plaintiff's efforts. Unless he gave his efforts, she could never get anything. Without an implied promise, the transaction cannot have such business "efficacy as both parties must have intended that at all events it should have" (BOWEN, L. J., in The Moorcock, 14 P. D. 64, 68). But the contract does not stop there. The plaintiff goes on to promise that he will account monthly for all moneys received by him, and that he will take out all such patents and copyrights and trademarks as may in his judgment be necessary to protect the rights and articles affected by the agreement. It is true, of course, as the Appellate Division has said, that if he was under no duty to try to market designs or to place certificates of indorsement, his promise to account for profits or take out copyrights would be valueless. But in determining the intention of the parties, the promise has a value. It helps to enforce the conclusion that the plaintiff had some duties. His promise to pay the defendant one-half of the profits and revenues resulting from the exclusive agency and to render accounts monthly, was a promise to use reasonable efforts to bring profits and revenues into existence. For this conclusion, the authorities are ample * * * *.

Because Wood actually promised something, Cardozo concluded, Lady Lucy could be bound to her own promises. But, Cardozo's analysis raises questions:

1. Who do you suppose drafted this agreement? Why was it drafted the way it was?

2. This is a four-three decision in the NY Court of Appeals. Would the dissenters hold that no mutuality existed? Under what circumstances would that be fair to Wood?
3. If the contract is taken as is, without any implied terms, what is Lucy's remedy if Wood does nothing to promote her designs?
4. Some have suggested that this case was decided on incorrect grounds and probably reached the wrong result, even though in the practical legal world the opinion is taken as unquestionable, though easily distinguishable, authority. Why wasn't this a case of unilateral contract—a bargain for some sort of action rather than a bargain for a promise in return?

Wood, that ingenious drafta

Wrote “duties” that he didn’t hafta,

But the court didn’t suffer

That clever old duffer

To lose, so he had the last laughta.

Of course, Lucy, Lady Duff-Gordon, is still famous as a designer, though somewhat out of fashion now. She is also famous as a Titanic survivor.

PROBLEM 16. Mattei, a real estate developer, was planning to build a shopping center on a tract next to Hopper’s land. Mattei wanted to include Hopper’s land in the development. For several months, a real estate agent tried to negotiate a sale of Hopper’s land to Mattei. After Hopper rejected several proposals, the agent suggested Hopper herself submit a proposal. She did, on a form supplied by the agent. Mattei accepted the offer on the day it was offered. Under the agreement, Mattei was required to deposit $1,000 and pay another $56,500 at closing. The agreement said that the parties would close in 120 days. The agreement also contained the following condition: “Subject to Coldwell Banker & Company obtaining leases satisfactory to the purchaser.” Leases for what? For the shopping center. Apparently, Mattei was not going to build it unless leases for space within it were already in place. If he was not going to build, then he did not want to buy Hopper’s land.

Mattei paid the $1,000 deposit. While Mattei was securing leases, and before the 120 days had ended, Hopper’s attorney gave notice that she would not sell. Later, Mattei gave Hopper notice that satisfactory leases had been obtained. Mattei offered to pay the balance. Hopper refused to tender a deed. Her argument? That Mattei’s promise was illusory. Was it?

PROBLEM 16 ANSWER: No. Here is the court's language, *Mattei v. Hopper*, 330 P.2d 265 (Cal. 1958):

> While contracts making the duty of performance of one of the parties conditional upon his satisfaction would seem to give him wide latitude in avoiding any obligation and thus present serious consideration problems, such "satisfaction" clauses have been given effect. They have been divided into two primary categories and have been accorded different treatment on that basis. First, in those contracts where the condition calls for satisfaction as to commercial value or quality, operative fitness, or mechanical utility, dissatisfaction cannot be claimed arbitrarily, unreasonably, or capriciously * * *, and the standard of a reasonable person is used in determining whether satisfaction has been received. * * * * Of the cited cases, two have expressly rejected the arguments that such clauses either rendered the contracts illusory (*Collins v. Vickter Manor, Inc*., *supra*) or deprived the promises of their mutuality of obligation. (*Melton v. Story*, *supra*.) The remaining cases tacitly assumed the creation of a valid contract. However, it would seem that the factors involved in determining whether a lease is satisfactory to the lessor are too numerous and varied to permit the application of a reasonable man standard as envisioned by this line of cases. Illustrative of some of the factors which would have to be considered in this case are the duration of the leases, their provisions for renewal options, if any, their covenants and restrictions, the amounts of the rentals, the financial responsibility of the lessees, and the character of the lessees' businesses.
>
> This multiplicity of factors which must be considered in evaluating a lease shows that this case more appropriately falls within the second line of authorities dealing with "satisfaction" clauses, being those involving fancy, taste, or judgment. Where the question is one of judgment, the promisor's determination that he is not satisfied, when made in good faith, has been held to be a defense to an action on the contract. * * * * Although these decisions do not expressly discuss the issues of mutuality of obligation or illusory promises, they necessarily imply that the promisor's duty to exercise his judgment in good faith is an adequate consideration to support the contract. None of these cases voided the contracts on the ground that they were illusory or lacking in mutuality of obligation. Defendant's attempts to distinguish these cases are unavailing, since they are predicated upon the assumption that the deposit receipt was not a contract making plaintiff's performance conditional on his satisfaction. As seen above, this was the precise nature of the agreement. Even though the "satisfaction" clauses discussed in the above-cited cases dealt with performances to be received as parts of the agreed exchanges, the fact that the leases here which determined plaintiff's satisfaction were not part of the performance to be rendered is not material. The standard of evaluating plaintiff's satisfaction—good faith—applies with equal vigor to this type of condition and prevents it from nullifying the consideration otherwise present in the promises exchanged.
>
> Moreover, the secondary authorities are in accord with the California cases on the general principles governing "satisfaction" contracts. "It has been questioned whether an agreement in which the promise of one party is conditioned on his own or the other party's satisfaction contains the elements of a contract—whether the agreement is not illusory in character because conditioned upon the whim or caprice of the party to be satisfied. Since, however, such a promise is generally considered as requiring a performance which shall be satisfactory to him in the exercise of an honest judgment, such contracts have been

> almost universally upheld." * * * * "A promise conditional upon the promisor's satisfaction is not illusory since it means more than that validity of the performance is to depend on the arbitrary choice of the promisor. His expression of dissatisfaction is not conclusive. That may show only that he has become dissatisfied with the contract; he must be dissatisfied with the performance, as a performance of the contract, and his dissatisfaction must be genuine." (Rest., Contracts (1932), § 265, comment a.)

Questions:

1. Is Mattei different from *Scott v. Moragues Lumber Co.*?

2. See if you can imagine examples of kinds of cases in which satisfaction is governed by a good faith standard, or by a reasonableness standard. Which standard is more likely to result in settlement before trial?

When Hopper spoke her bottom line,

And Mattei could finally sign,

He could be satisfied,

And she couldn't hide,

No matter how much she could whine.

Here is one last illusory promise case.

FORRESTER'S CASE

1 Siderfin 41 (1661)

A minor by his guardian brought an action on the case in assumpsit and [the jury] found for the minor. And it was moved in arrest of the judgment * * * * that the consideration for this promise being it was by a minor to pay a sum of money is void, * * * * so that the promise on which the action is brought lacks consideration. But by the whole Court it was held that if the money was paid according to the promise of the minor it is clear that this action well lies because the consideration is executed. And it was held and ruled by the whole Court that although the money was not paid (whereas it was not in this case) nevertheless the action well lies because it is solely in the election of the minor to make his promise void, and not in the election of the [other] party * * * *. And it was said by Twisden, J., that where a minor made a lease for annual rent that it is not at all in the election of the lessee [to avoid] this lease for the infancy of the lessor, and upon the selfsame reason is our principal case, upon that judgment * * * *.

Questions:

1. Is this case different than *West v. Stowell*? If you recall, in *West* the two parties, a participant and a bystander, bet on an archery match. Only one of the two could win the bet. That meant that only one party's promise could become enforceable. The promise made to the loser of the bet would not be enforceable by definition. What was the result in *West*?

2. According to *Forrester's Case* and Justice Mounsen's position in *West*, does a promise need to be enforceable in order to function as a valuable consideration?

3. A similar problem arises in cases in which the statute of frauds has effect. The statute of frauds, which we will study in Chapter 6, declares certain types of promises unenforceable if not in a writing signed by the promisor. Could such an unenforceable promise serve as consideration? For the most part, courts have said "yes," though a few states (such as the great state of Idaho, and also Michigan) dissent. Is it fair that an unenforceable promise serve as consideration? In *Coca-Cola Bottling Corp. v. Kosydar*, 331 N.E.2d 440, 444 (Ohio 1975), the court said, "The uttering of promises does not supply the actual consideration for the bargain. It is the content of the promise or the actual anticipated performance which supplies consideration for the bargain." *Accord* Restatement (Second) of Contracts §§ 75, 78 (1981).

4. Is this case different from *Scott v. Moragues Lumber*, the answer to Problem 14?

b. Note on Assent

For the last century and a half, courts have routinely held that one party to a contract must assent to another's promise before that promise is enforceable: "The essential elements of a valid contract must be present: competent parties, legal subject matter, valuable consideration, and mutual assent." *Blatt v. Blatt*, Opinion, 1988 WL 619305, *2 (Va. Cir. Ct. August 4, 1988). We will study mutual assent soon, but you should wonder already why both consideration and mutual assent are required. Is it possible for consideration to be present without mutual assent existing?

Justice Laurence Tanfielde in *Slade's Case*, which was argued several times before all the justices of England between 1597 and 1602, said the following:

> [A]s I have learned, an assumption is nothing but a mutual agreement between the parties for a thing to be performed by the defendant in consideration of [some benefit to the promisor or detriment to the promisee].

J.H. Baker, The Legal Profession and the Common Law 397 (1986, trans. by Baker). Justice Saunders said something similar in *Peters v. Opie*, 2 Keble 837, 84 Eng. Rep. 529, 530 (1671): "A mutual promise is but the construction of law on a mutual agreement." Both of these statements were made at least a century before assent was an element of contract law.

It is clearly possible to have assent without consideration. That's what happens when a gift promise is freely given and freely accepted, no?

The nations in continental Europe early and almost uniformly adopted assent as the touchstone of contract formation. Consider French jurist Pothier:

Robert J. Pothier, Treatise on the Contract of Sale § 31

(1752, transl. L.S. Cushing 1839)

The consent of the parties, which is of the essence of the contract of sale, consists in a concurrence of the will of the seller, to sell a particular thing to the buyer, for a particular price, and of the buyer, to buy of him the same thing for the same price.

Pothier and a few others like him wrote treatises that theorized contract law persuasively around consent. Pothier and Hugo Grotius, whose treatise was published in 1626, wielded great influence over English and American courts in the early part of the 19th century. America in particular was eager for new ideas from abroad, and some American lawyers tried somewhat successfully to extend French intellectual influence in American politics and law. During this time the common law of contracts adopted a requirement of mutual assent. We will study later in the semester how that came about. Now both of the following statements from courts are fairly common:

Turner-Bass Assocs. of Tyler v. Williamson,

932 S.W.2d 219, 222 (Tx. Ct. App. 1996).

Mutual assent or agreement is the essence of a contract.

Braddock v. Madison Cty.

34 F. Supp.2d 1098, 1104 (S.D. Ind. 1998).

At its core and in general, however, the essence of contract law is the enforcement of promises where the parties have manifested their assent to a mutual exchange of consideration.

So, is the essence assent or exchange? Courts don't even seem to see the tension between the two statements. Perhaps that is because so few agreements lack consideration, given most folks' evident self-interestedness, particularly if courts "intend" consideration as did the court in *Riches v. Bridges* (and they

do that, as we will see later). Is consideration essential to contract, or is agreement really what it is all about? You should continue to ponder that question. Is it possible to have consideration without assent?

c. A Note on Remedies

The following are rough definitions of contract law remedies. We are going to study these in detail later in the semester, but these definitions will give you enough until then.

Damages remedies—a sum of money ordered to be paid—originated in the English royal law courts and are thus often called legal remedies. Injunctive and declaratory remedies originated, for our purposes, in chancery, meaning the office of the chancellor of England, who was entrusted with that nation's public conscience. Often injunctive and declaratory remedies are called equitable remedies. Restitutionary remedies have a more difficult genealogy. They were granted by both the law courts and the chancery. Here, because they are an award of money for breach of contract, restitutionary damages are a legal remedy.

Soon, we will study the cause of action known as "unjust enrichment" or "restitution." This is also an action at law, traditionally, and the remedy for it is typically restitution of some sort. Because the law courts when granting remedy for unjust enrichment paid homage to "justice and conscience," restitution was (and is) often called equitable in nature, and damages for it are also equitable in nature and range beyond a mere order to pay a sum of money.

Only tradition stops the courts from rewarding damages outside of these categories, and occasionally courts become very creative in the relief they order. Most courts stick with these, choosing from among them the one/s they feel would best do justice (without duplication).

Expectation Damages: a sum of money intended to place the non-breaching party in the position that party would have been in had the promise at issue been performed.

Reliance Damages: a sum of money intended to place the non-breaching party in the position that party would have been in had the promise at issue not been made. Generally two kinds of costs to the non-breaching party form a basis for reliance damages: out-of-pocket costs—direct net costs incurred by a promisee in reliance on a promise prior to breach; and opportunity costs—indirect net value that the promisee would have enjoyed if the promisee had taken an opportunity that the promise led the promisee to forego.

Restitution Damages: an order that the promisor pay a sum of money equal in value to the benefit that has been conferred by the injured party on the promisor. The general purpose of restitution damages for breach of contract is to put the party in breach back in the position it would have been in had the contract not been made.

Some remedies are not meant to provide a substitute for harm done but order other relief:

Injunction: a court's order that a party do or not do something other than pay money damages. For example, in certain, special cases, a court may order specific performance, that the promisor perform as

promised. In other cases, a court may order that a party to a contract refrain from interfering with another party's performance. Courts often say that injunctive relief is inappropriate when legal remedies adequately compensate the plaintiff. The prototypical case in which damages are inadequate and specific performance is appropriate occurs when a promisor breaches a promise to sell land, because each piece of land is unique and determining the appropriate amount of damages involves too much speculation.

Rescission: Rescission means the undoing or canceling of a contract.

Declaratory Relief: a court's statement of a party's legal rights. For example, a court may state that a contract is void or voidable (rescindable) at the option of one or either party.

PROBLEM 17. A hires B to build a house for $100,000. B buys $20,000 worth of materials and does $15,000 worth of work that uses up all $20,000 in materials. Then A fires B for no good reason. The house would have cost B $90,000 to build. What are B's damages? The court will probably let B choose its legal remedy, if one of them is adequate to compensate B, so which should B choose?

In Texas, an additional element of damages is available: "A person may recover reasonable attorney's fees from an individual or organization [including a corporation, limited or general partnership, limited liability company, joint venture, association, bank, insurance company, and many others] . . . in addition to the amount of a valid claim and costs, if the claim is for: (1) rendered services; (2) performed labor; (3) furnished material; . . . or (8) an oral or written contract. Texas Civ. Prac. & Rem. § 38.001 (2025). Is this a good idea? Texas is not the only state with such a provision.

Chapter 2. How to Study for the Exam

A. What Most Casebooks Assume: Contract Law Meta Rules

Most casebooks leave the large-scale structure of the law unstated. It is possible to pick it up from the reading (somewhat from a casebook's table of contents, for example), but that requires already integrated knowledge greater than most first-semester law students have developed. You can start on the road to integrating the law in a cohesive format by following the large-scale structure here.

These are contract law's meta rules. You should probably commit them to memory. They would make a great outline format. Everything we study can be nicely placed somewhere in this structure.

Contract Law Meta Rules

The purpose of contract law is, in no particular order, to (a) enlarge freedom and autonomy, (b) encourage (fair) exchange, (c) promote human flourishing by supporting and encouraging productive activity and moral human relationships.[†] In some fact patterns, these purposes conflict and courts must choose between them.

A *promise* is (a) a manifestation of intent to commit to a future act or refrain from some future act (b) made so as to justify the promisee's reasonable belief that a commitment has been made.

"A contract is a promise or set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty." Restatement (Second) of Contracts § 1 (Am. Law Inst. 1981).

The focus of contract doctrine is on the enforcement of a promise (the breached promise, in a breach case).

Prima facie in law means that a thing is legally effective unless shown otherwise.

The plaintiff in a breach case must show:

(i) contract,
(ii) breach, and
(iii) injury.

[†] There are about a million ways to say these things. "Fair" is in parentheses because some lawyers would define *fair* as whatever parties freely agreed to, within some boundaries.

I. Elements

The elements of a contract are:

(1) promise,
(2) consideration,
(3) assent,
(4) certainty or specificity, and
(5) capacity.

The plaintiff has the burden to allege facts and (later) prove facts showing the elements of a contract.

Consistent with the definition of promise above, generally “the law is concerned with the external manifestation rather than the undisclosed mental state . . . .” R2K § 71 cmt. b.

Facts proving the elements of a contract create a prima facie contract.

II. Defenses

If the plaintiff shows a prima facie contract, the defendant may defeat the plaintiff’s case by showing facts proving that:

(i) any element does not in fact exist (in which case the contract is *void*) (this is defense by denial),

(ii) any defense to formation (in which case the contract is *avoidable*) (these are affirmative defenses that must be alleged and proved by the defendant),

(iii) the contract is unenforceable under the Statute of Frauds (in which case the court will not enforce it) (the Statute of Frauds is also an affirmative defense but not a defense to formation),

(iv) the contract is unenforceable because it violates a significant public policy;

(v) the duty was modified (including by accord and satisfaction);

(vi) a condition of the duty failed;

(vii) a supervening event occurred that excuses non-performance;

(viii) that non-performance was waived; or

(ix) the statute of limitations has run.

Other defenses may exist, but these cover most cases.

Defenses to formation include

(a) duress,

(b) undue influence,

(c) mutual mistake,

(d) unilateral mistake,

(e) misrepresentation, and

(f) unconscionability.

The most common procedure for contract avoidance is rescission, which may be legal or equitable. In legal rescission, the promisor declares to the promisee that the contract is rescinded and returns or offers to return any benefit obtained from the contract; frequently, the promisor will then seek (in court, if necessary) a return of any benefit given to the promisee. In equitable rescission, the promisor will ask a court to declare the contract rescinded, offer to return any benefit obtained pursuant to the contract, and ask the court to order the return of any benefit conferred on the promisee.

III. Content

A contract comprises the promises, conditions, representations, and warranties of the parties' agreed exchange.

A condition is "an act or event, other than a lapse of time, that, unless the condition is excused, must occur before a duty to perform a contractual promise arises (condition precedent), or that discharges a duty of performance that has already arisen (condition subsequent)." JOSEPH M. PERILLO, CONTRACTS § 11.2 (7th ed. 2014).

IV. Discharge, Breach, and Excuse

A contract's promised performance—the promisor's duty—must be discharged, breached, or excused (those are all the logical & legal possibilities).

Performance of a duty discharges the duty.

The duty arising from a promise to perform is discharged by failure of a condition of that promise or duty.[†††]

[†††] Logically, failure of a condition precedent means that a promised duty is never arises and so is never due—the duty never has to be performed but remains contingent until the time for performance is past. Because the duty never arises, there is nothing to excuse, so in the case of a condition precedent, it

Failure to perform is a breach.

A condition may be:

(i) express (or possibly implied in fact by express terms); or

(ii) constructive (imposed by law).

Constructive conditions are created by courts in order to make exchanges of promises fairer and more efficient as contracts. Material breach is a failure of a constructive condition and discharges the other party's duty (or, it may be proper to say in some cases, excuses its non-performance).

Non-performance of a promised performance is excused by impracticability, the application of a force majeure clause, or frustration.

V. Remedy

The breaching party owes the non-breaching party a legal or equitable remedy.

"Legal" damages are the natural and proximate harm caused by the breach.

Legal damages are typically measured by a standard of expectation (both direct and consequential damages), reliance, or restitution. Which one the plaintiff asks for is an important factor in which the court awards. Breach of contract is a legal harm in itself, so, if no damages are shown but harm occurred, a court will award nominal damages (e.g., $1).

When legal measures are inadequate to make the non-breaching party whole, a court may order an equitable remedy, including a positive injunction (e.g., that the breaching party specifically perform the promise) or negative injunction (that the breaching party not breach or not do some other act).

VI. Alternative Theories

Two theories of liability exist under which promises can be enforced even though the plaintiff need not formally prove consideration. These theories are: (i) promissory estoppel and (ii) unjust enrichment.

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seems illogical to say the non-occurrence of a condition excuses non-performance of a duty. Instead, the duty which might have arisen is discharged. A failure of a condition subsequent would also discharge a duty but might logically also excuse non-performance.

B. What Is an Outline For, and How to Make One

By this point in your law school career, someone probably has mentioned outlining to you or perhaps even lectured about it. If they tried to tell you how to do it, they probably suggested that you use the table of contents of your casebook as a structure for it. This is usually good advice and what many professors tell students in other courses. However, it is not true in every course, and it is almost certainly not true in this Contracts course.

Rather than use the table of contents, you would be much better served by using the Contract Law Meta Rules as the backbone and structure of your outline. They are already in outline form! And the outline came from your casebook author. The Meta Rules also track the process of a promise through litigation, which is how contract law rules make the most logical sense. And the Meta Rules outline how courts themselves appear to structure contract law rules. You could simply fill in Meta Rules' categories with the rules you learn from the casebook. They will all fit into that structure.

What is an outline? Why do we do them? Basically, an outline is a study tool and an exam prep tool. It is preparation to do legal analysis of fact patterns *that you have never seen before*.

Doing legal analysis well requires you to do several things:

1) figure out what is "at issue" in the fact pattern;

2) state the rule that addresses that issue;

3) apply the rule to tell your audience (you, the prof, the bar examiner, the jury) how the facts in the pattern prove or disprove each element or factor in the rule; and

4) add any policy or jurisprudential argument that may persuade your audience.

The outline is to prepare you to do these things by helping you think carefully through the content of each rule, how each element or factor applies to fact patterns, and how the rules work together to resolve issues and reach results in cases you might see. In part, the outline serves this purpose because writing these things out and editing them as you go requires you to think through them carefully. In part, the outline serves this purpose (if done usefully) by forcing you to state the rules in a useful way, for example, in a list of legally operative elements or factors, with extraneous language omitted. Also, practicing writing law is useful because it is part of what you will do on the exam.

If your outline serves all those purposes, then it is available to you as the best resource you can use to practice applying the rules to every relevant fact pattern you can find. In Contracts, every case is about the enforcement of a promise, so you can potentially (and usually profitably) apply every rule in the book to every fact pattern in the book (these, after all, are fact patterns your prof can assume students know and understand, because the fact patterns were assigned in the reading, and we probably talked about them in class). You might also find other fact patterns by "riffing" on the fact patterns in the book—changing this or that fact a bit until the result changes; the more intimately you study the materials in this way, the more familiar you will become with the limits of the rules we study. At the very least, try to apply each rule three

or more times. You have to understand when and why each element or factor of each rule applies or not, and practicing is the only way to gain this understanding.

So that is what an outline is, and how to make one. But the method for outlining is not set in stone. Your casebook author's own outlines looked a lot like the Meta Rules filled in with details and examples of their application (including long-form essay questions generated by pretending that the cases in the casebook were test questions that application of the rules). But not everyone writes outlines that way. Your author had a friend in law school who was an engineer (B.S., M.S., Ph.D.), and his outlines were typically 6-foot by 3-foot rolls of paper on which he had crafted flow charts. To many, they looked like cuneiform, but he was an excellent student, and his thoughtful outlining and study earned him high grades. No one knows your study skills and strengths better than you do, so do what works for you. But you should know what avenues are available as study methods, and, whatever you do, you must spend a great deal of time integrating what we learn in class until you can use it like a lawyer would. If you leave class and forget what you studied until you cram for the exam, you will not do well at all and may not pass.

Here is some advice now about what to do and what not to do:

> 1) Law is words, so the legally operative words that you include in your outline's rule statements—the words you claim are dictating the results of cases—should come directly from real sources of law: statutes, cases you are assigned, regulations;
>
> 2) Related to (1), don't paraphrase. Law is words, but not your words (unless you are a court of last resort, or next-to-last resort and not reversed);
>
> 3) If you obtain the words you write as law from a source other than your casebook (this book) or what the casebook or your professor tells you is an acceptable statement, you run the risk of using words that are not law. Your professors have seen this happen hundreds of times over the years. Literally anything can be incorrect. Or it might be correct but not relevant; you might think it is relevant and correct but you misunderstand it and it's not. Incorrect or irrelevant and misunderstood contract law words can come from any outside source, including R2K, Westlaw outlines, a commercial outline, a commercial brief, another student or former student's outline, anything online.

Finally, please note: Many law students are so afraid they will see a question and not know how to answer it that they create a template or plan in advance for answering any question. The template has to be pretty comprehensive because the questions on the exam could be about anything. The template might even look something like the Meta Rules, and typically the student will memorize it. The template makes the student feel safer. Having prepared such a template or plan the first thing the student may think of doing when they read a question is using their template or plan. (Having sunk all that energy into creating a fallback that they feel confident in, they retreat to safety (and to a person with a hammer, everything looks like a nail).) But—this is a mistake. There never has been a fact pattern in the history of contract law that raised every question in the Meta Rules or in any template you could create. You will get no points for discussing irrelevant issues in your essays, and making your prof read irrelevant discussion wastes your professor's time and makes the professor want to impose a word limit on your answers. You are to look at the fact pattern and determine which parts of contract law are relevant to the call of the question and only talk about those. If you want a strategy, you could start by naming and analyzing the issues you know are relevant and work out to the less relevant issues until you run out of time.

That's all for now.

C. Fact Patterns and Basic Legal Applications in Common Contracts

In this class and throughout law school, you will examine many different kinds of contractual transactions. They are all governed by the Meta Rules described in Section A. Most are also governed by the more specific common law of contracts rules described in this book. You should learn the basics of these transactions, mostly for two reasons: (i) Some kinds of contracts are so common that all lawyers are assumed to understand them, at least in their basic, standard form. Your fellow lawyers, the courts, the bar examiners, and your clients will expect you to know at least the types of transactions described here. (ii) You will understand the law much better if you know what is happening economically and formally in these facts patterns.

The following discussions uses certain law-talk conventions. For instance, real property being sold is traditionally known as Blackacre (or Greenacre, etc.) even though it is not a single acre but a parcel of uncertain size. Also, the parties and parts of these transactions are often called specific names.

How many of these have you actually participated in?

1. The Contract for Real Property

Alma wanted to sell Blackacre, which she had owned for 20 years. Ben wanted to buy Blackacre. Alma and Ben negotiated a price for Blackacre of $400,000. Alma and Ben signed a contract in which Alma promised to convey to Ben and Ben promised to buy Blackacre for $400,000. A contract formed at this time.

The contract's terms were these: Alma promised to convey Blackacre to Ben in fee simple absolute by warranty deed (this is a complete conveyance of all Alma's interest and it also promises that Ben will after the transaction own the property as completely as the law allows). Ben's duty is conditional on Ben's obtaining a loan of $360,000 within one month of the date of contract formation. Ben's duty to buy is also conditional on Ben's ability to obtain title insurance (which is a promise by a title insurance company that it will reimburse Ben for his losses if he does not own the property in "fee simple" (as completely as the law allows) after this transaction).

After contract formation, Alma and Ben prepare to perform their promises. Alma has a deed prepared. Ben applies for the loan and obtains it. Ben also applies for title insurance and obtains a commitment of title insurance for the property.

The contract does not specify who should perform first (kind of like the contract in *Nicholas v. Raynbred*). Both parties would have some natural hesitancy to perform first because Alma does not want to part with the property until she has the money and Ben does not want to part with the money until he has the property.

To overcome the parties' natural hesitancy and make the transaction secure, the two parties make a contract with a third party, called an "escrow." The word "escrow" is the title of a person performing a function and also refers to a fictitious location possessed by the escrow, so we say a thing is delivered to the escrow and also deposited "in escrow." *Escrow* is a funny word, and sometimes people call the escrow an "escrow agent," but the escrow is not an agent of anyone, so that is technically incorrect. The escrow is simply a party to an escrow contract with Alma and Ben. The escrow receives the parties' performances and holds them until everyone is ready to perform.

The escrow will, pursuant to the parties' instructions, examine the contract and make sure everyone's performance is ready before releasing that performance/s to the other party. For instance, Alma will deposit the deed in escrow. Ben and Ben's lender will deposit the money in escrow, and Ben's lender will probably take an interest in the property as collateral for the loan, so a deed of trust in favor of the lender will also be deposited in escrow for Ben's signature, at the time the lender sends the money. The escrow will also certify that Ben has title insurance. In a successful transaction, the escrow will certify that every other condition has been met and that every promise will be performed (this might include payment of a transaction tax, payment of realtors, payment to the escrow for the escrow service, etc.).

When every performance is ready, the parties perform the contract, an event called "closing." At the closing, Alma and Ben must sign all required documents and sign off that everything is prepared and ready, and they must authorize the escrow to close. Ben's lender will also sign off, as will any other interested party. Once all the signatures are obtained, the escrow closes the transaction by sending the money to the account of Alma and the deed to Ben or Ben's lender (probably the lender, who will hold it until Ben has paid off the loan). The contract has then been performed and is at an end.

The property is now Ben's to use and enjoy. After the contract is performed, Ben or Ben's lender or the escrow or the title company, as the parties designate, will take the deed to the local government records office to be recorded publicly. This helps Ben's title to be secure.

The formation of a contract to convey real estate gives the buyer significant rights. Because land is unique, legal damages for the seller's breach will always be inadequate to remedy the harm to the buyer, so the law provides the buyer a right to the seller's specific performance—the buyer can take the property itself. Thus, from the moment of formation, the buyer has an equitable interest in the property. In many states, this equitable interest can be recorded in local property records and will cloud the seller's title until the contract is performed.

2. The Lease

Our vocabulary here is *lessor* or *landlord*, the property owner who leases land to another, and *lessee* or *tenant*, the person who takes possession and pays rent. A lessee who rents the leased land to another is called a *sublessor* or *sublandlord*, and the sublessor's lessee is called *sublessee* or *subtenant*. The property

subject to the lease is called the *leasehold*, and the lessee's interest in the property is called the *leasehold* or *leasehold estate.*

The lease has been treated under the common law as both a transfer of an interest in real property (the older view) and a contract (the newer view). Lease cases over the last 150 years in particular show this shift, but even 450 years ago you can see it. The lease remains a transfer of an interest in land, however, because it gives the lessee the right to exclude even the lessor. A transfer of the use of land that did not include the right to exclude the lessee would probably be called simply a *contract* or perhaps a *license*. The lease's status as a real property transfer is thus ultimately inescapable, perhaps.

The transaction begins when Carrie and David negotiate a lease to David of Greenacre, which is owned by Carrie. In its basic form, the lease has two terms: length and rent. A lease it typically for a term of years or months, or it might be month-to-month and of indefinite duration. Rent can be anything Carrie and David agree. Typical terms for a residential lease include a flat monthly amount, with escalations over time if the lease lasts years. A commercial lease might have complex rent provisions, including a set amount per month and also a share of the lessee's revenue.

The lease might also allocate duties for various things between landlord and tenant. For instance, in a lease of land for a mobile home, the lessor might covenant to maintain common areas in the mobile home park, water to the property line, and a fence around the park. The tenant might covenant to keep the lot tidy and the home painted and refrain from loud noises at night. In a long-term lease of commercial space next to other areas the lessor owns, such as inside a shopping mall, the lease will typically allocate duties to maintain the parking lot, the HVAC system, the interior trade dress, the mall's outside signage, and a host of other things. Lawyers typically negotiate mall leases on behalf of lessors and significant lessees.

In the lease, performance begins immediately on formation. The lease itself is the instrument that conveys to the lessee a leasehold estate—an interest in real property; so, the lessee typically has a right to possession immediately after a lease "contract" forms.

Performance of the lease requires the lessor to allow the lessee possession and use of the property and requires the lessee to pay rent. Of course, the parties must perform the other promises they have made in the lease, too. Once the term of the lease ends and the last rent is paid (and any other promises performed), the lease is at an end.

3. Employment At Will

A person who employs another is an *employer*. A person who is employed by another is an *employee*, of course.

The key feature of most employment contracts is that, by default, employment is "at will." Here is how one recent decision quite typically described at-will employment:

> Employment in Texas is presumed to be at-will. *Montgomery Cnty. Hosp. Dist. v. Brown*, 965 S.W.2d 501, 502–03 (Tex.1998) . . . . "[A]bsent a specific agreement to the contrary,

> employment may be terminated by the employer or the employee at will for good cause, bad cause, or no cause at all." *Brown*, 965 S.W.2d at 502. To alter the at-will employment status, "the employer must unequivocally indicate a definite intent to be bound not to terminate the employee except under clearly specified circumstances." *Id.* In that connection, any such agreement must provide in a "special and meaningful way" that the employer does not have the right to terminate the employee's employment at will. It is the employee's burden to prove that the employer expressly, clearly, and specifically agreed to modify the employee's at-will employment status.

Queen v. RBG USA, Inc., 495 S.W.3d 316, 325 (Tex. App.—Houston 2016, pet. denied) (omitting citations except to *Brown*).

The promise of employment or work may therefore be terminated at any moment. In other words, employer and employee typically do not actually promise each other any future employment and work or, if they do, it is not much of a promise (and courts sometimes call promises of at-will employment illusory, for that reason). A contract for a specific term of employment will overcome the at-will presumption. For example, tenured faculty typically work on written, one-year terms of employment that are presumptively renewable. Officers of large companies also often work for a term. For the most part, associates at law firms are at will.

What the employer does promise (and this is backed up by federal wage laws) is that if you work while you have the job, you will be paid as promised. Many courts see the employment contract as a trade of this promise for the actual detriment of working, similar to *Webb's Case*.

Employment need not include any other promise than pay. However, it often includes other promises, such as health insurance, paid sick days, bonuses, retirement benefits of some sort, and so on. The employee may also make specific promises but typically promises only to work at will. For instance, some people believe that an employee should give a two-week notice before quitting, but no contract requires this by default—it just seems polite. Plenty of Walmart night stockers simply stop showing up for work, and they have not breached a contract.

As with most things in the law, at-will has some exceptions. Some courts hold that laws other than bargained-for contract, such as promissory estoppel, give employees some rights. The law also provides that at-will employment does not allow an employer to terminate employment in violation of express law (e.g., because of illegal discrimination) or strong public policy (such as for attending to jury duty). The contours of these exceptions to at will employment differ from state to state.

Another significant intrusion on at-will employment is created by collective bargaining agreements. Employment security of some sort is typically a goal of union negotiations with employers, so collective bargaining agreements that dictate employment terms between employers and employees in unionized employment places often limit at-will employment.

A side note: Sometimes people hear the phrase "right to work state" and assume it has something to do with at-will employment. Perhaps it means that employment is not at will! Actually, so-called "right to work" laws guarantee a worker's right not to be a member of a union even though the workplace is unionized. This significantly weakens union power in states with right-to-work laws. Without these laws, every employee of a unionized place of work (even the baggers at Kroger) would be forced to pay union dues out of each paycheck. But "right-to-work" means nothing more than this, and it does not guarantee employment

or dictate terms of any employment contract. Right-to-work laws thus do not formally have any effect on at-will employment.

4. Contract for Services

Not all services are considered employment. Sometime one person hires another to do something for a price. For instance, a property owner hires a contractor to build, repair, or remodel something. A client hires a lawyer to represent her in a dispute. A sick person hires a doctor to treat and hopefully heal the sick person. A business hires a consultant to do some specific task. A person needing a ride somewhere hires an Uber driver to provide it. You want a happy meal without going to McDonald's, so you hire DoorDash to bring it to you. Many millions of people make a living working "for themselves" by working for everyone who wants to hire them.

The transactional form for this sort of thing can be extremely simple or extremely complicated, depending on the service and its customs.

Uber. For instance, if you sign on to Uber's terms, you (probably) have entered into a contract with Uber, and that contract will dictate when you owe money for an individual trip you order. That contract can in some circumstances make you liable for cancellation fees for rides never taken, so an Uber user would be wise to know the rules very well. A contract between the user and the Uber driver also certainly forms by the time the car starts moving, but both rider and driver are already bound by Uber's terms, and those terms probably dictate how and when money is paid to the driver (and to Uber). See how complicated?

Lawyer. A lawyer may bill a client by the hour for time worked, in a very simple arrangement. A lawyer might also bill for a job done for a flat fee, in another simple arrangement. If the lawyer is worried about being paid, the lawyer might take a retainer from the client, put the money in the lawyer's trust account, and take payment from the retainer in the trust account as the lawyer earns the money. The lawyer might alternatively agree to take a fee only from a damage award or settlement of any money obtained by the client in a dispute. This is known as a contingency fee. The contract forms when the client hires the lawyer and the lawyer agrees to serve. Ethical rules require that a fee be reasonable, and putting it in writing to prevent misunderstandings later is an excellent practice.

Building contractor. Contractors for building, repair, and remodel can follow the simple model of the lawyer or be much more complicated. For the homeowner hiring an electrician to fix or repair some outlets, a simple agreement to pay and be paid for work done (often with an estimate of charges) creates a contract when the work starts. The contractor's doing the work and the owner's paying the contractor completes the transaction.

At the other end of the complication spectrum, large construction jobs are often not completed by a single person or business. Instead, an owner will hire a "general contractor" who will (i) hire many other "subcontractors" to do different parts of the work and (ii) manage the process so that a building gets built. For example, a general contractor for a home build will generally hire a plumber, a foundation pourer, a framer, and electrician, a roofer, and finish workers to put in the walls, texture, and paint. This is complicated

work and can take months. The owner will make a contract only with the general contractor, and the general contractor will make a separate contract with each individual subcontractor.

In the largest jobs, owners want competitive bidding, so they will ask general contractors to submit bids for the job. The owner is seeking the lowest bid from a general contractor who will do the job well. General contractors in creating their own bids also want to obtain the most competitive subcontract work, so they will similarly ask subcontractors to submit subcontract bids for parts of the job, and the general will create the general bid partly in reliance on the bids they receive from subcontractors. Obtaining bids from subcontractors and creating a general contractor bid can be complicated work, and managing the activities of numerous subcontractors through a large job is also complicated. Many universities offer degrees in construction management and the like to train people to do this work.

In such a large job, the contract between owner and general contractor to build the building does not form until after the general contractor wins the bid, negotiations settle on a final price and the job's specifications, and the general contractor and owner sign an actual general contract. Usually, the contract they sign is a contract form provided by the American Institute of Architects (AIA), a trade organization for people involved in overseeing big construction work. After the general has a contract with the owner, the general contractor will then negotiate and obtain contracts with subcontractors who will do the work—often the subcontractors whose bids the general contractor relied on to create its bid to the owner. On large jobs, the general and subcontractors, too, sign AIA form contracts between themselves.

Then the work of construction begins. Large jobs often come with payment schedules. These allow the general to pay subcontractors when individual subcontractors finish their work (the foundation company should not have to wait for the roofer to finish). Typically, an owner will hold back a certain percentage of the general's compensation until the work is accepted by the owner's architect and the owner itself. What sort of contract term would enable this to happen?

In its more complicated form, construction law is its own legal specialty and includes several other areas of law, including bonding, insurance, lien law, and business entity law.

5. A Loan

Lenders lend money. Borrowers borrow money and promise to pay it back. The debt contract can be mutual promises (to lend and repay) or a promise (to repay) for a performance (the lending).

Straightforward, unadorned, unsecured lending is a simple contract that we do not need to discuss much. It includes revolving credit arrangements such as you might have with a credit card company.

But most lending is "secured." That means that the borrower puts up collateral for the loan, and if the borrower does not repay, the lender can take or keep the collateral. The putting up of collateral, and the lender's taking a property or contractual interest in it, usually occur at the time the loan is made.

Mostly, we will not study the taking of collateral and the collection of it. That is the subject of other classes. If the collateral is real property, then you will learn about it Property, which should cover mortgages and

deeds of trust, instruments that grant lenders rights to collect real property on non-payment. If the collateral is personal property, then you will learn about it in a class called Secured Transactions, an elective course that you can take later. The law studied in Secured Transactions is contained mostly in Article 9 of the Uniform Commercial Code. Article 9 is a thing of beauty, carefully designed to resolve all the common problems lenders and borrowers have with regard to all personal property collateral. If you plan to handle business transactions as a lawyer, Secured Transactions should be high on your list of courses to take.

6. A Guarantee

A guarantee is a promise by someone to pay the debt of another if the other defaults. A *guarantor* is the person who promises to pay the debt if the debtor defaults. The guarantor usually promises this to the lender (unlike in *Edmonds Case* or *Hunt v. Bate I* where the guarantor promised the debtor or some third party).

What is consideration for the guarantee, do you suppose? The promisor does not get any obvious benefit.

7. Sale of Goods

A sale of goods involves a buyer and a seller. Goods are defined in the Uniform Commercial Code as “all things . . . which are movable at the time of identification to the contract for sale other than the money in which the price is to be paid, investment securities (Article 8) and things in action.” UCC § 2-105(1). Basically, most items of personal property are goods.

Sales of goods are like many other contracts: when buyer and seller agree to exchange, a contract forms that is performed when the seller delivers and the buyer pays. But commerce moves very quickly, and business people do not always communicate well. Moreover, statutes have governed this area for a long time. The 1906 Uniform Sales Act was an attempt to get state legislatures to standardize sales of goods law across the country. It was adopted in 34 states. Article 2 of the Uniform Commercial Code was drafted in the 1940s and 50s, but from 1960 through 1990 it was adopted (with small variations) by every state except Louisiana. This gave us a mostly uniform sales law in the United States.

Article 2 provides many default terms for sales of goods transactions. For instance, it provides who should perform first if the parties do not say, what “F.O.B.” means, who bears the risk of loss when goods are lost in shipping, whether a contract can form even though the parties do not agree on price (yes, it can), whether goods come by default with warrantees (yes), and whether those warrantees can be disclaimed (mostly yes). There are many other provisions special to sales of good. We are not going to study them in depth, but many of them are tested on the bar, so the materials will introduce you to many of them, and if you are particularly worried about them, please take a course in Sales.

Article 2 does not mandate that sales of goods require consideration. Why do you suppose that is?

8. License

Someone who legally controls access to, or use of, some thing or some right can grant permission to that access or use to another. For instance, a creator of software has ownership as its creator, as controller of access to it, and through intellectual property rights. Software is often licensed to another to use. The apps on your phone are licensed to the phone user.

A great deal of intellectual property is licensed: musical and theater compositions are licensed for performances; recordings are licensed for play in movies, TV shows, on the radio, and in restaurants; attendance at an entertainment event is often a license (usually embodied in a ticket).

Other things are licensed, too. An airline boarding pass is a license to board a plane for a flight. Airport parking lots sell a license to park. Allowing someone to use your car is a kind of license to use the car. All of these can be governed by contract, meaning the license can be a contract right, and many of them are also subject to government regulation.

Sometimes the government controls access and itself grants a license, for example, to marriage, operation of certain trades or professions (the practice of law, medicine, dentistry, optometry, auctioneering, cosmetology, and charitable bingo), operation of a business, driving a vehicle. These licenses are not contractual but are governed by statute and regulation.

Chapter 3. Consideration and Modification of a Pre-existing Duty

If a contract forms, then the promisor has a duty to perform. If the parties try to modify the contract by changing only the promisor's promise, is there consideration for that new promise? The other party's duties or performance remain unchanged; any duty the other party had is a pre-existing duty. Think back to *Abe v. Juanita* and *Hildegard v. Grace, Executor for Michael*. A person cannot bargain to do what they already have a duty to do. So is the modification enforceable? This question has troubled courts, as you'll see here. The drafters of UCC Article 2 decided to toss the whole problem by declaring, "[A]n agreement modifying a contract within this Article needs no consideration to be binding." UCC § 2-209. But that's only for sales of goods.

The law is also nuanced by the presence of two doctrines that can justify enforcing changes to contracts: modification and waiver.

A. Modification

1. Modification of Judgment Liabilities

You begin studying modifications with *Reynolds v. Pinhowe* and *Foakes v. Beer* because these cases show the legal issue that arises when the parties to a contract modify one parties' (A's) duties but not the other's (B's). A doesn't bargain for what B already has a duty to do—remember *Hildegard v. Michael*, Problem 5? So promises made by A with respect to the modification (i.e., I'll pay you the same, or more (even though you are doing what the contract or some other duty already requires you to do)) are not binding. Yet in many of these cases, such promises serve a public-policy-wise purpose, and perhaps a commercial purpose, and policy or theoretical reasons for enforcing them exist. What to do?

REYNOLDS v. PINHOWE

Queen's Bench (1594)

Cro. Eliz. 429, 78 ER 669

Assumpsit. [Most disputed lawsuits end with a "judgment," a document signed by a judge dismissing the suit or directing the defendant to do something such as pay money. After the court issues a judgment that a defendant pay money to a winning plaintiff, then, if the defendant refuses to pay, the plaintiff must initiate collection procedures, which are sort of separate from and collateral to the lawsuit that resulted in the judgment. In *Reynolds*, the defendant obtained a judgment for five pounds against the plaintiff in a prior lawsuit: The defendant in *Reynolds* was a winning *plaintiff* in a prior suit. Apparently, the plaintiff could not pay the five pounds, but the plaintiff and defendant reached an agreement, a settlement. They agreed that the plaintiff would give the defendant four pounds and, defendant promised, defendant would give the plaintiff a paper acknowledging that the judgment was satisfied. Plaintiff gave the defendant the four pounds pursuant to the agreement, but the defendant never produced the "satisfaction of judgment" document so that plaintiff could file it with the court. So, plaintiff sued the defendant for breach of promise. When plaintiff pleaded in assumpsit, plaintiff alleged that defendant had promised the document "in consideration of four pounds given" defendant by the plaintiff. But the four pounds was not given in consideration of defendant's promise! Why not? This is the argument defendant made in court. Amazingly, the court rejected the argument. Here is what Croke (pronounced "Crooke") reported, translated from law French:]

—But all the Court held it to be well enough; for it was a benefit unto him to have it without suit or charge: and it may be there was error in the record, so as the party might have avoided it. Wherefore it was adjudged for the plaintiff.

[Moore 412, 72 ER 663, offered a slightly different take:]

... But it was adjudged good, because speedy payment excuses & prevents travail & expense of suit.

Question: Is that consideration, really?

John Weston FOAKES v. Julia BEER

House of Lords (1884)

9 App. Cas. 605

[¶1] * * * * On the 11th of August 1875 [Beer] [obtained a] judgment against [Foakes] for £2077 17s. 2d. for [a] debt and £13 1s. 10d. for costs. On the 21st of December 1876 a memorandum of agreement was made and signed by [Foakes] and [Beer in which Foakes agreed to pay Beer £500 immediately and the remainder of the judgment principal in installments. In consideration of Foakes's making these payments, Beer agreed to forego interest on the judgment debt, to which she was otherwise entitled. Foakes paid the principal in full according to the agreement, but then Beer tried to initiate collection efforts for the interest. The trial judge refused to allow her to proceed. The initial appellate court to hear the matter affirmed, but the Court of Appeal reversed and entered judgment for Beer. Foakes then appealed to the House of Lords.]

[Holl, counsel for Foakes:]

[¶2] * * * * [T]here is no reason in sense or law why the agreement should not be valid, and the creditor prevented from enforcing his judgment if the agreement be performed. It may often be much more advantageous to the creditor to obtain immediate payment of part of his debt than to wait to enforce payment, or perhaps by pressing his debtor to force him into bankruptcy with the result of only a small dividend. Moreover, if a composition is accepted friends, who would not otherwise do so, may be willing to come forward to assist the debtor. And if the creditor thinks that the acceptance of part is for his benefit who is to say it is not? * * * * *Reynolds v. Pinhowe* * * * * decided that the saving of trouble was a sufficient consideration; "for it is a benefit unto him to have his debt without suit or charge." * * * * *Pinnel's Case* was decided on a point of pleading: the dictum that payment of a small sum was no satisfaction of a larger, was extra-judicial, and overlooked all considerations of mercantile convenience, such as mentioned in *Reynolds v. Pinhowe* * * * *. It is every day practice for tradesmen to take less in satisfaction of a larger sum, and give discount, where there is neither custom nor right to take credit. * * * * Mankind have never acted on the doctrine of [*Pinnel's Case*], but the contrary; nay few are aware of it. By overruling it the House will only declare the universal practice to be good law as well as good sense.

[¶3] [Earl of Selborne, L.C.:-Whatever may be the ultimate decision of this appeal the House is much indebted to Mr. Holl for his exceedingly able argument.]

* * * *

[¶4] Bompas Q.C. (Gaskell with him) for [Beer]:-

[¶5] * * * * There is a strong current of authority that what the law implies as a duty is no consideration. Therefore where a debt is due part payment is no reason for giving up the residue. The doctrine is too well settled to be now overthrown: see a long list of authorities * * * *. * * * * It is contrary to public policy to make the performance of a legal duty a good consideration; see the cases on seamen's wages * * *. Where law and practice are so well established this House will not now depart from them * * * *. * * * *

Earl of Selborne, L.C.:- * * * *

[¶6] * * * * The doctrine [of *Pinnel's Case*] itself, as laid down by Sir Edward Coke, may have been criticised, as questionable in principle, by some persons whose opinions are entitled to respect, but it has never been judicially overruled; on the contrary I think it has always, since the sixteenth century, been accepted as law. If so, I cannot think that your Lordships would do right, if you were now to reverse, as erroneous, a judgment of the Court of Appeal, proceeding upon a doctrine which has been accepted as part of the law of England for 280 years.

[¶7] The doctrine, as stated in *Pinnel's Case*, is "that payment of a lesser sum on the day" (it would of course be the same after the day), "in satisfaction of a greater, cannot be any satisfaction for the whole, because it appears to the Judges, that by no possibility a lesser sum can be satisfaction to the plaintiff for a greater sum." * * * *

[¶8] If the question be (as, in the actual state of the law, I think it is), whether consideration is, or is not, given in a case of this kind, by the debtor who pays down part of the debt presently due from him, for a promise by the creditor to relinquish, after certain further payments on account, the residue of the debt, I cannot say that I think consideration is given, in the sense in which I have always understood that word as used in our law. It might be (and indeed I think it would be) an improvement in our law, if a release or acquittance of the whole debt, on payment of any sum which the creditor might be content to receive * * * * (though less than the whole), were held to be, generally, binding, though not under seal; nor should I be unwilling to see equal force given to a prospective agreement, like the present, in writing though not under seal; but I think it impossible, without refinements which practically alter the sense of the word, to treat such a release or acquittance as supported by any new consideration proceeding from the debtor. * * * *

Lord Blackburn:- * * * *

[¶9] * * * * Lord Coke reports * * * * [in *Pinnel's Case*] "that payment of a lesser sum on the day in satisfaction of a greater cannot be any satisfaction for the whole, because it appears to the judges that by no possibility a lesser sum can be a satisfaction to the plaintiff for a greater sum: but the gift of a horse, hawk, or robe, &c., in satisfaction is good, for it shall be intended that a horse, hawk, or robe, &c., might be more beneficial to the plaintiff than the money, in respect of some circumstance, or otherwise the plaintiff would not have accepted of it in satisfaction. But when the whole sum is due, by no intendment the acceptance of parcel can be a satisfaction to the plaintiff; but in the case at bar it was resolved that the payment and acceptance of parcel before the day in satisfaction of the whole would be a good satisfaction in regard of circumstance of time; for peradventure parcel of it before the day would be more beneficial to him than the whole at the day, and the value of the satisfaction is not material; so if I am bound in £20 to pay you £10 at Westminster, and you request me to pay you £5 at the day at York, and you will accept it in full satisfaction for the whole £10, it is a good satisfaction for the whole, for the expenses to pay it at York is sufficient satisfaction."

[¶10] * * * * What principally weighs with me in thinking that Lord Coke made a mistake of fact [as to what the Judges in *Pinnel's Case* decided] is my conviction that all men of business, whether merchants or tradesmen, do every day recognise and act on the ground that prompt payment of a part of their demand may be more beneficial to them than it would be to insist on their rights and enforce payment of the whole. Even where the debtor is perfectly solvent, and sure to pay at last, this often is so. Where the credit of the debtor is doubtful it must be more so. I had persuaded myself that there was no such long-continued action on this dictum as to render it improper in this House to reconsider the question. I had written my reasons

for so thinking; but as they were not satisfactory to the other noble and learned Lords who heard the case, I do not now repeat them nor persist in them.

[¶11] I assent to the judgment proposed, though it is not that which I had originally thought proper.

[¶12] [Lord Watson and Lord Fitzgerald also voted to affirm, in opinions here omitted.]

Questions:

1. Review Reynolds v. Pinhowe. Can you distinguish Foakes from Reynolds factually, or are they legally the same?

2. Suppose Foakes had complied with the agreement and also given Beer a horse. Would she be bound?

3. Why would a hawk or robe, if given by Foakes, have bound Beer, when payment of part of the money owed would not?

4. Why would payment prior to the due date have been sufficient consideration when payment of part on the due date would not?

5. Why should Foakes be overruled? (You can collect several arguments from this case. Please list and be prepared to discuss them.)

6. Why should Foakes be retained as law? (Again, please look to the case first.)

7. You might compare Foakes with the settlement cases in Chapter 1. Why isn't Foakes a settlement case?

SUGARHOUSE FINANCE COMPANY v. Eugene L. ANDERSON and Colleen W. Anderson

Supreme Court of Utah (1980)

610 P.2d 1369

HALL, Justice:

[¶1] Plaintiff Sugarhouse Finance Company appeals the lower court's grant of a motion made by defendant Eugene L. Anderson for an order enforcing the terms of an agreement in settlement of a judgment held against him.

[¶2] On July 7, 1976, plaintiff filed a complaint against defendant for nonpayment of a promissory note. Judgment thereon was rendered in favor of plaintiff on December 17, 1976, in the amount of $2,423.86, plus interest, costs, and attorneys' fees. A copy of the judgment was docketed by plaintiff in Sevier County, defendant's county of residence.

[¶3] Some two years later, on January 29, 1979, plaintiff served defendant with an Order in Supplemental Proceedings, apparently due to the latter's failure during the interim to satisfy the judgment. Two days after receiving this notice, defendant met with plaintiff's president, Mr. Neuman Petty, for the purpose of discussing an alternative to full payment of the judgment. While reports conflict as to the exact content of that conversation, it is clear the defendant informed plaintiff of the existence of numerous outstanding obligations against him, including medical expenses incurred pursuant to treatment for injuries sustained in an automobile accident in 1978. Defendant initially proposed that plaintiff accept $1,500 in full settlement of the claim, which proposal was refused. Defendant then asserted that he was contemplating bankruptcy, and that such a measure would result in plaintiff's judgment being discharged. The parties finally settled on a figure of $2,200 in full satisfaction of the claim. Defendant issued Petty a check for this amount, asking him, however, not to negotiate it immediately, there being some uncertainty as to the sufficiency of funds in the account to cover it. At no time during the conversation did defendant represent to Petty that defendant had any ownership interest in real property, nor did Petty make inquiry in that regard.

[¶4] The day following these negotiations, plaintiff received a telephone call from a title company. Plaintiff learned from that call, allegedly for the first time, that defendant owned part interest in a 12-acre tract in Sevier County, Utah, four acres of which were the subject of a pending sale. The property was owned jointly with another party, and was otherwise encumbered, such that defendant hoped to receive no more than $2,000 from the transaction. The title company had telephoned to request that plaintiff file a satisfaction of judgment in order to clear title to the property in question; plaintiff refused the request.

[¶5] The next day, the defendant called to inform plaintiff that there were then sufficient funds in the account to cover the previously issued check. Plaintiff responded by indicating that it did not intend on going through with the settlement based on what it had learned from the title company. The check was subsequently returned to defendant.

[¶6] Defendant thereafter filed a motion in the original action, asking that the court order plaintiff to comply with the terms of the agreement of settlement. Hearing on the motion was convened on March 13, 1979, at the conclusion of which the motion was granted and the plaintiff was ordered upon receipt of the $2,200 payment, to file a satisfaction of judgment with the court. It is from this order that plaintiff appeals.

[¶7] Plaintiff first challenges the procedural propriety of defendant's petition for judicial redress by means of a motion in the initial action. Under plaintiff's view, defendant should be constrained to raise the alleged accord and satisfaction only as an affirmative defense to further attempts by the plaintiff to enforce the terms of the original promissory note. This contention is in error. * * * *

[¶8] Plaintiff next challenges the validity of the accord allegedly reached between the parties on the basis of adequacy of consideration. Plaintiff points out that, as defendant sought a substitute settlement of an undisputed and liquidated claim, separate and additional consideration was required to support the accord. It is plaintiff's position that no such consideration existed in the present case.

[¶9] Accord and satisfaction arises where the parties to an agreement resolve that a given performance by one party thereto, offered in substitution of the performance originally agreed upon, will discharge the obligation created under the original agreement. Essential to its validity are, (1) a proper subject matter; (2) competent parties; (3) an assent or meeting of the minds of the parties; and (4) a consideration given for the accord. Where the underlying claim is disputed or uncertain ("unliquidated"), the obligor's assent to the definite statement of performance in the accord amounts to sufficient consideration, as it constitutes a surrender of the right to dispute the initial obligation. Where, however, the underlying claim is liquidated and certain as to amount, separate consideration must be found to support the accord; otherwise, the obligor binds himself to do nothing he was not already obligated to do, and the obligee's promise to accept a substitute performance is unenforceable. The original obligation in the present case being of a definite and undisputed amount, the question presented is whether or not separate consideration was given to support the accord reached by the parties.

[¶10] No completely satisfactory and comprehensive definition of "consideration" has ever been devised. It is generally agreed, however, that where a promise is supported by the incurrence, on the part of the promisee, of a legal detriment in order to confer a benefit on the promisor, such is sufficient to serve as consideration, thereby rendering the promise legally enforceable. This is particularly so when an accord and satisfaction is involved, the modern trend among the courts being to uphold such agreements wherever possible. In such cases, consideration is often found in the obligor's agreement to alter the means or method of payment of the obligation initially owed, or to surrender the assertion of a legally enforceable right.

[¶11] It is to be noted that, in the present case, plaintiff held a judgment which had been outstanding for more than two years. Pursuant to the parties' conversation of January 31, 1979, defendant agreed that, for a release of the judgment upon payment of a lesser agreed amount, he would negotiate a loan with a third party to enable him to pay off the substitute obligation immediately. A check was given for the agreed amount at the conclusion of that conversation, and authorization to cash it followed two days later. In effect, defendant had agreed to transfer the debt represented by plaintiff's judgment to a third party, thereby immediately satisfying the obligation owed to plaintiff. This was something defendant had no legal obligation to do; by law, plaintiff could only move by levy of execution against property already owned by the defendant—plaintiff could not legally require defendant to incur additional obligations to satisfy the judgment. By so doing, defendant deliberately incurred the detriment of surrendering his right to limit plaintiff's ability to obtain satisfaction of the underlying judgment, and bestowed upon plaintiff the benefit of immediate payment by means of the incurrence of additional indebtedness. We hold such action to constitute sufficient consideration to support the accord negotiated by the parties.

[¶12] We note, in addition, that this jurisdiction recognizes the doctrine of promissory estoppel, whereby an individual who has made a promise which the individual should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce such action or forbearance is estopped to deny or repudiate the promise should the promisee or some third party suffer detriment thereby. We note that, in the present case, defendant agreed to incur additional indebtedness pursuant to the terms of the accord, in reliance on plaintiff's promise to accept immediate payment of a lesser amount in full satisfaction of the underlying obligation. As such, plaintiff should now be estopped to deny or reject the promise made.

[¶13] The trial court's decision is hereby affirmed. Costs to defendant.

CROCKETT, C. J., and MAUGHAN, WILKINS and STEWART, JJ., concur.

Question: What other acts in reliance by a debtor would have the same effect as Anderson's borrowing money?

2. Modification of Contractual Liabilities

ALASKA PACKERS' ASS'N v. DOMENICO

Circuit Court of Appeals, Ninth Circuit (1902)

117 F. 99

ROSS, Circuit Judge.

[¶1] The libel in this case was based upon a contract alleged to have been entered into between the libelants and the appellant corporation on the 22d day of May, 1900, at Pyramid Harbor, Alaska, by which it is claimed the appellant promised to pay each of the libelants, among other things, the sum of $100 for services rendered and to be rendered. In its answer the respondent denied the execution, on its part, of the contract sued upon, averred that it was without consideration, and for a third defense alleged that the work performed by the libelants for it was performed under other and different contracts than that sued on, and that, prior to the filing of the libel, each of the libelants was paid by the respondent the full amount due him thereunder, in consideration of which each of them executed a full release of all his claims and demands against the respondent.

[¶2] The evidence shows without conflict that on March 26, 1900, at the city and county of San Francisco, the libelants entered into a written contract with the appellants, whereby they agreed to go from San Francisco to Pyramid Harbor, Alaska, and return, on board such vessel as might be designated by the appellant, and to work for the appellant during the fishing season of 1900, at Pyramid Harbor, as sailors and fishermen, agreeing to do "regular ship's duty, both up and down, discharging and loading; and to do any other work whatsoever when requested to do so by the captain or agent of the Alaska Packers' Association." By the terms of this agreement, the appellant was to pay each of the libelants $50 for the season, and two cents for each red salmon in the catching of which he took part.

[¶3] On the 15th day of April, 1900, 21 of the libelants signed shipping articles by which they shipped as seamen on the Two Brothers, a vessel chartered by the appellant for the voyage between San Francisco and Pyramid Harbor, and also bound themselves to perform the same work for the appellant provided for by the previous contract of March 26th; the appellant agreeing to pay them therefor the sum of $60 for the season, and two cents each for each red salmon in the catching of which they should respectively take part. Under these contracts, the libelants sailed on board the Two Brothers for Pyramid Harbor, where the

appellants had about $150,000 invested in a salmon cannery. The libelants arrived there early in April of the year mentioned, and began to unload the vessel and fit up the cannery. A few days thereafter, to wit, May 19th, they stopped work in a body, and demanded of the company's superintendent there in charge $100 for services in operating the vessel to and from Pyramid Harbor, instead of the sums stipulated for in and by the contracts; stating that unless they were paid this additional wage they would stop work entirely, and return to San Francisco. The evidence showed, and the court below found, that it was impossible for the appellant to get other men to take the places of the libelants, the place being remote, the season short and just opening; so that, after endeavoring for several days without success to induce the libelants to proceed with their work in accordance with their contracts, the company's superintendent, on the 22d day of May, so far yielded to their demands as to instruct his clerk to copy the contracts executed in San Francisco, including the words "Alaska Packers' Association" at the end, substituting, for the $50 and $60 payments, respectively, of those contracts, the sum of $100, which document, so prepared, was signed by the libelants before a shipping commissioner whom they had requested to be brought from Northeast Point; the superintendent, however, testifying that he at the time told the libelants that he was without authority to enter into any such contract, or to in any way alter the contracts made between them and the company in San Francisco. Upon the return of the libelants to San Francisco at the close of the fishing season, they demanded pay in accordance with the terms of the alleged contract of May 22d, when the company denied its validity, and refused to pay other than as provided for by the contracts of March 26th and April 5th, respectively. Some of the libelants, at least, consulted counsel, and, after receiving his advice, those of them who had signed the shipping articles before the shipping commissioner at San Francisco went before that officer, and received the amount due them thereunder, executing in consideration thereof a release in full, and the others paid at the office of the company, also receipting in full for their demands.

[¶4] On the trial in the court below, the libelants undertook to show that the fishing nets provided by the respondent were defective, and that it was on that account that they demanded increased wages. On that point, the evidence was substantially conflicting, and the finding of the court was against the libelants * * * *.

[¶5] The evidence being sharply conflicting in respect to these facts, the conclusions of the court, who heard and saw the witnesses, will not be disturbed. * * * *

[¶6] The real questions in the case as brought here are questions of law, and, in the view that we take of the case, it will be necessary to consider but one of those. Assuming that the appellant's superintendent at Pyramid Harbor was authorized to make the alleged contract of May 22d, and that he executed it on behalf of the appellant, was it supported by a sufficient consideration? From the foregoing statement of the case, it will have been seen that the libelants agreed in writing, for certain stated compensation, to render their services to the appellant in remote waters where the season for conducting fishing operations is extremely short, and in which enterprise the appellant had a large amount of money invested; and, after having entered upon the discharge of their contract, and at a time when it was impossible for the appellant to secure other men in their places, the libelants, without any valid cause, absolutely refused to continue the services they were under contract to perform unless the appellant would consent to pay them more money. Consent to such a demand, under such circumstances, if given, was, in our opinion, without consideration, for the reason that it was based solely upon the libelants' agreement to render the exact services, and none other, that they were already under contract to render. The case shows that they willfully and arbitrarily broke that obligation. * * * *

[¶7] The circumstances of the present case bring it, we think, directly within the sound and just observations of the supreme court of Minnesota in the case of *King v. Railway Co*., 61 Minn. 482, 63 N.W. 1105:

"No astute reasoning can change the plain fact that the party who refuses to perform, and thereby coerces a promise from the other party to the contract to pay him an increased compensation for doing that which he is legally bound to do, takes an unjustifiable advantage of the necessities of the other party. Surely it would be a travesty on justice to hold that the party so making the promise for extra pay was estopped from asserting that the promise was without consideration. A party cannot lay the foundation of an estoppel by his own wrong, where the promise is simply a repetition of a subsisting legal promise. There can be no consideration for the promise of the other party, and there is no warrant for inferring that the parties have voluntarily rescinded or modified their contract. The promise cannot be legally enforced, although the other party has completed his contract in reliance upon it."

* * * *

[¶8] * * * * [T]he supreme court of Vermont [said] in the * * * * case of *Cobb v. Cowdery*, 40 Vt. 25, 94 Am.Dec. 370 * * * * [,]

> "A promise by a party to do what he is bound in law to do is not an illegal consideration, but is the same as no consideration at all, and is merely void; in other words, it is insufficient, but not illegal. Thus, if the master of a ship promise his crew an addition to their fixed wages in consideration for and as an incitement to, their extraordinary exertions during a storm, or in any other emergency of the voyage, this promise is nudum pactum; the voluntary performance of an act which it was before legally incumbent on the party to perform being in law an insufficient consideration; and so it would be in any other case where the only consideration for the promise of one party was the promise of the other party to do, or his actual doing, something which he was previously bound in law to do. Chit. Cont. (10th Am.Ed.) 51; Smith, Cont. 87; 3 Kent, Com.. 185."

* * * *

[¶9] It results from the views above expressed that the judgment must be reversed, and the cause remanded, with directions to the court below to enter judgment for the respondent, with costs. It is so ordered.

Questions:

1. What is the policy behind the pre-existing duty rule as used in this case?

2. Why did the superintendent wait so long to sign? (Please speculate. The answer is not explicit in the opinion.)

3. Generally, a mutual rescission of a contract in which each parties' duties are executory is binding. (Executory means, roughly, "not yet performed.") For instance, suppose I promise to sell you my cow and you promise to buy the cow for $500. After we have traded promises in assent, we are bound to a contract. But suppose we mutually release each other from our obligations under the contract before either of us performs. In that case, we are more or less mutually promising not to assert rights under the contract. This consensual trade of mutual promises ought to be just as binding as the original agreement, shouldn't it, either as a contract or as a mutual exchange of gifts? Wasn't that what happened in *Domenico*?

4. Please recall *Associated Builders, Inc. v. Coggins* in Chapter 1. An accord is a kind of modification in which, as *Coggins* said, the original obligation is not discharged (or replaced) until the satisfaction occurs. From reading *Coggins*, is it your impression that an accord, to be binding, requires consideration? If an accord has consideration and the satisfaction never occurs, can the promisee sue for breach of the accord? What was consideration in *Coggins*? Why did *Coggins* not run afowl of the pre-existing duty rule?

SCHWARTZREICH v. BAUMAN-BASCH, INC.

Court of Appeals of New York (1921)

131 N.E. 887

CRANE, J.

[¶1] On the 31st day of August, 1917, the plaintiff entered into the following employment agreement with the defendant:

> "BAUMAN-BASCH, INC.,
>
> "Coats & Wraps,
>
> "31-33 East 32nd Street,
>
> "New York
>
> "Agreement entered into this 31st day of August, 1917, by and between Bauman-Basch, Inc., a domestic corporation, party of the first part, and Louis Schwartzreich, of the Borough of Bronx, City of New York, party of the second part, Witnesseth:
>
> "The party of the first part does hereby employ the party of the second part, and the party of the second part agrees to enter the services of the party of the first part as a designer of coats and wraps.
>
> "The employment herein shall commence on the 22nd day of November, 1917, and shall continue for twelve months thereafter. The party of the second part shall receive a salary of Ninety ($90.00) per week, payable weekly.

> "The party of the second part shall devote his entire time and attention to the business of the party of the first part, and shall use his best energies and endeavors in the furtherance of its business.
>
> "In witness whereof, the party of the first part has caused its seal to be affixed hereto and these presents to be signed, and the party of the second part has here-unto set his hand and seal the day and year first above written.
>
> "BAUMAN-BASCH, INC.
>
> S. BAUMAN
>
> "LOUIS SCHWARTZREICH.
>
> "In the presence of:"

[¶2] In October the plaintiff was offered more money by another concern. Mr. Bauman, an officer of the Bauman-Basch, Inc., says that in that month he heard that the plaintiff was going to leave and thereupon had with him the following conversation.

> "A. I called him in the office, and I asked him, 'Is that true that you want to leave us?' and he said 'Yes,' and I said, 'Mr. Schwartzreich, how can you do that; you are under contract with us?' He said, 'Somebody offered me more money.' * * * * I said, 'How much do they offer you?' He said, 'They offered him $115 a week.' * * * * I said, 'I cannot get a designer now, and, in view of the fact that I have to send my sample line out on the road, I will give you a hundred dollars a week rather than to let you go.' He said, 'If you will give me $100, I will stay.'"

Thereupon Mr. Bauman dictated to his stenographer a new contract, dated October 17, 1917, in the exact words of the first contract and running for the same period, the salary being $100 a week, which contract was duly executed by the parties and witnessed. Duplicate originals were kept by the plaintiff and defendant.

[¶3] Simultaneously with the signing of this new contract, the plaintiff's copy of the old contract was either given to or left with Mr. Bauman. He testifies that the plaintiff gave him the paper but that he did not take it from him. The signatures to the old contract plaintiff tore off at the time according to Mr. Bauman.

[¶4] The plaintiff's version as to the execution of the new contract is as follows:

> "A. I told Mr. Bauman that I have an offer from Scheer & Mayer of $110 a week, and I said to him, 'Do you advise me as a friendly matter—will you advise me as a friendly matter what to do; you see I have a contract with you, and I should not accept the offer of $110 a week, and I ask you, as a matter of friendship, do you advise me to take it or not.' At the minute he did not say anything, but the day afterwards he came to me in and he said, 'I will give you $100 a week, and I want you to stay with me.' I said, 'All right, I will accept it; it is very nice of you that you do that, and I appreciate it very much.'"

The plaintiff says that on the 17th of October when the new contract was signed, he gave his copy of the old contract back to Mr. Bauman, who said: “You do not want this contract any more because the new one takes its place.”

[¶5] The plaintiff remained in the defendant’s employ until the following December when he was discharged. He brought this action under the contract of October 17th for his damages.

[¶6] The defense, insisted upon through all the courts, is that there was no consideration for the new contract as the plaintiff was already bound under his agreement of August 31, 1917, to do the same work for the same period at $90 a week.

[¶7] The trial justice submitted to the jury the question whether there was a cancellation of the old contract and charged as follows:

> “If you find that the $90 contract was prior to or at the time of the execution of the $100 contract cancelled and revoked by the parties by their mutual consent, then it is your duty to find that there was a consideration for the making of the contract in suit, viz., the $100 contract and, in that event, the plaintiff would be entitled to your verdict for such damages as you may find resulted proximately, naturally and necessarily in consequence of the plaintiff’s discharge prior to the termination of the contract period of which I shall speak later on.”

[¶8] Defendant’s counsel thereupon excepted to that portion of the charge in which the court permitted the jury to find that the prior contract may have been canceled simultaneously with the execution of the other agreement. Again the court said:

> “The test question is whether by word or by act, either prior to or at the time of the signing of the $100 contract, these parties mutually agreed that the old contract from that instant should be null and void.”

[¶9] The jury having rendered a verdict for the plaintiff the trial justice set it aside and dismissed the complaint on the ground that there was not sufficient evidence that the first contract was canceled to warrant the jury’s findings.

[¶10] The above quotations from the record show that a question of fact was presented and that the evidence most favorable for the plaintiff would sustain a finding that the first contract was destroyed, canceled or abrogated by the consent of both parties.

[¶11] The Appellate Term was right in reversing this ruling. Instead of granting a new trial, however, it reinstated the verdict of the jury and the judgment for the plaintiff. The question remains, therefore, whether the charge of the court, as above given, was a correct statement of the law or whether on all the evidence in the plaintiff’s favor a cause of action was made out.

[¶12] Can a contract of employment be set aside or terminated by the parties to it and a new one made or substituted in its place? If so, is it competent to end the one and make the other at the same time?

[¶13] It has been repeatedly held that a promise made to induce a party to do that which he is already bound by contract to perform is without consideration. But the cases in this state, while enforcing this rule,

also recognize that a contract may be canceled by mutual consent and a new one made. Thus *Vanderbilt v. Schreyer* (91 N. Y. 392, 402) held that it was no consideration for a guaranty that a party promise to do only that which he was before legally bound to perform. This court stated, however:

> "It would doubtless be competent for parties to cancel an existing contract and make a new one to complete the same work at a different rate of compensation, but it seems that it would be essential to its validity that there should be a valid cancellation of the original contract. Such was the case of *Lattimore v. Harsen* (14 Johns. 330)."

[¶14] In *Cosgray v. New England Piano Co.* (10 App. Div. 351, 353) it was decided that where the plaintiff had bound himself to work for a year at $30 a week, there was no consideration for a promise thereafter made by the defendant that he should notwithstanding receive $1,800 a year. Here it will be noticed there was no termination of the first agreement which gave occasion for BARTLETT, J., to say in the opinion:

> "The case might be different if the parties had, by word of mouth, agreed wholly to abrogate and do away with a pre-existing written contract in regard to service and compensation, and had substituted for it another agreement."

[¶15] Any change in an existing contract, such as a modification of the rate of compensation, or a supplemental agreement, must have a new consideration to support it. In such a case the contract is continued, not ended. Where, however, an existing contract is terminated by consent of both parties and a new one executed in its place and stead, we have a different situation and the mutual promises are again a consideration. Very little difference may appear in a mere change of compensation in an existing and continuing contract and a termination of one contract and the making of a new one for the same time and work, but at an increased compensation. There is, however, a marked difference in principle. Where the new contract gives any new privilege or advantage to the promisee, a consideration has been recognized, though in the main it is the same contract. (*Triangle Waist Co., Inc., v. Todd*, 223 N. Y. 27.)

[¶16] If this which we are now holding were not the rule, parties having once made a contract would be prevented from changing it no matter how willing and desirous they might be to do so, unless the terms conferred an additional benefit to the promisee.

[¶17] All concede that an agreement may be rescinded by mutual consent and a new agreement made thereafter on any terms to which the parties may assent. Prof. Williston in his work on Contracts says (Vol. 1, § 130a): "A rescission followed shortly afterwards by a new agreement in regard to the same subject-matter would create the legal obligations provided in the subsequent agreement."

[¶18] The same effect follows in our judgment from a new contract entered into at the same time the old one is destroyed and rescinded by mutual consent. The determining factor is the rescission by consent. Provided this is the expressed and acted upon intention, the time of the rescission, whether a moment before or at the same time as the making of the new contract, is unimportant. The decisions are numerous and divergent where one of the parties to a contract refuses to perform unless paid an additional amount. Some states hold the new promise to pay the demand binding though there be no rescission. It is said that the new promise is given to secure performance in place of an action for damages for not performing (*Parrot v. Mexican Central Railway Co*., 207 Mass. 184), or that the new contract is evidence of the rescission of the old one and it is the same as if no previous contract had been made (*Coyner v. Lynde*, 10 Ind. 282; *Connelly v. Devoe*, 37 Conn. 570; *Goebel v. Linn*, 47 Mich. 489), or that unforeseen difficulties and

hardships modify the rule (*King v. Duluth*, M. & N. Ry. Co., 61 Minn. 482), or that the new contract is an attempt to mitigate the damages which may flow from the breach of the first. (*Endriss v. Belle Isle Ice Co*., 49 Mich. 279.) * * * *

[¶19] The contrary has been held in such cases as * * * * *Alaska Packers' Association v. Domenico* (117 Fed. Rep. 99); * * * *. In none of these cases, however, was there a full and complete rescission of the old contract and it is this with which we are dealing in this case. Rescission is not presumed; it is expressed; the old contract is not continued with modifications; it is ended and a new one made. * * * *

[¶20] As before stated, in this case we have an express rescission and a new contract.

[¶21] There is no reason that we can see why the parties to a contract may not come together and agree to cancel and rescind an existing contract, making a new one in its place. We are also of the opinion that reason and authority support the conclusion that both transactions can take place at the same time.

[¶22] For the reasons here stated, the charge of the trial court was correct, and the judgments of the Appellate Division and the Appellate Term should be affirmed, with costs.

HISCOCK, C. J., and HOGAN, CARDOZO, McLAUGHLIN, and ANDREWS, JJ., concur.

CHASE, J., dissents.

Judgments affirmed.

Questions:

1. What difference factually is there between *Domenico* and *Schwartzreich*?

2. New Hampshire purports not to need a case such as *Schwartzreich.* Consider the following from *Kramas v. Beattie*, 221 A.2d 236 (N.H. 1966):

> A half century ago New Hampshire by judicial decision, quietly and unheralded, modernized a portion of the law of consideration by lopping off one of the historical errors of the common law. It repudiated *Pinnel's Case*, 5 Coke 177a (1602) and *Foakes v. Beer*, 9 App. Cas. 605 (1884) as being neither logical nor just. See, Ferson, *The Rule in* Foakes v. Beer, 31 Yale L.J. 15 (1921); Havighurst, *Consideration, Ethics and Administration*, 42 Colum. L. Rev. 127 (1942). 'The rule that the payment of a less sum can never sustain an agreement to discharge a greater, because without consideration, however well supported by authorities * * * * is based upon misconception, is not founded in reason, and cannot be followed without abandoning the greater principle that reason is the life of the law.' *Frye v. Hubbell*, 74 N.H. 358, 377, 68 A. 325, 334, * * * *. Consequently, in *Frye v. Hubbell*, *supra*, it was held that payment of part of a debt accepted in full payment discharged liability for the balance. * * * * Whether 'the claim be liquidated or unliquidated, the matter resolves itself into a question as to whether the lesser sum was accepted as satisfaction in full.'

> In the present case there is no doubt that the defendant was dissatisfied with the lease, was attempting to 'break the lease,' and wished to terminate the lease with the payment of rent for the month of March by the check which bore the notation 'final and terminating payment under lease.' There is also no doubt that the plaintiffs were aware of these facts because of the defendant's complaints and the letters he had received from the defendant's attorney. If the Presiding Justice had believed the defendant's testimony that she was terminating the lease by the check for the March rent and the [plaintiffs] accepted it as such, there would be an accord and satisfaction.

This last sentence from *Kramas* is dicta; the trial court found that plaintiffs did not accept the last check as a termination of the lease. But can you see how the sentence refuses to follow *Foakes*? If *Foakes* were the rule, what else besides that "the plaintiffs accepted it as such" would be required in order that an accord and satisfaction occur?

An earlier case following *Frye*, *Watkins & Son v. Carrig*, 21 A.2d 591 (N.H. 1941), involved an excavation contract. When the excavator actually began digging, it struck rock, something not anticipated, so the excavator made an "insistent request" to the property owner for a renegotiation of the contract. The owner renegotiated but later refused to pay the increased price. The court reasoned as follows:

> In common understanding there is, importantly, a wide divergence between a bare promise and a promise in adjustment of a contractual promise already outstanding. * * * * * * * * [P]arties to a valid contract generally understand that it is subject to any mutual action they may take in its performance. Changes to meet changes in circumstances and conditions should be valid if the law is to carry out its function and service by rules conformable with reasonable practices and understandings in matters of business and commerce. * * * *
>
> The foregoing views are considered to meet the reasonable needs of standard and ethical practices of men in their business dealings with each other. Conceding that the plaintiff threatened to break its contract because it found the contract to be improvident, yet the defendant yielded to the threat without protest, excusing the plaintiff, and making a new arrangement. Not insisting on his rights but relinquishing them, fairly he should be held to the new arrangement. The law is a means to an end. It is not the law because it is the law, but because it is adapted and adaptable to establish and maintain reasonable order. * * * * It is not practical that the law should adopt all precepts of moral conduct, but it is desirable that its rule and principles should not run counter to them in important conduct and transactions of life.

Is this a better approach?

3. Some states have statutes that make some modifications binding without consideration if they are in writing. The clearest example may be N.Y. Gen. Obligations Law § 5-1103:

> Written agreement for modification or discharge. An agreement, promise or undertaking to change or modify, or to discharge in whole or in part, any contract, obligation, or lease, or any mortgage or other security interest in personal or real property, shall not be invalid because of the absence of consideration, provided that the agreement, promise or undertaking changing, modifying, or discharging such contract, obligation, lease, mortgage

> or security interest, shall be in writing and signed by the party against whom it is sought to enforce the change, modification or discharge, or by his agent.

See also Mich. Comp. L. Ann. s 566.1. Some other states reach a similar result by means of part performance, in place of a writing, for modifications in the form of accord and satisfaction:

> Part performance of an obligation, promise or undertaking, either before or after a breach thereof, when expressly accepted by the creditor in satisfaction and rendered in pursuance of an agreement for that purpose, though without any new consideration, shall extinguish such obligation, promise, or undertaking.

Va. Code Ann. s 11-12. Would either of these be a better approach?

Alfred L. ANGEL v. John E. MURRAY, Jr., Director of Finance of the City of Newport, et al. (1974)

Supreme Court of Rhode Island

322 A.2d 630

OPINION

ROBERTS, Chief Justice.

[¶1] This is a civil action brought by Alfred L. Angel and others against John E. Murray, Jr., Director of Finance of the City of Newport, the city of Newport, and James L. Maher, alleging that Maher had illegally been paid the sum of $20,000 by the Director of Finance and praying that the defendant Maher be ordered to repay the city such sum. The case was heard by a justice of the Superior Court, sitting without a jury, who entered a judgment ordering Maher to repay the sum of $20,000 to the city of Newport. Maher is now before this court prosecuting an appeal.

[¶2] The record discloses that Maher has provided the city of Newport with a refuse-collection service under a series of five-year contracts beginning in 1946. On March 12, 1964, Maher and the city entered into another such contract for a period of five years commencing on July 1, 1964, and terminating on June 30, 1969. The contract provided, among other things, that Maher would receive $137,000 per year in return for collecting and removing all combustible and noncombustible waste materials generated within the city.

[¶3] In June of 1967 Maher requested an additional $10,000 per year from the city council because there had been a substantial increase in the cost of collection due to an unexpected and unanticipated increase of 400 new dwelling units. Maher's testimony, which is uncontradicted, indicates the 1964 contract had been predicated on the fact that since 1946 there had been an average increase of 20 to 25 new dwelling units per year. After a public meeting of the city council where Maher explained in detail the reasons for his request and was questioned by members of the city council, the city council agreed to pay him an additional $10,000 for the year ending on June 30, 1968. Maher made a similar request again in June of

1968 for the same reasons, and the city council again agreed to pay an additional $10,000 for the year ending on June 30, 1969.

[¶4] The trial justice found that each such $10,000 payment was made in violation of law. His decision, as we understand it, is premised on two independent grounds. First, he found that the additional payments were unlawful because they had not been recommended in writing to the city council by the city manager. Second, he found that Maher was not entitled to extra compensation because the original contract already required him to collect all refuse generated within the city and, therefore, included the 400 additional units. The trial justice further found that these 400 additional units were within the contemplation of the parties when they entered into the contract. It appears that he based this portion of the decision upon the rule that Maher had a preexisting duty to collect the refuse generated by the 400 additional units, and thus there was no consideration for the two additional payments.

[¶5] [Analysis of the first ground for appeal is omitted.]

[¶6] Having found that the city council had the power to modify the 1964 contract without the written recommendation of the city manager, we are still confronted with the question of whether the additional payments were illegal because they were not supported by consideration.

A

[¶7] As previously stated, the city council made two $10,000 payments. The first was made in June of 1967 for the year beginning on July 1, 1967, and ending on June 30, 1968. Thus, by the time this action was commenced in October of 1968, the modification was completely executed. That is, the money had been paid by the city council, and Maher had collected all of the refuse. Since consideration is only a test of the enforceability of executory promises, the presence or absence of consideration for the first payment is unimportant because the city council's agreement to make the first payment was fully executed at the time of the commencement of this action. * * * * However, since both payments were made under similar circumstances, our decision regarding the second payment (Part B, infra) is fully applicable to the first payment.

B

[¶8] It is generally held that a modification of a contract is itself a contract, which is unenforceable unless supported by consideration. See Simpson, *supra*, § 93. In *Rose v. Daniels*, 8 R.I. 381 (1866), this court held that an agreement by a debtor with a creditor to discharge a debt for a sum of money less than the amount due is unenforceable because it was not supported by consideration.

[¶9] *Rose* is a perfect example of the preexisting duty rule. Under this rule an agreement modifying a contract is not supported by consideration if one of the parties to the agreement does or promises to do something that he is legally obligated to do or refrains or promises to refrain from doing something he is not legally privileged to do, See Calamari & Perillo, Contracts § 60 (1970); 1A Corbin, Contracts §§ 171-72 (1963); 1 Williston, *supra*, § 130; Annot., 12 A.L.R.2d 78 (1950). In *Rose* there was no consideration for the new agreement because the debtor was already legally obligated to repay the full amount of the debt. * * * *

[¶10] The primary purpose of the preexisting duty rule is to prevent what has been referred to as the "hold-up game." See 1A Corbin, *supra*, § 171. A classic example of the "hold-up game" is found in *Alaska Packers' Ass'n v. Domenico*, 117 F. 99 (9th Cir. 1902). There 21 seamen entered into a written contract with

Domenico to sail from San Francisco to Pyramid Harbor, Alaska. They were to work as sailors and fishermen out of Pyramid Harbor during the fishing season of 1900. The contract specified that each man would be paid $50 plus two cents for each red salmon he caught. Subsequent to their arrival at Pyramid Harbor, the men stopped work and demanded an additional $50. They threatened to return to San Francisco if Domenico did not agree to their demand. Since it was impossible for Domenico to find other men, he agreed to pay the men an additional $50. After they returned to San Francisco, Domenico refused to pay the men an additional $50. The court found that the subsequent agreement to pay the men an additional $50 was not supported by consideration because the men had a preexisting duty to work on the ship under the original contract, and thus the subsequent agreement was unenforceable.

[¶11] Another example of the “hold-up game” is found in the area of construction contracts. Frequently, a contractor will refuse to complete work under an unprofitable contract unless he is awarded additional compensation. The courts have generally held that a subsequent agreement to award additional compensation is unenforceable if the contractor is only performing work which would have been required of him under the original contract. See, e.g., *Lingenfelder v. Wainwright Brewing Co*., 103 Mo. 578, 15 S.W. 844 (1891), which is a leading case in this area. * * * *

[¶12] These examples clearly illustrate that the courts will not enforce an agreement that has been procured by coercion or duress and will hold the parties to their original contract regardless of whether it is profitable or unprofitable. However, the courts have been reluctant to apply the pre-existing duty rule when a party to a contract encounters unanticipated difficulties and the other party, not influenced by coercion or duress, voluntarily agrees to pay additional compensation for work already required to be performed under the contract. For example, the courts have found that the original contract was rescinded, *Linz v. Schuck*, 106 Md. 220, 67 A. 286 (1907); abandoned, *Connelly v. Devoe*, 37 Conn. 570 (1871), or waived, *Michaud v. MacGregor*, 61 Minn. 198, 63 N.W. 479 (1895).

[¶13] Although the preexisting duty rule has served a useful purpose insofar as it deters parties from using coercion and duress to obtain additional compensation, it has been widely criticized as a general rule of law. With regard to the preexisting duty rule, one legal scholar has stated: “There has been a growing doubt as to the soundness of this doctrine as a matter of social policy. * * * * In certain classes of cases, this doubt has influenced courts to refuse to apply the rule, or to ignore it, in their actual decisions. Like other legal rules, this rule is in process of growth and change, the process being more active here than in most instances. The result of this is that a court should no longer accept this rule as fully established. It should never use it as the major premise of a decision, at least without giving careful thought to the circumstances of the particular case, to the moral deserts of the parties, and to the social feelings and interests that are involved. It is certain that the rule, stated in general and all-inclusive terms, is no longer so well-settled that a court must apply it though the heavens fall.” 1A Corbin, *supra*, § 171; see also Calamari & Perillo, *supra*, § 61.

[¶14] The modern trend appears to recognize the necessity that courts should enforce agreements modifying contracts when unexpected or unanticipated difficulties arise during the course of the performance of a contract, even though there is no consideration for the modification, as long as the parties agree voluntarily.

[¶15] Under the Uniform Commercial Code, § 2-209(1), which has been adopted by 49 states, “[a]n agreement modifying a contract [for the sale of goods] needs no consideration to be binding.” See G.L. 1956 (1969 Reenactment) § 6A-2-209(1). Although at first blush this section appears to validate

modifications obtained by coercion and duress, the comments to this section indicate that a modification under this section must meet the test of good faith imposed by the Code, and a modification obtained by extortion without a legitimate commercial reason is unenforceable.

[¶16] The modern trend away from a rigid application of the preexisting duty rule is reflected by § 89D(a) of the American Law Institute's Restatement Second of the Law of Contracts,[†††] which provides: "A promise modifying a duty under a contract not fully performed on either side is binding (a) if the modification is fair and equitable in view of circumstances not anticipated by the parties when the contract was made * * *."

[¶17] We believe that § 89D(a) is the proper rule of law and find it applicable to the facts of this case. It not only prohibits modifications obtained by coercion, duress, or extortion but also fulfills society's expectation that agreements entered into voluntarily will be enforced by the courts.[§§§] See generally

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[†††] [1] The first nine chapters of the Restatement Second of the Law of Contracts were given tentative approval by the American Law Institute at successive meetings from 1964 to 1972. These chapters, which include §§ 1-255, were published by the Institute in 1973 in a hard-cover edition. Herbert Wechsler, Director of the Institute, in a foreword to this edition indicates that although these sections are still tentative and await final approval, it is unlikely that any further changes will be made.

[§§§] [3] The drafters of § 89D(a) of the Restatement Second of the Law of Contracts use the following illustrations in comment (b) as examples of how this rule is applied to certain transactions:

> "1. By a written contract A agrees to excavate a cellar for B for a stated price. Solid rock is unexpectedly encountered and A so notifies B. A and B then orally agree that A will remove the rock at a unit price which is reasonable but nine times that used in computing the original price, and A completes the job. B is bound to pay the increased amount.
>
> "2. A contracts with B to supply for $300 a laundry chute for a building B has contracted to build for the government for $150,000. Later A discovers that he made an error as to the type of material to be used and should have bid $1,200. A offers to supply the chute for $1,000, eliminating overhead and profit. After ascertaining that other suppliers would charge more, B agrees. The new agreement is binding.
>
> "3. A is employed by B as a designer of coats at $90 a week for a year beginning November 1 under a written contract executed September 1. A is offered $115 a week by another employer and so informs B. A and B then agree that A will be paid $100 a week and in October execute a new written contract to that effect, simultaneously tearing up the prior contract. The new contract is binding.
>
> "4. A contracts to manufacture and sell to B 2,000 steel roofs for corn cribs at $60. Before A begins manufacture a threat of a nationwide steel strike raises the cost of steel about $10 per roof, and A and B agree orally to increase the price to $70 per roof. A thereafter manufactures and delivers 1,700 of the roofs, and B pays for 1,500 of them at the increased price without protest, increasing the selling price of the corn cribs by $10. The new agreement is binding.
>
> "5. A contracts to manufacture and sell to B 100,000 castings for lawn mowers at 50 cents each. After partial delivery and after B has contracted to sell a substantial number of lawn mowers at a fixed price, A notifies B that increased metal costs require that the price be increased to 75 cents. Substitute castings are available at 55 cents, but only

Horwitz, The Historical Foundations of Modern Contract Law, 87 Harv. L. Rev. 917 (1974). Section 89D(a), of course, does not compel a modification of an unprofitable or unfair contract; it only enforces a modification if the parties voluntarily agree and if (1) the promise modifying the original contract was made before the contract was fully performed on either side, (2) the underlying circumstances which prompted the modification were unanticipated by the parties, and (3) the modification is fair and equitable.

[¶18] The evidence, which is uncontradicted, reveals that in June of 1968 Maher requested the city council to pay him an additional $10,000 for the year beginning on July 1, 1968, and ending on June 30, 1969. This request was made at a public meeting of the city council, where Maher explained in detail his reasons for making the request. Thereafter, the city council voted to authorize the Mayor to sign an amendment to the 1954 contract which provided that Maher would receive an additional $10,000 per year for the duration of the contract. Under such circumstances we have no doubt that the city voluntarily agreed to modify the 1964 contract.

[¶19] Having determined the voluntariness of this agreement, we turn our attention to the three criteria delineated above. First, the modification was made in June of 1968 at a time when the five-year contract which was made in 1964 had not been fully performed by either party. Second, although the 1964 contract provided that Maher collect all refuse generated within the city, it appears this contract was premised on Maher's past experience that the number of refuse-generating units would increase at a rate of 20 to 25 per year. Furthermore, the evidence is uncontradicted that the 1967-1968 increase of 400 units "went beyond any previous expectation." Clearly, the circumstances which prompted the city council to modify the 1964 contract were unanticipated. Third, although the evidence does not indicate what proportion of the total this increase comprised, the evidence does indicate that it was a "substantial" increase. In light of this, we cannot say that the council's agreement to pay Maher the $10,000 increase was not fair and equitable in the circumstances.

[¶20] The judgment appealed from is reversed, and the cause is remanded to the Superior Court for entry of judgment for the defendants.

Questions:

1. Who is Angel? (Just guess. It's not in the case.)

2. If the court had found that lack of consideration meant that the modification was not binding, would Maher have had to repay the first $10,000?

3. If the city's promise to pay the second $10,000 was enforceable, was the promise to pay the first $10,000 likewise enforceable?

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after several months delay. B protests but is forced to agree to the new price to keep its plant in operation. The modification is not binding."

4. Does the court adopt the Restatement Rule exactly?

5. Would the rule the court adopts apply to *Foakes v. Beer*?

6. Do you recognize the facts of illustration no. 3 in the second footnote? The facts of illustration no. 1?

B. Waiver

R. CONRAD MOORE & ASSOCS., INC. v. LERMA

946 S.W.2d 90 (Tex. App.—El Paso 1997, writ denied)

OPINION

Larsen, Justice.

* * * * FACTS

[¶1] On January 30, 1990, the Lermas (Appellees) and R. Conrad Moore & Associates, Inc. (Appellant) entered into an earnest money contract for the purchase of two lots at 1900 Gus Moran in El Paso. The Lermas tendered a check to Moore for $13,500 as part of the earnest money contract. The sale of the lots was contingent upon the Lermas using Moore as a builder. On April 16, 1990, the Lermas and Moore incorporated the previous contract into a new home residential earnest money contract. This contract provided for the construction of a custom home on the lots for a total price, including the lots, of $180,000. The new contract called for an additional payment of $6,500 earnest money, due upon the Lermas' approval of the house plan. Paragraph 4 of the contract required the following:

> FINANCING CONDITIONS: This contract is subject to approval for Buyer of a conventional (type of loan) loan (the Loan) to be evidenced by a promissory note (the Note) in the amount of $180,000. Buyer shall apply for the Loan within 15 days from the effective date of this contract and shall make every reasonable effort to obtain approval from Competitive Mortgage Co., as lender, or any lender that will make the Loan. **If the Loan cannot be approved within 60 days from the effective date of this contract, this contract shall terminate and the Earnest Money shall be refunded to Buyer without delay.** [Emphasis added.]

[¶2] In addition to the standard provision of the preprinted contract, special handwritten provisions were included under Paragraph 11:

> 1) Seller give One Year (1) Builders Warranty and 10-Year H.O.W. warranty
>
> 2) On Lot held more than 60 days, Earnest Money is non-refundable.

> 3) Lot purchase contract dated January 30, 1990 is hereby transferred to this Home construction contract.
>
> 4) Balance of Down Payment to be made at time of sale of properties located at 1400 Bodega and 3509 Breckenridge. [Emphasis added.]

[¶3] Construction on the house began in December 1990, and was completed in the summer of 1991. The Lermas were ultimately denied credit and were unable to close on the house. In September 1991, after demanding the return of their earnest money, they initiated this suit in November 1992. After trial to a jury, the Lermas were awarded $20,000 in damages. The jury found that Moore breached the contract by failing to return the Lermas' earnest money upon the Lermas' failure to get loan approval within the 60 days contemplated by Paragraph 4 of the contract. Moore appeals.

STANDARD OF REVIEW: LEGAL AND FACTUAL SUFFICIENCY

[¶4] Moore asserts in its first six points of error that the evidence was legally or factual insufficient to support the jury's findings.

[¶5] In reviewing a "no evidence" or legal sufficiency claim, we examine only the evidence favorable to the verdict and disregard all evidence to the contrary. * * * *

[¶6] In reviewing a "matter of law" challenge, we first examine the record to see if any evidence supports the finding, ignoring all evidence to the contrary. If no evidence supports the finding, we then determine whether the evidence conclusively establishes its converse. If so, we must reverse. * * * *

Loan Approval

[¶7] In its first point of error, Moore asserts the evidence is legally and factually insufficient to support the jury finding that the Lermas failed to get loan approval for the purchase of the home. After a diligent search of the record, we have been unable to find any evidence that would support a finding that the Lermas did get financing for the purchase. Moore testified that "someone" at Sun World Savings informed her that the Lermas were approved within the 60 day period. However, Ms. Nancy Montes of Mortgage Plus, who took the Lermas' loan application, testified that they were never approved. She stated that a "take out" letter sent out in October 1990 was not final loan approval but a prequalification report that indicates a conditional approval subject to verification and continuing good credit. Ms. Montes further testified that she exhausted all her sources in attempting to get financing for the Lermas. Ultimately, the Lermas were denied credit and were unable to close on the house. The record overwhelmingly supports the jury's finding that the Lermas did not get loan approval for the purchase of the house. Therefore, Moore's first point of error is overruled.

Waiver

[¶8] In its second point of error, Moore asserts that the evidence establishes as a matter of law that the Lermas waived any right to have the earnest money refunded. We agree.

[¶9] Any contractual right can be waived. *Purvis Oil Corp. v. Hillin*, 890 S.W.2d 931, 937 (Tex. App.-El Paso 1994, no writ). A waiver is an intentional release, relinquishment, or surrender of a known right. *Id*. The following elements must be met to find waiver: (1) a right must exist at the time of the waiver; (2) the party who is accused of waiver must have constructive or actual knowledge of the right in question; and (3)

the party intended to relinquish its right. See *Riley v. Meriwether*, 780 S.W.2d 919, 922 (Tex. App.-El Paso 1989, writ denied). Intentional relinquishment of a known right can be inferred from intentional conduct which is inconsistent with claiming the contractual right. *Id.*

[¶10] It has been conclusively established that the Lermas did not obtain financing for the purchase of the house from Moore. Paragraph 4 of the contract clearly states that if the purchasers are unable to obtain financing within 60 days of the effective date of the contract, they had a right to have their money returned. Thus, on June 15, 1990, the Lermas had a right to the return of their earnest money. The Lermas' intention to relinquish their right to the return of the earnest money, however, is clearly established by their conduct after June 15. Between the date the contract was signed and the date construction began on the house, the Lermas participated in the design of the house, approved the blueprints in July 1990, and tendered an additional $6,500 in earnest money to Moore in October. The Lermas were then conditionally approved for financing which allowed Moore to get a construction loan to begin building the house.

[¶11] Additionally, after construction of the house began in December 1990, the Lermas monitored its progress on a daily basis. In March 1991, they requested and paid for an upgrade in tile for the house. In June, Isabel Lerma executed a promissory note in the principal amount of $6,000 to Moore to pay for the addition of another room to the house. During this same time period, the Lermas sold their home and another property, as agreed in the contract, to fund the down payment. Mr. Lerma testified that he fully intended to buy the house that Moore was building, and at no time prior to August 1991 did he consider the contract terminated. Mrs. Lerma also testified that until August 1991, they wanted and intended to purchase the home.

[¶12] Although the Lermas claim that they were unaware that they could get their money back on that date, both Mr. and Mrs. Lerma signed the contract. Mrs. Lerma testified that she read the contract. Mr. Lerma was not sure if he read the contract, but testified that no one prevented him from doing so. A person who signs a contract is presumed to know and understand its contents; absent a finding of fraud, failure to apprehend the rights and obligations under the contract will not excuse performance. *See G-W-L, Inc. v. Robichaux*, 643 S.W.2d 392 (Tex.1982); *Thigpen v. Locke*, 363 S.W.2d 247 (Tex.1962). There is no evidence of fraud, actual or constructive, on the part of Moore. Thus, we conclude the Lermas had knowledge of their right to a refund of the earnest money on June 15.

[¶13] There is no evidence to support the jury's finding that the Lermas did not waive the right to have the earnest money refunded. The Lermas' intentional conduct after the right to the return of the earnest money arose was inconsistent with claiming that right. They intentionally relinquished a known right, and therefore, we find as a matter of law, that the Lermas waived Paragraph 4 of the contract, and the contract continued in effect, including Paragraph 11 allowing Moore to retain the earnest money on the lots.

[¶14] The Lermas argue that Paragraph 4 operates as a condition precedent. When the Lermas failed to obtain financing within 60 days, the contract, including any forfeiture provisions, terminated. Thus, the Lermas assert Paragraphs 16 and 11 never became effective. Many Texas cases have construed provisions similar to Paragraph 4 as conditions precedent. *See, e.g.*, * * * * In this case, however, we have an additional handwritten provision that is somewhat out of the ordinary and distinguishable from the clauses considered in the cases finding conditions precedent. Under Paragraph 11, the "special provisions" section of the contract, the parties added the phrase "on Lot held more than 60 days, Earnest Money is non-refundable." This brief passage is less than a model of clarity. At first blush, it appears in direct contradiction to Paragraph 4, the termination clause.

[¶15] If a contract is worded so that it can be given a certain or definite legal meaning or interpretation, then it is not ambiguous and the court will construe the contract as a matter of law. *City of Pinehurst v. Spooner Addition Water Co*., 432 S.W.2d 515, 518 (Tex.1968); *First City Nat'l Bank of Midland v. Concord Oil Co*., 808 S.W.2d 133, 137 (Tex. App.-El Paso 1991, no writ). There is no allegation in this case that the earnest money contract is ambiguous, and it does not appear to us to be so. Generally, the parties to a contract intend every clause to have some effect and the Court may not ignore any portion of the contract unless there is an irreconcilable conflict. *Ogden v. Dickinson State Bank*, 662 S.W.2d 330, 332 (Tex.1983); *Woods v. Sims*, 154 Tex. 59, 273 S.W.2d 617 (1954). In the interpretation of contracts, the primary concern of courts is to ascertain and to give effect to the intentions of the parties as expressed in the instrument. *Coker v. Coker*, 650 S.W.2d 391, 393 (Tex.1983); *Deacon, Inc. v. Price*, 817 S.W.2d 147, 149 (Tex. App.-El Paso 1991, writ denied). This requires the court to examine and consider the entire instrument and reach a decision so that none of the provisions will be rendered meaningless. *Id*.

[¶16] By its wording, Paragraph 11 is not merely a forfeiture clause subject to the condition precedent stated in Paragraph 4. Paragraph 11 envisions the non-occurrence of the condition (in this case financing obtained within 60 days), references the 60-day provision, and provides for continuation of the contract beyond 60 days. To give effect to both provisions and render neither meaningless, we must construe the handwritten provision to allow the buyer, at its option, to continue the contract after 60 days in the absence of financing. A condition precedent like any other provision of a contract can be waived. Purvis Oil Corp., 890 S.W.2d at 931. Thus, if financing were not obtained in 60 days, the Lermas could do nothing, the contract would terminate, and the Lermas would be entitled to return of the earnest money. On the other hand, the Lermas could take action to have the lot "held more than 60 days" thereby waiving the right to the return of the earnest money.

[¶17] The record establishes that the Lermas chose the latter option. They worked with Moore on the design of the house, tendered additional earnest money four months after the contract would have expired under Paragraph 4, contracted with Moore to increase the square footage of the house, paid for tile upgrades, and sold both the home they were living in and another property in anticipation of closing on the house when it was completed. The record therefore conclusively establishes that the Lermas waived termination of the contract and instead continued to operate pursuant to the contract under Paragraph 11.

* * * *

[¶18] We must reject the Lermas' arguments and affirm Moore's second point of error.

* * * *

CONCLUSION

[¶19] Having sustained Moore's second point of error, we reverse the judgment of the trial court and render judgment that the Lermas take nothing on their contract * * * * cause[] of action.

Questions:

1. Is this a case of express waiver or implied waiver?

2. What facts show the Lermas' intent? Do you believe the Lermas intended to relinquish their right?

3. Did the Lermas promise to apply for a loan?

4. Is reliance on a waiver necessary for the waiver to have legal effect?

5. What exactly was waived?

6. Can anything be waived? In Clark v. West, 86 N.E. 1 (N.Y. 1908), Clark and West contracted for Clark to write a book (and perhaps several books) that West would publish. Clark was to be paid $2 per page "and if [Clark] abstains from the use of intoxicating liquor and otherwise fulfills his agreements as hereinbefore set forth, he shall be paid an additional $4 per page in manner hereinbefore stated." But, after Clark began writing, he drank, and West knew it, but West told Clark that he would pay $6 per page notwithstanding Clark's drinking, or at least that is what Clark later alleged. When West paid only $2 per page, Clark sued, and West defended by claiming Clark drank. In response, Clark claimed West had waived the requirement of Clark's abstinence. In return, West argued that Clark's abstinence was the consideration for the contract, and could not be waived. While the court agreed that the consideration for a contract cannot be waived, the court said that Clark's writing books—not Clark's abstinence—was consideration, and Clark's abstinence was a waivable point. The point of law, though, is not controversial: the consideration of a contract cannot be waived, though we say it differently now: "A material part of the agreed exchange cannot be waived." Was what the Lermas waived a material part of the agreed exchange? No. What would have been?

7. Is waiver, as it operates in contract law, just a kind of modification? How are they the same or different?

Note: Retraction of Waivers

Once a waiver occurs, can it be retracted? Is a waiver permanent? In other words, is the waiving party bound to it? Courts often see fact patterns where a party has waived a right and then tried to "unwaive," meaning they attempt to retract the waiver and get the right back. They may think, well, if what matters for waiver is expression of intent, then if I express the opposite intent, I can take it back.

In fussy correctness, what is often waived is the non-occurrence of a condition. The Lermas waived the non-occurrence of their loan's being approved (or the non-occurrence of their giving up the lot within 60 days). But few people talk with fussy correctness, and even the waiver rule is phrased in terms of "right." This is a part of the law that many lawyers have never thought about carefully.

To some extent, the law supports the intuition in favor of "unwaiving" (noted above) at least with respect to things that have not happened yet. Section 2-209(5) of the UCC Article 2 says, "A party who has made a waiver affecting an executory portion of the contract may retract the waiver by reasonable notification received by the other party that strict performance will be required of any term waived, unless the retraction

would be unjust in view of a material change of position in reliance on the waiver." *Executory* simply means not yet done (as in not yet executed). This part of the UCC is a restatement of a common law position.

But it is incomplete. For instance, we know from the modification cases we have just studied that a change in the contract given in exchange for actual consideration would also be binding. So a waiver that is supported by consideration also could not be retracted (regardless of whether the bargained-for detriment was "a material change of position in reliance").

But wait! There's more! Both of those rules only apply to future things. If the event whose effects are waived has already happened, then it is no longer executory. With respect to past acts, a party must either stand on their rights or not. If they waive their rights after the events determining those rights have already happened, they have lost those rights. In legal terms, they have "elected their remedy." The most succinct statement of this your casebook author discovered was in *Fitzgerald v. Hubert Herman, Inc*., 179 N.W.2d 252 (Mich. App. 1970): "[A] waiver ... partaking of the principle of an election needs no consideration ... and cannot be retracted." So the law for retraction is divided into two scenarios: executory waivers and waivers in the nature of an election of remedies. See if you can write a concise, workable rule capturing the rules for retraction.

Here are some hypotheticals against which to test your knowledge:

PROBLEM 18. In the facts of *Clark v. West*, West tells Clark that Clark may drink without forfeiting the $4 per page West would otherwise have a right to withhold under the contract. When Clark turns in his next installment, pages 220-230 (out of 3,470), West is not pleased with Clark's work. It is acceptable, but not as good as what Clark had been writing. West therefore sends a letter to Clark stating that West will from the date of the letter's receipt forward insist that Clark not drink on pain of losing the $4 per page. Should Clark now drink?

PROBLEM 19. Marco contracted with Andrea that Andrea would deliver to him 22 tons of long grain rice on November 4, 2020. Andrea delivered the rice on November 7, 2020, at which time Marco accepted it. Two weeks later, Marco called Andrea and informed her that he was declining the rice and that she could pick it up or pay storage for it. He said he was not going to pay her because the rice was late. Must Marco pay?

Chapter 4. Alternate Theories of Recovery: Promissory Estoppel & Unjust Enrichment

Lawyers representing plaintiffs wish to raise every argument supporting their client's case. Most lawyers have filed simple contract cases resting on many—three, four, five, maybe more—different theories of recovery, only one of which was grounded in a consensual contract showing consideration. The forms of action—covenant, debt, and so on—have been abolished, but because of developments over the centuries, it is still possible to recover for breach of promise on several grounds. Now, however, unlike in the medieval period, courts expect plaintiffs to raise every possible theory of recovery, not pick one and stick with it. The same procedures—just general civil procedures—now apply to the litigation of each.

This chapter provides materials for your study of the two most prominent alternative theories for recovery on a breach of promise. They are related to consensual contract in certain ways. For instance, consensual contracts are founded on a bargain under the doctrine of consideration. Promissory estoppel is akin to detriment consideration. Unjust enrichment, like moral obligation, is akin to benefit consideration. Each of these two alternate theories if proved is grounds for legal enforcement of a promise.

A. Promissory Estoppel

You recall that we almost discussed the effect of non-bargained-for detriment in the first chapter. Some cases such as *Storer's Case* hinted at it. Now we return to it.

KIRKSEY v. KIRKSEY

Alabama Supreme Court (1845)

8 Ala. 131

[¶1] Assumpsit by the defendant, against the plaintiff in error. The question is presented in this Court, upon a case agreed, which shows the following facts:

[¶2] The plaintiff was the wife of defendant's brother, but had for some time been a widow, and had several children. In 1840, the plaintiff resided on public land, under a contract of lease, she had held over, and was comfortably settled, and would have attempted to secure the land she lived on. The defendant resided in Talladega county, some sixty, or seventy miles off. On the 10th October, 1840, he wrote to her the following letter:

Dear sister Antillico—Much to my mortification, I heard, that brother Henry was dead, and one of his children. I know that your situation is one of grief, and difficulty. You had a bad chance before, but a great deal worse now. I should like to come and see you, but cannot with convenience at present. * * * * I do not know whether you have a preference on the place you live on, or not. If you had, I would advise you to obtain your preference, and sell the land and quit the country, as I understand it is very unhealthy, and I know society is very bad. If you will come down and see me, I will let you have a place to raise your family, and I have more open land than I can tend; and on account of your situation, and that of your family, I feel like I want you and the children to do well.

Within a month or two after the receipt of this letter, the plaintiff abandoned her possession, without disposing of it, and removed with her family, to the residence of the defendant, who put her in comfortable houses, and gave her land to cultivate for two years, at the end of which he notified her to remove, and put her in a house, not comfortable, in the woods, which he afterwards required her to leave.

[¶3] A verdict being found for the plaintiff, for two hundred dollars, the above facts were agreed, and if they will sustain the action, the judgment is to be affirmed, otherwise it is to be reversed.

[¶4] ORMOND, J. The inclination of my mind, is, that the loss and inconvenience, which the plaintiff sustained in breaking up, and moving to the defendant's, a distance of sixty miles, is a sufficient consideration to support the promise, to furnish her with a house, and land to cultivate, until she could raise her family. My brothers, however think, that the promise on the part of the defendant, was a mere gratuity, and that an action will not lie, for its breach. The judgment of the Court below must therefore be reversed, pursuant to the agreement of the parties.

Questions:

1. Why did the majority think that the promise was not enforceable?

2. If Antillico's (actually Angelico's) traveling from Marshall County with her 8+ children was not consideration, what was it? After all, Isaac requested it. A relatively recent case quoted Samuel Williston on this issue:

> The difference between a conditional gift and a contract has been famously explained by Samuel Williston as follows:

> If a benevolent man says to a tramp [a hundred years ago when Williston wrote this, *tramp* meant a hobo, as in Charlie Chaplin's *The Tramp* (1915)], "If you go around the corner to the clothing shop there, you may purchase an overcoat on my credit," no reasonable person would understand that the short walk was requested as the consideration for the promise; rather, the understanding would be that in the event of the tramp going to the shop the promisor would make him a gift. Yet the walk to the shop is in its nature capable of being consideration. It is a legal detriment to the tramp to take the walk, and the only reason why the walk is not consideration is because on a reasonable interpretation, it must be held that the walk was not requested as the price of the promise, but was merely a condition of a gratuitous promise.
>
> It is often a difficult question to decide whether words of condition in a promise indicate a request for consideration or state a mere condition in a gratuitous promise.
>
> Although no conclusive test exists for making the determination, an aid in determining which interpretation of the promise is more reasonable is an inquiry into whether the happening of the condition will benefit the promisor. If so, it is a fair inference that the happening was requested as a consideration. On the other hand, if, as in the case of the tramp stated above, the happening of the condition will not benefit the promisor but is obviously for the purpose of enabling the promisee to receive a benefit (a gift), the happening of the event on which the promise is conditional, though brought about by the promisee in reliance on the promise, will not be interpreted as consideration.

3 Samuel Williston & Richard A. Lord, A Treatise on the Law of Contracts § 7:18, at 412-18 (4th ed. 2008).

Fritz v. Fritz, 767 N.W.2d 420 (Table) (2009), at

http://statecasefiles.justia.com/documents/iowa/court-of-appeals/8-997-08-1088-(2009-03-26).pdf?ts=1370462790, at 9–10 (last accessed April 20, 2016).

3. What fact(s) would you add to the tramp hypothetical to give the tramp a right to recover in consensual contract? What fact(s) would you add to *Kirksey* to ensure that Angelico had a right to recover?

PROBLEM 20. If Bob says to Alice, "I will give you this new Jaguar if you will accept it," is Bob's promise enforceable as a contract? Under the theory set out in R2K § 90 (see the note after the next case)?

RICKETTS v. SCOTHORN

Supreme Court of Nebraska (1898)

77 N.W. 365

ERROR from the district court of Lancaster county. Tried below before HOLMES, J. Affirmed.

SULLIVAN, J.

[¶1] In the district court of Lancaster county the plaintiff Katie Scothorn recovered judgment against the defendant Andrew D. Ricketts, as executor of the last will and testament of John C. Ricketts, deceased. The action was based upon a promissory note, of which the following is a copy:

> May the first, 1891. I promise to pay to Katie Scothorn on demand, $2,000, to be at 6 per cent per annum.
>
> J. C. RICKETTS.

[¶2] In the petition the plaintiff alleges that the consideration for the execution of the note was that she should surrender her employment as bookkeeper for Mayer Bros, and cease to work for a living. She also alleges that the note was given to induce her to abandon her occupation, and that, relying on it, and on the annual interest, as a means of support, she gave up the employment in which she was then engaged. These allegations of the petition are denied by the executor. The material facts are undisputed. They are as follows: John O. Ricketts, the maker of the note, was the grandfather of the plaintiff. Early in May,—presumably on the day the note bears date,—he called on her at the store where she was working. What transpired between them is thus described by Mr. Flodene, one of the plaintiff's witnesses:

> A. Well the old gentleman came in there one morning about 9 o'clock,—probably a little before or a little after, but early in the morning,—and he unbuttoned his vest and took out a piece of paper in the shape of a note; that is the way it looked to me; and he says to Miss Scothorn, "I have fixed out something that you have not got to work any more." He says, "None of my grandchildren work and you don't have to."
>
> Q. Where was she?
>
> A. She took the piece of paper and kissed him; and kissed the old gentleman and commenced to cry.

[¶3] It seems Miss Scothorn immediately notified her employer of her intention to quit work and that she did soon after abandon her occupation. The mother of the plaintiff was a witness and testified that she had a conversation with her father, Mr. Ricketts, shortly after the note was executed in which he informed her that he had given the note to the plaintiff to enable her to quit work; that none of his grandchildren worked and he did not think she ought to. For something more than a year the plaintiff was without an occupation;

but in September, 1892, with the consent of her grandfather, and by his assistance, she secured a position as bookkeeper with Messrs. Funke & Ogden. On June 8, 1894, Mr. Ricketts died. He had paid one year's interest on the note, and a short time before his death expressed regret that he had not been able to pay the balance. In the summer or fall of 1892 he stated to his daughter, Mrs. Scothorn, that if he could sell his farm in Ohio he would pay the note out of the proceeds. He at no time repudiated the obligation. We quite agree with counsel for the defendant that upon this evidence there was nothing to submit to the jury, and that a verdict should have been directed peremptorily for one of the parties. The testimony of Flodene and Mrs. Scothorn, taken together, conclusively establishes the fact that the note was not given in consideration of the plaintiff pursuing, or agreeing to pursue, any particular line of conduct. There was no promise on the part of the plaintiff to do or refrain from doing anything. Her right to the money promised in the note was not made to depend upon an abandonment of her employment with Mayer Bros, and future abstention from like service. Mr. Ricketts made no condition, requirement, or request. He exacted no quid pro quo. He gave the note as a gratuity and looked for nothing in return. So far as the evidence discloses, it was his purpose to place the plaintiff in a position of independence where she could work or remain idle as she might choose. The abandonment by Miss Scothorn of her position as bookkeeper was altogether voluntary. It was not an act done in fulfillment of any contract obligation assumed when she accepted the note. The instrument in suit being given without any valuable consideration, was nothing more than a promise to make a gift in the future of the sum of money therein named. Ordinarily, such promises are not enforceable even when put in the form of a promissory note. (*Kirkpatrick v. Taylor*, 43 Ill. 207; *Phelps v. Phelps*, 28 Barb. [N.Y.] 121; *Johnston v. Griest*, 85 Ind. 503; *Fink v. Cox*, 18 Johns. [N.Y.] 145.) But it has often been held that an action on a note given to a church, college, or other like institution, upon the faith of which money has been expended or obligations incurred, could not be successfully defended on the ground of a want of consideration. (*Barnes v. Perine*, 12 N.Y. 18; *Philomath College v. Hartless*, 6 Ore. 158; *Thompson v. Mercer County*, 40 Ill. 379; *Irwin v. Lombard University*, 56 O. St. 9.) In this class of cases the note in suit is nearly always spoken of as a gift or donation, but the decision is generally put on the ground that the expenditure of money or assumption of liability by the donee, on the faith of the promise, constitutes a valuable and sufficient consideration. It seems to us that the true reason is the preclusion of the defendant, under the doctrine of estoppel, to deny the consideration. Such seems to be the view of the matter taken by the supreme court of Iowa in the case of *Simpson Centenary College v. Tuttle*, 71 Ia. 596, where Rothrock, J., speaking for the court, said:

> Where a note, however, is based on a promise to give for the support of the objects referred to, it may still be open to this defense [want of consideration], unless it shall appear that the donee has, prior to any revocation, entered into engagements or made expenditures based on such promise, so that he must suffer loss or injury if the note is not paid. This is based on the equitable principle that, after allowing the donee to incur obligations on the faith that the note would be paid, the donor would be estopped from pleading want of consideration.

[¶4] And in the case of *Reimensnyder v. Gans*, 110 Pa. St. 17, 2 Atl. Rep. 425, which was an action on a note given as a donation to a charitable object, the court said: "The fact is that, as we may see from the case of *Ryerss v. Trustees*, 33 Pa. St. 114, a contract of the kind here involved is enforceable rather by way of estoppel than on the ground of consideration in the original undertaking." It has been held that a note given in expectation of the payee performing certain services, but without any contract binding him to serve, will not support an action. (*Hulse v. Hulse*, 84 Eng. Com. Law 709.) But when the payee changes his position

to his disadvantage, in reliance on the promise, a right of action does arise. (*McClure v. Wilson*, 43 Ill. 356; *Trustees v. Garvey*, 53 Ill. 401.)

[¶5] Under the circumstances of this case is there an equitable estoppel which ought to preclude the defendant from alleging that the note in controversy is lacking in one of the essential elements of a valid contract? We think there is. An estoppel in pais is defined to be "a right arising from acts, admissions, or conduct which have induced a change of position in accordance with the real or apparent intention of the party against whom they are alleged." Mr. Pomeroy has formulated the following definition:

> Equitable estoppel is the effect of the voluntary conduct of a party whereby he is absolutely precluded, both at law and in equity, from asserting rights which might perhaps have otherwise existed, either of property, or contract, or of remedy, as against another person who in good faith relied upon such conduct, and has been led thereby to change his position for the worse, and who on his part acquires some corresponding right either of property, of contract, or of remedy. (2 Pomeroy, Equity Jurisprudence 804.)

[¶6] According to the undisputed proof, as shown by the record before us, the plaintiff was a working girl, holding a position in which she earned a salary of $10 per week. Her grandfather, desiring to put her in a position of independence, gave her the note, accompanying it with the remark that his other grandchildren did not work, and that she would not be obliged to work any longer. In effect, he suggested that she might abandon her employment and rely in the future upon the bounty which he promised. He doubtless desired that she should give up her occupation, but, whether he did or not, it is entirely certain that he contemplated such action on her part as a reasonable and probable consequence of his gift. Having intentionally influenced the plaintiff to alter her position for the worse on the faith of the note being paid when due, it would be grossly inequitable to permit the maker, or his executor, to resist payment on the ground that the promise was given without consideration. The petition charges the elements of an equitable estoppel, and the evidence conclusively establishes them. If errors intervened at the trial they could not have been prejudicial. A verdict for the defendant would be unwarranted.

[¶7] The judgment is right and is

AFFIRMED.

Questions:

1. Was there consideration for grandfather's promise?

2. The purpose and function of the doctrine of equitable estoppel or estoppel in pais is to establish statements of fact at trial. Traditionally, the doctrine applies when a person:

> (1) makes a statement of fact to another,

(2) the other (a) reasonably (b) relies on that statement of fact, and

(3) the reliance results in some detriment.

If the person relying on the statement of fact can prove these three elements, then the person who made the statement may not deny the truth of the statement at trial. A fine example is the case of *Griswold v. Haven*, 25 N.Y. 595 (1862), in which Wright, who ran a storage warehouse, signed a storage receipt for grain purportedly received by Wright from Ford. Wright then introduced Ford to Griswold as a person who wanted to borrow money and to put up grain in the warehouse as collateral. In reliance on Wright's statements, Griswold loaned Ford money and took as collateral an assignment of the grain in Wright's warehouse. When Ford failed to repay, Griswold came to Wright to collect the grain. Wright refused to give Griswold any grain, so Griswold sued Wright for conversion. One element of conversion is the exercise of dominion, if you recall. In defense to Griswold's suit, Wright claimed that he had none of Ford's grain, but then the court imposed equitable estoppel because of Wright's statement in the warehouse receipt that he had received Ford's grain. Wright was thereafter unable to deny in court that he had the grain, and Griswold was relieved of the requirement that he prove exercise of dominion, one element of his conversion case. Which facts support the *Griswold* court's finding that equitable estoppel applied?

3. Equitable estoppel, as traditionally set forth in note 2, does not technically apply to the facts of Ricketts. Why not?

4. Even if equitable estoppel did apply, would it help Katie Scothorn recover?

5. Is Ricketts different from Kirksey?

6. Ms. Scothorn's lost wages during the time she did not work were $520 less interest paid. Should she recover the $520 less interest or the face amount of the note, $2,000? (I'm asking you to speculate here on what the policy should be, but you should look back to the note on contract remedies and pick the one you think is most just.)

Note: Some of the other cases often cited to support promissory estoppel involved gifts promised to charitable organizations, mostly churches and schools. *A* would promise church *B* a gift of $100, for instance, to go toward building a meetinghouse. *B* would also obtain pledges from 49 other parishioners, and in reliance on the pledges, begin building. Once the church had begun building, courts often held that detriment consideration existed for the pledgor's promise, so that the promise was binding. But the promise was clearly given as a gift, not in exchange.

When contracts scholars and courts began to clarify contract doctrines in the second half of the nineteenth century, these consideration cases and others like them emerged as the anomaly that they are. Because no one disagreed with the results in the cases, some new formulation of doctrine was necessary to describe the cases so that they would no longer fall confusingly under the consideration doctrine.

Section 90 was in part the result. Samuel Williston first coined the term *promissory estoppel*, in his 1920 treatise, to describe these cases. He later played a leading role in writing the first Restatement of Contracts (Am Law Inst. 1932), and Williston probably wrote this language:

> A promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise.

RK § 90. The R2K § 90 reformulated slightly by omitting "of a definite and substantial character." It also added a sentence: "The remedy granted for breach may be limited as justice requires." Many thought this extra sentence a suggestion that the remedy be limited to reliance damages.

The language of the section 90s sounds rule-like, but applying it in court would be difficult because the last clause is unclear. What does "injustice" mean? Section 90 seems to describe the requirement of a prima facie case, but should a plaintiff win by showing only hypothetical damage? And anyway, damage probably already happened: would not a showing of detriment (moving costs, lost wages) be enough? And if the words outline a prima facie case for enforcement, then is nothing a defense? Shouldn't the law require the defendant have the burden to show parts of the case that favor the defendant (justice without enforcement) rather than require the plaintiff to negate such arguments in advance?

Some courts resolve these concerns by taking the meaning of section 90's final clause from the jury. It is "a question of law for the court." *Singer v. Lajaunie*, 339 P.3d 277, 283 (Wyo. 2014). This does not resolve the ambiguity. "There is no set criteria as to demonstrating the injustice element . . . ." *Loghry v. Unicover Corp.*, 926 p.2d 706, 711 (Wyo. 1996) (noting that "generally, a court should at least consider . . . the promisee's cost of reliance . . . and whether any other remedy is available to her," and in dicta opining that an at-will employee would not demonstrate the requisite harm because she could be "fired immediately for any reason or no reason").

Questions:

1. Does § 90, as formulated, apply to give a right to recover to the plaintiff in *Storer's Case,* "Antillico" Kirksey, and Katie Scothorn?

2. Under § 90, should Katie Scothorn receive $520 for lost wages or $2,000, what she was promised?

Promissory Estoppel Doctrine Today

We saw signs of promissory estoppel's need early on, such as in *Storer's Case*. But the doctrine evolved slowly. After (i) *Ricketts*'s misuse of equitable estoppel to generate a favorable outcome and (ii) the publication in 1932 of the Restatement (Second)'s section 90, courts and commentators struggled for decades to figure out what the doctrine is and should be. The courts in several states have now begun to settle on the language of the doctrine. Here is a fine statement of the emerging rule, from *Royal Associates v. Concannon*, 490 A.2d 358, 361 (N.J. Super. 1985), with most citations omitted:

> Given an appropriate case, the doctrine of promissory estoppel will be enforced. The four separate factual elements must be proved prima facie to justify application of the doctrine of promissory estoppel: (1) clear and definite promise by the promissor; (2) promise must be made with expectation that promisee will rely thereon; (3) promisee must in fact reasonably rely on the promise, and (4) detriment of a definite and substantial nature must be incurred in reliance on the promise. *E.A. Coronis Assoc. v. M. Gordon Construction Co.*, 90 N.J. Super. 69, 74–80, 216 A.2d 246 (App. Div.1966).

E.A. Coronis Associates is a leading case and was one of the first to formulate this now-common test.

The facts of *Coronis Associates* are these:

> Defendants [Kevin and Thora Concannon] initially occupied their apartment under a two year written lease from May 1, 1971 to April 30, 1973. This lease contained a provision prohibiting pets on the premises. When they moved in there were no dogs on the premises, but they noted that other tenants acquired dogs between 1971 and 1973. In December of 1973 defendants decided to purchase a dog for protection, after noting a number of break-ins in the apartment complex and due to the fact that defendant Kevin Concannon often worked at night leaving his wife home. Before purchasing the dog, however, Mr. Concannon telephoned Mr. Hamilton, the owner and operator of Royal Associates, and requested permission to purchase the dog. Defendant testified that Mr. Hamilton told him that since defendants were such good tenants they could have a dog so long as they took care of it and kept it on a leash. Further, he was told he could keep the dog for as long a period of time as he maintained it, but with no more specific comment as to duration. For the period in excess of ten years that they have had the dog [an Afghan Hound, for which they initially paid $225], defendants received no complaints from management or from other tenants regarding their dog.
>
> Mr. Hamilton testified that defendants were one of four or five tenants to whom he had given what he called “special permission” to have a dog for as long a period of time as they controlled the dog. No permanent term or duration, however, had been established. He admitted he had never seen defendants walking their dog without a leash and did not contest defendants’ assertion that they fully complied with plaintiff’s conditions regarding ownership of the dog.
>
> Through successive two year leases, plaintiff did nothing to enforce the “no pets” provision. On June 2, 1982, however, defendants received a letter addressed to all tenants in the apartments indicating that there was a problem with dogs in the complex and that all tenants would be required to get rid of their dogs. The same letter, however, contained a statement that “only people who had special permission to own a dog will be allowed to stay.” Defendants later learned that dispossess actions had been commenced against other pet owners in the complex, but not against them, and no further word was received concerning the issue until May 1983 when defendants’ lease was renewable. The proposed lease from plaintiff contained not only the “no pets” provision but a Rider wherein all tenants who still owned dogs specifically agreed to get rid of them by a specified date. Believing that this Rider did not apply to them because of their special permission, Mr. Concannon

> went to plaintiff's office in April 1983 and indicated to Mr. Hamilton that he would not sign the Rider in view of their specific agreement to the contrary, i.e., that defendants could keep their dog as long as they controlled it. Plaintiff and defendants then signed the lease without the Rider, Mr. Hamilton commenting that since the "no pets" provision was in the lease and defendants had been informed of his change in policy, the absence of the Rider would make no difference.

490 A.2d at 359–60. Then Mr. Hamilton for his company served a Notice to Quit on the Concannons and began an eviction action. The trial court ordered eviction, and the Concannons appealed. After noting earlier decisions arguing that each lease was only a contract for a limited time, the court sang music to pet-lovers everywhere: "[These cases] fail to recognize the attachment that a tenant may feel towards a pet, and the fact that an apartment, whether occupied by a tenant under successive leases or on a month-to-month arrangement, becomes the tenant's home." *Id.* at 360. And indeed, the Concannons were very fond of their dog, which had lived with them for over ten years. *Id.* at 362.

The court concluded that the Concannons had "the right to enforce their separate agreement in law or raise plaintiff's estoppel in equity." The court noted that everyone knows "that a dog's life-span is several times longer than [the] 2-year period" of Royal's leases. Since the dog's presence was the only reason to evict the Concannons, the court ordered entry of a judgment dismissing the eviction action. *Id.*

Questions:

1. The court relied completely on, but barely analyzed, promissory estoppel doctrine in its opinion. But you can do a much better analysis. The court said that four things must be shown to make a promise binding under promissory estoppel doctrine. Make a list of the four elements. Under each element, write out the factual evidence that proves each one. Your professor may ask in class what you have written.

2. What is the difference between elements (2) and (3)? Why is (2) important to the test? Why is (3) important?

3. What remedy did the court give for promissory estoppel in this case?

The next two cases are only excerpts of fact patterns. I'd like you to do the same thing for these that you did for *Coronis Associates*: write out the elements of the test and then list the facts as evidence and perhaps other arguments you would make under each element.

John GROUSE v. GROUP HEALTH PLAN, INC.

Supreme Court of Minnesota (1981)

306 N.W.2d 114

OTIS, Justice.

[¶1] Plaintiff John Grouse appeals from a judgment in favor of Group Health Plan, Inc., in this action for damages resulting from repudiation of an employment offer. The narrow issue raised is whether the trial court erred by concluding that Grouse's complaint fails to state a claim upon which relief can be granted. In our view, the doctrine of promissory estoppel entitles Grouse to recover and we, therefore, reverse and remand for a new trial on the issue of damages.

[¶2] The facts relevant to this appeal are essentially undisputed. Grouse, a 1974 graduate of the University of Minnesota School of Pharmacy, was employed in 1975 as a retail pharmacist at Richter Drug in Minneapolis. He worked approximately 41 hours per week earning $7 per hour. Grouse desired employment in a hospital or clinical setting, however, because of the work environment and the increased compensation and benefits. In the summer of 1975 he was advised by the Health Sciences Placement office at the University that Group Health was seeking a pharmacist.

[¶3] Grouse called Group Health and was told to come in and fill out an application. He did so in September and was, at that time, interviewed by Cyrus Elliott, Group Health's Chief Pharmacist. Approximately 2 weeks later, Elliott contacted Grouse and asked him to come in for an interview with Donald Shoberg, Group Health's General Manager. Shoberg explained company policies and procedures as well as salary and benefits. Following this meeting Grouse again spoke with Elliott who told him to be patient, that it was necessary to interview recent graduates before making an offer.

[¶4] On December 4, 1975, Elliott telephoned Grouse at Richter Drug and offered him a position as a pharmacist at Group Health's St. Louis Park Clinic. Grouse accepted but informed Elliott that 2 week's notice to Richter Drug would be necessary. That afternoon Grouse received an offer from a Veteran's Administration Hospital in Virginia which he declined because of Group Health's offer. Elliott called back to confirm that Grouse had resigned.

[¶5] Sometime in the next few days Elliott mentioned to Shoberg that he had hired, or was thinking of hiring, Grouse. Shoberg told him that company hiring requirements included a favorable written reference, a background check, and approval of the general manager. Elliott contacted two faculty members at the School of Pharmacy who declined to give references. He also contacted an internship employer and several pharmacies where Grouse had done relief work. Their responses were that they had not had enough exposure to Grouse's work to form a judgment as to his capabilities. Elliott did not contact Richter because Grouse's application requested that he not be contacted. Because Elliott was unable to supply a favorable reference for Grouse, Shoberg hired another person to fill the position.

[¶6] On December 15, 1975 Grouse called Group Health and reported that he was free to begin work. Elliott informed Grouse that someone else had been hired. Grouse complained to the director of Group Health who apologized but took no other action. Grouse experienced difficulty regaining full time

employment and suffered wage loss as a result. He commenced this suit to recover damages; the trial judge found that he had not stated an actionable claim.

Question: Assuming promissory estoppel applies, what should be Grouse's remedy? Here is what the court said: "[T]he measure of damages is not so much what he would have earned from respondent as what he lost in quitting the job he held and in declining at least one other offer of employment elsewhere." What would you call damages for "what he would have earned from respondent"? What would you call damages for "what he lost in quitting . . . and in declining"?

G.D. HOLDINGS, INC. v. H.D.H. LAND & TIMBER, L.P.

Twelfth Court of Appeals of Texas (Tyler (2013))

407 S.W.3d 856

JAMES T. WORTHEN, Chief Justice.

[¶1] G.D. Holdings, Inc. (GDH) appeals the trial court's judgment in favor of H.D.H. Land & Timber, L.P. (HDH). In one issue, GDH contends that the trial court erred because there is no evidence, or insufficient evidence, to support the trial court's contract and promissory estoppel findings. We affirm.

BACKGROUND

[¶2] On May 29, 2007, John D. Harvey, as general partner of HDH, and Dsirajlal Babaria, as president of GDH, signed a $300,000.00 real estate contract. John Griffin, an attorney, prepared the contract, which provided that HDH would sell, and GDH would purchase, nine acres of land in Joaquin, Shelby County, Texas. The contract also included the following clause:

> Buyer shall pay seller for dozer work and cleanup of property if transaction does not close.

[¶3] Harvey signed the contract, which was then sent to Babaria. However, Babaria struck out the above clause, initialed it, and returned it to Griffin. When Griffin notified Harvey that Babaria struck out the clause, Harvey refused to initial the change. Harvey stated that Babaria demanded the property be cleared before the sale closed. He testified that the cost of clearing the property was the reason Babaria deposited $30,000.00 with Griffin as earnest money. Babaria was unable to obtain financing for the purchase of the nine acres and the sale did not close. When Babaria requested that Griffin return the earnest money, Harvey refused to consent because the property had been cleared and the contractor paid.

[¶4] GDH sued HDH for the return of the earnest money. HDH filed an original answer and counterclaim, alleging that the parties had a valid written contract, that GDH failed to close the sale without cause or justification, and that HDH was entitled to cancel the contract and receive the earnest money as liquidated damages. In the alternative, HDH alleged that it was entitled to recover the monies because it relied upon GDH's representations. At some point, Griffin tendered the earnest money into the registry of the court.

[¶5] Following a bench trial, the trial court signed a judgment in favor of HDH, awarding it $27,390.00 in damages with interest at the rate of 5% per annum, and $7,500.00 in attorney's fees. At GDH's request, the trial court filed findings of fact and conclusions of law. This appeal followed.

[In the first part of the opinion, the court determined that no contract formed.]

PROMISSORY ESTOPPEL

[¶6] GDH also contends in its sole issue that HDH did not meet the requirements to recover under the theory of promissory estoppel. * * * *

Findings of Fact and Conclusions of Law

[¶7] The trial court made the following findings of fact and conclusions of law regarding HDH's recovery of damages based upon promissory estoppel:

FINDINGS OF FACT

> (9) [GDH], or [its] officers, employees, agents or associates, represented to [HDH] that [its] purchase of the property was contingent upon [HDH] obtaining an acceptable survey and clearing and leveling the property prior to closing.
>
> (10) Relying upon the representations of [GDH], or [its] officers, employees, agents or associates, [HDH] obtained a survey of the property at a cost of $1,500.00.
>
> (11) Relying upon the representations of [GDH], or [its] officers, employees, agents or associates, [HDH] cleared and leveled the property at a cost of $25,890.00.
>
> (12) [HDH] would not have obtained the survey or cleared and leveled the property but for [GDH's] representation that the same were necessary for the sale of the property to take place and that, if the sale did not take place, [HDH] would be reimbursed for the cost.
>
> (13) Neither the survey nor the clearing and leveling work done by [HDH] increased the value or marketability of the property.

CONCLUSIONS OF LAW

> (4) [HDH] is entitled to recover the amounts expended by it for surveying, clearing and leveling in reliance upon [GDH's] requests and representations.

Analysis

[¶9] At trial, Harvey testified that while he and Babaria were negotiating the terms of the contract, Babaria told him that he wanted the nine acres cleared before closing the sale. He stated that Babaria said he was not in a position to clear the land himself, and requested that Harvey clear the property prior to closing. Harvey testified that, during the negotiations, he and Babaria met on the site of the nine acres prior to Griffin's preparation of the written contract. According to Harvey, he arranged for Johnny Alford with North Toledo Bend Contractors, whom he hired to clear the property, to be at his meeting with Babaria. Harvey stated that Alford met Babaria before unloading his bulldozer to begin clearing the property. Harvey also testified that he told Babaria that clearing the property would cost approximately $30,000.00, and informed Babaria that this amount should be the earnest money for the contract. It is undisputed that Babaria tendered $30,000.00 in earnest money to Griffin, the closing agent for the transaction. Harvey also testified that Alford completed clearing the property in about two weeks. He stated that the clearing was substantially completed when he was informed by Griffin that Babaria struck out the clause in the real estate contract, refusing to pay for the clearing if the sale did not close. According to Harvey, he paid Alford and a subcontractor for clearing the property.

[¶10] Babaria denied that he spoke with Harvey regarding his need for the nine acres to be cleared prior to closing the sale. He also denied agreeing to pay for the clearing. Babaria testified that he did not remember seeing Alford. He stated that he believed the clearing began prior to his meeting with Harvey at the property site. Babaria based his belief on the fact that he saw cut logs on the property at that time. In rebuttal, Harvey testified that he had had timber cut off the property approximately six months earlier, and that Babaria saw the remains of that operation.

[¶11] * * * * Here, Babaria and Harvey testified to two different versions of the facts. The trial court believed Harvey, and as the trier of fact, it was within its province to do so in resolving conflicts in the evidence and judging the credibility and the weight of the witness's testimony.

Questions:

1. You have almost the whole opinion here, less the court's rule statement and conclusion. Do these facts—as they were believed by the trial court—warrant relief for promissory estoppel? What in particular was evidence of a promise?

2. Why do you think the trial court believed Harvey instead of Babaria?

3. Courts sometimes say that promissory estoppel does not apply to a promise covered by a contract. Why do you think that might be?

4. What remedy should the court order in this case?

B. Unjust Enrichment

Unjust Enrichment in its original, 1500s form comprised several, special species of assumpsit called *indebitatus assumpsit*. The phrase means literally "has assumed debt." The word *debt* here was key. In these cases, the common law courts decided that plaintiffs could bring writ of debt cases using a writ of assumpsit. Remember that the writ of debt was property-related. The point of the debt writ was to show that property had change hands by law and should be handed over to the new owner. If debt cases could be brought in assumpsit, then as long as the property-related debt theory was satisfied, the plaintiff should have a remedy in assumpsit.

Thus, we have a case like *Ireland v. Higgins* (Queen's Bench 1589), in which the plaintiff declared in an assumpsit case that the plaintiff lost his greyhound dog but that the defendant had found it and promised to deliver it to the plaintiff. The issue before the court was whether a greyhound was a wild dog or not, because no one could own a wild dog. But once the court decided that a greyhound could be tame, the court ruled for the plaintiff.

Notice that in *Ireland* there is no consideration for the defendant's promise. Someone raised that argument in a case just two years earlier, *Whorwood v. Gybbons* (Queen's Bench 1587), but the court decided, "[I]nsomuch as the [promise] was made by [Gybbons,] by whom the debt is due, that it is a good consideration, and that it is a common course in action upon the case against him by whom the debt is due, to [plead] without any words in consideration." The point was that the debt was due, and later in *Ireland* the defendant possessed the plaintiff's dog. If the plaintiff proved indebtedness, that was enough in these cases.

Not all the judges at the time thought this was a good idea. The writs were not supposed to overlap. The Queen's Bench was on the forefront of the innovation, and the Common Pleas court (just across Westminster Hall) was against it. Records from the time report the disagreement. In *Edmunds v. Barre* (Queen's Bench 1573), Edwards brought a case against Margaret Barre, administratrix of the estate of John Sidwell, alleging that Sidwell borrowed 40 shillings from Edwards and never repaid it but that Barre "has undertaken to pay" Edwards the 40 shillings. At trial, the plaintiff proved only that he lent Sidwell the 40 shillings. Under estate law of the time, the administratrix of an estate kept what was left of the estate after debts were paid. The plaintiff never showed a promise and of course never showed consideration for Barre's promise.

But Sidwell's borrowing 40 shillings was enough to bind his estate in the hands of Barre, so Justice Wray of the Queen's Bench said, "[I]f it be so [that] the plaintiff lent the said sum, then you ought to find for the plaintiff, because the debt is an undertaking in law." That's all you need, the debt. Edwards won without even showing that Barre promised.

The reporter of this case, Dalison, then noted that the Common Pleas disagreed and would have made Edwards prove the promise:

> But note that it was said that this is by reason of the custom of the Queen's Bench, because in the Common Pleas he would have to prove the undertaking, and it is not sufficient to prove the debt alone, because for the debt he should have an action for debt and not an

> action on the case, because the common law will not suffer a man to have an action on the case where he could have another remedy, and also, for * * * * the debtor if he [the creditor] was without [a sealed writing] could [wage] his law, and by an action on the case would be prevented from doing so, which is [not right]. And therefore in the Common Pleas he must prove the undertaking.

Dalison 104. And yet, neither court would have required Edwards to show that Barre's promise was given in plausible exchange. Still, the Common Pleas resisted the full incorporation of debt cases into assumpsit. The Queen's Bench was fine with a jury's hearing all these cases, but the Common Pleas wanted to preserve wager of law.

For a long time, the Common Pleas could do nothing about the Queen's Bench practice. Plaintiffs would simply bring their cases in the Queen's Bench rather than the Common Pleas. Defendants could appeal a Queen's Bench judgment only to Parliament, which was too expensive, and these cases were probably not worth Parliament's time. Then in 1585 Queen Elizabeth signed a law allowing the Common Pleas and the Court of Exchequer (the third national common-law court) to sit together as the "Exchequer Chamber" to review appeals from Queen's Bench judgments. There were more Common Pleas judges than Exchequer judges, so the Common Pleas views held sway in the new court. The Exchequer Chamber, in order to do away with the Queen's Bench practice, reversed the Common Pleas' own prior practice of allowing assumpsit in debt cases when a subsequent promise was alleged and also proved. Instead, the Common Pleas judges in the Exchequer Chamber held instead that no debt cases at all could be brought in assumpsit. This position continued in the Exchequer Chamber until all the judges on the Common Pleas who held the conservative view either died, were replaced, or changed their minds (probably only one changed his mind). By 1605 all the judges had come around to the (now) King's Bench view. Because the King's Bench view triumphed, the class of cases in assumpsit that escaped consideration's reach and also escaped the requirement of an actual promise increased and expanded in their own way, until they became today's unjust enrichment cases, in which neither promise nor consideration is required to be alleged.

In the sixteenth century, only a *debt* needed to be pleaded and proved. We do not call it *debt* today, or *indebitatus assumpsit*. We have since had the benefit of the *Restatement of Restitution* (Am. Law Inst. 1937) and later the *Restatement (Third) of Restitution and Unjust Enrichment* (Am. Law Inst. 2011), and restitution or unjust enrichment is what the action is now called. "Unjust enrichment" is not the name of a contract remedy and so is a less confusing name. But the coverage of the doctrine has not changed much, just the name, as you'll learn from the next few cases in this section.

So, you can see that we have a class of cases in which breach of contract is remedied but in which neither promise nor consideration need be pleaded or proved, and that this came about as a result of a jurisdictional squabble between courts and one court's preference for a jury trial over wager of law.

In re the Marriage of Margrethe May PYEATTE v. H. Charles PYEATTE[****]

Court of Appeals of Arizona, Division 1, Department B

661 P.2d 196, Oct. 28, 1982

OPINION

CORCORAN, Judge.

[¶1] This is an appeal by the husband from an award of $23,000 in favor of the wife as ordered in a decree of dissolution. Two issues are before us: (1) The validity of an oral agreement entered into by the husband and wife during the marriage, whereby each spouse agreed to provide in turn the sole support for the marriage while the other spouse was obtaining further education; and, (2) whether the wife is entitled to restitution for benefits she provided for her husband's educational support in a dissolution action which follows closely upon the husband's graduation and admission to the Bar. The word "agreement" is used as a term of reference for the stated understanding between the husband and wife and not as a legal conclusion that the agreement is enforceable at law as a contract.

[¶2] The husband, H. Charles Pyeatte (appellant), and the wife, Margrethe May Pyeatte (appellee), were married in Tucson on December 27, 1972. At the time of the marriage both had received bachelors degrees. Appellee was coordinator of the surgical technical program at Pima College. Appellant was one of her students. In early 1974, the parties had discussions and reached an agreement concerning postgraduate education for both of them.

[¶3] Appellee testified that they agreed she "would put him through three years of law school without his having to work, and when he finished, he would put [her] through for [her] masters degree without [her] having to work."

[¶4] Appellant concedes the existence of an agreement. Although there was a claim by appellant that his agreement with appellee was qualified by certain contingencies, there is substantial evidence in the record to support the findings made by the trial court after the trial:

> The Court is of the opinion that there was a definite agreement that the respondent [appellant] would pay for the support of petitioner [appellee] while the petitioner [appellee] obtained her master's degree without her having to work. The Court is further of the opinion that there was no contingency expressed or implied that this would not be carried out or enforced in the event of a divorce. Petitioner [appellee] carried out her part of the agreement in supporting the respondent [appellant] while he obtained his law degree.

[¶5] Appellant attended law school in Tucson, Arizona, from 1974 until his graduation. He was admitted to the State Bar shortly thereafter.

[****] Thanks to Charles Calleros for advocating the teaching of this case.

[¶6] During appellant's first two years of law school appellee supported herself and appellant on the salary she earned at Pima College. During the last year, appellee lost her job, whereupon savings were used to support the couple. Although each spouse contributed to the savings, a significant amount was furnished by appellee.

[¶7] After appellant's admission to the Bar, the couple moved to Prescott, Arizona, where appellant was employed by a law firm. Both parties realized that appellant's salary would not be sufficient to support the marriage and pay for appellee's education for a masters degree simultaneously. Appellee then agreed to defer her plans for a year or two until her husband got started in his legal career. In the meantime, she obtained part-time employment as a teacher.

[¶8] In April, 1978, appellant told appellee that he no longer wanted to be married to her, and in June of 1978, she filed a petition for dissolution. Trial was had in March of 1979, and a decree of dissolution was granted. At the time of the trial, there was little community property and no dispute as to division of any community or separate property. Spousal maintenance was neither sought by nor granted to appellee.

[¶9] The trial court determined that there was an agreement between the parties, that appellee fully performed her part of that agreement, that appellant had not performed his part of the agreement, and that appellee had been damaged thereby.

[¶10] Based on appellee's expert testimony on the cost of furthering her education, in accordance with the agreement, the trial court awarded judgment of $23,000 against appellant as damages for breach of contract, with additional directions that the judgment be payable through the court clerk on a quarterly basis in a sum of not less than ten percent of appellant's net quarterly income.

[¶11] The trial court directed appellant to use his best efforts to produce income and to keep accurate records of his income-producing activities, which records would be available to appellee upon request but not more frequently than on a quarterly basis. The court also retained jurisdiction of the case for the purpose of supervising the administration of the payment of the judgment and the keeping of records by the appellant. Appellant filed a timely notice of appeal from the judgment.

[¶12] On appeal, appellant argues that the agreement did not rise to the level of a binding contract because, among other things, the terms thereof were not definite and could not be legally enforced.

[¶13] Appellee advances three theories as grounds upon which the trial court's award should be upheld: [contract, community property, and unjust enrichment]. * * * *

[The court concluded that no contract existed because the agreements lacked definiteness or specificity, a topic handled in Chapter 9.]

[The court also decided in an omitted part that community property law did not support a recovery.]

The Restitution Claim

[¶14] Appellee's last contention is that the trial court's award should be affirmed as an equitable award of restitution on the basis of unjust enrichment. She argues that appellant's education, which she subsidized and which he obtained through the exhaustion of community assets constitutes a benefit for which he must,

in equity, make restitution. This narrow equitable issue is one of first impression in this court. We first addressed the broad outlines of the problem in *Wisner*, but in the context of significantly different facts and legal theories. Our recognition of the disparate considerations involved in a case such as the one before us led us to limit our holding in *Wisner* to its facts. 129 Ariz. at 341, 631 P.2d at 123.

[¶15] Restitution is available to a party to an agreement where he performs services for the other believing that there is a binding contract. * * * *

[¶16] In order to be granted restitution, appellee must demonstrate that appellant received a benefit, that by receipt of that benefit he was unjustly enriched at her expense, and that the circumstances were such that in good conscience appellant should make compensation. *John A. Artukovich & Sons v. Reliance Truck Co.*, 126 Ariz. 246, 614 P.2d 327 (1980); Restatement of Restitution § 1 at 13 (1937). In *Artukovich*, the Supreme Court discussed unjust enrichment.

> Contracts implied-in-law or quasi-contracts, also called constructive contracts, are inferred by the law as a matter of reason and justice from the acts and conduct of the parties and circumstances surrounding the transactions ... and are imposed for the purpose of bringing about justice without reference to the intentions of the parties....
>
> Restatement of Restitution § 1 provides, "A person who has been unjustly enriched at the expense of another is required to make restitution to the other." Comment (a) to that section notes that a person is enriched if he received a benefit and is unjustly enriched if retention of that benefit would be unjust. Comment (b) defines a benefit as being any form of advantage. . .
>
> Unjust enrichment does not depend upon the existence of a valid contract,
>
> ... nor is it necessary that plaintiff suffer a loss corresponding to the defendant's gain for there to be valid claim for an unjust enrichment...

126 Ariz. at 248, 614 P.2d at 329.

[¶17] A benefit may be any type of advantage, including that which saves the recipient from any loss or expense. See *Artukovich, supra*. Appellee's support of appellant during his period of schooling clearly constituted a benefit to appellant. Absent appellee's support, appellant may not have attended law school, may have been forced to prolong his education because of intermittent periods of gainful employment, or may have gone deeply into debt. Relieved of the necessity of supporting himself, he was able to devote full time and attention to his education.

[¶18] The mere fact that one party confers a benefit on another, however, is not of itself sufficient to require the other to make restitution. Retention of the benefit must be unjust.

[¶19] Historically, restitution for the value of services rendered has been available upon either an "implied-in-fact" contract or upon quasi-contractual grounds. D. Dobbs, Remedies § 4.2 at 237 (1973); 1 Williston, Contracts § 3 and 3A at 19-15 (3d ed. 1957). An implied-in-fact contract is a true contract, differing from an express contract only insofar as it is proved by circumstantial evidence rather than by express written or oral terms. *United States v. O. Frank Heinz Construction Co.*, 300 F.Supp. 396 (D.C.Ill.1969); *Plumbing*

Shop, Inc. v. Pitts, 67 Wash.2d 514, 408 P.2d 382, 383 (1965). In contrast, a quasi-contract is not a contract at all, but a duty imposed in equity upon a party to repay another to prevent his own unjust enrichment. The intention of the parties to bind themselves contractually in such a case is irrelevant. 1 Williston, Contracts § 3A at 12-15 (3d ed. 1957). * * * *

[¶20] Restitution is nevertheless available in quasi-contract absent any showing of mutual assent. While a quasi-contractual obligation may be imposed without regard to the intent of the parties, such an obligation will be imposed only if the circumstances are such that it would be unjust to allow retention of the benefit without compensating the one who conferred it. See Williston, *supra*. One circumstance under which a duty to compensate will be imposed is when there was an expectation of payment or compensation for services at the time they were rendered.

> [A]n obligation to pay, ordinarily, will not be implied in fact or by law if it is clear that there was indeed no expectation of payment, that a gratuity was intended to be conferred, that the benefit was conferred officiously, or that the question of payment was left to the unfettered discretion of the recipient.

Osborn v. Boeing Airplane Co., 309 F.2d at 102.

[¶21] Although we found that the spousal agreement failed to meet the requirements of an enforceable contract, the agreement still has importance in considering appellee's claim for unjust enrichment because it both evidences appellee's expectation of compensation and the circumstances which make it unjust to allow appellant to retain the benefits of her extraordinary efforts.

[¶22] We next address the question of whether restitution on the basis of unjust enrichment is appropriate in the context of the marital relationship. No authority is cited to the court in support of the proposition that restitution as a matter of law is inappropriate in a dissolution proceeding. In *Wisner*, we observed that "[i]n our opinion, unjust enrichment, as a legal concept, is not properly applied in the setting of a marital relationship." 129 Ariz. at 341, 631 P.2d at 123. Our observation was directed to the wife's claim in that case for restitution for the value of her homemaking services during the couple's 15-year marriage and for the couple's reduced income during the husband's lengthy training period. Where both spouses perform the usual and incidental activities of the marital relationship, upon dissolution there can be no restitution for performance of these activities. *Ibid*. Where, however, the facts demonstrate an agreement between the spouses and an extraordinary or unilateral effort by one spouse which inures solely to the benefit of the other by the time of dissolution, the remedy of restitution is appropriate.

[¶23] Arizona courts have traditionally utilized the equitable restitutionary device of the constructive trust to prevent unjust enrichment between spouses upon dissolution when there is property to which such a trust may attach. * * * * We see no reason in law or equity why restitution should not be available in an appropriate circumstance to prevent the unjust enrichment of a spouse when a constructive trust is not available, as here, when no property exists. We analogize the two restitutionary devices solely to the extent of illustrating their common essence—prevention of the unjust enrichment of one spouse at the expense of the other.

