

**An Introduction
to the Law
of Contracts**

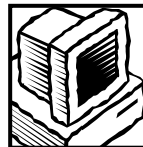
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An Introduction to the Law of Contracts

THIRD EDITION

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An Introduction to the Law of Contracts

THIRD EDITION

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TO David
AND Larry, Brian & Taylor



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Preface

The paralegal profession continues to grow dramatically. Each year more attorneys rely on the services of paralegals, and each year attorneys expect more sophisticated work from their paralegals. As attorney expectations increase, paralegal training becomes more demanding and more advanced.

As with all relatively new programs, paralegal teaching materials have lagged behind the demand. Often instructors have not had materials specifically designed for their needs. This has been true for the field of contracts law where the materials used were often borrowed from business law or law school programs rather than designed especially for paralegal programs. This text, originally titled *Introduction to Contracts and Restitution*, when published in 1988, was written specifically to meet the needs of paralegal education.

This is the third edition of our contracts text. Although the title has been changed to *An Introduction to the Law of Contracts* and the restitution material has been deemphasized, this edition retains the contract's "road map" along with other features that our readers have found helpful from the earlier editions.

A Well Organized, Functional Approach to the Law of Contracts

An Introduction to the Law of Contracts provides students with a well organized, functional approach to the law of contracts. Students learn an approach for analyzing contracts problems. This means they can readily transfer what they learn in class to what they need for their professional assignments. Our former students tell us that they remember and use the analysis in practice. This functional approach takes the form of a five step paradigm.

Step One: What law applies to this transaction?

Step Two: Has a contract been formed?

Step Three: Is the contract enforceable?

Step Four: Has the contract been breached?

Step Five: What remedies are available to the plaintiff for the defendant's breach of contract?

For those students who find visual aids reinforce their learning, the paradigm is presented as a "road map" for the law of contracts.

Organization of the Textbook

This text introduces the law of contracts to paralegal students. It is written with the basic premise that the law of contracts need not be a jumble of unrelated rules. To remove the mystery from the law of contracts, we developed the road map for analyzing breach of contract causes of action. The text follows the road map found in the Introduction.

An Introduction to the Law of Contracts is divided into six parts. Each of the first five parts takes students through a step in the road map analysis. The sixth part goes beyond the original two contracting parties and explores third party interests in the contract.

Part I. Step One: Determining the Applicable Law (Choice of Law)

Part II. Step Two: Contract Formation

Part III. Step Three: Contract Enforceability

Part IV. Step Four: Breach of Contract

Part V. Step Five: Plaintiff's Remedies for the Defendant's Breach of Contract

Part VI. Step Six: Third Party Interests

A new feature of the third edition is the reintroduction of the road map at the beginning of each chapter. The material covered in the chapter is highlighted on the road map. This will help students relate the chapters to each other.

Students learn that the rules of law are not unrelated rules that must be memorized in the abstract but are related and form a cohesive structure. A change of one rule may, therefore, have an impact on the other rules of the structure.

Primary Pedagogical Features

The primary pedagogical features of this text are the contracts paradigm, the active involvement of students in learning the rules and how they work, the comparative approach between a common law and a code solution, the straightforward use of terms and concepts, and drafting exercises.

The Contracts Paradigm (the road map)

The *Introduction* is devoted to presenting the contracts paradigm and its visual model, the road map. Thus the *Introduction* presents a summary of the course and is intended to be used as a review tool as the course evolves. The *Introduction* should be revisited as each chapter is begun.

The Development of the Rules of Law by Actively Involving Students

A rule of law is presented in three stages. Students first see the rule discussed in the abstract. Thus students acquire the "black letter rule." The rule will be followed by a clearly designated "Example." The example demonstrates how the rule relates to a concrete set of facts. The rule is no longer merely an

abstraction but becomes a tool for resolving a dispute. Finally, students will be asked to actively participate in a “Paralegal Exercise” by relating a given set of facts to the rule or by analyzing a short judicial opinion that demonstrates how a court relates a set of facts to the rule. The Paralegal Exercise is provided to enable students to develop their skills by applying what they have learned. It is a practical method of immediately reinforcing newly acquired knowledge. By actively participating in either a Paralegal Exercise or by analyzing a case, students gain an understanding of the dynamics of the rules and how the rules relate to each other.

Problem Resolution under the Common Law and under a Code

This text also teaches students how to analyze a contracts transaction using a common law approach and a code approach (Articles 1 and 2 of the Uniform Commercial Code). The code analysis is not only important in the abstract but is an essential tool now because contracts for the sale of goods are governed by code.

Straightforward Use of Terms and Concepts

The text approaches the law of contracts pragmatically. An attempt is made to cut through excess verbiage (e.g., consideration rather than adequate consideration; contract rather than valid contract) and outdated doctrine (e.g., manifestation of assent rather than meeting of the minds). This approach enables students to gain an understanding of the rules rather than merely parrot obsolete and often misleading terms and phrases.

Extrapolating Analytical Techniques to Other Fields of Law

Students learn that if a paradigm (road map) can be developed for this area of law, a paradigm can be designed for other areas as well.

Review and Study Materials

Every chapter ends with materials that reinforce the rules of the chapter. Chapter-ending materials include a “Paralegal Checklist” and a test bank of “Review Questions.”

Paralegal Checklist

The “Paralegal Checklist” feature was added for the second edition. The Checklist provides students with a brief, but detailed review of each chapter and is a most effective method of summarizing what was learned in the chapter. The Checklists have been rewritten for the third edition.

Review Questions

Following the Paralegal Checklist for each chapter is a new feature for the third edition, a test bank of “Review Questions.” Review Questions have five sections: (1) define the following new terms and phrases; (2) true/false questions;

(3) fill-in-the-blank questions; (4) multiple choice questions; and (5) short answer questions. These questions are designed to test the student's knowledge of the basic concepts discussed in the chapter. The answers are found in Appendix B.

Additional Pedagogical Features

We have included in *An Introduction to the Law of Contracts* a number of additional pedagogical features, including an introductory paragraph on chapter objectives and a chapter road map, multiple figures and charts, definitions of new terms and phrases, extensive examples, numerous paralegal exercises, selected edited cases, and drafting problems.

Chapter Objectives and Chapter Road Map

Each chapter begins with a paragraph orienting the student to the objectives of that chapter. A new feature for the third edition is the Chapter Road Map. Following the chapter's orientation paragraph is a chapter road map that places the topic of the chapter in the context of the contracts road map. By learning how concepts relate, students develop an approach to analyzing a contracts transaction.

Figures and Charts

Figures and charts have been added throughout the text. These figures and charts are designed to present material in a logical and easy to understand manner.

Definitions of New Terms and Phrases

A new feature for the third edition is the bolding of new terms and phrases. This is designed to capture the students' attention immediately. Care has been taken to define terms and phrases as they first appear in the text. All bold face terms and phrases are listed and defined again in the "Glossary" at the end of the text.

Extensive Examples

Each rule is illustrated with one or more examples. The examples demonstrate how the rule is used for resolving a dispute.

Numerous Paralegal Exercises

After the rule and its example, students are asked to apply the rule to a new set of facts. These brief Paralegal Exercises give students an opportunity to explore the rule and its application.

Selected Edited Cases

At times, a rule and its example are followed by a judicial opinion. In the third edition, the number of cases has been reduced to about twenty-five and the cases have been edited to highlight the rule being discussed.

Drafting Problems

A chapter on drafting a contract follows the chapters on contract formation. This chapter provides a change of pace for those who have the time and the desire to include some drafting exercises in the course. Also several short drafting exercises are sprinkled throughout the text. As with other pedagogical devices that are used through the text, the drafting exercises are designed to give students a “hands on” experience with the material.

Appendixes and Other Back Matter

The back matter is divided into a glossary, comments on briefing cases and analyzing statutes, answers to the review questions, the Uniform Commercial Code Articles 1 and 2 with selected comments, and an index.

Glossary

The Glossary has been expanded from 150 to 200 terms and phrases. The Glossary provides not only a quick reference for the definition of terms and phrases but a source for review prior to tests.

Briefing Cases and Analyzing Statutes

Appendix A discusses how to brief a case and how to analyze a statute. The briefing techniques presented in this appendix can be applied to the cases found in the text.

Answers to Review Questions

The answers to the chapter review questions are located in Appendix B. Student’s may check their answers after they have answered the review questions.

Uniform Commercial Code Articles 1 and 2 with Selected Comments

Articles 1 and 2 of the UCC with selected comments provides students with an opportunity to consider a code section in the context of other code sections. Students gain an understanding that the code is an integrated document and not merely a group of unrelated statutes. Once students understand the drafting organization of article 2 of the UCC, they will understand the drafting organization of other Uniform Codes.

Index

The extensive index at the end of the book assists students in quickly finding the location of materials within the text.

New Features of the Third Edition

Among the changes and new features of the third edition are:

- The balance between breach of contracts causes of actions and restitution causes of actions has been adjusted to emphasize breach of contract.

- The Road Map is reintroduced at the beginning of each chapter so students understand how the information in this chapter relates to the other chapters.
- Case names added to the table of contents for quick reference and for outlining purposes.
- The number of cases has been substantially reduced, several new short cases have been added, and many of the remaining cases have been edited so the text may be covered more rapidly.
- New terms and phrases now appear in boldface type and are defined when they first appear in the text to give students immediate access to new vocabulary.
- The Choice of Law chapter has been abbreviated so the contract formation, enforceability, breach, and remedy chapters can be reached more rapidly.
- The Preoffer and Offer chapters have been combined with offer being discussed first so students will know what an offer is before they explore why there was no offer.
- The number of diagrams has been significantly increased for the visual learner.
- The number of drafting documents has been increased so students can understand the blending of theory and practice.
- Several contracts have been added to the text so students can see a contract and reference is made to several web sites so students can explore and retrieve a number of types of contracts.
- Paralegal Checklists have been put into question form to provide a more interactive experience for the students.
- A test bank has been added at the end of each chapter so students can test their own level of comprehension.
- The Glossary has been substantially expanded.

Supplemental Teaching Materials

The supplemental teaching materials include an Instructor's Manual and a computerized test bank. These materials are designed to assist the instructor in class preparation and to provide a foundation for test writing.

Instructor's Manual

The third edition of *An Introduction to the Law of Contracts* is accompanied by an instructor's manual that includes sample course syllabi, answers to the Paralegal Exercises in the text, and synopses of the cases. Also included in the Instructor's Manual are transparency masters that will make teaching easier.

Computerized Test Bank

The test questions that appear in the Instructor's Manual will be available on computer disk. Also on disk are the transparency masters so they may be used in a power point presentation.

Web Site

Come visit our web site at www.westlegalstudies.com, where you will find valuable information specific to this book and other West Legal Studies texts.

Acknowledgments

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INTRODUCTION

A Road Map for Analyzing the Law of Contracts

This introduction is the most important section in this text. It gives an overview of the analytical process for evaluating a dispute involving a contract and is a point of reference for all topics discussed in the text. If students use this section as intended and review it as they work through each subsequent section, they will have firmly in mind an analytical process for evaluating a transaction involving a contract.

There are five steps for analyzing the law of contracts. Within each step, issues of major importance are identified and discussed. Because each step is the foundation for the next, it is important to understand each step before going on to the next.

The five steps and the chapters in which each will be examined in depth are:

- Step One: Determining the Applicable Law (Choice of Law)
 - Chapter 1
- Step Two: Contract Formation
 - Chapters 2 through 6
- Step Three: Contract Enforceability
 - Chapters 7 through 9
- Step Four: Breach of Contract
 - Chapter 10
- Step Five: Plaintiff's Remedies for the Defendant's Breach of Contract
 - Chapter 11

As is evident from this list, eleven chapters are necessary to cover the five steps in the analysis. Therefore, the Introduction provides only an overview of the issues in each step of the Road Map. Do not attempt to memorize the Introduction but return to it often for an overview of the course (see Figure I-1).

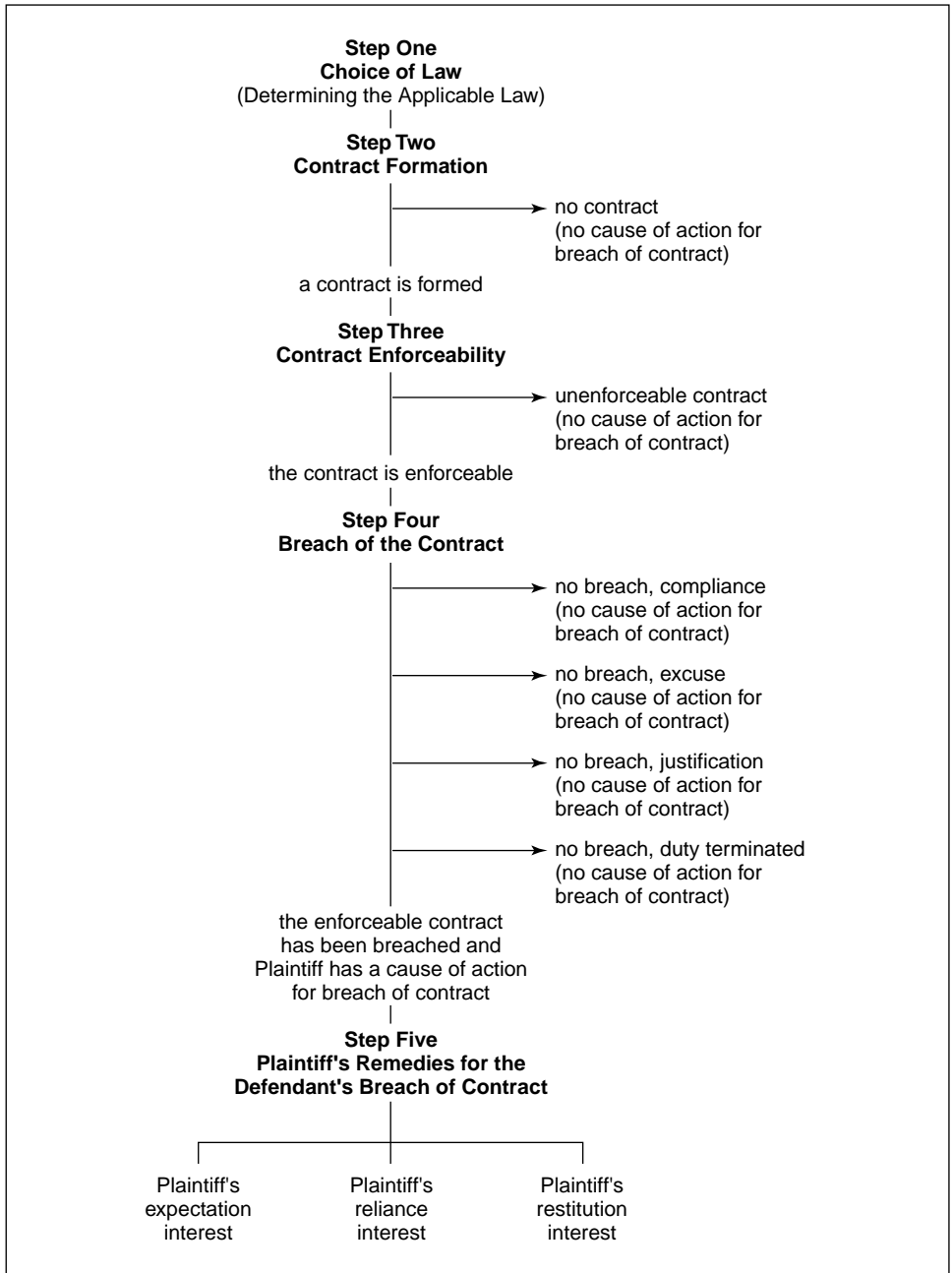
Step One: Determining the Applicable Law (Choice of Law)

Choice of Law is the selection of the legal rules under which the dispute will be resolved. Choice of law, therefore, is the threshold step in the contracts analysis. Choice of law questions arise in a number of settings: conflicting federal and state laws; conflicting laws of two different states; conflicting laws within a state.

A conflict may exist between federal and state law. Federal law, for example, may preempt or override state law in some aspects of a consumer transaction.

- **EXAMPLE** Buyer purchases a VCR for home use from a department store. The Seller of a consumer product, in making a written warranty, must follow the requirements set forth in the federal Magnuson-Moss Warranty—Federal Trade Commission Improvement Act. This Act establishes federal minimum standards for written warranties, limitations on disclaimers of

FIGURE I-1 Breach of Contract Road Map



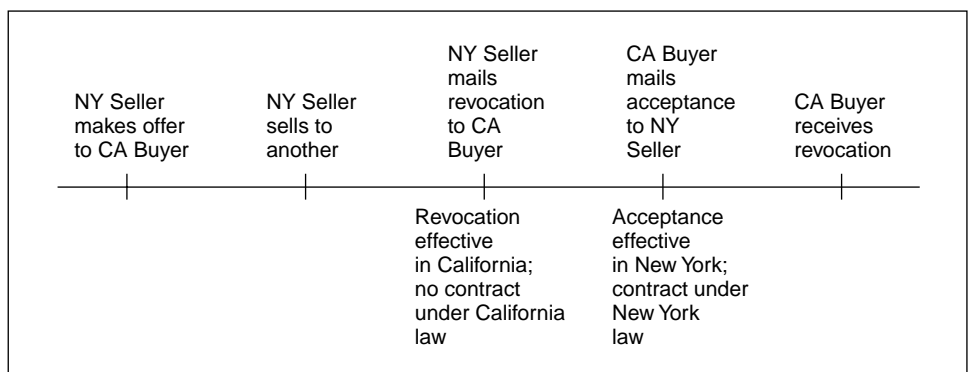
implied warranties, and remedies, separate and apart from state remedies. Buyer, therefore, acquires rights under federal law that exceed those rights acquired under state law.

If state law applies, geographic considerations raise choice of law questions. In a transaction spanning several states, which state's law governs must be determined at the outset. An **interstate transaction** (also known as a multi-state transaction) is a transaction spanning several states. Does the law of State A or the law of State B govern the transaction?

- **EXAMPLE** A New Yorker owns a yacht that she is interested in selling. The New Yorker mails a letter to a potential Buyer in California promising to sell the yacht for \$175,000. After sending this letter but before receiving a response from the California Buyer, the Seller sells the yacht to someone else for \$200,000. Upon completing this sale, the Seller mails a letter to the California Buyer revoking her offer. After Seller's letter of revocation has been sent but before it has been received, the California Buyer mails a letter to the Seller accepting Seller's offer. Upon receiving California Buyer's letter of acceptance, the Seller notifies the California Buyer that she has sold the yacht to someone else.

Under both New York and California law, an offer sent by mail is effective when sent. New York and California, however, have different rules as to when revocation is effective. In New York revocation is effective when received. In California revocation is effective when sent. If California law applies, the Seller's revocation of her offer was effective (when sent) before the Buyer's acceptance was effective (when sent). If New York law applies, the Buyer's acceptance is effective (when sent) before the Seller's revocation is effective (when received). Therefore, the choice between New York and California laws will determine whether a contract between the New York Seller and the California Buyer has been formed.

Once the appropriate state is determined, the investigation considers whether a special body of law within that state applies to the transaction. If the transaction is a sale of goods, for example, the appropriate state's version of Article 2 of the Uniform Commercial Code (UCC) will govern the transaction rather than the state's common law. The **Uniform Commercial Code** is a comprehensive compilation of rules drafted by the American Law Institute and the National Conference of Commissioners on Uniform State Laws. The UCC includes a number of topics including sale of goods. The UCC becomes the law of a given state upon



enactment by that state's legislature and signature of the governor. The **common law** is the body of law derived from judicial decisions (i.e., court made law).

- **EXAMPLE** Owner takes her car to Garage for repair. The car needs new parts, body work, and painting. The bill is itemized at \$300 labor and \$300 parts. After three months, the paint blisters. If the transaction is governed by Article 2 of the UCC (sale of goods), there will be an implied warranty that the paint would be fit for the ordinary purpose, and Owner could recover. If, however, the transaction is not viewed as a sale of goods but only as a sale of services, the transaction is not governed by Article 2 of the UCC, no implied warranty attaches to the transaction, and owner could not recover for the blistering paint job unless Garage expressly warranted that the paint would not blister.

While this example illustrates the impact of Article 2 of the UCC on contracts law, the UCC is not the only body of specialized state law that affects contracts. Another illustration involves identifiable groups of contracting parties who may be unable to protect themselves. A state legislature may enact special rules to protect consumers, minors, and the mentally incapacitated. The legislature may change other court-made rules of contracts law as well.

Once choice of law issues have been resolved, the next and one of the most important questions in the analysis must be raised—"Has a contract been created?"

Step Two: Contract Formation

The second step in the contracts analysis focuses on the two components of contract formation: the offer and the acceptance.

The Offer. An **offer** is a manifestation of willingness to enter into a bargain, which justifies another person in understanding that his or her assent to that bargain is invited and will conclude it. What constitutes an offer and when an offer has been made are basic inquiries at this stage. The **offeror** is the party who makes the offer. The **offeree** is the party who receives the offer and is asked to accept it and thus form a contract.

What constitutes an offer is determined by the components of the offer. An offer may be for a bilateral contract or for a unilateral contract. When the **offer is for a bilateral contract**, the offeror makes a promise to entice the offeree to make a promise (a promise for a promise). If the offeree accepts by promising, a contract is formed. The offeree's performance of his or her promise will be after contract formation. The components of an offer for a bilateral contract are:

- the offeror's promise
- the offeree's promise
- the offeror is making his or her promise to induce the offeree to promise
- **EXAMPLE** "I promise to pay you \$1,000 for your promise to paint my house."

When the **offer is for a unilateral contract**, the offeror makes a promise to entice the offeree to perform (a promise for a performance). The offeror does

not want the offeree's promise. The offeror only wants the offeree's performance. If the offeree accepts by performing, a contract is formed. The offeree's performance occurs before contract formation. The vast majority of contracts are bilateral. Unilateral contracts are very rare. The components of an offer for a unilateral contract are:

- the offeror's promise
- the offeree's performance
- the offeror is making his or her promise to induce the offeree to perform
- EXAMPLE "I promise to pay you \$1,000 for your painting my house."

Consideration is what the offeror wants in exchange for his or her promise. If the offeror makes a promise without demanding something in return, the offeror's promise is "not supported by consideration" and there is "no offer." The offeror has only made a promise to make a future gift.

We have chosen to include the concept of consideration as a crucial element of both offer and acceptance. Often, the concept of consideration is treated as a third element of contract formation: offer, acceptance, and consideration. If consideration is treated as a separate element and not a part of the offer, the conclusion might very well be "offer, but no consideration." Although this difference may appear to be semantic, it goes to the heart of what an offer is: a promise for consideration.

Even if the offeror has made a promise and has stated a consideration for his or her promise, the promise and consideration must be connected. The offeror must make his or her promise to induce the offeree to give what the offeror says he or she is seeking. Thus, the sequence of events is important.

- EXAMPLE When Henrietta returned John's lost dog, Toby, John promised to pay Henrietta \$50 for her efforts. Since Henrietta had already returned Toby to John when he made his promise to pay her, John's promise was not intended to induce her to act. Thus, there was no consideration for John's promise, and it was only a gift promise. If John refuses to pay Henrietta, she has no contract upon which to sue him.

The Acceptance. Once an offer has been made, attention focuses on acceptance. An **acceptance** is the offeree's manifestation of assent to the terms of the offer. The basic questions are: What constitutes acceptance and when does an attempt to accept become an effective acceptance? The components of acceptance parallel those of an offer. If the offer was for a bilateral contract (a promise for a promise), the following constitutes the acceptance:

- the offeree's promise
- the consideration for the offeree's promise (i.e., the offeror's promise)
- the fact that the offeree's promise was intended to secure the offeror's promise

- EXAMPLE

Offer: "I promise to pay you \$1,000 for your promise to paint my house."

Acceptance: "I promise to paint your house for your promise to pay \$1,000."

If the offer was for a unilateral contract (a promise for a performance), the acceptance is:

- the offeree's performance
- the consideration for the offeree's performance (i.e., the offeror's promise)
- the fact that the offeree's performance was intended to secure the offeror's promise

- EXAMPLE

Offer: "I promise to pay you \$1,000 for your painting my house."

Acceptance: Painting the house (i.e., painting the house for your promise to pay \$1,000).

The consideration for the offeree's promise or performance is the offeror's promise. If consideration for the offeree's promise or performance is lacking, the conclusion is "no acceptance" and not "acceptance but no consideration."

The fact that an attempt to accept an offer has taken place does not always lead to the conclusion that a contract has been formed. One of the following events may have occurred and rendered the attempted acceptance ineffective:

- the offer may have lapsed because it was not accepted within the time stated in the offer or, if no time was stated, within a reasonable time
- the offeror may have revoked the offer
- the offeree may have rejected the offer before attempting to accept it
- the offeror or offeree may have died or become incapacitated.

If none of these events has occurred, the attempted acceptance of the offer is effective, and a contract is formed.

Step Three: Contract Enforceability

Once a contract is formed, the next step is determining whether the contract is enforceable. The focus shifts from "freedom of contract" (i.e., the parties' power to create their own contract terms and structure their relationship as they choose) to the governmental regulation of contract. A number of policy considerations, resulting in legislative enactment or judicial decision, may preclude enforcement of the contract. These policy grounds may be grouped into three categories. The legislature or the judiciary may seek the following goals:

- to protect a selected class of people unable to protect themselves (e.g., minors and those who are mentally incapacitated)
- to protect a contracting party from the overreaching of the other contracting party (e.g., unconscionability, fraud, duress,) mistake in a basic

assumption of fact, and potential perjury due to a lack of writing [Statute of Frauds]

- to protect the integrity of the judicial process (e.g., illegality and inappropriate forum selection).

If unenforceable, the contract may be rescinded, or depending on the nature of the problem, the contract may be reformed, thereby eliminating the obstacle precluding its enforcement. **Rescission** is revocation (termination) of the contract. Unlike the revocation of an offer that has not been accepted and no contract formed, rescission is the revocation (termination) of an existing contract. **Reformation** is the revision of a writing to conform to the real agreement or intention of the parties.

Step Four: Breach of the Contract

When the conclusion at Step Three is that the contract is enforceable, the analysis focuses on the breach of the contract. Who is complaining and what is the complaint?

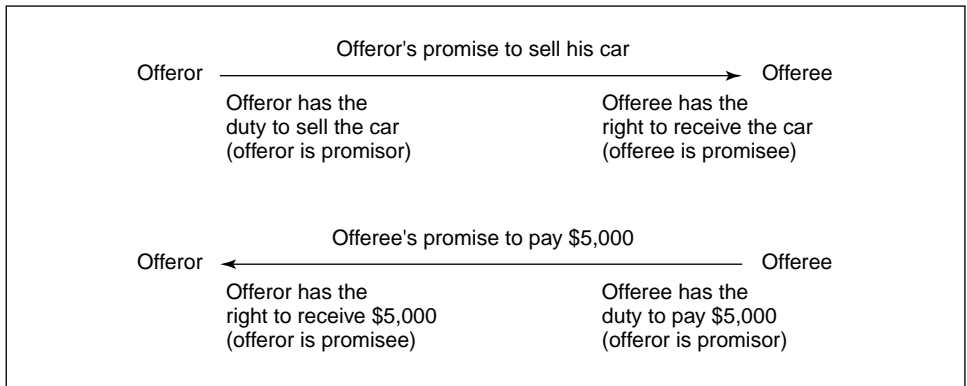
In a bilateral contract, the promises are reciprocal: the offeror promises the offeree and the offeree promises the offeror. The offeror, by promising the offeree, has a duty to the offeree to perform; the offeree, by being the recipient of the offeror's promise, has a right to receive the offeror's promised performance. The offeror, by having the duty, is the promisor. A **promisor** is the person who makes the promise. The offeree, by having the right, is the promisee. A **promisee** is the person to whom a promise is made. Therefore, when the offeror says "I promise to sell you my car," the offeror (promisor) has the duty to sell the car to the offeree, and the offeree (promisee) has the right to receive the car from the offeror.

The offeree, by promising the offeror, also has a duty to perform; the offeror, by being on the receiving end of the offeree's promise, has a right to receive the offeree's promised performance. The offeree, by having the duty, is the promisor; the offeror, by having the right, is the promisee. Therefore, when the offeree says "I promise to pay you \$5,000," the offeree (promisor) has the duty to pay the offeror \$5,000, and the offeror (promisee) has the right to receive \$5,000 from the offeree (see Figure I-2).

Because the offeror is both promisor and promisee and the offeree is both promisor and promisee in a bilateral contract, the label *promisee* refers to the party claiming the unperformed right, and the label *promisor* refers to the party who owes the duty associated with the right. Therefore, the complainant is the promisee.

If the promisee alleges that the promisor has breached a contractual duty (either by notifying the promisee that the promise will not be performed in the future or by actually not performing when the performance is due), the promisor has five responses to the promisee's allegation of breach.

FIGURE I-2 Reciprocal Promises with Offeror Being both Promisor and Promisee and Offeree Being both Promisor and Promisee



1. No breach, compliance—"I am complying with the terms of the contract."

- **EXAMPLE** A homeowner's insurance policy provides that Insurance Company will pay Insured for all losses due to fire. When Insured's valuable art collection is stolen, she files a claim, and Insurance Company rejects the claim on the ground that the loss was not due to fire. If Insured sues Insurance Company for breach of contract alleging that her claim was not paid, Insurance Company will respond, "No breach, compliance." Insurance Company is in compliance with the terms of the contract because it does not become obligated to pay until Insured has a loss by fire. Because no fire loss has occurred, the contract has not been breached, and Insured has no cause of action for breach of contract.

2. No breach, excuse—"Although I am not complying with the terms of the contract, my nonperformance was excused, and therefore I have not breached the contract."

This response combines the promisor's admission of nonperformance under the contract with the promisor's claim that this nonperformance was excused and therefore was not a breach. "It is true that I didn't do what the promisee said I didn't do, but I was excused from doing it."

- **EXAMPLE** Singer contracts to perform for a week for Hotel. After the first performance, Singer becomes seriously ill and cannot perform for the remainder of the engagement. If Hotel sues Singer for breach of contract alleging that Singer breached by not performing, Singer could respond, "No breach, excuse. Although I am not complying with the terms of the contract, I am excused from performing due to my serious illness." Unlike the first response ("No breach, compliance"), the condition (serious illness) was not an express term in the contract. Even though this condition (an act of God) was not an express term, it may excuse Singer's nonperformance. If Singer is excused, she is not in breach, and Hotel cannot maintain a cause of action for breach of contract.

3. No breach, justification—"Although I am not complying with the terms of the contract, my nonperformance was justified by your breach of this contract, and therefore I have not breached the contract."

This response to the plaintiff's allegation of breach joins the promisor's admission of nonperformance with the promisor's claim that his or her nonperformance was justified because the party alleging breach had breached the contract.

- **EXAMPLE** Builder contracts to build a house for Owner. Owner promises to pay every thirty days as the work progresses. Builder begins to build, but Owner does not pay. After two months, Builder stops work. If Owner sues Builder for breach of contract alleging that Builder breached by stopping work, Builder would respond, "No breach, justification. My stopping work was justified because you did not pay me." Builder's nonperformance is not a breach; it is a justified nonperformance. Because Owner rather than Builder is the breaching party, Owner's action for breach of contract against Builder cannot be maintained.

4. No breach, terminated duty—"Although I am not complying with the terms of the contract, my duty to perform the contract has been terminated, and therefore I have not breached the contract."

This response contains both the promisor's admission of nonperformance and a claim that the promisor's contractual duty has ended either by agreement or by law, and therefore the promisor has not breached the contract.

- **EXAMPLE** Employer and Employee have a contract whereby Employer is to pay Employee "a reasonable wage." After Employee works for a month, a dispute arises between the parties about the meaning of "a reasonable wage." Employer gives Employee a check that carries the notation "Payment in Full." Employee cashes the check and then demands still more money from Employer. The Employer refuses. If Employee sues Employer for breach of contract alleging that Employer breached by not paying him a reasonable wage, Employer would respond, "No breach, my duty has been terminated." Employer's duty to pay "a reasonable wage" is terminated by the subsequent contract in the form of Employer's check with the notation "Payment in Full" and by Employee's cashing the check. Because Employer is not a breaching party, Employee cannot maintain a breach of contract action.

The previous example demonstrates an accord and satisfaction. An **accord** is a contract to pay a stated amount to discharge an obligation which is uncertain either as to its existence or amount. The **satisfaction** is the performance of the accord contract. Employer's tendering the check is the offer for an accord contract ("I promise to pay you this amount for your promise to take this amount as full payment of my obligation to you"). Employee's cashing the check implies the Employee's "promise to take the check as full payment for Employer's promise to pay the stated amount" and therefore is the acceptance of the offer for the accord contract. Employee's cashing the check is also the "satisfaction" or the performance of the accord contract.

Another terminating event that is consensual is the substitute contract. A **substitute contract** is a contract between the original contracting parties that replaces the original contract. Under classical contract doctrine, the terminating event was really the mutual releases that preceded the substitute contract and not the substitute contract itself. The mutual releases terminated the parties' duties under the original contract. One party could now promise to do what he or she had already promised to do if the other would promise to do more.

- **EXAMPLE** Jones contracts to work for Salinas for one year at \$1,000 a week beginning on June 1. Prior to June 1, Jones and Salinas contract to release each other from their contractual obligations. They enter into a new contract whereby Jones contracts to work for Salinas for one year at \$1,200 a week beginning on June 1. If the parties have released each other from their original contractual duties, the \$1,200 a week contract is a substitute contract.

The terminating event may be unilateral such as a release. A **release** is the intentional relinquishment of a right.

- **EXAMPLE** Abner hires Rachel to work for him as an assistant manager for one year. After six months, Abner wrongfully fires Rachel. Rachel may release her right to recover under the contract, thus terminating Abner's duty.

The terminating event may occur by operation of law. A **Statute of Limitations** provides for a specified period of time within which a cause of action may be brought.

- **EXAMPLE** Martina entered into a written lease of a store front from Ricardo Realty Corporation. Prior to the time when Martina was to occupy the store front, Ricardo Realty told Martina that the property was no longer available. Three years and two days later, Martina brought a breach of contract action against Ricardo Realty. If the Statute of Limitations was three years, Ricardo Realty's duties under the contract terminated two days before Martina brought her breach of contract action.

5. Breach—"I admit I have breached the contract."

The fifth and final response to the plaintiff's allegation of defendant's breach is an admission by the defendant. Whether the defendant's breach is intentional or unintentional is irrelevant. The law of contracts does not evaluate the mental state accompanying nonperformance. The only question is whether the defendant has not performed his or her duty under the terms of the contract.

If the defendant is unable to maintain his or her response to the plaintiff's allegation of breach (the defendant is unable to prove "no breach, compliance," "no breach, excuse," "no breach, justification," or "no breach, terminated duty") or if the defendant admits breach, the plaintiff has established a cause of action for breach of contract. A **cause of action** is the theory upon which relief should be granted. The plaintiff can now proceed to step five of the analysis and pursue his or her remedies for the defendant's breach. A **remedy** is the relief sought if a cause of action can be maintained.

Step Five: Plaintiff's Remedies for the Defendant's Breach of Contract

The nonbreaching party may maintain an action for breach of contract and is entitled to a remedy if the conclusion at Step Four is that the contract has been breached. The remedies for breach of contract are designed to protect not only

the nonbreaching party's expectation interest but that party's reliance and restitution interests as well.

When parties enter into a contract, both have expectations regarding what the net economic gain will be once the contract has been fully performed. Protecting the nonbreaching party's **expectation interest** places him or her in as good a position as if both parties had fully performed the contract according to its terms. The nonbreaching party may receive damages. **Damages** are compensation awarded by a court to a party who has suffered loss or injury to rights or property. In the unusual case when money damages would be inadequate compensation and the subject of the contract is unique, the court may award specific performance. **Specific performance** is a remedy whereby a court directs the breaching party to deliver the subject of the contract to the nonbreaching party. In some cases, an appropriate remedy may be an injunction. An **injunction** is an order issued by a court directing the breaching party to refrain from doing specified acts.

When parties contract, each may perform relying on the other's promise to perform. Protecting the nonbreaching party's **reliance interest** places that party in the position that he or she was in before relying on the other's promise. The nonbreaching party is compensated, not on the basis of expectation, but for the injury suffered as a result of reliance on the other's promise. The measure of damages is the reasonable value to the nonbreaching party for the injury suffered by relying on the other's promise.

When parties contract, one party, while performing under the contract, may confer a benefit on the other party. Protecting the nonbreaching party's **restitution interest** will place that party in the position he or she was in before conferring the benefit on the other. The nonbreaching party is compensated, not on the basis of either expectation or reliance on the other's promise, but for the value of the benefit conferred. The measure of damages is the reasonable value of the benefit to the party receiving the benefit.

Third Party Interests

Although they are not involved as a step in the contracts analysis, three other groups of parties who were not parties to the original contract (third parties) may have or may acquire an interest in the contract. The first type of third party is the third party beneficiary to the contract. A **third party beneficiary** is a party who will be benefited by the performance of a contract and may be a creditor, donee, or incidental beneficiary. The creditor and donee beneficiaries are intended beneficiaries. Incidental beneficiaries, on the other hand, do not have a court-protected interest. The third party beneficiary acquires rights as a result of the contract but never acquires duties.

- **EXAMPLE** On Wednesday Jane borrowed \$100 from Caroline promising to repay her on Monday. On Friday Agnes borrowed \$100 from Jane promising to pay Caroline on Monday for Jane. Caroline is a creditor beneficiary of the Agnes/Jane contract.

- **EXAMPLE** Mary, wishing to leave her estate to her niece Sarah, contracts with an attorney for drafting her will. Sarah is the donee beneficiary of the attorney/client contract.
- **EXAMPLE** The City, in preparing for the Fourth of July, hires the Stars and Stripes Fireworks Company to supply the fireworks for the celebration. John Q. Public is only an incidental beneficiary of the City/Stars and Stripes contract.

The second type of third party consists of assignees and delegates. An **assignment** is the transfer of a contractual right to a third party who was not a party to the original contract. A **delegation** is the empowerment of a party who was not a party to the original contract to perform that party's contractual duty. Neither an assignee nor a delegatee was a party to the original contract. By an assignment, a third party (an assignee) acquires rights in the original contract. By a delegation, a third party (a delegatee) agrees to perform a duty of one of the original contracting parties.

- **EXAMPLE** Sally borrowed \$1,000 from Friendly Finance. Friendly transferred its right to receive Sally's repayment to Easy Credit Company. Friendly's transfer of its right to receive Sally's money is an assignment of that right.
- **EXAMPLE** The Six Flags Coal Company contracted to sell 300,000 carloads of coal to the Ever Ready Power Company. The contract provided that the coal was to be mined at Six Flags mine no. 6. Six Flags sold its mine no. 6 and its contract to deliver coal to Ever Ready to A-1 Coal Company. A-1 is the delegatee of the Six Flags/Ever Ready contract.

The third type of third party neither had a right under the original contract nor subsequently acquired a right or duty relating back to the original contract. This type of third party has committed a wrong by interfering with existing contract rights.

- **EXAMPLE** Rinaldo, a tenor, has a one-year contract to sing at the Gotham Opera Company. The Metropolis Opera Company offers Rinaldo more money and thus entices him to breach his contract with the Gotham Opera Company. The Metropolis Opera Company has committed a wrong by interfering with the Rinaldo/Gotham contract.

Contracts analysis is presented in chart form in Figure I-1.

REVIEW QUESTIONS

DEFINE THE FOLLOWING TERMS AND PHRASES

Acceptance

Accord

Allegation of breach

Assignment

Breach of contract

Cause of action

Choice of Law

Common law

Consideration

Consideration for the offeree's performance

Consideration for the offeree's promise

Consideration for the offeror's promise

Contract enforceability	Offeror
Contract formation	Promise
Damages	Promisee
Delegation	Promisor
Expectation interest	Reformation
Injunction	Release
Interstate transaction	Reliance interest
Multistate transaction	Remedy
No breach, compliance	Rescission
No breach, excuse	Restitution interest
No breach, justification	Satisfaction
No breach, terminated duty	Specific performance
Offer	Statute of Limitations
Offer for a bilateral contract	Substitute Contract
Offer for a unilateral contract	Third party beneficiary
Offeree	Uniform Commercial Code

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

1. T F The first step in the contract analysis is to determine the applicable law.
2. T F The second step in the contract analysis is to determine whether a contract has been formed.
3. T F The third step in the contract analysis is to determine the enforceability of the contract.
4. T F The fourth step in the contract analysis is to determine whether the contract has been breached.
5. T F The fifth step in the contract analysis is to determine the plaintiff's remedies for the defendant's breach of contract.
6. T F The following is an offer for a unilateral contract: "I promise to sell you my watch for your promise to pay \$500."
7. T F The following is an offer for a bilateral contract: "I promise to sell you my watch for your paying \$500."
8. T F A bilateral contract has not just one consideration but has consideration for both the offeror's promise and the offeree's promise.
9. T F Both the offeror and the offeree may breach a unilateral contract.
10. T F In a bilateral contract, the offeror is both a promisor and promisee and the offeree is both a promisor and promisee.
11. T F In a unilateral contract, the offeror is both a promisor and promisee and the offeree is both a promisor and promisee.
12. T F In a bilateral contract, the breaching party may be either the offeror or offeree.

13. T F In a unilateral contract, the breaching party may be only the offeror.
14. T F A “no breach, compliance” response is distinguished from the “no breach, excuse,” “no breach, justification,” and “no breach, terminated duty” responses in that the “no breach, compliance” response denies noncompliance with the terms of the contract while the other three responses admit noncompliance.
15. T F If a defendant in a breach of contract action responds to the plaintiff’s allegation of breach by stating “no breach, justification,” the defendant is saying my breach was justified by your breach.
16. T F Whether a defendant’s breach in a breach of contract action is intentional or unintentional is irrelevant.
17. T F If the plaintiff succeeds in maintaining a breach of contract cause of action against a defendant, the plaintiff may select among the expectation, reliance, and restitution remedies available in a breach of contract action.
18. T F Specific performance is always available as a remedy in a breach of contract action.

FILL-IN-THE-BLANK QUESTIONS

1. _____. Determining the set of rules under which the alleged cause of action will be resolved.
2. _____. A manifestation of willingness to enter into a bargain, which justifies another person in understanding that his or her assent to that bargain is invited and will conclude the bargain.
3. _____. The party making the offer.
4. _____. The party receiving the offer.
5. _____. The shorthand phrase for an offer for a bilateral contract.
6. _____. The shorthand phrase for an offer for a unilateral contract.
7. _____. The shorthand phrase for the defendant’s response: “I am complying with the terms of the contract.”
8. _____. The shorthand phrase for the defendant’s response: “Although I am not complying with the terms of the contract, my nonperformance was excused, and therefore I have not breached the contract.”
9. _____. The shorthand phrase for the defendant’s response: “Although I am not complying with the terms of the contract, my nonperformance was justified by your breach of this contract, and therefore I have not breached the contract.”

10. _____. The shorthand phrase for the defendant's response: "Although I am not complying with the terms of the contract, my duty to perform the contract has been terminated, and therefore I have not breached the contract."
11. _____. The shorthand phrase for the defendant's response: "I admit I have breached the contract."
12. Protecting the nonbreaching party's "_____" places that party in as good a position as if both parties had fully performed the contract according to its terms.
13. Protecting the nonbreaching party's "_____" places that party in the position that he or she was in before relying on the other's promise.
14. Protecting the nonbreaching party's "_____" places that party in the position he or she was in before conferring the benefit on the other.