[¶24] A number of jurisdictions have addressed the issue of restitution in the context of the marital relationship. The cases which have dealt with the issue involve two factual patterns: (1) The first group consists of those cases in which the couples had accumulated substantial marital assets over a period of

time from which assets the wife received large awards of property, maintenance and child support. The courts have refused to apply the theory of restitution on the basis of unjust enrichment in each of these cases. (2) The second group consists of those cases in which the parties are divorced soon after the student spouse receives his degree or license and there is little or no marital property from which to order any award to the working spouse.

[¶25] In the first group the courts have consistently refused to find a property interest in the husband's education, degree, license or earning capacity or to order restitution in favor of the wife. Because restitution is a matter of equity, the circumstances of these cases preclude at the outset any basis for a finding of inequitable circumstances sufficient to support restitution inasmuch as the wife in each case had received substantial awards of the marital assets and was seeking, in addition to those assets, a property interest in the husband's education, degree, license or earning capacity. Because the property award itself is largely the product of the education, degree, license or earning capacity in which the wife sought a monetary interest, the courts hold that the wife realized her "investment" in the husband's education by having received the benefits of his increased earning capacity during marriage and by receipt of an award of property upon its dissolution. * * * *

[¶26] The second group presents the more difficult problem of the "working spouse" claiming entitlement to an equitable recovery where there is little or no marital property to divide and therefore the conventional remedies of property division or spousal maintenance are unavailable. The emerging consensus among those jurisdictions faced with the issue in this factual context is that restitution to the working spouse is appropriate to prevent the unjust enrichment of the student spouse. *See Inman v. Inman*, 578 S.W.2d 266 (Ky.1979); *DeLa Rosa v. DeLa Rosa*, 309 N.W.2d 755 (Minn.1981); *Hubbard v. Hubbard*, 603 P.2d 747 (Okl.1979); *Lundberg v. Lundberg*, 107 Wis.2d 1, 318 N.W.2d 918 (1982); *Contra, In re Marriage of Graham*, 194 Colo. 429, 574 P.2d 75 (1978).

[¶27] Although in *Wisner* we dealt with the first group described above; i.e., a marital community with substantial accumulated assets, we anticipated the second type of case in which (1) the community estate is consumed by the education of the husband which was obtained in substantial measure by the efforts and sacrifices of his wife; (2) the working wife is not entitled to spousal maintenance, having demonstrated an ability to support not only herself but her husband as well; and (3) the divorce follows closely upon the husband's completion of his education before the community realizes any benefit from that education and before the working spouse is able to further her own education and thus increase her own earning capacity. * * * *

[¶28] The Oklahoma Supreme Court in *Hubbard* held that, while a degree is not "property" subject to valuation and division upon dissolution, equitable relief is not thereby precluded. The court then ordered that the wife be reimbursed in quasi-contract for the amounts she expended during the 12 years in which she supported her husband while he obtained his medical training.

> While it is true that Dr. Hubbard's license to practice medicine is his own to do with as he pleases, it is nonetheless also true that Ms. Hubbard has an equitable claim to repayment for the investment she made in his education and training. To hold otherwise would result in the unjust enrichment of Dr. Hubbard. He would leave the marriage with an earning capacity increased by $250,000 which was obtained in substantial measure through the efforts and sacrifices of his wife. She on the other hand would leave the marriage without

> either a return on her investment or an earning capacity similarly increased through joint efforts ... All the resources of the marriage had been dissipated on Dr. Hubbard's education. There is no reason in law or equity why Dr. Hubbard should retain the only valuable asset which was accumulated through joint efforts ... free of claims for reimbursement by his wife.

603 P.2d at 750.

[¶29] The Minnesota Supreme Court in *De La Rosa* similarly affirmed an award of restitution to the wife for the financial support she provided her husband while he attended medical school, in a dissolution which occurred shortly after the husband's graduation. * * * *

[¶30] The record shows that the appellee conferred benefits on appellant — financial subsidization of appellant's legal education — with the agreement and expectation that she would be compensated therefor by his reciprocal efforts after his graduation and admission to the Bar. Appellant has left the marriage with the only valuable asset acquired during the marriage — his legal education and qualification to practice law. It would be inequitable to allow appellant to retain this benefit without making restitution to appellee. However, we need not decide what limits or standards would apply in the absence of an agreement. Commentators have discerned in various statutory enactments and the developing case law a renewed and expanded recognition of marriage's economic underpinnings. See Comment, *The Interest of the Community in a Professional Education*, 10 Calif.W.L.Rev. 590 (1974); Erickson, *Spousal Support Toward the Realization of Educational Goals: How the Law Can Ensure Reciprocity*, 1978 Wis.L.Rev. 947. By our decision herein, we reject the view that the economic element necessarily inherent in the marital institution (and particularly apparent in its dissolution) requires us to treat marriage as a strictly financial undertaking upon the dissolution of which each party will be fully compensated for the investment of his various contributions. When the parties have been married for a number of years, the courts cannot and will not strike a balance regarding the contributions of each to the marriage and then translate that into a monetary award. To do so would diminish the individual personalities of the husband and wife to economic entities and reduce the institution of marriage to that of a closely held corporation.

The Measure of Recovery

[31] Generally, where claims are made by the working spouse against the student spouse, the trial court in each case must make specific findings as to whether the education, degree or license acquired by the student spouse during marriage involved an unjust enrichment of that spouse, the value of the benefit, and the amount that should be paid to the working spouse. A variety of methods of computing the unjust enrichment may be employed in ascertaining the working spouse's compensable interest in the attainment of the student spouse's education, degree or license.

[¶32] The award to appellee should be limited to the financial contribution by appellee for appellant's living expenses and direct educational expenses. *See De La Rosa v. De La Rosa*, 309 N.W.2d 755.

[¶33] Under the agreement between the parties, the anticipated benefit to appellee may involve a monetary benefit in a lesser amount than the benefit conferred by appellee on appellant. In that event, the award to appellee should be limited to the amount of the anticipated benefit to appellee. Appellee should not recover more than the benefit of her bargain. Restatement of Restitution, § 107, Comment b, at 449 (1937).

[¶34] Appellant further objects to the judgment of $23,000 against him on the ground that it directs the payment on terms over a period of time. The terms of payment were of benefit only to appellant. If he wanted to pay the judgment in a lump sum, he certainly could do so. In any event, the trial court, in entering an equitable judgment for money, has the authority to order that it be paid in periodic payments plus interest through the clerk of the court in a certain percentage of appellant's net income, and that appellee have the right to review his records to determine the accuracy of the net income calculations.

[¶35] The relief granted to appellee is equitable in nature. The rule regarding equitable awards is set forth in *Mason v. Ellison*, 63 Ariz. 196, 160 P.2d 326 (1945) in which the Arizona supreme court stated:

> In an equity case the court "... adapts its relief and molds its decrees to satisfy the requirements of the case and to conserve the equities of the parties litigant. The court has such plenary power since its purpose is the accomplishment of justice amid all of the vicissitudes and intricacies of life...."

63 Ariz. at 203, 160 P.2d at 329 (quoting 19 Am.Jur. Equity § 123 at 123-24 (1939)). * * *

[¶36] The nature of equity is individual justice. Since the benefit bestowed upon appellant by appellee was periodic in nature and dependent on her income, we find no abuse of the equity power of the court in awarding appellee periodic payments, especially where she can use them periodically to pursue her own education. By our affirmance of an instalment method of payment in this case, we do not mean to promulgate a rule that will uniformly govern all awards in subsequent cases of that nature. Each will, by virtue of the equitable nature of the claim, require relief tailored to the facts and circumstances of the individuals. *De La Rosa v. De La Rosa*, 309 N.W.2d at 759, n. 11.

[¶37] The portion of the judgment in the amount of $23,000 is reversed and remanded for proceedings in accordance with this opinion.

Questions:

1. Does the unjust enrichment law established or relied on this case require that the plaintiff show a detriment to the plaintiff? Would unjust enrichment warrant an award of restitution on the facts of Ricketts v. Scothorn? How about Edmunds v. Barre?

2. Why did the court reverse the damage award, do you think?

3. Recovery in unjust enrichment and recovery in contract often overlap. Can you think of any fact patterns in contract cases we have studied that would also support recover in unjust enrichment?

4. William Murray (commonly known as Lord Mansfield), Chief Justice of the King's Bench from 1756-88, said this of the cause of action we are considering:

> This kind of equitable action, to recover back money, which ought not in justice to be kept, is very beneficial, and therefore much encouraged. It lies only for money which *ex aequo et bono*, the defendant ought to refund . . . . [I]t lies for money paid by mistake, or upon a consideration which happens to fail, or for money got through . . . extortion, or oppression, or an undue advantage taken of the plaintiff's situation, contrary to laws made for the protection of persons under those circumstances. In one word, the gist of this kind of action is, that the defendant, upon the circumstances of the case, is obliged by the ties of natural justice to refund the money.

Moses v. Macferlan, 97 Eng. Rep. 676, 680-81 (K.B. 1760). It wasn't "one word" (it was twenty-one), but the rest of Mansfield's statement is accurate.

Consider some examples of the doctrine applied:

PROBLEM 21. In *Cotnam v. Wisdom*, 104 S.W. 164 (Ark. 1907), Harrison (H) was thrown from a street car and received injuries which rendered him unconscious. He never regained consciousness. Some spectators fetched two doctors, Wisdom and another, who performed a difficult operation to save Harrison's life, but they were unsuccessful, and Harrison died without regaining consciousness.

The doctors sued Harrison's estate for their services in trying to save Harrison's life. At trial, the judge instructed the jury: "If you find . . . that plaintiffs rendered professional services as physicians and surgeons to H, in a sudden emergency . . . , then you are instructed that plaintiffs are entitled to recover from the estate . . . such sum as . . . is a reasonable compensation for the services rendered." The jury found for the plaintiffs, and Cotnam, administrator of Harrison's estate, appealed. The Supreme Court of Arkansas affirmed but limited the rule to licensed medical persons. Is this justifiable? Should it matter that Harrison was never conscious?

PROBLEM 22. In *The Incredibles*, Mr. Incredible discovers a man about to commit suicide by jumping from a building. In an incredible burst of speed and jumping and grabbing ability, Mr. Incredible catches the man mid-fall and shelters him as they together smash through a skyscraper window and roll to a stop. The man who jumped sued Mr. Incredible for the harm done to him by the rescue. In a news report, Mr. Incredible says to the man, "I saved your life," and the victim says back to him, "You didn't save my life! You ruined my death; that's what you did." If Harrison had jumped from the street car in a suicide attempt, would we have the same result in *Cotnam*? In such a case, autonomy and the policies supporting *Cotnam* conflict. Make your best arguments.

PROBLEM 23. *Gikas v. Nicholis*, 71 A.2d 785 (N.H. 1950, illustrates that, under unjust enrichment, "the donor of an engagement ring may recover it from the donee who terminates the engagement." After you have worked through the elements of unjust enrichment to determine whether that is justified, consider this

variation: In *Lowe v. Quinn*, 27 N.Y.2d 397 (N.Y. 1971), Lowe, a married man, gave an engagement ring to Quinn (not Lowe's wife) in October 1968 on her promise to marry him when and if his divorce became final. Lowe had been living apart from his wife for years, and they contemplated a divorce. A month later, Quinn had second thoughts and said she had decided not to marry Lowe. He requested return of the ring, and she suggested he talk to her lawyer. He later sued for the ring or for $60,000, its asserted value. The trial court ruled for him, the intermediate appellate court for her, and he appealed. How would you argue this one?

PROBLEM 24. Winkler and Baltz were engaged. Three weeks before the wedding, Winkler signed a contract with JA-DEL, Inc. for JA-DEL to cater the reception for 120 guests for about $9,900. The contract called for payment in advance, but it did not occur. JA-DEL provided the food, anyway (which it probably had to pre-purchase). Winkler's and Baltz's friends and family attended the reception and ate the food. The contract price represented a fair value for the food and catering. JA-DEL was never paid. That was in June. In August, JA-DEL sued Winkler for breach of contract and Winkler and Baltz for unjust enrichment. The marriage was annulled in December. In May, Winkler settled with JA-DEL, but she never paid them a dime. Baltz, on the other hand, resisted JA-DEL's suit. After all, his name was not on the contract. He did, of course, know before the wedding that Winkler had ordered food catered for the reception. What do you think should be the result? The problem is based on *JA-DEL, Inc. v. Winkler*, No. 118,441 (Kan. App. Jan. 11, 2019) (mem. op.) (per curiam but over the dissent of Buser, J.).

PROBLEM 25. Suppose you own a home in another city (say, El Paso) and one day you receive a phone call. The caller says the following, then hangs up: "Hi, I'm Bob the painter. Your house in El Paso is an eyesore! I'm going to paint it and send you a bill. Just wanted to let you know! Bye!" A week later you get a bill from Bob. Must you pay it? (The rule in cases like this has been called the "officious intermeddler" rule. What does *officious* mean?)

Chapter 5. Limits on Bargains: Defenses

The cases in this Chapter answer the following question: Does enforcement depend on the bargain being roughly equal in value on both sides, or is the equality of the bargain left to the parties? Is some sort of just price required? You might be surprised at the answer, but to answer that question you must study all of the cases in this chapter. None of them is unusual. Each statement of law in them is mundane. But their doctrines leave in the law a striking paradox. The paradox is only apparent, however. As you learn how a contract breach case proceeds from complaint to answer, discovery, and trial, the regulatory goal of the doctrine begins to appear.

A. Introduction: Limits on Bargains?

How much will the courts trust parties to make their own bargains? The rule in this case addresses what plaintiffs need to show in order to stay in court as against (i) a motion to dismiss (12(b)(6)) if the defendant appears or (ii) a court's hesitancy to grant a default judgment when the defendant does not appear at all.

EDWARD NOWITZKE TRUST and Kristine M. Gillengerten, Trustee, v. Ronald DEYOUNG

No. 269597, Mich. App.

Aug. 5, 2008

PER CURIAM

[¶1] Defendant/counter-plaintiff appeals as of right from the judgment for plaintiffs/counterdefendants following a bench trial. Plaintiffs filed suit to quiet [meaning clear up legal ambiguities to] title in property, asking the court to set aside an agreement entered in 1996 between Edward Nowitzke and defendant whereby Nowitzke provided defendant a sixty day period in which he could elect to purchase the Nowitzke's Burt Lake property at the price of $150,000, in the event that Nowitzke died or received a written offer to purchase the property from a bona fide third-party. This agreement did not provide an escalation clause that would account for any appreciation in value of this property. Defendant counter-claimed for declaratory judgment concerning the validity of the above mentioned agreement. The trial court presided over a bench trial and concluded that the option agreement was void for insufficient consideration. On appeal, the litigants argue a single issue—whether the trial court erred in finding the consideration insufficient. We reverse the trial court's conclusion that the consideration was legally insufficient and remand for entry of judgment in favor of defendant on his counter-claim.

I. Facts and Proceedings

[¶2] In 1965, Nowitzke purchased by land contract property fronting Burt Lake in Indian River, Michigan. The purchase price under the land contract was $25,000. Nowitzke used the property for recreation. Over

the years, he developed a friendship with his next-door neighbors, defendant and his wife Barb DeYoung. In June 1996, the DeYoungs and Nowitzke discussed the sale of Nowitzke's property to the DeYoungs at a future point in time. Ultimately, the DeYoungs' attorney drafted a contract, which in consideration of the payment of $1 to Nowitzke, provided defendant an exclusive option to purchase the property. Under the terms of the contract, defendant was entitled to a sixty day period in which to elect to purchase the property in the event (1) that Nowitzke died, (2) Nowitzke sold the property, or (3) upon receipt of a written offer from a bonafide third-party purchaser, for the fixed price of for $150,000. The parties executed the document on October 5, 1996.

[¶3] On October 19, 2001, Nowitzke placed the property in the Edward Nowitzke Trust. On August 16, 2002, defendant recorded an affidavit of interest concerning the property consistent with the contract. In 2004, plaintiffs filed this action to quiet title in the property. Plaintiffs claimed that the contract was unenforceable and that defendant improperly recorded an affidavit of interest against the property.

[¶4] Following a bench trial, the trial court issued an opinion and order. The trial court concluded that the $1 paid for the option contract was inadequate consideration, and that the contract was unenforceable. The court noted that the property had appreciated significantly during the years since the contract was executed and that it was currently assessed at $370,000. The court rejected defendant's testimony that he did not consider that the property would continue to appreciate after the contract was executed. The court also found that Nowitzke relied on defendant, his long-time friend, to treat him fairly. The court concluded that defendant intentionally omitted an escalator clause to financially benefit himself to the detriment of Nowitzke. In doing so, the court reasoned:

> In the present case, the $150,000 purchase price was established by Mr. DeYoung with no input from Mr. Nowitzke. This contract did not come about through negotiations but instead under the guise of friendship. Mr. Nowitzke relied on that friendship and believed that his neighbor would treat his 76 year old friend in a reasonable and fair fashion, which, unfortunately, was not the case.
>
> The argument is essentially that for $1.00, Mr. DeYoung would have the option to receive all the future appreciation of Mr. Nowitzke's lake front property. At that time, this was property that was known to be appreciating at a very significant rate. If it appreciated only 10% per year and the option was exercised after only one year, then Mr. DeYoung would receive $15,000 value for this $1.00 investment. Nine years later he would receive $220,000 value for his $1.00 investment. By the date of this judgment, his windfall could very well exceed one quart[er] of a million dollars for his $1.00 investment. On the other hand, this generated absolutely no other benefit to Mr. Nowitzke except for $1.00.
>
> It seems impossible for anyone of common sense not to be offended and shocked by the inequality of the contract. It was and is so grossly unfair that it shocks the conscience and therefore must be set aside.

The trial court entered a judgment vesting title in the property in favor of the trust and an order rescinding the option contract was later entered.

II. Standard of Review

[¶5] Interpretation of a contract is a question of law reviewed de novo. * * * * Equitable actions, including actions to rescind a contract, are reviewed de novo, but the factual findings of the trial court are given great weight and reviewed for clear error. * * * * Clear error exists when some evidence supports a finding, but a review of the entire record leaves the reviewing court with the definite and firm conviction that a mistake has been made. * * * *

III. Analysis

[¶6] Defendant argues that the trial court improperly refused to enforce the contract. Defendant focuses on the trial court's conclusion that the option contract lacked consideration and argues the trial court improperly reviewed the fairness of the $1 option contract in terms of its present day value instead of its value at the time it was executed. We agree. In *General Motors Corp v Dept of Treasury*, 466 Mich 231, 634 NW2d 734 239 (2002), our Supreme Court reiterated that "courts do not generally inquire into the adequacy of consideration to support a contract." It has been said "[a] cent or a pepper corn, in legal estimation, would constitute a valuable consideration." *Id*. at 239, quoting *Whitney v Stearns*, 16 Me 394 (1839). Our Supreme Court quoted from Professor Williston to reinforce this point:

> It is an elementary and oft quoted principle that the law will not inquire into the adequacy of consideration so long as the consideration is otherwise valid to support a promise. By this is meant that so long as the requirement of a bargained-for benefit or detriment is satisfied, the fact that the relative value or worth of the exchange is unequal is irrelevant so that anything which fulfills the requirement of consideration will support a promise, regardless of the comparative value of the consideration and of the thing promised. The rule is almost as old as the doctrine of consideration itself. [*General Motors Corp, supra*, at 241 n 13, quoting 3 Williston, Contracts (4th ed), § 7:21, pp 383-386.]

"Mere inadequacy of consideration, unless it be so gross as to shock the conscience of the court, is not ground for rescission." *Rose v Lurvey*, 40 Mich App 230, 234-236 (1972), quoting *Hake v Youngs*, 254 Mich 545, 550, 236 NW 858, 859 (1931). Thus, "[e]quity will . . . grant relief where the inadequacy of consideration is particularly glaring." *Rose, supra*.

[¶7] Here, the trial court erred in concluding insufficient consideration supported the option contract. When viewed in the context of the execution of this agreement, the consideration of $1 is not so grossly inadequate as to shock the conscience of the court. All indications suggest that the $150,000 was a fair market price for the property at the time the parties executed it. Generally, claims of inadequate consideration are reviewed "at the time th[e] option was given," considering what "'would be a fair market price and all that could have been obtained in the open market for this property' in the condition it then was as to title and otherwise." *George v Schuman*, 202 Mich 241, 257-258; 168 NW 486 (1918) (internal citation omitted). Nowitzke had the power to force the option by placing his property for sale and obtaining an offer to purchase from a bona fide purchaser. There is no question that had Nowitzke elected to sell the property shortly after execution of the option, the option agreement would be valid and enforceable. This valid agreement is not rendered invalid merely because Nowitzke, a signatory to the contract, chose to permit time to pass.

[¶8] While we give deference to the factual findings of the trial court, we also note that many of the trial court's factual findings are legally irrelevant to the question of consideration. For example, the court found as a matter of fact that Nowitzke did not read the option agreement and, instead, relied on his friendship

with defendant concluding defendant would treat him in a reasonable and fair manner. Whether a party reads his contract before signing it has no impact on the consideration supporting the contract. Further, in *Moffit v Sederlund*, 145 Mich App 1, 9; 378 NW2d 491 (1985), this Court indicated that,

> [g]enerally, a failure to read a written contract document does not require rescission of the contract unless other facts indicate fraud, artifice, or deception. See, for example, *Vandendries v General Motors Corp*, 130 Mich App 195, 200; 343 NW2d 4 (1983). Failure to read a contract document provides a ground for rescission only where the failure was not induced by carelessness alone, but instead was induced by some stratagem, trick, or artifice by the parties seeking to enforce the contract. *Otto Baedeker & Associates, Inc v Hamtramck State Bank*, 257 Mich 435, 441; 241 NW 249 (1932).

[¶9] Here, the trial court made no findings that support the conclusion that defendant fraudulently induced him into executing the option agreement. While the trial court indicated Nowitzke relied on his friendship with defendant, there was no finding by the trial court or evidence presented at trial that defendant suggested Nowitzke need not read the contract or not seek the advice of counsel prior to signing it. In the absence of such findings, we hold that Nowitzke's failure to read his contract was induced by carelessness rather than fraud, deception or artifice, and does not render the contract invalid.

[¶10] The trial court also found unbelievable defendant's testimony that at the time the contract was executed, he never considered that the property might appreciate during the term of the agreement. The trial court also found that the $150,000 purchase price was unilaterally placed in the contract by defendant's counsel at defendant's direction. Again, these factors do not affect the adequacy of the consideration in this matter. And while the trial court's findings suggest that defendant presented Nowitzke with a contract drafted by defendant's counsel, which was beneficial to defendant, the trial court's conclusions of law do not support a finding of rescission based on defendant's conduct through the execution of this contract. Further, plaintiffs on appeal have presented us with no legal theory to support the conclusion that defendant's conduct makes the contract at issue subject to rescission. The trial court and the litigants focused almost exclusively on the question whether the consideration paid to Nowitzke was legally sufficient. On this point we conclude the trial court erred in assessing the sufficiency of the consideration.

[¶11] Reversed and remanded for entry of judgment in favor of defendant on his counter-claim. We do not retain jurisdiction.

Questions:

1. In an option contract, such as the one in this case, the optionor makes two promises. One is to sell the item on which the option is granted. What is the other promise? Which promise is at issue in DeYoung?

2. If the $1 had been for the other promise, the court would have ruled the other way. Why, do you suppose?

3. Would the court have enforced the contract if the $1 had not been paid? In some states, this might have worked. We will look at those exceptional decisions later.

*PROBLEM 26***.** In *Embola v. Tuppela*, 220 P. 789 (Wash. 1923), Tuppela obtained land during the Alaska gold rush. After a number of years, he was adjudicated insane and committed in Portland, Oregon. After four years, he was released, but he found that his mining properties had been sold by his guardian. Tuppela soon thereafter found Embola. They had been close friends for thirty years. Embola advanced money for Tuppela's support and brought him back to Seattle. Tuppela tried to raise money so that he could return to Alaska and re-obtain his mine, but no one was willing to lend to him. After a few months, Tuppela proposed to Embola, "You have already let me have $270. If you give me $50 more so I can go to Alaska and get my property back, I will pay you ten thousand dollars when I win my property." Embola agreed and gave Tuppela $50. Three years later, Tuppela recovered his property, which was worth about $500,000. Tuppela asked his trustee to pay $10,000 to Embola, but the trustee refused, so Embola sued Tuppela's trustee. From the analysis in *Edward Nowitzke Trust*, what result?

PROBLEM 27. In Texas, you can play the state-sponsored lottery called "Lotto" for $1. A "jackpot" lotto prize may exceed $100 million. Is $1 consideration for the promise of such a prize?

B. Duress

A law of duress existed when contracts first became enforceable in assumpsit in the 1500s, but it did not look much like the law we have today. Even as late as the mid-1800s, the duress standard was very difficult to meet. This is how Story on Contracts (4th ed. 1856) described the law:

> Assent . . . must be freely and voluntarily given in order to create a valid contract. Compulsion or duress will therefore void any agreement. Duress is either by imprisonment or by threats, and must be upon the *person*. § 393.
>
> In order to constitute duress by imprisonment, either the imprisonment, or the duress, consequent upon it, must be tortious and unlawful. § 395.
>
> Duress by threat is divided . . . into four classes[:] Through fear, 1st. Of Loss of Life; 2d. Of Loss of Member; 3d. Of Mayhem; 4th. Of imprisonment. § 397.

"Fear" required fear of the other three things. *Mayhem* meant to disable or disfigure. *E.g.*, *Republica v. Reiker*, 3 Yeates 282 (Pa. 1801) ("pull or put out an eye, while fighting or otherwise," quoting the statute). "A threat . . . to burn a house, or to destroy goods, was considered as void," meaning the threat was without legal effect. § 398. "But the loss of an arm struck a soldier from the ranks of those who could defend [the king's] majesty; and this could be ill sustained, while the wars were so deadly a canker to life." *Id.* It was a harsh world.

Not only was the standard high; it was not very clear. The point of the doctrine was that assent be "freely and voluntarily given," but there is a bit of necessity in almost everything. How much fear of harm was

necessary? Perhaps for some people, any sober threat to put out an eye would do, but could Chuck Norris ever claim duress?

In the 1900s, the American Law Institute's R2K tried to set forth better standards.

Dorale v. Dorale, No. 08-0560 (Iowa App. May 6, 2009) is a good example of the R2K duress analysis. Ray and Sandra Dorale were married when they came to own 160 acres of farmland. 2009 WL 1211969, *1. Sandra secured a protective order against Ray in July 2005, and Ray filed for divorce. In October 2006, the divorce decree gave Ray the west 80 acres and Sandra the east 80. At the time, Sandra's 80 was worth $224,000. *Id.*

But Ray wanted the whole 160, which "he had farmed for years." *Id.* The ongoing protective order prohibited him from talking to Sandra, but he could talk to Sandra's father. Ray went to visit him on March 12, 2007. Sandra happened to visit at the same time. "Discussions and arguments, contentions and sometimes heated," went on "for approximately four hours." Finally, "Ray, Sandra, and Sandra's father signed a paper" that said, "Ray Dorale will pay Sandy Dorale $125,000 plus $48,000 for the East half '80 acres' of the Viola Dorale farm. Sandy Dorale will give Ray the 'Deed' to the farm and get paid at the same time" at a local bank. Ray recorded the document, which prevented Sandra from selling to anyone else. *Id.*

Later, when Sandra received an offer from someone else for the 80 acres, the proposed purchaser refused to buy after examining the title records and seeing Ray's claim as a cloud on Sandra's title. Sandra filed a "quiet title" action to resolve whether Ray had an interest in the property. Trial evidence showed that the property had increased in value substantially.

In the trial court and at the court of appeals, the issue was whether Sandra signed under duress. The court employed the R2K version of the rule:

> Ray claims the trial court erred in concluding Sandra signed the paper in question under duress. In so concluding the court quoted and relied on Restatement (Second) of Contracts sections 175 and 176. Those provisions state:
>
> § 175. When Duress By Threat Makes A Contract Voidable
>
> 1) If a party's manifestation of assent is induced by an improper threat by the other party that leaves the victim no reasonable alternative, the contract is voidable by the victim.
>
> 2) If a party's manifestation of assent is induced by one who is not a party to the transaction, the contract is voidable by the victim unless the other party to the transaction in good faith and without reason to know of the duress either gives value or relies materially on the transaction.
>
> § 176. When A Threat Is Improper
>
> 1) A threat is improper if

> a) what is threatened is a crime or a tort, or the threat itself would be a crime or a tort if it resulted in obtaining property,
>
> b) what is threatened is a criminal prosecution,
>
> c) what is threatened is the use of civil process and the threat is made in bad faith, or
>
> d) the threat is a breach of the duty of good faith and fair dealing under a contract with the recipient.
>
> 2) A threat is improper if the resulting exchange is not on fair terms, and
>
> a) the threatened act would harm the recipient and would not significantly benefit the party making the threat,
>
> b) the effectiveness of the threat in inducing the manifestation of assent is significantly increased by prior unfair dealing by the party making the threat, or
>
> c) what is threatened is otherwise a use of power for illegitimate ends.

Restatement (Second) of Contracts § 175, at 475–76; § 176, at 481–82 (1981).

Id. at *2–3. Please answer some questions about these rules before reading what happened in Sandra's case.

1. Do the rules attempt to define "freely" or "voluntarily"? What replaces those? Can that be proved by objective evidence—evidence of a party's outward manifestations?

2. On a continuum between subjective and objective, where do these rules fall?

3. May duress come from a threat to property rather than to the person?

4. Does duress sometimes require a judgment about the fairness of the resulting exchange?

The Restatement sections have been widely adopted by the courts, as they were in *Dorale*.

As you have now noticed, the two Restatement sections work together. Section 175(1) defines duress as when a manifestation of assent is induced by an improper threat by the other party that leaves the victim no reasonable alternative. Given that definition, what are the elements of duress?

PROBLEMS 28-34. Section 176 gives examples of what might be improper threats. Please match the following examples with the subsections of section 176. (For a fuller understanding of the provisions themselves, you might find the R2K in the library or on Westlaw or LEXIS and read the comments and examples. The R2K also includes citations to cases which have used or cited to its provisions. On the other hand, courts seldom study the comments and illustrations extensively, and once R2K language is adopted into case law, the language develops a life of its own.)

28. Bob goes to look at a used car, a 1972 Nova, and finds that the seller is the brother of Bob's sister Marsha's employer. As the seller and Bob finish negotiations for this car, which is not in very good shape, the seller says to Bob, "Actually, I have a lot of pull with my brother Al and I really need to sell this car. If you buy the car for $10,000, I'll tell Al what a fine family Marsha has. If you don't, well, Marsha can kiss her job goodbye!" Employment is at-will in the state.

29. Bob embezzles money from Business. The Business sues Bob and threatens to take steps to encourage a criminal prosecution against Bob if he does not sign a promissory note to repay with interest what he took.

30. Bob is visiting his sister Marsha and sitting in the backyard drinking lemonade when Marsha's neighbor Andy walks up. Andy says to Bob, "I want to sell you my Mercedes for $10,000 cash." Bob agrees to look at the car. The car is only a few years old, and appears to be in excellent condition. Still, Bob had hoped to be driving something sportier, like a 1972 Nova, restored, with a big spoiler on the back. "I don't think so," Bob finally says, "I'm not in the market for this kind of car right now." "Yes, you are, "Andy replies, pulling a pistol from his coat. "Sign this contract for my car right now or I'll bury you under the garage." Bob gulps and signs. (Does the excellent price make a difference?)

31. Joe threatens to commence a lawsuit and file a lien on a house Bob just built, unless Bob signs a contract to release Joe from a disputed claim that Bob has against Joe regarding an entirely separate matter. Joe knows that he has no grounds to sue Bob or file a lien.

32. Bob is 82 years old and lives alone in a small apartment in Houston. Bob had no air conditioning until last August, when he was sitting alone one day in his apartment and heard a knock at the door. It was Andy, selling air conditioners. Bob really wanted to buy an air conditioner. Andy said the price for a window box air conditioner was only $1,200. "Twelve hundred!" Bob started, "That's outrageous!" "Don't complain about the price, or I'll take my business elsewhere," Andy said, "and just see if anyone else will sell to you on credit!" Bob knew his credit wasn't the best. "Ok," Bob said, "You stay and I'll sign."

33. Marsha, a fur store employee at Al's Furs, buys furs herself. Both Al's and Marsha store their furs at the same independent warehouse. Marsha has not paid her warehouse bill. Warehouse says to Al's Furs owner, Al, "Unless you sign on to pay for Marsha's fees, we will hold your furs indefinitely." The next time Al went to the warehouse, the warehouse refused to release Al's furs without his signature on a note to pay Marsha's debt. Al signs.

34. Andy intentionally misleads Bob into thinking that Andy will supply goods at the usual price and thereby causes Bob to delay any attempt to buy them elsewhere. Andy then later, when Bob really needs the goods,

threatens not to sell them unless Bob promises to pay an outrageous price. Bob, in great need, promises to pay. *See* R2K § 176 illus. 13.

Question: When was it relevant in applying § 176 that the price was too high?

In *Dorale*, the court of appeals affirmed. Interestingly, the court decided that section 175(2) applied:

> [1] Prior to the parties' recent divorce Sandra had been the victim of domestic abuse by Ray and she feared him. She testified that he had threatened her physically concerning the land. Ray's post-divorce approaches to Sandra's father, Mr. Thies, to get Mr. Theis to convince Sandra to sell the eighty acres to him, were in apparent violation of the protective order issued in the domestic abuse proceeding. When Sandra unexpectedly arrived at her father's residence while Ray was there, Ray did not leave. He instead seized the opportunity to invoke Mr. Thies's assistance, over a period of some three to four hours, to convince Sandra to sell the eighty acres to him.
>
> [2] According to Sandra, her father was fearful and wanted Ray to leave. Mr. Thies feared someone would get hurt. Ray demonstrated anger and an unwillingness to leave unless and until he got what he wanted. Sandra was fearful and crying. Mr. Thies pressured Sandra to give Ray what he wanted in order to end the situation and get him to leave. After lengthy pressure, including a great deal of pressure from her own father, Sandra signed the paper purporting to agree to sell to Ray for $173,000 her eighty acres. This land had six months earlier appraised at $224,000, and according to the evidence had thereafter increased substantially in value.
>
> [3] Upon our de novo review we find that Sandra's manifestation of assent was induced, in large part if not entirely, by her father, not a party to the transaction, and that Ray was well aware of the pressure exerted on Sandra by her father. We conclude Sandra's manifestation of assent was the product of duress, as described in Restatement (Second) of Contracts, section 175(2), and is thus voidable and unenforceable. We need not and do not decide whether the contract is also voidable pursuant to section 175(1). We have considered all issues presented, and find any not expressly addressed herein either controlled by the foregoing or unnecessary to resolution of the appeal. We agree with the trial court's denial of Ray's petition for specific performance and grant of a decree quieting title in Sandra.

2009 WL 1211969, *3–4.

Questions:

1. Under what subsection of section 176 were Ray's threats improper?

2. What is more important in Dorale, the (i) badness of Ray's behavior and pressure exerted by Ray and Mr. Thies or (ii) Sandra's level of fear?

Now here are some more examples, including one that reaches back to older law (where you can see how the older law differed from the R2K test, which is the majority now but not universally accepted as the rule). Older formulations of duress often focus on subjective traits and are difficult to understand.†††† You will see an example in the *Holler* case, *infra*.

ALLIED BRUCE TERMINIX CO., INC. v. GUILLORY

Court of Appeal of Louisiana, Third Circuit (1994)

649 So.2d 652

LUCIEN C. BERTRAND, Jr., Judge Pro Tem.

[¶1] Plaintiff, Allied Bruce Terminix Company, Inc., filed suit for injunction and damages against defendant, John R. Guillory, for the alleged breach of a non-compete agreement. The trial court granted a preliminary injunction and Guillory appeals. We affirm.

[¶2] The trial court made the following findings of fact and conclusions of law: * * * *

> The facts show that defendant was employed by Terminix as a pest control technician, and on September 7, 1990, defendant signed an employment agreement setting forth certain limitations on his actions during the course of his employment with Terminix for a period of two (2) years after termination. The agreement specifically provides in pertinent part:

---

†††† Consider the following from *Magoon v. Reber*, 45 N.W. 112 (Wisc. 1890):

> If the plaintiff was induced to sign the notes and power of attorney through compulsion or constraint of personal violence threatened or impending, or under the influence of such fear of actual violence as overcame his mind and will, so that he did not act freely and voluntarily in executing them, they are void in law, though there might be some consideration to support them; for the principle is elementary that a contract made by a party under compulsion is void, because the consent is of the essence of a contract, and where there is compulsion there is no consent, for that must be voluntary.

Magoon is about as useful as any subjective definition of duress, but what qualifies as "personal violence"? "Overcoming of mind and will"? Acting "freely and voluntarily"?

> For a period of two years following termination of employment with Employer, Employee will not, either directly or indirectly, solicit or accept termite and/or pest control work from, or perform termite and/or pest control work for, any customer of employer for himself or for any other person, firm or corporation, nor will Employee engage in, accept employment from, become affiliated or connected with, directly or indirectly, or by any means become interested in, directly or indirectly, any termite and/or pest control business, or any other line of business similar to or of a like nature to any work performed by Employer.

[¶3] The agreement further provides that said prohibition be limited to those parishes in which defendant has worked for Terminix during the term of the agreement. The Court finds these parishes to be Lafayette and Acadia.

[¶4] Defendant resigned from his employment effective July 6, 1993, and has opened up his own pest control service company, which is located in St. Landry Parish. The majority of defendant's client base is in Lafayette Parish, and he freely admits that some of these clients were former clients of Terminix.

[¶5] After considering the law, evidence and arguments of counsel, the Court grants the injunction and denies the Exception of No Cause of Action. The provision at issue is valid and enforceable * * * *. * * * *

[¶6] Further, we find no merit to Guillory's argument that his consent to the contract was vitiated by economic duress, i.e., the threat of his employment being terminated. * * * * [T]he threat of doing a lawful act does not constitute duress. Therefore, we reject the argument that Guillory signed the non-compete agreement under duress and did not consent to its terms. * * * *

[¶7] For the foregoing reasons, the judgment of the trial court is affirmed at defendant's cost.

AFFIRMED.

PROBLEM 35. A debtor threatens a creditor, "Either settle with me for less or I'll file bankruptcy." Is this threat improper?

In re the MARRIAGE OF John W. MILLER and Debra K. Miller

Court of Appeals of Iowa

2002 WL 31312840 (Oct. 16, 2002)

MAHAN, J.

[¶1] Debra Miller appeals a district court ruling upholding the validity of a prenuptial agreement she signed prior to her marriage to John Miller. We affirm.

[¶2] **Background Facts and Proceedings**. John and Debra were married in August 1990. At the time of the parties' marriage, Debra had two registered horses, a truck, and household items worth approximately $2000. John had a house located at 1007 College Drive in Decorah, Iowa, a couple of boats, outdoor equipment, and a 401(k) account.

[¶3] Both parties were previously married. As part of the decree dissolving John's first marriage, he was awarded the house located in Decorah, Iowa. In order to maintain the house and other assets from his first marriage as his own property, John asked Debra to sign a prenuptial agreement prepared by his lawyer. This was requested a day before the wedding, and Debra was not aware of the prenuptial agreement until that time. It was clear if she did not sign the prenuptial agreement John would not marry her. John's lawyer apparently advised Debra to have the prenuptial agreement reviewed by independent counsel although she did not do so. Paragraph three of the agreement provides:

> In the event of a dissolution of marriage or death of either party to the marriage, each party hereto waives, relinquishes, and renounces any right, title or interest in the property of another. This includes all rights of dower and courtesy in the estates of one another.

Paragraph four provides:

> All property, both real and personal, which belonged to John W. Miller and Debra L. Fjelstul separately before marriage shall be and remain his or hers and neither party shall have claim to the other person's property. This includes, but is not limited to John W. Miller's interest in a house in Decorah, Iowa, and various items of sports equipment owned by him at the time of this Agreement was executed.

[¶4] As part of the divorce decree issued in November 2001, the district court concluded the prenuptial agreement was valid. The court awarded the Decorah home to John, and he was ordered to pay any debt remaining against the house. The court also awarded each party his/her entire 401(k) account. Debra appeals. * * * *

[¶5] **Duress.** We follow the Restatement's rule concerning the effect of duress on the enforceability of a contract: '"If a party's manifestation of assent is induced by an improper threat by the other party that leaves the victim no reasonable alternative, the contract is voidable by the victim.'" *Id*. at 318 (quoting *Turner v. Low Rent Hous. Agency*, 387 N.W.2d 596, 598 (Iowa 1986); Restatement (Second) of Contracts § 175(1), at 475 (1981)). There are two essential elements one must prove in order to show duress. The first element is the victim had no reasonable alternative to entering into the contract. *Turner,* 387 N.W.2d at 598-99. In the present case, Debra had a reasonable alternative: she could have canceled the wedding. In *Spiegel*, the supreme court noted "social embarrassment from the cancellation of wedding plans, even on the eve of the wedding, [does not] render that choice unreasonable." *Spiegel*, 553 N.W.2d at 318.

[¶6] The other element of duress is the threat must be wrongful or unlawful. *In re C.K*., 315 N.W.2d 37, 43-44 (Iowa 1982). Here, John's threat was he would not marry Debra if she did not sign the prenuptial agreement. We find insistence on a prenuptial agreement as a condition of marriage is not a threat or unlawful. See *Spiegel*, 553 N.W.2d at 318; *Liebelt v. Liebelt*, 801 P.2d 52, 55 (Idaho Ct. App. 1990) ("The threat of a refusal to marry is not wrongful in the eyes of the law."). Consequently, while we do not admire John's actions, Debra has failed to show she acted under duress in signing the prenuptial agreement.

AFFIRMED.

Nataliya HOLLER v. William HOLLER

Court of Appeals of South Carolina (2005)

612 S.E.2d 469

ANDERSON, J.

[¶1] William Holler (Husband) appeals from the family court's determination that a premarital agreement signed by Nataliya Holler (Wife) is not enforceable. We affirm.

FACTUAL/PROCEDURAL BACKGROUND

[¶2] Wife is originally from Ukraine. She was educated in Ukraine and taught college students in that country. English is not Wife's first language. After seeing Husband's picture in "a feminine magazine," Wife wrote a letter to him in English and included her phone number. Thereafter, Husband and Wife talked on the phone for "[a]bout a year." Their conversations were in English. During this time, Husband visited Wife in Ukraine.

[¶3] On September 5, 1997, Wife traveled to the United States to marry Husband. At the time of her arrival, Wife's English was "really poor." Husband disputed Wife's inability to speak English, claiming she spoke "[v]ery well." Upon completing an English course, Wife received a certificate from Central Piedmont College in May of 1998.

[¶4] In October or early November 1997, Wife became pregnant with Husband's child. Wife's visa was scheduled to expire on December 4, 1997, and she would have to return to Ukraine unless she married Husband. Wife came to the United States without money and relied upon Husband to provide support.

[¶5] Wife admitted that, while she was still in Ukraine, Husband told her about the premarital agreement. However, Wife believed she "needed to sign some papers under the law of South Carolina before we g[o]t married." Wife claimed: "[Husband] faxed me some documents for American Embassy, and one page was he told me that we need—when you get to United States we have to sign that agreement before we get married because this is under [the] law of South Carolina." Husband delivered the premarital agreement to Wife sometime before the marriage. Husband first stated he faxed it to her five or six months before she arrived in the United States. Husband maintained he handed her a copy to sign within a week after she arrived. Yet, Wife declared Husband gave her a copy of the premarital agreement only two weeks before she signed it.

[¶6] Prior to signing the premarital agreement, Wife attempted to translate a portion of the agreement from English into Russian, but was unable to complete the translation. "Because it was too hard," Wife became frustrated with the translation and quit. Wife had eleven pages of translation before she determined the

effort was futile. Wife professed the agreement "had specific language which [she did not] understand even in Russian." Wife never retained counsel because she had no money to pay someone to review the agreement.

[¶7] Wife signed the agreement on November 25, 1997. The parties were married on December 1, 1997, merely three days before Wife's visa was set to expire.

[¶8] Husband and Wife separated on February 13, 2000. Wife brought this action seeking a divorce, custody of the parties' child, child support, equitable distribution of marital property, and alimony. Husband answered and counterclaimed. Subsequently, he filed a motion to dismiss the claims for alimony and equitable distribution asserting the premarital agreement controlled. After a hearing, the family court denied the motion to dismiss. The court ruled the premarital agreement was invalid and unenforceable because it was signed under duress * * * *. * * * *

II. PREMARITAL AGREEMENT

[¶9] Husband contends the trial court erred in finding the premarital agreement was invalid and unenforceable as a result of being * * * * signed under duress.

[¶10] Premarital agreements, also called antenuptial or prenuptial agreements, are agreements between prospective spouses made in contemplation of marriage. Black's Law Dictionary defines a prenuptial agreement as "[a]n agreement made before marriage usu[ally] to resolve issues of support and property division if the marriage ends in divorce or by the death of a spouse." Black's Law Dictionary 1220 (8th ed. 2004). Antenuptial settlements are contracts or agreements entered into between a man and woman before marriage, but in contemplation and generally in consideration of marriage, whereby the property rights and interests of either the prospective husband or wife, or of both of them, are determined, or where property is secured to either or to both of them, or to their children. 41 C.J.S. Husband and Wife § 61 (1991).

[¶11] The consideration for a premarital agreement is the marriage itself. Because such agreements are executory, they become effective only upon marriage. * * * * In *South Carolina Loan & Trust Co. v. Lawton*, the Supreme Court explained:

> There is not complete execution of such instruments until actual marriage, and it does not matter how many changes may be made, and how many different instruments may be signed, the settlement, in the last form it assumes before marriage, is the real contract supported by the consideration of marriage.

Id. at 349, 48 S.E. at 283.

[¶12] In *Stork v. First National Bank*, 281 S.C. 515, 316 S.E.2d 400 (1984), the Supreme Court inculcated:

> Antenuptial agreements * * * will be enforced if made voluntarily and in good faith and if fair and equitable. *Rieger v. Schaible*, 81 Neb. 33, 115 N.W. 560 (1908) (citing *Pierce v. Pierce*, 71 N.Y. 154, 27 Am. Rep. 22). Such contracts are not opposed to public policy but are highly beneficial to serving the best interest of the marriage relationship.

Id. at 516, 316 S.E.2d at 401. An antenuptial contract is valid and will be upheld when, and only when, it is entered into freely, fairly, and in good faith by parties legally competent to contract. 41 C.J.S. Husband and Wife § 62 (1991). An antenuptial agreement must be free from duress, fraud, deceit, misrepresentation, or overreaching. *Id*. * * * *

A. Duress

[¶13] Husband avers the family court improperly concluded Wife signed the premarital agreement while under duress. We disagree.

[¶14] Duress is a condition of mind produced by improper external pressure or influence that practically destroys the free agency of a party and causes him to do an act or form a contract not of his own volition. *Cherry v. Shelby Mut. Plate Glass & Cas. Co.*, 191 S.C. 177, 4 S.E.2d 123 (1939); *Cox & Floyd Grading, Inc. v. Kajima Constr. Servs., Inc.*, 356 S.C. 512, 589 S.E.2d 789 (Ct. App. 2003); *Willms Trucking Co. v. JW Constr. Co.*, 314 S.C. 170, 442 S.E.2d 197 (Ct. App. 1994).

[¶15] Corpus Juris Secundum defines duress:

> "Duress" may be defined as subjecting a person to a pressure which overcomes his or her will and coerces him or her to comply with demands to which he or she would not yield if acting as a free agent. Some definitions of "duress" contain not only the element of pressure overcoming the victim's will but also the element that the pressure or compulsion consists of improper, wrongful, or unlawful conduct, acts, or threats.
>
> Further, "duress" has been defined as the condition of mind produced by the wrongful conduct of another rendering a person incompetent to contract with the exercise of his or her free will power, or as the condition of mind produced by an improper external pressure destroying free agency so as to cause the victim to act or contract without use of his or her own volition, or as unlawful constraint whereby a person is forced to do some act against his or her will.

17A C.J.S. Contracts § 175 (1999) (footnotes omitted).

[¶16] The central question with respect to whether a contract was executed under duress is whether, considering all the surrounding circumstances, one party to the transaction was prevented from exercising his free will by threats or the wrongful conduct of another. 17A Am. Jur. 2d Contracts § 218 (2004). Freedom of will is essential to the validity of an agreement. *Id.* A party claiming "duress" can prevail if he shows that he has been the victim of a wrongful or unlawful act or threat of a kind that deprives the victim of unfettered will, with the result that he was compelled to make a disproportionate exchange of values. *Id.*

[¶17] In order to establish that a contract was procured through duress, three things must be proved: (1) coercion; (2) putting a person in such fear that he is bereft of the quality of mind essential to the making of a contract; and (3) that the contract was thereby obtained as a result of this state of mind. *In re Nightingale's Estate*, 182 S.C. 527, 189 S.E. 890 (1937). The fear which makes it impossible for a person to exercise his own free will is not so much to be tested by the means employed to accomplish the act, as by the state of mind produced by the means invoked. *Id.*; *Willms Trucking Co.*, 314 S.C. at 179, 442 S.E.2d at 202. If one of the parties to an agreement is in a position to dictate its terms to such an extent as to substitute his will for the will of the other party thereto, it is not a mutual, voluntary agreement, but becomes an agreement

emanating entirely from his own mind. *In re Nightingale's Estate*, 182 S.C. at 547, 189 S.E at 898; *Willms Trucking Co.*, 314 S.C. at 179, 442 S.E.2d at 202. If a party's manifestation of assent is induced by an improper threat by the other party that leaves the victim no reasonable alternative, the contract is voidable by the victim. *Willms Trucking Co.*, 314 S.C. at 179, 442 S.E.2d at 202. Whether or not duress exists in a particular case is a question of fact to be determined according to the circumstances of each case, such as the age, sex, and capacity of the party influenced. *Id*.; *see also Santee Portland Cement Corp. v. Mid-State Redi-Mix Concrete Co*., 273 S.C. 784, 260 S.E.2d 178 (1979) (stating whether or not duress was present is a question ordinarily determined on a case by case basis).

[¶18] Duress is viewed with a subjective test which looks at the individual characteristics of the person allegedly influenced, and duress does not occur if the victim has a reasonable alternative to succumbing and fails to take advantage of it. *Blejski v. Blejski*, 325 S.C. 491, 480 S.E.2d 462 (Ct. App. 1997) (citing Restatement (Second) of Contracts § 175 cmt. b & c (1981)). Duress is a defense to an otherwise valid contract. 17A Am. Jur. 2d Contracts § 218. Duress renders a contract voidable at the option of the oppressed party. *Santee Portland Cement Corp.*, 273 S.C. at 784, 260 S.E.2d at 178.

[¶19] Assumptively concluding Wife was allowed the opportunity to view the premarital agreement three months in advance, the evidence in the record indicates: (1) Wife did not understand the contents of the agreement; (2) she did not freely enter into the agreement; (3) she attempted to translate the agreement into Russian in order to better comprehend the document; (4) she became frustrated as she was unable to complete a satisfactory translation; and (5) her notes indicate there are several words for which she could not find a translation, including "undivided," "equitable," and "pro rata." Consequently, Wife could not understand the agreement.

[¶20] Additionally, Husband was aware of the deadline with respect to Wife's visa. According to his own testimony, Husband made it perfectly clear to Wife that she must sign the agreement if she wanted to be married prior to the expiration of her visa. Wife was in the United States with no means to support herself. She relied solely and completely on Husband for support. Wife had no money of her own with which to retain and consult an attorney or a translator. Whether a party obtained independent legal advice is a significant consideration in evaluating whether an antenuptial agreement was voluntarily and understandingly made. See 41 C.J.S. Husband and Wife § 62 (1991). The family court found if Wife was not able to marry, then she would be forced to return to Ukraine. Because she was pregnant with Husband's child, she sought to insure his continued support and to remain in the United States.

[¶21] Wife did not enter into the agreement freely and voluntarily. Ample evidence exists to support the family court's determination that Wife, given the circumstances she faced, signed the agreement under duress and without a clear understanding of what she was signing. The family court did not err in finding Wife signed the agreement under duress.

Question: Why do *Miller* and *Holler* reach different results?

BETHLEHEM STEEL CORPORATION, Plaintiff v. Sheldon H. SOLOW, etc. Defendants

Supreme Court, Appellate Division, First Department, New York

63 A.D.2d 611, 405 N.Y.S.2d 80

May 16, 1978

Before BIRNS, J. P., and EVANS, FEIN, MARKEWICH and SULLIVAN, JJ.

MEMORANDUM DECISION.

* * * *

[¶1] Defendants' contentions are that plaintiff submitted a bid to supply and erect structural steel at $420 per ton provided the bid was executed and returned within seven days; that defendants repeatedly attempted to meet with plaintiff until about six weeks after receipt of the initial bid and to their surprise and dismay learned that plaintiff had raised the price of their steel to $474 per ton; that this price was not based upon costs, materials or labor increases, but was an arbitrary inflated price interposed by plaintiff because it knew it was the only structural steel supplier available at the time; that defendants were in immediate need of the steel and had no alternative but to execute the contract under duress.

[¶2] It is not alleged that defendants accepted or responded to plaintiff's initial bid; nor is it alleged that plaintiff had any contractual relationship with defendants of any type prior to the time the parties entered into the contract which serves as the predicate for the economic duress defense.

[¶3] "Duress, in order to render voidable what was done, must involve a wrongful act or threat precluding the exercise of a free will." (17 NY Jur, Duress and Undue Influence, § 3.)

[¶4] The law in New York is clear that in order to have a situation involving "economic duress" there must have been some sort of obligation on the part of the party to perform. (*Salzman v Holiday Inns*, 48 A.D.2d 258, mod 40 N.Y.2d 919; *Muller Constr. Co. v New York Tel. Co.*, 50 A.D.2d 580, affd 40 N.Y.2d 955.)

[¶5] In the instant situation, the original bid was never accepted by defendants in any way, shape or form. Consequently, there is no showing of a prior contractual relationship or a showing that plaintiff had any obligation or duty to deal with defendants. Although it appears defendant was subject to financial pressures and may have lacked equal bargaining power, there nonetheless was an insufficient showing to constitute economic duress. (*Grubel v Union Mut. Life Ins. Co.*, 54 A.D.2d 686.) The law is well stated in *Hugo V. Lowei, Inc. v Kips Bay Brewing Co*. (63 N.Y.S.2d 289), where the defendant claimed that he had been induced to enter into a contract by economic duress because of existing war emergency conditions, leaving him unable to purchase his product from any other source than the plaintiff. The court held (p 290):

> "Assuming the truth of this, it does not constitute duress in law. The plaintiff was under no duty or obligation to do business with defendant and could have refused, arbitrarily, to do business with it, or if it decided to do business with defendant could name its own terms. Defendant could have declined to accept them; it was under no obligation to accept, other

> than its need to have the hops which it could not obtain elsewhere. Driving a hard bargain in the circumstances is not the type of duress which may be availed of as a ground for avoiding entering into a contract and liability thereunder. This defense is legally insufficient."

[¶6] *Austin Instrument v Loral Corp*. (29 N.Y.2d 124) is not controlling. In the Austin case there was a binding contract which was subsequently renegotiated as a result of the economic duress applied by Austin. Here there is no prior contractual relationship.

[¶7] One who would repudiate a contract procured by duress, must act promptly, or he will be deemed to have elected to affirm it. (*Port Chester Elec. Constr. Corp. v Hastings Terraces*, 284 App Div 966; *Fowler v Fowler*, 197 App Div 572.) Here the defendants waited six years from the commencement of this action before interposing the economic duress defense. In view of the inordinate length of time which has passed between the alleged economic duress and the assertion of that defense, it must be deemed waived. * * * *

Questions:

1. What could be the alleged wrongful act or threat here?

2. Why would a subjective duress defense make sense or not make sense when the promisor is a corporation?

3. In *Austin Instrument, Inc*., a supplier of electronics components, Austin, contracted to supply a set of parts for radar equipment to Loral, a radar equipment manufacturer. When Loral asked for bids for a second set of parts, Austin stopped performance on the first set and threatened to provide nothing more under its current contracts unless Loral awarded Austin the second set and increased the price on the first. After determining that no one on its approved list of suppliers could fill Austin's obligations, Loral agreed to Austin's demands. Immediately after receiving the last component under the second set of contracts, Loral refused to pay Austin the remainder of what the contracts required. When Austin sued, Loral argued duress. The court agreed with Loral. Can you see the difference between this case and *Bethlehem Steel*? How would you analyze the *Austin* facts under the Restatement (Second) test?

C. Undue Influence

Undue influence is used most often to contest a will. But it is also used to contest a conveyance by deed, and courts have sometimes employed it in contract cases. It is not common in contract cases, though, and to some extent is superseded by unconscionability doctrine. Perhaps that is why courts seem uncertain what its use is. The following was written lately, in 2021:

> The Texas Supreme Court has recognized that "[u]ndue influence itself is not an actionable tort." *Kinsel v. Lindsey*, 526 S.W.3d 411, 422 n.3 (Tex. 2017). "[C]onsequently, damages

> are not recoverable based solely on an undue-influence finding," and instead, a finding of undue influence is grounds for setting aside or rescinding an otherwise binding agreement. *Id.* To that end, courts have construed claims of "undue influence" as a possible basis for rescission as part of a breach of contract claim.

Brighthouse Life Ins. Co. v. Daboub, 577 F. Supp. 3d 504, 522 (N.D. Tex. 2021).

But you need a list of elements and an application. The case of *Rodriguez v. Garcia*, 519 S.W.2d 908 (Tex. App.—Corpus Cristi 1975, writ refused, n.r.e.), is a good example of undue influence. Here is how the court described Refugio Garcia, who signed two warranty deeds conveying to his niece, Evila Garcia Rodriguez, a mineral interest in 10.29 acres:

> Mr. Garcia was a seventy-three (73) year old male of Mexican ancestry. He resided in Raymondville, Texas, during the period in question. He was and still is unemployed. Garcia's only source of income at that time was royalty payments of approximately $60.00 per month from the property in question. At the time of trial, Garcia could not and never has been able to read, write or understand the English language. He had several physical disabilities. His niece, Evila Garcia Rodriguez, resides in Houston, Texas.

Id. at 909. Apparently, Evila took her uncle to Houston to visit a doctor, and while there she took him to see her attorney, who drew up the first deed. Evila gave no consideration for the deed. Mr. Garcia went in and out of and then again into the hospital for several weeks. After his second discharge from the hospital, Mr. Garcia signed the second deed, which differed from the first only in the description of the property conveyed. *Id.* Mr. Garcia later sued his niece to cancel and set aside the deeds, on grounds of undue influence. In the trial court, Evila contended that her uncle knew what he was doing, signed "because of love and affection for her," and that the deeds were translated into Spanish for him. *Id.* at 909–10. The trial court ruled for Mr. Garcia, and Ms. Garcia Rodriguez appealed.

Here is how the court resolved the appeal:

> Our Supreme Court has set down the elements of a contestant's cause of action as guidelines that must be proved before an instrument can be set aside on the grounds of undue influence. They are: (1) the existence and exertion of an influence; (2) the effective operation of such influence so as to subvert or overpower the mind of the grantor at the time of the execution of the instrument; and (3) the execution of the instrument which the maker thereof would not have executed but for such influence. *Scott v. Townsend*, 106 Tex. 322, 166 S.W. 1138 (1914); *Chapal v. Vela*, 461 S.W.2d 466 (Tex. Civ. App.—Corpus Christi 1970, no writ). The burden of proving undue influence is upon the party contesting the execution of this instrument. He must produce some tangible proof of the existence of each of such elements of undue influence. *Chapal v. Vela, supra*. Undue influence may be shown by circumstantial evidence. * * * * Prior to the execution of the two deeds the niece had never lived with her uncle, and during the last twenty (20) years, the niece had never taken care of him a single time. There is testimony by Maria Garcia that prior to the time the niece came to take her uncle to the hospital, the niece had never come even to visit with him before. The uncle testified in response to questions concerning his signature on the deed:
>
> > Q. This document was signed in Houston, Texas?

> A. In Houston? No. I was in Houston but I didn't sign anything over there, no, sir. She wanted that I sign and that I get the check for the pension and she wanted—
>
> Q. Who wanted?
>
> A. —Bad things
>
> Q. Who wanted you to sign to get the pension?
>
> A. Evila (the niece).

The record further discloses that the uncle's only source of income and support was from the oil royalties from the property conveyed. The niece testified concerning the consideration given for the conveyance of the property from her uncle:

> 'Q. Just one more question, Mrs. Rodriguez, and I want this clarified: When these properties—rather these deeds were executed and these interest were conveyed from Mr. Garcia to you, did you or did you not promise him that you were going to take care of him for the rest of his life?
>
> A. I didn't promise him anything. We just said that he would help me and I would help him. You can't promise a thing like that because I could die first.
>
> Q. There was no consideration for the transfer of these deeds?
>
> A. No.'
>
> After reviewing the above evidence, it is clear that there was evidence of probative force * * * to support the finding of the jury that the niece used undue influence upon Mr. Garcia to get him to sign and deliver the two mineral deeds. Appellant's second point of error is overruled.

Id. at 912. Most undue influence cases have fact recitations that go on for pages, as you might imagine. Proving by "tangible proof" that someone's mind was overpowered by an influence is no easy task.

D. Mutual Mistake

SHERWOOD v. WALKER and others

Supreme Court of Michigan (1887)

33 N.W. 919

MORSE, J.

[¶1] Replevin for a cow. Suit commenced in justice's court; judgment for plaintiff; appealed to circuit court of Wayne county, and verdict and judgment for plaintiff in that court. The defendants bring error, and set out 25 assignments of the same.

[¶2] The main controversy depends upon the construction of a contract for the sale of the cow. The plaintiff claims that the title passed, and bases his action upon such claim. The defendants contend that the contract was executory, and by its terms no title to the animal was acquired by plaintiff.

[¶3] The defendants reside at Detroit, but are in business at Walkerville, Ontario, and have a farm at Greenfield, in Wayne county, upon which were some blooded cattle supposed to be barren as breeders. The Walkers are importers and breeders of polled Angus cattle. The plaintiff is a banker living at Plymouth, in Wayne county. He called upon the defendants at Walkerville for the purchase of some of their stock, but found none there that suited him. Meeting one of the defendants afterwards, he was informed that they had a few head upon this Greenfield farm. He was asked to go out and look at them, with the statement at the time that they were probably barren, and would not breed. May 5, 1886, plaintiff went out to Greenfield and saw the cattle. A few days thereafter, he called upon one of the defendants with the view of purchasing a cow, known as "Rose 2d of Aberlone." After considerable talk, it was agreed that defendants would telephone Sherwood at his home in Plymouth in reference to the price. The second morning after this talk he was called up by telephone, and the terms of the sale were finally agreed upon. He was to pay five and one-half cents per pound, live weight, fifty pounds shrinkage. He was asked how he intended to take the cow home, and replied that he might ship her from King's cattle-yard. He requested defendants to confirm the sale in writing, which they did by sending him the following letter:

> "WALKERVILLE, May 15,1886.
>
> "T.C. SHERWOOD,
>
> President, etc.,—
>
> "Dear Sir: We confirm sale to you of the cow Rose 2d Aberlone, lot 56 of our catalogue, at five and a half cents per pound, less fifty pounds after shrink. We inclose herewith order on Mr. Graham for the cow. You might leave check with him, or mail to us here, as you prefer.
>
> "Yours truly,

"HIRAM WALKER & SONS."

The order upon Graham inclosed in the letter read as follows:

"WALKERVILLE, May 15, 1886.

"George Graham: You will please deliver at Kings cattle-yard to Mr. T.C. Sherwood, Plymouth, the cow Rose 2d of Aberlone, lot 56 of our catalogue. Send halter with cow, and have her weighed.

"Yours truly,

"HIRAM WALKER & SONS."

[¶3] On the twenty-first of the same month the plaintiff went to defendants' farm at Greenfield, and presented the order and letter to Graham, who informed him that the defendants had instructed him not to deliver the cow. Soon after, the plaintiff tendered to Hiram Walker, one of the defendants, $80, and demanded the cow. Walker refused to take the money or deliver the cow. The plaintiff then instituted this suit. After he had secured possession of the cow under the writ of replevin, the plaintiff caused her to be weighed by the constable who served the writ, at a place other than King's cattle-yard. She weighed 1,420 pounds.

[¶4] When the plaintiff, upon the trial in the circuit court, had submitted his proofs showing the above transaction, defendants moved to strike out and exclude the testimony from the case, for the reason that it was irrelevant, and did not tend to show that the title to the cow passed, and that it showed that the contract of sale was merely executory. The court refused the motion, and an exception was taken. The defendants then introduced evidence tending to show that at the time of the alleged sale it was believed by both the plaintiff and themselves that the cow was barren and would not breed; that she cost $850, and if not barren would be worth from $750 to $1,000; that after the date of the letter, and the order to Graham, the defendants were informed by said Graham that in his judgment the cow was with calf, and therefore they instructed him not to deliver her to plaintiff, and on the twentieth of May, 1886, telegraphed to the plaintiff what Graham thought about the cow being with calf, and that consequently they could not sell her. The cow had a calf in the month of October following. On the nineteenth of May, the plaintiff wrote Graham as follows:

"PLYMOUTH, May 19, 1886."

MR. GEORGE GRAHAM,

"Greenfield, —

"Dear Sir: I have bought Rose or Lucy from Mr. Walker, and will be there for her Friday morning, nine or ten o'clock. Do not water her in the morning.

"Yours, etc.,

"T. C. SHERWOOD."

Plaintiff explained the mention of the two cows in this letter by testifying that, when he wrote this letter, the order and letter of defendants were at his house, and, writing in a hurry, and being uncertain as to the name of the cow, and not wishing his cow watered, he thought it would do no harm to name them both, as his bill of sale would show which one he had purchased. Plaintiff also testified that he asked defendants to give him a price on the balance of their herd at Greenfield, as a friend thought of buying some, and received a letter dated May 17, 1886, in which they named the price of five cattle, including Lucy at $90, and Rose 2d at $80. When he received the letter he called defendants up by telephone, and asked them why they put Rose 2d in the list, as he had already purchased her. They replied that they knew he had, but thought it would make no difference if plaintiff and his friend concluded to take the whole herd.

[¶5] The foregoing is the substance of all the testimony in the case.

[¶6] The circuit judge instructed the jury that if they believed the defendants, when they sent the order and letter to plaintiff, meant to pass the title to the cow, and that the cow was intended to be delivered to plaintiff, it did not matter whether the cow was weighed at any particular place, or by any particular person; and if the cow was weighed afterwards, as Sherwood testified, such weighing would be a sufficient compliance with the order; if they believed that defendants intended to pass the title by the writing, it did not matter whether the cow was weighed before or after suit brought, and the plaintiff would be entitled to recover. The defendants submitted a number of requests, which were refused. The substance of them was that the cow was never delivered to plaintiff, and the title to her did not pass by the letter and order; and that under the contract, as evidenced by these writings, the title did not pass until the cow was weighed and her price thereby determined; and that, if the defendants only agreed to sell a cow that would not breed, then the barrenness of the cow was a condition precedent to passing title, and plaintiff cannot recover. The court also charged the jury that it was immaterial whether the cow was with calf or not. It will therefore be seen that the defendants claim that, as a matter of law, the title to this cow did not pass, and that the circuit judge erred in submitting the case to the jury, to be determined by them, upon the intent of the parties as to whether or not the title passed with the sending of the letter and order by the defendants to the plaintiff. * * * *

[¶7] It appears from the record that both parties supposed this cow was barren and would not breed, and she was sold by the pound for an insignificant sum as compared with her real value if a breeder. She was evidently sold and purchased on the relation of her value for beef, unless the plaintiff had learned of her true condition, and concealed such knowledge from the defendants. Before the plaintiff secured possession of the animal, the defendants learned that she was with calf, and therefore of great value, and undertook to rescind the sale by refusing to deliver her. The question arises whether they had a right to do so. The circuit judge ruled that this fact did not avoid the sale, and it made no difference whether she was barren or not. I am of the opinion that the court erred in this holding. I know that this is a close question, and the dividing line between the adjudicated cases is not easily discerned. But it must be considered as well settled that a party who has given an apparent consent to a contract of sale may refuse to execute it, or he may avoid it after it has been completed, if the assent was founded, or the contract made, upon the mistake of a material fact,—such as the subject-matter of the sale, the price, or some collateral fact materially inducing the agreement; and this can be done when the mistake is mutual, 1 Benj. Sales, §§ 605, 606; Leake, Cont. 339; Story, Sales (4th ed.), §§ 148, 377. See, also, *Cutts v. Guild*, 57 H. Y. 229; *Harvey v. Harris*, 112 Mass. 32; *Gardner v. Lane*, 9 Allen, 492; S. C. 12 Allen, 44; *Huthmacher v. Harris' Adm'rs*, 38 Penn. St. 491; *Byers v. Chapin*, 28 Ohio St. 300; *Gibson v. Pelkie*, 37 Mich. 380, and cases cited; *Allen v. Hammond*, 11 Pet. 63, 71.

[¶8] If there is a difference or misapprehension as to the substance of the thing bargained for, if the thing actually delivered or received is different in substance from the thing bargained for and intended to be sold, then there is no contract; but if it be only a difference in some quality or accident, even though the mistake may have been the actuating motive to the purchaser or seller, or both of them, yet the contract remains binding. “The difficulty in every case is to determine whether the mistake or misapprehension is as to the substance of the whole contract, going, as it were, to the root of the matter, or only to some point, even though a material point, an error as to which does not affect the substance of the whole consideration.” *Kennedy v. Panama*, etc., Mail Co., L. E. 2 Q. B. 580, 588. It has been held, in accordance with the principles above stated, that where a horse is bought under the belief that he is sound, and both vendor and vendee honestly believe him to be sound, the purchaser must stand by his bargain, and pay the full price, unless there was a warranty.

[¶9] It seems to me, however, in the case made by this record, that the mistake or misapprehension of the parties went to the whole substance of the agreement. If the cow was a breeder, she was worth at least $750; if barren, she was worth not over $80. The parties would not have made the contract of sale except upon the understanding and belief that she was incapable of breeding, and of no use as a cow. It is true she is now the identical animal that they thought her to be when the contract was made; there is no mistake as to the identity of the creature. Yet the mistake was not of the mere quality of the animal, but went to the very nature of the thing. A barren cow is substantially a different creature than a breeding one. There is as much difference between them for all purposes of use as there is between an ox and a cow that is capable of breeding and giving milk. If the mutual mistake had simply related to the fact whether she was with calf or not for one season, then it might have been a good sale; but the mistake affected the character of the animal for all time, and for her present and ultimate use. She was not in fact the animal, or the kind of animal, the defendants intended to sell or the plaintiff to buy. She was not a barren cow, and, if this fact had been known, there would have been no contract. The mistake affected the substance of the whole consideration, and it must be considered that there was no contract to sell or sale of the cow as she actually was. The thing sold and bought had in fact no existence. She was sold as a beef creature would be sold; she is in fact a breeding cow, and a valuable one. The court should have instructed the jury that if they found that the cow was sold, or contracted to be sold, upon the understanding of both parties that she was barren, and useless for the purpose of breeding, and that in fact she was not barren, but capable of breeding, then the defendants had a right to rescind, and to refuse to deliver, and the verdict should be in their favor.

[¶10] The judgment of the court below must be reversed, and a new trial granted, with costs of this Court to defendants.

CAMPBELL, C.J., and CHAMPLIN, J., concurred.

SHERWOOD, J. (dissenting).

[¶1] I do not concur in the opinion given by my brethren in this case. I think the judgments before the justice and at the circuit were right. * * * *

[¶2] As has already been stated by my brethren, the record shows that the plaintiff is a banker, and farmer as well, carrying on a farm, and raising the best breeds of stock, and lived in Plymouth, in the county of Wayne, 23 miles from Detroit; that the defendants lived in Detroit, and were also dealers in stock of the higher grades; that they had a farm at Walkerville, in Canada, and also one in Greenfield, in said county of

Wayne, and upon these farms the defendants kept their stock. The Greenfield farm was about 15 miles from the plaintiff's. In the spring of 1886 the plaintiff, learning that the defendants had some "polled Angus cattle" for sale, was desirous of purchasing some of that breed, and, meeting the defendants, or some of them, at Walkerville, inquired about them, and was informed that they had none at Walkerville, "but had a few head left on their farm in Greenfield, and they asked the plaintiff to go and see them, stating that in all probability they were sterile and would not breed." In accordance with said request, the plaintiff, on the fifth day of May, went out and looked at the defendants' cattle at Greenfield, and found one called "Rose 2d," which he wished to purchase, and the terms were finally agreed upon at five and one-half cents per pound, live weight, 50 pounds to be deducted for shrinkage. The sale was in writing, and the defendants gave an order to the plaintiff directing the man in charge of the Greenfield farm to deliver the cow to plaintiff. This was done on the fifteenth of May. On the twenty-first of May plaintiff went to get his cow, and the defendants refused to let him have her; claiming at the time that the man in charge at the farm thought the cow was with calf, and, if such was the case, they would not sell her for the price agreed upon. The record further shows that the defendants, when they sold the cow, believed the cow was not with calf, and barren; that from what the plaintiff had been told by defendants (for it does not appear he had any other knowledge or facts from which he could form an opinion) he believed the cow was farrow, but still thought she could be made to breed. The foregoing shows the entire interview and treaty between the parties as to the sterility and qualities of the cow sold to the plaintiff. The cow had a calf in the month of October.

[¶3] There is no question but that the defendants sold the cow representing her of the breed and quality they believed the cow to be, and that the purchaser so understood it. And the buyer purchased her believing her to be of the breed represented by the sellers, and possessing all the qualities stated, and even more. He believed she would breed. There is no pretense that the plaintiff bought the cow for beef, and there is nothing in the record indicating that he would have bought her at all only that he thought she might be made to breed. Under the foregoing facts,—and these are all that are contained in the record material to the contract,—it is held that because it turned out that the plaintiff was more correct in his judgment as to one quality of the cow than the defendants, and a quality, too, which could not by any possibility be positively known at the time by either party to exist, the contract may be annulled by the defendants at their pleasure. I know of no law, and have not been referred to any, which will justify any such holding, and I think the circuit judge was right in his construction of the contract between the parties.

[¶4] It is claimed that a mutual mistake of a material fact was made by the parties when the contract of sale was made. There was no warranty in the case of the quality of the animal. When a mistaken fact is relied upon as ground for rescinding, such fact must not only exist at the time the contract is made, but must have been known to one or both of the parties. Where there is no warranty, there can be no mistake of fact when no such fact exists, or, if in existence, neither party knew of it, or could know of it; and that is precisely this case. If the owner of a Hambletonian horse had speeded him, and was only able to make him go a mile in three minutes, and should sell him to another, believing that was his greatest speed, for $300, when the purchaser believed he could go much faster, and made the purchase for that sum, and a few days thereafter, under more favorable circumstances, the horse was driven a mile in 2 min. 16 sec., and was found to be worth $20,000, I hardly think it would be held, either at law or in equity, by any one, that the seller in such case could rescind the contract. The same legal principles apply in each case.

[¶5] In this case neither party knew the actual quality and condition of this cow at the time of the sale. The defendants say, or rather said, to the plaintiff, "they had a few head left on their farm in Greenfield, and asked plaintiff to go and see them, stating to plaintiff that in all probability they were sterile and would not breed." Plaintiff did go as requested, and found there three cows, including the one purchased, with a bull.

The cow had been exposed, but neither knew she was with calf or whether she would breed. The defendants thought she would not, but the plaintiff says that he thought she could be made to breed, but believed she was not with calf. The defendants sold the cow for what they believed her to be, and the plaintiff bought her as he believed she was, after the statements made by the defendants. No conditions whatever were attached to the terms of sale by either party. * * * *

Questions:

1. In *Allen v. Hammond*, 36 U.S. (11 Pet.) 63 (1837), a case cited by both the majority and the dissent, the court asked:

> Suppose a life-estate in land be sold, and at the time of the sale, the estate has terminated by the death of the person in whom the right vested; would not a court of equity relieve the purchaser? If the vendor knew of the death, relief would be given on the ground of fraud; if he did not know it, on the ground of mistake. * * * * If a horse be sold, which is dead, though believed to be living by both parties, can the purchaser be compelled to pay the consideration?"

The court thought not, under the doctrine of mutual mistake.

These cases fall into one category of mutual mistake—we might call them cases of present impossibility. In fact, there is no life estate or horse to sell, so the seller's performance is impossible at the time the contract is formed. Some jurisdictions actually have a doctrine called "present impossibility" that will also render a contract voidable.

2. In *Allen v. Hammond* itself, a ship was illegally captured by the Portuguese. Notice of the capture was given to Washington, D.C., but the ship and its cargo by that time had already been sold. This occurred in 1830. News of the capture took time to reach the ship's owner, Hammond. On January 27, 1832, Hammond hired Allen to petition for compensation with the federal government and the government of Portugal. Hammond agreed to pay Allen ten percent of the first $8,000 Hammond obtained and one-third of everything after that. At the time, Hammond and Allen didn't know that federal government agents had already complained to Portugal, which admitted a claim of $33,700 and paid one quarter of that. When Hammond learned this, he sued for a declaration that his contract with Allen was void. The court granted the declaration. This is another category of mutual mistake. The seller's performance is possible, here, because Allen could petition Portugal regarding the ship. But there would be no point to doing so. Allen's performance would be valueless to Hammond. We might call this a case of frustration of purpose. Some jurisdictions also have a doctrine called "present frustration of purpose" that will also render a contract voidable.

3. Does Sherwood v. Walker fit into the two categories described in questions 1 and 2?

4. Do you think Sherwood is correctly decided? Who should bear the risk of the mistake in this case? Is non-assumption of risk an element of mutual mistake? Most cases say it is. The court in *Robert v. Century Contractors, Inc.*, 592 S.E.2d 215, 219 (N.C. App. 2004) stated:

> Likewise, a party who assumed the risk of a mistaken fact cannot avoid a contract. Id.
>
> A party bears the risk of a mistake when:
>
> (a) the risk is allocated to him by agreement of the parties, or
>
> (b) he is aware, at the time the contract is made that he has only limited knowledge with respect to the facts to which the mistake relates but treats his limited knowledge as sufficient, or
>
> (c) the risk is allocated to him by the court on the ground that it is reasonable in the circumstances to do so.
>
> Restatement (Second) Contracts, § 154 (1979) * * * *.

Did the purchaser of Rose 2d of Aberlone assume the risk of the mistake? Did the seller? Did any of the judges consider assumption of risk?

5. Suppose a farmer sells his farm to another farmer who discovers oil under the property before closing. Can the first farmer sue to rescind the sale on the basis of mutual mistake, do you think?

6. In Lenawee County Bd. of Health v. Messerly, 331 N.W.2d 203 (Mich. 1982), the Michigan Supreme Court limited Sherwood "to its facts," which more or less takes away all of its precedential value but does not overrule the case.

Note: Consideration, Fairness of Exchange, and How Contract Breach Litigation Works

Now that we have studied duress and mutual mistake, you can begin to understand the courts' hands-off approach to consideration—that a court does not judge consideration's "adequacy"—and why that is necessary even while the court later looks at the exchange's fairness under other doctrines. The key lies in your recognition that consideration is an element of the plaintiff's prima facie case; it is something only the plaintiff proves.

"A plaintiff asserting a breach-of-contract claim must prove (1) the existence of a valid contract . . . ." *USAA Texas Lloyds Co. v. Menchaca*, 545 S.W.3d 479, 502 n.21 (Tex. 2018). How does the plaintiff allege or prove "the existence of a valid contract"? By alleging and offering evidence of each of the elements of a contract that we are studying: "competent parties, legal subject-matter, valuable consideration, and mutual

assent," as well as definiteness or specificity. *See Intro* to this book and also the Meta Rules. Alleging those things, any performance due from the plaintiff, breach, and harm gets the plaintiff into court. Plaintiffs bring cases. This is the way litigation works.

If the plaintiff's complaint does not allege facts that show prima facie formation of a valid contract, then the defendant can move for, and the court should grant, dismissal on grounds that the complaint fails to state a claim. Under the Federal Rules of Civil Procedure, the defendant generally makes the motion before or with the answer to the complaint. *See* FRCP 12(b), 12(h) ("A motion asserting any of these defenses must be made before pleading if a responsive pleading is allowed."). The court must be able to rule on a motion to dismiss at this point in the litigation.

The court also has an obligation to review a plaintiff's complaint for the elements of formation before the court grants the plaintiff a default judgment. *See* FRCP 55(b)(1) ("If the plaintiff's *claim* . . . ." (emphasis added)); *Gesualdi v. Quadrozzi Equip. Leasing Corp.*, 629 Fed.Appx. 111, 113 (2d Cir. 2015) ("Before a district court enters a default judgment, it must determine whether the allegations in a complaint establish the defendants' liability as a matter of law."). Plaintiffs can ask for a default judgment if the plaintiff has pleaded a valid prima facie claim, the court has subject matter jurisdiction and jurisdiction over the defendant, and the defendant has been served process. Due process is required, but many defendants never show up in court. Not showing up is not a way to avoid liability. The court must be able to grant default judgment. In these two instances, when the court has before it only the plaintiff's allegations—before the defendant has said anything—the court must be able to rule.

Because consideration is an element of the plaintiff's prima facie case, it must be provable on evidence that only the plaintiff would have and would offer. A plausible exchange—consideration—is just that sort of thing. The plaintiff can show the court the exchange. That gives the court a sneak peek into the fairness of the bargain, if only from the plaintiff's allegations.

But no one should expect *the plaintiff* to show that the exchange was unfair. That is defendant's evidence. It is evidence only the defendant has an incentive to show, and much of the time only the defendant would have access to evidence showing unfairness. So when the defendant answers, the defendant alleges doctrines that show that the bargain was unfair—duress, mistake, misrepresentation, unconscionability. These are defenses that the defendant raises by name (that is why they are called "affirmative" defenses). After the court has before it evidence from both the plaintiff and defendant regarding unfairness (the bargain and a defense), the court is free to consider unfairness, and the defenses are the court's tools to address that larger issue.

Given the way contract litigation works, then, the law is not conflicted when it says it will not consider the adequacy of consideration but will consider whether a threat is improper in part because "the resulting exchange is not on fair terms." R2K § 176(2). Unconscionability, when you get to it, is even more intrusive, and many courts under that doctrine will unwind a contract because the terms unreasonably favor one party. But that does not mean that contract law is contradictory; it merely means that the law is practical and requires judges to make important calls only when the proper evidence is introduced at the appropriate stage of litigation.

E. Unilateral Mistake

BARBER CONTRACTING COMPANY v. FIRST BAPTIST CHURCH OF MOULTRIE

Court of Appeals of Georgia (1989)

377 S.E.2d 717

McMURRAY, Presiding Judge.

[¶1] The First Baptist Church of Moultrie, Georgia, invited bids for the construction of a music, education and recreation building. The bids were to be opened on May 15, 1986. They were to be accompanied by a bid bond in the amount of 5 percent of the base bid. The bidding instructions provided, in pertinent part: "Negligence on the part of the bidder in preparing the bid confers no right for the withdrawal of the bid after it has been opened."

[¶2] Barber Contracting Company ("Barber") submitted a bid for the project in the amount of $1,860,000. The bid provided, in pertinent part: "For and in consideration of the sum of $1.00, the receipt of which is hereby acknowledged, the undersigned agrees that this proposal may not be revoked or withdrawn after the time set for the opening of bids but shall remain open for acceptance for a period of thirty-five (35) days following such time." The bid also provided that if it was accepted within 35 days of the opening of bids, Barber would execute a contract for the construction of the project within 10 days of the acceptance of the bid.

[¶3] A bid bond in the amount of 5 percent of Barber's bid ($93,000) was issued by The American Insurance Company to cover Barber's bid. With regard to the bid bond, the bid submitted by Barber provided: "If this proposal is accepted within thirty-five (35) days after the date set for the opening of bids and the undersigned [Barber] fails to execute the contract within ten (10) days after written notice of such acceptance ... the obligation of the bid bond will remain in full force and effect and the money payable thereon shall be paid into the funds of the Owner as liquidated damages for such failure ..."

[¶4] The bids were opened by the church on May 15, 1986, as planned. Barber submitted the lowest bid. The second lowest bid, in the amount of $1,975,000 was submitted by H & H Construction and Supply Company, Inc. ("H & H").

[¶5] Barber's president, Albert W. Barber was present when the bids were opened, and of course, he was informed that Barber was the low bidder. Members of the church building committee informally asked President Barber if changes could be made in the contract to reduce the amount of the bid. He replied that he was sure such changes could be made.

[¶6] On May 16, 1986, Albert W. Barber informed the architect for the project, William Frank McCall, Jr., that the amount of the bid was in error—the bid should have been $143,120 higher. In Mr. Barber's words: "[T]he mistake in Barber's bid was caused by an error in totaling the material costs on page 3 of Barber's estimate work sheets. The subtotal of the material cost listed on that page is actually $137,990. The total listed on Barber's summary sheet for the material cost subtotal was $19,214. The net error in addition was $118,776. After adding in mark-ups for sales tax (4 percent), overhead and profit (15 percent), and bond

procurement costs (.75 percent), the error was compounded to a total of $143,120 ...” The architect immediately telephoned Billy G. Fallin, co-chairman of the church building committee, and relayed the information which he received from President Barber.

[¶7] On May 20, 1986, Barber delivered letters to the architect and the church. In the letter to the architect, Barber enclosed copies of its estimate sheets and requested that it be permitted to withdraw its bid. In the letter to the church, Barber stated that it was withdrawing its bid on account of “an error in adding certain estimated material costs.” In addition, Barber sought the return of the bid bond from the church.

[¶8] On May 29, 1986, the church forwarded a construction contract, based upon Barber’s bid, to Barber. The contract had been prepared by the architect and executed by the church. The next day, Barber returned the contract to the church without executing it. In so doing, Barber pointed out that its bid had been withdrawn previously.

[¶9] On July 25, 1986, the church entered into a construction contract for the project with H & H, the second lowest bidder. Through deletions and design changes, the church was able to secure a contract with H & H for $1,919,272.

[¶10] In the meantime, the church demanded that Barber and The American Insurance Company pay it $93,000 pursuant to the bid bond. The demand was refused.

[¶11] On May 26, 1987, the church brought suit against Barber and The American Insurance Company seeking to recover the amount of the bid bond. Answering the complaint, defendants denied they were liable to plaintiff.

[¶12] Thereafter, defendants moved for summary judgment and so did the plaintiff. In support of their summary judgment motions, defendants submitted the affidavit of Albert W. Barber. He averred that in preparing its bid, Barber exercised the level of care ordinarily exercised by contractors submitting sealed bids. In support of its summary judgment motion, the church submitted the affidavit of a building contractor who averred that he would never submit a bid of any magnitude without obtaining assistance in verification and computation.

[¶13] The trial court denied the summary judgment motions, certified its rulings for immediate review and we granted these interlocutory appeals. Held:

[¶14] The question for decision is whether Barber was entitled to rescind its bid upon discovering that it was based upon a miscalculation or whether Barber should forfeit its bond because it refused to execute the contract following the acceptance of its bid by the church. We hold that Barber was entitled to rescind its bid.

[¶15] That equity will rescind a contract upon a unilateral mistake is a generally accepted principle. See Corbin on Contracts, § 609 (1960). As it is said: “Where a mistake of one party at the time a contract was made as to a basic assumption on which he made the contract has a material effect on the agreed exchange of performances that is adverse to him, the contract is voidable by him if he does not bear the risk of the mistake ... and (a) the effect of the mistake is such that enforcement of the contract would be unconscionable, or (b) the other party had reason to know of the mistake or his fault caused the mistake.” Restatement (2d) of Contracts, § 153 (1979).

[¶16] The following illustration demonstrates the rule: “In response to B’s invitation for bids on the construction of a building according to stated specifications, A submits an offer to do the work for $150,000. A believes that this is the total of a column of figures, but he has made an error by inadvertently omitting a $50,000 item, and in fact the total is $200,000. B, having no reason to know of A’s mistake, accepts A’s bid. If A performs for $150,000, he will sustain a loss of $20,000 instead of making an expected profit of $30,000. If the court determines that enforcement of the contract would be unconscionable, it is voidable by A.” Restatement (2d) of Contracts, § 153 (1979) (Illustration 1).

[¶17] Corbin explains: “Suppose ... a bidding contractor makes an offer to supply specified goods or to do specified work for a definitely named price, and that he was caused to name this price by an antecedent error of computation. If, before acceptance, the offeree knows, or has reason to know, that a material error has been made, he is seldom mean enough to accept; and if he does accept, the courts have no difficulty in throwing him out. He is not permitted ‘to snap up’ such an offer and profit thereby. If, without knowledge of the mistake and before any revocation, he has accepted the offer, it is natural for him to feel a sense of disappointment at not getting a good bargain, when the offeror insists on withdrawal; but a just and reasonable man will not insist upon profiting by the other’s mistake. There are now many decisions to the effect that if the error was a substantial one and notice is given before the other party has made such a change of position that he cannot be put substantially in status quo, the bargain is voidable and rescission will be decreed.” Corbin on Contracts, § 609 (1960).

[¶18] Georgia law is no different. It provides for rescission and cancellation “upon the ground of mistake of fact material to the contract of one party only.” OCGA § 23-2-31. The mistake must be an “unintentional act, or omission, or error arising from ignorance, surprise, imposition, or misplaced confidence.” OCGA § 23-2-21 (a). But relief will be granted even in cases of negligence if the opposing party will not be prejudiced. OCGA § 23-2-32.

[¶19] We can see these principles at work in *M. J. McGough Co. v. Jane Lamb Memorial Hosp.*, 302 F. Supp. 482 (SD Iowa 1969). In that case, a bid of $1,957,000 was submitted for a hospital improvement by a contractor. A bond in the amount of $100,000 was given to secure the contractor’s bid. The contractor submitted the lowest bid. After the bids were opened, but before its bid was accepted, the contractor informed the hospital that it erroneously transcribed numbers in computing the bid and that, therefore, it underbid the project by $199,800. Nevertheless, the hospital tried to hold the contractor to its bid. When the contractor refused to execute a contract, the hospital awarded the contract to the next lowest bidder. The contractor and surety sought rescission of the bid and the return of the bond. The hospital sued the contractor and surety for damages. The district court allowed the contractor to rescind. Its decision is noteworthy and illuminating. We quote it at length:

> [¶a] “By the overwhelming weight of authority a contractor may be relieved from a unilateral mistake in his bid by rescission under the proper circumstances. See generally Annot., 52 ALR2d 792 (1957). The prerequisites for obtaining such relief are: (1) the mistake is of such consequence that enforcement would be unconscionable; (2) the mistake must relate to the substance of the consideration; (3) the mistake must have occurred regardless of the exercise of ordinary care; (4) it must be possible to place the other party in status quo. [Cits.] It is also generally required that the bidder give prompt notification of the mistake and his intention to withdraw. [Cits.] ...

> [¶b] "Applying the criteria for rescission for a unilateral mistake to the circumstances in this case, it is clear that [the contractor] and his surety ... are entitled to equitable relief. The notification of mistake was promptly made, and [the contractor] made every possible effort to explain the circumstances of the mistake to the authorities of [the hospital]. Although [the hospital] argues to the contrary, the Court finds that notification of the mistake was received before acceptance of the bid. The mere opening of the bids did not constitute the acceptance of the lowest bid ... Furthermore, it is generally held that acceptance prior to notification does not bar the right to equitable relief from a mistake in the bid. [Cits.]
>
> [¶c] "The mistake in this case was an honest error made in good faith. While a mistake in and of itself indicates some degree of lack of care or negligence, under the circumstances here there was not such a lack of care as to bar relief....
>
> [¶d] "The mistake here was a simple clerical error. To allow [the hospital] to take advantage of this mistake would be unconscionable. This is especially true in light of the fact that they had actual knowledge of the mistake before the acceptance of the bid. [Cits.] Nor can it be seriously contended that a $199,800 error, amounting to approximately 10 percent of the bid, does not relate directly to the substance of the consideration. Furthermore, [the hospital] has suffered no actual damage by the withdrawal of the bid of [the contractor]. The Hospital has lost only what it sought to gain by taking advantage of [the contractor's] mistake. [Cits.] Equitable considerations will not allow the recovery of the loss of bargain in this situation." *M. J. McGough Co. v. Jane Lamb Memorial Hosp*., 302 F. Supp. 482, 485, 486, *supra*.

[¶20] In the case sub judice, Barber, the contractor, promptly notified the plaintiff that a mistake was made in calculating the amount of the bid. The plaintiff had actual knowledge of the mistake before it forwarded a contract to Barber. The mistake was a "simple clerical error." *M. J. McGough Co. v. Jane Lamb Memorial Hosp.*, 302 F. Supp. 482, 485, *supra*. *See* OCGA § 23-2-21 (a). It did not amount to negligence preventing equitable relief. *See* OCGA § 23-2-32 (a). Furthermore, it was a mistake which was material to the contract (OCGA § 23-2-31)—it went to the substance of the consideration. (The mistake amounted to approximately seven percent of the bid.) To allow the plaintiff to take advantage of the mistake would not be just. *M. J. McGough Co. v. Jane Lamb Memorial Hosp*., *supra* at 486. *See also Shelton & Co. v. Ellis*, 70 Ga. 297 (1883).

[¶21] The contention is made that Barber's miscalculation constituted negligence sufficient to prevent relief in equity. See OCGA § 23-2-32(a). Assuming, arguendo, that the error stemmed from such a want of prudence as to violate a legal duty (OCGA § 23-2-32 (a)), we must nevertheless conclude that Barber is entitled to rescission.

[¶22] Relief in equity "may be granted even in cases of negligence by the complainant if it appears that the other party has not been prejudiced thereby." OCGA § 23-2-32 (b). It cannot be said that plaintiff was prejudiced by Barber's rescission. After all, plaintiff "lost only what it sought to gain by taking advantage of [the contractor's] mistake." *M. J. McGough Co. v. Jane Lamb Memorial Hosp*., *supra* at 486.

[¶23] The plaintiff takes the position that rescission is improper since, pursuant to the language set forth in the bid, Barber agreed not to withdraw the bid for a period of 35 days after the bids were opened. It also asserts that the language set forth in the bidding instructions prohibited Barber from withdrawing the bid on

the ground of “negligence.” We disagree. “[P]rovisions such as these have been considered many times in similar cases, and have never been held effective when equitable considerations dictate otherwise. [Cits.]” *M. J. McGough Co. v. Jane Lamb Memorial Hosp*., 302 F. Supp. 482, 487, *supra.*

[¶24] The trial court properly denied the plaintiff’s (the church’s) motion for summary judgment. It erred in denying defendants’ (Barber’s and The American Insurance Company’s) motions for summary judgment.

[¶25] Judgment affirmed in Case No. 77340; judgment reversed in Case No. 77341.

POPE and BENHAM, JJ., concur.

Question: In what ways is unilateral mistake doctrine different from mutual mistake doctrine?

F. Misrepresentation

Misrepresentation Law

Misrepresentation renders a contract voidable by the party relying on the misrepresentation.

A misrepresentation exists if:

1) one party makes a false statement, or misleading omission in breach of a duty to speak,

2) of a material fact,

3) on which the other party relies in entering the contract,

4) reasonably.

The fact misrepresented need not be material if the false statement is made with the intent to mislead.

No duty to speak exists when the parties deal at arm’s length and the underlying facts are reasonably within the knowledge of both parties. Under such circumstances, the other party is obliged to take reasonable steps to inform himself, and to protect his own interests. A duty to speak arises, however, when the omitting party is or should be aware of circumstances that would make an omission misleading.

Does the falsity of a statement depend on whether the person making the statement knows it is false?

Consider the following case as an application of the rules:

Dale E. GEARHART v. Martin GOEHNER and Ella Goehner

Or. App. (1985)

701 P.2d 461

Opinion

ROSSMAN, Judge

[1] Plaintiff brought this action seeking specific performance of an installment land sale contract. Defendant Martin Goehner filed a counterclaim seeking rescission on the ground of misrepresentation. [Although Ella Goehner joined in the counterclaim, all references to the defendant will be to defendant Martin Goehner.] The trial court entered a judgment allowing rescission and restitution, and plaintiff appeals. On de novo review, we modify the judgment.

[2] On August 17, 1980, plaintiff and defendant entered into an earnest money agreement for the sale of a house divided into two rental units, and a building, part of which held a convenience grocery store called Jiffy Market. On September 3, 1980, they entered into an earnest money agreement for the sale of plaintiff's market business, which included gasoline sales. Defendant bought the properties primarily to remodel the unused part of the building and to operate a restaurant in it. He purchased the grocery business expecting that its profits would help him support the contract payments. Defendant began remodeling the building in September, even though the transaction did not close until October 24, 1980, when the installment contract was signed.

[3] Just before closing, defendant became concerned with his ability to make the contract payments. He asked Fay Priss, the real estate agent involved in the transaction, to arrange a meeting with plaintiff in order to examine the market's books and records. Priss, in turn, called her broker, Wallace, who arranged a meeting with plaintiff to take place that day at the market. All parties understood that the purpose of the meeting was to assess the profitability of the business.

[4] When defendant arrived, he was informed by plaintiff that the books and records were unavailable. Defendant testified that in response he proclaimed an end to the meeting and the entire transaction but that he was then persuaded by Wallace to remain and listen to plaintiff's information about the business.

[5] Plaintiff had just finished tallying the previous week's sales of groceries and gasoline. He handed the tally sheet to defendant, who sat down to do some computations. Plaintiff stood behind him and observed. Defendant first multiplied the week's sales figures by four to arrive at a monthly figure for groceries and gasoline. Defendant testified that he then asked for and received from plaintiff percentage figures, known as gross profit margin, that could be applied to the sales totals for groceries and gasoline to determine gross profit. Plaintiff testified that he was asked for and offered the markup percentage on the cost of the goods sold. [Footnote: The difference is significant. For example, if goods that cost $100 are sold for $150, for a gross profit of $50, the markup is 50 percent and the gross profit margin is 33 percent. Thus, if one mistakenly applied the markup percentage to the sales figure, the gross

profit would be incorrectly inflated to $75. That is the mistake plaintiff claims was made by defendant.] It is certain, however, that plaintiff had supplied to defendant only the sales figures, not the cost of the goods sold. Defendant testified that plaintiff represented the gross profit margin to be 30 percent for groceries and 25 percent for gasoline, although the actual gross profit margin was 25 percent for groceries and 15 percent for gasoline. Plaintiff testified that he represented those figures as markup percentages; as such, they are fairly accurate.

[6] In any event, defendant applied those percentages to the sales figures to arrive at a monthly gross profit for groceries and gasoline. Defendant then asked for and received the market's monthly operating expenses. Defendant subtracted those expenses from the gross profit to obtain a net profit of $5,171 per month. (During 1980, until the time of this transaction, the market had actually been averaging $1,400 net profit per month.)

[7] Defendant then deducted from his calculated figure the total monthly payments on the purchase of the property and the lease payments for some of the equipment, resulting in a positive cash flow of $2,501 per month. Plaintiff then told defendant that the rental house had two apartments and that the rent totalled $450 per month. Thus, defendant concluded that he would have approximately $3,000 per month to live on.

[8] The tally sheet with defendant's computations was handed back to plaintiff. Defendant testified that plaintiff then said, "Yes, this is okay." Plaintiff testified that he said either "It looks fine to me" or "It looks fine to him." His concerns allayed, defendant decided to complete the transaction.

[9] The installment contract was signed on October 24, 1980, and on the next day defendant began to operate the market. Within two to three months defendant became concerned that the market was not producing the anticipated income. Testimony by a third party indicates that in February defendant raised this issue with plaintiff who reaffirmed the figures given and computations made during the meeting in the grocery store. On March 1, 1981, defendant opened the restaurant. Later in March, defendant asked his accountant to analyze the market's operations, and his accountant expressed reservations. Defendant then sought legal advice and was advised to withhold further contract payments. During April and May, defendant and plaintiff attempted to meet to resolve their problems. Finally, on May 28, 1981, a meeting was arranged between them and their attorneys to look for a solution. They failed to reach an accord. On July 1 plaintiff filed his action for specific performance, and on July 2, defendant gave notice of rescission.

[10] Plaintiff's five assignments of error raise the following issues: (1) did defendant prove by clear and convincing evidence that plaintiff misrepresented the market "s profitability, either innocently or intentionally; (2) did defendant justifiably rely on plaintiff's representations in making his decision to purchase the property; (3) if there was a misrepresentation, did defendant, after discovery, promptly rescind the contract; (4) if the misrepresentation established was innocent, does the merger clause in the contract preclude relief . . . .

[11] Plaintiff contends that he made no false representations during the meeting in the office of the grocery store. However, he testified that, when he was handed defendant's worksheet, he affirmed, or at least did not dispute, its erroneous conclusion that the market netted approximately $5,000 per month, even though he knew that the market did not generate a net profit close to that amount. It is not necessary to discern plaintiff's precise words. If he said "It looks fine to me," he affirmatively misrepresented the

market's net monthly profit, and if he said, "It looks fine to him," he implicitly misrepresented the profit, because plaintiff had, at that time, a duty to clarify defendant's misapprehension. * * * * We conclude that plaintiff intentionally misrepresented the market's profitability.

[12] We are presented, therefore, with plaintiff's contention that defendant was not justified in relying on plaintiff's misrepresentation. That contention is based on the uncontroverted testimony of Priss, which indicates that plaintiff warned defendant "that a tape of any one particular week would not be indicative of what [the market] would do the rest of the year" and that "he couldn't guarantee what was going to happen when anybody else ran it."

[13] Plaintiff's contention is flawed for two reasons. First, defendant's claim relates to plaintiff's misrepresentation of the immediate past profitability of the market. As to that misrepresentation, plaintiff's disclaimers about the future performance of the business are immaterial. * * * *

"A purchaser who has, in fact, been induced to enter a contract by an intentional misrepresentation may rescind the contract even though his reliance may have been negligent." *Bodenhamer v. Patterson*, 278 Or. 367, 374, 563 P.2d 1212 (1977).

See also Hampton v. Sabin, 49 Or.App. 1041, 1049-50, 621 P.2d 1202 (1980). Thus defendant has established his claim of intentional misrepresentation. We turn, therefore, to the question of whether defendant waived his right to assert his claim by failing to rescind the contract promptly.

[14] What constitutes prompt rescission depends on when the rescinding party became reasonably certain of the misrepresentation and whether it thereafter continued to treat the contract as viable for any considerable length of time. * * * *

[15] Defendant was in possession of the property from October 24, 1980, to June 30, 1981. There is some evidence that in December, 1980, defendant became concerned with the market's performance. There is no evidence, however, that defendant was suspicious of plaintiff's representations until February, 1981, when he raised the issue with plaintiff, and plaintiff reaffirmed his representation and appeased defendant's concerns. There is no indication, therefore, that defendant became reasonably certain that he had been defrauded until March, when he asked his accountant to analyze the market's operations and his accountant expressed concern about the market's ability to generate the profits represented.

[16] In April, defendant obtained an attorney and sought to meet with plaintiff to resolve their dispute. Plaintiff, however, delayed this meeting until May 28, 1981. At that meeting the parties attempted, but failed, to resolve their dispute. Defendant abandoned the property on June 30 and gave notice of his rescission on July 2.

[17] From the time in March when defendant became reasonably certain that he had been defrauded until July 2, his conduct consistently indicated an intent to disaffirm the contract. He halted contract payments and attempted to negotiate new contract terms. Defendant rescinded in approximately one month, after it became clear that no accord was possible. That was not a significant delay. * * * *

[18] We conclude that, because defendant protested promptly after becoming reasonably certain that he had been defrauded and then entered into good faith but ultimately fruitless negotiations for a settlement, his claim for rescission filed promptly thereafter was not too late.

[19] Because we have concluded that the misrepresentation was intentional, no clause in the contract can prevent defendant from relying on the misrepresentation to bring a suit for rescission. *Wilkinson v. Carpenter*, 276 Or. 311, 314, 554 P.2d 512 (1976). Therefore, we do not address the issue of whether the contract's merger clause would prevent defendant from relying on an innocent misrepresentation to bring a suit for rescission. [Note: We will come back to merger clauses when we study the parol evidence rule. What the court says here is true. Anyway, the merger clause would not have precluded rescission for misrepresentation.] * * * *

[20] The purpose of a restitutionary award after the rescission of a contract is to restore both parties to their former positions. *Bodenhamer v. Patterson, supra*, 278 Or. at 376, 563 P.2d 1212. However, when both parties cannot be restored, the innocent party who rescinds is entitled to be restored to his former position. Thus,

> [w]here rescission is based on fraud, and where the innocent party, before discovering the fraud, has made reasonable expenditures in reliance on the bargain, those expenses may be recovered upon rescission.

Bodenhamer v. Patterson, supra, 278 Or. at 377, 563 P.2d 1212.

[21] Plaintiff first contends that the restitutionary award of $58,834.89 is improper, because it does not represent reasonable expenditures in reliance on the bargain for the grocery store business. The award represents defendant's labor and his material and equipment costs in opening the restaurant. Plaintiff's contention is misplaced, however, because it relies on the premise rejected above, which is that the contract is divisible. The appropriate inquiries are whether the expenditures were made in reliance on the entire bargain and whether they were reasonable.

[22] Plaintiff's second contention presents the first part of this inquiry. He states that it was improper to allow the recovery for 360 hours of labor by defendant before the misrepresentation, because it was not expended in reliance on the bargain. The phrase "expenditures in reliance on the bargain" has the same meaning as the phrase "expenditures made as a result of the fraud." *Bodenhamer v. Patterson, supra*, 278 Or. at 377-78, 563 P.2d 1212; *McCormick, Damages* 449 and 458 (1935).

[23] Therefore, only reasonable expenses incurred after the misrepresentation are recoverable on a claim for rescission. Although previous expenses could be recovered on a claim of unjust enrichment, defendant does not present that claim. Accordingly, it was error to allow recovery for the 360 disputed hours expended by defendant before the fraud.

[24] The expenditures after the fraud, however, are recoverable unless they were unreasonable, as plaintiff next contends. * * * *

[25] Defendant is entitled to rescission of the contract and restitution of all reasonable expenses incurred as a result of the fraud. Those expenses, however, do not include defendant's labor before the fraud. Therefore, the restitutionary award is reduced by $5,400.

Judgment for defendant is modified to reduce restitutionary award by $5,400 to $53,434.89; affirmed as modified.

Questions:

1. Was the misrepresented fact material? What evidence would you show to prove that?

2. Was the misrepresentation in this case a mere "false statement," or was it an omission that Gearhart should have known would be misleading?

3. The rescission in this case is "legal rescission," accomplished by giving notice. Even thought the Goehners legally rescinded, they still had to prove their defense to formation when Gearhart sued to enforce. This is common. Had they paid Gearhart money on the contract, they might also have had to bring a claim for the money's return. What cause of action or claim would have been appropriate to obtain return of the money paid to Gearhart? Not contract: Gearhart had never promised to return the money. But we have studied the appropriate cause of action. What is it?

4. What if the contract said, "We will not be liable to each other for fraud, and we waive any right to rescind this contract for fraud. We have done our own due diligence and are not relying on each other at all." Would intentional misrepresentation give a party a way out? Many courts enforce "disclaimer of reliance" clauses in contracts if they meet a certain level of clarity. *See, e.g.*, *Labyrinth, Inc. v. Urich*, No. 2023-0327-MTZ, 2024 WL 295996, * (Del. Ch. Jan. 26, 2024) ("[T]he contract must contain language that, when read together, can be said to add up to a clear anti-reliance clause by which the plaintiff has contractually promised that it did not rely upon statements outside the contract's four corners in deciding to sign the contract. [M]urky integration clauses, or standard integration clauses without explicit anti-reliance representations, will not relieve a party of its oral and extra-contractual fraudulent representations." (internal citations omitted)).

Jeffrey M. STAMBOVSKY v. Helen V. ACKLEY and Ellis Realty

Supreme Court, Appellate Division, First Department, New York (1991)
572 N.Y.S.2d 672

RUBIN, Justice.

[¶1] Plaintiff, to his horror, discovered that the house he had recently contracted to purchase was widely reputed to be possessed by poltergeists, reportedly seen by defendant seller and members of her family on numerous occasions over the last nine years. Plaintiff promptly commenced this action seeking rescission of the contract of sale. Supreme Court reluctantly dismissed the complaint, holding that plaintiff has no remedy at law in this jurisdiction.

[¶2] The unusual facts of this case, as disclosed by the record, clearly warrant a grant of equitable relief to the buyer who, as a resident of New York City, cannot be expected to have any familiarity with the folklore

of the Village of Nyack. Not being a “local”, plaintiff could not readily learn that the home he had contracted to purchase is haunted. Whether the source of the spectral apparitions seen by defendant seller are parapsychic or psychogenic, having reported their presence in both a national publication (Readers’ Digest) and the local press (in 1977 and 1982, respectively), defendant is estopped to deny their existence and, as a matter of law, the house is haunted. More to the point, however, no divination is required to conclude that it is defendant’s promotional efforts in publicizing her close encounters with these spirits which fostered the home’s reputation in the community. In 1989, the house was included in a five-home walking tour of Nyack and described in a November 27th newspaper article as “a riverfront Victorian (with ghost).” The impact of the reputation thus created goes to the very essence of the bargain between the parties, greatly impairing both the value of the property and its potential for resale. The extent of this impairment may be presumed for the purpose of reviewing the disposition of this motion to dismiss the cause of action for rescission (*Harris v City of New York*, 147 AD2d 186, 188–189) and represents merely an issue of fact for resolution at trial.

[¶3] While I agree with Supreme Court that the real estate broker, as agent for the seller, is under no duty to disclose to a potential buyer the phantasmal reputation of the premises and that, in his pursuit of a legal remedy for fraudulent misrepresentation against the seller, plaintiff hasn’t a ghost of a chance, I am nevertheless moved by the spirit of equity to allow the buyer to seek rescission of the contract of sale and recovery of his down payment. New York law fails to recognize any remedy for damages incurred as a result of the seller’s mere silence, applying instead the strict rule of caveat emptor. Therefore, the theoretical basis for granting relief, even under the extraordinary facts of this case, is elusive if not ephemeral.

[¶4] “Pity me not but lend thy serious hearing to what I shall unfold” (William Shakespeare, Hamlet, Act I, Scene V [Ghost]).

[¶5] From the perspective of a person in the position of plaintiff herein, a very practical problem arises with respect to the discovery of a paranormal phenomenon: “Who you gonna’ call?” as a title song to the movie “Ghostbusters” asks. Applying the strict rule of caveat emptor to a contract involving a house possessed by poltergeists conjures up visions of a psychic or medium routinely accompanying the structural engineer and Terminix man on an inspection of every home subject to a contract of sale. It portends that the prudent attorney will establish an escrow account lest the subject of the transaction come back to haunt him and his client—or pray that his malpractice insurance coverage extends to supernatural disasters. In the interest of avoiding such untenable consequences, the notion that a haunting is a condition which can and should be ascertained upon reasonable inspection of the premises is a hobgoblin which should be exorcised from the body of legal precedent and laid quietly to rest.

[¶6] It has been suggested by a leading authority that the ancient rule which holds that mere nondisclosure does not constitute actionable misrepresentation “finds proper application in cases where the fact undisclosed is patent, or the plaintiff has equal opportunities for obtaining information which he may be expected to utilize, or the defendant has no reason to think that he is acting under any misapprehension” (Prosser, Torts § 106, at 696 [4th ed 1971]). However, with respect to transactions in real estate, New York adheres to the doctrine of caveat emptor and imposes no duty upon the vendor to disclose any information concerning the premises (*London v Courduff*, 141 AD2d 803) unless there is a confidential or fiduciary relationship between the parties (*Moser v Spizzirro*, 31 AD2d 537, *affd* 25 NY2d 941; *IBM Credit Fin. Corp. v Mazda Motor Mfg. [USA] Corp.*, 152 AD2d 451) or some conduct on the part of the seller which constitutes “active concealment” (*see*, *17 E. 80th Realty Corp. v 68th Assocs.*, AD2d [1st Dept, May 9, 1991] [dummy ventilation system constructed by seller]; *Haberman v Greenspan*, 82 Misc 2d 263 [foundation cracks

covered by seller]). Normally, some affirmative misrepresentation (*e.g.*, *Tahini Invs. v Bobrowsky*, 99 AD2d 489 [industrial waste on land allegedly used only as farm]; *Jansen v Kelly*, 11 AD2d 587 [land containing valuable minerals allegedly acquired for use as campsite]) or partial disclosure (*Junius Constr. Corp. v Cohen*, 257 NY 393 [existence of third unopened street concealed]; *Noved Realty Corp. v A. A. P. Co.*, 250 App Div 1 [escrow agreements securing lien concealed]) is required to impose upon the seller a duty to communicate undisclosed conditions affecting the premises (*contra*, *Young v Keith*, 112 AD2d 625 [defective water and sewer systems concealed]).

[¶7] Caveat emptor is not so all-encompassing a doctrine of common law as to render every act of nondisclosure immune from redress, whether legal or equitable. “In regard to the necessity of giving information which has not been asked, the rule differs somewhat at law and in equity, and while the law courts would permit no recovery of *damages* against a vendor, because of mere concealment of facts *under certain circumstances*, yet if the vendee refused to complete the contract because of the concealment of a material fact on the part of the other, equity would refuse to compel him so to do, because equity only compels the specific performance of a contract which is fair and open, and in regard to which all material matters known to each have been communicated to the other” (*Rothmiller v Stein*, 143 NY 581, 591–592 [emphasis added]). Even as a principle of law, long before exceptions were embodied in statute law (*see, e.g.*, UCC 2-312, 2-313, 2-314, 2-315; 3-417 [2] [e]), the doctrine was held inapplicable to contagion among animals, adulteration of food, and insolvency of a maker of a promissory note and of a tenant substituted for another under a lease (*see*, *Rothmiller v Stein*, *supra*, at 592–593, and cases cited therein). Common law is not moribund. *Ex facto jus oritur* (law arises out of facts). Where fairness and common sense dictate that an exception should be created, the evolution of the law should not be stifled by rigid application of a legal maxim.

[¶8] The doctrine of caveat emptor requires that a buyer act prudently to assess the fitness and value of his purchase and operates to bar the purchaser who fails to exercise due care from seeking the equitable remedy of rescission (*see, e.g.*, *Rodas v Manitaras*, 159 AD2d 341). For the purposes of the instant motion to dismiss the action pursuant to CPLR 3211(a)(7), plaintiff is entitled to every favorable inference which may reasonably be drawn from the pleadings (*Arrington v New York Times Co.*, 55 NY2d 433, 442; *Rovello v Orofino Realty Co.*, 40 NY2d 633, 634), specifically, in this instance, that he met his obligation to conduct an inspection of the premises and a search of available public records with respect to title. It should be apparent, however, that the most meticulous inspection and the search would not reveal the presence of poltergeists at the premises or unearth the property’s ghoulish reputation in the community. Therefore, there is no sound policy reason to deny plaintiff relief for failing to discover a state of affairs which the most prudent purchaser would not be expected to even contemplate (*see*, *Da Silva v Musso*, 53 NY2d 543, 551).

[¶9] The case law in this jurisdiction dealing with the duty of a vendor of real property to disclose information to the buyer is distinguishable from the matter under review. The most salient distinction is that existing cases invariably deal with the physical condition of the premises (*e.g.*, *London v Courduff*, *supra* [use as a landfill]; *Perin v Mardine Realty Co.*, 5 AD2d 685, *affd* 6 NY2d 920 [sewer line crossing adjoining property without owner’s consent]), defects in title (*e.g.*, *Sands v Kissane*, 282 App Div 140 [remainderman]), liens against the property (*e.g.*, *Noved Realty Corp. v A. A. P. Co.*, *supra*), expenses or income (*e.g.*, *Rodas v Manitaras*, *supra* [gross receipts]) and other factors affecting its operation. No case has been brought to this court’s attention in which the property value was impaired as the result of the reputation created by information disseminated to the public by the seller (or, for that matter, as a result of possession by poltergeists).

[¶10] Where a condition which has been created by the seller materially impairs the value of the contract and is peculiarly within the knowledge of the seller or unlikely to be discovered by a prudent purchaser exercising due care with respect to the subject transaction, nondisclosure constitutes a basis for rescission as a matter of equity. Any other outcome places upon the buyer not merely the obligation to exercise care in his purchase but rather to be omniscient with respect to any fact which may affect the bargain. No practical purpose is served by imposing such a burden upon a purchaser. To the contrary, it encourages predatory business practice and offends the principle that equity will suffer no wrong to be without a remedy. * * * *

[¶11] To the extent New York law may be said to require something more than "mere concealment" to apply even the equitable remedy of rescission, the case of *Junius Constr. Corp. v Cohen* (257 NY 393, *supra*), while not precisely on point, provides some guidance. In that case, the seller disclosed that an official map indicated two as yet unopened streets which were planned for construction at the edges of the parcel. What was not disclosed was that the same map indicated a third street which, if opened, would divide the plot in half. The court held that, while the seller was under no duty to mention the planned streets at all, having undertaken to disclose two of them, he was obliged to reveal the third (*see also*, *Rosenschein v McNally*, 17 AD2d 834).

[¶12] In the case at bar, defendant seller deliberately fostered the public belief that her home was possessed. Having undertaken to inform the public-at-large, to whom she has no legal relationship, about the supernatural occurrences on her property, she may be said to owe no less a duty to her contract vendee. It has been remarked that the occasional modern cases which permit a seller to take unfair advantage of a buyer's ignorance so long as he is not actively misled are "singularly unappetizing" (Prosser, Torts § 106, at 696 [4th ed 1971]). Where, as here, the seller not only takes unfair advantage of the buyer's ignorance but has created and perpetuated a condition about which he is unlikely to even inquire, enforcement of the contract (in whole or in part) is offensive to the court's sense of equity. Application of the remedy of rescission, within the bounds of the narrow exception to the doctrine of caveat emptor set forth herein, is entirely appropriate to relieve the unwitting purchaser from the consequences of a most unnatural bargain.

[¶13] Accordingly, the judgment of the Supreme Court, New York County (Edward H. Lehner, J.), entered April 9, 1990, which dismissed the complaint pursuant to CPLR 3211 (a) (7), should be modified, on the law and the facts, and in the exercise of discretion, and the first cause of action seeking rescission of the contract reinstated, without costs. * * * *

[¶14] All concur except MILONAS, J.P. and SMITH, J., who dissent in an opinion by SMITH, J. [in which Smith argued for the application of caveat emptor].

(Images of the house are easy to find online, if you are interested.)

Question: The court in *Dana v. Hershey Co*., 180 F. Supp. 3d 652 (N.D. Cal. 2016), held that Hershey did not have to disclose on its products that its supply chain includes chocolate produced in Ivory Coast using

child and slave labor, a fact Hershey had acknowledged in a public statement. What's the difference between that case and this? *See also Hodsdon v. Mars, Inc.*, 162 F. Supp. 3d 1016 (N.D. Cal. 2016). Both are claims for damages under consumer protection law and so not actions to rescind. Does that justify the difference?

G. Unconscionability

The following case comes from the sale-of-goods context, but, aside from the language of the statute itself (which is merely persuasive and not controlling outside of transactions in goods), the analysis looks much like it would in any contract case. The reason for this is that Article 2 Section 2-302, discussed in the case, did much to persuade courts to apply the doctrine as a defense to formation and not merely as a limitation on equitable remedies, which was its ancient role.

Elizabeth A. MAXWELL v. FIDELITY FINANCIAL SERVICES, INC., an Arizona Corporation

Supreme Court of Arizona, In Banc (1995)

907 P.2d 51

OPINION

FELDMAN, Chief Justice.

[¶1] Elizabeth Maxwell petitions us to review a court of appeals opinion affirming a trial court ruling that the doctrine of novation barred Maxwell's claim that a contract was unconscionable and therefore unenforceable. *See Maxwell v. Fidelity Fin. Servs., Inc*., 179 Ariz. 544, 880 P.2d 1090 (Ct.App. 1993). We granted review to examine the law dealing with grounds for novation and unconscionability and to determine whether the principles of contract interpretation announced in *Taylor v. State Farm Mut. Auto. Ins. Co*., 175 Ariz. 148, 854 P.2d 1134 (1993), are applicable to these issues.

FACTS AND PROCEDURAL HISTORY

[¶2] The facts, taken in the light most favorable to Maxwell, against whom summary judgment was granted, are that in December 1984, Elizabeth Maxwell and her then husband, Charles, were approached by Steve Lasica, a door-to-door salesman representing the now defunct National Solar Corporation (National). Lasica sold the Maxwells a solar home water heater for a total purchase price of $6,512. Although National was responsible for installation, the unit was never installed properly, never functioned properly, and was eventually declared a hazard, condemned, and ordered disconnected by the City of Phoenix. Thus, although the unit may have been intrinsically worthless, the question of unconscionability is determined as of the time the contract was made. A.R.S. § 47-2302.

[¶3] Financing for the purchase was accomplished through a loan to the Maxwells from Fidelity Financial Services, Inc. (Fidelity). The sale price was financed for a ten-year period at 19.5 percent interest, making the total cost nearly $15,000.

[¶4] At the time of the transaction, Elizabeth Maxwell earned approximately $400 per month working part-time as a hotel maid and her husband earned approximately $1,800 per month working for the local paper. At Fidelity's request, an appraisal was made of the Maxwells' South Phoenix home, where they had resided for the preceding twelve years. The appraisal showed that the Maxwells lived in a modest neighborhood, that their 1,539 square foot home was in need of a significant amount of general repair and maintenance, and that its market value was approximately $40,000.

[¶5] In connection with the financing transaction, Elizabeth Maxwell signed numerous documents, including a loan contract, a deed of trust, a truth-in-lending disclosure form, and a promissory note and security agreement. The effect of these documents was not only to secure the deferred purchase price with a lien on the merchandise sold, but also to place a lien on Maxwell's house as additional security for payment on the water heater contract. The forms and their terms were unambiguous and clearly indicated that Maxwell was placing a lien on her house. Included in the consumer credit contract between Maxwell and Fidelity was a clause expressly stating that Fidelity was subject to all claims by and defenses that Maxwell could assert against National.

[¶6] Despite the fact that the water heater was never installed or working properly, Maxwell made payments on it for approximately three and one-half years, reducing the deferred purchase balance to $5,733. In 1988, Maxwell approached Fidelity to borrow an additional $800 for purposes unrelated to the original loan. In making this second loan, Fidelity required Maxwell to again sign a bundle of documents essentially identical to those she signed in 1984. Instead of simply adding $800 to Maxwell's outstanding balance on the 1984 contract, Fidelity created a new contract that included the unpaid balance of $5,733 on the 1984 loan, a term life insurance charge of $313, as well as the new $800 loan. In all, Maxwell financed the sum of $6,976 with this second loan. The terms of this latest loan also included interest at 19.5 interest and payments for a period of six years, making Maxwell's new payments, including interest, total nearly $12,000. The combined amount Maxwell would pay under the two contracts for a non-functioning water heater and the additional $800 loan thus totals approximately $17,000, or nearly one-half the value of her home.

[¶7] Maxwell continued to make payments until 1990, when she brought this declaratory judgment action seeking, inter alia, a declaration that the 1984 contract was unenforceable on the grounds that it was unconscionable.

[¶8] Following discovery, Fidelity moved for summary judgment asserting, among other things, that the statute of limitations had run on Maxwell's claim of unconscionability and, if not, that the 1988 contract worked a novation, thereby barring any action by Maxwell on the 1984 contract [Novations are addressed in Chapter 15 of this casebook.]. Maxwell filed a memorandum in opposition to this motion and pointed to sworn testimony in her deposition, which Fidelity submitted with its motion, as raising genuine issues of material fact.

[¶9] In a brief order, the trial court granted Fidelity's motion on the theory of novation:

> The court has had under advisement [Fidelity's] motion for summary judgment. The court has considered the pleadings, the argument, and the authorities. It is ordered granting the motion. By way of explanation, the court is of the opinion that although the statute of limitations does not bar this action, the doctrine of novation does.

Minute Entry, May 31, 1991.

[¶10] The court of appeals affirmed. *Maxwell*, 179 Ariz. 544, 880 P.2d 1090. In doing so, the court found that Maxwell did not properly respond to Fidelity's motion for summary judgment and did not present any controverting evidence. * * * *

[¶11] On review from summary judgment, the appellate court views the record in a light most favorable to the party opposing summary judgment (Maxwell) and will affirm only if no genuine issue of material fact exists. We therefore review this record to determine whether it could support a finding that Maxwell's claim of unconscionability was barred by the 1988 loan. * * * * [The court first held that whether a novation was effective depended on whether the underlying contract was unconscionable.]

DISCUSSION

A. Unconscionability

1. Is the determination of unconscionability for the trier of fact or for the court to decide?

[¶12] Maxwell contends that the determination of whether a contract is unconscionable is for the trier of fact. We find no support for this position given that Arizona law, which is consistent with the law in every other jurisdiction that has ruled on this issue, clearly provides that the determination of unconscionability is to be made by the court as a matter of law. *See* A.R.S. § 47-2302;‡‡‡‡ accord RESTATEMENT (SECOND) OF CONTRACTS § 208 cmt. f (hereinafter RESTATEMENT). *See also* RICHARD W. DUSENBERG & LAWRENCE P. KING, 3 BENDER'S UNIFORM COMMERCIAL CODE SERVICE 4-173 (1995) and cases cited therein.

[¶13] Obviously, the court cannot make its determination without first making factual findings upon which to base its legal analysis. *See* A.R.S. § 47-2302(B). Therefore, when it is claimed that the contract is

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‡‡‡‡ [2] Arizona's statutory provision on unconscionability, A.R.S. § 47-2302, provides:

> A. If the court as a matter of law finds the contract or any clause of the contract to have been unconscionable at the time it was made the court may refuse to enforce the contract, or it may enforce the remainder of the contract without the unconscionable clause, or it may so limit the application of any unconscionable clause as to avoid any unconscionable result.
>
> B. When it is claimed or appears to the court that the contract or any clause thereof may be unconscionable the parties shall be afforded a reasonable opportunity to present evidence as to its commercial setting, purpose and effect to aid the court in making the determination.

unconscionable, the parties must be given an opportunity to present evidence of its commercial setting, purpose, and effect to aid the court in making the determination. *Id.*

[¶14] Such factual findings do not, however, convert the determination on unconscionability from one that is a matter of law as applied to those facts to one that is in whole a matter of fact. *See Angus Medical Co. v. Digital Equip. Corp*., 173 Ariz. 159, 167, 840 P.2d 1024, 1032 (Ct.App. 1992) ("Incidental findings of fact are made by the court rather than by a jury, but are accorded the usual weight given to such findings of fact in appellate review.") (citing RESTATEMENT § 208 cmt. f). Nor is it required that in every instance a judge hold a separate, formal evidentiary hearing to determine the contract's commercial setting, purpose, and effect. Our statute only requires a reasonable opportunity to present evidence; on a developed record, such opportunity may be equally well afforded at the hearing on a motion for summary judgment. *See Golden Reward Mining Co. v. Jervis B. Webb Co*., 772 F. Supp. 1118 (D.S.D. 1991); *Earl M. Jorgensen Co. v. Mark Constr., Inc.,* 56 Haw. 466, 540 P.2d 978 (1975). In this case, however, neither Fidelity's motion for summary judgment, Maxwell's response thereto, nor the trial court's ruling addressed the merits of the unconscionability claim; instead, they focused on the novation issue.

2. The test for unconscionability

[¶15] * * * * This court has not previously had occasion to discuss the requisite elements of unconscionability under Arizona's adoption of the Uniform Commercial Code (U.C.C.). Because Maxwell raises this issue and because resolution hinges on whether the 1984 contract may be unconscionable, we turn to an examination of unconscionability under A.R.S. § 47-2302.

3. The history of unconscionability

[¶16] Traditionally, equity courts recognized the defense of unconscionability in denying relief to plaintiffs who were guilty of unconscionable conduct. *See* DAN B. DOBBS, 2 LAW OF REMEDIES 703 (2d ed. 1993). Because barring relief was a matter of the chancellor's discretion, equity never developed a clear set of rules for analyzing claims of unconscionability. *See id.* Additionally, in equity unconscionability served as a remedial doctrine, limiting a party's remedies without truly affecting its substantive legal rights. *Id.* at 704. However, the enactment of an unconscionability defense under U.C.C. Article 2 changed that. The rule as it now exists is largely substantive, working primarily as a defense both in law and in equity and applying to claims for damages as well as specific performance. *Id.* at 704-05.

[¶17] Although U.C.C. § 2-302 recognized and codified the amorphous equitable doctrine, it did little to provide a set of rules for analyzing claims of unconscionability. Also lacking in the statutory recognition of unconscionability is a definition of that term. Courts and respected commentators alike have grappled with defining and applying unconscionability under the Code since its adoption. To this day, both groups remain divided on the proper method for doing so, though they share some common ground on defining such a test.

[¶18] Within this common area, the elements of unconscionability can be ascertained to fulfill the Code's obvious intent of protecting against unconscionable contracts while not unnecessarily denying parties the

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(Emphasis added.) This provision is an exact analog of U.C.C. § 2-302. We note that subpart B allows the court to raise the issue of unconscionability sua sponte.

benefit of their bargain. Although no litmus test exists, the cases do provide a reasonable, workable analysis.

4. Divisions of unconscionability under the U.C.C.

[¶19] This court previously has acknowledged that the unconscionability principle involves an assessment by the court of:

> whether, in the light of the general commercial background and the commercial needs of the particular trade or case, the clauses involved are so one-sided as to be unconscionable under the circumstances existing at the time of the making of the contract. . . . The principle is one of the prevention of oppression and unfair surprise ... not of disturbance of allocation of risks because of superior bargaining power.

Seekings v. Jimmy GMC of Tucson, Inc., 130 Ariz. 596, 602, 638 P.2d 210, 216 (1981) (citations omitted). This somewhat circular articulation of the principle, however, is not readily applicable to the infinite variety of cases that may involve the doctrine of unconscionability.

[¶20] The framework upon which the vast majority of courts construct their analysis consists of the well recognized division of unconscionability into substantive and procedural parts. *See, e.g.*, JAMES J. WHITE & ROBERT S. SUMMERS, 1 UNIFORM COMMERCIAL CODE 204, n. 8 and cases cited therein; JOHN D. CALAMARI & JOSEPH M. PERILLO, CONTRACTS 406 (3d ed. 1987). Professor Dobbs provides the following explanation of the difference between these two types:

> Procedural or process unconscionability is concerned with “unfair surprise,” fine print clauses, mistakes or ignorance of important facts or other things that mean bargaining did not proceed as it should. Substantive unconscionability is an unjust or “one-sided” contract. Substantive unconscionability is important in two ways. First, substantive unconscionability sometimes seems sufficient in itself to avoid a term in the contract. Second, substantive unconscionability sometimes helps confirm or provide evidence of procedural unconscionability.

DOBBS, supra at 706 (footnote omitted). This dichotomy evolved from a distinction made by the late Professor Leff in his oft-cited article *Unconscionability and The Code: The Emperor’s New Clause*, 115 U.PA.L.REV. 485, 487 (1967). In his article, Professor Leff distinguished between “bargaining naughtiness” (procedural unconscionability) and overly harsh terms (substantive unconscionability). Id.

[¶21] Over the years, courts have refined the two divisions of unconscionability and identified several factors that are indicative of each. Procedural unconscionability was well-explained *in Johnson v. Mobil Oil Corp*.:

> Under the procedural rubric come those factors bearing upon ... the real and voluntary meeting of the minds of the contracting party: age, education, intelligence, business acumen and experience, relative bargaining power, who drafted the contract, whether the terms were explained to the weaker party, whether alterations in the printed terms were possible, whether there were alternative sources of supply for the goods in question.

415 F. Supp. 264, 268 (E.D.Mich. 1976) (internal quotations omitted). As Professors White and Summers have noted, procedural unconscionability bears a strong resemblance to its "common-law cousins" of fraud and duress. WHITE & SUMMERS, supra at 204.

[¶22] Substantive unconscionability concerns the actual terms of the contract and examines the relative fairness of the obligations assumed. *Resource Management Co. v. Weston Ranch & Livestock Co*., 706 P.2d 1028, 1041 (Utah 1985). Indicative of substantive unconscionability are contract terms so one-sided as to oppress or unfairly surprise an innocent party, an overall imbalance in the obligations and rights imposed by the bargain, and significant cost-price disparity. Id. (citations and internal quotations omitted).

[¶23] We believe these authorities provide useful illustrations of both divisions of unconscionability under the U.C.C., although we do not restrict applicability of the doctrine to the factors outlined.

5. Application

[¶24] The point of agreement by courts on the substantive-procedural elements also marks a point of departure in analyzing claims of unconscionability. *See generally* WHITE & SUMMERS, supra at 218-20. Many courts, perhaps a majority, have held that there must be some quantum of both procedural and substantive unconscionability to establish a claim, and take a balancing approach in applying them. *Id.* at 219. *See also* 2 WILLIAM D. HAWKLAND, UNIFORM COMMERCIAL CODE SERIES § 2-302:05 (1984) and cases cited therein. Other courts have held that it is sufficient if either is shown. *See, e.g., Gillman v. Chase Manhattan Bank, N.A*., 73 N.Y.2d 1, 537 N.Y.S.2d 787, 794, 534 N.E.2d 824, 829 (1988) ("While determinations of unconscionability are ordinarily based on the court's conclusion that both the procedural and substantive components are present ..., there have been exceptional cases where a provision of the contract is so outrageous as to warrant holding it unenforceable on the ground of substantive unconscionability alone.") (citing *State v. Wolowitz*, 96 A.D.2d 47, 468 N.Y.S.2d 131 (1983)). In addition to the numerous courts holding that either procedural or substantive unconscionability is sufficient,[§§§§] the leading commentators in this field have also endorsed this position. *See* WHITE & SUMMERS, supra at 220 (advocating the sufficiency of excessive price alone).

[§§§§] [3] See, e.g., Resource Management Co. v. Weston Ranch & Livestock Co., 706 P.2d 1028, 1043 (Utah 1985) ("Gross disparity in terms, absent evidence of procedural unconscionability, can support a finding of unconscionability."); American Home Improvement, Inc. v. MacIver, 105 N.H. 435, 201 A.2d 886, 889 (1964) (relying explicitly on U.C.S. § 2-302 and finding unconscionable, based on price-value disparity, a contract requiring payment of $1,609 for goods and services valued at "far less"); World Enter., Inc. v. Midcoast Aviation Serv., Inc., 713 S.W.2d 606, 610 (Mo. App. 1986) ("Unconscionability is defined as either procedural or substantive."); Frank's Maintenance & Eng'g, Inc. v. C.A. Roberts Co., 86 Ill. App.3d 980, 42 Ill. Dec. 25, 31-32, 408 N.E.2d 403, 409-10 (1980) ("Unconscionability can be either procedural or substantive or a combination of both.") (emphasis added). Cf. Schroeder v. Fageol Motors, Inc., 86 Wash.2d 256, 544 P.2d 20, 23 (1975) (en banc) (recognizing that cases fall within the two classifications of procedural and substantive unconscionability).

Indeed, it has long been recognized that gross disparity in terms may satisfy the standard for unconscionability by itself. See Marks v. Gates, 154 F. 481, 483 (9th Cir.1907) (inadequacy of consideration sufficient ground for withholding specific performance if it is so gross as to render the contract unconscionable).

[¶25] The cases that require a showing of both procedural and substantive unconscionability appear to be rather fact-specific, based more on the historical reluctance of courts to disturb contracts than on valid doctrinal under-pinning.

> In some cases substantive unconscionability is found because the contract price is grossly excessive (or sometimes grossly inadequate). Most of these cases present additional elements such as actual misrepresentations, gross mistreatment of people who are already disadvantaged, or a subject matter such as premarital settlements that calls for intense state scrutiny by judges. In some of them, the substantive unconscionability really seems to be evidentiary only, that is, as confirming the conclusion that the process of bargaining was itself defective.

DOBBS, supra at 707 (footnote omitted) (emphasis added); see also CALAMARI & PERILLO, supra at 406 ("[C]ontracts involving grossly unequal exchanges almost always involve some impropriety in the negotiating process or disability of a party."); WHITE & SUMMERS, supra at 218 ("Almost all of [the cases finding substantively unconscionable terms] exhibit creditor behavior that may be regarded as both procedurally and substantively unconscionable.").

[¶26] Additional evidence that the dual requirement position is more coincidental than doctrinal is found within the very text of the statute on unconscionability, which explicitly refers to "the contract or any clause of the contract." A.R.S. § 47-2302 (emphasis added). Conspicuously absent from the statutory language is any reference to procedural aspects. That the U.C.C. contemplated substantive unconscionability alone to be sufficient is the most plausible reading of the language in § 47-2302, given that the Code itself provides for per se unconscionability if there exists, without more, a substantive term in the contract limiting consequential damages for injury to the person in cases involving consumer goods. *See* A.R.S. § 47-2719(C). It is wholly inconsistent to assert that unconscionability under § 47-2302 requires some procedural irregularity when unconscionability under § 47-2719 clearly does not.

[¶27] Therefore, we conclude that under A.R.S. § 47-2302, a claim of unconscionability can be established with a showing of substantive unconscionability alone, especially in cases involving either price-cost disparity or limitation of remedies. If only procedural irregularities are present, it may be more appropriate to analyze the claims under the doctrines of fraud, misrepresentation, duress, and mistake, although such irregularities can make a case of procedural unconscionability. *See Resource Management Co.*, 706 P.2d at 1043. However, we leave for another day the questions involving the remedy for procedural unconscionability alone.

[¶28] We conclude further that this case presents a question of at least substantive unconscionability to be decided by the trial court. From the face of it, we certainly cannot conclude that the contract as a whole is not unconscionable, given the $6,500 price of a water heater for a modest residence, payable at 19.5 percent interest, for a total time-payment price of $14,860.43. These facts present at least a question of grossly-excessive price, constituting substantive unconscionability. *See* DOBBS, supra at 707; WHITE & SUMMERS, supra at § 4-5 and cases cited therein. This contract is made even more harsh by its security terms, which, in the event of non-payment, permit Fidelity not only to repossess the water heater but foreclose on Maxwell's home. The apparent injustice and oppression in these security provisions not only may constitute substantive unconscionability but also may provide evidence of procedural unconscionability. *See* DOBBS, supra at 706-07 (citing *Williams v. Walker-Thomas Furniture Co.*, 350 F.2d 445 (D.C. Cir.1965)).

[¶29] Under the U.C.C. as enacted in A.R.S. § 47-2302, the court may "refuse enforcement of the contract altogether." DOBBS, supra at 705; RESTATEMENT § 208. The present factual record, before the statutorily required evidentiary hearing, certainly contains some evidence that the entire 1984 contract, including sale price, security provisions, and remedies, is unenforceable. We therefore turn to the effect of the doctrine of novation in such a situation. * * * *

CONCLUSION

[¶30] We are not satisfied from the state of this record that Fidelity had a meaningful opportunity to present evidence on the commercial setting, purpose, and effect of the 1984 contract, as required by A.R.S. § 47-2302. * * * *

[¶31] Therefore, we vacate the court of appeals' opinion, reverse the trial court's judgment, and remand to the trial court for proceedings consistent with this opinion and A.R.S. § 47-2302.

MOELLER, V.C.J., and CORCORAN and ZLAKET, JJ., concur.

MARTONE, Justice, concurring in the judgment.

[¶1] I would hold that the 1984 contract and the 1988 contract are unconscionable as a matter of law. As the majority acknowledges, a declaration of unconscionability under A.R.S. § 47-2302(A) is a legal conclusion to be made by the court. And the evidence referred to in § 47-2302(B) "is for the court's consideration, and not the jury's." U.C.C. § 2-302, Comment 3 (1962). The facts as outlined by the majority lead to one inescapable conclusion: one of unconscionability. If these contracts are not unconscionable as a matter of law, what contract would be? * * * *

[¶2] On the undisputed facts, the commercial setting, purpose and effect of the contracts are tragically plain. The commercial setting: a "now defunct" entity, ante, at 84, 907 P.2d at 53, took advantage of a limited person living on the margin of human existence. The purpose: to extract "$17,000" from a "hotel maid" who earned "$400 per month." *Id.* at 84-85, 907 P.2d at 53-54. The effect: to subject a marginal person to the risk of loss of her home, all for a hot water heater that "was never installed properly, [and] never functioned properly." *Id.* at 84, 907 P.2d at 53.

[¶3] I would remand this case to the trial court for entry of judgment in favor of Maxwell. * * * *

Questions:

1. Are both substantive and procedural unfairness required for unconscionability?

2. Should this case be decided as a matter of law?

3. What is a "limited person"? "Marginal person"?

4. Do courts ever judge the adequacy of consideration?

5. Unconscionability was applied to a payday-type loan in *James v. National Fin., LLC*, 132 A.3d 799 (Del. Ch. 2016), and *New Mexico ex rel. King v. B&B Investment Grp., Inc.*, 329 P.3d 658 (N.M. 2014). The two cases are similar. In *James*, the lender gave a $200 loan to Ms. James. She may have borrowed the money for food or rent; at the time, she had less than $7. Like Ms. Maxwell, James worked as a hotel maid. James thought, based in part on National Financial's statements, that she would be able to pay the whole loan back in two $130 payments, one each on the next two paydays. In fact, the documents she signed actually required her to pay 26 interest-only payments of $60 each, followed by a balloon payment of $60 interest and the whole $200 principal. Had James actually paid according to the schedule, she would have paid $1,820. The annual percentage rate on the loan was over 800%. Fortunately, James found an excellent lawyer. Even so, the owner of National Financial was so angry with James that he showed up at her house and threatened her—at least, there was enough evidence to prompt the trial court to order him to remain at least 2,000 feet from James and refrain from contacting her except through counsel. After the trial was over, the court awarded James's attorney fees and costs of $331,024.50. *B&B Investment* was brought by the New Mexico Attorney General's office.

6. What if a party did not read a document? Does that make it unconscionable? Consider the following:

> Plaintiff argues repeatedly that he could not and did not read the forum selection clause, but this argument is a nonstarter: "[f]ailure to read a contract, particularly in a commercial contract setting, is not an excuse that relieves a person from the obligations of the contract." Pietroske, 2004 WI App 142, ¶ 11. "[I]n their dealings with each other, [parties] cannot close their eyes to the means of knowledge equally accessible to themselves and those with whom they deal, and then ask courts to relieve them from the consequences of their lack of vigilance." *Carney-Rutter Agency, Inc. v. Central Office Buildings, Inc.*, 263 Wis. 244, 253, 57 N.W.2d 348, 352 (1953); *see also Paper Express, Ltd v. Pfankuch Maschinen GmbH*, 972 F.2d 753, 757 (7th Cir. 1992) ("[A] blind or illiterate party (or simply one unfamiliar with the contract language) who signs the contract without learning of its contents would be bound. Mere ignorance will not relieve a party of her obligations and she will be bound by the terms of the agreement ... [sic] [A] party who agrees to terms in writing without understanding or investigating those terms does so at his own peril."). Equally unpersuasive is plaintiff's argument that the forum selection clause was written in a foreign language. *MCC-Marble Ceramic Center, Inc. v. Ceramica Nuova D'Agostino*, 144 F.3d 1384, 1387 n.9 (11th Cir. 1998):
>
> CC makes much of the fact that the written order form is entirely in Italian and that Monzon, who signed the contract on MCC's behalf directly below this provision incorporating the terms on the reverse of the form, neither spoke nor read Italian. This fact is of no assistance to MCC's position. We find it nothing short of astounding that an individual, purportedly experienced in commercial matters, would sign a contract in a foreign language and expect not to be bound simply because he could not comprehend its terms. We find nothing in the CISG that might counsel this type of reckless behavior and nothing that signals any retreat from the proposition that parties who sign contracts will be bound by them regardless of whether they have read them or understood them.
>
> "Rights under a contract are not forfeited by the other party's failure to read it." *United States v. Stump Home Specialties Manufacturing, Inc.*, 905 F.2d 1117, 1120 (7th Cir. 1990).

Israeli v. Dott.Gallina S.R.L., 632 F. Supp.2d 866, 870-71 (W.D. Wis. 2009).

7. When we say “free market,” what do we mean the market is free of? What is the relationship between law and a ”free market”? Isaiah Berlin famously said, “Freedom for the wolves has often meant death to the sheep.” Law in fact creates the property rights that we trade, including the property-like interest we have in a contract counterparty’s duties. Having created the powers in the first lace, the government is certainly justified in establishing their limits. Too philosophical for you? But that’s why unconscionability doctrine is so squishy.

8. You might consider whether the *Maxwell* case is justified as a matter of autonomy, welfare, or morality. Which? More than one?

9. What argument can be made for granting relief on a showing of substantive unconscionability alone? About half the states in the U.S. are willing to do this. *See, e.g.*, *Brower v. Gateway 2000, Inc.*, 676 N.Y.S.2d 569, (Sup. Ct. App. 1998) (“[T]he substantive element alone may be sufficient to render the terms of the provision at issue unenforceable.”). Is this a good idea? Consider this problem.

PROBLEM 36. Brower and others (Plaintiffs) bought computers and software from Gateway 2000, Inc. They ordered products by mail or telephone, and the products were shipped to them. Gateway promised “service when you need it,” including 24/7 technical support. As of July 3, 1995, Gateway included with the materials shipped to consumers a “Standard Terms and Conditions Agreement.” The document provided, “This document contains Gateway 2000’s Standard Terms and Conditions. By keeping your Gateway 2000 computer system beyond thirty (30) days after the date of delivery, you accept these Terms and Conditions.” Paragraph 10, titled “DISPUTE RESOLUTION,” said,

> Any dispute or controversy arising out of or relating to this Agreement or its interpretation shall be settled exclusively and finally by arbitration. The arbitration shall be conducted in accordance with the Rules of Conciliation and Arbitration of the International Chamber of Commerce. The arbitration shall be conducted in Chicago, Illinois, U.S.A. before a sole arbitrator. Any award rendered in any such arbitration proceeding shall be final and binding on each of the parties, and judgment may be entered thereon in a court of competent jurisdiction.

Plaintiffs sued as a class, alleging that Gateway did not provide any real technical support. Gateway moved for arbitration. Plaintiffs responded that the International Chamber of Commerce (ICC) was headquartered in France and was particularly difficult to contact. Further, under ICC arbitration rules, a claim of less than $50,000 required a $4,000 fee, including a non-refundable $2,000 registration fee. Because the ICC followed England’s “loser pays” rule, a consumer would pay Gateway’s legal fees if it won the arbitration. Consumers would also incur, of course, travel fees to Chicago. But all correspondence had to be sent to France. Of course, even some really smart, capable, wealthy people bought Gateway computers. Plaintiffs contended the arbitration clause was unconscionable.

Cases rescinding a contract for unconscionability as does *Maxwell* are a fairly recent phenomenon in common law history—only about seventy years old. More squarely in the unconscionability tradition is a

case such as *Wollums v. Horsley*, 20 S.W. 781 (Ky. App. 1892), our Problem 37. The court in this case refused the requested equitable remedy of specific performance, so the parties were already squarely in equity's jurisdiction.

PROBLEM 37. Wollums was 60 years old, a farmer, living on a mountain farm of 200 acres in Kentucky, in a very rural area. Wollums was uneducated, afflicted with a disabling disease, and owned no other land and little personal property. He knew little of what was going on in the world around him. Horsley was an experienced real estate speculator buying mineral rights. Through his agent, Horsley entered into a contract with Wollums to buy the mineral rights on Wollums's land for $0.40 per acre. The agent assured Wollums that he would never be bothered by the contract during his life, even though much mineral development was occurring locally and a railroad was being built through the area. Horsley paid the agent $80 for making this deal, the same amount Wollums would get in exchange for his mineral rights. Later, Horsley demanded a deed for the mineral rights, but Wollums refused to give one, so Horsley sued. At trial, Wollums proved that his land was worth about $15 per acre, or $3,000. The value came almost entirely from the mineral rights. Should Wollums have to give a deed? Try to apply the complete procedural and substantive unconscionability analysis from *Maxwell*. That is probably what a court would do now.

Federal Trade Commission Regulation—Door to Door Sales, especially §§ 429.1 and 429.2

Please find and read this regulation here:

https://www.ecfr.gov/current/title-16/chapter-I/subchapter-D/part-429

Question: This section mandates that the seller include in the written contract language granting a right to cancel. If the seller fails to include that language, does the consumer have a right to cancel?

Chapter 6. The Push Toward Assent

This chapter considers some doctrines that existed around the periphery of what are today's elements of formation. As you read at the beginning in the policy materials after *Vian v. Carey*, a party's sealing a document (which meant at the time literally melting wax on it and stamping it with a personal seal) caused it to be binding, at least if your lawyer bought a writ of covenant. In the United States, people have been much less formal, and most states have a statute that changes the effect of a seal. In fact, as evidence of a promise, a seal and a writing are not that much different, and in fact, the seal statutes give a strong nod to writings, so Subsection A considers them together.

But if seals were such a simple way to make a promise binding, why not a formal version of consideration? Subsections B and C address whether consideration is a formality.

The Statute of Frauds is not a defense to formation. It is a defense to enforcement, and it does require that some promises be in writing. It had to be in the casebook somewhere, and this chapter is a pretty good place because it is one of many contract rules that have been proposed to—but do not—make a promise enforceable.

Finally, there is a historical section introducing assent to you. Assent is another possible substitute for consideration (even though consideration evidence always proves it already). In continental Europe, people think of assent as the touchstone of contract liability. So you should learn how assent crept into the law, and why.

A. A Seal or Writing

PILLANS v. VAN MIEROP

King's Bench (1765)

3 Burr. 1663

[¶1] [In this case, White, a merchant in Ireland, wished to draw 800£. upon the credit of Pillans, a Dutch merchant and financier, to pacify White's creditor, Clifford. To induce Pillans to trust White's credit and make the advance, White proposed to obtain for Pillans the right to collect the money from a London financier should White default. White proposed Van Mierop as the London financier, whereupon Pillans honored White's draft and paid 800£. to Clifford. Both Pillans and White then wrote to Van Mierop to learn "whether [Van Mierop and his associates] would accept such bills as they, the plaintiffs, should in about a month's time draw upon the said Van Mierop's * * * * house here in London, for 800£ upon the credit of White." Van Mierop wrote a letter back agreeing to stand behind White, essentially as guarantor. Soon thereafter, White became insolvent, and when Pillans tried to draw upon his credit with Van Mierop, Van Mierop refused to pay. After a trial resulted in a verdict for Van Mierop, plaintiff's counsel moved for a new trial. Van Mierop's

counsel opposed a new trial on the ground that his promise was without consideration because Pillans granted credit to White before Van Mierop promised.]

[¶2] Lord Mansfield asked, if "any case could be found, where the undertaking holden to be a nudum pactum was in writing." * * * *

[¶3] [Mansfield continued:] This is a matter of great consequence to trade and commerce, in every light.

[¶4] If there was any kind of fraud in this transaction, the collusion and mala fides would have vacated the contract. But from these letters, it seems to me clear, that there was none. The first proposal from White, was "I to reimburse the plaintiffs by a remittance, or by credit on the house of Van Mierop": this was the alternative he proposed. The plaintiffs chose the latter. Both the plaintiffs and White wrote to Van Mierop and Company. They answered "that they would honour the plaintiffs' draughts" so that the defendants assent to the proposal made by White, and ratify it. And it does, not seem at all that the plaintiffs then doubted of White's sufficiency, or meant to conceal any thing from the defendants.

[¶5] If there be no fraud, it is a mere question of law. The law of merchants, and the law of the land, is the same * * * * . We must consider it as a point of law. A nudum pactum does not exist, in the usage and law of merchants.

[¶6] I take it, that the ancient notion about the want of consideration was for the sake of evidence only: for when it is reduced into writing, as in covenants, specialties, bonds, &c. there was no objection to the want of consideration. And the Statute of Frauds proceeded upon the same principle.

[¶7] In commercial cases amongst merchants, the want of consideration is not an objection. * * * * I think the point of law is with the plaintiffs.

[¶8] Mr. Justice Wilmot- * * * * I can find none of those cases that go upon its being nudum pactum, that are in writing; they are all, upon parol.

[¶9] I have traced this matter of the nudum pactum; and it is very curious.

[¶10] He then explained the principle of an agreement being looked upon as a nudum pactum: and how the notion of a nudum pactum first came into our law. He said, it was echoed from the civil law: -" Ex nudo pacto non oritur actio." * * * * There was no radical defect in the contract, for want of consideration. But it was made requisite, in order to put people upon attention and reflection, and to prevent obscurity and uncertainty * * * *.

[¶11] Therefore it was intended as a guard against rash inconsiderate declarations: but if an undertaking was entered into upon deliberation and reflection, it had activity; and such promises were binding. Both Grotius and Puffendorff, hold them obligatory by the law of nations. Grot lib. 2, c. 11, De Promissis. Puffend lib. 3, c. 5. They are morally good; and only require ascertainment. Therefore there is no reason to extend the principle, or carry it further.

[¶12] * * * * Our own lawyers have adopted exactly the same idea as the Roman law. Plowden, 308 b. in the case of [*Sharington v. Strotton*] * * * * mentions it: and no one contradicted it. He lays down the distinction between contracts or agreements in words (which are more base,) and contracts or agreements in writing, (which are more high,) and puts the distinction upon the want of deliberation in the former case,

and the still exercise of it in the latter. His words are the marrow of what the Roman lawyers had said. “Words pass from men lightly:” but where the agreement is made by deed, there is more stay: &c. &c. For, first, there is &c. &c. And, thirdly, he delivers the writing as his deed. “The delivery of the deed is a ceremony in law, signifying fully his good will that the thing in the deed should pass from him who made the deed, to the other. And therefore a deed, which must necessarily be made upon great thought and deliberation, shall bind without regard to the consideration.” * * * *

[¶13] Therefore, if it stood only upon the naked promise, its being, in this case, reduced into writing, is a sufficient guard against surprize; and therefore the rule of nudum pactum does not apply in the present case.

[¶14] I cannot find, that a nudum pactum evidenced by writing has been ever holden bad: and I should think it good; though, where it is merely verbal, it is bad; yet I give no opinion for its being good, always, when in writing. * * * *

The holding of *Pillans v. Van Mierop* that a promise in writing needs no consideration was overruled by the House of Lords in *Rann v. Hughes*, 7 T.R. 350 n.a,, 101 ER 1014 n.a. (House of Lords 1778), in which Chief Justice Skynner said, “All contracts are, by the laws of England, distinguished into agreements by specialty [meaning a sealed writing], and agreements by parol; nor is there any such third class as some of the counsel have endeavoured to maintain, as contracts in writing. If they be merely written and not specialties, they are parol, and a consideration must be proved.”

Questions:

1. Is there a bargain here?

2. Lord Mansfield, Chief Justice of the King’s Bench, was first trained in Scotland, where the civil law was employed, a derivation of Roman law and more akin to law used widely on the European continent. The linchpin of contract in civil law has for many centuries been assent, in line with what we read earlier from Pothier. How important does Mansfield think the consideration requirement is in this context? What does Mansfield say is the purpose for consideration?

3. How important does Justice Wilmot think consideration is? What does he think is the purpose of the consideration requirement? Does he think consideration exists here?

4. Is *Pillans* still the law?

Note: *Pillans* is a guarantee case in which the guarantor promises to the creditor. In our previous guaranty case, *Edmonds Case*, the guarantor promised to the debtor, who reciprocally promised to pay the guarantor back. In a typical guarantee case, the debtor suggests a guarantor, but the guarantor promises to the creditor-guarantee that the guarantor will pay the debtor’s debts if the debtor does not. What is consideration for the guarantor’s promise? Typically, courts hold that the creditor’s loan to the debtor, given

in exchange for the guaranty, is consideration for the guarantor's promise. Handing the loan funds over to the debtor is a bargained-for detriment to the promisee-creditor. But of course *Pillans* is different from that paradigmatic case.

Seals and Statutes

Tex. Civil Prac. & Rem. Code § 121.015. Private Seal or Scroll Not Required

> A private seal or scroll may not be required on a written instrument other than an instrument made by a corporation.

The traditional effect of a seal has declined since medieval times. In the United States, courts after the Revolution expanded greatly the kinds of marks on a paper that would count as a seal, until the seal itself lost much of its significance. In response, legislatures passed statutes such as the one above, and the Iowa statute below, which is less ambiguous. The Texas statute was construed in the following two cases, which explain its meaning.

WRIGHT v. ROBERT & ST. JOHN MOTOR CO.)

Commission of Appeals of Texas, Section A (1933)

58 S.W.2d 67, 69

* * * * [U]nder the common law, simple contracts in writing, under seal, implied a consideration. Since the necessity for a seal has been done away with, as applied to simple written contracts, all such contracts now imply a consideration. * * * *

John W. TAYLOR v. FRED CLARK FELT COMPANY

Court of Civil Appeals of Texas, Houston (14th Dist. 1978)

567 S.W.2d 863

J. CURTISS BROWN, Chief Justice.

[¶1] This is an appeal from a summary judgment granted the appellee in its suit on a promissory note.

[¶2] John W. Taylor (appellant), individually and doing business as John Taylor Co., is the maker of a promissory note for $22,862.19 payable to the order of Fred Clark Felt Company (appellee). The appellee filed suit on the note on June 17, 1977. The appellant's first amended answer contained a general denial and allegations of payment and fraud in the inducement. The appellee subsequently filed a motion for summary judgment, which was granted on September 27, 1977. * * * *

[¶3] There is a rebuttable statutory presumption that a written instrument imports consideration. *Thigpen v. Thigpen*, 563 S.W.2d 868 (Tex. Civ. App.—San Antonio 1978, no writ history); *Maykus v. Texas Bank & Trust Co. of Dallas*, 550 S.W.2d 396 (Tex. Civ. App.—Dallas 1977, no writ); see Tex. Rev. Civ. Stat. Ann. art. 27 (1969). The two opposing affidavits filed by the appellant contain statements that John Taylor Co. had no record of ever receiving the goods for which the promissory note was issued and that it was the customary practice of that company to keep records of the receipt of such goods. That summary judgment evidence counters the presumption of consideration and raises the inference that the goods were never delivered. See Tex. Rev. Civ. Stat. Ann. art. 3737e, § 3 (Supp. 1978). The appellant having raised a fact issue concerning the affirmative defense of failure of consideration, the trail court erred in granting summary judgment. *Hudnall v. Tyler Bank and Trust Company*, 458 S.W.2d 183 (Tex.Sup.1970).

[¶4] The judgment of the trial court is hereby reversed, and the case is remanded for a trial on the merits.

Reversed and remanded.

The *Taylor v. Fred Clark Felt Co*. case holds that the statute creates an "evidentiary presumption" in certain circumstances. An evidentiary presumption operates to show a fact or element of a law even though no evidence regarding that fact or element is submitted to the court. Thus, if an evidentiary presumption is available, a litigant can show a fact or element by either proving the fact itself or proving the facts which cause the evidentiary presumption to exist. When a party relies on an evidentiary presumption, the opposing party may, if the presumption is rebuttable, rebut the presumption by submitting evidence which disproves the fact or element of law that was presumed. If the opposing party submits no evidence, then the unrebutted presumption becomes established as a matter of law. *Taylor* says that according to the statute certain facts establish a certain presumption. Which facts? What presumption? Is the presumption rebuttable?

Iowa Code § 537A.1. Seals abolished

> The use of private seals in written contracts, or other instruments in writing, by individuals, firms, or corporations that have not adopted a corporate seal, is hereby abolished; but the addition of a seal to any such instrument shall not affect its character or validity in any respect.

Iowa Code § 537A.2. Consideration implied

> All contracts in writing, signed by the party to be bound or by the party's authorized agent or attorney, shall import a consideration.

Iowa Code § 537A.3. Failure of consideration

> The want or failure, in whole or in part, of the consideration of a written contract may be shown as a defense, total or partial * * * *.

Question: Is the effect of the Iowa statute different from that of the Texas statute?

SKF USA, INC. v. WORKERS' COMPENSATION APPEAL BOARD (SMALLS)

Commonwealth Court of Pennsylvania (1998)

714 A.2d 496

MIRARCHI, Jr., Senior Judge.

[¶1] [SKF employed Thomas Smalls. Smalls was injured in a work-related accident in which two of his fingers were amputated. Smalls received total and partial disability workers' compensation benefits for some time. Soon after his accident, Smalls sued Norton Industries, the manufacturer of the machine which caused Smalls's injuries. Smalls and Norton later settled, Norton agreeing to pay Smalls a lump sum of $430,000 and Mrs. Smalls $20,000 and certain other later periodic payments.

[¶2] When an employee is injured and recovers compensation from a person at fault other than his employer, the employer who has paid workers' compensation money in the meantime may then recover from the employee a portion of the money the employee receives from the third party, up to the amount of workers' compensation the employee received. This is called the employer's right of subrogation. Because SKF had paid Smalls workers' compensation benefits in compensation for injury caused by the fault of Norton, SKF had subrogation rights to a portion of the money Smalls received from Norton.

[¶3] After Smalls and Norton settled, SKF's lawyer wrote a letter to Smalls's lawyer claiming subrogation rights. The two lawyers soon settled on a sum. SKF's lawyer suggested also that Smalls forego any further

workers' compensation benefits. On January 31, 1986, SKF executed a general release, providing in relevant part:

> [T]he undersigned on behalf of SKF INDUSTRIES, INC. for and in consideration of $63,343.21, receipt of which is hereby acknowledged[,] do hereby remise, release, and forever discharge THOMAS SMALLS, ... of and from any and all manners of actions and causes of action, suits ... claims and demands whatsoever in law or equity, especially any and all past, present or future claims which SKF INDUSTRIES, INC. may have against THOMAS SMALLS pursuant to Section 319 of the Pennsylvania Workers' Compensation Act for Workers' Compensation benefits paid or to be paid to THOMAS SMALLS due to Mr. SMALLS' accident of April 22, 1980.

After SKF signed the release, Smalls again experienced periods of total and partial disability and became entitled to workers' compensation as a result of the work accident. On March 12, 1987, SKF filed a petition seeking subrogation credit for benefits payable to Smalls subsequent to January 1, 1986. SKF alleged that the release was void because it lacked consideration. The Workers Compensation Board held that the release was supported by consideration.

[¶4] After deciding that the release was valid under workers' compensation laws and that the release was actually supported by consideration, the Court stated as follows:]

[¶5] * * * * [T]he Release contained the language, "we have here unto set our hands and corporate seal," and the word "seal" was preprinted next to the signature of Allen Belenson, Employer's Secretary and General Counsel. In *Graybill v. Juniata County School District*, 21 Pa. Cmwlth. 630, 347 A.2d 524, 526 (1975), the contracts contained the similar language, "the parties above named hereunto set their hands and seal," along with the word "seal" or "L.S." affixed next to or under the signatures. Although no formal raised corporate seal was affixed, as in this matter, this Court held that the presence of these markings provided ample evidence that the contracts were executed under seal.

[¶6] As to the common law effect of a seal in a written document, the Supreme Court stated:

> [O]nce plaintiff has proved the signature, consideration … may be presumed from the fact that the instrument is under seal …. In other words, a plaintiff who relies upon a sealed instrument is not obliged to prove consideration to take the case to the jury. The seal imports consideration.

Selden v. Jackson, 425 Pa. 618, 619, 230 A.2d 197, 197-98 (1967). Thus, where, as here, a contract is executed under seal, a party may not raise, as a defense, want of consideration, distinguished from failure of consideration. *Barnhart v. Barnhart*, 376 Pa. 44, 101 A.2d 904 (1954). Hence, Employer in this matter may not raise lack or want of consideration to avoid the terms of the Release.

[¶7] Moreover, regardless of lack of consideration, the Release is also valid and enforceable under the Act of May, 13, 1927, P.L. 985, 33 P.S. § 6, commonly known as the Uniform Written Obligations Act, which provides:

> A written release or promise, hereafter made and signed by the person releasing or promising, shall not be invalid or unenforceable for lack of consideration, if the writing also

> contains an additional express statement, in any form of language, that the signer intends to be legally bound.

In the Release executed under seal, Employer unequivocally agreed to release and discharge Claimant from "any and all past, present or future claims" arising under Section 319 of the Act. The Release did not contain any condition or disclaimer which would refute Employer's intent to be legally bound by the terms therein. * * * *

[¶8] In conclusion, the Release is valid and enforceable. * * * *

ORDER

[¶9] AND NOW, this 23rd day of June, 1998, the order of the Workers' Compensation Appeal Board in the above-captioned matter is affirmed.

Questions:

1. Does a seal raise a presumption of consideration in Pennsylvania? Is the presumption rebuttable?

2. Would the release be enforceable without the seal?

3. What language shows that SKF intended to be bound?

B. Nominal and Recited Consideration Generally, and in Option Contracts

SCHNELL v. NELL

Supreme Court of Indiana (1861)

17 Ind. 29

[¶1] PERKINS, J.—Action by J. B. Nell against Zacharias Schnell, upon the following instrument:

> "This agreement, entered into this 13th day of February, 1856, between Zach. Schnell, of Indianapolis, Marion county, State of Indiana, as party of the first part, and J. B. Nell, of the same place, Wendelin Lorenz, of Stilesville, Hendricks county, State of Indiana, and Donata Lorenz, of Frickinger, Grand Duchy of Baden, Germany, as parties of the second part,

witnesseth: The said Zacharias Schnell agrees as follows: whereas his wife, Theresa Schnell, now deceased, has made a last will and testament, in which, among other provisions, it was ordained that every one of the above named second parties, should receive the sum of $200; and whereas the said provisions of the will must remain a nullity, for the reason that no property, real or personal, was in the possession of the said Theresa Schnell, deceased, in her own name, at the time of her death, and all property held by Zacharias and Theresa Schnell jointly, therefore reverts to her husband; and whereas the said Theresa Schnell has also been a dutiful and loving wife to the said Zach. Schnell, and has materially aided him in the acquisition of all property, real and personal, now possessed by him; for, and in consideration of all this, and the love and respect he bears to his wife; and, furthermore, in consideration of one cent, received by him of the second parties, he, the said Zach. Schnell, agrees to pay the above named sums of money to the parties of the second part, to wit: $200 to the said J. B. Nell; $200 to the said Wendelin Lorenz; and $200 to the said Donata Lorenz, in the following installments, viz., $200 in one year from the date of these presents; $200 in two years, and $200 in three years; to be divided between the parties in equal portions of $66⅔ each year, or as they may agree, till each one has received his full sum of $200.

"And the said parties of the second part, for, and in consideration of this, agree to pay the above named sum of money [one cent], and to deliver up to said Schnell, and abstain from collecting any real or supposed claims upon him or his estate, arising from the said last will and testament of the said Theresa Schnell, deceased.

"In witness whereof, the said parties have, on this 13th day of February, 1856, set hereunto their hands and seals.

"ZACHARIAS SCHNELL, [SEAL.]

"J. B. NELL, [SEAL.]

"WEN. LORENZ." [SEAL.]

[¶2] The complaint contained no averment of a consideration for the instrument, outside of those expressed in it; and did not aver that the one cent agreed to be paid, had been paid or tendered.

[¶3] A demurrer to the complaint was overruled.

[¶4] The defendant answered, that the instrument sued on was given for no consideration whatever.

[¶5] He further answered, that it was given for no consideration, because his said wife, Theresa, at the time she made the will mentioned, and at the time of her death, owned, neither separately, nor jointly with her husband, or any one else (except so far as the law gave her an interest in her husband's property), any property, real or personal, &c. * * * *

[¶6] The Court sustained a demurrer to these answers, evidently on the ground that they were regarded as contradicting the instrument sued on, which particularly set out the considerations upon which it was executed. But the instrument is latently ambiguous on this point. See Ind. Dig., p. 110.

[¶7] The case turned below, and must turn here, upon the question whether the instrument sued on does express a consideration sufficient to give it legal obligation, as against Zacharias Schnell. It specifies three distinct considerations for his promise to pay $600:

> 1. A promise, on the part of the plaintiffs, to pay him one cent.
>
> 2. The love and affection he bore his deceased wife, and the fact that she had done her part, as his wife, in the acquisition of property.
>
> 3. The fact that she had expressed her desire, in the form of an inoperative will, that the persons named therein should have the sums of money specified.

[¶8] The consideration of one cent will not support the promise of Schnell. It is true, that as a general proposition, inadequacy of consideration will not vitiate an agreement. *Baker v. Roberts*, 14 Ind. 552. But this doctrine does not apply to a mere exchange of sums of money, of coin, whose value is exactly fixed, but to the exchange of something of, in, itself, indeterminate value, for money, or, perhaps, for some other thing of indeterminate value. In this case, had the one cent mentioned, been some particular one cent, a family piece, or ancient, remarkable coin, possessing an indeterminate value, extrinsic from its simple money value, a different view might be taken. As it is, the mere promise to pay six hundred dollars for one cent, even had the portion of that cent due from the plaintiff been tendered, is an unconscionable contract, void, at first blush, upon its face, if it be regarded as an earnest one. *Hardesty v. Smith*, 3 Ind. 39. The consideration of one cent is, plainly, in this case, merely nominal, and intended to be so. As the will and testament of Schnell's wife imposed no legal obligation upon him to discharge her bequests out of his property, and as she had none of her own, his promise to discharge them was not legally binding upon him, on that ground. A moral consideration, only, will not support a promise. Ind. Dig., p. 13. And for the same reason, a valid consideration for his promise can not be found in the fact of a compromise of a disputed claim; for where such claim is legally groundless, a promise upon a compromise of it, or of a suit upon it, is not legally binding. *Spahr v. Hollingshead*, 8 Blackf. 415. There was no mistake of law or fact in this case, as the agreement admits the will inoperative and void. The promise was simply one to make a gift. The past services of his wife, and the love and affection he had borne her, are objectionable as legal considerations for Schnell's promise, on two grounds: 1. They are past considerations. Ind. Dig., p. 13. 2. The fact that Schnell loved his wife, and that she had been industrious, constituted no consideration for his promise to pay J. B. Nell, and the Lorenzes, a sum of money. Whether, if his wife, in her lifetime, had made a bargain with Schnell, that, in consideration of his promising to pay, after her death, to the persons named, a sum of money, she would be industrious, and worthy of his affection, such a promise would have been valid and consistent with public policy, we need not decide. Nor is the fact that Schnell now venerates the memory of his deceased wife, a legal consideration for a promise to pay any third person money.

[¶9] The instrument sued on, interpreted in the light of the facts alleged in the second paragraph of the answer, will not support an action. The demurrer to the answer should have been overruled. See *Stevenson v. Druley*, 4 Ind. 519.

[¶10] Per Curiam. — The judgment is reversed, with costs. Cause remanded &c.

Questions:

1. What possible consideration can you argue here?

2. What does *nominal* mean?

3. Do you think that consideration exists here under the *Kim v. Son* case? Under *Kalis*?

The next case is a variation on a theme we have studied already. Remember the *DeYoung* case, where an option was purchased for $1? Here is the Pennsylvania version of the case, where the dollar was never paid. Pennsylvania's is a minority view (*see also SKF*), but it is interesting.

REAL ESTATE CO. OF PITTSBURGH v. RUDOLPH

Supreme Court of Pennsylvania (1930)

153 A. 438

SIMPSON, J.

[¶1] Defendant executed and delivered to the legal plaintiff an option as follows:

> "April 18th, 1928.
>
> "Real Estate Company of Pittsburgh,
>
> "Wood and Fourth,
>
> "Pittsburgh, Pennsylvania.
>
> "Gentlemen:
>
> "In consideration of One ($1.00) Dollar in hand paid, I hereby give you the option to purchase my property situate 1628 Penn Ave., at the price of $15000.00. This option to expire at 12 o'clock noon, April 21th, 1928.
>
> "If this option is accepted by you and transaction closed, I agree to pay you a commission of 3% on the sale price. It is understood that the property is free and clear of encumbrances excepting a mortgage in the amount of $6,000.00.
>
> "Very truly yours, J. A. Rudolph."

The next day, and before he was formally notified of the acceptance of the option, defendant informed plaintiffs that he would not sell the property because his wife would not join in the conveyance. They were willing, however, to accept a title without the joinder of the wife, as, of course, they had the right to do (*Corson v. Mulvany*, 49 Pa. 88, 88 Am. Dec. 485; *Medoff v. Vandersaal*, 271 Pa. 169, 116 A. 525); but he persisted in his revocation, and refused even to discuss the matter with them, whereupon they filed the present bill in equity for specific performance. The learned president judge of the court below, who sat as chancellor, found all the disputed facts in favor of plaintiffs, and reported a decree nisi awarding specific performance, the deed to be executed by defendant alone, without the joinder of his wife. On exceptions filed, the court in banc decreed a dismissal of the bill, solely because the one dollar, specified in the option as having been paid, had not in fact been paid, and hence the optioner was well within his right in revoking it before acceptance. This raises the only point to be considered by us on plaintiffs' appeal from the decree. It must be admitted that the authorities elsewhere are not harmonious, but in our judgment the final decree is wrong.

[¶2] It is of course true that, if an option has no actual or legal consideration to support it, it may be revoked by the optioner at any time prior to acceptance. Defendant's answer does not aver a lack of consideration, however, and hence neither the fact nor effect of a want of it should have been considered by the court below. Moreover, this option has a legal consideration to support it. In *Lawrence v. McCalmont*, 2 How. (43 U. S.) 426, 452, 11 L. Ed. 326, it is said in an opinion by Mr. Justice Story:

> "The second [defense] is, that the payment of the one dollar is merely nominal and not sufficient to sustain the guarantee, if it had been received; and it is urged that it was not received. As to this last point, we feel no difficulty. The guarantor acknowledged the receipt of the one dollar, and is now estopped to deny it. If she has not received it, she would now be entitled to recover it. A valuable consideration, however small or nominal, if given or stipulated for in good faith, is, in the absence of fraud, sufficient to support an action on any parol contract; and this is equally true as to contracts of guarantee as to other contracts. A stipulation in consideration of one dollar is just as effectual and valuable a consideration as a larger sum stipulated for or paid. * * * * But, independently of all authority, we should arrive at the same conclusion. The receipt of the one dollar is acknowledged; no fraud is pretended or shown; and the consideration, if standing alone in a bona fide transaction would sustain the present suit."

[¶3] That case is apposite here, since the traditional statement in the option of the "$1 in hand paid" can only mean that appellant acknowledges the receipt of that sum.

[¶4] If this is so as concerns a guarantor, in whose favor the law leans, it must be so in cases like the present, and so it, has been held in *Watkins v. Robertson*, 105 Va. 269, 284, 285, 54 S. E. 33, 5 L. R, A. (N. S.) 1194, 115 Am. St. Rep. 880; *Hagen v. Lehmann*, 317 Ill. 227, 230, 148 N. E. 57; *Horbach v. Coyle* (C. C. A.) 2 F.(2d) 702; and in the cases cited in those authorities. * * * *

[¶5] * * * * It is elementary that the consideration imported from the use of a seal on such a paper may not be contradicted by proof. *Storm v. United States*, 94 U. S. 76, 83, 84, 24 L. Ed. 42. In the light of this, it, would be neither logical nor consistent to hold that the intentional insertion of an actual consideration may be overthrown whenever one of the parties desires to escape liability. * * * *

[¶6] Moreover, it is quite possible, when taken in conjunction with a finding of the chancellor that defendant knew the agreement was sought because of a hoped-for resale to a third party, that its true interpretation is that defendant gave to the legal plaintiff an option until "12 o'clock noon April 24th, 1928," to find a purchaser for the property at $15,000, and said to him, "if this option is accepted by you and transaction closed, I agree to give you a commission of three per cent on the sale price." No other construction satisfactorily explains why the vendor agreed to pay the vendee for buying the property, instead of merely stating that the sales price is to be $14,550. If that construction is correct, then the agreement contemplated services to be rendered by plaintiff to defendant forthwith which the former impliedly agrees to render, and hence an additional valuable consideration appears.

[¶7] The decree of the court below is reversed, at the cost of appellee, and the record is remitted that the decree nisi may be entered as the decree of the court.

Questions:

1. Is Rudolph consistent with Edward Nowitzke Trust?

2. Isn't $1 nominal, even if Rudolph is estopped to deny it?

3. Did the plaintiff in *Rudolph* rely on the statement of consideration in the option? Was that reliance reasonable? What detriment resulted?

4. Why allow a mere recital of consideration to make an option contract enforceable? Are option contracts different from other contracts in such a way that makes this holding appropriate? (The answer is not in the case, but this is the relevant policy question. If you think about what an option is worth, it's not difficult to figure out why courts allow $1 paid for an option on lake front property worth between $150k and $380k in *Edward Nowitzke Trust* and the $1 recited in *Rudolph* to be binding even though they are very small amounts.)

C. The Statute of Frauds

One immediate result of making generally enforceable (in assumpsit) parol promises based upon a consideration was that courts began enforcing promises on very little evidence. Particularly because of the mutual promise rule, no longer did a seal or a transaction of property evidence every actionable promise. As evidence of promises, consideration was not as good as a sealed writing. One reaction to the ease of proof brought on by the growth of assumpsit was the passage of a statute by Parliament in 1677 which has become known as the Statute of Frauds. The Statute of Frauds has been enacted in more or less similar

form by all fifty states. The following version is from Texas, but it is very much the same as other statutes enacted in the other 49 states:

> (a) A promise or agreement described in Subsection (b) of this section is not enforceable unless the promise or agreement, or a memorandum of it, is
>
> (1) in writing; and
>
> (2) signed by the person to be charged with the promise or agreement or by someone lawfully authorized to sign for him.
>
> (b) Subsection (a) of this section applies to:
>
> (1) a promise by an executor or administrator to answer out of his own estate for any debt or damage due from his testator or intestate;
>
> (2) a promise by one person to answer for the debt, default, or miscarriage of another person;
>
> (3) an agreement made on consideration of marriage * * * *;
>
> (4) a contract for the sale of real estate;
>
> (5) a lease of real estate for a term longer than one year;
>
> (6) an agreement which is not to be performed within one year from the date of making the agreement * * * *.

Questions:

1. Is a promise of guaranty required to be in writing? If so, under what section?

2. Does the statute require a promise to sell a house to be in writing?

3. Why do you suppose that Parliament in 1677 picked these categories of things to be in writing? Keep in mind that Parliament was composed of male landowners who were mostly heads of families, had inherited their wealth, and were for the most part trying to amass (or retain) an estate they could pass on to heirs.

The Texas statute includes other categories of promises for which a memorandum is required but which were not found in the original Statute of Frauds and may or may not be included in other states' statutes:

> ... (3) ... or on consideration of nonmarital conjugal cohabitation; ...
>
> (7) a promise or agreement to pay a commission for the sale or purchase of:

(A) an oil or gas mining lease;

(B) an oil or gas royalty;

(C) minerals; or

(D) a mineral interest; and

(8) an agreement, promise, contract, or warranty of cure relating to medical care or results thereof made by a physician or health care provider as defined in Section 74.001, Civil Practice and Remedies Code. This section shall not apply to pharmacists.

Please do not consider these provisions to be included in "The Statute of Frauds" as that term is generically used, but only when the Texas statute of frauds is itself specifically discussed.

Texas also has other "statutes of frauds" on the books. These are typical. They are referred to as "statutes of frauds" but not as "The Statute of Frauds," which refers only to the statute listed in the text above. One of these other statutes of frauds applies to loan agreements over a certain amount, *see* Tex. Bus. & Com. Code Ann. § 26.02 (2013), and one to premarital agreements, Tex. Fam. Code Ann. § 4.002 (2013) ("A premarital agreement must be in writing and signed by both parties."). Another is found in the Uniform Commercial Code § 2-201; it requires a signed writing evidencing "a contract for the sale of goods for the price of $500 or more" and is otherwise phrased similarly to the Statute of Frauds but contains useful exceptions, including one for contracts admitted in litigation to exist. Other states will have similar and other provisions.

If a writing is now required for some kinds of agreements, does that mean a consideration is no longer required for those agreements? See the following case.

RANN v. HUGHES (1778)

House of Lords

7 T.R. 350

* * * * All contracts are, by the laws of England, distinguished into agreements by specialty, and agreements by parol; nor is there any such third class as some of the counsel have endeavoured to maintain, as contracts in writing. If they be merely written and not specialties, they are parol, and a consideration must be proved. But it is said that the Statute of Frauds has taken away the necessity of any consideration in this case; the Statute of Frauds was made for the relief of personal representatives and others, and did not intend to charge them further than by common law they were chargeable. His Lordship here read those sections of that statute which relate to the present subject. He observed that the words were merely negative and that executors and administrators should not be liable out of their own estates, unless the agreement upon which the action was brought, or some memorandum thereof was in writing and signed by the party. But this does not prove that the agreement was still not liable to be tried and judged of as all other agreements merely in writing are by the common law, and does not prove the converse of the proposition, that when in writing the party must be at all events liable. He here observed upon the case of *Pillans v. Van*

Mierov in Burr and the case of *Losh v Williamson*, Mich. 16 G. 3- in B. R.: and so far as these cases went on the doctrine of nudum pactum, he seemed to intimate that they were erroneous. He said that all his brothers concurred with him that in this case there was not a sufficient consideration to support this demand as a personal demand against the defendant, and that its being now supposed to have been in writing, makes no difference. * * * *

Note: The Statute of Frauds and Formality

How much formality does the Statute of Frauds require? If a writing is required, what must it say?

This is such a simple question that you probably do not need a case for it, but here is an example.

In *Fulton v. Robinson*, 55 Tex. 401 (1881), the Supreme Court of Texas considered these facts: On March 23, 1859, Henderson bought 320 acres from Earles, for $1,120. Henderson paid $300 at that time. Earles gave Henderson a receipt for the $300. Here's what the receipt said:

> Received of James Henderson three hundred dollars, in part payment of a certain tract of land, being my own headright, lying on Rush creek, in the cross timbers, this 23rd March, 1859.
>
> Israel Earles [signature]

This is a great description of land title in pioneer Texas. A "headright" is a grant of land from the Republic of Texas that was contingent on certain conditions. When the conditions were met, the headright could ripen into a legal grant of land. Important for this case, a headright is issued by the government to an individual, so the government has a description of Earles's land "lying on Rush creek" recorded in public documents. Texas Headrights Link.

Henderson paid the balance of the purchase price, $820, to Russell, Earles's administrator, on February 11, 1860. Apparently Earles on his deathbed remembered that he had not given Henderson a deed. Russell collected the rest of the money and, by order of the probate court, gave Henderson a deed. The $820 was paid to the guardians of Earles's heirs.

In the case, the heirs sued fourteen years later claiming that the administrator had no power to make the conveyance (and the probate court lacked jurisdiction) because the promise was not in writing as required by the Statute of Frauds. In response, the court said, "The mere fact that it was in the form of a receipt would not of itself defeat it as a memorandum of contract for the sale of land, if sufficient in other respects." So the form of the writing did not matter, and courts have approved all sorts of forms: a telegram, letter, a record book, a check, a suicide note.

If the form is not relevant, what must the writing say? The court answered this, too:

> The general rule has often been announced in other courts as well as our own, that the memorandum under the statute of frauds should be so reasonably definite and certain

> within itself, or other writing referred to, as to parties, consideration and subject-matter, that specific performance can be enforced without a resort to parol testimony. * * * *
>
> In the elaborate opinion by Chief Justice Hemphill, * * * the authorities * * * were reviewed, and the construction given to the statute in *Packard v. Richardson*, 17 Mass., 124, that the consideration need not be expressed in the writing, but might be proved by parol, was adopted * * * .

Questions:

1. Under this language, is the consideration required to be stated in the writing? Does the receipt given by Earles pass the test?

2. The Uniform Electronic Transactions Act (UETA), passed in all but NY (which has something similar), helps electronic records and signatures count under the Statute of Frauds. The Act tries to equate writings in electronic form to writings on paper. A key section of the act provides:

> (a) A record or signature may not be denied legal effect or enforceability solely because it is in electronic form.
>
> (b) A contract may not be denied legal effect or enforceability solely because an electronic record was used in its formation.
>
> (c) If a law requires a record to be in writing, an electronic record satisfies the law.
>
> (d) If a law requires a signature, an electronic signature satisfies the law.

UETA § 7. An "electronic signature" "means an electronic sound, symbol, or process attached to or logically associated with a record and executed or adopted by a person with the intent to sign the record." UETA § 2(8). A "record" includes "information . . . that is stored in an electronic or other medium and is retrievable in perceivable form." UETA § 2(13). The Act is limited in scope: it "applies only to transactions between parties each of which has agreed to conduct transactions by electronic means." UETA § 5(b). If James Henderson and Israel Earles' transaction had occurred last year, the two had bargained for the sale of this property by email or text, and Earles' receipt had been sent as an email or text, would a court bound by UETA reach the same result?

A federal law attempts to reach a similar result by providing that, "with respect to any transaction in or affecting interstate . . . commerce—(1) a signature, contract, or other record relating to such transaction may not be denied legal effect, validity, or enforceability solely because it is in electronic form; and (2) a contract relating to such transaction may not be denied legal effect, validity, or enforceability solely because an electronic signature or electronic record was used in its formation." Electronic Signature in Global and National Commerce Act ("E-SIGN") § 101 (2000). The Uniform Law Commission proposed another uniform law that would have governed software and other computer information transactions, called the Uniform Computer Information Transactions Act (UCITA). UCITA contains provisions that might impact electronic signatures, but it is controversial for other reasons and is law only in Virginia and Maryland.

Mikio NAKAMURA v. Masaki FUJII

N.Y. Supreme Court, Appellate Division, First Department (1998)

677 N.Y.S.2d 113

MEMORANDUM DECISION

[¶1] Order, Supreme Court, New York County (Carol Huff, J.), entered March 17, 1997, which, to the extent appealed from, granted defendants' cross motion to dismiss the complaint as barred by the Statute of Frauds, and denied defendants' request for sanctions, unanimously modified, on the law, defendants' motion to dismiss is denied except as to the fourth cause of action on an indemnity theory, the balance of the complaint reinstated, and otherwise affirmed, without costs.

[¶2] Plaintiff alleges that in August 1992, defendants Masaki and Isako Fujii informed him that they could not afford to pay the tuition of their daughter, Aki, who was enrolled at the University of Southern California (USC). Defendants requested that plaintiff pay "certain tuition invoices" for Aki. Plaintiff orally agreed to pay the tuition in exchange for defendants' express promise to repay the amounts on demand. Thereafter, plaintiff had his corporation, Calinax, issue checks to USC on five occasions between August 1992 and December 1993, totalling $40,339.33. In August 1993, defendants made a similar request for their younger daughter, Sawako, and plaintiff orally agreed to make the tuition payments subject to the same repayment terms. Plaintiff had Calinax issue six checks to USC for Sawako's tuition between August 1993 and January 1996, totaling $60,964.20.

[¶3] According to plaintiff, defendants confirmed their repayment obligations in several meetings with plaintiff in New York. However, when plaintiff demanded repayment, defendants refused. By summons and complaint dated June 20, 1996, plaintiff commenced the instant action alleging, inter alia, a breach of the oral agreement to repay the tuition advances, * * * and that defendants' promise to repay the tuition advances constituted an indemnity. In their answer, defendants denied that they asked plaintiff to make any payments to USC or that they promised to repay him, and further denied having knowledge or information as to whether such payments were made by Calinax. Defendants also asserted six affirmative defenses, including * * * the Statute of Frauds. Defendants further asserted counterclaims for defamation, negligent and intentional infliction of emotional distress and tortious interference with contractual relations. The counterclaims were based on defendants' allegations that plaintiff sexually harassed Sawako, an employee of plaintiff, made disparaging comments about defendants and their daughter and threatened to damage Masaki Fujii's reputation with his employer.

[¶4] In October 1996, plaintiff moved to dismiss defendants' affirmative defenses and counterclaims as baseless and conclusory. Defendants cross-moved for dismissal of the complaint pursuant to CPLR 3211(a)(3), (5) and (7), and for sanctions pursuant to 22 NYCRR § 130-1.1. In their dismissal motion, defendants argued * * * that plaintiff's claims were barred by the Statute of Frauds because the promises alleged were to answer for the debt of another, and could not be performed within one year from their making.

[¶5] The IAS court denied plaintiff's motion to dismiss the affirmative defenses and counterclaims, and severed the latter. Additionally, although rejecting defendants' argument concerning [another matter], it

granted defendants' motion to dismiss the complaint on the ground that it was barred by the Statute of Frauds. The court found that the oral agreement to repay the tuition advances during the daughters' enrollment at USC was unenforceable since it was not, by its terms, to be performed within one year (General Obligations Law [GOL] § 5-701[a][1]), and because it constituted a promise to answer for the debt of another (GOL § 5-701[a][2]). The remainder of the motion and cross-motion was denied without discussion.

[¶6] In *Cron v. Hargro Fabrics*, 91 N.Y.2d 362, 366-367, 670 N.Y.S.2d 973, 694 N.E.2d 56, the Court of Appeals recently reiterated the contours of GOL § 5- 701(a)(1):

> New York law provides that an agreement will not be recognized or enforceable if it is not in writing and "subscribed by the party to be charged therewith" when the agreement "by its terms is not to be performed within one year from the making thereof ..." [GOL § 5-701(a) (1)]. We have long interpreted this provision of the Statute of Frauds to encompass only those contracts which, by their terms, "have absolutely no possibility in fact and law of full performance within one year" (*D & N Boening v. Kirsch Beverages*, 63 N.Y.2d 449, 454, 483 N.Y.S.2d 164, 472 N.E.2d 992). As long as the agreement may be "fairly and reasonably interpreted" such that it may be performed within a year, the Statute of Frauds will not act as a bar however unexpected, unlikely, or even improbable that such performance will occur during that time frame (*Warren Chem. & Mfg. Co. v. Holbrook*, 118 N.Y. 586, 593, 23 N.E. 908 [citations omitted]).

[¶7] Nothing in the oral agreement at issue sets the duration of plaintiff's obligation to pay the tuition. It certainly does not specifically require plaintiff to pay all four years of tuition for each daughter. By its terms, it merely requires plaintiff to pay "certain tuition invoices," without stating when those invoices must be paid, or even how many. Further, the agreement requires defendants to repay the sums not at some future time, but "on demand." Given the absence of any terms mandating payments by plaintiff, or repayments by defendants, at specific times, it cannot be said that the agreement could not be performed within one year, notwithstanding its duration in fact (see, *Mann v. Helmsley-Spear*, 177 A.D.2d 147, 149-150, 581 N.Y.S.2d 16).

[¶8] Additionally, there was no guarantee that defendants' daughters would remain at USC for the full four years, or even for one year (*see*, *Zimmerman v. Zimmerman*, 86 A.D.2d 525, 526, 447 N.Y.S.2d 675, appeal dismissed 56 N.Y.2d 806; but see, *Sud v. Sud*, 211 A.D.2d 423, 424, 621 N.Y.S.2d 37; *In re Galvin's Estate*, 148 Misc. 546, 547, 266 N.Y.S. 113). "The statute of frauds is not applicable to an agreement the performance of which depends on a contingency which may or may not happen within one year" (61 N.Y.Jur.2d Frauds, Statute of, § 28, p 65; see also, *North Shore Bottling Co. v. C. Schmidt & Sons*, 22 N.Y.2d 171, 176, 292 N.Y.S.2d 86, 239 N.E.2d 189). In this case, defendants' daughters could have left USC "for any of the reasons that commonly lead many college students either to drop out of school or to change schools" (see, *Zimmerman v. Zimmerman*, *supra*, at 526, 447 N.Y.S.2d 675). Where a third party to an oral contract has the right to terminate the agreement within one year, the contract is not within the Statute of Frauds (see, 61 N.Y.Jur.2d Frauds, Statute of, § 25, p 59; *Sawyer v. Sickinger*, 47 A.D.2d 291, 295, 366 N.Y.S.2d 435; *Metro-Goldwyn-Mayer v. Scheider*, 43 A.D.2d 922, 923, 352 N.Y.S.2d 205).

[¶9] Nor is GOL § 5-701(a)(2) a bar to the enforcement of this agreement. Contrary to defendants' argument, the complaint does not allege that defendants provided a guaranty to repay the debt of their daughter. Rather, it alleges an independent promise by defendants to repay monies advanced by plaintiff,

at their express request, to pay their children's tuition. Defendants' daughters owed no debt to plaintiff, and therefore GOL § 5-701(a)(2) is inapplicable. * * * *

[¶10] We have examined the parties' remaining contentions for affirmative relief and find them to be without merit.

The COLEMAN COMPANY, INC. v. CARGIL INTERNATIONAL CORP.

District Court of Appeal of Florida, Third District (1998)

731 So.2d 2

NESBITT, J.

[¶1] In the proceedings below, the jury found that camping supplies manufacturer Coleman breached an oral distributorship agreement with Cargil International, Coleman's distributor in Venezuela. Because the oral distributorship contract was for a period of more than one year, its enforcement is barred by the statute of frauds. Therefore, we reverse.

[¶2] The record reveals that the oral agreement at issue here was made in November 1993, and that the agreement anticipated performance for the entire calendar year 1994. Significantly, Cargil never disputed that the contract was made in November 1993. Nor could it: because the contract was to commence on January 1 of the calendar year 1994, and continue through December 31 of the same year; the contact, discussions, negotiations and agreement were necessarily reached sometime earlier. Thus, the entire term of the contract was for over one year. Such an oral contract is unenforceable pursuant to the statute of frauds. See §§ 672.201(1), 725.01, Fla. Stat. (1995). *See also Yates v. Ball*, 132 Fla. 132, 181 So. 341, 344 (Fla.1937) ("to make a parol contract void, it must be apparent that it was the understanding of the parties that it was not to be performed within one year from the time it was made"); *Khawly v. Reboul*, 488 So.2d 856 (Fla. 3d DCA 1986). * * * *

[¶3] In conclusion, the trial court should have entered a directed verdict for Coleman on the underlying action and on the counterclaim for account stated.

[¶4] The judgment appealed from is reversed with directions to enter a judgment consistent with this opinion. * * * *

Question: Does anyone doubt that Coleman made the promise at issue in *The Coleman Co., Inc*. case? If you are Coleman's attorney and the Coleman sales rep says he actually made this promise, should you raise the Statute of Frauds?

PROBLEMS 38–42. Consider the following hypotheticals. Are any of them unenforceable under the statute of frauds as agreements "not to be performed within one year" if not in writing?

38. A promise by a five-person corporation to build a 200-foot yacht.

39. A promise made on February 9, 2027, to appear live on a TV show on February 10, 2028.

40. A promise made on February 9, 2027, to cut down and deliver certain timber on or before February 10, 2028.

41. A promise to build a house within fifteen months.

42. A promise by a railroad to maintain a switch so long as the other railroad needs it.

HOOKS v. BRIDGEWATER

Supreme Court of Texas (1921)

229 S.W. 1114

PHILLIPS, C. J.

[¶1] The plaintiff, Bob Bridgewater, brought the suit against the administrator of the estate of John W. Davis, deceased, and the heirs at law of Davis, to recover Davis' estate. The suit was in fact one to enforce a verbal agreement claimed to have been entered into by the plaintiff's father—at that time his only surviving parent, when the plaintiff was a child of nine years of age—and Davis, whereby the father contracted to surrender plaintiff's custody and control to Davis, and Davis—a single man who never married—agreed upon that consideration to rear the plaintiff, giving him the care and rights of a son, make him his heir and leave to him at his death all of his property.

[¶2] The trial court found that the evidence established the making of the parol agreement; that Davis took charge of the plaintiff under the agreement when he was thus a child, and plaintiff's father never thereafter exercised any control over him; that the plaintiff lived with Davis thereafter, giving him the affection and obedience of a son, and performing chores and services around his home as needed, for which he received no wages or money consideration. Davis failed to bequeath any of his property to plaintiff, dying intestate, leaving an estate of both real and personal property. Before his death he had not placed the plaintiff in possession of any of it.

[¶3] Judgment for the defendants was rendered in the trial court. On the appeal, this was reversed by the honorable Court of Civil Appeals for the First District and judgment rendered for the plaintiff.

[¶4] As it affected the land belonging to Davis, the contract was plainly condemned by the statute of frauds. It was merely a parol agreement whereby in consideration of the father's surrender of the custody of the plaintiff and the latter's living with Davis as a son, Davis' lands owned at his death should become

the plaintiff's property. It was in effect but a parol sale of Davis' lands to be performed by him in the future, and has no higher dignity than such a sale. The question presented by this feature of the case is whether the performance of the contract by the plaintiff relieves it from the operation of the statute of frauds, or, as more accurately stated, renders the contract enforceable in equity notwithstanding the statute.

[¶5] The Court of Civil Appeals has held that it does, despite the fact that there was never any possession of the lands by the plaintiff in Davis' lifetime.

[¶6] To sustain this holding, there must be created by judicial authority another exception to the operation of the statute of frauds, one unsanctioned by any previous decision of this court, and of larger consequence than any heretofore recognized by it. This is evident. For if it be the law that a contract of this kind may, under the circumstances here present, be enforced against a decedent's estate, the entire inheritances of families are, for the benefit of strangers to the blood, put at the mercy of parol evidence.

[¶7] From an early time it has been the rule of this court, steadily adhered to, that to relieve a parol sale of land from the operation of the statute of frauds, three things were necessary: 1. Payment of the consideration, whether it be in money or services. 2. Possession by the vendee. And, 3. The making by the vendee of valuable and permanent improvements upon the land with the consent of the vendor; or, without such improvements, the presence of such facts as would make the transaction a fraud upon the purchaser if it were not enforced. Payment of the consideration, though it be a payment in full, is not sufficient. This has been the law since *Garner v. Stubblefield*, 5 Tex. 552. Nor is possession of the premises by the vendee. *Ann Berta Lodge v. Leverton*, 42 Tex. 18. Each of these three elements is indispensable, and they must all exist.

[¶8] Regardless of the disposition of other courts to engraft other exceptions upon a plain and salutary statute which had its origin in the prolific frauds and perjuries with which parol contracts concerning lands abounded, this court has always refused to further relax the statute. We think the wisdom of its course has been justified.

[¶9] Equity has no concern in such cases except to prevent the perpetration of a fraud. That is the only ground that can justify its interference. Otherwise, the exercise of its jurisdiction for the practical annulment of the statute would be but bare usurpation. It is not to remedy a possible loss to the purchaser that it may intervene. It is the operation of a plain and valid statute that is to be relieved against. For this reason eminent judges have doubted whether under any circumstances courts of equity had originally the power to enforce such parol agreements in open disregard of the statute, and have questioned the wisdom of departing from its certain rule however plausible the pretext. The statute is valid; it is imperative; it is emphatic. Its simple requirement that contracts for the transfer of lands be in writing, imposes no hardship. The effect of its relaxation in what seemed to the courts hard cases has produced abuses almost as great as would have its rigorous enforcement, in the substitution of a doubtful state of the law for a rule that was plain and certain and easily capable of observance. In a noted early English case the chancellor made the following observation of this trend of judicial decisions:

> The statute was made for the purpose of preventing frauds and perjuries, and nothing can be more manifest to any person who has been in the habit of practicing in the courts of equity than that the relaxation of the statute has been the ground of much perjury and much fraud. If the statute had been rigorously observed, the result would probably have been that few instances of parol agreements would have occurred. Agreements would, from the

> necessity of the case, have been reduced to writing; whereas it is manifest that the decisions on the subject have opened a new door to fraud, and that under the pretense of part execution, if possession is had in any way whatever, means are frequently found to put a court of equity in such a situation that, without departing from its rule, it feels obliged to break through the statute.

Whatever may be the diversity of views upon the general subject, it is clear that to warrant equity's 'breaking through the statute' to enforce such a parol contract, the case must be such that the nonenforcement of the contract—or the enforcement of the statute—would, itself, plainly amount to a fraud. This is the basis, and the only basis, for the jurisdiction which courts of equity have assumed in their creation of exceptions to the statute. When it is considered that the exercise of that jurisdiction results in any case in practically setting the statute aside, certainly there should exist some positive rule which will insure its exercise for only the prevention of an actual fraud as distinguished from a mere wrong, and by which the question of whether a failure to enforce the contract would result in such a fraud may be determined so surely as to leave the statute itself, through the exactness of the exception, with some definiteness of operation. The merit of the rule announced by this court in every decision where it has dealt with the subject is that it does this. By its requirement of payment of the consideration, adverse possession by the purchaser, and his making of valuable and permanent improvements in order for the contract to be exempt from the statute, it insures the application of the exemption only for the avoidance of actual fraud, and secures, as it should, the full operation of the statute in all other cases. Its purpose is both to prevent the perpetration of fraud and to safeguard the titles of lands. It is a rule founded in sound reason and common experience, and is fair and just.

[¶10] There is no fraud in refusing to enforce the contract where only the consideration is paid. The value of the consideration may in a law action be recovered. Nor where only possession of the premises is given. In such case there is no performance by the purchaser of any obligation. Nor even where there is both payment of the consideration and possession; without valuable and permanent improvements made on the faith of contract, or their equivalent. Merely the transfer of the possession by the vendor could create no estoppel against him. A transfer of the possession of the soil affords no presumption of a sale of the fee. As said by Judge Moore in *Ann Berta Lodge v. Leverton*, 42 Tex. 18, to permit a person who can show no other act done beyond the transfer of the possession of the soil from the owner to himself, to enforce an oral agreement for the sale of the fee, would practically repeal the statute of frauds and let in all the mischiefs it was intended to guard against. But where there is payment of the consideration, the surrender of possession and the making of valuable and permanent improvements on the faith of the purchase with the owner's knowledge or consent, there is created an estoppel against him and it may fairly be said that a fraud upon the purchaser would result if the owner were permitted to repudiate the contract.

[¶11] Not only can there be no fraud upon a purchaser in refusing to enforce a parol contract for the sale of land where there has been no performance beyond the payment of the consideration, but a further strong reason for the requirement of possession is that without it the existence of the contract rests altogether in parol evidence, which common experience has shown to be too unstable and uncertain to be permitted to work a divestiture of title to real property. If, however, the purchaser be let into possession, there is furnished by an affirmative act of the owner himself at least a corroborative fact that the contract was actually made.

[¶12] At all events it is a positive requirement under the holding of this court. It is a part of the settled law, and is not now to be dispensed with. * * * *

[¶13] The parol contract here has no basis for its enforcement, other than the plaintiff's performance by his assuming with Davis the relation and rendering him the service of a son. That was the consideration for Davis' agreement to make him the owner of his estate. The case, therefore, is simply one where the consideration for a parol agreement to transfer the title to land has been paid, with no possession of the land surrendered and no valuable and permanent improvements made by the purchaser on the faith of the agreement. In no other character of case resting only upon the payment of the consideration could such a contract be enforced in this State. If the consideration for Davis' agreement had been an amount of money, however large, and had been fully paid, without possession of the land and valuable and permanent improvements the contract would be held incapable of enforcement. If the payment of the consideration is to be held insufficient in one case, it should be so held in all cases. The test is not the character of the consideration or the value of the bargain. Why should the nature of the consideration or its exceptional value alone determine the question, instead of the rule itself which, in addition to the payment of the consideration, whatever its character and value, requires possession of the land and valuable and permanent improvements? And why should there be allowed the enforcement of a parol contract for the sale of land, the consideration being of the nature paid in this case, and deny its enforcement where the consideration has been fully paid in money? No satisfactory answer can be given to these questions.

[¶14] The holding of the Court of Civil Appeals is that a distinction should be made in this case because the value of the plaintiff's services in his assumed relation as Davis' son could not be measured in money. The plaintiff's father in the making of the contract and as its basis, as well as Davis, measured them in property.

[¶15] The father calculated the money value of the plaintiff's filial relation to himself, what it would be worth to surrender that relation to Davis and the value it would be to Davis, placed it all at the value of Davis' estate, and closed the bargain accordingly. The suit assumes that Davis was able to estimate the value of the relationship and services to himself, for it charges that he agreed to pay for them by the transfer of his estate. The entire case is one where the custody, the relationship and the services of the plaintiff were dealt with as property; where it was agreed that they should be exchanged for property, showing that the parties estimated their value in property; and where, now, it is sought, as in any other pecuniary bargain, to compel payment of them in property. If the parties to the agreement were able to estimate their value in property, a court should be competent to value them in money. The value of a child's services to his parents, and of a husband's or wife's relation and affection are every day the matter of assessment by courts. They are not held uncertain as a matter of judicial investigation. There would equally be no difficulty, we apprehend, in a similar determination of the value of the plaintiff's services and relationship to Davis.

[¶16] Aside from the invalidity of the contract as to the land of the estate under the statute of frauds and its being incapable of enforcement because there was no possession by the plaintiff of the land, it is a character of contract which should be held void as a matter of public policy. A parent has no property interest in his child and should not be permitted to deal with his child as property. The law should not encourage the relinquishment by parents of their children and the renunciation of a sacred relation imposed by nature merely for the children's enrichment by placing the seal of validity upon a contract in which a parent in effect barters his child away for a property return. It is more concerned in fostering and maintaining that relation and guarding its valuable and wholesome influences than in promoting the child's financial prosperity. Let it be once held that a parent's contract of this kind is valid and may be enforced, and every parent will be free to transfer his children to anyone willing to pay them well for the bargain. We are unwilling to subscribe to such a doctrine. It tends to the destruction of one of the finest relations of human life, to the subversion of the family tie, and to the reversal of an ordering of nature which is essential to human happiness and the

security of society. It reduces parental duty and the child's welfare to the sordid level of financial profit, and would license the easy surrender of that duty for merely the child's financial advantage. The custody of a child is not a subject matter of contract and therefore can constitute no consideration for a contract. The attempted agreement here was therefore not a contract. *Legate v. Legate*. Davis could not have enforced it because based upon a void consideration. If Davis could not have enforced it against the plaintiff, it is not enforceable in the plaintiff's favor.

[¶17] True, contracts between two persons upon a valuable consideration, that one will leave his property to the other, are enforceable where no statute is contravened. Such is the recognized law and was the holding in *Jordan v. Abney*, 97 Tex. 296, 78 S. W. 486. There, in addition to the contract made between the plaintiff's father and Mr. and Mrs. Ogle, there was a contract between the plaintiff herself and Mrs. Ogle, made after Ogle's death, confirming the previous contract and by which Mrs. Ogle agreed to leave the plaintiff her property. Here, there was no contract between the plaintiff and Davis for the former's service. The contract was between the plaintiff's father and Davis by which his custody and filial relation were attempted to be bargained away as though properly the subject matter of contract. They could not form the basis of a contract under the express holding in *Legate v. Legate*.

[¶18] The judgment of the honorable Court of Civil Appeals is reversed and the judgment of the District Court is affirmed.

Questions:

1. Is the oral contract valid under the Statute of Frauds?

2. On what section of the Statute does the court ground its ruling?

3. Of what legal relevance is the fact that Bob Bridgewater performed?

4. What is the policy of the Statute of Frauds?

5. Do you think that Bob Bridgewater was fabricating Davis's promise? Does it bother you that he could be sold as a child and then disinherited because his so-called adoptive father never promised in writing?

6. What is the alternate ground of this decision?

W. L. TANENBAUM v. BISCAYNE OSTEOPATHIC HOSPITAL, INC.

Supreme Court of Florida (1966)

190 So.2d 777

THOMAS, Justice.

[¶1] The facts in this case are simple. W. L. Tanenbaum, the petitioner, is an osteopathic physician specializing in radiography. In September 1961 he removed from Allentown, Pennsylvania, to North Miami Beach where he became osteopathic radiologist at respondent's North Miami Beach hospital. The parties entered into an oral contract providing for his services for a period of five years terminable only after the expiration of that period and even then only upon 90 days written notice by either party. There was evidence that petitioner importuned respondent to execute a written agreement but this was never accomplished.

[¶2] In April 1962 the respondent notified the petitioner that his services would be discontinued the first of the following July and in the next month petitioner filed his complaint for damages resulting from the respondent's action. Principal defense of the respondent, then defendant, was the Statute of Frauds, the relevant part of which provides, Sec. 725.01, that '(n)o action shall be brought * * * upon any agreement that is not be performed within the space of one year from the making thereof, unless the agreement or promise upon which such action shall be brought, or some note or memorandum thereof shall be in writing and signed by the party to be charged therewith or by some other person by him thereunto lawfully authorized.'

[¶3] So, as might have been expected, the respondent moved, at the end of plaintiff's case for a directed verdict in its favor. This was denied. The motion was repeated at the close of all testimony and evidence, and ruling upon it was reserved by the court. Then the jury returned a verdict for the plaintiff in the amount of $40 thousand. Later the respondent presented a motion for a judgment in accordance with the motion for directed verdict and the court granted it.

[¶4] The trial judge found that the Statute of Frauds had been properly pleaded and that the contract was 'within' the statute. He observed that the plaintiff, petitioner, had opposed the motion on the ground that the respondent was estopped from resorting to the statute. The judge rejected this view and entered judgment for the defendant, respondent, accordingly.

[¶5] The controversy then went to the District Court of Appeal, Third District, where the appellant presented the lone question whether or not the Circuit Court had ruled properly that his claim was, as a matter of law, barred by the Statute of Frauds. That Court commented that the sole reason urged for the non-applicability of the Statute was the doctrine of 'promissory estoppel' which the Court said did not appear in any of the Florida decisions. Such being the case the Court was of the opinion that great caution should be exercised 'in the consideration of the advisability of ingrafting onto the law of this State a provision which may have the effect of nullifying the legislative will of the State as expressed by the inactment (sic) of the Statute of Frauds * * *.'

[¶6] The District Court of Appeal referred to three decisions in which the doctrine of promissory estoppel had been recognized, *Alaska Airlines, Inc. v. Stephenson*, 15 Alaska 272, 217 F.2d 295; *Fibreboard Products, Inc. v. Townsend*, 9 Cir., 202 F.2d 180, and *Seymour v. Oelrichs*, 156 Cal. 782, 106 P. 88, and commented that no decision had been found indicating that the principle of promissory estoppel as related

to the Statute of Frauds had been 'favorably considered by any Florida court in a law action * * *.' We are unable to elaborate on this statement except to say that there have been brought to our attention two cases in which the doctrine had been mentioned, *South Investment Corporation, et al. v. Norton, et al*., Fla., 57 So.2d 1, and *Southeastern Sales & Service Co. v. T. T. Watson, Inc.*, Fla. App., 172 So.2d 239. But in neither was the doctrine of promissory estoppel embraced.

[¶7] The principle was also recognized in the Restatement of Contracts, s 90:

> 'A promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise.'

The language of the Statute of Frauds we have already quoted is quite clear and its origin and purpose were plainly stated in *Yates v. Ball*, 132 Fla. 132, 181 So. 341, as follows:

> 'The statute of frauds grew out of a purpose to intercept the frequency and success of actions based on nothing more than loose verbal statements or mere innuendos. To accomplish this, the statute requires that all actions based on agreements for longer than one year must depend on a written statement or memorandum, signed by the party to be charged. The statute should be strictly construed to prevent the fraud it was designed to correct, and so long as it can be made to effectuate this purpose, Courts should be reluctant to take cases from its protection.' (Italics supplied.)

Doubtless because this is a matter of first impression and therefore involves the introduction into the law of this State a relatively novel concept, the case was sent here on a certificate under Sec. 4(2), Article V of the Constitution, F.S.A. The question that emerges for resolution by us is whether or not we will adopt by judicial action the doctrine of promissory estoppel as a sort of counteraction to the legislatively created Statute of Frauds. This we decline to do.

[¶8] We agree with the conclusions of the Circuit Court and District Court of Appeal in rejecting the so-called doctrine of promissory estoppel and especially with the observation of the latter with reference to embracing it in view of the legislative prerogative of dealing with matters of this nature.

[¶9] The petitioner had but to follow the provisions of the Statute of Frauds to secure his rights under the arrangement with the respondent instead of taking the position, rather tardily that they did not apply to him. Thirty-three years have passed since the Restatement we have quoted was adopted and there have been about 15 intervening sessions of the legislature at which the contents of Sec. 90 of the Restatement could have been incorporated into the act yet we know of no such effort or accomplishment.

[¶10] Having undertaken to answer the question certified, the writ of certiorari which brought it here is discharged.

THORNAL, C.J., and DREW and CALDWELL, JJ., concur.

ERVIN, J., dissents with opinion.

O'CONNELL, J., dissents and concurs with ERVIN, J.

Questions:

1. Does the one-year rule apply in this case?

2. Why cannot a showing of promissory estoppel overcome the Statute of Frauds in Florida?

3. Compare the reasoning of *Tannenbaum* with the following excerpt from *Janke Construction Co., Inc. v. Vulcan Materials Co.*, 386 F. Supp. 687 (D. Wis. 1974):

> [¶1] One question remains. Can the statute of frauds, raised by defendant as a defense in the context of plaintiffs contractual claim, be raised as a defense to a claim for damages based on the theory of promissory estoppel? The issue has not been raised in the Wisconsin courts and there is a split of opinion in other jurisdictions where this question has been considered.
>
> [¶2] Some states, such as New York, have held that promissory estoppel has no application where the oral contract comes within the statute of frauds except in cases involving charitable subscriptions. *Kahn v. Cecelia Co.*, 40 F. Supp. 878 (S.D.N.Y.1941). Other jurisdictions have held that the defense of the statute is precluded either when there has been (1) a misrepresentation that the statute's requirements have been complied with, (2) a promise to make a memorandum which was also relied on by the promisee, or (3) a subsidiary promise not to raise the statute as a defense. *Tiffany Incorporated v. W.M.K. Transit Mix, Inc.*, 16 Ariz. App. 415, 493 P.2d 1220 (1972); *21 Turtle Creek Sq., Ltd. v. New York St. Teach. Retire Sys.*, 432 F.2d 64 (5th Cir. 1970) (Construing Texas Law); *Alaska Airlines v. Stephenson*, 15 Alaska 272, 217 F.2d 295 (9th Cir. 1954); *Easton v. Wycoff*, 4 Utah 2d 386, 295 P.2d 332 (1956); *Wolfe v. Wallingford Bank & Trust Co.*, 124 Conn. 507, 1 A.2d 146 (1938).[*****]
>
> [¶3] Some jurisdictions, recognizing that the doctrine of promissory estoppel is based essentially on the principles of equitable estoppel and fraud, are loath to deny relief where the statute of frauds is raised as a defense and will enforce an oral promise otherwise coming within the statute. *McIntosh v. Murphy*, 52 Haw. 29, 469 P.2d 177 (1970); *N. Litterio*

[*****] [7] Many of these cases cite Comment f to § 178, Restatement of the Law of Contracts, as a basis for their rulings. Comment f, which deals with the statute of frauds, states: 'Though there has been no satisfaction of the Statute, an estoppel may preclude objection on that ground in the same way that objection to the non-existence of other facts essential for the establishment of a right or a defense may be precluded. A misrepresentation that there has been such satisfaction if substantial action is taken in reliance on the representation, precludes proof by the party who made the representation that it was false; and a promise to make a memorandum, if similarly relied on, may give rise to an effective promissory estoppel if the Statute would otherwise operate to defraud.'

& Company v. Glassman Construction Company, *supra*; *Miller v. Lawlor*, 245 Iowa 1144, 66 N.W.2d 267 (1954); *Sessions v. Southern California Edison Co*., 47 Cal.App.2d 611, 118 P.2d 935 (1941).

[¶4] In *McIntosh* the Supreme Court of Hawaii held that an oral contract of employment was enforceable and that money damages would be granted notwithstanding that the contract allegedly violated the statute of frauds. It stated, 469 P.2d at 180:

'It is appropriate for modern courts to cast aside the raiments of conceptualism which cloak the true policies underlying the reasoning behind the many decisions enforcing contracts that violate the Statute of Frauds. There is certainly no need to resort to legal rubrics or meticulous legal formulas when better explanations are available. The policy behind enforcing an oral agreement which violated the Statute of Frauds, as a policy of avoiding unconscionable injury, was well set out by the California Supreme Court. In *Monarco v. Lo Greco*, 35 Cal.2d 621, 623, 220 P.2d 737, 739 (1950), a case which involved an action to enforce an oral contract for the conveyance of land on the grounds of 20 years performance by the promisee, the court said:

> 'The doctrine of estoppel to assert the statute of frauds has been consistently applied by the courts of this state to prevent fraud that would result from refusal to enforce oral contracts in certain circumstances. Such fraud may inhere in the unconscionable injury that would result from denying enforcement of the contract after one party has been induced by the other seriously to change his position in reliance on the contract * * *.'

In *Litterio* the District of Columbia Circuit employed a different rationale for precluding application of the statute of frauds in a construction bidding case. It held that a subcontractor would be held liable on his bid, not on the basis of a contractual obligation inasmuch as no contract existed, but under the doctrine of promissory estoppel if all the elements of the doctrine were shown to be present. Thereupon the Court commented in a footnote, 319 F.2d at 740:

> 'The issue as to the applicability of the Statute of Frauds is no longer germane in light of our holding that no contract was created.'

[¶5] I agree with the statement in *Litterio* as to the inapplicability of the statute. The statute of frauds relates to the enforceability of contracts; promissory estoppel relates to promises which have no contractual basis and are enforced only when necessary to avoid injustice. The Wisconsin Supreme Court clearly stated in Hoffman that a promise which could not meet the requirements of an offer that would ripen into a contract if accepted by the promisee is nonetheless enforceable to avoid injustice if the other elements of promissory estoppel are present. * * * * Accordingly, I find the statute is not applicable in an action based on promissory estoppel.

4. So, there is a split of authority about whether the Statute of Frauds applies to a promise that would otherwise be enforceable under promissory estoppel. The R2K authors had a chance to weigh in here but

sort of punted. According to R2K § 139, promissory estoppel can make an unwritten (unrecorded) promise binding under the Statute of Frauds but only when "injustice can be avoided only by enforcement of the promise." The section then gives five factors to consider in determining whether "injustice can be avoided only by enforcement." The factors include the availability of other remedies, the "definite and substantial character" of the reliance, and the extent to which the reliance corroborates that a promise was made. See R2K § 139(2).

Here's the difficulty. Remember in *Hooks*, the case you just read, where the court equated fraud, which creates an exception to the Statute, with estoppel? The court is talking about equitable estoppel. There is something similar between fraud and equitable estoppel. Both give a remedy for a non-factual statement, one in damages and the other in not allowing the statement maker to deny the statement's content. Both require reasonable reliance, and both are meant to protect the relying party from harm. But promissory estoppel is similar to both of these doctrines, too. Like fraud, it gives a remedy, and like both fraud and equitable estoppel, it requires reasonable reliance. The difference is that PE fact patterns start with a promise, not a misstatement of fact. Otherwise, PE fact patterns can look a lot like fraud. Actually, under the law, promising without having any intent to perform is considered a false statement for fraud law, and in such a case, a fact pattern could prove both fraud and promissory estoppel.

So perhaps the courts can be forgiven for waffling about here. Your casebook author's incomplete reading of the cases in this area suggests that which side the state falls on depends in part on how fraud-like was the first PE fact pattern in which the Statute of Frauds was raised before their courts.

5. The UCC Article 2 also has a statute of frauds, affectionately known as "the UCC statute of frauds." It states that "a contract for the sale of goods for the price of $500 or more is not enforceable . . . unless there is some writing [or record, in the UCC's latest version] sufficient to indicate that a contract for sale has been made between the parties and signed by the party against whom enforcement is sought . . . ." UCC § 2-201. The UCC famously allows the writing or record to omit the price of the goods. All that is necessary is the parties, the quantity of goods, and that the thing "indicate . . a contract for sale has been made." Look at the language of UCC § 2-201 and also the Statute of Frauds. Must both parties sign the writing or record?

D. The Final Push: When Does a Contract Form?

Eventually, the law adopted assent also as a paradigm. How it came to this result is fascinating. The three cases in this section were the mechanism for the adoption. Oddly, two are a response to a surrogate for the bargain rule that we have already read, in *Nicholas v. Raynbred*. Go back and read the timing rule in that case, if you will. Can you recall the purpose of that rule? Eventually, the timing rule became untenable.

COOKE v. OXLEY

King's Bench (1790)

3 Term Rep. 653

[¶1] This was an action [in assumpsit]; and the ... count in the declaration ... stated that on [a certain date] a discourse was had ... concerning the buying of 266 hogsheads of tobacco; and [in] that discourse [Oxley] proposed to [Cooke] that [Oxley] should sell and deliver to [Cooke] the said 266 hogsheads [at a certain price]; whereupon [Cooke] desired [Oxley] to give [Cooke] time to agree to or dissent from the proposal till the hour of four in the afternoon of that day, to which [Oxley] agreed; ... ; [Cooke also] averred that he did agree to purchase the same upon the terms aforesaid, and did give notice thereof to [Oxley] before the hour of four in the afternoon of that day; he also averred that he requested [Oxley] to deliver to him the said hogsheads, and offered to pay to [Oxley] the said price for the same, yet that [Oxley] did not, &c.

[¶2] [The question then arose whether there was consideration for Oxley's promise to sell.]

[¶3] Erskine and Wood [argued for Cooke that consideration existed]: This was a bargain and sale on condition; and though the plaintiff might have rescinded the contract before four o'clock, yet not having done so, the condition was complied with, and both parties were bound by the agreement. The declaration considered this as a complete bargain and sale; for the breach of the agreement is for not delivering the tobacco, and not for not selling it.

[¶4] Lord Kenyon, Ch. J. ...: Nothing can be clearer than that at the time of entering into this contract the engagement was all on one side; the other party was not bound; it was therefore nudum pactum.

[¶5] Buller, J.-It is impossible to support this declaration in any point of view. In order to sustain a promise, there must be either a damage to the plaintiff, or an advantage to the defendant: but here was neither when the contract was first made. Then as to the subsequent time, the promise can only be supported on the ground of a new contract made at four o'clock; but there is no pretence [sic] for that. It has been argued that this must be taken to be a complete sale from the time when the condition was complied with; but it was not complied with, for it is not stated that the defendant did agree at four o'clock to the terms of the sale; or even that the goods were kept till that time.

[¶6] Grose, J.-The agreement was not binding on the plaintiff before four o'clock; and it is not stated that the parties came to any subsequent agreement; there is therefore no consideration for the promise. ....

Questions:

1. How is this case different from *Nicholas v. Raynbred*?

2. What is the issue in *Cooke*? What was its resolution? What rule did the court follow?

Note: *Cooke* is one of the most misunderstood common law decisions of all time. Commentators and later courts argued over its meaning for fifty years after it was decided. The difficulty was in squaring *Cooke* with *Adams v. Lindsell*, which you will read shortly. *Cooke* has never been overruled, but, in fact, *Cooke* is no longer the law in American jurisdictions. However, *Cooke* provided the impetus for the introduction and development of the explicit assent requirement in Anglo-American contract law. Only by understanding *Cooke* can one see how the consideration doctrine caused the courts to approach assent in the way that they have.

PAYNE v. CAVE

King's Bench (1789)

3 Term Reports 148

[¶1] This was an action tried at the sittings after last term at Guildhall before Lord Kenyon, wherein the declaration stated, that the plaintiff, on 22d September 1788 was possessed of a certain worm-tub, and a pewter worm in the same, which were then and there about to be sold by public auction by one S. M. the agent of the plaintiff in that behalf; the conditions of which sale were to be the usual conditions of sale of goods sold by auction, &c. * * * *. And the plaintiff avers that the conditions of sale * * * are usual conditions of sale of goods sold by auction, to wit, that the highest bidder should be the purchaser, and should deposit five shillings in the pound, and that if the lot purchased were not paid for and taken away in two days time, it should be put up again and resold, &c. * * * *. It then stated, that the defendant became the purchaser of the lot in question for 40l. and was requested to pay the usual deposit, which he refused, &c. At the trial, the plaintiff's counsel opened the case thus: - The goods were put up in one lot at an auction; there were several bidders, of whom the defendant was the last, who bid 40l; the auctioneer dwelt on the bidding, on which the defendant said, "Why do you dwell? you will not get more." The auctioneer said that he was informed the worm weighed at least 1300 cwt. and was worth more than 40l; the defendant then asked him whether he would warrant it to weigh so much, and receiving an answer in the negative, he then declared that he would not take it, and refused to pay for it. It was resold on a subsequent day's sale for 30l. to the defendant, against whom the action was brought for the difference. Lord Kenyon being of opinion, on this statement of the case, that the defendant was at liberty to withdraw his bidding any time before the hammer was knocked down, nonsuited the plaintiff.

[¶2] Walton now moved to set aside the nonsuit, on the ground that the bidder was bound * * * * to abide by his bidding, and could not retract. By the act of bidding, he acceded to those conditions, one of which was, that the highest bidder should be the buyer. The hammer is suspended, not for the benefit of the bidder, or to give him an opportunity of repenting, but for the benefit of the seller: in the meantime the person who bid last is a conditional purchaser, if nobody bids more. Otherwise it is in the power of any person to injure the vendor, because all the former biddings are discharged by the last; and, as it happened in this very instance, the goods may thereby ultimately be sold for less than the person who was last out-bid would have given for them. * * * *

[¶3] The Court thought the nonsuit very proper. The auctioneer is the agent of the vendor, and the assent of both parties is necessary to make the contract binding; that is signified on the part of the seller by knocking down the hammer, which was not done here till the defendant had retracted. An auction is not unaptly called locus pœnitentiae. Every bidding is nothing more than an offer on one side, which is not binding on either side till it is assented to. But according to what is now contended for, one party would be bound by the offer, and the other not, which can never be allowed.

Rule refused.

Questions:

1. Was Cave's bid revocable?

2. What policy does the court cite in support of this decision? What authority have you seen for that policy in the case law we have studied?

3. What happens to prior bids when a bidder makes a higher bid?

4. UCC § 2-328 adopts the rule from *Payne v. Cave* as the default, but if you do auctions much, you will want to read that section.

ADAMS v. LINDSELL

1 Barnewall and Alderson 681 (1818)

[¶1] Action for non-delivery of wool according to agreement. At the trial at the last Lent Assizes for the county of Worcester, before Burrough J. it appeared that the defendants, who were dealers in wool, at St. Ives, in the county of Huntingdon, had, on Tuesday the 2d. of September 1817, written the following letter to the plaintiffs, who were woollen manufacturers residing in Bromsgrove, Worcestershire. "We now offer you eight hundred tods of wether fleeces, of a good fair quality of our country wool, at 35s. 6d. per tod, to be delivered at Leicester, and to be paid for by two months bill in two months, and to be weighed up by your agent within fourteen days, receiving your answer in course of post."

[¶2] This letter was misdirected by the defendants, to Bromsgrove, Leicestershire, in consequence of which it was not received by the plaintiffs in Worcestershire till 7 p.m. on Friday, September 5th. On that evening the plaintiffs wrote an answer, agreeing to accept the wool on the terms proposed. The course of the post between St. Ives and Bromsgrove is through London, and consequently this answer was not received by the defendants till Tuesday, September 9th. On the Monday September 8th, the defendants not having, as they expected, received an answer on Sunday September 7th, (which in case their letter had not been misdirected, would have been in the usual course of the post,) sold the wool in question to another

person. Under these circumstances, the learned Judge held, that the delay having been occasioned by the neglect of the defendants, the jury must take it, that the answer did come back in due course of post; and that then the defendants were liable for the loss that had been sustained: and the plaintiffs accordingly recovered a verdict.

[¶3] Jervis having in Easter term obtained a rule nisi for a new trial, on the ground that there was no binding contract between the parties,

[¶4] Dauncey, Puller, and Richardson, shewed cause. They contended, that at the moment of the acceptance of the offer of the defendants by the plaintiffs, the former became bound. And that was on the Friday evening, when there had been no change of circumstances. They were then stopped by the Court, who called upon

[¶5] Jervis and Campbell in support of the rule. They relied on Payne v Cave, and more particularly on Cooke v Oxley. In that case, Oxley, who had proposed to sell goods to Cooke, and given him a certain time at his request, to determine whether he would buy them or not, was held not liable to the performance of the contract, even though Cooke, within the specified time, had determined to buy them, and given Oxley notice to that effect. So here the defendants who have proposed by letter to sell this wool, are not to be held liable, even though it be now admitted that the answer did come back in due course of post. Till the plaintiffs answer was actually received, there could be no binding contract between the parties; and before then, the defendants had retracted their offer, by selling the wool to other persons. But

[¶6] The Court said, that if that were so, no contract could ever be completed by the post. For if the defendants were not bound by their offer when accepted by the plaintiffs till the answer was received, then the plaintiffs ought not to be bound till after they had received the notification that the defendants had received their answer and assented to it. And so it might go on ad infinitum. The defendants must be considered in law as making, during every instant of the time their letter was travelling, the same identical offer to the plaintiffs; and then the contract is completed by the acceptance of it by the latter. Then as to the delay in notifying the acceptance, that arises entirely from the mistake of the defendants, and it therefore must be taken as against them, that the plaintiffs answer was received in course of post.

Rule discharged.

Questions:

1. Okay, here it is! The moment we've all be waiting for: The BIRTH OF ASSENT! Congratulations for making it this far! Did a contract form in this case?

2. Why didn't *Cooke v. Oxley* control?

3. Do we have concerns that one promise may not have caused the other?

Historical Note on Assent v. Consideration

The need to form contracts by post was not the only reason to shift to an assent-focused doctrinal structure. Civil law in continental Europe always focused on assent rather than consideration and remedy. From the early 1700s forward, common law judges (most enthusiastically Lord Mansfield, CJKB 1756-88) began adopting vocabulary from the civil law and importing civil law positions into the common law. Mansfield also began importing merchants' customs into the common law. Merchants to a great extent favored assent as a juridical concept. Mansfield was also Chief Justice while the Americans revolted in favor of government by consent and the French planned their revolution. Consent seemed to be the buzzword for this time period. The popularity of French law also contributed to this change. As noted, Pothier became the contract law treatise of choice for common lawyers around this time. American lawyers who acted as French popularizers, James Kent (Chief Judge, NY Supreme Court, and Chancellor) and Joseph Story (U.S. Supreme Court Justice and Harvard law professor), wrote treatises adopting Pothier's positions into various aspects of contract law. In England, a commentator wrote that Pothier was "law at Westminster as well as Orleans." Sir W. Jones, ESSAY OF THE LAW OF BAILMENTS 29 (2d ed. 1804).

What happened to consideration in all of this? It ceased to be a criterion for recovery of damages and became instead just one element of the test to see whether a contract formed. The law didn't have to be put together that way. Consideration as a concept entirely subsumes assent. Courts alternatively could have grounded recovery in agreement and then limited damages based on the consideration existing, for example. But that's not what happened.

Note and Questions on the Mailbox Rule

The rule of *Adams v. Lindsell* became known as the mailbox rule. The mailbox rule applies whenever acceptance is attempted by post in a case in which posting would be an acceptable method of acceptance. The mailbox rule has been applied to the following circumstances:

1. Attempted Withdrawal: Cases in which an offeror attempts to withdraw the offer but the withdrawal reaches the offeree only after the offeree has dropped the acceptance in the post office box. Under American law, a withdrawal of an offer is effective only upon receipt of the withdrawal by the offeree. The acceptance is effective when it is dropped in the mail. Should a contract form in this instance? Why not use receipt of acceptance as the time for acceptance?

2. Repudiation of an Acceptance: Cases in which the offeree drops an acceptance in the post and then repudiates the acceptance before it is received by the offeror. In some cases, the offeree has phoned or wired the offeror to repudiate before the offeror receives the acceptance but after the offeree has dropped the acceptance in the post. In other cases, the offeree has retrieved the letter of acceptance before it has arrived. If the mailbox rule applies, a contract forms when the acceptance is dropped in the post. Because a contract has formed, the repudiation has no effect. Why should that be true? Can you think of a policy supporting that view? (Actually, the decisions in these cases are not uniform. The U.S. Court of Claims has held that the repudiation of an acceptance is effective if the repudiation is received by the offeror before the acceptance. *See Rhode Island Tool Co. v. United States*, 128 F. Supp. 417, 130 Ct. Cl. 698 (1955); *Dick v.*

United States, 82 F. Supp. 362, 113 Ct. Cl. 94 (1949). Only the Court of Claims so holds; so, unless you are suing the United States in the Court of Claims, the mailbox rule governs.)

3. Loss of Acceptance: Cases in which the offeree drops the acceptance in the post but the post office loses the acceptance and it never arrives. A contract forms when the acceptance is dropped in the post, even if the letter is later lost. If the offeror acted as if there was no contract, she must bear that loss. Thus, the rule places liability for the loss on the offeror in most cases. Who really should be liable?

4. Time Required for Acceptance: Cases in which the offeror specified that the offer was to be "accepted" within X period of time. If the offeror said "within 10 days," then dropping the acceptance in the post on the 10th day should suffice. What reason can you give for this rule?

Please note that if the offeror wishes to change the mailbox rule by specifying in the offer that the acceptance must be received, the offeror is free so to specify and the courts will respect that specification.

Should the mailbox rule apply to option contracts? Courts have said yes and no. *See, e.g.*, *Palo Alto Town and Country Village, Inc. v. BBTC Co.*, 11 Cal.3d 494 (1974) (yes); *Livesey v. COPPS Corp.*, 90 Wis.2d 577 (App. 1979) (no). Many (perhaps most) options contain language like the following: "Purchaser may exercise its right to purchase the Premises at any time during the Option Term by giving written notice thereof to Seller." What about that language seems to require more than mere mailing? Can it be construed to require something less than actual receipt?

The United Nations Convention on Contracts for the International Sale of Goods (1980), or CISG, is a treaty comprising contract law governing transactions between persons in different countries where both countries are covered by the treaty, for instance, between a person in the US and one in Zambia. I bring this up here because if you look at CISG articles 16, 18, and 22, you will see that there is no reason to adopt the mailbox rule to each category 1–4 above: the CISG quite successfully adopts it to resolve some issues and rejects it as a rule for other issues.

E. What is Assent, Really, in Contract Law?

W. O. LUCY and J. C. Lucy v. A. H. ZEHMER and Ida S. Zehmer

Supreme Court of Appeals of Virginia (1954)

84 S.E.2d 516

BUCHANAN, J., delivered the opinion of the court.

[¶1] This suit was instituted by W. O. Lucy and J. C. Lucy, complainants, against A. H. Zehmer and Ida S. Zehmer, his wife, defendants, to have specific performance of a contract by which it was alleged the Zehmers had sold to W. O. Lucy a tract of land owned by A. H. Zehmer in Dinwiddie county containing

471.6 acres, more or less, known as the Ferguson farm, for $50,000. J. C. Lucy, the other complainant, is a brother of W. O. Lucy, to whom W. O. Lucy transferred a half interest in his alleged purchase.

[¶2] The instrument sought to be enforced was written by A. H. Zehmer on December 20, 1952, in these words: 'We hereby agree to sell to W. O. Lucy the Ferguson Farm complete for $50,000.00, title satisfactory to buyer,' and signed by the defendants, A. H. Zehmer and Ida S. Zehmer.

[¶3] The answer of A. H. Zehmer admitted that at the time mentioned W. O. Lucy offered him $50,000 cash for the farm, but that he, Zehmer, considered that the offer was made in jest; that so thinking, and both he and Lucy having had several drinks, he wrote out 'the memorandum' quoted above and induced his wife to sign it; that he did not deliver the memorandum to Lucy, but that Lucy picked it up, read it, put it in his pocket, attempted to offer Zehmer $5 to bind the bargain, which Zehmer refused to accept, and realizing for the first time that Lucy was serious, Zehmer assured him that he had no intention of selling the farm and that the whole matter was a joke. Lucy left the premises insisting that he had purchased the farm.

[¶4] Depositions were taken and the decree appealed from was entered holding that the complainants had failed to establish their right to specific performance, and dismissing their bill. The assignment of error is to this action of the court.

[¶5] W. O. Lucy, a lumberman and farmer, thus testified in substance: He had known Zehmer for fifteen or twenty years and had been familiar with the Ferguson farm for ten years. Seven or eight years ago he had offered Zehmer $20,000 for the farm which Zehmer had accepted, but the agreement was verbal and Zehmer backed out. On the night of December 20, 1952, around eight o'clock, he took an employee to McKenney, where Zehmer lived and operated a restaurant, filling station and motor court. While there he decided to see Zehmer and again try to buy the Ferguson farm. He entered the restaurant and talked to Mrs. Zehmer until Zehmer came in. He asked Zehmer if he had sold the Ferguson farm. Zehmer replied that he had not. Lucy said, 'I bet you wouldn't take $50,000.00 for that place.' Zehmer replied, 'Yes, I would too; you wouldn't give fifty.' Lucy said he would and told Zehmer to write up an agreement to that effect. Zehmer took a restaurant check and wrote on the back of it, 'I do hereby agree to sell to W. O. Lucy the Ferguson Farm for $50,000 complete.' Lucy told him he had better change it to 'We' because Mrs. Zehmer would have to sign it too. Zehmer then tore up what he had written, wrote the agreement quoted above and asked Mrs. Zehmer, who was at the other end of the counter ten or twelve feet away, to sign it. Mrs. Zehmer said she would for $50,000 and signed it. Zehmer brought it back and gave it to Lucy, who offered him $5 which Zehmer refused, saying, 'You don't need to give me any money, you got the agreement there signed by both of us.'

[¶6] The discussion leading to the signing of the agreement, said Lucy, lasted thirty or forty minutes, during which Zehmer seemed to doubt that Lucy could raise $50,000. Lucy suggested the provision for having the title examined and Zehmer made the suggestion that he would sell it 'complete, everything there,' and stated that all he had on the farm was three heifers.

[¶7] Lucy took a partly filled bottle of whiskey into the restaurant with him for the purpose of giving Zehmer a drink if he wanted it. Zehmer did, and he and Lucy had one or two drinks together. Lucy said that while he felt the drinks he took he was not intoxicated, and from the way Zehmer handled the transaction he did not think he was either.

[¶8] December 20 was on Saturday. Next day Lucy telephoned to J. C. Lucy and arranged with the latter to take a half interest in the purchase and pay half of the consideration. On Monday he engaged an attorney to examine the title. The attorney reported favorably on December 31 and on January 2 Lucy wrote Zehmer stating that the title was satisfactory, that he was ready to pay the purchase price in cash and asking when Zehmer would be ready to close the deal. Zehmer replied by letter, mailed on January 13, asserting that he had never agreed or intended to sell.

[¶9] Mr. and Mrs. Zehmer were called by the complainants as adverse witnesses. Zehmer testified in substance as follows:

[¶10] He bought this farm more than ten years ago for $11,000. He had had twenty-five offers, more or less, to buy it, including several from Lucy, who had never offered any specific sum of money. He had given them all the same answer, that he was not interested in selling it. On this Saturday night before Christmas it looked like everybody and his brother came by there to have a drink. He took a good many drinks during the afternoon and had a pint of his own. When he entered the restaurant around eight-thirty Lucy was there and he could see that he was 'pretty high.' He said to Lucy, 'Boy, you got some good liquor, drinking, ain't you?' Lucy then offered him a drink. 'I was already high as a Georgia pine, and didn't have any more better sense than to pour another great big slug out and gulp it down, and he took one too.'

[¶11] After they had talked a while Lucy asked whether he still had the Ferguson farm. He replied that he had not sold it and Lucy said, 'I bet you wouldn't take $50,000.00 for it.' Zehmer asked him if he would give $50,000 and Lucy said yes. Zehmer replied, 'You haven't got $50,000 in cash.' Lucy said he did and Zehmer replied that he did not believe it. They argued 'pro and con for a long time,' mainly about 'whether he had $50,000 in cash that he could put up right then and buy that farm.'

[¶12] Finally, said Zehmer, Lucy told him if he didn't believe he had $50,000, 'you sign that piece of paper here and say you will take $50,000.00 for the farm.' He, Zehmer, 'just grabbed the back off of a guest check there' and wrote on the back of it. At that point in his testimony Zehmer asked to see what he had written to 'see if I recognize my own handwriting.' He examined the paper and exclaimed, 'Great balls of fire, I got 'Firgerson' for Ferguson. I have got satisfactory spelled wrong. I don't recognize that writing if I would see it, wouldn't know it was mine.'

[¶13] After Zehmer had, as he described it, 'scribbled this thing off,' Lucy said, 'Get your wife to sign it.' Zehmer walked over to where she was and she at first refused to sign but did so after he told her that he 'was just needling him [Lucy], and didn't mean a thing in the world, that I was not selling the farm.' Zehmer then 'took it back over there * * * * and I was still looking at the dern thing. I had the drink right there by my hand, and I reached over to get a drink, and he said, 'Let me see it.' He reached and picked it up, and when I looked back again he had it in his pocket and he dropped a five dollar bill over there, and he said, 'Here is five dollars payment on it.' * * * * I said, 'Hell no, that is beer and liquor talking. I am not going to sell you the farm. I have told you that too many times before.''

[¶14] Mrs. Zehmer testified that when Lucy came into the restaurant he looked as if he had had a drink. When Zehmer came in he took a drink out of a bottle that Lucy handed him. She went back to help the waitress who was getting things ready for next day. Lucy and Zehmer were talking but she did not pay too much attention to what they were saying. She heard Lucy ask Zehmer if he had sold the Ferguson farm, and Zehmer replied that he had not and did not want to sell it. Lucy said, 'I bet you wouldn't take $50,000 cash for that farm,' and Zehmer replied, 'You haven't got $50,000 cash.' Lucy said, 'I can get it.' Zehmer

said he might form a company and get it, ‘but you haven’t got $50,000.00 cash to pay me tonight.’ Lucy asked him if he would put it in writing that he would sell him this farm. Zehmer then wrote on the back of a pad, ‘I agree to sell the Ferguson Place to W. O. Lucy for $50,000.00 cash.’ Lucy said, ‘All right, get your wife to sign it.’ Zehmer came back to where she was standing and said, ‘You want to put your name to this?’ She said ‘No,’ but he said in an undertone, ‘It is nothing but a joke,’ and she signed it.

[¶15] She said that only one paper was written and it said: ‘I hereby agree to sell,’ but the ‘I’ had been changed to ‘We’. However, she said she read what she signed and was then asked, ‘When you read ‘We hereby agree to sell to W. O. Lucy,’ what did you interpret that to mean, that particular phrase?’ She said she thought that was a cash sale that night; but she also said that when she read that part about ‘title satisfactory to buyer’ she understood that if the title was good Lucy would pay $50,000 but if the title was bad he would have a right to reject it, and that that was her understanding at the time she signed her name.

[¶16] On examination by her own counsel she said that her husband laid this piece of paper down after it was signed; that Lucy said to let him see it, took it, folded it and put it in his wallet, then said to Zehmer, ‘Let me give you $5.00,’ but Zehmer said, ‘No, this is liquor talking. I don’t want to sell the farm, I have told you that I want my son to have it. This is all a joke.’ Lucy then said at least twice, ‘Zehmer, you have sold your farm,’ wheeled around and started for the door. He paused at the door and said, ‘I will bring you $50,000.00 tomorrow. * * * * No, tomorrow is Sunday. I will bring it to you Monday.’ She said you could tell definitely that he was drinking and she said to her husband, ‘You should have taken him home,’ but he said, ‘Well, I am just about as bad off as he is.’

[¶17] The waitress referred to by Mrs. Zehmer testified that when Lucy first came in ‘he was mouthy.’ When Zehmer came in they were laughing and joking and she thought they took a drink or two. She was sweeping and cleaning up for next day. She said she heard Lucy tell Zehmer, ‘I will give you so much for the farm,’ and Zehmer said, ‘You haven’t got that much.’ Lucy answered, ‘Oh, yes, I will give you that much.’ Then ‘they jotted down something on paper * * * * and Mr. Lucy reached over and took it, said let me see it.’ He looked at it, put it in his pocket and in about a minute he left. She was asked whether she saw Lucy offer Zehmer any money and replied, ‘He had five dollars laying up there, they didn’t take it.’ She said Zehmer told Lucy he didn’t want his money ‘because he didn’t have enough money to pay for his property, and wasn’t going to sell his farm.’ Both of them appeared to be drinking right much, she said.

[¶18] She repeated on cross-examination that she was busy and paying no attention to what was going on. She was some distance away and did not see either of them sign the paper. She was asked whether she saw Zehmer put the agreement down on the table in front of Lucy, and her answer was this: ‘Time he got through writing whatever it was on the paper, Mr. Lucy reached over and said, ‘Let’s see it.’ He took it and put it in his pocket,’ before showing it to Mrs**.** Zehmer. Her version was that Lucy kept raising his offer until it got to $50,000.

[¶19] The defendants insist that the evidence was ample to support their contention that the writing sought to be enforced was prepared as a bluff or dare to force Lucy to admit that he did not have $50,000; that the whole matter was a joke; that the writing was not delivered to Lucy and no binding contract was ever made between the parties.

[¶20] It is an unusual, if not bizarre, defense. When made to the writing admittedly prepared by one of the defendants and signed by both, clear evidence is required to sustain it.

[¶21] In his testimony Zehmer claimed that he 'was high as a Georgia pine, 'and that the transaction 'was just a bunch of two doggoned drunks bluffing to see who could talk the biggest and say the most.' That claim is inconsistent with his attempt to testify in great detail as to what was said and what was done. It is contradicted by other evidence as to the condition of both parties, and rendered of no weight by the testimony of his wife that when Lucy left the restaurant she suggested that Zehmer drive him home. The record is convincing that Zehmer was not intoxicated to the extent of being unable to comprehend the nature and consequences of the instrument he executed, and hence that instrument is not to be invalidated on that ground. 17 C.J.S., Contracts, § 133 b., p. 483; *Taliaferro v. Emery*, 124 Va. 674, 98 S.E. 627. It was in fact conceded by defendants' counsel in oral argument that under the evidence Zehmer was not too drunk to make a valid contract.

[¶22] The evidence is convincing also that Zehmer wrote two agreements, the first one beginning 'I hereby agree to sell.' Zehmer first said he could not remember about that, then that 'I don't think I wrote but one out.' Mrs. Zehmer said that what he wrote was 'I hereby agree,' but that the 'I' was changed to 'We' after that night. The agreement that was written and signed is in the record and indicates no such change. Neither are the mistakes in spelling that Zehmer sought to point out readily apparent.

[¶23] The appearance of the contract, the fact that it was under discussion for forty minutes or more before it was signed; Lucy's objection to the first draft because it was written in the singular, and he wanted Mrs. Zehmer to sign it also; the rewriting to meet that objection and the signing by Mrs. Zehmer; the discussion of what was to be included in the sale, the provision for the examination of the title, the completeness of the instrument that was executed, the taking possession of it by Lucy with no request or suggestion by either of the defendants that he give it back, are facts which furnish persuasive evidence that the execution of the contract was a serious business transaction rather than a casual, jesting matter as defendants now contend.

[¶24] On Sunday, the day after the instrument was signed on Saturday night, there was a social gathering in a home in the town of McKenney at which there were general comments that the sale had been made. Mrs. Zehmer testified that on that occasion as she passed by a group of people, including Lucy, who were talking about the transaction, $50,000 was mentioned, whereupon she stepped up and said, 'Well, with the high-price whiskey you were drinking last night you should have paid more. That was cheap.' Lucy testified that at that time Zehmer told him that he did not want to 'stick' him or hold him to the agreement because he, Lucy, was too tight and didn't know what he was doing, to which Lucy replied that he was not too tight; that he had been stuck before and was going through with it. Zehmer's version was that he said to Lucy: 'I am not trying to claim it wasn't a deal on account of the fact the price was too low. If I had wanted to sell $50,000.00 would be a good price, in fact I think you would get stuck at $50,000.00.' A disinterested witness testified that what Zehmer said to Lucy was that 'he was going to let him up off the deal, because he thought he was too tight, didn't know what he was doing. Lucy said something to the effect that 'I have been stuck before and I will go through with it.''

[¶25] If it be assumed, contrary to what we think the evidence shows, that Zehmer was jesting about selling his farm to Lucy and that the transaction was intended by him to be a joke, nevertheless the evidence shows that Lucy did not so understand it but considered it to be a serious business transaction and the contract to be binding on the Zehmers as well as on himself. The very next day he arranged with his brother to put up half the money and take a half interest in the land. The day after that he employed an attorney to examine the title. The next night, Tuesday, he was back at Zehmer's place and there Zehmer told him for the first time, Lucy said, that he wasn't going to sell and he told Zehmer, 'You know you sold that place fair

and square.' After receiving the report from his attorney that the title was good he wrote to Zehmer that he was ready to close the deal.

[¶26] Not only did Lucy actually believe, but the evidence shows he was warranted in believing, that the contract represented a serious business transaction and a good faith sale and purchase of the farm.

[¶27] In the field of contracts, as generally elsewhere, 'We must look to the outward expression of a person as manifesting his intention rather than to his secret and unexpressed intention. 'The law imputes to a person an intention corresponding to the reasonable meaning of his words and acts.'' *First Nat. Bank v. Roanoke Oil Co.*, 169 Va. 99, 114, 192 S.E. 764, 770.

[¶28] At no time prior to the execution of the contract had Zehmer indicated to Lucy by word or act that he was not in earnest about selling the farm. They had argued about it and discussed its terms, as Zehmer admitted, for a long time. Lucy testified that if there was any jesting it was about paying $50,000 that night. The contract and the evidence show that he was not expected to pay the money that night. Zehmer said that after the writing was signed he laid it down on the counter in front of Lucy. Lucy said Zehmer handed it to him. In any event there had been what appeared to be a good faith offer and a good faith acceptance, followed by the execution and apparent delivery of a written contract. Both said that Lucy put the writing in his pocket and then offered Zehmer $5 to seal the bargain. Not until then, even under the defendants' evidence, was anything said or done to indicate that the matter was a joke. Both of the Zehmers testified that when Zehmer asked his wife to sign he whispered that it was a joke so Lucy wouldn't hear and that it was not intended that he should hear.

[¶29] The mental assent of the parties is not requisite for the formation of a contract. If the words or other acts of one of the parties have but one reasonable meaning, his undisclosed intention is immaterial except when an unreasonable meaning which he attaches to his manifestations is known to the other party. Restatement of the Law of Contracts, Vol. I, § 71, p. 74.

[¶30] '* * * * The law, therefore, judges of an agreement between two persons exclusively from those expressions of their intentions which are communicated between them. * * * *.' Clark on Contracts, 4 ed., § 3, p. 4.

[¶31] An agreement or mutual assent is of course essential to a valid contract but the law imputes to a person an intention corresponding to the reasonable meaning of his words and acts. If his words and acts, judged by a reasonable standard, manifest an intention to agree, it is immaterial what may be the real but unexpressed state of his mind. 17 C.J.S., Contracts, § 32, p. 361; 12 Am. Jur., Contracts, § 19, p. 515.

[¶32] So a person cannot set up that he was merely jesting when his conduct and words would warrant a reasonable person in believing that he intended a real agreement, 17 C.J.S., Contracts, § 47, p. 390; Clark on Contracts, 4 ed., § 27, at p. 54.

[¶33] Whether the writing signed by the defendants and now sought to be enforced by the complainants was the result of a serious offer by Lucy and a serious acceptance by the defendants, or was a serious offer by Lucy and an acceptance in secret jest by the defendants, in either event it constituted a binding contract of sale between the parties.

[¶34] Defendants contend further, however, that even though a contract was made, equity should decline to enforce it under the circumstances. These circumstances have been set forth in detail above. They

disclose some drinking by the two parties but not to an extent that they were unable to understand fully what they were doing. There was no fraud, no misrepresentation, no sharp practice and no dealing between unequal parties. The farm had been bought for $11,000 and was assessed for taxation at $6,300. The purchase price was $50,000. Zehmer admitted that it was a good price. There is in fact present in this case none of the grounds usually urged against specific performance.

[¶35] Specific performance, it is true, is not a matter of absolute or arbitrary right, but is addressed to the reasonable and sound discretion of the court. *First Nat. Bank v. Roanoke Oil Co.*, *supra*, 169 Va. at p. 116, 192 S.E. at p. 771. But it is likewise true that the discretion which may be exercised is not an arbitrary or capricious one, but one which is controlled by the established doctrines and settled principles of equity; and, generally, where a contract is in its nature and circumstances unobjectionable, it is as much a matter of course for courts of equity to decree a specific performance of it as it is for a court of law to give damages for a breach of it. *Bond v. Crawford*, 193 Va. 437, 444, 69 S.E.2d 470, 475.

[¶36] The complainants are entitled to have specific performance of the contracts sued on. The decree appealed from is therefore reversed and the cause is remanded for the entry of a proper decree requiring the defendants to perform the contract in accordance with the prayer of the bill.

Reversed and remanded.

Questions:

1. What reasonable person is at issue—a person in the position of offeree or a third person who might have been watching?

2. Does this decision respect Zehmer's autonomy? What countervailing policy is at issue? (The answer to this question is not in the case. Please speculate what policy might support it.)

3. We have been following this case's rule all semester with regard to whether a person was "induced" for purposes of consideration doctrine. It is what *Vian* meant by "purport to be," and it is something like what the earlier English courts meant by "intendment." A contract formed in this case. So, does contract formation require a "meeting of the minds"? Did the minds of Lucy and Zehmer meet? Has that ever been required in all your study? What would evidence of such a thing look like?

The phrase "meeting of the minds" came from spurious etymology, reported (perhaps invented?) by a lawyer named Pollard around 1550. In an argument before the Court of Exchequer Chamber, Pollard claimed that the word *agreement* was a contraction of two Latin words, *aggregatio* and *mentium*. *See* Val Ricks, *Assent Is Not an Element of Contract Formation*, 61 KAN. L. REV. 591, 610 n.108 (2013). Pollard was wrong. The word *agreement* was borrowed from French (not surprising as lawyers in English courts of the time argued in a pidgin called Law French that used English grammar and French words). It is a combination of *agree* and the suffix *-ment*, which makes a noun of the verb (like *attachment*, *establishment*, *payment*).

4. When does drunkenness amount to lack of capacity? Apparently being drunk does not stop one from forming a contract. But what if one was *really* intoxicated? *Dewitt v. Bowers*, 1138 S.W. 1147, 1149 (Tex. Civ. App. 1911), gave the following recitation of the rule:

> It is the rule of law that a person cannot escape liability on a contract on the mere ground that he was intoxicated at the time of its execution, unless it is proved that he was so intoxicated that he was unable to understand the nature of the contract and the consequences of its execution. He may be intoxicated to such a degree as to be excited, or so as to prevent him from acting with that degree of care that he would use were he sober, still he would not be released from his contractual liability. His contract cannot be avoided, in other words, unless his drunkenness was of such a character that he did not know its true intent or meaning, which is an amelioration of the early common-law rule that asserted that a contract entered into by an intoxicated person was binding upon him. As said by this court, through Justice Neill, in *Wells v. Houston*, 23 Tex. Civ. App. 629, 57 S.W. 584: "To avoid a contract on this ground, the obligor must have been so drunk as to have dethroned reason, memory, and judgment, and impaired his mental faculties to an extent that would render him non compos mentis for the time being, especially where there is no pretense that any person connected with the transaction aided in or procured the drunkenness." It has been held that a less degree of intoxication than that required to absolutely invalidate a contract may serve as a basis for avoiding the same if the drunkenness was caused by the other party, or if he takes unfair advantage of it. This would involve questions of fraud and undue influence, however, and not those of capacity to execute the contract.

Jacob F. KELLER v. Jacob HOLDERMAN

Supreme Court of Michigan (1863)

11 Mich. 248

Error to Berrien Circuit.

[¶1] Action by Holderman against Keller upon a check for $300, drawn by Keller upon a banker at Niles, and not honored. The case was tried without a jury, and the circuit judge found as facts, that the check was given for an old silver watch, worth about $15, which Keller took and kept until the day of trial, when he offered to return it to the plaintiff, who refused to receive it. The whole transaction was a frolic and a banter—the plaintiff not expecting to sell, nor the defendant intending to buy the watch at the sum for which the check was drawn. The defendant, when he drew the check had no money in the banker's hands, and he had intended to insert a condition in the check that would prevent his being liable on it; but as he failed to do so, and had retained the watch, the judge held him liable, and judgement was rendered against him for the amount of the check. * * * *

Martin, Ch. J.: Per Curiam

[¶2] When the court below found that as a fact that "the whole transaction between the parties was a frolic and a banter, the plaintiff not expecting to sell, nor the defendant intending to buy the watch for the

sum for which the check was drawn," the conclusion should have been that no contract was ever made by the parties, and the finding should have been that no cause of action existed upon the check to the plaintiff.

[¶3] The judgment below is reversed, with cost of this court and the court below.

Question: Suppose Lucy had told his brother the next day, "I think Zehmer was trying to bluff me last night, as a joke, but he signed the document, and now I have got him." Would that change the result in *Lucy v. Zehmer*?

RAFFLES v. WICHELHAUS

Court of the Exchequer (1864)

2 Hurl. & C. 906

[¶1] Declaration. For that it was agreed between the plaintiff and the defendants, to wit, at Liverpool, that the plaintiff should sell to the defendants, and the defendants buy of the plaintiff, certain goods, to wit, 125 bales of Surat cotton, guaranteed middling fair merchant's Dhollorah, to arrive ex "Peerless" from Bombay; and that the cotton should be taken from the quay, and that the defendants would pay the plaintiff for the same at a certain rate, to wit, at the rate of 17½d. per pound, within a certain time then agreed upon after the arrival of the said goods in England. Averments: that the said goods did arrive by the said ship from Bombay in England, to wit, at Liverpool, and the plaintiff was then and there ready, and willing and offered to deliver the said goods to the defendants, &c. Breach: that the defendants refused to accept the said goods or pay the plaintiff for them.

[¶2] Plea. That the said ship mentioned in the said agreement was meant and intended by the defendants to be the ship called the "Peerless," which sailed from Bombay, to wit, in October; and that the plaintiff was not ready and willing and did not offer to deliver to the defendants any bales of cotton which arrived by the last mentioned ship, but instead thereof was only ready and willing and offered to deliver to the defendants 125 bales of Surat cotton which arrived by another and different ship, which was also called the "Peerless," and which sailed from Bombay, to wit, in December.

[¶3] Demurrer, and joinder therein.

[¶4] Milward, in support of the demurrer. The contract was for the sale of a number of bales of cotton of a particular description, which the plaintiff was ready to deliver. It is immaterial by what ship the cotton was to arrive, so that it was a ship called the Peerless. The words "to arrive ex 'Peerless,'" only mean that if the vessel is lost on the voyage, the contract is to be at an end. [Pollock C.B. It would be a question for the jury whether both parties meant the same ship called the Peerless.] That would be so if the contract was for the sale of a ship called the Peerless; but it is for the sale of cotton on board a ship of that name. [Pollock C.B.

The defendant only bought that cotton which was to arrive by a particular ship. It may as well be said, that if there is a contract for the purchase of certain goods in warehouse A., that is satisfied by the delivery of goods of the same description in warehouse B.] In that case there would be goods in both warehouses; here it does not appear that the plaintiff had any goods on board the other "Peerless." [Martin, B. It is imposing on the defendant a contract different from that which he entered into. Pollock C.B. It is like a contract for the purchase of wine coming from a particular estate in France or Spain, where there are two estates of that name.] The defendant has no right to contradict by parol evidence a written contract good upon the face of it. He does not impute misrepresentation or fraud, but only says that he fancied the ship was a different one. Intention is of no avail, unless stated at the time of the contract. [Pollock C.B. One vessel sailed in October and the other in December.] The time of sailing is no part of the contract.

[¶5] Mellish (Cohen with him), in support of the plea. There is nothing on the face of the contract to shew that any particular ship called the "Peerless" was meant; but the moment it appears that two ships called the "Peerless" were about to sail from Bombay there is a latent ambiguity, and parol evidence may be given for the purpose of shewing that the defendant meant one "Peerless," and the plaintiff another. That being so, there was no consensus ad idem, and therefore no binding contract. He was then stopped by the Court.

[¶6] Per Curiam. Judgment for the defendants.

Questions:

1. *Raffles* is another notoriously difficult case. Milward, Mellish, and Cohen are all lawyers for the parties. Pollock and Martin are judges-barons of the Exchequer. Do the judges say in this report why they give judgment for the defendants?

2. Why does it matter which ship it was?

3. Would you ground this decision on lack of subjective intent?

4. Oliver Wendell Holmes wrote to Baron Pollock a couple of time, asking what *Raffles* was supposed to mean. Pollock did not clearly say. Later, Holmes argued that the two parties never agreed because their objective manifestations of intent were different: "[T]here is no contract because the parties used different words." What could Holmes have meant by that?

5. Did the parties exchange promise for consideration? Is there any evidence the judges were thinking of it that way?

6. The Restatement authors came up with a clever way to explain the Peerless case. They thought the result should follow the relative fault of the party for the misunderstanding. Here is how they said it in R2K:

> § 20. Effect of Misunderstanding

> (1) There is no manifestation of mutual assent to an exchange if the parties attach materially different meanings to their manifestations and
>
> > (a) neither party knows or has reason to know the meaning attached by the other; or
> >
> > (b) each party knows or each party has reason to know the meaning attached by the other.
>
> (2) The manifestations of the parties are operative in accordance with the meaning attached to them by one of the parties if
>
> > (a) that party does not know of any different meaning attached by the other, and the other knows the meaning attached by the first party; or
> >
> > (b) that party has no reason to know of any different meaning attached by the other, and the other has reason to know the meaning attached by the first party.

Under subsection (1), the parties are equally innocent or guilty. When that is true, no contract forms. Under subsection (2), one party is relatively less innocent than the other, and the less innocent party loses.

How would *Lucy*, *Keller*, and *Raffles* come out under § 20?

Chapter 7. Offers

Think back on *Lucy v. Zehmer* and *Payne v. Cave*. One of the two parties made an offer, and the other accepted. Which came first, offer or acceptance?

A person who makes an offer is called *offeror*. A person who receives an offer is called an *offeree*.

After reading this material, you should be begin to answer these questions: Why must the offer come before the acceptance? How are the two (though they are both manifestations of assent) legally different? What different legal effects does each have?

A. What Is an Offer?

Many contracts casebooks start out by teaching assent and saving consideration for a later chapter. These casebooks perhaps inadvertently teach that one can understand what an offer is without seeing its complete conceptual dependence on consideration.

Maybe the most accurate definition of offer is R2K Section 24: “An offer is the manifestation of willingness to enter into a bargain, so made as to justify another person [the offeree] in understanding that [the offeree’s] assent to that bargain is invited and will conclude it.” Consider those words very carefully. All of them matter!

Taking R2K § 24’s definition at its words, consider: Would you be able to recognize an offer if you did not know what a “bargain” is? What is it that must be assented to by the offer? How complete must the offer’s description of the bargain be, do you suppose? Usually, the offeror—the one who makes an offer—pitches the bargain. That means the offeror must name what the offeror is going to do but also what else? What does it mean to “conclude” a bargain? Or, in other words, what else must occur after an offer for a contract to form?

The following popular case on offers oddly never gives a definition of offer, uses *bargain* only when quoting the R2K, and otherwise never mentions exchange or consideration. Can you find at least hints of R2K § 24 in the opinion? Please also read this entertaining opinion for the applications of the rule, which are correct. Please be prepared to explain why the applications of offer law in the opinion are justified in terms of § 24—including, of course, the application of offer law to the facts of the case itself.

John D.R. LEONARD v. PEPSICO, INC.

United States District Court, S.D. New York (August 5, 1999)

88 F. Supp. 2d (S.D.N.Y.)

OPINION & ORDER

WOOD, J.

[¶1] Plaintiff brought this action seeking, among other things, specific performance of an alleged offer of a Harrier Jet, featured in a television advertisement for defendant's "Pepsi Stuff" promotion. Defendant has moved for summary judgment pursuant to Federal Rule of Civil Procedure 56. For the reasons stated below, defendant's motion is granted.

I. Background

[¶2] This case arises out of a promotional campaign conducted by defendant, the producer and distributor of the soft drinks Pepsi and Diet Pepsi. (See PepsiCo Inc.'s Rule 56.1 Statement [of Uncontested Facts] ("Def. Stat .") ¶ 2.) The promotion, entitled "Pepsi Stuff," encouraged consumers to collect "Pepsi Points" from specially marked packages of Pepsi or Diet Pepsi and redeem these points for merchandise featuring the Pepsi logo. (*See id*. ¶¶ 4, 8.) Before introducing the promotion nationally, defendant conducted a test of the promotion in the Pacific Northwest from October 1995 to March 1996. (*See id*. ¶¶ 5-6.) A Pepsi Stuff catalog was distributed to consumers in the test market, including Washington State. (*See id*. ¶ 7.) Plaintiff is a resident of Seattle, Washington. (*See id*. ¶ 3.) While living in Seattle, plaintiff saw the Pepsi Stuff commercial (*see id*. ¶ 22) that he contends constituted an offer of a Harrier Jet.

A. The Alleged Offer

[¶3] Because whether the television commercial constituted an offer is the central question in this case, the Court will describe the commercial in detail. The commercial opens upon an idyllic, suburban morning, where the chirping of birds in sun-dappled trees welcomes a paperboy on his morning route. As the newspaper hits the stoop of a conventional two-story house, the tattoo of a military drum introduces the subtitle, "MONDAY 7:58 AM." The stirring strains of a martial air mark the appearance of a well-coiffed teenager preparing to leave for school, dressed in a shirt emblazoned with the Pepsi logo, a red-white-and-blue ball. While the teenager confidently preens, the military drumroll again sounds as the subtitle "T-SHIRT 75 PEPSI POINTS" scrolls across the screen. Bursting from his room, the teenager strides down the hallway wearing a leather jacket. The drumroll sounds again, as the subtitle "LEATHER JACKET 1450 PEPSI POINTS" appears. The teenager opens the door of his house and, unfazed by the glare of the early morning sunshine, puts on a pair of sunglasses. The drumroll then accompanies the subtitle "SHADES 175 PEPSI POINTS." A voiceover then intones, "Introducing the new Pepsi Stuff catalog," as the camera focuses on the cover of the catalog. (See Defendant's Local Rule 56.1 Stat., Exh. A (the "Catalog").)†††††

[¶4] The scene then shifts to three young boys sitting in front of a high school building. The boy in the middle is intent on his Pepsi Stuff Catalog, while the boys on either side are each drinking Pepsi. The three boys gaze in awe at an object rushing overhead, as the military march builds to a crescendo. The Harrier Jet is not yet visible, but the observer senses the presence of a mighty plane as the extreme winds generated by its flight create a paper maelstrom in a classroom devoted to an otherwise dull physics lesson. Finally, the Harrier Jet swings into view and lands by the side of the school building, next to a bicycle rack.

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††††† [2] At this point, the following message appears at the bottom of the screen: "Offer not available in all areas. See details on specially marked packages."

Several students run for cover, and the velocity of the wind strips one hapless faculty member down to his underwear. While the faculty member is being deprived of his dignity, the voiceover announces: “Now the more Pepsi you drink, the more great stuff you’re gonna get.”

[¶5] The teenager opens the cockpit of the fighter and can be seen, helmetless, holding a Pepsi. “[L]ooking very pleased with himself,” (Pl. Mem. at 3,) the teenager exclaims, “Sure beats the bus,” and chortles. The military drumroll sounds a final time, as the following words appear: “HARRIER FIGHTER 7,000,000 PEPSI POINTS .” A few seconds later, the following appears in more stylized script: “Drink Pepsi—Get Stuff.” With that message, the music and the commercial end with a triumphant flourish.

[¶6] Inspired by this commercial, plaintiff set out to obtain a Harrier Jet. Plaintiff explains that he is “typical of the ‘Pepsi Generation’ ... he is young, has an adventurous spirit, and the notion of obtaining a Harrier Jet appealed to him enormously.” (Pl. Mem. at 3.) Plaintiff consulted the Pepsi Stuff Catalog. The Catalog features youths dressed in Pepsi Stuff regalia or enjoying Pepsi Stuff accessories, such as “Blue Shades” (“As if you need another reason to look forward to sunny days.”), “Pepsi Tees” (“Live in ‘em. Laugh in ‘em. Get in ‘em.”), “Bag of Balls” (“Three balls. One bag. No rules.”), and “Pepsi Phone Card” (“Call your mom!”). The Catalog specifies the number of Pepsi Points required to obtain promotional merchandise. (See Catalog, at rear foldout pages.) The Catalog includes an Order Form which lists, on one side, fifty-three items of Pepsi Stuff merchandise redeemable for Pepsi Points (*see id*. (the “Order Form”)). Conspicuously absent from the Order Form is any entry or description of a Harrier Jet. (*See id*.) The amount of Pepsi Points required to obtain the listed merchandise ranges from 15 (for a “Jacket Tattoo” (“Sew ‘em on your jacket, not your arm.”)) to 3300 (for a “Fila Mountain Bike” (“Rugged. All-terrain. Exclusively for Pepsi.”)). It should be noted that plaintiff objects to the implication that because an item was not shown in the Catalog, it was unavailable. (*See* Pl. Stat. ¶¶ 23-26, 29.

[¶7] The rear foldout pages of the Catalog contain directions for redeeming Pepsi Points for merchandise. (See Catalog, at rear foldout pages.) These directions note that merchandise may be ordered “only” with the original Order Form. (*See id*.) The Catalog notes that in the event that a consumer lacks enough Pepsi Points to obtain a desired item, additional Pepsi Points may be purchased for ten cents each; however, at least fifteen original Pepsi Points must accompany each order. (*See id*.)

[¶8] Although plaintiff initially set out to collect 7,000,000 Pepsi Points by consuming Pepsi products, it soon became clear to him that he “would not be able to buy (let alone drink) enough Pepsi to collect the necessary Pepsi Points fast enough.” (Affidavit of John D.R. Leonard, Mar. 30, 1999 (“Leonard Aff.”), ¶ 5.) Reevaluating his strategy, plaintiff “focused for the first time on the packaging materials in the Pepsi Stuff promotion,” (id.,) and realized that buying Pepsi Points would be a more promising option. (*See id*.) Through acquaintances, plaintiff ultimately raised about $700,000. (*See id*. ¶ 6.)

B. Plaintiff’s Efforts to Redeem the Alleged Offer

[¶9] On or about March 27, 1996, plaintiff submitted an Order Form, fifteen original Pepsi Points, and a check for $700,008.50. (*See* Def. Stat. ¶ 36.) Plaintiff appears to have been represented by counsel at the time he mailed his check; the check is drawn on an account of plaintiff’s first set of attorneys. (*See* Defendant’s Notice of Motion, Exh. B (first).) At the bottom of the Order Form, plaintiff wrote in “1 Harrier Jet” in the “Item” column and “7,000,000” in the “Total Points” column. (*See id*.) In a letter accompanying his submission, plaintiff stated that the check was to purchase additional Pepsi Points “expressly for

obtaining a new Harrier jet as advertised in your Pepsi Stuff commercial." (*See* Declaration of David Wynn, Mar. 18, 1999 ("Wynn Dec."), Exh. A.)

[¶10] On or about May 7, 1996, defendant's fulfillment house rejected plaintiff's submission and returned the check, explaining that:

> The item that you have requested is not part of the Pepsi Stuff collection.
>
> It is not included in the catalogue or on the order form, and only catalogue merchandise can be redeemed under this program. The Harrier jet in the Pepsi commercial is fanciful and is simply included to create a humorous and entertaining ad. We apologize for any misunderstanding or confusion that you may have experienced and are enclosing some free product coupons for your use.

(Wynn Aff. Exh. B (second).) Plaintiff's previous counsel responded on or about May 14, 1996, as follows:

> Your letter of May 7, 1996 is totally unacceptable. We have reviewed the video tape of the Pepsi Stuff commercial ... and it clearly offers the new Harrier jet for 7,000,000 Pepsi Points. Our client followed your rules explicitly.... This is a formal demand that you honor your commitment and make immediate arrangements to transfer the new Harrier jet to our client. If we do not receive transfer instructions within ten (10) business days of the date of this letter you will leave us no choice but to file an appropriate action against Pepsi....

(Wynn Aff., Exh. C.) This letter was apparently sent onward to the advertising company responsible for the actual commercial, BBDO New York ("BBDO"). In a letter dated May 30, 1996, BBDO Vice President Raymond E. McGovern, Jr., explained to plaintiff that:

> I find it hard to believe that you are of the opinion that the Pepsi Stuff commercial ("Commercial") really offers a new Harrier Jet. The use of the Jet was clearly a joke that was meant to make the Commercial more humorous and entertaining. In my opinion, no reasonable person would agree with your analysis of the Commercial.

(Wynn Aff. Exh. A.) On or about June 17, 1996, plaintiff mailed a similar demand letter to defendant. (See Wynn Aff., Exh. D.)

[¶11] Litigation of this case initially involved two lawsuits, the first a declaratory judgment action brought by PepsiCo in this district (the "declaratory judgment action"), and the second an action brought by Leonard in Florida state court (the "Florida action"). PepsiCo brought suit in this Court on July 18, 1996, seeking a declaratory judgment stating that it had no obligation to furnish plaintiff with a Harrier Jet. That case was filed under docket number 96 Civ. 5320. In response to PepsiCo's suit in New York, Leonard brought suit in Florida state court on August 6, 1996, although this case had nothing to do with Florida. That suit was removed to the Southern District of Florida in September 1996. In an Order dated November 6, 1996, United States District Judge James Lawrence King found that, "Obviously this case has been filed in a forum that has no meaningful relationship to the controversy and warrants a transfer pursuant to 28 U.S.C. § 1404(a)." *Leonard v. PepsiCo*, 96-2555 Civ.-King, at 1 (S.D.Fla. Nov. 6, 1996). The Florida suit was transferred to this Court on December 2, 1996, and assigned the docket number 96 Civ. 9069.

[¶12] Once the Florida action had been transferred, Leonard moved to dismiss the declaratory judgment action for lack of personal jurisdiction. In an Order dated November 24, 1997, the Court granted the motion to dismiss for lack of personal jurisdiction in case 96 Civ. 5320, from which PepsiCo appealed. Leonard also moved to voluntarily dismiss the Florida action. While the Court indicated that the motion was proper, it noted that PepsiCo was entitled to some compensation for the costs of litigating this case in Florida, a forum that had no meaningful relationship to the case. (See Transcript of Proceedings Before Hon. Kimba M. Wood, Dec. 9, 1997, at 3.) In an Order dated December 15, 1997, the Court granted Leonard's motion to voluntarily dismiss this case without prejudice, but did so on condition that Leonard pay certain attorneys' fees.

[¶13] In an Order dated October 1, 1998, the Court ordered Leonard to pay $88,162 in attorneys' fees within thirty days. Leonard failed to do so, yet sought nonetheless to appeal from his voluntary dismissal and the imposition of fees. In an Order dated January 5, 1999, the Court noted that Leonard's strategy was " 'clearly an end-run around the final judgment rule." ' (Order at 2 (quoting *Palmieri v. DeFaria*, 88 F.3d 136 (2d Cir. 1996)).) Accordingly, the Court ordered Leonard either to pay the amount due or withdraw his voluntary dismissal, as well as his appeals therefrom, and continue litigation before this Court. (See Order at 3.) Rather than pay the attorneys' fees, Leonard elected to proceed with litigation, and shortly thereafter retained present counsel.

[¶14] On February 22, 1999, the Second Circuit endorsed the parties' stipulations to the dismissal of any appeals taken thus far in this case. Those stipulations noted that Leonard had consented to the jurisdiction of this Court and that PepsiCo agreed not to seek enforcement of the attorneys' fees award. With these issues having been waived, PepsiCo moved for summary judgment pursuant to Federal Rule of Civil Procedure 56. The present motion thus follows three years of jurisdictional and procedural wrangling.

II. Discussion

A. The Legal Framework

1. Standard for Summary Judgment

[¶15] On a motion for summary judgment, a court "cannot try issues of fact; it can only determine whether there are issues to be tried." *Donahue v. Windsor Locks Bd. of Fire Comm'rs*, 834 F.2d 54, 58 (2d Cir. 1987) (citations and internal quotation marks omitted). * * * *

2. Choice of Law

[¶16] * * * * The Court agrees with both parties that resolution of this issue requires consideration of principles of contract law that are not limited to the law of any one state. Most of the cases cited by the parties are not from New York courts. As plaintiff suggests, the questions presented by this case implicate questions of contract law "deeply ingrained in the common law of England and the States of the Union." (Pl. Mem. at 8.)

B. Defendant's Advertisement Was Not An Offer

1. Advertisements as Offers

[¶17] The general rule is that an advertisement does not constitute an offer. The Restatement (Second) of Contracts explains that:

> Advertisements of goods by display, sign, handbill, newspaper, radio or television are not ordinarily intended or understood as offers to sell. The same is true of catalogues, price lists and circulars, even though the terms of suggested bargains may be stated in some detail. It is of course possible to make an offer by an advertisement directed to the general public (see § 29), but there must ordinarily be some language of commitment or some invitation to take action without further communication.

Restatement (Second) of Contracts § 26 cmt. b (1979). Similarly, a leading treatise notes that:

> It is quite possible to make a definite and operative offer to buy or sell goods by advertisement, in a newspaper, by a handbill, a catalog or circular or on a placard in a store window. It is not customary to do this, however; and the presumption is the other way. ... Such advertisements are understood to be mere requests to consider and examine and negotiate; and no one can reasonably regard them as otherwise unless the circumstances are exceptional and the words used are very plain and clear.

1 Arthur Linton Corbin & Joseph M. Perillo, Corbin on Contracts § 2.4, at 116- 17 (rev. ed.1993) (emphasis added); see also 1 E. Allan Farnsworth, Farnsworth on Contracts § 3.10, at 239 (2d ed.1998); 1 Samuel Williston & Richard A. Lord, A Treatise on the Law of Contracts § 4:7, at 286-87 (4th ed.1990). New York courts adhere to this general principle. *See Lovett v. Frederick Loeser & Co*., 124 Misc. 81, 207 N.Y.S. 753, 755 (Mun. Ct. N.Y. City 1924) (noting that an "advertisement is nothing but an invitation to enter into negotiations, and is not an offer which may be turned into a contract by a person who signifies his intention to purchase some of the articles mentioned in the advertisement"); *see also Geismar v. Abraham & Strauss*, 109 Misc.2d 495, 439 N.Y.S.2d 1005, 1006 (Dist. Ct. Suffolk Cty. 1981) (reiterating *Lovett* rule); *People v. Gimbel Bros. Inc.*, 202 Misc. 229, 115 N.Y.S.2d 857, 858 (Ct. Spec. Sess. 1952) (because an "[a]dvertisement does not constitute an offer of sale but is solely an invitation to customers to make an offer to purchase," defendant not guilty of selling property on Sunday).

[¶18] An advertisement is not transformed into an enforceable offer merely by a potential offeree's expression of willingness to accept the offer through, among other means, completion of an order form. In *Mesaros v. United States*, 845 F.2d 1576 (Fed. Cir. 1988), for example, the plaintiffs sued the United States Mint for failure to deliver a number of Statue of Liberty commemorative coins that they had ordered. When demand for the coins proved unexpectedly robust, a number of individuals who had sent in their orders in a timely fashion were left empty-handed. *See id*. at 1578-80. The court began by noting the "well-established" rule that advertisements and order forms are "mere notices and solicitations for offers which create no power of acceptance in the recipient." *Id*. at 1580; *see also Foremost Pro Color, Inc. v. Eastman Kodak Co.*, 703 F.2d 534, 538-39 (9th Cir. 1983) ("The weight of authority is that purchase orders such as those at issue here are not enforceable contracts until they are accepted by the seller."); Restatement (Second) of Contracts § 26 ("A manifestation of willingness to enter a bargain is not an offer if the person to whom it is addressed knows or has reason to know that the person making it does not intend to conclude a bargain until he has made a further manifestation of assent."). The spurned coin collectors could not maintain a breach of contract action because no contract would be formed until the advertiser accepted the order form and processed payment. *See id*. at 1581; *see also Alligood v. Procter & Gamble*, 594 N.E.2d 668 (Ohio Ct. App. 1991) (finding that no offer was made in promotional campaign for baby diapers, in

which consumers were to redeem teddy bear proof-of-purchase symbols for catalog merchandise); *Chang v. First Colonial Savings Bank*, 410 S.E.2d 928 (Va. 1991) (newspaper advertisement for bank settled the terms of the offer once bank accepted plaintiffs' deposit, notwithstanding bank's subsequent effort to amend the terms of the offer). Under these principles, plaintiff's letter of March 27, 1996, with the Order Form and the appropriate number of Pepsi Points, constituted the offer. There would be no enforceable contract until defendant accepted the Order Form and cashed the check.

[¶19] The exception to the rule that advertisements do not create any power of acceptance in potential offerees is where the advertisement is "clear, definite, and explicit, and leaves nothing open for negotiation," in that circumstance, "it constitutes an offer, acceptance of which will complete the contract." *Lefkowitz v. Great Minneapolis Surplus Store*, 86 N.W.2d 689, 691 (Minn. 1957). In Lefkowitz, defendant had published a newspaper announcement stating: "Saturday 9 AM Sharp, 3 Brand New Fur Coats, Worth to $100 .00, First Come First Served $1 Each." *Id*. at 690. Mr. Morris Lefkowitz arrived at the store, dollar in hand, but was informed that under defendant's "house rules," the offer was open to ladies, but not gentlemen. *See id*. The court ruled that because plaintiff had fulfilled all of the terms of the advertisement and the advertisement was specific and left nothing open for negotiation, a contract had been formed. *See id*.; *see also Johnson v. Capital City Ford Co*., 85 So.2d 75, 79 (La. Ct. App. 1955) (finding that newspaper advertisement was sufficiently certain and definite to constitute an offer).

[¶20] The present case is distinguishable from *Lefkowitz*. First, the commercial cannot be regarded in itself as sufficiently definite, because it specifically reserved the details of the offer to a separate writing, the Catalog.[‡‡‡‡‡] The commercial itself made no mention of the steps a potential offeree would be required to take to accept the alleged offer of a Harrier Jet. The advertisement in *Lefkowitz*, in contrast, "identified the person who could accept." Corbin, *supra*, § 2.4, at 119. *See generally United States v. Braunstein*, 75 F. Supp. 137, 139 (S.D.N.Y. 1947) ("Greater precision of expression may be required, and less help from the court given, when the parties are merely at the threshold of a contract."); Farnsworth, *supra*, at 239 ("The fact that a proposal is very detailed suggests that it is an offer, while omission of many terms suggests that it is not.").[§§§§§] Second, even if the Catalog had included a Harrier Jet among the items that could be obtained by redemption of Pepsi Points, the advertisement of a Harrier Jet by both television commercial and catalog would still not constitute an offer. As the *Mesaros* court explained, the absence of any words of limitation such as "first come, first served," renders the alleged offer sufficiently indefinite that no contract could be formed. *See Mesaros*, 845 F.2d at 1581. "A customer would not usually have reason to believe that the shopkeeper intended exposure to the risk of a multitude of acceptances resulting in a number of

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‡‡‡‡‡ [6] It also communicated additional words of reservation: "Offer not available in all areas. See details on specially marked packages."

§§§§§ [7] The reservation of the details of the offer in this case distinguishes it from Payne v. Lautz Bros. & Co., 166 N.Y.S. 844 (City Ct. Buffalo 1916). In Payne, a stamp and coupon broker purchased massive quantities of coupons produced by defendant, a soap company, and tried to redeem them for 4,000 round-trip tickets to a local beach. The court ruled for plaintiff, noting that the advertisements were "absolutely unrestricted. It contained no reference whatever to any of its previous advertising of any form." Id. at 848. In the present case, by contrast, the commercial explicitly reserved the details of the offer to the Catalog.

contracts exceeding the shopkeeper's inventory." Farnsworth, *supra*, at 242. There was no such danger in Lefkowitz, owing to the limitation "first come, first served."

[¶21] The Court finds, in sum, that the Harrier Jet commercial was merely an advertisement. The Court now turns to the line of cases upon which plaintiff rests much of his argument.

2. Rewards as Offers

[¶22] In opposing the present motion, plaintiff largely relies on a different species of unilateral offer, involving public offers of a reward for performance of a specified act. Because these cases generally involve public declarations regarding the efficacy or trustworthiness of specific products, one court has aptly characterized these authorities as "prove me wrong" cases. *See Rosenthal v. Al Packer Ford*, 374 A.2d 377, 380 (Md. Ct. Spec. App. 1977). The most venerable of these precedents is the case of *Carlill v. Carbolic Smoke Ball Co*., 1 Q.B. 256 (Court of Appeal, 1892), a quote from which heads plaintiff's memorandum of law: "[I]f a person chooses to make extravagant promises ... he probably does so because it pays him to make them, and, if he has made them, the extravagance of the promises is no reason in law why he should not be bound by them." Carbolic Smoke Ball, 1 Q.B. at 268 (Bowen, L.J.).

[¶23] Long a staple of law school curricula, Carbolic Smoke Ball owes its fame not merely to "the comic and slightly mysterious object involved," A.W. Brian Simpson, Quackery and Contract Law: *Carlill v. Carbolic Smoke Ball Company* (1893), in Leading Cases in the Common Law 259, 281 (1995), but also to its role in developing the law of unilateral offers. The case arose during the London influenza epidemic of the 1890s. Among other advertisements of the time, for Clarke's World Famous Blood Mixture, Towle's Pennyroyal and Steel Pills for Females, Sequah's Prairie Flower, and Epp's Glycerine Jube-Jubes, *see Simpson*, *supra*, at 267, appeared solicitations for the Carbolic Smoke Ball. The specific advertisement that Mrs. Carlill saw, and relied upon, read as follows:

> 100£ reward will be paid by the Carbolic Smoke Ball Company to any person who contracts the increasing epidemic influenza, colds, or any diseases caused by taking cold, after having used the ball three times daily for two weeks according to the printed directions supplied with each ball. 1000£ is deposited with the Alliance Bank, Regent Street, shewing our sincerity in the matter.
>
> During the last epidemic of influenza many thousand carbolic smoke balls were sold as preventives against this disease, and in no ascertained case was the disease contracted by those using the carbolic smoke ball.

Carbolic Smoke Ball, 1 Q.B. at 256-57. "On the faith of this advertisement," *id.* at 257, Mrs. Carlill purchased the smoke ball and used it as directed, but contracted influenza nevertheless.[*****] The lower court held that she was entitled to recover the promised reward.

[*****] [8] Although the Court of Appeals's opinion is silent as to exactly what a carbolic smoke ball was, the historical record reveals it to have been a compressible hollow ball, about the size of an apple or orange, with a small opening covered by some porous material such as silk or gauze. The ball was partially filled with carbolic acid in powder form. When the ball was squeezed, the powder would be forced through the

[¶24] Affirming the lower court's decision, Lord Justice Lindley began by noting that the advertisement was an express promise to pay £100 in the event that a consumer of the Carbolic Smoke Ball was stricken with influenza. *See id*. at 261. The advertisement was construed as offering a reward because it sought to induce performance, unlike an invitation to negotiate, which seeks a reciprocal promise. As Lord Justice Lindley explained, "advertisements offering rewards ... are offers to anybody who performs the conditions named in the advertisement, and anybody who does perform the condition accepts the offer." *Id.* at 262; *see also id.* at 268 (Bowen, L.J.). Because Mrs. Carlill had complied with the terms of the offer, yet contracted influenza, she was entitled to £100.

[¶25] Like *Carbolic Smoke Ball*, the decisions relied upon by plaintiff involve offers of reward. In *Barnes v. Treece*, 549 P.2d 1152 (Wash.Ct.App.1976), for example, the vice-president of a punchboard distributor, in the course of hearings before the Washington State Gambling Commission, asserted that, " 'I'll put a hundred thousand dollars to anyone to find a crooked board. If they find it, I'll pay it." ' *Id*. at 1154. Plaintiff, a former bartender, heard of the offer and located two crooked punchboards. Defendant, after reiterating that the offer was serious, providing plaintiff with a receipt for the punchboard on company stationery, and assuring plaintiff that the reward was being held in escrow, nevertheless repudiated the offer. *See id*. at 1154. The court ruled that the offer was valid and that plaintiff was entitled to his reward. *See id*. at 1155. The plaintiff in this case also cites cases involving prizes for skill (or luck) in the game of golf. *See Las Vegas Hacienda v. Gibson*, 359 P.2d 85 (Nev.1961) (awarding $5,000 to plaintiff, who successfully shot a hole-in-one); *see also Grove v. Charbonneau Buick-Pontiac, Inc.*, 240 N.W.2d 853 (N.D.1976) (awarding automobile to plaintiff, who successfully shot a hole-in-one).

[¶26] Other "reward" cases underscore the distinction between typical advertisements, in which the alleged offer is merely an invitation to negotiate for purchase of commercial goods, and promises of reward, in which the alleged offer is intended to induce a potential offeree to perform a specific action, often for noncommercial reasons. In *Newman v. Schiff*, 778 F.2d 460 (5th Cir. 1985), for example, the Fifth Circuit held that a tax protestor's assertion that, "If anybody calls this show ... and cites any section of the code that says an individual is required to file a tax return, I'll pay them $100,000," would have been an enforceable offer had the plaintiff called the television show to claim the reward while the tax protestor was appearing. *See id*. at 466-67. The court noted that, like Carbolic Smoke Ball, the case "concerns a special type of offer: an offer for a reward." *Id*. at 465. *James v. Turilli*, 473 S.W.2d 757 (Mo. Ct. App. 1971), arose from a boast by defendant that the "notorious Missouri desperado" Jesse James had not been killed in 1882, as portrayed in song and legend, but had lived under the alias "J. Frank Dalton" at the "Jesse James Museum" operated by none other than defendant. Defendant offered $10,000 "to anyone who could prove me wrong." *See id*. at 758-59. The widow of the outlaw's son demonstrated, at trial, that the outlaw had in fact been killed in 1882. On appeal, the court held that defendant should be liable to pay the amount offered. *See id*. at 762; *see also Mears v. Nationwide Mutual Ins. Co.*, 91 F.3d 1118, 1122-23 (8th Cir. 1996) (plaintiff entitled to cost of two Mercedes as reward for coining slogan for insurance company).

[¶27] In the present case, the Harrier Jet commercial did not direct that anyone who appeared at Pepsi headquarters with 7,000,000 Pepsi Points on the Fourth of July would receive a Harrier Jet. Instead, the commercial urged consumers to accumulate Pepsi Points and to refer to the Catalog to determine how they

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opening as a small cloud of smoke. See Simpson, *supra*, at 262-63. At the time, carbolic acid was considered fatal if consumed in more than small amounts. *See id.* at 264.

could redeem their Pepsi Points. The commercial sought a reciprocal promise, expressed through acceptance of, and compliance with, the terms of the Order Form. As noted previously, the Catalog contains no mention of the Harrier Jet. Plaintiff states that he "noted that the Harrier Jet was not among the items described in the catalog, but this did not affect [his] understanding of the offer." (Pl. Mem. at 4.) It should have.††††††

[¶28] Carbolic Smoke Ball itself draws a distinction between the offer of reward in that case, and typical advertisements, which are merely offers to negotiate. As Lord Justice Bowen explains:

> It is an offer to become liable to any one who, before it is retracted, performs the condition.... It is not like cases in which you offer to negotiate, or you issue advertisements that you have got a stock of books to sell, or houses to let, in which case there is no offer to be bound by any contract. Such advertisements are offers to negotiate—offers to receive offers—offers to chaffer, as, I think, some learned judge in one of the cases has said.

Carbolic Smoke Ball, 1 Q.B. at 268; see also Lovett, 207 N.Y.S. at 756 (distinguishing advertisements, as invitation to offer, from offers of reward made in advertisements, such as Carbolic Smoke Ball). Because the alleged offer in this case was, at most, an advertisement to receive offers rather than an offer of reward, plaintiff cannot show that there was an offer made in the circumstances of this case.

C. An Objective, Reasonable Person Would Not Have Considered the Commercial an Offer

[¶29] Plaintiff's understanding of the commercial as an offer must also be rejected because the Court finds that no objective person could reasonably have concluded that the commercial actually offered consumers a Harrier Jet.

1. Objective Reasonable Person Standard

[¶30] In evaluating the commercial, the Court must not consider defendant's subjective intent in making the commercial, or plaintiff's subjective view of what the commercial offered, but what an objective, reasonable person would have understood the commercial to convey. *See Kay-R Elec. Corp. v. Stone & Weber Constr. Co.*, 23 F.3d 55, 57 (2d Cir. 1994) ("[W]e are not concerned with what was going through the heads of the parties at the time [of the alleged contract]. Rather, we are talking about the objective principles of contract law."); *Mesaros*, 845 F.2d at 1581 ("A basic rule of contracts holds that whether an offer has been made depends on the objective reasonableness of the alleged offeree's belief that the advertisement or solicitation was intended as an offer."); Farnsworth, *supra*, § 3.10, at 237; Williston, *supra*, § 4:7 at 296-97.

[¶31] If it is clear that an offer was not serious, then no offer has been made:

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†††††† [10] In his affidavit, plaintiff places great emphasis on a press release written by defendant, which characterizes the Harrier Jet as "the ultimate Pepsi Stuff award." (See Leonard Aff. ¶ 13.) Plaintiff simply ignores the remainder of the release, which makes no mention of the Harrier Jet even as it sets forth in detail the number of points needed to redeem other merchandise.

> What kind of act creates a power of acceptance and is therefore an offer? It must be an expression of will or intention. It must be an act that leads the offeree reasonably to conclude that a power to create a contract is conferred. This applies to the content of the power as well as to the fact of its existence. It is on this ground that we must exclude invitations to deal or acts of mere preliminary negotiation, and acts evidently done in jest or without intent to create legal relations.

Corbin on Contracts, § 1.11 at 30 (emphasis added). An obvious joke, of course, would not give rise to a contract. *See*, *e.g.*, *Graves v. Northern N.Y. Pub. Co.*, 260 A.D. 900, 22 N.Y.S.2d 537 (App. Div. 4th Dept. 1940) (dismissing claim to offer of $1000, which appeared in the "joke column" of the newspaper, to any person who could provide a commonly available phone number). On the other hand, if there is no indication that the offer is "evidently in jest," and that an objective, reasonable person would find that the offer was serious, then there may be a valid offer. *See Barnes*, 549 P.2d at 1155 ("[I]f the jest is not apparent and a reasonable hearer would believe that an offer was being made, then the speaker risks the formation of a contract which was not intended."); *see also Lucy v. Zehmer*, 84 S.E.2d 516, 518, 520 (Va. 1954) (ordering specific performance of a contract to purchase a farm despite defendant's protestation that the transaction was done in jest as "'just a bunch of two doggoned drunks bluffing'").

2. Necessity of a Jury Determination

[¶32] Plaintiff also contends that summary judgment is improper because the question of whether the commercial conveyed a sincere offer can be answered only by a jury. Relying on dictum from *Gallagher v. Delaney*, 139 F.3d 338 (2d Cir. 1998), plaintiff argues that a federal judge comes from a "narrow segment of the enormously broad American socio-economic spectrum," *id*. at 342, and, thus, that the question whether the commercial constituted a serious offer must be decided by a jury composed of, inter alia, members of the "Pepsi Generation," who are, as plaintiff puts it, "young, open to adventure, willing to do the unconventional." (*See* Leonard Aff. ¶ 2.) Plaintiff essentially argues that a federal judge would view his claim differently than fellow members of the "Pepsi Generation."

[¶33] Plaintiff's argument that his claim must be put to a jury is without merit. *Gallagher* involved a claim of sexual harassment in which the defendant allegedly invited plaintiff to sit on his lap, gave her inappropriate Valentine's Day gifts, told her that "she brought out feelings that he had not had since he was sixteen," and "invited her to help him feed the ducks in the pond, since he was 'a bachelor for the evening." *Gallagher*, 139 F.3d at 344. The court concluded that a jury determination was particularly appropriate because a federal judge lacked "the current real-life experience required in interpreting subtle sexual dynamics of the workplace based on nuances, subtle perceptions, and implicit communications." *Id.* at 342. This case, in contrast, presents a question of whether there was an offer to enter into a contract, requiring the Court to determine how a reasonable, objective person would have understood defendant's commercial. Such an inquiry is commonly performed by courts on a motion for summary judgment. *See Krumme*, 143 F.3d at 83; *Bourque*, 42 F.3d at 708; *Wards Co.*, 761 F.2d at 120.

3. Whether the Commercial Was "Evidently Done In Jest"

[¶34] Plaintiff's insistence that the commercial appears to be a serious offer requires the Court to explain why the commercial is funny. Explaining why a joke is funny is a daunting task; as the essayist E.B. White

has remarked, “Humor can be dissected, as a frog can, but the thing dies in the process....”‡‡‡‡‡‡ The commercial is the embodiment of what defendant appropriately characterizes as “zany humor.” (Def. Mem. at 18.)

[¶35] First, the commercial suggests, as commercials often do, that use of the advertised product will transform what, for most youth, can be a fairly routine and ordinary experience. The military tattoo and stirring martial music, as well as the use of subtitles in a Courier font that scroll terse messages across the screen, such as “MONDAY 7:58 AM,” evoke military and espionage thrillers. The implication of the commercial is that Pepsi Stuff merchandise will inject drama and moment into hitherto unexceptional lives. The commercial in this case thus makes the exaggerated claims similar to those of many television advertisements: that by consuming the featured clothing, car, beer, or potato chips, one will become attractive, stylish, desirable, and admired by all. A reasonable viewer would understand such advertisements as mere puffery, not as statements of fact, *see*, *e.g.*, *Hubbard v. General Motors Corp*., 95 Civ. 4362(AGS), 1996 WL 274018, at *6 (S.D.N.Y. May 22, 1996) (advertisement describing automobile as “Like a Rock,” was mere puffery, not a warranty of quality); *Lovett*, 207 N.Y.S. at 756; and refrain from interpreting the promises of the commercial as being literally true.

[¶36] Second, the callow youth featured in the commercial is a highly improbable pilot, one who could barely be trusted with the keys to his parents’ car, much less the prize aircraft of the United States Marine Corps. Rather than checking the fuel gauges on his aircraft, the teenager spends his precious preflight minutes preening. The youth’s concern for his coiffure appears to extend to his flying without a helmet. Finally, the teenager’s comment that flying a Harrier Jet to school “sure beats the bus” evinces an improbably insouciant attitude toward the relative difficulty and danger of piloting a fighter plane in a residential area, as opposed to taking public transportation.§§§§§§

[¶37] Third, the notion of traveling to school in a Harrier Jet is an exaggerated adolescent fantasy. In this commercial, the fantasy is underscored by how the teenager’s schoolmates gape in admiration, ignoring their physics lesson. The force of the wind generated by the Harrier Jet blows off one teacher’s clothes, literally defrocking an authority figure. As if to emphasize the fantastic quality of having a Harrier Jet arrive at school, the Jet lands next to a plebeian bike rack. This fantasy is, of course, extremely unrealistic. No school would provide landing space for a student’s fighter jet, or condone the disruption the jet’s use would cause.

[¶38] Fourth, the primary mission of a Harrier Jet, according to the United States Marine Corps, is to “attack and destroy surface targets under day and night visual conditions.” United States Marine Corps, Factfile: AV-8B Harrier II (last modified Dec. 5, 1995) <http://www.hqmc.usmc.mil/factfile.nsf>. Manufactured by McDonnell Douglas, the Harrier Jet played a significant role in the air offensive of Operation Desert Storm in 1991. *See id*. The jet is designed to carry a considerable armament load,

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‡‡‡‡‡‡ [11] Quoted in Gerald R. Ford, Humor and the Presidency 23 (1987).

§§§§§§ [12] In this respect, the teenager of the advertisement contrasts with the distinguished figures who testified to the effectiveness of the Carbolic Smoke Ball, including the Duchess of Sutherland; the Earls of Wharncliffe, Westmoreland, Cadogan, and Leitrim; the Countesses Dudley, Pembroke, and Aberdeen; the Marchionesses of Bath and Conyngham; Sir Henry Acland, the physician to the Prince of Wales; and Sir James Paget, sergeant surgeon to Queen Victoria. See Simpson, *supra*, at 265.

including Sidewinder and Maverick missiles. *See id*. As one news report has noted, "Fully loaded, the Harrier can float like a butterfly and sting like a bee—albeit a roaring 14-ton butterfly and a bee with 9,200 pounds of bombs and missiles." Jerry Allegood, Marines Rely on Harrier Jet, Despite Critics, News & Observer (Raleigh), Nov. 4, 1990, at C1. In light of the Harrier Jet's well-documented function in attacking and destroying surface and air targets, armed reconnaissance and air interdiction, and offensive and defensive anti-aircraft warfare, depiction of such a jet as a way to get to school in the morning is clearly not serious even if, as plaintiff contends, the jet is capable of being acquired "in a form that eliminates [its] potential for military use." (*See* Leonard Aff. ¶ 20.)

[¶39] Fifth, the number of Pepsi Points the commercial mentions as required to "purchase" the jet is 7,000,000. To amass that number of points, one would have to drink 7,000,000 Pepsis (or roughly 190 Pepsis a day for the next hundred years—an unlikely possibility), or one would have to purchase approximately $700,000 worth of Pepsi Points. The cost of a Harrier Jet is roughly $23 million dollars, a fact of which plaintiff was aware when he set out to gather the amount he believed necessary to accept the alleged offer. (*See* Affidavit of Michael E. McCabe, 96 Civ. 5320, Aug. 14, 1997, Exh. 6 (Leonard Business Plan)). Even if an objective, reasonable person were not aware of this fact, he would conclude that purchasing a fighter plane for $700,000 is a deal too good to be true.[*******]

[¶40] Plaintiff argues that a reasonable, objective person would have understood the commercial to make a serious offer of a Harrier Jet because there was "absolutely no distinction in the manner" (Pl. Mem. at 13,) in which the items in the commercial were presented. Plaintiff also relies upon a press release highlighting the promotional campaign, issued by defendant, in which "[n]o mention is made by [defendant] of humor, or anything of the sort." (Id. at 5.) These arguments suggest merely that the humor of the promotional campaign was tongue in cheek. Humor is not limited to what Justice Cardozo called "[t]he rough and boisterous joke ... [that] evokes its own guffaws." *Murphy v. Steeplechase Amusement Co.*, 250 N.Y. 479, 483, 166 N.E. 173, 174 (1929). In light of the obvious absurdity of the commercial, the Court rejects plaintiff's argument that the commercial was not clearly in jest. * * * *

D. The Alleged Contract Does Not Satisfy the Statute of Frauds

[¶41] The absence of any writing setting forth the alleged contract in this case provides an entirely separate reason for granting summary judgment. Under the New York Statute of Frauds:

> a contract for the sale of goods for the price of $500 or more is not enforceable by way of action or defense unless there is some writing sufficient to indicate that a contract for sale has been made between the parties and signed by the party against whom enforcement is sought or by his authorized agent or broker.

[*******] [13] In contrast, the advertisers of the Carbolic Smoke Ball emphasized their earnestness, stating in the advertisement that " £1,000 is deposited with the Alliance Bank, shewing our sincerity in the matter." Carbolic Smoke Ball, 1 Q.B. at 257. Similarly, in Barnes, the defendant's "subsequent statements, conduct, and the circumstances show an intent to lead any hearer to believe the statements were made seriously." Barnes, 549 P.2d at 1155. The offer in Barnes, moreover, was made in the serious forum of hearings before a state commission; not, as defendant states, at a "gambling convention." Compare Barnes, 549 P.2d at 1154, with Def. Reply Mem. at 6.

N.Y.U.C.C. § 2-201(1); *see also*, e.g., *AFP Imaging Corp. v. Philips Medizin System*, 92 Civ. 6211(LMM), 1994 WL 652510, at *4 (S.D.N.Y. Nov. 17, 1994)). Without such a writing, plaintiff's claim must fail as a matter of law. *See Hilord Chem. Corp. v. Ricoh Elecs., Inc.*, 875 F.2d 32, 36-37 (2d Cir. 1989) ("The adequacy of a writing for Statute of Frauds purposes 'must be determined from the documents themselves, as a matter of law."') (quoting *Bazak Int'l. Corp. v. Mast Indus., Inc.*, 73 N.Y.2d 113, 118, 538 N.Y.S.2d 503 (1989)).

[¶42] There is simply no writing between the parties that evidences any transaction. Plaintiff argues that the commercial, plaintiff's completed Order Form, and perhaps other agreements signed by defendant which plaintiff has not yet seen, should suffice for Statute of Frauds purposes, either singly or taken together. (See Pl. Mem. at 18-19.) For the latter claim, plaintiff relies on *Crabtree v. Elizabeth Arden Sales Corp.*, 305 N.Y. 48, 110 N.E .2d 551 (N.Y. 1953). *Crabtree* held that a combination of signed and unsigned writings would satisfy the Statute of Frauds, "provided that they clearly refer to the same subject matter or transaction." *Id*. at 55. Yet the Second Circuit emphasized in *Horn & Hardart Co. v. Pillsbury Co*., 888 F.2d 8 (2d Cir. 1989), that this rule "contains two strict threshold requirements." *Id*. at 11. First, the signed writing relied upon must by itself establish " 'a contractual relationship between the parties." ' *Id*. (quoting *Crabtree*, 305 N.Y. at 56); *see also O'Keeffe v. Bry*, 456 F. Supp. 822, 829 (S.D.N.Y. 1978) ("To the extent that Crabtree permits the use of a 'confluence of memoranda,' the minimum condition for such use is the existence of one [signed] document establishing the basic, underlying contractual commitment."). The second threshold requirement is that the unsigned writing must "'on its face refer to the same transaction as that set forth in the one that was signed.'' *Horn & Hardart*, 888 F.2d at 11 (quoting *Crabtree*, 305 N.Y. at 56); *see also Bruce Realty Co. of Florida v. Berger*, 327 F. Supp. 507, 510 (S.D.N.Y. 1971).

[¶43] None of the material relied upon by plaintiff meets either threshold requirement. The commercial is not a writing; plaintiff's completed order form does not bear the signature of defendant, or an agent thereof; and to the extent that plaintiff seeks discovery of any contracts between defendant and its advertisers, such discovery would be unavailing: plaintiff is not a party to, or a beneficiary of, any such contracts. Because the alleged contract does not meet the requirements of the Statute of Frauds, plaintiff has no claim for breach of contract or specific performance. * * * *

III. Conclusion

[¶44] In sum, there are three reasons why plaintiff's demand cannot prevail as a matter of law. First, the commercial was merely an advertisement, not a unilateral offer. Second, the tongue-in-cheek attitude of the commercial would not cause a reasonable person to conclude that a soft drink company would be giving away fighter planes as part of a promotion. Third, there is no writing between the parties sufficient to satisfy the Statute of Frauds.

[¶45] For the reasons stated above, the Court grants defendant's motion for summary judgment. The Clerk of Court is instructed to close these cases. Any pending motions are moot.

Questions:

1. Was the advertisement an offer?

2. Why is this case not like the rewards cases, such as the *Carbolic Smoke Ball* case, or *Barnes v. Treece*?

3. Who is the objective, reasonable person? Do you agree?

4. The plaintiff here is from Seattle. Who wants to litigate in Florida? Why? Who wants to litigate in New York? Name at least two reasons to litigate in New York?

5. What facts if added to those of *Leonard* would make Leonard's belief reasonable?

6. In *Lefkowitz v. Great Minneapolis Surplus Store, Inc*., 86 N.W.2d 689 (Minn. 1957), the Store placed the following ad in a Minneapolis newspaper:

> 'Saturday 9 A.M. Sharp 3 Brand New Fur Coats Worth to $100.00
>
> First Come First Served $1 Each'

One week later, the Store published the following ad:

> 'Saturday 9 A.M. 2 Brand New Pastel Mink 3-Skin Scarfs
>
> Selling for $89.50
>
> Out they go Saturday. Each ... $1.00
>
> 1 Black Lapin Stole Beautiful, worth $139.50 ... $1.00
>
> First Come First Served'

On each of the Saturdays named in the ads, Lefkowitz was the first to present himself at the store and demand the items offered. Each time he indicated his willingness to pay $1. The Store refused to sell to him. The first time, the Store said it had a "house rule" that the offer was intended only for women. On the second visit, the Store told Lefkowitz that he knew the house rules. Has the Store made an offer? Should the house rule affect the analysis? In the course of its analysis, the Store argued, citing numerous precedents, that

> where an advertiser publishes in a newspaper that he has a certain quantity or quality of goods which he wants to dispose of at certain prices and on certain terms, such advertisements are not offers which become contracts as soon as any person to whose notice they may come signifies his acceptance by notifying the other that he will take a certain quantity of them. Such advertisements have been construed as an invitation for an offer of sale on the terms stated, which offer, when received, may be accepted or rejected and which therefore does not become a contract of sale until accepted by the seller; and until a contract has been so made, the seller may modify or revoke such prices or terms.

Why might you hold that a Walmart ad (which you can find in a Google search or perhaps an ad service in the mail) was not an offer but was an "invitation for an offer"?

7. In *Owen v. Tunison*, 158 A. 926 (Me. 1932), Owen wrote to Tunison:

> Dear Mr. Tunison:
>
> Will you sell me your store property which is located on Main St. in Bucksport, Me. running from Montgomery's Drug Store on one corner to a Grocery Store on the other, for the sum of $6,000.00?

About six weeks later, Owen received the following reply, written four weeks earlier and mailed from France:

> In reply to your letter of Oct. 23rd which has been forwarded to me in which you inquire about the Bradley Block, Bucksport Me.
>
> Because of improvements which have been added and an expenditure of several thousand dollars it would not be possible for me to sell it unless I was to receive $16,000.00 cash.
>
> The upper floors have been converted into apartments with baths and the b'l'dg put into first class condition.
>
> Very truly yours,
>
> [Signed] R. G. Tunison."

Owen then wrote back:

> Accept your offer for Bradley block Bucksport Terms sixteen thousand cash send deed to Eastern Trust and Banking Co Bangor Maine Please acknowledge.

Four days later Tunison notified Owen that he did not wish to sell, so Owen sued. Did Tunison offer?

8. Norreasha Gill was listening to "DJ Slick" on WLTO-FM (Hot 102) on May 25, 2005. Slick announced that he would as part of an on-air contest give a "hundred grand" to the 10th caller. Ms. Gill heard the description of the contest and listened to the radio for two hours the next morning, hoping to win. She believed she would receive $100,000 if she were the 10th caller and, indeed, she was the 10th caller! Ms. Gill was told by DJ Slick on the air that she had won a "hundred grand" and was given instructions as to how to receive her prize. He said she would be a "hundred grand richer." That night, she told her children that they would buy a minivan and a home with a backyard. Pursuant to DJ Slick's instructions, she arrived at the Central Bank building the next day, where she was informed that she would not be receiving the money and that the contest was a joke. Assuming DJ Slick was its agent, did WLTO make an offer? [Your casebook author spoke with Lee Van Horn, counsel for Ms. Gill, on July 20, 2007. Mr. Van Horn said Ms. Gill's lawsuit settled. The amount of the settlement is to be kept confidential, according to its terms. Mr. Van Horn did say that his client was happy with the result but not as happy later when she did her taxes.]

In November 2000, Ben Stromberg (known as "Ben Stone" on the radio) told his listeners on KORB in Davenport, Iowa, that "anyone who would have the station's logo permanently tattooed across his or her forehead" would be paid $30,000 per year for five years. Two listeners called the station to make sure the offer was legitimate and were assured that it was. The two then went to a tattoo parlor with a person who

claimed to be a radio station employee. The person paid for the tattoos and snapped a photo of the two with the logo. But the station did not pay. *Branded*, ABA Journal, September 2002, 20. Should it have to?

9. See if you can find on the internet a military jet for sale. Look, for instance here—

https://www.everettaero.com/harrier.html

—and here—

http://www.wired.com/2014/07/harrier-silverstone-auction/.

Liquid Death apparently gave away a jet in a contest people can enter by buying their drinks. https://liquiddeath.com/pages/winajet

And here: https://www.ievenwrotethissickurl.com/work/liquiddeathjet

Yes, Netflix made a documentary about Leonard and his lawsuit. 2 stars? Judge Woods's opinion is far more interesting. You may find the Pepsi commercials (Pepsi made three different commercials, listed in order) at the following links:

#1: https://www.youtube.com/watch?v=ZdackF2H7Qc

#2: https://www.youtube.com/watch?v=Ln0VSA9UJ-w

#3: https://www.youtube.com/watch?v=Z4TQmazYyCU

We are about to study other rules that apply to offers, but in a real dispute, no offer ever stands alone. There is a response. What does the court's rule for responses, given in the next case, teach us about the nature of offers?

FOSTER v. OHIO STATE UNIVERSITY

Court of Appeals of Ohio, Tenth District, Franklin County (1987)

534 N.E.2d 1220

STRAUSBAUGH, Presiding Judge.

[¶1] This is an appeal by plaintiff from a summary judgment in the Court of Claims in favor of defendant and against plaintiff.