MULTIPLE CHOICE QUESTIONS (CIRCLE ALL THE CORRECT ANSWERS)

1. Emma Smythe, a California sculptor, was hired by the City Council of New York City to create a sculpture for Central Park. The offer was sent by mail to Smythe in California. She accepted by mail. The preliminary work on the sculpture was to be done in California, the casting in Oregon, and the final assembly in New York. After Smythe completed the design, the City Council canceled the contract due to lack of funds.
Identify the choice of law problem(s):
 - (a) Whether the law of California, Oregon, or New York governs this transaction.
 - (b) Whether Article 2 of the UCC or the state's common law governs this transaction.
 - (c) Whether federal or state law governs this transaction.
 - (d) This transaction does not involve a choice of law problem.
2. A Florida Buyer purchased a video camera from a Vermont Seller through a shopping channel on cable TV. The Buyer did not leave his home in Florida but telephoned his order to a telephone number in Georgia. When the Buyer received shipment of the camera, it was packaged along with a written warranty. The writing, however, disclaimed all implied warranties. The camera proved to be defective. The defect was not within the written warranty but was within an implied warranty of merchantability, had it not been disclaimed.
Identify the choice of law problem(s):
 - (a) Whether the law of Florida, Georgia, or Vermont governs this transaction.
 - (b) Whether Article 2 of the UCC or the state's common law governs this transaction.
 - (c) Whether federal or state law governs this transaction.
 - (d) This transaction does not involve a choice of law problem.

3. What constitutes acceptance of an offer for a unilateral contract?
 - (a) the offeree's promise
 - (b) the offeree's promise to perform
 - (c) the offeree's preparing to perform
 - (d) the offeree's partial performance
 - (e) the offeree's full performance

4. Bart Cartright purchased an automobile insurance policy from Guarantee Insurance Company. The policy covered damage to the vehicle due to collision but excluded damage due to natural disasters such as hail and flood. Cartright's automobile was heavily damaged by volcanic ash when Mt. St. Helens erupted. Cartright filed a claim with Guarantee, and Guarantee refused to pay.

If Cartright sued Guarantee for breach of contract alleging that Guarantee breached the contract by not paying his claim, Guarantee would respond:

 - (a) no breach, compliance
 - (b) no breach, excuse
 - (c) no breach, justification
 - (d) no breach, terminated duty
 - (e) breach

5. Ronald Redcloud entered into a contract with Universal Publishers for his memoirs. Redcloud died when he had completed about half of the project. If Universal sued Redcloud's estate for breach of contract alleging that Redcloud had failed to deliver a completed manuscript, the estate would respond:
 - (a) no breach, compliance
 - (b) no breach, excuse
 - (c) no breach, justification
 - (d) no breach, terminated duty
 - (e) breach

6. Gotham University contracted with Educational Excellence, a consulting corporation, for a thorough study of the University. The contract provided that Educational would be paid a consulting fee and expenses. The contract provided that the consulting fee would be paid in four quarterly payments and the expenses would be paid monthly. After working on the project for four months (project expected to last about a year), Educational refused to continue because it had been paid neither the first quarterly payment nor its expenses for the past three months.

If Gotham sued Educational for breach of contract alleging that Educational breached by notifying Gotham that it would not complete the work, Gotham would respond:

 - (a) no breach, compliance
 - (b) no breach, excuse
 - (c) no breach, justification
 - (d) no breach, terminated duty
 - (e) breach

7. Mary Lou Webster was hired by Gotham University as an assistant professor. Dr. Webster was given a three-year contract that would be automatically renewed for another three years unless Dr. Webster desired not to have the contract renewed or the University had cause not to renew. The contract defined cause for nonrenewal. Dr. Webster's contract was not renewed after the initial three-year term expired. The nonrenewal was not based on cause as was required by her contract.

Four years after her nonrenewal, Dr. Webster brought a breach of contract action against Gotham University alleging that Gotham breached the contract by not offering her a new three-year contract and that its refusal was not based on cause. Gotham responded with the Statute of Limitations. Gotham's response is:

- (a) no breach, compliance
- (b) no breach, excuse
- (c) no breach, justification
- (d) no breach, terminated duty
- (e) breach

SHORT ANSWER QUESTIONS

1. List the five steps in the Road Map for the law of contracts.
2. List three different settings in which a choice of law question may arise.
3. List the elements that constitute an offer for a bilateral contract.
4. Distinguish an offer for a bilateral contract from an offer for a unilateral contract.
5. Why does this text consider that a contract consists of two elements, an offer and an acceptance, rather than three elements, an offer, an acceptance, and consideration?
6. List the elements that constitute an acceptance for a bilateral contract.
7. List four events that could occur between the offer and the attempted acceptance that would render the attempted acceptance ineffective.
8. The legislature or the judiciary may seek to protect what three categories of policy grounds by precluding the enforcement of a contract?
9. After the plaintiff alleges that the defendant has breached the contract, the defendant's reply may be divided into what five responses?

PART

I

**Step One: Determining the
Applicable Law (Choice of Law)**

INTRODUCTION

Three Choice of Law Issues

CHAPTER 1

Determining the Rules Governing the Dispute

INTRODUCTION

Three Choice of Law Issues

The threshold step in a contracts problem involves “choice of law.” **Choice of law** is the selection of the legal rules under which the dispute will be resolved. Choice of law questions arise in a number of settings. Part One of this book (Chapter 1) introduces three settings: (1) determining the applicable rules when federal and state laws conflict; (2) determining the applicable rules in a multistate transaction where the dispute would be resolved differently under the rules of the different interested states; and (3) determining the applicable rules from among the different conflicting rules within a state.

The subject of choice of law is a complex one that goes beyond the needs of paralegal students in an introductory course in contracts law. Our goal in Part One of *Introduction to the Law of Contracts* is simply to educate students to recognize this issue when it arises. We have, therefore, chosen to provide the limited coverage of choice of law that we deem essential to meet this goal.



Determining the Rules Governing The Dispute

- ◆ Determining the Rules When Federal and State Laws Conflict
- ◆ Determining the Rules When More Than One State Has an Interest in the Transaction

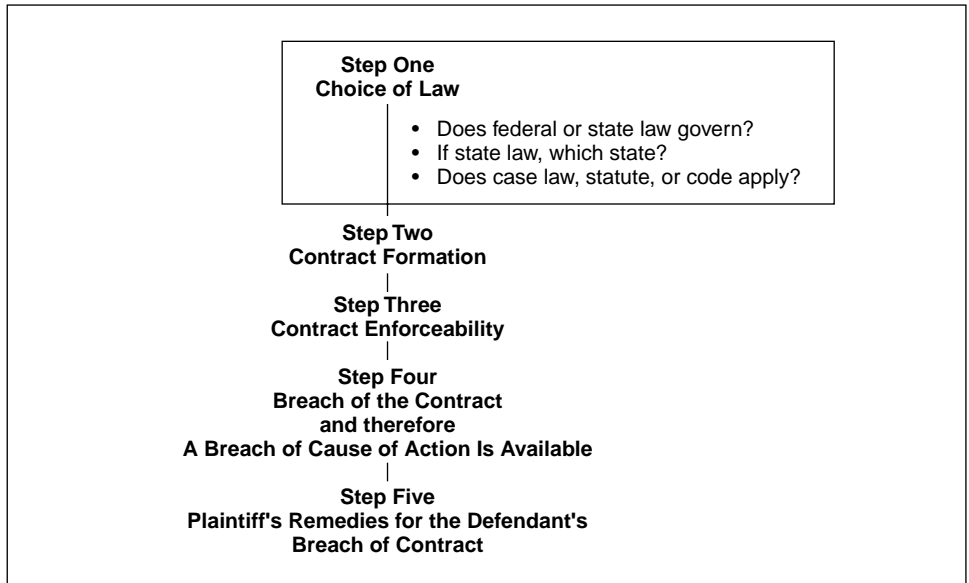
Selection of the Law by the Parties

The Law Governing in the Absence of an Effective Choice by the Parties

- ◆ Determining the Rules When a State Has Several Sets of Rules

Determining the rules that govern a dispute involves choice of law questions. Although the law of contracts is generally state law, Congress has passed legislation regulating certain types of transactions. When state law and federal law differ, the outcome of a dispute may again vary according to which law applies to the transaction.

Transactions frequently span several states. All fifty states and the District of Columbia formulate their own law of contracts. Consequently, there are fifty-one separate bodies of contracts law, one for each state and the District of Columbia. Fortunately, many of the rules are the same from jurisdiction to jurisdiction. Nevertheless, differences do exist. When the laws of these states differ,

FIGURE 1–1 The Choice of Law Phase of the Road Map

the outcome of a dispute may vary according to which state's law applies to the transaction.

Within each jurisdiction, the law of contracts has been created by the legislature (statutes and codes), the courts (case law), and by administrative agencies (regulations). Some laws apply to one type of transaction and other laws apply to another type of transaction.

The issues that arise when federal law and state law conflict, the issues that can occur when more than one state has an interest in the transaction, and the issues that arise when a state has statutory rules and case law that conflict will be discussed in this chapter (see Figure 1–1).

DETERMINING THE RULES WHEN FEDERAL AND STATE LAWS CONFLICT

In some instances, **federal preemption** causes state law, whether case law or statute, to be inoperative. Under the federal preemption doctrine, state law must give way to federal law when federal law either expressly regulates the matter or when a particular subject is regarded as being beyond the bounds of state action.

The area of warranties illustrates the federal preemption doctrine.

EXAMPLE 1–1

All states with the exception of Louisiana have enacted Article 2 of the Uniform Commercial Code (UCC). Article 2 of the UCC applies to transactions involving a sale of goods. Article 2 of the UCC permits a seller, who makes an express warranty, to disclaim an implied warranty. The United States Congress has enacted the Magnuson-Moss Warranty Act to regulate the sale of consumer goods distributed in commerce. Magnuson-Moss does not permit a seller who makes an express warranty to disclaim an implied warranty. Therefore, if a buyer purchases a product that is consumer goods, and if the seller makes an express warranty but attempts to disclaim an implied warranty under state statute, the attempted disclaimer is not effective because the federal statute will preempt the state statute. The buyer therefore purchases the consumer goods with an implied warranty.

DETERMINING THE RULES WHEN MORE THAN ONE STATE HAS AN INTEREST IN THE TRANSACTION

Which state's law applies when the laws of different states conflict? The answer may be provided by the contracting parties. When the contract was formed, the parties may have chosen the state whose laws would apply to the transaction. If the parties did not select the state or made an ineffective selection, then the answer is found in the choice of law rules of the **forum state** (the state where the lawsuit is filed). Unfortunately, several choice of law rules exist, producing different results.

Selection of the Law by the Parties

Contracting parties can choose the law of a particular state to govern their contractual rights and duties and include their choice as a provision in the contract.

EXAMPLE 1–2

A choice of law provision could take the following form: "This Agreement shall be governed and interpreted in accordance with the laws of the State of Indiana."

Because parties contract to create predictability in their relationship, courts will give effect to the parties' own choice of applicable law. The deference to the parties' own choice of applicable law is known as the "**party autonomy**" rule. The autonomy rule, however, is not a rule without limitations. If the contracting parties select a state and incorporate it as a provision in their contract, then

the court in the forum state will enforce this choice of law provision unless: (1) the chosen state has no substantial relationship to the parties or the transaction; or (2) the result obtained from the applicability of the law of the chosen state would be contrary to the forum state's public policy.

PARALEGAL EXERCISE 1.1 In *S. Leo Harmonay, Inc. v. Binks Manufacturing Co.*, General Motors hired Binks, a Delaware corporation with its principal place of business in Illinois, as general contractor to expand its assembly plant in Tarrytown, New York. Binks subcontracted the mechanical piping work to Harmonay, a New York Corporation, at a cost of approximately \$2 million.

A dispute arose regarding damages for delays, and Harmonay filed a breach of contract action against Binks in the United States District Court for the Southern District of New York.

The subcontract, a standard printed form, provided that the “contract resulting from the acceptance of this order is to be construed according to the law of the state from which this order issues, which is printed on the opposite side hereof.” Binks’s corporate headquarters’ address in Franklin Park, Illinois, was clearly printed on the form, signifying Illinois as the state. Binks argued that Illinois law should govern the dispute.

Harmonay countered that the choice of law provision in the subcontract was unenforceable because Illinois lacked a substantial relationship to the transaction and therefore New York law, rather than Illinois law, should govern. Under the law of Illinois, a “no damages for delay” clause would be incorporated into the subcontract, and Binks could successfully defend the lawsuit. Under New York law, a “no damages for delay” clause would not be incorporated into the subcontract, and Harmonay could recover.

Review the following excerpt from *S. Leo Harmonay, Inc. v. Binks Manufacturing Co.*, and determine whether the court applied Illinois or New York law and why.

CASE

S. Leo Harmonay, Inc. v. Binks Manufacturing Co.

United States District Court, Southern District of New York, 1984.
597 F.Supp. 1014, 1024–25.

I. CHOICE OF LAW

Jurisdiction in this case rests on diversity of citizenship, 28 U.S.C. § 1332, and therefore the Court must apply the substantive law of the forum state, including the conflict of law rules. See *Klaxon v. Stentor Elec. Mfg. Co.*, 313 U.S. 487, 61 S.Ct. 1020, 85 L.Ed. 1477 (1941). Thus, New York law applies to the conflicts question raised herein. See *La Beach v. Beatrice Foods Co.*, 461 F.Supp. 152 (S.D.N.Y.1978); *Business Incentives Co., Inc. v. Sony Corp. of America*, 397 F.Supp. 63 (S.D.N.Y.1975).

While it is true that some jurisdictions give determinative effect to a choice-of-law clause and thereby follow the so-called “autonomy rule,” see Note, *Effectiveness of Choice-of-Law*



Clauses in Contract Conflicts of Law: Party Autonomy or Objective Determination?, 82 Colum.L.Rev. 1659, 1660 (1982), New York is not one of them. See *La Beach, supra*; *Southern Intern. Sales Co. v. Potter & Brumfield*, 410 F.Supp. 1339 (S.D.N.Y.1976); *Business Incentives Co., supra*; *Fricke v. Isbrandtsen Co.*, 151 F.Supp. 465 (S.D.N.Y.1957).

A better rule, suggested by Judge Learned Hand, is that such clauses are prima facie valid and will be upheld absent a showing that they result from fraud or overreaching, that they are unreasonable or unfair, or that enforcement would contravene a strong public policy of the forum. See *Krenger v. Pennsylvania R. Co.*, 174 F.2d 556, 560–61 (2d Cir.) (L. Hand, Ch. J., concurring), cert. denied, 338 U.S. 866, 70 S.Ct. 140, 94 L.Ed. 531 (1949); *Bense v. Interstate Battery System of America, Inc.*, 683 F.2d 718, 721–22 (2d Cir.1982); *Richardson Greenshields Securities, Inc. v. Metz*, 566 F.Supp. 131, 133 (S.D.N.Y.1983).

The “substantial relationship” approach followed in New York, which parallels Judge Hand’s rule, is stated succinctly in Restatement (Second) of Conflicts of Law § 187. See *Nakhleh v. Chemical Construction Corp.*, 359 F.Supp. 357 (S.D.N.Y.1973). In relevant part, that section states:

“(2) The law of the state chosen by the parties to govern their contractual rights and duties will be applied, even if the particular issue is one which the parties could not have resolved by an explicit provision in their agreement directed to that issue (i.e., questions of validity, formalities and capacity) unless either

(a) the chosen state has no substantial relationship to the parties . . . or

(b) application of the law of the chosen state would be contrary to a fundamental policy of a state which has a materially greater interest than the chosen state . . .”

Thus, although New York does recognize the choice-of-law principle that parties to a contract have a right to choose the law to be applied to their contract, see *Compania de Inversiones Internacionales v. Industrial Mortgage Bank of Finland*, 269 N.Y. 22, 198 N.E. 617 (1935), this freedom of choice on the part of the parties is not absolute. See *Nakhleh, supra*.

With respect to the substantial relationship test, the New York Court of Appeals has held that while the parties’ choice of law is to be given considerable weight, the law of the jurisdiction with the “most significant contacts” is to be applied. *Haag v. Barnes*, 9 N.Y.2d 554, 559–60, 175 N.E.2d 441, 216 N.Y.S.2d 65 (1961); see *La Beach, supra*, at 155–56; *Southern Intern., supra*, at 1341.

Under this analysis, the parties’ “choice” of Illinois law in the Binks standard printed form diminishes when viewed against the facts of the case. The only Illinois contact is that it is the principal place of defendant’s business. The contract itself was executed in Michigan. On the other hand and most impressive are these factors: the place of performance of the work was in New York, all negotiations for the extra work and other claims occurred in New York, the prime contract is governed by the law of New York, and plaintiff, a New York corporation, has its principal place of business in New York. Illinois has no substantial relationship to the parties and New York would seem to have a materially greater interest in the application of its law. In light of the foregoing, the rights and duties of the parties to the contract are to be governed by the law of New York, despite the “agreement” of the parties to the contrary.

PARALEGAL EXERCISE 1.2 *Ryder Truck Lines, Inc. v. Goren Equipment Co.* involved a contract for the sale of seventy-five used diesel engines. Ryder, a Florida corporation with its headquarters in Florida, sold the engines to Goren, a Georgia corporation with its principal place of business in Georgia. Goren buys used truck engines and engine parts from companies like Ryder for resale to other trucking industry companies in the United States and internationally.

Upon receiving the seventy-five engines, Goren became dissatisfied and fell behind in its payments. Ryder sued Goren in the United States District Court for the Northern District of Georgia alleging a breach of contract. Goren responded with allegations of duress, fraud, and the unenforceability of the liquidated damages provision. The contract stated that Florida law would apply to any dispute between the parties.

Review the following excerpt from *Ryder Truck Lines, Inc. v. Goren Equipment Co.*, and determine whether the court applied Georgia or Florida law and why.



CASE

Ryder Truck Lines, Inc. v. Goren Equipment Co.

United States District Court, N.D. Georgia, 1983.
576 F. Supp. 1348, 1354.

A. CHOICE OF LAW

In resolving the various claims presented in this diversity action, the federal court must follow the Georgia conflict of laws rules. *Klaxon Co. v. Stentor Electric Manufacturing Co.*, 313 U.S. 487, 61 S.Ct. 1020, 85 L.Ed. 1477 (1941). Georgia's conflicts rule states that the law of the state where the contract is made and performed will govern the validity and interpretation of the contract, unless the parties have chosen the law of a particular state to govern their contractual rights and responsibilities. In that event, the choice of law provision in the contract will be applied, except where the chosen state has no substantial relationship to the parties or the transaction, or the result obtained from the applicability of the law of the chosen state would be contrary to Georgia's public policy. See, *5 Encyclopedia of Georgia Law, Conflict of Laws*, §§ 27, 11; *Restatement (Second) of Conflict of Laws*, § 187 (1971). Cf. *Nasco v. Gimbert*, 239 Ga. 675, 238 S.E.2d 368 (1977).

In the case at bar, paragraph 9 of the January contract provides that the agreement shall be governed by the laws of Florida. The issues of fraud and duress, however, relate to the validity of the contract as a result of alleged pre-contract misrepresentations, and are matters outside the contract. Furthermore, contracts procured by fraud and/or duress are contrary to the fundamental policy of the state of Georgia, as is a damages provision in a contract which purports to be liquidated damages, but instead is a penalty to deter a person from

breaching the contract. As these issues involve matters of public policy in Georgia, the court will apply Georgia law in resolving the issues of fraud, duress, and the enforceability of the liquidated damages provision, notwithstanding the parties' choice of Florida law provision in the Contract. On the other hand, the court does not find the questions of interest and attorney's fees to be matters of important public policy where such items are provided for in the contract. These issues are governed by the agreement, and therefore Florida law will be applied in deciding these issues.

The Law Governing in the Absence of an Effective Choice by the Parties

The following is a general discussion of several conflict of law rules used in the field of contracts when the parties have not included a choice of law provision in their contract. The choice of law rule specified by the forum state determines which state's law will govern.

EXAMPLE 1-3

A Texas Buyer, in preparation for a Fourth of July program, contracted to purchase one thousand cases of fireworks from an Oklahoma Manufacturer-Seller. Seller shipped the cases to Buyer in Texas. As Buyer was unloading and storing the fireworks, they exploded, severely injuring Buyer. Four years and two months after the explosion, Buyer filed a breach of contract action in a Texas court seeking damages for breach of an implied warranty of merchantability under Oklahoma's version of Article 2 of the Uniform Commercial Code. The contract did not include a choice of law provision.

Seller contended that the Texas court should apply Texas rather than Oklahoma law. Under the Texas version of the UCC (§ 2-725), "An action for breach of any contract for sale must be commenced within **four** years after the cause of action has accrued." (Emphasis added.) "A cause of action accrues when the breach occurs, regardless of the aggrieved party's lack of knowledge of the breach. A breach of warranty occurs when tender of delivery is made. . . ." Under the Oklahoma version of the UCC, the Statute of Limitations has been extended to **five** years. Therefore, if Oklahoma law applies, the suit is timely. If Texas law applies, the suit is barred by the Statute of Limitations.

Because the lawsuit was filed in a Texas court, Texas is the forum state. The Texas court will use the Texas choice of law rules to resolve whether the Texas court should use Texas or Oklahoma law.

Which choice of law rule applies is often a complex question. Jurisdictions do not share a uniform solution. One choice of law rule applies the law of the place of the making of the contract. Generally, the place of the making of the contract is the place where the last act necessary to form the contract occurs. The place of the last act may be the place of acceptance, the place of delivery of a document, or the regular place of business of the party who accepts the offer.

Another choice of law rule applies the law of the place of performance of the contract. This would be the place where the contract specifies that the performance is to occur.

A third choice of law rule is proposed by the Restatement (Second) of Conflicts. The **Restatements of the Law**, drafted by the American Law Institute (an organization composed of judges, practitioners, and academicians) are an attempt to codify the common law of the various states into black letter law with commentary and examples. At times, the Restatements exceed codification and propose what the law ought to be. The Restatements cover a number of areas including the Restatement of Conflicts, the Restatement (First) of Contracts, the Restatement (Second) of Contracts, and the Restatement of Restitution. The Restatement's rule applies the law of the state with the most significant contacts or relationship with the transaction. This rule is called the "center of gravity," "grouping of contacts," or "most significant relationship theory." This Restatement rule gives effect to the stated intent of the parties. If the contract fails to express the intent of the parties, the Restatement looks at the following list of contacts:

- Place of contracting
- Place of negotiation of the contract
- Place of performance
- Location of the subject matter of the contract
- Domicile, residence, nationality, place of incorporation, and place of business of the parties.

If the place of the making of the contract and the place of negotiating are the same, courts will tend to use the law of that place.

The following example illustrates the application of these basic conflict of law rules.

EXAMPLE 1-4

Gary, a resident of State A, purchased a BMW. Gary, while in State A, mailed an offer to Barbara in State B to sell her his BMW. Gary's offer stated that the car would be delivered to Barbara in State C. On the following Tuesday, Gary, having second thoughts about his offer to Barbara, mailed a letter to her revoking his offer. On Wednesday, Barbara received Gary's offer and not knowing that Gary had sent a letter of revocation, mailed a letter to Gary accepting his offer. On Thursday, Barbara received Gary's letter of revocation. On Friday, Gary received Barbara's letter of acceptance. When Barbara telephoned Gary demanding the car, Gary refused.

Under the laws of States A, B, and C, acceptance of an offer sent by mail is effective when the letter of acceptance is sent. Therefore, Barbara's letter of acceptance would be effective on Wednesday, the date it was mailed.

State B and State A, however, have different rules governing revocation of the offer. Under State B's law, revocation is effective when sent. Therefore, Gary's letter of revocation would be effective on Tuesday, the day it was sent. Gary's offer no longer existed for Barbara

to accept, and a contract was not formed because under State B’s law, the revocation was effective before the attempted acceptance was effective. Because a contract was never formed in the first place, Gary’s failure to deliver the BMW could not constitute a breach under State B’s law.

Under State A’s law, revocation is effective when received. Because the attempted revocation was effective on Thursday and the acceptance was effective on the previous Wednesday, Gary’s offer was accepted, and his attempted revocation arrived too late to be effective. Gary’s failure to deliver the BMW constituted a breach of contract.

Does the law of State B or State A apply? Could the law of State C, whatever it is, apply because the car was to be delivered in State C?



Under the law of the place of the making of the contract, the law of State B would probably apply because Barbara mailed her acceptance in State B.

Under the place of performance rule, the law of State C will probably govern because delivery was to be made there.

Under the Restatement’s most significant relationship theory, the place of contracting is State B, where Barbara accepted. The place of negotiating could be both State B and State A, especially if negotiations were made by mail. The place of performance would be State C where delivery was to be made; and the domiciles and residences of the parties are State B and State A. Under the Restatement rule, it is difficult to predict which law will be applied since it depends on how the forum jurisdiction will view the contacts.

PARALEGAL EXERCISE 1.3 Your supervising attorney is drafting a contract between the firm’s client, a manufacturer of computer equipment, and its foreign supplier of computer components. She has asked you whether the contract should include a choice of law provision. She has also asked you to draft a choice of law provision for the contract. She has given you the following sample choice of law provisions to assist you in drafting.

Florida law shall govern this agreement.

This agreement shall be governed by and construed in accordance with the law of the State of Arkansas.

The laws of the State of California govern and control this document, and all actions in conjunction with the enforcement of this document.

The construction and performance of this agreement shall be governed by the laws of the State of Pennsylvania, United States of America. If any provision of this agreement is held to be invalid or unenforceable, this agreement shall be considered divisible as to all such provisions and the balance of this agreement shall continue in full force and effect as though such invalid or unenforceable provisions were not included in this agreement.

DETERMINING THE RULES WHEN A STATE HAS SEVERAL SETS OF RULES

The previous section explored the various choice of law rules used in determining the rules for resolving a dispute when more than one state has an interest in the transaction. Once the appropriate state has been determined, attention focuses on the laws within that state. The law of contracts within a state comes from two primary sources: the legislature and agencies (statutes, codes, and regulations) and the courts (case law).

When the legislature enacts a statute addressing a specific issue, the law has been codified. Courts are not free to ignore the legislative mandate and create their own law.

EXAMPLE 1–5

A general rule under case law (court-made law) is that a person who enters into a contract while a minor may disaffirm the contract while still a minor or within a reasonable time after reaching majority. Suppose that Mary Smith purchases a VCR when she is seventeen years old. Six months after turning eighteen, Mary decides that she no longer wants the VCR and wants her money back. She therefore seeks to disaffirm the contract. Under the court-made law, Mary has a reasonable time after reaching majority (age eighteen) to disaffirm. If the merchant resists Mary's attempt to disaffirm, the court will be asked to determine whether six months after reaching eighteen was a reasonable time within which to disaffirm under the facts of this case. If, however, the legislature has enacted a statute that states that one year after reaching majority is a reasonable time to disaffirm, the statutory rule applies, rather than the case law. The courts cannot ignore a statute. The courts, however, have the duty to interpret the statute in light of the facts of the case before them.

When dealing with a code, such as the UCC, the paralegal's approach should differ from the approach involving an isolated statute and case law. First, the paralegal should review the relevant documents made by the parties.

Next, the paralegal should consult relevant code law, not case law. The code is the primary, principal, and often preemptive source of law. Do not disregard the code. The code is an integrated document with interrelated sections. It includes definitions as well as rules.

Article 2 of the UCC, dealing with the sale of goods, provides 104 interrelated sections on the law of contracts pertaining to the sale of goods. Therefore, as a threshold question, one must determine whether the transaction is controlled by Article 2 of the UCC or by the case law of the jurisdiction. If the UCC applies, the rules in the case law are irrelevant, unless the case law interprets the UCC or the UCC is silent on the issue. UCC section 1–103 provides:

Unless displaced by the particular provisions of this Act, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions.

The name “Uniform Commercial Code” is a misnomer. The code is not limited to commercial transactions. For example, the Uniform Commercial Code controls the contract between two neighbors for the sale of a used lawn mower as well as the contract between two large corporations for the sale of steel beams.

Article 2 of the UCC is limited, however, to “transactions in goods.” The term “transactions,” although not defined in the code, has generally been limited to sales. Therefore, Article 2, as its short title indicates, is the law of sale of goods. Because Article 2 is generally limited to sales, it does not govern transactions that are pure leases. Article 2A covers leases of goods.

Article 2 applies to transactions in “goods,” a term that is defined to mean all things that 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, and things in action. Whether a particular sales transaction is governed by Article 2 instead of other statutory or case law rules may, therefore, depend on whether the subject of the sale was within the UCC’s definition of “goods.”

PARALEGAL EXERCISE 1.4 Which of the following transactions are controlled by Article 2 of the UCC?

1. An employment contract
2. A contract to sell natural gas (after it has been extracted from a well)
3. A contract to sell electricity
4. A contract to sell advertising time on the radio
5. A contract to sell an airplane ticket
6. A contract to sell a cow with her calf
7. A contract to sell the Empire State Building
8. A contract to sell an automobile
9. A contract to sell timber standing in a forest
10. A contract to sell a business

Because Article 2 governs transactions for the sale of goods but not for the sale of services, a difficult question is posed when the sale is a mixed or hybrid transaction. **Hybrid transactions** are contracts for both goods and services. Examples include the sale and installation of an air conditioning system; the repair of an automobile; the construction of a bridge; the charge for a blood transfusion; and the charge for a beauty treatment. When faced with a hybrid transaction, courts most frequently use the rule that Article 2 is applicable if the sales aspect predominates and is inapplicable if the service aspect predominates. This is known as the **predominant factor test**.



PARALEGAL CHECKLIST

Determining the Rules Governing the Dispute

- ALTHOUGH questions of choice of law (selecting the rules governing the dispute) are complex and well beyond an introductory course in contracts law, paralegals should be able to identify when a choice of law problem exists. If a choice of law question goes undetected, the wrong set of rules may be applied to a given set of facts, resulting in an inaccurate solution and loss of valuable time. Choice of law is the threshold question, and its existence can be discovered using the following analysis.
 1. Does federal law apply to any issue in the dispute? If both federal law and state law address the same issue, federal law will preempt state law.
 2. Does the transaction relate to multiple states (whether by the parties, offer and acceptance, or the performance of the contract)? If more than one state is involved, a choice of law question may exist.
 - a. Did the parties contract as to which state's law would govern their dispute? Under the "party autonomy" rule, a court in the forum state (the state where the legal action is brought) will enforce the parties' choice unless:
 - the chosen state has no substantial relationship to the parties or to the transaction or
 - the parties' choice would result in a decision contrary to the forum state's public policy.
 - b. If the parties have not included a choice of law provision in their contract, the forum state's choice of law rule determines which state's law will govern. Because states do not share the same choice of law rules, the answer may vary depending on where the action was filed (i.e., which state was the forum state). The following list illustrates the variation in choice of law rules:
 - the law of the place of making the contract
 - the law of the place of performance of the contract
 - the law of the state with the most significant contacts with the transaction.
 3. Is there more than one rule within the state that could apply to this dispute? When case law and statutes conflict, statutes control. For example, Article 2 of the state's version of the Uniform Commercial Code will prevail over case law.

REVIEW QUESTIONS

DEFINE THE FOLLOWING NEW TERMS AND PHRASES

Choice of law
Federal preemption doctrine
Forum state
Hybrid transactions
Party autonomy rule
Predominant factor test
Restatements of the Law

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

1. T F The court in the forum state may apply the law of one state to one issue and the law of another state to another issue.
2. T F The law of contracts is generally a creation of federal law.
3. T F Contracting parties can choose the law of a particular state to govern their contractual rights and duties.
4. T F Choice of law rules do not vary from state to state.
5. T F Hybrid transactions are contracts for labor (services) only.
6. T F Under the federal preemption doctrine state law must always give way to federal law when federal law either expressly regulates the matter or when a particular subject is regarded as being beyond the bounds of state action.
7. T F When the legislature of a state has enacted a statute addressing a specific issue, courts may not ignore this statute or create their own law.
8. T F When a section of Article 2 of the UCC and those sections of Magnusen-Moss that deal with warranties conflict, the state's UCC provisions will apply.
9. T F A choice of law question may exist if the offer was made in one state, accepted in another state, and the contract performed in a third state.
10. T F The state hearing the case is called the forum state.
11. T F The following statement is an illustration of a forum selection provision: "This agreement shall be governed and interpreted in accordance with the law of the State of Maine."
12. T F If the parties have not included a choice of law provision in their contract, the choice of law rule of the forum state will determine which state's law will govern.
13. T F Article 2 of the UCC applies only to merchants.

14. T F The Uniform Commercial Code is divided into Chapters, Parts, and Sections.
15. T F Article 2 of the UCC applies to leases and sales of goods.
16. T F Although the title to Article 2 of the UCC is “Transactions in Goods,” it deals exclusively with the “Sale of Goods.”

FILL-IN-THE-BLANK QUESTIONS

1. _____. The determination of which law applies where more than one state is involved in a transaction, where conflicting laws within a state exist, or where federal law may preempt state law.
2. _____. Law derived from custom and usage and from judicial decisions recognizing and enforcing custom and usage.
3. _____. Law enacted by a state legislature.
4. _____. The Code that includes an article on sale of goods.
5. _____. The article of the UCC that deals with the sale of goods.
6. _____. Contracts for both parts or materials and labor.
7. _____. Under this doctrine state law must give way to federal law when federal law either expressly regulates the matter or when a particular subject is regarded as being beyond the bounds of state action.
8. _____. The state in which the case is filed.
9. _____. Deference given by the courts to the parties’ own choice of applicable law.
10. _____. The name of the choice of law rule proposed by the Restatement (Second) of Conflicts.
11. _____. The article in the UCC that deals with lease of goods.

MULTIPLE CHOICE QUESTIONS (CIRCLE ALL THE CORRECT ANSWERS)

1. The forum state is:
 - (a) the state hearing the case
 - (b) the state that has the governing law
 - (c) the state where the parties are located
 - (d) the state in which the case is filed
 - (e) the state where performance takes place

2. The following are known choice of law questions:
 - (a) selecting the rules when more than one state has an interest in the transaction
 - (b) selecting the rules when federal and state laws conflict
 - (c) selecting the rules when the parties dispute whether a law is applicable
 - (d) selecting the rules when the parties dispute whether the forum state has jurisdiction
 - (e) selecting the rules when a state has several sets of rules
3. Buyer (offeror) is located in Oregon and Seller (offeree) is located in Florida. The goods that will be the subject of this contract will be manufactured in Ohio and shipped by the Seller to the Buyer's warehouse in California. Under the party autonomy rule, which state or states could the parties select for their choice of applicable law:
 - (a) Oregon
 - (b) New Mexico
 - (c) Ohio
 - (d) California
 - (e) Florida
4. Buyer (offeror) is located in Oregon and Seller (offeree) is located in Florida. The goods that will be the subject of this contract will be manufactured in Ohio and shipped by the Seller to the Buyer's warehouse in California. The parties have not included a choice of law provision in their contract. Seller fails to deliver the goods to Buyer and Buyer brings a breach of contract action against the Seller in Oregon. The Oregon court will use the choice of law rule of which state to determine which state's law will govern:
 - (a) Florida
 - (b) Ohio
 - (c) California
 - (d) Oregon
 - (e) New Mexico
5. The following choice of law rules may apply to contracts:
 - (a) the law of the plaintiff's domicile
 - (b) the law of the place of the making of the contract
 - (c) the law of the place of performance of the contract
 - (d) the law of the state with the most significant contacts or relationship with the transaction
 - (e) the location of the forum court

SHORT ANSWER QUESTIONS

1. Buyer is located in Oregon and Seller is located in Florida. The goods that will be the subject of this contract will be manufactured in Ohio and shipped by the Seller to the Buyer's warehouse in California. Draft a choice of law provision for the parties.
2. Although courts will give effect to the parties' own choice of applicable law, this deference is not without limitations. If the contracting parties select the state with the applicable law and incorporate this selection in their contract for their choice of law, then the court in the forum state will enforce this choice of law provision unless:
3. Adam hired Quality to paint his house. Quality promised to do a turn-key job, that is to supply the paint as well as apply the paint. The contract was oral. Quality failed to complete the work and Adam sued Quality for breach of contract. If this transaction is a sale of goods, Article 2 of the UCC applies, and the contract must satisfy the Statute of Frauds provision of the UCC and be in writing to be enforceable. If this transaction is not a sale of goods, Article 2 is inapplicable, and the contract is enforceable regardless of whether it was oral or written. Does Article 2 of the UCC or state common law apply?
4. Describe the federal preemption doctrine.

PART

II

Step Two: Contract Formation

INTRODUCTION

A Transactional Guide to Contract Formation

CHAPTER 2

The Offer Phase

CHAPTER 3

The Post-Offer / Pre-Acceptance Phase

CHAPTER 4

The Acceptance Phase

CHAPTER 5

The Post-Acceptance Phase

CHAPTER 6

Drafting a Contract

INTRODUCTION

A Transactional Guide to Contract Formation

Part Two investigates the three phases of contract formation (offer, post-offer/pre-acceptance, and acceptance); the modification of an existing contract (the post-acceptance phase); and drafting a contract.

Chapter 2.	The Offer Phase
Chapter 3.	The Post-Offer/Pre-Acceptance Phase
Chapter 4.	The Acceptance Phase
Chapter 5.	The Post-Acceptance Phase
Chapter 6.	Drafting a Contract

Evaluating whether the parties have formed a contract follows the transaction's evolution from beginning to end. In the offer phase, the parties become acquainted with each other. They begin negotiating. When one party has enough information and is ready to enter into a binding transaction, that party makes an offer requesting an exchange. "I will do this if you will do that." The offeror states what he or she will do in exchange for what the other party, the offeree, must do. Implicit in the offer is the offeror's statement, "I will be bound by the terms that I have stated if you say yes."

The second phase, post-offer/pre-acceptance, may last no longer than an instant or may extend for hours, days, weeks, or even months. This post-offer/pre-acceptance phase is a waiting period for the offeror. The offeror waits for the offeree to either accept or reject the offer. The longer the wait, the greater the opportunity for the transaction to go awry.

A number of events can occur that will cause the offer to terminate before an attempted acceptance:

- The offeror may reconsider the wisdom of the offer and revoke it, in which case the offeree no longer has an offer to accept.
- The offeree may decide that a contract on the offeror's terms would not be in his or her best interest and therefore rejects the offer. A rejection extinguishes the offer. Because an offer no longer exists, the offeree may assume the role of offeror and propose an alternative offer (known as a counteroffer) with more favorable terms.
- The offer may have stated a time limit within which it must be accepted. If not accepted within this time, the offer ceases to exist (lapses).
- If the offer does not state how long the offeree has to accept, the offer will cease to exist (lapse) after the offeree has had a reasonable time to accept.
- Finally, the offeror or offeree could die or become incapacitated or the subject matter of the offer could be destroyed before the offer was accepted.

If the offer continues to exist, the offeree can accept the offer. To accept the offer, the offeree agrees to the terms the offeror has proposed. Because the offeror has control of the offer ("the offeror is the master of his or her offer"), the

offer is made on a “take it or leave it” basis. If the offeree accepts the offeror’s offer, the offeree’s acceptance concludes the transaction, and a contract is formed on the offeror’s terms. If the offeree finds the terms of the offer unacceptable, he or she can reject the offer and propose his or her own offer (a counteroffer). The offeree now has control over the terms of the offer and the original offeror must either “take it or leave it.” If the offeror accepts the offeree’s offer, the offeror’s acceptance concludes the transaction, and a contract is formed on the offeree’s terms.

Sometimes, the parties wish to change the terms of the existing contract or to correct an error in the written contract. They are now in the post-acceptance phase of contract formation, and they do not have the same flexibility that existed during prior phases. Although the relationship of the parties can be changed after a contract has been formed, they have surrendered their “freedom to contract” and now must follow the often intricate rules imposed upon them by the law.



The Offer Phase

- ◆ The Offer vs. Preliminary Negotiation (Creating the Power in the Offeree to Contract)
 - The Joke*
 - The Advertisement*
 - The Auction*
- ◆ The Elements of an Offer—The Offeror’s Promise and Consideration for That Promise
 - When a “Promise” Is Really a Promise*
 - Consideration for the Offeror’s Promise*
 - The Offeror’s Promise Must Be Made to Induce the Consideration*
- ◆ Alternatives to Classical Consideration
 - Tinkering with the Classical Doctrine*
 - Reliance as an Alternative to Consideration*
- ◆ Alternative Causes of Action If There Is No Offer
 - The Role of Reliance as a Cause of Action When There Is No Promise (No Unequivocal Assurance)*
 - The Role of Restitution as a Cause of Action When There Is No Promise*

Chapter Two, The Offer Phase, is the first chapter of Part II—Contract Formation. A contract consists of an offer and an acceptance. An offer is made when the offeror creates the power in the offeree to contract. In

addition to a general study of when an offer is created, Chapter 2 analyzes several special applications: the joke, the advertisement, and the auction.

Next, the focus changes from *when* an offer has been made to *what* constitutes an offer. The offeror, as the master of his or her offer, establishes the terms of the offer. An offer for a bilateral contract has three elements: (1) the offeror's promise (i.e., the unequivocal assurance of the action or forbearance that the offeror is willing to undertake); (2) consideration for the offeror's promise (i.e., the offeree's promise); and (3) the fact that the offeror made his or her promise to induce the offeree to promise. An offer for a unilateral contract also has three elements: (1) the offeror's promise (i.e., the unequivocal assurance of the action or forbearance that the offeror is willing to undertake); (2) consideration for the offeror's promise (i.e., the offeree's performance); and (3) the fact that the offeror made his or her promise to induce the offeree to perform. The offeror, by being the master of the offer, determines whether the offer should be for a bilateral contract (promise for a promise) or for a unilateral contract (promise for a performance).

When is a "promise" really a promise? Illusory promises and indefinite promises do not meet the test. What is "consideration," and why is consideration an essential element of an offer? Motives, moral obligations, and shams do not qualify.

In addition to studying the classical contract law of offer, Chapter Two explores the alternatives to classical consideration. The first alternative involves legislative and judicial tinkering with classical doctrine. The second alternative introduces reliance as an alternative to consideration.

Finally, if a "contract promise" (unequivocal assurance) is lacking, an alternative cause of action may exist. The courts have recognized a detrimental reliance cause of action and a restitution (unjust enrichment) cause of action (see Figure 2-1).

THE OFFER VS. PRELIMINARY NEGOTIATION (CREATING THE POWER IN THE OFFEREE TO CONTRACT)

The Restatement (Second) of Contracts § 24 defines an **offer** as "the manifestation of willingness to enter into a bargain, so made as to justify another person in understanding that his assent to that bargain is invited and will conclude it." Thus an offer by the offeror creates the power of acceptance in the offeree.

A synonym for *manifestation* is *demonstration*. A "manifestation of willingness" or a "demonstration of willingness" refers to the outward actions of the negotiating parties as understood by a third person watching the parties. This nonparticipant, who is evaluating whether the manifestation of willingness has occurred, is referred to as "the reasonable person." The **reasonable person's standard** is the measure used by an unbiased nonparticipating hypothetical observer.