[¶2] The record indicates that defendant, the Ohio State University, through Andrew Broekema, Dean of the Ohio State College of Arts, by letter dated May 3, 1983, offered plaintiff, Philip E. Foster, an eleven-month appointment as Chairperson and Associate Professor of the Department of History of Art at the Ohio State University beginning July 1, 1983. The letter concluded: "If the terms and conditions of this letter are acceptable to you, please sign the enclosed copy and return it to my office." Subsequently, Dean Broekema notified plaintiff by express mail dated May 25, 1983: "Unless an answer to letter of offer, dated May 3, 1983, is received in my office by Thursday, June 2, 1983, offer for position of Chairperson and Associate Professor, Department of History of Art at The Ohio State University, is withdrawn." The record further indicates that, on June 2, 1983, plaintiff telephoned Dean Broekema collect and left a message with his secretary that plaintiff accepted the position effective July 15, 1983. On June 7, 1983, defendant notified plaintiff that, since he had failed to accept in writing by June 2, the offer was revoked. On June 11, plaintiff signed the May 3 letter notifying defendant of his acceptance.

[¶3] The Court of Claims thereafter granted defendant's motion for summary judgment finding that plaintiff's failure to accept in writing the terms of defendant's offer by June 2 barred his later acceptance on June 11. It is from this finding and judgment that plaintiff appeals setting forth the following single assignment of error:

> "The lower court erred in failing to find that appellant's telephone acceptance of appellee's letter/offer of May 3, 1983, followed by a confirmatory writing delivered in a reasonable time, met all elements of appellee's offer and created an employment contract between the parties."

In support of his assignment of error, plaintiff argues first that there is no evidence to support a finding that plaintiff had to answer by June 2 or that the answer had to be in writing and, therefore, plaintiff had a reasonable time in which to respond. Second, even if the May 25 letter required a definite answer by June 2, there is no indication that the acceptance had to be in writing alone. Third, the question of whether the acceptance had sufficiently met an offer is a question of fact and as such the evidence shows that plaintiff accepted the offer as tendered. Fourth, to the extent that the Court of Claims relied upon time being the essence of the contract, there is no indication that defendant ever believed a timely answer was critical to the appointment of the position.

[¶4] The terms of defendant's offer to plaintiff were set forth in the May 3, 1983 letter and established the precise manner and place of acceptance—that a copy of the letter be signed and the copy be returned to Dean Broekema's office. Subsequently, Dean Broekema imposed an additional requirement as to time, prescribing that plaintiff's acceptance be received by June 2, 1983. The time requirement did not modify or alter any previous specifications but merely put a time limit on the duration of the offer. An offer which is unsupported by consideration is subject to revocation at any time. 1 Williston on Contracts (3 Ed.1957) 176-179, Section 55; *Franck v. Seavey Mfg. Co*. (1926), 21 Ohio App. 369, 4 Ohio Law Abs. 299, 153 N.E. 209. The offeror can wholly terminate or limit the power and mode of acceptance. 1 Corbin on Contracts (1963) 157- 166, Sections 38 and 39. When an acceptance to a contract for employment does not meet and correspond with the offer in every respect, no contract is usually formed. 1 Restatement of the Law 2d, Contracts (1981) 144, Section 58; *Schiff v. Schiff* (App.1942), 36 Ohio Law Abs. 626, 632, 45 N.E.2d 132,

136; *see, also, Karas v. Brogan* (1978), 55 Ohio St.2d 128, 129, 9 O.O.3d 107, 107-108, 378 N.E.2d 470, 471.

[¶5] Defendant's offer to plaintiff dated May 3, 1983 states that the position was to begin July 1, 1983. When plaintiff left his purported message of acceptance on June 2, 1983, he indicated July 15, 1983 as the desired date of commencement. A reply to an offer which purports to accept but is conditional on the offeror's assent to terms additional to or different from those offered is not an acceptance but is a counteroffer. 1 Restatement of the Law 2d, Contracts (1981) 145, Section 59. Plaintiff's telephonic purported acceptance of June 2, 1983 was therefore a counteroffer and not an unconditional acceptance which was rejected by Dean Broekema in his letter of June 7, 1983 and, therefore, no contract was created. The undisputed facts indicate that plaintiff simply failed to accept the terms of the offer and therefore no contract exists. Plaintiff's single assignment of error is overruled, and the judgment of the Court of Claims is affirmed.

[¶6] JUDGMENT AFFIRMED.

WHITESIDE and BOWMAN, JJ., concur.

WHITESIDE, Justice, concurring.

Although I concur in the judgment, I do solely for the reason that the June 2, 1983 telephone "acceptance" by plaintiff constituted a counteroffer which was rejected by the June 7, 1983 response letter, the effect of which was to rescind the original offer making the subsequent attempted "acceptance" by plaintiff's signing the original letter offer on June 11, 1983, ineffectual since there was no outstanding offer to accept at that time.

B. Termination of the Power of Acceptance

Recall from *Adams v. Lindsell* that the court held that an offer fictionally continued, as if in the ether, until it was accepted. The *Adams* fiction raised the specter of offers continuing indefinitely, in which case the sheer number of outstanding offers would soon, speaking tongue-in-cheek, fill the ether itself and crowd the metaphysical world with offers, bouncing this way and that, to the consternation of other metaphysical entities who must also share the space (if it is proper to speak of it as space (or crowded)). On a more practical note, offers that continued forever could be accepted forever, and that would disrupt the certainty in future planning that contract law is supposed to allow. So, metaphysically and practically, there must be a way to get rid of outstanding offers—ways for the viability of offers to end. The cases in this section outline those ways. See how many you can find and define.

DICKINSON v. DODDS

Court of Appeal, Chancery Division (1876)

2 Ch. Div. 463

[¶1] On Wednesday, the 10th of June, 1874, the Defendant John Dodds signed and delivered to the Plaintiff, George Dickinson, a memorandum, of which the material part was as follows:—

> I hereby agree to sell to Mr. George Dickinson the whole of the dwelling-houses, garden ground, stabling, and outbuildings thereto belonging, situate at Croft, belonging to me, for the sum of £800. As witness my hand this tenth day of June, 1874.
>
> £800. (Signed) *John Dodds*.
>
> P.S.—This offer to be left over until Friday, 9 o'clock, a.m. *J.D.* (the twelfth), 12th June, 1874.
>
> (Signed) *J. Dodds*.

[¶2] The bill alleged that Dodds understood and intended that the Plaintiff should have until Friday 9 A.M. within which to determine whether he would or would not purchase, and that he should absolutely have until that time the refusal of the property at the price of £800, and that the Plaintiff in fact determined to accept the offer on the morning of Thursday, the 11th of June, but did not at once signify his acceptance to Dodds, believing that he had the power to accept it until 9 A.M. on the Friday.

[¶3] In the afternoon of the Thursday the Plaintiff was informed by a Mr. Berry that Dodds had been offering or agreeing to sell the property to Thomas Allan, the other Defendant. Thereupon the Plaintiff, at about half-past seven in the evening, went to the house of Mrs. Burgess, the mother-in-law of Dodds, where he was then staying, and left with her a formal acceptance in writing of the offer to sell the property. According to the evidence of Mrs. Burgess this document never in fact reached Dodds, she having forgotten to give it to him.

[¶4] On the following (Friday) morning, at about seven o'clock, Berry, who was acting as agent for Dickinson, found Dodds at the Darlington railway station, and handed to him a duplicate of the acceptance by Dickinson, and explained to Dodds its purport. He replied that it was too late, as he had sold the property. A few minutes later Dickinson himself found Dodds entering a railway carriage, and handed him another duplicate of the notice of acceptance, but Dodds declined to receive it, saying, "You are too late. I have sold the property."

[¶5] It appeared that on the day before, Thursday, the 11th of June, Dodds had signed a formal contract for the sale of the property to the Defendant Allan for £800, and had received from him a deposit of £40.

[¶6] The bill in this suit prayed that the Defendant Dodds might be decreed specifically to perform the contract of the 10th of June, 1874; that he might be restrained from conveying the property to Allan; that Allan might be restrained from taking any such conveyance; that, if any such conveyance had been or should be made, Allan might be declared a trustee of the property for, and might be directed to convey the property to, the Plaintiff; and for damages. * * * *

James, L.J., after referring to the document of the 10th of June, 1874, continued:-

[¶7] The document, though beginning, “I hereby agree to sell,” was nothing but an offer, and was only intended to be an offer, for the Plaintiff himself tells us that he required time to consider whether he would enter into an agreement or not. Unless both parties had then agreed there was no concluded agreement then made; it was in effect and substance only an offer to sell. * * * * There was no consideration given for the undertaking or promise, to whatever extent it may be considered binding, to keep the property unsold until 9 o’clock on Friday morning; but apparently Dickinson was of opinion, and probably Dodds was of the same opinion, that he (Dodds) was bound by that promise, and could not in any way withdraw from it, or retract it, until 9 o’clock on Friday morning, and this probably explains a good deal of what afterwards took place. But it is clear settled law, on one of the clearest principles of law, that this promise, being a mere nudum pactum, was not binding, and that at any moment before a complete acceptance by Dickinson of the offer, Dodds was as free as Dickinson himself. Well, that being the state of things, it is said that the only mode in which Dodds could assert that freedom was by actually and distinctly saying to Dickinson, “Now I withdraw my offer.” It appears to me that there is neither principle nor authority for the proposition that there must be an express and actual withdrawal of the offer, or what is called a retractation. It must, to constitute a contract, appear that the two minds were at one, at the same moment of time, that is, that there was an offer continuing up to the time of the acceptance. If there was not such a continuing offer, then the acceptance comes to nothing. Of course it may well be that the one man is bound in some way or other to let the other man know that his mind with regard to the offer has been changed; but in this case, beyond all question, the Plaintiff knew that Dodds was no longer minded to sell the property to him as plainly and clearly as if Dodds had told him in so many words, “I withdraw the offer.” This is evidence from the Plaintiff’s own statements in the bill.

[¶8] The Plaintiff says in effect that, having heard and knowing that Dodds was no longer minded to sell to him, and that he was selling or had sold to some one else, thinking that he could not in point of law withdraw his offer, meaning to fix him to it, and endeavoring to bind him, “I went to the house where he was lodging, and saw his mother-in-law, and left with her an acceptance of the offer, knowing all the while that he had entirely changed his mind. I got an agent to watch for him at 7 o’clock the next morning, and I went to the train just before 9 o’clock, in order that I might catch him and give him my notice of acceptance just before 9 o’clock, and when that occurred he told my agent, and he told me, you are too late, and he then threw back the paper.” It is to my mind quite clear that before there was any attempt at acceptance by the Plaintiff, he was perfectly well aware that Dodds had changed his mind, and that he had in fact agreed to sell the property to Allan. It is impossible, therefore, to say that there was ever that existence of the same mind between the two parties which is essential in point of law to the making of an agreement. I am of opinion, therefore, that the Plaintiff has failed to prove that there was any binding contract between Dodds and himself.

[¶9] Mellish, L.J.:-I am of the same opinion. * * * *

[¶10] Baggallay, J.A.-I entirely concur in the judgments which have been pronounced.

[¶11] James, L.J.:-The bill will be dismissed * * * *. * * * *

Questions:

1. Was Dodds's promise to hold his offer open until Friday morning binding? Why or why not?

2. Suppose Berry did not tell Dickinson the facts that, when learned, terminated Dickinson's power of acceptance but otherwise the story stays the same. What result? (The answer to this question is not in the case, but you should be able to figure it out from the materials we have studied.)

3. Why does the court go out on a limb to let Dodds off after he was so sneaky? (The answer to this question is not in the case but if you think about policies underlying enforcement of promises, some answers should occur to you.)

Note: R2K § 43 is an acceptable recapitulation of *Dickinson v. Dodds*. That section says, "An offeree's power of acceptance is terminated when the offeror takes definite action inconsistent with an intention to enter into the proposed contract and the offeree acquires reliable information to that effect."

Charles William AKERS v. J. B. SEDBERRY, Inc., et al.

Court of Appeals of Tennessee (1956)

286 S.W.2d 617

FELTS, Judge.

[¶1] These two consolidated causes are before us upon a writ of error sued out by J. B. Sedberry, Inc., and Mrs. M. B. Sedberry, defendants below, to review a decree of the Chancery Court, awarding a recovery against them in favor of each of the complainants, Charles William Akers and William Gambill Whitsitt, for damages for breach of a contract of employment.

[¶2] The principal question presented is whether complainants resigned their employment, or were wrongfully discharged by defendants; and if there was a breach of contract for which complainants are entitled to recover, there are some further questions as to the measure or extent of the recovery.

[¶3] J. B. Sedberry, Inc., was a Tennessee corporation with its principal place of business at Franklin, Tennessee. Mrs. M. B. Sedberry owned practically all of its stock and was its president and in active charge of its affairs. It was engaged in the business of distributing 'Jay Bee' hammer mills, which were manufactured for it under contract by Jay Bee Manufacturing Company, a Texas corporation, whose plant was in Tyler, Texas, and whose capital stock was owned principally by L. M. Glasgow and B. G. Byars.

[¶4] On July 1, 1947, J. B. Sedberry, Inc., by written contract, employed complainant Akers as Chief Engineer for a term of five years at a salary of $12,000 per year, payable $1,000 per month, plus 1% of its net profits for the first year, 2% the second, 3% the third, 4% the fourth, and 5% the fifth year. His duties were to carry on research for his employer, and to see that the Jay Bee Manufacturing Company, Tyler, Texas, manufactured the mills and parts according to proper specifications. Mrs. M. B. Sedberry guaranteed the employer's performance of this contract.

[¶5] On August 1, 1947, J. B. Sedberry, Inc., by written contract, employed complainant Whitsitt as Assistant Chief Engineer for a term of five years at a salary of $7,200 per year, payable $600 per month, plus 1% of the corporation's net profits for the first year, 2% for the second, 3% for the third, 4% for the fourth, and 5% for the fifth year. His duties were to assist in the work done by the Chief Engineer. Mrs. M. B. Sedberry guaranteed the employer's performance of this contract.

[¶6] Under Mrs. Sedberry's instructions, Akers and Whitsitt moved to Tyler, Texas, began performing their contract duties in the plant of the Jay Bee Manufacturing Company, continued working there, and were paid under the contracts until October 1, 1950, when they ceased work, under circumstances hereafter stated.

[¶7] In 1947, when these employment contracts were made, Mrs. Sedberry owned no stock in the Jay Bee Manufacturing Company. In 1948 she purchased the shares of stock in this company which were owned by the Glasgow interests, and in 1949 she purchased the 750 shares owned by her brother, B. G. Byars, and gave him her note therefor in the sum of $157,333.93, pledging the 750 shares with him as collateral to her note.

[¶8] Glasgow had been general manager of the Jay Bee Manufacturing Company, but when he sold his stock, he was succeeded by A. M. Sorenson as manager. There soon developed considerable friction between Sorenson and complainants Akers and Whitsitt. The Jay Bee Manufacturing Company owed large sums to the Tyler State Bank & Trust Co.; and the bank's officers, fearing the company might fail under Sorenson's management, began talking to Akers and Whitsitt about the company's financial difficulties.

[¶9] One of the bank's vice-presidents, J. Harold Stringer, made a trip to Franklin to see Mrs. Sedberry about the company's indebtedness to the bank. He told her that they could not get along with Sorenson and did not agree with the way he was managing the company's affairs. Mrs. Sedberry asked Stringer as soon as he got back to Tyler to see Akers and Whitsitt and discuss with them plans for the refinancing and the operation of the company; and thereafter the bank's officers had a number of conferences with Akers and Whitsitt about these matters.

[¶10] While these matters were pending, Akers and Whitsitt flew to Nashville and went to Franklin to talk with Mrs. Sedberry about them. They had a conference with her at her office on Friday, September 29, 1950, lasting from 9:30 a. m. until 4:30 p. m. As they had come unannounced, and unknown to Sorenson, they felt Mrs. Sedberry might mistrust them; and at the outset, to show their good faith, they offered to

resign, but she did not accept their offer. Instead, she proceeded with them in discussing the operation and refinancing of the business.

[¶11] Testifying about this conference, Akers said that, at the very beginning, to show their good faith, he told Mrs. Sedberry that they would offer their resignations on a ninety-day notice, provided they were paid according to the contract for that period; that she pushed the offers aside—'would not accept them', but went into a full discussion of the business; that nothing was thereafter said about the offers to resign; and that they spent the whole day discussing the business, Akers making notes of things she instructed him to do when he got back to Texas.

[¶12] Whitsitt testified that at the beginning of the meeting Akers stated the position for both of them, and told Mrs. Sedberry, as evidence of their good faith, 'we would resign with ninety-days notice if she paid us the monies that she owed us to that date, and on the other hand, if she did not accept that resignation, we would carry forth the rest of our business.' He said that she did not accept the offer, but proceeded with the business, and nothing further was said about resigning.

[¶13] Mrs. Sedberry testified that Akers and Whitsitt came in and 'offered their resignations'; that they said they could not work with Sorenson and did not believe the bank would go along with him; and that 'they said if it would be of any help to the organization they would be glad to tender their resignation and pay them what was due them.' She further said that she 'did not accept the resignation', that she 'felt it necessary to contact Mr. Sorenson and give consideration to the resignation offer.' But she said nothing to complainants about taking the offer under consideration.

[¶14] On cross-examination she said that in the offer to resign 'no mention was made of any ninety-day notice'. Asked what response she made to the offer she said, 'I treated it rather casually because I had to give it some thought and had to contact Mr. Sorenson.' She further said she excused herself from the conference with complainants, went to another room, tried to telephone Sorenson in Tyler, Texas, but was unable to locate him.

[¶15] She then resumed the conference, nothing further was said about the offers to resign, nothing was said by her to indicate that she thought the offers were left open or held under consideration by her. But the discussion proceeded as if the offers had not been made. She discussed with complainants future plans for refinancing and operating the business, giving them instructions, and Akers making notes of them.

[¶16] Following the conference, complainants, upon Mrs. Sedberry's request, flew back to Texas to proceed to carry out her instructions. On the way back, and while in Nashville, Friday evening, Akers telephoned her in Franklin to tell her that he had just learned that the bank had sued both the companies and process had been served that day. On the next morning, September 30, Akers had a conference with the bank officials about the refinancing of the company, the results of which he reported to Mrs. Sedberry by long-distance telephone conversation that day.

[¶17] On Monday, October 2, 1950, Mrs. Sedberry sent to complainants similar telegrams, signed by 'J. B. Sedberry, Inc., by M. B. Sedberry, President', stating that their resignations were accepted, effective immediately. We quote the telegram to Akers, omitting the formal parts:

> 'Account present unsettled conditions which you so fully are aware we accept your kind offer of resignation effective immediately. Please discontinue as of today with everyone

> employed in Sedberry, Inc., Engineering Department, discontinuing all expenses in this department writing.'

While this said she was 'writing', she did not write. Akers wrote her, but held up sending his letter, at the request of her brother, Mr. Byars, who was one of the officers of the bank in Tyler, Texas. Akers later rewrote practically the same letter and mailed it to her on October 16, 1950. Whitsitt also sent her a similar letter on the same day.

[¶18] In his letter, Akers said that he was amazed to get her telegram, and called her attention to the fact that no offer to resign by him was open or outstanding when she sent the telegram; that while he had made a conditional offer to resign at their conference on September 29, she had immediately rejected the offer, and had discussed plans for the business and had instructed him and Whitsitt as to things she wanted them to do in the business on their return to Tyler.

[¶19] This letter further stated that Akers was expecting to be paid according to the terms of his contract until he could find other employment that would pay him as much income as that provided in his contract, and that if he had to accept a position with less income, he would expect to be paid the difference, or whatever losses he suffered by her breach of the contract. Whitsitt's letter contained a similar statement of his position.

[¶20] On November 10, 1950, Mrs. Sedberry wrote a letter addressed to both Akers and Whitsitt in which she said that 'no one deplored the action taken more than the writer', but she did not recede from her position as expressed in the telegram. She stated her contention that the offers to resign had been without condition; and though she also said she would like to make an amicable settlement, no settlement was made.

[¶21] As it takes two to make a contract, it takes two to unmake it. It cannot be changed or ended by one alone, but only by mutual assent of both parties. A contract of employment for a fixed period may be terminated by the employee's offer to resign, provided such offer is duly accepted by the employer. *Gentry Co. v. Margolius*, 110 Tenn. 669, 674, 75 S.W. 959; *Balderacchi v. Ruth*, 36 Tenn. App. 421, 424, 256 S.W.2d 390, 391.

[¶22] An employee's tender of his resignation, being a mere offer is, of course, not binding until it has been accepted by the employer. Such offer must be accepted according to its terms and within the time fixed. The matter is governed by the same rules as govern the formation of contracts. *Nesbit v. Giblin*, 96 Neb. 369, 148 N.W. 138, L.R.A.1915D, 477, Ann.Cas.1916A, 1008; 1 Labatt's Master & Servant (2d ed.) section 181; Note, Ann.Cas.1916A, 1011, 1012.

[¶23] An offer may be terminated in a number of ways, as, for example, where it is rejected by the offeree, or where it is not accepted by him within the time fixed, or, if no time is fixed, within a reasonable time. An offer terminated in either of these ways ceases to exist and cannot thereafter be accepted. 1 Williston on Contracts (1936), secs. 50A, 51, 53, 54; 1 Corbin on Contracts (1950), secs. 35, 36; 1 Rest., Contracts, secs. 35, 40.

[¶24] The question what is a reasonable time, where no time is fixed, is a question of fact, depending on the nature of the contract proposed, the usages of business and other circumstances of the case. Ordinarily,

an offer made by one to another in a face to face conversation is deemed to continue only to the close of their conversation, and cannot be accepted thereafter.

[¶25] The rule is illustrated by Restatement of Contracts, section 40, Illustration 2, as follows:

> '2. While A and B are engaged in conversation, A makes B an offer to which B then makes no reply, but a few hours later meeting A again, B states that he accepts the offer. There is no contract unless the offer or the surrounding circumstances indicate that the offer is intended to continue beyond the immediate conversation.'

[¶26] In *Mactier's Adm'rs v. Frith*, 1830, 6 Wend. N.Y., 103, 114, 21 Am.Dec. 262, 268, the rule was stated as follows:

> 'Although the will of the party making the offer may precede that of the party accepting, yet it must continue down to the time of the acceptance. Where parties are together chaffering about an article of merchandise and one expresses a present willingness to accept of certain terms, that willingness is supposed to continue, unless it is revoked, to the close of their interview and negotiation on the same subject, and if during this time the other party says he will take the article on the terms proposed, the bargain is thereby closed. Pothier, *Traité du contrat de vente*, p. 1, sec. 2, art. 3, no. 31.' * * * *

Professor Corbin says:

> 'When two negotiating parties are in each other's presence, and one makes an offer to the other without indicating any time for acceptance, the inference that will ordinarily be drawn by the other party is that an answer is expected at once. * * * * If, when the first reply is not an acceptance, the offeror turns away in silence, the proper inference is that the offer is no longer open to acceptance.' 1 Corbin on Contracts (1950), section 36, p. 111.

[¶27] The only offer by Akers and Whitsitt to resign was the offer made by them in their conversation with Mrs. Sedberry. They made that offer at the outset, and on the evidence it seems clear that they expected an answer at once. Certainly, there is nothing in the evidence to show that they intended the offer to continue beyond that conversation; and on the above authorities, we think the offer did not continue beyond that meeting.

[¶28] Indeed, it did not last that long, in our opinion, but was terminated by Mrs. Sedberry's rejection of it very early in that meeting. While she did not expressly reject it, and while she may have intended, as she says, to take the offer under consideration, she did not disclose such an intent to complainants; but, by her conduct, led them to believe she rejected the offer, brushed it aside, and proceeded with the discussion as if it had not been made.

[¶29] 'An offer is rejected when the offeror is justified in inferring from the words or conduct of the offeree that the offeree intends not to accept the offer or to take it under further advisement (Rest. Contracts sec. 36).' 1 Williston on Contracts, section 51.

[¶30] So, we agree with the Trial Judge that when defendants sent the telegrams, undertaking to accept offers of complainants to resign, there was no such offer in existence; and that this attempt of defendants to terminate their contract was unlawful and constituted a breach for which they are liable to complainants.

* * * *

[¶31] Finally, defendants contend that if complainants are entitled to any recovery at all, such recovery should have been limited to the ninety-day period from and after October 2, 1950, because complainants themselves admitted that they had offered to resign upon ninety days notice with pay for that period.

[¶32] The answer to this contention is that their offer to resign on ninety days notice was not accepted, but had terminated, and there was no offer in existence when Mrs. Sedberry undertook to accept their offers of resignation. Such attempt by defendants to terminate their contract was unlawful and was a breach for which they become liable for the measure of recovery as above stated. * * * *

[¶33] All of the assignments of error are overruled and the decree of the Chancellor is affirmed. Decrees will be entered here for complainants for the amount of the decrees below with interest. * * * * The causes are remanded to the Chancery Court for further proceedings not inconsistent with this opinion.

HICKERSON and SHRIVER, JJ., concur.

Questions:

1. What two ways for a power of acceptance to terminate are outlined in this case?

2. What did Mrs. Sedberry do to reject the offers?

3. How is this case the same as *Foster v. Ohio State University*?

4. Another longstanding common law rule is that the offeror's death or incapacity (e.g., the offeror is unconscious) terminates the power of acceptance. This rule holds (so far, in the rare cases where it comes up) even when the offeree has no idea the offeror is dead. *See In re Estate of Severtson*, 1998 WL 88253 (Minn. App.). There is no explanation for that rule consistent with the rule of *Lucy v. Zehmer*. The *Severtson* opinion justifies it by asserting that dead people cannot possibly assent, but *Lucy* and contract law generally does not require assent. A good alternative explanation would be that, on death, the property of the offeror passes to the offeror's estate, a different legal entity than the offeror. A contract right or duty, like a very similar property right or duty, passes to the estate when a contracting party dies, but an offer is not yet a contract right or duty.

If the offeree knows of the death, then the offeree should know that the offeror's estate will have (often wildly) different interests than the offeror, such that the offeree is no longer justified in believing that the offeree's assent is invited and will conclude a bargain.

If the offeree is unaware of the death, then one could argue that the offeree's assent manifested to the offeror should be inoperative. Even if the offeror has already assented, how will the offeree assent? What is a reasonable manifestation to a deceased person? In cases where it is possible to do this (where the offeree assents by email or text to a deceased email address or phone number), one could argue that

promissory estoppel should bind the estate to the promise, at least to pay for any definite and substantial detriment.

Questions from *Foster v. Ohio State University* and *Payne v. Cave*:

1. What is the effect of a counteroffer on the original offer?

2. What is the effect of a subsequent bid on a prior bid at an auction?

C. Extending the Time During Which Acceptance May Occur

Sometimes things happen that extend the period for acceptance or otherwise bind the offeror.

1. Option Contract

A binding option contract preserves the offeree's power of acceptance until the option period ends. Recall that an option includes a promise to sell (or enter into some other kind of contract). The power to accept would normally extend until the end of the option period or acceptance occurs, whichever is sooner.

2. Unilateral Contracts Where the Offeror Is the Promisor and Performance Has Begun

A contract forming through the exchange of mutual promises is called a "bilateral contract." The meaning of the phrase is somewhat slippery, but most usages of the phrase signal that both parties have promises to perform in the future.

In a unilateral contract, by contrast, a promise is made in exchange for a performance. By definition, at the moment of formation, one party has already performed and only the other party has made a promise to perform in the future. (Some courts also say that a bilateral contract becomes unilateral if one party has finished performing its promise and only the other party has something left to perform.)

Though, in a unilateral contract, either party might be the offeror, generally the promisor makes an offer: "If you mow my lawn, I'll pay you $30." A few law professors once argued that in such a case a contract would not form until the performance was complete because only then was consideration given as requested. But

that meant that the promisor/offeror was not bound during the promisee's performance and could withdraw the offer until the last blade of grass was cut. The most famous example, suggested by a Professor Wormser, involves an offer by A to pay $100 to B if B walked across the Brooklyn Bridge. Wormser argued that if A overtook B when B was halfway across and withdrew his offer, B would have no rights against A even though B had partially performed. Wormser, *The True Conception of Unilateral Contracts*, 26 Yale L.J. 136 (1916). That result seems harsh because the promisee has justifiably relied on the promise.

When A stops B from performing further, doesn't B have a claim against A? The lawn mowing deal is a better example, perhaps: When the lawn service mows half my lawn because I have told them if they mow the whole lawn I will pay them, don't they have a claim against me even after I stop them from completing the job?

Why would a promisor offer a unilateral rather than a bilateral contract?

The following case describes law formulated in part in response to Professor Wormser.

Louis W. and Sylvia V. RAGOSTA v. Allen S. WILDER, Jr.

Supreme Court of Vermont (1991)

592 A.2d 367

PECK, Justice.

[¶1] Defendant appeals from a judgment ordering him to convey to plaintiffs a piece of real property known as "The Fork Shop." Defendant argues that the court improperly found that a binding contract existed and that it misapplied the doctrine of equitable estoppel. He also contends that the ruling cannot be upheld under promissory estoppel principles since the court failed to examine the extent to which enforcement of defendant's promise to sell was required to prevent injustice. Because the trial court's ruling cannot stand on contract or equitable estoppel grounds and because the court's analysis of promissory estoppel is inextricably bound in its contractual analysis, we reverse and remand the cause for further proceedings consistent with the principles expressed herein.

[¶2] In 1985, plaintiffs became interested in purchasing "The Fork Shop" from defendant, but preliminary negotiations between the parties were fruitless. In 1987, plaintiffs learned that defendant was again considering selling the "The Fork Shop," mailed him a letter offering to purchase the property along with a check for $2,000 and began arrangements to obtain the necessary financing. By letter dated September 28, 1987, defendant returned the $2,000 check explaining that he had two properties "up for sale" and that he would not sign an acceptance to plaintiffs' offer because "that would tie up both these properties until [there was] a closing." In the letter, he also made the following counter-offer:

> I will sell you The Fork Shop and its property as listed in book 35, at page 135 of the Brookfield Land Records on 17 April 1972, for $88,000.00- (Eighty- eight thousand dollars), at anytime up until the 1st of November 1987 that you appear with me at the Randolph National Bank with said sum. At which time they will give you a certified deed to this property or to your agent as directed, providing said property has not been sold.

[¶3] On October 1st, the date plaintiffs received the letter, they called defendant. The court found that during the conversation plaintiffs told defendant that "the terms and conditions of his offer were acceptable and that they would in fact prepare to accept the offer." Defendant assured plaintiffs that there was no one else currently interested in purchasing "The Fork Shop."

[¶4] On October 6th, plaintiffs informed defendant that they would not close the sale on October 8th as discussed previously but that they would come to Vermont on October 10th. On October 8th, defendant called plaintiffs and informed them that he was no longer willing to sell "The Fork Shop." The trial court found that, at that time, defendant was aware plaintiffs "had processed their loan application and were prepared to close." Plaintiffs informed defendant that they would be at the Randolph National Bank at 10:00 a.m. on October 15th with the $88,000 purchase price and in fact appeared. Defendant did not. Plaintiffs claim they incurred $7,499.23 in loan closing costs.

[¶5] Plaintiffs sued for specific performance arguing that defendant had contracted to sell the property to them. They alleged moreover that defendant knew they would have to incur costs to obtain financing for the purchase but assured them that the sale would go through and that they relied on his assurances.

[¶6] The trial court concluded that defendant "made an offer in writing which could only be accepted by performance prior to the deadline." It concluded further that defendant could not revoke his offer on October 8th because plaintiffs, relying on the offer, had already begun performance and that defendant should be estopped from revoking the offer on a theory of equitable estoppel. It ordered defendant to convey to plaintiffs "The Fork Shop" for $88,000. This appeal followed.

I.

[¶7] Plaintiffs claim that defendant's letter of September 28, 1987 created a contract to sell "The Fork Shop" to them unless the property was sold to another buyer. Rather, defendant's letter contains an offer to sell the property for $88,000, which the trial court found could only be accepted "by performance prior to the deadline," and a promise to keep the offer open unless the property were sold to another buyer. Defendant received no consideration for either promise. In fact, defendant returned plaintiffs' check for $2,000 which would have constituted consideration for the promise to keep the offer open, presumably because he did not wish to make a firm offer. Thus, the promise to keep the offer to sell open was not enforceable and, absent the operation of equitable estoppel, defendant could revoke the offer to sell the property at any time before plaintiffs accepted it. *See Buchannon v. Billings*, 127 Vt. 69, 75, 238 A.2d 638, 642 (1968) ("An option is a continuing offer, and if supported by a consideration, it cannot be withdrawn before the time limit.") (emphasis added).

[¶8] Plaintiffs argue that the actions they undertook to obtain financing, which were detrimental to them, could constitute consideration for the promise to keep the offer to sell open. Their argument is unconvincing. Although plaintiffs are correct in stating that a detriment may constitute consideration, they ignore the rule that "[t]o constitute consideration, a performance or a return promise must be bargained for." Restatement (Second) of Contracts § 71(1) (1981). "A performance or return promise is bargained for if it is sought by the promisor in exchange for his promise and is given by the promisee in exchange for that promise." *Id*. at § 71(2). Plaintiffs began to seek financing even before defendant made a definite offer to sell the property. Whatever detriment they suffered was not in exchange for defendant's promise to keep the offer to sell open.

[¶9] The trial court ruled that the offer to sell "The Fork Shop" could only be accepted by performance but concluded that in obtaining financing plaintiffs began performance and that therefore defendant could not revoke the offer to sell once plaintiffs incurred the cost of obtaining financing. Section 45 of the Restatement (Second) of Contracts provides that "[w]here an offer invites an offeree to accept by rendering a performance and does not invite a promissory acceptance, an option contract is created when the offeree tenders or begins the invited performance or tenders a beginning of it." However, "[w]hat is begun or tendered must be part of the actual performance invited in order to preclude revocation under this Section." *Id.* at comment f.

[¶10] Here, plaintiffs were merely engaged in preparation for performance. The court itself found only that "plaintiffs had changed their position in order to tender performance." At most, they obtained financing and assured defendant that they would pay; plaintiffs never tendered to defendant or even began to tender the $88,000 purchase price. Thus, they never accepted defendant's offer and no contract was ever created. *See Multicare Medical Center v. State Social & Health Services*, 114 Wash.2d 572, 584, 790 P.2d 124, 131 (1990) ("under a unilateral contract, an offer cannot be accepted by promising to perform; rather, the offeree must accept, if at all, by performance, and the contract then becomes executed").†††††† * * * *

[¶11] On remand the court shall consider the case under promissory estoppel only and determine what remedy, if any, is necessary to prevent injustice. In making this determination the court should consider the fact that plaintiffs incurred the expense of obtaining financing although they could not be certain that the property would be sold to them. * * * *

[¶12] Reversed and the cause remanded for further proceedings consistent with the principles expressed herein.

Questions:

1. Could Wilder's offer be withdrawn or was a contract already formed?

2. Was Wilder's promise made with consideration at the time it was made? Why?

3. Did Ragosta's promise to perform render Wilder's promise binding? Why?

4. Did Ragosta's beginning to obtain financing bind Wilder? Why?

5. At what point in time would Wilder have been bound, had he not retracted?

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†††††† [*] Because defendant specified that the manner of acceptance would be performance, plaintiffs' argument that they accepted defendant's offer over the telephone must fail. In fact, plaintiffs admitted in their depositions that they were very worried that the property would be sold to someone else prior to closing. Thus, they should have understood that they had no enforceable contract until closing.

6. Should promissory estoppel principles apply to Wilder's promise made in the counter-offer recited in ¶2?

7. An option contract involves two promises by the optionor: one (offering) to perform and one to hold the offer open during a period of time. In an option contract created under section 45, who is the optionor—the promisor or the promisee? How long has the optionor promised to keep the offer open? (You might draw some argument from *Akins v. J.B. Sedberry, Inc*. in answer to this question.)

8. In a unilateral contract, one party makes no promise, so that party is not bound to perform. B could legally stop walking halfway across the Brooklyn Bridge and A would have no valid claim against him. But doesn't that mean that while B is walking, A is bound but B is not? Should we care?

3. The Special Case of a Subcontractor's Bid Used to Compute a General Contractor's Bid

The fact pattern in *Drennan* does not even involve an offer. However, the subcontractor's bid to the general contractor cannot be withdrawn. As you read the case, ask yourself the following: Why is the bid not an offer? Why is it not accepted? On what ground does it become binding? When it becomes binding in this way, can it be withdrawn?

The *Drennan* fact pattern is extremely common and is somewhat analogous to the other fact patterns in this section. This is as good a place as any to study it.

William A. DRENNAN v. STAR PAVING COMPANY

Supreme Court of California, In Bank (1958)

333 P.2d 757

TRAYNOR, Justice.

[¶1] Defendant appeals from a judgment for plaintiff in an action to recover damages caused by defendant's refusal to perform certain paving work according to a bid it submitted to plaintiff.

[¶2] On July 28, 1955, plaintiff, a licensed general contractor, was preparing a bid on the 'Monte Vista School Job' in the Lancaster school district. Bids had to be submitted before 8:00 p.m. Plaintiff testified that it was customary in that area for general contractors to receive the bids of subcontractors by telephone on the day set for bidding and to rely on them in computing their own bids. Thus on that day plaintiff's secretary, Mrs. Johnson, received by telephone between fifty and seventy-five subcontractors' bids for various parts of the school job. As each bid came in, she wrote it on a special form, which she brought into plaintiff's office. He then posted it on a master cost sheet setting forth the names and bids of all subcontractors. His own bid had to include the names of subcontractors who were to perform one-half of one per cent or more

of the construction work, and he had also to provide a bidder's bond of ten per cent of his total bid of $317,385 as a guarantee that he would enter the contract if awarded the work.

[¶3] Late in the afternoon, Mrs. Johnson had a telephone conversation with Kenneth R. Hoon, an estimator for defendant. He gave his name and telephone number and stated that he was bidding for defendant for the paving work at the Monte Vista School according to plans and specifications and that his bid was $7,131.60. At Mrs. Johnson's request he repeated his bid. Plaintiff listened to the bid over an extension telephone in his office and posted it on the master sheet after receiving the bid form from Mrs. Johnson. Defendant's was the lowest bid for the paving. Plaintiff computed his own bid accordingly and submitted it with the name of defendant as the subcontractor for the paving. When the bids were opened on July 28th, plaintiff's proved to be the lowest, and he was awarded the contract.

[¶4] On his way to Los Angeles the next morning plaintiff stopped at defendant's office. The first person he met was defendant's construction engineer, Mr. Oppenheimer. Plaintiff testified: 'I introduced myself and he immediately told me that they had made a mistake in their bid to me the night before, they couldn't do it for the price they had bid, and I told him I would expect him to carry through with their original bid because I had used it in compiling my bid and the job was being awarded them. And I would have to go and do the job according to my bid and I would expect them to do the same.'

[¶5] Defendant refused to do the paving work for less than $15,000. Plaintiff testified that he 'got figures from other people' and after trying for several months to get as low a bid as possible engaged L & H Paving Company, a firm in Lancaster, to do the work for $10,948.60.

[¶6] The trial court found on substantial evidence that defendant made a definite offer to do the paving on the Monte Vista job according to the plans and specifications for $7,131.60, and that plaintiff relied on defendant's bid in computing his own bid for the school job and naming defendant therein as the subcontractor for the paving work. Accordingly, it entered judgment for plaintiff in the amount of $3,817.00 (the difference between defendant's bid and the cost of the paving to plaintiff) plus costs.

[¶7] Defendant contends that there was no enforceable contract between the parties on the ground that it made a revocable offer and revoked it before plaintiff communicated his acceptance to defendant.

[¶8] There is no evidence that defendant offered to make its bid irrevocable in exchange for plaintiff's use of its figures in computing his bid. Nor is there evidence that would warrant interpreting plaintiff's use of defendant's bid as the acceptance thereof, binding plaintiff, on condition he received the main contract, to award the subcontract to defendant. In sum, there was neither an option supported by consideration nor a bilateral contract binding on both parties.

[¶9] Plaintiff contends, however, that he relied to his detriment on defendant's offer and that defendant must therefore answer in damages for its refusal to perform. Thus the question is squarely presented: Did plaintiff's reliance make defendant's offer irrevocable?

[¶10] Section 90 of the Restatement of Contracts states: 'A promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise.' This rule applies in this state. * * * *

[¶11] Defendant's offer constituted a promise to perform on such conditions as were stated expressly or by implication therein or annexed thereto by operation of law. (See 1 Williston, Contracts (3rd. ed.), s 24A, p. 56, s 61, p. 196.) Defendant had reason to expect that if its bid proved the lowest it would be used by plaintiff. It induced 'action * * * * of a definite and substantial character on the part of the promisee.'

[¶12] Had defendant's bid expressly stated or clearly implied that it was revocable at any time before acceptance we would treat it accordingly. It was silent on revocation, however, and we must therefore determine whether there are conditions to the right of revocation imposed by law or reasonably inferable in fact. In the analogous problem of an offer for a unilateral contract, the theory is now obsolete that the offer is revocable at any time before complete performance. Thus section 45 of the Restatement of Contracts provides: 'If an offer for a unilateral contract is made, and part of the consideration requested in the offer is given or tendered by the offeree in response thereto, the offeror is bound by a contract, the duty of immediate performance of which is conditional on the full consideration being given or tendered within the time stated in the offer, or, if no time is stated therein, within a reasonable time.' In explanation, comment b states that the 'main offer includes as a subsidiary promise, necessarily implied, that if part of the requested performance is given, the offeror will not revoke his offer, and that if tender is made it will be accepted. Part performance or tender may thus furnish consideration for the subsidiary promise. Moreover, merely acting in justifiable reliance on an offer may in some cases serve as sufficient reason for making a promise binding (see s 90).'

[¶13] Whether implied in fact or law, the subsidiary promise serves to preclude the injustice that would result if the offer could be revoked after the offeree had acted in detrimental reliance thereon. Reasonable reliance resulting in a foreseeable prejudicial change in position affords a compelling basis also for implying a subsidiary promise not to revoke an offer for a bilateral contract.

[¶14] The absence of consideration is not fatal to the enforcement of such a promise. It is true that in the case of unilateral contracts the Restatement finds consideration for the implied subsidiary promise in the part performance of the bargained-for exchange, but its reference to section 90 makes clear that consideration for such a promise is not always necessary. The very purpose of section 90 is to make a promise binding even though there was no consideration 'in the sense of something that is bargained for and given in exchange.' (*See* 1 Corbin, Contracts 634 et seq.) Reasonable reliance serves to hold the offeror in lieu of the consideration ordinarily required to make the offer binding. In a case involving similar facts the Supreme Court of South Dakota stated that 'we believe that reason and justice demand that the doctrine (of section 90) be applied to the present facts. We cannot believe that by accepting this doctrine as controlling in the state of facts before us we will abolish the requirement of a consideration in contract cases, in any different sense than an ordinary estoppel abolishes some legal requirement in its application. We are of the opinion, therefore, that the defendants in executing the agreement (which was not supported by consideration) made a promise which they should have reasonably expected would induce the plaintiff to submit a bid based thereon to the Government, that such promise did induce this action, and that injustice can be avoided only by enforcement of the promise.' *Northwestern Engineering Co. v. Ellerman*, 69 S.D. 397, 408, 10 N.W.2d 879, 884; *see also*, *Robert Gordon, Inc., v. Ingersoll-Rand Co*., 7 Cir., 117 F.2d 654, 661; *cf. James Baird Co. v. Gimbel Bros*., 2 Cir., 64 F.2d 344.

[¶15] When plaintiff used defendant's offer in computing his own bid, he bound himself to perform in reliance on defendant's terms. Though defendant did not bargain for this use of its bid neither did defendant make it idly, indifferent to whether it would be used or not. On the contrary it is reasonable to suppose that defendant submitted its bid to obtain the subcontract. It was bound to realize the substantial possibility that

its bid would be the lowest, and that it would be included by plaintiff in his bid. It was to its own interest that the contractor be awarded the general contract; the lower the subcontract bid, the lower the general contractor's bid was likely to be and the greater its chance of acceptance and hence the greater defendant's chance of getting the paving subcontract. Defendant had reason not only to expect plaintiff to rely on its bid but to want him to. Clearly defendant had a stake in plaintiff's reliance on its bid. Given this interest and the fact that plaintiff is bound by his own bid, it is only fair that plaintiff should have at least an opportunity to accept defendant's bid after the general contract has been awarded to him.

[¶16] It bears noting that a general contractor is not free to delay acceptance after he has been awarded the general contract in the hope of getting a better price. Nor can he reopen bargaining with the subcontractor and at the same time claim a continuing right to accept the original offer. *See*, *R. J. Daum Const. Co. v. Child*, Utah, 247 P.2d 817, 823. In the present case plaintiff promptly informed defendant that plaintiff was being awarded the job and that the subcontract was being awarded to defendant.

[¶17] Defendant contends, however, that its bid was the result of mistake and that it was therefore entitled to revoke it. It relies on the rescission cases of *M. F. Kemper Const. Co. v. City of Los Angeles*, 37 Cal.2d 696, 235 P.2d 7, and *Brunzell Const. Co. v. G. J. Weisbrod, Inc*., 134 Cal.App.2d 278, 285 P.2d 989. *See also*, *Lemoge Electric v. San Mateo County*, 46 Cal.2d 659, 662, 297 P.2d 638. In those cases, however, the bidder's mistake was known or should have been known to the offeree, and the offeree could be placed in status quo. Of course, if plaintiff had reason to believe that defendant's bid was in error, he could not justifiably rely on it, and section 90 would afford no basis for enforcing it. *Robert Gordon, Inc., v. Ingersoll-Rand, Inc.*, 7 Cir., 117 F.2d 654, 660. Plaintiff, however, had no reason to know that defendant had made a mistake in submitting its bid, since there was usually a variance of 160 per cent between the highest and lowest bids for paving in the desert around Lancaster. He committed himself to performing the main contract in reliance on defendant's figures. Under these circumstances defendant's mistake, far from relieving it of its obligation constitutes an additional reason for enforcing it, for it misled plaintiff as to the cost of doing the paving. Even had it been clearly understood that defendant's offer was revocable until accepted, it would not necessarily follow that defendant had no duty to exercise reasonable care in preparing its bid. It presented its bid with knowledge of the substantial possibility that it would be used by plaintiff; it could foresee the harm that would ensue from an erroneous underestimate of the cost. Moreover, it was motivated by its own business interest. Whether or not these considerations alone would justify recovery for negligence had the case been tried on that theory (*see Biakanja v. Irving*, 49 Cal.2d 647, 650, 320 P.2d 16), they are persuasive that defendant's mistake should not defeat recovery under the rule of section 90 of the Restatement of Contracts. As between the subcontractor who made the bid and the general contractor who reasonably relied on it, the loss resulting from the mistake should fall on the party who caused it. * * * *

[¶18] There is no merit in defendant's contention that plaintiff failed to state a cause of action, on the ground that the complaint failed to allege that plaintiff attempted to mitigate the damages or that they could not have been mitigated. Plaintiff alleged that after defendant's default, 'plaintiff had to procure the services of the L & H Co. to perform said asphaltic paving for the sum of $10,948.60.' Plaintiff's uncontradicted evidence showed that he spent several months trying to get bids from other subcontractors and that he took the lowest bid. Clearly he acted reasonably to mitigate damages. In any event any uncertainty in plaintiff's allegation as to damages could have been raised by special demurrer. Code Civ. Proc. s 430, subd. 9. It was not so raised and was therefore waived. Code Civ. Proc. s 434.

[¶19] The judgment is affirmed.

GIBSON C. J., and SHENK, SCHAUER, SPENCE and McCOMB, JJ., concur.

Questions:

1. Is Star Paving's bid enforceable? Why?

2. Was Star Paving's bid supported by consideration?

3. Did Drennan accept Star Paving's bid?

4. Was there a consensual contract in this case?

5. Courts all but uniformly hold that the general is not bound to use the sub even though the sub cannot back out without at least paying reliance damages. Why? Apply the promissory estoppel test to what the general does in the fact pattern.

6. Sometimes general contractors will shop the sub's bid to other subcontractors in an effort to obtain a lower subcontract bid? If the general does that, has the general relied on the bid in such a way that the sub should still be bound to the bid?

The Uniform Commercial Code Article 2 Section 2-205 provides a formal mechanism by which a merchant can make an offer and hold it open without consideration for a period of time not exceeding three months. If you study sales of goods, you get to learn about this exciting possibility.

Chapter 8. Acceptances

A. Acceptances: What Are They?

An offeree's manifestation of assent to an offer "in a manner invited or required by the offer" constitutes acceptance. R2K § 50. On acceptance, a contract forms.

You have already seen this happen in Chapter 6, in *Payne v. Cave*, *Adams v. Lindsell*, and *Lucy v. Zehmer*. In Chapter 7. Offers, you also saw it happen in note cases *Lefkowitz v. Great Minneapolis Surplus Store* and the two fact patterns in Question 8 after *Leonard v. Pepsico*, involving WLTO and KORB. Please pinpoint what acts counted as manifestation of assent to the offer in those cases.

You have also seen the process fail in *Foster v. Ohio State University* when Foster assented to something other than the offered exchange. That failure created a counteroffer.

B. Choice of Promise or Performance

Charles L. GLEESON v. Chris F. FRAHM and Olga K. Frahm

Supreme Court of Nebraska (1982)

320 N.W.2d 95

EMPSON, District Judge.

[¶1] This is an action for specific performance. On July 31, 1978, the defendants, Chris F. Frahm and Olga K. Frahm, executed for consideration an option, which is in pertinent part as follows:

> "KNOW ALL MEN BY THESE PRESENTS: That ... [Frahms] hereinafter referred to as First Party ... in consideration of the sum of One Dollar and other good and valuable consideration ... paid ... by ... second party ... hereby agree to hold, until the 1st day of January, 1980, 12:00 o'clock A.M., ... subject exclusively to the order of the said second party or his, her or their assigns, the following described property to wit: [property described] or to transfer and convey the said property by warranty deed ... at any time within the time above prescribed, to the said second party or to such person or persons as he ... may direct, at and for the price of One Thousand Two Hundred and Fifty (1,250) Dollars per acre payable on the following terms: 25% down payment, balance payable in ten (10) annual installments bearing interest at the rate of 8% per annum ....
>
> ....

> "... if there should be any delay on the part of the first party in perfecting the title to the above property for more than thirty (30) days, after notice shall have been given of the election of the holder of this option to purchase the aforesaid property, then, and in that event, the holder of this option shall have the right to cancel this option, and upon the exercise of such right of cancellation, shall receive back the consideration paid for this option ...."

The option was assigned to the plaintiff, Charles L. Gleeson.

[¶2] On December 28, 1979, Gleeson mailed to the Frahms a document entitled

> "Acceptance of Option to Purchase," which is in pertinent part as follows:
>
> "I, Charles L. Gleeson, as Assignee ... do under a certain option agreement made by you on the 31st day of July, 1978, for the purchase of the property described as follows: [property described] hereby elect to exercise such option to purchase, upon the terms as contained in said option agreement and do direct that you transfer and convey said property by Warranty Deed ... to myself, Charles L. Gleeson and Richard J. Gleeson, as tenants in common.
>
> "Please deliver abstract of title to the real estate certified to date, to my attorney ...."

[¶3] The document, received by the Frahms on December 29, 1979, neither contained nor was accompanied by any payment or specific offer of payment of any kind. Gleeson has never offered the Frahms any payment and the Frahms have never taken any steps to convey the property.

[¶4] No further action was taken by either party until about the middle of January 1980, when Gleeson stopped by the Frahms' home to ask about fencing the property. Chris Frahm told him to go see their attorney, who told Gleeson the sale would not be made. This lawsuit resulted.

[¶5] The Frahms' answer to Gleeson's petition alleged that the option was not exercised by Gleeson because the "downpayment" required was not tendered or paid before the option expired. They have defended throughout on that basis, and the trial court, upon that same theory, sustained the Frahms' motion to dismiss at the close of Gleeson's case.

[¶6] * * * * [T]he exercise of an option to buy or sell real estate must be unconditional and in accordance with the offer made. Those holdings, in turn, spring from long-standing principles of contract law that the acceptance of any offer, to result in a contract, must be absolute, unconditional, and unqualified. *See Roberts v. Cox*, 91 Neb. 553, 136 N.W. 831 (1912).

[¶7] The parties may contract to the effect that full or partial performance by the holder of the option is required to exercise the option. If they do so, the contract remains a unilateral one after the option is exercised, that is, the holder having performed, only the owner remains bound to perform. If they do not so contract, the holder may exercise by promising to perform, in which case the contract becomes bilateral—both parties are bound by their promises to perform the contract. Where the contract specifies the required manner of acceptance, the holder must conform. Where the manner of acceptance is not specified, the holder may exercise by promising to perform what the option requires of him. Restatement (Second) of

Contracts § 32 (1981). The option contract in this case does not specify any particular manner of exercise or acceptance.

[¶8] It is significant that the contract gives the Frahms 30 days to perfect title after notice of election of Gleeson to purchase. It is more significant that upon the Frahms' failure to perfect title, Gleeson shall "receive back" not the downpayment but the "consideration paid for this option," i.e., "One Dollar and other good and valuable consideration." The Frahms' contention that proper exercise of the option required a downpayment before the Frahms had displayed good title is untenable. Gleeson's letter of acceptance, couched in the words of the option contract itself, is a clear exercise of the option, by which Gleeson became bound to pay the price upon the Frahms' showing of good title and their offer of a warranty deed.

[¶9] The judgment is reversed and the cause is remanded to the District Court for further proceedings.

[¶10] REVERSED AND REMANDED FOR FURTHER PROCEEDINGS.

WHITE, Justice, dissenting.

[¶1] I dissent. The terms of the option require a downpayment of 25 percent at the time the option is exercised. Since no downpayment was received by January 1, 1980, the option expired. I would have sustained the District Court's order dismissing the plaintiff's petition.

[¶2] I am authorized to state that BROWER, D. J., joins in this dissent.

Question: Does it matter in this case whether consideration was paid for the option?

C. Issues of Intent

SIMMONS v. UNITED STATES

United States Court of Appeals Fourth Circuit (1962)

308 F.2d 160

SOBELOFF, Chief Judge.

[¶1] Diamond Jim III, a rock fish, was one of millions of his species swimming in the Chesapeake Bay, but he was a very special fish, and he occasions some nice legal questions. Wearing a valuable identification tag, he was placed on June 19, 1958, in the waters of the Bay by employees of the American

Brewery, Inc., with the cooperation of Maryland state game officials. According to the well-publicized rules governing the brewery-sponsored Third Annual American Beer Fishing Derby, anybody who caught Diamond Jim III and presented him to the company, together with the identification tag and an affidavit that he had been caught on hook and line, would be entitled to a cash prize of $25,000.00. The company also placed other tagged fish in the Chesapeake, carrying lesser prizes.

[¶2] Fishing on the morning of August 6, 1958, William Simmons caught Diamond Jim III. At first, he took little notice of the tag, but upon re-examining it a half hour later, he realized that he had caught the $25,000.00 prize fish. After Simmons and his fishing companions appropriately marked the happy event, he hastened to comply with the conditions of the contest. Soon thereafter, in the course of a television appearance arranged by the brewery, he received the cash prize. The record shows that Simmons knew about the contest, but, as an experienced fisherman, he also knew that his chances of landing that fish were minuscule, and he did not have Diamond Jim III in mind when he set out that morning.

[¶3] Thereupon, an alert District Director of the Internal Revenue Service came forward with the assertion that the cash prize was includable in Simmons' gross income under section 61(a) and section 74(a) of the Internal Revenue Code, 26 U.S.C.A. §§ 61(a), 74(a) and assessed a tax deficiency of $5,230.00. Promptly Simmons paid and filed a claim for refund. A small sum was refunded on the basis of very generous deductions allowed by the Internal Revenue Service. Not satisfied, however, Simmons brought an action in the District Court on the theory that no part of the cash prize can be included in gross income under sections 61(a) and 74(a) of the Internal Revenue Code * * *. * * * * On motion for summary judgment, the District Court held for the Government, and Simmons prosecutes this appeal. * * * *

II.

[¶4] The taxpayer's next point is that he was at least entitled to have a jury decide whether the $25,000.00 payment to him was a gift, excluded from gross income by section 102. The Supreme Court's exposition of this branch of the law in *Commissioner of Internal Revenue v. Duberstein*, 363 U.S. 278, 80 S. Ct. 1190 (1960), is of course controlling, and this court expressed its understanding of that decision in *Poyner v. Commissioner*, 301 F.2d 287 (4th Cir. 1962). Here it suffices to repeat that it is the function of the trier of fact to determine the basic facts and from these to infer the motivations of the donor. This does not mean, however, that in an appropriate case a district judge may not make a decision on summary judgment. Where, from the facts stipulated and submitted on affidavit, when viewed in the light most favorable to the taxpayer, it plainly appears that a jury could not reasonably infer that the payments were motivated 'out of affection, respect, admiration, charity or like impulses,' or from a 'detached or disinterested generosity,' or from similar sentiments, summary judgment for the Government is the correct disposition. Such is the present case.

[¶5] The established fact is that there was no personal relationship between Simmons and the brewery to prompt it to render him financial assistance. Nor was it impelled by charitable impulses toward the community at large, for the prize was to be paid to whoever caught Diamond Jim III, regardless of need or affluence. Rather, the taxpayer has apparently rendered the company a valuable service, for, by catching the fish and receiving the award amid fanfare, he brought to the company the publicity the Fishing Derby was designed to generate.

[¶6] Moreover, under accepted principles of contract law on which we may rely in the absence of pertinent Maryland cases, the company was legally obligated to award the prize once Simmons had caught

the fish and complied with the remaining conditions precedent. The offer of a prize or reward for doing a specified act, like catching a criminal, is an offer for a unilateral contract. For the offer to be accepted and the contract to become binding, the desired act must be performed with knowledge of the offer. The evidence is clear that Simmons knew about the Fishing Derby the morning he caught Diamond Jim III. It is not fatal to his claim for refund that he did not go fishing for the express purpose of catching one of the prize fish. So long as the outstanding offer was known to him, a person may accept an offer for a unilateral contract by rendering performance, even if he does so primarily for reasons unrelated to the offer. Consequently, since Simmons could require the company to pay him the prize, the case is governed by *Robertson v. United States*, 343 U.S. 711, 713-714, 72 S. Ct. 994, 96 L. Ed. 1237 (1952). There, the Supreme Court held that, since the sponsor of a contest for the best symphonies submitted was legally obligated to award prizes in accordance with his offer, the payment made was not a gift to the recipient. * ** *

[¶7] Affirmed.

Questions:

1. Would Simmons have won the prize if he had not known about the offer when he caught the fish?

2. What is consideration for the brewery's promise to pay $25,000 to the person who catches Diamond Jim III? Does a bargain exist in this case even though Bill was going fishing anyway?

D. Notice

CARLILL v. CARBOLIC SMOKE BALL CO.

Court of Appeal (1893)

1 Q.B. 256

[You know the facts of this case, from *Leonard*. Mrs. Carlill did not contact the Smoke Ball Co. until she tried to claim the reward. Was this a soon enough manifestation of assent to count as acceptance? Reward fact patterns often have this problem, and almost all of them resolve it the same way:]

LINDLEY, L.J. [The Lord Justice stated the facts, and proceeded:-] * * * *

* * * *

But then it is said, “Supposing that the performance of the conditions is an acceptance of the offer, that acceptance ought to have been notified.” Unquestionably, as a general proposition, when an offer is made, it is necessary in order to make a binding contract, not only that it should be accepted, but that the acceptance should be notified. But is that so in cases of this kind? I apprehend that they are an exception to that rule, or, if not an exception, they are open to the observation that the notification of the acceptance need not precede the performance. This offer is a continuing offer. It was never revoked, and if notice of acceptance is required * * *, the person who makes the offer gets the notice of acceptance contemporaneously with his notice of the performance of the condition. If he gets notice of the acceptance before his offer is revoked, that in principle is all you want. I, however, think that the true view, in a case of this kind, is that the person who makes the offer shows by his language and from the nature of the transaction that he does not expect and does not require notice of the acceptance apart from notice of the performance.

* * * *

Questions:

1. If I promise my young neighbor, “I’ll pay you $20 if you promise to mow my lawn,” then, if my neighbor accepts, how will I receive notice of that acceptance?

2. If I promise my young neighbor, “I’ll pay you $20 if you mow my lawn,” must my neighbor give notice of acceptance at the time of my promise or before mowing in order to collect later?

3. You know from *Leonard* that a Carbolic Smoke Ball is a rubber ball with a short, pipe-like, hollow extension. The extension is covered with a cloth. The ball is filled with carbolic acid in powder form. The user holds the extension under her nose and taps on the ball, which makes the powder arise through the cloth. When the user breaths in the carbolic acid, it induces sneezing. Considering what the smoke ball is and how it was used, you will appreciate the humor in another part of Justice Lindley’s opinion. The first issue Lindley addressed was whether the advertisement was an offer. He phrased it differently, however. He said, “We must first consider whether this was intended to be a promise at all, or whether it was a mere puff which meant nothing. Was it a mere puff?” A “mere puff”! What a lark!

4. What is consideration for the smoke ball company’s promise?

ELECTRIC STORAGE BATTERY CO. v. BLACK

Supreme Court of Wisconsin (1965)

27 Wis. 2d 366 (1965)

GORDON, J.

* * * * Notice of Acceptance.

[¶1] All courts agree that if the contract of guaranty affirmatively calls for notice, it is a condition which must be met in order to bind the guarantor on his promise. Mr. Milo Black's letter of guaranty, dated July 30, 1960, does not expressly cover the question whether he expected to be notified by the creditor that the latter accepted the guaranty and intended to make deliveries of merchandise in reliance thereon. Courts have not been uniform in their decisions on the issue whether notice of intention to accept such a guaranty is necessary in order to hold the guarantor liable.

[¶2] Some courts have held that if there is any fair reason for the guarantor to be uncertain that the creditor will accept the proposed guaranty, a notice of the intention to accept is a constructive condition to the liability of the guarantor. * * * *

[¶3] In Restatement, 1 Contracts, p. 64, sec. 56, appears the following illustration:

> "1. A writes to B: 'Let C have $100 and I guarantee its repayment.' Immediately on receiving this communication, B lets C have $100 but fails to notify A of the fact, although he knows that A is not otherwise likely to learn of it. B cannot enforce the guaranty if C fails to pay the debt."

[¶4] The decisions of the state of Wisconsin demonstrate that notice of acceptance to the guarantor is ordinarily required. In *A. B. Kuhlman Co. v. Cave* (1908), 135 Wis. 279, 115 N. W. 793, the guarantor wrote a letter to the creditor which contained the following:

> "I request that should Mr. Leon H. Cave . . . order goods from you at any time after date of this letter of credit until further notice, that you ship same to order of said agent, and I hereby guarantee payment for the same within twenty days after the arrival of the goods at destination."

The trial court rendered judgment in favor of the creditor against the guarantor, and the supreme court reversed, with the following holding, at page 280:

> "It is plain that this judgment was erroneous. The writing sued on was simply a letter of credit and constituted an offer merely on the part of the defendant, which would not become a contract until accepted and notice of acceptance given to the guarantor. This has been so recently held by this court that no extended discussion of the principle is either desirable or necessary. *Miami Co. Nat. Bank v. Goldberg*, 133 Wis. 175, 113 N. W. 391. See, also, *New Home S. M. Co. v. Simon*, 104 Wis. 120, 80 N. W. 71. No acceptance or notice of acceptance was found by the court; hence no completed contract of guaranty was made and no liability incurred."

[¶5] * * * * At page 180 of the *Miami County Nat. Bank* Case, the court cited *Acme Mfg. Co. v. Reed* (1900), 197 Pa. St. 359, 47 Atl. 205, for the policy behind this rule:

> "A guarantor of future credit or advancing is entitled to notice from the party giving the credit of his acceptance of the guaranty, inasmuch as such notice enables the guarantor to know the nature and extent of his liability, to exercise due diligence in guarding himself against losses which might otherwise be unknown to him, and to avail himself of the appropriate means in law and equity to compel the other parties to discharge him from future responsibility. . . . The corporation accepted and filled the order, but gave no notice of the acceptance to the guarantor. Held, that the guarantor was not liable." * * * *

[¶6] This rule followed in Wisconsin and in a number of other states has been questioned and circumscribed. When the guaranty contract is executed contemporaneously with the signing of the primary contract, it would be unsound to require formal notice. In addition, the guarantor may, by his conduct, waive the necessity of notice of acceptance.

[¶7] The plaintiff has referred the court to several cases which hold that notice of acceptance is not necessary when the guaranties are continuing in nature, as they are considered to be offers which become effective as soon as they are relied on by the creditor. *Klatte v. Franklin State Bank* (1933), 211 Wis. 613, 248 N. W. 158, 249 N. W. 72; *Chicago Lock Co. v. Kirchner* (1929), 199 Wis. 30, 225 N. W. 185; *International Textbook Co. v. Mabbott* (1915), 159 Wis. 423, 150 N. W. 429. However, in each of the foregoing cases (unlike the case at bar) the giving of the guaranty was contemporaneous with the execution of the primary contract; under such circumstances, notice of acceptance would indeed be a formality.

[¶8] Also, these cases can be distinguished on other grounds. In the *International Textbook Co*. Case, *supra*, the court points out, at page 427, that the guarantor expressly waived any notice of acceptance of the guaranty. In the *Chicago Lock Co.* Case, *supra*, the guarantor claimed he never received a formal notice of acceptance, but the court observed that the guarantor had actual knowledge of it from another source. In the *Klatte* Case, *supra*, the issue now being considered was not before the court. The main issue there involved the legal effect of a notice by a surety that he intended to terminate his future liability on the contract. * * * *

[¶9] Restatement, Security (1941), p. 248, sec. 86, asserts the following rule:

> "Where the surety offers to guarantee an extension of credit to the principal and the credit is extended as the sole consideration for the surety's promise, the contract is complete upon the extension of credit, but if the surety does not know of the extension of credit and has no adequate means of ascertaining with reasonable promptness and certainty that the credit has been extended and the creditor should know this, the contract of the surety is discharged unless within a reasonable time after the extension of credit the creditor exercises reasonable diligence to notify the surety thereof."

[¶10] The effect of the Restatement rule is to obviate the need of notice to the surety except in those cases wherein he is either unaware of the extension of credit or does not have adequate means to learn of it; under the Kuhlman Case and other decisions of this state, the emphasis is somewhat different: The guarantor is entitled to notice of acceptance unless there exists some special circumstance excusing it. There may even be contracts of guaranty which, by their special terms or particular circumstances, will

require not only an original notice of acceptance but additional notices of acceptance as to subsequent sales or shipments.

[¶11] The instant case was submitted upon stipulated facts. There is nothing in such facts or in the documentary exhibits that were received in evidence which would relieve the creditor of its responsibility to give notice of acceptance of Mr. Milo Black's offer to guarantee payment for material purchased by his son. The plaintiff urges that when Mr. Milo Black responded (in Exhibit 5) to the creditor's letter of May 7, 1962, he acknowledged, in effect, that he had never expected to receive notice of acceptance at the time he wrote the original letter. We are unable to derive such meaning from Exhibit 5. Therein Mr. Milo Black wrote:

> "I guaranteed his first shipment but that was nearly two years ago.
>
> "I would suggest your reducing your account to your cost and giving him a long term settlement. His intentions are good if given a chance."

In our opinion, the foregoing language neither demands nor waives acceptance in any degree greater than the original letter of July 30, 1960. Under the authority *of A. B. Kuhlman Co. v. Cave*, *supra*, we conclude that Mr. Milo Black was entitled to notice of acceptance, and, in the absence of such notice, he cannot be held liable on the contract. * * * *

We conclude that Mr. Milo Black was entitled to receive from the plaintiff notice of acceptance of his guaranty contract and, since such notice was not given, the guarantor cannot be held liable.

By the Court. Judgment affirmed.

Questions:

1. What did Black offer?

2. What was consideration for Black's offer?

3. Did the battery company accept Black's offer?

4. Would you have known that you were to give Black notice of acceptance, given such cases as *Carlill*?

5. When must such notice be given?

Jeffrey Galgoczy v. Chagrin Falls Auto Parts, Inc.

Court of Appeals of Ohio, Eighth District (2010)

MELODY J. STEWART, J.

[¶1] Plaintiff-appellant, Jeffrey Galgoczy, appeals from a summary judgment rendered in favor of defendant-appellee, Chagrin Falls Auto Parts, Inc., on his claims for wrongful termination and promissory estoppel. Chagrin Falls Auto Parts terminated Galgoczy because he had accrued 12 days of medical absences in a seven-month period. Galgoczy based his legal claims on the disciplinary procedures outlined in an employee handbook that he alleged created an implied contract of employment that Chagrin Falls Auto Parts breached. He also alleged that he reasonably relied on the promise of continued employment because Chagrin Falls Auto Parts hired him despite being aware that he suffered from chronic migraine headaches. Chagrin Falls Auto Parts defended by noting that it hired Galgoczy as an at-will employee and that it was entitled to terminate him at any time and for any reason. The court granted summary judgment without opinion.

I

[¶2] Galgoczy first argues that the court erred by granting summary judgment because issues of material fact existed demonstrating that Chagrin Falls Auto Parts breached an implied contract of employment. He maintains that his absences should have been considered "excused" and that Chagrin Falls Auto Parts failed in any event to follow the disciplinary procedures outlined in its employee handbook. * * * *

[¶3] Ohio adheres to the concept of at-will employment, meaning that in the absence of a contract, employment is terminable at-will by either the employer or the employee, at any time, and for any reason not contrary to law. *Leininger v. Pioneer Natl. Latex*, 115 Ohio St.3d 311, 2007-Ohio-4921, 875 N.E.2d 36, at ¶6. In some circumstances, however, an employee handbook can create a binding contract if it contains clear promissory language that the employee accepts by continuing to work after receiving it. *See Mers v. Dispatch Printing Co.* (1985), 19 Ohio St.3d 100, 483 N.E.2d 150, paragraph two of the syllabus. Given the presumption of at-will employment, the party seeking to prove the existence of an implied contract has a heavy burden because all of the elements of a contract must be established, including a "meeting of the minds" [Ricks: Cue eye roll, but you know what the court meant to say, yes? Even the court knows this isn't literal, which is why it put quotes around it.] to show that employment was intended to be other than at-will. *Penwell v. Amherst Hosp.* (1992), 84 Ohio App.3d 16, 21, 616 N.E.2d 254; *Cohen & Co. v. Messina* (1985), 24 Ohio App.3d 22, 24, 492 N.E.2d 867.

[¶4] Galgoczy points to a provision in the Chagrin Falls Auto Parts employee handbook relating to absences that required the employee to "call in each day the employee is absent unless prior arrangements have been made." He claimed that on all 12 occasions on which he missed work due to migraine headaches he called in to report his absences, so his compliance with the absence provision of the handbook precluded his discharge on that ground.

[¶5] Tellingly, Galgoczy's argument does not consider a provision of the handbook stating that "excessive" absenteeism may "result in discipline up to and including discharge." But regardless of whether the excused absences provision of the handbook could be interpreted to create a clear promise of continued employment despite excessive absences, any implied contract claim is defeated by the following statement

contained in the handbook: “The policies contained in this employee handbook are not intended as a contract of employment and may be added to or changed as needed by our company. Our company adheres to the policy of employment-at-will, which enables either the employee or the employer to terminate the employment relationship at any time.”

[¶6] Disclaimers like that used in this case preclude the use of a written employee handbook to demonstrate an implied contract of employment. *Wing v. Anchor Media, Ltd. of Texas* (1991), 59 Ohio St.3d 108, 110, 570 N.E.2d 1095; *Handler v. Merrill Lynch Life Agency, Inc.* (1993), 92 Ohio App.3d 356, 635 N.E.2d 1271. The disclaimer plainly states that nothing in the handbook could be construed as creating a contract of employment. Absent a meeting of the minds on the nature and extent of excused absences, Galgoczy could not as a matter of law show the existence of an implied contract on the issue of excused absences. *Mastromatteo v. Brown & Williamson Tobacco Corp.*, 2d Dist. No. 20216, 2004-Ohio-3776, at ¶18.

II

[¶7] Galgoczy next argues that the court erred by granting summary judgment on his promissory estoppel claim. He maintains that he informed Chagrin Falls Auto Parts about his migraine headaches prior to being hired and was told that it would not be a problem, so his hiring gave him the right to rely on continued employment in the event those headaches caused him to be absent.

[¶8] Ordinarily, a contract requires a promise supported by consideration. *Kostelnik v. Helper*, 96 Ohio St.3d 1, 2002-Ohio-2985, 770 N.E.2d 58, at ¶16. However, in some circumstances a promise can be binding if the promisee has suffered some detriment in reasonably relying on the promise, even if that detriment was not requested as consideration. This is known as promissory estoppel, and this doctrine of contract law can apply to oral, at-will employment contracts. *Mers*, 19 Ohio St.3d at paragraph three of the syllabus. However, a promisor is free by a suitable disclaimer to deny any legally binding effect to a promise. *Tohline v. Cent. Trust Co., N.A.* (1988), 48 Ohio App.3d 280, 282, 549 N.E.2d 1223.

[¶9] As earlier noted, Chagrin Falls Auto Parts’ employee handbook contained a disclaimer stating: “The policies contained in this employee handbook are not intended as a contract of employment * * *.” This disclaimer sufficiently showed Chagrin Falls Auto Parts’ intention to not create in the handbook any promises that would be enforceable. Id. With the absence of any promise, no enforceable contract existed as a matter of law. *Lenzo v. New Resources Corp.* (Mar. 26, 1998), 8th Dist. No. 72443.

[¶10] It follows that Chagrin Falls Auto Parts’ disclaimer of any contract of employment made Galgoczy’s reliance on the terms of the handbook unreasonable. *Olive v. Columbia/HCA Healthcare Corp.* (Mar. 9, 2000), 8th Dist. Nos. 75249 and 76349. Galgoczy admitted in his deposition that he was an at-will employee and that the handbook stated that Chagrin Falls Auto Parts reserved the right “to dismiss any employee at any time with or without cause and with or without notice.” He also admitted that the employee handbook stated that excessive absenteeism could result in termination and no one at Chagrin Falls Auto Parts told him that his job was secure no matter how many days he missed. In fact, Galgoczy conceded that he had been counseled about his absences in a review that took place a week or two before his termination, saying that it had been “brought up about me missing days.” When asked if it was his understanding that as long as he was missing days for health reasons his employment would not be affected, he could only respond, “[t]hat I couldn’t answer. That was never brought up to me.” He did concede, however, that he had not been told that as long as he missed work for a medical reason, he would not be terminated.

[¶11] The handbook provisions relating to at-will employment and his counseling for excessive absences belie Galgoczy's stated belief that his absences were "excused" as long as he called them in prior to the start of his shift. Galgoczy admitted that he had not been promised secure employment despite his medical absences and further admitted that he had been counseled about excessive absences prior to his termination. Galgoczy's purported reliance on the "excused absences" provision of the handbook was not only contrary to specific disclaimers and counseling made by Chagrin Falls Auto Parts, but also unreasonable based on his own understanding that his absences were having an effect on business. As a matter of law, Galgoczy did not establish the requisite elements of promissory estoppel. The court did not err by granting summary judgment.

Judgment affirmed.

Questions:

1. The court says it needs to look for a "meeting of the minds," but where does it actually look and what kinds of evidence does the court cite?

2. Without the excessive absence clause and the disclaimer mentioned in paragraph [5], what chances do you give Galgoczy's claim of surviving the summary judgment motion?

3. If the employment handbook is an offer, when did Galgoczy accept it? The court answers this question in paragraph [3]. See it? Does that answer seem plausible to you? How is intent manifested?

4. If the deal is that employment handbook terms are an offer and they are accepted in the way the court says, what is consideration for the promises in the employment handbook?

5. Ohio and many states, beginning in the 1970s and picking up in the 1980s, found that employment handbooks granted employees rights in conflict with at-will status. Other states (NC, Texas) were less likely to make such findings, reasoning that an employee handbook was employer policy, not language of contract. Can you make an argument that an employment handbook is not an offer?

6. Craft a deposition question for Galgoczy that he could answer using one of the statements in paragraph [10]. Your professor may ask you to share this question in class.

E. Silence

Gary F. KASKISTO v. NORTH AM. EQUITABLE LIFE ASSURANCE CO. (1981)

District Court of Appeal of Florida, Third District

405 So.2d 248

BASKIN, Judge.

[¶1] Because we find no evidence of appellant's acceptance of the changed contract terms submitted by appellee, we reverse the final judgment entered by the trial court. The court's announcement that its decision resulted from appellant's failure to object to the altered mortgage interest rate conflicts with the principle of law that silence does not constitute an acceptance of an offer unless a duty to speak has arisen from a past relationship of the parties, their previous dealings, or other circumstances. 17 C.J.S., Contracts, s 41(e) (1963). Appellant neither initialed the changes in the contract nor performed any act which might operate as an estoppel. *See Mayer v. First National Co. of Sarasota*, 99 Fla. 173, 125 So.2d 909 (Fla. 1930). The requirement that acceptance of an offer to sell realty must be absolute and unconditional, *Koplin v. Bennett*, 155 So.2d 568 (Fla. 1st DCA 1963), was not met.

[¶2] Reversed and remanded for further proceedings consistent with this opinion.

Question: Under unjust enrichment doctrine, a person who embarks on a contract performance before the other party has assented or given the performing party some reasonable expectation of compensation is called a what?

Note: *Kaskisto* states the general rule clearly. The question for the succeeding cases in this section is "when does a duty to speak arise?"

The next case is a sale of goods case, but it follows the rule in *Kaskisto*.

James R. LEE v. SHELLER GLOBE CORP. v. STAUFFER CHEMICAL COMPANY and Brent Chemical Corporation (1986)

United States District Court, S.D. Mississippi

661 F. Supp. 6

MEMORANDUM OPINION

GEX, District Judge.

[¶1] This matter is before the Court on the cross motions for summary judgment filed by Third Party Plaintiff Sheller Globe Corporation ("Sheller") and Third Party Defendant Stauffer Chemical Company ("Stauffer"). * * * *

[¶2] Plaintiff James Lee, while employed as a sales representative for Stauffer, was injured July 7, 1979, on the premises of Sheller's automotive plant then located in Kosciusko, Mississippi. Plaintiff was present in the plant in connection with the sale of certain chemicals from Stauffer to Sheller as evidenced by Sheller's purchase order numbered K 06099 issued June 20, 1979. Lee filed this action against Sheller to recover damages for personal injuries allegedly sustained in the accident upon which his complaint is based. Sheller filed a third party complaint seeking contractual indemnity from Stauffer based upon the pertinent terms of the purchase order. The reverse side of the purchase order contained the following provision:

> INDEMNIFICATION In the event that Seller is required to enter the premises owned, leased, occupied by, or under the control of Buyer during the performance of services hereunder or during delivery of articles herein contemplated, Seller agrees to indemnify and save harmless Buyer, officers, employees and agents from all costs, loss, expense, damages, claims, suits or liability resulting from injury, including death, to person or property damage arising from or in any manner growing out of the act or omission of Seller, its subcontractors, agents, or their respective employees, and Seller agrees to indemnify Buyer with respect to any claim or demand for damage for personal injury or death of, or property damage sustained by, Seller, its subcontractors, agents or their respective employees, which arise from any cause, including negligence of Buyer, its agents, subcontractors or, their respective employees.

Sheller's urging of its motion is premised upon a finding that the subject chemical sale constituted a contract for the sale of goods pursuant to the provisions of the Mississippi Uniform Commercial Code. * * * *

[¶3] The Court has considered the briefs and authorities submitted by the parties and is of the opinion that Sheller's premise is well founded. A contract was established by virtue of Sheller's purchase order (the offer) and Stauffer's shipment of the ordered goods (the acceptance). Miss. Code Ann. Sections 75-2-204, 75-2-206 (1972). Accordingly, the terms of the purchase order created the parties' respective obligations.

Question: How would you define the circumstances under which this duty arose?

JOSEPHINE AND ANTHONY CORP. et al. v. Norman P. HORWITZ

Supreme Court, Appellate Division, Second Department (1977)

396 N.Y.S.2d 53

MEMORANDUM BY THE COURT

[¶1] In an action inter alia to declare (1) that a certain stipulation is of no force and effect and (2) the amount due plaintiffs from defendant, plaintiffs appeal from a judgment of the Supreme Court, Kings County, dated March 16, 1976, which after a trial, is in favor of plaintiff Josephine Presti and against defendant, upon the court's declaration that the stipulation was in full force and effect and fixation of the amount due from defendant.

[¶2] Judgment affirmed, with costs.

[¶3] During the period from October, 1964 to March, 1965 the defendant borrowed from the plaintiff corporation. Part payment was made, resulting, as of May 18, 1971, in a balance due of $8,950. On that date the defendant offered plaintiffs a "stipulation", with terms, although no action was pending. The plaintiffs did not sign the stipulation as tendered, but instead modified it. By his attorney's letter, the defendant rejected the agreement as modified and renewed the original offer. A check for $75, the first payment, was enclosed with that letter. The plaintiffs never replied, but did cash that check and the subsequent 18 checks tendered pursuant to the renewed offer.

[¶4] Defendant ceased paying on May 3, 1973. Plaintiffs commenced this action, contending that no agreement had ever been entered into and seeking the remaining principal due, with interest from October, 1964. It is our opinion that the parties entered into a binding agreement, and, therefore, that interest should be computed from the date of default on that agreement.

[¶5] Plaintiffs' return of the modified agreement constituted a counteroffer. The defendant's attorney's letter rejected the counteroffer. However, that same letter also contained a renewal of the original offer. While silence, of itself, is not an acceptance absent a duty to speak, "(a) duty to speak is imperative as a matter of law where conduct, accompanied by silence, would be deceptive and beguiling" (*Brennan v. National Equit. Inv. Co.*, 247 N.Y. 486, 490, 160 N.E. 924, 925). When the plaintiffs cashed the checks, an acceptance of the renewed offer was indicated by their conduct.

Question: How would you define this circumstance in which a duty to speak arose? Is this case different from *Lee v. Sheller Globe Corp*.?

AUSTIN v. BURGE

Kansas City Court of Appeals, Missouri (1911)

137 S.W. 618

ELLISON, J.

[¶1] This action was brought on an account for the subscription price of a newspaper. The judgment in the trial court was for the defendant. It appears that plaintiff was publisher of a newspaper in Butler, Mo., and that defendant's father-in-law subscribed for the paper, to be sent to defendant for two years, and that the father-in-law paid for it for that time. It was then continued to be sent to defendant, through the mail, for several years more. On two occasions defendant paid a bill presented for the subscription price, but each time directed it to be stopped. Plaintiff denies the order to stop, but for the purpose of the case we shall assume that defendant is correct. He testified that, notwithstanding the order to stop it, it was continued to be sent to him, and he continued to receive and read it, until finally he removed to another state.

[¶2] We have not been cited to a case in this state involving the liability of a person who, though not having subscribed for a newspaper, continues to accept it by receiving it through the mail. There are, however, certain well-understood principles in the law of contracts that ought to solve the question. It is certain that one cannot be forced into contractual relations with another and that therefore he cannot, against his will, be made the debtor of a newspaper publisher. But it is equally certain that he may cause contractual relations to arise by necessary implication from his conduct. The law in respect to contractual indebtedness for a newspaper is not different from that relating to other things which have not been made the subject of an express agreement. Thus one may not have ordered supplies for his table, or other household necessities, yet if he continue to receive and use them, under circumstances where he had no right to suppose they were a gratuity, he will be held to have agreed, by implication, to pay their value. In this case defendant admits that, notwithstanding he ordered the paper discontinued at the time when he paid a bill for it, yet plaintiff continued to send it, and he continued to take it from the post office to his home. This was an acceptance and use of the property, and, there being no pretense that a gratuity was intended, an obligation arose to pay for it.

[¶3] A case quite applicable to the facts here involved arose in *Fogg v. Atheneum*, 44 N. H. 115, 82 Am. Dec. 191. There the Independent Democrat newspaper was forwarded weekly by mail to the defendant from May 1, 1847, to May 1, 1849, when a bill was presented, which defendant objected to paying on the ground of not having subscribed. Payment was, however, finally made, and directions given to discontinue. The paper changed ownership, and the order to stop it was not known to the new proprietors for a year; but, after being notified of the order, they nevertheless continued to send it to defendant until 1860, a period of 11 years, and defendant continued to receive it through the post office. Payment was several times demanded during this time, but refused on the ground that there was no subscription. The court said that: "During this period of time the defendants were occasionally requested, by the plaintiff's agent, to pay their bill. The answer was, by the defendants, 'We are not subscribers to your newspaper.' But the evidence is the defendants used or kept the plaintiff's * * * newspapers, and never offered to return a number, as they reasonably might have done, if they would have avoided the liability to pay for them. Nor did they ever

decline to take the newspapers from the post office." The defendant was held to have accepted the papers, and to have become liable for the subscription price by implication of law.

[¶4] In *Ward v. Powell*, 3 Har. (Del.) 379, it was decided that an implied agreement to pay for a newspaper or periodical arose by the continued taking and accepting the paper from the post office, and that "if a party, without subscribing to a paper, declines taking it out of the post office, he cannot become liable to pay for it; and a subscriber may cease to be such at the end of the year, by refusing to take the papers from the post office, and returning them to the editor as notice of such determination." In *Goodland v. Le Clair*, 78 Wis. 176, 47 N.W. 268, it was held that if a person receives a paper from the post office for a year, without refusing or returning it, he was liable for the year's subscription. And a like obligation was held to arise in the case of *Weatherby v. Bonham*, 5 C. & P. 228.

[¶5] The preparation and publication of a newspaper involves much mental and physical labor, as well as an outlay of money. One who accepts the paper, by continuously taking it from the post office, receives a benefit and pleasure arising from such labor and expenditure as fully as if he had appropriated any other product of another's labor, and by such act he must be held liable for the subscription price. On the defendant's own evidence, plaintiff should have recovered.

[¶6] The judgment will therefore be reversed, and the cause remanded.

All concur.

Questions:

1. Is Burge unjustly enriched?

2. Consider the following code provision:

> 39 U.S.C. § 3009. Mailing of unordered merchandise
>
> (a) Except for (1) free samples clearly and conspicuously marked as such, and (2) merchandise mailed by a charitable organization soliciting contributions, the mailing of unordered merchandise or of communications prohibited by subsection (c) of this section constitutes an unfair method of competition and an unfair trade practice in violation of section 45(a)(1) of title 15.
>
> (b) Any merchandise mailed in violation of subsection (a) of this section, or within the exceptions contained therein, may be treated as a gift by the recipient, who shall have the right to retain, use, discard, or dispose of it in any manner he sees fit without any obligation whatsoever to the sender. All such merchandise shall have attached to it a clear and conspicuous statement informing the recipient that he may treat the merchandise as a gift

> to him and has the right to retain, use, discard, or dispose of it in any manner he sees fit without any obligation whatsoever to the sender.
>
> (c) No mailer of any merchandise mailed in violation of subsection (a) of this section, or within the exceptions contained therein, shall mail to any recipient of such merchandise a bill for such merchandise or any dunning communications.
>
> (d) For the purposes of this section, "unordered merchandise" means merchandise mailed without the prior expressed request or consent of the recipient.

Would this section, if applied to the facts of *Austin v. Burge*, reverse it?

3. Here's a case somewhat similar to *Austin*: Statoil and Hydro were each contacted by a broker, Gasteam, for two, separate transactions. In the first, Hydro was to sell. In the second, Hydro was to buy more that it was to sell in the first deal. Gasteam sent out confirming memoranda faxes. The faxes reported the seller, buyer, product, quality, quantity, delivery, price, payment, title, risk, distribution, confidentiality, and commission. The faxes began by stating, "Further to recent conversations, we are pleased to confirm the following transaction ...." The faxes did not purport to require a response, and Hydro never responded. Hydro only corresponded with Gasteam about these transactions; no one from Hydro ever spoke with anyone from Statoil. However, Gasteam brokered 72 transactions for Hydro prior to these two and just after, and in none of them did Hydro ever require or give any additional documents or signatures or evidence of assent. Moreover, Hydro performed all the others. When time came for delivery on these two deals, though, Hydro refused to perform. Did Hydro assent? *Den Norske Stats Oljeselskap, AS v. Hydrocarbon Processing, Inc.*, 992 F. Supp. 913 (S.D. Tex. 1998) (yes). What language from *Kaskisto* best applies to reach this result?

A few of these cases are sales of goods, but the UCC Article 2 § 2-204(1) says, "A contract for sale of goods may be made in any manner sufficient to show agreement, including conduct by both parties which recognizes the existence of such a contract." This is the same rule. Are *Lee* and *Austin* consistent with the statute?

Note on Battle of the Forms

Commerce moves very fast, and business people are always coming up with new ways to buy and sell. In the past, most businesses took order forms and mailed products in response, with invoices requesting payment.

Buyers and sellers tried to manipulate the rules of offer and acceptance by controlling the contents of order forms and invoices. For instance, if a buyer sent an order form to a seller and the seller merely shipped in response, that act under *Kaskisto* and *Sheller Globe* probably accepted the terms of order form. Can you see why?

To prevent that response from constituting acceptance, sellers began putting different and additional terms in the invoice. This prevented the shipment and invoice from being an acceptance. Why? Instead of being

an acceptance, the shipment and invoice was something else: what? If the buyer simply paid after receiving such an invoice, what would be the significance of that payment for contract law?

To supersede this "battle of the forms," the UCC Article 2 includes a section, 2-207, that tries to let parties ignore the battling, different or additional terms in the forms they send each other. The section is extremely complicated and perhaps was not well-drafted, but the law under it is relatively settled now. We bring it up here because the problem that prompted 2-207's drafting is a classical example of the offer and acceptance rules in action, and a similar thing could happen in the service industries where 2-207 does not apply.

Other than that, you can look forward to studying 2-207 in another setting.

F. Web Contracts—Contracting Online

Test Case: The Uber Cases

"Uber provides a ride-sharing service . . . for a fee. Uber licenses the Uber mobile application (the "Uber App") to the public so that users may request transportation services from independent third party providers in the users' local area." To use the app, Uber "users must first register with Uber by creating an account" through the app itself or through Uber's website.

Uber's online registration process as a contract-formation event was at issue in three fairly recent, important cases. In two cases, the users downloaded the app and created an account through the app. In the latest case, the user registered on the website.

The users all had different disputes with Uber. In *Meyer v. Uber Technologies, Inc.*, 868 F.3d 66 (2d Cir. 2017), the plaintiff on behalf of a class of users sued Uber's CEO Travis Kalanick for price-fixing. The trial court granted Kalanick's motion to bring Uber into the litigation as a necessary party.

In *Cullinane v. Uber Technologies, Inc.*, 893 F.3d 53 (1st Cir. 2018), the plaintiffs on behalf of a class of users sued Uber for charging unnecessary fees. The facts in the first paragraph above were quoted and paraphrased from *Cullinane*.

In *Theodore v. Uber Technologies, Inc.*, 442 F. Supp.3d 433 (D. Mass. 2020), the wheel-chair-bound plaintiff sued for injunctive relief because Uber failed "to provide wheelchair accessible vehicles in the suburb where Mr. Theodore resides.

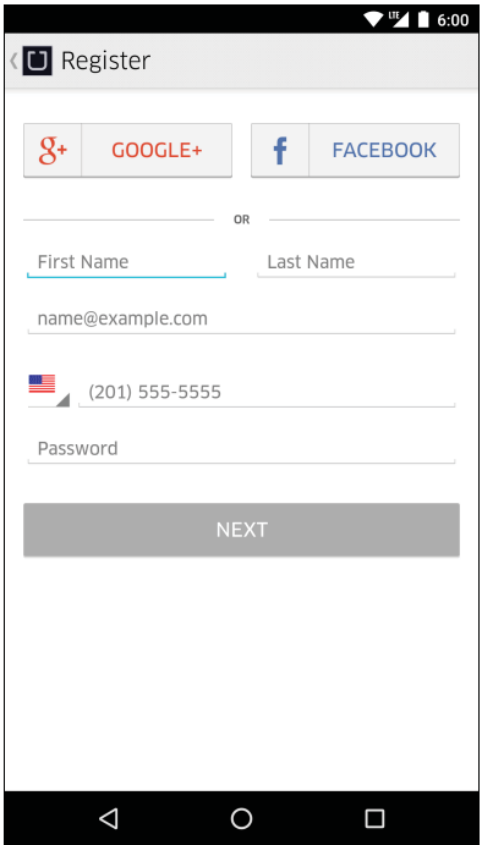
In each case, Uber moved to compel arbitration, and the court had to decide whether the plaintiffs were bound by the arbitration clause in Uber's terms of service.

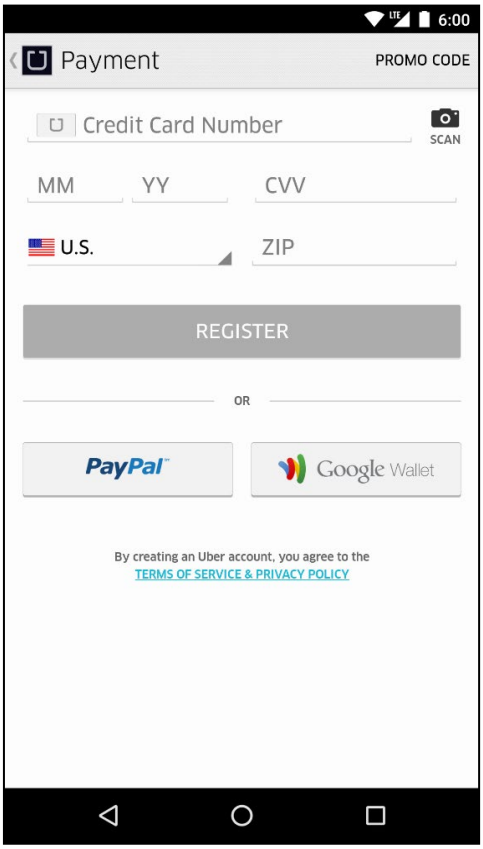
Uber's sign-up process was quite similar for all of these plaintiffs.

1. Meyer

Here is the way the *Meyer* court described the sign-up process:

> [¶1] The first screen, at which the user arrives after downloading the application and clicking a button marked “Register,” is labeled “Register” and includes fields for the user to enter his or her name, email address, phone number, and a password (the “Registration Screen”). The Registration Screen also offers the user the option to register via a Google+ or Facebook account. According to Uber's records, Meyer did not sign up using either Google+ or Facebook and would have had to enter manually his personal information. [Meyer’s phone screen was 5.1 inches, measured diagonally, and no images here are rendered at actual size.]





> [¶2] After completing the information on the Registration Screen and clicking “Next,” the user advances to a second screen labeled “Payment” (the “Payment Screen”), on which the user can enter credit card details or elect to make payments using PayPal or Google Wallet, third-party payment services. According to Uber’s records, Meyer entered his credit card information to pay for rides. To complete the process, the prospective user must click the button marked “REGISTER” in the middle of the Payment Screen.

[¶3] Below the input fields and buttons on the Payment Screen is black text advising users that "[b]y creating an Uber account, you agree to the TERMS OF SERVICE & PRIVACY POLICY." * * * * The capitalized phrase, which is bright blue and underlined, was a hyperlink that, when clicked, took the user to a third screen containing a button that, in turn, when clicked, would then display the current version of both Uber's Terms of Service and Privacy Policy. Meyer recalls entering his contact information and credit card details before registering, but does not recall seeing or following the hyperlink to the Terms and Conditions. He declares that he did not read the Terms and Conditions, including the arbitration provision.

[¶4] When Meyer registered for an account, the Terms of Service contained the following mandatory arbitration clause [and *Cullinane* and *Theodore* appear to have had equivalents]:

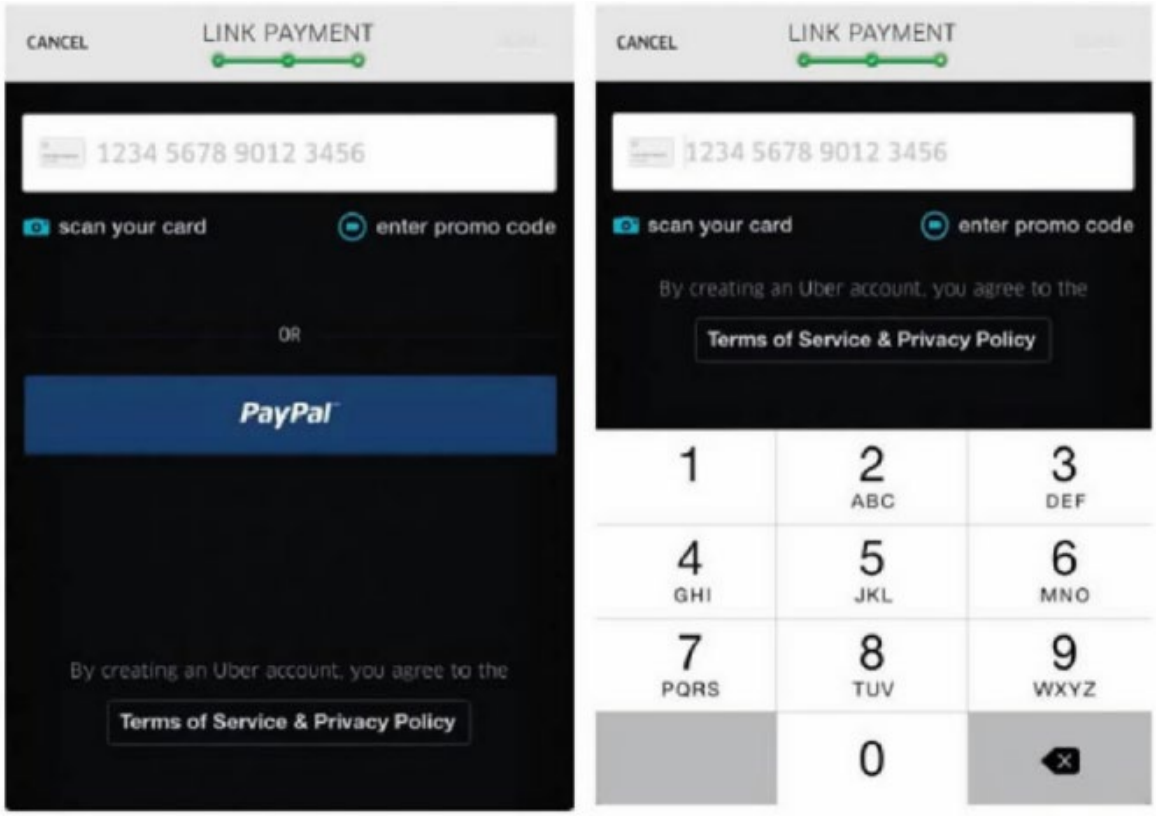
> Dispute Resolution
>
> You and Company agree that any dispute, claim or controversy arising out of or relating to this Agreement or the breach, termination, enforcement, interpretation or validity thereof or the use of the Service or Application (collectively, "Disputes") will be settled by binding arbitration, except that each party retains the right to bring an individual action in small claims court and the right to seek injunctive or other equitable relief in a court of competent jurisdiction to prevent the actual or threatened infringement, misappropriation or violation of a party's copyrights, trademarks, trade secrets, patents or other intellectual property rights. You acknowledge and agree that you and Company are each waiving the right to a trial by jury or to participate as a plaintiff or class User in any purported class action or representative proceeding.
>
> Further, unless both you and Company otherwise agree in writing, the arbitrator may not consolidate more than one person's claims, and may not otherwise preside over any form of any class or representative proceeding. If this specific paragraph is held unenforceable, then the entirety of this "Dispute Resolution" section will be deemed void. Except as provided in the preceding sentence, this "Dispute Resolution" section will survive any termination of this Agreement.

Appellants' App. at 111-12. The Terms of Service further provided that the American Arbitration Association ("AAA") would hear any dispute, and that the AAA Commercial Arbitration Rules would govern any arbitration proceeding.

2. Cullinane

The *Cullinane* process was slightly different. The first screen was entitled "Create an Account" and required an email address, mobile phone number, and password. A second screen entitled "Create a Profile" required first and last name and a picture. The third screen said either "Link Card" or "Link Payment" and, like the second screen in *Meyer*, asked the user to enter payment information.

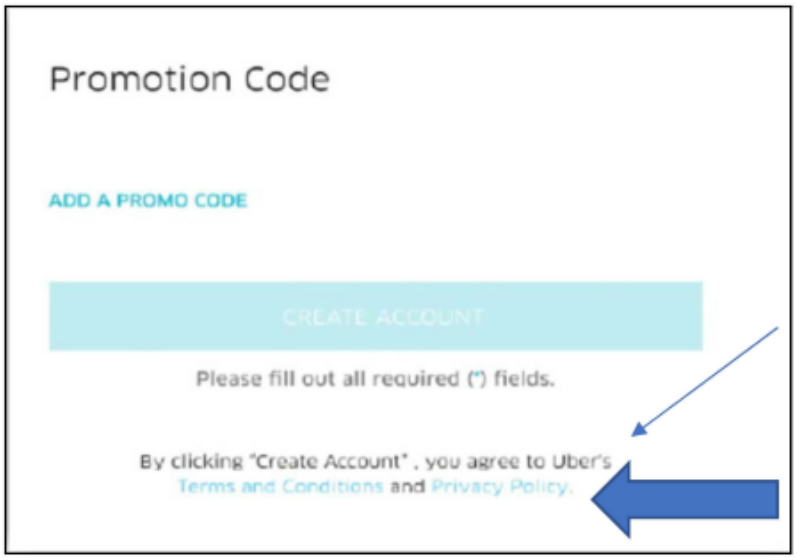
The third screen looked like one of the following. Earlier users only saw something like the right screen, but after Uber added a PayPal option, users were taken to the left screen first; if they chose credit card, then they saw something like the right screen. Uber claimed that the rectangular box around its Terms of Service & Privacy Policy was a clickable link. After payment information was entered, a “Done” button in the upper right corner became visible and operable.



3. Mr. Theodore

3.

Theodore’s case is a little different because he never registered through the app. In 2016, he “created an account on Uber’s website.” The website’s screen (below) looked similar to that from *Meyer* and *Cullinane* with regard to the terms and conditions; other information on those pages in the app was, on the website, entered on prior screens, however.



After registering, Mr. Theodore could not find wheelchair accessible vehicles through the app and never used Uber's service.

4. The Dispute

In none of these cases was the user required to click on the Terms of Service link in order to complete the registration process. Each could (and did) register without clicking on the link. The question the court addressed was whether the plaintiffs—users—had agreed to the arbitration agreements.

This issue is probably (technically) about Uber's offer. It's safe to say that no human on Uber's side exercised any thought about whether to accept a user's registration after the user was finished registering. Thus, if a contract formed, the offer was probably Uber's. Surely what Uber proposed was an exchange to which it had already assented, on condition of a valid payment method. But we place the issue here at the end of the chapter on acceptance because the cases addressed both offer and acceptance, as you will see.

5. The Law

All three courts used substantially the same law, and all cite ultimately to *Specht v. Netscape Communications Corp*. 306 F.3d 17 (2d Cir. 2002), an opinion by then-Judge Sotomayor that has become the foundational precedent in the area. *Cullinane* and *Theodore* cite also to *Meyer*, and *Theodore* cites also to *Cullinane*. The cases follow in line.

Here is the recitation of law from ***Cullinane*** with most citations and other extraneous verbiage removed:

> [A] It is well settled that "arbitration is a matter of contract." "When deciding whether the parties agreed to arbitrate a certain matter (including arbitrability), courts generally . . . should apply ordinary state-law principles that govern the formation of contracts."
>
> [B] [I]n *Ajemian v. Yahoo!, Inc*., 83 Mass. App. Ct. 565, 987 N.E.2d 604, 611-15 (2013), the Massachusetts Appeals Court addressed the enforceability of forum selection and limitation clauses within an online contract and that court's decision is "trustworthy data for

ascertaining state law." While the clauses at issue in *Ajemian* did not include an arbitration clause, "the essential question presented was the same: what level of notice and assent is required in order for a court to enforce an online adhesion contract?" Consequently, we apply the principles stated in *Ajemian*.

[C] In *Ajemian*, the Appeals Court determined that there was "no reason to apply different legal principles [of contract enforcement] simply because a forum selection clause . . . is contained in an online contract." Therefore, "such clauses will be enforced provided they have been reasonably communicated and accepted." The Appeals Court explained that "[r]easonably conspicuous notice of the existence of contract terms and unambiguous manifestation of assent to those terms by consumers are essential if electronic bargaining is to have integrity and credibility." *Id*. at 612 ([ultimately] quoting *Specht v. Netscape Commc'ns Corp*., 306 F.3d 17, 35 (2d Cir. 2002)). With this in mind, the Appeals Court set forth a two-step inquiry for the enforceability of forum selection clauses in online agreements. The first inquiry is whether the contract terms were "reasonably communicated to the plaintiffs." The second is whether the record shows that those terms were "accepted and, if so, the manner of acceptance." The court further clarified that the burden to show that the terms were reasonably communicated and accepted lies on the party seeking to enforce the forum selection clause.

Compare those statements with ***Meyer*'s**:

[A] Where there is no evidence that the offeree had actual notice of the terms of the agreement, the offeree will still be bound by the agreement if a reasonably prudent user would be on inquiry notice of the terms.

[B] Whether a reasonably prudent user would be on inquiry notice turns on the "[c]larity and conspicuousness of arbitration terms," *Specht*, 306 F.3d at 30; in the context of web-based contracts, as discussed further below, clarity and conspicuousness are a function of the design and content of the relevant interface.

[C] Thus, only if the undisputed facts establish that there is "[r]easonably conspicuous notice of the existence of contract terms and unambiguous manifestation of assent to those terms" will we find that a contract has been formed. See *Specht*, 306 F.3d at 35. * * * *

[D] "Courts around the country have recognized that [an] electronic 'click' can suffice to signify the acceptance of a contract," and that "[t]here is nothing automatically offensive about such agreements, as long as the layout and language of the site give the user reasonable notice that a click will manifest assent to an agreement."

[E] With these principles in mind, one way in which we have previously distinguished web-based contracts is the manner in which the user manifests assent—namely, "clickwrap" (or "click-through") agreements, which require users to click an "I agree" box after being presented with a list of terms and conditions of use, or "browsewrap" agreements, which generally post terms and conditions on a website via a hyperlink at the bottom of the

> screen. Courts routinely uphold clickwrap agreements for the principal reason that the user has affirmatively assented to the terms of agreement by clicking “I agree.” Browsewrap agreements, on the other hand, do not require the user to expressly assent. “Because no affirmative action is required by the website user to agree to the terms of a contract other than his or her use of the website, the determination of the validity of the browsewrap contract depends on whether the user has actual or constructive knowledge of a website’s terms and conditions.”
>
> [F] Of course, there are infinite ways to design a website or smartphone application, and not all interfaces fit neatly into the clickwrap or browsewrap categories. Some online agreements require the user to scroll through the terms before the user can indicate his or her assent by clicking “I agree.” [Scrollthrough or scrollwrap?] Other agreements notify the user of the existence of the website’s terms of use and, instead of providing an “I agree” button, advise the user that he or she is agreeing to the terms of service when registering or signing up. * * * *
>
> [G] Classification of web-based contracts alone, however, does not resolve the notice inquiry. Insofar as it turns on the reasonableness of notice, the enforceability of a web-based agreement is clearly a fact-intensive inquiry. Nonetheless, on a motion to compel arbitration, we may determine that an agreement to arbitrate exists where the notice of the arbitration provision was reasonably conspicuous and manifestation of assent unambiguous as a matter of law. See *Specht*, 306 F.3d at 28.

These rules from *Meyer* might have a slightly different focus, but is it hard to predict what difference will occur in actual application merely by reading the rules from the two cases?

6. The Application

Nevertheless, the courts differed in application of the test. The ***Meyer*** court held that the plaintiff “was on inquiry notice of the arbitration provision by virtue of the hyperlink . . . and, thus, manifested his assent to the agreement by clicking ‘Register.’” It reasoned that (i) normal people know how to use a smartphone and can recognize a link, (ii) this hyperlink was in blue like any normal hyperlink would be, and (iii) the sign-up page was uncluttered and clear enough. The notice was “spatially and temporally coupled” with the button designated for assent. The court also stressed the “transactional context”: “Meyer located and downloaded the Uber App, signed up for an account, and entered his credit card information with the intention of entering into a forward-looking relationship with Uber[,] . . . one that would require some terms and conditions.”

Cullinane, on the other hand, found “that the Plaintiffs were not reasonably notified of the terms of the Agreement.” The highlights include these:

> [D] We note at the outset that Uber chose not to use a common method of conspicuously informing users of the existence and location of terms and conditions: requiring users to click a box stating that they agree to a set of terms, often provided by hyperlink, before

> continuing to the next screen. Instead, Uber chose to rely on simply displaying a notice of deemed acquiescence and a link to the terms.
>
> [E] Uber's "Terms of Service & Privacy Policy" hyperlink did not have the common appearance of a hyperlink. While not all hyperlinks need to have the same characteristics, they are "commonly blue and underlined." [The court cited *Meyer* after this sentence.]
>
> [F] Along with the "Terms of Service & Privacy Policy" hyperlink, the "Link Card" and "Link Payment" screens contained other terms displayed with similar features. For example, the terms "scan your card" and "enter promo code" were also written in bold and with a similarly sized font as the hyperlink. Both versions of the third screen also included the words "CANCEL" and "DONE,"—the latter being barely visible until the user had entered the required payment information—in all capital letters and dark colored font. Meanwhile, the top of the screens featured the terms "Link Card" or "Link Payment" in large capital letters and dark colored font. These had the largest-sized font in both versions of the third screen.
>
> [G] Uber's "Terms of Service & Privacy Policy" hyperlink was even less conspicuous on the "Link Payment" screen. The inclusion of the additional payment option and the placement of a large blue PayPal button in the middle of the screen were more attention-grabbing and displaced the hyperlink to the bottom of the screen.

This is just a small portion of the analyses from *Cullinane* and *Meyer*, but you can get what the courts are doing: parsing through the website design to argue whether the terms and conditions link was conspicuous—reasonably communicated.

Ah, but ***Theodore*** included the terms and conditions link in blue on a white background, just as we saw in *Meyer*! The *Theodore* court noted the similarity to *Meyer* but also reasoned that:

> some of the other terms on the page were still in the same color as the hyperlink, including "enter promo code," and the links to the "Terms and Conditions" and "Privacy Policy" were still not the largest text on the screen. The hyperlinks also continued to appear without any underlining. Finally, as before, the Terms and Conditions were linked at the bottom of the screen and did not require an affirmative acknowledgment from the prospective user that he or she was agreeing to be bound by the Terms and Conditions or the Privacy Policy by creating an Uber account.

The court also noted that it was bound by *Cullinane* (D. Mass is within the 1st Cir.). One could also almost hear the court whisper "and not bound by *Meyer*." At any rate, the *Theodore* court refused to order arbitration, on grounds that no agreement to arbitrate existed.

Here is an assignment for class:

1) Taking the facts of *Meyer*, choose what result you think a court should reach—agreement or not, then construct your legal argument (a) using the best standards used by these courts, to the extent you can discern them, and (b) naming at least five facts, from most persuasive to least persuasive, in favor of your

result. Your professor may ask you for your legal argument, and may poll the class to see what facts each of you chose.

2) Given the state of the law, how would you recommend that clients design their websites? Please name the key design feature/s and give reasons.

Questions:

1. The *Meyer* court held that Meyer also had to arbitrate against Kalanick:

> Although Kalanick is not a party to the Terms and Conditions between Uber and Meyer, he is nonetheless protected by them. “Courts in this and other circuits consistently have held that employees or disclosed agents of an entity that is a party to an arbitration agreement are protected by that agreement.”

Op. at 39 n.11. The law reasons that these claims, too, are within the language of the arbitration clause. What do you think? The courts have also cited in support the federal policy in favor of arbitration. Whether Kalanick himself, a non-party, can claim the right to arbitrate is the question, though. *Roby v. Corp. of Lloyd’s*, 996 F.2d 1353 (2d Cir. 1993), reasoned that employees and agents are intended beneficiaries of the arbitration clauses. (The doctrine of third-party beneficiaries is a topic addressed in the last chapter of this casebook.) How hard would it be to escape arbitration with an entity if you could force into court all the people who acted on the entity’s behalf?

2. Binding Meyer to the arbitration agreement in this case is most like which other case we have studied? *Austin v. Burge*? *Lee v. Sheller Globe*? *Lucy v. Zehmer*?

Chapter 9. Definiteness

A. The General Principle

ACADEMY CHICAGO PUBLISHERS v. Mary W. CHEEVER

Supreme Court of Illinois (1991)

578 N.E.2d 981

Justice HEIPLE delivered the opinion of the court:

[¶1] This is a suit for declaratory judgment. It arose out of an agreement between the widow of the widely published author, John Cheever, and Academy Chicago Publishers. Contact between the parties began in 1987 when the publisher approached Mrs. Cheever about the possibility of publishing a collection of Mr. Cheever's short stories which, though previously published, had never been collected into a single anthology. In August of that year, a publishing agreement was signed which provided, in pertinent part:

> "Agreement made this 15th day of August 1987, between Academy Chicago Publishers or any affiliated entity or imprint (hereinafter referred to as the Publisher) and Mary W. Cheever and Franklin H. Dennis of the USA (hereinafter referred to as Author).
>
> Whereas the parties are desirous of publishing and having published a certain work or works, tentatively titled The Uncollected Stories of John Cheever (hereinafter referred to as the Work):
>
> * * * *
>
> 2. The Author will deliver to the Publisher on a mutually agreeable date one copy of the manuscript of the Work as finally arranged by the editor and satisfactory to the Publisher in form and content.
>
> * * * *
>
> 5. Within a reasonable time and a mutually agreeable date after delivery of the final revised manuscript, the Publisher will publish the Work at its own expense, in such style and manner and at such price as it deems best, and will keep the Work in print as long as it deems it expedient; but it will not be responsible for delays caused by circumstances beyond its control."

[¶2] Academy and its editor, Franklin Dennis, assumed the task of locating and procuring the uncollected stories and delivering them to Mrs. Cheever. Mrs. Cheever and Mr. Dennis received partial advances for manuscript preparation. By the end of 1987, Academy had located and delivered more than

60 uncollected stories to Mrs. Cheever. Shortly thereafter, Mrs. Cheever informed Academy in writing that she objected to the publication of the book and attempted to return her advance.

[¶3] Academy filed suit in the circuit court of Cook County in February 1988, seeking a declaratory judgment: (1) granting Academy the exclusive right to publish the tentatively titled, "The Uncollected Stories of John Cheever"; (2) designating Franklin Dennis as the book's editor; and (3) obligating Mrs. Cheever to deliver the manuscript from which the work was to be published. The trial court entered an order declaring, inter alia: (1) that the publishing agreement executed by the parties was valid and enforceable; (2) that Mrs. Cheever was entitled to select the short stories to be included in the manuscript for publication; (3) that Mrs. Cheever would comply with her obligations of good faith and fair dealing if she delivered a manuscript including at least 10 to 15 stories totaling at least 140 pages; (4) Academy controlled the design and format of the work to be published, but control must be exercised in cooperation with Mrs. Cheever.

[¶4] Academy appealed the trial court's order, challenging particularly the declaration regarding the minimum story and page numbers for Mrs. Cheever's compliance with the publishing agreement, and the declaration that Academy must consult with defendant on all matters of publication of the manuscript.

[¶5] The appellate court affirmed the decision of the trial court with respect to the validity and enforceability of the publishing agreement and the minimum story and page number requirements for Mrs. Cheever's compliance with same. The appellate court reversed the trial court's declaration regarding control of publication, stating that the trial court erred in considering extrinsic evidence to interpret the agreement regarding control of the publication, given the explicit language of the agreement granting exclusive control to Academy. (200 Ill.App.3d 677, 146 Ill. Dec. 386, 558 N.E.2d 349.) Appeal is taken in this court pursuant to Supreme Court Rule 315(a) (134 Ill.2d R. 315(a)).

[¶6] The parties raise several issues on appeal; this matter, however, is one of contract and we confine our discussion to the issue of the validity and enforceability of the publishing agreement.

[¶7] While the trial court and the appellate court agreed that the publishing agreement constitutes a valid and enforceable contract, we cannot concur. The principles of contract state that in order for a valid contract to be formed, an "offer must be so definite as to its material terms or require such definite terms in the acceptance that the promises and performances to be rendered by each party are reasonably certain." (1 Williston, Contracts §§ 38 through 48 (3d ed. 1957); 1 Corbin, Contracts §§ 95 through 100 (1963).) Although the parties may have had and manifested the intent to make a contract, if the content of their agreement is unduly uncertain and indefinite no contract is formed. 1 Williston § 37; 1 Corbin § 95.

[¶8] The pertinent language of this agreement lacks the definite and certain essential terms required for the formation of an enforceable contract. (*Midland Hotel Corp. v. Reuben H. Donnelley Corp*. (1987), 118 Ill.2d 306, 113 Ill. Dec. 252, 515 N.E.2d 61.) A contract "is sufficiently definite and certain to be enforceable if the court is enabled from the terms and provisions thereof, under proper rules of construction and applicable principles of equity, to ascertain what the parties have agreed to do." (*Morey v. Hoffman* (1957), 12 Ill.2d 125, 145 N.E.2d 644.) The provisions of the subject publishing agreement do not provide the court with a means of determining the intent of the parties.

[¶9] Trial testimony reveals that a major source of controversy between the parties is the length and content of the proposed book. The agreement sheds no light on the minimum or maximum number of stories or pages necessary for publication of the collection, nor is there any implicit language from which we can

glean the intentions of the parties with respect to this essential contract term. The publishing agreement is similarly silent with respect to who will decide which stories will be included in the collection. Other omissions, ambiguities, unresolved essential terms and illusory terms are: No date certain for delivery of the manuscript. No definition of the criteria which would render the manuscript satisfactory to the publisher either as to form or content. No date certain as to when publication will occur. No certainty as to style or manner in which the book will be published nor is there any indication as to the price at which such book will be sold, or the length of time publication shall continue, all of which terms are left to the sole discretion of the publisher.

[¶10] A contract may be enforced even though some contract terms may be missing or left to be agreed upon, but if the essential terms are so uncertain that there is no basis for deciding whether the agreement has been kept or broken, there is no contract. (*Champaign National Bank v. Landers Seed Co*. (1988), 165 Ill.App.3d 1090, 116 Ill. Dec. 742, 519 N.E.2d 957, Restatement (Second) of Contracts § 33 (1981).) Without setting forth adequate terms for compliance, the publishing agreement provides no basis for determining when breach has occurred, and, therefore, is not a valid and enforceable contract.

[¶11] An enforceable contract must include a meeting of the minds or mutual assent as to the terms of the contract. (*Midland Hotel*, 118 Ill.2d at 313, 113 Ill. Dec. 252, 515 N.E.2d 61.) It is not compelling that the parties share a subjective understanding as to the terms of the contract; the parties' conduct may indicate an agreement to the terms of same. (*Steinberg v. Chicago Medical School* (1977), 69 Ill.2d 320, 13 Ill. Dec. 699, 371 N.E.2d 634.) In the instant case, however, no mutual assent has been illustrated. The parties did not and do not share a common understanding of the essential terms of the publishing agreement.

[¶12] In rendering its judgment, the trial court supplied minimum terms for Mrs. Cheever's compliance, including story and page numbers. It is not uncommon for a court to supply a missing material term, as the reasonable conclusion often is that the parties intended that the term be supplied by implication. However, where the subject matter of the contract has not been decided upon and there is no standard available for reasonable implication, courts ordinarily refuse to supply the missing term. (1 Williston § 42; 1 Corbin § 100.) No suitable standard was available for the trial court to apply. It is our opinion that the trial court incorrectly supplied minimum compliance terms to the publishing agreement, as the agreement did not constitute a valid and enforceable contract to begin with. As noted above, the publishing agreement contains major unresolved uncertainties. It is not the role of the court to rewrite the contract and spell out essential elements not included therein.

[¶13] In light of our decision that there was no valid and enforceable contract between the parties, we need not address other issues raised on appeal. For the foregoing reasons, the decisions of the trial and appellate courts in this declaratory judgment action are reversed.

Reversed.

Justices CLARK and FREEMAN took no part in the consideration or decision of this opinion.

Questions:

1. Did a contract form here?

2. Why doesn't the court simply imply a reasonable term?

3. Did the parties agree to an exchange, here? Of what?

4. Why don't parties fill out terms? (The answer to this is not in the case, but please speculate as to what reasons might be.)

Note: The Amazon review of the book, Anita Miller, UNCOLLECTING CHEEVER: THE FAMILY OF JOHN CHEEVER VS. ACADEMY CHICAGO PUBLISHERS (2001), details the history of this litigation. Miller was part owner of the publishing house and wrote the book in order to grind her ax (she has an ax to grind). In the end, Academy did publish a small collection of 13 stories in 1994, which left 55 still uncollected. Why did the Cheevers (more than Mrs. Cheever were involved) back out? One Cheever child said, "I'm a greedy pig. All my life I've wanted to be rich. Haven't you?" Of course, that's not what they argued in court.

JOSEPH MARTIN, JR., DELICATESSEN, INC. v. Henry D. SCHUMACHER

Court of Appeals of New York (1981)

436 N.Y.S.2d 247

FUCHSBERG, Judge.

[¶1] This case raises an issue fundamental to the law of contracts. It calls upon us to review a decision of the Appellate Division, 70 A.D.2d 1, 419 N.Y.S.2d 558 which held that a realty lease's provision that the rent for a renewal period was "to be agreed upon" may be enforceable.

[¶2] The pertinent factual and procedural contexts in which the case reaches this court are uncomplicated. In 1973, the appellant, as landlord, leased a retail store to the respondent for a five-year term at a rent graduated upwards from $500 per month for the first year to $650 for the fifth. The renewal clause stated that "(t)he Tenant may renew this lease for an additional period of five years at annual rentals to be agreed upon; Tenant shall give Landlord thirty (30) days written notice, to be mailed certified mail, return receipt requested, of the intention to exercise such right." It is not disputed that the tenant gave timely notice of its desire to renew or that, once the landlord made it clear that he would do so only at a rental starting at $900 a month, the tenant engaged an appraiser who opined that a fair market rental value would be $545.41.

[¶3] The tenant thereupon commenced an action for specific performance in Supreme Court, Suffolk County, to compel the landlord to extend the lease for the additional term at the appraiser's figure or such other sum as the court would decide was reasonable. For his part, the landlord in due course brought a holdover proceeding in the local District Court to evict the tenant. On the landlord's motion for summary

judgment, the Supreme Court, holding that a bald agreement to agree on a future rental was unenforceable for uncertainty as a matter of law, dismissed the tenant's complaint. Concordantly, it denied as moot the tenant's motion to remove the District Court case to the Supreme Court and to consolidate the two suits.

[¶4] It was on appeal by the tenant from these orders that the Appellate Division, expressly overruling an established line of cases in the process, reinstated the tenant's complaint and granted consolidation. In so doing, it reasoned that "a renewal clause in a lease providing for future agreement on the rent to be paid during the renewal term is enforceable if it is established that the parties' intent was not to terminate in the event of a failure to agree". It went on to provide that, if the tenant met that burden, the trial court could proceed to set a "reasonable rent". One of the Justices, concurring, would have eliminated the first step and required the trial court to proceed directly to the fixation of the rent. Each party now appeals by leave of the Appellate Division pursuant to CPLR 5602 (subd. (b), par. 1). The tenant seeks only a modification adopting the concurrer's position. The question formally certified to us by the Appellate Division is simply whether its order was properly made. Since we conclude that the disposition at the Supreme Court was the correct one, our answer must be in the negative.

[¶5] We begin our analysis with the basic observation that, unless otherwise mandated by law (e. g., residential emergency rent control statutes), a contract is a private "ordering" in which a party binds himself to do, or not to do, a particular thing (*Fletcher v. Peck*, 6 Cranch (10 U.S.) 87, 136; 3 L. Ed. 162. Hart and Sachs, Legal Process, 147- 148 (1958)). This liberty is no right at all if it is not accompanied by freedom not to contract. The corollary is that, before one may secure redress in our courts because another has failed to honor a promise, it must appear that the promisee assented to the obligation in question.

[¶6] It also follows that, before the power of law can be invoked to enforce a promise, it must be sufficiently certain and specific so that what was promised can be ascertained. Otherwise, a court, in intervening, would be imposing its own conception of what the parties should or might have undertaken, rather than confining itself to the implementation of a bargain to which they have mutually committed themselves. Thus, definiteness as to material matters is of the very essence in contract law. Impenetrable vagueness and uncertainty will not do (1 Corbin, Contracts, s 95, p. 394; 6 Encyclopedia of New York Law, Contracts, s 301; Restatement, Contracts 2d, s 32, Comment a).

[¶7] Dictated by these principles, it is rightfully well settled in the common law of contracts in this State that a mere agreement to agree, in which a material term is left for future negotiations, is unenforceable (*Willmott v. Giarraputo*, 5 N.Y.2d 250, 253, 184 N.Y.S.2d 97, 157 N.E.2d 282; *Sourwine v. Truscott*, 17 Hun. 432, 434). [Editor Notes: Citations to other state court decisions in accord are omitted.] This is especially true of the amount to be paid for the sale or lease of real property (*see Forma v. Moran*, 273 App. Div. 818, 76 N.Y.S.2d 232; *Huber v. Ruby*, 187 Misc. 967, 969, 65 N.Y.S.2d 462, app. dsmd 271 App. Div. 927, 67 N.Y.S.2d 710, *see, generally*, 58 A.L.R. 3d 500, Validity and Enforceability of Provision for Renewal of Lease at Rental to be Fixed by Subsequent Agreement of the Parties). The rule applies all the more, and not the less, when, as here, the extraordinary remedy of specific performance is sought (11 Williston, Contracts (Jaeger 3d ed.), s 1424; Pomeroy, Equity Jurisprudence, s 1405).

[¶8] This is not to say that the requirement for definiteness in the case before us now could only have been met by explicit expression of the rent to be paid. The concern is with substance, not form. It certainly would have sufficed, for instance, if a methodology for determining the rent was to be found within the four corners of the lease, for a rent so arrived at would have been the end product of agreement between the parties themselves. Nor would the agreement have failed for indefiniteness because it invited recourse to

an objective extrinsic event, condition or standard on which the amount was made to depend. All of these, inter alia, would have come within the embrace of the maxim that what can be made certain is certain (9 Coke, 47a). (*Cf. Backer Mgt. Corp. v. Acme Quilting Co*., 46 N.Y.2d 211, 219, 413 N.Y.S.2d 135, 385 N.E.2d 1062 (escalation of rent keyed to building employees' future wage increases); *City of Hope v. Fisk Bldg. Assoc*., 63 A.D.2d 946, 406 N.Y.S.2d 472 (rental increase to be adjusted for upward movement in US Consumer Price Index); *see, generally*, 87 A.L.R. 3d 986; Lease Provisions Providing for Rent Adjustment Based on Event or Formula Outside Control of Parties.)

[¶9] But the renewal clause here in fact contains no such ingredients. Its unrevealing, unamplified language speaks to no more than "annual rentals to be agreed upon". Its simple words leave no room for legal construction or resolution of ambiguity. Neither tenant nor landlord is bound to any formula. There is not so much as a hint at a commitment to be bound by the "fair market rental value" which the tenant's expert reported or the "reasonable rent" the Appellate Division would impose, much less any definition of either. Nowhere is there an inkling that either of the parties directly or indirectly assented, upon accepting the clause, to subordinate the figure on which it ultimately would insist, to one fixed judicially, as the Appellate Division decreed be done, or, for that matter, by an arbitrator or other third party. * * * *

[¶10] For all these reasons, the order of the Appellate Division should be reversed, with costs, and the orders of the Supreme Court, Suffolk County, reinstated. The certified question, therefore, should be answered in the negative. As to the plaintiff's appeal, since that party was not aggrieved by the order of the Appellate Division, the appeal should be dismissed (CPLR 5511), without costs. * * * *

JASEN, Judge (dissenting in part):

While I recognize that the traditional rule is that a provision for renewal of a lease must be "certain" in order to render it binding and enforceable, in my view the better rule would be that if the tenant can establish its entitlement to renewal under the lease, the mere presence of a provision calling for renewal at "rentals to be agreed upon" should not prevent judicial intervention to fix rent at a reasonable rate in order to avoid a forfeiture. Therefore, I would affirm the order of the Appellate Division for the reasons stated in the opinion of Justice LEON D. LAZER at the Appellate Division.

COOKE, C. J., and GABRIELLI, JONES and WACHTLER, JJ., concur with

FUCHSBERG, J.

MEYER, J., concurs * * * .

JASEN, J., dissents in part and on defendant's appeal votes to affirm * * *.

(On defendant's appeal: Order reversed, with costs, the orders of Supreme Court,

Suffolk County, reinstated and the question certified answered in the negative.

On plaintiff's appeal: Appeal dismissed, without costs.)

Questions:

1. Why wasn't the landlord held to have violated a duty to negotiate in good faith?

2. Suppose the parties had specified that rent on renewal will be current rent plus a percentage of current rent equal to the percentage by which the consumer price index has increased from time of lease formation to the time of renewal. Would this be enforceable?
3. Suppose the parties had specified that an arbitrator would set a rate. Would this be enforceable?

4. Courts go both ways on this issue. For example, the court in *Cassinari v. Mapes*, 542 P.2d 1069 (Nev. 1975), said this:

> 1. A covenant to extend a lease upon such terms as may be agreed upon is a nullity and unenforceable since all the terms of the extension are left for future agreement. *City of Reno v. Silver State Flying Serv*., 84 Nev. 170, 175, 438 P.2d 257 (1968). In the case before us, however, all terms and conditions of the renewal were settled, leaving only the rental to later be determined. There is a division of authority as to enforceability in this circumstance. We are persuaded that the better view is to enforce such a provision for extension. * * * *
>
> It is appropriate to enforce such a provision since the clause for renewal constitutes part of the consideration for the original lease, and was without question intended by the parties to have meaning and to be effective. Surely we may not presume that one of the signatories agreed to the provision only in the secret belief that it would prove unenforceable. It is proper, then, to imply that the parties intended a reasonable rent for the extended period. If unable to agree, a court should be allowed to fix the rental since economic conditions are ascertainable with sufficient certainty to make the clause capable of enforcement. This view, we think, carries out the true intention of the parties, and does not constitute a making of a lease by the court in opposition to the desire of lessor and lessee.
>
> Consequently, we reverse the determination below that the provision for extending the term of the lease is too vague to be enforceable.

Which do you find more persuasive? For record, the UCC Article 2 follows the approach of *Cassinari*. The code is very clear that a contract for the sale of goods may form without any agreement on price. *See* UCC 2-305 (Open Price Term). About the only thing parties must agree on is quantity: which goods are agreed to be sold. The code has default provisions that fill in everything else, including warranties regarding ownership and quality of the goods themselves.

B. The Preliminary Agreement

The DACOURT GROUP, INC. v. BABCOCK INDUSTRIES, INC.FKI Babcock PLC, Dennis F. Flint, Jeffrey L. Currier, Peter W. Krehbiel,and Robert M. Miller

United States District Court, D. Connecticut (1990)

747 F. Supp. 157

RULING ON MOTION TO DISMISS OR FOR SUMMARY JUDGMENT

EGINTON, District Judge.

[¶1] Plaintiff, The Dacourt Group, Inc. ("Dacourt"), brought this action against defendants Babcock Industries, Inc. ("Babcock"), FKI Babcock PLC ("FKI"), the corporate parent of Babcock, and certain named officers of Babcock. This action arises out of a proposed $80 million sale-leaseback transaction involving commercial properties owned by Babcock. Dacourt, as the prospective purchaser and lessor, alleges that it suffered damages when, due to the actions of the various defendants, the sale and leaseback were not consummated. Jurisdiction in this action is based on diversity of citizenship, pursuant to 28 U.S.C. § 1332.

FACTS

[¶2] In 1988, Babcock and Dacourt entered into negotiations for the sale and leaseback of sixteen commercial properties owned by Babcock. The initial marketing package for the transaction circulated to potential investors by Babcock's broker made the representation that FKI would provide a "keep-well" letter to assure an institutional investor/lessor interested in the properties that its subsidiary, Babcock, would maintain a certain, unspecified, minimum net worth. This representation allegedly had the express approval of Babcock and FKI.

[¶3] On November 3, 1988 the representatives for the parties met to negotiate the terms of the sale-leaseback transaction. At the conclusion of the meeting, two documents were drafted to memorialize the negotiations. A "revised Offer to Purchase and Leaseback the [Babcock] Properties" (the "Revised Offer") was drafted and executed by the President of Dacourt. The Revised Offer was never subscribed to by Babcock or any authorized agent. Next, the attorney for Babcock drafted a letter (the "November 3 Letter") on Babcock's behalf which stated that "[w]e have come to a tentative agreement on basic terms." The letter was signed by Babcock's broker, David J. Daddario, who was retained for the transaction. Daddario had no express authority to execute documents or to enter into contractual agreements on behalf of Babcock. The specific terms of the FKI "keep-well" remained unresolved.

[¶4] Substantial negotiations did not resume until April 11, 1989. At this meeting Dacourt demanded from FKI, in addition to the "keep-well" guaranty, a complete indemnification for all environmental liabilities on the sixteen properties. FKI refused to satisfy either of Dacourt's demands and the transaction was placed on "hold."

[¶5] Dacourt alleges that the individual defendants contacted FKI and attempted to discourage it from completing the Dacourt financing by impressing upon FKI that a contemplated management buy-out of

Babcock would be less likely if Babcock had closed the sale-leaseback transaction with Dacourt. Dacourt maintains that as a result of these communications FKI notified the parties that it would not be willing to provide a “keep-well” agreement or any other form of guaranty. In May, 1989, Dacourt was informed that Babcock would not proceed with the sale-leaseback because FKI was auctioning Babcock.

[¶6] In its eleven count complaint, Dacourt asserts that Babcock is liable for breach of contract, breaches of obligations to negotiate in good faith, negligent misrepresentation and on promissory estoppel grounds. Dacourt claims that FKI is liable to it under promissory estoppel because Dacourt relied to its detriment on FKI’s representation that it would provide a “keep-well” guaranty as part of the sale-leaseback transaction. Dacourt also asserts claims for tortious interference against the individual defendants arising from the named officers’ alleged attempts to influence FKI to abandon the sale-leaseback transaction. Defendants have moved to dismiss the complaint pursuant to Fed.R.Civ.P. 12(b)(2) for lack of jurisdiction over FKI, pursuant to Fed.R.Civ.P. 12(b)(6) for failure to state a claim upon which relief can be granted, or for summary judgment.

I. Motion to Dismiss on Jurisdictional Grounds

[Ricks-The court concluded it lacked jurisdiction over FKI and dismissed all claims against it.]

II. Motion to Dismiss for Failure to State a Claim Upon Which Relief Can be Granted or for Summary Judgment

* * * *

A. Breach of Contract Claim

[¶7] The threshold issue to be addressed is whether the parties ever entered into a binding agreement for the sale-leaseback transaction. Plaintiff argues that the Revised Offer and the November 3 Letter evidence the existence of an agreement between the parties. The Court does not find that the parties, as of November 3, 1988, had come to an agreement as to the terms of the transaction.

[¶8] A binding agreement can arise, if the parties so intend, prior to the signing of a formal contract. *Arcadian Phosphates, Inc. v. Arcadian Corp*., 884 F.2d 69 (2d Cir. 1989); *Teachers Ins. and Annuity Assoc. v. Tribune Co*., 670 F. Supp. 491 (S.D.N.Y. 1987). The Court does not find Babcock ever evidenced the requisite intent to be bound by the documentation prepared on November 3. It is clear from the documents and the affidavits that the Revised Offer reflected the status of negotiations as of that date, but that material terms remained open for negotiation. The Revised Offer expressly called for the preparation of formal contractual documentation, and escrow deposit and financial and environmental covenants remained material open terms. “There is a strong presumption against finding binding obligation in agreements which include open terms, call for future approvals and expressly anticipate future preparation and execution of documents.” Teachers Ins. and Annuity Assoc., 670 F. Supp. at 499. The absence of an expression of intent by an officer of Babcock to be bound by the terms of the Revised Offer and the fact that material terms remained unresolved as of November 3, 1988, lead the Court to conclude that as a matter of law a binding agreement for the sale-leaseback transaction did not exist between Dacourt and Babcock. Summary judgment is therefore granted in favor of the defendants on Count I of the complaint.

B. Claims for Breach of the Duty of Good Faith

[¶9] Counts II, V and IX of the complaint assert claims that Babcock breached its duty to negotiate in good faith. Absent an agreement between the parties, no duty of good faith can be implied. *Reprosystem B.V. v. SCM Corp*., 727 F.2d 257, 264 (2d Cir.), *cert. denied*, 469 U.S. 828, 105 S. Ct. 110, 83 L. Ed. 2d 54 (1984). In opposing the motion for summary judgment, the plaintiff asserts that the November 3 Letter "created a binding preliminary agreement" sufficient to support the finding of an implied duty of good faith. *Teachers Ins. and Annuity Assoc. v. Tribune*, 670 F. Supp. at 498. Based upon the evidence presented, the Court does not find that, as of November 3, 1988, a binding preliminary agreement sufficient to support an implied duty of good faith existed. The parties negotiating this transaction were experienced professionals and there is insufficient evidence to conclude that there was a bilateral intention to be bound by the November 3 documentation prior to the execution of a formal contract or prior to the resolution, through further negotiation, of the numerous open terms. Given the absence of an enforceable obligation, no duty of good faith can be implied. * * * *

D. Claims for Promissory Estoppel

[¶10] Counts VI and VII assert claims against Babcock * * * for promissory estoppel arising from representations or promises which were allegedly made by the defendants during the negotiations. * * *

[¶11] A claim for promissory estoppel requires "[1] a clear and unambiguous promise; [2] a reasonable and foreseeable reliance by the party to whom the promise is made; and [3] an injury sustained by ... reason of his reliance." *R.G. Group, Inc. v. Horn & Hardart Co*., 751 F.2d 69, 78 (2d Cir. 1984). Dacourt bases its promissory estoppel claims on Babcock's alleged representations to third parties that "Babcock had agreed to the Dacourt financing," and Babcock's alleged representations to Dacourt that it would "proceed diligently to negotiate all relevant documents" and that "FKI would provide a keep-well agreement." The Court finds that while these representations may have been made they do not constitute "clear and unambiguous promises" sufficient to support a claim for damages on promissory estoppel grounds. Each of these representations were made in the course of negotiations and are too vague to satisfy the requirement of a "clear and unambiguous promise" on the part of the promisee. *Id*.; *D'Ulisse-Cupo v. Board of Directors*, 202 Conn. 206, 213, 520 A.2d 217, 221 (1987). At the time these alleged promises were made, material terms remained unresolved regarding each of the representations. Given the context in which the alleged representations were made, the Court concludes that no "clear and unambiguous promises" were made by Babcock and the defendant is entitled to summary judgment on Counts VI and VII of the complaint.

E. Claims for Negligent Misrepresentation

[¶12] In Count VIII of the complaint, Dacourt alleges that Babcock's representation in the marketing package circulated for the transaction and in the November 3 documentation that a "keep-well" guaranty would be provided constitutes a negligent misrepresentation. Plaintiff has failed to submit any credible evidence which would lead the Court to conclude that at the time the representations were made Babcock knew or had reason to know they were false. Absent evidence to support plaintiff's claims that Babcock knew or should have known that FKI's willingness to provide a "keep-well" guaranty was not certain, the Court finds such claims unpersuasive. Rather, it appears the "keep-well" guaranty was withdrawn as a result of the flow of the negotiations. The withdrawal of guaranties or indemnifications being a result not uncommon in the negotiation of sophisticated corporate transactions. Finding no genuine issue of material

fact as to the negligent misrepresentation claim, the defendants are entitled to summary judgment on Count VIII of the complaint.

CONCLUSION

[¶13] For the foregoing reasons, FKI's motion to dismiss is GRANTED and the only claims which remain to be litigated are Counts X and XI of the complaint. Summary judgment is GRANTED on all other counts in accordance with this ruling.

SO ORDERED.

Questions:

1. Why didn't the court hold that Babcock breached a duty of good faith?

2. Why did the promissory estoppel claim fail?

3. In *Channel Home Centers v. Grossman*, 795 F.2d 291 (3d Cir. 1986), the Grossmans offered to lease a mall space to Channel. The Channel people looked at the space and wanted to go ahead, so the business people from each organization met and worked out terms for a 25-year lease. The two parties wanted to remember what they had negotiated, and the Grossmans also said at the time that they wanted a letter of intent from Channel so that they could "show it to banks, or whatever." The Grossmans were probably thinking that if they had a large store such as Channel "anchoring" a large space in the mall, they could more easily obtain financing for the mall renovation they planned. They perhaps also wanted to show the letter to smaller tenants who might want a store next to Channel's (say, a RadioShack). So the lawyer from Channel wrote up a "letter of intent" that listed out the lease terms. The letter stated explicitly that a lease was contingent on permits and corporate board approvals, but the letter also contained this statement, near the end: "To induce the Tenant to proceed with the leasing of this Store, you will withdraw the Store from the rental market, and only negotiate the above described leasing transaction to completion." The Grossmans signed the letter and sent it back to Channel. A few weeks later, the Grossmans made a deal to lease the same space to a competitor of Channel, an action that would breach the promise made in the letter of intent. Was that promise binding? In other words, even if the letter of intent was not a lease, was it a contract?

Chapter 10. Limits on the Reach of Contract Law: Violation of Public Policy (or, “Illegality”)

The policy positions of the jurisdiction always put limits on which promises its courts enforce, as the Meta Rules and some cases (e.g., *Hooks v. Bridgewater*) and discussions (e.g., Chapter II.3.C) in the book have already noted. While some of these policy positions become firmed up into legal rules over time (as in the *Freiburger* case at the end of this chapter), some of them are more original or do not have a legal rule describing them yet. That was mostly true in *Hooks*, and it is mostly true when courts recognize new exceptions to at-will employment.

Because some policy positions do not have legal rules describing them yet and each new position is produced by a different set of courts, substantial variety exists in practice from state to state on how courts approach and decide intersections of public policy and contract. Advocacy matters quite a lot. At the most general level, the law is not very helpful. Here for instance is the North Dakota legislature’s general statement on the issue:

> 9-08-01. Provisions that are unlawful.
>
> Any provision of a contract is unlawful if it is:
>
> 1. Contrary to an express provision of law;
>
> 2. Contrary to the policy of express law, though not expressly prohibited; or
>
> 3. Otherwise contrary to good morals.

The cases that follow are illustrative of the way litigation has worked in the past on certain issues. Some of this has changed, and some has changed in some places but not others. Your professor may or may not fill you in on the legal variation in other states, or what has happened since in the jurisdiction at issue. Please consider what the lawyers did or did not do in each case. (You will have to infer this to some extent.)

Hazel Virginia REHAK v. Archie S. MATHIS

Supreme Court of Georgia (1977)

238 S.E.2d 81

BOWLES, Justice.

[¶1] This is an appeal from an order of the Superior Court of Floyd County granting appellee’s motion for summary judgment.

[¶2] The appellant, Hazel Rehak, filed an action in equity against the appellee, Archie Mathis, and in her complaint alleged that the parties, in 1957, had jointly purchased a home in Floyd County, Georgia. For the first two years, 1957 and 1958, she paid all installment payments upon the home. From 1959 through February of 1975, the appellant and appellee each made one-half of the monthly installment payments on the house. The complaint further alleged that both parties lived and cohabited together in the house for 18 years, during which time, appellant alleged she “cooked for, cleaned for, and in general cared for the comforts, needs, and pleasures of the (appellee) . . . while they cohabited together.” The appellant alleged that on numerous occasions the appellee told her that the house belonged to them jointly and that for the rest of her life he would support and take care of her and her financial needs.

[¶3] In December of 1975, the appellee moved out of the house and told the appellant to vacate the home. The appellee refused to pay her anything for her purchase money interest in the house or for the services rendered to the appellee over the 18-year period during which they cohabited.

[¶4] The appellant, in January of 1976, filed a verified petition for divorce against appellee in the Superior Court of Floyd County, wherein the appellant admitted that she cohabited with the appellee for 18 years. Following repeated hearings and negotiations between the parties, the appellant filed a motion to dismiss the divorce action with prejudice. The court entered an order dismissing the complaint, said dismissal to affect the question of marriage only and in no way to affect any future civil suit of equitable action by either party against the other.

[¶5] Following the dismissal, the appellant brought the present equitable action seeking an award of $100.00 a month for the 18 years that she lived with and took care of the needs of the appellee and additionally sought exclusive title and possession to the house in Floyd County.

[¶6] Subsequent to the filing of the complaint a motion for summary judgment was made by the appellee, which motion was supported by a brief. The appellant filed no response to appellee’s motion. The court entered an order granting the appellee’s motion for summary judgment for reason that there was no genuine issue as to any material fact and, therefore, appellee was entitled to judgment as a matter of law. The appellant appeals that order.

[¶7] Summary judgment will be granted only where there is no issue as to any material fact, and as a matter of law the moving party is entitled to a judgment. Code Ann. s 81A-156(c). * * * *

[¶8] In the instant case, the appellee moved for a summary judgment contending “the pleadings in this case conclusively show that all property and monetary claims asserted thereon are based upon a

meretricious relationship, which claims are not recoverable because contrary to the public policy of this State.”

[¶9] It is well settled that neither a court of law nor a court of equity will lend its aid to either party to a contract founded upon an illegal or immoral consideration. Code Ann. § 20-501; *Wellmaker v. Roberts*, 213 Ga. 740, 101 S.E.2d 712 (1958); *Watkins v. Nugen*, 118 Ga. 372, 45 S.E. 262 (1903).

[¶10] The appellee’s motion for summary judgment was supported by the verified pleadings in the former complaint for divorce between the parties, and the pleadings in the present case. The parties being unmarried and the appellant having admitted the fact of cohabitation in both verified pleadings, this would constitute immoral consideration under Code Ann. §g 20-501, and it was appellant’s duty to come forward and introduce evidence which would rebut that conclusion. Appellant having failed to introduce any rebuttal evidence sufficient to show to the court that there was a genuine issue of fact to be decided, it was not error for the court to grant summary judgment in favor of the appellee.

[¶11] Judgment affirmed.

All the Justices concur, except HALL and HILL, JJ., who dissent.

HILL, Justice, dissenting.

[¶1] Courts normally do not deny judicial relief to sinners. If that were the rule, the caseload in all courts would be drastically reduced. Courts normally do not deny judicial relief where both plaintiff and defendant have been immoral. If that were the rule, the divorce rate would be reduced.

[¶2] What courts invariably do is refuse to enforce a contract where, as the majority says, the contract is “founded upon” an illegal or immoral consideration; i.e., where the consideration for the contract is the agreement by one or both parties to perform an illegal or immoral act. Thus, where a man and woman have contracted with each other to cohabit together illegally, a court will not require the woman to perform her promise nor will it require the man to pay for her services. However, where a man hires a maid to clean house for him, his obligation to pay wages is enforceable in court even though he seduces her. The difference is that in the former case the illegal conduct is part of the consideration for the contract whereas in the latter case the illegal conduct is not part of the consideration but is incidental to the contract. I do not find evidence that the female in this case agreed to make house payments in consideration of the male’s promise to seduce her or to cohabit with her illegally.

[¶3] In the case before us, the movant has not carried the burden on a movant for summary judgment of showing that sex was any part of the consideration of this alleged contract. This court has simply presumed that sex was agreed to. We will not guess at the terms of contracts in other cases but here we knowingly imagine what the terms of this agreement were. In my opinion we should not use conjecture to imagine what the parties agreed to do.

[¶4] Let the defendant state under oath what he says was agreed to and what he says was done and if the contract be illegal let the district attorney represent the state. This court should not deny relief to the plaintiff based on our inference as to what constituted the consideration for the alleged agreement sued on here. I therefore dissent.

[¶5] I am authorized to say, that Justice HALL joins in this dissent.

Questions:

1. What rule of law resolves the case?

2. What does the court say is immoral consideration here?

3. What is the dissent’s primary point of contention?

4. How does the majority know that sex was what induced the promise to pay?

5. Why does the dissent say at the end, “Let the defendant state under oath what he says was agreed to and what he says was done and if the contract be illegal let the district attorney represent the state”?

6. Is this case really about illegal consideration?

7. Does religion influence this decision?

8. What should Rehak have alleged?

9. As you might expect, bargains in violation of public policy fall are often less controversial. A murder-for-hire contract cannot be enforced. The bargain between Abe and Juanita to provide Abe compensation for doing his duty as a peace officer is illegal. Similarly, agreements to bribe public officials are not binding.

Campaign Promises

Are campaign promises enforceable? Consider the following from *May v. Kennard Indep. Sch. Dist.*, Memorandum Order Adopting the Magistrate Judge’s Report and Recommendation, 1996 WL 768039, at *7 (E.D. Texas 1996):

> * * * * Breach of Contract Claim
>
> [¶1] Plaintiff claims breach of contract against former Texas Governor Ann Richards. He claims that a legally enforceable contract was formed between former governor Richards and the citizens of the state based upon certain campaign promises made during her gubernatorial campaign. Plaintiff asserts Richards breached this contract by failing to segregate proceeds from the state lottery in a separate fund to be used solely for education-related expenses. He complains that the filtering of lottery proceeds into a

general fund "is a flagrant breach of contract and faith with the Texas state taxpayers." Plaintiff's Amended Complaint at 2.

[¶2] A political campaign promise is legally insufficient to create a binding contract unless it is so intended by the promisor and promisee. *Russell v. District of Columbia,* 747 F. Supp. 72, 80 (D.D.C.1990), aff'd, 984 F.2d 1255 (D.C. Cir. 1993). Plaintiff neither presents evidence nor claims of any personal representations by Richards that he would not have to pay his property taxes. Thus, the Court must determine whether Richards' campaign speeches created an oral contract with plaintiff.

[¶3] The statements upon which plaintiff's claim are based were not made specifically to plaintiff by then gubernatorial candidate Richards. It may be reasonably concluded that she made them for the general benefit of the citizens of the state of Texas. It would be wholly unreasonable for any listener to interpret a campaign promise, by its inherent nature, to serve as an offer to enter into a legally binding contract. Thus, it would be unreasonable for plaintiff to believe that Richards had made a legally enforceable promise. Plaintiff also had reason to know that the candidate did not intend for her statements to be legally binding. Because plaintiff had reason to know that Richards would not intend for her statements to create a binding contract, there could be no mutual assent and no contract.‡‡‡‡‡‡

[¶4] Plaintiff's attempted breach of contract claim should be dismissed as frivolous.
* * * *

Question: Should the plaintiff have alleged promissory estoppel? Unjust enrichment? What possible public policy arguments does the excerpt miss? Do any constitutional law arguments come to mind, and which side do they support?

‡‡‡‡‡‡ [6] Further, May does not present any evidence that he performed any action that constitutes acceptance or consideration for the candidate's promise even if, assuming arguendo, there had been an offer.

C. Covenants Not to Compete

Stephen FREIBURGER v. J-U-B ENGINEERS, INC.

Supreme Court of Idaho (2005)

111 P.3d 100

TROUT, Justice.

[¶1] Stephen Freiburger brought this declaratory judgment action against J-U-B Engineers, Inc. (J-U-B), seeking a judicial declaration that J-U-B’s non-compete clause in his employment contract was invalid and unenforceable under Idaho law. The district court granted summary judgment to Freiburger, from which J-U-B now appeals. Because we agree with the trial court that the clause is unreasonable and greater than necessary to protect J-U-B’s legitimate business interests, we affirm.

I.

FACTUAL AND PROCEDURAL BACKGROUND

[¶2] In December 1991, J-U-B hired Stephen Freiburger and, as part of his employment application, he signed an Applicant’s Certification and Agreement (Agreement). The Agreement included a restrictive covenant (Covenant), which is at the center of this controversy. That Covenant reads, in part:

> Should I become an employee of JUB, it is anticipated that my responsibilities may increase with time and that I may be an official representative to many clients served by JUB. Therefore, *I agree that for a period of two years following any date of termination of my employment with JUB, I would not attempt to take, take or join with anyone to take, (without the written consent of JUB) any of past or present clients or projects or any pending clients or projects, for which JUB has or would be providing professional services.* (emphasis added).

J-U-B Engineering is one of the largest privately owned engineering firms in the State of Idaho with offices in Boise, Twin Falls, Pocatello, Coeur d’Alene and Nampa, and employs approximately 250 people. It does business throughout the Northwest and has been in business for more than 30 years.

[¶3] Freiburger became a professional engineer in 1991, just as he joined J-U-B. When he was hired, he had prior experience in consulting engineering and technical expertise in both transportation and solid waste engineering. Freiburger served as J-U-B’s project manager in Twin Falls, moving to the Boise office and then to Nampa. While with J-U-B, Freiburger participated in all aspects of client development and knew how J-U-B engaged in client development and client service. He attended manager meetings and was privy to proprietary information concerning existing clients and projects.

[¶4] According to J-U-B, Freiburger participated in its “inner circle” and in planning efforts to “capture more of the transportation engineering work” available in J-U-B’s area of practice. Also, it appears that

because of his prominence in the transportation group, he built a relationship base with the Idaho Department of Transportation (IDOT), becoming one of J-U-B’s primary liaisons with IDOT, and embodying J-U-B’s goodwill effort with IDOT to secure IDOT projects and contracts.

[¶5] On April 25, 2001, Freiburger resigned from J-U-B. About six months later, Freiburger joined Riedesel Engineering, LLC (Riedesel). Soon after Freiburger began his new employment, Riedesel wanted to propose on an IDOT project and tout Freiburger’s qualifications in order to secure IDOT projects. At that time, Freiburger wanted to make sure he was not in conflict with the Covenant and, therefore, made several attempts, both directly and through his attorney, to obtain from J-U-B a list of clients that J-U-B considered to be covered under the terms of the Covenant. When J-U-B refused to provide any list of those clients, and simply instructed Freiburger that he should run any potential clients by them first, Freiburger initiated this declaratory judgment action on September 12, 2002, asking the court to declare the Covenant overbroad, unreasonable, void and unenforceable as a matter of law. * * * *

[¶6] Freiburger then filed a motion for summary judgment, seeking to have the Covenant declared unenforceable as a matter of law. After oral argument on the matter, the trial court issued its memorandum decision, granting summary judgment to Freiburger. The court found the Covenant unreasonable and fatally overbroad and declined to strike the offending language in the Covenant to make it reasonable, finding that the court would essentially have to rewrite the entire Covenant to make it reasonable. Freiburger then requested costs and attorney fees pursuant to I.C. § 12-120(3). The court granted Freiburger’s request, awarding him $117.00 in costs and $9,360.00 in fees. J-U-B timely filed this appeal. * * * *

III.

ANALYSIS

A. The Covenant Not to Compete

[¶7] J-U-B’s primary contention on appeal is that the district court erred in granting Freiburger summary judgment because it has a legitimate interest in protecting its business from former employees who may endeavor to take J-U-B clients and the Covenant contained in the Agreement reasonably protects that interest. Restrictive covenants not to compete in an employment contract, though enforceable, are disfavored and will be strictly construed against the employer. *See Stipp v. Wallace Plating, Inc.,* 96 Idaho 5, 6, 523 P.2d 822, 823 (1974); *Shakey’s Inc. v. Martin,* 91 Idaho 758, 762, 430 P.2d 504, 508 (1967). In order to be enforceable, a covenant not to compete must be ancillary to a lawful contract supported by adequate consideration, and consistent with public policy. *McCandless v. Carpenter,* 123 Idaho 386, 390, 848 P.2d 444, 447 (Ct.App.1993).

[¶8] In addition, a covenant not to compete contained in an employment contract must be reasonable as applied to the employer, the employee, and the public. *See Stipp,* 96 Idaho at 6, 523 P.2d at 823; *Insurance Ctr., Inc. v. Taylor,* 94 Idaho 896, 899, 499 P.2d 1252, 1255 (1972); *Marshall,* 81 Idaho at 203, 339 P.2d at 508; *McCandless,* 123 Idaho at 390, 848 P.2d at 447. In other words, a covenant not to compete is reasonable only if the covenant: (1) is not greater than is necessary to protect the employer in some legitimate business interest; (2) is not unduly harsh and oppressive to the employee; and (3) is not injurious to the public. *See* Restatement (Second) Of Contracts § 188 (1981).