The reasonable person's standard is an objective standard. Objectivity focuses on taking the transaction at face value. If strangers observe the negotiations, their conclusions would be objective. The strangers would possess only

FIGURE 2-1 The Offer Phase of the Road Map

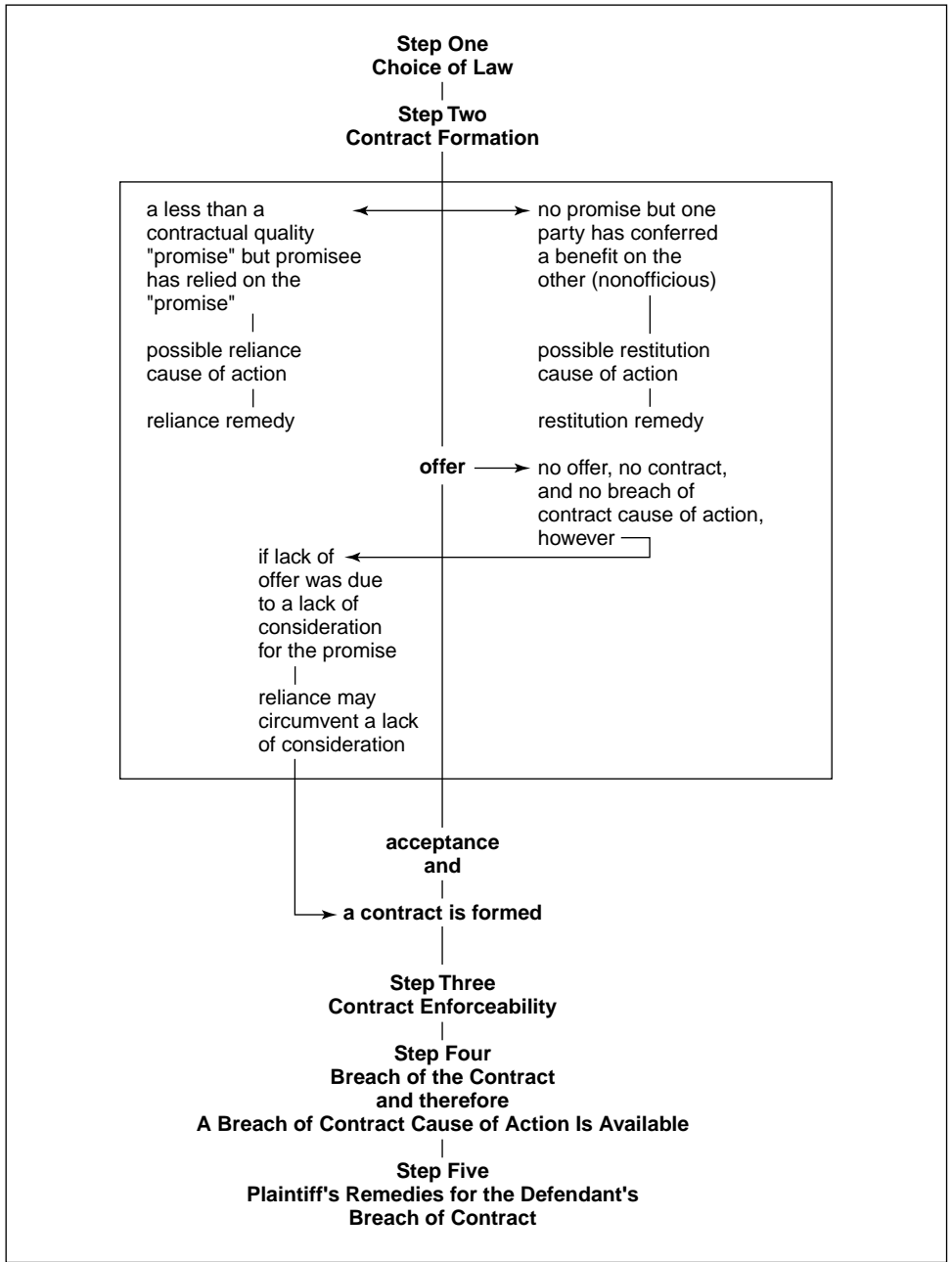


FIGURE 2–2 Offer vs. Preliminary Negotiation Using a Subjective or an Objective Standard

The Facts:	#1	#2
The Offeror's perception of the facts	offer	offer
The Offeree's perception of the facts	offer	preliminary negotiation
Conclusion	offer	preliminary negotiation

Offer vs. Preliminary Negotiation Using a Subjective Standard

The Facts:	#1	#2	#3
The Offeror's perception of the facts	offer	offer	offer
The Offeree's perception of the facts	offer	preliminary negotiation	preliminary negotiation
The Reasonable Person's perception of the facts	if offer	if offer	if preliminary negotiation
Conclusion	offer	offer	preliminary negotiation

Offer vs. Preliminary Negotiation Using an Objective Standard

those facts appearing on the face of the negotiation and would not be aware of underlying motivations or intent. The manifestation of willingness is evaluated by this **objective standard**—the reasonable person's standard.

Both the Restatement (First) and the Restatement (Second) of Contracts use an objective standard for the law of contracts. Early contracts cases, however, used a subjective standard. The **subjective standard** evaluated communications by asking how the person making the communications would interpret them and not how a reasonable person would interpret them. The **"meeting of the minds"** concept depends on subjective evaluations by both parties to the contract. The subjective "meeting of the minds" has been replaced by the objective "manifestation of assent." Unfortunately, old phraseology dies hard. Although the standard in the Restatement's definition of contract is clearly objective, many current cases parrot subjective language. Care must be taken when reading cases that use "meeting of the minds" language (see Figure 2–2).

The manifestation by the offeror must be sufficient to justify an understanding by the offeree that his or her assent to that bargain is invited and will

conclude it. A contract will be formed, and the offeror will be bound by the contract when the offeree assents. After the offeree accepts the offer, it will be too late for the offeror to unilaterally add, delete, or modify the terms of the offer.

Fairmount Glass Works v. Grunden-Martin Woodenware Co., although an old case, provides an excellent set of facts upon which to determine whether a communication is an offer or merely preliminary negotiation. The opinion begins by describing the various communications between Grunden-Martin, the potential buyer, and Fairmount Glass, the potential seller. While reading through the opinion, place each communication in chronological order. Next, begin with the first communication and determine whether it was an offer or merely preliminary negotiation. Consider the following:

Did Grunden-Martin intend to be bound by its letter if Fairmount Glass responded yes without stating any additional or different terms, or did Grunden-Martin want Fairmount Glass to make the offer so Fairmount Glass could evaluate the terms and would be the party that responded by saying yes?

If the first Grunden-Martin letter was not the offer, was Fairmount's letter in reply the offer, or was it still only preliminary negotiation?

Did Fairmount Glass intend to be bound by its letter if Grunden-Martin responded yes without stating any additional or different terms?

If the Fairmount letter was not the offer but still only preliminary negotiations, then evaluate the remaining communications, in order, until an offer has been found or all the communications have been exhausted.

In reading *Fairmount Glass*, determine whether the judge's evaluation of each communication is based on a subjective or an objective standard. Was the judge concerned with what each party thought it was saying (subjective) or how the communication would be understood by a reasonable person (objective)?



CASE

Fairmount Glass Works v. Grunden-Martin Woodenware Co.

Court of Appeals of Kentucky, 1899. 106 Ky. 659, 51 S.W. 196.

HOBSON, J. On April 20, 1895, appellee wrote appellant the following letter:

"St. Louis, Mo., April 20, 1895. Gentlemen: Please advise us the lowest price you can make us on our order for ten car loads of Mason green jars, complete, with caps, packed one dozen in a case, either delivered here, or f.o.b. cars your place, as you prefer. State terms and cash discount. Very truly, Grunden-Martin W.W. Co."

To this letter appellant answered as follows:

"Fairmount, Ind., April 23, 1895. Grunden-Martin Wooden Ware Co., St. Louis, Mo.—Gentlemen: Replying to your favor of April 20, we quote you Mason fruit jars, complete, in one-dozen boxes, delivered in East St. Louis, Ill.: Pints \$4.50, quarts \$5.00, half gallons \$6.50, per gross, for immediate acceptance, and shipment not later than May 15, 1895; sixty days' acceptance, or 2 off, cash in ten days. Yours truly, Fairmount Glass Works

.....

For reply thereto, appellee sent the following telegram on April 24, 1895:

"Fairmount Glass Works. Fairmount, Ind.: Your letter twenty-third received. Enter order ten car loads as per your quotation. Specifications mailed. Grunden-Martin W.W. Co."

In response to this telegram, appellant sent the following:

"Fairmount, Ind., April 24, 1895. Grunden-Martin W.W. Co., St. Louis, Mo.: Impossible to book your order. Output all sold. See letter. Fairmount Glass Works."

Appellee insists that, by its telegram sent in answer to the letter of April 23d, the contract was closed for the purchase of 10 car loads of Mason fruit jars. Appellant insists that the contract was not closed by this telegram, and that it had the right to decline to fill the order at the time it sent its telegram of April 24. This is the chief question in the case. The court below gave judgment in favor of appellee, and appellant has appealed, earnestly insisting that the judgment is erroneous.

We are referred to a number of authorities holding that a quotation of prices is not an offer to sell, in the sense that a completed contract will arise out of the giving of an order for merchandise in accordance with the proposed terms. There are a number of cases holding that the transaction is not completed until the order so made is accepted. 7 Am. & Eng. Enc. Law (2d Ed.) p. 138; *Smith v. Gowdy*, 8 Allen, 566; *Beaupre v. Telegraph Co.*, 21 Minn. 155. But each case must turn largely upon the language there used. In this case we think there was more than a quotation of prices, although appellant's letter uses the word "quote" in stating the prices given. The true meaning of the correspondence must be determined by reading it as a whole. Appellee's letter of April 20th, which began the transaction, did not ask for a quotation of prices. It reads: "Please advise us the lowest price you can make us on our order for ten car loads of Mason green jars. * * * State terms and cash discount." From this appellant could not fail to understand that appellee wanted to know at what price it would sell its ten car loads of these jars; so when, in answer, it wrote: "We quote you Mason fruit jars * * * pints \$4.50, quarts \$5.00, half gallons \$6.50, per gross, for immediate acceptance; * * * 2 off, cash in ten days,"—it must be deemed as intending to give appellee the information it had asked for. We can hardly understand what was meant by the words "for immediate acceptance," unless the latter was intended as a proposition to sell at these prices if accepted immediately. In construing every contract, the aim of the court is to arrive at the intention of the parties. In none of the cases to which we have been referred on behalf of appellant was there on the face of the correspondence any such expression of intention to make an offer to sell on the terms indicated. In *Fitzhugh v. Jones*, 6 Munf. 83, the use of the expression that the buyer should reply as soon as possible, in case he was disposed to accede to the terms offered, was held sufficient to show that there was a definite proposition, which was closed by the buyer's acceptance. The expression in appellant's letter, "for immediate acceptance," taken in connection with appellee's letter, in effect, at what price it would sell the goods, is, it seems to us, much stronger evidence of a present offer, which, when accepted immediately, closed the contract. Appellee's letter was plainly an inquiry for the price and terms on which appellant would sell the goods, and appellant's answer to it was not a quotation of prices, but a definite offer to sell on the terms indicated, and could not be withdrawn after the terms had been accepted. It will be observed that the telegram of acceptance refers to the specifications mailed. These specifications were contained in the following letter: "St. Louis, Mo., April 24, 1895. Fairmount Glass-Works Co., Fairmount, Ind.—Gentlemen: We received your letter of 23rd this morning, and telegraphed you in reply as follows: 'Your letter 23rd received. Enter order ten car loads as per your quotation. Specifications mailed,'—which we now confirm. We have accordingly entered this contract on our books for the ten cars Mason green jars, complete, with caps and rubbers, one dozen in case, delivered to us in East St. Louis at \$4.50 per gross for pint, \$5.00 for quart, \$6.50 for one-half gallon. Terms,

60 days' acceptance, or 2 per cent. for cash in ten days, to be shipped not later than May 15, 1895.

. . . .

You may ship the first car to us here assorted: Five gross pint, fifty-five gross quart, forty gross one-half gallon. Specifications for the remaining 9 cars we will send later. Grunden-Martin W.W. Co."

. . . .

Appellant also insists that the contract was indefinite, because the quantity of each size of the jars was not fixed, that 10 car loads is too indefinite a specification of the quantity sold, and that appellee had no right to accept the goods to be delivered on different days. The proof shows that "10 car loads" is an expression used in the trade as equivalent to 1,000 gross, 100 gross being regarded a car load. The offer to sell the different sizes at different prices gave the purchaser the right to name the quantity of each size, and, the offer being to ship not later than May 15th, the buyer had the right to fix the time of delivery at any time before that. *Sousely v. Burns' Adm'r*, 10 Bush, 87; *Williamson's Heirs v. Johnston's Heirs*, 4 T.B. Mon. 253; *Wheeler v. Railroad Co.*, 115 U.S. 34, 5 Sup.Ct. 1061, 1160. The petition, if defective, was cured by the judgment, which is fully sustained by the evidence. Judgment affirmed.

The question of *when* an offer has been made also arises in disputes involving jokes, advertisements, and auctions. These three variations on the theme of creation of the offer are discussed next.

The Joke

What people say and what they actually mean may be entirely different. The outward expression (objective) rather than the secret or unexpressed intent (subjective) determines whether a statement is intended as an offer. Thus, the objective intent rather than the subjective intent determines whether an offer has been extended.

A graphic illustration of this principle is the joke. In *Lucy v. Zehmer*, A. H. and Ida Zehmer, owners of the Ferguson farm, operated a local restaurant. One evening their old friend W. O. Lucy met them at the restaurant, and after a few drinks and a lot of talk, the Zehmers signed a writing that said that they promised to sell W. O. Lucy the Ferguson farm for \$50,000 cash.

Consider the following questions when reading the case. As each question is answered, complete the two charts below.

1. Did A. H. Zehmer believe that his writing was an offer or a joke?
2. Did W.O. Lucy believe that Zehmer's writing was an offer or a joke?
3. Would a reasonable person, viewing the events at the restaurant, believe that the writing was an offer or a joke?
4. Did the court use an objective or subjective standard to resolve whether Zehmer's writing was an offer or a joke?
5. What facts were useful in reaching your conclusions?

The Facts: Zehmer's writing	
Zehmer's perception of his writing	offer? or joke?
Lucy's perception of Zehmer's writing	offer? or joke?
Conclusion	offer? or joke?

The Facts: Zehmer's writing	
Zehmer's perception of his writing	offer? or joke?
Lucy's perception of Zehmer's writing	offer? or joke?
Reasonable Person's perception of Zehmer's writing	offer? or joke?
Conclusion	offer? or joke?



CASE

Lucy v. Zehmer

Supreme Court of Appeals of Virginia, 1954. 196 Va. 493, 84 S.E.2d 516.

Before EGGLESTON, BUCHANAN, MILLER, SMITH and WHITTLE, JJ.
 BUCHANAN, Justice.

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.

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.

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.

. . . .

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.

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."

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.

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.

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.

Mr. and Mrs. Zehmer were called by the complainants as adverse witnesses. Zehmer testified in substance as follows:

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."

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 \$50,000.00 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."

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 'Ferguson' 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."

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.' "

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 \$50,000.00 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.

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.

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."

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.

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.

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 in-

ention. 'The law imputes to a person an intention corresponding to the reasonable meaning of his words and acts.' " *First Nat. Exchange Bank of Roanoke v. Roanoke Oil Co.*, 169 Va. 99, 114, 192 S.E. 764, 770.

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.

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.

. . . .

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.

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.

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.

. . . .

The complainants are entitled to have specific performance of the contract 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.

The Advertisement

All offers discussed thus far have been directed to a specific party. Advertisements, by contrast, are made to the general public. Simply because an advertisement is directed to the general public, however, does not preclude it from being an offer. Offers need not be made to a specific party. The offer of a reward, for example, is an offer made to the general public.

The general rule followed in most states is that advertisements are not offers, but merely invitations to bargain. Exceptions to this general rule do exist.

PARALEGAL EXERCISE 2.1 Compare the following two advertisements. Are both advertisements offers, or are they simply invitations to negotiate?

Saturday 9 A.M. Sharp
3 Brand New Fur Coats
Worth to \$100.00
First Come
First Served
\$1 Each

Saturday 9 A.M.
1 Black Lapin Stole
Beautiful,
Worth \$139.50 . . . \$1.00
First Come
First Served

What factors did the Supreme Court of Minnesota use in *Lefkowitz v. Great Minneapolis Surplus Store, Inc.*, to determine whether these advertisements were offers or only invitations to negotiate (preliminary negotiations)?

CASE

Lefkowitz v. Great Minneapolis Surplus Store, Inc.

Supreme Court of Minnesota, 1957. 86 N.W.2d 689.

MURPHY, Justice.

This is an appeal from an order of the Municipal Court of Minneapolis denying the motion of the defendant for amended findings of fact, or, in the alternative, for a new trial. The order for judgment awarded the plaintiff the sum of \$138.50 as damages for breach of contract.

This case grows out of the alleged refusal of the defendant to sell to the plaintiff a certain fur piece which it had offered for sale in a newspaper advertisement. It appears from the record that on April 6, 1956, the defendant published the following advertisement in a Minneapolis newspaper:

*"Saturday 9 A.M. Sharp
3 Brand New
Fur
Coats
Worth to \$100.00
First Come
First Served
\$1
Each"*

On April 13, the defendant again published an advertisement in the same newspaper as follows:

*"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"*

The record supports the findings of the court that on each of the Saturdays following the publication of the above-described ads the plaintiff was the first to present himself at the appropriate counter in the defendant's store and on each occasion demanded the coat and the stole so advertised and indicated his readiness to pay the sale price of \$1. On both occasions, the defendant refused to sell the merchandise to the plaintiff, stating on the first occasion that by a "house rule" the offer was intended for women only and sales would not be made to men, and on the second visit that plaintiff knew defendant's house rules.

The trial court properly disallowed plaintiff's claim for the value of the fur coats since the value of these articles was speculative and uncertain. The only evidence of value was the advertisement itself to the effect that the coats were "Worth to \$100.00," how much less being speculative especially in view of the price for which they were offered for sale. With reference to the offer of the defendant on April 13, 1956, to sell the "1 Black Lapin Stole * * * worth \$139.50 * * *" the trial court held that the value of this article was established and granted judgment in favor of the plaintiff for that amount less the \$1 quoted purchase price.

1. The defendant contends that a newspaper advertisement offering items of merchandise for sale at a named price is a "unilateral offer" which may be withdrawn without notice. He relies upon authorities which hold 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. *Montgomery Ward & Co. v. Johnson*, 209 Mass. 89, 95 N.E. 290; *Nickel v. Theresa Farmers Co-op. Ass'n*, 247 Wis. 412, 20 N.W.2d 117; *Lovett v. Frederick Loeser & Co. Inc.*, 124 Misc. 81, 207 N.Y.S. 753; *Schenectady Stove Co. v. Holbrook*, 101 N.Y. 45, 4 N.E. 4; *Georgian Co. v. Bloom*, 27 Ga.App. 468, 108 S.E. 813; *Craft v. Elder & Johnston Co.*, 38 N.E.2d 416, 34 Ohio L.A. 603; Annotation, 157 A.L.R. 746.

. . . .

There are numerous authorities which hold that a particular advertisement in a newspaper or circular letter relating to a sale of articles may be construed by the court as constituting an offer, acceptance of which would complete a contract. *J.E. Pinkham Lumber Co. v. C. W. Griffin & Co.*, 212 Ala. 341, 102 So. 689; *Seymour v. Armstrong & Kassebaum*, 62 Kan. 720, 64 P. 612; *Payne v. Lautz Bros. & Co.*, City Ct., 166 N.Y.S. 844, affirmed, 168 N.Y.S. 369, affirmed, 185 App.Div. 904, 171 N.Y.S. 1094; *Arnold v. Phillips*, 1 Ohio Dec. Reprint 195, 3 West. Law J. 448; *Oliver v. Henley*, Tex.Civ.App., 21 S.W.2d 576; Annotation, 157 A.L.R. 744, 746.

The test of whether a binding obligation may originate in advertisements addressed to the general public is “whether the facts show that some performance was promised in positive terms in return for something requested.” 1 Williston, Contracts (Rev. ed.) § 27.

The authorities above cited emphasize that, where the offer is clear, definite, and explicit, and leaves nothing open for negotiation, it constitutes an offer, acceptance of which will complete the contract. The most recent case on the subject is *Johnson v. Capital City Ford Co.*, La.App., 85 So.2d 75, in which the court pointed out that a newspaper advertisement relating to the purchase and sale of automobiles may constitute an offer, acceptance of which will consummate a contract and create an obligation in the offeror to perform according to the terms of the published offer.

Whether in any individual instance a newspaper advertisement is an offer rather than an invitation to make an offer depends on the legal intention of the parties and the surrounding circumstances. Annotation, 157 A.L.R. 744, 751; 77 C.J.S., Sales, § 25b; 17 C.J.S., Contracts, § 389. We are of the view on the facts before us that the offer by the defendant of the sale of the Lapin fur was clear, definite, and explicit, and left nothing open for negotiation. The plaintiff having successfully managed to be the first one to appear at the seller’s place of business to be served, as requested by the advertisement, and having offered the stated purchase price of the article, he was entitled to performance on the part of the defendant. We think the trial court was correct in holding that there was in the conduct of the parties a sufficient mutuality of obligation to constitute a contract of sale.

2. The defendant contends that the offer was modified by a “house rule” to the effect that only women were qualified to receive the bargains advertised. The advertisement contained no such restriction. This objection may be disposed of briefly by stating that, while an advertiser has the right at any time before acceptance to modify his offer, he does not have the right, after acceptance, to impose new or arbitrary conditions not contained in the published offer. *Payne v. Lautz Bros. & Co.*, City Ct., 166 N.Y.S. 844, 848; *Mooney v. Daily News Co.*, 116 Minn. 212, 133 N.W. 573, 37 L.R.A., N.S., 183.

Affirmed.

PARALEGAL EXERCISE 2.2 Find three different types of advertisements in your local newspaper, and determine whether each is an offer or only an invitation to negotiate (preliminary negotiation).

The Auction

An auction may be either “with reserve” or “without reserve.” Whether the auction is with or without reserve is the key to whether the auctioneer (as agent for the seller) or the bidder is the offeror.

In an **auction with reserve**, the auctioneer may withdraw the property at any time until he or she announces the completion of the sale. Therefore, the auctioneer, rather than being the offeror, is asking potential bidders to make an offer. The auctioneer evaluates the bidder’s offer and either accepts it by the fall of the hammer or in another customary manner (thus concluding the sale) or rejects it by withdrawing the property from the auction. Since the seller may withdraw the property from the auction, the seller may also bid.

EXAMPLE 2-1

In an auction with reserve on Greenacre, the auctioneer asked whether anyone would open the bid at \$200,000. The bidding, however, began at \$10,000 and ended at \$100,000. The auctioneer could reject the \$100,000 bid and withdraw Greenacre from the auction or bring the hammer down and accept the bid.

Since the auction was with reserve, the bidders were the offerors and the auctioneer, as offeree, had the power to either accept or reject the highest offer.

In an **auction without reserve** (an absolute auction), the auctioneer is the offeror and the bidders are the offerees. After the auctioneer calls for bids on the property, the auctioneer cannot withdraw the property if a bid is made within a reasonable time. Each bid is an acceptance conditioned on there being no higher bidder. Therefore, the auctioneer must sell to the highest bidder. Since the auctioneer (acting for the seller) is the offeror, the seller cannot bid.

EXAMPLE 2-2

In an auction without reserve on Greenacre, the auctioneer asked whether anyone would open the bid at \$200,000. The bidding, however, began at \$10,000 and ended at \$100,000. The auctioneer could not reject the \$100,000 bid and withdraw Greenacre from the auction, but must bring the hammer down and conclude the sale.

Since the auction was without reserve, the auctioneer was the offeror and each bidder exercised the power to accept the auctioneer's offer to sell.

An auction is with reserve unless a contrary intention is apparent from a statute, court order, or advertisement or by an announcement at the beginning of the auction. A statement in an advertisement, however, "that the property will be offered to the highest bidder" does not mean that the auction will be conducted without reserve. Such a statement is considered only preliminary negotiation.

PARALEGAL EXERCISE 2.3 Sam Brown, the auctioneer, presented a Louis XV ormolu clock to the potential bidders at the auction. Susan Sanchez, the owner of the valuable antique clock, had told Sam not to sell it for less than \$5,000. In spite of Sam's best efforts, the highest bid was \$2,500.

Could Sam withdraw the clock from the auction?

At times in an auction with reserve, the seller does not give the auctioneer authority to conclude the sale. Rather the seller reserves the power to accept or reject the highest bid (i.e., the bidder's offer). In *Cuba v. Hudson & Marshall*, consider whether the auction is with or without reserve. If the auction is with reserve, does the auctioneer or the seller have the power to accept the bidder's offer? What facts did you consider when making this decision?



CASE

Cuba v. Hudson & Marshall

Court of Appeals of Georgia, 1994.
213 Ga. App. 639, 445 S.E.2d 386.

POPE, Chief Judge.

Defendants are auctioneers who conducted an auction of real estate for the Resolution Trust Corporation ("RTC"). Plaintiffs attended the auction and were the high bidder for a particular parcel, Property No. 230. After the bidding was ended by the fall of the auctioneer's hammer, however, plaintiffs were told that the RTC rejected their bid. Plaintiffs sued defendants for damages, and after discovery, plaintiffs and defendants filed crossmotions for summary judgment. The trial court denied plaintiffs' motion and granted defendants', and plaintiffs appeal from both rulings.

The parties essentially agree on the facts. Defendants prepared an auction brochure listing and describing the various RTC properties to be auctioned. Some of the properties were listed with the word "absolute" next to them; others, including Property No. 230, were not. On the back cover, under the heading "AUCTION INFORMATION & TERMS," the brochure stated that properties without "absolute" next to them were being sold with reserve, and that "[f]or property being sold 'With Reserve,' the highest bid is subject to the approval of the seller." (Emphasis supplied.) Defendant Asa Marshall, who conducted the actual auction, stated in his introductory remarks that with respect to those properties being auctioned with reserve, "I can assure you you're not wasting your time. We have officials from RTC all over the country here. The only thing they want to make sure of is that they do have active bidding on those properties auctioned on reserve, and if they do they are going to sell them. I can assure you of that. They are not here to waste your time or to get this property appraised." Immediately following Asa Marshall's introductory remarks, however, another employee of defendant Hudson & Marshall, Inc. got up and pointed out to the audience that the terms of the auction were set forth on the back cover of the brochure. He held up a brochure and showed the audience exactly where the terms and conditions were and then said they would abide by those terms.

1. Plaintiffs first argue that a contract for the sale of Property No. 230 was formed at the time the auctioneer's hammer fell, and that defendant auctioneers are liable for the breach of that contract. As a general rule, even if an auction is with reserve (and all auctions are presumed to be with reserve unless they are expressly stated to be without reserve), the seller must exercise his right to withdraw the property from sale before the auctioneer accepts the high bid by letting his hammer fall; immediately after the hammer falls, an irrevocable contract is formed. See *Stanley v. Whitmire*, 233 Ga. 675, 212 S.E.2d 845 (1975); *Tillman v. Dunman*, 114 Ga. 406, 409(1), 40 S.E. 244 (1901); *Coleman v. Duncan*, 540 S.W.2d 935, 937-938 (Mo.Ct.App.1976). Compare also OCGA § 11-2-328.¹ Yet at the same time, the seller has the right to establish any terms and conditions for the sale he wishes, and where the seller explicitly reserves the right to reject any bid made, the contract for sale is not formed until the seller actually accepts the bid. *Rountree v. Todd*, 210 Ga. 226, 78 S.E.2d 499 (1953). We think the only way to reconcile these cases is to recognize, as other courts have, that there is a distinction between auctions which are merely conducted with reserve and those in which the seller explicitly reserves the right to approve, confirm or reject the high bid. *Coleman*, 540 S.W.2d at 938. ("[S]uch a reservation sets a sale apart from the garden variety of auctions with reserve.") See also *Continental Can Co. v. Commercial Waterway Dist.*, 56 Wash.2d 456, 347 P.2d 887 (1959); *Moore v. Berry*, 40 Tenn.App. 1, 288 S.W.2d 465 (1955); *New York v. Union News Co.*, 222 N.Y. 263, 118 N.E. 635 (1917). Where the seller explicitly reserves the right to

reject or approve, the auctioneer is without authority to accept for the seller. Thus, the fall of the hammer in such auctions merely ends the bidding, and no contract is formed until the seller actually accepts the high bid. See *Continental Can*, 347 P.2d at 888-889; *Moore*, 288 S.W.2d at 467-468; *Union News*, 118 N.E. at 636-637.

The seller in this case explicitly reserved the right to reject or approve the high bid in the brochure. And Asa Marshall's "assurance" that all properties would be sold as long as the bidding was active did not modify this reservation since it was immediately followed by the announcement of another speaker who called the bidders' attention to the terms in the brochure and stated that "we will abide by those terms." Accordingly, the fall of the auctioneer's hammer merely ended the bidding and no enforceable contract was formed.

Judgment affirmed.

McMURRAY, P.J., and SMITH, J., concur.

1. This statute is part of our codification of Article 2 of the Uniform Commercial Code and thus does not directly apply to auctions of real property.

See OCGA § 11-2-102. Courts in other states have recognized that this portion of the Article reflects common law principles applicable to land auctions as well as auctions of goods, however, and have borrowed rules from it or applied it to land auctions by analogy. See, e.g., *Chevalier v. Sanford*, 475 A.2d 1148 (Me.1984); *Hoffman v. Horton*, 212 Va. 565, 186 S.E.2d 79 (1972).

THE ELEMENTS OF AN OFFER—THE OFFEROR'S PROMISE AND CONSIDERATION FOR THAT PROMISE

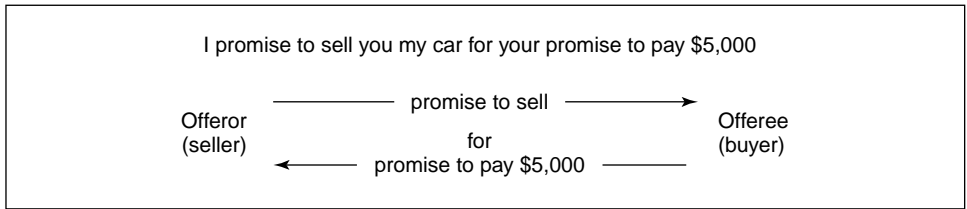
The previous section dealt with the question of determining when an offer is made. An offer is made when the offeror creates the power in the offeree to form a contract. This power is created when the offeror manifests a willingness to enter into a contract by inviting the offeree to agree to the offeror's terms. In other words, the offeror creates the power in the offeree when the offeror determines there is nothing remaining to negotiate. Acceptance by the offeree of the offeror's terms forms the contract.

Although it may appear that the transaction has moved from the preliminary negotiation to the offer phase, this conclusion may be premature. In the sequence of events, a communication may appear to be an offer, but it is still necessary to determine whether that communication has the essential elements of an offer. Simply stated, an offer has three elements:

- the offeror's promise
- the consideration for the offeror's promise (commonly referred to as the "price" for the offeror's promise)
- the offeror's promise must be made to induce the consideration

The **promisor** is the person making the promise. The **offeror** is the person making the offer. The promisor does not become an offeror until all three elements of offer are satisfied.

Although every offer begins with the offeror's promise, the consideration for the offeror's promise may be either a promise or a performance. The offeror may

FIGURE 2-3 An Offer for a Bilateral Contract

want the offeree to promise now and perform later or to perform and not promise to perform. The former offer is a “promise for a promise,” the latter offer is a “promise for a performance.” The offeror, who is the master of the offer, controls whether the offer is a promise for a promise or a promise for a performance.

A **bilateral contract** is often referred to as a “promise for a promise.” *Bi* is the Latin prefix meaning two. Here we have two promises in the offer. The offeror makes a promise in order to entice the offeree to promise (see Figure 2-3).

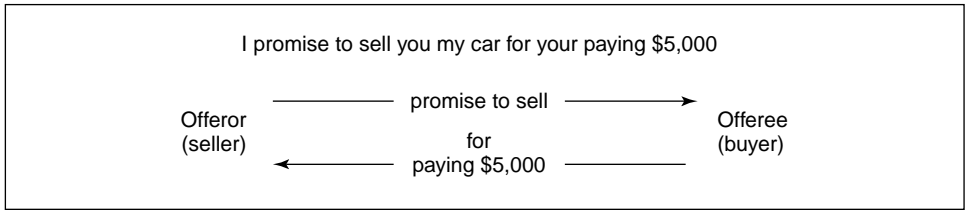
When the offeree promises, the offeree accepts the offer and a bilateral contract is formed. The offeree need not perform his or her promise for the contract to be formed. Contract formation occurs when the offeree promises and not when the offeree performs. Once the contract is formed, each party has a duty to perform his or her promise, and each has a right to receive the other party’s performance. Since both the offeror and the offeree have duties toward the other, either could be the breaching party.

The second form of offer is an offer for a unilateral contract. An **offer for a unilateral contract** is “a promise for a performance.” *Uni* is the Latin prefix meaning one. Here we have only one promise between the parties. The offeror makes a promise in order to entice the offeree to perform. The consideration for the offeror’s promise to sell is the offeree’s “paying \$5,000.” The offeror is not asking the offeree to promise to pay. The offeror is asking for the actual payment in return for his or her promise to sell (see Figure 2-4).

An offer for a unilateral contract does not become a contract until the offeree has fully performed. Once the offeree has fully performed and a unilateral contract is formed, only the offeror has a duty to perform. Therefore, only the offeror could be the breaching party.

Most offers are for bilateral contracts. “I promise to work for you for one year for your promise to pay \$800 a week.” “I promise to paint your house for your promise to pay \$1,500.” “I promise to build you a house for your promise to pay \$125,000.” “I promise to sell you this yacht for your promise to pay \$17,000.”

Most people do not speak or write in the formal “I promise for your promise.” Usually, the offer takes the form “I’ll sell you my car for \$5,000.” “I’ll sell” means “I promise to sell,” and the “\$5,000” means “for your promise to pay \$5,000.” Because the formal designation provides clarity in legal analysis, common usage will be upgraded to the formal “I promise.”

FIGURE 2-4 An Offer for a Unilateral Contract

Only in an unusual transaction, often in a family, friend, or reward setting or in a situation where the likelihood of success is uncertain, will an offeror make an offer for a unilateral contract. “I promise to give you Blackacre if you care for me for the remainder of my life.” “I promise to pay you \$10,000 if you provide information leading to the conviction of a known criminal.” “I promise to pay you \$100 if you win the race tomorrow.” “I promise to give you a half interest in Greenacre if you discover gold.” Note that in each of these offers, the offeree cannot accept unless he or she fully performs what the offeror has requested—caring for the offeror for the offeror’s lifetime, winning the race, and discovering gold. Indeed, had the offeror created an offer for a bilateral contract that required a promise to care for the offeror for the offeror’s lifetime, a promise to win the race, or a promise to discover gold, the offeree may not have promised since a promise that could not be performed at a later date would be a breach. As a rule, however, an offer will be an offer for a bilateral contract unless the offer clearly articulates that it is the offeree’s performance and not the offeree’s promise that is required for the contract to be formed.

The following material explores the three elements of an offer: the offeror’s promise, the consideration for the offeror’s promise, and the inducement connecting the offeror’s promise to the consideration for that promise.

When a “Promise” Is Really a Promise

A **promise** is an unequivocal assurance that something will or will not be done. “I may sell my car to you” is not unequivocal and therefore is less than a promise. On the other hand, “I will sell you my car” is an unequivocal assurance and is a promise. The unequivocal assurance could be to refrain from doing something as well as to do something. Thus, “I will not sell my car to Marylou” is as much a promise as “I will sell my car to Marylou.”

Two situations in which it is difficult to determine whether a “promise” exists are the illusory promise and the indefinite promise.

The Illusory Promise. The phrase “illusory promise” is a misnomer because an illusory promise is not a promise. It is less than a promise and does not create the power in the offeree to accept an offer. An illusory promise is not an unequivocal assurance that something will or will not be done.

EXAMPLE 2–3

“I may sell you my car” is an illusory promise. It is not the unequivocal statement “I will sell you my car.” The same is true for the statement “I will work for you next Monday if I feel like it.” There is no commitment to do or to refrain from doing something.

PARALEGAL EXERCISE 2.4 Is the term in the writing in *Rosenberg v. Lawrence* a promise or an illusory promise? What specific language is used by the court to distinguish a promise from an illusory promise?

**CASE*****Rosenberg v. Lawrence***

District Court of Appeal of Florida, 1988. 541 So. 2d 1204.

Before NESBITT, DANIEL S. PEARSON, and JORGENSON, JJ.

ON MOTION FOR CLARIFICATION AND REHEARING

NESBITT, Judge.

We grant the appellant’s motion for clarification and deny the appellee’s motion for rehearing; vacate our previous opinion and replace it with the following:

Charles and Cynthia divorced in 1976 and in 1978 entered into an agreement to provide for the support of their sons. In pertinent part, the agreement provided:

The parties are equally desirous of providing for the health, education, maintenance and support of their four sons, notwithstanding that three of their sons have reached majority. To that end, each of Charles and Cynthia, promises the other, and each of the children, to share on an equal basis, the expenses of educating, maintaining, supporting and providing health care for each of their four children. In an effort to encourage consistent attitudes toward their children, the parties shall encourage the love and affection of the children for each other and shall consult one another before incurring a material expense which would be governed hereby.

Various disputes arose under this agreement. During earlier litigation, the parties entered into a modification of the agreement, which was incorporated into an amended final judgment entered on June 3, 1982, which provides in part:

This will confirm the understanding of both parties and their counsel that paragraph 8 of the Final Judgment, as it relates to Howard’s conferring with both Plaintiff and Defendant before incurring, material, unusual or extraordinary expenses, means that neither Plaintiff nor Defendant will be obligated for any material, unusual or extraordinary expense to which he or she does not consent.

When the 1982 agreement was made, son Howard was enrolled in college. Subsequently, he withdrew from school, returned to Miami and began working. In September 1984, he commenced his college career anew at a different university. Without previous con-

sultation, negotiation, or any consent from the father, Howard's mother paid all of his expenses in connection with his education, boarding, lodging, and maintenance from September 1984 through November 17, 1985, exclusive of a summer term, in an aggregate amount of \$43,616.38. Thereafter, the mother demanded that the father reimburse her for one-half of those expenses. The father's defense to payment was that he had never been consulted, nor had he consented to the educational plan or any of the expenses. The trial court entered the money judgment against the father from which he appeals.

Under the initial contract, the parties exchanged mutual promises to each defray one-half of son Howard's college education. The specific details of payment were to be implemented by [reasonable] negotiation. The 1982 amendment attempted to change the method by which the son was to obtain needed funds. Our initial opinion held that the failure of Cynthia to negotiate the plan and costs with Charles rendered the contract unenforceable. Charles's motion for clarification represented that the duty of consultation and negotiation was removed from the original agreement in order to avoid further acrimony between the parties. Cynthia conceded this point in her motion for rehearing. Due to the language employed and the parties' own interpretation of the agreement, we agree that the 1982 amendment terminated the duty of negotiation between the ex-spouses.

Where one party retains to itself the option of fulfilling or declining to fulfill its obligations under the contract, there is no valid contract and neither side may be bound. *Miami Coca-Cola Bottling Co. v. Orange-Crush Co.*, 291 F. 102 (D.C.Fla. 1923), *aff'd*, 296 F. 693 (5th Cir.1924). "One who in words promises to render a future performance, if he so wills and desires when the future time arrives, has made no real promise at all." 1 *Corbin on Contracts* § 149 (1963). See also *Port Largo Club, Inc. v. Warren*, 476 So.2d 1330 (Fla. 3d DCA 1985) (vendor's contract obligation wholly illusory where he could breach contract with impunity); *Young v. Johnston*, 475 So.2d 1309 (Fla. 1st DCA 1985) and cases cited therein (where one party retains to itself the option of fulfilling or declining to fulfill its obligations under the contract, there is no valid contract and neither side may be bound); *Spooner v. Reserve Life Ins. Co.*, 47 Wash.2d 454, 287 P.2d 735 (1955) (statement by insurance company that sales bonus was voluntary and could be withheld with or without notice rendered promise illusory and unenforceable). "An illusory promise is no promise at all as that term has been. . . defined. If the expression appears to have the form of a promise, this appearance is 'an illusion.'" 1 *Corbin on Contracts* § 16 (1963). "As a matter of course, no action will lie against the party making the illusory promise. Having made no promise, it is not possible for him to be guilty of a breach." 1 *Corbin on Contracts* § 145 (1963).

Under the 1982 modification, the parties were not "obligated for any material, unusual or extraordinary expense to which he or she does not consent." Because payment was contingent upon each parent's consent to undertake an obligation, Charles and Cynthia's "promise" represented no more than an illusion which did not obligate either party to act. The illusory nature of each parent's promise made that promise void and the mother has no right to seek reimbursement based on that illusory commitment, either by way of direct action for breach or under an estoppel theory. See 1A *Corbin on Contracts* § 201 (1963) (action in reliance on a supposed promise creates no obligation on a man whose only promise is wholly illusory). Their "obligation" meant nothing more than, "I will if I want to."

For the foregoing reasons, the trial court's order finding the father responsible for one-half of the son's expenditures is reversed and the cause remanded with directions for the mother to receive payment for the outstanding allowance funds only.

NESBITT and JORGENSON, JJ., concur.

DANIEL S. PEARSON, J., concurs in the result only.

The Indefinite Promise. The phrase “indefinite promise” is a misnomer because an indefinite promise is not a promise.

An **indefinite promise** omits terms essential in enabling the court to determine an appropriate remedy in the event the promise is breached.

EXAMPLE 2-4

Seller says “I promise to sell you a cow for your promise to pay \$750.” When Seller owns a Holstein herd and does not designate a specific animal, Seller has made an indefinite promise. The animals vary in value; some are worth substantially more than \$750 and some substantially less. If Seller does not deliver a cow, how will the court determine the appropriate remedy for Seller’s refusal to deliver? Even if Seller does deliver a cow but Buyer complains that this was not the cow she wanted, how will the court determine whether the promise to deliver has been breached and, if breached, the appropriate remedy?

PARALEGAL EXERCISE 2.5 What makes the following promise indefinite? “I promise to pay you if you promise to work for me.”

If the transaction involves a sale of goods, Article 2 of the Uniform Commercial Code governs. Section 2-204(3) provides the following statement as to indefiniteness:

(3) Even though one or more terms are left open a contract for sale does not fail for indefiniteness if the parties have intended to make a contract and there is a reasonably certain basis for giving an appropriate remedy.

Under section 2-204(3), the parties must “[intend] to make a contract.” If the parties do not intend to make a contract, there is no contract. Also there must be “a reasonably certain basis for giving an appropriate remedy.” Without a reasonably certain basis for giving an appropriate remedy, there is no contract. If the parties have intended to make a contract but have failed to supply key terms, Article 2 may supply these terms. **Gap fillers** are those terms supplied by Article 2 of the UCC that supplement the terms supplied by the contracting parties. The gap fillers are generally found in Part 3 (2-300s) of Article 2 of the UCC. The gap fillers include provisions as to price (§ 2-305), place of delivery (§ 2-308), time for shipment or delivery (§ 2-309), payment or running of credit (§ 2-310), warranty of title (§ 2-312), warranty against infringement (§ 2-312), implied warranty of merchantability (§ § 2-314(1), (2)), implied warranty of usage of trade (§ 2-314(3)), and implied warranty of fitness for a particular purpose (§ 2-315).

EXAMPLE 2-5

Uniform Commercial Code § 2-305. Open Price Term.

- (1) The parties if they so intend can conclude a contract for sale even though the price is not settled. In such a case the price is a reasonable price at the time for delivery if
- (a) nothing is said as to price; or
 - (b) the price is left to be agreed by the parties and they fail to agree; or
 - (c) the price is to be fixed in terms of some agreed market or other standard as set or recorded by a third person or agency and it is not so set or recorded.

PARALEGAL EXERCISE 2.6 Apex Oil Co., a manufacturer and seller of petroleum products, including asphalt used in paving, and Mathy Construction Co., a road builder, discussed by telephone the possibility of Mathy purchasing 30,000 barrels of asphalt, to be picked up at Apex's Wood River, Illinois, plant for shipment up the Mississippi River to La Crosse, Wisconsin, during the week of July 30th. Apex and Mathy agreed on a price of \$75 a ton and Apex assured Mathy that 30,000 barrels could be available. At this time, Mathy was uncertain whether it needed 120–150 pen grade product or 85–100 pen grade product. The parties did not reach an agreement as to the type and grade of asphalt and whether any agreement was contingent on the availability of barge transportation to move the barrels from Wood River to La Crosse. Mathy could not secure a barge and did not pick up the asphalt. If Apex sues Mathy alleging breach of contract, consider the following:

1. Does Article 2 of the UCC govern this transaction (i.e., is this a contract for the sale of goods under § 2-102)?
2. Were one or more terms left open?
3. Did the parties intend to make a contract?
4. Could a court find a reasonably certain basis for giving an appropriate remedy?
 - a. Are these terms essential in enabling the court to determine an appropriate remedy in the event the promise is breached?
 - b. Are any of these open terms supplied in the gap fillers of Part 3 of Article 2 (the 2-300s)?

Consideration for the Offeror's Promise

The second element of an offer is the consideration for the offeror's promise. In the offer "I promise to sell you my car for your promise to pay \$5,000," the phrase "I promise to sell you my car" is the offeror's promise and "your promise to pay \$5,000" is the consideration for the offeror's promise.

Consideration is the "price" that the offeror expects to receive for his or her promise. "Price" has been placed in quotation marks to emphasize that the term "price" is not limited to dollars and cents. It can be anything that the law

recognizes as consideration. It could be a promise to barter. “I promise to sell you my car for your promise to roof my house.” The consideration for the offeror’s promise can easily be found by asking “what is the price for the offeror’s promise”? In this example, the “price” for the offeror’s promise to sell the car is the offeree’s return promise to roof the offeror’s house.

Every contract has two considerations. If the contract is bilateral, the first consideration is the “price” in the offer for the offeror’s promise, and the second consideration is the “price” in the acceptance for the offeree’s promise.

Offer: “I promise to sell you my car for your promise to pay \$5,000.”

Offeror’s promise: “I promise to sell you my car.”

Consideration for the offeror’s promise: “Your promise to pay \$5,000.”

Acceptance of the offer: “I promise to pay \$5,000 for your promise to sell me your car.”

Offeree’s promise: “I promise to pay \$5,000.”

Consideration for the offeree’s promise: “Your promise to sell me your car.”

If the contract is unilateral, the first consideration is the “price” in the offer for the offeror’s promise and second consideration is the “price” in the acceptance for the offeree’s performance.

Offer: “I promise to sell you my car for your paying \$5,000.”

Offeror’s promise: “I promise to sell you my car.”

Consideration for the offeror’s promise: “Your paying \$5,000.”

Acceptance of the offer: “My paying \$5,000 for your promise to sell me your car.”

Offeree’s performance: “My paying \$5,000.”

Consideration for the offeree’s performance: “Your promise to sell me your car.”

For clarity, these two considerations will be distinguished by referring to “consideration for the offeror’s promise” and “consideration for the offeree’s promise” (if the offer is for a bilateral contract) or “consideration for the offeree’s performance” (if the offer is for a unilateral contract). The term “consideration” standing alone, will be used only when a general reference to consideration is made.

We have just made the point that “consideration” is an element in the offer and an element in the acceptance. An offer does not exist without “consideration for the offeror’s promise” and an acceptance does not exist without “consideration for the offeree’s promise or performance.” It is not uncommon, however, to find judicial opinions and texts that describe a contract as consisting of an offer, an acceptance, and consideration. Viewing consideration as a separate element is redundant since the concept of consideration has already been addressed—not once but twice—once when evaluating the offer and once when evaluating the acceptance. Therefore, this text will describe a contract as consisting of only an offer and an acceptance.

The following materials discuss five consideration-related problems:

- The promise to make a future gift;
- Adequacy of consideration;
- Motive as consideration;
- Moral obligation as consideration; and
- Sham consideration.

The Promise to Make a Future Gift. Early in the history of contracts law, the judges decided that some promises should be enforced while others should not be enforced. The promise of a future gift fell in the latter category. The only promise to make a gift that would be enforced would be that where the gift had already been made. That is, if a donor changed his or her mind and wanted the gift returned, the court would not require the gift already conveyed to be returned. On the other hand, a person who promised to make a gift in the future but who had not yet conveyed the gift would not be forced by the court to follow through with his or her promise.

A promise to make a future gift is a one-sided promise since it requests nothing in return for the promisor's promise. An offer, on the other hand, is more than a one-sided promise. An offer for a contract requires "something" in return for the promisor's promise. This "something" is the consideration or the "price" for the offeror's promise.

EXAMPLE 2-6

Gift Promise: "I promise to give you \$15,000."

Offer: "I promise to give you \$15,000 for your promise to give me your car."

In a commercial setting, most promisors seek something in exchange for their promises. If the transaction involves sale of goods, construction, or employment, there is always an exchange. Neither party to the transaction promises to give something for nothing. The promisor's motivation in making a promise may be quite different in the commercial world than it is in a family or interpersonal setting. In the family or interpersonal setting, the promisor may make a promise and not seek something in return. When a mother promises her daughter a weekly allowance of \$4 (with no strings attached) or a new dress for the spring dance, the mother is making nothing more than a promise of a future gift.

Adequacy of Consideration (the Peppercorn Theory of Contracts). The law of contracts does not concern itself with the size or value of the consideration. The court will not investigate whether the consideration sought

by the offeror is “adequate.” Adequacy of consideration is irrelevant. What is relevant is that there be some consideration, no matter how small. Consideration may be as small as a peppercorn, if that is what the offeror is bargaining to receive in exchange for his or her promise.

EXAMPLE 2-7

The following are offers since the adequacy of the consideration is irrelevant.

“I promise to sell you my car for your promise to pay \$15,000.”

“I promise to sell you my car for your promise to pay \$5,000.”

“I promise to sell you my car for your promise to pay \$500.”

“I promise to sell you my car for your promise to pay one peppercorn.”

As we all know, promises are not made to get peppercorns. Most contracts are performed, and the parties are satisfied with the results (or are not so dissatisfied that they will do anything more than grumble). In some cases, one party may feel that he or she has paid too much or received too little. At the time of contracting, the parties were free to design the contract to their own specifications. If, after the fact, one party feels dissatisfied with the terms to which he or she agreed, this is not the concern of the court. A judge will not evaluate whether one party received more under the contract than the other and will not evaluate the adequacy of the consideration.

Although the law recognizes something the size of a peppercorn as consideration, it does not recognize everything as potential consideration. “Love and affection” cannot serve as consideration. If “love and affection” were to be consideration, the entire concept of consideration would crumble because the distinction between a promise to make a future gift and a contract promise would no longer exist. All promises would have legal significance and could be enforceable regardless of whether they were intended as gifts.

EXAMPLE 2-8

The following is a gift promise and not an offer.

“I promise to give you my car since you are a loving niece.”

Motive as Consideration. Motive cannot be consideration for a promise. The offeror’s motive must be separated from the consideration for his or her promise.

Consider the following statement: “I promise to sell you my car for your promise to pay \$5,000.” The offeror’s motive for promising to sell her car might be to buy a newer car, to take a trip to Europe, to bury \$5,000 in a tin can in the backyard, to pay a hospital bill, or to bet on a horse. Whatever the motive or motives, and no matter how interesting or unique, motives are irrelevant. Although motive may explain why the offeror is doing or not doing something, what is relevant is that there be consideration for the offeror’s promise—what will be received by the offeror in return for his or her “promise to sell the car.”

In the following problems, identify the motive and determine whether consideration exists separate and apart from motive.

PARALEGAL EXERCISE 2.7 A budding sculptor, seeking public exposure for her work, promises to lend a large sculpture to the First Bank if First Bank will promise to exhibit it in its foyer for one year.

1. What is the sculptor’s motive or motives for promising to lend the sculpture to the Bank?
2. What is the consideration for the sculptor’s promise to lend the sculpture to the Bank?

PARALEGAL EXERCISE 2.8 A grandmother promises to pay her granddaughter’s tuition if the granddaughter will go to college.

1. What is the grandmother’s motive for her promise to pay her granddaughter’s tuition?
2. What is the consideration for the grandmother’s promise to pay the tuition?

PARALEGAL EXERCISE 2.9 Mary lost her wedding ring and placed an advertisement in the personal column of the local newspaper: “I promise to pay a \$400 reward to the person who finds and returns my diamond ring.”

1. What is Mary’s motive for making the promise to pay \$400?
2. What is the consideration for Mary’s promise to pay \$400?

Moral Obligation as Consideration. The fact that someone feels morally obligated to make a promise cannot be consideration for a promise. Moral obligation is not consideration. It is synonymous with motive and, as discussed in the preceding section, motive is not consideration.

EXAMPLE 2-9

Shortly after Allen became estranged from his mother, Allen's sister, Linda, promised him that if he were disinherited by their mother, Linda would give him half of their mother's estate. Prior to their mother's death, the mother executed a will that left her entire estate to Linda. When Allen sought to enforce Linda's promise to share their mother's estate, the court in *In re Estate of Poncin*, 1998 WL 8470 (Minn. App.) discussed whether Linda's promise suffered from a lack of consideration.

Appellant [Allen] concedes that there was no consideration given for respondent's [Linda's] statement. Consideration insures that a promise enforced as a contract is not "accidental, casual, or gratuitous" but has been made with "some deliberation, manifested by reciprocal bargaining or negotiation." *Cederstrand v. Lutheran Brotherhood*, 263 Minn. 520, 531, 117 N.W.2d 213, 220 (1962) (citation omitted). Promises that lack any consideration are "bare moral obligations, binding only on the conscience, a breach of which is not redressible in the courts." *Rask v. Norman*, 141 Minn. 198, 201-02, 169 N.W. 704, 706 (1918).

PARALEGAL EXERCISE 2.10 Mills nurses Wyman's emancipated son who is seriously ill. After Wyman's son dies, Wyman promises to reimburse Mills for any expenses incurred by Mills for this care. Because Wyman's son was emancipated, Wyman is under no legal obligation to reimburse Mills. Wyman has a change of heart and subsequently refuses to pay Mills. Mills claims that Wyman made an offer.

1. What was Wyman's motive in making his promise to reimburse Mills?
2. What was the consideration that Wyman requested in exchange for his promise to pay Mills?

Sham Consideration. **Sham consideration** is feigned or pretended consideration. Sham consideration is not consideration. The stated consideration for a promise may be a sham when the promisor is attempting to disguise the promise, which is intended as a future gift, to be a contract offer.

EXAMPLE 2-10

A father, intending to give his son a car as a gift, says to his son, "I promise to sell you my car for your promise to pay \$5,000." Because the father had no intention of receiving the \$5,000 payment but had clothed his promise of a future gift in offer apparel, the stated consideration for the father's promise ("your promise to pay \$5,000") is a sham and does not count as consideration.

Sham consideration relates to both adequacy of consideration and motive. Although a court will not investigate whether the consideration for a promise is adequate, the court might investigate whether the stated consideration is a sham. While motive will not be consideration, motive may play a role in determining whether the consideration stated is a sham.

The Offeror's Promise Must Be Made to Induce the Consideration

The third element of an offer is the glue that sticks the offeror's promise to the consideration for the offeror's promise. The offer anticipates a "bargained for exchange." The phrase "bargained for exchange" does not require hard bargaining with protracted negotiation. The requirement is that the offeror, by his or her promise, must be seeking the offeree's promise or performance (the consideration). The offeror's promise must be made to induce (entice) the consideration.

The following material explores three inducement problems: past consideration, pre-existing duty, and conditions.

Past Consideration. The past consideration problem is a timing issue. In an offer the offeror must make his or her promise to induce the offeree to promise or to perform. If the offeree has already promised or performed, the offeror would not be making his or her promise to induce the offeree to promise or perform.

The issue of past consideration more often occurs when the offeror is asking the offeree to perform rather than to promise. Therefore, a past consideration issue occurs when the offer is for a unilateral contract rather than for a bilateral contract.

PARALEGAL EXERCISE 2.11 Several months after Stan Hall was injured in an automobile accident, Stan learned that Mary Little had rendered first aid and that Mary's quick action probably saved his life.

Acting upon this information, Stan promised to pay Mary \$2,000 for saving his life.

1. What is the consideration for Stan's promise to pay Mary \$2,000?
2. Did Stan make his promise to induce Mary to render the consideration for his promise?

PARALEGAL EXERCISE 2.12 At his granddaughter's graduation, Granddad promises to pay her \$5,000 for graduating with honors.

1. What is the consideration for Granddad's promise to pay \$5,000?
2. Did Granddad make his promise to induce his granddaughter to render the consideration for his promise?

Pre-Existing Duty. Consideration for the offeror's promise must be free from obligation already owed to the offeror. If the offeree has a duty to perform that which the offeror is currently seeking to induce, the duty previously owed cannot be used as consideration for the offeror's new promise. The offeree is already committed to perform that duty.

EXAMPLE 2-11

Ron Armstrong has a three-year contract to play football for the Chicago Bears at \$1 million a year. Ron's performance during the first year under the contract was outstanding, and the Bears decided to increase his salary for the remaining two years of the contract. The Bears promised to pay Ron \$1,200,000 a year for his promise to play for them for the next two years. The consideration for the Bears' promise to pay Ron \$1,200,000 a year is his promise to play for them for the next two years. This promise to play for the Bears for the next two years is a promise to which Ron is already committed in his original contract. Therefore, his promise to play for the Bears for the next two years cannot be consideration for the Bears' promise to pay him \$1,200,000 a year.

Original contract:

Offer: "I promise to play for the Bears for three years for your promise to pay \$1 million a year."

Acceptance: "We promise to pay \$1 million a year for *your promise to play for the Bears for three years.*"

The attempt at renegotiating the contract:

Offer: "I promise to play for the Bears for the remaining two years for your promise to pay \$1.2 million a year."

Attempted acceptance: "We promise to pay \$1 million a year for *your promise to play for the Bears for the remaining two years.*"

If the source of the pre-existing duty comes from a contract and if the parties enter into a contract for mutual releases of their contractual duties, the parties no longer have pre-existing duties and may contract.

EXAMPLE 2-12

Original contract:

Offer: "I promise to play for the Bears for three years for your promise to pay \$1 million a year."

Acceptance: "We promise to pay \$1 million a year for *your promise to play for the Bears for three years.*"

Release contract:

Offer: "I promise to release you from your duty to pay \$1 million a year for your promise to release me from my duty to play for the Bears for the remaining two years of my contract."

Acceptance: "We promise to release you from your duty to play for the Bears for the remaining two years of your contract for your promise to release us from our duty to pay \$1 million a year."

Renegotiated contract:

Offer: "I promise to play for the Bears for the remaining two years for your promise to pay \$1.2 million a year."

Acceptance: "We promise to pay \$1.2 million a year for *your promise to play for the Bears for the remaining two years.*"

At the time of entering into the renegotiated contract, the player did not have a duty to play for the Bears for what would be the remaining two years of the original three-year term. Therefore, the promise to play for the Bears for the remaining two years could be consideration for the Bears' promise to pay \$1.2 million a year.

PARALEGAL EXERCISE 2.13 Singleton, a clothing designer, contracted to work for J. Smyth, Inc., a clothing manufacturer, for one year at \$1,000 a week. A short time later, Singleton was offered \$1,500 a week to work for a competitor. Upon hearing that they may be losing Singleton's services, J. Smyth offered to increase Singleton's salary to \$1,300 a week for the remainder of the contract term. Three months later, J. Smyth fired Singleton without cause. Singleton brought a breach of contract action against J. Smyth seeking damages based on \$1,300 a week. Answer the following questions:

1. What was the original offer by J. Smyth?
2. What was the consideration for J. Smyth's promise in that offer?
3. What was the new offer by J. Smyth?
4. What was the consideration for J. Smyth's promise in this new offer?
5. Was the consideration for J. Smyth's new promise the same as the consideration for J. Smyth's original promise?
6. Has J. Smyth made a new offer or is the consideration for J. Smyth's promise lacking due to Singleton's pre-existing duty?

PARALEGAL EXERCISE 2.14 Singleton, a clothing designer, contracted to work for J. Smyth, Inc., a clothing manufacturer, for one year at \$1,000 a week. A short time later, Singleton was offered \$1,500 a week to work for a competitor. Upon hearing that they may be losing Singleton's services, J. Smyth offered to rescind Singleton's original contract and to increase Singleton's salary to \$1,300 a week for the remainder of the contract term. Three months later, J. Smyth fired Singleton without cause. Singleton brought a breach of contract action against J. Smyth seeking damages based on \$1,300 a week. Answer the following questions:

1. What was the original offer by J. Smyth?
2. What was the consideration for J. Smyth's promise in that offer?
3. Did J. Smyth make an offer to rescind the original contract?
4. What was the consideration for J. Smyth's promise to rescind?

5. Was the consideration for J. Smyth's promise the same as the consideration for J. Smyth's original promise?
6. Have the parties entered into a rescission contract?
7. What was the third offer by J. Smyth?
8. What was the consideration for J. Smyth's promise in this new offer?
9. Was the consideration for J. Smyth's new promise the same as the consideration for J. Smyth's original promise?
10. Has J. Smyth made a new offer or is the consideration for J. Smyth's promise lacking due to Singleton's pre-existing duty?

Conditions vs. Consideration. The condition/consideration problem will occur only in situations when the offer is for a unilateral contract (promise for a performance) and not when the offer is for a bilateral contract (promise for a promise). Unlike the past consideration and pre-existing duty problems that are timing issues, the condition/consideration problem is a question of pure inducement. "Why did the offeror make his or her promise?" Was the offeror's motive to induce the offeree to perform or was the offeror's motive only to make the offeree a gift and the offeree had to put himself or herself into a position to receive the gift? In the former, the offeror is using his or her promise to entice the offeree's performance. Since the offeror's promise is being used to induce the offeree's performance, the offeree's performance is the consideration for the offeror's promise and the offeror is making an offer. In the latter, the offeror is not using his or her promise to entice the offeree's performance. The offeree, however, must perform in order to be in a position to receive the offeror's gift. Since the offeror's promise is *not* being used to induce the offeree's performance, the offeree's performance is *not* the consideration for the offeror's promise and the offeror is not making an offer. The offeror's motive, therefore, is the key to resolving the condition/consideration issue.

EXAMPLE 2-13

"I promise to give you \$5,000 if you refrain from smoking for one year." Why did the offeror make her promise? If the offeror is making her promise to get the offeree to stop smoking, the offeror is using her promise to induce the offeree to stop smoking. The "not smoking for one year" is the consideration for the offeror's promise to pay.

EXAMPLE 2–14

“I promise to give you a place to live if you move here.” Why did the offeror make her promise? If the offeror was trying to get the offeree to move, then “if you move here” is consideration for the offeror’s promise to give her a place to live. The offeror is using “the place to live” to induce the offeree to move there. If, however, the offeror did not care whether the offeree moved there or not but would provide her with a place to live if she did move, then “if you move here” is only a condition that the offeree must fulfill before she can partake in the offeror’s gift promise.

PARALEGAL EXERCISE 2.15 Professor Williston, in his treatise on Contracts (1 Williston on Contracts 445 (Jaeger 3d ed. 1957)), used the following illustration to demonstrate the difference between consideration and a condition: “[A] benevolent man says to a tramp,—‘If you go around the corner to the clothing store there, you may purchase an overcoat on my credit.’”

1. What is the benevolent man’s promise?
2. What was required of the tramp?
3. What was the benevolent man’s motivation in asking the tramp to “go around the corner to the clothing store”?
4. Was the benevolent man asking for an exchange (a promise to purchase a coat in exchange for the tramp’s walk), or did the benevolent man not seek an exchange but only that the tramp be in a position to receive the gift?

PARALEGAL EXERCISE 2.16 A father told his son that if the son would move back to town, the father would start him in business.

1. What was the father’s promise?
2. What did the father require the son to do?
3. Why did the father require the son to do this?
4. Is the father using his promise to induce the son to perform or does the father not really care whether the son performs?

ALTERNATIVES TO CLASSICAL CONSIDERATION

Under classical contracts law, consideration for the offeror's promise is an essential element of an offer. Without consideration, the offeror's promise is merely a promise to make a future gift and is unenforceable in court. Rigid adherence to this consideration doctrine in the past often led to unnecessarily harsh results. Modern contracts law employs several methods to rectify this. The first involves legislative and judicial tinkering with the classical doctrine. The second introduces reliance as an alternative to consideration. Both lead to the conclusion of offer and contract.

Tinkering with the Classical Doctrine

Both legislative bodies and courts tinker with the classical consideration doctrine. A legislature, by statute, may substitute a writing for consideration. A statute could take one of the following forms:

A written promise signed by the person promising is not unenforceable for lack of consideration.

A written promise signed by the person promising is not unenforceable for lack of consideration if the writing contains an express statement, in any form of language, that the signer intends to be legally bound.

Rather than substitute a writing, the legislature may alter the rule about which party has the burden of proving consideration. Traditional contracts law required the party introducing the contract to prove offer and acceptance, including the element of consideration for the offeror's promise. The following pair of statutes shifts the burden of proof from the party introducing the contract to the party challenging the contract. A number of states have this statutory pattern.

A written instrument is presumptive evidence of a consideration.

The burden of showing a want of consideration sufficient to support an instrument lies with the party seeking to invalidate or avoid it.

These illustrative statutes apply to all transactions. A legislature may, however, write with a finer pen. It may eliminate the need for consideration in a specific type of transaction rather than in all transactions. Article 2 of the Uniform Commercial Code, which has been enacted by the legislatures of all states except Louisiana, provides a good example. Article 2 deals with transactions involving a sale of goods. UCC § 2-209(1) provides:

(1) An agreement modifying a contract within this Article needs no consideration to be binding.

PARALEGAL EXERCISE 2.17 Describe how the legislature is tinkering with the classical consideration doctrine in the following statute. Does the statute apply to all types of contracts or only to a specific type of transaction? Does the statute dispense with the need for consideration, or does it merely substitute something in its place?

Every contract in writing hereafter made shall import a consideration in the same manner and as fully as sealed instruments have heretofore done.

PARALEGAL EXERCISE 2.18 Describe how the legislature is tinkering with the classical consideration doctrine in the following statute. Does the statute apply to all types of contracts or only to a specific type of transaction? Does the statute dispense with the need for consideration, or does it merely substitute something in its place?

An offer by a merchant to buy or sell goods in a signed writing which by its terms gives assurance that it will be held open is not revocable, for lack of consideration, during the time stated or if no time is stated for a reasonable time, but in no event may such period of irrevocability exceed three months; but any such term of assurance on a form supplied by the offeree must be separately signed by the offeror.

The legislatures have not been the only tinkers with the classical consideration doctrine. The courts, at times, also have been active. The following case, *Webb v. McGowin*, presents an excellent illustration. On August 3, 1925, Joe Webb, an employee of the W.T. Smith Lumber Company, was clearing the upper floor of a company mill by dropping the wood on that floor to the ground below. While Webb was in the act of dropping a seventy-five-pound pine block from the upper floor to the ground below, he saw J. Greeley McGowin standing on the ground below. Webb knew that he could remain safely on the upper floor of the mill and allow the block to drop, but the block would fall on McGowin and cause him serious injury or death. Webb chose to hold on to the block as it fell to the ground, thus diverting it from McGowin's direction. McGowin was saved, but Webb suffered serious bodily injuries that left him crippled for life. On September 1, 1925, McGowin promised to pay Webb \$15 every two weeks for the remainder of Webb's life for Webb's having prevented McGowin from sustaining death or serious bodily harm and for the injuries Webb received. The payments, made for almost nine years, were discontinued when McGowin died.

Webb sued McGowin's estate for breach of contract, and the estate responded by claiming a lack of consideration for McGowin's promise to pay. Webb's injury and saving of McGowin's life occurred before McGowin made his promise to pay Webb \$15 every two weeks. McGowin's promise to pay did not induce Webb to act.

The Court of Appeals of Alabama found in favor of Webb. In reading *Webb v. McGowin*, consider:

1. How does the court tinker with the classical consideration doctrine to resolve the timing problem? The problem with the classical consideration doctrine was that the consideration was performed before the offeror promised; therefore, the offeror's promise could not have been made to induce the offeree to perform.
2. Is the court's attempted analogy between a physician and a patient sound? Was relief in the physician-patient situation based on breach of contract?

We have discussed the inability of a moral obligation to serve as consideration. In *Webb v. McGowin*, the court linked moral obligation with a material benefit received by the offeror. The court stated that the moral obligation was the consideration for the offeror's promise (see paragraph number 2 in the court's opinion). Is this rationale acceptable?

The court referred to an alternative solution involving a prior legal or equitable obligation, which has become unenforceable, followed by subsequent promise to pay (see paragraph number 3). Is this rationale applicable to this case? Did McGowin have either a legal or equitable obligation to pay Webb before he made his promise to Webb?

Is the outcome acceptable? Is either rationale acceptable? If the outcome is acceptable but the rationale is not, suggest a better rationale. Could the promise to pay have occurred by implication when McGowin looked up and saw the block with his name on it, teetering on the edge of the upper floor of the mill?



CASE

Webb v. McGowin

Court of Appeals of Alabama, 1935. 27 Ala. App. 82, 168 So. 196, certiorari denied, 232 Ala. 374, 168 So. 199 (1936).

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.

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.

Where the promisee cares for, improves, and preserves the property of the promisor, though done without his request, it is sufficient consideration for the promisor's subsequent agreement to pay for the service, because of the material benefit received. *Pittsburg Vitrified Paving & Building Brick Co. v. Cerebus Oil Co.*, 79 Kan. 603, 100 P. 631; *Edson v. Poppe*, 24 S.D. 466, 124 N.W. 441, 26 L.R.A.(N.S.) 534; *Drake v. Bell*, 26 Misc. 237, 55 N.Y.S. 945.

In *Boothe v. Fitzpatrick*, 36 Vt. 681, the court held that a promise by defendant to pay for the past keeping of a bull which had escaped from defendant's premises and been cared for by plaintiff was valid, although there was no previous request, because the subsequent promise obviated that objection; it being equivalent to a previous request. On the same principle, had the promisee saved the promisor's life or his body from grievous harm, his subsequent promise to pay for the services rendered would have been valid. Such service would have been far more material than caring for his bull. 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.

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.

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.

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. *Lycoming County v. Union County*, 15 Pa. 166, 53 Am.Dec. 575, 579, 580; *Ferguson v. Harris*, 39 S.C. 323, 17 S.E. 782, 39 Am.St.Rep. 731, 734; *Muir v. Kane*, 55 Wash. 131, 104 P. 153, 26 L.R.A.(N.S.) 519, 19 Ann.Cas. 1180; *State ex rel. Bayer v. Funk*, 105 Or. 134, 199 P. 592, 209 P. 113, 25 A.L.R. 625, 634; *Hawkes v. Saunders*, 1 Cowp. 290; *In re Sutch's Estate*, 201 Pa. 305, 50 A. 943; *Edson v. Poppe*, 24 S.D. 466, 124 N.W. 441, 26 L.R.A.(N.S.) 534; *Park Falls State Bank v. Fordyce*, 206 Wis. 628, 238 N.W. 516, 79 A.L.R. 1339; *Baker v. Gregory*, 28 Ala. 544, 65 Am.Dec. 366. In the case of *State ex rel. Bayer v. Funk*, supra, the court held that a moral obligation is a sufficient consideration to support an executory promise where the promisor has received an actual pecuniary or material benefit for which he subsequently expressly promised to pay.

The case at bar is clearly distinguishable from that class of cases where the consideration is a mere moral obligation or conscientious duty unconnected with receipt by promisor of benefits of a material or pecuniary nature. *Park Falls State Bank v. Fordyce*, supra. Here the promisor received a material benefit constituting a valid consideration for his promise.

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 affirmation or ratification of the services rendered carrying with it the presumption that a previous request for the service was made. *McMorris v. Herndon*, 2 Bailey (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.

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

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.

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.

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.

Reliance as an Alternative to Consideration

Legislative and judicial tinkering have produced results in a crazy quilt fashion. Sometimes judicial tinkering has resolved only the dispute between a specific plaintiff and defendant. Legislative tinkering has been limited to certain types of transactions, such as sale of goods, or has distinguished written from unwritten promises. This tinkering has not produced a solution applicable to all transactions.

A solution that applies to all transactions is currently emerging in the courts. It is based on reliance as an alternative to consideration. The Restatement (Second) of Contracts § 90, entitled "Promise Reasonably Inducing Action or Forbearance," has become the focus for this movement:

(1) A promise which the promisor 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 binding if injustice can be avoided only by enforcement of the promise. The remedy granted for breach may be limited as justice requires.

The four elements of reliance as an alternative to consideration are:

- a promise by the promisor (offeror)
- the promisor should reasonably expect the promisee (offeree) to induce action or forbearance on the part of the promisee
- the promise does induce such action or forbearance and
- injustice can be avoided only by enforcement of the promise

The Restatement (Second) of Contracts § 90 makes the point that the "remedy granted for breach may be limited as justice requires." Since reliance substitutes for consideration, justice may require the remedy for breach of the offeror's promise be limited to compensation for the injury induced by the offeree's reliance on the offeror's promise. Courts, however, have paid little attention to this limitation and have given the offeree an expectation remedy. That is, the courts have given the remedy that would place the offeree in the position he or she would have been in had the contract been fully performed.

EXAMPLE 2–15

A father promised his twenty-two-year-old son \$20,000 when his son became twenty-five. The father knew that if he made the promise his son would probably purchase a new car. In anticipation of receiving \$20,000 at age twenty-five, the son spent \$17,000 on a new car, a purchase he would not have made if his father had not promised him the gift. When the son became twenty-five, the father refused to pay. Because the father's promise was for a future gift, there was no consideration for the father's promise, and it would not constitute an offer.

Since reliance is a substitute for consideration and the father's promise is enforceable, the question remains to what extent is the father's promise enforceable? Under § 90, the son would be entitled to a remedy that "may be limited as justice requires." Because the son's recovery is based on reliance, his remedy should be based on reliance as well. Therefore, the son's reliance interest should be protected, and he should recover for his injury suffered by relying—\$17,000 or less. In practice, however, the courts will tend to protect the son's expectation interest and place the son in the position he would have been in had the father's promise been fully performed—\$20,000.

The following two cases, *Ricketts v. Scothorn* and *Feinberg v. Pfeiffer Co.*, illustrate the use of reliance before and after the promulgation of Restatement of Contracts § 90. In *Ricketts*, a case involving the early evolution of the reliance doctrine, Miss Scothorn had been given a \$2,000 note by her grandfather. When her grandfather died and his executor refused to pay, Miss Scothorn sued to enforce his note.

1. Was the grandfather's promise really without consideration?
2. In looking for precedent, does the court agree with the rationale of the church and college cases that "the expenditure of money or assumption of liability by the donee on the faith of the promise constitutes a valuable and sufficient consideration"?
3. What rationale did the *Ricketts* court prefer?

The court used the phrase "equitable estoppel." Compare the elements for "equitable estoppel" in *Ricketts* with those set forth previously for reliance. In this context, equitable estoppel means the party challenging the lack of consideration for his or her promise is precluded from doing so because his or her promise induced the other party to rely to his detriment. If equitable estoppel is taken to its logical conclusion, the preclusion of the lack of consideration argument leaves the promise as if it had consideration and thus an offer. The offer forms a contract, and the contract is enforced as are all other contracts. Thus the nonbreaching party would be entitled to protection of his or her expectation, reliance, or restitution interests and not just his or her reliance interest. What interest did the *Ricketts* court protect?



CASE

Ricketts v. Scothorn

Supreme Court of Nebraska, 1898. 57 Neb. 51, 77 N.W. 365.

SULLIVAN, J. 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."

The material facts are undisputed. They are as follows: John C. 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 nine 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." 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 of 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. 121; *Johnston v. Griest*, 85 Ind. 503; *Fink v. Cox*, 18 Johns. 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 Or. 158; *Thompson v. Board*, 40 Ill. 379; *Irwin v. Lombard University*, 56 Ohio St. 9, 46 N.E. 63. 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 Iowa, 596, 33 N.W. 74, 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."

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. The judgment is right, and is affirmed.

In *Feinberg v. Pfeiffer Co.*, Mrs. Feinberg, a longtime employee of the Pfeiffer Company, was promised retirement income when she retired. Eighteen months later, Feinberg, relying on Pfeiffer's promise, retired. When Pfeiffer Company changed management and subsequently refused to pay, Mrs. Feinberg sued to enforce the company's promise.

1. Was the Pfeiffer Company's promise really without consideration?
2. Why does the court use the phrase "promissory estoppel" rather than "equitable estoppel"? Should the term "estoppel" even be used? Would "reliance" or "detrimental reliance" be a better term? Does the Restatement of Contracts § 90 use the term "estoppel"?
3. What is the rationale used by the *Feinberg* court to resolve the dispute? Does Feinberg's recovery protect her expectation or reliance interest?



CASE

Feinberg v. Pfeiffer Co.

Court of Appeals of Missouri, 1959. 322 S.W.2d 163.

DOERNER, Commissioner.

This is a suit brought in the Circuit Court of the City of St. Louis by plaintiff, a former employee of the defendant corporation, on an alleged contract whereby defendant agreed to pay plaintiff the sum of \$200 per month for life upon her retirement. A jury being waived, the case was tried by the court alone. Judgment below was for plaintiff for \$5,100, the amount of the pension claimed to be due as of the date of the trial, together with interest thereon, and defendant duly appealed.

The parties are in substantial agreement on the essential facts. Plaintiff began working for the defendant, a manufacturer of pharmaceuticals, in 1910, when she was but 17 years of age. By 1947 she had attained the position of bookkeeper, office manager, and assistant treasurer of the defendant.

. . . .

On December 27, 1947, the annual meeting of the defendant's Board of Directors was held at the Company's offices in St. Louis, presided over by Max Lippman, its then president and largest individual stockholder. The other directors present were George L. Marcus, Sidney Harris, Sol Flammer, and Walter Weinstock, who, with Max Lippman, owned 5,007 of the 6,503 shares then issued and outstanding. At that meeting the Board of Directors adopted the following resolution, which, because it is the crux of the case, we quote in full:

"The Chairman thereupon pointed out that the Assistant Treasurer, Mrs. Anna Sacks Feinberg, has given the corporation many years of long and faithful service. Not only has she served the corporation devotedly, but with exceptional ability and skill. The President pointed out that although all of the officers and directors sincerely hoped and desired that Mrs. Feinberg would continue in her present position for as long as she felt able, nevertheless, in view of the length of service which she has contributed provision should be made to afford her retirement privileges and benefits which should become a firm obligation of the corporation to be available to her whenever she should see fit to retire from active duty, however many years in the future such retirement may become effective. It was, accordingly, proposed that Mrs. Feinberg's salary which is presently \$350.00 per month, be increased to \$400.00 per month, and that Mrs. Feinberg would be given the privilege of retiring from active duty at any time she may elect to see fit so to do upon a retirement pay of \$200.00 per month for life, with the distinct understanding that the retirement plan is merely being adopted at the present time in order to afford Mrs. Feinberg security for the future and in the hope that her active services will continue with the corporation for many years to come. After due discussion and consideration, and upon motion duly made and seconded, it was—

"Resolved, that the salary of Anna Sacks Feinberg be increased from \$350.00 to \$400.00 per month and that she be afforded the privilege of retiring from active duty in the corporation at any time she may elect to see fit so to do upon retirement pay of \$200.00 per month, for the remainder of her life."

At the request of Mr. Lippman his sons-in-law, Messrs. Harris and Flammer, called upon the plaintiff at her apartment on the same day to advise her of the passage of the resolution. Plaintiff testified on cross-examination that she had no prior information that such a pension

plan was contemplated, that it came as a surprise to her, and that she would have continued in her employment whether or not such a resolution had been adopted. It is clear from the evidence that there was no contract, oral or written, as to plaintiff's length of employment, and that she was free to quit, and the defendant to discharge her, at any time.

Plaintiff did continue to work for the defendant through June 30, 1949, on which date she retired. In accordance with the foregoing resolution, the defendant began paying her the sum of \$200 on the first of each month. Mr. Lippman died on November 18, 1949, and was succeeded as president of the company by his widow. Because of an illness, she retired from that office and was succeeded in October, 1953, by her son-in-law, Sidney M. Harris. Mr. Harris testified that while Mrs. Lippman had been president she signed the monthly pension check paid plaintiff, but fussed about doing so, and considered the payments as gifts. After his election, he stated, a new accounting firm employed by the defendant questioned the validity of the payments to plaintiff on several occasions, and in the Spring of 1956, upon its recommendation, he consulted the Company's then attorney, Mr. Ralph Kalish. Harris testified that both Ernst and Ernst, the accounting firm, and Kalish told him there was no need of giving plaintiff the money. He also stated that he had concurred in the view that the payments to plaintiff were mere gratuities rather than amounts due under a contractual obligation, and that following his discussion with the Company's attorney plaintiff was sent a check for \$100 on April 1, 1956. Plaintiff declined to accept the reduced amount, and this action followed. Additional facts will be referred to later in this opinion.

Appellant's next complaint is that there was insufficient evidence to support the court's findings that plaintiff would not have quit defendant's employ had she not known and relied upon the promise of defendant to pay her \$200 a month for life, and the finding that, from her voluntary retirement until April 1, 1956, plaintiff relied upon the continued receipt of the pension installments. The trial court so found, and, in our opinion, justifiably so. Plaintiff testified, and was corroborated by Harris, defendant's witness, that knowledge of the passage of the resolution was communicated to her on December 27, 1947, the very day it was adopted. She was told at that time by Harris and Flammer, she stated, that she could take the pension as of that day, if she wished. She testified further that she continued to work for another year and a half, through June 30, 1949; that at that time her health was good and she could have continued to work, but that after working for almost forty years she thought she would take a rest.

We come, then, to the basic issue in the case. While otherwise defined in defendant's third and fourth assignments of error, it is thus succinctly stated in the argument in its brief: ". . . whether plaintiff has proved that she has a right to recover from defendant based upon legally binding contractual obligation to pay her \$200 per month for life."

It is defendant's contention, in essence, that the resolution adopted by its Board of Directors was a mere promise to make a gift, and that no contract resulted either thereby, or when plaintiff retired, because there was no consideration given or paid by the plaintiff. It urges that a promise to make a gift is not binding unless supported by a legal consideration; that the only apparent consideration for the adoption of the foregoing resolution was the "many years of long and faithful service" expressed therein; and that past services are not a valid consideration for a promise. Defendant argues further that there is nothing in the resolution which made its effectiveness conditional upon plaintiff's continued employment, that she was not under contract to work for any length of time but was free to quit whenever she wished, and that she had no contractual right to her position and could have been discharged at any time.

By the terms of the resolution defendant promised to pay plaintiff the sum of \$200 a month upon her retirement. . . .

Section 90 of the Restatement of the Law of Contracts states that: "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 doctrine has been described as that of "promissory estoppel," as distinguished from that of equitable estoppel or estoppel in pais, the reason for the differentiation being stated as follows:

"It is generally true that one who has led another to act in reasonable reliance on his representations of fact cannot afterwards in litigation between the two deny the truth of the representations, and some courts have sought to apply this principle to the formation of contracts, where, relying on a gratuitous promise, the promisee has suffered detriment. It is to be noticed, however, that such a case does not come within the ordinary definition of estoppel. If there is any representation of an existing fact, it is only that the promisor at the time of making the promise intends to fulfill it. As to such intention there is usually no misrepresentation and if there is, it is not that which has injured the promisee. In other words, he relies on a promise and not on a misstatement of fact; and the term 'promissory' estoppel or something equivalent should be used to make the distinction." Williston on Contracts, Rev.Ed., Sec. 139, Vol. 1.

In speaking of this doctrine, Judge Learned Hand said in *Porter v. Commissioner of Internal Revenue*, 2 Cir., 60 F.2d 673, 675, that "... 'promissory estoppel' is now a recognized species of consideration." . . .

Was there such an act on the part of plaintiff, in reliance upon the promise contained in the resolution, as will estop the defendant, and therefore create an enforceable contract under the doctrine of promissory estoppel? We think there was. One of the illustrations cited under Section 90 of the Restatement is: "2. A promises B to pay him an annuity during B's life. B thereupon resigns a profitable employment, as A expected that he might. B receives the annuity for some years, in the meantime becoming disqualified from again obtaining good employment. A's promise is binding."

At the time she retired plaintiff was 57 years of age. At the time the payments were discontinued she was over 63 years of age. It is a matter of common knowledge that it is virtually impossible for a woman of that age to find satisfactory employment, much less a position comparable to that which plaintiff enjoyed at the time of her retirement.

As the trial court correctly decided, such action on plaintiff's part was her retirement from a lucrative position in reliance upon defendant's promise to pay her an annuity or pension. In a very similar case, *Ricketts v. Scothorn*, 57 Neb. 51, 77 N.W. 365, 367, 42 L.R.A. 794, the Supreme Court of Nebraska said:

". . . 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 Commissioner therefore recommends, for the reasons stated, that the judgment be affirmed.

PER CURIAM.

The foregoing opinion by DOERNER, C., is adopted as the opinion of the court. The judgment is, accordingly, affirmed.

WOLFE, P.J., and ANDERSON and RUDDY, JJ., concur.

PARALEGAL EXERCISE 2.19 Marylou Maxwell, an honors student in high school, was offered a full tuition scholarship by Utopia College. Marylou turned down partial scholarships from other colleges so she could attend Utopia. After the second week of classes, Marylou was informed that Utopia could not honor its commitment to give her a full scholarship.

Did Utopia College make an offer to Marylou? What were the promisor’s promise and the consideration for the promisor’s promise?

If Utopia college did not extend an offer to Marylou because its promise lacked consideration, is there an alternative ground upon which she could recover? Could Marylou satisfy the four elements of reliance? Would she be entitled to protection of her expectation or reliance interest?

ALTERNATIVE CAUSES OF ACTION IF THERE IS NO OFFER

An offer requires an offeror’s promise—an unequivocal assurance that something will or will not be done. Without this unequivocal assurance, there can be no offer, no contract, no breach of contract action, and no remedy for breach of contract. If the parties walk away without there being a promise (an unequivocal assurance), neither could successfully maintain a breach of contract cause of action and claim injury to an expectation interest. A breach of contract action, however, is not the only action in this field. A reliance action and a restitution action may at times be available even if neither party made an unequivocal assurance.

The Role of Reliance as a Cause of Action When There Is No Promise (No Unequivocal Assurance)

If a party acts or refrains from acting because he or she is relying on the other party’s encouragement, a reliance interest comes into being even though no contract caliber promise (unequivocal assurance) has been made.

EXAMPLE 2–16

New World Corporation and Green Construction Company are negotiating for construction of a new production plant for New World. At this time, although neither has made an offer to the other, New World says to Green, "Although I am not ready to make you an offer now, you should buy a large earthmover so you can start work as soon as we contract." If Green buys the earthmover but New World never makes an offer, Green has suffered an injury by relying on New World's encouragement.

Although traditional contracts law emphasizes expectation interests, several cases in recent years have permitted recovery although the transaction never reached the promise (unequivocal assurance) phase. Because a contract had not been formed, recovery was based on reliance on statements made during preliminary negotiations rather than on the breach of a "contract promise."

The most famous case in this area, *Hoffman v. Red Owl Stores, Inc.*, was decided by the Wisconsin Supreme Court in 1965. Joseph Hoffman owned and operated a bakery in Wautoma, Wisconsin, where his success led him to consider expanding his operations to include a grocery store. With this in mind, he bought a small grocery store in Wautoma. A short time later, Hoffman contacted a Red Owl Representative to discuss establishing a Red Owl franchise store. After their initial negotiations, the following events took place:

- June 6, 1961: Hoffman sold his grocery store in Wautoma.
- Hoffman bought an option to buy a building site in Chilton.
- September 15, 1961: Hoffman exercised his option to buy the building site in Chilton by paying \$1,000 down.
- November 6, 1961: Hoffman sold his bakery business and bakery building in Wautoma.
- November 1961: Hoffman moved to Neenah and obtained employment at an Appleton bakery.