[¶9] We note that some jurisdictions have applied different standards of reasonableness, depending on the type of restrictive covenant involved and what it is seeking to accomplish. For instance, some courts have held that covenants not to compete ought to be analyzed differently than anti-piracy covenants. *See, e.g., Merrill Lynch, Pierce, Fenner Smith Inc. v. Ran,* 67 F. Supp.2d 764 (E.D.Mich.1999). Under this view, covenants not to compete preclude employees from working in the same business as the employers' for certain periods of time and thus, are strictly construed against employers. *See Hilb, Rogal and Hamilton Co. of Arizona, Inc. v. McKinney,* 190 Ariz. 213, 946 P.2d 464, 467 (Ct.App.1997). On the other hand, anti-piracy agreements restrict the terminated employee from soliciting customers of his former employer or making use of confidential information from his previous employment. *Id.* These agreements have been held to a less stringent test of reasonableness than blanket prohibitions of competition, as they are not considered nearly as oppressive and unreasonable as noncompete agreements. *See Corroon Black of Ill., Inc. v. Magner,* 145 Ill.App.3d 151, 98 Ill. Dec. 663, 494 N.E.2d 785 (1986); *Olliver/Pilcher Ins., Inc. v. Daniels,* 148 Ariz. 530, 715 P.2d 1218 (1986).

[¶10] However, we think the more reasoned approach is to simply determine whether or not the clause is no more restrictive than necessary to protect the employer's legitimate business interests. This test can aptly be applied regardless of whether the clause itself seeks to limit the employee's work in the field entirely, or seeks only to limit the employee in approaching former clients. Indeed, we have in the past upheld the application of a restrictive covenant, no matter what it is termed, only after a determination that it was no broader than necessary to protect an employer's legitimate business interest. *See Magic Lantern Prod., Inc. v. Dolsot,* 126 Idaho 805, 892 P.2d 480 (1995); *Insurance Center, Inc. v. Taylor,* 94 Idaho 896, 499 P.2d 1252 (1972).

1. J-U-B's Legitimate Business Interest

[¶11] The first issue the Court must consider is whether J-U-B has a legitimate business interest worthy of protection. The burden is on the employer to prove the extent of its protectable interest. *McCandless,* 123 Idaho at 391, 848 P.2d at 449. The general rule is that an employer is not entitled to protection against ordinary competition. *See Pinnacle Performance, Inc. v. Hessing,* 135 Idaho 364, 367, 17 P.3d 308, 311 (Ct.App.2001) (citing 54A Am.Jur.2d Monopolies § 916 (1996)). However, employers are entitled to protect their businesses from the detrimental impact of competition by employees who, but for their employment, would not have had the ability to gain a special influence over clients or customers. *See Amex Distrib. Co., Inc. v. Mascari,* 150 Ariz. 510, 724 P.2d 596, 605 (Ct.App.1986); *American Software USA, Inc. v. Moore,* 264 Ga. 480, 448 S.E.2d 206, 208 (1994); *Holloway v. Faw, Casson Co.,* 319 Md. 324, 572 A.2d 510, 515 (1990); *Prof'l Bus. Services Co. v. Rosno,* 256 Neb. 217, 589 N.W.2d 826, 831 (1999). Thus, “the employer has a protectable interest in the customer relationships its former employee established and/or nurtured while employed by the employer, and is entitled to protect itself from the risk that a former employee might appropriate customers by taking unfair advantage of the contacts developed while working for the employer.” *W.R. Grace Co. v. Mouyal,* 262 Ga. 464, 422 S.E.2d 529, 531 (1992); *See also* 54a Am.Jur.2d Monopolies § 919 (1996).

[¶12] Freiburger entered into an employment relationship with J-U-B that clearly both placed him in direct contact with J-U-B clients, as well as placed him in the forefront in developing J-U-B's goodwill effort with several clients. Therefore, we conclude that J-UB has a legitimate business interest worthy of protection in the client relationships Freiburger helped to develop while in J-U-B's employ.

2. The Covenant as a Reasonable Means of Protecting the Interest

[¶13] The second step in analyzing the Covenant is to determine whether it is a reasonable means of protecting J-U-B’s legitimate business interest. The core provision in the Covenant provides:

> ... I agree that for a period of two years following any date of termination of my employment with J-U-B, I would not attempt to take, take or join with anyone to take, (without the written consent of J-U-B) any of past or present clients or projects or any pending clients or projects, for which JU-B has or would be providing professional services....

[¶14] The district court found that the Covenant was an overbroad means of protecting J-U-B’s interest in the goodwill developed by Freiburger because the Covenant unreasonably prohibited Freiburger from providing any services to J-U-B’s clients, current, past and potential, without regard to whether Freiburger had any contact with these clients. This conclusion is similar to an Idaho Court of Appeals decision that analyzed a restrictive covenant similar to the one at issue here. *See Pinnacle Performance, Inc. v. Hessing,* 135 Idaho 364, 17 P.3d 308 (Ct.App.2001).

[¶15] In *Pinnacle,* the employer entered into a written employment agreement with Hessing, as an independent contractor, to develop a prototype card shuffler for the employer’s client, Casinovations. The agreement contained a non-competition clause that read: “Contractor agrees to not offer, sell, or trade his services directly to Company clients, both current and past, for a period of two (2) years from completion of Contractor’s work for the Company ....” *Pinnacle,* 135 Idaho at 366, 17 P.3d at 310. After developing the prototype, Hessing signed an employment agreement with Casinovations, and the employer filed a complaint against Hessing alleging that he had breached the covenant not to compete.

[¶16] The Court of Appeals noted that if a court finds that an employer has a legitimate business interest, such a business interest is reasonably protected by prohibiting the employee from providing services to those clients with whom the employee developed customer goodwill. *Id.* at 368, 17 P.3d at 312. “However, a prohibition against doing business with an employer’s clients, without regard to whether a relationship existed between the client and the employee, is an overbroad means of protecting the employer’s interest in the goodwill developed by the employee.” *Id.* (citing *American Software,* 448 S.E.2d at 209). Thus, the court found that since the covenant not to compete failed to reasonably limit the scope of the prohibited activity to those clients with whom Hessing had contact, the prohibitive impact of the covenant was greater than necessary to protect the employer’s legitimate business interest.

[¶17] The decision also noted that a covenant not to compete which prohibits an employee from working in any capacity or which fails to specify with particularity the activities the employee is prohibited from performing is too overbroad and indefinite to be considered reasonable. *Id.* at 368-69, 448 S.E.2d 206, 17 P.3d at 312-13; *See also National Teen-Ager Co. v. Scarborough,* 254 Ga. 467, 330 S.E.2d 711, 713 (Georgia 1985); *American Family Life Assurance Co. v. Tazelaar,* 135 Ill.App.3d 1069, 90 Ill. Dec. 789, 482 N.E.2d 1072, 1075 (1985). The court found that the term “services” was not expressly defined in the covenant and, therefore, it failed to limit the scope of activities Hessing was prohibited from performing. The covenant was too overbroad and indefinite to be considered reasonable.

[¶18] The Covenant at issue here is clearly an overbroad means of protecting J-U-B’s legitimate business interest. First, J-U-B has actively operated throughout the Northwest region for nearly thirty years and

clearly has a large client base both past and present, yet the Covenant prohibits Freiburger from taking any of this large group of clients regardless of whether Freiburger helped to develop J-U-B’s goodwill effort toward that client. Instead of the reference point of the Covenant being goodwill created through the efforts of Freiburger, the Covenant prohibits contact with any past, present or potential client of J-U-B at the time Freiburger left J-U-B’s employ. It is possible, under the plain language of the Covenant, that if J-U-B had a client or project twenty years ago and had not had contact with that client since, Freiburger would still be prohibited from taking that client for a period of two years after he left J-U-B. Since the Covenant includes past clients or projects, without any meaningful limitation, it is an overbroad means of protecting the employer’s interest in the goodwill Freiburger helped to develop.

[¶19] Secondly, just as in *Pinnacle,* the Covenant at issue unreasonably prohibits Freiburger from providing any services to J-U-B’s clients, current, past, or pending. We note that nothing in the Covenant limits the scope of activities Freiburger is prohibited from offering. The prohibitive impact of this limitation is especially harsh and oppressive to Freiburger considering the nature of the clients involved in this area of business. The Covenant would likely prevent Freiburger from performing any services to a number of state and local governmental agencies throughout the Northwest.

[¶20] Third, the portion of the Covenant that refers to taking any “pending” clients or projects for whom J-U-B “would be providing professional services” is also unreasonable and overbroad. J-U-B contends that “pending” can reasonably be defined as “imminent,” and should be interpreted to mean identified clients in whom J-U-B has invested goodwill and to whom J-U-B has sufficiently recruited and engaged such that the client will hire J-U-B. However, this ignores the fact that the term is not defined in the Agreement and can reasonably be given more than one possible interpretation, making it an overbroad description of the clients Freiburger is prohibited from “taking.” There is no “goodwill” limitation to be found, nor is there language that limits the interpretation of “pending” clients or projects. Instead, the clause appears to require Freiburger to know to which “pending” clients or projects J-U-B “would be” providing professional services in the future. Therefore, it is clear that the Covenant is overbroad and an unreasonable means of protecting J-U-B’s legitimate business interest.

3. Judicial Modification of the Covenant

[¶21] J-U-B finally argues that even if the Covenant is determined to be too overbroad to be enforced, Idaho case law suggests that a non-compete covenant can be altered by the court to render it reasonable and enforceable. In fact, J-U-B argues this Court should do so unless it determines the Covenant was not drafted in good faith. *See Data Management, Inc. v. Greene.,* 757 P.2d 62 (Alaska 1988). This Court has approved of the modification of otherwise unreasonable covenants not to compete. *See Insurance Ctr., Inc., v. Taylor,* 94 Idaho 896, 899, 499 P.2d 1252, 1255 (1972). In doing so the Court explained:

> It is the conclusion of this Court that the cases which authorize a modification of restrictive covenants ancillary to employment agreements are more consistent with the inherent concerns of a court of equity—fairness and reasonableness. Adoption of the modification principle allows a court to escape the rule of arbitrary refusal to enforce a covenant which, while unreasonable or indefinite in some of its terms, nevertheless serves to protect a legitimate interest of the parties or the public as the case may be .... [T]his Court seeks to provide flexibility to determining remedies available to the parties and the public. Consequently, enforcement is variable upon the circumstances of each case. Rather than

> choosing between absolute enforcement or unenforcement, there will be a wide range of alternatives available to meet the particular facts of the case being tried.

Id. at 900-901, 499 P.2d at 1255-56. Nevertheless, “a covenant not to compete may not be modified to make it reasonable if the covenant is ‘so lacking in the essential terms which would protect the employee’ such that the trial court is no longer modifying but rewriting the covenant.” *Pinnacle Performance,* 135 Idaho at 369, 17 P.3d at 313 (*quoting Insurance Ctr.,* 94 Idaho at 900, 499 P.2d at 1256).

[¶22] Here, it would be necessary not only to strike some of the words of the Covenant, but in addition, to add clauses relating to good will and relationships between Freiburger and the clients and defining the parameters of what services Freiburger would be prohibited from providing to J-U-B clients. This is far more than a “blue pencil” approach to an unreasonable word or two and would have the district court or this Court re-writing the parties’ contract. The district court correctly concluded that merely striking a few words from the Covenant could not achieve the goals of making it reasonable and enforceable and we agree that the only alternative was to declare the entire clause void and unenforceable as a matter of law. * * * *

IV.

CONCLUSION

[¶23] The Covenant at issue is unenforceable as a matter of law because it is unreasonable and much broader than necessary to protect J-U-B’s legitimate business interest in the client goodwill developed by Freiburger while in J-U-B’s employ. The Court cannot simply strike a few words from the Covenant to make it reasonable and enforceable and would be forced to rewrite the contract, adding essential limiting language in order to bring the Covenant into compliance with applicable law. * * * *

Chief Justice SCHROEDER and Justices EISMANN, BURDICK and JONES concur.

Questions:

1. What does ancillary mean? In what ways could a covenant not to compete be ancillary to the sale of a business? An employment agreement? When would a covenant not to compete not be ancillary?

2. Courts often draw a distinction between sales of business and employment agreements when judging whether an ancillary covenant not to compete should be enforceable. Why might a court be less likely to enforce a covenant not to compete in an employment agreement, or to enforce it less rigidly?

3. The “blue pencil” approach that the court names allows a court to cut back to a reasonable limit the scope, time, or geographic reach of a non-compete clause. Some courts have rejected the use of the blue pencil rule in employment cases, instead striking the clause at issue down.

Note on non-competes for employees: Even though we have a longstanding rule for judging whether non-competes comply with public policy in favor of competition—still, on this issue as with the other issues of public policy in this chapter, approaches differ by jurisdiction. *Freiburger* is quite traditional. Taking a different approach, California by statute makes most non-competes unenforceable:

> (a) Except as provided in this chapter, every contract by which anyone is restrained from engaging in a lawful profession, trade, or business of any kind is to that extent void.
>
> (b)(1) This section shall be read broadly, in accordance with *Edwards v. Arthur Andersen LLP*, [189 P.3d 285] ([Cal.] 2008) . . . .

Cal. Bus. & Prof. Code § 16600 (2024). *Edwards* stated,

> Under the common law, . . . contractual restraints on the practice of a profession, business, or trade, were considered valid, as long as they were reasonably imposed. . . . However, in 1872 California settled public policy in favor of open competition, and rejected the common law “rule of reasonableness,” when the Legislature enacted the Civil Code. . . . Today in California, covenants not to compete are void, subject to several exceptions discussed briefly below.

189 P.3d at 290–91 (“The chapter excepts noncompetition agreements in the sale or dissolution of corporations [and other business entities].”). The *Edwards* court declared a non-compete otherwise binding an employee void even when “narrowly drawn.” *Id.* at 955. Minnesota, North Dakota, and Oklahoma have similar provisions. Some states have special provisions for physicians, or a wage threshold for enforceability. Rules vary considerably from state to state. Legislatures have been active recently, and where legislatures have not acted, courts continue to guide policy.

A federal rule on this issue would create uniformity, of course, and the FTC in fact banned non-competes in 2024, but, as the FTC’s website now reports, the new rule is not in effect and it is not enforceable. On August 20, 2024, a district court issued an order stopping the FTC from enforcing the rule. The FTC appealed that decision on October 18, 2024. On September 5, 2025, the FTC took steps to dismiss its appeal in the Fifth Circuit.

FTC Announces Rule Banning Noncompetes, https://www.ftc.gov/news-events/news/press-releases/2024/04/ftc-announces-rule-banning-noncompetes (April 23, 2024). In this way, the FTC effectively abandoned the new rule.

Chapter 11. What Is the Bargain? Content

Contracts are made up of words, usually. Lately, someone began writing them in pictures for people they believe won't understand contract words. See https://creative-contracts.com/ (motto: "Contracts everyone understands"). At least people who understand the pictures will understand. Most contracts are words. The words' meaning might be clear or unclear. The words might be written or oral. They might be gathered in one place or scattered among many documents. They might even be placed in a document by mistake. The words might be words of promise, but contracts often also contain conditions, representations, statements of factual background, and other terms. Sometimes courts by law "read into" or imply in contracts terms that the parties were not aware they needed but that are suggested by the parties' bargain.

In this chapter, we examine ways by which courts determine the content of the bargain. We will examine how a court determines what words in a contract mean (Subsection A), how the court decides whether any words can be added to the contract (Subsection B), what other obligations are implied by the parties' bargain (Subsection C), what courts do with language of condition (Subsection D), and how courts decide who should perform first if the parties have not said (Subsection E).

Most contract litigation is about the content of the bargain—what the words mean and whether any can be added.

A. The Meaning of the Words: Interpretation or Construction?

After a contract forms, any attempt to enforce it requires the parties and the court to know what the words of the contract mean. As you might expect, the meaning of contractual words is sometimes not obvious. What is a court to do when the parties have agreed to words the meaning of which is unclear?

1. The "Plain Meaning" Rule or Not—When to Take Evidence About Meaning

The following case, *Coker*, illustrates a threshold issue for all interpretation cases: whether the courts will consider evidence beyond the "four corners" of the document. The court decides that the contract is ambiguous, so more is needed. Justice Spears in dissent follows what the law calls the "plain meaning rule." Are we looking for the intent of the parties when we apply the rules in this section?

Coker v. Coker (Tex. 1983)

BARROW, Justice.

[¶1] This suit was brought by Frances Kincaid Coker (Frances) against her former husband, Mac L. Coker, Jr. (Mac), on a property settlement agreement incorporated into their divorce decree. The decree awarded Frances a real estate commission previously earned by Mac from the sale of certain ranch property. The seller of the property was to pay the commission in seven annual installments as payments were made by the purchaser. After Frances received payments totaling $14,317.16, the purchaser defaulted and no further commissions were receivable. The question presented here is whether Mac agreed to pay Frances a minimum of $25,000 or whether Frances was assigned all of Mac's interest in the commissions to be paid by the seller in this particular transaction.

[¶2] Both parties asserted that the property settlement agreement was unambiguous and each moved for a favorable summary judgment. The trial court construed the agreement as one of guaranty and rendered summary judgment that Frances recover the sum of $10,682.84 from Mac. The court of appeals affirmed in an unpublished opinion. * * * * We reverse the judgments of the courts below and remand the cause to the trial court.

[¶3] The parties were divorced on September 24, 1971 after being married about ten years. They had accumulated community property consisting of a 1969 Buick automobile, two Dallas Cowboy seat options, unpaid real estate commissions earned by Mac while employed as a broker for the real estate firm of Majors & Majors and certain personal effects. The parties entered into a property settlement agreement which was approved by the trial court and incorporated into the divorce decree. The decree provides in relevant part:

> IT IS THEREFORE FURTHER ORDERED, ADJUDGED AND DECREED that Petitioner Frances Kincaid Coker have and she hereby is awarded as her sole and separate property one 1969 Buick automobile, Serial No. 4443792127816, all household goods and personal possessions now in her possession or located at her place of residence, one Texas Stadium Bond along with season ticket sold in connection therewith, and those certain commissions *and accounts receivable heretofore earned by husband during his employment with the firm of Majors and Majors in connection with the sale of the "Jinkens Ranch property in Tarrant County, Texas"*; that Respondent have and he hereby is awarded as his sole and separate property one Texas Stadium Bond along with season ticket sold in connection therewith, all personal effects in his possession and those certain commissions or accounts receivable owing to him from Majors and Majors being the monthly commissions on leases negotiated while Respondent was in the employment of Majors and Majors. (emphasis added).

The property settlement agreement provides in part:

> 5. Wife shall receive as her sole and separate property, free and clear of any claim, right or title of husband, the following described property: one 1969 Buick automobile, serial no. 4443792127816, all household goods and personal possessions now in the wife's possession or located at her place of residence, (except that the husband shall receive one bedroom suite now located in Crowell, Texas), and one Texas Stadium bond, free of all indebtedness, along with the season ticket sold in connection therewith. *The wife shall*

> *further have as her sole and separate property, free and clear of all claim, right or title asserted by husband, that certain right, commission or account receivable heretofore earned by husband during his employment with the firm of Majors & Majors in connection with the sale of the "Jinkens ranch property in Tarrant County, Texas,"* such future commission or account receivable being in the approximate sum of $25,-000.00.
>
> 8. Husband represents and warrants to the wife that, to the best of his knowledge, approximately $25,000.00 remains due and owing to him as his portion of commissions earned in connection with the sale of the "Jinkens property in Tarrant County, Texas," and he hereby guarantees to wife that she will receive the said sum of $25,000.00, from Majors & Majors, or from any other payor of such commissions receivable. *Such commission is payable to her as payments are made by purchasers to sellers*, and will normally be received by her through the office of Majors & Majors. In the event, for any reason she fails to receive such installments of commission exactly as husband would have prior to his assignment of his rights thereto to wife, *husband agrees to pay to wife in Dallas County, Texas all such sums of money, which she has failed to receive, up to the guaranteed sum of $25,000.00*. (emphasis added).

[¶4] The parties thereby agreed that Mac would keep his rights to the monthly commissions earned on leases he had negotiated and Frances would be assigned the commission earned by Mac from the sale of the "Jinkens ranch property in Tarrant County." Prior to the divorce, Mac had participated in the sale of the Jinkens ranch whereby he would receive 40% of the sales commission payable by the seller to Majors & Majors over a seven year period contingent on the annual payments being made by the purchaser. In 1976, however, the purchaser defaulted and according to the terms of the sales contract, the seller was not required to continue payments of the commission. Therefore, Mac's rights in the commission were terminated.

[¶5] Frances admitted that she had received all the commission payable to Mac prior to default, but she contends that under the property settlement agreement she was to receive a minimum of $25,000. The trial court and the court of appeals agreed with Frances. We must attempt to construe this contract and determine the intent of the parties as shown by the written instruments.

[¶6] In construing a written contract, the primary concern of the court is to ascertain the true intentions of the parties as expressed in the instrument. [Citation omitted.] To achieve this objective, courts should examine and consider the entire writing in an effort to harmonize and give effect to all the provisions of the contract so that none will be rendered meaningless. [Citation omitted.] No single provision taken alone will be given controlling effect; rather, all the provisions must be considered with reference to the whole instrument. [Citation omitted.] * * * *

[¶7] If the written instrument is so worded that it can be given a certain or definite legal meaning or interpretation, then it is not ambiguous and the court will construe the contract as a matter of law. [Citation omitted.] A contract, however, is ambiguous when its meaning is uncertain and doubtful or it is reasonably susceptible to more than one meaning. [Citation omitted.] Whether a contract is ambiguous is a question of law for the court to decide by looking at the contract as a whole in light of the circumstances present when the contract was entered. [Citation omitted.] When a contract contains an ambiguity, the granting of a motion for summary judgment is improper because the interpretation of the instrument becomes a fact issue. [Citation omitted.]

[¶8] The court of appeals determined that Mac had absolutely guaranteed the payment of $25,000 to Frances. Although the court of appeals recognized that the liability of a guarantor is generally measured by the liability of the principal, it held that paragraph 8 of the settlement agreement created a broader obligation than the commission sales agreement. This interpretation conflicts with paragraph 5 of the agreement and the language used in the divorce decree.

[¶9] According to the rules of construction, paragraph 8 must be considered along with paragraph 5 and the underlying circumstances to ascertain the true intention of the parties. [Citation omitted.] The court of appeals failed to fully consider paragraph 5 of the agreement which clearly states that Mac only assigned that "certain right, commission or account receivable heretofore earned by husband." Also, the language of the divorce decree supports an interpretation only assigning Mae's interest in the commission.

[¶10] When the language in paragraph 8 is considered alone and particularly the last sentence thereof, the meaning is unclear. The provision could be construed as a guarantee by Mac that Frances would receive $25,000 or merely a promise that he would not interfere with the payments made by Majors & Majors to her after they received the commission from the seller. If we construe the agreement as a contract of guaranty, any uncertainty must be resolved in favor of Mac as guarantor. [Footnote: A guarantor is entitled to have his agreement strictly construed so that it is limited to his undertakings, and it will not be extended by construction or implication. * * * * Where uncertainty exists as to the meaning of a contract of guaranty, its terms should be given a construction which is most favorable to the guarantor. * * * *] Even if we conclude the rules of guaranty do not apply, we could not say with certainty that Mac promised to pay Frances $25,000 regardless of the payment of the commission. Such an interpretation would render the provisions in the divorce decree and paragraph 5 relating to the assignment of the commission surplusage. Courts must favor an interpretation that affords some consequence to each part of the instrument so that none of the provisions will be rendered meaningless. [Citation omitted.]

[¶11] The divorce decree and paragraph 5 state what interest is assigned to Frances. Unless paragraph 8 is construed to merely set out the manner in which Frances would receive the annual payments, this paragraph conflicts with paragraph 5 and the divorce decree. This conflict creates an ambiguity as to the intent of the parties as expressed in the written agreement and the decree.

[¶12] The court of appeals held the provisions of the property settlement agreement unambiguously required Mac to pay Frances $25,000 regardless of whether the commissions were in fact paid by the purchaser. This construction conflicts with paragraph 5 as well as the divorce decree. Therefore, this agreement is ambiguous and the trial court erred in granting summary judgment. The trier of fact must resolve the ambiguity by determining the true intent of the parties. [Citation omitted.]

We reverse the judgments of the courts below and remand the cause to the trial court.

SPEARS, J., dissents in which POPE, C.J., and RAY and ROBERTSON, JJ., join.

I respectfully dissent.

[¶2] I do not believe that the property settlement agreement entered into by the Cokers is ambiguous. If a written instrument can be given a definite interpretation, it is not ambiguous and the court will construe the contract as a matter of law. *R & P Enterprises v. La Guarta, Gavrel & Kirk, Inc.*, 596 S.W.2d 517, 518 (Tex.1980).

[¶3] The majority correctly states that the primary objective in the interpretation of contracts is to give effect to the intentions of the parties as expressed in the instrument. *R & P Enterprises v. La Guarta, Gavrel & Kirk, Inc*., 596 S.W.2d at 518; *Citizens National Bank in Abilene v. Texas & P. Ry. Co.,* 136 Tex. 333, 150 S.W.2d 1003, 1006 (1944). Also, the court must consider the entire instrument so that none of the provisions will be rendered meaningless. *R & P Enterprises,* 596 S.W.2d at 519; *Myers v. Gulf Coast Minerals Management Corp.,* 361 S.W.2d 193, 196 (Tex.1962).

[¶4] By applying these rules of construction and looking at the contract as a whole, we see the clear, unambiguous meaning of the words used. It is obvious to me that Frances was to receive a minimum of $25,000. The divorce decree awarded her “those certain commissions and accounts receivable heretofore earned by husband .... “ (emphasis added). Paragraph five of the property settlement provides that Frances shall have as her separate property “that certain right, commission or account receivable heretofore earned by husband .... “ (emphasis added).

[¶5] In the first sentence of paragraph eight, Mac unconditionally represented and warranted that the “Jinkins property” commission was due and owing to him. He then assigned the commission to Frances and “guaranteed” receipt by her of $25,000. While it is true that the payments of the commission were due only so long as payments on the purchase of the property were made, and upon default no commission would be paid, this limitation is not incorporated in nor alluded to in the agreement setting forth his obligation to pay his wife the $25,000. In fact, the agreement is quite to the contrary.

[¶6] The third sentence of paragraph eight provides:

> “In the event, for any reason she fails to receive such installments of commission exactly as Husband would have prior to this assignment of his rights thereto to Wife, Husband agrees to pay Wife in Dallas County, Texas all such sums of money, which she has failed to receive, up to the guaranteed sum of $25,000.00.” (emphasis added).

[¶7] When this statement is construed with the other provisions of the agreement it is clear that Mac guaranteed that Frances would receive $25,000 regardless of what might happen to the commission. The sentence is a directional provision indicating when and how she is to receive the payments. No other provision in the contract pointed to by the majority negates this guarantee; rather, all other provisions are consistent with it. Mac “warranted” the commission was due him and he “guaranteed” the sum of $25,000 would be paid to his ex-wife. In other words, Mac guaranteed that Frances would receive approximately $25,000 from Majors & Majors or any other payor. He further promised that if she failed to receive these payments as he would have prior to assignment directly from the third party payors, he would pay the balance up to $25,000.

[¶8] Mac’s guarantee is unqualified and expresses no other condition for its enforceability than default of performance by the principal obligor. It should be treated, therefore, as the guaranty of payment that it is. An unconditional guaranty for payment becomes a primary obligation upon default. *See Ferguson v. McCarrell*, 588 S.W.2d 895 (Tex.1979); *Universal Metal & Machinery, Inc. v. Bohart*, 539 S.W.2d 874, 877 (Tex.1976).

[¶9] The majority curiously finds ambiguity in the words “guarantee,” “for any reason,” “agrees to pay wife,” “all such sums of money which she failed to receive,” and “up to the guaranteed sum of $25,000.” No

draftsman could have made it any plainer. The finding of an ambiguity in this language, which is neither negated nor qualified elsewhere in the contract, expressly or impliedly, is without justification.

[¶10] I would, therefore, affirm the judgment of the court of appeals, and hold that Mac agreed to pay Frances the $25,000, and that she is entitled to recover the balance of $10,682.84 from him.

Questions:

1. What do you think? Who has the better argument in this 5–4 decision?

2. If the commission on the Jinkens ranch sale had been paid to Majors & Majors but Majors & Majors had refused to pay it to Frances, would we have any ambiguity?

3. Who decides whether a provision is ambiguous, jury or court?

4. Now the case is going back to trial. What do you suppose will be offered in evidence to show the “true intent of the parties” now that the contract itself has been ruled ambiguous on that issue? Why don’t we just ask the parties what they meant?

5. In paragraph [10] of the majority opinion, in the footnote insert, you have a substantive presumption in favor of non-liability of guarantors. By “substantive presumption,” we mean that the court by law construes contractual language in favor of a substantive position, here the non-liability of guarantors. What policy do you suppose supports the interpretive presumption in favor of guarantors?

6. What is Justice Speers doing in order to claim that no ambiguity exists?

7. In this case, the trial court, the intermediate court of appeals (3 judges), and the dissent (4 judges) believe the contract is not ambiguous. Five justices in the Supreme Court’s majority think it is ambiguous. If we count judicial noses, the majority is wrong. Does that mean the contract is not ambiguous under the law?

8. Both parties here claimed that the contract was not ambiguous; they just claimed that it unambiguously meant different things. Does the parties’ agreement that the contract is not ambiguous play any role in the court’s decision? If both parties believed that the contract was ambiguous, do you think that it would play any greater role? Whose opinion matters?

9. What sorts of policy concerns could possibly justify this holding? The trial court evidence will be he-said, she-said, perhaps. On the other side, doesn’t Justice Spears care what actually happened? Policy-wise, what would you argue on either side?

10. What should be your advice to drafters after reading this case?

Caution! The Parol Evidence Rule.

Coker did not do this, but most cases in this area of the law (and this section of the casebook) mention a rule of contract law called the "parol evidence rule."

The word *parol* is an older "Law French" term meaning words or speech. J.H. Baker, *Manual of Law French* 165 (1990). Its legal meaning has expanded to include something like "anything that is not written in the document at issue." This might be spoken words but it also might be writing in other documents not formally connected to the contract or other actions of the parties. A letter written between the parties during negotiations, for instance, would be "parol" as the word is often used. Parol evidence is always outside the "four corners."

The parol evidence rule is a different rule than the plain meaning rule, though some courts and commentators confusingly use the "parol evidence rule" label for both the parol evidence rule and the plain meaning rule. The two rules have very different functions within the law. Be careful not to confuse them.

The plain meaning rule applies to all words in a contract, whether oral or written.

The parol evidence rule applies, on the other hand, *because* the parties have chosen to put their contract in a writing. Putting a contract in writing is a significant act, and the parol evidence rule takes account of that significance. The rule attaches great importance to the document. The basic terms of the parol evidence rule are simply stated:

> If the parties have agreed that a written document will be the final expression of their agreement, then the document cannot be contradicted by evidence of (or from) any prior or contemporaneous promise or agreement.
>
> If the parties have agreed that the document is complete, then it cannot be supplemented by any prior or contemporaneous promise or agreement.

The "parol" evidence rule's name includes the word "parol," yes; but with the expanded meaning of that word, the "parol evidence rule" applies to any (and all) prior or contemporaneous promise or agreement, including other written ones, that contradict or supplement the specified written contract. In this usage, the document designated by the parties controls, and everything else is just "words." The parol evidence rule polices the content of a contract by saying which words are included in the contract. The parol evidence rule is not about the meaning of those words; that is determined by the plain meaning rule and the other rules you learn in this section. The parol evidence rule is about what words are included in the contract at all, and the parol evidence rule applies any time the parties have put their agreement in writing.

The parol evidence rule is harder to apply than to state, for various reasons we will talk about soon when we cover the rule. However, you should know that courts often refer explicitly or implicitly to the parol evidence rule when they discuss the plain meaning rule. Courts also use language that sometimes makes you think they may be referring to both rules, and if you are confused, you may have to determine from context which one they are applying.

Many of the policy concerns that animate the plain meaning rule also support the parol evidence rule, and that leads some less careful courts to mix the two rules together. In fact, judicial statements about the parol evidence rule are famously confusing. Let the language above describing the parol evidence rule be your guide, put yourself in information-gathering mode only on the parol evidence rule for now, and we will try to sort it out when we get to it. For now, remember this: The parol evidence rule does not address the meaning of words; it is not about ambiguity and what language means. The parol evidence rule is irrelevant to those issues.

Aside—Canons of Construction and Plain Meaning

Some rules of interpretation seem to be pretty universal. For example, rules written down by Rabbi Yishmael around 200 C.E. for interpreting Jewish Law indicate that "a matter is elucidated from its context." As an example, one of the Ten Commandments is "thou shalt not steal." This is considered a capital offense in Jewish Law because it falls between two other capital offenses—"thou shalt not kill" and "thou shalt not commit adultery." Because only one kind of theft in Jewish law could be a capital offense—kidnapping a fellow Jew and treating him as a slave—Jewish legal scholars conclude that "thou shalt not steal" in the Ten Commandments refers only to kidnapping.[1] Which of the following canons or maxims of contract interpretation is most like "a matter is elucidated from its context"?

Expressio unius exclusio alterius est: The expression of one is the exclusion of the other. In *Ulmer v. Harsco Corp.*, the court considered whether severance payments had to be paid to employees who were terminated as part of the sale of the business. The employer's "Severance Pay Policy" or "Plan" stated when severance would be paid and specified exceptions. The Court reasoned:

> In sum, while the language of the Plan is general, it is not ambiguous on its face. It clearly states that "where employment is terminated"—the language Harsco used to describe its action in its letter to employees—severance would be paid. Jt. App. at 449. Since the Plan gives several exemptions to this rule—"death, disability, retirement and military leave," Jt. App. at 450—one may assume under the principle of *expressio unius exclusio alterius* that other exemptions such as going concern sales were not intended.

Ulmer v. Harsco Corp., 884 F.2d 98, 103-04 (3d Cir. 1989). For this and other reasons, the court reversed summary judgment in favor of the employer.

[1] Thanks to Michael Rothenberg, STCLH Class of '02, for the translation and explanation.

Noscitur a sociis: It is known from its associates. Under the doctrine of *noscitur a sociis*, "the meaning of a word or phrase may be ascertained by reference to the meaning of other words and phrases with which it is associated." *Wolfe v. Forbes*, 217 S.E.2d 899, 900 (W. Va. 1975).

United States Supreme Court Justice Antonin Scalia discussed the meaning of this rule by illustration: "If you tell me, 'I took the boat out on the bay,' I understand 'bay' to mean one thing; if you tell me, 'I put the saddle on the bay,' I understand it to mean something else." *A Matter of Interpretation*, (Princeton, New Jersey: Princeton University Press, 1997), p 26.

G.C. Timmis & Co. v. Guardian Alarm Co., 2003 WL 21399027 (Mich., June 18, 2003) (Young, J. dissenting).

Ejusdem generis: In applying this maxim, meaning is given to a general term in the following manner:

> [T]he general term is restricted to include only things of the same kind, class, character, or nature as those specifically enumerated"; that is, because the listed items have a commonality, the general term is taken as sharing it.
>
> In *A Matter of Interpretation* (Princeton, New Jersey: Princeton University Press, 1997), p. 26, United States Supreme Court Justice Antonin Scalia explains that the *ejusdem generis* canon of statutory construction stands for the proposition that when a text lists a series of items, a general term included in the list should be understood to be limited to items of the same sort. For instance, if someone speaks of using "tacks, staples, screws, nails, rivets, and other things," the general term "other things" surely refers to other fasteners.

Weakland v. Toledo Engineering Co., Inc., 656 N.W.2d 175, 178 & n.1 (Mich. 2003).

> Under the doctrine of *ejusdem generis*, when a statutory clause specifically describes several classes of things and then includes "other things," the word "other" is interpreted as meaning "other such like." *People v. Davis*, 199 Ill.2d 130, 138, 262 Ill. Dec. 721, 766 N.E.2d 641, 645 (2002).
>
> Applying the doctrine of *ejusdem generis* and strictly construing the container exemption, we determine a vehicle's glove compartment is not an "other container" under the container exemption. A glove compartment is fundamentally different from a case, firearm carrying box, or shipping box because those receptacles are portable whereas a glove compartment is a fixed area in the dashboard of a vehicle. Therefore, a glove compartment is not an "other container" similar to the ones enumerated in the container exemption.

People v. Cameron, 784 N.E.2d 438 (Ill. App. 4 Dist., 2003). *Ejusdem generis* is a subcategory of *noscitur a sociis*.

Omnia praesumuntur contra proferentem: Ambiguous terms must be construed against the drafter of the contract.

> Because the contract as a whole can be reasonably interpreted to support either Mead's or ABB Power's position regarding the scope of the indemnity clause, we conclude that the contract is ambiguous as to this issue. Under Ohio law, "[a]mbiguous contractual language will be construed against the drafter of the contract." *Lelux v. Chernick*, 119 Ohio App.3d 6, 694 N.E.2d 471, 473 (1997) (citing *Cent. Realty Co. v. Clutter*, 62 Ohio St.2d 411, 406 N.E.2d 515, 517 (1980)). Because Mead drafted the contract, the ambiguity should be resolved in favor of ABB Power.

Mead Corp. v. ABB Power Generation, Inc., 319 F.3d 790, 798-99 (6th Cir. 2003).

Ut magis valeat quam pereat: "It is a fundamental rule that a contract must, if possible, be so construed as to effectuate the intention of the parties and to sustain the contract, *ut res magis valeat quam pereat*." *Baker v. Baker*, 139 Ill. App. 217 (Ill. App. 1 Dist. 1908). "First, it is fundamental that an interpretation of a contract which results in termination of the contract is disfavored over one which affirms the existence of the contract." *Simeone v. First Bank Nat. Ass'n*, 971 F.2d 103, 107 (8th Cir. 1992).

An operative intention is presumed:

> We follow the established general rules that provisions of a contract must be so construed as to effectuate its spirit and purpose, that it must be considered as a whole and interpreted so as to harmonize and give meaning to all of its provisions, and that an interpretation which gives a reasonable meaning to all parts will be preferred to one which leaves a portion of it useless, inexplicable, inoperative, void, insignificant, meaningless, superfluous . . . ."

State of Ariz. v. U. S., 575 F.2d 855, 863 (Ct. Cl. 1978). This rule is an application of or at least is related to *ut magis valeat quam pereat*. Something like this rule is often said when courts consider the recitals, or "whereas" clauses, at the beginning of a contract: they "may be looked to in determining the proper construction of the contract and the parties' intention." In re *Strickland's Estate*, 149 N.W.2d 344, 351 (Neb. 1967).

Specific terms control over conflicting general terms:

> We have held that a contract will be construed most strongly against the party who drafted it. *Security State Bank of Basin v. Newton*, Wyo., 707 P.2d 173 (1985). We also have held that general terms and provisions in a contract yield to specific ones, if not reconcilable. *Flora Construction Company v. Bridger Valley Electric Association, Inc.*, Wyo., 355 P.2d 884 (1960). Applying these rules, we find that the specific typewritten description of the collateral which the parties inserted into the printed form controls over the general description contained in the standard printed form.

Landen v. Production Credit Ass'n of Midlands, 737 P.2d 1325, 1328 (Wyo. 1987).

"When construing a contract on a printed form and there is an apparent conflict, writing prevails over printing, handwriting over typewriting, and typewriting over printing." *In re Greives*, 81 B.R. 912, 953 (Bkrtcy., N.D. Ind. 1987). Why do you suppose this is? (By printing, the court meant "pre-printed," not printed on a printer receiving files from a laptop—the case is from 1987, after all.)

In contracts affecting the public interest, an interpretation favoring the public interest is preferred:

> The court is mindful that "contracts affecting the public's interest generally are liberally interpreted to favor the public." *Simon v. Farmland Indus., Inc.*, 505 F. Supp. 59, 61 (D.Kan.1980) (citing *United States v. Kan. Gas and Elec. Co.*, 215 F. Supp. 532, 542 (D.Kan.1963)). Here, the Agreement clearly affects the public interest.
>
> The public, as consumers of cable television services, has an interest in paying reasonable rates for those services. Thus, the public interest is served when consumers are given choices about whom they can select to provide their cable service. Moreover, the public has an interest in avoiding the potential disruption of having their home wiring removed upon the voluntary termination of the incumbent provider's service and then, subsequently, having the new provider install its home run wiring. The FCC Report makes clear that these are stated purposes of the Telecommunications Act of 1996, the act under which the FCC Home Run Wiring Rules were promulgated. See e.g., FCC Report ¶ 36 ("[The Telecommunication Acts] was [sic] intended to promote consumer choice and competition by permitting subscribers to avoid the disruption of having their home wiring removed upon voluntary termination and to subsequently utilize that wiring for an alternative service[.]"). Accordingly, because the Agreement at issue affects the public interest, the court will, where appropriate, liberally construe the Agreement to favor the public.

Time Warner Entertainment Co., L.P. v. Atriums Partners, L.P., 232 F. Supp.2d 1257, 1265-66 (D. Kan. 2002).

Grammar and punctuation rules normally apply:

> Absent the presentation of other evidence, the trial court resolves ambiguity by interpreting the contract using accepted canons of construction and traditional rules of grammar and punctuation.

Monette v. Tinsley, 975 P.2d 361 ¶ 13 (N.M. App. 1999).

PROBLEM 43: Jill agreed to assign and sell to Sam her ten-agent insurance office and business. The two obtained Jill's landlord's permission to transfer her lease. Sam's lawyer drew up an agreement for the sale, which both signed. The agreement stated in the recitals that its purpose was "to allow Sam to continue on in the business just as Jill had done." Handwritten and initialed above this recital and inserted after it were the words, "and to allow Jill to retire and reap the rewards of years of service in the insurance industry." A clause in the contract (immediately following a description of the leased premises) included in the sale and assignment, stated:

> all computer hardware and software, files and databases, copy machines, cash registers, telephone system, and other personal property.

A separate provision of the agreement provided for transfer of software licenses. After Jill and Sam signed the sale agreement, relations soured. On the day set for the closing of the sale and the transfer of the premises, Sam arrived at the office to find that Jill had taken all of the furniture, including numerous file cabinets and their contents. Sam sued for an injunction ordering return of the files and furniture (or, for the furniture, in the alternative, damages). Sam argued that the files contained current customer records necessary for the business to continue. Jill countered that she needed the files' contents in order to collect ongoing commissions on policy renewals, and that the files were not part of their deal.

What effect do the canons have on this dispute?

PACIFIC GAS AND ELECTRIC COMPANY v. G. W. THOMAS DRAYAGE & RIGGING COMPANY, INC.

California Supreme Court (1968)

69 Cal. Rptr. 561, 422 P.2d 641

OPINION

TRAYNOR, C. J.

[¶1] Defendant appeals from a judgment for plaintiff in an action for damages for injury to property under an indemnity clause of a contract.

[¶2] In 1960 defendant entered into a contract with plaintiff to furnish the labor and equipment necessary to remove and replace the upper metal cover of plaintiff's steam turbine. Defendant agreed to perform the work "at [its] own risk and expense" and to "indemnify" plaintiff "against all loss, damage, expense and liability resulting from . . . injury to property, arising out of or in any way connected with the performance of this contract." Defendant also agreed to procure not less than $50,000 insurance to cover liability for injury to property. Plaintiff was to be an additional named insured, but the policy was to contain a cross-liability clause extending the coverage to plaintiff's property.

[¶3] During the work the cover fell and injured the exposed rotor of the turbine. Plaintiff brought this action to recover $25,144.51, the amount it subsequently spent on repairs. During the trial it dismissed a count based on negligence and thereafter secured judgment on the theory that the indemnity provision covered injury to all property regardless of ownership.

[¶4] Defendant offered to prove by admissions of plaintiff's agents, by defendant's conduct under similar contracts entered into with plaintiff, and by other proof that in the indemnity clause the parties meant to

cover injury to property of third parties only and not to plaintiff's property.******** Although the trial court observed that the language used was "the classic language for a third party indemnity provision" and that "one could very easily conclude that . . . its whole intendment is to indemnify third parties," it nevertheless held that the "plain language" of the agreement also required defendant to indemnify plaintiff for injuries to plaintiff's property. Having determined that the contract had a plain meaning, the court refused to admit any extrinsic evidence that would contradict its interpretation. * * * *

[¶5] The test of admissibility of extrinsic evidence to explain the meaning of a written instrument is not whether it appears to the court to be plain and unambiguous on its face, but whether the offered evidence is relevant to prove a meaning to which the language of the instrument is reasonably susceptible. [Omitted: a long list of citations.]

[¶6] A rule that would limit the determination of the meaning of a written instrument to its four-corners merely because it seems to the court to be clear and unambiguous, would either deny the relevance of the intention of the parties or presuppose a degree of verbal precision and stability our language has not attained.

[¶7] Some courts have expressed the opinion that contractual obligations are created by the mere use of certain words, whether or not there was any intention to incur such obligations.†††††††† Under this view, contractual obligations flow, not from the intention of the parties but from the fact that they used certain magic words. Evidence of the parties' intention therefore becomes irrelevant.

[¶9] In this state, however, the intention of the parties as expressed in the contract is the source of contractual rights and duties.‡‡‡‡‡‡‡‡ A court must ascertain and give effect to this intention by determining what the parties meant by the words they used. Accordingly, the exclusion of relevant, extrinsic, evidence to explain the meaning of a written instrument could be justified only if it were feasible to determine the meaning the parties gave to the words from the instrument alone.

******** [1] Although this offer of proof might ordinarily be regarded as too general to provide a ground for appeal (Evid. Code, § 354, subd. (a); Beneficial etc. Ins. Co. v. Kurt Hitke & Co. (1956) 46 Cal.2d 517, 522; Stickel v. San Diego Elec. Ry. Co. (1948) 32 Cal.2d 157, 162-164; Douillard v. Woodd (1942) 20 Cal.2d 665, 670), since the court repeatedly ruled that it would not admit extrinsic evidence to interpret the contract and sustained objections to all questions seeking to elicit such evidence, no formal offer of proof was required. (Evid. Code, § 354, subd. (b); Beneficial etc. Ins. Co. v. Kurt Hitke & Co., supra, 46 Cal.2d 517, 522; Estate of Kearns (1950) 36 Cal.2d 531, 537.)

†††††††† [4] "A contract has, strictly speaking, nothing to do with the personal, or individual, intent of the parties. A contract is an obligation attached by the mere force of law to certain acts of the parties, usually words, which ordinarily accompany and represent a known intent." (Hotchkiss v. National City Bank of New York (S.D.N.Y. 1911) 200 F. 287, 293. See also C. H. Pope & Co. v. Bibb Mfg. Co. (2d Cir. 1923) 290 F. 586, 587; see 4 Williston on Contracts (3d ed. 1961) § 612, pp. 577-578, § 613, p. 583.)

‡‡‡‡‡‡‡‡ [5] "A contract must be so interpreted as to give effect to the mutual intention of the parties as it existed at the time of contracting, so far as the same is ascertainable and lawful." (Civ. Code, § 1636; see also Code Civ. Proc., § 1859; Universal Sales Corp. v. California Press Mfg. Co. (1942) 20 Cal.2d 751, 760; Lemm v. Stillwater Land & Cattle Co. (1933) 217 Cal. 474, 480.)

[¶10] * * * * Words, however, do not have absolute and constant referents. * * * * The meaning of particular words or groups of words varies with the ". . . verbal context and surrounding circumstances and purposes in view of the linguistic education and experience of their users and their hearers or readers (not excluding judges). . . . A word has no meaning apart from these factors; much less does it have an objective meaning, one true meaning." (Corbin, The Interpretation of Words and the Parol Evidence Rule (1965) 50 Cornell L.Q. 161, 187.) Accordingly, the meaning of a writing ". . . can only be found by interpretation in the light of all the circumstances that reveal the sense in which the writer used the words. The exclusion of parol evidence regarding such circumstances merely because the words do not appear ambiguous to the reader can easily lead to the attribution to a written instrument of a meaning that was never intended. * * * *" * * * *

[¶11] Although extrinsic evidence is not admissible to add to, detract from, or vary the terms of a written contract, these terms must first be determined before it can be decided whether or not extrinsic evidence is being offered for a prohibited purpose. The fact that the terms of an instrument appear clear to a judge does not preclude the possibility that the parties chose the language of the instrument to express different terms. That possibility is not limited to contracts whose terms have acquired a particular meaning by trade usage,§§§§§§§§ but exists whenever the parties' understanding of the words used may have differed from the judge's understanding.

[¶12] Accordingly, rational interpretation requires at least a preliminary consideration of all credible evidence offered to prove the intention of the parties.********* (Civ. Code, § 1647; Code Civ. Proc., § 1860; see also 9 Wigmore on Evidence, op. cit. supra, § 2470, fn. 11, p. 227.) Such evidence includes testimony as to the "circumstances surrounding the making of the agreement . . . including the object, nature and subject matter of the writing . . ." so that the court can "place itself in the same situation in which the parties found themselves at the time of contracting." [Citations.] If the court decides, after considering this evidence, that the language of a contract, in the light of all the circumstances, "is fairly susceptible of either one of the

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§§§§§§§§ [6] Extrinsic evidence of trade usage or custom has been admitted to show that the term "United Kingdom" in a motion picture distribution contract included Ireland (Ermolieff v. R.K.O. Radio Pictures, Inc. (1942) 19 Cal.2d 543, 549-552); that the word "ton" in a lease meant a long ton or 2,240 pounds and not the statutory ton of 2,000 pounds (Higgins v. California Petroleum etc. Co. (1898) 120 Cal. 629, 630-632); that the word "stubble" in a lease included not only stumps left in the ground but everything "left on the ground after the harvest time" (Callahan v. Stanley (1881) 57 Cal. 476, 477-479); that the term "north" in a contract dividing mining claims indicated a boundary line running along the "magnetic and not the true meridian" (Jenny Lind Co. v. Bower (1858) 11 Cal. 194, 197-199) and that a form contract for purchase and sale was actually an agency contract. (Body-Steffner Co. v. Flotill Products (1944) 63 Cal.App.2d 555, 558-562). See also Code Civ. Proc., § 1861; Annot., 89 A.L.R. 1228; Note (1942) 30 Cal. L. Rev. 679.)

********* [7] When objection is made to any particular item of evidence offered to prove the intention of the parties, the trial court may not yet be in a position to determine whether in the light of all of the offered evidence, the item objected to will turn out to be admissible as tending to prove a meaning of which the language of the instrument is reasonably susceptible or inadmissible as tending to prove a meaning of which the language is not reasonably susceptible. In such case the court may admit the evidence conditionally by either reserving its ruling on the objection or by admitting the evidence subject to a motion to strike. (See Evid. Code, § 403.)

two interpretations contended for . . .” * * * , extrinsic evidence relevant to prove either of such meanings is admissible.†

[¶13] In the present case the court erroneously refused to consider extrinsic evidence offered to show that the indemnity clause in the contract was not intended to cover injuries to plaintiff’s property. Although that evidence was not necessary to show that the indemnity clause was reasonably susceptible of the meaning contended for by defendant, it was nevertheless relevant and admissible on that issue. Moreover, since that clause was reasonably susceptible of that meaning, the offered evidence was also admissible to prove that the clause had that meaning and did not cover injuries to plaintiff’s property.‡ Accordingly, the judgment must be reversed. * * * *

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† [8] Extrinsic evidence has often been admitted in such cases on the stated ground that the contract was ambiguous (e.g., Universal Sales Corp. v. California Press Mfg. Co., supra, 20 Cal.2d 751, 761). This statement of the rule is harmless if it is kept in mind that the ambiguity may be exposed by extrinsic evidence that reveals more than one possible meaning.

‡ [9] The court’s exclusion of extrinsic evidence in this case would be error even under a rule that excluded such evidence when the instrument appeared to the court to be clear and unambiguous on its face. The controversy centers on the meaning of the word “indemnify” and the phrase “all loss, damage, expense and liability.” The trial court’s recognition of the language as typical of a third party indemnity clause and the double sense in which the word “indemnify” is used in statutes and defined in dictionaries demonstrate the existence of an ambiguity. (Compare Civ. Code, § 2772, “Indemnity is a contract by which one engages to save another from a legal consequence of the conduct of one of the parties, or of some other person,” with Civ. Code, § 2527, “Insurance is a contract whereby one undertakes to indemnify another against loss, damage, or liability, arising from an unknown or contingent event.” Black’s Law Dictionary (4th ed. 1951) defines “indemnity” as “A collateral contract or assurance, by which one person engages to secure another against an anticipated loss or to prevent him from being damnified by the legal consequences of an act or forbearance on the part of one of the parties or of some third person.” Stroud’s Judicial Dictionary (2d ed. 1903) defines it as a “Contract . . . to indemnify against a liability . . . .” One of the definitions given to “indemnify” by Webster’s Third New International Dict. (1961 ed.) is “to exempt from incurred liabilities.”)

Plaintiff’s assertion that the use of the word “all” to modify “loss, damage, expense and liability” dictates an all inclusive interpretation is not persuasive. If the word “indemnify” encompasses only third-party claims, the word “all” simply refers to all such claims. The use of the words “loss,” “damage,” and “expense” in addition to the word “liability” is likewise inconclusive. These words do not imply an agreement to reimburse for injury to an indemnitee’s property since they are commonly inserted in third-party indemnity clauses, to enable an indemnitee who settles a claim to recover from his indemnitor without proving his liability. (Carpenter Paper Co. v. Kellogg (1952) 114 Cal.App.2d 640, 651. Civ. Code, § 2778, provides: “1. Upon an indemnity against liability . . . the person indemnified is entitled to recover upon becoming liable; 2. Upon an indemnity against claims, or demands, or damages, or costs . . . the person indemnified is not entitled to recover without payment thereof; . . .”)

The provision that defendant perform the work “at his own risk and expense” and the provisions relating to insurance are equally inconclusive. By agreeing to work at its own risk defendant may have released plaintiff from liability for any injuries to defendant’s property arising out of the contract’s performance, but this provision did not necessarily make defendant an insurer against injuries to plaintiff’s property. Defendant’s agreement to procure liability insurance to cover damages to plaintiff’s property does not indicate whether the insurance was to cover all injuries or only injuries caused by defendant’s negligence.

The judgment is reversed.

Peters, J., Mosk, J., Burke, J., Sullivan, J., and Peek, J., fn.* concurred.

McComb, J., dissented.

Questions:

1. How does Justice Traynor know even without extrinsic evidence that the word *indemnify* is reasonably susceptible to the meaning that excluded coverage of injuries to the plaintiff's property? Evidence of what kind of meaning for the word *indemnify* would be excluded under Traynor's view?

2. Would Traynor accept evidence that the word *indemnify* meant that the defendant was supposed to pay for a backpacking trip in the Himalayas?

3. To whom was the contract written? Should that make a difference?

4. One of the reasons *PG&E* is worth your time is ¶¶ 11–12's description of the process of evidence-taking. Given the plain meaning rule, the process for determining whether to admit evidence regarding the meaning of words in a contract—deciding whether to send the issue to the jury—requires several steps. First, one of the lawyers proposes introducing evidence. Often, the motion will state what that evidence is. Sometimes, the motion will attach an affidavit or deposition testimony showing the evidence. At least, the motion will offer the evidence to the court (sometimes we use the Anglo-French word *proffer*, as in "proffer the evidence"). The opposing party will oppose the motion with arguments that the evidence should not be admitted (go to the jury) because it is factually or legally irrelevant. Almost always, the court has to know what the evidence is in order to rule whether it is admissible. That is what *PG&E* is talking about in those paragraphs. After the court hears arguments on both sides and considers the evidence itself (if it thinks that is necessary), the court will decide whether to let the evidence go to the jury.

Courts necessarily have a lot of discretion at that stage because each case is unique. The contract term at issue is probably different than any other contract term, and these parties and their circumstances and the evidence they present for this contract have never occurred in this combination before. Moreover, judges' experience and understanding of the law and the situation differ. Likely no two judges would agree wholly on the results in any twenty fact patterns, and probably the number should be much lower than twenty. The presence of discretion and the uniqueness of the facts to each case make interpretation the most litigated issue in contract law.

In *PG&E* itself, the trial court decided not to exercise its discretion. The trial court oddly concluded both that *indemnity* could mean only one of two things (see ¶ 4: "one could very easily conclude that . . . its whole intendment is to indemnify third parties") but that in this case *indemnity* plainly meant, on its face, the other of the two things. This made no sense. In reversing, the court instructed trial courts everywhere to consider the proffered evidence. After all, the evidence might reveal some ambiguity that was not obvious—a latent ambiguity. That was not the case in *PG&E* itself, but courts should be ready for the possibility.

Soper's Estate is a good example of how that possibility can become reality. *In re Soper's Estate*, 264 N.W. 427 (Minn. 1935), reported the following facts: Ira Soper married Adeline Westphal in October 1911. He lived with her in Louisville, Kentucky, until August 1921, when he suddenly disappeared. Their marriage was not always happy. Soper would go on "drunken sprees." He had gone on a spree just prior to disappearing. But, just prior to disappearing, he had written suicide notes to his wife: "If there is any hereafter may meet you again." Soper's car was found at the bank of a nearby canal along with his hat and portions of his clothing. Pinned to his business card and left in his car was a note reading, "This belongs to Mrs. Soper."

In fact, Soper went to Canada and then Minneapolis, where he called himself John W. Young. He started a fuel company, the Young Fuel Company, with another fellow, Karstens. In May 1927, he purported to marry Gertrude Whitby, a widow, and they lived together as husband and wife until Soper-Young really did commit suicide in 1932. Ms. Whitby had believed Soper to be a widower when they met.

After Soper married Whitby, he and Karstens created a joint stock insurance plan under which one was to buy the stock of the other if the other should die. The payments were to come from the insurance plan, and they were to be paid to the surviving "wife" of the other, if living. Soper referred to Whitby as his wife during the negotiations. The premiums were paid by the company as an expense.

When Soper died, the insurance trustee paid the proceeds over to Ms. Whitby. At the time, no one involved knew of Adeline Westphal Soper. Several months elapsed before the real Mrs. Soper showed up. The administrator of Soper's estate then sued Ms. Whitby for return of the funds so that they could be awarded to the "wife." Is "wife" ambiguous without the extrinsic evidence? With it? Who should win? There could only be one legal wife. Is there any way to identify "wife" without extrinsic evidence? The court let Whitby keep the money over a dissenting vote.

5. The idea that extrinsic evidence could show ambiguity that would not exist without that evidence seems contrary to much of the rhetoric of Justice Spears's dissent in *Coker*. Would it surprise you to hear that courts have argued over the meaning and effect of *PG&E*? The court in *Trident Center v. Connecticut General Life Ins. Co.*, 847 F.2d 564 (9th Cir. 1988), said,

> Under *Pacific Gas,* it matters not how clearly a contract is written, nor how completely it is integrated, nor how carefully it is negotiated, nor how squarely it addresses the issue before the court: the contract cannot be rendered impervious to attack by parol evidence. If one side is willing to claim that the parties intended one thing but the agreement provides for another, the court must consider extrinsic evidence of possible ambiguity. If that evidence raises the specter of ambiguity where there was none before, the contract language is displaced and the intention of the parties must be divined from self-serving testimony offered by partisan witnesses whose recollection is hazy from passage of time and colored by their conflicting interests.

A California court of appeals countered in *ACL Technologies, Inc. v. Northbrook Property & Casualty Ins. Co.*, 22 Cal. Rptr. 2d 206, 219 (Cal. App. 4 Dist. 1993),

> With all due respect to the critics of *Pacific Gas*, the case is not an endorsement of linguistic nihilism. Despite what might be called its "deconstructionist" dictum, the actual holding of

> the case is a fairly modest one: courts should allow parol evidence to explain special meanings which the individual parties to a contract may have given certain words.

Is either one an adequate characterization of *PG&E*?

2. Substantive Presumptions

Sometimes public policy outside of the general rules of contract law is so influential that it requires that words of contract be construed other than the way we might (even reasonably) expect. You have already seen one substantive presumption in favor of guarantors. What policy is at issue in the following case? What affect does that policy have on the legal meaning of which words?

MONTGOMERY COUNTY HOSPITAL DISTRICT f/d/b/a Medical Center Hospital v. Valarie BROWN

Supreme Court of Texas (1998)

965 S.W.2d 501

[¶1] The principal issue before us is whether at-will employment can be modified by nothing more than an employer's oral assurances that an employee whose work is satisfactory will not be terminated without good cause. We hold that an employer's oral statements do not modify an employee's at-will status absent a definite, stated intention to the contrary. * * * *

[¶2] For ten years Valarie Brown was employed by the Montgomery County Hospital District as laboratory systems manager for Medical Center Hospital. After her employment terminated, Brown brought this action against the District and its president and vice president (collectively, "the District") for breach of oral and written contracts of employment and deprivation of property and liberty interests protected by the Texas Constitution. The district court granted summary judgment for the District. The circumstances surrounding the termination of Brown's employment, vigorously disputed by the parties, are largely irrelevant to the contract issues before us. Given the conflict in the summary judgment record, we accept as true Brown's assertion that she did not voluntarily resign but was fired without good cause. We assume that Brown is not estopped by acceptance of her severance pay to assert that she was wrongfully terminated. And we take Brown's word that:

> At the time I was hired as well as during my employment, I was told by [the Hospital administrator] that I would be able to keep my job at the Hospital as long as I was doing my job and that I would not be fired unless there was a good reason or good cause to fire me. This representation was important to me since I was going to have to relocate from Houston to the Conroe area if I accepted the position with the Hospital.

[¶3] The court of appeals held as a matter of law that the Hospital's employee manual was not an employment contract as Brown claimed, *Brown v. Montgomery County Hosp.,* 929 S.W.2d at 583 (Tex. App.-Beaumont 1996), and Brown has not appealed that ruling. But the appeals court held that fact questions subsisted concerning the existence of an oral employment contract, based on the hospital administrator's alleged assurances, that precluded summary judgment. 929 S.W.2d at 583-585. The court also held that such a contract was not, as a matter of law, barred by the Statute of Frauds, *Tex. Bus. & Com. Code* § 26.01. 929 S.W.2d at 584-585. Because the effect of an employer's oral assurances on at-will employment is an important and recurring issue, we granted the District's application for writ of error. * * * *

[¶4] For well over a century, the general rule in this State, as in most American jurisdictions, has been that absent a specific agreement to the contrary, employment may be terminated by the employer or the employee at will, for good cause, bad cause, or no cause at all. *Federal Express Corp. v. Dutschmann*, 846 S.W.2d 282, 283 (Tex.1993) (per curiam*); Schroeder v. Texas Iron Works*, 813 S.W.2d 483, 489 (Tex.1991); *Winters v. Houston Chronicle Pub. Co.,* 795 S.W.2d 723, 723 (Tex.1990); *Sabine Pilot Serv., Inc. v. Hauck*, 687 S.W.2d 733, 734-35 (Tex.1985); *East Line & R.R.R. Co. v. Scott*, 72 Tex. 70, 10 S.W. 99, 102 (1888). The District argues that its assurances to Brown were too indefinite to constitute an agreement limiting the District's right to discharge Brown at will. We agree.

[¶5] A promise, acceptance of which will form a contract, "is a manifestation of intention to act or refrain from acting in a specified way, so made as to justify a promisee in understanding that a commitment has been made." *Restatement (Second) of Contracts* § 2(1) (1981). General statements like those made to Brown simply do not justify the conclusion that the speaker intends by them to make a binding contract of employment. For such a contract to exist, the employer must unequivocally indicate a definite intent to be bound not to terminate the employee except under clearly specified circumstances.

[¶6] General comments that an employee will not be discharged as long as his work is satisfactory do not in themselves manifest such an intent. Neither do statements that an employee will be discharged only for "good reason" or "good cause" when there is no agreement on what those terms encompass. Without such agreement the employee cannot reasonably expect to limit the employer's right to terminate him. An employee who has no formal agreement with his employer cannot construct one out of indefinite comments, encouragements, or assurances.

[¶7] This is the rule in other states. For example, in *Rowe v. Montgomery Ward & Co.,* 437 Mich. 627, 473 N.W.2d 268 (1991), the court held that a supervisor's assurance that employees would have their jobs "generally, as long as they generated sales and were honest" did not limit the employer's right to discharge an employee at will. Id. at 270. Noting that a decade earlier it had "joined the forefront of a nationwide experiment in which, under varying theories, courts extended job security to nonunionized employees," the court retreated from earlier decisions in which it had been more inclined to find an employment agreement in general assurances made by the employer. Id. at 269. "[C]alling something a contract that is in no sense a contract cannot advance respect for the law," the court wrote. Id. It concluded: "[O]ral statements of job security must be clear and unequivocal to overcome the presumption of employment at will." Id. at 275.

[¶8] Likewise, in *Hayes v. Eateries, Inc.,* 905 P.2d 778 (Okla.1995), the court held that oral assurances that an employee "would be employed as long as he did an adequate job and/or performed his duties satisfactorily" did not constitute "a binding agreement that protected him from discharge except for 'just cause'." Id. at 782. The court explained:

> Courts "must distinguish between carefully developed employer representations upon which an employee may justifiably rely, and general platitudes, vague assurances, praise, and indefinite promises of permanent continued employment." Only when the promises are definite and, thus, of the sort which may be reasonably or justifiably relied on by the employee, will a contract claim be viable, not when the employee relies on only vague assurances that no reasonable person would justifiably rely upon. There is, thus, an objective component to the nature of such a contract claim in the form of definite and specific promises by the employer sufficient to substantively restrict the reasons for termination.

Id. at 783 * * * .

[¶9] There are scores of cases like these throughout the country, and courts in different jurisdictions have reached different conclusions, sometimes on the basis of the particular circumstances, and sometimes because of their view that oral, informal statements in the employment context should simply be given more effect. See generally Theresa Ludwig Kruk, *Annotation, Right to Discharge Allegedly "At-Will" Employee as Affected by Employer's Promulgation of Employment Policies as to Discharge*, 33 A.L.R.4th 120 (1984). From our review of these cases we conclude that those we have cited are better reasoned.

[¶10] Consistent with our holding in the case, the court in *Byars v. City of Austin*, 910 S.W.2d 520, 523-524 (Tex. App.—Austin 1995, writ denied), held that an employee handbook's description of usual disciplinary procedures were not "clear and specific" so as to modify an employment at will. Three other decisions of our intermediate courts that have dealt with statements similar to those made to Brown in this case did not consider whether the statements made were definite enough to constitute an enforceable contract. *Hardison v. A.H. Belo Corp.,* 247 S.W.2d 167 (Tex. Civ. App.—Dallas 1952, no writ); *Johnson v. Ford Motor Co.,* 690 S.W.2d 90 (Tex. App.—Eastland 1985, writ ref'd n.r.e.); *Morgan v. Jack Brown Cleaners, Inc.,* 764 S.W.2d 825 (Tex. App.—Austin 1989, writ denied). To the extent these cases can be read to reach a result contrary to our holding here, we disapprove them.

Accordingly, the judgment of the court of appeals is reversed and judgment is rendered for the District.

Questions:

1. If someone told you that "you will be able to keep your employment as long as you are doing your job and that you will not be fired unless there is a good reason or good cause to fire you," would you reasonably believe that your employment could not be terminated for no reason at all?

2. If you answered "yes" to question 1 or believe that it is plausible to answer "yes" to question 1, under what rule can the court then hold as a matter of law that your reasonable belief does not matter? In other words, why did the court think it necessary to grant review in this case and issue an opinion?

3. Paragraph 9 suggests decisions are not uniform on this issue. Why is this case satisfactory or not as a matter of policy?

4. What is the role of words like *reasonably*, *justifiably*, *objective*, *definite*, and *specific* in paragraph 8?

5. What would Brown have to show that the hospital did in order to escape the holding in this case?

6. Was Brown deceived?

7. What policy would explain the traditional Japanese presumption of lifetime employment?
8. Can you think of any other examples of substantive interpretive presumptions? Why or why not? Consider: "[A] court can compel arbitration where there is an indisputably valid and enforceable arbitration provision and that arbitration provision can be interpreted to encompass the parties' disputes." *Severstal U.S. Holdings, LLC v. RG Steel, LLC*, 865 F. Supp. 2d 430, 439 (S.D.N.Y. 2012). Also consider this: "[B]ecause plea agreements' constitutional and supervisory implications raise concerns over and above those present in the traditional contract context, in interpreting such agreements we hold the government to a greater degree of responsibility than the defendant . . . for imprecisions or ambiguities in the plea agreements. Ambiguities in a plea agreement are therefore construed against the government . . . ." *U.S. v. Bowman*, 634 F.3d 357, 360 (6th Cir. 2011) (internal quotations and citations omitted).

3. Usage, Custom, and Prior Practice

All contracts have context, and sometimes only a reference to the context can resolve a dispute over the meaning of contractual language. The doctrine in this section allows the court access to that context.

Herman FISHER v. CONGREGATION B'NAI YITZHOK

Pa. Superior Ct. (1955)

110 A.2d 881

OPINION BY HIRT, J.

[¶1] Plaintiff is an ordained rabbi of the orthodox Hebrew faith. He however does not officiate except on occasion as a professional rabbi-cantor in the liturgical service of a synagogue. The defendant is an incorporated Hebrew congregation with a synagogue in Philadelphia. Plaintiff, in response to defendant's advertisement in a Yiddish newspaper, appeared in Philadelphia for an audition before a committee representing the congregation. As a result, a written contract was entered into on June 26, 1950, under the terms of which plaintiff agreed to officiate as cantor at the synagogue of the defendant congregation "for the High Holiday Season of 1950", at six specified services during the month of September 1950. As full compensation for the above services the defendant agreed to pay plaintiff the sum of $1,200.

[¶2] The purpose upon which the defendant congregation was incorporated is thus stated in its charter: "The worship of Almighty God according to the faith, discipline, forms and rites of the orthodox Jewish religion." And up to the time of the execution of the contract the defendant congregation conducted its

religious services in accordance with the practices of the orthodox Hebrew faith. On behalf of the plaintiff there is evidence that under the law of the Torah and other binding authority of the Jewish law, men and women may not sit together at services in the synagogue. In the orthodox synagogue, where the practice is observed, the women sit apart from the men in a gallery, or they are separated from the men by means of a partition between the two groups. The contract in this case is entirely silent as to the character of the defendant as an orthodox Hebrew congregation and the practices observed by it as to the seating at the services in the synagogue. At a general meeting of the congregation on July 12, 1950, on the eve of moving into a new synagogue, the practice of separate seating by the defendant formerly observed was modified and for the future the first four rows of seats during religious services were set aside exclusively for the men, and the next four rows for the women, and the remainder for mixed seating of both men and women. When plaintiff was informed of the action of the defendant congregation in deviating from the traditional practice as to separate seating, he through his attorney notified the defendant that he, a rabbi of the orthodox faith, would be unable to officiate as cantor because "this would be a violation of his beliefs." Plaintiff persisted in the stand taken that he would not under any circumstances serve as cantor for defendant as long as men and women were not seated separately. And when defendant failed to rescind its action permitting men and women to sit together during services, plaintiff refused to officiate. It then was too late for him to secure other employment as cantor during the 1950 Holiday season except for one service which paid him $100, and he brought suit for the balance of the contract price.

[¶3] The action was tried before the late Judge Fenerty, without a jury, who died before deciding the issue. By agreement the case was disposed of by the late President Judge Frank Smith "on the notes of testimony taken before Judge Fenerty." At the conclusion of the trial, counsel had stipulated that the judge need not make specific findings of fact in his decision. This waiver applied to the disposition of the case by Judge Smith. Nevertheless Judge Smith did specifically find that defendant, at the time the contract was entered into, "Was conducting its services according to the Orthodox Hebrew Faith." Judge Smith accepted the testimony of three rabbis learned in Hebrew law, who appeared for plaintiff, to the effect: "That Orthodox Judaism required a definite and physical separation of the sexes in the synagogue." And he also considered it established by the testimony that an orthodox rabbi-cantor "could not conscientiously officiate in a 'trefah' synagogue, that is, one that violates Jewish law"; and it was specifically found that the old building which the congregation left, "had separation in accordance with Jewish orthodoxy." The ultimate finding was for the plaintiff in the sum of $1,100 plus interest. And the court entered judgment for the plaintiff on the finding. In this appeal it is contended that the defendant is entitled to judgment as a matter of law.

[¶4] The finding for the plaintiff in this trial without a jury has the force and effect of a verdict of a jury and in support of the judgment entered by the lower court, the plaintiff is entitled to the benefit of the most favorable inferences from the evidence. *Jann v. Linton's Lunch,* 150 Pa. Superior Ct. 653, 29 A.2d 219. Findings of fact by a trial judge, sitting without a jury, which are supported by competent substantial evidence are conclusive on appeal. *Scott-Smith Cadillac Co., Inc. v. Rajeski*, 166 Pa. Superior Ct. 116, 70 A.2d 454.

[¶5] Although the contract is silent as to the nature of the defendant congregation, there is no ambiguity in the writing on that score and certainly nothing was omitted from its terms by fraud, accident or mistake. The terms of the contract therefore could not be varied under the parol evidence rule. *Bardwell v. The Willis Company*, 375 Pa. 503, 100 A.2d 102*; Mathers v. Roxy Auto Company*, 375 Pa. 640, 101 A.2d 680. Another principle controls the interpretation of this contract.

[¶6] There is sufficient competent evidence in support of the finding that this defendant was an orthodox congregation, which observed the rule of the ancient Hebrew law as to separate seating during the services of the High Holiday Season; and also to the effect that the rule has been observed immemorially and invariably by the defendant in these services, without exception. As bearing on plaintiff's bona fide belief that such was the fact, at the time he contracted with the defendant, plaintiff was permitted to introduce the declaration of Rabbi Ebert, the rabbi of the defendant congregation, made to him prior to signing of the contract, in which the rabbi said: "There always was a separation between men and women' and 'there is going to be strict separation between men and women', referring to the seating in the new synagogue. Rabbi Lipschitz, who was present, testified that Rabbi Ebert, in response to plaintiff's question 'Will services be conducted as in the old Congregation' replied 'Sure. There is no question about that' referring to the prior practice of separate seating. The relationship of rabbi to the congregation which he serves does not create the legal relationship of principal and agent [meaning the rabbis' words were not legally binding on the congregation just because the Rabbi spoke them—Ricks]. * * * *

[¶7] In determining the right of recovery in this case the question is to be determined under the rules of our civil law, and the ancient provision of the Hebrew law relating to separate seating is read into the contract only because implicit in the writing as to the basis—according to the evidence—upon which the parties dealt. *Cf. Canovaro et al. v. Bros. of H. of St. Aug.,* 326 Pa. 76, 86, 191 A. 140. In our law the provision became a part of the written contract under a principle analogous to the rule applicable to the construction of contracts in the light of custom or immemorial and invariable usage. It has been said that: "When a custom or usage is once established, in absence of express provision to the contrary it is considered a part of a contract and binding on the parties though not mentioned therein, the presumption being that they knew of and contracted with reference to it": 1 *Henry Pa. Evid*., 4th Ed., § 203. Cf. *Restatement, Contracts*, § 248(2) and § 249. In this case there was more than a presumption. From the findings of the trial judge supported by the evidence it is clear that the parties contracted on the common understanding that the defendant was an orthodox synagogue which observed the mandate of the Jewish law as to separate seating. That intention was implicit in this contract though not referred to in the writing, and therefore must be read into it. It was on this ground that the court entered judgment for plaintiff in this case.

Disposition

Judgment affirmed.

Questions:

1. Did Congregation Bnai Yitzhok agree to this provision?

2. Does this case set forth an exception to the plain meaning rule?

3. Did the cantor agree to this provision?

FRIGALIMENT IMPORTING CO., Ltd. v. B.N.S. INTERNATIONAL SALES CORP.

S.D. N.Y. (1960)

190 F. Supp. 116

FRIENDLY, Circuit Judge.

[¶1] The issue is, what is chicken? Plaintiff says "chicken" means a young chicken, suitable for broiling and frying. Defendant says "chicken" means any bird of that genus that meets contract specifications on weight and quality, including what it calls "stewing chicken" and plaintiff pejoratively terms "fowl". Dictionaries give both meanings, as well as some others not relevant here. To support its, plaintiff sends a number of volleys over the net; defendant essays to return them and adds a few serves of its own. Assuming that both parties were acting in good faith, the case nicely illustrates Holmes' remark "that the making of a contract depends not on the agreement of two minds in one intention, but on the agreement of two sets of external signs—not on the parties' having *meant* the same thing but on their having *said* the same thing." *The Path of the Law, in Collected Legal Papers*, p. 178. I have concluded that plaintiff has not sustained its burden of persuasion that the contract used "chicken" in the narrower sense.

[¶2] The action is for breach of the warranty that goods sold shall correspond to the description, *New York Personal Property Law, McKinney's Consol. Laws*, c. 41, § 95. Two contracts are in suit. In the first, dated May 2, 1957, defendant, a New York sales corporation, confirmed the sale to plaintiff, a Swiss corporation, of:

> "US Fresh Frozen Chicken, Grade A, Government Inspected, Eviscerated
>
> 2½-3 lbs. and 1½-2 lbs. each
>
> all chicken individually wrapped in cryovac, packed in secured fiber cartons or wooden boxes, suitable for export
>
> 75,000 lbs. 2½-3 lbs. . . . .@$33.00
>
> 25,000 lbs. 1½-2 lbs. . . . .@$36.50
>
> per 100 lbs. FAS New York
>
> scheduled May 10, 1957 pursuant to instructions from Penson & Co., New York."

[¶3] The second contract, also dated May 2, 1957, was identical save that only 50,000 lbs. of the heavier "chicken" were called for, the price of the smaller birds was $37 per 100 lbs., and shipment was scheduled for May 30. The initial shipment under the first contract was short but the balance was shipped on May 17. When the initial shipment arrived in Switzerland, plaintiff found, on May 28, that the 2½-3 lbs. birds were not young chicken suitable for broiling and frying but stewing chicken or "fowl"; indeed, many of the cartons and bags plainly so indicated. Protests ensued. Nevertheless, shipment under the second contract was made on May 29, the 2½-3 lbs. birds again being stewing chicken. Defendant stopped the transportation of these at Rotterdam.

[¶4] This action followed. Plaintiff says that, notwithstanding that its acceptance was in Switzerland, New York law controls under the principle of *Rubin v. Irving Trust Co.,* 1953, 305 N.Y. 288, 305, 113 N.E.2d 424 431; defendant does not dispute this, and relies on New York decisions. I shall follow the apparent agreement of the parties as to the applicable law.

[¶5] Since the word "chicken" standing alone is ambiguous, I turn first to see whether the contract itself offers any aid to its interpretation. Plaintiff says the 1½-2 lbs. birds necessarily had to be young chicken since the older birds do not come in that size, hence the 2½-3 lbs. birds must likewise be young. This is unpersuasive; a contract for "apples" of two different sizes could be filled with different kinds of apples even though only one species came in both sizes. Defendant notes that the contract called not simply for chicken but for "US Fresh Frozen Chicken, Grade A, Government Inspected." It says the contract thereby incorporated by reference the Department of Agriculture's regulations, which favor its interpretation; I shall return to this after reviewing plaintiff's other contentions.

[¶6] The first hinges on an exchange of cablegrams which preceded execution of the formal contracts. The negotiations leading up to the contracts were conducted in New York between defendant's secretary, Ernest R. Bauer, and a Mr. Stovicek, who was in New York for the Czechoslovak government at the World Trade Fair. A few days after meeting Bauer at the fair, Stovicek telephoned and inquired whether defendant would be interested in exporting poultry to Switzerland. Bauer then met with Stovicek, who showed him a cable from plaintiff dated April 26, 1957, announcing that they "are buyer" of 25,000 lbs. of chicken 2½-3 lbs. weight, Cryovac packed, grade A Government inspected, at a price up to 33¢ per pound, for shipment on May 10, to be confirmed by the following morning, and were interested in further offerings. After testing the market for price, Bauer accepted, and Stovicek sent a confirmation that evening. Plaintiff stresses that, although these and subsequent cables between plaintiff and defendant, which laid the basis for the additional quantities under the first and for all of the second contract, were predominantly in German, they used the English word "chicken"; it claims this was done because it understood "chicken" meant young chicken whereas the German word, "Huhn," included both "Brathuhn" (broilers) and "Suppenhuhn" (stewing chicken), and that defendant, whose officers were thoroughly conversant with German, should have realized this. Whatever force this argument might otherwise have is largely drained away by Bauer's testimony that he asked Stovicek what kind of chickens were wanted, received the answer "any kind of chickens," and then, in German, asked whether the cable meant "Huhn" and received an affirmative response. Plaintiff attacks this as contrary to what Bauer testified on his deposition in March, 1959, and also on the ground that Stovicek had no authority to interpret the meaning of the cable. The first contention would be persuasive if sustained by the record, since Bauer was free at the trial from the threat of contradiction by Stovicek as he was not at the time of the deposition; however, review of the deposition does not convince me of the claimed inconsistency. As to the second contention, it may well be that Stovicek lacked authority to commit plaintiff for prices or delivery dates other than those specified in the cable; but plaintiff cannot at the same time rely on its cable to Stovicek as its dictionary to the meaning of the contract and repudiate the interpretation given the dictionary by the man in whose hands it was put. *See Restatement of the Law of Agency, 2d*, § 145; 2 *Mecham, Agency* § 1781 (2d ed. 1914); *Park v. Moorman Mfg. Co.,* 1952, 121 Utah 339, 241 P.2d 914 919 40 A.L.R.2d 273; *Henderson v. Jimmerson*, Tex. Civ. App.1950, 234 S.W. 2d 710 717-718. Plaintiff's reliance on the fact that the contract forms contain the words "through the intermediary of: ", with the blank not filled, as negating agency, is wholly unpersuasive; the purpose of this clause was to permit filling in the name of an intermediary to whom a commission would be payable, not to blot out what had been the fact.

[¶7] Plaintiff's next contention is that there was a definite trade usage that "chicken" meant "young chicken." Defendant showed that it was only beginning in the poultry trade in 1957, thereby bringing itself within the principle that "when one of the parties is not a member of the trade or other circle, his acceptance of the standard must be made to appear" by proving either that he had actual knowledge of the usage or that the usage is "so generally known in the community that his actual individual knowledge of it may be inferred." 9 *Wigmore, Evidence* (3d ed. 1940) § 2464. Here there was no proof of actual knowledge of the alleged usage; indeed, it is quite plain that defendant's belief was to the contrary. In order to meet the alternative requirement, the law of New York demands a showing that "the usage is of so long continuance, so well established, so notorious, so universal and so reasonable in itself, as that the presumption is violent that the parties contracted with reference to it, and made it a part of their agreement." *Walls v. Bailey*, 1872, 49 N.Y. 464, 472-473.

[¶8] Plaintiff endeavored to establish such a usage by the testimony of three witnesses and certain other evidence. Strasser, resident buyer in New York for a large chain of Swiss cooperatives, testified that "on chicken I would definitely understand a broiler." However, the force of this testimony was considerably weakened by the fact that in his own transactions the witness, a careful businessman, protected himself by using "broiler" when that was what he wanted and "fowl" when he wished older birds. Indeed, there are some indications, dating back to a remark of Lord Mansfield, *Edie v. East India Co*., 2 Burr. 1216, 1222 (1761), that no credit should be given "witnesses to usage, who could not adduce instances in verification." 7 *Wigmore, Evidence* (3d ed. 1940), § 1954; *see McDonald v. Acker, Merrall & Condit Co*., 2d Dept.1920, 192 App. Div. 123 126 182 N.Y.S. 607. While Wigmore thinks this goes too far, a witness' consistent failure to rely on the alleged usage deprives his opinion testimony of much of its effect. Niesielowski, an officer of one of the companies that had furnished the stewing chicken to defendant, testified that "chicken" meant "the male species of the poultry industry. That could be a broiler, a fryer or a roaster", but not a stewing chicken; however, he also testified that upon receiving defendant's inquiry for "chickens", he asked whether the desire was for "fowl or frying chickens" and, in fact, supplied fowl, although taking the precaution of asking defendant, a day or two after plaintiff's acceptance of the contracts in suit, to change its confirmation of its order from "chickens," as defendant had originally prepared it, to "stewing chickens." Dates, an employee of Urner-Barry Company, which publishes a daily market report on the poultry trade, gave it as his view that the trade meaning of "chicken" was "broilers and fryers." In addition to this opinion testimony, plaintiff relied on the fact that the Urner-Barry service, the Journal of Commerce, and Weinberg Bros. & Co. of Chicago, a large supplier of poultry, published quotations in a manner which, in one way or another, distinguish between "chicken," comprising broilers, fryers and certain other categories, and "fowl," which, Bauer acknowledged, included stewing chickens. This material would be impressive if there were nothing to the contrary. However, there was, as will now be seen.

[¶9] Defendant's witness Weininger, who operates a chicken eviscerating plant in New Jersey, testified, "Chicken is everything except a goose, a duck, and a turkey. Everything is a chicken, but then you have to say, you have to specify which category you want or that you are talking about." Its witness Fox said that in the trade "chicken" would encompass all the various classifications. Sadina, who conducts a food inspection service, testified that he would consider any bird coming within the classes of "chicken" in the Department of Agriculture's regulations to be a chicken. The specifications approved by the General Services Administration include fowl as well as broilers and fryers under the classification "chickens." Statistics of the Institute of American Poultry Industries use the phrases "Young chickens" and "Mature chickens," under the general heading "Total chickens," and the Department of Agriculture's daily and weekly price reports avoid use of the word "chicken" without specification.

[¶10] Defendant advances several other points which it claims affirmatively support its construction. Primary among these is the regulation of the Department of Agriculture, 7 C.F.R. § 70.300-70.370, entitled, "Grading and Inspection of Poultry and Edible Products Thereof." and in particular § 70.301 which recited:

"*Chickens.* The following are the various classes of chickens:

(a) Broiler or fryer . . .

(b) Roaster . . .

(c) Capon . . .

(d) Stag . . .

(e) Hen or stewing chicken or fowl . . .

(f) Cock or old rooster . . .

[¶11] Defendant argues, as previously noted, that the contract incorporated these regulations by reference. Plaintiff answers that the contract provision related simply to grade and Government inspection and did not incorporate the Government definition of "chicken," and also that the definition in the Regulations is ignored in the trade. However, the latter contention was contradicted by Weininger and Sadina; and there is force in defendant's argument that the contract made the regulations a dictionary, particularly since the reference to Government grading was already in plaintiff's initial cable to Stovicek.

[¶12] Defendant makes a further argument based on the impossibility of its obtaining broilers and fryers at the 33¢ price offered by plaintiff for the 2½-3 lbs. birds. There is no substantial dispute that, in late April, 1957, the price for 2½-3 lbs. broilers was between 35 and 37¢ per pound, and that when defendant entered into the contracts, it was well aware of this and intended to fill them by supplying fowl in these weights. It claims that plaintiff must likewise have known the market since plaintiff had reserved shipping space on April 23, three days before plaintiff's cable to Stovicek, or, at least, that Stovicek was chargeable with such knowledge. It is scarcely an answer to say, as plaintiff does in its brief, that the 33¢ price offered by the 2½-3 lbs. "chickens" was closer to the prevailing 35¢ price for broilers than to the 30¢ at which defendant procured fowl. Plaintiff must have expected defendant to make some profit; certainly it could not have expected defendant deliberately to incur a loss.

[¶13] Finally, defendant relies on conduct by the plaintiff after the first shipment had been received. On May 28 plaintiff sent two cables complaining that the larger birds in the first shipment constituted "fowl." Defendant answered with a cable refusing to recognize plaintiff's objection and announcing "We have today ready for shipment 50,000 lbs. chicken 2½-3 lbs. 25,000 lbs. broilers 1½-2 lbs.," these being the goods procured for shipment under the second contract, and asked immediate answer "whether we are to ship this merchandise to you and whether you will accept the merchandise." After several other cable exchanges, plaintiff replied on May 29 "Confirm again that merchandise is to be shipped since resold by us if not enough pursuant to contract chickens are shipped the missing quantity is to be shipped within ten days stop we resold to our customers pursuant to your contract chickens grade A you have to deliver us

said merchandise we again state that we shall make you fully responsible for all resulting costs."* Defendant argues that if plaintiff was sincere in thinking it was entitled to young chickens, plaintiff would not have allowed the shipment under the second contract to go forward, since the distinction between broilers and chickens drawn in defendant's cablegram must have made it clear that the larger birds would not be broilers. However, plaintiff answers that the cables show plaintiff was insisting on delivery of young chickens and that defendant shipped old ones at its peril. Defendant's point would be highly relevant on another disputed issue: whether if liability were established, the measure of damages should be the difference in market value of broilers and stewing chicken in New York or the larger difference in Europe, but I cannot give it weight on the issue of interpretation. Defendant points out also that plaintiff proceeded to deliver some of the larger birds in Europe, describing them as "poulets"; defendant argues that it was only when plaintiff's customers complained about this that plaintiff developed the idea that "chicken" meant "young chicken." There is little force in this in view of plaintiff's immediate and consistent protests.

[¶14] When all the evidence is reviewed, it is clear that defendant believed it could comply with the contracts by delivering stewing chicken in the 2½-3 lbs. size. Defendant's subjective intent would not be significant if this did not coincide with an objective meaning of "chicken." Here it did coincide with one of the dictionary meanings, with the definition in the Department of Agriculture Regulations to which the contract made at least oblique reference, with at least some usage in the trade, with the realities of the market, and with what plaintiff's spokesman had said. Plaintiff asserts it to be equally plain that plaintiff's own subjective intent was to obtain broilers and fryers; the only evidence against this is the material as to market prices and this may not have been sufficiently brought home. In any event it is unnecessary to determine that issue. For plaintiff has the burden of showing that "chicken" was used in the narrower rather than in the broader sense, and this it has not sustained.

This opinion constitutes the Court's findings of fact and conclusions of law. Judgment shall be entered dismissing the complaint with costs.

Questions:

1. Every year thousands of law students read the chicken case. What if anything do you learn from it? Will you be a better lawyer for having read it? How?

2. What did Holmes mean when he said that "the making of a contract depends not on the agreement of two minds in one intention, but on the agreement of two sets of external signs—not on the parties' having meant the same thing but on their having said the same thing"?

3. Why does Friendly say that this case "nicely illustrates" Holmes' remark?

4. Judge Friendly later wrote that this case might be about assent. He said that lack of assent was proved because of the misunderstanding between the parties. Is the chicken case like the case of the two ships

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* [2] These cables were in German; "chicken", "broilers" and, on some occasions, "fowl," were in English.

Peerless? Can you resolve the chicken case on the basis of rules from the Restatement (Second) of Contracts § 20? Interestingly enough, the statement of Holmes that Friendly quoted was about the *Peerless* case. If Judge Friendly's later assertion is correct, then his earlier assumption that a contract existed in the case is wrong. And if there was no contract, the buyer would not have to pay the price of the chicken, only the chicken's value.

B. Writing the Promise: What Effect?

Some contracts have traditionally been written: promissory notes, which could be traded as cash (and still are when they qualify as negotiable instruments like the check in *Havard*); land sales; and marriage contracts in some cultures, for example. Some promises, such as those in sealed documents, could be enforced under the common law through a streamlined procedure called *debt sur obligacion*. Defendants subject to an action of *debt sur obligacion* had very few defenses. The writing determined almost everything the court needed to know to impose a remedy. The push to capture bargains in writing was strengthened by the Statute of Frauds (1677), which required that certain important kinds of contract be written and also signed by the promisor.

Once parties decide to write a promise, the courts have to decide whether to give legal effect to the fact that the parties put the promise in writing, and what that effect will be. Neither is a foregone conclusion.

Why would one want to write a promise? Should the reason for writing a promise affect what importance a court decides to give to the writing?

1. Mistake in Transmission

BALLARD v. CHAVEZ

N.M. (1994)

868 P.2d 646

[¶1] Plaintiff appellants, James, Wayne, and Glenn Ballard doing business as Ballard and sons (Ballard), appeal from the district courts order dismissing their contract suit against Defendants-Appellants, members of the Board of Trustee of the Loving Municipal School District (Loving School District), for failure to state a claim upon which relief can be granted. Ballard, who had entered a contract with Loving School District to build Phase I of Loving High School, sued Loving School District to recover costs it claimed were mistakenly deducted twice from its contract price. Finding that Ballard was improperly attempting to change its bid in violation of [a New Mexico statute], the District Court dismissed Ballard's complaint. We reverse.

[¶2] Because we are reviewing a motion to dismiss for failure to state a claim . . . , we accept as true all well-pleaded facts in the complaint and ask whether the plaintiff can prevail under any state of facts provable under the claim. * * * Accordingly, the following recitation of facts is based upon the well-pleaded allegations of Ballard's amended complaint.

[¶3] Ballard, a general contractor, submitted a bid to construct Phase I of Loving High School, and Ballard's bid was accepted. On December 26, 1988, Ballard signed a written contract with Loving School District to construct Phase I of Loving High School. Simultaneously with the signing of the contract, the parties executed a change order that modified the contract by deducting the cost of paving certain parking areas. When Ballard and Loving School District Executed the contract and change order, they did not realize that the cost of paving deducted in the change order had already been deducted in the contract from the total cost of construction. Thus, the contracting parties he made a mutual mistake by inadvertently deducting the paving cost twice. The double deduction allegedly cost Ballard $93,840, $20,000 of which has been paid to Ballard by Loving School District. Ballard seeks equitable relief through contract reformation to compensate its loss.

[¶4] The district court dismissed Ballard's complaint because it concluded that reforming the contract would constitute a modification of the bid price in violation of [the statute]. . . . [T]he district court further held that Ballard's Claim is barred by the rule that a bidder who fails to learn what could have been discovered by careful review of contract documents cannot rely upon his misunderstanding to seek contract reformation.

[¶5] Ballard is not requesting modification of its bid; it is requesting modification of a written contract. When the mistake of the double deduction was discovered, Ballard and Loving School District had already entered into the contract, including the written change order that amended the contract and became an integral part thereof. Because [the statute] relates to bids and not contracts, it is not applicable and it does not preclude contract reformation based upon mutual mistake discovered after contract formation as in this case.

[¶6] Mutual mistake is grounds for contract reformation in New Mexico. *State ex rel. State Highway & Transp. Dep't v. Garley*, 111 N.M. 383, 388, 806 P.2d 32, 37 (1991). *Restatement (Second) of Contracts*, Section 155, states:

> Where a writing that evidences or embodies an agreement in whole or in part fails to express the agreement because of a mistake of both parties as to the contents or effect of the writing, the court may at the request of a party reform the writing to express the agreement . . . .

Restatement (Second) of Contracts § 155 (1979). The Restatement further explains that "[t]he error in expressing the agreement [which may be reformed under Section 155] may consist in the omission or erroneous reduction to writing of a term agreed upon or the inclusion of a term not agreed upon." *Restatement (Second) of Contracts* § 155 cmt. A (1979). Thus, A mutual mistake by Ballard and Loving School District of accidentally deducting the same paving expense twice can be subject to reformation. This is so despite the fact that each party to a contract has a duty to read and familiarize himself with the contents of the contract, each party generally is presumed to know the terms of the agreement, and each is ordinarily bound thereby, *Smith v. Price's Creameries, a Div. of Creamland Dairies, Inc.,* 650 P.2d 825, 829 (1982). "A mistaken party's fault in failing to know or discover the facts before making the contract does not bar him from . . . reformation under [Restatement (Second) of Contracts Section 155], unless his fault amounts to a failure to act in good faith and in accordance with reasonable standards of fair dealing." *Restatement*

(Second) of Contracts § 157 (1979). Thus, when reformation based upon mutual mistake is appropriate, reformation is an exception to the general rule that parties will be bound to the terms of their express, written contracts and will not be excused from their duty to know these terms. * * * *

[7] In sum, the equitable remedy of reformation is potentially available to Ballard. We express no opinion on the merits of this action, leaving evaluation of the facts to the district court. * * * *

Questions:

1. Please do not be confused by the court's use of the phrase "mutual mistake." We studied a doctrine of mutual mistake earlier in the semester. What was the remedy for the earlier doctrine of mutual mistake we studied? Also, the things the parties must be mistaken about in the two doctrines are wildly different. How? That is why the two doctrines are often distinguished as "mutual mistake of fact" and "scrivener's error."

2. What sort of evidence would Ballard present in order to prove that the contract documents and the modification both deducted a paving cost that was supposed to be deducted only once? Who would testify? What would they testify? What would you expect the other side to testify?

3. The court makes a distinction between a bid, on the one hand, and a subsequent construction contract, on the other. Why would a contracting party not ask for reformation of a mere bid?

2. Parol Evidence

Now we reach the parol evidence rule—the rule you were cautioned about after *Coker*. Please remember the issue that the parol evidence rule addresses: whether any words should be added to or taken from the parties' written contract, when they have a written contract. The parol evidence rule is not about the meaning of words, whether in the contract or out of it. It is about which words or terms are included in the contract.

Please keep in mind what was said before: Courts sometimes mention the plain meaning rule in the same passage as the parol evidence rule, and you will have to use context to determine what they are doing. If they are ruling on ambiguity in the words, that is about meaning. If they are ruling on whether some term not in the written agreement belongs in it or otherwise modifies the writing, that is parol evidence rule territory.

COLLIERS, DOW AND CONDON, INC. v. Leonard J. SCHWARTZ et al.

Conn. App. (2003)

823 A.2d 438

Opinion

[¶1] WEST, J. The plaintiff, Colliers, Dow and Condon, Inc., appeals from the judgment of the trial court rendered in favor of the defendants in this breach of contract action. The plaintiff claims that the court improperly (1) relied on parol evidence to vary an express term of a real estate brokerage agreement * * * .† We agree with the plaintiff and reverse the judgment of the trial court.

[¶2] The following facts are relevant to our disposition of the plaintiff's appeal. The controversy between the parties arises from the leasing of certain commercial property at 631-635-637 Farmington Avenue in West Hartford and owned by the defendant K.F. Associates, LLP. The defendant Leonard J. Schwartz is a managing partner in K.F. Associates, LLP.†

[¶3] The parties have conducted business with each other on several prior occasions. The plaintiff leased, and subsequently sold, one of Schwartz's buildings located in Bloomfield. The plaintiff later sold a small office building in West Hartford for Schwartz. In 1994, the defendants engaged the plaintiff's services to lease 1450 square feet of the subject property.‡ Following the success of those endeavors, the parties, in 1995, signed an agreement captioned ''Exclusive Right To Sell/ Exchange Agreement,'' under which the plaintiff was to secure a buyer for the subject premises.

[¶4] In 1997, the parties signed an agreement captioned ''Exclusive Right to Sell/Exchange/Lease Agreement,'' which is the subject of this appeal. At that time, a company named Imagineers was occupying approximately 86 percent of the subject property as a tenant. Schwartz asked John Tully, a licensed brokerage representative of the plaintiff, to approach Imagineers about buying the property. Tully's discussions with Imagineers culminated in a letter in which he presented two proposed acquisition plans for the property. Imagineers responded with a counteroffer at a price well below either of the plaintiff's

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† [1] As framed by the plaintiff, the parol evidence claim challenges: (1) the court's conclusion that the parties' contract did not allow the plaintiff to recover a commission in the event that the subject property was leased, and (2) the court's finding that there was no understanding between the parties that the plaintiff would be entitled to a commission for leasing the premises. Because we conclude that the court's reliance on parol evidence was improper, we need not reach the issue of whether the finding derived from that evidence, that there was no meeting of the minds between the parties as to leasing of the subject property, was clearly erroneous.

† [2] K.F. Associates, LLP, a limited liability partnership formed on October 22, 1996, is the successor in interest to K.F. Associates, a general partnership formed on January 25, 1983. Schwartz also was the managing partner of the general partnership. Any references to K.F. Associates regarding transactions that occurred prior to October 22, 1996, are to the general partnership, rather than to the limited liability partnership.

‡ [3] That brokerage service was provided pursuant to a contract captioned ''Exclusive Right To Lease Agreement.''

proposals. As an alternative, Imagineers proposed to Schwartz directly that it continue to rent the building under a five year lease, with an option to renew for another five years, at $120,000 a year for the first five years and $130,000 a year for the second five year period. Under that arrangement, Imagineers would make certain improvements to the property, and provide landscaping and snow removal. A final counteroffer proposed an initial five year lease at $135,000 with an option for an additional five year lease at $145,000, with the defendants making necessary repairs.

[¶5] Between March 3 and August 26, 1998, a series of letters were exchanged between Imagineers and Schwartz. On August 26, 1998, Schwartz and Imagineers signed a lease agreement, effective February 1, 1999. On April 19, 1999, the plaintiff sent the defendants a bill for real estate brokerage services rendered pursuant to their exclusive listing agreement. The amount requested was 5 percent of the anticipated rent to be paid during the first five year lease period, or $42,750.80. Schwartz refused to make payment, and this action followed.

I

[¶6] The plaintiff's first claim is that the court improperly relied on parol evidence to contradict an express term of the parties' contract. We agree.

[¶7] At the outset, we set forth the applicable standard of review. Ordinarily, ''[o]n appeal, the trial court's rulings on the admissibility of evidence are accorded great deference. . . . Rulings on such matters will be disturbed only upon a showing of clear abuse of discretion. . . . Because the parol evidence rule is not an exclusionary rule of evidence, however, but a rule of substantive contract law . . . the defendants' claim involves a question of law to which we afford plenary review.'' (Citations omitted; internal quotation marks omitted.) *Harold Cohn & Co.* v. *Harco International*, *LLC*, 72 Conn. App. 43, 48, 804 A.2d 218, cert. denied, 262 Conn. 903, 810 A.2d 269 (2002).

[¶8] The parol evidence rule is ''premised upon the idea that when the parties have deliberately put their engagements into writing, in such terms as import a legal obligation, without any uncertainty as to the object or extent of such engagement, it is conclusively presumed, that the whole engagement of the parties, and the extent and manner of their understanding, was reduced to writing. After this, to permit oral testimony, or prior or contemporaneous conversations, or usages [etc.], in order to learn what was intended, or to contradict what is written, would be dangerous and unjust in the extreme. . . .

[¶9] ''The parol evidence rule does not of itself, therefore, forbid the presentation of parol evidence, that is, evidence outside the four corners of the contract concerning matters covered by an integrated contract, but forbids only the use of such evidence to vary or contradict the terms of such a contract. Parol evidence offered solely to vary or contradict the written terms of an integrated contract is, therefore, legally irrelevant. When offered for that purpose, it is inadmissible not because it is parol evidence, but because it is irrelevant. By implication, such evidence may still be admissible if relevant . . . to show mistake or fraud. . . . [This] recognized [exception is], of course, only [an example] of [a situation] where the evidence . . . tends to show that the contract should be defeated or altered on the equitable ground that relief can be had against any deed or contract in writing founded in mistake or fraud.'' (Citations omitted; internal quotation marks omitted.) *Heyman Associates No. 1 v. Ins. Co. of Pennsylvania*, 231 Conn. 756, 780–81, 653 A.2d 122 (1995).

[¶10] As an initial matter, we must frame the issue before this court. The plaintiff contends that the trial court relied on parol evidence to vary an express term of a contract, specifically, to read the word ‘‘lease’’ out of an otherwise valid contract. The defendants argue that the court relied on the parol evidence to make a preliminary finding that because there was no meeting of the minds between the parties as to the leasing of the subject property, there was no contract at all. We agree with the plaintiff.

[¶11] Because the defendants conceded in their answer to the complaint that Schwartz had entered into a contract with the plaintiff for professional real estate brokerage services, the validity of the contract was not before the court; only the scope of that contract was at issue. Moreover, the court's memorandum of decision does not state that there was no agreement. The court found only that there was no agreement as to leasing, implicitly leaving intact that portion of the agreement relating to efforts to sell the property. The legal consequence of the court's finding, therefore, was to strike that portion of the contract relating to leasing. We analyze the claims raised in this appeal in that light.

[¶12] The defendants contend that the renewal of the parties' agreement was solely for the purpose of securing a buyer for the property and was not intended to include any efforts to lease the premises. Schwartz testified in support of that proposition. He stated that upon receiving the agreement, he called Tully and asked if the agreement meant that he was going to sell the building, if, in effect, the agreement was essentially the same as the earlier ‘‘right to sell/exchange’’ agreement. According to Schwartz, Tully responded, ‘‘Yes, it's only for selling the building.’’ On the basis of that parol evidence, the court found that there was no meeting of the minds that the plaintiff would be entitled to a commission for leasing the premises. Specifically, the court found that in entering into the agreement, the defendants had not intended to retain the services of the plaintiff to lease the subject property, but had intended to retain the plaintiff's services solely for the purpose of selling that property.[§]

[¶13] That finding, however, directly contradicts the express terms of the contract. The parties' written agreement provides that a commission is to be paid to the plaintiff upon either the sale or lease of the premises. Paragraph five of that agreement states in relevant part: ‘‘Broker earns its commission . . . if during the term of this Agreement: (a) a prospective buyer or lessee is ready, willing and able to PURCHASE or EXCHANGE or LEASE the Property at the price shown in paragraph 4 above, or at any other price or terms acceptable to Owner; or (b) any contract for the SALE or TRANSFER or LEASE of the Property or any portion thereof or interest therein is entered into by Owner; or (c) Owner and a prospective buyer or tenant enter into a legally binding contract for the SALE or EXCHANGE or LEASE of the Property or any portion thereof or any interest therein and such contract is breached or rescinded by a party or the parties; or (d) Owner SELLS, LEASES or TRANSFERS the Property or any portion thereof or interest therein . . . .’’ Paragraph four states: ‘‘Owner authorizes Broker to quote a SALE/EXCHANGE price of: $500,000, and a lease rental price of $13.50 gross per square foot, per annum.’’

[¶14] Given the substance of the parol evidence admitted in the present case, it might be supposed that Schwartz was attempting to establish that the lease term contained in the agreement was the result of either

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[§] [4] In looking to the circumstances surrounding the making of the agreement, the court relied on *Lar-Rob Bus Corp.* v. *Fairfield*, 170 Conn. 397, 407–408, 365 A.2d 1086 (1976). *Lar-Rob Bus Corp.* did not involve a situation in which the trial court relied on parol evidence to contradict the express terms of a written contract. Rather, the court relied on such evidence only to resolve an ambiguity in the contract's language. * * * *

mistake or misrepresentation. We refer specifically to Schwartz's testimony that he asked Tully whether the 1997 contract was the same as the 1995 sale-exchange agreement. Schwartz testified that Tully replied that it was essentially the same and that it contemplated only the sale of the subject property.

[¶15] As stated previously, parol evidence may be introduced to show fraud in the inducement or a mistake in memorializing the terms of an agreement. Where fraudulent misrepresentation is alleged, parol evidence may be introduced to show that the legal effect of a term was misrepresented and that such misrepresentation was relied on by a party in signing the agreement. See id. The pleadings filed in the present case, however, preclude any such application of the parol evidence rule. The only special defense that the defendants raised was the assertion that the contract failed to comply with the provisions of [a statute requiring real estate brokers to serve only pursuant to a written contract]. The defendants did not raise any issue with respect to mistake or fraud.[*] Even if we were to conclude that Schwartz's testimony at trial was aimed at establishing fraud or misrepresentation by the plaintiff respecting the terms of the agreement, we could not conclude that the court was entitled to entertain such testimony. Fraud is an affirmative defense that to be availed of, must specifically be pleaded. * * * * Because it was not pleaded, the defendants are not entitled to a judgment premised on that defense even if the evidence supports a finding of fraud. * * * *

[¶16] We conclude, therefore, that the court's reliance on parol evidence to contradict an express term of the parties' contract was improper. Accordingly, we reverse the court's judgment that the brokerage agreement did not cover the leasing of the property. * * * *

[¶17] The judgment is reversed and the case is remanded for further proceedings (1) to consider the defendants' special defense relating to § 20-325a (b) and (2) for a determination of the appropriate amount of damages.

In this opinion the other judges concurred.

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[*] [6] Although the defendants pleaded a counterclaim against the plaintiff, alleging a violation of the Connecticut Unfair Trade Practices Act, General Statutes § 42-110a et seq., the court found that the defendants had failed to brief that claim and deemed it to be abandoned.

Questions:

1. What did the trial court do wrong?

2. Why doesn't the court allow evidence of either mistake in transcription or fraud?

3. Had the contract been ambiguous, would Tully's response have been admissible?

4. Should the phone conversation between Tully and Schwartz matter?

5. Is there anything in the parol evidence rule about ambiguity? Plain meaning?

6. What public policy might support the parol evidence rule?

7. Why is the parol evidence rule "not an exclusionary rule of evidence, however, but a rule of substantive contract law"? Why then do we call it an "evidence rule"?

8. The court mentions the "four corners of the contract" in its description of the parol evidence rule. Would the parol evidence rule exclude written evidence of Tully's response?

Some written contracts are obviously final, and some are obviously final and complete. Some are not obviously final. Some are obviously not complete. For example, thousands of cases involve homeowners who hire contractors to do yard projects, and the writing at issue is only a signed bid. It might be final, but it is obviously not complete. Can the court consider evidence besides the written document to determine whether the written document is final and/or complete?

Bennie D. HERRING v. Hubert M. PRESTWOOD, Jr., et al.

Supreme Court of Alabama (1979)

379 So.2d 548

TORBERT, Chief Justice.

[Excerpt from the Opinion:

[¶1] Appellant, Bennie Herring, filed suit below for a declaratory judgment to define the terms of an option to purchase land from the appellees, Hubert and Mary Prestwood. The option granted Herring the right to purchase 320 acres of land from the Prestwoods for a purchase price of $208,000 consisting of a down payment of $96,000 with the balance of $112,000 to be paid in annual installments over a period of ten to twenty years with interest at 8%. The evidence is in dispute as to whether any consideration was paid for the option.

[¶2] The first amendment to the complaint re-worded the complaint to allege that the written option did not reflect the total agreement of the parties and added two counts to the complaint, one for breach of contract in refusing to convey, the other for fraud. Herring insists that the written option agreement is incomplete because it does not contain that portion of the actual agreement which would allow Herring to use the 320 acres as security for a loan to pay the down payment. The Prestwoods filed a motion to strike those allegations of the complaint which referred to the alleged oral promise and that motion was granted by the court because that court found proof of those allegations would be inadmissible.]

ON APPLICATION FOR REHEARING

[¶3] On application for rehearing the opinion is extended to address the parol evidence rule issue, in order to give the trial court guidance on remand.

[¶4] We hold that the trial court committed reversible error in finding that the parol evidence rule barred any testimony to the effect that the written option did not reflect the total agreement of the parties. The appellant contends that the entire agreement of the parties included the seller's agreement to allow him to place a first mortgage on the property. The appellee contends that the entire agreement included the buyer's agreement to abstain from placing any encumbrance on the property which would impair the vendor's lien. The written option is silent as to first mortgages. Because the writing does not cover the issue of first mortgages, parol evidence is admissible to establish the agreement of the parties.

> The parol evidence rule, therefore, does not apply to every contract of which there exists written evidence, but applies only when the parties to an agreement reduce it to writing, *and agree or intend that the writing shall be their complete agreement*. * * * * Where there exists doubt that the written agreement was ever intended to reflect the full agreement of the parties, the courts of this State have not hesitated to admit contradictory parol evidence. * * * *

Hibbett Sporting Goods v. Biernbaum, 375 So.2d 431 (Ala.1979) (emphasis added).

[¶5] This writer expressed his understanding of the parol evidence rule in a dissenting opinion in Hibbett Sporting Goods, supra. There he disagreed with the majority because the specific issue about which the admission of parol evidence was sought had been covered in the writing. In the instant case, the writing was completely silent as to first mortgages or vendor's liens.

> It is fundamental that the parol evidence rule prohibits the contradiction of a written agreement by evidence of a prior oral agreement. The rule provides that when the parties reduce a contract to writing, no extrinsic evidence of prior or contemporaneous agreements will be admissible to change, alter, or contradict such writing. *Hartford Fire Insurance Co. v. Shapiro,* 270 Ala. 149, 117 So.2d 348 (1960); *Richard Kelley Chevrolet Co. v. Seibold,* 363 So.2d 989 (Ala.Civ.App.1978); 3 A. Corbin*, Corbin on Contracts* § 573, at 357 (1969). When the writing is a final expression of the parties' agreement, it is said to be integrated. If the writing is final but not complete, it is partially integrated and consistent terms only can be supplied by extrinsic evidence. If the writing is final and complete, it is totally integrated and not even evidence of consistent terms can be admitted. J. Murray, Jr., *Murray on Contracts* § 105 (1974); J. Calamari & J. Perillo, *The Law of Contracts* § 40, at 76 (1970). Whether the instrument is a final and complete expression of the agreement is to be

> determined from the conduct and language of the parties, the surrounding circumstances, and the instrument itself. *Southern Guaranty Insurance Co. v. Rhodes*, 46 Ala. App. 454, 243 So.2d 717 (1971); *Pasquale Food Co. v. L & H International Air, Inc.,* 51 Ala. App. 127, 283 So.2d 438 (1973); 9 J. Wigmore, *Evidence* § 2430, at 98 (3d ed. 1940). In making such a determination, "the chief and most satisfactory index for the judge is found in the circumstance whether or not the particular element of the alleged extrinsic negotiation is dealt with at all in the writing. If it is mentioned, covered, or dealt with in the writing, then presumably the writing was meant to represent all of the transaction on that element; if it is not, then probably the writing was not intended to embody that element of the negotiation." Id. at 98-99; *Southern Guaranty Insurance Co. v. Rhodes,* supra.

Hibbett Sporting Goods v. Biernbaum, 375 So.2d at 437 (Ala.1979).

[¶6] Since the written option in the instant case was silent as to vendor's liens or first mortgages, it does not embody that element of the negotiation and parol evidence is admissible to establish the understanding or agreement of the parties in regard to a first mortgage.

OPINION EXTENDED; APPLICATION FOR REHEARING OVERRULED.

BLOODWORTH, FAULKNER, ALMON and EMBRY, JJ., concur.

Questions:

1. Do you find it odd that the court considers the alleged extraneous provisions in order to determine whether the contract is integrated? Not every court is willing to do this. Consider the following from *State* ex rel. *MHTC v. Maryville Land Partnership*, 62 S.W.3d 485 (Mo. App. 2001):

> [¶1] The parol evidence rule has been described as "a deceptive maze rather than a workable rule." *Jake C. Byers, Inc. v. J.B.C. Investments,* 834 S.W.2d 806, 812 (Mo. App. E.D.1992). There is a general consensus that when the parties have reduced their final and complete agreement to writing, the parol evidence rule does not permit the writing to be varied or contradicted and this principle is a substantive rule of law and not a rule of evidence. *Id.* (citing *Commerce Trust Co. v. Watts,* 360 Mo. 971, 231 S.W.2d 817, 820 (1950)); Restatement (Second) Contracts § 213. The parol evidence rule does not prevent relevant parol evidence from being admitted; but prohibits the trier of fact from using that evidence to vary, alter or contradict the terms of a binding, unambiguous and integrated written contract. Restatement (Second) Contracts § 214. The essence of the parol evidence rule is, therefore, that evidence outside a completely integrated contract cannot be used to change the agreement.
>
> [¶2] The parol evidence rule does not, however, prohibit the presentation of parol evidence to determine *if* the contract is integrated. All authorities agree that the court must determine if the contract is integrated before it applies the parol evidence rule. *Wulfing v.*

Kansas City Southern Industries, Inc., 842 S.W.2d 133, 146 (Mo. App. W.D.1992); Restatement (Second) Contracts § 209. A written agreement is integrated if it represents a final expression of one or more terms of the agreement. Restatement (Second) Contracts § 209(1). Contracts can be either completely or partially integrated. If a written contract is a completely integrated agreement even consistent additional terms within its scope are precluded. *Centerre Bank of Kansas City v. Distributors,* 705 S.W.2d 42, 51 (Mo. App. W.D.1985); Restatement (Second) Contracts § 209 (cmt.a). If, however, the writing omits a consistent additional term that is either agreed to for separate consideration or might naturally have been omitted in the circumstances, the agreement is considered only partially integrated and collateral facts and circumstances may be introduced to prove consistent additional terms. *Craig v. Jo B. Gardner, Inc.,* 586 S.W.2d 316, 324 (Mo. banc 1979); Restatement (Second) Contracts § 216(2).

[¶3] Scholars disagree, however, on the method by which courts should determine if the contract is integrated. *Compare* 4 WILLISTON, CONTRACTS § 633 (3rd ed.1961) and 1 Restatement, Contracts, §§ 237, 240, with 3 Corbin, Contracts § 582 (1960), Restatement (Second) Contracts § 209 and UCC 2-202; *see generally,* Farnsworth, Contracts § 7.3. Williston's position is that "the contract must appear on its face to be incomplete in order to permit parol evidence of additional terms." 4 Williston, Contracts § 633. If the contract appears on its face to be completely integrated, the court should simply accept that this is so, without looking to the surrounding circumstances. *Id.* The modern trend has been to reject this view on the ground that a "writing cannot prove its own completeness and accuracy." Corbin, *The Parol Evidence Rule,* 53 Yale L.J. 603, 630 (1944). Corbin, the Second Restatement, and the UCC have all taken the position that the court should take into consideration all relevant circumstances before determining that the contract is integrated. 3 Corbin, Contracts § 582; Restatement (Second) Contracts § 209 (cmt.b); UCC 2-202 Cmt. 1.

[¶4] The Missouri Supreme Court has not spoken to the question; but the language used in its decisions has led this court to adopt the position advocated by Williston and the First Restatement. *Jake C. Byers, Inc.,* 834 S.W.2d at 811-12. So, the initial inquiry is to determine if the Escrow Agreement here is completely or partially integrated on its face. Under present Missouri law, if it is a complete agreement on its face, it is conclusively presumed to be a final as well as a complete agreement between the parties. *Id.* at 812. We look to the Escrow Agreement and find the following relevant provisions:

> THIS ESCROW AGREEMENT, made and entered into as of this 31st day of October, 1985 by and between Lindbergh-Warson Properties, Inc. ("Lindbergh"), and Maryville Land Partnership, a Joint Venture ("Maryville"), the Missouri Highway and Transportation Commission ("Commission"), Community Title Company ("Community") and Centerre Bank, National Association ("Bank").
>
> WHEREAS, Lindbergh and the Commission heretofore entered into a certain Agreement . . . wherein Lindbergh agreed to pay a sum not exceeding One Million and no/100 Dollars ($1,000,000.00) in reimbursement of the Commission for the actual construction cost of the Grade Separation and the North Outer Roadway on

Highway 40 in St. Louis County, Missouri, approximately midway between Route 141 and the Mason Road interchange; and

WHEREAS, Lindbergh and the Commission heretofore entered into a supplemental agreement wherein Lindbergh agreed to pay an additional sum of Ninety Thousand and no/100 ($90,000.00) for certain “culvert work”; and

WHEREAS, Maryville, of which Lindbergh is a general partner, has heretofore succeeded to the rights and obligations of Lindbergh in the Agreement; and

WHEREAS, Bank has heretofore loaned to Maryville the monies necessary to fund Maryville’s obligations to the Commission under the Agreement and in connection therewith Bank agreed to advance the proceeds of said loan at the request of, and at the direction of, the Commission upon receipt from the Commission of its certification that (a) the cost of the overpass and culvert work completed to date, as a percentage of the total projected cost of said work, is not less than the amount previously disbursed plus the amount of the requested advance, expressed as a percentage of Maryville’s total obligation to Commission and (b) all previous advances have been used to satisfy Maryville’s obligation to partially defray the costs of the culvert and overpass work (the “Certification”) and

WHEREAS, Bank would like to be relieved of its direct obligation to the Commission in this regard and the parties hereto are mutually agreed that Community shall serve as the Escrow Agent pursuant to the terms hereinafter specified. . . .

NOW, THEREFORE, in consideration of the promises and of the mutual covenants and agreements hereinafter set forth, and of other good and valuable consideration, the parties hereto covenant and agree as follows:

1. Escrowed Funds. Maryville shall, upon execution of the Escrow Agreement, cause to be deposited with Community the sum of One Million Thirty Four Thousand Five Hundred Sixty and no/100 Dollars ($1,034,560.00), being the balance of Maryville’s obligation to Commission (the “Escrowed Funds”), to secure the obligations of Maryville under the Agreement. . . .

2. Investment. The Escrowed Funds shall be invested in Certificates of deposit with Bank in such amounts and with such maturity dates as Maryville shall direct.

3. Escrow Funds. The Escrowed Funds shall be advanced as directed by Commission within five (5) business days of receipt of the written request of the Commission. Each such request shall be accompanied by a Certification in the form annexed hereto as Exhibit B. . . .

* * * * * *

5. Accumulation of Income. All income accumulated from the investment of the Escrowed Funds and not used to satisfy interest or other loan charges, if

> any, shall be the property of Maryville and shall be paid to Maryville, from time to time, upon request.
>
> [¶5] The Escrow Agreement simply makes no reference to what would happen to any unused funds in the escrow account, but recitals in the Escrow Agreement reference both the Construction Agreement and a supplemental agreement. These references show that the fundamental purpose of the Escrow Agreement was to facilitate the Construction Agreement by replacing Lindbergh-Warson's letter of credit with an escrow account furnished by Maryville Land, who had succeeded to Lindbergh Warson's interests. The face of the Escrow Agreement itself makes clear that a number of documents, read together, make up the entire agreement between the Commission, Lindbergh-Warson and Maryville Land. The Escrow Agreement merely supplements terms in the underlying Construction Agreement and does not represent the entire agreement of the parties. Importantly, it does not provide for the possibility that the parties would succeed in obtaining state and federal funds for the construction of the overpass. We therefore conclude that the Escrow Agreement was not a completely integrated agreement and collateral facts and circumstances could be introduced to show consistent additional terms. *See Craig v. Jo B. Gardner, Inc.,* 586 S.W.2d 316, 324 (Mo. 1979). The court did not err in allowing evidence to show that the parties' agreement assumed that Maryville Land would be entitled to a return of the escrowed funds if MHTC obtained state and federal funding. MHTC's first and third points of error therefore fail.

2. Interestingly, though *Herring* and *MHTC* follow different rules, their reasoning is similar. What key fact persuades the court in both cases that the agreement is not integrated so as to keep out the suggested evidence? How often do you think two parol evidence cases arise in which the writings say exactly the same thing and the proffered evidence is exactly the same? If each case is different from all the others, then there is quite a bit of discretion in the analysis each time, no matter what rule the court uses.

3. Had the *MHTC* court followed the Corbin rule, what evidence would you expect the parties to have offered? Would use of the Corbin rule have changed the result? Justice Traynor, in *Masterson v. Sine*, 436 P.2d 561, 565 (Cal. 1968), wrote:

> Corbin suggests that, even in situations where the court concludes that it would not have been natural for the parties to make the alleged collateral oral agreement, parol evidence of such an agreement should nevertheless be permitted if the court is convinced that the unnatural actually happened in the case being adjudicated. (3 Corbin, Contracts, s 485, pp. 478, 480; cf. Murray, The Parol Evidence Rule: A Clarification (1966) 4 Duquesne L. Rev. 337, 341--342.) This suggestion may be based on a belief that judges are not likely to be misled by their sympathies. If the court believes that the parties intended a collateral agreement to be effective, there is no reason to keep the evidence from the jury.

Who resolves parol evidence questions—judge or jury? Does Corbin's suggestion conflict with what you learned from *Colliers, Dow & Condon, Inc.* about the parol evidence rule's underlying policy?

4. Doesn't the *MHTC* court stop the analysis of integration a bit early? If the Escrow Agreement was supposed to function in tandem with the Construction Agreement and a supplemental agreement, shouldn't the question be whether these three agreements were integrated?

5. The use of recitals in the *MHTC* Escrow Agreement is pretty standard. What is the role or function of the recitals in this contract?

Luther WILLIAMS, Jr. v. JOHNSON

D.C. Court of Appeals (1967)

229 A.2d 163

QUINN, J.

[¶1] Appellant (plaintiff below) sought to recover $670 as liquidated damages under a contract for improvements on appellees' home. Appellees' defense was that the contract never came into existence because of an unfulfilled condition precedent. This appeal raises the sole question of whether the parol evidence rule required exclusion of all testimony regarding the alleged condition.

[¶2] At the trial, Luther Williams, Jr., president of appellant corporation, testified that prior to the signing of the contract, he offered to arrange any necessary financing for appellees, but was advised that they had their own. He was further informed that the down payment would be made in a few days when they received their funds. After drawing plans and contacting appellees several times, he was told that their financing had not been obtained and that they had procured another contractor to make certain improvements on the property.

[¶3] Appellees testified that they signed the contract thinking it was merely an estimate; that they told Mr. Williams the improvements would depend upon approval of their financing by their bank; and that it was their understanding with him that they would not become obligated until they had procured the funds. Appellant objected to the introduction of all testimony concerning a parol agreement regarding financing, and later objected to jury instructions on that subject. The objections were overruled, and the jury returned a verdict for appellees.

[¶4] As previously stated, the issue here is a narrow one, namely, whether the admission of testimony concerning the oral condition precedent violated the parol evidence rule. Briefly stated, that rule provides that when the parties to a contract reduce their agreement to writing, that writing is presumed to be the final repository of all prior negotiations, and testimony concerning prior or contemporaneous oral agreements which tends to vary, modify or contradict the terms of the writing is inadmissible. See 3 Corbin, *Contracts* § 573 (1960); 4 Williston, Contracts § 631 (3d ed. 1961).

[¶5] In this jurisdiction, however, it is well settled that a written contract may be conditioned on an oral agreement that the contract shall not become binding until some condition precedent resting in parol shall have been performed. *Burke v. Dulaney*, 153 U.S. 228, 14 S. Ct. 816, 38 L. Ed. 698 (1894); *Lippincott v. Kerr*, 59 App. D.C. 290, 40 F.2d 802 (1930); *Robertson v. Ramsay*, 54 App. D.C. 346, 298 F. 557 (1924); *Northeast Motor Co. v. Neal,* D.C. Mun. App., 162 A.2d 287 (1960); *Jess Fisher & Co. v. Darby*, D.C. Mun. App., 96 A.2d 270 (1953*); Wetzel v. DeGroot*, D.C. Mun. App., 86 A.2d 737 (1952); *Glascoe v. Miletich*, D.C. Mun. App., 83 A.2d 587 (1951). Furthermore, parol testimony to prove such a condition is admissible when

the contract is silent on the matter, the testimony does not contradict nor is it inconsistent with the writing, and if under the circumstances it may properly be inferred that the parties did not intend the writing to be a complete statement of their transaction. *Seitz v. Brewers' Refrigerating Mach. Co.*, 141 U.S. 510, 12 S. Ct. 46, 35 L. Ed. 837 (1891); *Jess Fisher & Co. v. Darby*, *supra; Glascoe v. Miletich, supra; Mitchell v. David*, D.C. Mun. App., 51 A.2d 375 (1947).

[¶6] The contract in question contained the following clause:

> "This contract embodies the entire understanding between the parties, and there are no verbal agreements or representations in connection therewith."

Two problems thus arise when applying the above rules to the instant case. First, in the light of an "integration clause," can evidence be admitted to show that the parties did not intend the writing to be a complete statement of their transaction? Second, can it be said that the testimony regarding the condition precedent does not contradict the writing when the contract states there are no agreements other than those contained in the writing?

[¶7] As to the first question, it has always been presumed that a written contract is the final repository of the agreement of the parties. 4 Williston, op. cit. supra § 631 at 953-954. In this regard, an integration clause merely strengthens this presumption. However, intent is a question of fact, and to determine the intent of the parties, it is necessary to look not only to the written instrument, but to the circumstances surrounding its execution.

[¶8] In *Mitchell v. David, supra*, we quoted with approval from 9 Wigmore, *Evidence* § 2430 (3d ed. 1940) as follows:

> "Whether a particular subject of negotiation is embodied by the writing depends wholly upon the intent of the parties thereto. In this respect the contrast is between voluntary integration and integration by law. Here the parties are not obliged to embody their transaction in a single document; yet they may, if they choose. Hence it becomes merely a question whether they have intended to do so." "This intent must be sought where always intent must be sought, namely, in the conduct and language of the parties and the surrounding circumstances. The document alone will not suffice. What it was intended to cover cannot be known till we know what there was to cover. The question being whether certain subjects of negotiation were intended to be covered, we must compare the writing and the negotiations before we can determine whether they were in fact covered. Thus the apparent paradox is committed of receiving proof of certain negotiations in order to determine whether to exclude them; and this doubtless has sometimes seemed to lower the rule to a quibble. But the paradox is apparent only. The explanation is that these alleged negotiations are received only provisionally. Although in form the witnesses may be allowed to recite the facts, yet in truth the facts will be afterwards treated as immaterial and legally void, if the rule is held applicable. There is a preliminary question for the judge to decide as to the intent of the parties, and upon this he hears evidence on both sides; his decision here, pro or con, concerns merely this question preliminary to the ruling of law. If he decides that the transaction was covered by the writing, he does not decide that the excluded negotiations did not take place, but merely that if they did take place they are nevertheless legally immaterial. If he decides that the transaction was not intended to be covered by the

> writing, he does not decide that the negotiations did take place, but merely that if they did, they are legally effective, and he then leaves to the jury the determination of fact whether they did take place." 51 A.2d at 378.

See also, Giotis v. Lampkin, D.C. Mun. App., 145 A.2d 779 (1958); 3 *Corbin*, op. cit. supra § 582. We are still of the opinion that this expresses the better practice.

[¶9] As to the second question, we are aware that some courts have answered it in the negative. *See, e.g., Rowe v. Shehyn*, 192 F. Supp. 428 (D.D.C.1961); *J & J Construction Co. v. Mayernik*, 241 Or. 537, 407 P.2d 625 (1965). We believe, however, that this is an erroneous interpretation of *Restatement, Contracts* § 241 (1932) which provides as follows:

> "Where parties to a writing which purports to be an integration of a contract between them orally agree, before or contemporaneously with the making of the writing, that it shall not become binding until a future day or until the happening of a future event, the oral agreement is operative if there is nothing in the writing inconsistent therewith." (Emphasis added.)

To explain this section, the following illustration is given:

> "A and B make and sign a writing in which A promises to sell and B promises to buy goods of a certain description at a stated price. The parties at the same time orally agree that the writing shall not take effect unless within ten days their local railroad has cars available for shipping the goods. The oral agreement is operative according to its terms. If, however, the writing provides 'delivery shall be made within thirty days' from the date of the writing, the oral agreement is inoperative."

In our opinion, it is clear from the example that what is intended is not the exclusion of evidence because of the existence of an "integration clause," 3 Corbin, op. cit. supra § 578 at 405-407, but an exclusion only if the alleged parol condition contradicts some other specific term of the written agreement. *See Fadex Foreign Trad. Corp. v. Crown Steel Corp.*, 272 App. Div. 273, 70 N.Y.S.2d 892, aff'd, 297 N.Y. 903, 79 N.E.2d 739 (1947); 3 *Corbin*, op. cit. supra § 577 example (5). In the instant case, no provision was made regarding financing. Therefore, the parol condition would not contradict the terms of the writing.

[¶10] For the above-stated reasons, we hold that it was not error to admit testimony tending to show that the writing was not intended to be a complete statement of the agreement of the parties and to instruct the jury to find for appellees if they determined that the negotiations regarding the condition precedent had taken place and that the contract was not to become binding unless the financing was first obtained.

Affirmed.

Questions:

1. Is the integration clause conclusive?

2. Is the integration clause consistent with the oral condition?

3. Evidence submitted to prove a contract void or voidable—fraud, mistake, duress, illegality, etc.—is admissible notwithstanding the parol evidence rule. Why?

4. Conditions—you saw some when you studied illusory promises. Understanding them depends on seeing what it is that they make conditional. Can you discern the difference between a condition of a contract and a condition of a duty? Does the latter prevent a contract from forming?

RIGGS BANK, N.A. v. Edward J. HARRIS, Jr., et al.

D. Md. (2000)

MEMORANDUM

[¶1] Riggs Bank has brought this action against Edward J. Harris, Jr. and Andre Downey to collect on guaranties executed by defendants with respect to a commercial term loan in the original principal amount of $500,000 made to Abatement Environment Resources, Inc. ("AER"). AER, which is now in bankruptcy, defaulted on the loan. Proper demand for payment has been made upon AER and upon defendants. After defendants refused to pay, Riggs filed this action and moves for summary judgment.

[¶2] Defendants assert that the loan made to AER was to finance the sale of AER to themselves. They further allege that their guaranties were subject to an oral condition precedent that this sale would close.

[¶3] Under the law of the District of Columbia—which the parties appear to agree is governing—where the parties' intentions are "clear, unambiguous and not 'reasonably or fairly susceptible of different constructions or interpretations, or of two or more different meanings,' . . . no evidence may be introduced of prior agreements or terms, whether consistent or inconsistent, within the scope of the written agreement." *Bolle v. Hume*, 619 A.2d 1192, 1196 (D.C. 1993) * * * .

[¶4] Here, the guaranties executed by defendants contained an integration clause providing that:

> This Guaranty, together with any Related Documents, constitutes the entire understanding and agreement of the parties as to matters set forth in this Guaranty. No alteration of or amendment of this this Guaranty shall be effective unless given in writing and signed by the party or parties sought to be charged or bound by the alteration or amendment.

Each of the guaranties also provided that it "would take effect when received by Lender [Riggs] . . . ." Nothing in the related loan documents suggests that the oral condition precedent alleged by defendants existed. To the contrary, the only condition precedents mentioned in the loan documents were in favor of

Riggs. The commitment letter conditioned Riggs' obligations upon the execution of a management agreement between defendants and Joseph Downey, the owner of AER, and the business loan agreement between Riggs and AER conditioned Riggs' obligations under the loan upon Riggs' receipt of defendants' guaranties.

[¶5] Defendants rely upon an exception to the parole evidence rule permitting extrinsic evidence that a contract containing unconditional obligations was not itself to become effective until an oral condition precedent had been met. As a matter of abstract logic, this exception could virtually swallow the rule. Therefore, its parameters must be judged by the context in which it has been articulated.

[¶6] The three cases cited by defendants in which the exception was applied are clearly different from the present case. Two of them, *Williams v. Johnson*, 229 A.2d 163 (D.C. 1967) and * * * involved consumer transactions and presented factual disputes as to whether the party seeking to enforce the contract had been guilty of heavy-handed treatment if not outright fraud. * * * *

[¶7] It might appear that the easy way to avoid a collision between the parole evidence rule and the "oral condition precedent" exception to the rule relied upon by defendants would be to deny Riggs' motion for summary judgment and permit discovery to proceed. That course would, however, result in substantial litigation expense and at least some delay. It would thus defeat the very purpose of the parole evidence rule "to promote the stability of transactions by preventing disgruntled parties from avoiding obligations by alleging oral understandings that conflict with their written agreement when those agreements were reduced to writing in order to forestall just such contentions." * * * *

[The court refused to allow discovery and granted Riggs Bank summary judgment on the issue of defendant's liability.]

Question: What is going on here?

C. Implied Obligations

Even while contract law takes words seriously, the law also recognizes that the words used in a contract could not possibly include everything the parties mean to say. Our inability to specify obligations with perfect completeness sometimes tempts people to read their contracts in a wooden or technical way in favor of their own positions. Non-lawyers call such a reading "finding a loophole." But the duties of cooperation and good faith can ensure that the bargain's substance is enforced notwithstanding the incompleteness of our contracts.

In the following cases, what did the parties fail to promise to do, or not do, specifically, that a judge later decides to include in one party's obligation? Do you feel safer making contracts, generally speaking—are you more willing to become a contracting party—because you know courts may add specificity to your or your counter-party's contractual obligations under the duty of cooperation or the duty of good faith?

1. Duty of Cooperation

PATTERSON v. MEYERHOFER

Court of Appeals of New York (1912)

97 N.E. 472

WILLARD BARTLETT, J.

[¶1] The parties to this action entered into a written contract whereby the plaintiff [Patterson] agreed to sell, and the defendant [Meyerhofer] agreed to buy, four several parcels of land with the houses thereon for the sum of $23,000, to be partly in cash and partly by taking title subject to certain mortgages upon the property. When she executed this contract, the defendant knew that the plaintiff was not then the owner of the premises which he agreed to sell to her, but that he expected and intended to acquire title thereto by purchasing the same at a foreclosure sale. Before this foreclosure sale took place, the defendant stated to the plaintiff that she would not perform the contract on her part, but intended to buy the premises for her own account without in any way recognizing the said contract as binding upon her, and this she did, buying the four parcels for $5,595 each. The plaintiff attended the foreclosure sale, able, ready, and willing to purchase the premises, and he bid for the same, but in every instance of a bid made by him the defendant bid a higher sum. The result was that she acquired each lot for $155 less than she had obligated herself to pay the plaintiff therefor under the contract for $620 less in all.

[¶2] In the foreclosure sale was included a fifth house, which the defendant also purchased. This was not mentioned in the written contract between the parties, but, according to the complaint, there was a prior parol agreement which provided that the plaintiff should buy all five houses at the foreclosure sale, and should convey only four of them to the defendant, retaining the fifth house for himself.

[¶3] Upon these facts the plaintiff brought the present action, demanding judgment that the defendant convey to him the fifth house, and declaring that he has a lien upon the premises purchased by her at the foreclosure sale, and that she holds the same in trust for the plaintiff subject to the contract. The complaint also prays that the plaintiff be awarded the sum of $620 damages, being the difference between the price which the defendant paid at the foreclosure sale for the four houses mentioned in the contract and the price which she would have had to pay the plaintiff thereunder. The learned judge who tried the case at Special Term rendered judgment in favor of the defendant, holding that, under the contract of sale, there was no relation of confidence between the vendor and vendee. 'In the present case,' he said, 'each party was free to act for his own interest, restricted only by the stipulations of the contract.' He was, therefore, of the opinion that 'the defendant had a right to buy in at the auction, and that she is entitled to hold exactly as though she

had been a stranger, and that the plaintiff is not entitled to recover the difference between the price paid at the auction and the contract price.'

[¶4] I am inclined to agree with the trial court that no relation of trust can be spelled out of the transactions between the parties. There is no finding of any parol agreement in respect to the fifth house which has been mentioned, and, even if there had been such an agreement resting merely in parol, I do not see that it would have been enforceable. As to the four parcels which constituted the subject-matter of the written contract, the defendant avowed her intention to ignore that contract before bidding for them, and cannot be regarded as having gone into possession under the plaintiff as vendor, but did so rather in defiance of any right of his * * * . * * * *

[¶5] There is no need of judicially declaring any trust in the defendant, however, to secure to the plaintiff the profit which he would have made if the defendant had not intervened as purchase at the foreclosure sale, and had fulfilled the written contract on her part. This is represented by his claim for $620 damages. That amount, under the facts as found, I think the plaintiff was entitled to recover. He has demanded it in his complaint, and he should not be thrown out of court because he has also prayed for too much equitable relief.

[¶6] In the case of every contract there is an implied undertaking on the part of each party that he will not intentionally and purposely do anything to prevent the other party from carrying out the agreement on his part. This proposition necessarily follows from the general rule that a party who causes or sanctions the breach of an agreement is thereby precluded from recovering damages for its nonperformance or from interposing it as a defendant to an action upon the contract. *Young v. Hunter*, 6 N.Y. 203; *Barton v. Gray*, 57 Mich. 622, 24 N.W. 638, and cases there cited. 'Where a party stipulates that another shall do a certain thing, he thereby impliedly promises that he will himself do nothing which may hinder or obstruct that other in doing that thing.' *Gay v. Blanchard*, 32 La. Ann. 497.

[¶7] By entering into the contract to purchase from the plaintiff property which she knew he would have to buy at the foreclosure sale in order to convey it to her, the defendant impliedly agreed that she would do nothing to prevent him from acquiring the property at such a sale. The defendant violated the agreement thus implied on her part by bidding for and buying the premises herself. Although the plaintiff bid therefor, she uniformly outbid him. Presumably, if she had not interfered, he could have bought the property for the same price which she paid for it. He would then have been able to sell it to her for the price specified in the contract (assuming that she fulfilled the contract), which was $620 more. This sum, therefore, represents the loss which he has suffered. It is the measure of the plaintiff's damages for the defendant's breach of contract.

[¶8] I see no escape from this conclusion. It is true that the contract contemplated that the four houses should go to the defendant and they have gone to her; but that is not all. The contract contemplated that they should go to the plaintiff first. In that event the plaintiff would have received $620 which he has not got. This would have had to be paid by the defendant if she had fulfilled her contract; and she should be required to pay it now unless she can present some better defense than is presented in this record. This will place both parties in the position contemplated by the contract. The defendant will have paid no more than the contract obligated her to pay. The plaintiff will have received all to which the contract entitled him. I leave the fifth house out of consideration because as to that it seems to me there was no enforceable agreement.

[¶9] For these reasons, the judgments of the Appellate Division and the Special Term should be reversed and a new trial granted, with costs to abide the event.

CHASE, J. (dissenting). [Omitted.] * * * *

Judgment reversed, etc.

Questions:

1. Did Patterson breach? The answer to this question is “yes,” but Patterson’s breach is excused for failure of a condition precedent. Under the doctrine of constructive conditions, which we will soon study, the law implies that the parties’ performances which are to occur simultaneously are conditions of each counterparties’ duty to perform. Meyerhofer’s duty of cooperation is to occur simultaneously with Patterson’s performance, so Meyerhofer’s performance of the duty of cooperation is deemed a constructive condition of Patterson’s duty. When Meyerhofer does not perform, Patterson’s performance does not become due, and Patterson’s failure to perform is excused.

2. What is the source of the duty to cooperate?

3. What was Meyerhofer thinking?

4. Should Meyerhofer be liable for the tort of interference with contractual relations? The “elements of a cause of action for tortious interference with contractual relations are (1) there was a contract subject to interference, (2) the act of interference was willful and intentional, (3) such intentional act was a proximate cause of plaintiff’s damage, and (4) actual damage or loss occurred.” *Juliette Fowler Homes, Inc. v. Welch Associates, Inc.*, 793 S.W.2d 660 (Tex. 1990).

PROBLEM 44: Hensel contracted to sell a house to Billman for $54,000 cash. Billman gave a check for $1,000 earnest money. “A condition of the contract was the ability of the buyers to secure a conventional mortgage on the property for not less than $35,000 within thirty (30) days.” On the day following execution of the contract, Billman met with an agent of Lincoln Bank. The Bank told Billman that he “could not obtain a mortgage loan of $35,000 unless he could show he had the difference between the purchase price and the amount of the mortgage. After totaling his available resources, including a 90-day short term note for $10,000 representing the proceeds from the sale of his present home, Billman was $6,500 short of the required $19,000 balance.” Billman then invited his parents to tour the home. Billman’s father did not like the home. In the meantime, Hensel deposited the earnest money check. Billman then told Hensel that he could not buy the house because he could not obtain a $5,000 gift from his parents. Hensel replied that she would lower the price of the home by $5,000. Billman then said he was still $1,500 short. Billman did not deposit funds to cover the check and stopped payment on it. Billman then claimed to cancel the contract. Billman never contacted another financial institution and never formally applied for a loan. Hensel sued for the earnest money. Should she get it? Can you construct an argument based on *Patterson v. Meyerhofer*? *Billman v. Hensel*, 391 N.E.2d 671 (Ind. Ct. App. 1979).

Questions:

1. In *Seaward Construction Company, Inc. v. City of Rochester*, 383 A.2d 707 (N.H. 1978), Seaward Construction entered into a contract to install sewer pipe for the City at a rate of $19 per foot for pipe installed 0-10 feet and $60 per foot installed at 10-18 feet. The contract stated:

> 2. All monies due under the Contract are subject to the receipt of said monies by said Rochester Housing Authority from the Federal Housing and Urban Development Agency (HUD) and turned over to said City of Rochester for payment of the construction of said facilities.
>
> 5. The City of Rochester shall be under no legal obligation to advance any of its own funds for said construction.
>
> 6. Payment to said Seaward Construction Company, Inc. is contingent upon receipt of funds by the Rochester Housing Authority and turning same over to the City of Rochester for payment to said Seaward Construction Company.

Throughout the course of the contract, Seaward claimed funds for over 1,000 feet of pipe laid. The City paid most (920 feet worth) at a rate of $19 over Seaward's objection that this pipe was installed lower than 10 feet deep. When Seaward filed a formal claim for the difference between $19 and $60 for the 920 feet, the City claimed that it had never received funds from HUD. No evidence showed that the City had applied for funds, however. The court stated:

> In every agreement there exists an implied covenant that each of the parties will act in good faith and deal fairly with the other. *Griswold v. Heat Corporation*, 108 N.H. 119, 124, 229 A.2d 183, 187 (1967). The mere fact that the defendant is a city does not release it from this implied obligation to act in good faith and deal fairly with the plaintiff. *See Leary v. City of Manchester*, 90 N.H. 256, 257, 6 A.2d 760, 761 (1939). The express language in the agreement is perfectly clear that the city will not be required to expend its own funds for payment of the installation of the sewer line, but it is also reasonably clear that the city was under an implied obligation to make a good-faith effort to obtain funds from HUD to pay the plaintiff. *Rochester Park, Inc. v. City of Rochester*, 38 Misc.2d 714, 238 N.Y.S.2d 822, 826-27 (1963) aff'd 19 A.D.2d 776, 241 N.Y.S.2d 763 (1963). *Public Market Co. v. Portland*, 171 Or. 522, 588-89, 130 P.2d 624, 649-50 (1942).

The court held that, if Seaward showed that it had buried the pipe deeper than 10 feet, and the City had made no attempt to obtain funds, Seaward should be given judgment. Is there any difference between *Seaward Construction* and *Billman*? Is there any difference between these two and *Patterson*?

2. What was the City thinking?

3. Why was the financing clause a condition precedent and not subsequent (in either *Billman* or *Seaward Constr. Co*.)?

4. For whose benefit is the "subject to financing" clause inserted?

5. If the purchaser doesn't obtain financing but wants to and is able to close, anyway, can the purchaser do so? What argument suggests it can?

6. The buyer need not apply for a loan if the effort would be futile. In *Nicholls v. Pitoukkas*, 491 N.E.2d 574 (Ind. App. 1986), the financing condition stipulated that the buyer would apply for a loan within six days. The Pitoukkases, buyers, did not apply during that time. Their efforts thereafter were unsuccessful. The anticipated mortgage payment was $719.58 per month. The Pitoukkases together had income of only $806 per month. The court found, "Mr. and Mrs. Pitoukkas could not have obtained financing had they made ten timely and diligent applications for financing." *Id*. at 575. Then the court explained, "It is this undisputed fact which distinguishes this case from *Billman v. Hensel* (1979), 181 Ind. App. 272, 391 N.E.2d 671. In *Billman* the evidence did not exclude the possibility a reasonable and good faith effort to obtain financing would have been successful." *Id.* n.3.

7. What is the source of the duty here?

2. Good Faith

DESERT HERITAGE LIMITED PARTNERSHIP v. CITY OF TUCSON

Ariz. App. (2008)

HOWARD, Presiding Judge.

[¶1] Appellant Desert Heritage Limited Partnership appeals from the trial court's grant of appellee City of Tucson's motion for summary judgment on Desert Heritage's claim that the City breached a lease by cancelling it and of the City's motion to dismiss Desert Heritage's claims of unpaid rent and unamortized tenant improvements. Because issues of fact preclude summary judgment on the cancellation claim, we reverse that ruling, but affirm the dismissal of the unpaid rent claim.

Factual and Procedural Background

[¶2] The basic factual background is undisputed. The City leased office space in a building owned by Desert Heritage. Although there were multiple leases for different spaces, the lease at the center of this controversy involved space used by the City's Human Resources Department ("HR lease" or "the lease"). An addendum to the lease included a cancellation clause providing circumstances under which the City could cancel the lease before the end of its term, March 31, 2008. The clause reads:

> In the event that the Mayor and Council of the City of Tucson shall not appropriate sufficient funds for the payment of the rent (as set forth by the Lease) in the adopted budget for the fiscal years subsequent to 2000 – 2001, then [the City] shall have the right annually upon the anniversary of its lease term, with 90 days prior written notice to [Desert Heritage], to cancel the lease. In such an event, [the City] will immediately pay to [Desert Heritage] the total sum of any unamortized costs for tenant[']s improvements to the demised premises.

In December 2005, the Mayor and Council adopted a resolution directing the City Manager to "eliminate funding from the annual City budget for outside rental of office space for the City of Tucson Department of Human Resources for fiscal Year 2006–2007." One week later, the City notified Desert Heritage that it would exercise the cancellation clause in the lease, effective April 1, 2006.

[¶3] Desert Heritage then sued the City, claiming it had breached the lease by failing to comply with the cancellation clause and by violating the covenant of good faith and fair dealing in exercising that clause. It also sought damages for unpaid rent and unamortized tenant improvement costs. The City moved for partial summary judgment, contending that it had complied with the cancellation clause and that it did not violate the covenant of good faith and fair dealing. The trial court granted that motion. * * * *

Compliance with the Cancellation Clause

[¶4] Desert Heritage first argues the trial court erred by granting summary judgment against it on its claim that the City breached the lease by failing to properly comply with the cancellation clause. We review the grant of summary judgment de novo and view the facts in the light most favorable to the opposing party. *Liberty Mut. Fire Ins. Co. v. Mandile*, 192 Ariz. 216, 222, 963 P.2d 295, 301 (App. 1997). "[W]e reverse the summary judgment if our review reveals that reasonable inferences concerning material facts could be resolved in favor of the opposing party." *Id.*

[¶5] Our goal in interpreting a contract is to determine the parties' intent and give effect to the contract as a whole. *Potter v. U.S. Specialty Ins. Co.*, 209 Ariz. 122, ¶ 7, 98 P.3d 557, 559 (App. 2004). We view the language of the contract in the context of the surrounding circumstances. *Id.* We will enforce a valid contract even if the result is harsh. *Freedman v. Cont'l Serv. Corp.*, 127 Ariz. 540, 545, 622 P.2d 487, 492 (App. 1980).

[¶6] Desert Heritage contends the cancellation clause requires that the Mayor and Council fail to appropriate funds and asserts the process of cancellation and relocation had begun before the Mayor and Council were even involved. But the cancellation clause does not require that the idea of cancellation originate with the Mayor and Council. It simply requires that they fail to appropriate funds and allows the City to cancel the lease on an anniversary date so long as it provides Desert Heritage with ninety days' notice. It did provide such notice. The trial court did not err in finding that the City had complied with the express terms of the cancellation clause.

[¶7] * * * *

[¶8] Finally, Desert Heritage contends that the only valid reason for cancellation under the clause is a lack of sufficient funds to pay for the lease. But the cancellation clause does not limit the reasons for cancellation to a lack of funds. Instead, the decision to "appropriate" funds is a discretionary, legislative act. Therefore, this argument also fails.

[¶9] Even assuming the City's cancellation was "self-serving," as Desert Heritage argues, the trial court correctly determined that the City properly had complied with the express terms of the cancellation clause. And, therefore, the City was entitled to summary judgment on that portion of the cancellation claim.

Covenant of Good Faith and Fair Dealing

[¶10] Desert Heritage next argues the trial court erred by determining that Desert Heritage had not raised a genuine issue of material fact concerning the City's alleged breach of the lease's implied covenant of good faith and fair dealing. Again our review is de novo. *Liberty Mut. Fire Ins. Co.*, 192 Ariz. at 222, 963 P.2d at 301.

[¶11] The covenant of good faith and fair dealing is implied in every contract. *Bike Fashion Corp. v. Kramer*, 202 Ariz. 420, ¶ 13, 46 P.3d 431, 434 (App. 2002). "A party may breach an express covenant of the contract without breaching the implied covenant of good faith and fair dealing." *Wells Fargo Bank v. Ariz. Laborers, Teamsters & Cement Masons Local No. 395 Pension Trust Fund*, 201 Ariz. 474, ¶ 64, 38 P.3d 12, 29 (2002). "Conversely, because a party may be injured when the other party to a contract manipulates bargaining power to its own advantage, a party may nevertheless breach its duty of good faith without actually breaching an express covenant in the contract." *Id.*

[¶12] It follows from this that "'[i]nstances inevitably arise where one party exercises discretion retained or unforeclosed under a contract in such a way as to deny the other a reasonably expected benefit of the bargain.'" *Bike Fashion Corp.*, 202 Ariz. 420, ¶ 14, 46 P.3d at 435, *quoting Wells Fargo Bank*, 201 Ariz. 474, ¶ 66, 38 P.3d at 30 (alteration in *Bike Fashion Corp.*).

> Thus, Arizona law recognizes that a party can breach the implied covenant of good faith and fair dealing both by exercising express discretion in a way inconsistent with a party's reasonable expectations and by acting in ways not expressly excluded by the contract's terms but which nevertheless bear adversely on the party's reasonably expected benefits of the bargain. *Id.*

[¶13] In *Wells Fargo Bank*, the court quoted Professor Steven J. Burton's explanation of the duty of good faith:

> "'The good faith performance doctrine may be said to permit the exercise of discretion for any purpose—including ordinary business purposes—reasonably within the contemplation of the parties. A contract thus would be breached by a failure to perform in good faith if a party uses its discretion for a reason outside the contemplated range—a reason beyond the risks assumed by the party claiming a breach.'"

201 Ariz. 474, ¶ 66, 38 P.3d at 30, *quoting Sw. Sav. & Loan Ass'n v. SunAmp Sys., Inc.*, 172 Ariz. 553, 558-59, 838 P.2d 1314, 1319-20 (App. 1992) (footnotes omitted in *Sw. Sav.& Loan*), *quoting* Steven J. Burton, *Breach of Contract and the Common Law Duty to Perform in Good Faith*, 94 Harv. L. Rev. 369, 385-86 (1980). The court further observed:

> Burton's recitation fully comports with RESTATEMENT (SECOND) OF CONTRACTS § 205 cmt. a (1981), which states, "Good faith performance or enforcement of a contract emphasizes faithfulness to an agreed common purpose and consistency with the justified expectations of the other party." Consistent with Burton and the RESTATEMENT, this court has held in a variety of contexts that a contracting party may not exercise a retained contractual power in bad faith. *See Rawlings [v. Apodaca*, 151 Ariz. 149,] 153-157, 726 P.2d [565,] 569-73 [(1986)] (power to adjust claims in an insurance contract); *Wagenseller [v. Scottsdale Memorial Hosp.*, 147 Ariz. 370,] 385-86, 710 P.2d [1025,] 1040-41 [(1985)] (power to fire employee at will for a bad cause).

Wells Fargo Bank, 201 Ariz. 474, ¶ 66, 38 P.3d at 30. Whether a party's actions constitute a breach of the covenant of good faith and fair dealing is a question of fact. *See id.* ¶¶ 69-70.

[¶14] Desert Heritage produced evidence of continuous conflict between it and representatives of the City that had been ongoing before the City exercised the cancellation clause. This included evidence that the City had offered to remain at Desert Heritage's building if Desert Heritage dropped its claim for unpaid rent. Desert Heritage also claimed that, when the City was unable to obtain the concessions it wanted concerning the lease during settlement negotiations, the City decided to exercise the cancellation clause. A jury could determine that the City's alleged use of the cancellation clause to force Desert Heritage to make other concessions regarding the lease was ""outside the contemplated range—a reason beyond the risks assumed by the party claiming a breach."" *Wells Fargo Bank*, 201 Ariz. 474, ¶ 66, 38 P.3d at 30, *quoting Sw. Sav. & Loan*, 172 Ariz. at 558-59, 838 P.2d at 1319-20, *quoting* Burton, *supra*, at 385-86.

[¶15] The City claims that it cancelled the lease to reduce expenses and to increase efficiency. But Desert Heritage produced evidence that the City had another motivation and therefore has raised a genuine issue of material fact. Furthermore, based on the limited arguments and evidence presented so far, a jury reasonably could conclude that these goals should have been considered by the City before it entered the lease and, accordingly, were outside the contemplated range. Conversely, a jury could conclude these reasons were not outside the contemplated range. Therefore, even if the jury finds that the City was motivated by cost savings and efficiency, an issue of fact exists at this point in time with regard to whether those motivations constitute bad faith. Accordingly, we conclude the trial court erred by granting summary judgment on this portion of the claim.

[¶16] The City, however, relies on *Southwest Savings & Loan* for the proposition that "'[a]cts in accord with the terms of one's contract cannot *without more* be equated with bad faith.'" *Sw. Sav. & Loan*, 172 Ariz. at 558, 838 P.2d at 1319 (emphasis in *Sw. Sav. & Loan*), *quoting Balfour, Guthrie & Co. v. Gourmet Farms*, 166 Cal. Rptr. 422, 427-28 (Ct. App. 1980). We agree with that statement of the law. But here Desert Heritage produced some evidence from which a reasonable jury could conclude the City had acted in bad faith. If the jury determines that the City acted in bad faith as outlined above, the cancellation was not an act in accord with the terms of the contract, *without more*.

[¶17] Because we have concluded an issue of fact exists as to whether the City breached the covenant of good faith and fair dealing by cancelling the lease, we need not address Desert Heritage's argument that, even if cancellation was proper, the City could not cancel the lease until March 2007. Additionally, Desert Heritage's claim for unamortized tenant improvements may become moot, and we will not, therefore, address whether the trial court properly dismissed the claim. * * * *

Conclusion

[¶25] For the foregoing reasons, * * * we reverse the summary judgment with respect to Desert Heritage's claim that the City violated the covenant of good faith and fair dealing when it cancelled the lease. We remand the case for proceedings consistent with this decision. * * * *

Questions:

1. Choose a source for the good faith obligation as described and applied by the *Desert Heritage* court: (a) community standards, (b) economic efficiency, (c) agreement, (d) the bargain of the parties. Why?

2. Not all courts have been so functional with their definitions of good faith. The courts have struggled for a long time with what good faith requires. The law has coalesced around something like what the *Desert Heritage* case describes. Consider the following from *Wilson v. Amerada Hess Corp.*, 773 A.2d 1121, 1126-31 (N.J. 2001):

> [¶1] A covenant of good faith and fair dealing is implied in every contract in New Jersey. *Sons of Thunder, Inc. v. Borden, Inc.*, 148 N.J. 396, 420, 690 A.2d 575 (1997) (citing numerous cases of this Court holding covenant implied in every contract). That covenant is among the few terms that "[c]ourts have been called upon to supply." E. Allan Farnsworth, Contracts § 1.5, at 12-14 (1990).
>
> [¶2] Implied covenants are as effective components of an agreement as those covenants that are express. *Aronsohn v. Mandara*, 98 N.J. 92, 100, 484 A.2d 675 (1984). Although the implied covenant of good faith and fair dealing cannot override an express term in a contract, a party's performance under a contract may breach that implied covenant even though that performance does not violate a pertinent express term. *Sons of Thunder, Inc., supra*, 148 N.J. at 419, 690 A.2d 575. Unlike many other states, in New Jersey "a party to a contract may breach the implied covenant of good faith and fair dealing in performing its obligations even when it exercises an express and unconditional right to terminate." *Id.* at 422, 690 A.2d 575; *see also Bak-A-Lum Corp. v. Alcoa Bldg. Prods., Inc.*, 69 N.J. 123, 129-30, 351 A.2d 349 (1976) (finding that defendant's conduct in terminating contract constituted bad faith although conduct did not violate express terms of written agreement); cf. *Burger King Corp. v. Weaver*, 169 F.3d 1310, 1316 (11th Cir.1999) (finding that under Florida law action for breach of implied covenant of good faith and fair dealing cannot be maintained in absence of breach of express contract provision); *Payne v. McDonald's Corp.*, 957 F. Supp. 749, 758 (D.Md.1997) (determining that under Illinois law covenant of good faith and fair dealing does not provide independent source of duties). Other jurisdictions regard the implied covenant of good faith and fair dealing as merely a guide in the construction of explicit terms in an agreement. *See Payne*, *supra*, 957 F. Supp. at 758 (citing *Beraha v. Baxter Health Care Corp.*, 956 F.2d 1436, 1443 (7th Cir.1992)).
>
> [¶3] What constitutes good faith performance and fair dealing has been the subject of considerable analysis. For transactions involving merchants and the sale of goods, the Uniform Commercial Code has defined good faith as "honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade." N.J.S.A. 12A:2-103(1)(b). The Restatement (Second) of Contracts notes that every contract imposes on each party a duty of good faith and fair dealing in its performance and enforcement. Restatement (Second) of Contracts § 205 (1981). A comment to the Restatement states that "[g]ood faith performance or enforcement of a contract emphasizes faithfulness to an agreed common purpose and consistency with the justified expectations of the other party; it excludes a

variety of types of conduct characterized as involving 'bad faith' because they violate community standards of decency, fairness or reasonableness." Restatement (Second) of Contracts § 205 comment a (1981). In *Sons of Thunder, Inc., supra*, we reaffirmed our earlier formulation:

> In every contract there is an implied covenant that neither party shall do anything which will have the effect of destroying or injuring the right of the other party to receive the fruits of the contract; which means that in every contract there exists an implied covenant of good faith and fair dealing.

[148 N.J. at 421, 690 A.2d 575 (quoting *Palisades Properties, Inc. v. Brunetti*, 44 N.J. 117, 130, 207 A.2d 522 (1965))(citing 5 Williston on Contracts § 670, at 159-60 (3d ed.1961)).]

[¶4] * * * * Here we are confronted with the question of the appropriate force of the implied covenant of good faith and fair dealing in reviewing the actions of a contracting party expressly vested with unilateral discretionary authority over pricing. Stated differently, the task here is to identify in that context the parties' reasonable expectations.

[¶5] In his widely cited law review article, Professor Steven J. Burton discusses the implied covenant of good faith and fair dealing in respect of contracts authorizing one party to have the discretion to make decisions as to quantity, price, time, and other conditional aspects of a contract. Steven J. Burton, *Breach of Contract and the Common Law Duty to Perform in Good Faith*, 94 Harv. L. Rev. 369 (1980). Professor Burton comments that decisions concerning price that are deferred to the discretion of one of the parties must be made in good faith. *Id.* at 381-82. He explains that "[a] party with discretion may withhold all benefits for good reasons. . . . The fact that a discretion-exercising party causes the dependent party to lose some or all of its anticipated benefit from the contract thus is insufficient to establish a breach of contract by failing to perform in good faith." *Id.* at 384-85. A good faith performance doctrine may be said to permit the exercise of discretion for any purpose—including ordinary business purposes—reasonably within the contemplation of the parties. *Id.* at 385-86. It follows, then, that "[a] contract thus would be breached by a failure to perform in good faith if a party uses its discretion for a reason outside the contemplated range— a reason beyond the risks assumed by the party claiming the breach." Id. at 386.

[¶6] Professor Burton's approach respects the express bargain of parties that gave unilateral authority over price to one party alone. That approach also requires that the discretion-exercising party not unilaterally use that authority in a way that intentionally subjects the other party to a risk beyond the normal business risks that the parties could have contemplated at the time of contract formation. In this manner:

> [t]he good faith performance doctrine may be said to enhance economic efficiency by reducing the costs of contracting. The costs of exchange include the costs of gathering information with which to choose one's contracting partners, negotiating and drafting contracts, and risk taking with respect to the future. The good faith performance doctrine reduces all three kinds of costs by allowing parties to rely on the law in place of incurring some of these costs.

[*Id.* at 393.]

[¶7] In the same vein, various courts have stated that a party must exercise discretion reasonably and with proper motive when that party is vested with the exercise of discretion under a contract. * * * *

III.

[¶8] The question remaining is whether plaintiffs had a full opportunity to show bad motive on Hess's part before Hess was granted summary judgment. Plaintiffs claim that they were denied information that would provide circumstantial evidence of lack of good faith. Plaintiffs' bad faith claim is that Hess set its DTW prices with the specific intent to impair the ability of the dealers to compete in the gasoline market or, alternatively, to discourage the franchisees from continuing in the business in order to replace them with Hess co-op stations.

[¶9] Plaintiffs moved to compel the production of documents showing the performance, costs, volumes, margins, and profits of the Hess co-op stations and DAP stations in the marketing areas of plaintiffs' stations. They contend that those documents would have shown that Hess knew that based on the necessary operating costs involved with running plaintiffs' stations, plaintiffs could not sustain their businesses on the pricing differential allowed and the resultant decreased sales volume. Plaintiffs contend that that information, in conjunction with information showing that, since the 1980s, Hess stations have changed from being predominantly run by franchisees to predominantly Hess-run, would create a jury question concerning whether Hess acted with an improper motive. Plaintiffs' requested discovery was denied by the trial court. Although deference is generally accorded to the trial court on such matters, *see Connolly v. Burger King Corp.,* 306 N.J. Super. 344, 349, 703 A.2d 941 (App. Div.1997) (stating that abuse of discretion standard applies to review of decision regarding discovery), in this instance we cannot dismiss the possibility that the information plaintiffs sought would raise a jury question on the issue of breach of the implied covenant. * * * *

[¶10] We part company with the Appellate Division * * * in respect of its conclusion that the further discovery sought by plaintiffs was unlikely to lead to the discovery of relevant evidence on the question of breach by Hess. Here, the contention is that Hess set prices intending to destroy plaintiffs economically. Although that allegation may be difficult to prove, our province is not to decide questions of fact, but only to determine whether sufficient information has been presented to warrant a jury determination. A corollary of that principle is that a plaintiff must have a reasonable opportunity to obtain facts not available to it other than through formal discovery.

Choose a source for the good faith obligation as described and applied by the *Amerada Hess* court: (a) community standards, (b) economic efficiency, (c) agreement, (d) the bargain of the parties. Why?

3. Does the good faith standard allow sufficient certainty that parties may *ex ante* be assured of the economic efficiency of their deals?

4. If you had to choose a moral basis for the good faith standard, what would it be?

5. Is the good faith obligation an extension of the cooperation requirement? Vice versa? Are they separate?

The UCC imposes an obligation of good faith explicitly on a parties performing contracts subject to the UCC's provisions, including sales of goods. The following is a sale of goods case, but it illustrates the general rule of good faith so well that it will be useful to you.

NEUMILLER FARMS, INC. v. Jonah D. CORNETT et al.

Alabama Supreme Court (1979)

368 So.2d 272

SHORES, Justice.

[¶1] Jonah D. Cornett and Ralph Moore, Sellers, were potato farmers in DeKalb County, Alabama. Neumiller Farms, Inc., Buyer, was a corporation engaged in brokering potatoes from the growers to the makers of potato chips. The controversy concerns Buyer's rejection of nine loads of potatoes out of a contract calling for twelve loads. A jury returned a verdict of $17,500 for Sellers based on a breach of contract. Buyer appealed. We affirm.

[¶2] From the evidence, the jury could have found the following:

[¶3] On March 3, 1976, the parties signed a written contract whereby Sellers agreed to deliver twelve loads of chipping potatoes to Buyer during July and August, 1976, and Buyer agreed to pay $4.25 per hundredweight. The contract required that the potatoes be United States Grade No. 1 and "chipt [sic] to buyer satisfaction." As the term was used in this contract, a load of potatoes contains 430 hundredweight and is valued at $1,827.50.

[¶3] Sellers' potato crop yielded twenty to twenty-four loads of potatoes and Buyer accepted three of these loads without objection. At that time, the market price of chipping potatoes was $4.25 per hundredweight. Shortly thereafter, the market price declined to $2.00 per hundredweight.

[¶4] When Sellers tendered additional loads of potatoes, Buyer refused acceptance, saying the potatoes would not "chip" satisfactorily. Sellers responded by having samples of their crop tested by an expert from the Cooperative Extension Service of Jackson County, Alabama, who reported that the potatoes were suitable in all respects. After receiving a letter demanding performance of the contract, Buyer agreed to "try one more load." Sellers then tendered a load of potatoes which had been purchased from another grower, Roy Hartline. Although Buyer's agent had recently purchased potatoes from Hartline at $2.00 per hundredweight, he claimed dissatisfaction with potatoes from the same fields when tendered by Sellers at $4.25 per hundredweight. Apparently the jury believed this testimony outweighed statements by Buyer's agents that Sellers' potatoes were diseased and unfit for "chipping."

[¶5] Subsequently, Sellers offered to purchase the remaining nine loads of potatoes from other growers in order to fulfill their contract. Buyer's agent refused this offer, saying ". . . 'I'm not going to accept any more of your potatoes. If you load any more I'll see that they're turned down.'. . . 'I can buy potatoes all day for $2.00.'" No further efforts were made by Sellers to perform the contract.

[¶6] At the time of Buyer's final refusal, Sellers had between seventeen and twenty-one loads of potatoes unharvested in their fields. Approximately four loads were sold in Chattanooga, Tennessee; Atlanta, Georgia; and local markets in DeKalb County. Sellers' efforts to sell their potato crop to other buyers were hampered by poor market conditions. Considering all of the evidence, the jury could properly have found that Sellers' efforts to sell the potatoes, after Buyer's final refusal to accept delivery, were reasonable and made in good faith.

[¶7] This case presents three questions: 1) Was Buyer's refusal to accept delivery of Sellers' potatoes a breach of contract? 2) If so, what was the proper measure of Sellers' damages? and 3) Was the $17,500 jury verdict within the amount recoverable by Sellers under the proper measure of damages?

[¶8] § 7-2-703, Code of Alabama 1975 (UCC), specifies an aggrieved seller may recover for a breach of contract "Where the buyer *wrongfully* rejects . . . goods . . . ." (Emphasis Added.) We must determine whether there was evidence from which the jury could find that the Buyer acted wrongfully in rejecting delivery of Sellers' potatoes.

[¶9] A buyer may reject delivery of goods if either the goods or the tender of delivery fails to conform to the contract. § 7-2-601, Code of Alabama 1975. In the instant case, Buyer did not claim the tender was inadequate. Rather, Buyer asserted the potatoes failed to conform to the requirements of the contract: i. e., the potatoes would not chip to buyer satisfaction.

[¶10] The law requires such a claim of dissatisfaction to be made in good faith, rather than in an effort to escape a bad bargain. *Shelton v. Shelton*, 238 Ala. 489, 192 So. 55 (1939); *Jones v. Lanier*, 198 Ala. 363, 73 So. 535 (1916); *Electric Lighting Co. v. Elder Bros.*, 115 Ala. 138, 21 So. 983 (1896).

[¶11] Buyer, in the instant case, is a broker who deals in farm products as part of its occupation and, therefore, is a "merchant" with respect to its dealings in such goods. § 7-2-104, *Code of Alabama* 1975. In testing the good faith of a merchant, § 7-2-103, Code of Alabama 1975, requires ". . . honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade." A claim of dissatisfaction by a merchant-buyer of fungible goods must be evaluated using an objective standard to determine whether the claim is made in good faith. Because there was evidence that the potatoes would "chip" satisfactorily, the jury was not required to accept Buyer's subjective claim to the contrary. A rejection of goods based on a claim of dissatisfaction, which is not made in good faith, is ineffectual and constitutes a breach of contract for which damages are recoverable. * * * *

[¶12] Suffice it to say that there is evidence in the record from which the jury could reasonably conclude that the Sellers substantially performed their part of the bargain and had incurred substantially all of the expenses incidental to performance on their part. This being so, the jury's verdict of $17,500 was within those damages recoverable by Sellers as a consequence of Buyer's breach of contract.

AFFIRMED.

TORBERT, C. J., and MADDOX, JONES and BEATTY, JJ., concur.

Question: Did the court use the *Desert Heritage* definition of good faith? The *Amerada Hess* standard? If you were to make explicit what good faith required in this contract that was breached by the Buyer, how would you state it?

Paul REID v. KEY BANK OF SOUTHERN MAINE, INC.

1st Cir. U.S. Ct. App. (1987)

821 F.2d 9

BOWNES, Circuit Judge.

[¶1] Plaintiffs Paul and Mary J. Reid brought a seventeen-count action in United States District Court for the District of Maine against Key Bank of Southern Maine, Inc., defendant. Plaintiffs alleged various federal and state claims resulting from the actions of Depositors Trust Co. of Southern Maine (Depositors), Key Bank's predecessor in interest. The suit grew out of the circumstances surrounding the termination by Depositors of plaintiffs' credit arrangement with it. A jury trial resulted in a verdict for plaintiffs on one of the counts and an award of damages. Both parties have appealed.

I. SUMMARY OF THE FACTS

[¶2] In mid-1975, Paul Reid approached Depositors to obtain financing for the establishment of a painting business. From 1976 through 1979, Depositors granted Reid a series of loans which Reid used for the operation of his business, Pro Paint and Decorating. During this period, Peter H. Traill was the loan officer responsible for Reid's accounts, Marco F. DeSalle was the president of the bank, and Henry Lawson was, for a time, an assistant vice-president.

[¶3] On March 2, 1979, Reid and Depositors entered into a $25,000 commercial credit agreement. The agreement was variously explained at trial as a "line of credit" and an "incomplete loan." However defined, it was the largest amount of credit Depositors had yet extended to Reid. Reid sought the credit primarily to finance work he was performing at the Bucksport Housing Project for Nickerson & O'Day, Inc., a general contractor.

[¶4] In mid-May, 1979, Traill telephoned Reid and informed him that Depositors would not grant him any further advances under the March agreement. Reid had thought at the time that this halt of further advances might only be temporary. Defendant claimed that Traill sent Reid a follow-up letter on May 18, 1979, stating that Depositors would no longer honor overdrafts on Reid's accounts and suggesting that Reid restructure his debts with another lender. Reid denied receiving the letter and alleged that it was never, in fact, sent to him.

[¶5] On May 29, 1979, Nickerson & O'Day sent a check to Depositors as payment for Reid's work at the Bucksport Housing Project. The check was for $6,507.90. It was made out to Depositors and to Pro

Paint pursuant to an agreement between Depositors and Reid whereby Reid assigned his accounts receivable to Depositors as security for the March loan. Depositors credited $2,500 to the account of Pro Paint and applied the remaining $4,007.90 to offset part of the outstanding balance on Reid's March loan. Reid claimed that Depositors undertook this action without his authorization.

[¶6] Reid claimed that another check was also inappropriately handled by Depositors. He testified that on June 8, 1979, he gave Traill a check for an amount somewhere between eleven and fifteen thousand dollars. Reid contended that this check represented the proceeds for work he performed at Brunswick Naval Air Station. He alleged that Depositors converted the check and used it to offset part of the balance on the March loan. Defendant strongly contested this claim and implied at trial that the check in question existed only in Reid's imagination.

[¶7] On September 20, 1979, Reid received a past-due notice on the March loan. The notice requested payment of $694.84 in interest and stated that the payment had been due on September 5, 1979. Reid testified that this was the first notice he had received concerning the March loan.

[¶8] On November 5, 1979, Depositors repossessed Reid's personal automobile and one of his vans. Reid discovered one of the vehicles in a lot and attempted to drive it away. He testified that he did not know it had been repossessed and thought it had been stolen. On a complaint by Lawson, Reid was arrested in connection with this incident and was placed for a time in jail.

[¶9] Reid's business collapsed and he lost his four vehicles and his home. On November 7, 1979, Reid filed a Chapter 13 bankruptcy proceeding which was converted to a Chapter 11 proceeding in January, 1980. Mrs. Reid suffered emotional problems and drug dependency. The couple separated for a period of a year and a half.

[¶10] The Reids, who are black, claimed that Depositors acted in bad faith to limit and then terminate their credit. They also claimed that Depositors' actions were motivated by racial prejudice. Defendant claimed that Depositors acted in good faith to secure its financial interests when it learned of Reid's personal difficulties and mismanagement of his business; it denied that its actions were racially motivated.

[¶11] At trial, the district court directed a verdict for defendant on plaintiffs' claims for violations of the Fair Credit Reporting Act and for breach of fiduciary duties. Plaintiffs withdrew their claims for interference with contractual relations and wrongful dishonoring of checks. The jury found for defendant on plaintiffs' claims for violation of the express terms of the credit agreement, racial discrimination, two counts for infliction of emotional distress, and failure to comply with Article 9 of the Uniform Commercial Code. The jury found for plaintiffs on their pendent state claim for breach of the March loan agreement based on violation of an implied covenant of good faith and fair dealing. It awarded plaintiffs $100,000 in compensatory and $500,000 in exemplary damages; the exemplary damages award was struck by the court. Both parties have appealed. In Part II, we address defendant's arguments on appeal; in Parts III-VI we address those of plaintiffs.

II. IMPLIED COVENANT OF GOOD FAITH AND FAIR DEALING

A. The Existence of the Cause of Action in Maine

[¶12] Plaintiffs' recovery in contract was based on the theory that when Depositors, in May 1979, and thereafter, shut off Reid's credit and took steps to realize upon its collateral, it violated an implied covenant of good faith contained in the March loan agreement between plaintiffs and Depositors. The district court took as self-evident the proposition that Maine contract law required good faith performance. *See generally* Burton, *Breach of Contract and the Common Law Duty to Perform in Good Faith*, 94 Harv. L. Rev. 369 (1980). The Uniform Commercial Code, as adopted by Maine, states: "Every contract or duty within this Title imposes an obligation of good faith in its performance or enforcement." 4 Me. Rev. Stat. Ann. tit. 11, Sec. 1-203 (1964). That this obligation carries with it a cause of action seems clear from another provision of the Code: "Any right or obligation declared by this Title is enforceable by action unless the provision declaring it specifies a different and limited effect." *Id.* at Sec. 1-106(2). *See also Restatement (Second) of Contracts* Sec. 205 (1979).

[¶13] We interpret the Maine cases making reference to the general duty of good faith in light of this general acceptance of the principle. The Maine Supreme Judicial Court has explicitly recognized the U.C.C.'s "broad requirements of good faith, commercial reasonableness and fair dealing." *Schiavi Mobile Homes, Inc. v. Gironda*, 463 A.2d 722, 724-25 (Me.1983) (citing *U.C.C*. Secs. 1-203, 2-103 & 1-106, Comment 1). In addition, some aspects of the present case concern the handling of Reid's bank accounts with Depositors and would thus be governed by the standard of "good faith" and "ordinary care" under section 4-103 of the U.C.C. *See C-K Enterprises v. Depositors Trust Co*., 438 A.2d 262, 265 (Me.1981).

[¶14] In *Linscott v. State Farm Mutual Auto Ins. Co*., 368 A.2d 1161 (Me.1977), the court discussed whether a duty of good faith existed between an insurer and a third-party tort claimant. The court stated that, while such a duty is "implicit" in the contract between an insurer and its insured, the essentially "adversary" relationship between an insurer and a third-party claimant precludes the finding of such an implicit duty in their dealings. Defendant would have us view the court's finding of a good faith duty between the insurer and the insured as exceptional; under defendant's interpretation, an "adversary" relationship, whether contractual or not, would have no good faith requirement.

[¶15] We cannot agree with this reading of Linscott. The general principles of modern contract law, as embodied in Maine's Uniform Commercial Code and recognized in *Schiavi*, mandate that we interpret Linscott as finding no duty of good faith toward a third-party claimant primarily because of the absence of a contractual relationship. We view the Maine court as implicitly recognizing that contractual relationships of the present nature are governed by a requirement of good faith performance. We do not think that this duty to perform in good faith is altered merely by calling the contractual relationship "adversary."

[¶16] Defendant next argues that a cause of action based on the duty is not generally accepted, even if the principle of good faith performance has been widely acknowledged. Defendant cites several cases finding no such cause of action in their jurisdictions. *See, e.g.*, *Management Assistance, Inc. v. Computer Dimensions, Inc*., 546 F. Supp. 666 (N.D.Ga.1982), aff'd, 747 F.2d 708 (11th Cir.1984). These cases generally cite as their authority *Chandler v. Hunter,* 340 So.2d 818, 821 (Ala.App.1976), for the proposition that no jurisdiction has been found that allows such a cause of action.

[¶17] We reject the applicability of *Chandler* and the cases based on it for two reasons. First, a determination that no such cause of action exists would conflict with the clear meaning of section [1-304] of the U.C.C. * * * . We assume that the Maine courts would adhere to the plain language of th[is provision], as well as to generally accepted modern contract principles. Secondly, the fact that numerous jurisdictions have allowed recovery on theories of breach of good faith refutes the empirical assumption upon which Chandler appears to have been based. *See, e.g.*, *K.M.C. Co. v. Irving Trust Co*., 757 F.2d 752 (6th Cir.1985) (suit under New York law by borrower against lender for arbitrary termination of credit); *Power Motive Corp. v. Mannesmann Demag Corp.,* 617 F. Supp. 1048 (D.Colo.1985) (Ohio law); *Fortune v. National Cash Register Co.,* 373 Mass. 96, 364 N.E.2d 1251 (1977) (Massachusetts law). *See also Atlas Truck Leasing, Inc. v. First NH Banks, Inc.*, 808 F.2d 902 (1st Cir.1987) (interpreting New Hampshire law).[§]

[¶18] Defendant argues that the "demand" provision of the note establishing the credit agreement precludes a good faith requirement in this case, even if such a requirement is recognized in general. Defendant contends that this exception to the general good faith requirement is mandated by section [1-208 [now 1-309] of the U.C.C., as interpreted by the U.C.C. Comment to the section. Section 1-208 states:

> Sec. 1-208. Option to accelerate at will
>
> A term providing that one party or his successor in interest may accelerate payment or performance or require collateral or additional collateral "at will" or "when he deems himself insecure" or in words of similar import shall be construed to mean that he shall have power to do so only if he in good faith believes that the prospect of payment or performance is impaired. . . .

The U.C.C. Comment observes:

> Obviously this section has no application to demand instruments or obligations whose very nature permits call at any time with or without reason.

[¶19] We turn, therefore, to the documents establishing the loan to see whether they clearly gave Depositors the right to demand payment or terminate the relationship on demand and without cause. The "Secured Interest Note," dated March 2, 1979, states in its opening paragraph:

> On Demand, after date, for value received, [Paul Reid d/b/a Pro Paint & Decorating] . . . promise[s] to pay to the order of [Depositors] . . . Twenty-five Thousand and no/100 DOLLARS with interest at 13.75 per cent per annum payable quarterly.

[¶20] This provision appears, at first glance, to be an unambiguous demand clause. It cannot, however, possibly be read literally in the context of the kind of agreement entered into here. Although the note seems to grant Depositors the right to immediate repayment of $25,000 "on demand," Reid had not yet received

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[§] [1] For an extensive list of jurisdictions recognizing the general obligation of good faith, see the appendix to Burton, Breach of Contract and the Common Law Duty to Bargain in Good Faith, 94 Harv. L. Rev. at 404. [Editor: Burton's article is actually entitled ". . . *Duty to Perform in Good Faith*, not *Bargain*.]

that sum of money from the bank. Indeed, he was never to receive the full amount. The “demand” provision thus cannot represent the beginning and end of the inquiry into the time term of the contract.

[¶21] DeSalle, president of Depositors, testified to similar effect at trial, based on his knowledge of banking practices. He said that the “demand” provision in such an agreement is to be interpreted in light of the other conditions in the note and that a bank could not simply terminate the agreement capriciously. He also thought that the absence of a time term in such a note indicated the likelihood that the schedule for repayment of the principal was governed by a verbal agreement between the loan officer and the debtor. In view both of our reading of the document and of DeSalle’s testimony about banking practices, we find that the “demand” provision in the note should not be understood as a completely integrated agreement on the time term of the contract. *See Astor v. Boulos Co.,* 451 A.2d 903, 905 (Me.1982); *Restatement (Second) of Contracts* Sec. 209 (1979).

[¶22] Furthermore, the documents establishing the loan place conditions on the acceleration of payment or termination of the agreement. The “Secured Interest Note” provides for various conditions which would “render” the obligation “payable on demand.” The “Security Agreement,” also signed March 2, 1979, lists a series of events whose occurrence would signify that Reid would be in “default.” The presence of such conditions in both documents indicates that the agreement could not simply be terminated at the whim of the parties; rather, the right of termination or acceleration was subjected to various limitations. The detailed enumeration of events that would “render “ the note “payable on demand,” or which would put Reid in “default,” shows the qualified and relative nature of any “demand” provision. It would be illogical to construe an agreement, providing for repayment or default in the event of certain contingencies, as permitting the creditor, in the absence of the occurrence of those contingencies, to terminate the agreement without any cause whatsoever. Under such a construction, the enumerated conditions would be rendered meaningless. We find, therefore, that the documents establishing the loan defeat neither the legal obligation nor the justifiable expectation of the parties that the contract be performed in good faith.

C. The Standard

[¶23] Defendant challenges the district court’s formulation of the test of “good faith” in its instruction to the jury. Defendant claims that the judge instructed the jury that the test for good faith comprises both an objective and a subjective component. Defendant argues that under Maine law an objective standard, such as a “reasonable man” test, may only be applied in cases involving the sales of goods that fall under Article 2 of the U.C.C. Otherwise, defendant claims, any consideration of “good faith” should be limited to its subjective definition in section 1-201(19) [now 1-201(20)] as “honesty in fact.”

[¶24] We have examined the judge’s original instructions as well as his subsequent clarification of those instructions to determine the precise nature of the test submitted to the jury. In regard to the contract claim, the judge initially formulated two standards. First, he stated that the contract, as a whole, was subject to a “covenant of good faith and fair dealing.” Second, with specific reference to the claim that Depositors inappropriately disposed of Reid’s collateral, he stated that the bank had a duty to act in a “commercially reasonable manner.” In setting the latter standard, he cited Article 9 of the U.C.C. *See* 5 *Me. Rev. Stat. Ann*. tit. 11, Secs. 9-501-504. He then twice defined “good faith” in terms indicating a purely subjective standard. He concluded the instruction, however, by reformulating the “good faith” test as including an objective standard of reasonableness.

[¶25] The jury later requested that the judge clarify these instructions. In his new instructions, the judge clearly formulated a subjective standard for good faith:

> Now good faith is defined as honesty in fact.
>
> One acts with good faith, in general, when one acts honestly.
>
> Good faith means that one acts without any improper motivation. One acts with the truth and not for some ulterior motive that is unconnected with the substance of the agreement in question when one is acting with good faith.

The judge again referred to the "commercially reasonable" standard only in connection with Article 9 violations.

[¶26] We find, therefore, that the judge ultimately instructed the jury to decide the issue of good faith under the subjective standard. "Honesty in fact" is required under all interpretations of the duty of good faith under section 1-203. Thus, even if we agreed with defendant that the Maine courts would limit an objective standard for good faith to Article 2 cases, we would not find a fatal error in the judge's instructions here.[*]

D. Sufficiency of Evidence

[¶27] Finally, defendant contends that there was insufficient evidence to support a finding of an absence of good faith, particularly in view of the jury's failure to find that racial discrimination had been an "effective factor" in the termination of Reid's credit at Depositors. We disagree. We affirm the district court's holding that evidence concerning the manner in which Depositors conducted their dealings with Reid was sufficient to support a jury verdict of bad faith and was not based on mere speculation. The standard for defendant's motion for a judgment notwithstanding the verdict was whether the evidence, viewed in the light most favorable to plaintiffs, would lead to the conclusion that no reasonable jury could have found for plaintiffs on the good faith issue. This heavy burden was not met by defendant.

[¶28] We think the jury could have reasonably inferred that Depositors' actions were not taken in good faith. The March, 1979, credit agreement represented the largest amount of credit extended to Reid by the

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[*] [2] Moreover, we think there are strong indications that such a limitation would not represent the Maine court's future, or even current, thinking on this matter. First, we note that many courts have construed the "good faith" provision of Sec. 1-208 as including an objective component. See, e.g., K.M.C. Co. v. Irving Trust Co., 757 F.2d 752, 760-61 (6th Cir.1985). This construction was supported by the views of Professor Gilmore, one of the drafters of the U.C.C. See 2 G. Gilmore, Security Interests in Personal Property Sec. 43.4 at 1197 (1965). See also J. White and R. Summers, Uniform Commercial Code 1088 (2d ed.1980) ("The draftsmen apparently intended an objective standard."). Moreover, as many commentators have shown, the difference between so-called "objective" and "subjective" standards is often minimal in practice. See, e.g., J. White and R. Summers at 1088-90. Finally, we note the following pronouncement of the Maine court, broadly paraphrasing Sec. 4-103 of the U.C.C.: "[I]n fact the Uniform Commercial Code imposes a duty of ordinary care and good faith on banks in their dealings with customers." C-K Enterprises v. Depositors Trust Co., 438 A.2d 262, 264 (1981). The use of the sweeping phrase, "in their dealings with customers," arguably extends the protection of "ordinary care" in Maine beyond those bank transactions specifically covered in Article 4.

bank, and could be seen as the culmination of an ongoing and mutually beneficial relationship. The jury could have found that by mid-May, when Reid's line of credit was abruptly shut off, he was not in default and his overall position had not changed that significantly, especially as the bank did not first register complaints to him or ask him to alter his conduct in some manner. The bank's president testified that it was customary before cutting off a customer's line of credit to send notices in advance and call the customer to the bank for discussion. This was not done as to Reid, nor was any convincing reason advanced by the bank for not doing so. (The bank, indeed, did not even call as a witness the officer who had dealt directly with Reid and could have best explained why the bank acted as it did.) The jury could have found that in restricting Reid's credit when and as it did the bank was motivated by ulterior considerations, not a good faith concern for its financial security. The jury could have found that the bank decided in bad faith and without notice to terminate the credit relationship as a whole. The jury might have viewed the bank's actions to restrict and terminate Reid's credit to be in bad faith in part because they were taken only a short time after the bank had shown confidence in Reid and had given him grounds to rely on the continuation of the relationship. The jury might have inferred bad faith from these actions of the bank, even if it did not believe that racial prejudice was the effective factor that motivated the bank's bad faith. In sum, the jury could have reasonably found that the bank acted in bad faith in precipitously and without warning halting further advances on which it knew Reid's business depended, in failing to make a sufficient effort to negotiate alternative solutions to any problems it perceived in its relationship with Reid, and in failing to give notice that it intended to terminate the relationship entirely. The evidence concerning these and other aspects of Depositors' actions provided a sufficient basis for a jury finding that the bank's actions were not taken in good faith. * * * *

[¶29] Affirmed. No costs to either party.

Questions:

1. Does the provision of the note stating that payment shall be "on demand" preclude a good faith obligation relevant to this claim?

2. Bonus question: Why doesn't a demand note lack consideration? If the lender can demand the money back immediately, the lender has no obligation.

3. Did the trial court here mis-instruct as to the definition of good faith?

4. Was evidence sufficient to show lack of good faith?

5. What does good faith mean in this case?

6. How does the Burton test work out here?

7. Is this court's understanding of good faith based on the same juridical principles as the Burton test or on some other basis?

LARESE v. CREAMLAND DAIRIES, INC.

10th Cir. U.S. Ct. App. (1985)

767 F.2d 716

McKAY, Circuit Judge.

[¶1] The issue in this case is whether a franchisor has an absolute right to refuse to consent to the sale of a franchisee's interest to another prospective franchisee.

[¶2] Plaintiffs entered into a 10-year franchise agreement with defendant, Creamland Dairies, in 1974. The franchise agreement provided that the franchisee "shall not assign, transfer or sublet this franchise, or any of [the] rights under this agreement, without the prior written consent of Area Franchisor [Creamland] and Baskin Robbins, any such unauthorized assignment, transfer or subletting being null and without effect." The plaintiffs attempted to sell their franchise rights in February and August of 1979, but Creamland refused to consent to the sales. Plaintiffs brought suit, alleging that Creamland had interfered with their contractual relations with the prospective buyers by unreasonably withholding its consent. The district court granted summary judgment for the defendant on the ground that the contract gave the defendant an absolute, unqualified right to refuse to consent to proposed sales of the franchise rights. Plaintiffs appeal, claiming that defendant franchisor has a duty to act in good faith and in a commercially reasonable manner when a franchisee seeks to transfer its rights under the franchise agreement.

[¶3] The Colorado courts have never addressed the question of whether a franchisor has a duty to act reasonably in deciding whether to consent to a proposed transfer. The Colorado courts have, however, imposed a reasonableness requirement on consent to transfer clauses in other types of contracts. In *Basnett v. Vista Village Mobile Home Park*, 699 P.2d 1343 (Colo.App.1984), the Colorado appellate court held that a landlord cannot unreasonably refuse to consent to assignment or subleasing by a tenant. While the court indicated that the courts would enforce a provision expressly granting the landlord an absolute right to consent if such a provision was freely negotiated, it refused to find such an absolute right in a provision which provided simply that the landlord must consent to assignment. At 1346 (citing Restatement (2d) of Property Sec. 15.2(2) (1977)). The question before us, therefore, is whether the Colorado courts would impose a similar requirement of reasonableness on restraint on alienation clauses in franchise agreements.

[¶4] Counsel for both parties have argued that the franchisor-franchisee relationship is a special one which is not directly analogous to that of a landlord and tenant. As the Supreme Court of Pennsylvania has noted, "[u]nlike a tenant pursuing his own interests while occupying a landlord's property, a franchisee . . . builds the good will of both his own business and [the franchisor*]." Atlantic Richfield v. Razumic*, 480 Pa. 366, 390 A.2d 736, 742 (1978). This aspect of the relationship has led a number of courts to hold that the franchise relationship imposes a duty upon franchisors not to act unreasonably or arbitrarily in terminating the franchise. *See, e.g., Atlantic Richfield*, 390 A.2d at 742; *Arnott v. American Oil Co.,* 609 F.2d 873 (8th Cir.1979), *cert. denied*, 446 U.S. 918, 100 S. Ct. 1852, 64 L. Ed. 2d 272 (1980); *Shell Oil Co. v. Marinello*, 63 N.J. 402, 307 A.2d 598 (1973). As did these courts, we find that the franchisor-franchisee relationship is one which requires the parties to deal with one another in good faith and in a commercially reasonable manner. See *Arnott*, 609 F.2d at 881 (finding fiduciary duty inherent in franchise relationship); *Atlantic*

Richfield, 390 A.2d at 742 (basing decision that franchisor cannot arbitrarily terminate relationship on franchisor's "obligation to deal with its franchisees in good faith and in a commercially reasonable manner").

[¶5] Defendants argue that the franchise assignment situation differs from the franchise termination situation in that the franchisor must work with the person to whom the franchise is assigned. To impose a duty of reasonableness, they argue, would violate the rule of *United States v. Colgate & Co.*, 250 U.S. 300, 307, 39 S. Ct. 465, 468, 63 L. Ed. 992 (1919), that a manufacturer engaged in private business has the right "freely to exercise his own independent discretion as to parties with whom he will deal." This right, however, must be balanced against the rights of the franchisees. As is true in the termination cases, the franchisee has invested time and money into the franchise and, in doing so, has created benefits for the franchisor. We do not find it an excessive infringement of the franchisor's rights to require that the franchisor act reasonably when the franchisee has decided that it wants out of the relationship. The franchisee should not be forced to choose between losing its investment or remaining in the relationship unwillingly when it has provided a reasonable alternative franchisee.

[¶6] We do not hold that a provision which expressly grants to the franchisor an absolute right to refuse to consent is unenforceable when such an agreement was freely negotiated. We do not believe the Colorado courts would find such an absolute right, however, in a provision such as the one involved in this case which provides simply that the franchisee must obtain franchisor consent prior to transfer. See *Vista Village*, at 1346. Rather, the franchisor must bargain for a provision expressly granting the right to withhold consent unreasonably, to insure that the franchisee is put on notice. Since, in this case, the contracts stated only that consent must be obtained, Creamland did not have the right to withhold consent unreasonably.

[¶7] Reversed and remanded for further proceedings consistent with this opinion.

Questions:

1. What is the source of the good faith obligation here?

2. Suppose you are the franchisor in this case. Why do you want to control who owns the franchise?

3. What kind of franchisee would pass in any event?

4. Why did the parties provide for approval of an assignment rather than a clause with greater specificity?

D. Express Conditions

PREFERRED MORTGAGE BROKERS, INC. v. Hervin BYFIELD

Supreme Ct., App. Div., 2d Dept. (2001)

723 N.Y.S.2d 230

[¶1] On November 3, 1997, the defendants retained the plaintiff mortgage broker to assist them in securing financing to purchase a house. The parties' contract required the defendants to pay the plaintiff a fee "directly upon [the] signed acceptance of a commitment." Although the plaintiff alleges that it earned its fee by obtaining a mortgage loan commitment on the defendants' behalf, it is undisputed that the defendants never signed any document accepting the commitment, and did not close on the proposed loan. When the defendants refused to pay the plaintiff a fee, the plaintiff commenced this action seeking damages for breach of contract.

[¶2] The defendants contend that the Supreme Court erred in granting the plaintiff's motion for summary judgment because their signed acceptance of a commitment was a condition precedent to their obligation to pay the plaintiff a broker's fee. We agree. A condition precedent is "an act or event * * * which, unless the condition is excused, must occur before a duty to perform a promise in the agreement arises" (*Oppenheimer & Co. v Oppenheim, Appel, Dixon & Co.*, 86 N.Y.2d 685, 690; Calamari and Perillo, *Contracts* § 11-2, at 438 [3d ed]). Express conditions precedent, which are those agreed to and imposed by the parties themselves, "must be literally performed" (*Oppenheimer & Co. v Oppenheim, Appel, Dixon & Co., supra*, at 690). Since the record reveals that the defendants never accepted the loan commitment in writing, the express condition precedent contained in the contract was not satisfied, and the defendants were not obligated to pay a broker's fee (*see, Oppenheimer & Co. v Oppenheim, Appel, Dixon & Co., supra*; *Bradenton Realty Corp. v United Artists Prop. I Corp.,* 264 A.D.2d 405; *Stanton v Power*, 254 A.D.2d 153). Therefore, the Supreme Court erred in granting summary judgment to the plaintiff.

[¶3] Furthermore, although the defendants did not cross-move for summary judgment, this Court is authorized by CPLR 3212 (b) to search the record and grant summary judgment to a nonmoving party (see, *Dunham v Hilco Constr. Co*., 89 N.Y.2d 425*; Bartley v Accu-Glo Elec.Corp*., 272 A.D.2d 352). Accordingly, summary judgment is granted to the defendants dismissing the complaint.

Questions:

1. What language made signed acceptance a condition (instead of just a promise)?

2. What's the difference between the legal effect of the condition in this case and that of the condition in *Luther Williams, Inc.*?

3. Why wasn't the defendants' failure to sign the commitment a failure to cooperate or a breach of the duty of good faith?

4. Please consider the facts of *Dove v. Rose Acre Farms, Inc.*, 434 N.E.2d 931 (Ind. App. 1982):

> [¶1] The evidence most favorable to support the judgment and the facts found specially by the trial court are as follows. Dove had been employed by Rose Acre Farms, operated by David Rust (Rust), its president and principal owner, in the summers and other times from 1972 to 1979. The business of Rose Acre was the production of eggs, and, stocked with 4,000,000 hens and staffed with 300 employees, it produced approximately 256,000 dozen eggs per day. Rust had instituted and maintained extensive bonus programs, some of which were for one day only, or one event or activity only. For example, one bonus was the white car bonus; if an employee would buy a new white car, keep it clean and undamaged, place a Rose Acre sign on it, commit no tardiness or absenteeism, and attend one management meeting per month, Rose Acre would pay $100 per month for 36 months as a bonus above and beyond the employee's regular salary, to apply on payments. Any slight violation, such as being a minute late for work, driving a dirty or damaged car, or missing work for any cause, would work a forfeiture of the bonus. Other bonuses consisted of egg production bonuses, deed conversion bonuses, house management bonuses, and a silver feather bonus. This last bonus program required the participant to wear a silver feather, and a system of rewards and penalties existed for employees who participated. While the conditions of the bonuses varied, one condition existed in all bonus programs: during the period of the bonus, the employee must not be tardy for even a minute, and must not miss work any day for any cause whatever, even illness. If the employee missed any days during the week, he was sometimes permitted to make them up on Saturday and/or Sunday. Any missed work not made up within the same week worked a forfeiture of the bonus. These rules were explained to the employees and were stated in a written policy. The bonus programs were voluntary, and all the employees did not choose to participate in them. When a bonus was offered a card was issued to the participant stating his name and the terms and amount of the bonus. Upon completion of the required tasks, the card was attached to the pay sheet, and the bonus was added to the paycheck. Rust was strict about tardiness and absenteeism, whether an employee was on a bonus program or not. If an employee was tardy, his pay would be docked to the minimum wage, or he would be sent home and lose an entire day. A minute's tardiness would also deprive the employee of a day for purposes of seniority. As was stated in the evidence, bonuses were given for the "extra mile" or actions "above and beyond the call of duty." The purpose of the bonus programs and penalties was to discourage absenteeism and tardiness, and to promote motivation and dependability.

[¶2] In June 1979, Rust called in Dove and other construction crew leaders and offered a bonus of $6,000 each if certain detailed construction work was completed in 12 weeks. As Dove conceded in his own testimony, the bonus card indicated that in addition to completing the work, he would be required to work at least five full days a week for 12 weeks to qualify for the bonus. On the same day Dove's bonus agreement, by mutual consent, was amended to ten weeks with a bonus of $5,000 to enable him to return to law school by September 1. Dove testified that there was no ambiguity in the agreement, and he understood that to qualify for the bonus he would have to work ten weeks, five days a week, commencing at starting time and quitting only at quitting time. Dove testified that he was aware of the provisions concerning absenteeism and tardiness as they affected bonuses, and that if he missed any work, for any reason, including illness, he would forfeit the bonus. The evidence disclosed that no exception had ever been made except as may have occurred by clerical error or inadvertence.

[¶3] In the tenth week Dove came down with strep throat. On Thursday of that week he reported to work with a temperature of 104°, and told Rust that he was unable to work. Rust told him, in effect, that if he went home, he would forfeit the bonus. Rust offered him the opportunity to stay there and lay on a couch, or make up his lost days on Saturday and/or Sunday. Rust told him he could sleep and still qualify for the bonus. Dove left to seek medical treatment and missed two days in the tenth week of the bonus program.

[¶4] Rust refused Dove the bonus based solely upon his missing the two days of work. While there was some question of whether the construction job was finished, Rust does not seem to have made that issue the basis of his refusal. Bonuses to other crew leaders were paid. The trial court denied Dove's recovery and, in the conclusions of law, stated that Dove had not shown that all of the conditions of the bonus contract had been met. Specifically, Dove failed to work five full days a week for ten weeks.

Dove appealed.

Questions on *Dove*:

a. Can you think of any arguments (legal, moral, philosophical, or economic) in his favor?

b. Remember that the non-occurrence of conditions can be waived by the party in whose favor the condition is made. (Often lawyers informally say that the "condition," not its non-occurrence, can be waived.) So, the failure of a "subject to financing" condition in a real property sale can be waived by the buyer. Who would waive the condition in Rose? Waiving the non-occurrence of a condition is legally equivalent in result to the condition occurring.

OPPENHEIMER & CO., INC. v. OPPENHEIM, APPEL, DIXON & CO.

N.Y. (1995)

636 N.Y.S.2d 734

CIPARICK, J.

[¶1] The parties entered into a Letter Agreement setting forth certain conditions precedent to the formation and existence of a sublease between them. The agreement provided that there would be no sublease between the parties "unless and until" plaintiff delivered to defendant the prime landlord's written consent to certain "tenant work" on or before a specified deadline. If this condition did not occur, the sublease was to be deemed "null and void." Plaintiff provided only oral notice on the specified date. The issue presented is whether the doctrine of substantial performance applies to the facts of this case. We conclude it does not for the reasons that follow.

I.

[¶2] In 1986, plaintiff Oppenheimer & Co. moved to the World Financial Center in Manhattan, a building constructed by Olympia & York Company (O & Y). At the time of its move, plaintiff had three years remaining on its existing lease for the 33rd floor of the building known as One New York Plaza. As an incentive to induce plaintiff's move, O & Y agreed to make the rental payments due under plaintiff's rental agreement in the event plaintiff was unable to sublease its prior space in One New York Plaza.

[¶3] In December 1986, the parties to this action entered into a conditional Letter Agreement to sublease the 33rd floor. Defendant already leased space on the 29th floor of One New York Plaza and was seeking to expand its operations. The proposed sublease between the parties was attached to the Letter Agreement. The Letter Agreement provided that the proposed sublease would be executed only upon the satisfaction of certain conditions. Pursuant to paragraph 1(a) of the agreement, plaintiff was required to obtain "the Prime Landlord's written notice of confirmation, substantially to the effect that [defendant] is a subtenant of the Premises reasonably acceptable to Prime Landlord." If such written notice of confirmation were not obtained "on or before December 30, 1986, then this letter agreement and the Sublease * * * shall be deemed null and void and of no further force and effect and neither party shall have any rights against nor obligations to the other."

[¶4] Assuming satisfaction of the condition set forth in paragraph 1(a), defendant was required to submit to plaintiff, on or before January 2, 1987, its plans for "tenant work" involving construction of a telephone communication linkage system between the 29th and 33rd floors. Paragraph 4(c) of the Letter Agreement then obligated plaintiff to obtain the prime landlord's "written consent" to the proposed "tenant work" and deliver such consent to defendant on or before January 30, 1987. Furthermore, if defendant had not received the prime landlord's written consent by the agreed date, both the agreement and the sublease were to be deemed "null and void and of no further force and effect," and neither party was to have "any rights against nor obligations to the other." Paragraph 4(d) additionally provided that, notwithstanding satisfaction of the condition set forth in paragraph 1(a), the parties "agree not to execute and exchange the Sublease unless and until * * * the conditions set forth in paragraph (c) above are timely satisfied."

[¶5] The parties extended the Letter Agreement's deadlines in writing and plaintiff timely satisfied the first condition set forth in paragraph 1(a) pursuant to the modified deadline. However, plaintiff never

delivered the prime landlord's written consent to the proposed tenant work on or before the modified final deadline of February 25, 1987. Rather, plaintiff's attorney telephoned defendant's attorney on February 25 and informed defendant that the prime landlord's consent had been secured. On February 26, defendant, through its attorney, informed plaintiff's attorney that the Letter Agreement and sublease were invalid for failure to timely deliver the prime landlord's written consent and that it would not agree to an extension of the deadline. The document embodying the prime landlord's written consent was eventually received by plaintiff on March 20, 1987, 23 days after expiration of paragraph 4(c)'s modified final deadline.

[¶6] Plaintiff commenced this action for breach of contract, asserting that defendant waived and/or was estopped by virtue of its conduct* from insisting on physical delivery of the prime landlord's written consent by the February 25 deadline. Plaintiff further alleged in its complaint that it had substantially performed the conditions set forth in the Letter Agreement.

[¶7] At the outset of trial, the court issued an order in limine barring any reference to substantial performance of the terms of the Letter Agreement. Nonetheless, during the course of trial, the court permitted the jury to consider the theory of substantial performance, and additionally charged the jury concerning substantial performance. Special interrogatories were submitted. The jury found that defendant had properly complied with the terms of the Letter Agreement, and answered in the negative the questions whether defendant failed to perform its obligations under the Letter Agreement concerning submission of plans for tenant work, whether defendant by its conduct waived the February 25 deadline for delivery by plaintiff of the landlord's written consent to tenant work, and whether defendant by its conduct was equitably estopped from requiring plaintiff's strict adherence to the February 25 deadline. Nonetheless, the jury answered in the affirmative the question, "Did plaintiff substantially perform the conditions set forth in the Letter Agreement?," and awarded plaintiff damages of $1.2 million.

[¶8] Defendant moved for judgment notwithstanding the verdict. Supreme Court granted the motion, ruling as a matter of law that "the doctrine of substantial performance has no application to this dispute, where the Letter Agreement is free of all ambiguity in setting the deadline that plaintiff concededly did not honor." The Appellate Division reversed the judgment on the law and facts, and reinstated the jury verdict. The court concluded that the question of substantial compliance was properly submitted to the jury and that the verdict should be reinstated because plaintiff's failure to deliver the prime landlord's written consent was inconsequential.

[¶9] This Court granted defendant's motion for leave to appeal and we now reverse.

II.

[¶10] Defendant argues that no sublease or contractual relationship ever arose here because plaintiff failed to satisfy the condition set forth in paragraph 4(c) of the Letter Agreement. Defendant contends that the doctrine of substantial performance is not applicable to excuse plaintiff's failure to deliver the prime landlord's written consent to defendant on or before the date specified in the Letter Agreement and that the

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* [1] Plaintiff argued that it could have met the deadline, but failed to do so only because defendant, acting in bad faith, induced plaintiff into delaying delivery of the landlord's consent. Plaintiff asserted that the parties had previously extended the agreement's deadlines as a matter of course.

Appellate Division erred in holding to the contrary. Before addressing defendant's arguments and the decision of the court below, an understanding of certain relevant principles is helpful.

[¶11] A condition precedent is "an act or event, other than a lapse of time, which, unless the condition is excused, must occur before a duty to perform a promise in the agreement arises" (Calamari and Perillo*, Contracts* § 11-2, at 438; see *Restatement [Second] of Contracts* § 224; see also *Merrit Hill Vineyards v Windy Hgts. Vineyard*, 61 NY2d 106, 112-113). Most conditions precedent describe acts or events which must occur before a party is obliged to perform a promise made pursuant to an existing contract, a situation to be distinguished conceptually from a condition precedent to the formation or existence of the contract itself (see *M.K. Metals v Container Recovery Corp.,* 645 F2d 583). In the latter situation, no contract arises "unless and until the condition occurs" (Calamari and Perillo*, Contracts* § 11-5, at 440).

[¶12] Conditions can be express or implied. Express conditions are those agreed to and imposed by the parties themselves. Implied or constructive conditions are those "imposed by law to do justice" (Calamari and Perillo*, Contracts* § 11-8, at 444). Express conditions must be literally performed, whereas constructive conditions, which ordinarily arise from language of promise, are subject to the precept that substantial compliance is sufficient. The importance of the distinction has been explained by Professor Williston:

> Since an express condition * * * depends for its validity on the manifested intention of the parties, it has the same sanctity as the promise itself. Though the court may regret the harshness of such a condition, as it may regret the harshness of a promise, it must, nevertheless, generally enforce the will of the parties unless to do so will violate public policy. Where, however, the law itself has imposed the condition, in absence of or irrespective of the manifested intention of the parties, it can deal with its creation as it pleases, shaping the boundaries of the constructive condition in such a way as to do justice and avoid hardship.

(5 Williston on Contracts § 669, at 154 [3d ed].)

In determining whether a particular agreement makes an event a condition, courts will interpret doubtful language as embodying a promise or constructive condition rather than an express condition. This interpretive preference is especially strong when a finding of express condition would increase the risk of forfeiture by the obligee (see *Restatement [Second] of Contracts* § 227[1]).

[¶13] Interpretation as a means of reducing the risk of forfeiture cannot be employed if "the occurrence of the event as a condition is expressed in unmistakable language" (*Restatement [Second] of Contracts* § 229 comm b, at 185; see § 227, comm b [where language is clear, "[t]he policy favoring freedom of contract requires that, within broad limits, the agreement of the parties should be honored even though forfeiture results"]). Nonetheless, the nonoccurrence of the condition may yet be excused by waiver, breach or forfeiture. The Restatement posits that "[t]o the extent that the non-occurrence of a condition would cause disproportionate forfeiture, a court may excuse the non-occurrence of that condition unless its occurrence was a material part of the agreed exchange" (*Restatement [Second] of Contracts* § 229).

[¶14] Turning to the case at bar, it is undisputed that the critical language of paragraph 4(c) of the Letter Agreement unambiguously establishes an express condition precedent rather than a promise, as the parties employed the unmistakable language of condition ("if," "unless and until"). There is no doubt of the parties' intent and no occasion for interpreting the terms of the Letter Agreement other than as written.

[¶15] Furthermore, plaintiff has never argued, and does not now contend, that the nonoccurrence of the condition set forth in paragraph 4(c) should be excused on the ground of forfeiture.† Rather, plaintiff's primary argument from the inception of this litigation has been that defendant waived or was equitably estopped from invoking paragraph 4(c). Plaintiff argued secondarily that it substantially complied with the express condition of delivery of written notice on or before February 25th in that it gave defendant oral notice of consent on the 25th.

[¶16] Contrary to the decision of the court below, we perceive no justifiable basis for applying the doctrine of substantial performance to the facts of this case.

[¶17] The flexible concept of substantial compliance "stands in sharp contrast to the requirement of strict compliance that protects a party that has taken the precaution of making its duty expressly conditional" (*Farnsworth on Contracts* § 8.12, at 415). If the parties "have made an event a condition of their agreement, there is no mitigating standard of materiality or substantiality applicable to the non-occurrence of that event" (*Restatement [Second] of Contracts* § 237 comm d, at 220). Substantial performance in this context is not sufficient, "and if relief is to be had under the contract, it must be through excuse of the non-occurrence of the condition to avoid forfeiture" (id.; *see Brown- Marx Associates, Ltd. v Emigrant Savings Bank*, 703 F2d 1361, 1367- 1368 [11th Cir]; see also Childres, *Conditions in the Law of Contracts*, 45 NYU L Rev 33, 35]).

[¶18] Here, it is undisputed that plaintiff has not suffered a forfeiture or conferred a benefit upon defendant. Plaintiff alludes to a $1 million licensing fee it allegedly paid to the prime landlord for the purpose of securing the latter's consent to the subleasing of the premises. At no point, however, does plaintiff claim that this sum was forfeited or that it was expended for the purpose of accomplishing the sublease with defendant. It is further undisputed that O & Y, as an inducement to effect plaintiff's move to the World Financial Center, promised to indemnify plaintiff for damages resulting from failure to sublease the 33rd floor of One New York Plaza. Consequently, because the critical concern of forfeiture or unjust enrichment is simply not present in this case, we are not presented with an occasion to consider whether the doctrine of substantial performance is applicable, that is, whether the courts should intervene to excuse the nonoccurrence of a condition precedent to the formation of a contract.

[¶19] The essence of the Appellate Division's holding is that the substantial performance doctrine is universally applicable to all categories of breach of contract, including the nonoccurrence of an express condition precedent. However, as discussed, substantial performance is ordinarily not applicable to excuse the nonoccurrence of an express condition precedent.

[¶20] Our precedents are consistent with this general principle. In *Maxton Bldrs. v Lo Galbo* (68 NY2d 373) the defendants contracted on August 3 to buy a house, but included in the contract the condition that if real estate taxes were found to be above $3,500 they would have the right to cancel the contract upon written notice to the seller within three days. On August 4 the defendants learned that real estate taxes would indeed exceed $3,500. The buyers' attorney called the seller's attorney and notified him that the defendants were exercising their option to cancel. A certified letter was sent notifying the seller's attorney of that decision on August 5 but was not received by the seller's attorney on August 9. We held the

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† [2] The Restatement defines the term "forfeiture" as "the denial of compensation that results when the obligee loses [its] right to the agreed exchange after [it] has relied substantially, as by preparation or performance on the expectation of that exchange" (section 229 comm b).

cancellation ineffective and rejected defendants' argument that reasonable notice was all that was required, stating: "It is settled * * * that when a contract requires that written notice be given within a specified time, the notice is ineffective unless the writing is actually received within the time prescribed" (id. at 378). We so held despite the fact that timely oral notice was given and the contract did not provide that time was of the essence. * * * *

[¶21] Plaintiff's reliance on the well-known case of *Jacob & Youngs v Kent (supra)* is misplaced. There, a contractor built a summer residence and the buyer refused to pay the remaining balance of the contract price on the ground that the contractor used a different type of pipe than was specified in the contract. The buyer sought to enforce the contract as written. This would have involved the demolition of large parts of the structure at great expense and loss to the seller. This Court, in an opinion by then-Judge Cardozo, ruled for the contractor on the ground that "an omission, both trivial and innocent, will sometimes be atoned for by allowance of the resulting damage and will not always be the breach of a condition to be followed by a forfeiture" (230 NY, at 241). But Judge Cardozo was careful to note that the situation would be different in the case of an express condition:

> This is not to say that the parties are not free by apt and certain words to effectuate a purpose that performance of every term shall be a condition of recovery. That question is not here. This is merely to say that the law will be slow to impute the purpose, in the silence of the parties, where the significance of the default is grievously out of proportion to the oppression of the forfeiture (*id*. at 243-244).

The quoted language contradicts the Appellate Division's proposition that the substantial performance doctrine applies universally, including when the language of the agreement leaves no doubt that an express condition precedent was intended (*see* 205 AD2d, at 414). More importantly, *Jacob & Youngs* lacks determinative significance here on the additional ground that plaintiff conferred no benefit upon defendant. The avoidance-of-forfeiture rationale which engendered the rule of Jacob & Youngs is simply not present here, and the case therefore "should not be extended by analogy where the reason for the rule fails" (*Van Iderstine Co. v Banet Lumber Co.,* 242 NY 425, 434). * * * *

III

[¶22] In sum, the Letter Agreement provides in the clearest language that the parties did not intend to form a contract "unless and until" defendant received written notice of the prime landlord's consent on or before February 25, 1987. Defendant would lease the 33rd floor from plaintiff only on the condition that the landlord consent in writing to a telephone communication linkage system between the 29th and 33rd floors and to defendant's plans for construction effectuating that linkage. This matter was sufficiently important to defendant that it would not enter into the sublease "unless and until" the condition was satisfied. Inasmuch as we are not dealing here with a situation where plaintiff stands to suffer some forfeiture or undue hardship, we perceive no justification for engaging in a "materiality-of-the- nonoccurrence" analysis. To do so would simply frustrate the clearly expressed intention of the parties. Freedom of contract prevails in an arm's length transaction between sophisticated parties such as these, and in the absence of countervailing public policy concerns there is no reason to relieve them of the consequences of their bargain. If they are dissatisfied with the consequences of their agreement, "the time to say so [was] at the bargaining table" (Maxton, supra, at 382).

[¶23] Finally, the issue of substantial performance was not for the jury to resolve in this case. A determination whether there has been substantial performance is to be answered, "if the inferences are certain, by the judges of the law" (*Jacob & Youngs v Kent*, 230 NY 239, 243).

[¶24] Accordingly, the order of the Appellate Division should be reversed, with costs, and the complaint dismissed.

E. Implied in Law or Constructive Conditions (Including Order of Performance: Who Performs First If the Parties Did Not Say)

The doctrine of constructive conditions may be the most counter-intuitive doctrine you will study in this class. Most law students never understand the doctrine because they do not see the need for it. They fail to see even the issue that the doctrine addresses.

There was no doctrine of constructive conditions in 1615, when *Nicholas v. Raynbred* was decided, so that case gives you some idea of what occurs when the doctrine is absent. Remember that case? We have thought about *Nicholas* as a mutual promise case (still good law) and as a requirement that mutual promises must occur at the same time (superseded by *Adams v. Lindsell*). Now, please read *Nicholas* to discern whether either party's duty depended on the other's performance, and which party was supposed to perform first (A? B?). The court in *Kingston* is going to abandon *Nicholas*'s wisdom on that issue.

Nicholas v. Raynbred

King's Bench and Exchequer Chamber (1615)

Jenk. 296, 145 ER 215, Hob. 88, 80 ER 238

[¶1] A sells a cow to B for 5£. and assumes to deliver her to him at a certain day; at the same time B assumes to A to pay him 5£. for the said cow, at the said day. A brings an assumpsit for the 5*l*. not paid, and does not aver delivery of the cow: it need not be averred; but the writ ought to aver the mutual assumpsit; for they are reciprocal assumpsits: and such mutual assumpsits are a good consideration, and each of them has a remedy against the other; one for the cow, and other for the 5£.

[¶2] Judged in both courts [the King's Bench and the Exchequer]. * * * *

Questions:

1. Does A have to deliver the cow before he sues for the money? Is delivery of the cow a condition precedent to B's duty to pay the money? Is delivery of the money a condition precedent to A's duty to deliver the cow? Is either duty conditional on the other party's performance?

2. How will B get the cow?

3. Let's suppose a court followed *Nicholas* in a sale of property. Suppose A was to deliver not a cow but a deed. Under *Nicholas*, need A deliver the deed before suing for the money?

4. In a case from the 1670s called *Peters v. Opie*, a worker was supposed to build a house in exchange for money. The worker sued the owner but did not allege that he had built the house (or allege that he had done anything at all). The owner argued that the worker had to allege that he had done the work before he could collect the money. What result, under *Nicholas*? In the course of the argument, one judge, Chief Justice Hale, showed his disagreement with the *Nicholas* rule. He said he never let workers win unless they alleged that they had performed; otherwise the owner might be forced to pay, and then sue, a beggar! 2 Keble 837, 84 ER 529, 530 (1671). Imagine, forcing landowners to pay for work before it was done!

5. If the parties choose mutual promises as the form of their exchange, aren't they simply extending credit to each other? They don't have to do that. B could have exchanged her promise of 5*l*. for actual delivery of the cow. That would be a unilateral contract—a promise in exchange for a performance. And A could agree to deliver the deed only after B paid the money. And the landowner could bargain for the completed work in exchange for his promise to pay money. If the parties could easily have protected themselves in this manner (and most did in the days of *Nicholas*), then why should the law step in paternalistically and protect them from their own folly?

Nicholas is no longer good law on this issue. *Kingston v. Preston* is.

Kingston v. Preston

King's Bench (1773)

2 Doug. 690, 99 E.R. 437 (report taken from arguments of counsel in *Jones v. Barkley* (1781))

[¶1] [Kingston (the plaintiff) alleged as follows: Richard Preston was a mercer, meaning a dealer in fabric, especially silk. Kingston wanted to buy Preston's business. On March 24, 1770, John Kingston promised to serve Preston as an employee for fifteen months at a salary of £200 per year. Preston promised in exchange that, at the end of fifteen months, Preston would convey his mercer business, including all his inventory, at a "fair valuation" to Kingston and Preston's nephew, or some other person nominated by Preston, who would become partners in the mercer business for a 14-year period. Kingston, for his part, also promised to accept the mercer business and enter into the partnership. But the partners were to pay for the mercer business over a period of time, presumably out of profits. To induce Preston to allow the partners to pay out of profits, Kingston also promised to "cause and procure good and sufficient security to be given" to Preston, approved by Preston, for the payment of £250 per month to Preston until the debt for the mercer business could be reduced to the value of £4,000.]

[¶2] Then the plaintiff averred, that he had performed, and been ready to perform, his covenants, and assigned for breach on the part of the defendant, that he had refused to surrender and give up his business, at the end of the said year and a quarter. —The defendant pleaded, 1. That the plaintiff did not offer sufficient security; and, 2. That he did not give sufficient security for the payment of the £250, &c. — And the plaintiff demurred generally to both pleas. [If you read this language correctly and thoughtfully, you realize now that the arguments in court are going to be about who is supposed to perform first. Arguments about who is supposed to perform first only make sense if failure of one party to perform means the other party does not have to perform: Preston's defense is essentially that he doesn't have to perform because Kington did not perform. This is the opposite of what the court held in *Nicholas*.]

[¶3] On the part of the plaintiff, the case was argued by Mr. Buller, who contended, that the covenants were mutual and independent [Buller is arguing *Nicholas*], and, therefore, a plea of the breach of one of the covenants to be performed by the plaintiff was no bar to an action for a breach by the defendant of one of which he had bound himself to perform, but that the defendant might have his remedy for the breach by the plaintiff, in a separate action. On the other side, Mr. Grose insisted, that the covenants were dependent in their nature, and, therefore, performance must be alleged: the security to be given for the money, was manifestly the chief object of the transaction, and it would be highly unreasonable to construe the agreement, so as to oblige the defendant to give up a beneficial business, and valuable stock in trade, and trust, to the plaintiff's personal security, (who might, and, indeed, was admitted to be worth nothing,) for the performance of his part. [This is like an argument from the Hale's statement in *Peters v. Opie*.]

[¶4] In delivering the judgment of the Court, Lord Mansfield expressed himself to the following effect: There are three kinds of covenants: 1. Such as are called mutual and independant, where either party may recover damages from the other, for the injury he may have received by a breach of the covenants in his favour, and where it is no excuse for the defendant, to allege a breach of the covenants on the part of the plaintiff. 2. There are covenants which are conditions and dependent, in which the performance of one depends on the prior performance of another, and, therefore, till this prior condition is performed, the other party is not liable to an action on his covenant. 3. There is also a third sort of covenants, which are mutual conditions to be performed at the same time; and, in these, if one party was ready, and offered, to perform

his part, and the other neglected, or refused, to perform his, he who was ready, and offered, has fulfilled his engagement, and may maintain an action for the default of the other; though it is not certain that either is obliged to do the first act. — His Lordship then proceeded to say, that the dependence, or independence, of covenants, was to be collected from the evident sense and meaning of the parties, and, that, however transposed they might be in the deed, their precedency must depend on the order of time in which the intent of the transaction requires their performance. That, in the case before the Court, it would be the greatest injustice if the plaintiff should prevail: the essence of the agreement was, that the defendant should not trust to the personal security of the plaintiff, but, before he delivered up his stock and business, should have good security for the payment of the money. The giving such security, therefore, must necessarily be a condition precedent. - Judgment was accordingly given for the defendant, because the part to be performed by the plaintiff was clearly a condition precedent.

Questions:

1. Must Kingston prove that he has given sufficient security before he may sue Preston for breach?

2. Mansfield's opinion actually changes one rule and adds another. Both are necessary for the court to rule for Preston. The first rule is the general default that mutual promises create independent covenants. Which precedent does Mansfield side with, *Nicholas* or *Peters*? Knowing this tells you what Mansfield changed the default rule to. And if that is not clear, please read *Goodison*, where Kenyon states it much more plainly.

3. How does Mansfield say the courts should determine dependence and order of performance, in the structure that he creates? What standard should courts use to determine those things?

4. How much of Mansfield's application of the new rule actually discerns the intent of the parties?

5. If it's fair that Kingston had to trust Preston for 15 months, while Kingston worked in contemplation that Preston would convey his stock in trade and let Kingston take over the mercer business, without security, isn't it fair to make Preston trust Kingston for a little while, or let Preston sue for failure to obtain security?

6. If Preston didn't want Kingston's promise as consideration, why did he agree to it? If he didn't bargain for Kingston's performance as consideration, why does the court require it? Doesn't that give Preston more than he bargained for?

7. Kingston actually brought a cause of action for debt, not assumpsit, but everyone saw the writing on the wall, and this opinion has been universally adopted. It is still not a bad summary, which is why this area of the law is so counter-intuitive to some students.

Goodison v. Nunn

King's Bench (1792)

4 T.R. 761, 100 E.R. 1288

Lord Kenyon, Ch. J. - This case is extremely clear, whether considered on principles of strict law or of common justice. The plaintiff engaged to sell an estate to the defendant, in consideration of which the defendant undertook to pay 210£; and, if he did not carry the contract into execution, he was to pay 21£; and [plaintiff's] now not having conveyed his estate, or offered to do so, or taken any one step towards it, the plaintiff has brought this action for the penalty. Suppose the purchase-money of an estate was 40,000£. [I]t would be absurd to say that the purchaser might enforce a conveyance without payment, and compel the seller to have recourse to him, who perhaps might be an insolvent person. The old cases, cited by the plaintiff's counsel, have been accurately stated; but the determinations in them outrage common sense, I admit the principle on which they profess to go: but I think that the Judges misapplied that principle. It is admitted in them all that where they are dependent Covenants, no action will lie by one party unless he have performed, or offered to perform his covenant. Then the question is, whether these are, or are not, dependent covenants? I think they are; the one is to depend on the other; when the one party conveyed his estate he was to receive the purchase-money; and when the other parted with his money he was to have the estate. They were reciprocal acts, to be performed by each other at the same time. It seems, from the case in Strange, that the Judges were surprised at the old decisions; and in order to get rid of the difficulty, they said that a tender and refusal would amount to a performance * * * . It is our duty, when we see that principles of law have been misapplied, in any case, to overrule it. The principle is admitted in all the cases alluded to, that, if they be dependent covenants, performance, or the offer to perform, must be pleaded on the one part, in order to found the action against the other. The mistake has been in the misapplication of that principle in the cases cited; and I am glad to find that the old cases have been overruled; and that we are now warranted by precedent as well as by principle to say that this action cannot be maintained.

Questions:

1. Must Goodison allege performance or at least try to perform (tender)?

2. How does Kenyon know that the covenants are dependent? What is the test for that?

3. Kenyon's opinion suggests that this problem arose only because the courts held that a promise was consideration for another promise. It is true that courts say that a promise is consideration. They still say that. Kenyon's opinion does not purport to overrule the rule that a mutual promise is consideration. Is it consistent to say that a promise is consideration but that the promisor must actually perform or at least tender performance before the defendant is obligated? What exactly is bargained for when a mutual promise is consideration? If Nunn didn't want Goodison's promise but instead wanted actual payment, why did Nunn promise in exchange for Goodison's promise? Consistent or not, tender or performance is now

required. The next case, *Pittman*, is a modern example of the *Goodison* type of transaction in which neither party tendered or performed.

Jeffrey A. PITTMAN v. Lily V. CANHAM

Cal. Ct. App. (1992)

3 Cal. Rptr. 2d 340

OPINION

GILBERT, J.

[¶1] When is a contract no longer a contract? When it contains concurrent conditions and neither party tenders timely performance. Unlike love or taxes, concurrent conditions do not last forever.

[¶2] We hold that where a contract creates concurrent conditions and neither party tenders timely performance, both parties are discharged. We affirm the judgment.

Facts

[¶3] Jeffrey A. Pittman was a licensed real estate broker. In 1987 he contacted Lily V. Canham, then 85 years old, to purchase a parcel of property she owned in San Luis Obispo County. After many telephone calls to Canham between May and November 1987, she agreed to sell a 56-acre parcel to Pittman for $250,000.

[¶4] Pittman drafted the contract dated November 24, 1987, and deposited $1,000 in escrow. The contract called for a further deposit of $24,000 in cash, with the balance of the purchase price to be paid by a note secured by a deed of trust on the property. Closing of escrow was to be within 30 days. The contract provided that "[t]ime is of the essence. All modification or extensions shall be in writing signed by the parties."

[¶5] The parties executed escrow instructions that provided: "Time is of the essence of these instructions. If this escrow is not in condition to close by the Time Limit Date of December 24, 1987 and written demand for cancellation is received by you from any principal to this escrow after said date, you shall act in accordance with [other provisions of the instructions]. . . . [¶] If no demand for cancellation is made, you will proceed to close this escrow when the principals have complied with the escrow instructions." Paragraph 2 of section 4 of the instructions provided, however, that the instructions were not intended to amend, modify or supersede the contract.

[¶6] About the second week of December Canham gave a signed copy of the escrow instructions to Pittman for delivery to escrow. With the instructions, Canham included a signed deed to the property. The escrow company pointed out, however, that the deed had not been notarized. When Pittman contacted Canham, she told him she would have it notarized at an escrow company near her home.

[¶7] The December 24 closing date came and went. Canham had not tendered a notarized deed nor had Pittman tendered $24,000, a promissory note or deed of trust.

[¶8] By March 1988, Canham had been contacted by another broker who wanted to list the property. On March 21 she told Pittman she wanted $10,000 per acre. Pittman embarked on an effort to find out what a fair price for the property was.

[¶9] In May 1988, Canham told Pittman that she had entered into a contract with other purchasers to buy the property for $600,000. Pittman wrote a letter demanding that she perform on his contract, but she sold the property to the other buyers.

[¶10] Pittman sued Canham for breach of contract. At trial he attributed the difference in the $250,000 he offered Canham and the $600,000 sales price six months later to an escalating real estate market.

[¶11] At the end of Pittman's case, Canham moved for a judgment of nonsuit. (Code Civ. Proc., § 581c.) A ruling on the motion was reserved, however, until all the evidence was presented. After the presentation of the evidence, the court granted the motion on the ground that time was of the essence of the contract and neither party tendered performance. The court also gave a statement of decision in which it found that Pittman and not Canham was responsible for the delay in performance, that Canham had not waived time for performance, and that Pittman defaulted when he failed to tender the purchase money, note and deed of trust by December 24, 1987.

Discussion

[¶12] Pittman contends the trial court erred in finding he was in default for failing to tender the purchase money note and deed of trust. He concedes that the result reached by the trial court would be proper if his performance had been a condition precedent, but he points out that here the contract provision requiring Canham to deliver a recordable deed into escrow and the provision requiring him to deposit money, a note and a deed of trust are concurrent conditions. Pittman claims that unlike the failure to perform a condition precedent, the failure of both parties to perform concurrent conditions does not automatically terminate the contract, but that one party must tender performance before the other party is in default. (Citing *Chan v. Title Ins. & Trust Co.* (1952) 39 Cal. 2d 253 [246 P.2d 632*]; Rubin v. Fuchs* (1969) 1 Cal. 3d 50 [81 Cal. Rptr. 373, 459 P.2d 925]; 1 Miller & Starr, *Cal. Real Estate* (2d ed. 1989) § 1:135, p. 488.)

[¶13] Concurrent conditions are conditions precedent which are mutually dependent, and the only important difference between a concurrent condition and a condition precedent is that the condition precedent must be performed before another duty arises, whereas a tender of performance is sufficient in the case of a concurrent condition. (1 Witkin, *Summary of Cal. Law* (9th ed. 1987) Contracts, § 737, pp. 667-668.)

[¶14] Contrary to Pittman's assertion, the failure of both parties to perform concurrent conditions does not leave the contract open for an indefinite period so that either party can tender performance at his leisure. The failure of both parties to perform concurrent conditions during the time for performance results in a discharge of both parties' duty to perform. Thus, where the parties have made time the essence of the contract, at the expiration of time without tender by either party, both parties are discharged. (3A *Corbin on Contracts* (1960) § 663, p. 181.) Here, because time was made the essence of the contract, the failure of both parties to tender performance by December 24, 1987, discharged both from performing. Neither party

can hold the other in default and no cause of action to enforce the contract arises. (*See Pitt v. Mallalieu* (1948) 85 Cal. App. 2d 77, 81 [192 P.2d 24].)

[¶15] Pittman relies on the portion of the escrow instructions that states: "Time is of the essence of these instructions. . . . If this escrow is not in condition to close by the Time Limit Date of December 24, 1987 and . . . [i]f no demand for cancellation is made, you will proceed to close this escrow when the principals have complied with the escrow instructions." He claims this provision shows that time was not truly of the essence in this transaction.

[¶16] But it is difficult to see how a paragraph that begins with the words "[t]ime is of the essence" could reasonably be construed as meaning time is not truly of the essence. The provision relied on by Pittman merely instructs the escrow holder not to cancel escrow on its own initiative, but to close escrow should the parties voluntarily and notwithstanding discharge mutually decide to perform. As we read the paragraph, it does not purport to give a party the unilateral right to demand performance after the time for performance has passed. Such a construction would render meaningless the parties' agreement that time is of the essence.

[¶17] We appreciate the reluctance of a buyer to act first by placing money into escrow. But in a contract with concurrent conditions, the buyer and seller cannot keep saying to one another, "No, you first." Ultimately, in such a case, the buyer seeking enforcement comes in second; he loses. * * * *

[¶18] The judgment is affirmed. Costs are awarded to Canham.

Questions:

1. Is there any contract left at this point?

2. What's the difference between a condition precedent and a concurrent condition?

3. Are concurrent conditions here express conditions?

4. How does the court know they are supposed to be concurrent and not precedent?

From *K & G Const. Co. v. Harris*, 164 A.2d 451, 455 (Md. 1960):

> In the early days, it was settled law that covenants and mutual promises in a contract were prima facie independent, and that they were to be so construed in the absence of language in the contract clearly showing that they were intended to be dependent. Williston, *op. cit.*, ¶816; Page, *op. cit.*, ¶¶2944, 2945. In the case of *Kingston v. Preston*, 2 Doug. 689, decided in 1774, Lord Mansfield, contrary to three centuries of opposing precedents, changed the rule, and decided that performance of one covenant might be dependent on prior performance of another, although the contract contained no express condition to that effect. Page, *op. cit.*, ¶2946; Williston, *op. cit.*, ¶817. The modern rule, which seems to be of almost universal application, is that there is a presumption that mutual promises in a

> contract are dependent and are to be so regarded, whenever possible. Page, *op. cit.*, ¶2946; *Restatement, Contracts*, ¶ 266. *Cf.* Williston, *op. cit.*, ¶812.

5. In *Pittman*, the parties agreed that time was "of the essence" and named a time within which closing had to occur. How long would the parties be allowed to tender if the contract had not named a time at all? "The absence of an express time for performance does not necessarily mean that the parties did not enter into an enforceable agreement; generally, the law will imply a reasonable time." *Yazdani-Beioky v. Sharifan*, 550 S.W.3d 808, 827 (Tex. App.—Houston 2018, pet. denied). Of course, that will create a fact issue. When you draft a contract, you could usually help your client by writing in termination provisions.

(And what if there is no termination provision in a contract in which performances themselves, after having begun, just seem to go on an on indefinitely? The following approach is pretty standard:

> In general, contracts of perpetual duration are disfavored as a matter of public policy; thus, while we will enforce a contract that unambiguously expresses an intent to be of perpetual duration, we construe ambiguous language regarding duration against perpetual duration.
> * * * *
>
> Because the durational language of the contract [at issue here] is ambiguous, we will construe it against perpetual duration. As there is no definite duration expressed in the contract, we conclude that the contract must be one of indefinite duration. A contract of indefinite duration is terminable at will upon reasonable notice to the other party after a reasonable time has passed.

Glacial Plains Coop. v. Chippewa Valley Ethanol Co., LLLP, 912 N.W.2d 233, 237 (Minn. 2018).)

Thomas R. MOORE v. Martin KOPEL

Supr. Ct. App. Div. (1997)

237 A.D.2d 124, 653 N.Y.S.2d 927

[¶1] Defendant Martin Kopel, D.V.M., purchased the veterinary practice of Pasquale Campanile, D.V.M., for whom he had worked for the previous six years. Finding the income from the practice less than sufficient to meet the $20,000 monthly payments to Dr. Campanile, defendant engaged the services of plaintiff Thomas R. Moore, Esq., to seek a reduction in the purchase price, and in certain tax liabilities, in exchange for a contingent fee of one third of whatever reductions were obtained. Plaintiff was successful in obtaining certain reductions in defendant's liabilities and billed defendant for his services. Upon defendant's failure to remit payment, plaintiff brought this action to recover legal fees.

[¶2] Defendant argues that plaintiff failed to perform a condition precedent to collection of his fee pursuant to the parties' written agreement. He further maintains that the agreement presents certain issues of fact with respect to the reasonableness of the fee.

[¶3] Insofar as pertinent, the agreement states:

> "Whereas Kopel has engaged Moore to seek to reduce payments from Kopel to Pasquale Campanile, P. C. ('Campanile') and to Federal, State and local tax authorities ('T.A.') and otherwise reduce Kopel's liabilities and debt, and increase Kopel's assets and income,
>
> "Now, therefore, Kopel agrees to pay Moore one-third of any said savings achieved through Moore's efforts in reducing Kopel's payments to Campanile and T.A. and in increasing Kopel's assets and income through refunds or rebates from Campanile and T.A., such payments to be made to Moore by Kopel when such reduced payments are made by Kopel and such refunds or rebates are received by Kopel."

[¶4] Defendant contends that the recitation in the agreement that plaintiff has been engaged, inter alia, to "increase Kopel's assets and income" constitutes a condition precedent. He concludes that plaintiff's failure to demonstrate that there has been an increase in the assets and income of the veterinary practice therefore precludes summary judgment in his favor.

[¶5] We do not agree. The agreement does not employ express language of condition (see, e.g., *Charles Hyman, Inc. v Olsen Indus*., 227 A.D.2d 270 [joint venture agreement]; *Lindenbaum v Royco Prop. Corp*., 165 A.D.2d 254 [mortgage contingency clause]), nor has defendant demonstrated that the parties, by the language employed, implicitly agreed that an increase in the assets and income of the practice would be a prerequisite to payment (*cf., World Point Trading PTE v Credito Italiano*, 225 A.D.2d 153, 160; Calamari and Perillo, *Contracts* § 141, at 229-230). While performance of work under a contract is a constructive condition to payment (Calamari and Perillo, *Contracts* § 156, at 244), it is subject to the general rule that payment is due when the promisee has substantially performed his obligations under the agreement (Calamari and Perillo, *Contracts* § 157 [b], at 248). Moreover, it is clear that the basis of compensation, stated in the "Now" clause, is "reducing Kopel's payments" and "increasing Kopel's assets and income through refunds or rebates" (emphasis supplied). Therefore, the recitation to "increase Kopel's assets and income" is not a condition precedent. It is not an express condition. It is not even a constructive condition. It is merely one of the objectives of the contract, as recited in the "Whereas" clause of the agreement. * * * *

[¶6] Order of the Supreme Court, New York County * * * , which, inter alia, denied plaintiff's motion for partial summary judgment as to liability and dismissal of defendants' first and second counterclaims, unanimously reversed, on the law, without costs, the motion granted, and the matter remanded to Supreme Court for assessment of damages.]

Questions:

1. While the court says that "increase Kopel's assets and income" is not a condition precedent, either express or constructive, what *is* clearly a constructive condition of payment? One court put the matter obscurely by referring to one performance as *faciendo* and one as *dando*, and saying that, when that is the case, *faciendo* must precede *dando*. *Coletti v. Knox Hat*, 252 N.Y. 468, 472, 169 N.E. 649, 649 (1930).

2. Is the *and* in “increase Kopel’s assets and income” disjunctive? An *and* can mean *both* or *either*. If I say, “I am looking for deer and antelope,” I want to know where either one of them is—disjunctive. If I say, “We must have skill, speed, and strength to win,” I mean all of them—conjunctive. Which is the *and* connecting “Kopel’s assets and income,” given the other goals in the document?

3. Why should a constructive condition be subject to the doctrine of substantial performance, while express condition must be strictly performed?

4. Interestingly, the *Moore v. Kopel* court suggested the application of substantial performance law to what well may have been a unilateral contract. In a unilateral contract, a promise is exchanged for a performance. Because the performance is consideration for the promise, the promise is not binding until the performance is finished. (Section 45 of the Restatement, if adopted, binds the promisor to an option to give the promisee a reasonable time to finish, but the promisor is bound to the promise only if the promisee finishes.) No doctrine of constructive conditions is necessary because the promise is not binding at all, even contingently, until the performance occurs.

A bargain comprising mutual promises is different. There, a binding contract forms when the promises are traded, as *Nicholas v. Raynbred* affirmed. But who is to say whether the promises are conditions of each other, and which should be performed first? That is why we have the doctrine of constructive conditions with its attached order of performance doctrines. We presume the two promises are dependent—are conditioned on the performance of the other. If one promise is for work and the other for payment, then the *Moore* rule applies to show the order of performance.

If the contract in *Moore v. Kopel* was a unilateral contract, then the constructive conditions doctrine was irrelevant. If it was a trade of mutual promises, then the doctrine applied. Can you tell which it was? Does it make a difference as to the result? In either case, performance had to occur before pay was warranted, so the legal result was the same in that case. That it was and is the same in so many other cases is probably one reason so many lawyers confuse the doctrines. The way the result is reached is very different, however, and the difference is not just a technicality. Many of the doctrines we are about to study—substantial performance, divisible contract, and so on—apply only when the constructive conditions doctrine applies. They do not apply at all to the performance that is consideration in a unilateral contract.

Tying mutual promises to each other in a dependency relationship through the doctrine of constructive conditions, as demonstrated in *Pittman* and *Moore*, means that one party’s duty does not arise until the other party has performed or tendered. But it has another, further-reaching consequence. It means that a breach of certain seriousness can break that dependency and release the other party from further performance. The next case gives an example.

JAMES JAY FORBES and FAY ANNETTE FORBES V. PRIME GENERAL CONTRACTORS, INC, a Florida Corporation

Florida Court of Appeals (2018)

225 So.3d 448

SALARIO, Judge.

[¶1] This is an appeal from a final judgment on a claim for breach of contract. James and Fay Forbes sued Prime General Contractors, Inc. for breach after Prime walked off a home construction job. The Forbeses sought damages that included payments they made to Prime under the contract, payments they made for updated architectural plans, certain other expenses, and a loss of equity in their home. After a bench trial, the trial court found that Prime had materially breached its contract with the Forbeses but declined to award these three items of damage. We reverse the damage award in the final judgment and remand with instructions to award the Forbeses such damages as will restore them to the position they enjoyed right before they inked their contract with Prime. We affirm the judgment in all other respects.

[¶2] The Forbeses and Prime signed a written contract under which Prime agreed to renovate the Forbeses' home in accord with plans drawn up by an architect. In exchange, the Forbeses agreed to pay Prime a total of $276,000 in five separate draws. Under the draw schedule, the Forbeses were to pay (a) 25% of the contract price upon signing, (b) 25% upon completion of demolition, (c) 25% upon completion of the "dry-in" stage of construction [Footnote: The contract defines the "dry-in" stage as "demo, framing rough-in electric, plumbing and mechanical, roof sheeting and felt and exterior windows and doors if available."], (d) 15% after roofing and siding installation, and (e) the remaining 10% upon completion of the job. The contract provided that "any alteration or deviation from this agreement must be made in writing and signed by the Parties." Prime began the job as agreed, and the Forbeses paid the first two contract draws—totaling $138,000. They also paid an additional $6000 for updated architectural plans.

[¶3] Under the contract, the Forbeses should not have had to pay anything more until the dry-in phase of the project was done. Unfortunately, things hit a snag before then. Prime said that the cost of the materials it needed to do the job had gone up. It told the Forbeses that the work would now cost at least $550,000—almost twice the original contract price—and demanded that the Forbeses immediately pay the third draw plus an additional $31,450 for work Prime had already done and for which the Forbeses had already paid. Prime presented the Forbeses with a written change order making these adjustments. The Forbeses refused to sign it and told Prime that they were prepared to move forward at the contract price. Prime refused and walked off the job, leaving the Forbeses' home unfinished and uninhabitable.

[¶4] Because they could not live in their home, the Forbeses began renting a house nearby so that they had somewhere to stay. In the meantime, they looked for another contractor to finish the work on their home—ultimately talking with five potential candidates to perform the service—but none was willing to handle the job. After five months of living in a rental with no luck getting the work on their house finished, the Forbeses bought a new house and moved into it. They were unable, however, to pay a mortgage on their new house and another mortgage on the home that Prime left uninhabitable. So they let the uninhabitable home go into foreclosure. At the time they contracted with Prime, the Forbeses had about $45,000 in equity in the house. That equity was lost in the foreclosure.

[¶5] The Forbeses sued Prime for breach of contract, and the case went to a bench trial at which the evidence was consistent with the facts related above. The Forbeses argued that Prime materially breached the contract by demanding payments to which it was not entitled under the contract and thereafter walking off the job. Prime contended, among other things, that the Forbeses also failed to perform under the contract, to which the Forbeses answered that they were entitled to suspend performance due to Prime's material breach. The Forbeses requested the following items of damages: $138,000 in payments made pursuant to their contract with Prime, $6000 for updated architectural plans, $45,000 of lost equity in their home, $5600 in rent, and various other expenses incurred in reliance on their contract with Prime. It is clear from the damages the Forbeses requested that they were asking to be put in the position they would have occupied had they not contracted with Prime in the first place. Prime asserted and litigated at trial an affirmative defense that the Forbeses failed to mitigate their damages.

[¶6] About a month after the bench trial wrapped, the trial court entered a final judgment. It found that Prime had materially breached the contract as the Forbeses argued. However, it awarded the Forbeses as damages only the $5600 in rent they paid while searching for a new contractor. The trial court explained that "[t]he purpose of contract damages is to put the injured party in as good a position as that in which full performance would have put him" and concluded that the Forbeses:

> failed to offer persuasive or credible evidence at trial of the difference between the market value of the home had it been completed, less such part of the contract price that has not been paid, and the value of the construction that has been furnished by [Prime] thus far.

The court also found, without elaboration, that the Forbeses "made a financial decision not to engage in reasonable mitigation efforts" with respect to their damages.

[¶7] This is the Forbeses' timely appeal of the final judgment. They argue two points: (1) by looking to place them in the position they would have occupied had Prime fully performed instead of the position they would have occupied had they never contracted with Prime, the trial court used an incorrect method of calculating damages; and (2) the trial court's finding that the Forbeses failed to mitigate their damages is unsupported by the evidence. We review the first point de novo, *see Tubby's Customs, Inc. v. Euler*, 225 So. 3d 405, 407 (Fla. 2d DCA 2017), and the second for competent substantial evidence, *cf. RNK Family Ltd. P'ship v. Alexander-Mitchell Assocs.*, 890 So.2d 297, 299 (Fla. 2d DCA 2004). *See also Craigside, LLC v. GDC View, LLC*, 74 So.3d 1087, 1089 (Fla. 1st DCA 2011) ("While the parties are entitled to de novo review of the trial court's rulings with respect to the legal effect of the contract, we are bound by the trial court's findings of fact in a case, like the present one, where competent, substantial evidence supports the findings."). Both points have merit.

[¶8] **Method of calculating damages.** In calculating damages, the trial court erred by failing to honor the Forbeses' choice to deem the contract totally breached and recover those damages that would restore them to the position they occupied immediately before contracting with Prime. When one party to a contract commits a material breach, the nonbreaching party has the option to treat the breach "as a breach of the entire contract—in other words, an entire or total breach." [Footnote: No one in this appeal has challenged the trial court's finding that Prime materially breached its contract with the Forbeses.] *Hyman v. Cohen*, 73 So. 2d 393, 397 (Fla. 1954) (quoting 12 Am. Jur. *Contracts* § 389); *see also* 24 Richard A. Lord, *Williston on Contracts* § 64:27 (4th ed. 2018). From the perspective of the nonbreaching party, there are two main consequences of that decision: (1) the nonbreaching party may suspend his or her own performance of the contract, *see Rector v. Larson's Marine, Inc.*, 479 So. 2d 783, 785 (Fla. 2d DCA 1985), and (2) the

nonbreaching party can elect one of two damage remedies in a suit for breach, *see City of Miami Beach v. Carner*, 579 So. 2d 248, 251 (Fla. 3d DCA 1991).

[¶9] When a party seeks damages for a total breach, "[h]e may treat the contract as void and seek the damages that will restore him to the position he was in immediately prior to entering the contract." *Rector*, 479 So. 2d at 785; *see also McCray v. Murray*, 423 So. 2d 559, 561 (Fla. 1st DCA 1982). Or, in the alternative, he may instead "affirm the contract, 'insist upon the benefit of his bargain, and seek the damages that would place him in the position he would have been in had the contract been completely performed.'" *Tubby's Customs*, 225 So. 3d at 407 (quoting *Citizen's Prop. Ins. Corp. v. Amat*, 198 So. 3d 730, 734 (Fla. 2d DCA 2016)). In the case of a breached construction contract like Prime's contract with the Forbeses, the benefit-of- the-bargain remedy is "either the reasonable cost of completion, or the difference between the value the construction would have had if completed and the value of the construction that has been thus far performed." *Rector*, 479 So. 2d at 785 (citing *Grossman Holdings Ltd. v. Hourihan*, 414 So. 2d 1037 (Fla. 1982) (adopting section 346(1)(a) of the Restatement (First) of Contracts (Am. Law Inst. 1932) to cases involving breach of a construction contract)).

[¶10] Here, the final judgment on its face shows that the trial court believed that the Forbeses were entitled only to the benefit-of-the-bargain remedy. As reflected in the language from its final judgment quoted above, the trial court concluded that the Forbeses were entitled to be put in the position they would have occupied had Prime fully performed and that they had failed to present evidence to establish the key factors that go into that remedy in a construction contract case.

[¶11] But the reason the Forbeses did not produce that evidence was because they did not seek benefit-of-the-bargain damages. They sought to be put in the position they would have occupied had they never contracted with Prime. It was clear at trial that the Forbeses regarded the breach as total; indeed, they were explicit that they were entitled to suspend their own performance under the contract. And the damages they asked the court to award—return of payments made under the contract and the equity in their home at the time of contracting—were of a type that regarded the contract as void and attempted to restore the Forbeses to their precontractual situation. Those damages were inconsistent with an affirmance of the contract and request for damages approximating full performance. *Cf. Sec. & Inv. Corp. of the Palm Beaches v. Droege*, 529 So. 2d 799, 802 (Fla. 4th DCA 1988) ("If the two remedies are inconsistent or mutually exclusive, . . . then the mere choice of one remedy and . . . pursuit of one remedy to judgment . . . operates as an election."); *McCray*, 423 So. 2d at 561 (holding that a trial court did not err in failing to instruct a jury on benefit-of-the-bargain damages where the evidence supported damages to restore plaintiff to his original condition). In the final analysis, then, the remedy the Forbeses chose and pursued was not the remedy the trial court either considered or awarded.

[¶12] **Mitigation of damages.** We agree with the Forbeses that the trial court's finding that they failed to mitigate damages was mistaken. The concept of mitigation is often used, as it appears to have been in this case, to refer to the doctrine of avoidable consequences. In contract cases, there is really no "duty to mitigate" because the claimant "is not compelled to undertake any ameliorative efforts"; rather, he is merely prevented from recovering damages he "could have reasonably avoided." *Sys. Components Corp. v. Fla. Dep't of Transp.*, 14 So. 3d 967, 982 (Fla. 2009) (quoting The Florida Bar, *Florida Civil Practice Damages* § 2.43, at 2–30 (6th ed. 2005)); *see also Penton Bus. Media Holdings, LLC v. Orange County*, 236 So. 3d 495, 496 (Fla. 5th DCA 2018). The word "reasonably" is important. *See* Fla. Std. Jury Instr. (Contract & Bus.) 504.9 (requiring a jury to consider which damages could have been avoided through the plaintiff's reasonable efforts). The doctrine of avoidable consequences does not allow a trial court to reduce damages

"based on what 'could have been avoided' through Herculean efforts." *Sys. Components*, 14 So. 3d at 982. It applies only where a claimant fails to undertake measures to avoid damages that are available to him without undue effort or expense. *Id.*

[¶13] Here, there is no competent substantial evidence that the Forbeses could have taken any measure without undue effort or expense to avoid the damages they sought. When Prime walked off the job, the Forbeses were left with an uninhabitable home that no other contractor would finish. At that point, the money they paid for Prime's work and updated plans was sunk; to avoid that loss they would have had to have been able to finish the home, and there was no evidence that they could have done that with another contractor at the price at which Prime was contractually required to do it.

[¶14] With respect to the lost equity, the Forbeses spent five months living in a rental property as they searched for someone to finish the renovations. After that proved futile, they used their remaining resources to buy a new home rather than continue to make rent payments indefinitely. On the evidence here, had the Forbeses not bought the new house and instead continued paying rent without end, they still would have found themselves unable to continue paying the mortgage on the home that Prime left uninhabitable. This record establishes no course of action available to the Forbeses without undue effort or expense to avoid their damages. Thus, there was no competent substantial evidence to support a damage reduction based on the doctrine of avoidable consequences here. *See, e.g., Graybar Elec. Co. v. Stratton of Fla., Inc.*, 509 So. 2d 1133, 1134 (Fla. 2d DCA 1987) (reversing a final judgment in which the trial court erroneously applied the doctrine of avoidable consequences despite "insufficient evidence to support the application of that doctrine").

[¶15] In sum, the trial court's use of the wrong method for calculating damages together with its erroneous application of the doctrine of avoidable consequences denied the Forbeses the full amount of damages to which they were entitled. We reverse the damages award and remand this case to the trial court for entry of an amended final judgment awarding those damages it finds, after hearing any arguments the parties decide to make, are necessary to place the Forbeses in the position they occupied immediately before they contracted with Prime. In all other respects, the final judgment is affirmed.

Affirmed in part; reversed in part; remanded with instructions.

Questions:

1. Contracts are, under one economic view, essentially a risk allocation device. Under this construction contract, who assumed the risk of an increase of the costs of building materials?

2. What connects the premise of total breach to the conclusion that the contract may be treated as void? The court uses "void" here as an emphatic way of saying it is now without effect. Set out as a syllogism, we need another premise:

1. _____

2. Prime totally breached.

Therefore, the contract is void.

What's the other premise?

3. If the Forbeses elected to affirm the contract, what would they be doing with their right to treat the contract as void? Is that allowed?

4. We are going to look later at damages rules and the relationship between reliance and expectation. You are going to see that the courts often respect the non-breaching party's choice of how to measure damages. The consequences that flow from material breach are one reason they do so. Does the rule applied by the court in this case treat the contractor fairly?

5. Most well-educated contract lawyers would be happy to hear the court describe mitigation as it did. Mitigation is truly part of the measure of damages, not a duty actually to do anything. Can you think of anything else the Forbeses could have done to "reasonably" mitigate?

On remand, the trial court awarded the Forbeses the $138,000 in payments made, $6,000 for updated architectural plans made useless because of the breach, $45,000 for the equity the Forbeses lost in the home, and $5,600 for rental payments, for a total of $194,600 in damages alone. *Forbes v. Prime General Contractors, Inc.*, 2019 WL 816916 (Fla. Cir. Ct. Jan. 14, 2019) (reserving a determination of costs and attorneys' fees). In its opinion, the trial court explained that the homeowners should collect back the $138,000 in part because the contractor should not be made better off by the breach. *Id.* at *10. This was also true before the appeal, of course, and would have occurred under the trial court's original ruling since the contractor had already been paid half the contract amount for doing nothing other than demolition.

Chapter 12. Mitigating the Effect of Conditions

We have already studied waiver, which, when it occurs, can entirely remove the effect of a condition's failure.

But waiver is not alone. Because express conditions must be strictly enforced, they sometimes cause very harsh results—too harsh in some cases. This section starts with equitable relief from forfeiture, a doctrine that mitigates the effects even of express conditions.

Because the courts created the constructive conditions doctrine and imposed it on the parties—out of a sense of fairness and for the sake of (partly economic, partly judicial) efficiency—courts feel special responsibility for the doctrine's effects. Some of the following are doctrines that mitigate the harshness of making a condition out of a promise. These include the doctrines of substantial performance and of divisibility. Others mitigate by dealing with the logical problem of tying mutual promises' performance together by making the duty to do one depend on the duty to do another; this is what anticipatory repudiation is about.

A. Equitable Relief from Forfeiture

William LEWIS v. PREMIUM INVESTMENT CORP.

S.C. (2002)

568 S.E.2d 361

Burnett, J.

[¶1] The Court granted a writ of certiorari to review the Court of Appeals' decision in *Lewis v. Premium Investment Corp.,* 341 S.C. 539, 535 S.E.2d 139 (Ct.App.2000). We affirm as modified.

FACTS

[¶2] On October 29, 1976, Respondent William Lewis (Purchaser) entered into an installment sales contract to purchase real estate in North Myrtle Beach from Petitioner Premium Investment Corporation (Seller). The contract contains the following default provision:

> In the event the Purchaser should fail to make any due installment, and such default shall continue for a period of thirty (30) days, the Seller shall have the right to declare this contract terminated and all amounts previously paid by the Purchaser will be retained by the Seller as rent.

Four months after executing the contract, Purchaser placed a mobile home on the lot and his family moved in. Purchaser made all payments through July 1988.* After July 1988, no further payments were made.

[¶3] In October 1989, one year after Purchaser's default, Seller mailed Purchaser a notice canceling the contract. The notice was returned "unclaimed" to Seller. Although sent by certified mail to the correct address, Purchaser asserts he did not receive the notice.

[¶4] In 1992, Purchaser's wife contacted Seller's representative to determine if he would allow her to assume the payments. The representative passed away without making a commitment.

[¶5] On August 27, 1996, Purchaser's attorney forwarded Seller a check for $2,451.34. Seller refused to accept the check.

[¶6] At the time of default (August 1988), Purchaser had made 141 of the approximately 182 monthly payments and owed $2,440.14. The balance as of August 31, 1998, was $7,726.33.

[¶7] Purchaser brought this action for breach of contract and specific performance. In its amended answer and counterclaim, Seller alleged Purchaser was in default and sought an order terminating the contract. Alternatively, Seller sought judgment in the amount of $7,443, reasonable attorney's fees, and foreclosure of any equitable interest Purchaser may have obtained as a result of the transaction.†

[¶8] The master-in-equity determined Purchaser was in default of the agreement and Seller had the right to terminate the agreement pursuant to its terms. The Court of Appeals reversed, holding Purchaser had an equitable interest in the property and, therefore, Seller's right to seek forfeiture or to foreclose was subject to Purchaser's right of redemption which could not have been waived by the agreement. Id.

ISSUE

[¶9] Did the Court of Appeals err by declining to apply the forfeiture provision of the installment land contract, instead determining Purchaser has an equitable interest in the property which includes a right of redemption upon default?

DISCUSSION

[¶10] Whether an equitable right of redemption exists in spite of a strict forfeiture provision in an installment land contract has not been specifically decided by this Court. In deciding the answer to this question, we must determine whether equitable principles may alter the clear and unambiguous terms of the parties' contract.

Installment Land Contracts

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* [1] The contract price was $7,500 plus interest. Purchaser paid $75.00 as a down payment. Monthly payments were $75.00.

† [2] The parties agree this is an action in equity. * * * *

> [¶11] Real property is often sold under contracts that provide for the payment of the purchase price in a series of installments. These contracts, usually termed installment land contracts, are drafted in many ways. Typically, the vendor retains legal title to the property until all of the purchase price has been paid. Also typically, the purchaser is entitled to immediate possession. Installment contracts almost always contain forfeiture clauses. When enforced, these clauses enable the vendor to terminate the contract, recover the property, and retain all installments paid when the purchaser defaults.

15 Richard R. Powell, *Real Property '*84D.01 at 3 (2000)*; Ellis v. Butterfield*, 98 Idaho 644, 570 P.2d 1334, 1336 (1977) (installment land contract is "frequently called a 'poor man's mortgage' because the vendor, as with a mortgage, finances the purchaser's acquisition of the property by accepting installment payments on the purchase price over a period of years, but the purchaser does not receive the benefit of those remedial statutes protecting the rights of mortgagors.").[§] Contrary to existing mortgage protections, a seller may typically avoid foreclosure procedures by including a forfeiture remedy in the installment land contract. *See* Matthew Cole Bormuth, note, *Real Estate B The Wyoming Installment Land Contract: A Mortgage in Sheep's Clothing? Or What You See Isn't What You Get,* 28 Land and Water Law Review 309 (1993); Juliet M. Moringiello, *A Mortgage by Any Other Name: A Plea for the Uniform Treatment of Installment Land Contracts and Mortgages under the Bankruptcy Code*, 100 Dick. L.R.. 733 (1996) (forfeiture remedy makes installment land contract more favorable to vendor than seller-financed mortgage).

South Carolina Law

[¶12] Basic contract law provides that when a contract is clear and unambiguous, the language alone determines the contract's force and effect. * * * *

[¶13] Parties to a contract may stipulate as to the amount of liquidated damages owed in the event of nonperformance*. Tate v. Le Master*, 231 S.C. 429, 99 S.E.2d 39 (1957). Where, however, the sum stipulated is plainly disproportionate to any probable damage resulting from breach of contract, the stipulation is an unenforceable penalty. *Id.*; *Kirkland Distributing Co. of Columbia, S.C. v. United States*, 276 F.2d 138 (4th Cir.1960). Equity will not enforce a penalty for breach of contract. *South Carolina Dep't of Health and Envtl. Control v. Kennedy*, 289 S.C. 73, 344 S.E.2d 859 (Ct.App.1986). "Equity does not favor forfeitures or penalties and will relieve against them when practicable in the interest of justice." *Lane v. New York Life Ins. Co.,* 147 S.C. 333, 374, 145 S.E. 196, 209 (1928) *citing Bangert v. John L. Roper Lumber Co.,* 169 N.C. 628, 86 S.E. 516, 517 (1915).

[¶14] The above-stated principles of contract law are consistent with the conclusion that a provision in an installment land contract declaring forfeiture in the event of purchaser default can, in particular circumstances, constitute a penalty. In those circumstances, as in other contractual instances where a stipulated sum amounts to a penalty, we conclude it would be inequitable to enforce the forfeiture provision

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[§] [3] An installment land contract does have advantages for buyers. In addition to immediate possession, installment land contracts offer the benefits of a low down payment and easy credit requirements. Buyers do not have to procure expensive and, sometimes unavailable, traditional mortgage financing. Closing costs are often minimal and, since there is no outside lender, there are no loan origination fees. Eric T. Freyfogle, Vagueness and the Rule of Law: Reconsidering Installment Land Contract Forfeitures, 1988 Duke L.J. 609.

without first allowing the purchaser an opportunity to redeem the installment contract by paying the entire purchase price.

[¶15] Our conclusion is supported by authority from other jurisdictions. In numerous other states, courts claim an equitable power to "deny or delay forfeiture when fairness demands." *Freyfogle, supra* 620; *see Hatfield v. Mixon Realty Co.,* 269 Ark. 803, 601 S.W.2d 894 (Ct.App.1980); *Cedar Lane Investments v. American Roofing Supply of Colorado Springs, Inc.*, 919 P.2d 879 (Colo.Ct.App.1996); *Ellis v. Butterfield, supra*; *Nelson v. Robinson*, 184 Kan. 340, 336 P.2d 415 (1959); *Perkins v. Penney*, 387 A.2d 205 (Me.1978); *Rothenberg v. Follman*, 19 Mich. App. 383, 172 N.W.2d 845 (1969); *O'Meara v. Olson*, 414 N.W.2d 563 (Minn.Ct.App.1987); *Beck v. Strong*, 572 S.W.2d 484 (Mo.Ct.App.1978); *Sharp v. Holthusen*, 189 Mont. 469, 616 P.2d 374 (1980); *Martinez v. Martinez,* 101 N.M. 88, 678 P.2d 1163 (1984); *Lamberth v. McDaniel*, 131 N.C. App. 319, 506 S.E.2d 295 (1998); *Straub v. Lessman*, 403 N.W.2d 5 (N.D.1987); *T-Anchor Corp. v. Travarillo Assocs.*, 529 S.W.2d 622 (Tex. Civ. App.1975); *Call v. Timber Lakes Corp.,* 567 P.2d 1108 (Utah 1977); *Bailey v. Savage*, 160 W.Va. 523, 236 S.E.2d 203 (1977); *see also* 4 Richard R. Powell, *Real Property* § 37.21[1] [c] at 132 (2001) ("[t]he main problem with the forfeiture remedy is that it often puts the seller in too favorable a position and, therefore, is subject to attacks based on equitable considerations of unfairness and unconscionability."). In fact, the authoritative treatise on real property law provides, "no state today is likely to condone a purchaser forfeiture that greatly exceeds the vendor's loss." 15 Powell, *Real Property* § 84D.01[4] at 12.

[¶16] As discussed at length in *Bartles v. Livingston*, 282 S.C. 448, 319 S.E.2d 707 (Ct.App.1984), the common law recognized an equitable right of redemption in the context of mortgages well before any statutory right was granted. The mortgagor was given an equitable right to redeem the property irrespective of the terms of the mortgage and this right to redeem was considered an equitable interest in the land. For years, in an executory contract for the sale of land our Court has equated the vendor with the mortgagee and the vendee with the mortgagor. *Dempsey v. Huskey*, 224 S.C. 536, 80 S.E.2d 119 (1954).‡ There is no equitable reason why the right of redemption should not likewise be afforded to vendees in an installment land contract in appropriate circumstances.

[¶17] For the above reasons, we hold courts of equity can relieve a defaulting purchaser from the strict forfeiture provision in an installment land contract and provide the opportunity for redemption when equity so demands.** Accordingly, this matter is remanded to the master-in-equity to determine whether Purchaser has an equitable right of redemption.

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‡ [4] The Court of Appeals has specifically held that in an installment land contract, the vendee in possession of the land is considered the owner of an equitable interest in the property. Southern Pole Bldgs., Inc. v. Williams, 289 S.C. 521, 347 S.E.2d 121 (Ct.App.1986). We note the right of redemption is distinguishable from an equitable estate which may pass to the purchaser under the theory of equitable conversion. Unlike the equitable right of redemption, the theory of equitable conversion does not apply if the parties provide to the contrary by contract. Brook v. Council of Co-Owners of Stones Throw Horiz. Prop. Regime I, 315 S.C. 474, 445 S.E.2d 630 (1994). In this case, the contract provides that, upon default, all amounts previously paid will be retained by Seller as rent. Although this provision may prevent Purchaser from claiming an equitable estate in the property for the amount of the payments made, it cannot defeat his equitable right of redemption.

** [5] A variety of case-specific factors should be considered to determine if redemption is equitable under the circumstances. See Cedar Lane Investments v. American Roofing Supply of Colorado Springs, Inc.,

[¶18] The decision of the Court of Appeals is AFFIRMED AS MODIFIED.

Questions:

1. The court mentions several items that should be considered in a determination of whether equity should grant relief from forfeiture. Can you generalize these?

2. Paragraph 13 mentions a rule governing liquidated damage clauses, a subject we take up more fully in Chapter 14.C.5. The court analogized to this rule for a reason. Can a forfeiture clause be like a liquidated damages clause that, in advance, sets an amount for damages that is "plainly disproportionate to any probable damage"?

3. Other courts asking whether equity should avoid a forfeiture have also considered the degree of fault of the defaulting party and whether the condition that did not occur was a condition precedent or a condition subsequent. Relief is much more likely in the case of a condition subsequent. One can in fact argue that in the case a condition precedent, nothing can be forfeited, because the failure of the condition means that no benefit ever arises such that it can be forfeited. Was the condition in *Lewis* a condition precedent or subsequent? Which of these is a notice condition for the renewal of a lease?

PROBLEM 45: Juan's garage caught fire and burned. It was separate from the house. Juan quickly called the fire department, and his work with a water hose and the fire department's help with their water contained the fire to the garage and eventually put it out. Juan immediately called his home insurance company to report the loss. The next day, he uploaded pictures to the insurance company's website of various items destroyed by the fire. Juan guessed that it will require around $35,000 to rebuild the garage and replace the items. An adjuster (hired by the insurance company) arrived a few days later, took several hundred pictures, and told Juan that she would file a report. The next day, a fire investigator arrived who also took several hundred pictures. Three weeks later, the insurance company posted a notice to Juan on its website notifying him that it was denying coverage solely because of Juan's failure to file a written claim notifying them of the loss. He checked his policy. Sure enough, it provided as follows:

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supra (the amount of the purchaser's equity, the length of the default period and the number of defaults, the amount of monthly payments in relation to rental value, the value of improvements to the property, the adequacy of the property's maintenance); Rothenberg v. Follman, 19 Mich. App. 383, 172 N.W.2d 845 (1969) (whether forfeiture is unreasonable depends upon amount and length of default, amount of forfeiture, reason for delay in payment, and speed in which equity is sought); 4 Powell, Real Property § 37.21[1] at 135 ("In determining whether the attempted forfeiture should be set aside, courts consider the amount of default, the reason for the purchaser's default, the amount of money the purchaser would forfeit compared to the purchase price, and the relationship of the monthly payments to the fair rental value of the property.").

> "Notice of Claim: Written notice of claim must be given to the insurance company within twenty (20) days after the occurrence or commencement of any loss covered by the policy, or as soon thereafter as is reasonably possible. Written notice given by or on behalf of the insured to the insurance company at 435 S. Surety Drive, Actuary, OK 35580, or to any authorized agent of the insurance company, with information sufficient to identify the insured, shall be deemed notice to the insurance company."

Will this provision be enforced? How?

B. Substantial Performance

JACOB & YOUNGS, INC. v. KENT

N.Y. (1921), 230 N.Y. 239

OPINION OF THE COURT

CARDOZO, J.

[¶1] The plaintiff built a country residence for the defendant at a cost of upwards of $77,000, and now sues to recover a balance of $3,483.46, remaining unpaid. The work of construction ceased in June, 1914, and the defendant then began to occupy the dwelling. There was no complaint of defective performance until March, 1915. One of the specifications for the plumbing work provides that "all wrought iron pipe must be well galvanized, lap welded pipe of the grade known as 'standard pipe' of Reading manufacture." The defendant learned in March, 1915, that some of the pipe, instead of being made in Reading, was the product of other factories. The plaintiff was accordingly directed by the architect to do the work anew. The plumbing was then encased within the walls except in a few places where it had to be exposed. Obedience to the order meant more than the substitution of other pipe. It meant the demolition at great expense of substantial parts of the completed structure. The plaintiff left the work untouched, and asked for a certificate that the final payment was due. Refusal of the certificate was followed by this suit.

[¶2] The evidence sustains a finding that the omission of the prescribed brand of pipe was neither fraudulent nor willful. It was the result of the oversight and inattention of the plaintiff's subcontractor. Reading pipe is distinguished from Cohoes pipe and other brands only by the name of the manufacturer stamped upon it at intervals of between six and seven feet. Even the defendant's architect, though he inspected the pipe upon arrival, failed to notice the discrepancy. The plaintiff tried to show that the brands installed, though made by other manufacturers, were the same in quality, in appearance, in market value and in cost as the brand stated in the contract—that they were, indeed, the same thing, though manufactured in another place. The evidence was excluded, and a verdict directed for the defendant. The Appellate Division reversed, and granted a new trial.

[¶3] We think the evidence, if admitted, would have supplied some basis for the inference that the defect was insignificant in its relation to the project. The courts never say that one who makes a contract fills the measure of his duty by less than full performance. They do say, however, that an omission, both trivial and innocent, will sometimes be atoned for by allowance of the resulting damage, and will not always be the breach of a condition to be followed by a forfeiture (*Spence v. Ham*, 163 N. Y. 220; *Woodward v. Fuller*, 80 N. Y. 312; *Glacius v. Black*, 67 N. Y. 563, 566; *Bowen v. Kimbell*, 203 Mass. 364, 370). The distinction is akin to that between dependent and independent promises, or between promises and conditions (*Anson on Contracts* [Corbin's ed.], sec. 367; 2 *Williston on Contracts*, sec. 842). Some promises are so plainly independent that they can never by fair construction be conditions of one another. (*Rosenthal Paper Co. v. Nat. Folding Box & Paper Co.,* 226 N. Y. 313; *Bogardus v. N. Y. Life Ins. Co.,* 101 N. Y. 328). Others are so plainly dependent that they must always be conditions. Others, though dependent and thus conditions when there is departure in point of substance, will be viewed as independent and collateral when the departure is insignificant (2 *Williston on Contracts*, secs. 841, 842; *Eastern Forge Co. v. Corbin*, 182 Mass. 590, 592; Robinson v. Mollett, L. R., 7 Eng. & Ir. App. 802, 814; *Miller v. Benjamin*, 142 N. Y. 613). Considerations partly of justice and partly of presumable intention are to tell us whether this or that promise shall be placed in one class or in another. The simple and the uniform will call for different remedies from the multifarious and the intricate. The margin of departure within the range of normal expectation upon a sale of common chattels will vary from the margin to be expected upon a contract for the construction of a mansion or a 'skyscraper.' There will be harshness sometimes and oppression in the implication of a condition when the thing upon which labor has been expended is incapable of surrender because united to the land, and equity and reason in the implication of a like condition when the subject-matter, if defective, is in shape to be returned. From the conclusion that promises may not be treated as dependent to the extent of their uttermost minutiae without a sacrifice of justice, the progress is a short one to the conclusion that they may not be so treated without a perversion of intention. Intention not otherwise revealed may be presumed to hold in contemplation the reasonable and probable. If something else is in view, it must not be left to implication. There will be no assumption of a purpose to visit venial faults with oppressive retribution.

[¶4] Those who think more of symmetry and logic in the development of legal rules than of practical adaptation to the attainment of a just result will be troubled by a classification where the lines of division are so wavering and blurred. Something, doubtless, may be said on the score of consistency and certainty in favor of a stricter standard. The courts have balanced such considerations against those of equity and fairness, and found the latter to be the weightier. The decisions in this state commit us to the liberal view, which is making its way, nowadays, in jurisdictions slow to welcome it (*Dakin & Co. v. Lee*, 1916, 1 K. B. 566, 579). Where the line is to be drawn between the important and the trivial cannot be settled by a formula. 'In the nature of the case precise boundaries are impossible' (2 *Williston on Contracts*, sec. 841). The same omission may take on one aspect or another according to its setting. Substitution of equivalents may not have the same significance in fields of art on the one side and in those of mere utility on the other. Nowhere will change be tolerated, however, if it is so dominant or pervasive as in any real or substantial measure to frustrate the purpose of the contract (*Crouch v. Gutmann*, 134 N. Y. 45, 51). There is no general license to install whatever, in the builder's judgment, may be regarded as "just as good" (*Easthampton L. & C. Co., Ltd., v. Worthington*, 186 N. Y. 407, 412). The question is one of degree, to be answered, if there is doubt, by the triers of the facts (*Crouch v. Gutmann; Woodward v. Fuller, supra*), and, if the inferences are certain, by the judges of the law (*Easthampton L. & C. Co., Ltd., v. Worthington*, supra). We must weigh the purpose to be served, the desire to be gratified, the excuse for deviation from the letter, the cruelty of enforced adherence. Then only can we tell whether literal fulfilment is to be implied by law as a condition. This is not to say that the parties are not free by apt and certain words to effectuate a purpose that performance of every term shall be a condition of recovery. That question is not here. This is merely to say that the law will

be slow to impute the purpose, in the silence of the parties, where the significance of the default is grievously out of proportion to the oppression of the forfeiture. The willful transgressor must accept the penalty of his transgression (*Schultze v. Goodstein*, 180 N. Y. 248, 251*; Desmond-Dunne Co. v. Friedman-Doscher Co*., 162 N. Y. 486, 490). For him there is no occasion to mitigate the rigor of implied conditions. The transgressor whose default is unintentional and trivial may hope for mercy if he will offer atonement for his wrong (*Spence v. Ham, supra*).

[¶5] In the circumstances of this case, we think the measure of the allowance is not the cost of replacement, which would be great, but the difference in value, which would be either nominal or nothing. Some of the exposed sections might perhaps have been replaced at moderate expense. The defendant did not limit his demand to them, but treated the plumbing as a unit to be corrected from cellar to roof. In point of fact, the plaintiff never reached the stage at which evidence of the extent of the allowance became necessary. The trial court had excluded evidence that the defect was unsubstantial, and in view of that ruling there was no occasion for the plaintiff to go farther with an offer of proof. We think, however, that the offer, if it had been made, would not of necessity have been defective because directed to difference in value. It is true that in most cases the cost of replacement is the measure (*Spence v. Ham*, *supra*). The owner is entitled to the money which will permit him to complete, unless the cost of completion is grossly and unfairly out of proportion to the good to be attained. When that is true, the measure is the difference in value. Specifications call, let us say, for a foundation built of granite quarried in Vermont. On the completion of the building, the owner learns that through the blunder of a subcontractor part of the foundation has been built of granite of the same quality quarried in New Hampshire. The measure of allowance is not the cost of reconstruction. “There may be omissions of that which could not afterwards be supplied exactly as called for by the contract without taking down the building to its foundations, and at the same time the omission may not affect the value of the building for use or otherwise, except so slightly as to be hardly appreciable” (*Handy v. Bliss*, 204 Mass. 513, 519. *Cf. Foeller v. Heintz*, 137 Wis. 169, 178; *Oberlies v. Bullinger*, 132 N. Y. 598, 601; 2 *Williston on Contracts*, sec. 805, p. 1541). The rule that gives a remedy in cases of substantial performance with compensation for defects of trivial or inappreciable importance, has been developed by the courts as an instrument of justice. The measure of the allowance must be shaped to the same end.

The order should be affirmed, and judgment absolute directed in favor of the plaintiff upon the stipulation, with costs in all courts.

MCLAUGHLIN, J. (dissenting).

[¶1] I dissent. The plaintiff did not perform its contract. Its failure to do so was either intentional or due to gross neglect which, under the uncontradicted facts, amounted to the same thing, nor did it make any proof of the cost of compliance, where compliance was possible.

[¶2] Under its contract it obligated itself to use in the plumbing only pipe (between 2,000 and 2,500 feet) made by the Reading Manufacturing Company. The first pipe delivered was about 1,000 feet and the plaintiff’s superintendent then called the attention of the foreman of the subcontractor, who was doing the plumbing, to the fact that the specifications annexed to the contract required all pipe used in the plumbing to be of the Reading Manufacturing Company. They then examined it for the purpose of ascertaining whether this delivery was of that manufacture and found it was. Thereafter, as pipe was required in the progress of the work, the foreman of the subcontractor would leave word at its shop that he wanted a specified number of feet of pipe, without in any way indicating of what manufacture. Pipe would thereafter be delivered and installed in the building, without any examination whatever. Indeed, no examination, so

far as appears, was made by the plaintiff, the subcontractor, defendant's architect, or any one else, of any of the pipe except the first delivery, until after the building had been completed. Plaintiff's architect then refused to give the certificate of completion, upon which the final payment depended, because all of the pipe used in the plumbing was not of the kind called for by the contract. After such refusal, the subcontractor removed the covering or insulation from about 900 feet of pipe which was exposed in the basement, cellar and attic, and all but 70 feet was found to have been manufactured, not by the Reading Company, but by other manufacturers, some by the Cohoes Rolling Mill Company, some by the National Steel Works, some by the South Chester Tubing Company, and some which bore no manufacturer's mark at all. The balance of the pipe had been so installed in the building that an inspection of it could not be had without demolishing, in part at least, the building itself.

[¶3] I am of the opinion the trial court was right in directing a verdict for the defendant. The plaintiff agreed that all the pipe used should be of the Reading Manufacturing Company. Only about two-fifths of it, so far as appears, was of that kind. If more were used, then the burden of proving that fact was upon the plaintiff, which it could easily have done, since it knew where the pipe was obtained. The question of substantial performance of a contract of the character of the one under consideration depends in no small degree upon the good faith of the contractor. If the plaintiff had intended to, and had complied with the terms of the contract except as to minor omissions, due to inadvertence, then he might be allowed to recover the contract price, less the amount necessary to fully compensate the defendant for damages caused by such omissions. (*Woodward v. Fuller*, 80 N. Y. 312*; Nolan v. Whitney*, 88 N. Y. 648.) But that is not this case. It installed between 2,000 and 2,500 feet of pipe, of which only 1,000 feet at most complied with the contract. No explanation was given why pipe called for by the contract was not used, nor was any effort made to show what it would cost to remove the pipe of other manufacturers and install that of the Reading Manufacturing Company. The defendant had a right to contract for what he wanted. He had a right before making payment to get what the contract called for. It is no answer to this suggestion to say that the pipe put in was just as good as that made by the Reading Manufacturing Company, or that the difference in value between such pipe and the pipe made by the Reading Manufacturing Company would be either "nominal or nothing." Defendant contracted for pipe made by the Reading Manufacturing Company. What his reason was for requiring this kind of pipe is of no importance. He wanted that and was entitled to it. It may have been a mere whim on his part, but even so, he had a right to this kind of pipe, regardless of whether some other kind, according to the opinion of the contractor or experts, would have been "just as good, better, or done just as well." He agreed to pay only upon condition that the pipe installed were made by that company and he ought not to be compelled to pay unless that condition be performed. (*Schultze v. Goodstein*, 180 N. Y. 248; *Spence v. Ham, supra*; *Steel S. & E. C. Co. v. Stock*, 225 N. Y. 173; *Van Clief v. Van Vechten*, 130 N. Y. 571; *Glacius v. Black*, 50 N. Y. 145; *Smith v. Brady*, 17 N. Y. 173, and authorities cited on p. 185.) The rule, therefore, of substantial performance, with damages for unsubstantial omissions, has no application. (*Crouch v. Gutmann*, 134 N. Y. 45; *Spence v. Ham*, 163 N. Y. 220.)

[¶4] What was said by this court in *Smith v. Brady* (*supra*) is quite applicable here: "I suppose it will be conceded that everyone has a right to build his house, his cottage or his store after such a model and in such style as shall best accord with his notions of utility or be most agreeable to his fancy. The specifications of the contract become the law between the parties until voluntarily changed. If the owner prefers a plain and simple Doric column, and has so provided in the agreement, the contractor has no right to put in its place the more costly and elegant Corinthian. If the owner, having regard to strength and durability, has contracted for walls of specified materials to be laid in a particular manner, or for a given number of joists and beams, the builder has no right to substitute his own judgment or that of others. Having departed from the agreement, if performance has not been waived by the other party, the law will not allow him to allege

that he has made as good a building as the one he engaged to erect. He can demand payment only upon and according to the terms of his contract, and if the conditions on which payment is due have not been performed, then the right to demand it does not exist. To hold a different doctrine would be simply to make another contract, and would be giving to parties an encouragement to violate their engagements, which the just policy of the law does not permit." (p. 186.)

[¶5] I am of the opinion the trial court did not err in ruling on the admission of evidence or in directing a verdict for the defendant.

[¶6] For the foregoing reasons I think the judgment of the Appellate Division should be reversed and the judgment of the Trial Term affirmed.

HISCOCK, Ch. J., HOGAN and CRANE, JJ., concur with CARDOZO, J.; POUND and ANDREWS, JJ., concur with MCLAUGHLIN, J.

Order affirmed, etc.

Questions:

1. Did Jacob & Youngs' failure to perform exactly what was in the contract—install Reading pipe—deprive it of its right to Kent's performance?

2. Would this case come out differently if we learned that the president of Reading Pipe had been Jacob's rival since they were kids? Would this case come out differently if we learned that Mrs. Kent had been Miss Reading Pipe in a "scholarship pageant" while in high school?

3. Why is good faith part of this doctrine? Will lack of good faith preclude substantial performance or only make it less likely?

4. Suppose the contract said that payment shall be conditioned on compliance with the requirement that Reading Pipe be installed. Any difference? Would substantial performance be available to Jacobs & Young?

5. If Reading and Cohoes pipe are the same, why doesn't Kent just pay the bill?

TOMPKINS et al. v. DUDLEY

N.Y. (1862), 25 N.Y. 272

DAVIES, J.

[¶1] On the 31st of August, 1857, Cornelius Chambers, by a written contract, agreed to make, erect, build and furnish for the plaintiffs a school-house, according to certain plans and specifications, and to furnish the materials for the sum of $678.50. The school-house was to be completed on the 1st day of October, 1857. The defendants guaranteed the performance of the contract on the part of the builder. The building was not completed on the 1st day of October, and it was burned down on the night of the 5th of October. The judge who tried the cause found, as matter of fact, that the contract was substantially performed by Chambers, but that the building was not entirely completed according to the specifications, there remaining to be done a small amount of painting and the hanging of the window blinds, and that the same had not been formally accepted nor the key delivered on the 5th of October. This action is brought to recover the money paid on account to Chambers as the building progressed, and for the damages which the plaintiffs have sustained by reason of the non-completion of the contract, the fulfillment of which was guaranteed by the defendants. It is undeniable that the school house was not completed, nor delivered and accepted by the plaintiffs at the time of its destruction. They had a right to insist upon the completion of the contract according to its terms, and the builder did not allege or pretend that he had completed it. A substantial compliance with the terms of the contract will not answer when the contractor, as in this case, admits and concedes that the work was incomplete; he was still in possession, engaged in its completion. According to the testimony, about $60 was yet to be expended on the building. Had the builder completed the building and complied with his contract at the time of the destruction of the school house? I am constrained to say he had not. He was not only to complete it in accordance with its terms, but was to deliver it over to the plaintiffs thus finished, or offer to deliver it, before his whole duty was performed. Now it is undeniable that the builder did not do this. A portion of the work was yet to be done; the builder was still in possession, and actually engaged in the work of completion at the time of its destruction. * * * * In *Mucklow v. Mangles* (1 Taunt., 218), which arose out of a contract for building a barge, the whole price was paid in advance, the vessel was built and the name of the person who contracted for it was painted on the stern, yet it was held that the title remained in the builder. LAWRENCE, J., said, “No property vests till the thing is finished and delivered.” * * * *

[¶2] The builder, in the present case, by his own contract, created a liability and incurred a duty, which the defendants guaranteed he should perform, and which he has not performed. In justification of such non-performance, he alleges the destruction of the building by fire and inevitable accident, without any fault on his part. The law is well settled, that this is no legal justification for the non-performance of the contract. * * * *

[¶3] The only additional case needful to refer to, is that of *School Trustees of Trenton v. Bennett* (3 Dutcher [N. J.], 514). In that case a person had contracted with the owner of a lot to build, erect and complete a building thereon, and by reason of a latent defect in the soil the building fell down before it was completed, and the Supreme Court of New Jersey held that the loss fell upon the contractor, and that when the contract was, by its terms, to build and complete a building, and find materials for a certain entire price, payable in instalments as the work progresses, the contract is entire, and if the building, either by fault of the builder or by inevitable accident, is destroyed before completion, the owner may recover back the instalments he has paid.

[¶4] The court, in its opinion, says:

> "No rule of law is more firmly established by a long train of decisions than this, that where a party, by his own contract, creates a duty or charge upon himself, he is bound to make it good, notwithstanding any accident by inevitable necessity, because he might have provided against it by his contract."

And in reference to the argument of hardship, the court very justly says:

> "No matter how harsh and apparently unjust in its operation the rule may occasionally be, it cannot be denied that it has its foundation in good sense and inflexible honesty. The party that agrees to do an act should do it, unless absolutely impossible. He should provide against contingencies in his contract. When one of two innocent persons must sustain a loss, the law casts it upon him who has agreed to sustain it, or, rather, the law leaves it where the agreement of the parties has put it; the law will not insert for the benefit of one of the parties, by construction, an exception which the parties have not, either by design or neglect, inserted in their engagement. If a party, for a sufficient consideration, agrees to erect and complete a building upon a particular spot, and find all the materials, and do all the labor, he must erect and complete it, because he has agreed so to do."

[¶5] I arrive at the conclusion that the law is well settled that the defence interposed by the defendants constitutes no justification to Chambers, the builder, for the non-performance of his contract with the plaintiffs, and that, having guaranteed for an adequate consideration, expressed therein, its performance, they are liable to respond to the plaintiffs for the damages which they have sustained by reason of such non-performance. If these views are concurred in by my brethren, the judgment appealed from must be reversed, and a new trial should be had, with costs to abide the event.

WRIGHT, GOULD, ALLEN and SMITH, Js., concurred.

Judgment reversed, and new trial ordered.

Questions:

1. Can Chambers keep anything?

2. Did Chambers breach?

3. Did the plaintiff have to allege tender before recovering? Why or why not?

4. What would you advise Chambers if he brought this contract to you to look over just after it was signed?

PROBLEM 46. On March 1, Irene (the vendor) contracted to sell land to Hannah (vendee) for $8,000 and turned over possession of the property. Hannah paid $2,000 at the time of contracting and agreed to pay $1,000 by the first of each succeeding month until the total price was paid. Irene agreed to convey the deed on September 1, the day final payment was due. Hannah failed to make the June 1 payment. (There is no express condition here as in *Lewis*.) Can Irene recover possession without tendering?

Suppose instead that Irene agreed to put a deed in escrow at the signing of the contract. Different result?

PROBLEM 47. The following evidence was presented at trial:

> The written contract required defendant to install a new roof on plaintiff's home for $648.00. The contract describes the color of the shingles to be used as "russet glow," which defendant defined as a "brown varied color." Defendant acknowledges that it was his obligation to install a roof of uniform color.
>
> After defendant had installed the new roof, plaintiff noticed that it had streaks which she described as yellow, due to a difference in color or shade of some of the shingles. Defendant agreed to remedy the situation and he removed the nonconforming shingles. However, the replacement shingles do not match the remainder, and photographs introduced in evidence clearly show that the roof is not of a uniform color. Plaintiff testified that her roof has the appearance of having been patched, rather than having been completely replaced. According to plaintiff's testimony, the yellow streaks appeared on the northern, eastern and southern sides of the roof, and defendant only replaced the non-matching shingles on the northern and eastern sides, leaving the southern side with the yellow streaks still apparent. The result is that only the western portion of the roof is of uniform color.
>
> When defendant originally installed the complete new roof, it used 24 "squares" of shingles. In an effort to achieve a roof of uniform color, five squares were ripped off and replaced. There is no testimony as to the number of squares which would have to be replaced on the southern, or rear, side of the house in order to eliminate the original yellow streaks. Although there is expert testimony to the effect that the disparity in color would not be noticeable after the shingles have been on the roof for about a year, there is testimony to the effect that, although some nine or ten months have elapsed since defendant attempted to achieve a uniform coloration, the roof is still "streaky" on three sides. One of defendant's experts testified that if the shingles are properly applied the result will be a "blended" roof rather than a streaked roof.
>
> In view of the fact that the disparity in color has not disappeared in nine or ten months, and in view of the fact that there is testimony to the effect that it would be impossible to secure matching shingles to replace the nonconforming ones, it can reasonably be inferred that a roof or uniform coloration can be achieved only by installing a completely new roof.
>
> The evidence is undisputed that the roof is a substantial roof and will give plaintiff protection against the elements.

After the roofer did what the facts relate, the roofer filed a lien on the plaintiff's house. The plaintiff sued to get the lien removed and for damages. The roofer counterclaimed for payment for the roof. The plaintiff continued to live in the house. She paid nothing for the roof before suit, because she objected to the work for the reasons related. Does plaintiff owe for the roof? *O.W. Grun Roofing and Constr. Co. v. Cope*, 529 S.W.2d 258 (Tex. App. 1975).

Note: The UCC Article 2 purports to reject the substantial performance rule. Section 2-601 allows the buyer to reject the whole "if the goods or the tender of delivery fail in any respect to conform to the contract." Lawyers affectionately call this the "perfect tender" rule. Notwithstanding 2-601, Article 2 provides a rule of substantial performance in substance for almost every act of the seller other than delivery or tender of delivery when due. For example, if the seller tenders early, and this is rejected, the seller can cure, 2-508(1); and even if the seller might be late, the seller might have a little more time to cure if it is reasonable in the circumstances, 2-508(2); and revocation of acceptance requires "substantial impair[ment of] value," 2-608(1); and nonconformity in a single installment of an installment contract requires "the non-conformity [to] substantially impair the value of that installment, 2-612(2); and non-conformity in one or more installments is not a breach of the whole unless it "substantially impairs the value of the whole contract," 2-612(3).

C. Divisibility

Marcus LOWY v. UNITED PACIFIC INS. CO.

Cal. (1967), 67 Cal. 2d 87

McCOMB, J.

[¶1] Plaintiffs appeal from a judgment in favor of defendant Arnold Wolpin (hereinafter referred to as "defendant") on a cross-complaint for damages for breach of an excavation and grading contract.

[¶2] Facts: Plaintiffs, owners and subdividers, entered into a contract with defendant, a licensed contractor, for certain excavation and grading work on lots and streets, together with street improvement work consisting of paving the streets and installing curbs and gutters, in a subdivision containing 89 residential lots.

[¶3] After defendant had performed 98 percent of the contracted excavation and grading work, a dispute arose between the parties regarding payment of $7,200 for additional work, consisting of importing dirt for fills, necessitated by changes made by plaintiffs in the plans.

[¶4] Defendant ceased performance. Plaintiffs immediately employed others to do street improvement work called for by the contract and thereafter sued defendant and his bonding company for breach of contract. Defendant answered and cross-complained for damages for breach of contract and reasonable services rendered. The trial court determined that plaintiffs were entitled to nothing against defendant and his bonding company and allowed defendant recovery on his cross-complaint.

[¶5] Questions: First. Was the contract between the parties divisible and the doctrine of substantial performance applicable?

[¶6] Yes.

[¶7] The contract provided, in part, as follows: "[Defendant] agrees to provide and pay for all materials, labor, tools, equipment, light, transportation and other facilities necessary for the execution, in a good and workmanlike manner, of all the following described work: Excavation, Grading and Street Improvements in Tracts No. 26589 and 19517 in accordance with plans and specifications . . . and Exhibit 'A' attached hereto . . . ."

[¶8] "The price which [plaintiffs] shall pay [defendant] for performing his obligations, as aforesaid or as hereunder set forth, is at the following prices indicated: . . . ."

[¶9] "See Exhibits 'A' and 'B' attached hereto." (Italics added.)

[¶10] Exhibit "A" states in part: "[Defendant] agrees to furnish all equipment, labor and material necessary for street improvements, onsite and offsite grading, grade and excavation and erosion control on Tracts 26589 and 19517 . . . for the lump sum price of Seventy-Three Thousand, Five Hundred Dollars ($73,500.00) including, without limitation, all grading, compaction, cleaning, grade and erosion control and dumping, all of which are to be performed to satisfaction of [plaintiffs]. . . ." (Italics added.)

[¶11] The construction of pavement, curbs and gutters is not included in the list of specific items for which the sum of $73,500 is to be paid.

[¶12] Exhibit "B" lists 45 unit prices ranging from $.04 to $4.50 per unit for use in the computation of the amount to be charged for the performance of that part of the street improvement work consisting of paving the streets and installing curbs and gutters. The unit prices are entirely unrelated to excavation and grading.

[¶13] The contract further provides: "In invoicing [plaintiffs], multiply all the final quantities by the unit prices set forth in Exhibit 'B.' All quantities will be determined by Delta Engineering & Surveying Co. and approved by [defendant] and [plaintiffs], with the exception of grading, etc., mentioned in Exhibit 'A' of this Agreement, which is a lump sum price for a complete job without any limitations." (Italics added.)

[¶14] The latter paragraph of the contract shows clearly that the lump sum of $73,500 was not intended to include payment for paving the streets and installing curbs and gutters.

[¶15] The trial court found that under the contract there were two phases of work to be performed, (1) grading and (2) street improvements; that defendant performed all the terms and conditions thereof relating to grading, except work which could be completed for $1,470, being 2 percent of the total grading cost contracted for; that defendant performed additional grading work, reasonably worth $7,200, necessitated by changes in plans on the part of plaintiffs and not attributable to defendant, which additional work was also authorized by plaintiffs through their superintendent; that plaintiffs breached the contract by employing others to do street improvement work and by not making payments to defendant for grading work done by him when due, thereby excusing further performance by defendant; and that defendant was entitled to recover on his cross-complaint for damages, as follows:

Contract price for grading	$73,500.00

Additional work	7,200.00	
		80,700.00
Less amount paid defendant	-60,227.50	
		20.472.50
Less credit for uncompleted work	-1,470.00	
		19,002.50
Less credit for items paid for	-1,166.00	
defendant's account		$17,836.50

[¶16] The trial court also found that defendant was entitled to reasonable attorney's fees in the sum of $4,000, the contract providing for reasonable attorney's fees to be awarded to the prevailing party in any action brought to enforce the terms and conditions thereof.

[¶17] The trial court further found that defendant had breached that portion of the contract relating to street improvement work and was not entitled to recover damages for loss of profits in connection therewith.

[¶18] As indicated above, the contract required the performance of two kinds of work. First, certain excavation and grading work was to be done on lots and streets. Thereafter, street improvement work, consisting of paving the streets and installing curbs and gutters was required.

[¶19] Plaintiffs agreed to pay defendant for the excavation and grading work (including street grading work) the sum of $73,500, as set forth in Exhibit "A" of the contract; and they agreed to pay defendant for the paving of the streets and the installation of curbs and gutters (all commonly called "street improvement work") pursuant to the unit prices set forth in Exhibit "B" of the contract.

[¶20] Accordingly, since the consideration was apportioned, the contract was a severable or divisible one. [Footnote: Williston defines a divisible contract, as follows: "A contract under which the whole performance is divided into two sets of partial performance, each part of each set being the agreed exchange for a corresponding part of the set of performances to be rendered by the other promisor, is called a divisible contract. Or, as expressed in the cases:

> "A contract is divisible where by its terms, 1, performance of each party is divided into two or more parts, and 2, the number of parts due from each party is the same, and 3, the performance of each part by one party is the agreed exchange for a corresponding part by the other party." 96 Williston, Contracts (3d ed. 1962) s 860, pp. 252-254.)]

* * * *

[¶21] Before defendant commenced the excavation and grading work, for which a lump sum price of $73,500 was set by the contract, he gave a surety bond for $73,500. When the excavation and grading work was nearing completion, and it was almost time for work under the second phase to begin, plaintiffs

requested that defendant provide a surety bond for “street improvements” in the sum of $125,000, stating that “no work should be performed on any portion of the street improvement portion of the contract until such bond is furnished.” Thus, it is clear that the parties treated the contract as a divisible one.

[¶22] Under the circumstances, the fact that defendant did not perform the second phase of the contract does not prevent his recovering for work done under the first phase.

[¶23] Defendant did not entirely perform under the first phase of the contract. However, the doctrine of substantial performance, ordinarily applied to building contracts, is here applicable, since the evidence shows that defendant completed 98 percent of the work under the first phase and was prevented from completing the balance through the fault of plaintiffs. * * * *

[¶24] The judgment is affirmed. * * * *

TRAYNOR, C. J., PETERS, J., TOBRINER, J., MOSK, J., BURKE, J., and SULLIVAN, J., concurred.

Questions:

1. Was this contract divisible?

2. What is the legal effect of finding a contract divisible?

3. Did Wolpin substantially perform? A portion?

4. How does the divisible contract doctrine relieve from forfeiture?

5. What about a contract to work for one year at $1,000 per week. Is that divisible? How about at-will employment? Is that divisible? How?

NEW ERA HOMES CORP. v. FORSTER

N.Y. (1949), 86 N.E.2d 757

DESMOND, J.

[¶1] Plaintiff entered into a written agreement with defendants, to make extensive alterations to defendants’ home, the reference therein to price and payment being as follows:

> ‘All above material, and labor to erect and install same to be supplied for $3,075.00 to be paid as follows:

$150.00 on signing of contract,

$1,000.00 upon delivery of materials and starting of work,

$1,500.00 on completion of rough carpentry and rough plumbing,

$425.00 upon job being completed.'

[¶2] The work was commenced and partly finished, and the first two stipulated payments were made. Then, when the 'rough work' was done, plaintiff asked for the third installment of $1,500 but defendants would not pay it, so plaintiff stopped work and brought suit for the whole of the balance, that is, for the two last payments of $1,500 and $425. On the trial plaintiff stipulated to reduce its demand to $1,500, its theory being that, since all the necessary 'rough carpentry and rough plumbing' had been done, the time had arrived for it to collect $1,500. It offered no other proof as to its damages. Defendants conceded their default but argued at the trial, and argue here, that plaintiff was entitled not to the $1,500 third payment, but to such amount as it could establish by way of actual loss sustained from defendants' breach. In other words, defendants say the correct measure of damage was the value of the work actually done, less payments made, plus lost profits. The jury, however, by its verdict gave plaintiff its $1,500. The Appellate Division, Second Department, affirmed the judgment, and we granted defendants leave to appeal to this court.

[¶3] The whole question is as to the meaning of so much of the agreement as we have quoted above. Did that language make it an entire contract, with one consideration for the doing of the whole work, and payments on account at fixed points in the progress of the job, or was the bargain a severable or divisible one in the sense that, of the total consideration, $1,150 was to be the full and fixed payment for 'delivery of materials and starting of work', $1,500 the full and fixed payment for work done up to and including 'completion of rough carpentry and rough plumbing', and $425 for the rest. We hold that the total price of $3.075 was the single consideration for the whole of the work, and that the separately listed payments were not allocated absolutely to certain parts of the undertaking, but were scheduled part payments, mutually convenient to the builder and the owner. That conclusion, we think, is a necessary one from the very words of the writing, since the arrangement there stated was not that separate items of work be done for separate amounts of money, but that the whole alteration project, including material and labor, was 'to be supplied for $3,075.00'. There is nothing in the record to suggest that the parties had intended to group, in this contract, several separate engagements, each with its own separate consideration. They did not say, for instance, that the price for all the work up to the completion of rough carpentry and plumbing was to be $1,500. They did agree that at that point $1,500 would be due, but as a part payment on the whole price. To illustrate: it is hardly conceivable that the amount of $150, payable 'on signing of the contract' was a reward to plaintiff for the act of affixing its corporate name and seal.

[¶4] We would, in short, be writing a new contract for these people if we broke this single promise up into separate deals; and the new contract so written by us might be, for all we know, most unjust to one or the other party.

[¶5] We find no controlling New York case, but the trend of authority in this State, and elsewhere, is that such agreements express an intent that payment be conditioned and dependent upon completion of all the agreed work. *Tompkins v. Dudley*, 25 N.Y. 272, 82 Am. Dec. 349; *Ming v. Corbin*, 142 N.Y. 334, 37 N.E. 105; *United States v. United States Fidelity & Guaranty Co.,* 236 U.S. 512, 35 S. Ct. 298, 59 L. Ed. 696; *Integrity Flooring v. Zandon Corp.,* 130 N.J.L. 244, 32 A.2d 507; *Peist v. Richmond*, 97 Vt. 97, 122 A. 420;

17 C.J.S. Contracts §§ 331-334; 1 Restatement of Contracts § 266 [Am. Law Inst. 1932], illustration 4 on p. 386. We think that is the reasonable rule after all, a house holder who remodels his home is, usually, committing himself to one plan and one result, not a series of unrelated projects. The parties to a construction or alteration contract may, of course, make it divisible and stipulate the value of each divisible part. But there is no sign that these people so intended, *see Integrity Flooring v. Zandon, supra*. It follows that plaintiff, on defendants' default, could collect either in quantum meruit for what had been finished*, Heine v. Meyer*, 61 N.Y. 171, or in contract for the value of what plaintiff had lost that is, the contract price, less payments made and less the cost of completion. *Witherbee v. Meyer*, 155 N.Y. 446, 50 N.E. 58; *Washburne v. Property Owners' Co-operative Ass'n of Middlesex Country*, 209 App. Div. 365, 205 N.Y.S. 36, affirmed 240 N.Y. 663, 148 N.E. 749.

[¶6] The judgments should be reversed, and a new trial granted, with costs to abide the event.

[¶7] Loughran, C.J., and Dye, Fuld and Bromley, JJ., concur with Desmond, J.

[¶8] Lewis, J., dissents in opinion in which Conway, J., concurs.

[¶9] Judgements reversed, etc.

Questions:

1. Is this contract divisible under the test given in *Lowy*? (This is actually the second time we have seen this fact pattern. What was the first? Can you see why the court did not mention divisibility in that case?)

2. Does the formula for damages given by the court put the builder in the position it would have been in had there been no breach?

3. How does the formula protect expectation interests?

4. How does the formula protect reliance interests?

5. Why did the builder want a different formula to be used?

D. Unjust Enrichment

BRITTON v. TURNER

N.H. (1834), 6 N.H. 481

[¶1] ASSUMPSIT for work and labour, performed by the plaintiff, in the service of the defendant, from March 9th, 1831, to December 27, 1831.

[¶2] The declaration contained the common counts, and among them a count in *quantum meruit*, for the labor, averring it to be worth one hundred dollars.

[¶3] At the trial in the C. C. Pleas, the plaintiff proved the performance of the labor as set forth in the declaration.

[¶4] The defence was that it was performed under a special contract—that the plaintiff agreed to work one year, from some time in March, 1831, to March 1832, and that the defendant was to pay him for said year's labor the sum of one hundred and twenty dollars; and the defendant offered evidence tending to show that such was the contract under which the work was done.

[¶5] Evidence was also offered to show that the plaintiff left the defendant's service without his consent, and it was contended by the defendant that the plaintiff had no good cause for not continuing in his employment.

[¶6] There was no evidence offered of any damage arising from the plaintiff's departure, farther than was to be inferred from his non fulfilment of the entire contract.

[¶7] The court instructed the jury, that if they were satisfied from the evidence that the labor was performed, under a contract to labor a year, for the sum of one hundred and twenty dollars, and if they were satisfied that the plaintiff labored only the time specified in the declaration, and then left the defendant's service, against his consent, and without any good cause, yet the plaintiff was entitled to recover, under his *quantum meruit* count, as much as the labor he performed was reasonably worth, and under this direction the jury gave a verdict for the plaintiff for the sum of $95.

[¶8] The defendant excepted to the instructions thus given to the jury.

[¶9] PARKER, J. delivered the opinion of the court.

[¶10] It may be assumed, that the labor performed by the plaintiff, and for which he seeks to recover a compensation in this action, was commenced under a special contract to labor for the defendant the term of one year, for the sum of one hundred and twenty dollars, and that the plaintiff has labored but a portion of that time, and has voluntarily failed to complete the entire contract.

[¶11] It is clear, then, that he is not entitled to recover upon the contract itself, because the service, which was to entitle him to the sum agreed upon, has never been performed.

[¶12] But the question arises, can the plaintiff, under these circumstances, recover a reasonable sum for the service he has actually performed, under the count in quantum meruit.

[¶13] Upon this, and questions of a similar nature, the decisions to be found in the books are not easily reconciled.

[¶14] It has been held, upon contracts of this kind for labor to be performed at a specified price, that the party who voluntarily fails to fulfil the contract by performing the whole labor contracted for, is not entitled to recover any thing for the labor actually performed, however much he may have done towards the performance, and this has been considered the settled rule of law upon this subject. * * * *

[¶15] That such rule in its operation may be very unequal, not to say unjust, is apparent.

[¶16] A party who contracts to perform certain specified labor, and who breaks his contract in the first instance, without any attempt to perform it, can only be made liable to pay the damages which the other party has sustained by reason of such non performance, which in many instances may be trifling—whereas a party who in good faith has entered upon the performance of his contract, and nearly completed it, and then abandoned the further performance—although the other party has had the full benefit of all that has been done, and has perhaps sustained no actual damage—is in fact subjected to a loss of all which has been performed, in the nature of damages for the non fulfilment of the remainder, upon the technical rule, that the contract must be fully performed in order to a recovery of any part of the compensation.

[¶17] By the operation of this rule, then, the party who attempts performance may be placed in a much worse situation than he who wholly disregards his contract, and the other party may receive much more, by the breach of the contract, than the injury which he has sustained by such breach, and more than he could be entitled to were he seeking to recover damages by an action.

[¶18] The case before us presents an illustration. Had the plaintiff in this case never entered upon the performance of his contract, the damage could not probably have been greater than some small expense and trouble incurred in procuring another to do the labor which he had contracted to perform. But having entered upon the performance, and labored nine and a half months, the value of which labor to the defendant as found by the jury is $95, if the defendant can succeed in this defence, he in fact receives nearly five sixths of the value of a whole year’s labor, by reason of the breach of contract by the plaintiff a sum not only utterly disproportionate to any probable, not to say possible damage which could have resulted from the neglect of the plaintiff to continue the remaining two and an half months, but altogether beyond any damage which could have been recovered by the defendant, had the plaintiff done nothing towards the fulfillment of his contract. * * * *

[¶19] There are other cases, however, in which principles have been adopted leading to a different result.

[¶20] It is said, that where a party contracts to perform certain work, and to furnish materials, as, for instance, to build a house, and the work is done, but with some variations from the mode prescribed by the contract, yet if the other party has the benefit of the labor and materials he should be bound to pay so much as they are reasonably worth. * * * *

[¶21] It is in truth virtually conceded in such cases that the work has not been done, for if it had been, the party performing it would be entitled to recover upon the contract itself, which it is held he cannot do.

[¶22] Those cases are not to be distinguished, in principle, from the present, unless it be in the circumstance, that where the party has contracted to furnish materials, and do certain labor, as to build a house in a specified manner, if it is not done according to the contract, the party for whom it is built may refuse to receive it—elect to take no benefit from what has been performed—and therefore if he does receive, he shall be bound to pay the value—whereas in a contract for labor, merely, from day to day, the party is continually receiving the benefit of the contract under an expectation that it will be fulfilled, and cannot, upon the breach of it, have an election to refuse to receive what has been done, and thus discharge himself from payment.

[¶23] But we think this difference in the nature of the contracts does not justify the application of a different rule in relation to them.

[¶24] The party who contracts for labor merely, for a certain period, does so with full knowledge that he must, from the nature of the case, be accepting part performance from day to day, if the other party commences the performance, and with knowledge also that the other may eventually fail of completing the entire term.

[¶25] If under such circumstances he actually receives a benefit from the labor performed, over and above the damage occasioned by the failure to complete, there is as much reason why he should pay the reasonable worth of what has thus been done for his benefit, as there is when he enters and occupies the house which has been built for him, but not according to the stipulations of the contract, and which he perhaps enters, not because he is satisfied with what has been done, but because circumstances compel him to accept it such as it is, that he should pay for the value of the house.

[¶26] Where goods are sold upon a special contract as to their nature, quality, and price, and have been used before their inferiority has been discovered, or other circumstances have occurred which have rendered it impracticable or inconvenient for the vendee to rescind the contract in toto, it seems to have been the practice formerly to allow the vendor to recover the stipulated price, and the vendee recovered by a cross action damages for the breach of the contract. * * * *

[¶27] So where a person contracts for the purchase of a quantity of merchandize, at a certain price, and receives a delivery of part only, and he keeps that part, without any offer of a return, it has been held that he must pay the value of it. 5 Barn. & Cres. *Shipton v. Casson*; Com. Dig. Action F. *Baker v. Sutton*; 1 Camp. 55, note. * * * *

[¶28] There is a close analogy between all these classes of cases, in which such diverse decisions have been made. * * * *

[¶29] It is as “hard upon the plaintiff to preclude him from recovering at all, because he has failed as to part of his entire undertaking,” where his contract is to labor for a certain period, as it can be in any other description of contract, provided the defendant has received a benefit and value from the labor actually performed.