The first half of the following appellate court opinion chronicles the negotiations between Hoffman and various Red Owl representatives. Analyze this part of the opinion as follows:

1. Create a time line for the Hoffman/Red Owl negotiations by listing in chronological order each request made by the Red Owl representatives and each response made by Hoffman.
2. Beginning with the first request listed on the time line, decide whether that request constitutes an offer for the franchise.
3. When the relationship between the parties deteriorated and they walked away from each other, determine whether an offer for the franchise had been made or whether the parties were still in the preliminary negotiation phase of the transaction.

In the second half of the opinion, focus on Chief Justice Currie's statements for the court and answer the following questions:

1. When Hoffman was awarded a judgment against Red Owl, did the court base recovery on a breach of contract or on promissory estoppel?
2. Under the theory of recovery used by the court, was recovery intended to compensate Hoffman for an injury based on his expectation or for an injury suffered as a result of his reliance?
3. What did Hoffman need to prove to be entitled to a recovery under the cause of action used by the court?



CASE

Hoffman v. Red Owl Stores, Inc.

Supreme Court of Wisconsin, 1965.
26 Wis. 2d 683, 133 N.W.2d 267.

Action by Joseph Hoffman (hereinafter "Hoffman") and wife, plaintiffs, against defendants Red Owl Stores, Inc. (hereinafter "Red Owl") and Edward Lukowitz.

The complaint alleged that Lukowitz, as agent for Red Owl, represented to and agreed with plaintiffs that Red Owl would build a store building in Chilton and stock it with merchandise for Hoffman to operate in return for which plaintiffs were to put up and invest a total sum of \$18,000; that in reliance upon the above mentioned agreement and representations plaintiffs sold their bakery building and business and their grocery store and business; also in reliance on the agreement and representations Hoffman purchased the building site in Chilton and rented a residence for himself and his family in Chilton; plaintiffs' actions in reliance on the representations and agreement disrupted their personal and business life; plaintiffs lost substantial amounts of income and expended large sums of money as expenses. Plaintiffs demanded recovery of damages for the breach of defendants' representations and agreements.

The action was tried to a court and jury. The facts hereafter stated are taken from the evidence adduced at the trial. Where there was a conflict in the evidence the version favorable to plaintiffs has been accepted since the verdict rendered was in favor of plaintiffs.

Hoffman assisted by his wife operated a bakery at Wautoma from 1956 until sale of the building late in 1961. The building was owned in joint tenancy by him and his wife. Red Owl is a Minnesota corporation having its home office at Hopkins, Minnesota. It owns and operates a number of grocery supermarket stores and also extends franchises to agency stores which are owned by individuals, partnerships and corporations. Lukowitz resides at Green Bay and since September, 1960, has been divisional manager for Red Owl in a territory comprising Upper Michigan and most of Wisconsin in charge of 84 stores. Prior to September, 1960, he was district manager having charge of approximately 20 stores.

In November, 1959, Hoffman was desirous of expanding his operations by establishing a grocery store and contacted a Red Owl representative by the name of Jansen, now deceased. Numerous conversations were had in 1960 with the idea of establishing a Red Owl franchise store in Wautoma. In September, 1960, Lukowitz succeeded Jansen as Red Owl's representative in the negotiations. Hoffman mentioned that \$18,000 was all the capital he had available to invest and he was repeatedly assured that this would be sufficient to set him

up in business as a Red Owl store. About Christmastime, 1960, Hoffman thought it would be a good idea if he bought a small grocery store in Wautoma and operated it in order that he gain experience in the grocery business prior to operating a Red Owl store in some larger community. On February 6, 1961, on the advice of Lukowitz and Sykes, who had succeeded Lukowitz as Red Owl's district manager, Hoffman bought the inventory and fixtures of a small grocery store in Wautoma and leased the building in which it was operated.

After three months of operating this Wautoma store, the Red Owl representatives came in and took inventory and checked the operations and found the store was operating at a profit. Lukowitz advised Hoffman to sell the store to his manager, and assured him that Red Owl would find a larger store for him elsewhere. Acting on this advice and assurance, Hoffman sold the fixtures and inventory to his manager on June 6, 1961. Hoffman was reluctant to sell at that time because it meant losing the summer tourist business, but he sold on the assurance that he would be operating in a new location by fall and that he must sell this store if he wanted a bigger one. Before selling, Hoffman told the Red Owl representatives that he had \$18,000 for "getting set up in business" and they assured him that there would be no problems in establishing him in a bigger operation. The makeup of the \$18,000 was not discussed; it was understood plaintiff's father-in-law would furnish part of it. By June, 1961, the towns for the new grocery store had been narrowed down to two, Kewaunee and Chilton. In Kewaunee, Red Owl had an option on a building site. In Chilton, Red Owl had nothing under option, but it did select a site to which plaintiff obtained an option at Red Owl's suggestion. The option stipulated a purchase price of \$6,000 with \$1,000 to be paid on election to purchase and the balance to be paid within 30 days. On Lukowitz's assurance that everything was all set plaintiff paid \$1,000 down on the lot on September 15th.

On September 27, 1961, plaintiff met at Chilton with Lukowitz and Mr. Reymund and Mr. Carlson from the home office who prepared a projected financial statement. Part of the funds plaintiffs were to supply as their investment in the venture were to be obtained by sale of their Wautoma bakery building.

On the basis of this meeting Lukowitz assured Hoffman: " * * * [E]verything is ready to go. Get your money together and we are set." Shortly after this meeting Lukowitz told plaintiffs that they would have to sell their bakery business and bakery building, and that their retaining this property was the only "hitch" in the entire plan. On November 6, 1961, plaintiffs sold their bakery building for \$10,000. Hoffman was to retain the bakery equipment as he contemplated using it to operate a bakery in connection with his Red Owl store. After sale of the bakery Hoffman obtained employment on the night shift at an Appleton bakery.

The record contains different exhibits which were prepared in September and October, some of which were projections of the fiscal operation of the business and others were proposed building and floor plans. Red Owl was to procure some third party to buy the Chilton lot from Hoffman, construct the building, and then lease it to Hoffman. No final plans were ever made, nor were bids let or a construction contract entered. Some time prior to November 20, 1961, certain of the terms of the lease under which the building was to be rented by Hoffman were understood between him and Lukowitz. The lease was to be for 10 years with a rental approximating \$550 a month calculated on the basis of 1 percent per month on the building cost, plus 6 percent of the land cost divided on a monthly basis. At the end of the 10-year term he was to have an option to renew the lease for an additional 10-year period or to buy the property at cost on an installment basis. There was no discussion as to what the installments would be or with respect to repairs and maintenance.

On November 22nd or 23rd, Lukowitz and plaintiffs met in Minneapolis with Red Owl's credit manager to confer on Hoffman's financial standing and on financing the agency. Another projected financial statement was there drawn up entitled, "Proposed Financing For An

Agency Store." This showed Hoffman contributing \$24,100 of cash capital of which only \$4,600 was to be cash possessed by plaintiffs. Eight thousand was to be procured as a loan from a Chilton bank secured by a mortgage on the bakery fixtures, \$7,500 was to be obtained on a 5 percent loan from the father-in-law, and \$4,000 was to be obtained by sale of the lot to the lessor at a profit.

A week or two after the Minneapolis meeting Lukowitz showed Hoffman a telegram from the home office to the effect that if plaintiff could get another \$2,000 for promotional purposes the deal could go through for \$26,000. Hoffman stated he would have to find out if he could get another \$2,000. He met with his father-in-law, who agreed to put \$13,000 into the business provided he could come into the business as a partner. Lukowitz told Hoffman the partnership arrangement "sounds fine" and that Hoffman should not go into the partnership arrangement with the "front office." On January 16, 1962, the Red Owl credit manager teletyped Lukowitz that the father-in-law would have to sign an agreement that the \$13,000 was either a gift or a loan subordinate to all general creditors and that he would prepare the agreement. On January 31, 1962, Lukowitz teletyped the home office that the father-in-law would sign one or other of the agreements. However, Hoffman testified that it was not until the final meeting some time between January 26th and February 2nd, 1962, that he was told that his father-in-law was expected to sign an agreement that the \$13,000 he was advancing was to be an outright gift. No mention was then made by the Red Owl representatives of the alternative of the father-in-law signing a subordination agreement. At this meeting the Red Owl agents presented Hoffman with the following projected financial statement:

"Capital required in operation:		
"Cash		\$ 5,000.00
"Merchandise		20,000.00
"Bakery		18,000.00
"Fixtures		17,500.00
"Promotional Funds		1,500.00
	"TOTAL:	<u>\$62,000.00</u>
"Source of funds:		
"Red Owl 7-day terms		\$ 5,000.00
"Red Owl Fixture contract (Term 5 years)		14,000.00
"Bank Loans (Terms 9 years Union State Bank "of Chilton)		8,000.00
"(Secured by Bakery Equipment)		
"Other loans (Term No-pay) No interest "Father-in-law		13,000.00
"(Secured by None)		
"(Secured by Mortgage on "Wautoma Bakery Bldg.)		2,000.00
"Resale of Land		6,000.00
"Equity Capital: \$5,000.00-Cash		
"Amount owner has 17,500.00-Bakery Equip. "to invest:		<u>22,500.00</u>
	"TOTAL:	<u>\$70,500.00"</u>

Hoffman interpreted the above statement to require of plaintiffs a total of \$34,000 cash made up of \$13,000 gift from his father-in-law, \$2,000 on mortgage, \$8,000 on Chilton bank

loan, \$5,000 in cash from plaintiff, and \$6,000 on the resale of the Chilton lot. Red Owl claims \$18,000 is the total of the unborrowed or unencumbered cash, that is, \$13,000 from the father-in-law and \$5,000 cash from Hoffman himself. Hoffman informed Red Owl he could not go along with this proposal, and particularly objected to the requirement that his father-in-law sign an agreement that his \$13,000 advancement was an absolute gift. This terminated the negotiations between the parties.

The case was submitted to the jury on a special verdict with the first two questions answered by the court. This verdict, as returned by the jury, was as follows:

"Question No. 1: Did the Red Owl Stores, Inc. and Joseph Hoffman on or about mid-May of 1961 initiate negotiations looking to the establishment of Joseph Hoffman as a franchise operator of a Red Owl Store in Chilton? Answer: Yes. (Answered by the Court.)

"Question No. 2: Did the parties mutually agree on all of the details of the proposal so as to reach a final agreement thereon? Answer: No. (Answered by the Court.)

"Question No. 3: Did the Red Owl Stores, Inc., in the course of said negotiations, make representations to Joseph Hoffman that if he fulfilled certain conditions that they would establish him as a franchise operator of a Red Owl Store in Chilton? Answer: Yes.

"Question No. 4: If you have answered Question No. 3 'Yes,' then answer this question: Did Joseph Hoffman rely on said representations and was he induced to act thereon? Answer: Yes.

"Question No. 5: If you have answered Question No. 4 'Yes,' then answer this question: Ought Joseph Hoffman, in the exercise of ordinary care, to have relied on said representations? Answer: Yes.

"Question No. 6: If you have answered Question No. 3 'Yes' then answer this question: Did Joseph Hoffman fulfill all the conditions he was required to fulfill by the terms of the negotiations between the parties up to January 26, 1962? Answer: Yes.

"Question No. 7: What sum of money will reasonably compensate the plaintiffs for such damages as they sustained by reason of:

"(a) The sale of the Wautoma store fixtures and inventory?

"Answer: \$16,735.00.

"(b) The sale of the bakery building?

"Answer: \$2,000.00.

"(c) Taking up the option on the Chilton lot?

"Answer: \$1,000.00.

"(d) Expenses of moving his family to Neenah?

"Answer: \$140.00.

"(e) House rental in Chilton?

"Answer: \$125.00."

Plaintiffs moved for judgment on the verdict while defendants moved to change the answers to Questions 3, 4, 5, and 6 from "Yes" to "No", and in the alternative for relief from the answers to the subdivisions of Question 7 or a new trial. On March 31, 1964, the circuit court entered the following order:

"IT IS ORDERED in accordance with said decision on motions after verdict hereby incorporated herein by reference:

"1. That the answer of the jury to Question No. 7(a) be and the same is hereby vacated and set aside and that a new trial be had on the sole issue of the damages for loss, if any, on the sale of the Wautoma store, fixtures and inventory.

"2. That all other portions of the verdict of the jury be and hereby are approved and confirmed and all after-verdict motions of the parties inconsistent with this order are hereby denied."

Defendants have appealed from this order and plaintiffs have cross-appealed from paragraph 1. thereof.

CURRIE, Chief Justice.

The instant appeal and cross-appeal present these questions:

1. Whether this court should recognize causes of action grounded on promissory estoppel as exemplified by sec. 90 of Restatement, 1 Contracts?
2. Do the facts in this case make out a cause of action for promissory estoppel?
3. Are the jury's findings with respect to damages sustained by the evidence?

RECOGNITION OF A CAUSE OF ACTION GROUNDED ON PROMISSORY ESTOPPEL

Sec. 90 of Restatement, 1 Contracts, provides (at p. 110):

"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."

.

Many courts of other jurisdictions have seen fit over the years to adopt the principle of promissory estoppel, and the tendency in that direction continues. As Mr. Justice McFADDIN, speaking in behalf of the Arkansas court, well stated, that the development of the law of promissory estoppel "is an attempt by the courts to keep remedies abreast of increased moral consciousness of honesty and fair representations in all business dealings." *Peoples National Bank of Little Rock v. Linebarger Construction Company* (1951), 219 Ark. 11, 17, 240 S.W.2d 12, 16. For a further discussion of the doctrine of promissory estoppel, see 1A Corbin, *Contracts*, pp. 187, et seq., secs. 193–209; 3 *Pomeroy's Equity Jurisprudence* (5th ed.), pp. 211, et seq., sec. 808b; 1 *Williston, Contracts* (Jaeger's 3d ed.), pp. 607, et seq., sec. 140; Boyer, *Promissory Estoppel: Requirements and Limitations of the Doctrine*, 98 *University of Pennsylvania Law Review* (1950), 459; *Seavey Reliance Upon Gratuitous Promises or Other Conduct*, 64 *Harvard Law Review* (1951), 913; *Annos*. 115 A.L.R. 152, and 48 A.L.R.2d 1069.

The Restatement avoids use of the term "promissory estoppel," and there has been criticism of it as an inaccurate term. See 1A Corbin, *Contracts*, p. 232, et seq., sec. 204. On the other hand, *Williston* advocated the use of this term or something equivalent. 1 *Williston, Contracts* (1st ed.), p. 308, sec. 139. Use of the word "estoppel" to describe a doctrine upon which a party to a lawsuit may obtain affirmative relief offends the traditional concept that estoppel merely serves as a shield and cannot serve as a sword to create a cause of action. See *Utschig v. McClone* (1962), 16 *Wis.2d* 506, 509, 114 *N.W.2d* 854. . . . We have employed its use in this opinion not only because of its extensive use by other courts but also since a more accurate equivalent has not been devised.

Because we deem the doctrine of promissory estoppel, as stated in sec. 90 of Restatement, 1 *Contracts*, is one which supplies a needed tool which courts may employ in a proper case to prevent injustice, we endorse and adopt it.

APPLICABILITY OF DOCTRINE TO FACTS OF THIS CASE

The record here discloses a number of promises and assurances given to Hoffman by Lukowitz in behalf of Red Owl upon which plaintiffs relied and acted upon to their detriment.

Foremost were the promises that for the sum of \$18,000 Red Owl would establish Hoffman in a store. After Hoffman had sold his grocery store and paid the \$1,000 on the Chilton lot, the \$18,000 figure was changed to \$24,100. Then in November, 1961, Hoffman was assured that if the \$24,100 figure were increased by \$2,000 the deal would go through. Hoffman was induced to sell his grocery store fixtures and inventory in June, 1961, on the promise that he would be in his new store by fall. In November, plaintiffs sold their bakery building on the urging of defendants and on the assurance that this was the last step necessary to have the deal with Red Owl go through.

We determine that there was ample evidence to sustain the answers of the jury to the questions of the verdict with respect to the promissory representations made by Red Owl, Hoffman's reliance thereon in the exercise of ordinary care, and his fulfillment of the conditions required of him by the terms of the negotiations had with Red Owl.

There remains for consideration the question of law raised by defendants that agreement was never reached on essential factors necessary to establish a contract between Hoffman and Red Owl. Among these were the size, cost, design, and layout of the store building; and the terms of the lease with respect to rent, maintenance, renewal, and purchase options. This poses the question of whether the promise necessary to sustain a cause of action for promissory estoppel must embrace all essential details of a proposed transaction between promisor and promisee so as to be the equivalent of an offer that would result in a binding contract between the parties if the promisee were to accept the same.

Originally the doctrine of promissory estoppel was invoked as a substitute for consideration rendering a gratuitous promise enforceable as a contract. See Williston, *Contracts* (1st ed.), p. 307, sec. 139. In other words, the acts of reliance by the promisee to his detriment provided a substitute for consideration. If promissory estoppel were to be limited to only those situations where the promise giving rise to the cause of action must be so definite with respect to all details that a contract would result were the promise supported by consideration, then the defendants' instant promises to Hoffman would not meet this test. However, sec. 90 of Restatement, 1 *Contracts*, does not impose the requirement that the promise giving rise to the cause of action must be so comprehensive in scope as to meet the requirements of an offer that would ripen into a contract if accepted by the promisee. Rather the conditions imposed are:

1. Was the promise one which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee?
2. Did the promise induce such action or forbearance?
3. Can injustice be avoided only by enforcement of the promise?

We deem it would be a mistake to regard an action grounded on promissory estoppel as the equivalent of a breach of contract action. As Dean Boyer points out, it is desirable that fluidity in the application of the concept be maintained. 98 *University of Pennsylvania Law Review* (1950), 459, at page 497. While the first two of the above listed three requirements of promissory estoppel present issues of fact which ordinarily will be resolved by a jury, the third requirement, that the remedy can only be invoked where necessary to avoid injustice, is one that involves a policy decision by the court. Such a policy decision necessarily embraces an element of discretion.

We conclude that injustice would result here if plaintiffs were not granted some relief because of the failure of defendants to keep their promises which induced plaintiffs to act to their detriment.

DAMAGES

Defendants attack all the items of damages awarded by the jury.

Plaintiffs never moved to Chilton because defendants suggested that Hoffman get some experience by working in a Red Owl store in the Fox River Valley. Plaintiffs, therefore, moved to Neenah instead of Chilton. After moving, Hoffman worked at night in an Appleton bakery but held himself available for work in a Red Owl store. The \$140 moving expense would not have been incurred if plaintiffs had not sold their bakery building in Wautoma in reliance upon defendants' promises. We consider the \$140 moving expense to be a proper item of damage.

We turn now to the damage item with respect to which the trial court granted a new trial, i.e., that arising from the sale of the Wautoma grocery store fixtures and inventory for which the jury awarded \$16,735. The trial court ruled that Hoffman could not recover for any loss of future profits for the summer months following the sale on June 6, 1961, but that damages would be limited to the difference between the sales price received and the fair market value of the assets sold, giving consideration to any goodwill attaching thereto by reason of the transfer of a going business. There was no direct evidence presented as to what this fair market value was on June 6, 1961. The evidence did disclose that Hoffman paid \$9,000 for the inventory, added \$1,500 to it and sold it for \$10,000 or a loss of \$500. His 1961 federal income tax return showed that the grocery equipment had been purchased for \$7,000 and sold for \$7,955.96. Plaintiffs introduced evidence of the buyer that during the first eleven weeks of operation of the grocery store his gross sales were \$44,000 and his profit was \$6,000 or roughly 15 percent. On cross-examination he admitted that this was gross and not net profit. Plaintiffs contend that in a breach of contract action damages may include loss of profits. However, this is not a breach of contract action.

The only relevancy of evidence relating to profits would be with respect to proving the element of goodwill in establishing the fair market value of the grocery inventory and fixtures sold. Therefore, evidence of profits would be admissible to afford a foundation for expert opinion as to fair market value.

Where damages are awarded in promissory estoppel instead of specifically enforcing the promisor's promise, they should be only such as in the opinion of the court are necessary to prevent injustice. Mechanical or rule of thumb approaches to the damage problem should be avoided. In discussing remedies to be applied by courts in promissory estoppel we quote the following views of writers on the subject:

"The wrong is not primarily in depriving the plaintiff of the promised reward but in causing the plaintiff to change position to his detriment. It would follow that the damages should not exceed the loss caused by the change of position, which would never be more in amount, but might be less, than the promised reward." Seavey, *Reliance on Gratuitous Promises or Other Conduct*, 64 *Harvard Law Review* (1951), 913, 926.

At the time Hoffman bought the equipment and inventory of the small grocery store at Wautoma he did so in order to gain experience in the grocery store business. At that time

discussion had already been had with Red Owl representatives that Wautoma might be too small for a Red Owl operation and that a larger city might be more desirable. Thus Hoffman made this purchase more or less as a temporary experiment. Justice does not require that the damages awarded him, because of selling these assets at the behest of defendants, should exceed any actual loss sustained measured by the difference between the sales price and the fair market value.

Since the evidence does not sustain the large award of damages arising from the sale of the Wautoma grocery business, the trial court properly ordered a new trial on this issue.

Order affirmed. Because of the cross-appeal, plaintiffs shall be limited to taxing but two-thirds of their costs.

The *Hoffman* court derived the elements for promissory estoppel from section 90 of the Restatement (First) of Contracts (1932):

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.

After *Hoffman v. Red Owl* was decided, the American Law Institute, the drafters of the Restatements, revised the Restatement of Contracts. Restatement (Second) of Contracts includes section 90 in a slightly revised form:

(1) A promise which the promisor 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 binding if injustice can be avoided only by enforcement of the promise. The remedy granted for breach may be limited as justice requires.

How does the revision of section 90 change the three elements for promissory estoppel?

PARALEGAL EXERCISE 2.20 Pursuant to its decision to begin distributing its beer in Missouri, Adolph Coors Company, a Colorado corporation, created a distribution plan that divided Missouri into thirteen separate geographical areas. In August 1977, Coors released news reports requesting any person interested in becoming a Coors distributor to write the company requesting an application. Coors mailed formal applications and copies of Coors' "Basic Distributor Selection Guidelines" to Burst and approximately 1,600 other prospective applicants. Three hundred seventy-nine applications were completed and returned to Coors of which thirty-five, including Burst's, were for the Area No. 10 distributorship. Burst was one of four applicants selected for a field interview for Area No. 10 and the only one asked to Coors' headquarters for an in-house interview. However, on February 7, 1978, Burst received a letter notifying him that his application to become a Coors distributor had been rejected. Coors found none of the original applicants for Area No. 10 satisfactory and did not award the distributorship to any of them. Instead, Coors had Coors Distributing Company, a subsidiary, handle the distribution of its products until early 1979, when Coors awarded United City Distrib-

utors, which had not been one of the original thirty-five applicants, the distributorship for a part of original Area No. 10. Coors Distributing Company retained the remainder.

Based on the three elements for promissory estoppel (update the requirements so they relate to the Restatement (Second) of Contracts), should Burst prevail if he sues Coors? *Burst v. Adolph Coors Co.*, 650 F.2d 930 (8th Cir. 1981).

The Role of Restitution as a Cause of Action When There Is No Promise

Even though classical contracts law emphasized the expectation interest, it also recognized a restitution interest. The courts have protected the restitution interest by granting an injured party a restitution remedy in a breach of contract action. The courts also have created a cause of action for restitution, separate from an action for breach of contract.

A restitution cause of action is not based on a contract, neither one that is express (stated) nor one implied in fact (implied from the facts), but on the court's imagination. Over the years, the restitution cause of action has been referred to by various names: a contract implied by law, a contract implied in law, a constructive contract, a quasi-contract, and an implied contract (which means implied by law and not implied in fact). At times, a restitution action has also been referred to as an action for quantum meruit, although quantum meruit may also refer to a remedy for a breach of contract action. Quantum meruit means "as much as it is worth."

Restitution, the cause of action, is based on the policy of preventing "unjust enrichment." A restitution action requires:

- a benefit conferred by one party on another (the enrichment) and
- the retention of the benefit without compensating the party conferring the benefit would be unjust

Finding the enrichment is often relatively easy. The difficult question is determining whether it would be unjust to allow the benefit to be retained without compensating the party conferring the benefit.

A person who interferes in the affairs of another by conferring an unnecessary or unwanted benefit cannot successfully seek compensation for his or her interference. Such a person is officious, that is, a meddler.

The Comments to the Restatement explore the concept of officiousness:

- a. Officiousness means interference in the affairs of others not justified by the circumstances under which the interference takes place. Policy ordinarily requires that a person who has conferred a benefit either by way of giving another services or by adding to the value of his land or by paying his debt or even by transferring property to him should not be permitted to require the other to pay therefor, unless the one conferring the benefit had a valid reason for so doing. A person is not

required to deal with another unless he so desires and, ordinarily, a person should not be required to become an obligor unless he so desires.

The principle stated in this Section is not a limitation of the general principle stated in § 1 [“A person who has been unjustly enriched at the expense of another is required to make restitution to the other.”]; where a person has officiously conferred a benefit upon another, the other is enriched but is not considered to be unjustly enriched. The rule denying restitution to officious persons has the effect of penalizing those who thrust benefits upon others and protecting persons who have had benefits thrust upon them (see § 112). . . . Restatement of Restitution § 2, comment a (1937).

Using the following two steps, analyze Paralegal Exercises 2.21 through 2.27:

1. Focus on the benefit (the enrichment). Identify:
 - a. What was the benefit conferred?
 - b. Who conferred the benefit?
 - c. Upon whom was the benefit conferred?
2. Consider whether it would be unjust to permit the party receiving the benefit to retain it without compensating the party who conferred the benefit.

PARALEGAL EXERCISE 2.21 Last Christmas, Aunt Jane gave her niece Sylvia \$1,000 as a gift. Aunt Jane had hoped that Sylvia would use this money to further her education. Shortly after Christmas, Sylvia squandered \$600. Should Aunt Jane be entitled to restitution of the \$600 Sylvia spent? Should Aunt Jane be entitled to restitution of the remaining \$400?

PARALEGAL EXERCISE 2.22 When business was slow for the Quality Paving Company, employees would cruise neighborhoods in search of vacant houses with “For Sale” signs. If the driveway was in a state of disrepair, Quality would repave the drive and send a bill to the owner. Should Quality be entitled to restitution for the new driveway?

PARALEGAL EXERCISE 2.23 Under state statute, a father is required to provide support for his minor children. When Mr. Stephens failed to provide his minor son, Tommy, with adequate food and clothing, a neighbor fed and clothed the child. Is this neighbor entitled to restitution?

PARALEGAL EXERCISE 2.24 Would your answer to this problem be the same if a store instead of a neighbor had supplied the food and clothing?

PARALEGAL EXERCISE 2.25 Would your answer be the same if Mr. Stephens had been out of town and did not know that his son was improperly fed and clothed?

PARALEGAL EXERCISE 2.26 Would your answer be the same if the state had neither a common law nor a statutory rule requiring a father to support his minor children?

PARALEGAL EXERCISE 2.27 How should the following case be resolved?

The streetcar in which Harrison was riding was involved in an accident. Harrison was thrown from the streetcar with such force that he hit his head on the sidewalk and was rendered unconscious. A spectator summoned Dr. Wisdom, who had an office down the street. In an effort to save Harrison's life, Dr. Wisdom performed a difficult operation, but Harrison died without regaining consciousness.

Should Dr. Wisdom be entitled to recover in a restitution action against Harrison's estate?

If Dr. Wisdom should be compensated for the injury to his restitution interest, what factors are relevant in determining how much he should recover?



PARALEGAL CHECKLIST

The Offer Phase

- After all of the communications and events have been placed on a time line, the paralegal and the supervising attorney can use the following checklist to determine whether an offer has been made.
 1. Is the first communication an offer?
 - a. Use an objective (reasonable person) standard
 - b. Has the offeror, through the offer, created the power of acceptance in the offeree—was there promissory language and were no necessary terms left open for further negotiation?
 - If promissory language or necessary terms are missing, check the next communication. Is this communication an offer? Continue down the time line until a communication that creates the power to form a contract is found.
 - c. Use this strategy for determining whether a communication is an offer or a joke, or whether the setting is an advertisement or an auction.
 2. Does the communication have the elements of an offer—is there a promise by the offeror, consideration for the offeror's promise (the "price" for the offeror's promise), and has the offeror made his or her promise to entice the offeree to give the "price"?
 - a. The offeror's promise must be a promise—an unequivocal assurance that something will or will not be done.
 - (1) An illusory promise is not a promise because it is uncertain—something may or may not be done depending on whether the offeror feels like doing it.
 - (2) An indefinite promise is not a promise because it omits terms that the court must

consider when determining an appropriate remedy for breach of contract.

- b. The offer must contain consideration for the offeror's promise—what the offeror expects to receive for his or her promise.
 - (1) The consideration for the offeror's promise is the offeree's performance if the offer is for a unilateral contract. An offer for a unilateral contract is rarely made.
 - (2) The consideration for the offeror's promise is the offeree's promise if the offer is for a bilateral contract. The fact that the offeree's promise ultimately involves the offeree's performance does not change the promise into a performance.
- Motives, moral obligations, and shams do not qualify as consideration.
 - (1) Motive cannot be consideration for the offeror's promise. Consideration is *what* the offeror wants to get in return for his or her promise and not *why* the offeror wants to get it.
 - (2) Moral obligation cannot be consideration for the offeror's promise. Consideration is what the offeror wants to get in return for his or her promise and not the fact that the offeror feels obligated to promise.
 - (3) Sham consideration is pretended or phony consideration—the “price” that the offeror never intends to collect. Sham consideration is not consideration.
 - (4) Adequacy (sufficiency) of consideration is irrelevant because the courts will not be concerned with the size or value of the consideration. Something as small as a “peppercorn” can be consideration.
- c. The offeror's promise must be made to induce the stated consideration.
 - (1) Past consideration—a timing problem—cannot be consideration for the offeror's promise. The offeror's promise cannot be used to get something that already occurred.
 - (2) A pre-existing duty—a duty the offeree has already committed to perform cannot be consideration for the offeror's promise.

The offeror's promise is not being used to entice the offeree to perform. The offeree is already obligated to perform.
- (3) A condition to the offeror's promise cannot be consideration. The offeror's motive distinguishes whether the offeror is attempting to entice the offeree's performance by using his or her own promise or whether the offeree must perform to put himself or herself in the position to receive the offeror's performance of a gift promise.
 3. Is an alternative to classical consideration available if the offeror's promise lacks consideration?
 - a. Determine whether the legislature, by statute, has:
 - (1) substituted a writing for consideration;
 - (2) altered the rule about which party has the burden of proving consideration; or
 - (3) eliminated the consideration requirement in specific types of transactions.
 - b. Analyze whether the courts have:
 - (1) implied a promise thereby supplying consideration;
 - (2) implied a promise to correct a timing problem; or
 - (3) recognized the doctrine of promissory estoppel (detrimental reliance) to enforce a promise that lacks consideration. The elements of promissory estoppel are:
 - (a) a promise by the offeror;
 - (b) the offeror should reasonably have expected that the promise would induce action or forbearance on the part of the offeree;
 - (c) the promise did induce such action or forbearance; and
 - (d) injustice could be avoided only by the enforcement of the promise.
 4. Does an alternative cause of action exist if a “contract promise” (unequivocal assurance) is lacking?
 - a. Determine whether the courts have recognized a detrimental reliance cause of action. The elements are the same as for detrimental reliance as a substitute for consideration except the “promise” may be less than an unequivocal assurance.

- b. Review whether the courts have recognized a restitution (unjust enrichment) cause of action. The elements are:

- (1) a benefit conferred by one party on the other; and
- (2) the retention of the benefit without compensation would be unjust.

REVIEW QUESTIONS

DEFINE THE FOLLOWING NEW TERMS AND PHRASES

Auction with reserve	Offeror
Auction without reserve	Officious
Bilateral contract	Pre-existing duty
Condition	Preliminary negotiation
Consideration	Promise
Consideration for the offeree's promise or performance	Promisee
Consideration for the offeror's promise	Promisor
Gap filler	Promissory estoppel
Illusory promise	Reasonable person's standard
Indefinite promise	Reliance cause of action
Meeting of the minds	Restitution cause of action
Objective standard	Sham consideration
Offer	Subjective standard
Offeree	Unilateral contract
	Unjust enrichment

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

1. T F The pre-offer phase of a transaction may last for months or even years.
2. T F The pre-offer phase of a transaction is also known as preliminary negotiation.
3. T F Preliminary negotiation takes place after an offer has been made.
4. T F The Restatement (Second) of Contracts § 24 defines an offer as: the manifestation of willingness to enter into a bargain, so made as to justify another person in understanding that his assent to that bargain is invited and will conclude it.
5. T F Offer, as defined in the Restatement (Second) of Contracts § 24, is based on an objective standard rather than on a subjective standard.
6. T F The offeror, to create the power of acceptance in the offeree, must state the terms of the contract so nothing remains for the offeror to negotiate once the offeree assents to these terms.

7. T F An offer is a promise made by one party to another in exchange for the other's promise or performance.
8. T F An offer has three elements.
9. T F An offeror must make a promise for there to be an offer.
10. T F The consideration for the offeror's promise is also called the "price" for the offeror's promise and is part of a "bargained for exchange."
11. T F Consideration for the offeror's promise may be either the offeree's promise or performance, depending on which the offeror prefers.
12. T F An offer which is a "promise for a promise" is an offer for a unilateral contract.
13. T F A "manifestation of willingness" or a "demonstration of willingness" refers to the outward actions of the negotiating parties as understood by an impartial third person watching the parties.
14. T F The third person who is evaluating the outward actions of the negotiating parties is referred to as "the reasonable person."
15. T F The reasonable person standard is a subjective standard.
16. T F Early contracts cases used an objective standard.
17. T F Both the Restatement (First) and the Restatement (Second) of Contracts use an objective standard for the law of contracts.
18. T F An advertisement made to the general public may be an offer.
19. T F An advertisement may never be an offer.
20. T F An offer must always be made to a specific party.
21. T F In an auction "with reserve," the auctioneer is the offeror.
22. T F In an auction "with reserve," the auctioneer may withdraw the property at any time until he or she announces the completion of the sale.
23. T F Once a bidder had made a bid in an auction, he or she may not retract this bid.
24. T F A statement in an advertisement for an auction that says "the property will be offered to the highest bidder" means that the auction will be conducted "without reserve."
25. T F An auction is with reserve unless a contrary intention is apparent from a statute, court order, or advertisement or by an announcement at the beginning of the auction.
26. T F Sam Brown, the auctioneer, presented a Louis XV ormolu clock to the potential bidders at an auction. Susan Sanchez, the owner of this valuable antique clock, had told Sam not to sell it for less than \$5,000. In spite of Sam's best efforts, the highest bid was \$2,500. Sam could withdraw the clock from the auction.
27. T F A person with a secret (subjective) intent to make a joke while outwardly expressing (objective) intent to make an offer will be judged on his or her subjective intent.
28. T F Contract formation occurs upon acceptance of the offer.
29. T F If the offeror proposes a unilateral contract, the offeree must fully perform to accept the offer.

30. T F An illusory promise is an unequivocal assurance that something will or will not be done.
31. T F An indefinite promise contains all essential terms to allow the court, in the event of breach, to fashion a remedy.
32. T F The UCC may supply terms (gap fillers) omitted in the offer.
33. T F Consideration is the “price” that the offeror demands in return for his or her promise.
34. T F Every contract has not one but two considerations: one for the offeror’s promise and one for the offeree’s promise or performance.
35. T F The consideration for the offeror’s promise in the offer is the same as the offeree’s promise or performance in the acceptance.
36. T F The consideration for the offeree’s promise or performance in the acceptance is the same as the offeror’s promise in the offer.
37. T F The offeror’s promise to make a future gift lacks consideration and therefore cannot be an offer.
38. T F If a donor changes his or her mind, a gift that has already been made must be returned.
39. T F For an offer to exist, the consideration for the offeror’s promise must be adequate.
40. T F A “peppercorn” cannot be consideration for the offeror’s promise.
41. T F “I promise to pay you \$1,000 for your love and affection” is an offer.
42. T F “I promise to paint your barn for \$10” is an offer.
43. T F Motive can be consideration for a promise.
44. T F Moral obligation may be consideration for a promise.
45. T F An obligation already owed to the offeror (a pre-existing duty) may be consideration for the offeror’s promise.
46. T F If the offeree has already promised or performed (past consideration), the offeror would not be making his or her promise to induce a promise or performance and there would be no “bargained for exchange.”
47. T F Modern contract law allows a less rigid adherence to the classical consideration doctrine.
48. T F Reliance can never be an alternative to consideration.
49. T F Gloria VanFleet had a five-year contract to coach the Springfield Volunteers, a professional football team. During Gloria’s second year as coach, her team won its league championship. The owners were so delighted that they offered to replace Gloria’s contract with a new five-year contract at a 50% increase in salary. Gloria’s promise to coach for five years would be consideration for the owner’s promise to pay 50% more.
50. T F The restitution cause of action is based on the policy of preventing unjust enrichment.
51. T F The restitution cause of action is based on the fact that the offeree relied on the offeror’s promise to his or her detriment.
52. T F A restitution cause of action is based on a contract.

53. T F A restitution remedy in a breach of contract action is the same as a restitution cause of action.
54. T F *Quantum meruit* means “as much as it is worth.”
55. T F Under the Restatement of Restitution § 2 (1937), an officious person is one who is entitled to receive compensation for a benefit conferred upon another while serving in an official capacity.
56. T F An officious person is a meddler.
57. T F Restitution actions are often called contracts implied by law.
58. T F When negotiations end without one party making an offer, the parties are *always* free to walk away from each other without any obligation.
59. T F Restitution may be both a cause of action and a remedy.
60. T F Reliance may be both a cause of action and a remedy.
61. T F The elements for the reliance cause of action come from Restatement of Contracts § 90.
62. T F An express contract and an implied in fact contract are real contracts and may form the basis for a breach of contract action. A contract implied by law is not a real contract but rather a judicial construct and may form the basis for a restitution cause of action.
63. T F A person who is officious can recover in a restitution action for a benefit that he or she has conferred on another party.
64. T F When business was slow for the Quality Paving Company, employees would cruise neighborhoods in search of vacant houses with “For Sale” signs. If the driveway was in a state of disrepair, Quality would repave the drive and send a bill to the owner. Quality could not successfully maintain a restitution cause of action for compensation for the new driveway because Quality was officious.

FILL-IN-THE-BLANK QUESTIONS

- _____. A third person who is evaluating the outward actions of the negotiating parties.
- _____. The reasonable person standard.
- _____. Standard used in early contracts cases.
- _____. An auction in which the auctioneer is the offeror.
- _____. An auction in which the bidder is the offeror.
- _____. A contract that results from a promise for a performance.
- _____. A contract that results from a promise for a promise.
- _____. Terms that may be supplied by the UCC when they have been omitted in the contract.
- _____. The “price” that the offeror expects to receive for his or her promise.

10. _____. May sometimes be an alternative to consideration under modern contracts law.
11. _____. An unequivocal assurance that something will or will not be done.
12. _____. An equivocal assurance that something will or will not be done.
13. _____. "I promise to sell you my car if I feel like it."
14. _____. A promise that omits terms essential for the court to determine an appropriate remedy in the event the promise is breached.
15. _____. Feigned or pretended consideration.
16. _____. An obligation already owed to the offeror by the offeree.
17. _____. A cause of action based on the policy of preventing unjust enrichment.
18. _____. Preclusion of an assertion by the promisor that is inconsistent with a previously made promise upon which the promisee has relied.
19. _____. A figment of the court's imagination.
20. _____. A Latin expression meaning "as much as it is worth."
21. _____. A term used to describe what takes place when the plaintiff has conferred a benefit on the defendant and it would be unfair to permit the defendant to retain this benefit without compensating the plaintiff.
22. _____. A promise that is neither express nor implied in fact but is a legal fiction which represents the court's label attached to a set of facts to reach a desired result.
23. _____. A promise that is inferred from conduct rather than expressed orally or in writing.

MULTIPLE CHOICE QUESTIONS (CIRCLE ALL THE CORRECT ANSWERS)

1. The following statements are preliminary negotiation:
 - (a) "What will you take for your car?"
 - (b) "I will give you \$1,500 for your car."
 - (c) "Will you take \$1,500 for your car?"
 - (d) "Quote me a price for your car."
 - (e) "I will pay you no more than \$1,500 for your car."
2. Identify the offer in the following sequence of events.
 - (a) Please advise us of the lowest price you can make on our order for ten car loads of Mason green jars, complete, with caps, packed one dozen in a case, either delivered here, or f.o.b. cars your place, as you prefer. State terms and cash discount.

- (b) Replying to your letter, we quote you Mason fruit jars, complete, in one-dozen boxes, delivered to your place: pints \$4.50, quarts \$5.00, half gallons \$6.50, per gross, for immediate acceptance. Credit sixty days' trade acceptance or 2% off if cash in ten days. Your order subject to the approval of our executive officer.
 - (c) Your letter received. Enter order for ten car loads as per your quotation.
 - (d) Replying to your letter, price now pints \$5.00, quarts \$5.50, half gallon \$6.50, per gross, for immediate acceptance.
 - (e) Seller ships ten carloads to the Buyer.
3. Identify which of the following are offers for a unilateral contract.
- (a) "I promise to pay \$500 for your promise to sell me your gold watch."
 - (b) "I promise to pay \$500 for your selling me your gold watch."
 - (c) "I promise to sell you my gold watch for your promise to pay \$500."
 - (d) "I promise to sell you my gold watch for your paying me \$500."
 - (e) "I promise to pay you \$500 for your refraining from smoking for five years."
4. Identify which of the following is an offer.
- (a) "I may sell you my car for \$5,000."
 - (b) "I will sell you my car for \$5,000."
 - (c) "I will sell you one of my cars for \$5,000."
 - (d) "I might sell you my car for \$5,000."
 - (e) "I will consider selling you my car for \$5,000."
5. Identify which of the following is an offer.
- (a) "I promise to sell you my car."
 - (b) "I will sell you my car for your promise to pay \$5."
 - (c) "I promise to give you my car if you roof my house."
 - (d) "I will give you my car for your having roofed my house."
 - (e) "I will give you \$1,000 for your having taken care of me while I was ill."
6. Under classical contract law, the court will investigate the following:
- (a) whether there is consideration for the offeror's promise
 - (b) whether what appears to be consideration is really a sham
 - (c) whether there is mutuality of obligation
 - (d) whether the offeror's motive is appropriate
 - (e) whether the consideration is adequate
7. A restitution cause of action has also been known as a cause of action based upon:
- (a) a contract implied by law
 - (b) a constructive contract
 - (c) an express contract
 - (d) quasi-contract
 - (e) an implied contract

8. A cause of action for reliance may occur:
 - (a) when the parties have not negotiated
 - (b) when the parties have negotiated, but no offer has been made
 - (c) after an offer has been revoked
 - (d) after an offer has been rejected
 - (e) after an offer has been accepted
9. A restitution cause of action requires:
 - (a) a promise by the offeror
 - (b) a benefit must be conferred by one party on another
 - (c) the offeror reasonably expected to induce action or forbearance on the part of the other party
 - (d) the retention of the benefit without compensating the party conferring the benefit would be unjust
 - (e) injustice could be avoided only by enforcement of the promise
10. Anderson's car skidded off the highway during an ice storm and hit a tree. Anderson was knocked unconscious by the impact. McGill, a doctor of internal medicine, came upon the accident scene on her way home from making rounds at the local hospital. Dr. McGill rendered first aid at the scene and later sent Anderson a bill for her services. Anderson refused to pay claiming that he did not request her services.
 - (a) Dr. McGill could not successfully maintain either a breach of contract or a restitution cause of action against Anderson.
 - (b) Dr. McGill could successfully maintain a breach of contract action against Anderson but not a restitution cause.
 - (c) Dr. McGill could successfully maintain a restitution cause of action against Anderson but not a breach of contract cause of action.
 - (d) Dr. McGill could successfully maintain both a breach of contract cause of action and a restitution cause of action against Anderson.