[¶30] We, hold then, that where a party undertakes to pay upon a special contract for the performance of labor, or the furnishing of materials, he is not to be charged upon, such special agreement until the money

is earned according to the terms of it, and where the parties have made an express contract the law will not imply and raise a contract different from that which the parties have entered into, except upon some farther transaction between the parties.

[¶31] In case of a failure to perform such special contract, by the default of the party contracting to do the service, if the money is not due by the terms of the special agreement he is not entitled to recover for his labor, or for the materials furnished, unless the other party receives what has been done, or furnished, and upon the whole case derives a benefit from it. 14 Mass. 282, *Taft v. Montague*; 2 Stark. Ev. 644.

[¶32] But if, where a contract is made of such a character, a party actually receives labor, or materials, and thereby derives a benefit and advantage, over and above the damage which has resulted from the breach of the contract by the other party, the labor actually done, and the value received, furnish a new consideration, and the law thereupon raises a promise to pay to the extent of the reasonable worth of such excess. This may be considered as making a new case, one not within the original agreement, and the party is entitled to "recover on his new case, for the work done, not as agreed, but yet accepted by the defendant." 1 *Dane's Abr*. 224. * * * *

[¶33] In fact we think the technical reasoning, that the performance of the whole labor is a condition precedent, and the right to recover any thing dependent upon it—that the contract being entire there can be no apportionment—and that there being an express contract no other can be implied, even upon the subsequent performance of service—is not properly applicable to this species of contract, where a beneficial service has been actually performed; for we have abundant reason to believe, that the general understanding of the community is, that the hired laborer shall be entitled to compensation for the service actually performed, though he do not continue the entire term contracted for, and such contracts must be presumed to be made with reference to that understanding, unless an express stipulation shows the contrary.

[¶34] Where a beneficial service has been performed and received, therefore, under contracts of this kind, the mutual agreements cannot be considered as going to the whole of the consideration, so as to make them mutual conditions, the one precedent to the other, without a specific proviso to that effect. 1 *H. Black*. 273, note*, Boone v. Eyre*; 6 D. & E. 570, *Campbell v. Jones*; 10 East, 295, *Ritchie v. Atkinson*; 4 Taunt. 745, *Burn v. Miller*.

[¶35] It is easy, if parties so choose, to provide by an express agreement that nothing shall be earned, if the laborer leaves his employer without having performed the whole service contemplated, and then there can be no pretence for a recovery if he voluntarily deserts the service before the expiration of the time.

[¶36] The amount, however, for which the employer ought to be charged, where the laborer abandons his contract, is only the reasonable worth, or the amount of advantage he receives upon the whole transaction, (*ante* 15, *Wadleigh v. Sutton*,) and, in estimating the value of the labor, the contract price for the service cannot be exceeded. 7 Green. 78; 4 Wendell, 285, *Dubois v. Delaware & Hudson Canal Company*; 7 Wend. 121, *Koon v. Greenman*. * * * *

[¶37] If in such case it be found that the damages are equal to, or greater than the amount of the labor performed so that the employer, having a right to the full performance of the contract, has not upon the whole case received a beneficial service, the plaintiff cannot recover.

[¶38] This rule, by binding the employer to pay the value of the service he actually receives, and the laborer to answer in damages where he does not complete the entire contract, will leave no temptation to the former to drive the laborer from his service, near the close of his term, by ill treatment, in order to escape from payment; nor to the latter in desert his service before the stipulated time, without a sufficient reason; and it will in most instances settle the whole controversy in one action, and prevent a multiplicity of suits and cross actions. * * * *

[¶39] Applying the principles thus laid down, to this case, the plaintiff is entitled to judgment on the verdict.

[¶40] The defendant sets up a mere breach of the contract in defence of the action, but this cannot avail him. He does not appear to have offered evidence to show that he was damnified by such breach, or to have asked that a deduction should be made upon that account. The direction to the jury was therefore correct, that the plaintiff was entitled to recover as much as the labor performed was reasonably worth, and the jury appear to have allowed a pro rata compensation, for the time which the plaintiff labored in the defendant's service. * * * *

[¶41] Judgment on the verdict.

Questions:

1. What is the measure of Britton's damages?

2. Should willfulness of the breach stop a restitution action?

3. Most hornbooks report *Britton* as the minority rule. I'm not so sure that it is. In the employment context, it has largely been superseded by statute. But there are some courts that affirmatively hold opposite *Britton*. Suppose *Cope* were decided in New Hampshire. Same result?

4. What does Justice Parker mean in [¶15] when he says that the rule "may be very unequal"?

5. Why does Parker say in [¶32] that "a new case" arises, "one not within the original agreement"? Where does the promise to pay in this "new case" come from?

6. Does Parker always insist that the plaintiff's case here is one of *quantum meruit* or unjust enrichment?
7. Aren't you glad you did not write the sentence in [¶33]? Epaphroditus Peck, in The Law of Persons: Or, Domestic Relations 275 n.10 (1913), reported that Parker regarded *Britton* "as his chief title to fame; and when he sat for his portrait, ordered by the state of New Hampshire, he held a law book open before him, plainly showing the volume and page of that decision." What did Parker see in the decision, do you suppose?

8. Does [¶34] provide an independent ground for the decision?

9. In ¶ 36, Justice Parker wrote that, "in estimating the value of the labor [for which the court awards restitution for unjust enrichment], the contract price for the service cannot be exceeded." One reason for

that may be that the court did not want to encourage a party to breach in order to avoid losing money on a contract. Consider what might happen if the rule were otherwise. Suppose Contractor contracted to build Owner a house for $100 but found it would cost $120 to build the house. If Contractor spent the $120 to perform the contract in full, it would receive $100 in payment; Contractor would have a $20 loss. However, if Contractor instead breached after building $115 worth of house, then Contractor could collect $115 restitution damages - $5 cost of completion = $110. Contractor would be paid $110 for the house, more than it contracted for. It would come out ahead by breaching. Would you want a rule that encouraged parties to breach? Interestingly, in this hypothetical, the value of the construction is assumed to be the cost of providing it. When the construction is new and has never been sold, that is probably our best evidence; that assumption is common in litigation of such fact patterns.

Ellis SATCHELL v. Derrick V. VAN BRODE

Fla. App. (1971), 248 So.2d 245

PER CURIAM.

[¶1] Plaintiff-appellee Van Brode ("Buyer") sued defendant-appellant Satchell ("Seller") for return of a $500.00 earnest money deposit on a written purchase-sale agreement for a residence owned by the Seller for $28,000.00. The Seller counterclaimed for damages for breach of the agreement. A final judgment in a non-jury trial awarded the Buyer his $500.00 earnest money deposit and denied recovery on the Seller's counterclaim.

[¶2] The contract, which was not drafted by an attorney, contained no provisions for what was to be the disposition of the deposit in the event of a breach.

[¶3] The instant appeal presents the following threshold question: Where a contract for the purchase of real property fails to contain a liquidated damages provision, may the defaulting purchaser recover his $500.00 earnest money deposit? We express the view that the case is governed by the following rule, which is stated in *Beatty v. Flannery*, Fla. 1950, 49 So.2d 81, 82:

> "It is well settled that, even in the absence of such a forfeiture provision, a vendee in default is not entitled to recover from the vendor money paid in part performance of an executory contract." (Citations omitted.)

Accord: *Haas v. Crisp Realty Co.*, Fla. 1953, 65 So.2d 765, 768-769. We note that there are exceptions to the rule quoted, and they are adequately discussed in the cases cited; the exceptions do not apply here.

[¶4] The appellant Seller contends that an adverse judgment on his counterclaim is erroneous. Here, the court sat without a jury and determined the facts, and his findings are clothed with a presumption of correctness. Reversible error not having been demonstrated, that portion of the final judgment is affirmed.

[¶5] For the reasons stated, that portion of the final judgment awarding $500.00 to the plaintiff-appellee Van Brode, the buyer, is reversed.

Reversed in part and affirmed in part.

Note: In *Beatty v. Flannery*, cited in *Satchell*, the court wrote regarding exceptions:

> We recognize that there are exceptions to the general rule that a vendee in default cannot recover, but we find no such circumstances in this case. There was no intimation of fraud on the part of the vendor, nor that the vendee's failure to fulfill the contract was due to any misfortune beyond his control that gave the vendor a benefit, the retention of which was shocking to the conscience of the court. Nor is it here contended that there was a mutual rescission of the contract.

49 So.2d at 82.

Questions:

1. Is *Satchell* inconsistent with *Britton*?

2. *Satchell* is the rule in a great number of American jurisdictions with regard to earnest money. Can you think of reasons for it?

3. What if the vendee had paid half the payments in an installment contract? Same result?

4. Why would one choose *Britton* or *Satchell*?

E. Anticipatory Repudiation

HOCHSTER v. DE LA TOUR

Queen's Bench (1852)

2 Ellis and Blackburn 678, 118 ER 922

* * * *

[¶1] On the trial, before Erle J. at the London sittings in last Easter Term, it appeared that plaintiff was a courier, who, in April, 1852, was engaged by defendant to accompany him on a tour, to commence on lst June 1852, on the terms mentioned in the declaration. On the 11th May 1852, defendant wrote to plaintiff that he had changed his mind, and declined his services. He refused to make him any compensation. The action was commenced on 22d. May. The plaintiff, between the commencement of the action and the lst June, obtained an engagement with Lord Ashburton, on equally good terms, but not commencing till 4th July. —The defendant's counsel objected that there could be no breach of the contract before the 1st of June. The learned Judge was of a contrary opinion, but reserved leave to enter a nonsuit on this objection. The other questions were left to the Jury, who found for plaintiff. * * * *

[¶2] Lord Campbell C.J. now delivered the judgment of the Court.

[¶3] On this motion in arrest of judgment, the question arises, Whether, if there be an agreement between A. and B. whereby B. engages to employ A. on and from a future day for a given period of time, to travel with him into a foreign country as a courier, and to start with him in that capacity on that day, A. being to receive a monthly salary during the continuance of such service, B. may, before the day, refuse to perform the agreement and break and renounce it, so as to entitle A. before the day to commence an action against B. to recover damages for breach of the agreement; A. having been ready and willing to perform it, till it was broken and renounced by B. The defendant's counsel very powerfully contended that, if the plaintiff was not contented to dissolve the contract, and to abandon all remedy upon it, he was bound to remain ready and willing to perform it till the day when the actual employment as courier in the service of the defendant was to begin; and that there could be no breach of the agreement, before that day, to give a right of action. But it cannot be laid down as a universal rule that, where by agreement an act is to be done on a future day, no action can be brought for a breach of the agreement till the day for doing the act has arrived. If a man promises to marry a woman on a future day, and before that day marries another woman, he is instantly liable to an action for breach of promise of marriage; *Short v Stone* (8 Q. B. 358). If a man contracts to execute a lease on and from a future day for a certain term, and, before that day, executes a lease to another for the same term, he may be immediately sued for breaking the contract; *Ford v Tiley* (6 B. & C. 325). So, if a man contracts to sell and deliver specific goods on a future day, and before the day he sells and delivers them to another, he is immediately liable to an action at the suit of the person with whom he first contracted to sell and deliver them; *Bowdell v Parsons* (10 East, 359). One reason alleged in support of such an action is, that the defendant has, before the day, rendered it impossible for him to perform the contract at the day: but this does not necessarily follow; for, prior to the day fixed for doing the act, the first wife may have died, a surrender of the lease executed might be obtained, and the defendant might have repurchased the goods so as to be in a situation to sell and deliver them to the plaintiff. Another reason,

may be, that, where there is a contract to do an act on a future day, there is a relation constituted between the parties in the meantime by the contract, and that they impliedly promise that in the meantime neither will do any thing to the prejudice of the other inconsistent with that relation. As an example, a man and woman engaged to marry are affianced to one another during the period between the time of the engagement and the celebration of the marriage. In this very case, of traveller and courier, from the day of the hiring till the day when the employment was to begin, they were engaged to each other; and it seems to be a breach of an implied contract if either of them renounces the engagement. * * * * The declaration in the present case, in alleging a breach, states a great deal more than a passing intention on the part of the defendant which he may repent of, and could only be proved by evidence that he had utterly renounced the contract, or done some act which rendered it impossible for him to perform it. If the plaintiff has no remedy for breach of the contract unless be treats the contract as in force, and acts upon it down to the 1st June 1852, it follows that, till then, he must enter into no employment which will interfere with his promise “to start with the defendant on such travels on the day and year,” and that he must then be properly equipped in all respects as a courier for a three months’ tour on the continent of Europe. But it is surely much more rational, and more for the benefit of both parties, that, after the renunciation of the agreement by the defendant, the plaintiff should be at liberty to consider himself absolved from any future performance of it, retaining his right to sue for any damage he has suffered from the breach of it. Thus, instead of remaining idle and laying out money in preparations which must be useless, he is at liberty to seek service under another employer, which would go in mitigation of the damages to which he would otherwise be entitled for a breach of the contract. It seems strange that the defendant, after renouncing the contract, and absolutely declaring that he will never act under it, should be permitted to object that faith is given to his assertion, and that an opportunity is not left to him of changing his mind. If the plaintiff is barred of any remedy by entering into an engagement inconsistent with starting as a courier with the defendant on the lst June, he is prejudiced by putting faith in the defendant’s assertion: and it would be more consonant with principle, if the defendant were precluded from saying that he had not broken the contract when he declared that he entirely renounced it. Suppose that the defendant, at the time of his renunciation, had embarked on a voyage for Australia, so as to render it physically impossible for him to employ the plaintiff as a courier on the continent of Europe in the months of June, July and August 1852: according to decided cases, the action might have been brought before the lst June; but the renunciation may have been founded on other facts, to be given in evidence, which would equally have rendered the defendant’s performance of the contract impossible. The man who wrongfully renounces a contract into which he has deliberately entered cannot justly complain if he is immediately sued for a compensation in damages by the man whom he has injured: and it seems reasonable to allow an option to the injured party, either to sue immediately, or to wait till the time when the act was to be done, still holding it as prospectively binding for the exercise of this option, which may be advantageous to the innocent party, and cannot be prejudicial to the wrongdoer. An argument against the action before the lst of June is urged from the difficulty of calculating the damages: but this argument is equally strong against an action before the lst of September, when the three months would expire. In either case, the Jury in assessing the damages would be justified in looking to all that had happened, or was likely to happen, to increase or mitigate the loss of the plaintiff down to the day of trial. We do not find any decision contrary to the view we are taking of this case. * * * *

[¶4] Upon the whole, we think that the declaration in this case is sufficient. It gives us great satisfaction to reflect that, the question being on the record, our opinion may be reviewed in a Court of Error. In the meantime we must give judgment for the plaintiff.

[¶5] Judgment for plaintiff.

Questions:

1. C.J. Campbell suggests that there is a “relation constituted between the parties in the meantime by the contract, and that they impliedly promise that in the meantime neither will do any thing to the prejudice of the other inconsistent with that relation.” What have we called that relation?

2. What is meant by “passing intention on the part of the defendant which he may repent of”? Can you give an example?

3. Why isn’t this case grounded on impossibility?

4. Why is it necessary to treat renunciation (the word this court uses) or repudiation as a breach?

5. What happens if one sues before the duty is due, absent a renunciation?

H.B. TAYLOR v. Elizabeth G. JOHNSTON

Cal. (1975), 123 Cal. Rptr. 641

OPINION

SULLIVAN, J.

[¶1] In this action for damages for breach of contract defendants Elizabeth and Ellwood Johnston, individually and as copartners doing business as Old English Rancho, appeal from a judgment entered after a nonjury trial in favor of plaintiff H.B. Taylor and against them in the amount of $132,778.05 and costs.

[¶2] Plaintiff was engaged in the business of owning, breeding, raising and racing thoroughbred horses in Los Angeles County. Defendants were engaged in a similar business, and operated a horse farm in Ontario, California, where they furnished stallion stud services. In January 1965 plaintiff sought to breed his two thoroughbred mares, Sunday Slippers and Sandy Fork to defendants’ stallion Fleet Nasrullah. To that end, on January 19 plaintiff and defendants entered into two separate written contracts—one pertaining to Sunday Slippers and the other to Sandy Fork. Except for the mare involved the contracts were identical. We set forth in the margin the contract covering Sunday Slippers.[*]

[*] [1] [The contract follows:]

“Original IMPORTANT

PLEASE SIGN ORIGINAL AND RETURN AS QUICKLY AS POSSIBLE RETAINING DUPLICATE FOR YOUR OWN FILE.

January 8, 1965

“OLD ENGLISH RANCHO

Route 1, Box 224-A

Ontario, California 91761

“Gentlemen:

“I hereby confirm my reservation for one services to the stallion FLEET NASRULLAH for the year 1966.

“TERMS: $3,500.00 — GUARANTEE LIVE FOAL.

“FEE is due and payable on or before Sept. 1, 1966.

“IF stud fee is paid in full, and mare fails to produce a live foal (one that stands and nurses without assistance) from this breeding, a return breeding the following year to said mare will be granted at no additional stallion fee.

“FEE is due and payable prior to sale of mare or prior to her departure from the state. If mare is sold or leaves the state, no return breeding will be granted.

“STUD CERTIFICATE to be given in exchange for fees paid.

“VETERINARIAN CERTIFICATE due in lieu of payment if mare is barren.

“I hereby agree that OLD ENGLISH RANCHO shall in no way be held responsible for accidents of any kind or disease.

Mr. H.B. Taylor

“Mare: SUNDAY SLIPPERS

Roan filly 1959

[¶3] The contract provided that Fleet Nasrullah was to perform breeding services upon the respective mares in the year 1966 for a fee of $3,500, payable on or before September 1, 1966. If the stud fee was paid in full and the mares failed to produce a live foal (one that stands and nurses without assistance) from the breeding a return breeding would be provided the following year without additional fee.

[¶4] On October 4, 1965, defendants sold Fleet Nasrullah to Dr. A.G. Pessin and Leslie Combs II for $1,000,000 cash and shipped the stallion to Kentucky. Subsequently Combs and Pessin syndicated the sire by selling various individuals 36 or 38 shares, each share entitling the holder to breed one mare each season to Fleet Nasrullah. Combs and Pessin each reserved three shares.

[¶5] On the same day defendants wrote to plaintiff advising the latter of the sale and that he was "released" from his "reservations" for Fleet Nasrullah.† Unable to reach defendants by telephone, plaintiff had his attorney write to them on October 8, 1965, insisting on performance of the contracts. Receiving no answer, plaintiff's attorney on October 19 wrote a second letter threatening suit. On October 27, defendants advised plaintiff by letter that arrangements had been made to breed the two mares to Fleet Nasrullah in Kentucky.‡ However, plaintiff later learned that the mares could not be boarded at Spendthrift Farm where Fleet Nasrullah was standing stud and accordingly arranged with Clinton Frazier of Elmhurst Farm to board the mares and take care of the breeding.

[¶6] In January 1966 plaintiff shipped Sunday Slippers and Sandy Fork to Elmhurst Farm. At that time, however, both mares were in foal and could not be bred, since this can occur only during the five-day period in which they are in heat. The first heat period normally occurs nine days, and the second heat period thirty days, after foaling. Succeeding heat periods occur every 21 days.

MOOLAH BUX-MAOLI-ORMESBY

112 North Evergreen Street

Burbank, California 91505

"(Veterinary certificate must accompany all barren mares.)

"Stakes winner of $64,000.00 last raced in 1962

/s/ H.B. Taylor"

† [2] Defendants' letter stated in part: "We wish to inform you that FLEET NASRULLAH has been sold and will stand the 1966 season in Kentucky. You are, therefore, released from your reservations made to the stallion."

‡ [3] Defendants' letter stated in part: "Mr. Johnston has made arrangements for you to breed SANDY FORK . . . and SUNDAY SLIPPERS . . . to FLEET NASRULLAH for the 1966 season. Therefore, you should communicate with Dr. A.G. Pessin of Spendthrift Farm, Lexington, Kentucky, to finalize breeding arrangements. . . ."

[¶7] On April 17, 1966, Sunday Slippers foaled and Frazier immediately notified Dr. Pessin. The latter assured Frazier that he would make the necessary arrangements to breed the mare to Fleet Nasrullah. On April 26, the ninth day after the foaling, Frazier, upon further inquiry, was told by Dr. Pessin to contact Mrs. Judy who had charge of booking the breedings and had handled these matters with Frazier in the past. Mrs. Judy, however, informed Frazier that the stallion was booked for that day but would be available on any day not booked by a shareholder. She indicated that she was acting under instructions but suggested that he keep in touch with her while the mare was in heat.

[¶8] Sunday Slippers came into heat again on May 13, 1966. Frazier telephoned Mrs. Judy and attempted to book the breeding for May 16.[§] She informed him that Fleet Nasrullah had been reserved by one of the shareholders for that day, but that Frazier should keep in touch with her in the event the reservation was cancelled. On May 14 and May 15 Frazier tried again but without success; on the latter date, Sunday Slippers went out of heat.

[¶9] On June 4, the mare went into heat again. Frazier again tried to book a reservation with Fleet Nasrullah but was told that all dates during the heat period had been already booked. He made no further efforts but on June 7, on plaintiff's instructions, bred Sunday Slippers to a Kentucky Derby winner named Chateaugay for a stud fee of $10,000.

[¶10] Sandy Fork, plaintiff's other mare awaiting the stud services of Fleet Nasrullah, foaled on June 5, 1966. Frazier telephoned Mrs. Judy the next day and received a booking to breed the mare on June 14, the ninth day after foaling. On June 13, 1966, however, she cancelled the reservation because of the prior claim of a shareholder. Frazier made no further attempts and on June 14 bred Sandy Fork to Chateaugay.

[¶11] Shortly after their breeding, it was discovered that both mares were pregnant with twins. In thoroughbred racing twins are considered undesirable since they endanger the mare and are themselves seldom valuable for racing. Both mares were therefore aborted. However, plaintiff was not required to pay the $20,000 stud fees for Chateaugay's services because neither mare delivered a live foal.

[¶12] The instant action for breach of contract proceeded to trial on plaintiff's fourth amended complaint, which alleged two causes of action, the first for breach of the two written contracts, the second for breach of an oral agreement. Defendants cross-complained for the stud fees. The court found the facts to be substantially as stated above and further found and concluded that by selling Fleet Nasrullah defendants had "put it out of their power to perform properly their contracts," that the conduct of defendants and their agents Dr. Pessin and Mrs. Judy up to and including June 13, 1966, constituted a breach[**] and plaintiff "was

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[§] [4] Frazier did not seek to breed Sunday Slippers on May 13, 1966, because the mare's follicle had not yet ruptured; conception can occur up to 12 hours after rupture of the follicle. Accordingly, Frazier normally tried to book a breeding for three days after the onset of heat.

[**] [5] We set forth the significant paragraph of the findings at length: "When defendants sold Fleet Nasrullah in 1965 to a purchaser who shipped him to Kentucky, defendants put it out of their power to perform properly their contracts with plaintiff. Those contracts did not require that plaintiff's rights to the breeding services of Fleet Nasrullah should be relegated to a secondary or subordinate position to that of any other person, whether he be a holder of shares in the stallion or not. No such conditions were stated in the contracts and none can be inferred therefrom. From the conduct of the defendants, their agent Dr. Pessin, and their subagent Mrs. Judy, plaintiff was justified in concluding that the defendants were just giving him the runaround and had no intention of performing their contract in the manner required by its

then justified in treating it as a breach and repudiation of their contractual obligations to him," and that defendants unjustifiably breached the contracts but plaintiff did not.[††] The court awarded plaintiff damages for defendants' breach in the sum of $103,122.50 ($99,800 net damage directly sustained plus $3,322.50 for reasonable costs and expenses for mitigation of damages). "Because of defendants' wholly unwarranted, high-handed, and oppressive breach of their contractual obligation to plaintiff, the plaintiff is entitled to recover from the defendants pre-judgment interest at the rate of 7% per annum on the sum of $99,800.00 from August 1, 1968. . . ." It was concluded that defendants should take nothing on their cross-complaint. Judgment was entered accordingly. This appeal followed.

[¶13] Defendants' main attack on the judgment is two-pronged. They contend: first, that they did not at any time repudiate the contracts; and second, that they did not otherwise breach the contracts because performance was made impossible by plaintiff's own actions. To put it another way, defendants argue in effect that the finding that they breached the contracts is without any support in the evidence. Essentially they take the position that on the uncontradicted evidence in the record, as a matter of law there was neither anticipatory nor actual breach. As will appear, we conclude that the trial court's decision was based solely on findings of anticipatory breach and that we must determine whether such decision is supported by the evidence.

[¶14] Nevertheless both aspects of defendants' argument require us at the outset to examine the specifications for performance contained in the contracts. (See fn. 1, ante.) We note that the reservation for "one services" for Fleet Nasrullah was "for the year 1966." As the evidence showed, a breeding is biologically possible throughout the calendar year, since mares regularly come into heat every 21 days, unless they are pregnant. The contracts therefore appear to contemplate breeding with Fleet Nasrullah at any time during the calendar year 1966. The trial court made no finding as to the time of performance called for by the contracts.[‡‡] There was testimony to the effect that by custom in the thoroughbred racing business the breeding is consummated in a "breeding season" which normally extends from January until early July, although some breeding continues through August. It is possible that the parties intended that the mares be bred to Fleet Nasrullah during the 1966 breeding season rather than the calendar year 1966.[§§]

[¶15] However, in our view, it is immaterial whether the contract phrase "for the year 1966" is taken to mean the above breeding season or the full calendar year since in either event the contract period had not

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terms and as required by the covenant of good faith and fair dealing. Their conduct and that of their agent Dr. Pessin, and their subagent Mrs. Judy up to and including June 13, 1966 constituted a breach of defendants' breeding contracts with plaintiff (plaintiff's Exhibits 8, 9 and 10) and plaintiff was then justified in treating it as a breach and repudiation of their contractual obligation to him."

[††] [6] The court concluded that "The defendants unjustifiably breached these contracts; the plaintiff did not breach these contracts."

[‡‡] [7] The trial court was not compelled to specify the exact time for performance because it concluded that defendants had breached the contracts by anticipatory repudiation, i.e., a breach which occurs prior to the time for performance.

[§§] [8] Perhaps the fact that the stud fees were due to be paid September 1, 1966, at the close of the breeding season supports such a conclusion. Moreover, defendants concede without argument that the trial court impliedly found the time of performance to be the breeding season.

expired by June 7 and June 14, 1966, the dates on which Sunday Slippers and Sandy Fork respectively were bred to Chateaugay[***] and by which time, according to the findings (*see* fn. 5, ante) defendants had repudiated the contracts. There can be no actual breach of a contract until the time specified therein for performance has arrived. (*Gold Min. & Water Co. v. Swinerton,* (1943) 23 Cal.2d 19, 29 [142 P.2d 22]; 1 *Witkin, Summary of Cal. Law* (8th ed.) § 629, p. 536; *see Rest. 2d Contracts* (Tent. Draft No. 8, 1973) § 260.) Although there may be a breach by anticipatory repudiation: "[b]y its very name an essential element of a true anticipatory breach of a contract is that the repudiation by the promisor occur before his performance is due under the contract." (*Gold Min. & Water Co. v. Swinerton, supra*, 23 Cal.2d at p. 29.) In the instant case, because under either of the above interpretations the time for performance had not yet arrived, defendants' breach as found by the trial court was of necessity an anticipatory breach and must be analyzed in accordance with the principles governing such type of breach. To these principles we now direct our attention.

[¶16] Anticipatory breach occurs when one of the parties to a bilateral contract repudiates the contract. The repudiation may be express or implied. An express repudiation is a clear, positive, unequivocal refusal to perform (*Guerrieri v. Severini,* (1958) 51 Cal.2d 12, 18 [330 P.2d 635]; *Gold Min. & Water Co. v. Swinerton, supra*, 23 Cal.2d 19, 29*; Whitney Inv. Co. v. Westview Dev. Co.,* (1969) 273 Cal. App.2d 594, 602-603 [78 Cal. Rptr. 302]; *Atkinson v. District Bond Co.,* (1935) 5 Cal. App.2d 738, 743-744 [43 P.2d 867]); an implied repudiation results from conduct where the promisor puts it out of his power to perform so as to make substantial performance of his promise impossible (*Zogarts v. Smith,* (1948) 86 Cal. App.2d 165 [194 P.2d 143]; *1 Witkin, Summary of Cal. Law* (8th ed.) § 632, pp. 538-539; 4 *Corbin, Contracts* (1951) § 984, pp. 949-951).

[¶17] When a promisor repudiates a contract, the injured party faces an election of remedies: he can treat the repudiation as an anticipatory breach and immediately seek damages for breach of contract, thereby terminating the contractual relation between the parties, or he can treat the repudiation as an empty threat, wait until the time for performance arrives and exercise his remedies for actual breach if a breach does in fact occur at such time. (*Guerrieri v. Severini*, *supra*, 51 Cal.2d 12, 18-19.) However, if the injured party disregards the repudiation and treats the contract as still in force, and the repudiation is retracted prior to the time of performance, then the repudiation is nullified and the injured party is left with his remedies, if any, invocable at the time of performance. (*Id*., at pp. 19-20; *Salot v. Wershow*, (1958) 157 Cal. App.2d 352, 357-358 [320 P.2d 926]; *see Cook v. Nordstrand*, (1948) 83 Cal. App.2d 188, 194-195 [188 P.2d 282]; *Atkinson v. District Bond Co., supra*, 5 Cal. App.2d 738, 743-744.

[¶18] As we have pointed out, the trial court found that the whole course of conduct of defendants and their agents Dr. Pessin and Mrs. Judy from the time of the sale of Fleet Nasrullah up to and including June 13, 1966, amounted to a repudiation which plaintiff was justified in treating as an anticipatory breach. (See fn. 5, ante.) However, when the principles of law governing repudiation just described are applied to the facts constituting this course of conduct as found by the trial court, it is manifest that such conduct cannot be treated as an undifferentiated continuum amounting to a single repudiation but must be divided into two separate repudiations.

[***] [9] Both Sunday Slippers and Sandy Fork would have had at least one more heat during the 1966 breeding season — that of Sunday Slippers commencing on June 26, 1966, and that of Sandy Fork commencing on July 7, 1966.

[¶19] First, defendants clearly repudiated the contracts when, after selling Fleet Nasrullah and shipping him to Kentucky, they informed plaintiff "[y]ou are, therefore, released from your reservations made to the stallion." However, the trial court additionally found that "[p]laintiff did not wish to be 'released' from his 'reservations' . . . insist[ed] on performance of the stud service agreements . . . [and] threaten[ed] litigation if the contracts were not honored by defendants. . . ." Accordingly defendants arranged for performance of the contracts by making Fleet Nasrullah available for stud service to plaintiff in Kentucky through their agents Dr. Pessin and Mrs. Judy. Plaintiff elected to treat the contracts as in force and shipped the mares to Kentucky to effect the desired performance. The foregoing facts lead us to conclude that the subsequent arrangements by defendants to make Fleet Nasrullah available to service plaintiff's mares in Kentucky constituted a retraction of the repudiation. Since at this time plaintiff had not elected to treat the repudiation as an anticipatory breach[****] and in fact had shipped the mares to Kentucky in reliance on defendants' arrangements, this retraction nullified the repudiation. Thus, plaintiff was then left with his remedies that might arise at the time of performance.

[¶20] The trial court found that after the mares had arrived in Kentucky, had delivered the foals they were then carrying and were ready for servicing by Fleet Nasrullah, plaintiff was justified in concluding from the conduct of defendants, their agent Dr. Pessin, and their subagent Mrs. Judy, that "defendants were just giving him the runaround and had no intention of performing their contract in the manner required by its terms" and in treating such conduct "as a breach and repudiation of their contractual obligation to him." (See fn. 5, ante.) Since, as we have explained, defendants retracted their original repudiation, this subsequent conduct amounts to a finding of a second repudiation.

[¶21] There is no evidence in the record that defendants or their agents Dr. Pessin and Mrs. Judy ever stated that Sunday Slippers and Sandy Fork would not be serviced by Fleet Nasrullah during the 1966 breeding season or that they ever refused to perform. Frazier, plaintiff's agent who made arrangements for the breeding of the mares admitted that they had never made such a statement to him.[††††] Accordingly, there was no express repudiation or unequivocal refusal to perform. (*Guerrieri v. Severini, supra,* 51 Cal.2d 12, 18; *Atkinson v. District Bond Co., supra,* 5 Cal. App.2d 738, 743-744.)

[¶22] The trial court's finding of repudiation, expressly based on the "conduct of the defendants" and their agents suggests that the court found an implied repudiation. However, there is no implied repudiation, i.e., by conduct equivalent to unequivocal refusal to perform, unless "the promisor puts it out of his power to perform." (*Zogarts v. Smith, supra*, 86 Cal. App.2d 165, 172-173; 1 *Witkin, Summary of Cal. Law* (8th ed.) § 632, p. 538; 4 *Corbin, Contracts, supra,* § 984, pp. 949-951; *Rest. 2d Contracts* (Tent. Draft No. 8, 1973) §§ 268, 274.) Once the mares arrived in Kentucky, defendants had the power to perform the contracts; Fleet Nasrullah could breed with the mares. No subsequent conduct occurred to render this performance impossible. Although plaintiff was subordinated to the shareholders with respect to the priority of reserving a breeding time with Fleet Nasrullah, there is no evidence in the record that this subordination of reservation

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[****] [10] Plaintiff concedes that the repudiation was not "accepted by plaintiff."

[††††] [11] "Q. . . . At any time, did Mrs. Judy or anyone else ever tell you that she could not or would not breed either mare to Fleet Nasrullah before the end of 1966? . . .

"THE WITNESS: No."

rights rendered performance impossible. Rather it acted to postpone the time of performance, which still remained within the limits prescribed by the contracts. It rendered performance more difficult to achieve; it may even have cast doubt upon the eventual accomplishment of performance; it did not render performance impossible.‡‡‡‡

[¶23] Because there was no repudiation, express or implied, there was no anticipatory breach. Plaintiff contends that defendants' conduct, as found by the trial court, indicated that "defendants were just giving him the runaround and had no intention of performing their contract" and therefore that this conduct was the equivalent of an express and unequivocal refusal to perform. Plaintiff has not presented to the court any authority in California in support of his proposition that conduct which has not met the test for an implied repudiation, i.e. conduct which removed the power to perform, may nonetheless be held to amount to the equivalent of an express repudiation and thus constitute an anticipatory breach. Without addressing ourselves to the question whether some conduct could ever be found equal to an express repudiation, we hold that defendants' conduct in this case as a matter of law did not constitute an anticipatory breach.

[¶24] To constitute an express repudiation, the promisor's statement, or in this case conduct, must amount to an unequivocal refusal to perform: "A mere declaration, however, of a party of an intention not to be bound will not of itself amount to a breach, so as to create an effectual renunciation of the contract; for one party cannot by any act or declaration destroy the binding force and efficacy of the contract. To justify the adverse party in treating the renunciation as a breach, the refusal to perform must be of the whole contract . . . and must be distinct, unequivocal and absolute." (*Atkinson v. District Bond Co., supra,* 5 Cal. App.2d 738, 743.)

[¶25] To recapitulate, Sandy Fork was in foal in January 1966, the commencement of the 1966 breeding season, and remained so until June 5, 1966. Throughout this period Fleet Nasrullah could not perform his services as contracted due solely to the conduct of plaintiff in breeding Sandy Fork in 1965. Biologically the first opportunity to breed Sandy Fork was on June 14, 1966, nine days after foaling. Frazier telephoned Mrs. Judy on June 6, 1966, and received a booking with Fleet Nasrullah for June 14, 1966. On June 13 Mrs. Judy telephoned Frazier and informed him she would have to cancel Sandy Fork's reservation for the following day because one of the shareholders insisted on using that day. Mrs. Judy gave no indication whatsoever that she could not or would not breed Sandy Fork on any of the following days in that heat period or subsequent heat periods. Frazier made no further attempts to breed Sandy Fork with Fleet Nasrullah. Thus, plaintiff, who delayed the possibility of performance for five months, asserts that the delay of performance occasioned by defendants' cancellation of a reservation on the first day during the six-month period that plaintiff made performance possible amounts to an unequivocal refusal to perform, even though

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‡‡‡‡ [12] Plaintiff suggests that this conduct, namely delaying plaintiff's breeding until a day not reserved by a shareholder, amounted to an anticipatory breach because Mrs. Judy inserted a condition to defendants' performance, which as the trial court found was not contemplated by the contracts. Assuming arguendo that this conduct might have amounted to a breach of contract by improperly delaying performance, at most it would have constituted only a partial breach—insufficiently material to terminate the contracts (see Rest. 2d Contracts (Tent. Draft No. 8, 1973) §§ 262, 266, 268, 274). It did not constitute a repudiation of the contracts which was the sole basis of the trial court's decision since "[t]o justify the adverse party in treating the renunciation as a breach, the refusal to perform must be of the whole contract or of a covenant going to the whole consideration. . . ." (Atkinson v. District Bond Co., supra, 5 Cal. App.2d 738, 743.)

there was adequate opportunity for Fleet Nasrullah to perform within the period for performance specified in the contract and even though defendants never stated any intention not to perform. We conclude that as a matter of law this conduct did not amount to an unequivocal refusal to perform and therefore did not constitute an anticipatory breach of the contract covering Sandy Fork.

[¶26] Sunday Slippers foaled on April 17, 1966, first came into heat on April 26 and then successively on May 13 and June 4, 1966. Mrs. Judy informed Frazier that she would breed Sunday Slippers on any day that one of the shareholders did not want to use the stallion. Frazier unsuccessfully sought to breed the mare on April 26, May 14, May 15 and June 4, 1966, Fleet Nasrullah being reserved on those dates. Mrs. Judy continued to assure Frazier that the breeding would occur. Sunday Slippers was due to come into heat again twice during the breeding season: June 25 and July 16, 1966. At most this conduct amounts to delay of performance and a warning that performance might altogether be precluded if a shareholder were to desire Fleet Nasrullah's services on all the remaining days within the period specified for performance in which Sunday Slippers was in heat. We conclude that as a matter of law this conduct did not amount to an unequivocal refusal to perform and therefore did not constitute an anticipatory breach of the contract covering Sunday Slippers.

[¶27] In sum, we hold that there is no evidence in the record supportive of the trial court's finding and conclusion that defendants repudiated and therefore committed an anticipatory breach of the contracts. * * * *

The judgment is reversed.

Questions:

1. Did anticipatory repudiation occur?

2. What would be smoking gun evidence of implied anticipatory repudiation before the mares' owners agreed to ship them to Kentucky?

3. Suppose the shareholders said, "We have sold the horse, but you must be able to breed your mares this month or not at all"—would that be anticipatory repudiation?

4. Why wasn't forcing the mare owners to go to Kentucky an anticipatory repudiation? Why did that not end the parties' contract?

5. Why wasn't having to wait for the shareholders an anticipatory repudiation? Why did that not end the parties' contract?

6. Suppose a vendor of land conveys it to another person. Is that anticipatory repudiation?

7. Suppose a vendee of land discovers before closing that the vendor's Aunt Lulu, a living person but not a party to the contract, has an interest in the land by inheritance. Is that a repudiation?

8. If the mare owners failed to show that the former stud owner breached in Kentucky, then how should we characterize what happened to the contract, legally?

9. In order to sue for stud fees, does the stud owner have to show that it kept Fleet Nasrullah available?

10. Would it be useful to have a legal mechanism to force the promisor to affirm or deny their intention to perform in a case like this? The UCC Article 2 provides such a mechanism in the sale of goods context. Section 2-609, referring obliquely to the parties' good faith obligations, states that "[a] contract for sale imposes an obligation on each party that the other's expectations of receiving due performance will not be impaired." Then, on the assumption that acting as if the promisor might not perform breaches this obligation, says, "When reasonable grounds for insecurity arise with respect to the performance of either party the other may in writing demand adequate assurance of due performance and until he receives such assurance may if commercially reasonable suspend any performance for which he has not already received the agreed return." If the promisor does not provide assurance "adequate under the circumstances" within "a reasonable time not exceeding thirty days," the code declares this anticipatory repudiation. This is a very useful mechanism if the promisor's actions are not quite anticipatory repudiation but make the promisee uncertain. Sometimes parties have tried to do something like this outside the context of the code. If, after the promisor has acted like it is not going to perform, you point blank ask them if they are or not and to answer before a certain day because we all have obligations we need to meet, normal social behavior demands a response. Failure to give one might still not meet the *Taylor* standard, however; silence is not really "positive, unequivocal refusal." Do you wish the law extended the 2-609 mechanism to all contracts? Section 251 of the Restatement (Second) of Contracts suggests that the UCC doctrine also be adopted into the common law of contracts.

More of a comment than a question: You might also want a 2-609 mechanism if you think the other party is not going to perform because it cannot—because it is on the verge of insolvency or actually insolvent (meaning unable to pay debts as they become due). It's very difficult to tell whether someone else is insolvent; often, it is sometimes difficult for they themselves to know. You could try to force the issue by asking them, as per question 10, but if they do not respond, you still do not know.

Roger DIAMOND v. UNIVERSITY OF SOUTHERN CALIFORNIA

Cal. App. (1970), 11 Cal. App. 3d 49

Opinion

KAUS, P.J.

[¶1] Plaintiff, an attorney, who in this class action represents himself and about six hundred others "similarly situated," appeals from a judgement in defendant's favor. * * * *

[¶2] The complaint was filed on December 9, 1968, two weeks after defendant's football team had been selected to play in the Rose Bowl game on January 1, 1969. It contained the following allegations: before the start of the 1968 football season defendant had offered to sell to the public so-called "economy" season

tickets, promising that each buyer of such a ticket would be given an option to purchase a Rose Bowl ticket, if the team were to be selected to play there. Plaintiff and the members of his class purchased economy season tickets for the 1968 season. This was the first time they had done so. After the team's selection for the Rose Bowl game, on or about December 4, 1968, instead of the promised application for a Rose Bowl ticket, plaintiff received a note to the effect that for reasons beyond defendant's control, first time economy season ticket holders could not be furnished with such applications. The note, however, thanked plaintiff for his support of Trojan football. From the receipt of this note plaintiff concluded that defendant had breached its contract with all first time economy season ticket holders, each of who was alleged to have been damaged in the sum of $12, the difference between the market value of a Rose Bowl ticket and the price which defendant would have charged, had it fulfilled its agreement. Since, according to the complaint, the total number of season tickets purchased by the six hundred members of plaintiff's class was three thousand, total damages alleged are $36,000. The complaint also prays for costs, attorney fees, "such other relief as the court deems just and proper" and "[t]hat upon rendition of judgement against defendant as a condition of participation in said judgement by any of the other parties plaintiff similarly situated, that such party pay [a] proportionate share to plaintiff of the cost and expenses of this litigation." A demurrer was overruled on January 6, 1969. In the meanwhile the game had become history.

[¶3] On January 23, 1969, defendant filed its notice of motion for summary judgement which was accompanied by the declaration of Elton D. Phillips, the business manager of defendant and the chairman of its "Football Ticket Committee."

[¶4] According to Mr. Phillips' declaration the university had sold a total of 46,052 season tickets for the 1968 football season, all with the representation that the purchaser would receive an option to buy a Rose Bowl ticket. After the selection of defendant's team to play in the Rose Bowl, the Pasadena Tournament of Roses Association allotted defendant 53,003 tickets of which 10,590 were to go to certain "specifically named groups, companies and associations." This left 42,513 tickets for the 46,052 season ticket holders. A system of priorities was then established and first time economy season ticket holders were given the lowest priority. Applications for Rose Bowl tickets were then mailed to all other season ticket holders. They contained a proviso that orders for tickets had to be mailed to defendant no later than December 4, 1968. Between December 8 and December 16 it appeared that a sufficient number of season ticket holders had not availed themselves of their option so that it became possible to send applications for tickets to those who had previously received none, this is to say, the first time economy ticketed holders. This was done on December 17.

[¶5] It thus appeared that, somewhat belatedly, defendant met its obligation to the members of plaintiff's class. * * * *

[¶6] Defendant's motion for summary judgment was granted on February 10, 1969, and the judgement from which this appeal is taken was entered on March 4.

[¶7] Admittedly the sole purpose of the appeal is to vindicate plaintiff's right to attorney's fees.

[¶8] Plaintiff reasons that he is entitled to attorney's fees on the following analysis:

1. The notice of December 4 was an anticipatory repudiation of defendant's obligation to furnish plaintiff with a ticket application.
2. The filing of the action on December 9 was a change in position which terminated defendant's power to retract the repudiation. * * * *

[¶9] Plaintiff's argument breaks down at step one. Granting, at least for the sake of argument, that the filing of an action is a sufficient change in position to destroy the power to retract an anticipatory repudiation of a contract, plaintiff forgets that, logically or not, it is the general rule, recognized in this state, that the doctrine of breach by anticipatory repudiation does not apply to contracts which are unilateral in their inception or have become so by complete performance by one party. * * * * The theory underlying this rule is that since the plaintiff has no future obligations to perform, he is not prejudiced by having a wait for the arrival of the defendant's time for performance in order to sue for breach. * * * *

[¶10] It is quite evident that when defendant repudiated its obligation on December 4, the contract had become unilateral. Plaintiff and the members of his class had done all that they had ever been obligated to do, that is to pay the price of a season ticket. Nothing was left but for defendant to furnish the applications of the Rose Bowl Tickets. The action was, therefore, premature.

Questions:

1. An "annuity" is a contract in which one party (the "annuitant") pays a premium, often a lump sum just after the contract forms, in exchange for regular, guaranteed payments over a long period of time. Insurance companies sell annuities, often to people planning to retire. Under the rule from *Diamond*, if the annuitant pays a single lump sum to an insurance company for the annuity, is it possible for the insurance company to anticipatorily breach the annuity contract?

2. You might think that consumers who buy cars on multi-year finance contracts might also be unable to commit an anticipatory breach. However, the point is moot because finance companies always write into the finance contract a clause dealing with early breach. What does the clause require, do you suppose?

3. Not every court is so stuffy, and the *Diamond* doctrine was rejected in *Pollack v. Pollack*, 46 S.W.2d 292 (Tex. Comm'n of App. 1932). In this case, Charles conveyed to his brother Henry some property; in return, Henry promised to pay Charles $5,000 per year in equal monthly installments as long as Charles lives, if Henry outlives Charles, in which case the obligation to pay would end; but if Henry died before Charles, then Henry promised to bequeath to Charles property with a value of $100,000, and if the property cannot be partitioned out of Henry's estate to Charles in that amount, then part of Henry's estate would be sold as necessary to pay Charles $100,000. That sounds complicated, but the facts fit the *Diamond* rule because Charles's performance was complete when Charles conveyed the property to Henry. Henry then breached a couple of payments and "absolutely repudiated the obligation, all without just excuse."

In *Pollack*, the court let Charles recover the remaining payments discounted to present value even though there was no acceleration clause. Why? The court said that this:

> Simply stated, the rule of anticipatory breach is founded on the theory that the repudiation of the contract by one of the parties to it before the time of performance has arrived amounts to a tender of a breach of the entire contract, and, if it is accepted by the other party, it constitutes what is known in law as an anticipatory breach of such contract as a whole, and in such event the injured party is at liberty to at once demand his damages for such breach, and, if necessary, begin an action therefor. The damages are to be ascertained as of date of the breach, but such damages are to be full compensation for the loss occasioned by depriving plaintiff of the benefit of the contract. The doctrine of anticipatory breach is not founded on the theory that it moves the performance ahead of the time provided in the contract, but on the theory that, when a party bound to perform under the contract repudiates it and denies his liability thereunder, he thereby wrongfully destroys the contract so far as he is able to do so, and is liable for damages for such wrongful act. Also, since the injury is to the contract as a whole, the measure of damages is the value of the thing injured or destroyed regarded as an article of property. Segwick on Damages, Vol 2, p. 1249, § 636-d. It is also held that the promisee has a right to have the contract kept open and recognized as an article of property, and as a valid, subsisting, and effective contract. The repudiation of the contract denies the promisee all of these rights.

Sound familiar? If you think about contracts this way, there is no reason to draw a distinction between contracts that remain bilateral and contracts that are or have become only unilateral.

Which do you think is the better position?

Chapter 13. Excuse by Subsequent Events

Recall that fact patterns to which the mutual mistake of fact doctrine applies (Chapter 5.D., notes after *Sherwood*) generally fall into one of three types: present impossibility or impracticability, present frustration of purpose, and drastic change in the value of the agreed exchange (this last category being rare). Values in a contract are supposed to be fixed or established at the time of contract formation—based on the parties' beliefs about the facts at the time and what they believe will happen afterward. But facts can change after the contract is formed in ways that violate the contract's basic assumptions. Generally, nothing is more basic to a contract than that the promised performance is possible and that it has some value to the person receiving it. So, when events occur after formation that impact one or both of these two things, the law sometimes allows non-performance to be excused even though it is due. Sometimes the parties include a clause in a contract that allocates the risk of some of these events, called a "force majeure" clause, so we will deal with those here, too.

This chapter's teaching strategy is a bit different. The text will give you some workable rules and edit the primary sources very heavily. There are two reasons to do this:

> 1) Resolving common fact patterns requiring these doctrines more often requires reaching conceptual clarity than sorting out factual ambiguity. Courts do not grant relief very often under these two doctrines. Contracts are supposed to be risk allocation devices. Mostly, assigning a party to perform means that the party takes the risk of non-performance. And, a party's bargaining for a performance means that the party has agreed already that the performance is meaningful and, since they bargained for it, they normally take the risk of its becoming meaningless. In other words, the risk of these supervening events is often allocated by the contract. Seeing whether and how that has been done is often dispositive.
>
> 2) The courts do not state the doctrines very concisely or usably. Rules tend to have between three and five elements, and many rule statements contain duplicative elements. After a long discussion with several rule statements, it can be hard to tell what the rule is.

A. Impracticability

Here are some rules you can use in impracticability cases.

A contractual duty is impracticable and its non-performance excused when:

> (1) a supervening event has occurred that made the performance impracticable,
>
> (2) the nonoccurrence of the event was a basic assumption on which the contract was made, and

> (3) the party seeking excuse for non-performance did not assume the risk of the event (say, by causing it, agreeing to perform in spite of it, failing to foresee it when it should have, or because the court thinks the party should bear the risk, for some reason).

Impracticable does not require impossibility, but the performance must—because of the supervening event—become so difficult and costly as to be commercially senseless, outside both parties' contemplation of the contract.

Would some explanation of the rules be helpful? Here is a passage from *Waddy v. Riggleman*, 606 S.E.2d 222 (W.V. 2004), recited after quoting a bunch of rule statements from various sources and finally settling on something like the R2K § 261, which uses the "basic assumption" concept, too:

> The event made the performance impracticable. The issue of the impracticability of performance is elaborated on in Comment d to the *Restatement (Second) of Contracts* § 261 as follows:
>
> > Events that come within the rule stated in this Section are generally due either to "acts of God" or to acts of third parties. . . . Performance may be impracticable because extreme and unreasonable difficulty, expense, injury, or loss to one of the parties will be involved. A severe shortage of raw materials or of supplies due to war, embargo, local crop failure, unforeseen shutdown of major sources of supply, or the like, which either causes a marked increase in cost or prevents performance altogether may bring the case within the rule stated in this Section. Performance may also be impracticable because it will involve a risk of injury to person or to property, of one of the parties or of others, that is disproportionate to the ends to be attained by performance. *However, "impracticability" means more than "impracticality." A mere change in the degree of difficulty or expense due to such causes as increased wages, prices of raw materials, or costs of construction, unless well beyond the normal range, does not amount to impracticability since it is this sort of risk that a fixed-price contract is intended to cover. Furthermore, a party is expected to use reasonable efforts to surmount obstacles to performance (see § 205), and a performance is impracticable only if it is so in spite of such efforts.*
>
> (Emphasis added). It is additionally explained, in Comment e to Section 261, that:
>
> > It is sometimes said that the rule stated in this Section applies only when the performance itself is made impracticable, without regard to the particular party who is to perform. The difference has been described as that between "the thing cannot be done" and "I cannot do it," and the former has been characterized as "objective" and the latter as "subjective." *This Section recognizes that if the performance remains practicable and it is merely beyond the party's capacity to render it, he is ordinarily not discharged*, but it does not use the terms "objective" and "subjective" to express this. Instead, *the rationale is that a party generally assumes the risk of his own inability to perform his duty. Even if a party contracts to render a performance that depends on some act by a third party, he is not ordinarily discharged because of a failure by that party because this is also a risk that is commonly understood to be on the obligor.*

> (Emphasis added) (citations omitted). As the foregoing comments demonstrate, a party relying on a defense of impracticability must show more than a mere increase in difficulty and/or cost to be excused from performance of a contractual obligation. In addition, one seeking relief under the doctrine of impracticability must have made reasonable efforts to overcome the obstacles to performance.

OK, so now some examples. Your first example might be from Question 1 after *Sherwood v. Walker*. The case of the life estate dependent on a dead person and the sale of a dead horse might be examples of supervening impracticability if the deaths occurred just after the contract formed rather than before. If the person on whose life a life estate depends dies after the life estate is promised but before closing, the vendor's non-performance will probably be excused. If the horse dies between the time of contract formation and the time for performance, there is a good chance the supervening death makes performance impracticable. You'd have to make sure all the elements apply, of course.

Here are some more examples:

Maple Farms, Inc. v. City School District of Elmira, NY, 76 Misc. 2d 1080 (N.Y. Supr. Ct. 1974)

The price of raw milk in a certain geographical area was controlled by the government. Maple Farms was a milk dealer. It had for 10 years bid on contracts to supply milk to City School District of Elmira (ESD). Maple Farms's president knew milk prices and costs and claimed that ESD knows them, too.

The mandated price of raw milk fluctuated. Between '69 and '72 it moved 1% to 4.5% per year. In the '72-'73 years, it went up 9.5%. On June 15, 1973, Maple Farms agreed to supply milk to ESD for the '73-'74 school year at a certain price named in the contract. Then the price of raw milk began to rise again in October 1973, more in November, and by December it was up 23% over the June 1973 price.

In October, Maple Farms began to request that ESD put the contract out for rebidding. ESD refused. Maple Farms claimed that it would lose $7,350.55 on the contract if made to perform at the contract price, given the price of raw milk mandated by the government. It had contracts with other school districts, too, and it faced the same problem there, so that it will actually lose three times that much overall. [Probably this was a test case for Maple Farms, and it meant to take this case to the other districts.]

There were numerous reasons for the price rise, including that the US decided to sell huge amounts of grain to Russia. Some crops also failed. Why would that be relevant to the price of milk? Maple Farms claims these events were unforeseeable.

Is Maple Farms's performance impracticable? Write out your analysis. [FWIW, this case involves the sale of a good, but the UCC standard here only says "made impracticable by the occurrence of a contingency the non-occurrence of which was a basic assumption on which the contract was made." UCC § 2-615. Because the statute says no more than this, courts routinely draw on common law to inform the statute (so basically, courts are doing the same thing both in the common law and Article 2, for this issue).]

Chugach Elec. Ass'n v. Northern Corp., 562 P.2d 1053 (AK 1977)

Here are the facts of *Chugach* excerpted from the opinion:

> In 1966 Northern Corporation and Chugach Electric Association entered into a contract for the repair and protection of the upstream face of the Cooper Lake Dam. Due to circumstances not here relevant, Northern and Chugach amended the contract to provide that riprap and filter layer stone was to be quarried at the opposite end of the lake from the dam and transported across Cooper Lake to the dam site when the lake was frozen to a sufficient depth to permit the hauling of heavy loads. Northern began the ice haul method in the winter of 1966-67 but encountered serious difficulties. By the time the ice was thick enough to support hauling, there were water overflows of one to two feet in certain areas. Northern tried many routes in an attempt to find a safe crossing and made objections to Chugach about the condition of the ice, but Chugach insisted on performance. On March 11, 1967, a Euclid front end loader, which was used to clear the snow from the ice, broke through the ice and was lost. Chugach was informed of the loss but, in a letter dated March 21, again insisted on performance. On March 27, Northern was directed by Chugach to resume operations by the following morning or be held in default. Northern complied with this directive. After repeated efforts to haul the rock involving a number of near losses of equipment, including one small tractor, Northern stopped work on March 31, 1967. A letter, dated March 31, 1967, was sent to Chugach informing them of the suspension of all work. The stoppage of work at this time was done apparently with the approval of Chugach. Some of Northern's equipment was left at the work site.
>
> During the summer and fall of 1967, Northern made repeated attempts to ascertain their position with respect to the subject contract; Chugach did not respond until January 8, 1968. The January 8 letter from Chugach informed Northern that:
>
> > . . . Because CEA cannot permit this work to drag on indefinitely, please take notice that, except that you commence this work and prosecute it with proper diligence so as to have hauled all rock by April 1, 1968, CEA will declare you in default under the contract and take such further steps with your surety or otherwise as may be necessary under the circumstances.
>
> In a letter dated January 20, 1968, Northern informed Chugach they were mobilizing for a haul at Cooper Lake. The ice conditions at Cooper Lake were much improved over what they had been the previous winter. There was only a small amount of snow, the ice was frozen to what was believed to be the proper depth, and there were no overflow problems.
>
> On February 1, 1968, Northern began hauling the rock across the ice in trucks that were only partially loaded. Two trucks broke through the ice, resulting in the death of both drivers and the loss of the trucks. Northern stopped all operations at this point and informed Chugach on February 16, 1968, that it would "make no further attempts to haul across the ice." By letter of March 28, 1968, Northern declared a termination of the contract.
>
> In September 1968, Northern brought suit against Chugach seeking $139,957.25 in damages, the difference between the amount it expended in attempting to perform the

> contract and the amount received from Chugach. Chugach counterclaimed for liquidated damages in the amount of $28,250.

Northern's bid was only for $63,655. A later letter increased the contract price by $42,000 to account for preparation of materials and the cost of their transport. The increased cost—over hauling—of barging the material across the lake would have been $59,520, evidence showed.

What do you think? The earlier opinion in *Northern Corp. v. Chugach Elec. Ass'n*., 518 P.2d 76 (AK 1974), held as follows (before remanding for further fact-finding and consideration of remedies, at which time the trial court took more evidence, which is why the case came back to the court for the 1977 opinion):

> [¶1] The focal question is whether the amended contract was impossible of performance. The September 27, 1966 directive specified that the rock was to be transported 'across Cooper Lake to the dam site when such lake is frozen to a sufficient depth to permit heavy vehicle traffic thereon,' and the formal amendment specified that the hauling to the dam site would be done during the winter of 1966-67. It is therefore clear that the parties contemplated that the rock would be transported across the frozen lake by truck. Northern's repeated efforts to perform the contract by this method during the winter of 1966-67 and subsequently in February 1968, culminating in the tragic loss of life, abundantly support the trial court's finding that the contract was impossible of performance by this method.
>
> [¶2] Chugach contends, however, that Northern was nevertheless bound to perform, and that it could have used means other than hauling by truck across the ice to transport the rock. The answer to Chugach's contention is that, as the trial court found, the parties contemplated that the rock would be hauled by truck once the ice froze to a sufficient depth to support the weight of the vehicles. The specification of this particular method of performance presupposed the existence of ice frozen to the requisite depth. Since this expectation of the parties was never fulfilled, and since the provisions relating to the means of performance was clearly material, Northern's duty to perform was discharged by reason of impossibility.
>
> [¶3] There is an additional reason for our holding that Northern's duty to perform was discharged because of impossibility. It is true that in order for a defendant to prevail under the original common law doctrine of impossibility, he had to show that no one else could have performed the contract. However, this harsh rule has gradually been eroded, and the Restatement of Contracts has departed from the early common law rule by recognizing the principle of 'commercial impracticability'. Under this doctrine, a party is discharged from his contract obligations, even if it is technically possible to perform them, if the costs of performance would be so disproportionate to that reasonably contemplated by the parties as to make the contract totally impractical in a commercial sense. This principle was explicated in *Natus Corp. v. United States*, where the Court of Claims, although holding that the defense was not justified on the facts of that case, went on to explain:
>
> In taking this position, we readily concede that the doctrine of legal impossibility does not demand a showing of actual or literal impossibility.

> Removed from the strictures of the common law, 'impossibility' in its modern context has become a coat of many colors, including among its hues the point argued here-namely, impossibility predicated upon 'commercial impracticability.' This concept-which finds expression both in case law . . . and in other authorities . . . is grounded upon the assumption that in legal contemplation something is impracticable when it can only be done at an excessive and unreasonable cost. As stated in *Transatlantic Financing Corp. v. United States* . . .:
>
> . . . The doctrine ultimately represents the ever-shifting line, drawn by courts hopefully responsive to commercial practices and mores, at which the community's interest in having contracts enforced according to their terms is outweighed by the commercial senselessness of requiring performance . . . (citations omitted).
>
> [¶4] Sec. 465 of the Restatement also provides that a serious risk to life or health will excuse nonperformance.
>
> [¶5] Alaska has adopted the Restatement doctrine whereby commercial impracticability may under certain circumstances justify regarding a contract as impossible to perform. In *Merl F. Thomas Sons, Inc. v. State*, * * * * * * * [w]e quoted with approval Professor Williston's analysis of the concept of impossibility:
>
> > The true distinction is not between difficulty and impossibility. As has been seen, a man may contract to do what is impossible, as well as what is difficult. The important question is whether an unanticipated circumstance, the risk of which should not fairly be thrown upon the promisor, has made performance of the promise vitally different from what was reasonably to be expected (footnote omitted).
>
> In the case before us the detailed opinion of the trial court clearly indicates that the appropriate standard was followed. There is ample evidence to support its findings that '(t)he ice haul method of transporting riprap ultimately selected was within the contemplation of the parties and was part of the basis of the agreement which ultimately resulted in amendment No. 1 in October 1966,' and that that method was not commercially feasible within the financial parameters of the contract. We affirm the court's conclusion that the contract was impossible of performance.

How would you decide this? Impracticable?

Note: As between sellers and buyers, who would use the doctrine of impracticability?

B. Force Majeure

It is possible to write a contract provision that encapsulates something like impracticability doctrine. Parties who have been in a business for a long time are not often surprised by unusual events. After they have learned what events might make performance impracticable, they may want to tie down what should happen if those events occur. Sometimes, contract drafters find standardized provisions in contract forms that they include in contracts, sometimes without thinking about them much. The next case is pretty typical and also provides an important ruling on impracticability.

George SEITZ v. MARK-O-LITE SIGN CONTRACTORS, INC.

N.J. Super. Ct. (1986), 510 A.2d 319

MILBERG, A.J.S.C.

[¶1] This is an action for breach of contract in which plaintiff, George Seitz, seeks damages from defendant, Mark-O-Lite Sign Contractors, Inc., in the amount of $7,200.

[¶2] At trial, counsel for the parties agreed to submit the dispute to the court's determination based on the following stipulated facts:

> [Seitz submitted a bid as general contractor to do renovation work on the Strand Theater. Seitz won the contract. Seitz needed a sub to do work on the Theater's neon sign marquee. Plaintiff obtained an estimate from Mark-O-Lite and later signed a contract with Mark-O-Lite for the work, for $12,800.]
>
> 10. The contract between the parties contained a provision in paragraph (2) which reads as follows: "The Company shall not be liable for any failure in the performance of its obligation under this agreement which may result from strikes or acts of labor union, fires, floods, earthquakes, or acts of God, or other conditions or contingencies beyond its control."
>
> 11. Within a few days of the execution of the contract, defendant discovered that its expert sheet metal worker, Al Jorgenson, a diabetic, was required to enter the hospital and would be unable to work for an unknown period of time. Jorgenson was the only employee of defendant capable of performing the expert and detailed sheet metal work required.
>
> 12. Defendant advised plaintiff of the situation with its employee by telephone and on May 3, 1984, sent a letter to plaintiff returning the uncashed deposit check offering to complete any portion of the work which defendant was able to perform.
>
> [Mark-O-Lite contacted other sign companies, but they wanted far more money to do the work than Mark-O-Lite was making from this job. Seitz eventually hired someone else to do it for $20,000, including some additional items.]

> 15. The total damages claimed by plaintiff are in the amount of $7,200, representing the difference between the City Sign Service price of $20,000 and the price of $12,800 stated in the contract between the parties.

Defendant asserts the defense of impossibility of performance due to the disability of its sheet metal worker, Jorgenson. Specifically, defendant urges that the illness of Jorgenson discharged its obligation of performance pursuant to paragraph 2 of the contract. Paragraph 2, commonly known as a force majeure clause, reads:

> The Company shall not be liable for any failure in the performance of its obligations under this agreement which may result from strikes or acts of Labor Union, fires, floods, earthquakes, or acts of God, War or other conditions or contingencies beyond its control. [Emphasis supplied]

Defendant contends that Jorgenson's disability was a "condition or contingency beyond its control," that its obligation of performance was therefore excused under the above-quoted, exculpatory language.

[¶3] In construing broad, exculpatory language of this type, however, the courts of this State and the majority of jurisdictions invoke the rule of ejusdem generis. *See Abeles v. Adams Engineering Co.,* 64 N.J. Super. 167, 176 (App. Div.), mod. 35 N.J. 411 (1961); 17 *Am.Jur.2d, Contracts*, § 270 (1964). Under this principle, the catch-all language of the force majeure clause relied upon by defendant is not to be construed to its widest extent; rather, such language is to be narrowly interpreted as contemplating only events or things of the same general nature or class as those specifically enumerated. *Buono Sales, Inc. v. Chrysler Motors Corp.,* 363 F.2d 43, 47 (3 Cir.1966), cert. den. 385 U.S. 971, 87 S. Ct. 510, 17 L. Ed. 2d 435 1966); 17 *Am.Jur.2d, supra*, § 409; 24 P.O.F.2d at 291 (1980); *see Abeles v. Adams Engineering Co., supra*, 64 N.J. Super. at 176.

[¶4] Jorgenson's disability does not fall into the same class as that of labor strikes, fires, floods, earthquakes or war. Nor can it be termed an "act of God." Jorgenson's condition was not the consequence of a stroke or a heart attack, either of which might, in a particular case, be deemed an "act of God" because of its suddenness. See 1 *Am.Jur.2d, Act of God,* § 10. Jorgenson is a diabetic. His disability—a partial amputation of his foot—was the result of the progressive aggravation of an infection, which aggravation was apparently rooted in his diabetes. Jorgenson's affliction was not sudden; indeed, his disability was a reasonably foreseeable consequence of his unfortunate malady. Hence, Jorgenson's incapacitation cannot be classed an "act of God" by any logical stretch of the term. *See generally* 1 *Am.Jur.2d, Act of God, supra*, § 3. Defendant's force majeure clause does not apply.

[¶5] It does not necessarily follow, however, that defendant is bereft of the defense of impossibility of performance; thus far, it has merely been determined that the force majeure clause is unavailing.

[¶6] There is very little, if any, recent New Jersey case law pertinent to the impossibility defense asserted herein; yet the general principles are well settled and relatively unchanged.

[¶7] The traditional rule with respect to impossibility by virtue of the death or illness of a particular person is set forth in the *Restatement, Contracts*, § 459 (1932):

> A duty that requires for its performance action that can be rendered only by the promisor or some other particular person is discharged by his death or by such illness as makes the

> necessary action by him impossible or seriously injurious to his health, unless the contract indicates a contrary intention or there is contributing fault on the part of the person subject to the duty.

See generally 84 *A.L.R.2d*, § 8[c] at 49 (1962).

[¶8] A more modern formulation of the doctrine is found in §§ 261 and 262 of the *Restatement, Contracts 2d* (1981), which speak in terms of "impracticability" rather than "impossibility":

> § 261. Discharge by Supervening Impracticability
>
> Where, after a contract is made, a party's performance is made impracticable without his fault by the occurrence of an event the non-occurrence of which was a basic assumption on which the contract was made, his duty to render that performance is discharged, unless the language or the circumstances indicate the contrary.
>
> § 262. Death or Incapacity of Persons Necessary for Performance
>
> If the existence of a particular person is necessary for the performance of a duty, his death or such incapacity as makes performance impracticable is an event the non-occurrence of which was a basic assumption on which the contract was made.

Section 262 states a specific instance for the application of the rule stated in § 261 and, thus, is subject to the qualifications stated in that preceding section. See Comment a to § 262, supra.

[¶9] Regardless of which Restatement is adopted with respect to impossibility, however, the success of the defense in the particular mode asserted herein turns on a determination that the duty in question, as understood by the parties, can be performed only by a particular person. *Restatement, Contracts 2d,* § 459, Comment c, § 262, Comment b; *see Calamari & Perillo, Contracts*, § 13-6 at 489 (1977). Such has long been the governing standard in this State * * * , as well as in the majority of jurisdictions. See generally 17 *Am.Jur.2d, Contracts, supra*, § 414; 84 *A.L.R.2d, supra*, § 8[a], [c].

[¶10] Thus, it is clear from the foregoing that the primary application of the impossibility defense in the form asserted by defendant is in the area of personal service contracts, that is, contracts which contemplate the peculiar skill or discretion of a particular person. *Restatement, Contracts 2d, supra,* § 262 Comment b; *see Walter E. Heller & Co. v. American Flyers Airline Corp.,* 459 F.2d 896, 901 (2 Cir.1972); *see generally*, 17 *Am.Jur.2d, Contracts, supra*, §§ 413, 414. Where, as here, the agreement is silent as to whether a particular person is or is not necessary for performance, all the circumstances will be considered to determine whether the duty, as understood by the parties, sufficiently involves elements of personal service or discretion as to require performance by a particular individual. *Restatement, Contracts 2d*, § 262, Comment b.

[¶11] The real question, therefore, is whether the duty of performance can be delegated to another: If the act to be performed is delegable, then the illness of the promisor or of a third person who is expected to perform the act does not excuse performance. *Calamari & Perillo, supra,* § 13-6 at 489; *see Restatement, Contracts 2d*, § 262, Comment b ("If an obligor can discharge his duty by the performance of another, his own disability will not discharge him."); *Restatement, Contracts 2d*, § 459, Comment c ("If a contractor without violation of duty can go abroad and perform by means of another, his death or illness will not make

subsequent performance of his contract impossible."). The preceding is merely a corollary of the general rule that, for impossibility to operate as an excuse, it must be objective ("the thing cannot be done") rather than subjective ("I cannot do it"). *Calamari & Perillo, supra*, § 13-12 at 497; *see Restatement, Contracts 2d*, § 261, Comment e; *Duff v. Trenton Beverage Co.,* 4 N.J. 605, 606 (1950).

[¶12] It is readily apparent from an application of the foregoing principles that defendant cannot prevail on its claim of impossibility of performance. Nothing in the language of the contract contemplates performance only by Jorgenson; nor do the circumstances demonstrate that the performance to be rendered by Jorgenson was so personal in nature, calling for a peculiar skill or special exercise of discretion, as to make it nondelegable. To be sure, the conduct of defendant—and that of plaintiff—following the advent of Jorgenson's incapacitation belies any claim of special need for his services. Defendant contacted a number of outside shops in an attempt to engage someone else to perform the sheet metal work. Defendant admitted that the sheet metal work could still be performed, albeit through someone other than Jorgenson. *Cf.* 13 *Am.Jur.2d, Building and Construction Contracts*, § 63 (A contract to build a house does not involve such a personal relation that it may not be performed by persons other than the contracting parties thereto and, therefore, is not terminated by the death of one of the parties).

[¶13] At best, defendant's claim is that of subjective impossibility which, as was previously stated, is no excuse for nonperformance. *Duff v. Trenton Beverage Co., supra*, 4 N.J. at 606.

[¶14] Any claim by defendant that its obligation of performance should be excused, because to assume the higher cost of subcontracting the sheet metal work would have resulted in a marginal profit or even a loss, must fail. "Where one agrees to do, for a fixed sum, a thing possible to be performed, he will not be excused or become entitled to additional compensation because unforeseen difficulties are encountered."

Questions:

1. Did Mark-O-Lite anticipatorily breach?

2. Consider ¶ 5: are force majeure and impracticability different doctrines? Is a ruling on one a ruling one a ruling on the other? Does the legal rule applied in ¶¶ 3–4 apply to impracticability doctrine? The force majeure holding here is typical.

3. The ruling on impracticability in this opinion was not surprising at all. As the court says in ¶ 12, "[i]t is readily apparent . . . that defendant cannot prevail." There are some contracts that require a certain person to perform them; they cannot be delegated. Examples include a promise to play for an NBA team, a promise to sing in an opera, and a promise to serve as a judge. But if the person is not part of the promised performance, then delegation is allowed and a person's disappearance/illness/death makes no difference. In *Seitz*, Seitz made a contract with a corporation, not an individual. There was almost no chance that some individual's illness would make performance by the corporation impracticable. You should take seriously the language near the end of ¶ 11 about objective v. subjective impracticability: If the objection is "I cannot do it," nothing is excused; if the objection is "the thing cannot be done," then it may be impracticable. If

LeBron's basketball playing is the performance, then LeBron's illness makes it impracticable. If LeBron makes a contract to haul lumber, then his illness will not be an excuse.

4. Quite a few businesses tried to get out of obligations during COVID shutdowns. It was a period of reduced profit. Their lawyers tried everything they could think of. The following from *A/R Retail LLC v. Hugo Boss Retail, Inc.*, 72 Misc. 3d 627 (N.Y. Sup. Ct. 2021), was typical regarding impracticability and force majeure:

> [¶1] Tenant's claims, defenses, and counterclaims for rescission or reformation based on impossibility of performance are also unavailing. "Impossibility excuses a party's performance only when the destruction of the subject matter of the contract or the means of performance makes performance objectively impossible" (*Kel Kim Corp. v. Cent. Markets, Inc.,* 70 N.Y.2d 900, 902, 524 N.Y.S.2d 384, 519 N.E.2d 295 [1987]). Indeed, "[f]inancial difficulty or economic hardship, even to the extent of insolvency or bankruptcy," is not sufficient to invoke the doctrine (* * * ; *Warner v. Kaplan,* 71 A.D.3d 1, 5, 892 N.Y.S.2d 311 [1st Dept. 2009] ["where performance is possible, albeit unprofitable, the legal excuse of impossibility is not available"]).
>
> [¶2] Moreover, "the impossibility must be produced by an unanticipated event that could not have been foreseen or guarded against in the contract" (*Kel Kim Corp.,* 70 N.Y.2d at 902, 524 N.Y.S.2d 384, 519 N.E.2d 295; *see Gander Mtn. Co. v. Islip U-Slip LLC*, 923 F. Supp. 2d 351, 362 [N.D. N.Y. 2013], *affd,* 561 Fed. Appx. 48 [2d Cir. 2014] ["Impossibility and frustration of purpose refer to two distinct doctrines in contract law, but both require unforeseeability."]; *see also Gregg L. Weiner, et al., New York Contract Law Remedies in the Face of Disruption Caused by COVID-19*, March 10, 2020 ["In the context of the coronavirus outbreak, impossibility may provide grounds for excusing performance ... even then, the party invoking the doctrine must show that the measures were unforeseeable and the risk associated with them could not have been built into the contract."]).
>
> [¶3] A number of courts have rejected the impossibility defense as an excuse for tenants not performing contractual obligations, such as payment of rent, during the COVID-19 pandemic (*e.g.*, *Maesa LLC v. TPR Holdings LLC,* 2020 WL 5499231 [Sup. Ct., New York County Sept. 9, 2020] ["defendant submits no evidence or explanation of how performance was impossible ... rather than being difficult due to the pandemic"]; *Louboutin,* 2020 N.Y. Slip Op. 34063[U], 3-4 [Sup Ct, New York County 2020] ["the impossibility doctrine does not compel the Court to deny the instant motion. The subject matter of the contract--the physical location of the retail store--is still intact. And defendant is permitted to sell its products. The issue is that it cannot sell enough to pay the rent. That does not implicate the impossibility doctrine."]; *1140 Broadway LLC v. Bold Food, LLC*, 2020 N.Y. Slip Op. 34017[U], 4, 2020 WL 7137817 [Sup. Ct., New York County 2020] ["find[ing] that the impossibility doctrine does not compel the Court to deny the motion" where tenant's primary business — managing and consulting for a group of restaurants — was made unprofitable by the shutdown of the restaurant industry]).
>
> [¶4] This Court agrees with those decisions and finds that the impossibility defense does not apply here. As noted in Gap, the "impossibility defense fails because the very text of the Lease demonstrates that the conditions that [the tenant] claims render performance impossible were foreseeable" (—— F.Supp.3d at ——, 2021 WL 861121, at *10, citing

> *Gander Mtn. Co.,* 923 F. Supp. 2d at 362). To the extent Tenant's impossibility argument is predicated on government orders — both during the shutdown period and afterward — the force majeure provisions in the Lease indicate that the risk of such disruptions were not unforeseeable. And for the reopening period, Tenant fails to raise a genuine issue of fact because it is undisputed that Tenant operated the Store during that time. Although its business was made difficult by the pandemic, Tenant's performance under the Lease was not objectively impossible (*e.g.*, *Maesa LLC,* 2020 WL 5499231 ["defendant submits no evidence or explanation of how performance was impossible ... rather than being difficult due to the pandemic"]).
>
> [¶5] Therefore, Landlord is entitled to summary judgment dismissing Tenant's defenses and counterclaims in Action 1 to the extent they are based on Tenant's purported impossibility of performance.

Under the law recited in this passage, would a COVID shutdown of the Strand Theater have excused non-performance of Seitz in its contract with Mark-O-Lite? Can you even imagine a circumstance in which an obligation to pay money is impracticable?

C. Frustration of Purpose

You can use this rule:

> The non-performance of the duty of the person receiving a performance is excused when:
>
> (1) a supervening event has occurred that frustrates the purpose of the contract recognized as the contract's purpose by both parties,
>
> (2) the nonoccurrence of the event was a basic assumption on which the contract was made, and
>
> (3) the party seeking excuse for non-performance did not assume the risk of the event (say, by causing it, agreeing to perform in spite of it, failing to foresee it when it should have, or because the court thinks the party should bear the risk, for some reason).

We looked at a relevant case of present frustration when we studied mutual mistake. Please go back and look at Chapter 5.D *Sherwood v. Walker* question 2. *Allen v. Hammond* is an excellent example—or would be if the Portuguese paid after the lawyer was hired but before the lawyer had done anything. Only a shift in time for the supervening event separates present frustration from supervening frustration.

Please consider these cases:

Peoplesoft U.S.A., Inc. v. Softek, Inc., 227 F. Supp. 2d 1116 (N. Dist. Cal. (2002).

Peoplesoft designs and sells business software products. Softek provides software development services. In March 2000, the two executed a "Software License and Services Agreement." Peoplesoft agreed to provide software, and Softek agreed to pay license and maintenance fees and installation and training fees, which were by the terms of the agreement "noncancellable and nonrefundable." The contract also said that Softek "is responsible for and guarantees all payment to Peoplesoft on behalf of itself and of its customer, Policia de Puerto Rico." The agreement specified that the right to use Peoplesoft's software was exclusively for the purpose of internal data processing of the Policia de Puerto Rico (the language is in ¶8 of the contract: "shall only use the Software solely for the benefit of Policia de Puerto Rico, Transportation Division" and shall ensure that Policia de Puerto Rico uses it only for their own internal purposes; this clause is more or less repeated two other times elsewhere in the contract). The agreement also said that "neither party shall be liable for any failure to perform due to causes beyond its reasonable control."

Peoplesoft shipped software and billed Softek. But the Policia de Puerto Rico decided not to use the software, which Softek returned to Peoplesoft unopened. Softek told Peoplesoft that, though Policia de Puerto Rico had breached its contract with Softek, it preferred not to sue Policia de Puerto Rico because it was a frequent government contractor. But Peoplesoft demanded payment. Softek agreed to pay $87,931.63 of the amount, for the training expenses and airfares. But Softek says it should not have to pay the $150k license fee for software it returned to Peoplesoft.

Peoplesoft sued, alleging breach. Softek alleged 17 defenses one of which was frustration of purpose. Peoplesoft sought summary judgment that there was no such defense on these facts, and Softek opposed on grounds that an issue of facts existed. Should the trial court grant summary judgment? Write out your analysis. This case might be a sale of a good (if software is considered a good), but the UCC Article 2 has no doctrine of frustration of purpose, so the common law would apply.

Howard v. Nicholson, 556 S.W.2d 477 (Mo. App. 1977)

Howard promised to construct a building in accordance with certain plans and specifications provided by Honey's Int'l, Ltd. (Honey's), a chain of bridal salons. The building would not be suited for other uses. Howard had obtained the plans directly from Honey's; in fact, he had visited Honey's corporate offices several times in the hopes of landing construction contracts for Honey's salons. The building was to be built on land Honey's owned. Prior to signing a construction contract with Howard, the Nicholsons had signed a 20-year lease with Honey's for the premises. Howard and the Nicholsons signed a construction contract on November 6, 1969, with a completion date of May 1, 1970. Howard began demolition work but did not obtain building permits until March 6. By that date, it was impossible to complete construction by May 1 in time for the 1970 bridal season. This was the date that Honey's required occupancy. In the meantime, Honey's had financial problems. It filed for bankruptcy on December 16, 1969. It appears to have completely gone out of business shortly thereafter. What are the Nicholsons' chances of avoiding its obligation to pay for the construction? The lease?

D. Failure of Consideration

The defense of failure of consideration, recognized most often with respect to negotiable instruments and regarded by many courts as a matter of general contract law, is related to the defenses of impracticability and frustration—and also to breach. The materials on impracticability and frustration outlined how subsequent events can excuse the non-performance of a promise. We know also from the section on constructive conditions that failure to perform one of two bargained-for mutual promises may excuse non-performance of the other promise. Language describing "failure of consideration" is so general that the defense is broad enough to cover both kinds of excusing events. See, for example, the earlier case of *Taylor v. Fred Clark Felt Co.* (Chapter 6.A), where the phrase was meant to name a material breach excusing the nonbreaching party's nonperformance. Here, also, for another example, is language from a recent opinion; distinguishing lack of consideration, the court said:

> Failure of consideration, however, occurs when, due to a supervening cause after an agreement is reached, the promised performance fails. * * * * The distinction between the two is that lack of consideration exists, if at all, immediately after the execution of the contract while failure of consideration arises because of subsequent events. * * * * Thus, failure of consideration may result as a consequence of one party's failure to perform its obligations under the agreement, resulting in the other party's failure to receive the consideration set forth in the agreement.

City of The Colony v. North Texas Mun. Water Dist., 272 S.W.3d 699, 733 (Tex. App. 2008). The key to the language's generality is the verb "fails." The phrasing of the rule allows the cause of the failure to be either breach or something else.

Here are some cases that use the "failure of consideration" language. What is the cause or supposed cause of the failure in each?

Schaufelberger v. Mister Softee

Fla. App. (1972), 259 So.2d 175

OWEN, J.

[¶1] Appellee, the payee-holder of a promissory note made by Hoffman Company, Inc., brought this suit against appellant, as a guarantor of the note. The appeal is from an adverse final judgment entered upon a jury verdict. We reverse the judgment because the court erred in striking certain of appellant's affirmative defenses.

[¶2] Appellant, Irving A. Schaufelberger, was president of Hoffman Company, Inc., which had its place of business in Washington, D.C. Appellee, Mister Softee, Inc., a corporation with its principal offices located in New Jersey, sold Hoffman Company, Inc., four Mister Softee ice cream trucks for a total purchase price of approximately $53,000. Part of the purchase price of the trucks was paid by Hoffman Company, Inc.,

executing and delivering its promissory note for $10,000 payable to appellee at its offices in New Jersey. It is the guaranty of this note which is involved here. * * * *

[¶3] Some seven years after maturity this suit was filed. In his answer to the complaint, Schaufelberger set up various defenses, including among others, (1) failure of consideration for the guaranty contract * * * . On plaintiff's motion the court struck these two defenses, which order has been assigned as error and gives rise to the two points which we discuss.

[¶4] We turn first to the defense of the failure of consideration. While the answer was rather prolix, it alleged inferentially that (1) the principal contract (i.e., the note) and the contract of guaranty were part of the same transaction and supported by the same consideration, and (2) there was a partial failure of that consideration in that the ice cream trucks were delivered in a defective condition, at least one of which was returned to appellee and while in the latter's custody was totally demolished. Where the consideration for both the principal contract and the guaranty is the same, and the principal contract is divisible as this one, a partial failure of consideration is a defense on behalf of the guarantor to the extent of such failure. *See* 38 *C.J.S. Guaranty* § 27. It was error to strike this defense.

Jones v. Fuller-Garvey Corporation

AK (1963), 386 P.2d 838

AREND, Justice.

[¶1] This appeal comes to us upon an agreed statement in which the parties stipulate that the point to be relied upon by the appellant is this: "Did the Lower Court error [sic], under the facts of this case, in holding that the December 3, 1960 fire and consequent destruction of the building on the leased premises, brought the landlord-tenant relationship between the parties to an end and thereby discharged Fuller-Garvey [the tenant-appellee] from its obligation to pay $400.00 per month rent from December 1, 1960 through September 30, 1965 inclusive [the period stated representing the unexpired term under the lease]?"

[¶2] The facts * * * which we consider pertinent to the issue raised are as follows: By written lease the appellee corporation rented a nightclub from the appellant for a ten-year term commencing October 1, 1955. On November 5, 1960, the appellee, without legal justification, abandoned the premises. His rent at the time of the abandonment was paid through November, 1960. On December 3, 1960, the nightclub burned to the ground, apparently while unoccupied. The appellee let it be known that it would not move back onto the premises even if the nightclub were rebuilt. As for the appellant, he did not offer or intend to rebuild the nightclub.

[¶3] The appellant claimed that the appellee, in abandoning the nightclub, caused damage thereto in the sum of $6,850 by removing equipment and fixtures, which belonged to the appellant, and by leaving the building open so that all the plumbing froze. In addition to the damages mentioned, the appellant also

sought to recover rent at the rate of $400 per month for the entire unexpired term. The trial court gave judgment for damages in the amount claimed but allowed nothing by way of rent.

[¶4] The record contains a copy of the lease agreement which we have examined. We find therein no acceleration clause for payment of rent in the event of some breach of the agreement by the lessee. Nor does the lease contain any provision regarding the rights and obligations of the parties in case the demised building should be destroyed by a chance fire rendering it unfit for tenancy. The lease does state that it is entered into for the purpose of conducting a nightclub. It also provides that the "lessee will use due care against fire hazards" and that, if the lessee defaults in the payment of rent or fails to perform any of the conditions and covenants of the lease, the lessor may evict the lessee, declare the lease forfeited and retain all moneys paid as rent and liquidated damages.

[¶5] The general rule at common law is that a tenant remains under the obligation to pay rent to become due in the future, notwithstanding the destruction of the leased premises, so long as any part thereof remains in existence capable of being occupied or enjoyed by him. However, by the terms of the lease its purpose was for the conducting of a nightclub; and this fact places the instant case in the well recognized exception to the general rule that when the purpose of the lease is totally frustrated by a supervening event of which the lease says nothing, the lease shall be dissolved and the parties shall be excused from their obligations thereunder.

[¶6] Appellant's counsel contends that the exception should not be applied in this case for the reason that the tenant, the appellee, had tortiously abandoned the premises and was wrongfully out of possession when the fire occurred. We cannot subscribe to such reasoning if the appellant implies or infers by it that the fire would not have occurred but for the wrongful conduct of the appellee in abandoning the building. There is no factual basis in the stipulated record of this case to support such an inference. * * * *

[¶7] Neither can we subscribe to such reasoning if the appellant means thereby that the cause of action as to the future rental payments and the damages thereon became fixed on the date of the abandonment. This would in effect be asking this court to apply the doctrine of anticipatory breach to the lease contract. If we were to consider the appellee's abandonment as an anticipatory breach of the lease contract, the appellant still could not recover damages for that future period after the fire, for evidence became available after the cause of action arose, but prior to judgment thereon, of the supervening impossibility which constituted a complete failure of consideration for all rent due in the future. The loss should rest where chance has placed it. The fire destroyed any cause of action as to anticipatory breach that the appellant had. * * * *

Judgment affirmed.

Godwin v. Cooper

N.C. (1947), 41 S.E. 2d 734

Per Curiam.

Plaintiff declared on two checks issued by defendant and delivered to plaintiff in payment for a stock of goods and the assignment of a written lease on the store building in which the goods were housed. Defendant admitted giving the checks, but alleged as an affirmative defense that the lease was invalid, and that consequently there was a failure of consideration. However, no defects appear on the face of the lease, nor are any facts alleged in the answer which would render the lease invalid. The court below entered judgment in favor of the plaintiff on the pleadings, and on the record before us that ruling must be upheld and the judgment

Affirmed.

Note: The UCC Article 2 has additional provisions besides impracticability and not-displaced-by-the-code, common-law frustration of purpose doctrine that impact what would otherwise be supervening events. The code at sections 2-509 and 2-510 specifically and clearly says who bears the risk of loss that occurs during shipping and when that risk shifts from seller to buyer.

Chapter 14. Remedies

We saw an introduction to contract breach remedies earlier, and the casebook provided some rules. They are quite workable formulations, and you are welcome to use them. Please refresh your memory by reading them again with other details here:

Damages

Damages are substitutional as opposed to specific remedies. Damages mean to substitute an award of money for a measure of harm: the value of a contractual performance, loss from reliance on a contract, or a value conferred on the breaching party. Damages were originally awarded in the law courts.

Expectation Damages: a sum of money intended to place the non-breaching party in the position that party would have been in had the promise at issue been performed.

Reliance Damages: a sum of money intended to place the non-breaching party in the position that party would have been in had the promise at issue not been made. Generally, two kinds of costs to the non-breaching party form a basis for reliance damages: out-of-pocket costs—direct net costs incurred by a promisee in reliance on a promise prior to breach; and opportunity costs—indirect net value that the promisee would have enjoyed if the promisee had taken an opportunity that the promise led the promisee to forego.

Restitution Damages: an order that the promisor pay a sum of money equal in value to the benefit that has been conferred by the injured party on the promisor. The general purpose of restitution damages for breach of contract is to put the party in breach back in the position it would have been in had the contract not been made.

While the law provides three measures of damages, double recovery is not allowed. For example, consider a case in which a property owner breaches a contract with a home builder by refusing to pay for a completed home after the owner takes possession. Expectation would be the contract price. Reliance would include the cost of building the home. Restitution would require that the breaching owner pay the value of the home. All these measures are a way to quantify the harm to the builder from the breach, but the builder will not be able to obtain all three measures of damages. The builder's contract rights are arguably worth each of these—but not all three together.

In practice, then, the plaintiff will frequently seek the highest amount of damages that the plaintiff believes will be supported by the evidence. That is often expectation, and expectation is often the highest amount because contracting parties normally contract to obtain more than their performance costs them (for instance, the home builder promises to build a home in exchange for $400,000, but the home only costs the builder $350,000 to build; the other $50,000 is profit). However, if expectation is for some reason not available or not chosen, courts award damages according to another damages rule. Plaintiffs who prove harm from breach are allowed to recover "'all damages which are the normal and foreseeable results of a

breach of contract.'" *Harrison v. Am. Airlines, Inc*., 760 F. Supp. 3d 545, 568 (M.D. Tenn. 2024) (quoting *Morrow v. Jones*, 165 S.W.3d 254, 259 (Tenn. Ct. App. 2004)). Normal and foreseeable results of a breach usually include the harms measured by these different damages standards. Courts therefore can and do award plaintiffs damages from more than one category, if there is not overlap.

Relatedly, courts often do not let a breach victim obtain more in contract damages than expectation. They reason that a damage award should not make the breach victim better off than the victim would have been had the promise been performed. Courts therefore routinely cap reliance damages at the amount of expectation and often cap restitution likewise (as we saw in *Britton v. Turner* (Chapter 12.D) but not always, as *Satchell v. Van Brode* (right after *Britton*) shows.

Equitable Remedies

Equitable remedies were originally awarded by the chancellor, in equity. In jurisdictions where law and equity are merged (or states like Texas where they were never separate), law courts administer equitable remedies.

Injunction: a court's order that a party do or not do something other than pay money damages. For example, in certain, special cases, a court may order specific (as opposed to substitutional) performance, that the promisor perform as promised. In other cases, a court may order that a party to a contract refrain from interfering with another party's performance. Courts often say that injunctive relief is inappropriate when legal remedies adequately compensate the plaintiff. The prototypical case in which damages are inadequate and specific performance is appropriate occurs when a promisor breaches a promise to sell land, because each piece of land is unique and determining the appropriate amount of damages involves too much speculation.

Declaratory Relief: a court's statement of a party's legal rights. For example, a court may state that a contract is void or voidable (rescindable) at the option of one or either party, or rescinded.

Rescission: Rescission means the undoing or canceling of a contract. It may be done by agreement as described in *Schwartzreich*, at law by a party with a right to rescind, or in equity. Rescission at law and in equity were described in the Contract Law Meta Rules. Rescission at law was attempted in *Sherwood v. Walker* and was successfully done in *First Baptist Church of Moultrie v. Barber Contracting Co*. (remember Barber's bid and bond were contracts) and *Gearhart v. Goehner*.

A. Damages

1. Are Damages Necessary? Of Nominal Damages

Some courts say loosely that damages are an element of a breach case. But contract duties are chosen by the parties, not imposed by the state, and respect for those duties requires that courts recognize them even

though breach causes no cognizable damages. After all, breach may be ongoing, and the plaintiff's interest may be in having the defendant perform. The following view expressed by a Texas court is closer to the truth:

> [¶1] In its motion for JMOL [judgment as a matter of law] or a new trial on the breach of contract claim due to lack of injury (Dkt. No. 351), Versata argues that Autodata failed to prove that it suffered monetary damages on its breach of contract claim and that the jury's award of $1 in nominal damages was therefore improper. * * * *
>
> [¶2] Versata first argues that proof of damages is an essential element of an action for breach of contract under Texas law and that because Autodata did not offer evidence that it was entitled to money damages, its cause of action for contract breach failed. Contrary to Versata's statement, however, it is proof of injury that is an essential element of a contract breach under Texas law, not proof of "damages." In contract cases, injury (or "damage") can often be remedied only by an award of "damages," and often only money damages are sought. If that is the case, proof of money damages is, of course, essential to recovery. But monetary relief is not invariably the objective of breach of contract claims. As long as there is injury from the breach, liability attaches under Texas law * * * * . * * * * A claim for breach of contract in which actual damages are not the sole objective therefore does not fail because of the plaintiff's inability to prove monetary loss and entitlement to an award of damages.
>
> [¶3] Prior to trial, Autodata asserted that Versata's contract breaches were material and had caused harm to Autodata, and that it would seek an injunction against the use of Autodata's confidential and trade secret information, and an award of attorney's fees. Autodata did not assert that it would seek an award of monetary damages if it were able to prove the alleged breaches. Consistently with that position, Autodata did not seek actual damages for the breach at trial. Instead, Autodata sought nominal damages of $1, which the jury awarded. Autodata then sought equitable relief from the Court, as it had earlier indicated that it intended to do.
>
> [¶4] Versata argues that because Autodata did not seek, and did not prove, actual monetary damages, Autodata failed to satisfy one of the essential elements of breach of contract under Texas law. The Court disagrees. The jury was instructed that in order to rule in favor of Autodata on the breach of contract claim, it had to find that Versata's breach caused injury to Autodata. Autodata's evidence regarding the misappropriation of its confidential information was sufficient to support the jury's conclusion that the contract breach injured Autodata. In particular, the jury could have concluded, based on testimony from Autodata's employees, that Autodata was harmed by Versata's acts of depriving Autodata of the benefits of exclusive control over and use of its trade secrets and using the information to obtain patents that were asserted against Autodata, even though Autodata was not able to quantify its injury so as to establish a right to actual monetary damages. * * * * Versata's argument that Autodata failed to prove breach of contract therefore fails.
>
> [¶5] Versata's second, and related, argument is that because Autodata did not prove actual damages, it was not entitled to nominal damages on its breach of contract claim. Again, the Court disagrees. As the Texas Supreme Court wrote recently, "nominal damages

are available for breach of contract, as this Court has stated at least a dozen times." *MBM Fin. Corp. v. Woodlands Operating Co.*, 292 S.W.3d 660, 664 (Tex.2009). The court in the MBM case explained that nominal damages are available in situations in which a legal injury is suffered yet "there is no substantial loss or injury to be compensated." 292 S.W.3d 660, 665 n. 19 (Tex.2009); *see also Trevino v. Sw. Bell Tel. Co.*, 582 S.W.2d 582, 584 (Tex. Civ. App.1979) ("Nominal damages are those damages recoverable where a legal right is to be vindicated against an invasion that produced no actual loss, or where, from the very nature of the case, some injury has been done, the amount of which the proof fails to show.").

[¶6] It is true, as Versata points out, that Texas courts have held that nominal damages are not appropriate "when the harm is entirely economic and subject to proof" but the plaintiff fails to prove the amount of its loss. *MBM Fin.*, 292 S.W.3d at 665; *see also Intercont'l Grp.*, 295 S.W.3d at 660 ("[A] breach-of-contract plaintiff who seeks nothing beyond economic damages cannot receive a judgment based on breach alone."); * * *. But the unauthorized disclosure of confidential information is a type of harm that can have consequences that are not readily measurable in the form of monetary loss. In such cases, non-monetary relief can be appropriate, and Autodata made clear that it was requesting such non-monetary relief for the contract breach in this case. This is therefore not a case in which the asserted harm was purely economic and the party seeking relief simply failed to prove the amount of its loss.

Versata Software, Inc. v. Internet Brands, Inc., 902 F. Supp. 2d 841, 858–60 (E.D. Tex. 2012), aff'd, 550 F. App'x 897 (Fed. Cir. 2014).

2. Expectation

American Standard, Inc. v. Schectman

Supreme Court of New York, App. Div. (1981), 439 N.Y.S.2d 529

HANCOCK, JR., J.

[¶1] Plaintiffs have recovered a judgment on a jury verdict of $90,000 against defendant for his failure to complete grading and to take out certain foundations and other subsurface structures to one foot below the grade line as promised. Whether the court should have charged the jury, as defendant Schectman requested, that the difference in value of plaintiffs' property with and without the promised performance was the measure of the damage is the main point in his appeal. We hold that the request was properly denied and that the cost of completion—not the difference in value—was the proper measure. Finding no basis for reversal, we affirm.

[¶2] Until 1972, plaintiffs operated a pig iron manufacturing plant on land abutting the Niagara River in Tonawanda. On the 26-acre parcel were, in addition to various industrial and office buildings, a 60-ton blast furnace, large lifts, hoists and other equipment for transporting and storing ore, railroad tracks, cranes,

diesel locomotives and sundry implements and devices used in the business. Since the 1870's plaintiffs' property, under several different owners, had been the site of various industrial operations. Having decided to close the plant, plaintiffs on August 3, 1973 made a contract in which they agreed to convey the buildings and other structures and most of the equipment to defendant, a demolition and excavating contractor, in return for defendant's payment of $275,000 and his promise to remove the equipment, demolish the structures and grade the property as specified.

[¶3] We agree with Trial Term's interpretation of the contract as requiring defendant to remove all foundations, piers, headwalls, and other structures, including those under the surface and not visible and whether or not shown on the map attached to the contract, to a depth of approximately one foot below the specified grade lines. The proof from plaintiffs' witnesses and the exhibits, showing a substantial deviation from the required grade lines and the existence above grade of walls, foundations and other structures, support the finding, implicit in the jury's verdict, that defendant failed to perform as agreed. Indeed, the testimony of defendant's witnesses and the position he has taken during his performance of the contract and throughout this litigation (which the trial court properly rejected), *viz.*, that the contract did not require him to remove all subsurface foundations, allow no other conclusion.

[¶4] We turn to defendant's argument that the court erred in rejecting his proof that plaintiffs suffered no loss by reason of the breach because it makes no difference in the value of the property whether the old foundations are at grade or one foot below grade and in denying his offer to show that plaintiffs succeeded in selling the property for $183,000—only $3,000 less than its full fair market value. By refusing this testimony and charging the jury that the cost of completion (estimated at $110,500 by plaintiffs' expert), not diminution in value of the property, was the measure of damage the court, defendant contends, has unjustly permitted plaintiffs to reap a windfall at his expense. Citing the definitive opinion of Judge Cardozo in *Jacob & Youngs v. Kent* (230 NY 239), he maintains that the facts present a case "of substantial performance" of the contract with omissions of "trivial or inappreciable importance" and that because the cost of completion was "grossly and unfairly out of proportion to the good to be attained," the proper measure of damage is diminution in value.

[¶5] The general rule of damages for breach of a construction contract is that the injured party may recover those damages which are the direct, natural and immediate consequence of the breach and which can reasonably be said to have been in the contemplation of the parties when the contract was made (*see* 13 *NY Jur, Damages,* §§ 46, 56; *Chamberlain v. Parker,* 45 NY 569; *Hadley v. Baxendale*, 9 Exch [Welsby, Hurlstone & Gordon] 341; *Restatement, Contracts*, § 346). In the usual case where the contractor's performance has been defective or incomplete, the reasonable cost of replacement or completion is the measure (*see Bellizzi v. Huntley Estates*, 3 NY2d 112; *Spence v. Ham*, 163 NY 220; *Condello v. Stock*, 285 App Div 861, mod on other grounds 1 NY2d 831; *Along-The-Hudson Co. v. Ayres*, 170 App Div 218; 13 *NY Jur, Damages*, § 56, p 502; *Restatement, Contracts*, § 346). When, however, there has been a substantial performance of the contract made in good faith but defects exist, the correction of which would result in economic waste, courts have measured the damages as the difference between the value of the property as constructed and the value if performance had been properly completed (*see Jacob & Youngs v. Kent, supra*; *Droher & Sons v. Toushin*, 250 Minn 490; *Restatement, Contracts*, § 346, subd [1], par [a], cl [ii], p 573; comment b, p 574; 13 *NY Jur, Damages*, § 58; Ann., 76 ALR2d 805, § 4, pp 812-815). *Jacob & Youngs* is illustrative. There, plaintiff, a contractor, had constructed a house for the defendant which was satisfactory in all respects save one: the wrought iron pipe installed for the plumbing was not of Reading manufacture, as specified in the contract, but of other brands of the same quality. Noting that the breach was unintentional and the consequences of the omission trivial, and that the cost of replacing the pipe would be "grievously

out of proportion" (*Jacob & Youngs v. Kent, supra*, p 244) to the significance of the default, the court held the breach to be immaterial and the proper measure of damage to the owner to be not the cost of replacing the pipe but the nominal difference in value of the house with and without the Reading pipe.

[¶6] Not in all cases of claimed "economic waste" where the cost of completing performance of the contract would be large and out of proportion to the resultant benefit to the property have the courts adopted diminution in value as the measure of damage. Under the Restatement rule, the completion of the contract must involve "unreasonable economic waste" and the illustrative example given is that of a house built with pipe different in name but equal in quality to the brand stipulated in the contract as in *Jacob & Youngs v. Kent* (230 NY 239, *supra*) (*Restatement, Contracts*, § 346, subd [1], par [a], cl [ii], p 573; Illustration No. 2, p 576). In *Groves v. Wunder Co*. (205 Minn. 163), plaintiff had leased property and conveyed a gravel plant to defendant in exchange for a sum of money and for defendant's commitment to return the property to plaintiff at the end of the term at a specified grade—a promise defendant failed to perform. Although the cost of the fill to complete the grading was $60,000 and the total value of the property, graded as specified in the contract, only $12,160 the court rejected the "diminution in value" rule, stating:

> "The owner's right to improve his property is not trammeled by its small value. It is his right to erect thereon structures which will reduce its value. If that be the result, it can be of no aid to any contractor who declines performance. As said long ago in Chamberlain Parker, 45 N.Y. 569, 572: 'A man may do what he will with his own, . . . and if he chooses to erect a monument to his caprice or folly on his premises, and employs and pays another to do it, it does not lie with a defendant who has been so employed and paid for building it, to say that his own performance would not be beneficial to the plaintiff.'"

(*Groves v. Wunder Co., supra*, p 168.)

[¶7] The "economic waste" of the type which calls for application of the "diminution in value" rule generally entails defects in construction which are irremediable or which may not be repaired without a substantial tearing down of the structure as in *Jacob & Youngs* (*see Bellizzi v. Huntley Estates*, 3 NY2d 112, 115, *supra*; *Groves v. Wunder Co., supra*; *Slugg Seed & Fertilizer v. Paulson Lbr.,* 62 Wis 2d 220; *Restatement, Contracts*, § 346, subd [1], Illustration Nos. 2, 4, pp 576-577; Ann., 76 *ALR2d* 805, § 4, pp 812-815).

[¶8] Where, however, the breach is of a covenant which is only incidental to the main purpose of the contract and completion would be disproportionately costly, courts have applied the diminution in value measure even where no destruction of the work is entailed (*see, e.g., Peevyhouse v. Garland Coal & Min. Co.,* 382 P2d 109 [Okla], cert. denied, 375 U.S. 906, holding [contrary *to Groves v. Wunder Co., supra*] that diminution in value is the proper measure where defendant, the lessee of plaintiff's lands under a coal mining lease, failed to perform costly remedial and restorative work on the land at the termination of the lease. The court distinguished the "building and construction" cases and noted that the breach was of a covenant incidental to the main purpose of the contract which was the recovery of coal from the premises to the benefit of both parties; and *see Avery v. Fredericksen & Westbrook,* 67 Cal App 2d 334).

[¶9] It is also a general rule in building and construction cases, at least under *Jacob & Youngs (supra)* in New York (*see Groves v. Wunder Co., supra*; Ann., 76 *ALR2d* 805, § 6, pp 823-826), that a contractor who would ask the court to apply the diminution of value measure "as an instrument of justice" must not have breached the contract intentionally and must show substantial performance made in good faith (*Jacob & Youngs v. Kent, supra,* pp 244, 245).

[¶10] In the case before us, plaintiffs chose to accept as part of the consideration for the promised conveyance of their valuable plant and machines to defendant his agreement to grade the property as specified and to remove the foundations, piers and other structures to a depth of one foot below grade to prepare the property for sale. It cannot be said that the grading and the removal of the structures were incidental to plaintiffs' purpose of "achieving a reasonably attractive vacant plot for resale" *(cf. Peevyhouse v. Garland Coal & Min. Co., supra).* Nor can defendant maintain that the damages which would naturally flow from his failure to do the grading and removal work and which could reasonably be said to have been in the contemplation of the parties when the contract was made would not be the reasonable cost of completion (see 13 *NY Jur, Damages*, §§ 46, 56; *Hadley v. Baxendale*, 9 Exch [Welsby, Hurlstone & Gordon] 341, *supra*). That the fulfillment of defendant's promise would (contrary to plaintiffs' apparent expectations) add little or nothing to the sale value of the property does not excuse the default.

[¶11] As in the hypothetical case, posed in *Chamberlain v. Parker* (45 NY 569, *supra*) (*cited in Groves v. Wunder Co*., 205 Minn 163, *supra*), of the man who "chooses to erect a monument to his caprice or folly on his premises, and employs and pays another to do it", it does not lie with defendant here who has received consideration for his promise to do the work "to say that his own performance would not be beneficial to the [plaintiffs]" (*Chamberlain v. Parker, supra*, p 572).

[¶12] Defendant's completed performance would not have involved undoing what in good faith was done improperly but only doing what was promised and left undone (*cf. Jacob & Youngs v. Kent,* 230 NY 239, *supra*; *Restatement, Contracts*, § 346, subd [1], Illustration No. 2, p 576). That the burdens of performance were heavier than anticipated and the cost of completion disproportionate to the end to be obtained does not, without more, alter the rule that the measure of plaintiffs' damage is the cost of completion. Disparity in relative economic benefits is not the equivalent of "economic waste" which will invoke the rule in *Jacob & Youngs v. Kent (supra) (see Groves v. Wunder Co., supra).* Moreover, faced with the jury's finding that the reasonable cost of removing the large concrete and stone walls and other structures extending above grade was $90,000, defendant can hardly assert that he has rendered substantial performance of the contract or that what he left unfinished was "of trivial or inappreciable importance" (*Jacob & Youngs v. Kent, supra,* p 245). Finally, defendant, instead of attempting in good faith to complete the removal of the underground structures, contended that he was not obliged by the contract to do so and, thus, cannot claim to be a "transgressor whose default is unintentional and trivial [and who] may hope for mercy if he will offer atonement for his wrong" (*Jacob & Youngs v. Kent, supra*, p 244). We conclude, therefore, that the proof pertaining to the value of plaintiffs' property was properly rejected and the jury correctly charged on damages.

[¶13] The judgment and order should be affirmed.

Questions:

1. Do you think that American Standard or the new owner used the money to tear out the foundations and regrade the property?

2. Suppose that the breach of the contract was for leaving a building standing rather than just failing to tear out foundations, and that prior to the sale of the property the vacant building was used by a young movie producer to shoot a movie. Suppose further that the movie comes out and is a tremendous hit before it is time for Schectman to tear down the building, and Schectman decides not to tear down the building because the purchaser of the property wants to build a dance and comedy club in it. Because of these novel events, the price of the sale is $286,000, over $100,000 more than the appraised price of the lot. With these added facts, should American Standard be awarded diminution in value or cost of completion?

3. Suppose Jean, whose residential lot in the back borders the local state courthouse lot, wants artist Mark to build a statue in her backyard called “salute to waste.” In Mark’s model, the statue is twelve feet tall and five feet wide. It is to be covered with non-biodegradable waste materials—various plastic items, including milk cartons, fast food restaurant straws and drink covers, garbage bags; various metal items, including broken appliances and parts of appliances; various rubber items, including bald tires, of course; and broken glass. In addition to the monument itself, various similar items of garbage are to be attached to the ground around the monument. Jean is to pay Mark $20,000 for the statue. Mark is only one of two garbage artists working in the state. Now suppose Mark repents and refuses to complete it after he is half done. The other, more well-known artist, Oscar, will complete the job for no less than $25,000. In fact, the salute to waste had decreased the value of the property considerably, as well as that of neighboring properties. Jean has sued Mark for breach. What should a court do?

4. Why can’t the court in *American Standard* fix an intermediate amount that is fair?

Rivers v. Deane

Supreme Court of New York, App. Div. (1994), 619 N.Y.S.2d 419

[¶1] Judgment unanimously modified on the law and as modified affirmed without costs and matter remitted to Supreme Court for further proceedings in accordance with the following Memorandum: Defendant appeals from a judgment of Supreme Court awarding plaintiffs damages for defendant’s breach of contract for the construction of an addition to plaintiffs’ home. Defendant in his brief challenges only that aspect of the judgment that awarded damages to plaintiffs for the difference between the market value of the structure had it been completed pursuant to the terms of the contract and the market value of the structure as actually completed. We agree with defendant’s assertion that the record does not support the court’s award for diminution in value, because no such proof was presented.

[¶2] At trial plaintiffs produced two experts who testified that defendant failed to construct the addition in a good and workmanlike manner. They further testified that the inadequate structural support of the addition rendered unusable the third floor of the addition, which plaintiffs had intended to use as a master bedroom and bathroom. The appeal by defendant, as limited by his brief (*see, Ciesinski v Town of Aurora*, 202 A.D.2d 984; *Hodge v LoRusso*, 181 A.D.2d 1009), does not contest those findings of fact.

[¶3] The general rule in cases of faulty construction is that the measure of damages is the market value of the cost to repair the faulty construction (*see, American Std. v Schectman*, 80 A.D.2d 318, lv denied 54

N.Y.2d 604). The court erred in applying the “difference in value rule”, as initially set forth by Justice Cardozo in *Jacob & Youngs v Kent* (230 N.Y. 239, 241), which is limited to instances where the builder’s failure to perform under a construction contract is “both trivial and innocent”, such that damages may be measured by the diminution in value of the building rather than the cost of tearing apart the structure and properly completing the project. Where, as here, the defect arising from the breach of the contract “is so substantial as to render the finished building partially unusable and unsafe, the measure of damage is ‘the market price of completing or correcting the performance’” (*Bellizzi v Huntley Estates,* 3 N.Y.2d 112, 115, quoting 5 *Williston, Contracts* § 1363, at 3825 [rev ed]). Thus, on the facts found by the court, plaintiffs are entitled to the market value of the cost of correcting the deficiencies in the addition arising from defendant’s breach.

[¶4] The trier of fact is in the best position to evaluate the credibility of the witnesses, who gave conflicting testimony concerning the cost of repair to the addition. Therefore, we modify the judgment appealed from by vacating the court’s award of $10,000 for diminution in value due to inadequate structural support, and we remit the matter to Supreme Court for further findings of fact on the actual cost of repair for inadequate structural support and direct that judgment be entered accordingly.

[¶5] Judgment unanimously modified on the law and as modified affirmed without costs and matter remitted to Supreme Court for further proceedings.

Questions:

1. What is the general rule?

2. Did the builder substantially perform?

3. In *Jacob & Youngs v. Kent* the contractor wanted diminution of value to be the measure of damages, not cost of completion of the structure according to the contract. In this case, the contractor wants the opposite. Why was the construction company here wanting to change the measure to cost of repair from diminution in value, do you think?

4. Suppose the owner collects repair costs because they are greater than diminution, and then sells the property. If the owner collects repair costs because they are greater than diminution in value, and then sells the property, doesn’t the owner get a windfall?

5. Read again *New Era Homes v. Foster*. Is the damage formula in that case consistent with the formula in this case?

3. Reliance

BECO CONSTRUCTION COMPANY, INC. v. HARPER CONTRACTING, INC.

Idaho App. (1997), 936 P.2d 202

[¶1] In this appeal we are asked to review the district court's order denying motions for directed verdict, judgment notwithstanding the verdict and new trial. * * * * We affirm.

I.

FACTS AND PROCEDURE

[¶2] Harper Contracting, Inc., was a subcontractor involved in the construction of a prison in Ely, Nevada. The general contractor, Layton Construction, contacted Beco Construction Co., Inc., regarding the placement of asphalt at the prison construction site. Harper, relying on a proposal submitted by Beco to Layton, hired Beco to produce and lay asphalt for the site. Beco prepared gravel and provided gravel testing, but did not place the asphalt. The parties terminated their relationship, and Beco filed a complaint seeking compensation from Harper for the gravel and gravel testing. Beco's complaint alleged that Harper owed money to Beco "on open account."

[¶3] During a hearing on a motion in limine, Harper moved to exclude evidence regarding the circumstances surrounding the termination of the asphalt contract. The district court granted the motion in part, but indicated it would allow information regarding the termination of the contract to be introduced as evidence relating to impeachment, credibility or perspective. The case then proceeded to trial before a jury. After Beco rested its case, Harper moved for a directed verdict. The district court denied the motion, stating that the question at issue was whether there was a contract, and that substantial evidence existed which justified submission of the issue to the jury.

[¶4] At the conclusion of the trial, the jury returned a verdict which was internally inconsistent. The jury found that Beco had waived its right to reimbursement for the testing services and then went on to award damages to Beco for those services. After discussion with counsel, and over the objection of Harper, the district court refused the verdict and asked the jury to continue its deliberations. The jury later returned a consistent verdict awarding Beco $1,484.20 for the testing services and $6,412.50 for the gravel. Harper then filed a motion for judgment notwithstanding the verdict (j.n.o.v.) or, in the alternative, for a new trial. The district court denied the motion. * * * *

[¶5] Harper appeals, claiming that the district court erred in denying the motions for directed verdict, j.n.o.v. and new trial. * * * *

II.

ANALYSIS

A. Direct Appeal Issues * * * *

(2) J.N.O.V.

[¶6] After the completion of the trial, Harper moved for a j.n.o.v., I.R.C.P. 50(b), or, in the alternative, for a new trial, I.R.C.P. 59(a). In considering the district court's denial of Harper's j.n.o.v. motion, this Court is to review the record of the trial court and determine whether, as a matter of law, there was sufficient evidence upon which reasonable jurors could return a verdict in favor of the plaintiffs; or, as stated by our Supreme Court, whether "there can be but one conclusion as to the verdict that reasonable minds could have reached." * * * *

[¶7] On appeal, Harper argues that no contract issues could be raised at trial for two reasons: (1) Beco's complaint sought compensation on a non-contract theory, open account, and Harper never consented to try another issue; and (2) the district court's order on Harper's motion in limine limited the scope of the trial. Harper also claims that regardless of the nature of the claim, Beco failed to provide sufficient evidence to support the jury's verdict or award.

[¶8] We note, first, that Harper seems to misapprehend the nature of an open account. Harper argues that Beco provided inadequate notice that a contract claim would be pursued at trial; however, the very basis of the action was a contract claim. An open account refers to a continuing series of transactions between the parties, where the balance is unascertained and future transactions between the parties are expected. *Seubert Excavators, Inc. v. Eucon Corp.*, 125 Idaho 409, 415, 871 P.2d 826, 832 (1994). Although an open account is a particularized type of contract claim, it is a contract claim. Harper had notice that a contract claim would be presented to the jury. Therefore, Harper's "consent" to try a contract claim was not required. * * * *

[¶9] Beco sought recovery of the out-of-pocket expenses incurred in anticipation of performance of the contract with Harper. A party aggrieved by a breach of contract may be entitled to reimbursement for losses caused by its reliance on the contract, even if the aggrieved party elects to rescind the contract. *Brown v. Yacht Club of Coeur d'Alene, Ltd.,* 111 Idaho 195, 198, 722 P.2d 1062, 1065 (Ct.App.1986). Reliance damages include expenses reasonably related to the purposes of the contract which would not have been incurred but for the contract's existence. *Id.* at 198-200, 722 P.2d at 1065-1067. Beco's evidence showed that it incurred expenses in crushing and testing gravel in preparation for performance of the asphalt contract. After a thorough review of the record, we conclude that there was substantial competent evidence to support the jury's verdict that Harper was obligated to pay Beco for the crushing and testing of gravel.

[¶10] Harper claims that the amount of the jury award was unsupported in the record. Beco's prayer for relief sought compensation for 1,200 tons of gravel. However, Beco's president, Doyle Beck, testified that Beco estimated 1,500 tons of asphalt would be needed for the prison construction job. He further testified that approximately ninety-five percent of the weight of asphalt can be attributed to the gravel. According to Beck's testimony, 1,425 tons of gravel would be needed for the production of asphalt for the prison site. Beck indicated that Beco had actually prepared 1,700 to 1,800 tons of gravel. When asked why Beco only billed Harper for 1,200 tons, Beck explained:

> That was still, in my mind, at that point I didn't know for sure how many tons it was going to take. Okay. I didn't want to bill for something that could be disputed.
>
> In situations like this if we get enough to cover the diesel fuel and labor and some raw expenses, that's really all we want at that point.

[¶11] Evidence presented at trial also indicated that the cost to Beco for crushing gravel was approximately $4.50 per ton or higher and that this was a competitive price. The jury awarded $6,412.50, the product of 1,425 tons multiplied by $4.50 per ton. Thus, there was substantial competent evidence in the record to support the amount of the jury's verdict.* * * *

III.

CONCLUSION

[¶12] The district court correctly perceived that the parties tried a simple contract claim and that Harper had adequate notice of that fact. Further, the district court properly determined that there was sufficient, competent evidence to support the jury's verdict, including the amount of the award. * * * *

Questions:

1. What is the difference between expectation and reliance damages? Can you state the difference succinctly?

2. Given that expectation gives what it does, one might suspect most parties would prefer it; it reflects the value of the parties' bargain. Why do the courts grant Beco reliance damages instead of expectation, according to this opinion?

3. Are reliance damages available even for costs incurred in preparing to perform?

4. For what amount of gravel did Beco bill Harper? For what amount did it actually incur costs? For what amount did the jury actually award damages?

5. Courts hold fast to the rule that reliance damages should be capped at the contract price:

> The district court suggested that its award of the $500,000 payment might alternatively be appropriate pursuant to the doctrine of reliance damages. Under this doctrine, a plaintiff may recover "his expenses of preparation and of part performance, as well as other foreseeable expenses incurred in reliance upon the contract." J. Calimari & J. Perillo, *Contracts* § 14–9, at 603 (3d ed. 1987); *see also L. Albert & Son v. Armstrong Rubber Co.,* 178 F.2d 182, 190–91 (2d Cir.1949). However, the alternative reliance "measure of damages rests on the premise that the injured party's reliance interest is no greater than the party's expectation interest." 3 Farnsworth, *supra,* § 12.16, at 265. And courts will not "knowingly put the plaintiff [receiving a reliance recovery] in a better position than he would have occupied had the contract been fully performed." Fuller & Perdue, *The Reliance Interest in Contract Damages (Pt. 1),* 46 Yale L.J. 52, 59 (1936); *see L. Albert & Son,* 178 F.2d at 191. Thus, a reliance recovery will be offset by the amount of "any loss that the party in breach can prove with reasonable certainty the injured party would have suffered had the contract been fully performed." *Restatement (Second) of Contracts* § 349 (1979); * * * . If the breaching party establishes that the plaintiff's losses upon full performance

> would have equalled or exceeded its reliance expenditures, the plaintiff will recover nothing under a reliance theory.

Bausch & Lomb Inc. v. Bressler, 977 F.2d 720, 729 (2d Cir. 1992). In *Beco Construction*, the defendant did not even attempt to show that the plaintiff would have lost money had the defendant fully performed. But a hypothetical somewhat similar to the one after *Britton v. Turner* (above Chapter 12.D, where the court capped restitution damages for the breaching party at the contract price) illustrates the concept: Owner hires Contractor to build a house for $100. Contractor while building discovers the house will cost $120 to build. If Owner breaches after Contractor has built $115 worth of house, should Contractor collect $115 in damages? The rule from *L. Albert & Sons* and R2K § 349 requires the $115 to be offset by the amount that "the injured party would have suffered had the contract been fully performed." The $20 loss, if Owner proves it, would be subtracted from the $115, and Contractor awarded $95. This is the contract amount less the $5 cost saved by not having to build the last $5 of house. The rule thus prevents Contractor from obtaining more than Contractor bargained for. If the rule were otherwise, how would Contractor's incentives change? Do you think it is possible that Contractor would at some point want to encourage Owner to breach? Inducing breach is a tricky social move, but reports of it occur in litigation from time to time.

Note: Damages for Promissory Estoppel

Are expectation damages recoverable under promissory estoppel? Some states (Texas, Indiana) say no. Others are less committed to a limitation. Look back at the promissory estoppel cases earlier in the book. In *Ricketts*, the court granted the face amount of the note. Is that an expectation measure? In *Concannon*, the court ordered the landlord to perform. What kind of remedy is that? In *Grouse*, the measure of damages awarded is in the question after the case. What is that? In *G.D. Holdings*, the court affirmed the trial court's award of $27,390, for what? Is that expectation or something else?

In general, there is no clear national rule. Which rule holds in a state may depend in part on what fact pattern first required the courts in that state to address the issue. Here are two more examples:

ZBS Indus., Inc. v. Anthony Cocca Videoland, Inc., 93 Ohio App. 3d 101 (1994): Z promised to supply Videoland with 1k movies per month at $60 per movie for two years. Videoland could rent those movies to movie watchers for $2 per day for 45 days. Blockbuster had agreed to buy 1k used movies each month from Videoland at $30 per movie. When Z breached the promise, Videoland lost the profits it was making from Blockbuster. The court granted these lost profits in a promissory estoppel case. Was that expectation or reliance?

I.G. Katz v. Danny Dare, Inc., 610 S.W.2d 121 (Mo. App. 1981): Katz had a job at corporation but was older. Corporation wanted Katz to retire but for internal political reasons did not want to fire him. So corporation offered Katz a pension if he would retire. The pension amount was less than the wages he was giving up, but Katz was older and slowing down, and the pension amount was sufficient for him to live, with social security. Katz quit and took the pension. In this case, the court granted the amount of the pension as the remedy—expectation.

4. Restitution

David O. JOHNSON v. John W. BOVEE and Alice M. Bovee

Colo. App. (1978), 574 P.2d 513

PIERCE, J.

[¶1] Plaintiff, David O. Johnson, doing business as David O. Johnson Construction Company, appeals a judgment of the trial court entered in his favor and against John and Alice Bovee, arguing that the court erred in its measure of damages. We disagree, and affirm the judgment in its entirety.

[¶2] The Bovees and Johnson entered into a written contract under which Johnson agreed to build a house for the Bovees according to a specified set of plans, in exchange for a contract price of $47,176. During the course of the house's construction, Johnson and the Bovees orally agreed to many deviations from the original plans—resulting in both additions ("extras") and deletions.

[¶3] The Bovees became dissatisfied with the quality of the construction. They then stopped making payments to Johnson and his suppliers, payments which were required under the contract. Johnson therefore stopped working on the house, and filed this suit to foreclose on his mechanic's lien. The Bovees, who finished the house, counterclaimed for the costs of repairing the defective workmanship.

[¶4] The trial court found that Johnson had substantially performed his obligations under the contract and therefore that the Bovees' refusal to make payments constituted a breach. It also found that the house was 90% complete when construction stopped. The damages awarded to Johnson were based on the contract price and were calculated in the following manner:

Contract price	. . . .. $47,176.00
Net value of the agreed extras	. . . .. 7,700.78
Payments made by the Bovees	. . . .. -49,485.18
Cost to Johnson had he completed the house (10% of $47,176)	. . . .. - 4,717.60
TOTAL:	. . . .. $ 674.00

[¶5] The court awarded the Bovees $2,427.55 on their counterclaim for remedial work. Johnson does not dispute the trial court's factual findings upon which these calculations were based. Rather, he argues that he is entitled to recover in quantum meruit for the reasonable value of the services he rendered which he claims to be $9,000 over the original contract price and agreed extras.

[¶6] We are therefore faced with the issue of whether restitution can be recovered in an amount in excess of the contract price, an issue which is a matter of first impression in Colorado.

[¶7] Since the Bovees breached the contract by refusing to make the required payments, Johnson was entitled to consider the contract a nullity, and recover the reasonable value of his services. *See, e. g., Jacobs v. Jones*, 161 Colo. 505, 423 P.2d 321 (1967*); Zion Baptist Church v. Hebert*, 94 Colo. 59, 28 P.2d 799 (1933). But none of the cases supporting this principle involved a contractor who had overspent and was asking for more than the contract price.

[¶8] Courts and commentators are divided over the question of whether restitution should be limited by the contract. Compare Palmer, *The Contract Price as a Limit on Restitution for Defendant's Breach*, 20 Ohio State L.J. 264 (1959) with Childres & Garamella, *The Law of Restitution and the Reliance Interest in Contract*, 64 Nw. U. L. Rev. 433 (1969). For a survey of arguments on both sides of this issue, see D. Dobbs, *Law of Remedies* § 12.1, at 794-795 (1973).

[¶9] We believe using the contract price as a ceiling on restitution is the better-reasoned resolution of this question. Had Johnson fully performed, his recovery would be limited to the contract price, since he would be suing for specific performance of the liquidated debt obligation under the contract. *See* 5 A. *Corbin, Contracts*, § 1110 (1964). It is illogical to allow him to recover the full cost of his services when, if he completed the house, he would be limited to the contract price plus the agreed upon extras.

Accordingly, the judgment of the trial court is affirmed.

COYTE and ENOCH, JJ., concur.

Note: The notion that restitution is limited by expectation is not the majority rule. The different, majority rule was followed in *Salo Landscape & Constr. Co., Inc. v. Liberty Elec. Co.*, 119 R.I. 269, 274 (1977):

> There remains only the question of the proper measure of plaintiff's recovery for the work done. The theory urged by plaintiff and adopted by the trial justice is that defendant's failure to make the agreed upon progress payments constituted a total breach of the substituted contract and entitled plaintiff to recover the reasonable value of the work performed rather than damages based on the contract price. In support of its claim under that theory, plaintiff presented testimony that the fair and reasonable value of the performance rendered was $26,644.79. The defendant, on the other hand, argues that plaintiff had agreed in its subcontract that its compensation was to be based upon the unit price schedule stipulated in defendant's contract with the Commonwealth and that its damages should therefore be limited to a sum arrived at by multiplying the units of work completed by the prices stipulated therefor. That sum, according to defendant, is only $14,436.87.
>
> The defendant's theory falls short and plaintiff's hits the mark, however, for an owner or prime contractor who fails to pay an installment due on a construction contract is guilty of

> a breach that goes to the essence of the contract and that entitles the injured party to bring an action based on a quantum meruit theory for the fair and reasonable value of the work done. *Pelletier v. Masse*, 49 R.I. 408, 410-11, 143 A. 609, 610 (1928); *Greene & Brown v. Haley*, 5 R.I. 260, 262 (1858); Restatement, Contracts § 347 (1932); 5 Corbin, *supra* § 1109. The plaintiff in this case has brought such an action; and defendant, having offered no evidence suggesting that plaintiff's claim is not a fair and reasonable charge for the work done, has given us no reason for disturbing the trial justice's acceptance of that claim.

Why would you do one or the other? The Restatement rule cited by the court reads as follows: "For the total breach of a contract, the injured party can get judgment for the reasonable value of a performance rendered by him, measured as of the time it was rendered, less the amount of benefits received as part performance of the contract and retained by him . . . ." RK § 347(1). What about this language suggests that restitution is not limited to the contract price?

B. Limiting Doctrines

1. Speculation

However we figure them, expectations damages are always hypothetical: We imagine where the non-breaching party would be if the breaching party had performed, then try to put the non-breaching party in that position economically. But the breacher breached, so expectation damages are an exercise in imagination. Probably this is why courts have been concerned about speculation. (A similar exercise occurs with regard to reliance damages, especially with lost opportunities.)

MINDGAMES, INC. v. WESTERN PUBLISHING CO., INC.

218 F.3d 652 (7th Cir. 2000)

POSNER, Chief Judge.

[¶1] This is a diversity suit for breach of contract, governed by Arkansas law because of a choice of law provision in the contract. The plaintiff, MindGames, was formed in March of 1988 by Larry Blackwell to manufacture and sell an adult board game, "Clever Endeavor," that he had invented. The first games were shipped in the fall of 1989 and by the end of the year, 75 days later, 30,000 had been sold. In March of 1990, MindGames licensed the game to the defendant, Western, a major marketer of games. Western had marketed the very successful adult board games "Trivial Pursuit" and "Pictionary" and thought "Clever Endeavor" might be as successful. The license contract, on which this suit is premised, required Western to pay MindGames a 15 percent royalty on all games sold. The contract was by its terms to remain in effect until the end of January of 1993, or for another year if before then Western paid MindGames at least $1.5

million in the form of royalties due under the contract or otherwise, and for subsequent years as well if Western paid an annual renewal fee of $300,000.

[¶2] During the first year of the contract, Western sold 165,000 copies of "Clever Endeavor" and paid MindGames $600,000 in royalties. After that, sales fell precipitously (though we're not told by how much) but the parties continued under the contract through January 31, 1994, though Western did not pay the $900,000 ($1.5 million minus $600,000) that the contract would have required it to pay in order to be entitled to extend the contract for a year after its expiration. In February of 1994 the parties finally parted. Later that year MindGames brought this suit, which seeks $900,000, plus lost royalties of some $40 million that MindGames claims it would have earned had not Western failed to carry out the promotional obligations that the contract imposed on it, plus $800,000 on the theory that Western renewed the contract for a third year, beginning in February of 1994; Western sold off its remaining inventory of "Clever Endeavor" in that year.

[¶3] The district court granted summary judgment for Western, holding that the contract did not entitle MindGames to a renewal fee and that Arkansas's "new business" rule barred any recovery of lost profits. 944 F.Supp. 754 (E.D.Wis.1996); 995 F.Supp. 949 (E.D.Wis.1998). Although the victim of a breach of contract is entitled to nominal damages, * * * , MindGames does not seek them; and so if it is not entitled to either type of substantial damages that it seeks, judgment was correctly entered for Western. By not seeking nominal damages, incidentally, MindGames may have lost a chance to obtain significant attorneys' fees, to which Arkansas law entitles a prevailing party in a breach of contract case. * * * *

[¶4] The rejection of MindGames' claim to the renewal fee for the second year (and a fortiori the third) was clearly correct. * * * *

[¶5] The more difficult issue is MindGames' right to recover lost profits for Western's alleged breach of its duty to promote "Clever Endeavor." A minority of states have or purport to have a rule barring a new business, as distinct from an established one, from obtaining damages for lost profits as a result of a tort or a breach of contract. * * * * The rule of *Hadley v. Baxendale*, 9 Ex. 341, 156 Eng. Rep. 145 (1854), often prevents the victim of a breach of contract from obtaining lost profits, but that rule is not invoked here. Neither the "new business" rule nor the rule of *Hadley v. Baxendale* stands for the general proposition that lost profits are never a recoverable item of damages in a tort or breach of contract case.

[¶6] Arkansas is said to be one of the "new business" rule states on the strength of a case decided by the state's supreme court many years ago. The appellants *in Marvell Light & Ice Co. v. General Electric Co.*, 162 Ark. 467, 259 S.W. 741 (1924), sought to recover the profits that they claimed to have lost as a result of a five and a half month delay in the delivery of icemaking machinery; the delay, the appellants claimed, had forced them to delay putting their ice factory into operation. The court concluded, however, that because there was no indication "that the manufacture and sale of ice by appellants was an established business so that proof of the amount lost on account of the delay ... might be made with reasonable certainty," "the anticipated profits of the new business are too remote, speculative, and uncertain to support a judgment for their loss." * * * * On its facts, moreover, Marvell was a classic *Hadley v. Baxendale* type of case—in fact virtually a rerun of *Hadley* [*Hadley* is the next opinion you will read in this casebook], except that the appellants alleged that they had notified the seller of the icemaking machinery of the damages that they would suffer if delivery was delayed, and the seller had agreed to be liable for those damages. The decision is puzzling in light of that allegation; it is doubly puzzling because, assuming that by the time of the trial the ice factory was up and running, it should not have been difficult to compute the damages that the appellants

had lost by virtue of the five and a half month delay in placing the factory in operation. Presumably it would have had five and a half months of additional profits.

[¶7] Marvell has never been overruled * * * . * * * * [But, that Marvell will not be followed] is the best prediction in this case. Marvell was decided more than three quarters of a century ago, and the "new business" rule which it has been thought to have announced has not been mentioned in a published Arkansas case since. The opinion doesn't make a lot of sense on its facts, as we have seen, and the Eighth Circuit case on which it relied has long been superseded in that circuit. *See, e.g., Central Telecommunications, Inc. v. TCI Cablevision, Inc.*, 800 F.2d 711, 727-28 (8th Cir.1986). The Arkansas cases decided since Marvell that deal with damages issues exhibit a liberal approach to the estimation of damages that is inconsistent with a flat rule denying damages for lost profits to all businesses that are not well established. * * * *

[¶8] The [new business] rule doesn't work because it manages to be at once vague and arbitrary. One reason is that the facts that it makes determinative, "new," "business," and "profits," are not facts, but rather are the conclusions of a reasoning process that is based on the rationale for the rule and that as a result turns the rule into an implicit standard. What, for example, is a "new" business? What, for that matter, is a "business"? And are royalties what the rule means by "profits"? MindGames was formed more than a year before it signed the license agreement with Western, and it sold 30,000 games in the six months between the first sales and the signing of the contract. MindGames' only "business," moreover, was the licensing of intellectual property. An author who signs a contract with a publisher for the publication of his book would not ordinarily be regarded as being engaged in a "business," or his royalties or advance described as "profits." He would be surprised to learn that if he sued for unpaid royalties he could not get them because his was a "new business." * * * *

[¶9] Western goes even further, arguing that even if it, Western, a well-established firm, were the plaintiff, it could not recover its lost profits because the sale of "Clever Endeavor" was a new business. On this construal of the rule, "business" does not mean the enterprise; it means any business activity. * * * *

[¶10] The rule could be made sensible by appropriate definition of its terms, but we find it hard to see what would be gained, given the existence of the serviceable and familiar standard of excessive speculativeness. The rule may have made sense at one time; the reduction in decision costs and uncertainty brought about by avoiding a speculative mire may have swamped the increased social costs resulting from the systematically inadequate damages that a "new business" rule decrees. But today the courts have become sufficiently sophisticated in analyzing lost-earnings claims, and have accumulated sufficient precedent on the standard of undue speculativeness in damages awards, to make the balance of costs and benefits tip against the rule. In any event we are far in this case, in logic as well as time, from the ice factory whose opening was delayed by the General Electric Company. We greatly doubt that there is a "new business" rule in the common law of Arkansas today, but if there is it surely does not extend so far beyond the facts of the only case in which the rule was ever invoked to justify its invocation here. There is no authority for, and no common sense appeal to, such an extension.

[¶11] But that leaves us with the question of undue speculation in estimating damages. Abrogation of the "new business" rule does not produce a free-for-all. What makes MindGames' claim of lost royalties indeed dubious is not any "new business" rule but the fact that the success of a board game, like that of a book or movie, is so uncertain. Here newness enters into judicial consideration of the damages claim not as a rule but as a factor in applying the standard. Just as a start-up company should not be permitted to obtain pie-in-the-sky damages upon allegations that it was snuffed out before it could begin to operate (unlike the ice

factory in Marvell, which did begin production, albeit a little later than planned), capitalizing fantasized earnings into a huge present value sought as damages, so a novice writer should not be permitted to obtain damages from his publisher on the premise that but for the latter's laxity he would have had a bestseller, when only a tiny fraction of new books achieve that success. Damages must be proved, and not just dreamed, though "some degree of speculation is permissible in computing damages, because reasonable doubts as to remedy ought to be resolved against the wrongdoer." *Jones Motor Co. v. Holtkamp, Liese, Beckemeier & Childress, P.C., supra*, 197 F.3d at 1194; *see Restatement, supra*, § 352, comment a.

[¶12] This is not to suggest that damages for lost earnings on intellectual property can never be recovered; that "entertainment damages" are not recoverable in breach of contract cases. That would just be a variant of the discredited "new business" rule. What is important is that Blackwell had no track record when he created "Clever Endeavor." He could not point to other games that he had invented and that had sold well. He was not in the position of the bestselling author who can prove from his past success that his new book, which the defendant failed to promote, would have been likely — not certain, of course — to have enjoyed a success comparable to that of the average of his previous books if only it had been promoted as promised. That would be like a case of a new business launched by an entrepreneur with a proven track record.

[¶13] In the precontract sales period and the first year of the contract a total of 195,000 copies of "Clever Endeavor" were sold; then sales fizzled. The public is fickle. It is possible that if Western had marketed the game more vigorously, more would have been sold, but an equally if not more plausible possibility is that the reason that Western didn't market the game more vigorously was that it correctly sensed that demand had dried up.

[¶14] Even if that alternative is rejected, we do not see how the number of copies that would have been sold but for the alleged breach could be determined given the evidence presented in the summary judgment proceedings (a potentially important qualification, of course); and so MindGames' proof of damages is indeed excessively speculative. * * * * Those proceedings were completed with no evidence having been presented from which a rational trier of fact could conclude on this record that some specific quantity, or for that matter some broad but bounded range of alternative estimates, of copies of "Clever Endeavor" would have been sold had Western honored the contract. MindGames obtained $600,000 in royalties on sales of 165,000 copies of the game, implying that Western would have had to sell more than 10 million copies to generate the $40 million in lost royalties that MindGames seeks to recover. * * * *

[¶15] When the breach occurred, MindGames should have terminated the contract and sought distribution by other means. See *Farnsworth, supra*, § 12.12, pp. 806-08. The fact that it did not do so — that so far as appears it has made no effort to market "Clever Endeavor" since the market for the game collapsed in 1991 — is telling evidence of a lack of commercial promise unrelated to Western's conduct.

[¶16] Although Western in its brief in this court spent most of its time misguidedly defending the "new business" rule, clinging to Marvell for dear life (a case seemingly on point, however vulnerable, is a security blanket that no lawyer feels comfortable without), it did argue that in any event MindGames' claim for lost royalties was too speculative to ground an award of damages for that loss. The argument was brief but not so brief as to fail to put MindGames on notice of a possible alternative ground for upholding the district court's judgment; we may of course affirm an award of summary judgment on any ground that has not been forfeited or waived in the district court. * * * * MindGames did not respond to the argument in its reply brief. It pointed to no evidence from which lost royalties could be calculated to even a rough approximation. We find its silence eloquent and Western's argument compelling, and so the judgment in favor of Western is

Affirmed.

FAIRCHILD, Circuit Judge, dissenting in part.

[¶1] I agree that (1) MindGames' claim for a renewal fee for the year following the initial term of the Licensing Agreement was properly dismissed, and (2) we are not bound by *Marvell Light & Ice Co. v. General Electric Co.,* 162 Ark. 467, 259 S.W. 741 (1924) to affirm the dismissal of Mind-Games' claim for loss of royalties caused by breach of contract. I do, however, respectfully disagree with the conclusion that, as a matter of law, that claim is too speculative to support an award of damages. * * * *

[¶2] I would not hold that MindGames has waived or forfeited its opportunity to produce evidence of damages. It is true that in responding to Western's motion for partial summary judgment, MindGames did not provide evidentiary material tending to show the breaches by Western nor that such breaches caused a loss of sales. This should not be deemed a waiver or forfeiture of an opportunity to do so because of Western's complete reliance in its motion on the new business rule and Marvell, which, if applied, would prevent proof of breach and causation of loss. Western's motion did not reach the issue of breach, and establishing damages would require MindGames to prove that the breach occurred and caused loss of sales. Although Western, in its memorandum in support of its motion did include a section making the point that the success of a new product in the entertainment industry is especially difficult to predict, it used that point to support an argument that the new business rule was particularly appropriate in this case, and that the Arkansas Supreme Court would be unlikely to retreat from the new business rule under circumstances like these. Western did not squarely assert, as an alternative ground, that Mind-Games could not prove to a reasonable certainty that any breach by Western caused loss of sales. Rather, Western urged that the district court should strictly apply the new business rule. * * * *

I would remand for further proceedings on this part of MindGames' complaint.

Questions:

1. Do you find Judge Posner's arguments in ¶¶ 8–10 too clever? In law, definitions must end at some point so that the law can be more general than the facts. And in the end, the words of the law always mean their application. Moreover, prudential reasons exist not to make the law too specific. At some point, too particular a rule might make the precedent too narrow to govern later cases. At the time a rule is written, the judges might not know or be able to forecast what particularities it is important to capture. And every act of lawmaking uses political capital (for example, Judge Posner spent political capital disagreeing with Judge Fairchild).

Anyway, why wasn't creation and promotion of Clever Endeavor a new business? Shouldn't evidence of the destruction of an untested profit-making opportunity always be proved, not dreamt? Is it possible that Judge Posner described the new business rule in a too narrow or crabbed way in order to argue against it? Is that a fair way to argue? What would you call that kind of argument?

2. In ¶ 10, Judge Posner argues that judges are so sophisticated today that we don't need the new business rule. This is a presentist argument, of a sort. Presentists argue that "modern" positions are better. Every once in a while a presentist will talk about people in the past as if they were all neanderthals (sometimes they even say this, *e.g.*, *Nehring v. LaCounte,* 712 P.2d 1329, 1335 (Mont. 1986) (overruling a "Neanderthal approach to causation")). Most of the time, old legal positions were much better justified in the facts and culture of their own time and place; the old positions were not adopted because judges were unintelligent or ignorant. Do you argue differently for a judge who thinks he is smarter than other judges (in the past or present)?

3. What does it mean to "capitaliz[e] . . . earnings into a . . . present value"? Typically, we do this by looking at how much money we will have at some future point in time, consider the similarly risky ways we could make money now, and then discount the future amount to the value we would need to invest (today) at a "risk-adjusted rate" in order to have the future amount at the future point in time. For example, if we think Clever Endeavor will earn $1,000,000 in profits next year, and the risk-free rate (taken from U.S. Treasury bonds) is 4%, then, to start with, we could divide 1,000,000 by 1.04, and this gives us $961,538.46, which is the present value of $1,000,000. Clever Endeavor is not a risk-free opportunity, so we want to add riskiness as a factor. If I think a new game is pretty risky but not terribly risky (compared to other money-making opportunities I know of), I might say the risk-adjusted rate is around 15%. $1,000,000 divided by 1.15 is $ 869,565.22. Probability can get us a number, always. Where is the uncertainty in the calculation?

4. What kind of evidence would show non-speculative lost profits in a new business? Can you see where the court points you toward the answer?

5. What is the dissent's point, and does it persuade you?

6. In *Hall v. Nassau Consumers' Ice Co., Inc.*, 183 N.E. 903 (N.Y. 1933), the plaintiff was a purchaser of seven debentures of gold bonds issued by Nassau Consumers in 1925. The bonds were payable May 1, 1940 unless sooner called for payment. The company was to pay interest of 8% each year until the bonds were redeemed. But each bond also contained the following clause: "On the 1st day of May, in each of the years 1930 to 1939, inclusive, there shall be called for payment by lot under procedure to be determined by the Board of directors of the Nassau Consumers Ice Co., Inc., the sum of Five Thousand ($5,000) Dollars. This bond may be called for redemption at 105 per cent of its face value and accrued interest." The plaintiff alleged in the suit that none of the bonds were called for payment in 1930 or 1931. Would damages for failing to call a bond by lot be speculative?

Suppose your professor enters a beauty contest with a $10,000 prize and the entity conducting the contest breaches its contract by conducting it on terms different in a material way from those promised—say, by rigging the competition so that Miss Texas City wins for sure and your professor is given no chance. Let's suppose there are 10 contestants total, and Miss Texas City had no idea that the contest was rigged and did not contribute to the breach. What are your professor's damages?

Are these two scenarios different enough from *MindGames* to justify letting the plaintiff's complaint go forward? If I am not able to show evidence with which a reasonable trier of fact could find I had any chance of winning the beauty contest, am I just out of luck?

2. Foreseeability

Hadley v. Baxendale

9 Exchequer 341 (1854), 156 ER 145

[¶1] At the trial before Crompton, J. at the last Gloucester Assizes, it appeared that the plaintiffs carried on an extensive business as millers at Gloucester; and that, on the 11th of May, their mill was stopped by a breakage of the crank shaft by which the mill was worked. The steam-engine was manufactured by Messrs. Joyce & Co. the engineers, at Greenwich, and it became necessary to send the shaft as a pattern for a new one to Greenwich. The fracture was discovered on the 12th, and on the 13th the plaintiffs sent one of their servants to the office of the defendants, who are the well known carriers trading under the name of Pickford & Co. for the purpose of having the shaft carried to Greenwich. The plaintiffs' servant told the clerk that the mill was stopped, and that the shaft must be sent immediately; and in answer to the inquiry when the shaft would be taken, the answer was, that if it was sent up by twelve o'clock any day, it would be delivered at Greenwich on the following day. On the following day the shaft was taken by the defendants, before noon, for the purpose of being conveyed to Greenwich, and the sum of 2l. 4s. was paid for its carriage for the whole distance; at the same time the defendants' clerk was told that a special entry, if required, should be made to hasten its delivery. The delivery of the shaft at Greenwich was delayed by some neglect; and the consequence was, that the plaintiffs did not receive the new shaft for several days after they would otherwise have done, and the working of their mill was thereby delayed, and they thereby lost the profits they would otherwise have received.

[¶2] On the part of the defendants, it was objected that these damages were too remote, and that the defendants were not liable with respect to them. The learned Judge left the case generally to the jury, who found a verdict with 25l. damages beyond the amount paid into Court.

[¶3] Whateley, in last Michaelmas Term, obtained a rule nisi for a new trial, on the ground of misdirection.

[¶4] Keating and Dowdeswell (Feb. 1) shewed cause. The plaintiffs are entitled to the amount awarded by the jury as damages. These damages are not too remote, for they are not only the natural and necessary consequence of the defendants' default, but they are the only loss which the plaintiffs have actually sustained. * * * *

[¶5] Whateley, Willes, and Phipson, in support of the rule. It has been contended, on the part of the plaintiffs, that the damages found by the jury are a matter fit for their consideration; but still the question remains, in what way ought the jury to have been directed? It has been also urged, that, in awarding damages, the law gives compensation to the injured individual. But it is clear that complete compensation is not to be awarded; for instance, the non-payment of a bill of exchange might lead to the utter ruin of the holder, and yet such damage could not be considered as necessarily resulting from the breach of contract, so as to entitle the party aggrieved to recover in respect of it. * * * * The damages here are too remote. * * * * The rule, therefore, that the immediate cause is to be regarded in considering the loss, is applicable here. There was no special contract between these parties. A carrier has a certain duty cast upon him by law, and that duty is not to be enlarged to an indefinite extent in the absence of a special contract, or of fraud or malice. * * * * Here the declaration is founded upon the defendants' duty as common carriers, and indeed there is no pretence for saying that they entered into a special contract to bear all the consequences

of the non-delivery of the article in question. They were merely bound to carry it safely, and to deliver it within a reasonable time. The duty of the clerk, who was in attendance at the defendants' office, was to enter the article, and to take the amount of the carriage; but a mere notice to him, such as was here given, could not make the defendants, as carriers, liable as upon a special contract. * * * * This therefore is a question of law, and the jury ought to have been told that these damages were too remote; and that, in the absence of the proof of any other damage, the plaintiffs were entitled to nominal damages only: *Tindall v. Bell* (11 M. & W. 232). * * * * If the defendants should be held responsible for the damages awarded by the jury, they would be in a better position if they confined their business to the conveyance of gold. They cannot be responsible for results which, at the time the goods are delivered for carriage, are beyond all human foresight. * * * * Where the contracting party is shewn to be acquainted with all the consequences that must of necessity follow from a breach on his part of the contract, it may be reasonable to say that be takes the risk of such consequences. * * * *

The judgment of the Court was now delivered by

[¶6] ALDERSON, B. We think that there ought to be a new trial in this case; but, in so doing, we deem it to be expedient and necessary to state explicitly the rule which the Judge, at the next trial, ought, in our opinion, to direct the jury to be governed by when they estimate the damages. * * * *

[¶7] Now we think the proper rule in such a case as the present is this: - Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, i, e. according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it. Now, if the special circumstances under which the contract was actually made were communicated by the plaintiffs to the defendants, and thus known to both parties, the damages resulting from the breach of such a contract, which they would reasonably contemplate, would be the amount of injury which would ordinarily follow from a breach of contract under these special circumstances so known and communicated. But, on the other hand, if these special circumstances were wholly unknown to the party breaking the contract, he, at the most, could only be supposed to have had in his contemplation the amount of injury which would arise generally, and in the great multitude of cases not affected by any special circumstances, from such a breach of contract. For, had the special circumstances been known, the parties might have specially provided for the breach of contract by special terms as to the damages in that case; and of this advantage it would be very unjust to deprive them. Now the above principles are those by which we think the jury ought to be guided in estimating the damages arising out of any breach of contract. It is said, that other cases such as breaches of contract in the nonpayment of money, or in the not making a good title to land, are to be treated as exceptions from this, and as governed by a conventional rule. But as, in such cases, both parties must be supposed to be cognisant of that well-known rule, these cases may, we think, be more properly classed under the rule above enunciated as to cases under known special circumstances, because there both parties may reasonably be presumed to contemplate the estimation of the amount of damages according to the conventional rule. Now, in the present case, if we are to apply the principles above laid down, we find that the only circumstances here communicated by the plaintiffs to the defendants at the time the contract was made, were, that the article to be carried was the broken shaft of a mill, and that the plaintiffs were the millers of that mill. But how do these circumstances shew reasonably that the profits of the mill must be stopped by an unreasonable delay in the delivery of the broken shaft by the carrier to the third person? Suppose the plaintiffs had another shaft in their possession put up or putting up at the time, and that they only wished to send back the broken shaft to the engineer

who made it; it is clear that this would be quite consistent with the above circumstances, and yet the unreasonable delay in the delivery would have no effect upon the intermediate profits of the mill. Or, again, suppose that, at the time of the delivery to the carrier, the machinery of the mill had been in other respects defective, then, also, the same results would follow. Here it is true that the shaft was actually sent back to serve as a model for a new one, and that the want of a new one was the only cause of the stoppage of the mill, and that the loss of profits really arose from not sending down the new shaft in proper time, and that this arose from the delay in delivering the broken one to serve as a model. But it is obvious that, in the great multitude of cases of millers sending off broken shafts to third persons by a carrier under ordinary circumstances, such consequences would not, in all probability, have occurred; and these special circumstances were here never communicated by the plaintiffs to the defendants. It follows, therefore, that the loss of profits here cannot reasonably be considered such a consequence of the breach of contract as could have been fairly and reasonably contemplated by both the parties when they made this contract. For such loss would neither have flowed naturally from the breach—each of this contract in the great multitude of such cases occurring under ordinary circumstances, nor were the special circumstances, which, perhaps, would have made it a reasonable and natural consequence of such breach of contract, communicated to or known by the defendants. The Judge ought, therefore, to have told the jury, that, upon the facts then before them, they ought not to take the loss of profits into consideration at all in estimating the damages. There must therefore be a new trial in this case.

Rule absolute.

Questions:

1. Is this rule default or mandatory?

2. Given how old *Hadley* is and how difficult it is to read, you should not be surprised that various interpretations exist. On one end of a spectrum, some courts require foreseeability tantamount to a tacit agreement to pay the damages if they exist. More reasonably in the middle of the spectrum some courts require only that reasonable people in the position of the parties would have foreseen the damages as a probable result of breach. *See, e.g.*, *Troxler Elec. Labs., Inc. v. Solitron Devices, Inc.*, 722 F.2d 81 (4th Cir. 1984).

3. If you were helping Fedex to plan its business, would you let such facts control? Find Fedex's standard terms of service online. Do they let the Hadley rule function, or do they override it?"

3. Mitigation

Courts are fond of saying that non-breaching parties have a "duty to mitigate damages arising from breach of contract." *E.g.*, *Mack Cali Realty, L.P. v. Everfoam Insulation Sys., Inc.*, 972 N.Y.S.2d 310, 312 (N.Y. App., 2d Dept. 2013). However, the expectation measure includes within it the cost of the non-breaching party's performance; in other words, that the breacher breached does not mean that the breacher must provide the promised benefit cost-free to the non-breaching party. The mitigation "duty," so-called, to some extent takes account of the missing cost by imposing on the non-breaching party the cost of "avoidable harm." Alternatively, expectation damages must still be caused by the breach, and that causation is muddled when the non-breaching party changes its usual course in order to lie on the beach rather than work. Also, the law wants to encourage productive use of time, talents, and assets. So, the law assumes the non-breaching party will make reasonable efforts and pays the non-breacher no more expectation damages than are consistent with that effort.

29 Holding Corp. v. Diaz

775 N.Y.S.2d 807 (N.Y. Supr. App. 1st Dep't 2004)

OPINION OF THE COURT

Paul A. Victor, J.

* * * *

Facts

[¶1] Plaintiff is the owner of premises located at 707 East 187th Street in Bronx County. In 1992, defendant Lizabeth Diaz entered into a residential lease for an apartment at the premises.

[¶2] Defendant Colon, who was apparently a tenant at the premises, and defendants Miguel Lopez and Luis R. Acosta executed a guarantee of Ms. Diaz' lease. The guarantee provided: "The undersigned Guarantor guarantees to Owner the strict performance and observation by Tenant of all the agreements, provisions and rules in the attached Lease. Guarantor agrees to waive all notices when Tenant is not paying rent or not observing and complying with all of the provisions of the attached Lease. Guarantor agrees to be equally liable with tenant so that Owner may sue Guarantor directly without first suing tenant. The Guarantor further agrees that his guarantee shall remain in full force and effect even if the lease is renewed, changed or extended in any way and even if Owner has to make a claim against Guarantor. Owner and Guarantor agree to waive trial by jury in any action, proceeding or counterclaim brought against the other on any matters concerning the attached Lease or the Guaranty." (Emphasis added.)

[¶3] Ms. Diaz renewed her lease in 1993 and 1995, ostensibly without the knowledge or participation of the defendant. The 1995 renewal was for a two-year period commencing May 1, 1996 and expiring April 30, 1998. It is not disputed that Lizabeth Diaz vacated the premises in May 1997, and failed to pay the rental owed from May 1997 to April 1998, for a total of 12 months' rent in the amount of $6,963.84.

[¶4] Plaintiff seeks to recover the rent owed from the named tenant, as well as from defendant Colon and the other guarantors. In his verified answer, defendant Colon raised the defenses * * * that the plaintiff is responsible at least for the damages sustained; that the plaintiff failed to mitigate damages * * * .; and that premises were not registered with the Division of Housing and Community Renewal.

Discussion

* * * *

Mitigation of Damages

[¶5] It is not clear from the papers submitted if the landlord actually held the premises vacant for the period from May 1997 to April 1998, but the landlord does claim an entitlement to rent for this entire period. The landlord argues specifically that it has no duty to mitigate damages.