SHORT ANSWER QUESTIONS

1. Describe the difference between evaluating a communication using an objective standard rather than a subjective standard.
2. Discuss the practical significance between an offer for a unilateral contract and an offer for a bilateral contract.
3. Discuss why past services cannot be consideration for the offeror's promise.
4. A father told his son that if the son would move back to town, the father would start him in business. Is the son's moving back to town consideration for the father's promise or only a condition?

5. Discuss several ways various legislatures have tinkered with the classical consideration doctrine.
6. Discuss several ways various courts have tinkered with the classical consideration doctrine.
7. List the four elements of the reliance doctrine necessary to enable it to be used as an alternative to consideration.
8. List the four elements for a cause of action for reliance.
9. Andrew Ricketts promised his granddaughter, Katie Scothorn, that he would give her a \$2,000 note that would bear 6% interest annually so she could stop working. Katie took the note and quit her job. After her grandfather died and his estate did not pay her, could Katie successfully sue the estate for breach of contract?
10. Describe the role of expectation when negotiations fail to produce an offer.
11. Describe the role of reliance when negotiations fail to produce an offer.
12. Describe the role of restitution when negotiations fail to produce an offer.
13. Are implied by law, implied in fact and implied contracts real contracts?
14. When is a person officious?



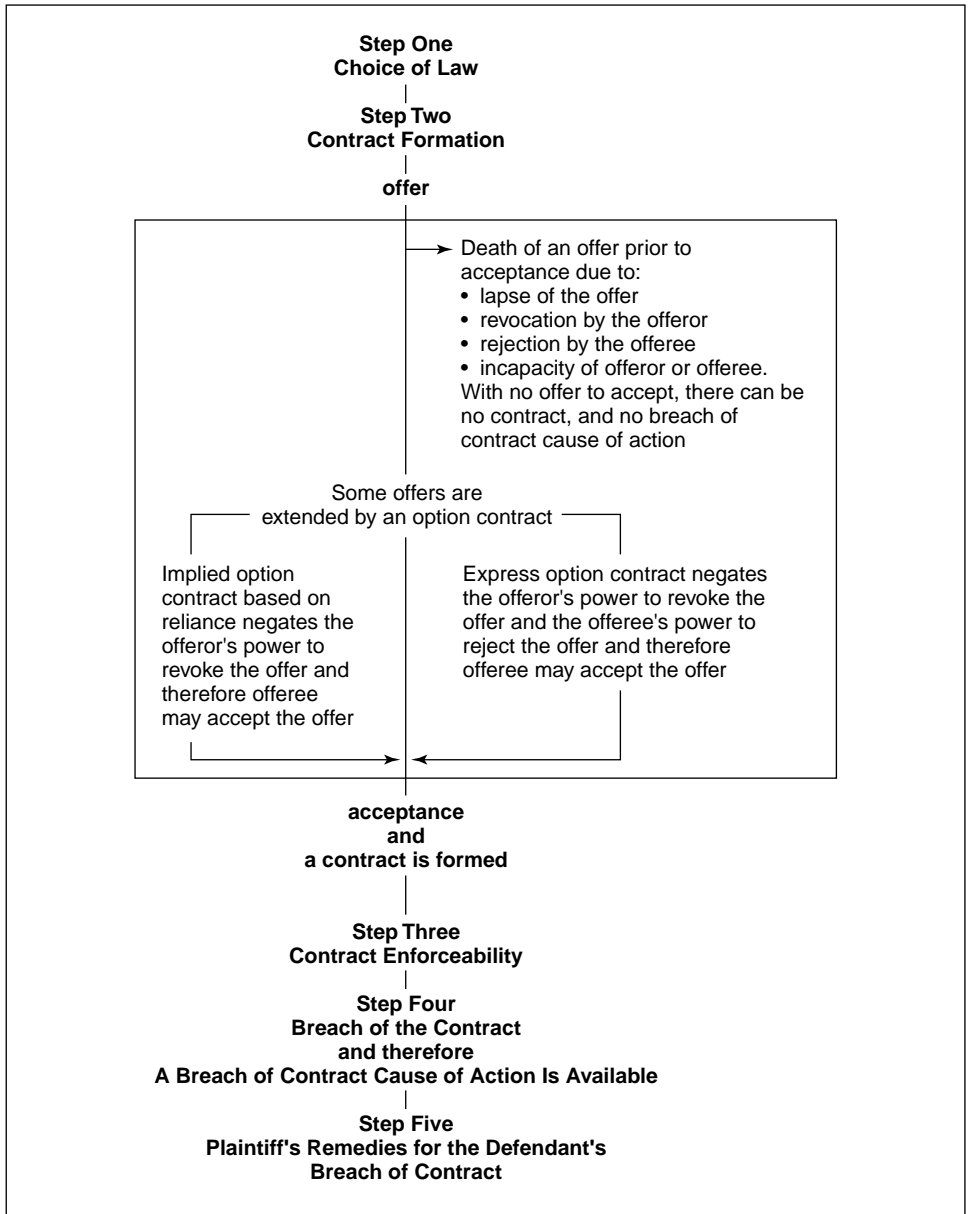
The Post-Offer/ Pre-Acceptance Phase

- ◆ The Death of an Offer Prior to Acceptance
 - Death of the Offer by the Offeree's Inaction (Lapse)*
 - Death of the Offer by Revocation of the Offer*
 - Death of the Offer by Rejection of the Offer*
 - Death of the Offer by the Death or Incapacity of the Offeror or the Offeree*
- ◆ The Offer That Refuses to Die
 - The Classical (Express) Option Contract*
 - The Implied Option Contract*

Chapter Three focuses on the time after the offer is made but before it is accepted. If the offer is accepted a contract is formed. If, however, the offeree does not accept the offer within the time specified in the offer, or if no time is specified and a reasonable time has passed, the offer will lapse. The offer may cease to exist if the offeror revokes the offer or the offeree rejects the offer. The death or incapacity of the offeror or offeree may also end the offer.

An offer may be kept open through a second contract called an option contract. Classical contract law recognized a subsidiary contract called an express option contract. Modern contract law has extended the option contract concept to recognize an implied option contract if the offeree to the main contract offer has relied on the offer (see Figure 3–1).

FIGURE 3-1 The Post-Offer/Pre-Acceptance Phase of the Road Map



THE DEATH OF AN OFFER PRIOR TO ACCEPTANCE

After the offeror has made an offer, thereby conferring the power of acceptance on the offeree, the offeree's power can be terminated in several ways:

- By the offeree's inaction so the offer lapses
- By the offeror's revocation of the offer
- By the offeree's rejection of the offer
- By death or incapacity of the offeror or offeree

Death of the Offer by the Offeree's Inaction (Lapse)

An offer may state an expiration time: "This offer will end at noon on Saturday, July 16th." Unless the offeree accepts by that time, the offer ceases to exist. A provision of this type gives the parties some certainty. The offeror knows that if the offeree fails to accept the offer before the specified time, the offeror is free to make other plans without informing the offeree. The offeree, on the other hand, knows there is only a limited time in which to decide to accept the offer. The offeree knows that the offer will lapse at the stated termination time and that the offeror may revoke the offer prior to that time.

PARALEGAL EXERCISE 3.1 Describe a situation in which the offeror would find it desirable to have an express termination date in the offer.

If the offer does not state a time by which the offer must be accepted, the offer will lapse if the offer is not accepted within a reasonable time. **Lapse**, therefore, is the termination of the offer through the offeree's failure to accept it within the time specified in the offer or if no time is specified then within a reasonable time. What is "a reasonable time" will vary with each transaction. One important factor in determining reasonable time is the subject matter of the contract.

EXAMPLE 3-1

An offeree should have a substantially shorter time to accept an offer to sell grapes than an offer to sell an encyclopedia.

PARALEGAL EXERCISE 3.2 Arrange the following four situations in time from the shortest "reasonable time" to the longest "reasonable time." None of the offers contains an express expiration time.

- An offer to sell Blackacre (100 acres of undeveloped farmland).
- An offer by the Ringling Brothers Circus to sell Sally, a trained elephant, to the Bumbling Brothers Circus.
- An offer to sell a truckload of vine-ripened tomatoes to Safeway Stores.
- An offer to buy a used automobile from the automobile's current owner.

Death of the Offer by Revocation of the Offer

The offeror may revoke an offer prior to the time it is accepted or lapses. As master of the offer, the offeror may terminate, as well as create, the power to accept.

Revocation is the offeror's manifestation to withdraw the offer. As a general rule, revocation is effective when received by the offeror. The Restatement (Second) of Contracts § 42 provides:

An offeree's power of acceptance is terminated when the offeree receives from the offeror a manifestation of an intention not to enter into the proposed contract.

Revocation does not require special language. The offeror need not say "revoke" to achieve a revocation. The only requirement for revocation is that it be clear to the offeree that the offer has been revoked.

The offeror may directly communicate to the offeree that the offer has been revoked. An example of direct communication is *Hoover Motor Express Co. v. Clements Paper Co.*

Analyze *Hoover Motor Express* as follows:

1. Record each event on a time line.
2. Determine whether the first event on the time line is an offer or preliminary negotiation.
3. Evaluate each subsequent event on the time line until the offer is reached.
4. Evaluate each subsequent event on the time line until the acceptance is reached.
5. Change the facts to weaken Hoover's assertion that its statement was a revocation.

CASE

Hoover Motor Express Co. v. Clements Paper Co.

Supreme Court of Tennessee, 1951. 241 S.W.2d 851.

TOMLINSON, Justice.

On November 19, 1949, the Hoover Motor Express Company delivered to the Clements Paper Company a written offer to purchase certain real estate. Although Williams, a Vice President at Clements, had been authorized in December to accept Hoover's offer, Williams believed that he would accept the offer unless he could negotiate a better deal. Williams did not, however, contact Hoover until January 13, 1950, when he spoke to Hoover



by telephone. On January 20, 1950, Clements made a written acceptance of Hoover's offer. Hoover refused to perform claiming that it had revoked its offer on January 13. Clements claimed that Hoover did not revoke its offer on January 13 but rather Clements had accepted Hoover's offer on January 20.

Clements sued Hoover for breach of contract and asked the Chancery Court for specific performance or damages. The Chancellor sided with Clements in holding that Hoover's offer had not been revoked on January 13. Hoover appealed to the Court of Appeals and that court affirmed the Chancellor's decree. Hoover petitioned for certiorari before the Supreme Court of Tennessee.

We join the Supreme Court of Tennessee's opinion as the court discusses Williams' testimony before the Chancellor.]

Mr. Williams testified that he got Mr. Hoover on the phone on January 13 and "told him that we were ready to go through with it and I would like to discuss it with him." The matter which he testifies that he wanted to discuss with Mr. Hoover was whether Hoover would permit Clements to retain an easement for certain purposes through the property which Hoover had offered to buy.

Williams testifies that in reply to Williams' statement that he, Williams, wanted to discuss the offer with Hoover that Hoover replied "Well, I don't know if we are ready. We have not decided, we might not want to go through with it."

Williams made several other statements in his testimony as to what Hoover said in this phone conversation. The following are quotations from Williams' testimony: "He said he thought they might not go through with it."

"Q. After you had talked to him on January 13, on the telephone, that is Mr. Eph Hoover, Jr., he indicated to you that he had made other plans or in some way 'indicated' to you that the company had made other plans?

A. Yes."

.....

"Q. You had been told that they had made other plans? A. No, I had not been told. He said that he didn't think they were going through with the proposal and that he would call me on January 17."

(Hoover did not call Williams after the January 13 phone conversation.)

.....

"A. That they had other plans in mind and he would let me know. He was not sure if he was going through with the original proposition."

"Q. Did he definitely refuse to positively commit himself on January 13 that he would go through with it? A. That is right."

.....

"It was a very short discussion. Frankly, I was very much shocked when I heard from him that they didn't plan to go through with it. I had made my plans and had gone to the extent of having this elevation made."

The interpretation which Mr. Williams placed upon what Hoover said to him in the phone conversation of January 13 is stated in Clements' bill of complaint as follows: "This was the first information, suggestion or intimation that complainant had received that the defendant would not or might not carry out its agreement or offer."

Our problem is reduced to answering the question as to whether there can reasonably be placed upon the above quoted testimony of Williams a construction that prevents the statement of Hoover, as testified to by Williams, from amounting to a withdrawal on January 13 of the offer before it was attempted on January 20 to accept it. This is true because "the continued existence of the offer until acceptance is, however, necessary to make possible the formation of the contract." 12 American Jurisprudence, page 531.

Although there is no Tennessee case deciding the point, in so far as we can find, the general rule is that express notice, in so many words, of withdrawal before acceptance of an offer of the character we have here is not required. In 55 American Jurisprudence, page 488, under a discussion of "Termination of Offer", there appears in the text, supported by reference to decisions, this statement: "It is sufficient to constitute a withdrawal that knowledge of acts by the offerer inconsistent with the continuance of the offer is brought home to the offeree."

Restatement of the Law of Contracts, Section 41, page 49, has this to say: "Revocation of an offer may be made by a communication from the offeror received by the offeree, which states or implies that the offeror no longer intends to enter into the proposed contract, if the communication is received by the offeree before he has exercised his power of creating a contract by acceptance of the offer."

Applying to the undisputed testimony as furnished by Williams the rule clearly stated in all the authorities from which we have above quoted—and we find none to the contrary—we think it must be concluded that Hoover's written offer of November 19 was withdrawn on January 13 thereafter prior to its attempted acceptance on January 20, and that the concurrent finding of the Chancellor and the Court of Appeals to the contrary is not supported by any material evidence. There can be no doubt as to it being a fact that on January 13 knowledge was brought home to Williams that Hoover no longer consented to the transaction. There was, therefore, no offer continuing up to the time of the attempted acceptance on January 20.

The decree of the Court of Appeals and of the Chancellor will be reversed and the cause remanded for entry of a decree in keeping with this opinion. All costs in all Courts will be adjudged against Clements Paper Company.

Revocation may also be indirectly communicated to the offeree if the offeror takes action inconsistent with her intention to enter into the proposed contract with the offeree and this information is "brought home" to the offeree before the offeree attempts to accept the offer.

EXAMPLE 3-2

On Monday, Mary offers to sell her house to Ted for \$250,000. The offer provides that it shall remain open until Saturday at noon. On Thursday, Ted learns from a reliable source that Mary has accepted Seymour's offer to pay \$275,000 for the house. Although Mary has not directly communicated to Ted that her offer to him has been revoked, the revocation has been indirectly communicated to Ted. Mary's offer to Ted has been revoked.

Although Mary said that her offer to Ted would "remain open until Saturday at noon," Mary's statement was no more than a time when the offer would lapse. Mary retained the power to revoke her offer and this power could be exercised at anytime prior to the time Ted accepted Mary's offer.

Death of the Offer by Rejection of the Offer

The offer will cease to exist when the offeree rejects it. **Rejection** is the offeree's manifestation of nonacceptance of the offer. The offeree may reject without making a new offer.

EXAMPLE 3-3

A-1 Used Cars does not post prices on its cars but has a big sign that reads: "Make us an offer." Tommy Thomas found a car that he liked on A-1's lot and made A-1 the following offer: "I promise to pay you \$1,200 for that red convertible." A-1 responded: "You must be kidding." A-1 has rejected Tommy's offer, and the parties no longer have an offer pending before them.

In addition to being a rejection, the offeree's rejection could include a new offer. In this case, the offeree's rejection is referred to as a counteroffer. A **counteroffer** is an offer made by the offeree to the offeror that deals with the subject matter of the original offer made by the offeror to the offeree but with some variation in terms. With a counteroffer the whole process of offer and acceptance begins again. The only difference is that the original offeree is now the offeror.

EXAMPLE 3-4

Consider the A-1/Tommy Thomas hypothetical again. This time A-1 responded: "No, but we will sell it to you for \$1,500." A-1 has rejected Tommy's offer and has made its own offer, now known as a counteroffer.

Once the offeree has rejected an offer, the offeree cannot accept the offer. The original offer can only be accepted if one of the parties resubmits the original offer and the other accepts it. Even though the original and the new offer are identical, the offeree technically accepts the new, not the original offer.

PARALEGAL EXERCISE 3.3 On December 5, the B & O Railroad wrote the following letter to Baltimore Rolling Mill: "Please quote me prices for 500 to 3,000 tons 50-pound steel rails and for 2,000 to 5,000 tons 50-pound iron rails."

On December 8, the Mill sent the following letter to B & O: "We do not make steel rails. For iron rails, we will sell 2,000 to 5,000 tons of 50-pound rails for \$54 per ton."

On December 16, B & O sent a letter to the Mill: "Please enter our order for 1,200 tons 50-pound iron rails."

On December 18, the Mill telegraphed B & O: "We cannot book your order at present at that price."

On December 19, B & O telegraphed the Mill: "Please enter an order for 2,000 tons 50-pound iron rails."

The Mill did not respond to B & O's telegram nor did it ship the rails.

Answer the following:

1. Was B & O's letter of December 5th preliminary negotiation or an offer?
2. Was the Mill's letter of December 8th preliminary negotiation, an offer, a rejection with a counteroffer, or an acceptance?
3. Was B & O's letter of December 16th preliminary negotiation, an offer, a rejection with a counteroffer, or an acceptance?
4. Was the Mill's telegram of December 18th preliminary negotiation, an offer, a rejection, a rejection with a counteroffer, an acceptance, or of no significance?
5. Was B & O's telegram of December 19th preliminary negotiation, an offer, a rejection, a rejection with a counteroffer, an acceptance, or of no significance?
6. Based on your answers, did B & O and the Mill have a contract, and if so, for what?

As a general rule, rejection is effective when received by the offeror. Since both the acceptance and the rejection are sent by the offeree, the offeree may, after sending one, have a change of mind and send the other. Thus an offeree may send a rejection and then an acceptance or send an acceptance and then a rejection. The offeror may not necessarily receive the communications in the order in which they were sent. The Restatement (Second) of Contracts § 40 not only deals with the general rule that a rejection is effective when received, but also with the acceptance that overtakes a previously sent rejection. The Restatement, however, does not resolve whether the rejection that overtakes a previously sent acceptance is effective, whether the acceptance is effective, or whether the rejection is effective only if the offeror relies on the rejection.

Rejection or counter-offer by mail or telegram does not terminate the power of acceptance until received by the offeror, but limits the power so that a letter or telegram of acceptance started after the sending of an otherwise effective rejection or counter-offer is only a counter-offer unless the acceptance is received by the offeror before he receives the rejection or counter-offer.

Often when the offeror has made an offer, the offeree may want to investigate whether the terms of the offer are negotiable. Can the offeree strike a better deal with the offeror? Once the offeror has made an offer, the offeree must use great care when probing for better terms. The offeree's probing may signal to the offeror that the offer is rejected. The test is not whether the offeror or the offeree perceived the offeree's response to be a rejection and counteroffer. What is important is whether a reasonable person would perceive the offeree's response to be a rejection and counteroffer.

EXAMPLE 3-5

Seller states to Buyer “I promise to sell you my car for \$15,000.” Buyer responds, “I will pay \$12,000 for your car.” Buyer is rejecting Seller’s offer and making a counteroffer.

PARALEGAL EXERCISE 3.4 Seller states to Buyer “I promise to sell you my car for \$15,000.”

1. Buyer responds, “Would you take \$12,000 for your car”? Is Buyer rejecting Seller’s offer and making a counteroffer?
2. Buyer responds, “I am considering your offer to sell me your car for \$15,000, but would you take \$12,000”? Is Buyer rejecting Seller’s offer and making a counteroffer?
3. Buyer responds, “I am not rejecting your offer to sell me your car for \$15,000, but would you take \$12,000”? Is Buyer rejecting Seller’s offer and making a counteroffer?

Death of the Offer by the Death or Incapacity of the Offeror or the Offeree

After an offer has been made but before the offeree has accepted (that is, before contract formation), either the offeror or the offeree may die or become legally incapacitated. Does the offeree still have the power to accept the offer and form a contract or has this power come to an end with the death or incapacity of the offeror? Does the offeree retain the power to accept the offer and form a contract or has this power come to an end with the death or incapacity of the offeree? The Restatement (Second) of Contracts § 48 answers both questions:

An offeree’s power of acceptance is terminated when the offeree or offeror dies or is deprived of legal capacity to enter into the proposed contract.

PARALEGAL EXERCISE 3.5 Mary Randolph, an artist of some renown, told Joan Scott: “I will sell you my latest landscape for \$25,000. Let me know by next Friday.” On Wednesday, while vacationing in the Caribbean, Mary was involved in a boating accident. Although Mary died that evening in a local hospital, the news of her death was not reported in the United States until the following Saturday. Meanwhile Joan, not knowing that Mary had died the previous evening, mailed a letter attempting to accept Mary’s offer. Joan even enclosed a \$25,000 check.

Has Joan effectively accepted Mary’s offer? Under the Restatement’s rule, must the offeree know that the offeror is dead for the attempted acceptance to be ineffective?

THE OFFER THAT REFUSES TO DIE

The offeree's power of acceptance need not be terminated by the offeror's attempted revocation, the offeree's attempted rejection, or the death or incapacity of the offeror or offeree. Some offers refuse to die. These offers are supported by a subsidiary contract—an option contract. An **option contract** is a contract that negates the offeror's power to revoke during the term of the option contract. Option contracts may be express or implied by law.

The Classical (Express) Option Contract

When an offeror makes an offer that creates in the offeree the power to accept, the offeror retains the power to revoke the offer. Under classical contracts law, the offeror may exercise this power at any time prior to acceptance by the offeree.

At times, it is important for the offeree to have time to evaluate the offer without being concerned that the offeror may revoke.

EXAMPLE 3-6

A real estate developer needs several months to evaluate whether a certain location now for sale would be well suited for commercial development.

EXAMPLE 3-7

An apartment tenant needs an apartment for a year and possibly for a longer period of time if she decides not to buy a house.

EXAMPLE 3-8

A professional soccer team wants to play in a stadium for a season and will want to play there for the following season if the team is successful at the gate.

PARALEGAL EXERCISE 3.6 Describe three additional situations where it would be advantageous for the offeree to have time to evaluate the offeror's offer, without having to be concerned with whether the offer may be revoked.

FIGURE 3–2 Option Contract Where the Offeror of the Main Contract Offer Is the Offeror in the Option Contract

<u>Main contract</u>	<u>Option contract (subsidiary contract)</u>
<p>Offer</p> <p>"I promise to sell you my car for your promise to pay me \$15,000"</p>	<p>Offer</p> <p>"I promise not to revoke my offer to sell you my car for \$15,000 for your promise to pay me \$100"</p> <p>Acceptance</p> <p>"I promise to pay you \$100 for your promise not to revoke your offer to sell me your car for \$15,000"</p>

The solution to the offeree's dilemma is for the offeree to buy the offeror's power to revoke. The offeree can do this with an option contract. The option contract is subsidiary to the main contract offer. Because the option contract is a contract, the option contract offer must have both a promise and consideration for that promise. The offeror of the option contract may be either the offeror or the offeree of the main contract offer.

If the offer for the option contract comes from the offeror of the main contract offer, the promise in the option offer is "I promise not to revoke my main contract offer." The consideration for this promise may be either the main contract offeree's promise or performance: "for your promise to pay . . ." or "for your paying. . ." The option contract offer would be "I promise not to revoke my main contract offer for your promise to pay . . ." or "I promise not to revoke my main contract offer for your paying me. . ." (see Figure 3–2).

If the offer for the option contract comes from the offeree of the main contract offer, the promise in the option offer is "I promise to pay. . ." The consideration for this promise is the main contract offeror's "promise not to revoke his or her main contract offer." The option contract offer would be "I promise to pay . . . for your promise not to revoke your main contract offer." (see Figure 3–3).

Although a main contract offer and an option contract offer are often made at the same time, the consideration in the option contract offer and acceptance must not be the same as the consideration in the main contract offer. If the main contract offer is "I promise to sell you my car for your promise to pay \$15,000," and the option contract offer is "I promise not to revoke my main contract offer for your promise to pay \$100," the offeree's promise to pay \$100 in the option contract offer must not be a part of the offeree's promise to pay \$15,000 in the main contract offer. The need for unrelated consideration is apparent when the offer for the option contract is spelled out in full: "I promise not to revoke my offer to sell you my car for your promise to pay \$15,000 for your promise to pay me \$100." Because the purpose of the option contract is to

FIGURE 3–3 Option Contract Where the Offeree of the Main Contract Offer Is the Offeror in the Option Contract

<u>Main contract</u>	<u>Option contract (subsidiary contract)</u>
<p>Offer</p> <p>"I promise to sell you my car for your promise to pay me \$15,000"</p>	<p>Offer</p> <p>"I promise to pay you \$100 for your promise not to revoke your offer to sell me your car for \$15,000"</p> <p>Acceptance</p> <p>"I promise not to revoke my offer to sell you my car for \$15,000 for your promise to pay me \$100"</p>

provide the offeree time to evaluate the main contract offer, it is only the offer for the option contract that is accepted at this time. It is "the promise to pay \$100" and not "the promise to pay \$15,000."

What at first may appear to be an option contract may only be the time after which the offer will lapse.

EXAMPLE 3–9

The main contract offer is "I promise to sell you my car for your promise to pay \$15,000 and I will not revoke my offer for 15 days." There is no consideration for the offeror's promise not to revoke for 15 days and therefore the 15 days is the time when the offer will lapse. Without an option contract the offeror retains the power to revoke the offer at any time.

EXAMPLE 3–10

The main contract offer is "I promise to sell you my car for your promise to pay \$15,000 and I will not revoke my offer for 15 days for your promise to pay \$100." The promise to pay \$100 is consideration for the offeror's promise not to revoke for 15 days. If the offeree promises to pay \$100 for the offeror's promise not to revoke, an option contract is created and the offeror cannot revoke the main contract offer for 15 days. The 15 days no longer represents the time when the offer will lapse. The offer will lapse after a reasonable time with the minimum time being 15 days.

Once the offer for the option contract has been accepted, the option contract is formed, and the offeror no longer has the power to revoke the main contract offer.

EXAMPLE 3–11

Main contract offer

I promise to sell you Blackacre for your promise to pay \$250,000.

Option contract offer

I promise not to revoke my offer to sell you Blackacre for \$250,000 for thirty days for your promise to pay me \$100.

Option contract acceptance

I promise to pay you \$100 for your promise not to revoke for thirty days your offer to sell me Blackacre for \$250,000.

For the next thirty days, the offeror may not revoke the original offer to sell Blackacre to the offeree for \$250,000.

PARALEGAL EXERCISE 3.7 David promised to sell his *Mad* magazine collection to Mary Jane for \$200. When can David sell his *Mad* magazine collection to Darron for \$300 without being in breach of contract with Mary Jane?

PARALEGAL EXERCISE 3.8 David promised to sell his *Mad* magazine collection to Mary Jane for \$200. Mary Jane paid David \$10 for a three-month option contract. When can David sell his *Mad* magazine collection to Darron for \$300 without being in breach of contract with Mary Jane?

Not only will an express option contract negate the offeror's power to revoke, it also affects rejection and death or incapacity of the offeror. The Restatement (Second) of Contracts § 37 provides:

[T]he power of acceptance under an option contract is not terminated by rejection or counter-offer, by revocation, or by death or incapacity of the offeror. . . .

EXAMPLE 3–12

On June 1st, Seller offers to sell her car to Buyer for \$15,000. Also on June 1st, Seller promises not to revoke her offer to sell for 30 days for Buyer's promise to pay \$100 and Buyer promises to pay \$100, thus forming an option contract. On June 15th, Buyer offers to buy Seller's car for \$12,000. On June 20th, Seller rejects Buyer's counteroffer. On June 25th, Buyer accepts Seller's offer of June 1st.

Because of the option contract, Buyer's counteroffer of June 15th did not reject Seller's offer of June 1st. Therefore, on June 25th when Buyer accepted Seller's offer of June 1st, a contract was formed.

EXAMPLE 3–13

On June 1st, Seller offers to sell her car to Buyer for \$15,000. Also on June 1st, Seller promises not to revoke her offer to sell for 30 days for Buyer's promise to pay \$100 and Buyer promises to pay \$100, thus forming an option contract. On June 15th, Seller died. On June 25th, Buyer accepts Seller's offer of June 1st.

Because of the option contract, Seller's death did not terminate Buyer's power to accept so on June 25th when Buyer accepted Seller's offer of June 1st, a contract was formed.

PARALEGAL EXERCISE 3.9 Why does the Restatement (Second) of Contracts § 37 address the death or incapacity of the offeror but not the death or incapacity of the offeree?

The Restatement (Second) of Contracts § 63(b) provides that an offer of an option contract is accepted when received by the offeree:

Unless the offer provides otherwise,

. . .

(b) an acceptance under an option contract is not operative until received by the offeror.

The Implied Option Contract

If the offeror enters into an express option contract, the offeror may not revoke the main contract offer for the duration of the option contract. This protects the offeree from the offeror's change of heart. But what if the offeror and offeree have not entered into an express option contract? It is common for the offeree, without having accepted the offeror's main contract offer, to change his or her conduct in reliance on that offer. Will this reliance create an implied option contract? The analysis will differ depending on whether the main contract offer was for a unilateral or bilateral contract.

In an offer for a unilateral contract, the offer is "I promise for your performance." This type of offer (a promise for a performance) can only be accepted by the offeree's performance. Because the offeror has asked the offeree to accept by performing (and not by promising), a promise by the offeree is ineffective as acceptance.

The offeree is required to perform in full in order to accept the offer. Beginning the performance is not full performance any more than almost completing the performance is full performance. If the offeror has the power to revoke and may exercise this power at any time prior to acceptance, the offeree may begin the requested performance only to have the offeror revoke the offer prior to the offeree's full performance. Therefore, all offers for a unilateral contract would place the offeree at risk.

EXAMPLE 3–14

Farmer Jones promised to pay Simon \$1,000 for painting Farmer Jones's barn. Simon began to paint and completed three sides of the barn when Farmer Jones walked up to Simon and said, "Mighty nice job, Simon, but I revoke my offer." Because the offer was a promise for a performance, Simon could accept only by performing in full, that is, painting all four sides of the barn. Painting three sides was not full performance, and the offeror could revoke prior to Simon's having fully performed. Simon did not have an express option contract that would prevent Farmer Jones from revoking his offer. Without an offer and an acceptance, Simon could not successfully sue Farmer Jones under classical contract theory for a breach of contract.

The Restatement (Second) of Contracts § 45 came to the aid of the Simons of the world with an implied option contract:

(1) Where 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.

(2) The offeror's duty of performance under any option contract so created is conditional on completion or tender of the invited performance in accordance with the terms of the offer.

Under section 45, when the offeree begins the performance requested by the offeror under the main contract offer, an implied option contract is created that deprives the offeror of the power to revoke the main contract offer. Technically, the offeree's beginning of the performance is the consideration for the offeror's implied promise not to revoke. The implied option contract exists long enough for the offeree to have an opportunity to complete the performance requested in the main contract offer. Upon completion, the offeree accepts the main contract offer, and a contract is formed.

If section 45 were operative in the Farmer Jones illustration, Farmer Jones's attempted revocation would be ineffective. When Simon began to paint the barn, an implied option contract came into being. During the life of the option contract, the offeror was powerless to revoke the main contract offer. If Simon painted the last side of the barn, he would have completed the requested performance and thus accepted the offer. He could successfully maintain a breach of contract action if Farmer Jones refused to pay the contract price.

In an offer for a bilateral contract, the offer is "I promise for your promise." This type of offer can only be accepted by the offeree's promise to do or not do what the offeror requested. The offeree's promise may be express or implied from the offeree's conduct. Unlike the offer for a unilateral contract, which requires full performance by the offeree to constitute acceptance of the offer, the offeree in an offer for a bilateral contract has a rapid and easy method of acceptance—simply promise. If the offeree begins to perform without expressly promising the offeror, a promise implied from the offeree's performance constitutes acceptance of the offer. The problem generally is not with the offeree's beginning the performance requested by the offeror but preparing to begin the performance.

EXAMPLE 3–15

Consider Farmer Jones again. This time, Farmer Jones promised to pay Simon \$1,000 if Simon promised to paint Farmer Jones's barn. Simon did not respond to Farmer Jones but bought paint and brushes for the job. Before Simon told Farmer Jones that he promised to paint or before he started painting, Farmer Jones wrote Simon stating, "I revoke my offer." Because the offer has not been accepted and because Simon did not have an express option contract, Farmer Jones could revoke because the attempted revocation occurred prior to Simon's attempted acceptance. Without an acceptance, Simon could not successfully sue Farmer Jones in classical contract theory for breach of contract.

Section 45 of the Restatement (Second) of Contracts was not designed to give the Simons of the world any help in this situation. Section 45 only applies to an offer for a unilateral contract. Farmer Jones's offer was for a bilateral contract. The Restatement (Second) of Contracts § 87(2) was created to address the offer for a bilateral contract:

(2) An offer which the offeror should reasonably expect to induce action or forbearance of a substantial character on the part of the offeree before acceptance and which does induce such action or forbearance is binding as an option contract to the extent necessary to avoid injustice.

Section 87(2) provides that once the offeree either begins preparation or begins performance as defined by the terms of the offer, an implied option contract is created.

EXAMPLE 3–16

When Simon bought the paint and brushes, an implied option contract was created with the beginning of the preparation acting as the consideration for the offeror's implied promise not to revoke. Simon would have a reasonable time to promise Farmer Jones.

The language of section 87(2) is not limited to the offer for a bilateral contract. Its language encompasses both offers for bilateral and unilateral contracts. By using preparation as the time for implying the option contract, section 87(2) creates the option contract at an earlier point than section 45.

EXAMPLE 3–17

Under section 87(2), Simon's purchase of paint brushes acts as consideration for the offeror's implied promise not to revoke. Simon would have the opportunity to perform fully if the offer were for a unilateral contract or to promise to perform if the offer were for a bilateral contract.

PARALEGAL EXERCISE 3.10 Aunt Martha wrote her niece Ellen, “I promise to leave you Blackacre in my will if you live with and care for me for the remainder of my life.” Aunt Martha attempts to revoke her offer while Ellen is preparing to move so she could live with and care for Aunt Martha (i.e., Ellen is preparing to perform the requested performance and has not begun to perform the requested performance). Could Ellen successfully maintain a breach of contract action against Aunt Martha using:

1. classical contract theory (which requires an express option contract to negate Aunt Martha’s power to revoke her offer);
2. Restatement (Second) of Contracts § 45; or
3. Restatement (Second) of Contracts § 87(2)?

PARALEGAL EXERCISE 3.11 Aunt Martha wrote her niece Ellen, “I promise to leave you Blackacre in my will if you live with and care for me for the remainder of my life.” Aunt Martha attempts to revoke her offer after Ellen has begun to live with and care for her (i.e., Ellen is performing the requested performance). Could Ellen successfully maintain a breach of contract action against Aunt Martha using:

1. classical contract theory (which requires an express option contract to negate Aunt Martha’s power to revoke her offer);
2. Restatement (Second) of Contracts § 45; or
3. Restatement (Second) of Contracts § 87(2)?

PARALEGAL EXERCISE 3.12 Aunt Martha wrote her niece Ellen, “I promise to leave you Blackacre in my will if you promise to live with and care for me for the remainder of my life.” Aunt Martha has changed her offer from an offer for a unilateral contract to an offer for a bilateral contract. Aunt Martha attempts to revoke her offer while Ellen is preparing to move so she could live with and care for Aunt Martha but before Ellen has promised to live with and care for Aunt Martha for the remainder of her life (i.e., Ellen is preparing to perform the requested performance but has neither begun to perform the requested performance nor has promised to perform). Could Ellen successfully maintain a breach of contract action against Aunt Martha using:

1. classical contract theory (which requires an express option contract to negate Aunt Martha’s power to revoke her offer);
2. Restatement (Second) of Contracts § 45; or
3. Restatement (Second) of Contracts § 87(2)?

PARALEGAL EXERCISE 3.13 Aunt Martha wrote her niece Ellen, “I promise to leave you Blackacre in my will if you promise to live with and care for me for the remainder of my life.” Aunt Martha attempts to revoke her offer after Ellen has begun to live with and care for her but before Ellen has expressly promised Aunt Martha to live with and care for her for the remainder of her life (i.e., Ellen is performing the requested performance although has not expressly promised). Could Ellen successfully maintain a breach of contract action against Aunt Martha using:

1. classical contract theory (which requires an express option contract to negate Aunt Martha’s power to revoke her offer);
2. Restatement (Second) of Contracts § 45; or
3. Restatement (Second) of Contracts § 87(2)?



PARALEGAL CHECKLIST

The Post-Offer/Pre-Acceptance Phase

- After all the communications and events have been placed on a time line and the paralegal and his or her supervising attorney have determined an offer has been made, the following questions should be answered to determine whether something has occurred prior to an attempted acceptance that negates the attempt to accept the offer.
1. Has the offeree’s power to accept the offer expired during the period between the offer and the attempted acceptance?
 - a. Does the offer state an expiration date that would have ended the offer prior to the offeree’s attempted acceptance? If the offer states an expiration date, the offer will expire at the expiration date unless something occurs that causes the offer to expire earlier.
 - b. If the offer did not state an expiration date, has a reasonable time expired since the time the offer was made so the offer has lapsed? A “reasonable time” will vary with each transaction.
 - c. Has the offer been revoked by the offeror? Revocation may be by either a direct or an indirect communication from the offeror. Revocation requires no specific language but does require a clear understanding (from a reasonable person’s standpoint) that the offer has been revoked.
 - d. Has the offer been rejected by the offeree? The offeree may merely reject the offer or may substitute its own offer, which is called a counteroffer. The same tests apply for a counteroffer as for an offer. Once the offeree has rejected an offer, the offeree cannot accept the offer unless the offeror makes a new offer. The new offer may even be identical to the original offer, but must be made anew.
 - e. Has either the offeror or the offeree died or become incapacitated? When either the offeror or the offeree has died or has become incapacitate, the offeree’s power to accept is terminated.
 2. Is there an option contract that would keep the offer open even though the offeror has attempted to revoke the offer, the offeree has attempted to reject the offer, or the offeror has died or become incapacitated?
 - a. Is there an express option contract? An express option contract (“I promise not to revoke my offer for your promise to pay . . .”) is known as a subsidiary contract (the original offer is known as the offer for the main contract) and requires an offer and an acceptance (which includes consideration for the offeror’s promise and consideration for the offeree’s promise or performance).
 - b. If there is no express option contract, is there an implied (by law) option contract? Distinguish whether the offer for the main contract was an offer for a unilateral or a bilateral contract.

- (1) If the offer for the main contract was an offer for a unilateral contract, follow Restatement (Second) of Contracts § 45, which creates an option contract “when the offeree tenders or begins the invited performance or tenders a beginning of it.” The offeree must then complete the performance to accept the offer for the main contract. It should be noted that Restatement (Second) of Contracts § 87(2) also applies to an offer for a unilateral contract and may create an option contract at an earlier point than section 45.
- (2) If the offer for the main contract was an offer for a bilateral contract, follow Restatement (Second) of Contracts § 87(2), which states that an option contract is created to the extent necessary to avoid injustice when “an offer which the offeror should reasonably expect to induce action or forbearance of a substantial character on the part of the offeree before acceptance and which does induce such action or forbearance.”
3. Continue the analysis with the acceptance if the offer has not been terminated or if a terminating event has occurred but an option contract has prevented the terminating event from being effective.

REVIEW QUESTIONS

DEFINE THE FOLLOWING NEW TERMS AND PHRASES

Counteroffer
Lapse
Option contract
Rejection
Revocation

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

1. T F An offer must state a termination date.
2. T F If an offer states a termination date, the offer ceases to exist after that date.
3. T F An offer that states it will be held open until Wednesday, March 3d, cannot be revoked prior to that date.
4. T F An offer that does not state a termination date will end after “a reasonable time.”
5. T F “A reasonable time” is a period set by statute.
6. T F The offeror may reject the offer and the offeree may revoke the offer.
7. T F An offer can be revoked through a direct communication between the offeror and offeree.
8. T F An offer will cease to exist when the offeree rejects it.
9. T F An offeree’s rejection can include a new offer.

10. T F A counteroffer is a new offer by the original offeree who then becomes the offeror.
11. T F Even after an offeree has rejected an offer, he or she can still accept it.
12. T F Samantha offered to sell Rollo, a polo pony, to Jorge for \$4,000. Jorge told Samantha that he would pay \$3,500 for the pony. Samantha rejected Jorge's counteroffer. When Jorge promised to pay Samantha \$4,000 for the pony, a contract was formed.
13. T F Under the Restatement (Second) of Contracts § 48, an offer dies when either the offeror or offeree dies or becomes legally incapacitated.
14. T F Under the Restatement (Second) of Contracts § 48, an offer cannot be accepted after the offeree or offeror dies or becomes legally incapacitated.
15. T F An option contract is a contract subsidiary to the main contract offer.
16. T F Option contracts must be express contracts. They may not be implied by law.
17. T F An option contract eliminates the risk that the offeror will revoke the offer before the offer is accepted.
18. T F Modern contract law may imply an option contract when there has been reliance by the offeree.
19. T F An option contract will keep the power of acceptance alive in spite of the death or incapacity of the offeror or offeree.
20. T F Josephine promised to pay Rolfe \$200 if Rolfe would paint her portrait. Rolfe began to paint but before he could complete his work, Josephine decided that she no longer wanted her portrait painted. Under classical contract law, Josephine's revocation is effective.
21. T F Josephine promised to pay Rolfe \$200 if Rolfe would paint her portrait. Rolfe began to paint but before he could complete his work, Josephine decided that she no longer wanted her portrait painted. Under modern contract law (Restatement (Second) of Contracts § 45), Josephine's revocation is effective.
22. T F Josephine promised to pay Rolfe \$200 if Rolfe would paint her portrait. Rolfe began to paint but before he could complete his work, Josephine decided that she no longer wanted her portrait painted. Under modern contract law (Restatement (Second) of Contracts § 45), Rolfe must complete his performance to accept the offer.

FILL-IN-THE-BLANK QUESTIONS

1. _____. The time at which an offer will cease to exist if there is no stated time limit for accepting or rejecting the offer.
2. _____. Termination of the offer by the offeror.
3. _____. Termination of the offer by the offeree.

4. _____. The new offer that is made by the original offeree after the offeree has rejected the offeror's offer.
5. _____. A contract that is subsidiary to the main contract offer and negates the offeror's power to revoke.
6. _____. A contract implied by law when the offeree has relied on the offeror's offer but has not as yet accepted the offer.
7. _____. A contract that allows the offeree to buy the offeror's power to revoke.
8. _____. Under this section of the Restatement (Second) of Contracts, an offer for a unilateral contract cannot be revoked "when the offeree tenders or begins the invited performance or tenders a beginning of it."
9. _____. Under this section of the Restatement (Second) of Contracts, an offer for a bilateral contract cannot be revoked if the offeree either begins preparation or begins performance as defined by the terms of the offer.
10. _____. Under this section of the Restatement (Second) of Contracts, an offer for a unilateral contract cannot be revoked if the offeree begins preparation for the performance as defined by the terms of the offer.

MULTIPLE CHOICE QUESTIONS (CIRCLE ALL THE CORRECT ANSWERS)

1. The offeree's power to accept an offer may be terminated by:
 - (a) the offeree's inaction
 - (b) the offeror's revocation of the offer
 - (c) the offeree's rejection of the offer
 - (d) the death or incapacity of the offeror or offeree
 - (e) the sale of the subject matter to a third person when the offeree has no notice of the sale
2. An offer that states that it shall be held open until Sunday, noon:
 - (a) cannot be revoked prior to Sunday, noon
 - (b) will cease to exist on Sunday, noon
 - (c) must be held open until Sunday, noon
 - (d) can be rejected and then accepted prior to Sunday, noon
 - (e) is not an option contract
3. Which offer has the longest life span:
 - (a) an offer to sell 10 acres of real estate in an area that is being developed rapidly
 - (b) an offer to sell a puppy
 - (c) an offer to sell a truckload of peaches currently being harvested

- (d) an offer to buy a new automobile from a dealer
 - (e) an offer to buy 180 acres of undeveloped farmland
4. On March 1, the Katy Railroad sent a letter to the A-1 Steel Company asking the price of 50,000 tons of steel rails.
- On March 5, A-1 responded by letter offering to sell Katy 50,000 tons of steel rails for \$75 a ton and stating that this offer would remain open for 30 days.
 - On March 10, Katy wrote that it would buy 100,000 tons at \$75 a ton.
 - On March 15, A-1 responded that it could not fill an order for 100,000 tons.
 - On March 20, Katy wrote back stating that it would buy 50,000 tons at \$75 a ton.
 - On March 25, A-1 responded that it could not fill Katy's order.
- (a) a contract was formed for 50,000 tons when Katy accepted A-1's offer to sell 50,000 tons at \$75 a ton
 - (b) no contract was formed because Katy's letter offering to buy 100,000 tons was a rejection of A-1's offer and once rejected, A-1's offer could not be accepted
 - (c) a contract was formed for 50,000 tons since the express option contract precluded A-1 from revoking its offer
 - (d) a contract was formed for 50,000 tons since the express option contract kept A-1's offer open even though Katy attempted to reject it
 - (e) the transaction ended with Katy making an offer to buy 50,000 tons and A-1 rejecting this offer
5. An option contract may be:
- (a) express
 - (b) implied by law
 - (c) either express or implied by law
 - (d) express only
 - (e) implied by law only
6. An offer for an express option contract:
- (a) may be proposed by the party who proposed the offer for the main contract
 - (b) may be proposed by the party who is the offeree in the main contract
 - (c) may be proposed by either the offeror or the offeree in the main contract
 - (d) must be proposed when the offer for the main contract is proposed
 - (e) may be proposed at any time after the offer for the main contract has been proposed (contemporaneous or subsequent)
7. An offer for an express option contract may be proposed:
- (a) prior to the offer of the main contract
 - (b) contemporaneous with the offer of the main contract
 - (c) subsequent to the offer of the main contract
 - (d) after the offer of the main contract has been rejected
 - (e) after the offer of the main contract has been accepted
8. An implied contract is:
- (a) implied by law
 - (b) implied from the facts

- (c) implied by the offeree
 - (d) implied by the offeror
 - (e) implied by the courts
9. Under modern contract law, an option contract:
- (a) may be implied by law
 - (b) may be expressly agreed upon by the parties
 - (c) no longer exists
 - (d) may be implied where the offer in the main contract is for a unilateral contract or for a bilateral contract
 - (e) not only negates the offeror's power to revoke his or her offer, but also applies where the offeree has previously attempted to reject the offer
10. Restatement (Second) of Contracts § 87(2) applies to the following offers:
- (a) offer for a unilateral contract only
 - (b) offer for a bilateral contract only
 - (c) offer for either a unilateral or bilateral contract
 - (d) neither an offer for a unilateral nor a bilateral contract
 - (e) offer for the sale of goods

SHORT ANSWER QUESTIONS

1. The City of Metropolis intends to build an expressway along the river. To acquire the property needed for the expressway, the City has made offers to various property owners. What should be considered to determine how long a property owner has to accept the City's offer?
2. On March 1, the Katy Railroad sent a letter to the A-1 Steel Company asking the price on 50,000 tons of steel rails.
On March 5, A-1 responded by letter offering to sell Katy 50,000 tons of steel rails for \$75 a ton and that this offer would remain open for 30 days.
On March 10, Katy wrote that it would buy 100,000 tons at \$75 a ton.
On March 15, A-1 responded that it could not fill an order for 100,000 tons.
On March 20, Katy wrote back stating that it would buy 50,000 tons at \$75 a ton.
On March 25, A-1 responded that it could not fill Katy's order.
Analyze each communication and determine whether a contract has been formed.
3. Martha Jennings wrote a letter to her nephew, John, promising to pay him \$5,000 if he would perform the duties of executor of her estate when she died. After Martha died, John acted as her executor, but the court refused to recognize the existence of a contract between Martha and John. Has a contract been formed?
4. Charles made a written offer to sell Blackacre to Mary for \$250,000. In addition to Charles's promise to sell Blackacre to Mary, Charles promised not to revoke his offer for 60 days for Mary's promise to pay him \$1,000. Mary promised to pay Charles the \$1,000. Several days later, Mary sent Charles a check for \$1,000.

Thirty days later Charles wrote Mary stating he was revoking his offer and returning her \$1,000 check. Mary wrote Charles that she had decided to accept his offer to sell her Blackacre and she was returning her \$1,000 check.

Has a contract to sell Blackacre been formed?

5. Martina promised to pay Rachael \$450 if Rachael would teach Martina's daughter, Erica, French during the summer. Rachael spent June and July teaching Erica French. On August 1st, Martina told Rachael that she was revoking her offer.

Analyze whether a contract has been created between Martina and Rachael.

6. Martina promised to pay Rachael \$450 if Rachael would promise to teach Martina's daughter, Erica, French during the summer. Prior to the beginning of summer vacation, Rachael spent time purchasing French books and preparing her lesson plan. Late in May, Martina notified Rachael that she had changed her mind and was not interested in having Erica learn French. Rachael wrote Martina attempting to accept Martina's offer.

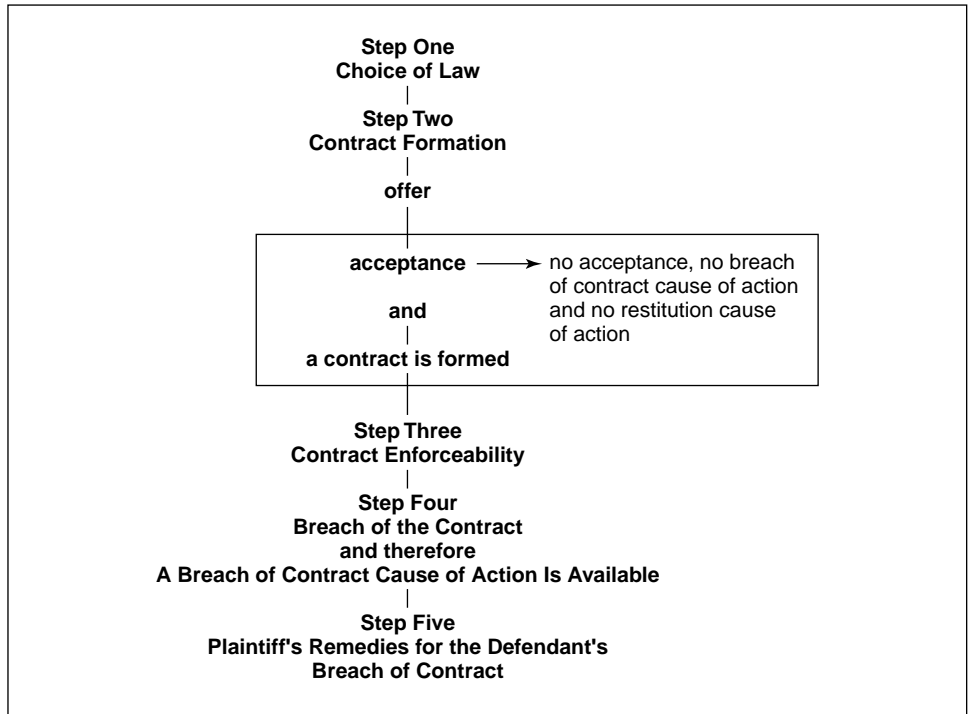
Analyze whether a contract has been created between Martina and Rachael.



The Acceptance Phase

- ◆ The Elements of an Acceptance—The Offeree’s Promise and Consideration for that Promise or the Offeree’s Performance and Consideration for that Performance
 - The Acceptance Must Be in Response to the Offer*
 - The Offeree Must Agree to All of the Offeror’s Terms*
 - Miscommunication between the Offeror and the Offeree*
 - The Parties Who Can Accept the Offer*
- ◆ The Method for Accepting an Offer
 - Notice to the Offeror that the Offer Has Been Accepted*
- ◆ When an Attempted Acceptance Is Effective
- ◆ Is a Restitution Action an Alternative to Acceptance?

Chapter Four explores the acceptance. The ingredients of an acceptance depend on whether the offer is for a bilateral or unilateral contract. If the offer is for a bilateral contract (offeror’s promise for the offeror’s promise), the acceptance is the offeree’s promise for the offeror’s promise. If the offer is for a unilateral contract (offeror’s promise for the offeree’s performance), the acceptance is the offeree’s performance (full performance) for the offeror’s

FIGURE 4–1 The Acceptance Phase of the Road Map

promise. Chapter Four explores a number of problems that may surface when investigating the elements of an acceptance (see Figure 4–1).

- Must acceptance be in response to the offer (must the offeree have knowledge of the offer prior to attempting to accept the offer)?
- Must the offeror's promise not be subject to a pre-existing duty?
- Must the terms of the acceptance mirror the offer?
- Does acceptance occur when the attempted acceptance reflects a miscommunication between the parties?
- Is the offeree required to notify the offeror that the offer has been accepted?
- May the offeror limit who may accept the offer?

In addition to problems inherent with the elements of an offer, Chapter Four also considers several additional problems that may preclude an acceptance from being effective:

- What method of acceptance must the offeree follow?
- When is acceptance effective?

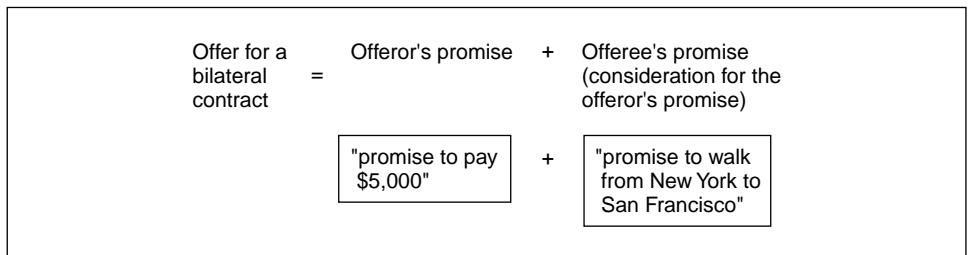
The final topic in Chapter Four involves the restitution cause of action.

- Is a restitution cause of action available when the offeror, after making the offer, confers a benefit on the offeree, and the offeree *rejects* the offer but retains the benefit?

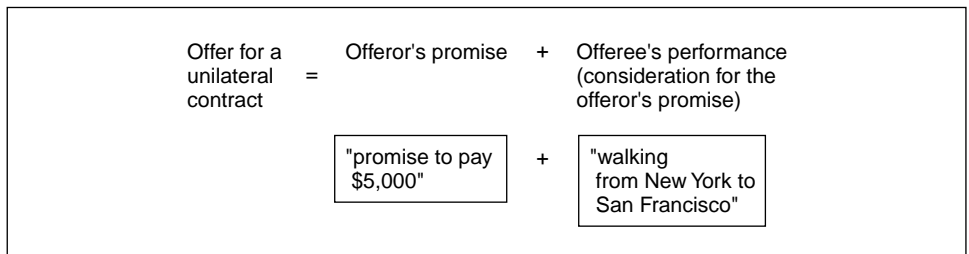
- Is a restitution cause of action available when the offeror, after making the offer, confers a benefit on the offeree, and the offeree *accepts* the offer and retains the benefit?

THE ELEMENTS OF AN ACCEPTANCE—THE OFFEREE’S PROMISE AND CONSIDERATION FOR THAT PROMISE OR THE OFFEREE’S PERFORMANCE AND CONSIDERATION FOR THAT PERFORMANCE

An offeror, as master of the offer, can propose to the offeree that the contract be bilateral or unilateral. If the offeror proposes that the contract be bilateral, the offeror’s offer will be a promise for a promise. The offeror is seeking to exchange his or her promise for the offeree’s promise. “I promise to pay you \$5,000 for your promise to walk from New York to San Francisco.” The “price,” the “exchange,” or the “consideration” for the offeror’s promise is the offeree’s promise (promise to walk from New York to San Francisco).

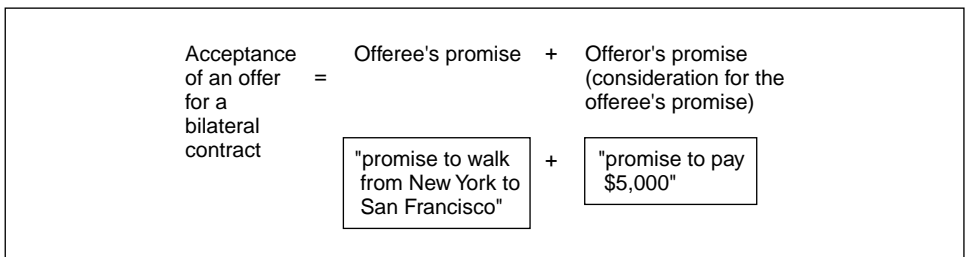
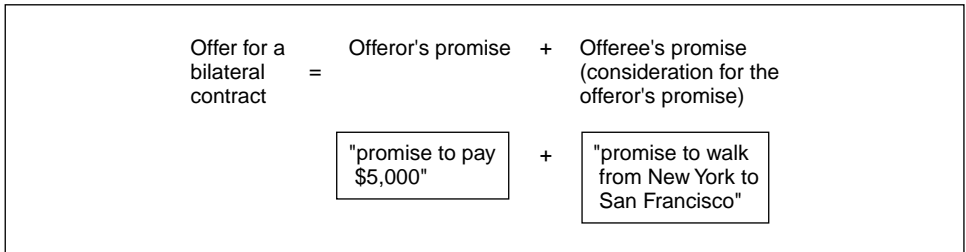


If the offeror proposes that the contract be unilateral, the offeror’s offer will be a promise for a performance. The offeror is seeking to exchange his or her promise for the offeree’s performance. “I promise to pay you \$5,000 for walking from New York to San Francisco.” The “price,” the “exchange,” or the “consideration” for the offeror’s promise is the offeree’s performance (walking from New York to San Francisco).

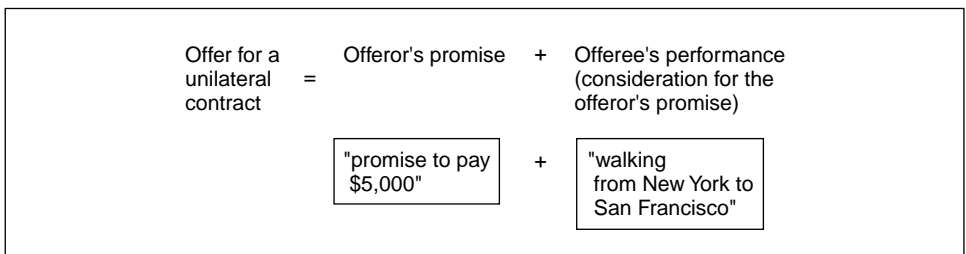


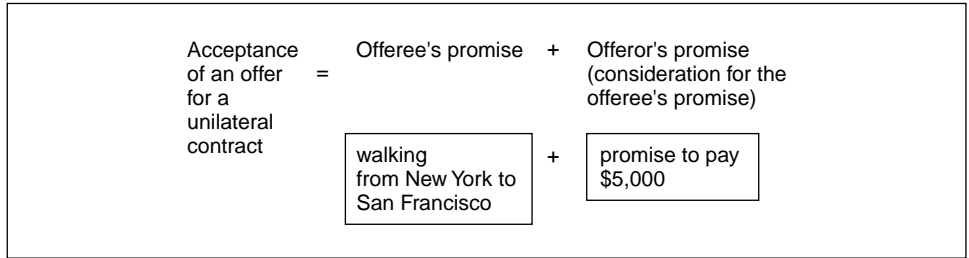
The offeree’s acceptance must be responsive to the offeror’s offer. If the offer is for a bilateral contract (promise for a promise), the acceptance must also be bilateral (promise for a promise). The promises in the acceptance are the mirror image of the promises in the offer. In other words, the promises are

reversed in order. The offeree is exchanging his or her promise for the offeror's promise. If the offeror says "I promise to pay you \$5,000 for your promise to walk from New York to San Francisco," the offeree, by responding "OK," "I'll do it," or "I promise to walk," is in fact responding "I promise to walk from New York to San Francisco for your promise to pay \$5,000." The "price," the "exchange," or the "consideration" for the offeree's promise is the offeror's promise to pay \$5,000.



If the offer is for a unilateral contract (promise for a performance), the acceptance must also be unilateral (performance for a promise). The promise and performance, however, are reversed. The performance and promise in the acceptance are the mirror image of the promise and performance in the offer. The offeree is exchanging a performance for the offeror's promise. If the offeror proposes "I promise to pay you \$5,000 for walking from New York to San Francisco," the offeree would respond *not* by promising since a promise is not what the offeror is seeking in exchange for his or her promise, but by actually walking from New York to San Francisco. The "price," the "exchange," or the "consideration" for the offeree's performance is the offeror's promise to pay \$5,000.





The Acceptance Must Be in Response to the Offer

The offeror, when making the offer, makes a promise to entice the offeree to promise (offer for a bilateral contract) or to perform (offer for a unilateral contract). The offeree, when making the acceptance, must promise (acceptance of the offer for the bilateral contract) or perform (acceptance of the offer for the unilateral contract) in response to the offer. It is not enough that the offeree's promise or performance happens by coincidence.

Knowledge of the Offer. If the offer is for a bilateral contract, the offeree must have knowledge of the offer before responding with a promise. Otherwise, the offer is not inducing the offeree's response, and the offeree's response is not an effective acceptance.

PARALEGAL EXERCISE 4.1 David, who lives in Texas, is the original owner of a 1966 Mustang, which is in mint condition. His cousin Susan, who lives in Georgia, has often stated that she would like to buy it. David has always said it was not for sale.

On March 1st, David wrote Susan that he was now ready to sell her his Mustang for \$8,000. On March 2d, Susan, *not* knowing that David was ready to sell, decided to press David on the issue of the Mustang. She wrote him saying that she would pay \$8,000 for the Mustang. Susan received David's letter on March 4th.

David received Susan's letter on March 8th but has second thoughts about selling his Mustang. From the postmark on Susan's letter, he knows that she could not have received his letter before writing hers. If Susan does not write a second letter to David, has Susan accepted David's offer?

If the offer is for a bilateral contract, the acceptance is the offeree's promise, an event that is completed during a relatively short period of time. A promise therefore is almost an instantaneous event. Except for factual issues regarding whether the offeree had knowledge of the offer prior to accepting, the law is straightforward. The offer could not induce the offeree if the offeree has no knowledge of the offer.

If the offer is for a unilateral contract, the offeree's performance often requires time to complete. "Walking from New York to San Francisco" could take months. "Refraining from drinking until twenty-one" could take years. When

must the offeree learn of the offeror's promise? Must the offeree have knowledge of the offer before beginning the requested performance, or would having knowledge before completing performance be sufficient?

The Restatement of Contracts has changed its stance over the years. The Restatement (First) of Contracts § 53 (1932) affirmed the rigid common law position that the offeree was required to have knowledge of the offer before beginning the requested performance.

The whole consideration requested by an offer must be given after the offeree knows of the offer.

The Restatement (Second) of Contracts § 51 (1979) took a more tolerant stance by requiring the offeree to have knowledge of the offer prior to completing the requested performance.

Unless the offeror manifests a contrary intention, an offeree who learns of an offer after he has rendered part of the performance requested by the offer may accept by completing the requested performance.

PARALEGAL EXERCISE 4.2 Bonney, a convicted murderer, escaped from the county jail. The City Council offered a \$50,000 reward to any person who captured and returned Bonney to jail.

Bonney fled to another county and before the news of the reward spread to that county, Oliver, a private detective, captured Bonney. As Oliver was driving Bonney back to the county jail, he learned about the reward on his car radio.

If Oliver does not release Bonney and recapture him, is he contractually entitled to the reward? Would your answer be the same under the Restatement (First) or Restatement (Second) of Contracts?

Pre-Existing Duty. While exploring the components of offer, we discussed the requirement that consideration for the offeror's promise be "new" consideration and not something already required of the offeree. If the offeror requested the offeree to promise or perform some act or forbearance that the offeree already had a duty to perform, the offeree's promise or performance violates the "pre-existing duty" rule, and the offeror's promise would lack consideration. The offeror's attempt to make an offer fails.

EXAMPLE 4-1

Under state law a law enforcement officer is required to apprehend escaped convicts. Bonney, a convicted murderer, escaped from the city jail. The City Council promised a \$50,000 reward to any law enforcement officer who promised to capture and return Bonney to jail. The City Council is attempting to make *an offer for a bilateral contract* that states: "We promise to pay \$50,000 if you promise to capture and return Bonney to jail." Because law enforcement officers have a pre-existing duty to apprehend escaped convicts, the City Council's promise to pay lacks consideration and therefore is not an offer.

EXAMPLE 4-2

Under state law a law enforcement officer is required to apprehend escaped convicts. Bonney, a convicted murderer, escaped from the city jail. The City Council promised a \$50,000 reward to any law enforcement officer who captures and returns Bonney to jail. The City Council is attempting to make *an offer for a unilateral contract* that states: "We promise to pay \$50,000 for your capturing and returning Bonney to jail." Because law enforcement officers have a pre-existing duty to apprehend escaped convicts, the City Council's promise to pay lacks consideration and therefore is not an offer.

The same "pre-existing duty" rule applies to acceptance. If the offeree promises (if the offer was for a bilateral contract) or if the offeree performs (if the offer was for a unilateral contract) and the offeror was already obligated to do what his or her promise entailed, the offeror's promise violates the "pre-existing duty" rule and could not be consideration for the offeree's promise or performance. The offeree's promise or performance lacks consideration. The offeree's attempt to accept the offer fails.

EXAMPLE 4-3

Under state law a law enforcement officer is required to apprehend escaped convicts. Bonney, a convicted murderer, escaped from the city jail. A law enforcement officer promised to capture and return Bonney to jail if the City Council would promise to pay him a \$50,000 reward. The officer's *offer for a bilateral contract* was: "I promise to capture and return Bonney for your promise to pay \$50,000. The City Council could not accept this offer because of the pre-existing duty rule. The attempted acceptance would be the mirror image of the offer: "We promise to pay \$50,000 for your promise to capture and return Bonney." The officer has a pre-existing duty to capture and return escapees which means there could be no consideration for the City Council's promise to pay and no acceptance of the offer and no contract.

EXAMPLE 4-4

Under state law a law enforcement officer is required to apprehend escaped convicts. Bonney, a convicted murderer, escaped from the city jail. A law enforcement officer promised to capture and return Bonney to jail if the City Council pays him a \$50,000 reward. The officer's *offer for a unilateral contract* was: "I promise to capture and return Bonney for your paying me \$50,000." Even if the City Council paid the officer \$50,000 and the officer then captured and returned Bonney, there would be no acceptance of the offer. The City Council could not accept the offer because of the pre-existing duty rule. The attempted acceptance would be the mirror image of the offer: "Paying \$50,000 for the officer's promise to capture and return Bonney." The officer has a pre-existing duty to capture and return escapees which means there could be no consideration for the City Council's paying and therefore no acceptance and no contract.

It is important to consider “pre-existing duty” when evaluating both the attempted offer and the attempted acceptance. The offer may not involve a pre-existing duty problem, but the attempted acceptance may.

PARALEGAL EXERCISE 4.3 William was the sole heir under his father’s will. When William’s father died, the executor said to William, “I promise to pay you your inheritance, if you promise to donate 10 percent to charity.” William responded, “I promise to donate 10 percent to charity if you promise to pay me my inheritance.” Did the executor make an offer to William, or does the attempted offer suffer from a lack of consideration due to the pre-existing duty rule? If the executor has made an offer, did William accept the offer, or does William’s attempted acceptance lack consideration due to the pre-existing duty rule?

The Offeree Must Agree to All of the Offeror’s Terms

The offeror is the master of the offer and, as such, controls the terms of the contract.

Common Law Mirror Image Rule. The offeree cannot change the terms of the offer. The offeree must either promise or perform as the offeror has required, and the offeree must do so to receive what the offeror has promised.

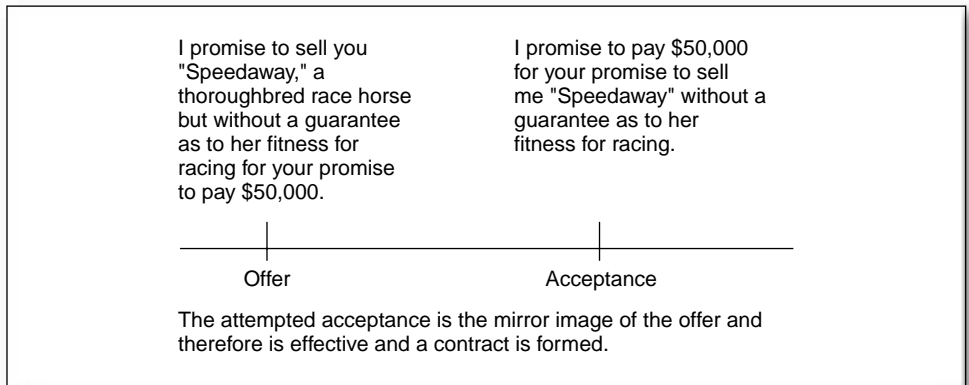
EXAMPLE 4–5

If a homeowner promises to pay a painter \$1,500 to paint his house white, the painter must respond that she will paint the owner’s house white for \$1,500. If the painter responds with either \$1,600 or gray rather than white, the attempted acceptance does not mirror the offer and is treated as a rejection of the offer. If the rejection meets the requirements of an offer, it would be considered a counteroffer, and it would be up to the original offeror (by counteroffer, the original offeror becomes the offeree), the homeowner, to accept the counteroffer.

PARALEGAL EXERCISE 4.4 PG Studios, a motion picture company, promised to pay Cynthia \$5 million if she promised to star in PG’s new picture, with filming to begin on August 1st. Cynthia wrote PG that she accepted the offer but could not begin filming until August 10th. PG did not respond to Cynthia’s letter. PG began filming on August 1st but used another actress. Was there a contract between PG Studios and Cynthia?

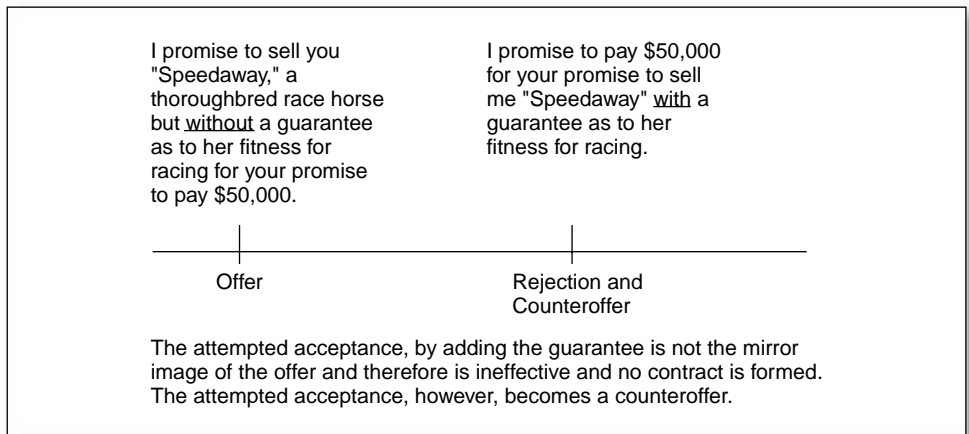
The common law mirror image rule leaves the parties in an all-or-nothing situation. **Mirror image** means that the offeree must accept the offer without changing it. If the attempted acceptance mirrors the offer, a contract is formed, and the terms are those of the offer.

EXAMPLE 4-6

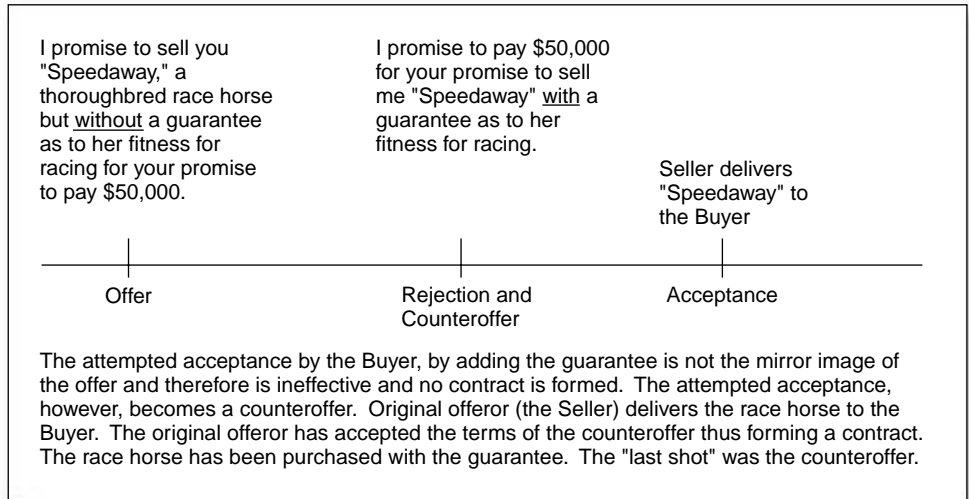


If the attempted acceptance is not the mirror image, the offer is not accepted but is rejected, and the attempted acceptance becomes a counteroffer.

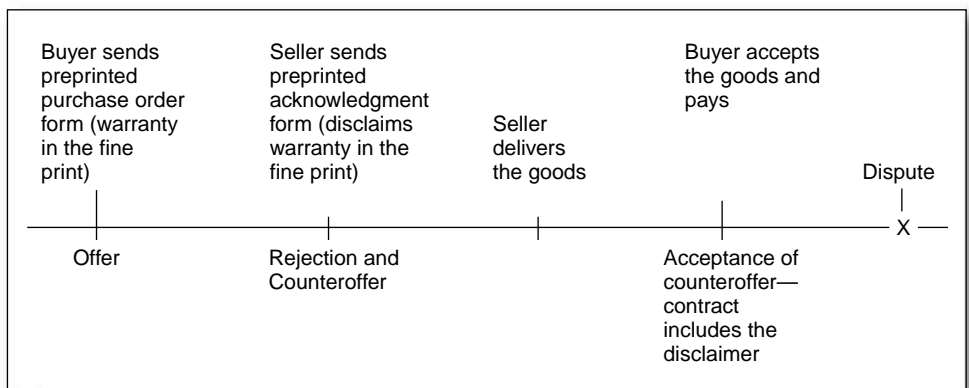
EXAMPLE 4-7



If the original offeror takes no further action, the parties are without a contract. If the original offeror accepts the counteroffer, a contract is formed with the terms being those of the counteroffer. This is known as the **last shot doctrine**. The "last shot" is the last offer and it dictates all the terms.

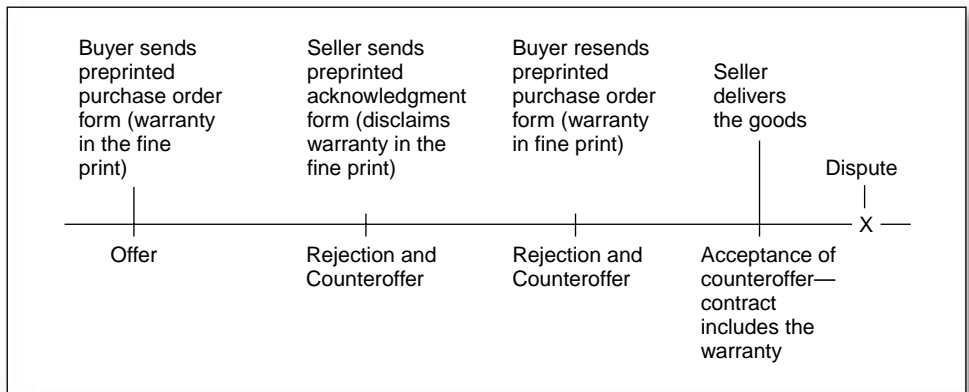
EXAMPLE 4-8

In most commercial transactions that are based on an exchange of written forms, the preprinted terms on the forms neither agree nor are read before the seller delivers or the buyer accepts delivery. Under the common law "last shot" doctrine if the seller sends the last form (counteroffer) and delivers the goods, and the buyer accepts the delivery and pays for the goods (acceptance of the counteroffer), a contract is formed and the terms are those found in the seller's form, regardless of whether they are in the fine print and the buyer has never read them.

EXAMPLE 4-9

If the buyer sends the last form (counteroffer) and the seller delivers the goods (acceptance of the counteroffer), a contract is formed and the terms are those found in the buyer's form, even if they are in the fine print and the seller has never read them.

EXAMPLE 4-10



The Uniform Commercial Code § 2-207. The drafters of the Uniform Commercial Code sought to change the common law's mirror image rule in those transactions involving sale of goods. The drafters set up the following scheme:

Section 2-207. Additional Terms in Acceptance or Confirmation

(1) A definite and seasonable expression of acceptance or a written confirmation which is sent within a reasonable time operates as an acceptance even though it states terms additional to or different from those offered or agreed upon, unless acceptance is expressly made conditional on assent to the additional or different terms.

(2) The additional terms are to be construed as proposals for addition to the contract. Between merchants such terms become part of the contract unless:

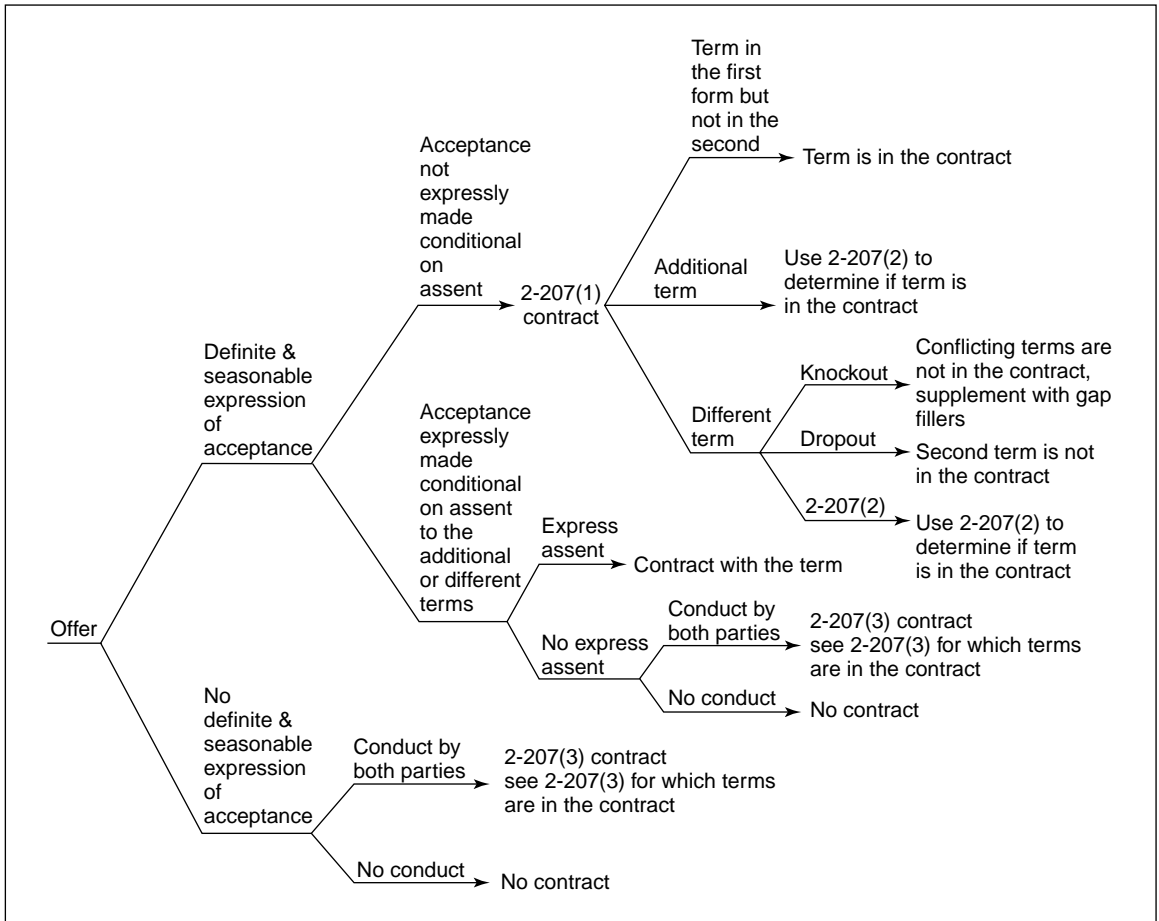
- (a) the offer expressly limits acceptance to the terms of the offer;
- (b) they materially alter it; or
- (c) notification of objection to them has already been given or is given within a reasonable time after notice of them is received.

(3) Conduct by both parties which recognizes the existence of a contract is sufficient to establish a contract for sale although the writings of the parties do not otherwise establish a contract. In such case the terms of the particular contract consist of those terms on which the writings of the parties agree, together with any supplementary terms incorporated under any other provisions of this Act.

While the common law "last shot" doctrine may, at times, have given harsh results, the section 2-207 scheme creates an almost unworkable maze with often unpredictable results. The Decision Tree in Figure 4-2 will provide the routes through section 2-207. These steps must be followed carefully and in order.

Before discussing these steps, it is important to look at sample preprinted forms (Buyer's Purchase Order and Seller's Acknowledgment Form). (See Figures 4-3 and 4-4).

FIGURE 4-2 UCC § 2-207 Decision Tree



The forms have variable terms (price, quantity, subject matter, and delivery) and fixed terms (often the small print). The **“bargained for” terms** are the variable terms. The **“boiler plate” terms** are the fixed terms. The boiler plate terms may be either substantive terms (warranty, disclaimer, credit, arbitration, risk of loss, choice of law, and choice of forum) or procedural terms (“only my terms shall apply” and “this is not an acceptance unless you agree to all of our terms”).

The section 2-207 analysis begins with subsection (1). The initial phrase “A definite and seasonable expression of acceptance or a written confirmation which is sent within a reasonable time” establishes that 2-207(1) deals with two very different types of factual situations. The first is the traditional offer and acceptance, or in this case, one form and response form. The second is an oral contract followed by a written confirmation. For our purposes, we will focus only on the first situation.

FIGURE 4-3 Buyer's Purchase Order

PURCHASE ORDER			
Seller's Name:		Buyer's Name:	
Address:		Address:	
Telephone No. ()		Telephone No. ()	
FAX: ()		FAX: ()	
E-Mail:		E-Mail:	
Description	Quantity	Price/Unit	Total Price
Shipping Terms:			
Payment Terms:			
Additional Terms:			
This Purchase Order is subject to the terms on the back of this form.			
Signatures			
Buyer:		Date:	
Title:			
Seller:		Date:	
Title:			
This Purchase Order does not become effective until it is signed by both the Buyer and the Seller, or unless accepted by the Seller in accordance with Section 1 on the back of this Purchase Order.			

Continued

FIGURE 4-3 Buyer's Purchase Order (*Continued*)

Additional Terms

1. **Acceptance** (Governed by UCC § 2-207)

This Purchase Order must be signed and returned to the Buyer within ten (10) business days. Any additional terms suggested by the Seller are declined unless expressly agreed to by the Buyer. Any delivery or beginning of delivery of either part or all of the goods listed on this Purchase Order will constitute an acceptance by the Seller of all of the terms listed on this form.

2. **Choice of Law** (Governed by UCC § 1-105)

This Purchase Order and any other additions to this Purchase Order shall be governed by the state where the Buyer is located.

3. **Choice of Forum**

Any dispute that arises from this transaction shall be resolved in the state where the Buyer is located.

4. **Choice of Dispute Resolution**

Any dispute that arises from this transaction shall be resolved by mediation. If the parties cannot resolve their dispute through mediation, then the dispute shall be resolved by arbitration.

5. **Changes** (Governed by UCC §§ 2-202, 2-209)

Buyer has the opportunity to change the following items without being in violation of the terms of this Purchase Order:

- a. Method of shipment;
- b. Time or place of delivery;
- c. Quantity of items purchased as long as it does not exceed 5% of the original order.

6. **Delivery** (Governed by UCC §§ 2-503, 2-601)

Any failure of the Seller to follow the terms regarding delivery as stated in this Purchase Order will constitute a breach of contract.

7. **Warranty** (Governed by UCC §§ 2-312 thru 2-314)

The Buyer reserves all of the express and implied warranties under Article 2 of the Uniform Commercial Code.

8. **Remedies** (Governed by UCC §§ 2-711 thru 2-717)

In the event of the Seller's breach of contract, the Buyer reserves all of its remedies under Article 2 of the Uniform Commercial Code.

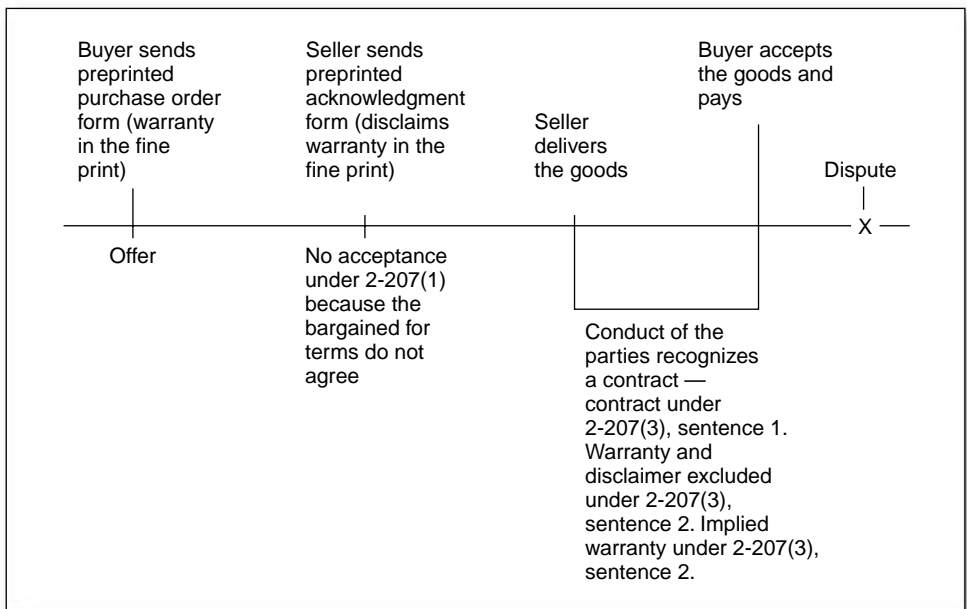
FIGURE 4-4 Seller's Acknowledgment Form

ACKNOWLEDGMENT FORM		
This Acknowledgment Form confirms the receipt of your order of _____ for:		
Month	Day	Year
Description: _____		
Quantity: _____		
Price per Unit: _____		
Total price: _____		
To be shipped on: _____		
To: _____		
Shipment arrangements: _____		
Payment arrangements: _____		
This Acknowledgment Form must be signed and returned to the Seller within ten business days. Any acceptance of delivery of either a part or all of the goods listed in this Acknowledgment Form will constitute an acceptance by the Buyer and all the terms listed in this Acknowledgment Form shall apply to this transaction.		
The following terms apply to this contract for sale:		
1. Terms. Only the terms stated in this Acknowledgment Form apply to this contract for sale. Any additional terms suggested by the Buyer are declined unless expressly agreed to by the Seller.		
2. Choice of Law Provision. The law of Seller's state shall apply to this contract for sale.		
3. Payment. Any failure of the Buyer to follow the terms regarding payment as stated in this Acknowledgment Form will constitute a breach of contract.		
4. Warranty. The Seller disclaims all express and implied warranties with the exception that the Seller warrants that the goods shall not be defective. Any claim that the goods are defective must be made in writing within 30 days of receipt. If goods are defective, the Seller has the option to repair or replace the goods.		
5. Dispute Resolution. All disputes shall be resolved by litigation in the state where the Seller is located.		
6. Breach. Any failure of the Buyer to comply with the terms of this Acknowledgment Form as supplemented by Article 2 of the Uniform Commercial Code shall constitute a breach.		
7. Remedies. In the event of the Buyer's breach of contract, the Buyer reserves all of its remedies under the Uniform Commercial Code.		
_____ (Seller)	_____ (Title)	_____ (Date)
_____ (Buyer)	_____ (Title)	_____ (Date)

“A definite and seasonable expression of acceptance” assumes that the first form is an offer. Therefore focus on the second form which is the attempted acceptance. The “**definite . . . expression of acceptance**” refers to the “bargained for” terms in the forms. “**Bargained for**” terms are not preprinted terms and must be supplied by the parties on the forms. If the bargained for terms in the second form are not the mirror image of the bargained for terms in the first form, the second form is not a “definite . . . expression of acceptance.” If the parties by their conduct recognize the existence of a contract, a contract is formed under subsection (3), sentence 1. Subsection (3), sentence 2 provides for the terms. “In such case the terms of the particular contract consist of those terms on which the writings of the parties agree, together with any supplementary terms incorporated under any other provision of this Act.” Under sentence 2, the substantive boiler plate terms of the two forms are compared. The terms will sort into three patterns: those that agree, those that disagree, and those that are only in one form. Those boiler plate terms that are the same are terms of the contract. Those terms that are different or those that appear in only one form are not terms of the contract. The final step is to check the Uniform Commercial Code for terms that the Code supplies if the contract is silent. Many of these terms, know as “gap filler” terms, are found in Part 3 of Article 2 (the 2-300s). For example, section 3-305 supplies a price term and section 2-314 supplies implied warranties.