[¶6] The issue is one which appears to have generated considerable confusion and somewhat inconsistent determinations * * *. The seminal case in this area is *Becar v. Flues* (64 NY 518 [1876]), a case involving an oral residential leasehold for an additional one-year term which was to commence May 1. The tenant died in April, and his family gave notice that they would not retain the leasehold. The defendant argued that because the contract was executory, plaintiff was obligated to mitigate damages. The Court held, to the contrary, that the contract was not executory, and that the defendant was responsible for the rent of the house — meaning the full amount of the agreed rent, not subject to mitigation based on an offer by a prospective tenant to lease the premises for an amount only slightly less than the agreed rental.

[¶7] The rule in *Becar* was subject to criticism, and in fact rejected by Judge Bentley Kassal who held that a residential landlord had a duty to mitigate its damages, recognizing that “there is no longer good reason — if there ever was — why leases should be governed by rules different from those applying to contracts in general.” (*Parkwood Realty Co. v Marcano,* 77 Misc 2d 690, 691 [Civ Ct 1974] * * * .) This “progressive” trend which recognized a duty to mitigate in the residential context gained momentum until it appeared to gain acceptance as the prevailing rule. * * * *

[¶8] This “modernizing” trend was thrown into a sudden tailspin in 1995 when the Court of Appeals, although dealing with a written lease for commercial premises, cited the *Becar* case with approval [in a case called “*Holy Props*” and held that, under the lease terms,] the landlord had no duty to mitigate by reletting the premises. * * * * The Court of Appeals held (at 133-134):

> “ * * * * Once the tenant abandoned the premises prior to the expiration of the lease, * * * the landlord was within its rights under New York law to do nothing and collect the full rent due under the lease * * * . * * * *
>
> “Defendant urges us to reject this settled law and adopt the contract rationale recognized by some courts in this State and elsewhere. We decline to do so.” * * * * * “ [Some commentators then read the tea leaves from the Court of Appeals and started saying that the *Becar* rule had risen again.]

The Appellate Term, First Department, subsequently * * * declined to recognize a limitation on this doctrine to the commercial context, extending the holding to the residential arena in *Whitehouse Estates v. Post* (173 Misc 2d 558 [App Term, 1st Dept 1997]). * * * *

[¶9] Despite these seemingly clear pronouncements, and the absence of any case decided by the Appellate Division adopting a duty to mitigate in residential cases, other courts (especially the lower courts in the Second Department) appear to adhere to the distinction in treatment between residential and commercial cases, which existed prior to the decision in *Holy Props*. These cases hold that there exists a duty to mitigate in the context of residential leases, but not with respect to commercial leases. * * * * And, in this judicial district, a landlord has a duty to mitigate damages by reletting the premises when the tenant leaves before the end of the term. * * * * The landlord must make 'reasonable and diligent efforts to rerent the premises.' * * * *

Supreme Court Not Bound by Appellate Term Precedent

[¶10] This court is not bound by the precedents of the Appellate Term, either in this department or in other departments. * * * *

[¶11] In any event, this court declines to follow the holding in *Whitehouse*. Nor does this court accept the proposition that *Holy Props*, governs in the residential landlord-tenant context. The concept that a landlord can hold a residential tenant hostage to the terms of a lease, doing nothing and permitting damages to accrue when leased premises are readily marketable, is clearly contrary to common sense, the reasonable expectations of the public, and notions of justice and equity. It is already harsh justice which imposes an indefinite obligation upon a guarantor of a residential lease. To superimpose upon this harsh result the right of a landlord to make no effort to minimize damages is unconscionable, and violative of public policy. It is almost axiomatic that commercial leases may and should be governed by a different rule than residential leases. A commercial tenant which has negotiated a lease which provides that the landlord need not mitigate damages may take proper precautions against the possibility of default, may seek to assign or sublet, or may simply defer abandoning the lease. The same cannot be said of the average citizen in a mobile society, who may choose to or be required to relocate for a myriad of health-related or other personal reasons. Nor can this court endorse an antiquated rule of law which would encourage the warehousing of residential apartments, frustrate the mobility of the population, and result in an inequitable and intolerable burden on residential tenants. Accordingly, at the inquest on damages, the landlord should be prepared to demonstrate reasonable and diligent efforts to rerent the premises.

[¶12] The motion is granted.

In a footnote, the court added this:

> This decision accords with the majority view. As was reported in one scholarly article (Flynn, *Duty to Mitigate Damages Upon a Tenant's Abandonment*, *supra*, 34 Real Prop Prob & Tr J 721 [Winter 2000]):
>
> > "[T]he shift toward the view that a landlord should mitigate damages seems to have continued. Although courts often refer to the non-mitigation rule as the majority rule, twenty-eight states now impose an affirmative duty to mitigate on residential landlords. These states include Alaska, Arizona, California, Connecticut, Delaware, Hawaii, Illinois, Iowa, Kansas, Kentucky, Maine, Maryland, Montana, Nebraska, Nevada, New Jersey, New Mexico, North Carolina, North Dakota, Oklahoma, Oregon, Rhode Island, South Carolina, Tennessee, Texas, Washington, Wisconsin, and Wyoming. Five additional states — Idaho, Indiana, Michigan, Ohio, and Utah —

likely would agree. The trend clearly is to adopt the duty to mitigate by statute, largely because of the application of contract principles to lease agreements. Furthermore, states recognize that the duty to mitigate serves several important public policies, which are often enumerated by the courts.

"On the other hand, only fourteen states would hold that the residential landlord owes no duty to the tenant to mitigate damages on a tenant's abandonment of the premises. The states that refuse to recognize a duty to mitigate certainly give the landlord the option of mitigating on behalf of the tenant, but they refuse to impose an absolute duty because landlords and tenants rely on the long-standing non-mitigation rule. These states include Alabama, Arkansas, Colorado, Florida, Georgia, Massachusetts, Minnesota, Missouri, Mississippi, New Hampshire, Pennsylvania, Vermont, Virginia, and West Virginia. One additional state, New York, likely would agree."

Questions:

1. Is it your impression that commercial landlords can simply let the property lie empty, do nothing, and still collect rent? Which rule is more consistent with the lease as a grant of property?

2. Is this court's decision based on the agreement of the parties?

3. What public policies can you pick out in support of the avoidable consequences doctrine used in this case?

ZAYRE CORP. v. CREECH

Fla. App. (1986), 497 So.2d 706

DOWNEY, J.

[¶1] Zayre Corporation appeals a final judgment in favor of appellee James R. Creech for breach of an employment agreement.

[¶2] It appears that Creech had been employed by Zayre for a number of years until his employment was terminated as of September 1984. He sued Zayre claiming that he had an oral contract of employment from June 1, 1984 to May 31, 1985 and that his termination without cause was a breach of said contract. The trial court ruled in Creech's favor finding that Zayre had paid Creech for forty-four weeks by including vacation and severance pay and that Zayre owed him for several weeks' salary plus a bonus of $7,338.

[¶3] Zayre contends on appeal that within ten weeks after he was terminated Creech was employed by Richway at an annual salary of $34,000. As a result, Zayre argues that Creech's damages were completely

mitigated because his earnings for the annual period in question exceeded the salary due him under his contract with Zayre. The trial judge rejected this defense and made no deduction for the earnings recovered by Creech during the remainder of the term in question. That ruling is erroneous because the established rule in Florida in employment situations of this kind is set forth in *Juvenile Diabetes Research Foundation v. Rievman*, 370 So.2d 33, 35-36 (Fla.3d DCA 1979), as follows:

> The law is clear that the purpose of an award of damages in a breach of contract action is to place the injured party in the same financial position as he would have occupied if the contract has been fully performed. *Hodges v. A.P. Fries & Co.*, 34 Fla. 63, 69, 15 So. 682, 684 (1894); *Popwell v. Abel*, 226 So.2d 418, 422 (Fla. 4th DCA 1969); *First National Insurance Agency, Inc. v. Leesburg Transfer & Storage, Inc.*, 139 So.2d 476, 482 (Fla. 2d DCA 1962). It is, therefore, the established law of this state that in an action for breach of an employment contract [brought by an employee for an alleged wrongful discharge prior to completion of the contract] the prima facie measure of damages is the contract price of salary or wages for the unexpired term of the contract together with any unpaid balance due under the contract for services rendered before the wrongful discharge. *Hazen v. Cobb*, 96 Fla. 151, 117 So. 853 (1928); 2 Fla.Jur.2d "Agency and Employment" § 134, p. 315 (1977) . . . .
>
> These prima facie damages, however, are subject to reduction upon proof of an amount which the employee actually earned, or could have earned through the use of due diligence in other employment of like nature, for the remainder of his term of employment under the contract. *Southern Keswick, Inc. v. Whetherholt*, 293 So.2d 109 (Fla. 2d DCA 1974). In this connection, it is often said that the plaintiff employee has a duty to mitigate his damages by reasonably seeking other employment of like nature subsequent to the breach of contract; the penalty for failing to comply with that duty is a reduction in his recoverable damages in the amount he could have earned had he complied with such duty.

Accordingly, Creech was not entitled to recover the balance of his salary or bonus for the 1984-85 year because the amount he earned after his wrongful discharge exceeded the balance due him from Zayre for salary and bonus.

[¶4] Nevertheless, the general rule in cases of this type is that the measure of damages recoverable for breach of a contract of employment for a definite term is the amount of compensation agreed upon for the remainder of the period involved, less the amount which the servant earned, or with reasonable diligence might have earned, from other employment during that period. However, if following the discharge, the former employee has earned more than the price agreed to be paid, his recovery is limited to nominal damages only. 53 *Am.Jur.2d Master and Servant* § 62 (1970). *E.g. Board of Education of Alamogordo Public School District No. 1*, 102 N.M. 762, 701 P.2d 361 (1985). This rule is also followed in Florida where a contract has been breached but for one reason or another recoverable damages were not proven. *See AMC/Jeep of Vero Beach, Inc. v. Funston,* 403 So.2d 602 (Fla. 4th DCA 1981); *Muroff v. Dill*, 386 So.2d 1281 (Fla. 4th DCA 1980).

[¶5] In view of the foregoing, the provisions of the judgment awarding Creech $13,378 are reversed and the cause is remanded to the trial court with directions to enter a judgment for Creech for nominal damages only.

Questions:

1. Would it be possible for a fired employee to win on the mitigation issue even though the employee did nothing to find another job? Would it be possible for the fired employee to have no reduction for mitigation even though the employee immediately started working in another job and continued in that job until the end of the term? Reading the rule very carefully should show you the answers to these questions.

2. In one well-known case, *Parker v. Twentieth Century-Fox Film Corp*., 89 Cal. Rptr. 737 (Cal. 1970), Shirley MacLaine Parker signed a contract with Twentieth Century-Fox ("TCF") to star in TCF's production of the movie-musical "Bloomer Girl." The contract was to last from May 23, 1966, for fourteen weeks and pay $53,571.42. The film was to be made in California, and under the contract Ms. Parker had approval rights for the director, dance director, and screenplay. Prior to May 1966, TCF notified Ms. Parker that it had decided not to make the movie and would not pay her. The letter notifying Parker offered her the starring role in another film called "Big Country, Big Man," a western to be filmed in Australia, for the same compensation—"to avoid any damages to you," the letter said. The attached, proffered contract for "Big Country, Big Man," unlike the contract for the first movie, gave TCF the option to decline to make the movie and pay Ms. Parker her compensation instead. And, in this second contract Ms. Parker had no rights to approve anyone or the screenplay, but TCF promised to consult with her as to those things. Ms. Parker declined to sign the second contract. Instead, she sued for breach. TCF argued that Parker had, by failing to sign onto the "Big Country, Big Man" project, failed to mitigate. What result should the court reach? Consider also the following:

> a. Suppose TCF sold its rights in the Bloomer Girl project to Paramount, which then offered to employ Parker in the same role under the exact same terms except that Parker's pay would be 25% less. Would TCF then owe her 75% less in damages?
>
> b. TCF's lawyer may have made an error in TCF's argument about mitigation by limiting it to the "Big Country" project. What was the error?
>
> c. Might the case reach the same result if Parker declined all other movies for the relevant time period, did not seek to perform in any movies then, and instead moved to the mountains of New Mexico to live a life of meditation? Even with complete mitigation, shouldn't a plaintiff such as Ms. Parker be awarded something?

PROBLEM 48: A hires B to build a house for $100,000. B buys $20,000 worth of materials and does $15,000 worth of work that uses up all $20,000 in materials. Then A fires B for no good reason. The house would have cost B $90,000 to build. What are B's expectation damages? Why is the amount less than $100,000?

4. Punitive Damages

WERNER, ZAROFF, SLOTNICK, STERN & ASKENAZY v. Donald R. LEWIS

Civ. Ct., N.Y. Cty. (1992), 588 N.Y.S.2d 960

BRAUN, J.

[¶1] This is an action for, inter alia, breach of contract, in which this court held a nonjury trial over the course of eight days. Plaintiff is a law firm which has a subspecialty of assisting its clients to collect claims under the No-Fault Insurance Law. Defendant is a computer consultant. Plaintiff was having some difficulties with its computer so it contracted with defendant to remedy the problems. Defendant did so, and plaintiff paid him for his services. Defendant then convinced plaintiff to upgrade its computer system. Plaintiff orally agreed to retain defendant for that purpose. With defendant's assistance, plaintiff purchased a new computer, and defendant modified plaintiff's software to make it compatible with the new computer.

[¶2] Defendant estimated that the cost to plaintiff on this second contract would be $4,000-$5,000. The work took much longer than had been anticipated, and plaintiff ended up paying defendant a total of $21,375 on the second contract. On January 18, 1986, plaintiff made its last payment to defendant on the second contract. The payment was made at plaintiff's office. Defendant then put a floppy disk into plaintiff's computer, and said to one of plaintiff's partners that, if plaintiff had not paid defendant, he would not have entered the data contained on the floppy disk into the computer, which would have subsequently crashed.

[¶3] After that date, once per month defendant telephoned the person employed by plaintiff who did the computer data entry work for plaintiff, and asked her how the computer was performing and what claim number plaintiff had reached. Plaintiff's computer contained a software program modified by defendant, which included data on plaintiff's no-fault insurance clients. Each claim of those clients was assigned a claim number.

[¶4] That computer program in plaintiff's system shut down at claim number 56789 in July 1986. After that number, the system could not be utilized in the directory existing for the program, which significantly interfered with plaintiff's ability to work on its clients' claims and do billing. Although plaintiff's program could have functioned again if a new subdirectory was created each time that it stopped working at 56789, plaintiff was not aware that such a solution to the problem was possible. The cause of the problem was that defendant intentionally placed in the program a conditional statement, of which plaintiff had been unaware. The conditional statement was a hidden directive in the program which caused the program to stop working when it reached claim number 56789. Although defendant denied doing so, the court does not credit his testimony, in part because number 56789 is an inherently suspicious number at which the program stopped functioning.

[¶5] The subject program in plaintiff's computer was in executable form only. This means that, although the program was used on the computer screen in English and numbers, its structure was entered in the computer only in computer language. Thus, in order to modify the structure of the program, one had to have the source code for the program. Defendant had kept the source code. Defendant told one of plaintiff's partners that he had destroyed the source code and that it would have had to be redone to modify the program.

[¶6] Defendant gave no warranties to plaintiff. Defendant solicited a maintenance contract from plaintiff to cover any problems that might arise with plaintiff's system after defendant had completed his work, but plaintiff declined the offer because its partners thought that it had already paid defendant too much money for his services.

[¶7] After the computer program shut down, plaintiff hired another computer consultant to work on the computer system, so that the program could function again. He was successful, and plaintiff paid him $7,000 for his services. That consultant testified credibly that it was his opinion that the computer program had crashed due to a conditional statement that defendant had secretly placed in the program.

[¶8] Defendant's computer consulting business had slowed to a trickle at the time that he completed his work for plaintiff. It is this court's conclusion that defendant intentionally put the conditional statement into plaintiff's software, with the hope that, after the system stopped, plaintiff would retain him again to correct the problem.

[¶9] Defendant breached his second contract with plaintiff, although he did provide some services to plaintiff thereunder. Plaintiff is entitled to compensatory damages from defendant in the amount of $7,000 in order to reimburse plaintiff for its cost of hiring the second computer consultant to cure the problems created by defendant with plaintiff's computer program.

[¶10] In one of its causes of action, plaintiff seeks only punitive damages against defendant. Punitive damages are not a separate cause of action. (*APS Food Sys. v Ward Foods*, 70 A.D.2d 483, 488 [1st Dept 1979]; *Levine v Constanzo*, NYLJ, Nov. 1, 1991, at 21, col 4 [App Term, 1st Dept].) However, punitive damages need not be specifically requested in a complaint. (*Gill v Montgomery Ward & Co*., 284 App Div 36, 40 [3d Dept 1954]; *Korber v Dime Sav. Bank*, 134 App Div 149, 150 [2d Dept 1909]; *Sanders v Rolnick*, 188 Misc. 627, 631 [App Term, 1st Dept], affd without opn 272 App Div 803 [1st Dept 1947].) In order to justify an imposition of punitive damages, a complaint must allege the elements of malice, willfulness, wantonness or recklessness, or at least facts supporting the imposition of punitive damages. (*See, Fittipaldi v Legassie*, 18 A.D.2d 331, 337 [4th Dept 1963]; *Gill v Montgomery Ward & Co., supra*, 284 App Div, at 40; *Bingham v Gaynor,* 135 App Div 426, 427 [1st Dept 1909*]; Kipsborough Realty Corp. v Goldbetter*, 81 Misc.2d 1054 [Civ Ct, NY County 1975]; *Dembar v Reynolds & Co.,* 40 Misc.2d 84 [Sup Ct, NY County 1963].)

[¶11] Although the general rule is that punitive damages are not awarded for breach of contract claims, they "may be awarded when to do so would 'deter morally culpable conduct.' (*Halpin v Prudential Ins. Co.,* 48 N.Y.2d 906, 907; *Williamson, Pickett, Gross v Hirschfeld,* 92 A.D.2d 289, 295 [punitive damages for conduct involving bad faith].)" (*Minjak Co. v Randolph*, 140 A.D.2d 245, 249 [1st Dept 1988]; *see, Hubbell v Trans World Life Ins. Co.,* 50 N.Y.2d 899, 901 [1980]; *Mandelblatt v Devon Stores*, 132 A.D.2d 162, 167 [1st Dept 1987].) "It is not the form of the action that gives the right * * * to give punitory damages, but the moral culpability of the defendant." (*Hamilton v Third Ave. R. R. Co.*, 53 N.Y. 25, 30 [1873].) As the Court of Appeals stated in the lead case of *Walker v Sheldon* (10 N.Y.2d 401, 404 [1961]):

> "Punitive or exemplary damages have been allowed in cases where the wrong complained of is morally culpable, or is actuated by evil and reprehensible motives, not only to punish the defendant but to deter him, as well as others who might otherwise be so prompted, from indulging in similar conduct in the future. (*See, e.g.*, *Tommey v. Farley*, 2 N.Y.2d 71, 83; *Krug v. Pitass*, 162 N.Y. 154, 161; *Hamilton v. Third Ave. R. R. Co.*, 53 N.Y. 25, 28;

> *Oehlhof v. Solomon*, 73 App. Div. 329, 333-334.) * * * Moreover, the possibility of an award of such damages may not infrequently induce the victim, otherwise unwilling to proceed because of the attendant trouble and expense, to take action against the wrongdoer."

[¶12] Plaintiff did plead in its breach of contract cause of action under which compensatory damages are being awarded that defendant's conduct was done "with malicious intent". This is a sufficient pleading to entitle plaintiff to punitive damages, and defendant's actions here call out for the imposition of punitive damages against him.

[¶13] Defendant's actions were arguably the commission of a class A misdemeanor. Penal Law § 156.20 provides:

> "A person is guilty of computer tampering in the second degree when he uses or causes to be used a computer or computer service and having no right to do so he intentionally alters in any manner or destroys computer data or a computer program of another person."

Certainly, defendant had no right to do so when he put the conditional statement in plaintiff's program and caused it to crash. His act was clearly intentional. It would thus appear that he committed a crime when he acted as he did. (See, People v Versaggi, 136 Misc.2d 361 [Rochester City Ct 1987].) To the extent that defendant's actions may not fit under the Penal Law, the New York State Legislature should act in this computer age to amend the law.

[¶14] Computers are intricate machines, and their software programs are often complexly designed, and written in mathematical language. Most people who use computers do not have the expertise to remedy problems that arise with computers and computer software. Thus, members of the general public are often captives of those who have developed the expertise needed to understand computers and computer programs, and must rely upon those experts to act with good faith.

[¶15] Some people with computer expertise have utilized their advanced knowledge to instill great anxiety in the computer-using business and consumer public, and have caused great damage to some of them. Only a few months ago, the users of computers nationwide, including those in the courts of Manhattan, were plagued by fears that computer viruses had been planted in their computer programs which would have caused, and in some cases did cause, their computers to crash. (See, *NY Times*, Mar. 7, 1992, at 1, col 5; at 6, col 2 [Natl ed]; Pines, *Federal, State Courts Attack Computer Virus and Prevail — So Far*, NYLJ, Mar. 4, 1992, at 1, col 3.) Although the culprits there may not have been caught, defendant has been, and the imposition of punitive damages against defendant should send a message to others who would consider committing similar acts in the future, and even to some who may eradicate their already planted, as yet silent viruses which are presently waiting to awaken and wreak their havoc.

[¶16] This court regrets that it is confined by the complaint before it to be able to only award punitive damages of $18,000 against defendant, that being the total of $25,000 sought in the subject cause of action minus the $7,000 already awarded as compensatory damages. Defendant's actions in breaching his contract with plaintiff were morally culpable and seemingly criminal. Therefore, this court finds for plaintiff against defendant in the amount of $7,000 compensatory damages and $18,000 punitive damages.

Questions:

1. Punitive damages are appropriate in cases of intentional tort. Did Lewis commit an intentional tort?

2. Why not allow punitive damages for breach of contract? Is it because the moral prohibition against breach of contract extends only to the point of satisfying the non-breaching party's expectations? We don't believe that breach is in and of itself wrong? Or perhaps we do not believe, for some other reason, that the state should be punishing it?

3. Would awarding punitive damages for breach of contract force parties to act inefficiently? If a seller can breach a contract with a buyer, compensate the buyer for its loss, and still come out ahead, shouldn't the seller do so? In such a case, the seller is better off, the buyer is no worse off, and the products that the seller is selling end up in the hands of the person who values them most. In most cases, it's only money at issue. What do you think?

4. What purposes do punitive damages serve? Are those purposes served well here?

5. Another exception to the general rule has arisen in cases in which an insurance company refuses to pay for a loss clearly covered under a policy. The California Supreme Court led the way in imposing on such insurers a tort of "bad faith breach" of an insurance contract, often found when the insurer had rejected a reasonable settlement offer. *See, e.g.*, *Neal v. Farmers Ins. Exch.*, 148 Cal. Rptr. 389 (Cal. 1978). Punitive damages were available. Many states followed California's lead. Some suggested that courts should go further, offering punitive damages for all breaches in bad faith, and California arguably did so, for a time, but the California and other courts have now mostly stopped the growth of this "tort" and firmly restricted it to the insurance area. Is the idea of punishing "bad faith breach" a good one?

5. Liquidated Damages

BOWBELLS PUBLIC SCHOOL DISTRICT NO. 14 v. Marcia WALKER

North Dakota (1975), 231 N.W.2d 173

Paulson, J.

[¶1] This is an appeal from a judgment in which we are to determine the validity of a contract clause providing for the payment of a fixed amount of damages by Marcia Walker, a married teacher, who breached her employment contract with Bowbells Public School District No. 14.

[¶2] The Grand Forks District Court found that Mrs. Walker breached her employment contract with the Bowbells Public School District No. 14. The court also found that the employment contract contained a valid liquidated-damages provision, and, on that basis, ordered Mrs. Walker to pay to the school district the sum

stipulated in the contract as damages. On December 16, 1974, judgment was entered for the school district in the amount of $252, plus costs and disbursements. It is from this judgment that Mrs. Walker appeals.

[¶3] The parties to this action have stipulated to the following facts:

> "a. The defendant [Marcia Walker] was an employee of the plaintiff [school district] during the 1972-1973 school year which began in September of 1972.
>
> "b. In September of 1972 the defendant joined the Bowbells Education Association, the North Dakota Education Association and the National Education Association by paying her yearly dues.
>
> "c. In order to negotiate contract terms for the 1973-1974 school year the plaintiff and the Bowbells Education Association each chose negotiating committees to represent them at the contract negotiation meetings. These meetings began early in 1973.
>
> "d. The negotiation committee of the Bowbells Education Association was given the power by the association members to make binding agreements with the plaintiff.
>
> "e. During their January 10, 1973 meeting the negotiation committees agreed that a release from a signed contract could be granted until May 15 at no expense to the teacher; 1% of the contracted amount [after May 15; 2%] after June 15; 3% after July 15; and 4% after August 15.
>
> "f. The defendant signed a contract to teach for the plaintiff during the 1973-1974 school year. The contract is dated March 23, 1973.
>
> "g. The defendant contracted to teach for 180 days beginning on September 1, 1973. She was to receive $6300.
>
> "h. On August 19, 1973, the defendant asked the Superintendent of the Bowbells School District to be released from her March 23, 1973 contract as her husband was moving from the area and she wanted to go with him.
>
> "i. In a letter to the plaintiff dated August 26, 1973 the defendant stated she would not be able to remain at Bowbells and asked for her release.
>
> "j. On August 30, 1973, after finding a replacement, the plaintiff released the defendant from her contract and requested that she pay the damages in accordance with the agreement between the plaintiff and the Bowbells Education Association. The defendant has not paid."

[¶4] The principal question is whether the fixed-damages provision of the contract, as outlined in paragraph "e" of the stipulated facts, constitutes a valid liquidated-damages clause or whether it is void, as constituting a penalty, under § 9-08-04, N.D.C.C., which provides:

> "Fixing damages for breach void--Exception.--Every contract by which the amount of damages to be paid, or other compensation to be made, for a breach of an obligation is

> determined in anticipation thereof is to that extent void, except that the parties may agree therein upon an amount presumed to be the damage sustained by a breach in cases where it would be impracticable or extremely difficult to fix the actual damage."

It is Mrs. Walker's contention that the contract clause in question comes within the proscription of § 908-04, N.D.C.C., and is, therefore, void. The school district maintains that the damages occasioned by Mrs. Walker's breach of contract are extremely difficult to ascertain and, thus, the clause in question is valid as an exception to the statutory prohibition. We hold that the contract clause providing for fixed damages is valid and we affirm the decision of the district court.

[¶5] Pursuant to § 9-08-04, N.D.C.C., our primary consideration is whether the damages stemming from a particular breach of contract are "impracticable" or "extremely difficult" to ascertain--a prerequisite to the use of a fixed-damage provision. The determination of this issue necessarily depends upon the facts of each particular case and in making this determination, we must look at the facts of each case as they appeared to the parties at the time the contract was made. *Hofer v. W. M. Scott Livestock Company,* 201 N.W.2d 410 (N.D. 1972).

[¶6] We recognize, initially, that in cases where an employee has breached an employment contract, the damages generally recoverable and, thus, properly anticipated, are limited to the costs of replacing the employee. We are not unmindful of the fact that this is a public contract and that it is the public as a whole that suffers when such a contract is breached. In this respect, this case is not unlike those cases in which a governmental body liquidates the amount of damages it may recover for a delay in the performance of a public construction contract. Although the damages suffered by the governmental body itself may be readily ascertainable, the damages sustained by the public are not readily ascertainable, and, on such basis, liquidated-damages provisions are generally upheld, even in States having statutes similar to § 9-08-04, N.D.C.C. *See, e.g., Dave Gustafson & Co. v. State*, 156 N.W.2d 185 (S.D. 1968); *Six Companies of California v. Joint Highway Dist. No. 13 of California*, 110 F.2d 620 (9th Cir. 1940), *rev'd on other grounds* in 311 U.S. 180, 61 S. Ct. 186, 85 L. Ed. 114.

[¶7] The courts have recognized that the actual loss is suffered by the public for whose benefit such contracts are made and that because of the extreme difficulty in ascertaining this public loss, liquidated-damages provisions in those cases are properly enforced.

[¶8] Although we have not previously decided this issue, we indicated in *Hofer, supra* 201 N.W.2d at 416, that:

> "There may be circumstances involved in public contracts and other laws relating to public contracts that justify a more liberal treatment of forfeiture clauses in public contract cases."

These words from *Hofer* indicate an awareness of the issue with which we are presently confronted. Thus, when we consider the damages caused by a teacher's breach of an employment contract, we cannot ignore the interruption to the school system and the resultant debilitating effect such interruption has upon the learning process of students in the school system. The possibility that the replacement teacher who was obtained may be less experienced or less qualified and, thus, a less effective instructor must also be considered in the assessment of damages. It would not be possible at the time of contracting to foresee all these elements of damage that may occur. Even if known, it would be extremely difficult to evaluate these damages on a monetary basis. These losses to the public are no less the proper subject of a liquidated-

damage provision than are the losses sustained by the public in delay-of-performance situations. In either case, the damage to the public is real, although most difficult to evaluate. Such damages are not legally compensable but constitute a public injury which the school district was entitled to consider. For these reasons we find that the present case falls within the exception of § 9-08-04, N.D.C.C.

[¶9] A contract provision, to be upheld as a valid liquidated damages clause, must not only meet the statutory requirement of § 9-08-04, N.D.C.C., but also must fulfill the requirements imposed by case law. In *Hofer, supra*, in paragraph 2 of the syllabus, we delineated these requirements:

> "Under South Dakota law a provision for payment of a stipulated sum as a liquidation of damages will be sustained if it appears that at the time the contract was made the damages in the event of a breach will be incapable or very difficult of accurate estimation, that there was a reasonable endeavor by the parties to fix their compensation, and that the amount stipulated bears a reasonable relation to the probable damages and is not disproportionate to any damages reasonably to be anticipated."

Although in *Hofer* we were construing South Dakota law, the South Dakota statutes are similar to § 9-08-04, N.D.C.C. We find the rationale of that case in accord with § 9-08-04, N.D.C.C., and, accordingly, adopt Hofer as a proper construction of such section.

[¶10] *Hofer* requires, in addition to the statutory requisite, that there be a reasonable endeavor by the parties to fix their compensation and that the amount stipulated bears a reasonable relationship, and is not disproportionate to, any anticipated damages.

[¶11] It is argued by Mrs. Walker that there was no endeavor to fix compensation in this case, as evidenced by the fact that the same liquidated-damages provision was used in all teacher employment contracts, regardless of differences in individual characteristics of the teachers. We do not find that the inclusion of a standard liquidated-damages clause in more than one contract is necessarily incompatible with a reasonable endeavor to pre-determine compensatory damages. The law requires only that the purpose of the clause be primarily to pre-determine damages, as opposed to imposing a penalty for breach. In this regard, it is to be noted that the liquidated-damages provision under consideration is graduated, i.e., it provides for progressively larger payments for breach of the contract as the time for commencing the school term approaches. We recognized in Hofer that this factor indicates a bona fide attempt to pre-determine damages. It is reasonable to estimate that it will be more difficult and more costly to replace a teacher who breaches a contract during the school term or shortly before it commences than to replace one who breaches shortly after the contract is signed. The fact that this provision is contained in more than one employment contract does not render it any less an endeavor to fix damages. Furthermore, the argument that the provision in question was intended as an insurance of performance is weakened when one considers § 15-47-28, N.D.C.C., which provides:

> "Suspension of teacher's certificate for breach of contract.--In the event of breach of contract on the part of a teacher, the superintendent of public instruction shall suspend such teacher's certificate for a period not to exceed one year, during which time it shall be unlawful for such teacher to receive payment for teaching in the public schools of North Dakota."

It may be seen that § 15-47-28, N.D.C.C., imposes a severe penalty upon a teacher for breach of contract. In light of the provisions of § 15-47-28, it is not persuasive to argue that the school district intended to insure performance by the imposition of what would be a much lesser penalty.

[¶12] The second requirement of *Hofer* is that the amount of stipulated damages must bear a reasonable relationship to the damages that may be expected to result from a breach. In the instant case the amount of damages was fixed at 4 percent of Mrs. Walker's salary, or $252. When one considers the damages that may be caused by a breach, the dollar amount in this case is reasonable. Although we do not wish to imply that this factor is to be determined with mathematical preciseness, we do note that the percentage in this case is much smaller than the 14 1/2 percent rate that was declared void in Hofer. After applying the guidelines of Hofer, and § 9-08-04 N.D.C.C., and after considering the facts of this particular case, we conclude that the contract clause in question is valid.

[¶13] We turn now to two secondary arguments urged by Mrs. Walker. The first is that the school district "released" Mrs. Walker and that there was, therefore, no breach of contract. There was no release in this case, as that word is used in its legal sense. The school district treated Mrs. Walker's actions as a breach of her teacher's contract. Her release was subject to the payment of the liquidated damages as required by her contract; thus, this argument is not persuasive. * * * *

[¶14] It is incumbent upon the parties seeking enforcement of a liquidated-damages clause to prove that the clause is valid as an exception to the general prohibition of § 9-08-04, N.D.C.C. Hofer, supra. * * * * We hold that the school district has sustained its burden of proof.

[¶15] The decision of the district court is affirmed.

Questions:

1. Did the court care, in applying the test, whether the school district actually suffered any real damages? In a case decided with *Walker*, *Bottineau Public School Dist. No. 1 v. Zimmer*, 231 N.W.2d 178, 179 (N.D. 1975), the court said:

> Of the issues presented and argued by Mr. Zimmer, we find but one that is not covered . . . in the *Bowbells* case. That is Mr. Zimmer's contention that the school district may not recover the damages stipulated in the contract because it found a replacement for Mr. Zimmer at a lower salary and, thus, suffered no actual damage.

Id. at 179. Given what the court said in *Walker*, what should be its response? But consider the next question.

2. Though the test is ostensibly aimed at conditions existing at formation, courts are not always consistent regarding the evidence they allow to show a reasonable or unreasonable relation to actual damages. The Restatement (Second) of Contracts itself comments, "If on the other hand, proof of loss is slight, less latitude is allowed in [approximating anticipated or actual harm]. If, to take an extreme case, it is clear that no loss at all has occurred, a provision fixing a substantial sum as damages is unenforceable." Restatement (Second) of Contracts § 356 cmt. b (1981). Should that change your answer to Question 1?

The Uniform Commercial Code Article 2-718(1), applicable to a sale of goods, includes actual harm as part of the formal rule: "(1) Damages for breach by either party may be liquidated in the agreement but only at an amount which is reasonable in the light of the anticipated or actual harm caused by the breach, the difficulties of proof of loss, and the inconvenience or nonfeasibility of otherwise obtaining an adequate remedy. A term fixing unreasonably large liquidated damages is void as a penalty."

The common law rule actually presents something of a dilemma: Element 1 requires that damages at the time of formation be "incapable or very difficult of accurate estimation," but element 2 requires a reasonable effort to estimate, and element 3 requires that "the amount stipulated bears a reasonable relation to the probable damages and is not disproportionate to any damages reasonably to be anticipated." Element 1 says it should be hard to do, and elements 2 and 3 say we did it regardless. The litigant trying to prove this test has a fine line to walk. If, after breach, actual damages are in reality clear and certain, evidence for each of those elements looks different in hindsight. If the actual damages, when known, are clear and much less than the liquidated sum, this difference will pull the court toward holding the stipulated sum a penalty.

3. How can a stipulated amount be both "incapable or very difficult of accurate estimation" and also have "a reasonable relation to the probable damages"? This may make little sense in theory. What evidence did the court accept in the case that allowed it to apply the test?

4. Why is the court so concerned about liquidated damages—what is the purpose of the test? Would a liquidated damages clause requiring that damages "ten times the amount of actual damages" pass the test?

5. If the parties have freely chosen a remedy in a contract that is not unconscionable, should not the court award it? Is not unconscionability an ultimate backstop doctrine for liquidated damage provisions, too? Could the test for unconscionability substitute in for the liquidated damages test? Courts often call a clause failing the test an "unconscionable penalty," *see Garziano v. Louisiana Log Home Co.*, 569 Fed. Appx. 292, 302 (5th Cir. 2014), and a few courts have subsumed the entire liquidated damages test under unconscionability doctrine, *see Arrowhead School Dist. No. 75 Park Cty. v. Klyap*, 79 P.3d 250 (Mont. 2003) (resolving to "analyze liquidated damages clauses from the perspective of whether or not the clause is unconscionable"). The Uniform Commercial Code's comment 1 to § 2-718 (2-718(1) was quoted in part above in question 2) suggests that unconscionability is an overarching doctrine that applicable in addition to the liquidated damages test: "An unreasonably small amount . . . might be stricken under the section on unconscionable contracts or clauses."

6. Agreements to Limit Damages

Joyce UNDERWOOD v. NATIONAL ALARM SERVICES, INC.

Tenn. App. (May 14, 2007)

LEE, J.

OPINION

* * * *

I. Background

[¶1] This negligence case stems from a house fire which occurred at the Knoxville home of Joyce Underwood in the early morning hours of July 21, 1999. Two children died as a result of the blaze, another two were injured, and Ms. Underwood sustained a heart attack and other injuries during the incident. Before discussing the details of the fire, we will recount the legal framework that forms the basis for this lawsuit.

[¶2] Approximately five months before the fire, Ms. Underwood contracted with the defendant, National Alarm Services, Inc., d/b/a Volunteer Alarm, to install a smoke detector and provide monitoring services for the security and smoke detection system at her house, where she also operated a licensed day care facility. The system installed at Ms. Underwood's house was selected to meet state day care standards. Ms. Underwood signed an "Alarm System Monitoring and Installation Agreement" ("Agreement") with National Alarm on February 3, 1999, which provided a limitation of liability as follows:

> Subscriber understands and agrees that if Company should be found liable for loss or damage due from a failure of Company to perform any of the obligations herein, including but not limited to installation, maintenance, monitoring or service or the failure of the system or equipment in any respect whatsoever, Company's liability shall be limited to Two Hundred Fifty ($ 250) Dollars as liquidated damages/limitation of liability and not as a penalty and this liability shall be exclusive; and that the provisions of this section apply if loss or damage, irrespective of cause of origin, results directly or indirectly to persons or property from performance or non-performance of the obligations imposed by this contract, or from negligence, active or otherwise, [of] its agents, assigns or employees.
>
> If [S]ubscriber wishes Company to assume limited liability in lieu of the liquidated damages as herein above set forth, Subscriber may obtain from Company a limitation of liability by paying an additional monthly service charge to Company. If Subscriber elects to exercise this option, a rider shall be attached to this agreement setting forth the terms, conditions and the amount of the limited liability, and the additional monthly charge. Such rider and additional obligation shall in no way be interpreted to hold Company as an insurer.

[¶3] The fee for National Alarm's monthly monitoring service was $ 19.95. According to an affidavit provided by the company's president, Steve Choura, Ms. Underwood paid the initial monitoring fee in February of 1999 when she signed the contract, but she did not pay any monitoring fees after that. Ms.

Underwood's account was in default at the time of her house fire in July of 1999. However, neither party contends that National Alarm terminated its contract with Ms. Underwood for nonpayment, although it had the option to do so.

[¶4] On the night of the blaze, Joyce Underwood was asleep in her Knoxville residence. Staying with her that night were four young relatives, Joshua Underwood, age 10; Isaiah Underwood, age 6; 9-year-old Stefon Colquitt; and Jonesha Colquitt, age 8. According to Ms. Underwood's deposition, she was awakened by her neighbor, Robert Dixon, Jr. After she was awakened, she heard the smoke detector in her hall and the alarm system going off. Joshua Underwood also confirmed that he could hear the alarms while he was running through the house and after he got out of the house.

[¶5] Several neighbors also heard the alarms. Robin Johnson stated in her deposition that an alarm of some sort woke her up at 12:30 a.m., and she thought that it was a car alarm. Ms. Johnson said she knew the exact time because she looked at her bedside clock. She then drifted back to sleep with the alarm still ringing. Ms. Johnson said she was awakened a short time later by a "loud banging in my backyard." In her affidavit, Ms. Johnson stated that when she looked out the window, she saw her neighbor, Mr. Dixon, beating on the patio door of Ms. Underwood's home. In response to her inquiry, Mr. Dixon stated that Ms. Underwood's house was on fire and he was trying to wake her. At that time, Ms. Johnson stated that she noticed smoke coming from Ms. Underwood's home. She also said that "there were no emergency vehicles of any kind assisting despite the continual sounding of the alarm. It wasn't until some time later that the emergency vehicles arrived."

[¶6] According to Mr. Choura, National Alarm contacted 911 within 42 seconds of receiving the signal from the smoke detector system at Ms. Underwood's residence. Upon doing so, National Alarm was informed that the fire had already been reported by a neighbor and emergency units were on their way to the home. In his affidavit, Mr. Choura did not state what time National Alarm received the signal from Ms. Underwood's alarm system, nor did he specify the time that National Alarm contacted 911. Evidence provided by Ms. Underwood indicates that National Alarm did not notify 911 of the fire until 1:39 a.m.

[¶7] Although everyone in the Underwood home escaped the fire, Stefon and Jonesha Colquitt died at the hospital a few hours later as a result of smoke inhalation and carbon monoxide poisoning. Joshua and Isaiah Underwood were treated for burns, smoke inhalation, and carbon monoxide poisoning. [Joshua Underwood died on January 29, 2002, as a result of an unrelated automobile accident.] While trying to save the children, Ms. Underwood suffered a heart attack, for which she also required medical treatment.

[¶8] Gary Young, a fire investigator employed by Allstate Insurance Company, testified that the fire began due to a short in an electrical cord. The leg of a freezer had been placed on the power cord, resulting in the cord's failure. He stated that the fire in Ms. Underwood's home burned for a maximum of 30 minutes, including the time it took firefighters to extinguish the blaze. Mr. Young said that the room where the freezer was kept sustained severe fire damage, and it was the only room that showed evidence of "significant structural damage" as a result of the fire. He also stated that none of the bedrooms had fire damage, although the bedrooms did incur smoke damage.

[¶9] Ms. Underwood filed suit on behalf of herself and Joshua and Isaiah Underwood, alleging that National Alarm was negligent in virtually every aspect of its operations relating to the alarm system in her home. National Alarm filed a motion for summary judgment, which was granted by the trial court. Ms. Underwood appeals.

II. Issue

[¶10] The sole issue presented for review, as restated, is whether the trial court erred by granting summary judgment to National Alarm. * * * *

IV. Analysis

[¶12] In its order granting summary judgment to National Alarm, the trial court made the following findings:

> 1. At the time of the fire in July, 1999, the Plaintiff Joyce Underwood had not paid fees due under the service contract. As such, no duty was owed by the Defendants. Failure by the Plaintiff to pay the fees under the contract was a substantial breach of the contract.
>
> 2. The exculpatory clauses and the clauses limiting liability are valid under Tennessee law. Those exculpatory clauses and limits of liability form a part of this contract and operate as intended to limit liability.
>
> 3. The Defendant has established through expert proof, both deposition and affidavit, that it was not negligent in the monitoring of this fire on July 21, 1999. The Plaintiff has presented no counter-veiling [sic] proof to create a material issue of fact.

We will review each of these findings separately.

A. Duty

[¶13] To establish her negligence claim, Ms. Underwood must prove: (1) a duty of care owed to her by National Alarm; (2) a breach of that duty; (3) an injury or loss; (4) causation in fact; and (5) proximate or legal cause. *Coln v. City of Savannah*, 966 S.W.2d 34, 39 (Tenn. 1998) (*citing Bradshaw v. Daniel*, 854 S.W.2d 865, 869 (Tenn. 1993)). Whether a duty of care is owed is a question of law to be decided by the trial court. *Id.*

[¶14] In order to prevail on its motion for summary judgment, National Alarm must affirmatively negate an essential element of Ms. Underwood's claim or conclusively establish an affirmative defense. Thus, if National Alarm established that it did not owe a duty to Ms. Underwood because she failed to pay her monitoring fees for several months, then National Alarm would be entitled to judgment as a matter of law.

[¶15] National Alarm asserts that it owed no duty to Ms. Underwood because she had already breached the contract by failing to pay the monthly monitoring fee. The Agreement provided as follows regarding nonpayment:

> In the event the Customer fails to make timely payments for monitoring services or files for bankruptcy protection, the Company may at it[s] sole discretion terminate monitoring services, terminate this Agreement and in such an event all payments due under this Agreement or any renewal shall be immediately due and owing by Customer to the Company.

[¶16] Thus, under the provisions of the Agreement, National Alarm could have terminated its contract with Ms. Underwood because she did not pay the $ 19.95 per month fee. If National Alarm had terminated the Agreement, it would not owe a duty to Ms. Underwood on that basis. However, there is no evidence in the record to indicate, nor does National Alarm assert, that it exercised its right to terminate the Agreement. Therefore, National Alarm was bound by the terms of its Agreement with Ms. Underwood, and it owed Ms. Underwood a duty to perform the obligations of that contract with reasonable care. * * * *

[¶17] We find that National Alarm owed a duty to Ms. Underwood as a matter of law, and the trial court erred by finding otherwise.

B. Limitation of Liability/Liquidated Damages Clause

[¶18] Although the trial court referred to "exculpatory clauses and clauses limiting liability" in its order, the parties' contract did not contain an exculpatory clause, but rather a limitation of liability/liquidated damages clause. If this clause is valid, Ms. Underwood may only recover a maximum of $ 250, even if she is able to prove all of the allegations enumerated in her complaint.

[¶19] In Tennessee, clauses limiting liability for negligence or breach of contract have generally been upheld in the absence of fraud or overreaching. *Houghland v. Security Alarms & Servs., Inc.*, 755 S.W.2d 769, 773 (Tenn. 1988). Consistent with the parties' freedom to construct their own bargain, they are free to allocate liability for future damages, provided that such clauses do not violate public policy. * * * * Furthermore, limitations of liability in alarm service contracts have been enforced by this state's highest court, as well as the courts of many other jurisdictions. [Long string-cite omitted.]

[¶20] In *Houghland*, the Tennessee Supreme Court upheld the validity of an alarm services contract with terms very similar to those agreed to by National Alarm and Ms. Underwood, describing the contract as follows:

> The original contract recited that Security Alarms was not in the business of writing burglary or other kinds of insurance. . . . The contract also contained a liquidated damages clause which fixed the liability of appellant at a specified sum. This amount was agreed upon as liquidated damages and as the exclusive remedy unless the subscriber desired the appellant to assume greater liability on a graduated scale of increasing rates. No such additional coverage was purchased by the subscribers.

755 S.W.2d at 771. After determining that there was no proof of fraud or intentional misrepresentation by the alarm company, the Court found the liquidated damages clause to be a valid limitation upon any recovery by the homeowners. *Id*. at 774.

[¶21] In the case at bar, Ms. Underwood signed a contract with language that bears a remarkable likeness to the contract at issue in Houghland. By signing the contract, Ms. Underwood acknowledged that National Alarm was not an insurer of property. The contract also provided that, in the event National Alarm was held liable for any loss relating to the provision of alarm services under the terms of the contract, then National Alarm's liability would be limited to $ 250. The contract further stated that the sum was liquidated damages, not a penalty, and that the remedy was exclusive. Ms. Underwood had the opportunity to pay an additional fee for National Alarm to assume greater liability than the $ 250 limit established by the contract; however, she opted not to incur the extra expense.

[¶22] Ms. Underwood has not alleged any fraud or intentional misrepresentation that might provide this Court with justification for voiding the contract or any portion thereof. Although this may be a harsh result, given the substantial damages sustained by Ms. Underwood and her family in the house fire, we are bound by precedent to enforce the liquidated damages clause that was signed by Ms. Underwood and a National Alarm representative.

[¶23] In the alternative, Ms. Underwood argues that the liquidated damages clause is ambiguous and therefore, pursuant to the rules of contract interpretation, should be construed against the drafter. This is a correct statement of the law; however, we find it inapplicable to this contract. There is no ambiguity in the limitation of liability at issue in this case; indeed, it is a very sweeping and all-inclusive clause. The allegations of wrongful conduct made by Ms. Underwood fall within the scope of this clause. Therefore, Ms. Underwood's recovery, if any, is limited to $ 250. * * * *

V. Conclusion

[¶25] * * * * [We affirm the trial court's ruling that the limitation of liability/liquidated damages clause is valid. We vacate and remand this case to the trial court for further proceedings consistent with this opinion. * * * *

Questions:

1. Ms. Underwood promised to pay the monthly charge, and National Alarm promised to do whatever it promised to do. Yet Underwood did not pay the monthly fee after February, and the fire happened in July. Usually, mutual promises are constructive conditions. Do we have constructive conditions here, or was the "evidence sense and meaning of the parties" to create an express condition? Why was National Alarm still bound? What happened to the termination right? You know enough to state the holding with much greater clarity than the court stated it.

2. On the limitation of remedy clause, several courts have now held that, though such a clause is enforceable with regard to the promisor's negligence, it will not be for the promisor's gross negligence. How comfortable are you that you can discern in advance the difference between ordinary and gross negligence? *See, e.g., Abacus Federal Savings Bank v. ADT Security Servs., Inc.*, 18 N.Y. 3d 675 (2012) (finding gross negligence possible on the facts alleged and reversing the Appellate Division (which found only ordinary negligence possible), reversing the Supreme Court (which found gross negligence possible)). If you as a judge dislike the holding in *Underwood*, how will that affect your thinking about gross negligence in alarm company cases?

3. Why did the court not apply the *Bowbells Publ. Sch. Dist. No. 14 v. Walker* rule to the clause?

4. Purveyors of dangerous experiences (sky diving schools, river rafting adventure tours, fitness clubs, shooting ranges, etc.) often require customers to sign a release and waiver of liability, including liability for the seller's negligence. The document often requires the signer to assume the risk of death and continued life with catastrophic injuries. The enforceability of such waivers varies from state to state. Edward K. Cheng, Ehud Guttel, and Yuval Procaccia in *Unenforceable Waivers*, 76 Vand. L. Rev. 571 (2023), report that Louisiana has a blanket statutory prohibition; other states have statutes that cover "specific contexts,

such as skiing" or health clubs; and courts are hostile to waivers that extend beyond ordinary negligence, or in the context of employment, medical malpractice, or products liability. *Id.* at 580–81. And, "[i]n other contexts, enforceability can vary widely by state." *Id.* at 581. Parents also routinely sign waivers on "behalf of their children." *Id.* at 582. Even when the law declares them unenforceable, "declarations of unenforceability are ignored" by those who ask for the waivers. *Id.* The unenforceable waivers deter plaintiffs even when the waivers are unenforceable, the authors report. *Id.* at 588–92. "To discourage unenforceable waivers then, the law must somehow penalize their use," the authors assert. *Id.* at 593. Would that be a good idea?

C. Specific Performance

Richard A. ALBA et al. v. Jean-Claude KAUFMANN

N.Y. Supr. Ct. App. Div. (2006), 810 N.Y.S.2d 539

CREW III, J.

[¶1] Defendant is the owner of approximately 37 acres of real property located in the Town of Stephentown, Rensselaer County. The property, which contains a pond and is located in a wooded area, is improved with a 19th-century farmhouse. Defendant and his spouse, Christine Cacace, reside in New York City and use the Rensselaer County property as a weekend or vacation home.

[¶2] Defendant lost his full-time job in 1998 and, having apparently grown tired of the upkeep associated with maintaining an older home, decided to sell the property in 2001. Although defendant took the property off the market following the events of September 11, 2001, when Cacace lost her job in December 2003, financial considerations prompted defendant to again list the property for sale.

[¶3] Plaintiffs were shown defendant's property and, after brief negotiations, offered the full asking price of $325,000. The parties executed a contract for sale in May 2004, and plaintiffs thereafter paid a deposit, obtained a mortgage commitment and, apparently, procured a satisfactory home inspection and title insurance. A closing was scheduled for July 15, 2004 but, on June 23, 2004, Cacace sent plaintiffs an e-mail indicating that she and defendant had "a change of heart" and no longer wished to go forward with the sale. Plaintiffs sent a reply e-mail two days later expressing their regret that the impending sale allegedly was causing Cacace distress, but indicating their intent to go forward with the scheduled closing. Cacace responded with another e-mail on June 27, 2004, this time informing plaintiffs that she suffered from multiple sclerosis and alleging that the "remorse and dread" over the impending sale was making her ill.

[¶4] When defendant refused to close, plaintiffs commenced this action seeking specific performance of the underlying real estate contract. Defendant answered and raised various affirmative defenses, including, insofar as is relevant to this appeal, that plaintiffs had an adequate remedy at law and that specific performance would lead to an inequitable result. Plaintiffs thereafter moved for summary judgment, but Supreme Court denied the motion, finding questions of fact regarding whether specific performance is plaintiffs' only remedy and whether performance of the contract would result in an unreasonable hardship. This appeal by plaintiffs ensued.

[¶5] There must be a reversal. In order to establish their entitlement to summary judgment, plaintiffs were required to demonstrate that they substantially performed their contractual obligations and were ready, willing and able to fulfill their remaining obligations, that defendant was able but unwilling to convey the property and that there is no adequate remedy at law (*see EMF Gen. Contr. Corp. v Bisbee*, 6 A.D.3d 45, 51 [2004], lv dismissed 3 N.Y.3d 656 [2004], lv denied 3 N.Y.3d 607 [2004]; *Morgan v Eitt*, 111 A.D.2d 586, 587 [1985]). Plaintiffs plainly discharged that burden here. After executing the underlying contract, plaintiffs paid a deposit, obtained a mortgage commitment, demonstrated that they had the financial wherewithal to purchase what was to be for them a vacation home, obtained a satisfactory home inspection and procured title insurance. In short, the record demonstrates that plaintiffs were ready, willing and able to close on July 15, 2004 and, but for defendant's admitted refusal to do so, would have consummated the transaction.

[¶6] As to the remedy plaintiffs seek, the case law reveals that "the equitable remedy of specific performance is routinely awarded in contract actions involving real property, on the premise that each parcel of real property is unique" (*EMF Gen. Contr. Corp. v Bisbee, supra* at 52). Although certain defenses do exist including, insofar as is relevant here, unreasonable hardship, "'the court's discretion to grant or deny specific performance of a contract for the sale of realty is not unlimited; unless the court finds that granting a decree of specific performance would be a drastic or harsh remedy, or work injustice, the court must direct specific performance'" (*id.*, quoting 91 *NY Jur 2d, Real Property Sales and Exchanges* § 204). Moreover, "[v]olitional unwillingness, as distinguished from good faith inability, to meet contractual obligations furnishes neither a ground for cancellation of the contract nor a defense against its specific performance" (*Meisels v 1295 Union Equities Corp.,* 306 A.D.2d 144, 145 [2003]).

[¶7] Here, defendant argues and Supreme Court found that summary judgment was inappropriate because defendant raised a question of fact as to the uniqueness of the property and, hence, whether plaintiffs had an adequate remedy at law, and further, whether ordering specific performance would work an undue hardship. We disagree. As noted previously, each parcel of real property is presumed to be unique (*see EMF Gen. Contr. Corp. v Bisbee, supra* at 52), and defendant's conclusory and self-serving assertion — unaccompanied by any evidence of comparable listings or sales — that there are many similar properties for sale in and around Rensselaer County is insufficient to raise a question of fact as to the uniqueness of the property. Hence, in our view, Supreme Court erred in finding that defendant tendered sufficient admissible proof to raise a question of fact as to whether plaintiffs had an adequate remedy at law.

[¶8] We reach a similar conclusion with regard to defendant's claim of undue hardship. Defendant's entire argument on this point is premised upon the allegedly deleterious effects that the impending sale of the property had upon Cacace's health. Specifically, defendant contends that the stress from the proposed sale exacerbated Cacace's fatigue and other physical symptoms of her disease. It is critical to note, however, that Cacace is not a titled owner of the property in question, nor is she a signatory to the underlying real estate contract. Thus, defendant is asking this Court to effectively set aside his contractual obligations not because the proposed sale allegedly constitutes an undue hardship for him but, rather, because of the purported effect such sale would have upon his wife. This we cannot do.

[¶9] Even accepting, for purposes of this discussion, that the alleged exacerbation of Cacace's symptoms is both genuine and causally related to the proposed sale of property, as she is not a party to the contract, her connection to the transaction is simply too attenuated for defendant to claim undue hardship. In our view, permitting a third party who is not a signatory to a real estate contract, such as a spouse or, potentially, a child, sibling or parent, to assert, via the titled owner, an undue hardship claim by voicing objection to or otherwise contending that the proposed sale is simply too much to bear would

interject uncertainty and chaos into the otherwise orderly world of contract law. Simply put, permitting a defendant to raise an undue hardship defense under the circumstances present here would place a nearly impossible burden upon potential purchasers of real property — namely, to ascertain whether any of the signatories' relatives had any potential objection to the sale in question.

[¶10] Moreover, even if we were to accept defendant's premise that the sanctity of the marital relationship and Cacace's longstanding attachment to the property at issue could form the basis for him to claim undue hardship, the medical evidence submitted in opposition to plaintiffs' motion falls far short of its mark. Preliminarily, we note that even Cacace acknowledged in her June 27, 2004 e-mail to plaintiffs regarding the then impending sale that she had received "assurances by all that [she would] get over it," and her e-mail suggests that those assurances were derived, in part, from professional counseling sessions. Additionally, the affidavit from defendant's expert, Daniel Silverman, who admittedly based his opinion upon the assumption that the stress allegedly experienced by Cacace was sincere, establishes, at best, that such stress "could explain" the change in symptoms that Cacace described, "could explain" the increase in the degree of fatigue Cacace purportedly experienced and "could account" for the increased limb weakness Cacace reported. And the unsworn letter from Cacace's treating physician, even if considered, reflects only that "[a]n increased level of stress can have the potential of exacerbating multiple sclerosis." To interpret such statements as drawing any sort of definitive correlation between the proposed sale and the onset or exacerbation of Cacace's symptoms would be entirely speculative. Thus, in our view, the record as a whole fails to contain sufficient admissible proof to raise a question of fact as to whether Cacace's medical condition constitutes an undue hardship for defendant. Accordingly, Supreme Court erred in denying plaintiffs' motion for summary judgment.

Ordered that the order is reversed, on the law, with costs, and plaintiffs' motion granted.

Question: The presumption of a real estate parcel's uniqueness is traditionally difficult to overcome. It has been questioned in a few decisions. With what kind of real estate should it be most vulnerable?

BEVERLY GLEN MUSIC, INC. v. WARNER COMMUNICATIONS, INC.

Cal. App. (1986), 178 Cal. App. 3d 1143

OPINION

KINGSLEY, Acting P. J.

[¶1] The plaintiff appeals from an order denying a preliminary injunction against the defendant, Warner Communications, Inc. We affirm.

Facts

[¶2] In 1982, plaintiff Beverly Glen Music, Inc., signed to a contract a then-unknown singer, Anita Baker. Ms. Baker recorded an album for Beverly Glen which was moderately successful, grossing over $1 million. In 1984, however, Ms. Baker was offered a considerably better deal by defendant Warner Communications. As she was having some difficulties with Beverly Glen, she accepted Warner's offer and notified plaintiff that she was no longer willing to perform under the contract. Beverly Glen then sued Ms. Baker and sought to have her enjoined from performing for any other recording studio. The injunction was denied, however, as, under Civil Code section 3423, subdivision Fifth, California courts will not enjoin the breach of a personal service contract unless the service is unique in nature and the performer is guaranteed annual compensation of at least $6,000, which Ms. Baker was not.

[¶3] Following this ruling, the plaintiff voluntarily dismissed the action against Ms. Baker. Plaintiff, however, then sued Warner Communications for inducing Ms. Baker to breach her contract and moved the court for an injunction against Warner to prevent it from employing her. This injunction, too, was denied, the trial court reasoning that what one was forbidden by statute to do directly, one could not accomplish through the back door. It is from this ruling that the plaintiff appeals.

Discussion

[¶4] From what we can tell, this is a case of first impression in California. While there are numerous cases on the general inability of an employer to enjoin his former employee from performing services somewhere else, apparently no one has previously thought of enjoining the new employer from accepting the services of the breaching employee. While we commend the plaintiff for its resourcefulness in this regard, we concur in the trial court's interpretation of the maneuver.

[¶5] "It is a familiar rule that a contract to render personal services cannot be specifically enforced." *(Foxx v. Williams* (1966) 244 Cal.App.2d 223, 235 [52 Cal. Rptr. 896].) An unwilling employee cannot be compelled to continue to provide services to his employer either by ordering specific performance of his contract, or by injunction. To do so runs afoul of the Thirteenth Amendment's prohibition against involuntary servitude. (*Poultry Producers etc. v. Barlow* (1922) 189 Cal.278, 288 [208 P. 93].) However, beginning with the English case of *Lumley v. Wagner* (1852) 42 Eng. Rep. 687, courts have recognized that, while they cannot directly enforce an affirmative promise (in the *Lumley* case, Miss Wagner's promise to perform at the plaintiff's opera house), they can enforce the negative promise implied therein (that the defendant would not perform for someone else that evening). Thus, while it is not possible to compel a defendant to perform his duties under a personal service contract, it is possible to prevent him from employing his talents anywhere else. The net effect is to pressure the defendant to return voluntarily to his employer by denying him the means of earning a living. Indeed, this is its only purpose, for, unless the defendant relents and honors the contract, the plaintiff gains nothing from having brought the injunction.

[¶6] The California Legislature, however, did not adopt this principle when in 1872 it enacted Civil Code section 3423, subdivision Fifth, and Code of Civil Procedure section 526, subdivision 5. These sections both provided that an injunction could not be granted:

> "To prevent the breach of a contract the performance of which would not be specifically enforced." In 1919, however, these sections were amended, creating an exception for: "a contract in writing for the rendition or furnishing of personal services from one to another where the minimum compensation for such service is at the rate of not less than six

> thousand dollars per annum and where the promised service is of a special, unique, unusual, extraordinary or intellectual character . . .".

[¶7] The plaintiff has already unsuccessfully argued before the trial court that Ms. Baker falls within this exception. It has chosen not to appeal that judgment, and is therefore barred from questioning that determination now. The sole issue before us then is whether plaintiff—although prohibited from enjoining Ms. Baker from performing herself—can seek to enjoin all those who might employ her and prevent them from doing so, thus achieving the same effect.

[¶8] We rule that plaintiff cannot. Whether plaintiff proceeds against Ms. Baker directly or against those who might employ her, the intent is the same: to deprive Ms. Baker of her livelihood and thereby pressure her to return to plaintiff's employ. Plaintiff contends that this is not an action against Ms. Baker but merely an equitable claim against Warner to deprive it of the wrongful benefits it gained when it "stole" Ms. Baker away. Thus, plaintiff contends, the equities lie not between the plaintiff and Ms. Baker, but between plaintiff and the predatory Warner Communications company. Yet if Warner's behavior has actually been predatory, plaintiff has an adequate remedy by way of damages. An injunction adds nothing to plaintiff's recovery from Warner except to coerce Ms. Baker to honor her contract. Denying someone his livelihood is a harsh remedy. The Legislature has forbidden it but for one exception. To expand this remedy so that it could be used in virtually all breaches of a personal service contract is to ignore over 100 years of common law on this issue. We therefore decline to reverse the order.

The order is affirmed.

Question: Though Ms. Baker was successful, other performers have not been, including boxer Ernie Shavers, *Madison Square Garden Boxing, Inc. v. Shavers*, 434 F. Supp. 449 (S.D.N.Y. 1977); singer James Brown, *King Records v. Brown*, 252 N.Y.S.2d 988 (Supr. Ct. App. Div. (1964); and actress Bette Davis, *Warner Bros. Pictures, Inc. v. Nelson*, [1937] 1 K.B. 209 (Eng.) (1936) 3 All E.R. 160. One performer, William Comstock (known as "Billy House"), before being ordered not to perform, went so far as to claim that his services were not unique. *Harry Rogers Theatrical Enterps. v. Comstock*, 232 N.Y.S. 1 (Supr. Ct. App. Div. 1928). However, a recital in his contract admitted that they were:

> Next we have the uncontroverted fact that the ability of Comstock is regarded as unique upon the Albee-Keith circuit and that a substitute will not be accepted. Hence in this well-known vaudeville office Comstock cannot be replaced. Again, Comstock is now admittedly receiving a salary of $1,000 a week, which, in his work, is very large and compares most favorably with that received by the leaders in the scientific, artistic, and political world.

232 N.Y.S. at 3. The court even cited the fact that Comstock's co-defendant, who had tried to hire Comstock away from Harry Rogers, "was willing to risk a lawsuit and pay $1,000 a week to secure the services of Comstock." *Id.* at 4. Uniqueness, indeed. The court ended with a plea to basic reliance on the institution of contract:

> If the time shall ever come when a court of equity must stand helplessly by while unique and unusual theatrical performers may be induced to breach contracts with impunity, except for such damages as a jury may see fit to award at some distant date, theatrical corporations will find their business hampered by intolerable conditions.

Id. Where should the line be between the performers' and promoters' interests?

D. Agreements to Arbitrate

The Federal Arbitration Act ("FAA") requires courts to enforce promises to arbitrate. The most important provisions are sections 2 and 3:

> A written provision in * * * a contract evidencing a transaction involving commerce to settle by arbitration a controversy thereafter arising out of such contract or transaction, or the refusal to perform the whole or any part thereof, or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract, transaction, or refusal, shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.
>
> If any suit or proceeding be brought in any of the courts of the United States upon any issue referable to arbitration under an agreement in writing for such arbitration, the court in which such suit is pending, upon being satisfied that the issue involved in such suit or proceeding is referable to arbitration under such an agreement, shall on application of one of the parties stay the trial of the action until such arbitration has been had in accordance with the terms of the agreement, providing the applicant for the stay is not in default in proceeding with such arbitration.

Other provisions supplement. Section 4 provides a procedure to ask U.S. district courts to assist in compelling arbitration. Section 5 describes how arbitrators are chosen if the parties' agreement provides no means. Section 7 empowers arbitrators to compel witnesses or other evidence and gives U.S. district courts power to enforce arbitrators' summonses under threat of contempt. Section 9 specifies how an arbitration award can be enforced in court:

> If the parties in their agreement have agreed that a judgment of the court shall be entered upon the award made pursuant to the arbitration, and shall specify the court, then at any time within one year after the award is made any party to the arbitration may apply to the court so specified for an order confirming the award, and thereupon the court must grant such an order unless the award is vacated, modified, or corrected as prescribed in sections 10 and 11 of this title.

A judicially confirmed arbitration award is enforceable as a judgment of the court itself.

Because an arbitration award does not have the backing of the state or federal government until a judge confirms the award, one might think that there would be a chance for judicial review of what the arbitrator does. This would be mistaken. Section 10, which names the substantive grounds for vacatur of arbitration

awards,[*] allows relief only where "the award was procured by corruption, fraud, or undue means" or there was some misconduct by the arbitrators, including "where the arbitrators exceeded their powers." When do arbitrators exceed their powers? The US Supreme Court has held that they do not exceed their powers when they err in discerning or applying the law, even if they commit "a serious error." *Stolt-Nielsen S.A. v. AnimalFeeds Int'l Corp*., 559 U.S. 662, 671 (2010). But there are limits. *Stolt-Nielsen S.A.* reversed a decision of arbitrators reached not on the basis of the contract, the FAA, or state or federal law but in which the arbitration panel "imposed its own policy preference." *Id.* at 676. The Court condemned the panel because it "proceeded as if it had the authority of a common-law court to develop what it viewed as the best rule to be applied in such a situation." *Id.* at 673-74. The Court declined to decide whether another standard for vacating arbitration awards existed: "manifest disregard for the law." *Id.* at 672 n.3. This has been defined as where arbitrators "knew of the relevant [legal] principle, appreciated that this principle controlled the outcome of the disputed issue, and nonetheless willfully flouted the governing law by refusing to apply it." *Id.* (internal quotations omitted). Some courts have applied such a standard under the FAA. But the Court said that, if such a standard does exist, it was met in *Stolt-Nielsen S.A. Id.* In any event, so long as the arbitrators do not appear to be making law or flouting clear law, their errors are irrelevant.

For a while, it was not clear that the FAA was enforceable in state court (that state courts were required to follow it), but the US Supreme Court made clear that it was in *Moses H. Cone Mem'l Hosp. v. Mercury Constr. Corp.*, 460 U.S. 1 (1983). State law also often mandates agreed-upon arbitration, so state courts have their own opinions about what should be arbitrable. Not surprisingly, the policy choices made by state law actors do not always accord with what the federal courts see as required by the FAA. The following case addresses some disjuncts.

BUCKEYE CHECK CASHING, INC. v. CARDEGNA

U.S. (2005), 546 U.S. 440

JUSTICE SCALIA delivered the opinion of the Court.

[¶1] We decide whether a court or an arbitrator should consider the claim that a contract containing an arbitration provision is void for illegality.

I

[¶2] Respondents John Cardegna and Donna Reuter entered into various deferred-payment transactions with petitioner Buckeye Check Cashing (Buckeye), in which they received cash in exchange for a personal check in the amount of the cash plus a finance charge. For each separate transaction they

[*] Section 11 names grounds for "modifying or correcting" an award for largely formal errors "so as to effect the intent thereof and promote justice between the parties."

signed a “Deferred Deposit and Disclosure Agreement” (Agreement), which included the following arbitration provisions:

> “1. *Arbitration Disclosure* By signing this Agreement, you agree that i[f] a dispute of any kind arises out of this Agreement or your application therefore or any instrument relating thereto, th[e]n either you or we or third-parties involved can choose to have that dispute resolved by binding arbitration as set forth in Paragraph 2 below . . . .
>
> 2. *Arbitration Provisions* Any claim, dispute, or controversy . . . arising from or relating to this Agreement . . . or the validity, enforceability, or scope of this Arbitration Provision or the entire Agreement (collectively ‘Claim’), shall be resolved, upon the election of you or us or said third-parties, by binding arbitration . . . . This arbitration Agreement is made pursuant to a transaction involving interstate commerce, and shall be governed by the Federal Arbitration Act (‘FAA’), 9 U. S. C. Sections 1–16. The arbitrator shall apply applicable substantive law constraint [sic] with the FAA and applicable statu[t]es of limitations and shall honor claims of privilege recognized by law . . . .”

[¶3] Respondents brought this putative class action in Florida state court, alleging that Buckeye charged usurious interest rates and that the Agreement violated various Florida lending and consumer-protection laws, rendering it criminal on its face. Buckeye moved to compel arbitration. The trial court denied the motion, holding that a court rather than an arbitrator should resolve a claim that a contract is illegal and void ab initio. The District Court of Appeal of Florida for the Fourth District reversed, holding that because respondents did not challenge the arbitration provision itself, but instead claimed that the entire contract was void, the agreement to arbitrate was enforceable, and the question of the contract’s legality should go to the arbitrator.

[¶4] Respondents appealed, and the Florida Supreme Court reversed, reasoning that to enforce an agreement to arbitrate in a contract challenged as unlawful “ ‘could breathe life into a contract that not only violates state law, but also is criminal in nature . . . .’ ” 894 So. 2d 860, 862 (2005) (*quoting Party Yards, Inc. v. Templeton*, 751 So. 2d 121, 123 (Fla. App. 2000)). We granted certiorari. 545 U. S. ___ (2005).

II

A

[¶5] To overcome judicial resistance to arbitration, Congress enacted the Federal Arbitration Act (FAA), 9 U.S.C. §§1–16. Section 2 embodies the national policy favoring arbitration and places arbitration agreements on equal footing with all other contracts:

> “A written provision in . . . a contract . . . to settle by arbitration a controversy thereafter arising out of such contract . . . or an agreement in writing to submit to arbitration an existing controversy arising out of such a contract . . . shall be valid, irrevocable, and enforceable, save upon such grounds as exist at law or in equity for the revocation of any contract.”

Challenges to the validity of arbitration agreements “upon such grounds as exist at law or in equity for the revocation of any contract” can be divided into two types. One type challenges specifically the validity of the agreement to arbitrate. *See*, *e.g.*, *Southland Corp. v. Keating*, 465 U. S. 1, 4–5 (1984) (challenging the agreement to arbitrate as void under California law insofar as it purported to cover claims brought under

the state Franchise Investment Law). The other challenges the contract as a whole, either on a ground that directly affects the entire agreement (e.g., the agreement was fraudulently induced), or on the ground that the illegality of one of the contract's provisions renders the whole contract invalid.* Respondents' claim is of this second type. The crux of the complaint is that the contract as a whole (including its arbitration provision) is rendered invalid by the usurious finance charge.

[¶6] In *Prima Paint Corp. v. Flood & Conklin Mfg. Co.,* 388 U. S. 395 (1967), we addressed the question of who—court or arbitrator—decides these two types of challenges. The issue in the case was "whether a claim of fraud in the inducement of the entire contract is to be resolved by the federal court, or whether the matter is to be referred to the arbitrators." *Id.*, at 402. Guided by §4 of the FAA, we held that "if the claim is fraud in the inducement of the arbitration clause itself—an issue which goes to the making of the agreement to arbitrate—the federal court may proceed to adjudicate it. But the statutory language does not permit the federal court to consider claims of fraud in the inducement of the contract generally." *Id.*, at 403–404 (internal quotation marks and footnote omitted). We rejected the view that the question of "severability" was one of state law, so that if state law held the arbitration provision not to be severable a challenge to the contract as a whole would be decided by the court. *See id.*, at 400, 402–403.

[¶7] Subsequently, in *Southland Corp.*, we held that the FAA "create[d] a body of federal substantive law," which was "applicable in state and federal court." 465 U. S., at 12 (internal quotation marks omitted). We rejected the view that state law could bar enforcement of §2, even in the context of state-law claims brought in state court. *See id.*, at 10–14; *see also Allied-Bruce Terminix Cos. v. Dobson,* 513 U. S. 265, 270–273 (1995).

B

[¶8] *Prima Paint* and *Southland* answer the question presented here by establishing three propositions. First, as a matter of substantive federal arbitration law, an arbitration provision is severable from the remainder of the contract. Second, unless the challenge is to the arbitration clause itself, the issue of the contract's validity is considered by the arbitrator in the first instance. Third, this arbitration law applies in state as well as federal courts. The parties have not requested, and we do not undertake, reconsideration of those holdings. Applying them to this case, we conclude that because respondents challenge the Agreement, but not specifically its arbitration provisions, those provisions are enforceable apart from the remainder of the contract. The challenge should therefore be considered by an arbitrator, not a court.

[¶9] In declining to apply *Prima Paint*'s rule of severability, the Florida Supreme Court relied on the distinction between void and voidable contracts. "Florida public policy and contract law," it concluded, permit

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* [1] The issue of the contract's validity is different from the issue of whether any agreement between the alleged obligor and obligee was ever concluded. Our opinion today addresses only the former, and does not speak to the issue decided in the cases cited by respondents (and by the Florida Supreme Court), which hold that it is for courts to decide whether the alleged obligor ever signed the contract, *Chastain v. Robinson-Humphrey Co.*, 957 F. 2d 851 (CA11 1992), whether the signor lacked authority to commit the alleged principal, *Sandvik AB v. Advent Int'l Corp.,* 220 F. 3d 99 (CA3 2000); *Sphere Drake Ins. Ltd. v. All American Ins. Co.,* 256 F. 3d 587 (CA7 2001), and whether the signor lacked the mental capacity to assent, *Spahr v. Secco*, 330 F. 3d 1266 (CA10 2003).

"no severable, or salvageable, parts of a contract found illegal and void under Florida law." 894 So. 2d, at 864. *Prima Paint* makes this conclusion irrelevant. That case rejected application of state severability rules to the arbitration agreement without discussing whether the challenge at issue would have rendered the contract void or voidable. *See* 388 U. S., at 400–404. Indeed, the opinion expressly disclaimed any need to decide what state-law remedy was available, *id.*, at 400, n. 3, (though Justice Black's dissent asserted that state law rendered the contract void, *id.*, at 407). Likewise in *Southland*, which arose in state court, we did not ask whether the several challenges made there—fraud, misrepresentation, breach of contract, breach of fiduciary duty, and violation of the California Franchise Investment Law—would render the contract void or voidable. We simply rejected the proposition that the enforceability of the arbitration agreement turned on the state legislature's judgment concerning the forum for enforcement of the state-law cause of action. *See* 465 U. S., at 10. So also here, we cannot accept the Florida Supreme Court's conclusion that enforceability of the arbitration agreement should turn on "Florida public policy and contract law," 894 So. 2d, at 864.

C

[¶10] * * * * Respondents point to the language of §2, which renders "valid, irrevocable, and enforceable" "a written provision in" or "an agreement in writing to submit to arbitration an existing controversy arising out of" a "contract." Since, respondents argue, the only arbitration agreements to which §2 applies are those involving a "contract," and since an agreement void ab initio under state law is not a "contract," there is no "written provision" in or "controversy arising out of" a "contract," to which §2 can apply. This argument echoes Justice Black's dissent in *Prima Paint*: "Sections 2 and 3 of the Act assume the existence of a valid contract. They merely provide for enforcement where such a valid contract exists." 388 U. S., at 412–413. We do not read "contract" so narrowly. The word appears four times in §2. Its last appearance is in the final clause, which allows a challenge to an arbitration provision "upon such grounds as exist at law or in equity for the revocation of any contract." (Emphasis added.) There can be no doubt that "contract" as used this last time must include contracts that later prove to be void. Otherwise, the grounds for revocation would be limited to those that rendered a contract voidable—which would mean (implausibly) that an arbitration agreement could be challenged as voidable but not as void. Because the sentence's final use of "contract" so obviously includes putative contracts, we will not read the same word earlier in the same sentence to have a more narrow meaning.† We note that neither *Prima Paint* nor *Southland* lends support to respondents' reading; as we have discussed, neither case turned on whether the challenge at issue would render the contract voidable or void.

* * *

[¶11] It is true, as respondents assert, that the *Prima Paint* rule permits a court to enforce an arbitration agreement in a contract that the arbitrator later finds to be void. But it is equally true that respondents' approach permits a court to deny effect to an arbitration provision in a contract that the court later finds to

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† [3] Our more natural reading is confirmed by the use of the word "contract" elsewhere in the United States Code to refer to putative agreements, regardless of whether they are legal. For instance, the Sherman Act, ch.647, 26 Stat. 209, as amended, states that "[e]very contract, combination . . . , or conspiracy, in restraint of trade [is] hereby declared to be illegal." 15 U.S.C. § 1. Under respondents' reading of "contract," a bewildering circularity would result: A contract illegal because it was in restraint of trade would not be a "contract" at all, and thus the statutory prohibition would not apply.

be perfectly enforceable. Prima Paint resolved this conundrum—and resolved it in favor of the separate enforceability of arbitration provisions. We reaffirm today that, regardless of whether the challenge is brought in federal or state court, a challenge to the validity of the contract as a whole, and not specifically to the arbitration clause, must go to the arbitrator.

[¶12] The judgment of the Florida Supreme Court is reversed, and the case is remanded for further proceedings not inconsistent with this opinion.

Questions:

1. Would lack of consideration for an agreement containing an arbitration clause be for the court or arbitrators to consider? Would this be different or the same as lack of assent addressed in the footnote? Why or why not?

2. If someone held a gun to your head and forced you to sign a contract containing an arbitration clause, where would you present that evidence—in court or to the arbitrators?

3. Is the arbitration term specifically enforceable? What justifies enforcing it specifically on principles different than other contract terms?

4. What if the particular arbitration clause was unconscionable? Would that ever go to arbitration? Consider this case: An 86-year-old man with a 6th-grade education living alone on (i) social security and (ii) profits from cash-only work fixing lawn-mower engines and without knowledge of what is happening in the world or even in his own neighborhood signs a deal to sell his only real asset, a real property parcel of 10 acres, for 100% of its value as land but only 10% of its market value in mineral rights, to a mineral rights speculator who knew that drilling would promptly commence. The agreement also has a long arbitration clause. This clause is a three-page, 12,000-word arbitration agreement to arbitrate any dispute in Paris before an arbitration panel of the International Board of Mineral Speculation, which, in highly convoluted language and very small print, requires an up-front, non-refundable fee of $15,000 and allows the speculator to choose all of the arbitrators, who will arbitrate according to the trade practices of the Int'l Board of Mineral Speculation, none of which are written. Can the arbitration clause itself be challenged in court?

5. Error in arbitration is not fixable by an appeal afterward to real judges, the Court has said. Yet a quite large percentage of disputes are resolved today by arbitration. Does this have ramifications for the rule of law? If you as a consumer object to having disputes resolved by arbitrators rather than courts, what can you do about it?

6. If consumers do not like arbitration, how can sellers of goods and services insist on it? Why isn't refusal to insist on arbitration a point of pride with sellers? Can you think of any arguments for arbitration from a consumer's perspective?

Chapter 15. Third-Party Rights and Obligations

Conceptually, people who are not parties to a contract obtain interests in them in three ways:

(1) Rights might be assigned. Your mortgage originator usually will transfer its rights to your payments to someone else.

(2) Duties might be delegated to a non-party to do. For example, a general contractor delegates many of its construction duties to subcontractors.

(3) The parties might agree that one of them is contracting for the benefit of someone else, so that that third party will have the benefit (which is why we call that person a third-party beneficiary). A parent might buy life insurance and name a child as a beneficiary, for instance.

Though, conceptually, there are three primary ways to involve third parties, courts do not keep the vocabulary tidy. For instance, they often talk of “assigning a contract” which contains both rights and duties. See if you can distinguish between duties and rights and determine which the court is talking about when.

A. Assignment

Fitzroy v. Cave

Court of Appeal (1905), 2 K.B. 364

[¶1] Appeal from the judgment of Lawrance J. in an action tried before him without a jury.

[¶2] The action was brought by the plaintiff as the assignee of certain debts.

[¶3] It appeared that the defendant was at the date of the after-mentioned deed indebted to five tradesmen in Ireland in various sums, amounting in all to 90l. 11s. 5d., in respect of goods sold and delivered by them respectively to him. By a deed dated October 13, 1904, and made between these tradesmen of the one part and the plaintiff of the other part, after reciting that the parties of the first part had agreed to assign the said debts to the plaintiff upon the terms and for the consideration thereinafter set forth, it was witnessed that, in pursuance of such agreement, and for and in consideration of the covenant and agreement on the part of the plaintiff thereinafter contained, the parties of the first part thereby respectively assigned to the plaintiff the said debts to hold the same respectively to the plaintiff absolutely. The deed then proceeded: “And the assignee hereby covenants with the assignors, and with each of them, that, in case he shall be able to recover and realize the amount of the said debts from the said Arthur Oriel Singer Cave, he will immediately thereupon pay over to them, the assignors, their executors, administrators, and assigns, the said respective amounts, or so much thereof as he may be able to recover or realize, after

payment of all costs necessarily incurred by him." Notice in writing of this assignment had been given to the defendant.

[¶4] It appeared in evidence that the plaintiff was interested in, and a director of, a company called the Cork Mineral Development Company. The defendant was a co-director and the local manager of the company. The plaintiff, being dissatisfied with the action of the defendant as a director of the company, had, acting under the advice of a solicitor, taken the assignment of the before-mentioned debts with the view of procuring an adjudication in bankruptcy against the defendant, and so getting him removed from the directorate of the company.

[¶5] Lawrance J. held, with some doubt, that, under these circumstances, the assignment was invalid as savouring of maintenance or otherwise against public policy, and therefore gave judgment for the defendant. * * * *

[¶6] Cozens-Hardy L.J. read the following judgment: –This is an appeal from the judgment of Lawrance J. in favour of defendant. The plaintiff is the assignee of five debts amounting together to over 50l. due from the defendant to five creditors resident in Ireland. The assignment is effected by a deed dated October 13, 1904. It is in the common form of an absolute assignment, but there is no pecuniary consideration, and the assignee takes no beneficial interest, for he covenants that, in case he is able to recover the amount of the debts from the defendant, he will pay over to the assignors the respective amounts or so much thereof as he may be able to recover or realize after payment of all costs necessarily incurred by him. Now the existence of the debts is not disputed, and unless the plaintiff can recover the amounts the defendant has been relieved from all responsibility. It has, however, been strenuously contended by Mr. Gregory in his very able argument that the plaintiff's action is open to the objection of maintenance, or is otherwise such that on grounds of public policy the Court ought to refuse its assistance. This view was adopted by the learned [trial] judge

[¶7] It is desirable to consider the limits of the doctrine of maintenance as applied to choses in action. There are undoubtedly many choses in action which are not and never were assignable either at law or in equity. * * * *

[¶8] There are, however, other choses in action which, though not assignable at common law, were always regarded as assignable in equity. A debt presently due and payable is an instance. At common law such a debt was looked upon as a strictly personal obligation, and an assignment of it was regarded as a mere assignment of a right to bring an action at law against the debtor. Hence an assignment was, with some exceptions which need not be referred to * * * , looked upon as open to the objection of maintenance. After a time the Common Law Courts recognised the right of any one who had a pecuniary interest in the debt to sue in the name of the debtor. This, however, was the limit of their departure from the old strict rule, so far as I have been able to discover. But the Courts of Equity took a different view: Row v. Dawson. They admitted the title of an assignee of a debt, regarding it as a piece of property, an asset capable of being dealt with like any other asset, and treating the necessity of an action at law to get it in as a mere incident. They declined to hold such a transaction open to the charge of maintenance. * * * * A Court of Equity recognised not merely transactions which amounted to sales or mortgages of debts, under which the assignee took a beneficial interest in the debt, but also the creation of trusts, under which the trustee took no interest. Thus A., the creditor, might assign the debt to B., with or without a power of attorney, upon trust for C. Or A. might simply declare himself a trustee of the debt for C. In either case the trustee would take no beneficial interest, and would, by virtue of his position as trustee, be entitled to be indemnified out of the

moneys recovered against all costs of the action brought in the name of A. against the debtor. If the debt were secured by a promissory note or bill or other negotiable instrument, A. might deliver the instrument to B. upon trust for C., and B. could sue at law on it. Or A. might create a trust in favour of himself by delivering the instrument to B. upon trust for himself. It would, I apprehend, in this case be no objection to say that B. had no interest in the debt. It has never, so far as I am aware, been suggested that a trustee to whom a debt is assigned is exposed to a charge of maintenance. Mortgages are every day dealt with in this fashion, including an assignment of the debt. From time to time particular classes of obligation have by statute been rendered assignable at law, and by the Judicature Act, 1873, s. 25, sub-s. 6, any debt is made assignable at law by an absolute assignment in writing, of which notice is given to the debtor. Henceforth in all Courts a debt must be regarded as a piece of property capable of legal assignment in the same sense as a bale of goods. And on principle I think it is not possible to deny the right of the owner of any property capable of legal assignment to vest that property in a trustee for himself, and thereby to confer upon such trustee a right of indemnity. It is not easy to see how the doctrine of maintenance can be applied to a case like the present. * * * * The plaintiff is merely seeking by this action to recover payment of debts admitted to be justly due. It is said that the plaintiff does not really desire to be paid and can take nothing for his own benefit under the judgment. For the reasons above stated I think this is of no moment. It is further argued that his only object is to obtain a judgment which may serve as the foundation of bankruptcy proceedings, the ultimate result of which will be the removal of the defendant from his position as director of a company in which the plaintiff is largely interested. But I fail to see that we have anything to do with the motives which actuate the plaintiff, who is simply asserting a legal right consequential upon the possession of property which has been validly assigned to him. If the defendant pays, no bankruptcy proceedings will follow. If he does not pay, bankruptcy is a possible result. In my opinion this appeal must be allowed.

* * * Appeal allowed.

Questions:

1. What is maintenance? One attorney claimed that “the common law made it unlawful to solicit claims, to render aid where there was no interest, to institute fraudulent claims, and to acquire a contingent interest in causes of action, because contrary to public policy.” *McCloskey v. San Antonio Traction Co*., 192 S.W. 1116, 1118 (Tex. App. 1917). Obviously, we do not follow this kind of rule now, at least not as lawyers. The court in *Fitzroy* suggests that instead claims can be solicited, aid rendered where there is no interest, and legally recognized assignments made to those who in fact mean to harm the interests of the debtor. Do you see anything immoral in this? Inefficient?

2. Do debtors care about the identity of their creditors? The money is owed in any event, right? Why should anyone care to whom it is paid? Consider the facts of the following case:

> MBank El Paso hired El Paso Recovery Service to repossess Yvonne Sanchez’s automobile because of her default on a note. Two men dispatched to Sanchez’s home found the car parked in the driveway, and hooked it to a tow truck. Sanchez demanded that they cease their efforts and leave the premises; but the men nonetheless continued with the repossession. Before the men could tow the automobile into the street, Sanchez

> jumped into the car, locked the doors, and refused to leave. The men then towed the car at a high rate of speed, with Sanchez inside, to the repossession yard. They parked the car in the fenced repossession yard and padlocked the gate. Sanchez was left in the repossession lot, with a Doberman pinscher guard dog loose in the yard, until later rescued by her husband and police.

Mbank El Paso, N.A. v. Sanchez, 836 S.W.2d 151 (Tex. 1992). The Texas Supreme Court in this case held that, pursuant to UCC § 9-503 (prohibiting breach of the peace in self-help repossession), the bank could be liable for breaches of the peace committed by an independent contractor. MBank hired El Paso Recovery Service to collect the car, but it could also have assigned the debt to them. Should you care who owns your debt?

Note. The UCC at Section 2-210(1)(2) lays out the doctrines governing assignment and delegation with remarkable clarity and great similarity to the doctrines of the common law. The text of this statute follows. Please pick out which sentences apply to delegation and which to assignment alone:

> (1) A party may perform his duty through a delegate unless otherwise agreed or unless the other party has a substantial interest in having his original promisor perform or control the acts required by the contract. No delegation of performance relieves the party delegating of any duty to perform or any liability for breach.
>
> (2) Unless otherwise agreed all rights of either seller or buyer can be assigned except where the assignment would materially change the duty of the other party, or increase materially the burden or risk imposed on him by his contract, or impair materially his chance of obtaining return performance. * * * *

The EVENING NEWS ASSOCIATION v. Gordon PETERSON

D. D.C. (1979), 477 F. Supp. 77

PARKER, J.:

[¶1] The question presented in this litigation is whether a contract of employment between an employee and the owner and licensee of a television station, providing for the employee's services as a newscaster-anchorman, was assigned when the station was sold and acquired by a new owner and licensee.

[¶2] Plaintiff Evening News Association (Evening News), a Michigan Corporation, acquired station WDVM-TV (Channel 9) a District of Columbia television station from Post-Newsweek Stations, Inc. (Post-Newsweek) in June of 1978. At that time, the defendant Gordon Peterson was and had been employed for several years as a newscaster-anchorman by Post-Newsweek. This defendant is a citizen of the State of Maryland. The plaintiff claims that Peterson's employment contract was assignable without the latter's consent, was indeed assigned, and thus otherwise enforceable. The defendant contends, however, that his Post-Newsweek contract required him to perform unique and unusual services and because of the personal relationship he had with Post-Newsweek the contract was not assignable.

[¶3] Mr. Peterson was employed by the plaintiff for more than one year after the acquisition and received the compensation and all benefits provided by the Post-Newsweek contract. In early August, 1979, he tendered his resignation to the plaintiff. At that time the defendant had negotiated an employment contract with a third television station located in the District of Columbia, a competitor of the plaintiff. The Evening News then sued Peterson, seeking a declaration of the rights and legal relations of the parties under the contract and permanent injunctive relief against the defendant.

[¶4] Following an accelerated briefing schedule and an expedited bench trial on the merits, the Court concludes that the contract was assignable and that Evening News is entitled to appropriate permanent injunctive relief against the defendant Gordon Peterson.

[¶5] In accordance with Rule 52(a) Fed.R.Civ.P., the Court's findings of fact and conclusions of law in support of that determination are set forth.

FINDINGS OF FACT

[¶6] The defendant was employed by Post-Newsweek Stations, Inc. from 1969 to 1978. During that period he negotiated several employment contracts. Post-Newsweek had a license to operate television station WTOP-TV (Channel 9) in the District of Columbia. In June of 1978, following approval by the Federal Communications Commission, Post-Newsweek sold its operating license to Evening News and Channel 9 was then designated WDVM-TV. A June 26, 1978, Bill of Sale and Assignment and Instrument of Assumption and Indemnity between the two provided in pertinent part:

> PNS has granted, bargained, sold, conveyed and assigned to ENA, . . . all the property of PNS . . . including, . . . all right, title and interest, legal or equitable, of PNS in, to and under all agreements, contracts and commitments listed in Schedule A hereto. . . .

[¶7] When Evening News acquired the station, Peterson's Post-Newsweek employment contract, dated July 1, 1977, was included in the Bill of Sale and Assignment. The contract was for a three-year term ending June 30, 1980, and could be extended for two additional one-year terms, at the option of Post-Newsweek. The significant and relevant duties and obligations under that contract required Peterson:

> to render services as a news anchorman, and to perform such related services as news gathering, writing and reporting, and the organization and preparation of program material, to the extent required by the Stations, as are consistent with [his] primary responsibility as a news anchorman. . . . [To participate] personally as a newsman, announcer, on-the-air personality or other performer in any news, public affairs, documentary, news analysis, interview, special events or other program or segment of any program, designated by . . . and to the extent required by the Stations . . . as may reasonably be required by the Stations. . . .

[¶8] As compensation the defendant was to receive a designated salary which increased each year from 1977 through the fifth (option) year. Post-Newsweek was also obligated to provide additional benefits including term life insurance valued at his 1977 base salary, disability insurance, an annual clothing allowance and benefits to which he was entitled as provided in an underlying collective bargaining agreement with the American Federation of Television and Radio Artists.

[¶9] There was no express provision in the 1977 contract concerning its assignability or nonassignability. However, it contained the following integration clause:

> This agreement contains the entire understanding of the parties . . . and this agreement cannot be altered or modified except in a writing signed by both parties.

A.

[¶10] Aside from the various undisputed documents and exhibits admitted into evidence, there were sharp conflicts in testimony concerning various events and what was said and done by the parties and their representatives, both before and after the Evening News' acquisition. As trier of fact, having heard and seen the several witnesses testify and after assessing and determining their credibility, the Court makes the following additional findings.

[¶11] The defendant's duties, obligations and performance under the 1977 contract did not change in any significant way after the Evening News' acquisition. In addition, the Evening News met all of its required contract obligations to the defendant and its performance after acquisition in June, 1978, was not materially different from that of Post-Newsweek.

[¶12] Mr. Peterson testified that he had "almost a family relationship" with James Snyder, News Director, and John Baker, Executive Producer, for Post-Newsweek, which permitted and promoted a free exchange of ideas, frank expressions of dissent and criticism and open lines of communication. These men left Channel 9 when Post-Newsweek relinquished its license, and they have since been replaced by Evening News personnel. According to Mr. Peterson, the close relationship and rapport which existed between him and them was an important factor as he viewed the contract; these relationships made the contract in his view nonassignable and indeed their absence at the Evening News prevented defendant from contributing his full efforts. Even if Mr. Peterson's contentions are accepted, it should be noted that he contracted with the Post-Newsweek corporation and not with the News Director and Executive Producer of that corporation. Indeed, the 1977 contract makes no reference to either officer, except to provide that vacations should be scheduled and coordinated through the News Director. Had the defendant intended to condition his performance on his continued ability to work with Snyder and Baker, one would have expected the contract to reflect that condition.

[¶13] The close, intimate and personal relationship which Mr. Peterson points to as characterizing his association with Post-Newsweek and its personnel, was highly subjective and was supported only by his testimony. The Court cannot find that Peterson contracted with Post-Newsweek in 1977 to work with particular individuals or because of a special policy-making role he had been selected to perform in the newsroom. For the fourteen-month period of Peterson's employment at the Evening News, there is no showing that he was in any way circumscribed, limited in his work or otherwise disadvantaged in his performance. Nor is there any credible evidence that the News Director or other top personnel of Evening News were rigid, inflexible, warded off any of Mr. Peterson's criticisms or even that at any time he gave suggestions and criticisms which were ignored or rejected. Finally, the Court does not find that Post-Newsweek contracted with Peterson because of any peculiarly unique qualities or because of a relationship of personal confidence with him.

B.

[¶14] In his direct testimony, Mr. Peterson expressed a degree of disappointment because of Evening News' failure to keep apace with advances in technology and to seize opportunities for live in-depth coverage of current events. He characterized the plaintiff's news coverage as "less aggressive" than what he had experienced with Post-Newsweek.

[¶15] On cross-examination, however, he was shown an exhibit comparing the broadcast of special assignments reported and produced by him for two one-year periods, one before and one after the June, 1978 acquisition. While he admitted to its accuracy with some reservation, the exhibit clearly showed that a comparable number of such assignments of similar quality, were broadcast within the two years. He also conceded that for the same period Evening News received two Peabody awards, an award for best editorials, and a number of Emmy awards for public affairs exceeding those received in prior years by Post-Newsweek. Finally, he acknowledged that Channel 9 still maintained the highest ratings for audience viewing among the television stations in the Washington, D.C. market area.

[¶16] A great amount of testimony was generated as to when Peterson learned of the Evening News' acquisition and what then occurred relative to the assignment of the contract. The testimony on this issue was conflicting, largely cumulative and as now viewed, over-emphasized by the parties. The Court finds that the defendant gained first knowledge of a possible sale and transfer of the station in December, 1977. At that time, the president of Post-Newsweek publicly announced to the station's employees, including Peterson, that an agreement in principle had been reached, subject to approval by the Federal Communications Commission. At no time from December, 1977, until December, 1978, did the defendant or his attorney ever indicate or venture an opinion that the contract was not assignable. Indeed, through at least April, 1979, the defendant's attorney made representations that assignment of the contract presented no problem to his client.

[¶17] In summary, the Court finds that the performance required of Mr. Peterson under the 1977 contract was (1) not based upon a personal relationship or one of special confidence between him and Post-Newsweek or its employees, and (2) was not changed in any material way by the assignment to the Evening News.

CONCLUSIONS OF LAW

[¶18] There is diversity of citizenship; the amount in controversy exceeds $10,000; and the Court has jurisdiction over this proceeding by virtue of 28 U.S.C. § 1332.

A.

[¶19] The distinction between the assignment of a right to receive services and the obligation to provide them is critical in this proceeding. This is so because duties under a personal services contract involving special skill or ability are generally not delegable by the one obligated to perform, absent the consent of the other party. The issue, however, is not whether the personal services Peterson is to perform are delegable but whether Post-Newsweek's right to receive them is assignable.

[¶20] Contract rights as a general rule are assignable. *Munchak Corp. v. Cunningham*, 457 F.2d 721 (4th Cir. 1972); *Meyer v. Washington Times Co.,* 64 App. D.C. 218, 76 F.2d 988 (D.C. Cir.) cert. denied 295 U.S. 734, 55 S. Ct. 646, 79 L. Ed. 1682 (1935); 4 A. *Corbin, Contracts* § 865 (1951); *Restatement (First) of Contracts* § 151 (1932). This rule, however, is subject to exception where the assignment would vary

materially the duty of the obligor, increase materially the burden of risk imposed by the contract, or impair materially the obligor's chance of obtaining return performance. Corbin § 868; Restatement § 152. There has been no showing, however, that the services required of Peterson by the Post-Newsweek contract have changed in any material way since the Evening News entered the picture. Both before and after, he anchored the same news programs. Similarly he has had essentially the same number of special assignments since the transfer as before. Any additional policy-making role that he formerly enjoyed and is now denied was neither a condition of his contract nor factually supported by other than his own subjective testimony.

[¶21] The general rule of assignability is also subject to exception where the contract calls for the rendition of personal services based on a relationship of confidence between the parties. *Munchak*, 457 F.2d at 725; *Meyer*, 64 App. D.C. at 219, 76 F.2d at 989. As Corbin has explained this limitation on assignment:

> In almost all cases where a "contract" is said to be non-assignable because it is "personal," what is meant is not that the contractor's right is not assignable, but that the performance required by his duty is a personal performance and that an attempt to perform by a substituted person would not discharge the contractor's duty.

Corbin § 865. In *Munchak*, the Court concluded that a basketball player's personal services contract could be assigned by the owner of the club to a new owner, despite a contractual prohibition on assignment to another club, on the basis that the services were to the club. The Court found it "inconceivable" that the player's services "could be affected by the personalities of successive corporate owners." 457 F.2d at 725. The policy against the assignment of personal service contracts, as the Court noted, "is to prohibit an assignment of a contract in which the obligor undertakes to serve only the original obligee." 457 F.2d at 726.

[¶22] Given the silence of the contract on assignability, its merger clause, and the usual rule that contract rights are assignable, the Court cannot but conclude on the facts of this case that defendant's contract was assignable. Mr. Peterson's contract with Post-Newsweek gives no hint that he was to perform as other than a newscaster-anchorman for their stations. Nor is there any hint that he was to work with particular Post-Newsweek employees or was assured a policy-making role in concert with any given employees. Defendant's employer was a corporation, and it was for Post-Newsweek Stations, Inc. that he contracted to perform. The corporation's duties under the contract did not involve the rendition of personal services to defendant; essentially they were to compensate him. Nor does the contract give any suggestion of a relation of special confidence between the two or that defendant was expected to serve the Post-Newsweek stations only so long as the latter had the license for them.

B.

[¶23] As noted, the 1977 contract contained a clause providing that the entire understanding between the parties was contained within the four corners of the agreement. The contract contains no provision relating to assignment. The defendant's counsel asserts, however, that an ambiguity exists and he therefore seeks to introduce certain exhibits and other extrinsic evidence for purposes of explaining and discerning the intentions of the parties. Specifically, he seeks to introduce four documents: an earlier 1973 contract; a draft of a proposed 1974 contract; the final 1974 contract; and a letter of 1975 from the president of Post-Newsweek to the defendant. The Court reserved decision on admissibility of the exhibits and now rules that

they are inadmissible for the purposes intended by the defendant. The 1977 contract makes no reference to any prior agreements, to any negotiations between the parties, or specifically to the four proffered exhibits. To make use of them to show the intention of the parties in 1977, or to show what happened in past contract negotiations, simply asks too much.

[¶24] The Court does not share the defendant's belief that silence on the issue of assignability creates ambiguity, and he fails to provide any legal authority to warrant such an inference. An unsupported assertion that ambiguity exists is insufficient to give a different meaning to a contract when there is in fact no contractual provision. For the Court to accept the defendant's exhibits in an effort to explain the parties' intent would modify and enlarge the provisions of the agreement and bestow upon the defendant an advantage which he did not originally have. The law of this Circuit is clearly set forth in *Clayman v. Goodman Properties, Inc.,* 171 U.S. App. D.C. 88, 95, 518 F.2d 1026, 1033 (D.C. Cir. 1973), where Circuit Judge Robinson said in part:

> [W]e perceive no basis for resort to evidence depicting the circumstances surrounding the making of the contract before us. We need do little more than reiterate that "[t]he parol evidence rule requires that '[w]hen two parties have made a contract and have expressed it in a writing to which they have both assented as the complete and accurate integration of that contract, evidence, whether parol or otherwise, of antecedent understandings and negotiations will not be admitted for the purpose of varying or contradicting the writing.'" The consequences which the law attaches to a written contract are as much a part of it as the terms it sets forth, and the legal effect of the contract can no more be changed or modified by parol evidence than it could have had it been made express.

[¶25] The contract before the Court, as the agreement in *Clayman*, contains a merger clause stating that the contract embodies the final and exclusive understanding of the parties. Such a stipulation is given full effect in this jurisdiction absent the Court's finding of any ambiguity in the contract. *Lee v. Flintkote Co.,* 193 U.S. App. D.C. 121, 127, 593 F.2d 1275, 1281 (D.C. Cir. 1979).

C.

[¶26] Plaintiff's argument that defendant has waived any objection to the assignment by accepting the contract benefits and continuing to perform for the Evening News for over a year has perhaps some merit. If defendant has doubts about assignability, he should have voiced them when he learned of the planned transfer or at least at the time of transfer. His continued performance without reservation followed by the unanticipated tender of his resignation did disadvantage Evening News in terms of finding a possible replacement for him and possibly in lost revenues. The Court, however, concludes that the contract was assignable in the first instance and thus it is not necessary to determine whether defendant's continued performance constitutes a waiver of objection to the assignment.

[¶27] During the course of this trial Edwin W. Pfeiffer, an executive officer of WDVM-TV, testified that Mr. Peterson allegedly stated "if the Judge decides I should stay, I will stay." Assuming that he did not overstate Mr. Peterson's position and that Mr. Peterson was quoted in appropriate context, the television audience of the Washington, D.C. metropolitan area should anticipate his timely reappearance as news anchorman for station WDVM-TV. Of course, the avenue of appeal is always available.

[¶28] An order consistent with this Memorandum Opinion will be entered. Counsel for the plaintiff shall submit immediately an appropriate order.

Questions:

1. What was the injunctive relief against Peterson?

2. Why did Peterson quit, do you suppose?

3. Peterson continued at Channel 9 until 2003, when he moved to Channel 7. He left Channel 7 at the end of 2014. Why do you suppose Channel 9 still wanted him?

4. Generally, rights are assigned and duties are delegated. The rules for transferring each to a non-party differ. Which was at issue in *Peterson*?

5. You should think about a fact pattern where the assignment would "increase materially the burden of risk imposed by the contract." What would that look like? How about this?

A small, local grocer, Ralph's Grocery Corporation, owned and operated three stores in Midville. Ralph's Grocery Corporation was entirely owned by Ralph. State Farm insured Ralph's Grocery Corporation against fire in the buildings. Ralph decided to sell to HEB, a much larger grocery chain operating throughout the state. In the transaction, Ralph transferred all the shares of Ralph's Grocery Corporation to HEB, which then became the sole shareholder. HEB intended to employ Ralph as manager of the three stores and slowly grow and improve them but otherwise operate them as grocery stores, just as before. A week after the transfer of shares, a fire broke out in one of the new Midville HEB stores. Can State Farm claim that it no longer insures the stores?

Would your answer change if, rather than transferring the shares, Ralph's Grocery Corporation had transferred the stores and insurance policies to HEB?

Would your answer change if Ralph's Grocery Corporation had transferred the stores and policies to Walmart?

If an assignment does occur, how does the obligor of the right assigned find out about it? Why should the obligor perform to the assignee? The law on this issue has changed as statutes have modified the common law. Please read the case, and then we will introduce some statutes that modify its law.

CONTINENTAL PURCHASING CO., INC. v. VAN RAALTE CO., INC.

N.Y. Supr. Ct., App. Div. (1937), 251 App. Div. 151

EDGECOMB, Justice.

[¶1] This action is brought by the plaintiff, as assignee of Ethel L. Potter, to recover from the Van Raalte Co., Inc., the employer of Mrs. Potter, the sum of nineteen dollars and twenty cents, wages earned by her while employed by the company. The defendant claims exoneration from liability by reason of having paid the amount involved direct to the assignor.

[¶2] It is conceded that on April 21, 1934, Mrs. Potter assigned to the plaintiff all wages, or claims for wages, salary or commission earned, or to be earned, and all claims or demands due her from any person, firm or corporation by whom she was employed, or who might owe her money, as security for the payment of an account which the Steckler Sporting Goods Store had against her, and which account had been purchased by and assigned to the plaintiff.

[¶3] This assignment, having been made prior to July 1, 1934, when section 46 was added to the Personal Property Law by chapter 738 of the laws of that year, is not void by reason of any statutory prohibition relating to wage assignments. Neither is such transfer contrary to public policy. * * * *

[¶4] While the assignee of a chose in action succeeds to all the rights of the assignor, a debtor is not affected by the assignment until he has notice thereof. If he pays his indebtedness to the assignor in ignorance of the assignment, he is relieved from all liability to the assignee. He may set up against the claim of the assignee any defense acquired prior to notice which would have been available against the assignor had there been no assignment. * * * *

[¶5] After notice of the transfer, however, the debtor is put on his guard, and if he pays the assignor any money which, under the assignment, belongs to the assignee, or if he does anything prejudicial to the rights of the latter, he is liable for the resulting damage. (* * * *

[¶6] No set form of notice is required. It is sufficient if such information is given the debtor as will fully inform him that the alleged assignee is the owner of the chose in action, or as will serve to put him on inquiry. * * * *

[¶7] Here the plaintiff protected itself against any bona fide payments made by the debtor to its employee by giving the defendant a written notice of this assignment on September 12, 1934. Seven days later defendant acknowledged receipt of the notice, and suggested that, inasmuch as Mrs. Potter had no other income except her weekly earnings, it would be a great accommodation if a deduction of two dollars per week could be made until the total amount of plaintiff's claim was paid. Plaintiff consented to this adjustment, and withdrew its formal notice. But defendant still knew of the assignment, and on six occasions during the following two months deducted one dollar and fifty cents from Mrs. Potter's wages, and forwarded the same to the plaintiff. This arrangement was discontinued after November twentieth. Plaintiff then gave defendant another formal notice of the assignment, and demanded payment direct to it of the wages due Mrs. Potter, and called attention to the fact that any sums paid to the employee would not relieve the defendant from its obligation to the plaintiff. With full knowledge that the plaintiff was entitled to receive Mrs. Potter's wages, defendant has chosen to pay them to Mrs. Potter. In so doing defendant acted at its peril.

[¶8] Defendant claims immunity from liability in this action because of the fact that neither the original assignment, nor a copy thereof, was ever filed with or exhibited to it. This defense has found favor in the courts below. Such a requirement is not necessary to render a debtor liable to the assignee of a chose in action for the failure to pay him a debt owed to the assignor. Especially is that so where, as here, no such demand or request has ever been made. (*Davenport v. Woodbridge*, 8 Me. 17; *Bean v. Simpson*, 16 *id.* 49; *North Penn Iron Co. v. International Lithoid Co., 217 Penn. St*., 538; 66 A. 860.) The cases relied upon by the respondent do not lay down any different rule.

[¶9] Here a full and complete notice of the assignment was given to the defendant, and a demand was made that the assignor's wages be paid to the plaintiff. Defendant never questioned the existence or validity of the transfer, nor asked for any additional proof thereof. On the contrary, it acknowledged its validity, and made six separate payments to the assignee, totaling nine dollars, in reliance thereon. Later it utterly ignored plaintiff's rights in the premises, and paid the assignor her wages as they became due, notwithstanding the fact that it knew this money belonged to the plaintiff. Its only excuse for so doing was the fact that Mrs. Potter was receiving aid from a local charitable organization, and that the matter had been referred to that organization for a decision. Under these circumstances defendant cannot escape its liability to the plaintiff because it paid Mrs. Potter's wages to her.

[¶10] For the reasons stated, we think that the judgments of the City Court of Dunkirk, and of the County Court of Chautauqua county, should be reversed, with costs, and that judgment should be ordered in favor of the plaintiff for the sum of nineteen dollars and twenty cents, with interest thereon from the 21st day of November, 1934.

All concur.

Judgments reversed on the law, with costs in all courts, and judgment directed in favor of the plaintiff in the sum of nineteen dollars and twenty cents, with interest thereon from the 21st day of November, 1934, with costs.

Questions—with answers under the common law:

1. Was it okay to pay Ms. Potter before notice was given? Yes. The obligor is not affected by the assignment until the obligor has notice of the assignment, as ¶4 says.

2. For notice to be effective, must the assignee give the debtor or obligor a copy of the assignment itself? No, as ¶8 says. Notice that the assignment has occurred is all that is necessary.

3. Let's say that you owe Ricks money because Ricks sold you his 1991 Geo Prism. He gave you a month to come up with the money. Three weeks after you take possession of the car (such as it is), you receive an informal letter in the mail from a person named Kaminski saying that Ricks has assigned the debt to him and that payment in a week should be made to Kaminski. Ricks is out of town backpacking somewhere, but he had formerly said to mail the check to him, Ricks. What should you do? This is a difficult problem.

Kaminski, if the assignment is real, has no obligation even to give a copy of the assignment, let alone prove that it occurred. Notice has been given in this case. But you understand from Ricks that you were to pay Ricks. You can take some solace from the fact that Kaminski should not have known about the debt unless Ricks told him, but you do not know that an assignment occurred; you only know that Kaminski says one occurred. If you pay Kaminski and no assignment occurred, you will still owe Ricks. If you pay Ricks and the assignment occurred, then you still owe Kaminski. Perhaps you have an honest assignor (if Ricks had been paid after actually assigning, Ricks would send the money back to you so that you could pay Kaminski), but even if you do, the assignment is a hassle. Who has the burden to determine whether the assignment is valid? Under the common law, you do.

4. For whose benefit is the assignment? Certainly not the obligor. At best, the assignment is for the parties to the assignment. So why does the obligor have the obligation to determine whether the assignment is valid? That's a good question.

5. Who is the better bearer of the risk that the assignment is invalid? As between assignee and obligor, the assignee, surely.

6. Should the obligor receive a discharge for paying the assignor? The law says "no" when the payment is made after notice of the assignment.

7. Does the assignor warrant that the obligor is solvent? No, not by default. This is a risk that the assignee takes.

8. *Continental Purchasing* is a wage garnishment, and wage garnishment is now subject to all sorts of restrictions and is sometimes prohibited. (In Texas, for instance, the state constitution mostly prohibits it.[*]) But *Continental Purchasing* accurately reports the baseline common law of assignments.

Now read—

> Uniform Commercial Code § 9-406(a)-(d)
>
> (a) [Discharge of account debtor; effect of notification.]
>
> Subject to subsections (b) through (i), an account debtor on an account * * * may discharge its obligation by paying the assignor until, but not after, the account debtor receives a notification, authenticated by the assignor or the assignee, that the amount due or to become due has been assigned and that payment is to be made to the assignee. After receipt of the notification, the account debtor may discharge its obligation by paying the assignee and may not discharge the obligation by paying the assignor. * * * *
>
> (c) [Proof of assignment.]

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[*] "No current wages for personal service shall ever be subject to garnishment, except for the enforcement of court-ordered: (1) child support payments; or (2) spousal maintenance." TEX. CONST. ART. 16 § 28.

> Subject to subsection (h), if requested by the account debtor, an assignee shall seasonably furnish reasonable proof that the assignment has been made. Unless the assignee complies, the account debtor may discharge its obligation by paying the assignor, even if the account debtor has received a notification under subsection (a).

Now consider the same questions again:

1. Under the statute, you are the account debtor, Ricks is the assignor, and Kaminski is the assignee. If this statute were the law, was it okay to pay Ms. Potter before notice was given?

2. For notice to be effective, must the assignee give the debtor or obligor a copy of the assignment itself? What does the statute add to the common law to account for the obligor's need to know the details of the assignment?

3. Let's say that you owe Ricks money because Ricks sold you his 1991 Geo Prism. He gave you a month to come up with the money. Three weeks after you take possession of the car (such as it is), you receive an informal letter in the mail from a person named Kaminski saying that Ricks has assigned the debt to him and that payment in a week should be made to Kaminski. Ricks is out of town backpacking somewhere, but he had formerly said to mail the check to him, Ricks. What should you do? How does the statute resolve this problem?

4. For whose benefit is the assignment? Who is the better bearer of the risk that the assignment is invalid? How does the statute place the burden with the benefit?

UCC §9-406 is a good example of ways in which Article 9 tries to make assignment of debts simpler, more transparent, and cheaper. This is important because the activities of buying and selling goods is routinely financed by those who can assign debts freely. For example, if you go to the car dealership and look at a car, that car will probably be subject to an inventory financing arrangement between the dealership and its lender, a finance company. The finance company usually makes one loan per car, and that car is collateral for the loan. If the dealer has 200 cars on the lot, the dealer may have 200 separate contracts financing the dealer's ownership of each car.

When you buy a car, if you pay cash, the dealer will take that cash and pay off the finance company's loan on that car. If you borrow money to buy the car, say from Customer Bank (CB), the dealer will take your loan proceeds and pay off the finance company's loan on that car. The law of sales of goods helps this arrangement. Article 2 provides a default warranty that, when the dealership sells you the car, the car comes to you free of the dealership's lender's interest in the car as collateral for the dealer financing; so, even if the dealership never pays the inventory financing debt back to the lender, the dealer's lender cannot take the car from you, the purchaser.

After you buy the car, CB may have no interest in keeping your loan on its books. After "originating" a loan to you, it may assign the loan to an aggregator of loans who may sell a package of the loans to investors. Because the loans may be traded freely in this way, a market for loan contracts exists, and the liquidity in this market persuades many more investors to put money into it. This is why the interest rate on auto loans is as low as it is. It would be much higher if lenders were unable to freely assign. When your loan is assigned, you will receive a notice of the assignment. The notice will tell you where to send the check. You may have

been surprised by this had you not gone to law school, but now you will know it is routine. You also know that you can ask for proof of the assignment, if you want it.

The code does many other tricks to protect consumers and other buyers of financed goods, and we don't have time to go into them here. You can learn about them in a class on Article 9, often called Secured Transactions, where you can study the law of the whole goods financing system.

Marco RUMBIN v. UTICA MUT. INS. CO.

Conn. (2001), 757 A.2d 526

[¶1] * * * * The record reveals the following facts. In April, 1998, the plaintiff and Utica Mutual entered into a structured settlement agreement to resolve a personal injury claim. * * * * [Under the terms of the settlement agreement, the plaintiff was entitled to receive $52,000 within thirty days of its execution, thirty semiannual payments of $1323.09 beginning on March 6, 1999, and a final lump sum payment of $44,000 on March 6, 2014.] The structured portion of the settlement was funded by the annuity contract issued by Safeco. The annuity contract provided under its ''Assignment'' provision that ''[n]o payment under this annuity contract may be . . . assigned . . . in any manner by the [plaintiff] . . . .''

[¶2] Approximately six months after the execution of the settlement agreement and the issuance of the annuity, the plaintiff had become unemployed and faced a mortgage foreclosure action against his home, where he lived with his family. In order to resolve his financial troubles, the plaintiff decided to sell his right to the annuity payments. In November, 1998, he filed a declaratory judgment action seeking court approval [of the] * * * transfer [of] his right to the remaining annuity payments to Wentworth in exchange for a lump sum payment and other consideration. Safeco objected to the assignment, claiming that because the annuity contract contained an antiassignment provision, [the assignment was invalid] * * *. Utica Mutual neither appeared at that hearing, nor provided an explanation for its failure to appear, and the trial court issued an order of default for failure to appear against Utica Mutual.

[¶3] The trial court [allowed the assignment notwithstanding the anti-assignment clause]. * * * * Safeco appealed from the trial court's judgment to the Appellate Court, and we transferred the case to this court * * *. * * * *

II

[¶4] The primary issue raised by this case is whether, under Connecticut common law, an antiassignment provision in an annuity contract invalidates the plaintiff payee's transfer of his right to future payments under the annuity to a third party. We conclude, in accordance with case law and § 322 of the Restatement (Second) of Contracts, that the antiassignment provision at issue here does not render the assignment of the annuity ineffective, but, instead, gives the annuity issuer, Safeco, the right to recover damages for breach of the antiassignment provision.

[¶5] Although we previously have addressed the issue of the validity of contractual provisions prohibiting the assignment of contractual rights; *see Lewin & Sons, Inc. v. Herman*, 143 Conn. 146, 149, 120 A.2d 423

(1956) (upholding validity of contractual provision that prohibited assignment without consent); the law of contracts has changed considerably since our earlier decision. Accordingly, we now reexamine the basic legal principles regarding contractual antiassignment provisions.

[¶6] Our analysis of the effect of the antiassignment provision begins by emphasizing that the modern approach to contracts rejects traditional common-law restrictions on the alienability of contract rights in favor of free assignability of contracts. *See* 3 *Restatement (Second), Contracts* § 317, p. 15 (1981) (''[a] contractual right can be assigned''); *J. Murray, Jr., Contracts* (3d Ed. 1990) (''the modern view is that contract rights should be freely assignable''); 3 *E. Farnsworth, Contracts* (2d Ed. 1998) § 11.2, p. 61 (''[t]oday most contract rights are freely transferable''). Common-law restrictions on assignment were abandoned when courts recognized the necessity of permitting the transfer of contract rights. ''The force[s] of human convenience and business practice [were] too strong for the common-law doctrine that [intangible contract rights] are not assignable.'' (Internal quotation marks omitted.) *J. Murray, Jr., supra*, § 135, p. 791. ''If the law were otherwise, our modern credit economy could not exist.'' 3 *E. Farnsworth, supra*, § 11.2, p. 61. As a result, an assignor typically can transfer his contractual right to receive future payments to an assignee. * * * *

[¶7] The parties to a contract can include express language to limit assignment and courts generally uphold these contractual antiassignment clauses. *See* 3 *Restatement (Second), supra*, § 317, p. 15 (''[a] contractual right can be assigned unless . . . assignment is validly precluded by contract''); 3 *E. Farnsworth, supra*, § 11.4, pp. 82 (''most courts have upheld [terms prohibiting assignment] as precluding effective assignment''). Given the importance of free assignability, however, antiassignment clauses are construed narrowly whenever possible. *See* 3 *E. Farnsworth, supra*, § 11.4, pp. 82–83.

[¶8] In interpreting antiassignment clauses, the majority of jurisdictions now distinguish between the assignor's ''right'' to assign and the ''power'' to assign (modern approach). For example, in *Bel-Ray Co. v. Chemrite (Pty.) Ltd.,* 181 F.3d 435, 442 (3d Cir. 1999), the United States Court of Appeals for the Third Circuit recognized that numerous jurisdictions followed the general rule ''that contractual provisions limiting or prohibiting assignments operate only to limit [the] parties' right to assign the contract, but not their power to do so, unless the parties manifest an intent to the contrary with specificity.'' (Emphasis added.) The court concluded, however, that the ''assignment clauses [did] not contain the requisite clear language to limit [the] 'power' to assign'' and, therefore, held the assignment valid and enforceable. *Id.,* 443. The court acknowledged that contracting parties could limit the power to assign by including an ''assignment provision [that] generally state[s] that nonconforming assignments (i) shall be 'void' or 'invalid,' or (ii) that the assignee shall acquire no rights or the nonassigning party shall not recognize any such assignment.'' *Id*., 442. Without such express contractual language, however, ''the provision limiting or prohibiting assignments will be interpreted merely as a covenant not to assign . . . . Breach of such a covenant may render the assigning party liable in damages to the non-assigning party. The assignment, however, remains valid and enforceable against both the assignor and the assignee.'' *Id.*

[¶9] Many other courts similarly have held that an anti-assignment provision that limits the right to assign does not void an assignment between an assignor and assignee unless there is also an express provision limiting the power to assign or a provision voiding the assignment itself. *See, e.g., Pravin Banker Associates, Ltd. v. Banco Popular Del Peru*, 109 F.3d 850, 856 (2d Cir. 1997) (' '[t]o reveal the intent necessary to preclude the power to assign, or cause an assignment violative of contractual provisions to be wholly void, [a contractual] clause must contain express provisions that any assignment shall be void or invalid if not made in a certain specified way' ''); *Cedar Point Apartments, Ltd. v. Cedar Point Investment*

Corp., 693 F.2d 748, 754 (8th Cir. 1982) (concluding that ‘‘[m]erely the ‘right to assign,’ not the power to assign, [was] limited by the express language of the [antiassignment] clause. No intent is thereby revealed to avoid an assignment not meeting the restrictions.’’); * * * *Pro Cardiaco Pronto Socorro Cardiologica, S.A. v. Trussell*, 863 F. Supp. 135, 138 (S.D.N.Y. 1994) (‘‘assignments are enforceable unless expressly made void’’); * * * [very long string cite omitted]. Thus, the modern approach finds support in the majority of jurisdictions.

[¶10] The modern approach, however, is not adopted by some courts, which uphold antiassignment clauses regardless of whether the parties have included contractual language that expressly limits the power to assign or expressly invalidates the assignment itself. We agree with these courts that contracting parties can exercise their freedom to contract to overcome free alienability when they include the appropriate contractual language. *See Parrish Chiropractic Centers, P.C. v. Progressive Casualty Ins. Co*., 874 P.2d 1049, 1054–55 (Colo. 1994) (‘‘The policy supporting free alienability is not such an absolute one that it must override a contract provision prohibiting assignment in a specific context. . . . To hold otherwise would be to force [the obligor] to deal with parties with whom it has not contracted, regardless of . . . express contractual provision . . . .’’ [cleaned up])*; Portland Electric & Plumbing Co. v. Vancouver*, 29 Wash. App. 292, 295, 627 P.2d 1350 (1981) (‘‘The primary purpose of clauses prohibiting the assignment of contract rights without a contracting party’s permission is to protect him in selecting the persons with whom he deals. . . . When a contract prohibits assignment in ‘very specific’ and ‘unmistakable terms’ the assignment will be void against the obligor.’’ [Citation omitted.]). We disagree, however, with these courts that the anti-assignment provisions in these cases contained the necessary contractual language. * * * * These courts ignore the rule adopted by the majority of jurisdictions, which requires that in order to invalidate the assignment, the parties must include in their anti-assignment provision language that specifically limits the power to assign or invalidates the assignment itself.

[¶11] The modern approach offers the advantage of free assignability together with full protection for any obligor who actually suffers damages as a result of an assignment. An assignor who breaches a contractual provision limiting his or her right to assign will be liable for any damages that result from that assignment. [Long string citation from cases in numerous jurisdictions.] Thus, courts in numerous jurisdictions have recognized the evenhandedness of the modern approach.

[¶12] This approach is also adopted in the *Restatement (Second) of Contracts*. Section 322 (2) (b) of the *Restatement (Second), supra*, provides that the general rule is ‘‘[a] contract term prohibiting assignment of rights under the contract, unless a different intention is manifested . . . (b) gives the obligor a right to damages for breach of the terms forbidding assignment but does not render the assignment ineffective . . . .’’ *See, e.g., Bel-Ray Co. v. Chemrite (Pty.) Ltd., supra*, 181 F.3d 442; * * * . In the present case, the annuity contract provided that ‘‘[n]o payment under this annuity contract may be . . . assigned’’ by the plaintiff. This anti-assignment provision limited the plaintiff’s right to assign, but not his power to do so. The provision did not contain any express language to limit the power to assign or to void the assignment itself. Therefore, in accordance with the modern approach, we conclude that the plaintiff’s assignment to Wentworth is valid and enforceable despite the plaintiff’s breach of the contract’s anti-assignment provision. We further conclude, however, that Safeco is free to sue for any damages that it might sustain as a result of the assignment by bringing an action for breach of contract against the plaintiff as assignor. * * * *

[¶13] The modern approach thus serves the dual objectives of free assignability of contracts together with full compensation for any actual damages that might result from an assignment made in breach of an anti-assignment provision.

The judgment is affirmed.

In this opinion BORDEN and PALMER, Js., concurred.

Questions:

1. Do you suppose that Safeco wrote the anti-assignment clause into the contract in order to make sure that, if assignment occurs, it would receive a damage award?

2. Why do you suppose Safeco, the liability insurer, was so bothered by the assignment? The court related that Safeco made rumblings about losing a tax-favored status, but the supreme court affirmed, "At the trial court hearing, Safeco did not show any actual damages resulting from the assignment." 757 A.2d at 536 n.11. Does this finding affect how you see the justice of the "modern" approach?

3. What policies support a broader interpretation of anti-assignment clauses, the minority rule? If the parties are not assigning merely a right to receive money, but something else is at stake, the court may see the anti-assignment clause in a different light.

In *Condo v. Conners*, 266 P.3d 1110 (Colo. 2011) (en banc), Thomas Banner was a member of Hut at Avon, LLC. The operating agreement of Hut contained an anti-assignment clause: "a Member shall not sell, assign, pledge or otherwise transfer any portion of its interest in" the LLC "without the prior written approval of all of the Members"; and if "at any time any Member proposes to sell, assign or otherwise dispose of all or any part of its interest in the [LLC], such Member . . . shall first obtain written approval of all of the Members to such transfer." *Id.* at 1113. As part of Banner and Elizabeth Condo's divorce settlement, Banner agreed to assign to Condo his right to receive distributions from Hut and his right to vote as a LLC member. Banner sought the approval of the other LLC members, but they refused. Banner then purported to assign the right to distributions and voting to Condo without their approval. When the other members objected and offered in response to buy out Banner, Banner sold to them. Condo then sued for tortious interference with contract, and this claim depended on her having the rights Banner purported to assign to her. Would the rule in *Rumbin* allow Banner's assignment to Condo to be effective?

In *Condo*, the court rejected the *Rumbin* rule and Condo's claim. The court explained:

> [¶1] We first note that the court of appeals resolved this issue by looking to what it considered to be our application of the classical approach in *Parrish Chiropractic Centers, P.C. v. Progressive Casualty Insurance Co.*, 874 P.2d 1049, 1051 (Colo. 1994), and extending this principle to the context of an anti-assignment clause in an LLC operating agreement. *Condo*, slip op. at 13-14. Under the classical approach, an assignment made

in violation of an express anti-assignment clause is void ab initio because the assignor is powerless to make a nonconforming transfer. *See id.*

[¶2] Now, Condo urges us to depart from *Parrish Chiropractic* and adhere to the modern approach as set forth in *Rumbin v. Utica Mutual Insurance Co*.,757 A.2d 526 (Conn. 2000). Under the modern approach, an anti-assignment clause creates a duty by which a party is contractually obligated to refrain from making a nonconforming assignment, but does not restrict the power of a member to nevertheless do so. *Id.* at 530-31. Instead of classifying a nonconforming assignment as void, the modern approach treats this unlawful act as a breach of the duty not to assign, which can then be enforced by the other party or parties to the contract through a breach of contract action. *Id.* As adopted in *Rumbin*, the modern approach allows for parties to contractually restrict the power — again, as opposed to the right — to assign, but such a clause will only render the parties powerless to assign when it expressly states that any nonconforming assignment is "void" or "invalid." *See id*. at 531-33 (collecting cases that apply the modern approach); *see also Travertine Corp. v. Lexington-Silverwood*, 683 N.W.2d 267, 272 (Minn. 2004) (adopting the classical approach, but characterizing the exception to the modern approach as the "magic words" requirement) [hereinafter, the "strict 'magic words' approach"].

[¶3] The Restatement, however, does not adopt the strict "magic words" approach, and instead states that whether an anti-assignment clause merely creates a duty not to assign turns on the language used and the context in which the contract is made. *Restatement (Second) of Contracts* § 322(2)(a) (1981) (noting that the general presumption that an assignment in violation of an anti-assignment clause is merely a breach of the contract and is therefore still legally effective, can be overcome if "a different intention is manifested" in the anti-assignment clause); id. cmt.c (explaining that it "depends on all the circumstances" whether the nonassigning contract parties are bound to perform any rights that are assigned in violation of the terms of an anti-assignment clause). Thus, although the Restatement is similar to *Rumbin* in that it creates a presumption in favor of treating an anti-assignment clause as a duty not to assign, given specific language in an anti-assignment clause and under the appropriate circumstances, it allows that an anti-assignment clause may render the parties powerless to assign, even in the absence of "magic words."

[¶4] Applying our previous holding in *Parrish Chiropractic* and considering the rationale underlying the Restatement approach, we hold that the Operating Agreement rendered the parties powerless to assign any portion of the membership interest without the consent of all other members. Two of the rationales we applied in *Parrish Chiropractic* are pertinent to our resolution of the present matter. First, we highlighted the strong public policy in favor of freedom of contract — that is, the ability of a party to contractually restrict the ability of other parties to assign their rights and/or duties. *Parrish Chiropractic*, 874 P.2d at 1054. Second, we emphasized "the corollary right of the [nonassigning party] to deal only with whom it contracted." *Id*. at 1054-55. Thus, we applied the classical approach in *Parrish Chiropractic* to afford contracting parties the maximum flexibility to shape their contract within the confines of the law, while simultaneously allowing for the option of increased predictability and stability in contractual relations through the use of an anti-assignment clause. *See id.* * * * *

> [¶5] * * * * Unlike the court of appeals, however, we do not treat *Parrish Chiropractic* a blanket rejection of the modern approach to assignments as adopted by the Restatement (Second) of Contracts. *See Condo*, slip op. at 13. Rather, in light of the Restatement's express limitation that the application of the modern approach is necessarily dependent on the circumstances and the express terms of the operating agreement, we narrowly hold that the strict "magic words" approach is inapplicable to the present case.

Condo, 266 P.3d at 1117-18. Sometimes it matters who you contract with. In a business owned and operated by only a few people, who those people are matters. Does the different wording between R2K § 322 and the *Rumbin* rule justify distinguishing *Rumbin*, which quoted § 322 in support? Do the meaning of § 322's words change in the application?

B. Delegation

Mostly, we have already studied this:

1. Were the station's duties to Gordon Peterson delegable?

2. Are a contractor's duties delegable?

3. What is the legal effect of holding a duty not delegable? Consider *Seitz*.

4. Let's suppose that the duty can be delegated. Is the delegating party released? No.

5. Why are rights freely assignable but duties not freely delegable?

6. Are restrictions on delegation harsher than on assignment?

Howard M. BERG and Sandra Berg v. LIBERTY FEDERAL SAVINGS AND LOAN ASS'N

Del. (1981), 428 A.2d 347

HORSEY, Justice.

[¶1] This appeal concerns whether a mortgage lender's otherwise available remedies on borrower's default are compromised by lender's dealings with a third party grantee under a debt arrangement with borrower.

[¶2] In 1970, Howard M. Berg and Sandra Berg (borrowers) executed, for valuable consideration, a bond [essentially, a promise to pay] and mortgage of real estate in favor of Liberty Federal Savings and

Loan Association (lender). In 1973, borrowers sold the real estate to a third party (grantee) who assumed liability for the mortgage indebtedness. Lender was not a party to the transaction and did not execute any contract of novation or instrument releasing borrowers from liability under their bond and mortgage. However, lender thereafter accepted timely monthly payments on the mortgage from grantee; and all further correspondence from lender concerning the mortgage was with grantee until payments ceased in late 1977.

[¶3] In early 1978 lender, after notifying borrowers that the mortgage was four months in arrears and hence in default, instituted suit against borrowers on their bond. Borrowers resisted, contending that lender, by its conduct, had "accepted" or "recognized" grantee's assumption of the mortgage and thereby legally relinquished its right otherwise to pursue concurrent remedies: that is to sue either on the bond or mortgage.[*] Lender then moved for partial summary judgment on borrowers' defense.

[¶4] Accepting for purposes of the motion borrowers' factual pleading of "recognition," Superior Court granted lender partial summary judgment. The Court found no legal support for the proposition that lender, by accepting mortgage payments from grantee, "was required to look to the land and foreclose on the mortgage prior to bringing an action on the bond."

[¶5] Later, Superior Court, after further discovery and hearing, summarily granted lender a money judgment against borrowers or their bond notwithstanding borrowers' affidavit of defense. Borrowers then docketed this appeal from both orders.

I

[¶6] The first issue in this appeal concerns a mortgage lender's available remedies against a mortgagor upon default of a nonconsensual assuming grantee,[†] absent a novation or release of the mortgagor. Appellants-mortgagors contend that lender, by accepting timely mortgage payments from grantee and by otherwise dealing with grantee rather than with mortgagor until default, was required to foreclose the mortgage before proceeding against mortgagors on their underlying bond. Mortgagors contend that Superior Court erred in applying irrelevant novation and release criteria in granting lender-plaintiff partial summary judgment dismissing mortgagors' "recognition" defense as insufficient as a matter of law.

A.

[¶7] As between a mortgage lender and a borrower-mortgagor who, by bond or note is personally bound, the law is clear and undisputed as to the creditor's rights: that on debtor's default, lender may, at its option, either sue on the bond or foreclose on the mortgage. 59 *C.J.S. Mortgages* § 342, p. 473. No implication arises from the mere taking of collateral security that a creditor will look only or primarily to the security for repayment of the loan. 55 Am.Jur.2d, Mortgages, § 536, p. 517. A creditor-mortgagee may pursue all available remedies concurrently or successively, to the extent that separate and distinct remedies

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[*] [1] Borrowers also raised an alternative defense of "release" that lender, by its conduct, had released borrowers from liability on their bond. However, borrowers did not pursue this defense either by motion to dismiss or cross-motion for summary judgment.

[†] [2] I. e., a grantee who assumed the mortgage on purchase of the real estate securing the loan from mortgagor without the knowledge and consent of mortgagee.

are recognized at law or in the controlling instrument. 59 *C.J.S. Mortgages* § 485, p. 767 and 3 *Jones on Mortgages* (8th Ed.), § 1565. Such has been the law of Delaware for over a century and a half. *Newbold v. Newbold*, Del.Ch., 1 Ch. 310 (1825), stating that it was "clearly and reasonably settled that a mortgagee may use all the remedies upon a bond and mortgage which the law affords, at the same time, and consequently any one of them which he prefers." 1 Ch. at 315.

[¶8] Absent a release or contract of novation, a mortgagor is not exonerated from personal liability on his bond or note by conveying the mortgaged premises to a third party who assumes the mortgage regardless of lender's acceptance of grantee's payments on the mortgage, assuming the terms of repayment are not varied. 2 *Jones on Mortgages* (8th Ed.), § 920; *55 Am. Jur.2d, Mortgages*, § 1045, p. 886, 59 *C.J.S. Mortgages* § 415, p 592; 41 *A.L.R.*, 317 Ann.: *Assumption of Mortgage by Grantee as Affecting Right of Mortgagee to Proceed Against the Mortgagor*.

[¶9] A novation will not be presumed but must be proved, with the burden of proof thereof resting on the proponent. 58 *Am.Jur.2d, Novation*, § 20, p. 535 and § 32, p. 542. It has been held that a creditor's knowledge of a debt assumption and acceptance of payments on the debt from assumptor is not sufficient to effect a novation or release of the original debtor. Creditor's expressed assent to give up the original debt is required. *North Western Mut. Life Ins. Co. v. Eddleman*, Ky., 247 Ky. 116, 56 S.W.2d 561 (1933); *Davenport v. Dickson*, Kan. Supr., 211 Kan. 306, 507 P.2d 301 (1973) and *Miami Nat. Bank v. Forecast Const. Corp.*, Fla. App., 366 So.2d 1202 (1979).

B.

[¶10] Appellants do not dispute the foregoing rule of law but contend that it does not control the instant case because appellants are not seeking exoneration based on release or novation but merely a reordering of lender's remedial rights. Appellants contend that Delaware case law supports their position regardless of foreign authority. * * * *

[¶11] Here there is no allegation or evidence that lender varied the terms of the debt instruments after grantee assumed the mortgage and became the primary obligor. Hence, Superior Court's finding of lender's acceptance or "recognition" of grantee's assumption of the mortgage does not remove the case from the controlling rules set out under I A * * * above.

[¶12] Lender's acceptance of timely mortgage payments from grantee over a period of four years and related correspondence was insufficient as a matter of law to alter lender's right under the terms of mortgagor's bond and firmly established precedent to proceed, on default, at its option either on the bond or to foreclose on the mortgage. The terms of appellants' bond expressly conferred this right upon lender. * * * *

AFFIRMED.

Questions:

1. An accord is an agreement by an obligee to accept a substitute performance in place of the obligor's original obligation. Satisfaction is the performance of the substitute performance. What is the difference between a novation and an accord and satisfaction?

2. Smith Homes, Inc., a homebuilder, contracts to build me a house. Immediately after executing the contract, Smith Homes calls subcontractors. For instance, Smith Homes hired Moore Plumbing to install all the plumbing. Has Smith breached? If Moore installs the plumbing badly, has Smith breached? Also, can I sue Moore? That last question is addressed in the next section.

C. Third-Party Beneficiaries

Sometimes contracts obviously mean to give rights to third parties. A life insurance policy is a good example: Arturo bought $750,000 of life insurance from Prudential Ins. Co. and named Irasema primary beneficiary of half the amount and his adult children primary beneficiaries of the other half. Arturo then died, at which point Prudential owed somebody the life insurance proceeds. But whom? Prudential resisted paying because Arturo did not name clear contingent beneficiaries, but after the court overruled that objection to Arturo's beneficiary designation form, it confirmed that (i) Irasema was a third-party beneficiary of the life insurance policy, with standing to sue for breach; (ii) Prudential breached; and (iii) Irasema was entitled to half the death benefit. *Prudential Ins. Co. v. Durante*, 443 S.W.3d 499, 502, 505, 509-10, 515 (Tex. App.—El Paso 2014, pet. denied).

That's an easy case once Prudential's objection is rejected. The policy named Irasema "beneficiary," even. But sometimes a contract fairly obviously benefits a nonparty without calling them "beneficiary" and sometimes without naming them at all. Do these people have rights? Such cases can be tricky. Many contracts are arguably for the benefit of others, and each situation is to some extent unique. Moreover, courts have offered a couple of tests for whether legal rights arise.

The ultimate issue, despite the long rule statements courts use, is whether the parties to the contract intended that a third party be able to enforce it. That was true in *Prudential Ins. Co* because Arturo was going to be deceased when Prudential's contract performance fell due. Sometimes courts are also influenced by the absence of any other party with an incentive to enforce—also a factor in *Irasema v. Prudential*. Consider some other fact patterns:

James C. BAIN v. John GILLISPIE

Iowa App. (1984), 357 N.W.2d 47

SNELL, Presiding Judge.

[¶1] James C. Bain serves as a referee for college basketball games. During a game which took place on March 6, 1982, Bain called a foul on a University of Iowa player which permitted free throws to a Purdue University player. That player scored the point that gave Purdue a last-minute victory. Some fans of the University of Iowa team blamed Bain for their team's loss, asserting that the foul call was clearly in error.

[¶2] John and Karen Gillispie operate a novelty store in Iowa City, specializing in University of Iowa sports memorabilia. The store is known as Hawkeye John's Trading Post. Gillispie's business is a private enterprise for profit having no association with the University of Iowa or its sports program.

[¶3] A few days after the controversial game, Gillispies began marketing T-shirts bearing a reference to Bain. It showed a man with a rope around his neck and was captioned "Jim Bain Fan Club." On learning of it, Bain sued Gillispies for injunctive relief, actual and punitive damages. Gillispies counterclaimed, alleging that Bain's conduct in officiating the game was below the standard of competence required of a professional referee. As such, it constituted malpractice which entitles Gillispies to $175,000 plus exemplary damages. They claim these sums because Iowa's loss of the game to Purdue eliminated Iowa from the championship of the Big Ten Basketball Conference. This in turn destroyed a potential market for Gillispies' memorabilia touting Iowa as a Big Ten champion. Their claim for actual damages is for loss of earnings and business advantage, emotional distress and anxiety, loss of good will, and expectancy of profits. Exemplary damages are asked because Bain's calls as a referee were baneful, outrageous, and done with a heedless disregard for the rights of the Gillispies.

[¶4] The trial court found the Gillispies had no rights and sustained a motion for summary judgment dismissing Gillispies' counterclaim. They appeal, contending the trial court erred in finding no genuine issue of material fact. The triable issues claimed are: * * * that Gillispies are beneficiaries of an employment contract between Bain and the Big Ten Athletic Conference. * * * *

[¶5] In addition to the parties' briefs, the National Association of Sports Officials (NASO) has filed a motion to appear as amicus curiae and to file a brief on behalf of appellee Bain. NASO is an association of sports officials who officiate sports at all levels of competition. It has approximately 9000 members residing in all 50 states. We have granted the motion and considered the brief. * * * *

[¶6] The trial court also found that there was no issue of material fact on the Gillispies' claim that they were beneficiaries under Bain's contract with the Big 10. Gillispies argue that until the contract is produced, there exists a question of whether they are beneficiaries. There is some question of whether there is a contract between Bain and the Big 10. In his response to interrogatories, Bain stated that he had no written contract with the Big 10, but that there was a letter which defined "working relationship." Although this letter was never produced and ordinarily we would not decide an issue without the benefit of examining the letter's contents, we nevertheless find the issue presently capable of determination. By deposition Gillispies answered that there was no contract between them and Bain, the Big 10 Athletic Conference, the University of Iowa, the players, coaches, or with any body regarding this issue. Thus, even if the letter were considered a contract, Gillispies would be considered third-party beneficiaries. Because Gillispies would not be privy

to the contract, they must be direct beneficiaries to maintain a cause of action, and not merely incidental beneficiaries. *Khabbaz v. Swartz*, 319 N.W.2d 279, 284 (Iowa 1982).

[¶7] A direct beneficiary is either a donee beneficiary or a creditor beneficiary. *Id*. In *Olney v. Hutt*, 251 Iowa 1379, 105 N.W.2d 515 (1960), the Iowa Supreme Court defined these terms as follows:

> (1) Where performance of a promise in a contract will benefit a person other than the promisee that person is * * * (a) a donee beneficiary if it appears from the terms of the promise in view of the accompanying circumstances that the purpose of the promisee in obtaining the promise of all or part of the performance thereof is to make a gift to the beneficiary or to confer upon him a right against the promisor to some performance neither due nor supposed or asserted to be due from the promisee to the beneficiary; (b) a creditor beneficiary if no purpose to make a gift appears from the terms of the promise in view of the accompanying circumstances and performance of the promise will satisfy an actual or supposed or asserted duty of the promisee to the beneficiary.

Id. at 1386, 105 N.W.2d at 519.

[¶8] Gillispies make no claim that they are creditor beneficiaries of Bain, the Big 10 Athletic Conference, or the University of Iowa. “The real test is said to be whether the contracting parties intended that a third person should receive a benefit which might be enforced in the courts.” *Bailey v. Iowa Beef Processors, Inc*., 213 N.W.2d 642, 645 (Iowa 1973), cert. denied 419 U.S. 830, 95 S. Ct. 52, 42 L. Ed. 2d 55 (1974). It is clear that the purpose of any promise which Bain might have made was not to confer a gift on Gillispies. Likewise, the Big 10 did not owe any duty to the Gillispies such that they would have been creditor beneficiaries. If a contract did exist between Bain and the Big 10, Gillispies can be considered nothing more than incidental beneficiaries and as such are unable to maintain a cause of action. *Olney v. Hutt*, 251 Iowa 1379, 1386, 105 N.W.2d 515, 518 (1960).

[¶9] Consequently, there was no genuine issue for trial which could result in Gillispies obtaining a judgment under a contract theory of recovery. The ruling of the trial court sustaining the summary judgment motion and dismissing the counterclaim is affirmed.

AFFIRMED.

Questions:

1. Iowa followed the Restatement of Contracts categories. Can you think of an example of a creditor beneficiary? Why would the court want to grant rights to a creditor beneficiary?

2. What is a donee beneficiary? Why would the court want to grant rights to a donee beneficiary?

3. Does the *Bain* case have anything to do with the intent of the Big 10?

SIMON v. ZIPPERSTEIN

Ohio (1987), 512 N.E.2d 636

Per Curiam.

[¶1] The sole consideration presented by this appeal is whether in the absence of fraud, collusion or malice, an attorney may be held liable in a malpractice action by a beneficiary or purported beneficiary of a will where privity is lacking. For the reasons that follow, we answer this question in the negative and reverse the judgment of the court of appeals.

[¶2] It is by now well-established in Ohio that an attorney may not be held liable by third parties as a result of having performed services on behalf of a client, in good faith, unless the third party is in privity with the client for whom the legal services were performed, or unless the attorney acts with malice. [Long list of citations omitted.]

[¶3] The rationale for this posture is clear: the obligation of an attorney is to direct his attention to the needs of the client, not to the needs of a third party not in privity with the client. As was stated by the court in *W.D.G., Inc., supra*:

> "* * * Some immunity from being sued by third persons must be afforded an attorney so that he may properly represent his client. To allow indiscriminate third-party actions against attorneys of necessity would create a conflict of interest at all times, so that the attorney might well be reluctant to offer proper representation to his client in fear of some third-party action against the attorney himself."

Id. at 399-400.

We emphasize that our view on the liability of attorneys to third-persons as a result of services performed in good faith on behalf of a client is shared by other jurisdictions. See [long list of citations, omitted].

[¶4] In the instant case, appellee's complaint set forth no special circumstances such as fraud, bad faith, collusion or other malicious conduct which would justify departure from the general rule. In addition, privity was lacking since appellee, as a potential beneficiary of his father's estate, had no vested interest in the estate. *Cf. Cunningham v. Edward*, (1936), 52 Ohio App. 61, 6 O.O. 98, 3 N.E.2d 58. Although the court of appeals acknowledged the applicability of Scholler, supra, it elected to disregard the holding based upon "public policy" grounds. We disapprove of the approach taken by the court of appeals and its refusal to adhere to precedent. We reiterate our holding in the first paragraph of the syllabus of Scholler that "[a]n attorney is immune from liability to third persons arising from his performance as an attorney in good faith on behalf of, and with the knowledge of his client, unless such third person is in privity with the client or the attorney acts maliciously."

[¶5] For the foregoing reasons, the judgment of the court of appeals is hereby reversed, and the judgment of the trial court is reinstated.

Judgment reversed.

BROWN, J., dissenting.

[¶1] I must respectfully dissent. The result reached by the majority means that an attorney who negligently prepares a will is immune from liability for malpractice. For example, if an attorney carelessly fails to see that the will is signed by the required number of witnesses, no action can be brought against the inattentive lawyer. This is so because the client, the testator, must die before the will becomes operative. Nonetheless, only the client, says the majority, may bring the malpractice action. To reach this undesirable result, the majority trots out that old chestnut, privity.

[¶2] In the law of torts, the use of privity as a tool to bar recovery has been riddled (and rightly so) to the extent that we are left with legal malpractice as, perhaps, the only surviving relic. For example, a physician who negligently injures a spouse or a minor child is responsible to the other spouse or to the parent(s) for their corresponding loss of consortium or loss of services, notwithstanding the absence of privity. * * * * Likewise, an architect or builder who defectively designs or constructs a building is liable to a person thereby injured, despite a lack of privity. * * * * Additionally, the manufacturer of a defective product is not excused for want of privity from liability to an injured user. * * * * Even an accountant is no longer immune from liability to third persons who foreseeably rely upon his or her negligent representations. * * * *

[¶3] While the court of appeals below should perhaps have given greater obeisance to *Scholler v. Scholler,* (1984), 10 Ohio St.3d 98, 10 OBR 426, 462 N.E.2d 158, this court is under no such duty. The requirement of privity in a legal malpractice action should be put to a well-deserved burial. Such is not to abandon stare decisis, but rather to bring attorney malpractice—based upon professional negligence—into line within the body of tort law.

[¶4] What the majority has done is to make a mechanical application of Scholler, supra, to the facts of the cause sub judice. Then, the majority blandly claims that its view is "shared by other jurisdictions." The issue before us is not that simple. An examination of the seven cases cited by the majority reveals that only two involve an attorney's negligence in drafting a will. *See St. Mary's Church of Schuyler v. Tomek,* (1982), 212 Neb. 728, 325 N.W.2d 164, and *Maneri v. Amodeo,* (1963), 38 Misc.2d 190, 238 N.Y. Supp. 2d 302. The remaining five cases arise from a potpourri of factual situations, having nothing to do with the issue before us.

[¶5] Actually, most courts that have faced the issue have been unwilling to use privity to insulate attorneys from liability for negligent will preparation. See [long list of citations]. These courts have perceptively emphasized that in drafting a will, the attorney knows that (1) the client has employed him or her for the specific purpose of benefiting third persons, and (2) the consequences of an error by the lawyer will most likely fall upon those intended beneficiaries rather than upon the client.

[¶6] The majority has unfortunately been blinded by the mirage of conflict of interest. The majority states, and I agree, that "the obligation of an attorney is to direct his [or her] attention to the needs of the client, not to the needs of a third party not in privity with the client." Where the attorney's job is to draft a will, however, the needs of the client simply require the attorney to competently construct an instrument that will carry out the client's intentions as to the distribution of his or her property upon death. If the attorney negligently fails to fulfill those needs, with the result that an intended beneficiary receives less than the client desired, surely

the client, if he or she were still alive, would want the intended beneficiary to bring an action against the attorney. The conflict-of-interest bugaboo is nonexistent in such a case.*

[¶7] I would hold that an attorney who negligently drafts a will is not immune from liability to those persons whom the testator intends to be beneficiaries thereunder.

Question: The Oregon Supreme Court, in *Hale v. Groce*, 744 P.2d 1289 (Or. 1987), said in a similar case, "We agree that the beneficiary in these cases is not only a plausible but a classic 'intended' [or direct] third-party beneficiary of the lawyer's promise to his client within the rule of Restatement section 302(1)(2) and may enforce the duty so created . . . ." The testator is dead. Do you suppose that, when the testator was alive, the testator considered whether and then concluded that it would be appropriate for the devisees of the testator's will to sue the lawyer who is drafting the will if the will did not actually convey the property that the testator intended? The lawyer is the other party to the contract. What do you suppose the lawyer intended?

PROBLEMS

For these problems, see if you can determine what the answer should be.

PROBLEM 49: A mortgages Blackacre to Bank to secure a thirty-year promissory note. After five years of making payments, A sells Blackacre to C, and C assumes the loan, meaning that C promises A that C will pay all of the remaining payments to Bank and, in general, perform as A would have under the promissory note and mortgage. Is Bank a third-party beneficiary of the contract between A and C?

PROBLEM 50: A mortgages Blackacre to Bank to secure a thirty-year promissory note. After five years of making payments, A sells Blackacre to C subject to the mortgage. In this deal, C promises to pay A the

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* [4] The California Supreme Court has explained: "When an attorney undertakes to fulfill the testamentary instructions of his client, he realistically and in fact assumes a relationship not only with the client but also with the client's intended beneficiaries. The attorney's actions and omissions will affect the success of the client's testamentary scheme; and thus the possibility of thwarting the testator's wishes immediately becomes foreseeable. Equally foreseeable is the possibility of injury to an intended beneficiary. In some ways, the beneficiary's interests loom greater than those of the client. After the latter's death, a failure in his testamentary scheme works no practical effect except to deprive his intended beneficiaries of the intended bequests." Heyer v. Flaig (1969), 70 Cal.2d 223, 228, 74 Cal. Rptr. 225, 228-229, 449 P.2d 161, 164-165.

exact payments that A will owe to Bank under A's promissory note and mortgage. Is Bank a third-party beneficiary of the contract between A and C?

PROBLEM 51: Owner hires Contractor to remodel owner's home. Contractor hires Subcontractor to change the plumbing in the kitchen. Later, the plumbing in the kitchen installed by Subcontractor breaks, and Owner's house is flooded. May Owner sue Subcontractor for the damages?

PROBLEM 52: Owner, a state agency, hired Contractor to build a school. Owner required Contractor as part of the deal to obtain a surety bond in favor of the Owner called a "Payment Bond." The bond was in the total amount of the contract, and in it the surety company promised to pay subcontractors, workers, and suppliers if the Contractor failed to pay. On payment of all subcontractors, workers, and suppliers, the bond by its terms becomes void. Contractor proceeded with the building, but as the building was substantially finished, the Contractor became insolvent and filed for bankruptcy. Owner had already paid Contractor 90% of the contract price. Several subcontractors were not paid, however. They would file mechanics' liens on the property if it were not property of the state, but because it is, they cannot. Subcontractors are owed funds equaling 30% of the entire cost of the building. Owner refused to pay. Should the subcontractors file an action against the surety company?

PROBLEM 53: Twelve families, each headed by a US veteran, bought homes from Schmidt. The homes were built pursuant to a contract Schmidt had with the Federal Home Administration, or FHA, which engaged in such contracts pursuant to a regulation that gave priority in building materials to construction of homes for veterans. When Schmidt applied for his priority, he was required to submit plans that complied with FHA regulations. The homes had to include exterior wood walls, two 30,000 BTU gas floor furnaces, and interior walls of plaster. The homes also had to sell for $120,000 or less. When the homes were built, instead of wood exterior walls, they had paper covered with stucco. They each had only one gas furnace. Interior walls were built with sheet rock. The homes leaked, were cold, and developed mold and mildew because of Schmidt's failures to perform according to his agreement with the FHA. However, when the twelve families bought the homes, each was aware of how they were made and that they each contained only the one heater. None of the families was aware of the content of Schmidt's contract with the FHA. The twelve families later sued Schmidt as third-party beneficiaries of Schmidt's contract with the FHA. What result? This problem is based on *Shell et al. v. Schmidt*, 272 P.2d 82 (Cal. App. 1954).

Courts normally hold that a third-party beneficiary's rights are subject to any claims or defenses that the promisor has against the promisee.

PROBLEM 54: Jim owned a 1972 Nova, red, with a big spoiler on the back. Jim was insured by All-State Insurance Co. with auto insurance required by law. The auto policy contained an arbitration clause requiring arbitration of any claims arising out of or in connection with the obligation to provide insurance in the contract. Jim negligently caused an accident in which Shelley's 1972 Nova, blue, with custom leather seats, was wrecked and Shelley was injured. Jim is poor, and his car was his sole asset of any value. Shelley

therefore has sued All-State, claiming to be a third-party beneficiary of Jim’s policy. Assuming she is, will she have to arbitrate her claim?