For the following example, assume that the “bargained for” terms do not agree between the Buyer’s purchase order and the Seller’s acknowledgment form. A **purchase order** is the buyer’s offer form. The **acknowledgment form** is the seller’s acceptance form.

EXAMPLE 4–11



PARALEGAL EXERCISE 4.5 If, in the previous example, the Buyer's purchase order did not contain the warranty term, would the contract be with or without an implied warranty?

PARALEGAL EXERCISE 4.6 If, in the previous example, the Seller's acknowledgment form did not contain the disclaimer of warranty term, would the contract be with or without an implied warranty?

PARALEGAL EXERCISE 4.7 If, in the previous example, the Seller's acknowledgment form contained a mandatory arbitration term and the Buyer's purchase order was silent on this issue, would the contract be with or without a mandatory arbitration term?

If the bargained for terms in the second form are the mirror image of the bargained for terms in the first form, the second form is a "definite . . . expression of acceptance." The second form, however, must be a "definite and *seasonable* expression of acceptance. "**Seasonable . . . expression of acceptance**" refers to the fact that the second form must have been sent within a reasonable time after receiving the first form. Subsection (1) continues by stating that the second form "operates as an acceptance even though it states terms additional to or different from those offered." The additional or different terms are boiler plate terms. At this point section 2-207(1) deviates from the common law mirror image rule. Under the common law, the second form with additional or different terms in the boiler plate would operate as a rejection of the offer and would become a counteroffer. Under 2-207(1), the second form operates as an acceptance regardless of the additional or different terms in the boiler plate. An **additional term** is a substantive boiler plate term that appears in the second form but not in the first form. A **different term** is a substantive boiler plate term that appears in both forms but one is not the mirror image of the other.

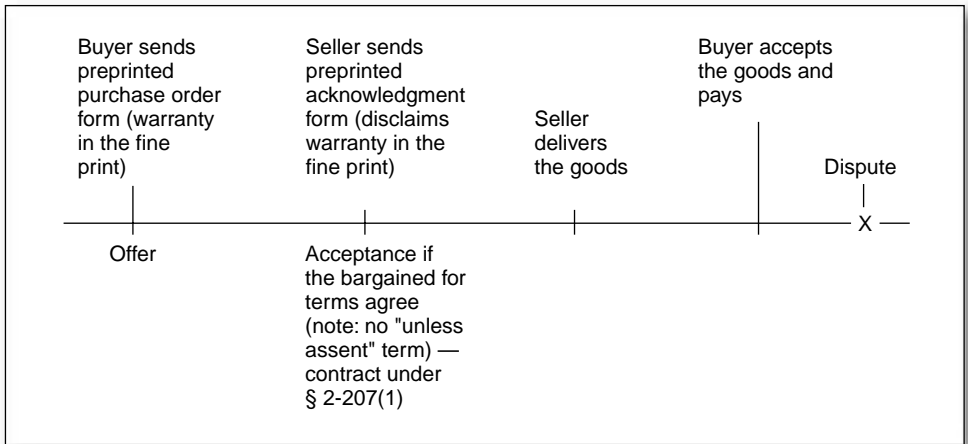
One issue remains under section 2-207(1). Subsection (1) ends with the phrase "unless acceptance is expressly made conditional on assent to the additional or different terms." This statement requires us to focus on the procedural terms in the boiler plate. We are looking for a term that states "this is not an acceptance unless you agree to all of our terms." A term that states "All of our terms govern" will be insufficient because it does not withhold acceptance. If an "unless acceptance" term is found in the second form, the form does not act as an acceptance but is a counteroffer and the party who sent the first form must assent to the terms in the second form. If the party who sent the first form expressly assents to the fact that all of the second form terms govern, a contract is formed and the terms are those in the counteroffer (the second form). If there is no express assent by the party who sent the first form, assent may be implied

by the conduct of the parties under subsection (3). If the parties by their conduct do not recognize the existence of a contract, no contract is formed.

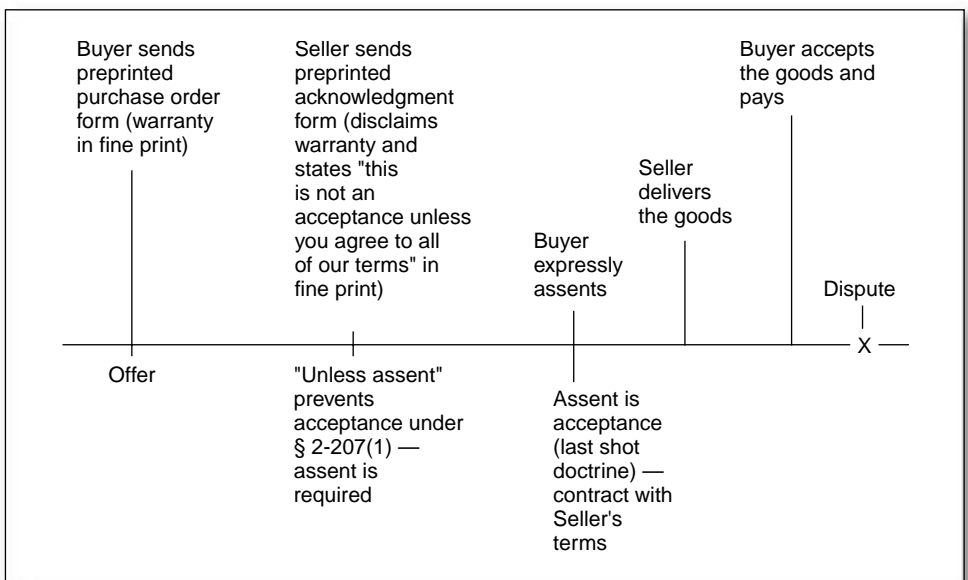
If no “unless acceptance” term is found in the second form, the form acts as an acceptance and a contract is formed under subsection (1). It is important to note that subsection (1) only creates the contract. It does not discuss which terms are in the contract.

In the following examples, assume that the “bargained for” terms agree between the Buyer’s purchase order and the Seller’s acknowledgment form.

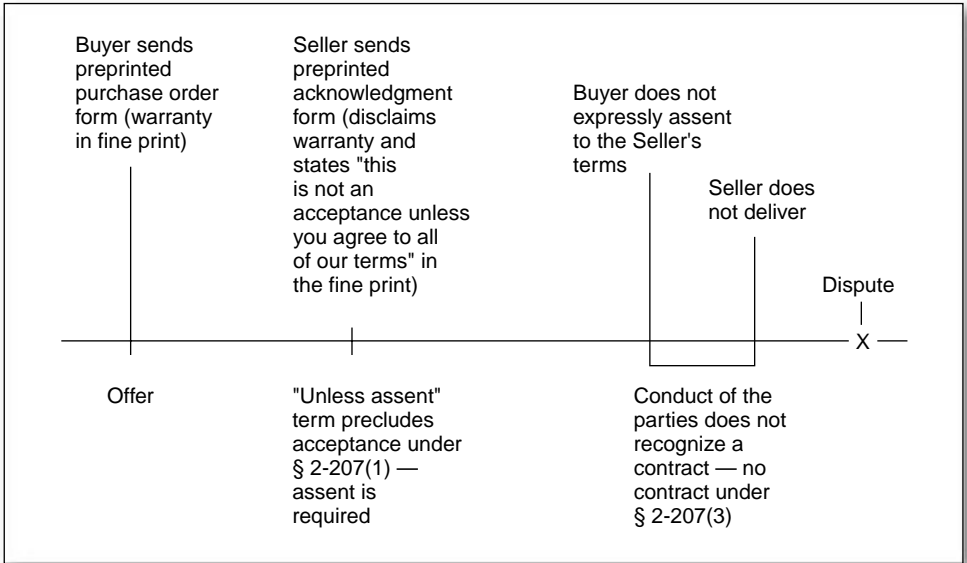
EXAMPLE 4–12



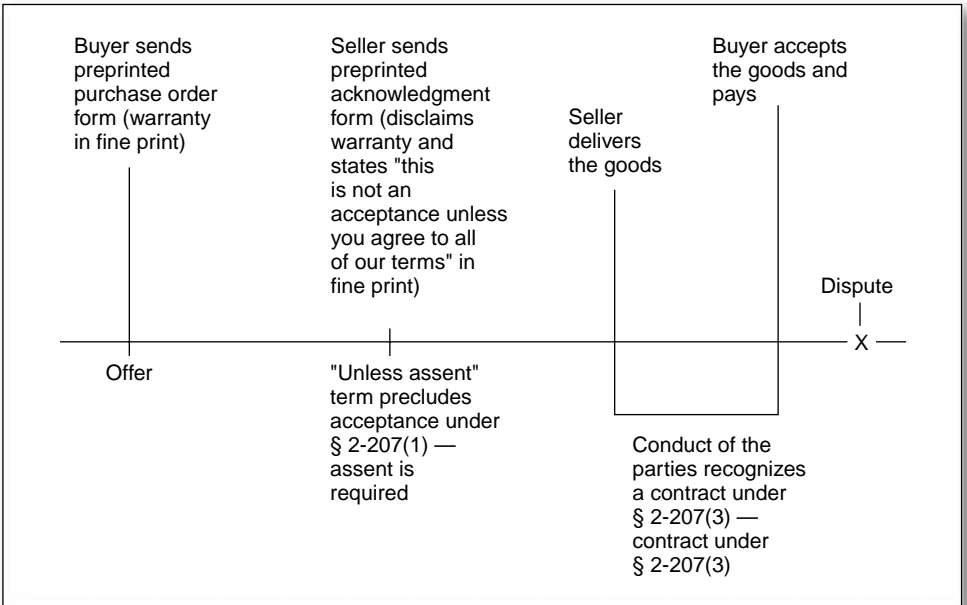
EXAMPLE 4–13



EXAMPLE 4-14



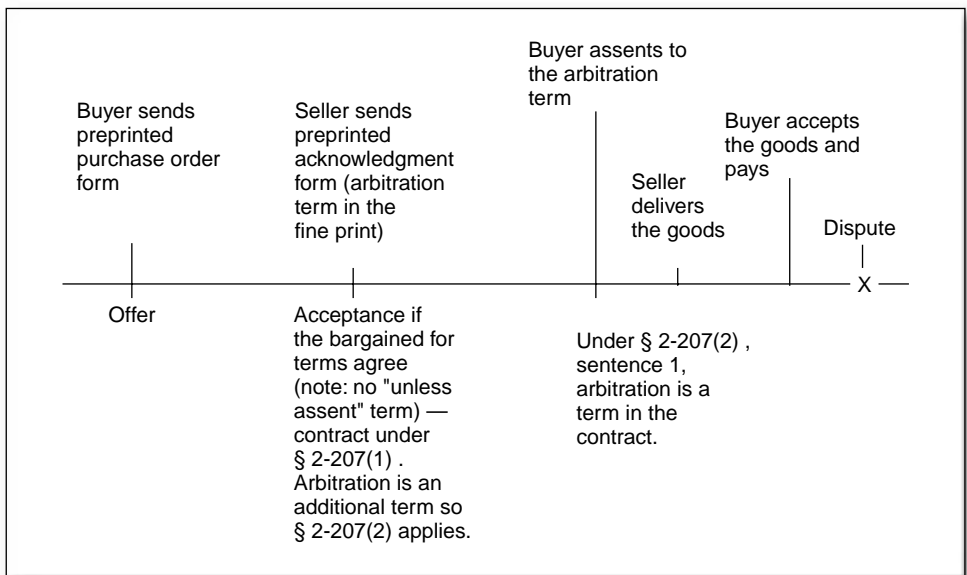
EXAMPLE 4-15



Now that a contract has been formed under subsection (1), it is necessary to determine what boiler plate terms are in this contract. The substantive boiler plate terms of the two forms are compared. The terms will sort into four patterns: those that agree, those that are in the first form but not in the second, those that are in the second form but not in the first, and those that disagree. The boiler plate terms that match are terms of the contract. The boiler plate terms that are in the first form but not in the second are in the contract. The party who issued the second form had an opportunity to object to the first form's term but did not and therefore accepted that term. The boiler plate terms that are in the second form but not in the first form are known as "additional terms" and are discussed in subsection (2). The boiler plate terms that conflict are known as "different terms."

If a term is an additional term, then under the first sentence of subsection (2), it becomes a "proposal for addition to the contract." If the term is accepted, it becomes a part of the contract.

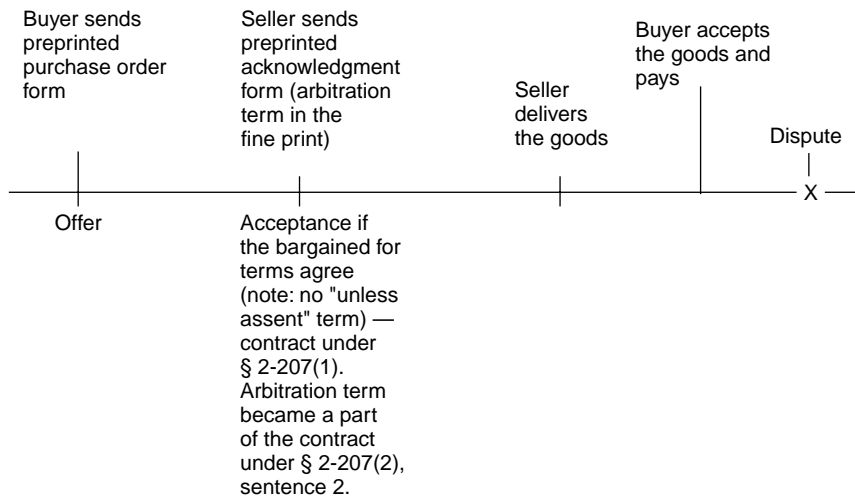
EXAMPLE 4-16



If no action is taken as to the additional term under the first sentence of subsection (2), the second sentence of subsection (2) will come into play. The additional term will become a part of the contract if the contract is "between merchants" and the offer has not expressly limited acceptance to the terms of the offer, the additional term does not materially alter the contract, and notification of objection to the additional term has not already been given or is given within a reasonable time after notice of the additional term is received.

EXAMPLE 4-17

Assume the Buyer and Seller are members of a trade that routinely does business by sending preprinted purchase order forms and preprinted acknowledgment forms and therefore are considered “merchants” for section 2-207(2), sentence 2, purposes. “Merchant” and “between merchants” are defined in section 2-104 and its comment 2. Also assume that the Buyer’s purchase order did not have a term in its boiler plate limiting acceptance to its terms, that the arbitration term did not materially alter the contract since arbitration was the normal method of dispute resolution in that trade, and that the Buyer did not object to the arbitration term until after the dispute arose.



The final step is to check the Uniform Commercial Code for terms that the Code supplies if the contract is silent.

If a substantive boiler plate term in the acceptance is a different term (conflicts with a substantive boiler plate term in the offer), courts are divided in their approach for resolving the issue. Should subsection (2) apply, although subsection (2) does not expressly apply to different terms? Comment 3 to § 2-207 suggests subsection (2) be read “additional or different.” Should the terms knock each other out so neither is in the contract and the terms of the contract are supplemented by the Code’s gap fillers? Comment 6 to § 2-207 suggests this result. Should the term in the acceptance drop out because the offeree had an opportunity to object to this term and did not do so?

PARALEGAL EXERCISE 4.8 The ABC Company sent its purchase order to the Quality Brick Company for six million bricks at \$10 per hundred. ABC's purchase order form was silent as to warranty.

Quality responded by sending its acknowledgment form, which stated six million bricks at \$10 per hundred. Preprinted on Quality's form was the statement "all bricks warranted for ninety days as to defects in materials or workmanship. All other express and implied warranties are disclaimed."

Quality sent the bricks, and ABC accepted the shipment and paid. A year later and after a winter's use, ABC noticed that some bricks were cracking because they were improperly dried during manufacture.

Under UCC § 2-207(1), is there a contract for the sale of the bricks? If there is a contract, then under 2-207(2), is the contract with or without the limited warranty expressed in Quality's acknowledgment form?

PARALEGAL EXERCISE 4.9 The ABC Company sent its purchase order to the Quality Brick Company for six million bricks at \$10 per hundred. ABC's purchase order form was silent as to warranty.

Quality responded by sending its acknowledgment form, which stated six million bricks at \$12 per hundred. Preprinted on Quality's form was the statement "all bricks warranted for ninety days as to defects in material or workmanship. All other express and implied warranties are disclaimed."

Although the forms did not agree as to price, Quality sent the bricks, and ABC accepted the shipment and paid the higher price. A year later and after a winter's use, ABC noticed that some bricks were cracking because they were improperly dried during manufacture.

Under UCC § 2-207(1), is there a contract for the sale of the bricks? If not, is there a contract for the sale of the bricks under 2-207(3)? If there is a contract under 2-207(3), then, under 2-207(3), is the contract with or without the limited warranty expressed in Quality's acknowledgment form?

As this text goes to press, the drafters of the Uniform Commercial Code (the National Conference of Commissioners on Uniform State Laws and the American Law Institute) are considering revisions to Article 2 of the UCC. The revised Article 2 will include a major revision to § 2-207. Once the new Official Draft is finalized, each state's legislature must decide whether to enact it into law for that state. The National Conference of Commissioners on Uniform State Laws, in association with the University of Pennsylvania Law School, is making the drafts of Article 2 available on the web. "UCC Article 2. Sales" may be accessed at the website "Uniform Law Commissioners Drafts" under "Index to

In-Process Draft” or at the website “The Law School at the University of Pennsylvania” under “Biddle Law Library” and the subheading “NCCUSL Uniform and Model Acts.”

Miscommunication between the Offeror and Offeree

An interesting problem occurs when the offeror and offeree say the same thing but mean different things.

EXAMPLE 4–18

Imagine a situation where the buyer and seller of chickens used the term “chickens” but the seller was thinking of “stewing chickens” and the buyer was thinking of “frying chickens.” The seller ships chickens to the buyer, and the buyer is surprised to discover that the chickens are “stewing chickens.”

This miscommunication can be resolved by considering what a reasonable person would have meant had that person been placed in this situation. If the reasonable person had meant what the offeror meant, there would be a contract, and the offeror’s meaning would govern. The offeree’s meaning is disregarded because it does not coincide with the reasonable person’s meaning and is therefore unreasonable.

If the reasonable person had meant what the offeree meant, there would be a contract, and the offeree’s meaning would govern. The offeror’s meaning is disregarded because it does not coincide with the reasonable person’s meaning and is therefore unreasonable.

If the reasonable person would perceive that both meanings are plausible, there would be no contract because the offeror and the offeree do not mean the same thing and the acceptance is not a response to the offer.

Returning to the chickens: if the reasonable person had meant stewing chickens, and stewing chickens happened to coincide with the offeror-seller’s meaning, then the contract would be for stewing chickens, and the seller would not have breached the contract. On the other hand, if the reasonable person had meant frying chickens, and frying chickens happened to coincide with the offeree-buyer’s meaning, then the contract would be for frying chickens, and the seller would have breached the contract by sending stewing chickens. If the reasonable person would perceive that both frying chickens and stewing chickens were plausible, there would be no contract because the offeror (seller) had offered to sell stewing chickens and the offeree (buyer) had attempted to accept frying chickens.

FIGURE 4–5 Miscommunication between the Offeror and Offeree Using an Objective Standard

What the parties said: “chicken”			
What the offeror (seller) meant	stewing chickens	stewing chickens	stewing chickens
What the offeree (buyer) meant	frying chickens	frying chickens	frying chickens
What the reasonable person would have meant	if stewing chickens	if frying chickens	if either stewing or frying chickens
Conclusion	contract for stewing chickens	contract for frying chickens	no contract

PARALEGAL EXERCISE 4.10 In June, Mary planned a dinner party for twenty-eight people and had it catered by Le Gourmet, a French restaurant that specializes in catering dinner parties. In discussing the menu, Mary discovered that Le Gourmet had a “special” that consisted of roast duckling with all the trimmings for \$60 per person. She chose “the special” and the party was a success.

The next month, Mary planned a second dinner party, again for twenty-eight people, and telephoned Le Gourmet and ordered “the special.” Much to Mary’s surprise, when dinner was served, it was pheasant under glass for \$100 per person.

While both Mary and Le Gourmet agreed on “the special,” Mary meant the roast duckling at \$60 per person, while Le Gourmet meant the July special of pheasant under glass at \$100 per person. Has a contract been formed between Mary and Le Gourmet and, if so, was it for the duckling or the pheasant?

The Parties Who Can Accept the Offer

The offeror, by being master of the offer, controls who may accept the offer. An offer made to a specific party can only be accepted by that party. The offeree may not empower someone else to accept, thereby making the other person the offeree.

An offer need not, however, be limited to one party. A number of offers are made to the public in general.

EXAMPLE 4–19

A reward for information leading to the arrest and conviction of the perpetrator of a violent crime is an offer to anyone who supplies the information.

EXAMPLE 4–20

The auctioneer who announces that the auction will be without reserve makes an offer to all those present.

EXAMPLE 4–21

An advertisement that contains the elements of offer is an offer to anyone who reads the ad.

It should be noted that in all of these situations, the offer, while it may be accepted by any party, can be accepted by only one party. Only one party can supply the information, make the highest bid, or purchase each individual item advertised.

THE METHOD FOR ACCEPTING AN OFFER

The offeror, by being the master of the offer, not only establishes the terms of the contract but also establishes how the offeree must accept the offer. The Restatement (Second) of Contracts § 50(1) defines acceptance of an offer as:

a manifestation of assent to the terms thereof made by the offeree in a manner invited or required by the offer.

The offer may be silent as to the method of acceptance, may suggest a method, or may mandate a method. If the offer mandates a method, then that method is how the offer must be accepted.

If the offer does not mandate a method of acceptance, the general rules of contracts law apply, and this takes the discussion back to offers for unilateral and bilateral contracts. If the offer is for a unilateral contract, a promise for a performance, the offer must be accepted by performance. A promise will not do; nor can a promise be used to imply the required performance. Beginning or nearly completing performance is also inadequate as the method of acceptance. Full performance is the method of acceptance unless the offeror has dictated another method.

If the offer is for a bilateral contract, a promise for a promise, it is accepted by a different method. The offer must be accepted by a promise. Full performance is not the method of acceptance. Full performance or even part performance, however, may *imply* the required promise. Implying a promise from performance is not the same as stating that the method of acceptance of an offer for a bilateral contract is performance. The method is a promise, although the promise may be implied from performance.

PARALEGAL EXERCISE 4.11 The Black Forest, a Bavarian restaurant, promised to pay Media International, an advertising agency, \$40,000 for Media's planning and executing a three-month advertising campaign for Black Forest. Media telephoned Black Forest to say that it "accepted" the offer. Has Media accepted the offer?

PARALEGAL EXERCISE 4.12 Same facts as Paralegal Exercise 4.11 but instead of telephoning Black Forest, Media began planning the campaign. Has Media accepted the offer?

PARALEGAL EXERCISE 4.13 The Black Forest promised to pay Media \$40,000 for Media's promise to plan and execute a three-month advertising campaign. Media telephoned Black Forest to say that Media "accepted" the offer. Has Media accepted Black Forest's offer?

PARALEGAL EXERCISE 4.14 Same facts as Paralegal Exercise 4.13 except Media did not telephone but rather began planning the campaign. Has Media accepted Black Forest's offer? Can this question be answered without additional facts? What would these facts be, and why are they essential?

When an offeror specifies a method of acceptance, care should be exercised to determine whether the method stated is the only method or an optional method.

EXAMPLE 4-22

The offer for a bilateral contract states, "This offer may be accepted by beginning performance." Since the offer is in terms of "may," the offeree could accept either by complying with the method stated in the offer (beginning performance) or by following the traditional method for accepting an offer for a bilateral contract (a promise).

PARALEGAL EXERCISE 4.15 The Black Forest promised to pay Media \$40,000 for Media's promise to plan and execute a three-month advertising campaign. The offer stated that Media could accept by either notifying Black Forest or by beginning the advertising campaign. Black Forest first learned that Media was working on a campaign when a Black Forest advertisement appeared in a local newspaper. Has Media accepted Black Forest's offer?

Notice to the Offeror that the Offer Has Been Accepted

When an offer is accepted, the offeror must notify the offeree of the acceptance unless the offer states that the offeree need not notify the offeror. The notice will be different depending on whether the offeror proposes a unilateral or a bilateral contract.

If the offeror proposes a bilateral contract, the offeree must communicate his or her promise to the offeror. If the parties are standing face-to-face or are communicating by telephone, this communication may be oral. If the parties are not in voice contact, then another form of communication, such as a letter, telegram, fax, E-mail, or messenger, could provide the notice.

If the offeror proposes a unilateral contract, the offeree must communicate that his or her performance to the offeror has been completed. If the performance, by its very nature, is known to the offeror as it occurs, then the offeree's act of performance is itself notice to the offeror. If, however, the performance occurs at a distant location so the offeror would not know about it, the offeree must, in some fashion, communicate the completion of performance to the offeror.

WHEN AN ATTEMPTED ACCEPTANCE IS EFFECTIVE

An attempted acceptance is effective when it gives notice to the offeror that the offeree has accepted. If the parties are dealing face-to-face or are in voice contact, such as by telephone, the offeree has the opportunity to give the offeror instant notification.

If, however, the parties are dealing at a distance and are not in voice contact, then each party will be unaware of the other's actions. The offeror will not know that the offeree has mailed an acceptance, nor will the offeree know that the offeror has received the mailed acceptance. Each party operates in the dark for at least a part of the time.

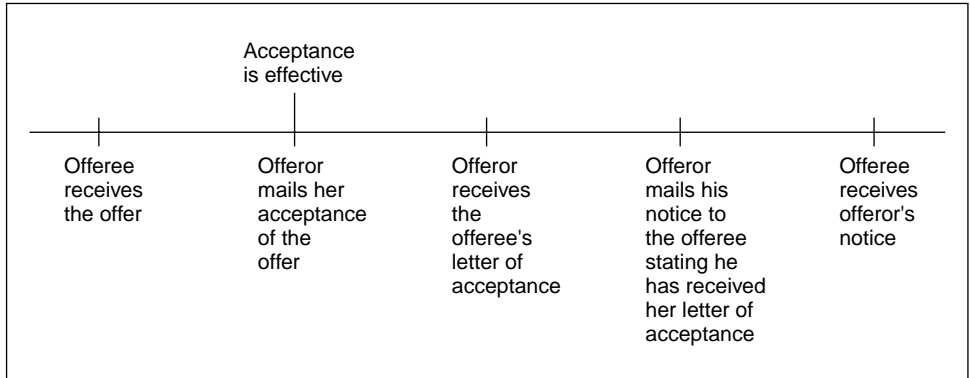
At which point will the mailed acceptance be effective:

1. When the offeree posts her acceptance;
2. When the offeror receives the offeree's acceptance;
3. When the offeror posts his notice to the offeree that he has received her acceptance;
4. When the offeree receives the offeror's notice; or
5. When the offeree posts her notice to the offeror that she has received his notice that he has received her acceptance?

The judges, who shaped the law, selected the least complicated approach—when the offeree posts the acceptance if posting is a medium reasonable in the circumstances. This rule has become known as the **“posting”** or **“mailbox” rule**. The Restatement (2d) of Contracts § 63 (a) follows the mailbox rule:

Unless the offer provides otherwise,

(a) an acceptance made in a manner and by a medium invited by an offer is operative and completes the manifestation of mutual assent as soon as put out of the offeree's possession, without regard to whether it ever reaches the offeror . . .



When the offeror sends the offeree an offer and does not specify a specific method of acceptance, the offeror builds in the risk that the offer may be accepted before the offeror learns of the acceptance. The offeror had the opportunity to create an offer that would minimize these risks. If the offeror chooses not to take advantage of this opportunity, the offeror assumes the risk.

EXAMPLE 4-23

On May 1, the Apex Fireworks Company sent a purchase order to the Zippy Chemical Company to buy all of its requirements of potassium nitrate (saltpeter) for one year for \$100 a ton. Zippy received Apex's purchase order on May 5. On June 1, Apex entered into a requirements contract with Megga Chemical Company at \$90 a ton. Apex did not know that Zippy had mailed an acceptance of Apex's May 1st offer on May 15th. Zippy's letter arrived on June 2d. Since Apex did not specify a method of acceptance that would insure immediate notice of acceptance, Apex now has two contracts to buy all of its requirements of saltpeter: one with Zippy and one with Megga.

Just when an attempted acceptance is effective becomes more complicated when the offeror attempts to revoke the offer. The Restatement (2d) of Contracts § 42 provides the following rule:

An offeree's power of acceptance is terminated when the offeree receives from the offeror a manifestation of an intention not to enter into the proposed contract.

EXAMPLE 4-24

Seller sent a letter to Buyer offering to sell Buyer a computer for \$2,000. Buyer received Seller's letter on June 1st. On June 5th Seller sent a letter to Buyer revoking her offer. On June 6th Buyer sent a letter of acceptance to the Seller. On June 7th Buyer received Seller's letter attempting to revoke the offer. On June 8th Seller received Buyer's letter.

Seller sends Buyer offer	Buyer receives Seller's offer	Seller sends Buyer attempted revocation	Buyer sends Seller attempted acceptance	Buyer receives Seller's attempted revocation	Seller receives Buyer's attempted acceptance
	6/1	6/5	6/6	6/7	6/8
			Acceptance is effective		

Under the Restatement (2d) of Contracts § 63(a), the Buyer's acceptance was effective on June 6th, the date when the acceptance was sent. Under the Restatement (2d) of Contracts § 42, the Seller's attempted revocation was effective on June 7th, the date when the attempted revocation was received. Since the Buyer's acceptance was effective before the Seller's attempted revocation, the contract was formed.

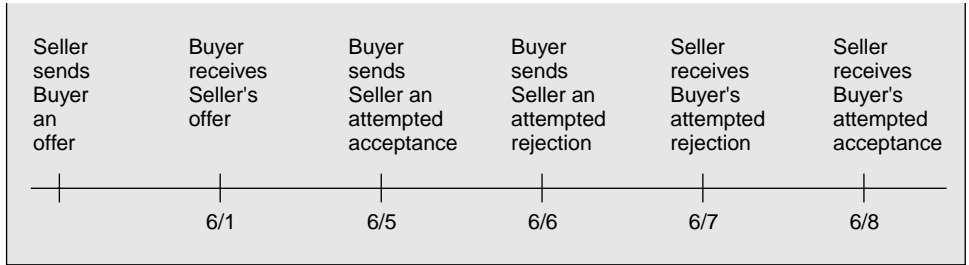
PARALEGAL EXERCISE 4.16 Seller sent a letter to Buyer offering to sell Buyer a computer for \$2,000. Buyer received Seller's letter on June 1st. On June 5th Buyer sent a letter to Seller attempting to accept the offer. On June 6th Seller sent a letter of revocation to the Buyer. On June 7th Seller received Buyer's letter attempting to accept its offer. On June 8th Buyer received Seller's letter. Has the Buyer accepted the Seller's offer?

Seller sends Buyer an offer	Buyer receives Seller's offer	Buyer sends Seller an attempted acceptance	Seller sends Buyer an attempted revocation	Seller receives Buyer's attempted acceptance	Buyer receives Seller's attempted revocation
	6/1	6/5	6/6	6/7	6/8

Just when an attempted acceptance is effective becomes even more complicated when the offeree attempts to reject the offer. If the offeree sends an acceptance before sending a rejection, the general rule is that a rejection is not effective until it is received by the offeror.

PARALEGAL EXERCISE 4.17 If an acceptance is effective when sent and a rejection is effective when received, has a contract been formed in the following two situations?

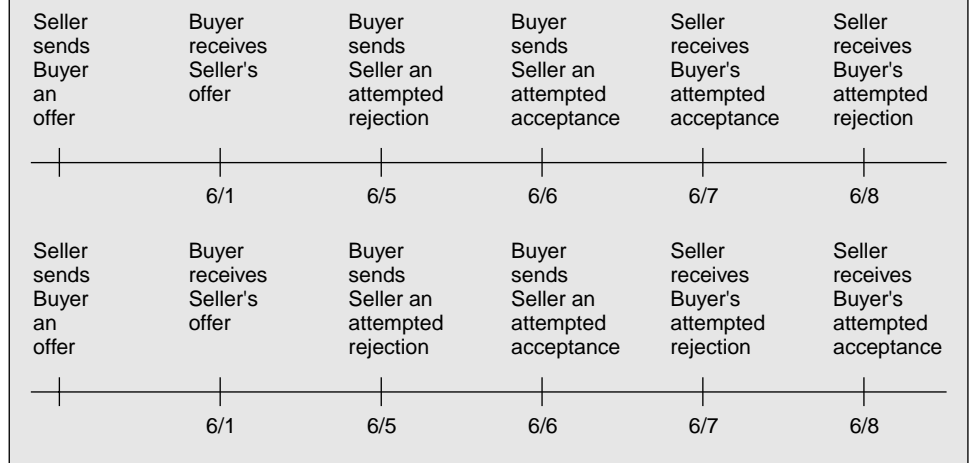
Seller sends Buyer an offer	Buyer receives Seller's offer	Buyer sends Seller an attempted acceptance	Buyer sends Seller an attempted rejection	Seller receives Buyer's attempted acceptance	Seller receives Buyer's attempted rejection
	6/1	6/5	6/6	6/7	6/8



If, however, the offeree sends the rejection before sending the acceptance, the rule reaches a new level of complexity. The Restatement (2d) of Contracts § 40 formulates the rule as follows:

Rejection . . . by mail or telegram does not terminate the power of acceptance until received by the offeror, but limits the power so that a letter or telegram of acceptance started after the sending of an otherwise effective rejection . . . is only a counter-offer unless the acceptance is received by the offeror before he receives the rejection. . . .

PARALEGAL EXERCISE 4.18 Using Restatement (2d) of Contracts §§ 42 and 63(a), has a contract been formed in the following two situations?



A final problem remains. If an offer is made that is followed by an option contract negating the offeror's power to revoke its offer and the offeree's power to reject the offer, the time when the attempted acceptance of the original offer shifts from the time when the attempted acceptance is sent (Restatement (2d) of Contract § 63(a)) to the time when the attempted acceptance is received (Restatement (2d) of Contracts § 63(b)).

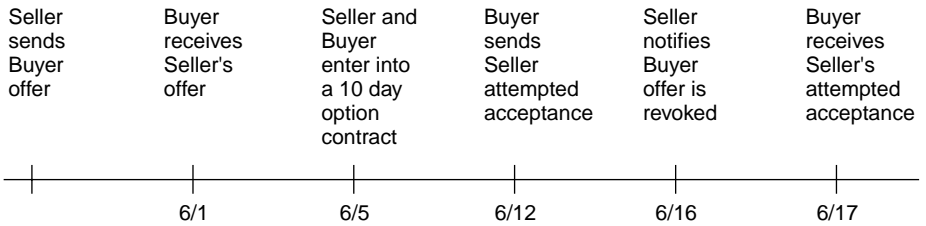
Unless the offer provides otherwise,

(a) an acceptance made in a manner and by a medium invited by an offer is operative and completes the manifestation of mutual assent as soon as put out of the offeree's possession, without regard to whether it ever reaches the offeror; but

(b) an acceptance under an option contract is not operative until received by the offeror.

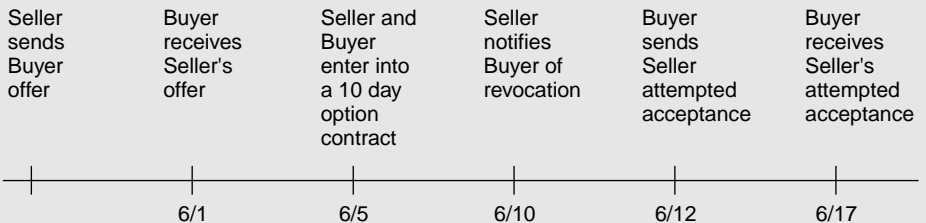
EXAMPLE 4-25

Seller sent a letter to Buyer offering to sell Buyer a computer for \$2,000. Buyer received Seller's letter on June 1st. On June 5th Seller and Buyer entered into an option contract whereby Seller promised not to revoke her offer for 10 days. On June 12th Buyer sent a letter attempting to accept Seller's offer. On June 16th, Seller notified Buyer that her offer was revoked. On June 17th Buyer received Seller's letter of acceptance.



Under the Restatement (2d) of Contracts § 63(a), Buyer's acceptance was effective on June 12th, the date when the acceptance was sent. The option contract, however, changes the rules. Under the Restatement (2d) of Contracts § 63(b), Buyer's acceptance is not effective until it is received. Since Buyer's acceptance was not received until June 17, a day after Seller revoked her offer, Buyer's attempted acceptance was ineffective and no contract was formed.

PARALEGAL EXERCISE 4.19 Seller sent a letter to Buyer offering to sell Buyer a computer for \$2,000. Buyer received Seller's letter on June 1st. On June 5th Seller and Buyer entered into an option contract whereby Seller promised not to revoke her offer for 10 days. On June 10th, Seller notified Buyer that her offer was revoked. On June 12th Buyer sent a letter attempting to accept Seller's offer. On June 17th Buyer received Seller's letter of acceptance. Has a contract been formed?

**IS A RESTITUTION ACTION AN ALTERNATIVE TO ACCEPTANCE?**

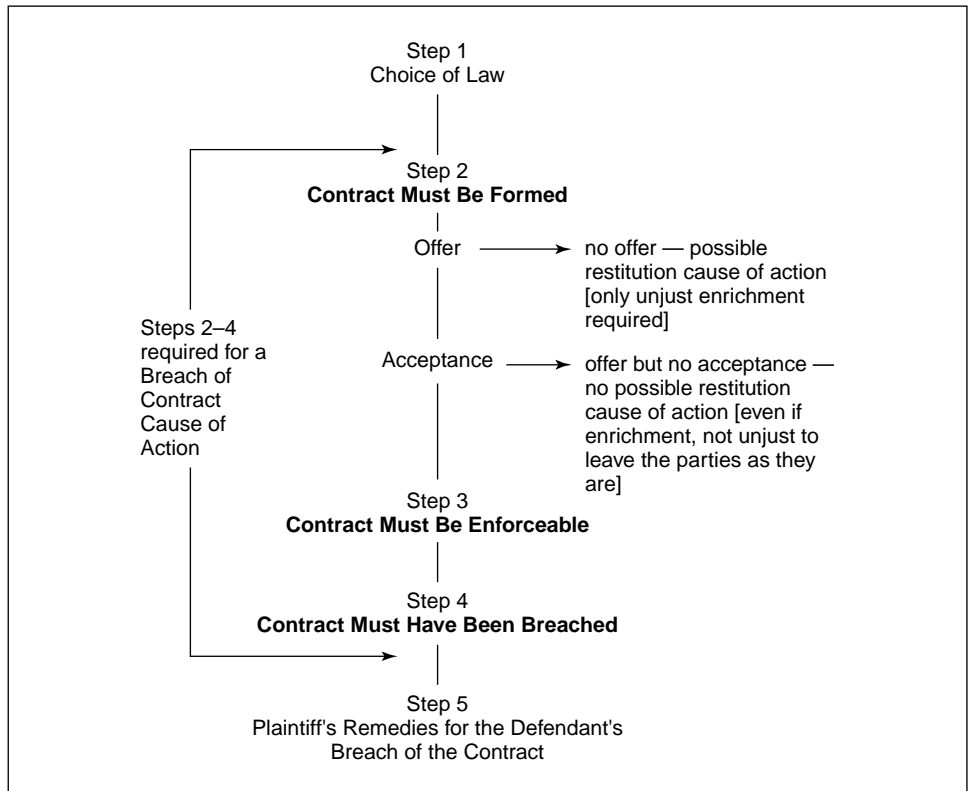
If the offer is not accepted, no contract is formed and neither party may maintain a cause of action for breach of contract. Is another cause of action, a restitution cause of action, available?

Before answering this question, it is important to understand that the phrase "restitution cause of action" has been selected to encompass all the *actions*

based on unjust enrichment. This *unjust enrichment cause of action* often masquerades under many names, such as an action in quasi contract, an action on an implied (by law) or constructive contract, or an action for assumpsit, *quantum meruit* (a common law form of action meaning “as much as he deserves for his work and labor”), or *quantum valebant* (a common law form of action meaning “as much as the goods sold and delivered were worth”). To add to the confusion, a breach of contract cause of action also masquerades as an action for assumpsit, *quantum meruit*, or *quantum valebant*. What the cause of action is labeled is unimportant. What is important are the requirements necessary for the cause of action. For a restitution cause of action, the requirement is unjust enrichment. For a breach of contract cause of action, the requirements are a contract, that is enforceable, and that has been breached.

In Chapter 2 we have seen the availability of a restitution cause of action if no offer has been made and if one party conferred a benefit on another party and it would be unjust to permit the party with the benefit to retain it without compensating the party who conferred the benefit. This was a restitution cause of action based on unjust enrichment and not a breach of contract action.

FIGURE 4–6 Comparing the Requirements for a Breach of Contract Cause of Action with the Requirements for a Restitution Cause of Action



In Chapter 4 we have moved beyond the offer but because the offer has not been accepted, no contract has been formed and neither party can maintain a cause of action for breach of contract. If the offer has not been accepted and if one party conferred a benefit on another party, would it be unjust to permit the party who received the benefit to retain it without compensating the party who conferred it? Could a restitution cause of action based on unjust enrichment be maintained when an offer has not been accepted? A restitution cause of action cannot be maintained if the benefit was conferred by a volunteer. An offeror who confers a benefit after making an offer runs the risk of being labeled a volunteer and as such will be denied a restitution cause of action if the offeree does not accept the offer (see Figure 4–6).

The situation in *Gould v. American Water Works* presents the problem of the offeror. Gould, the landowner, offered to sell his land to the Bernards Water Company and sought to entice the Water Company by drilling a productive water well on his own land. The Water Company, now knowing that the land would produce the water required, purchased land adjacent to Gould's since that land could be purchased at a better price. Did Gould confer a benefit on the Water Company? Does this benefit constitute an enrichment? Was the Water Company *unjustly* enriched?



CASE

Gould v. American Water Works Service Co.

Supreme Court of New Jersey, 1958. 52 N.J. 226, 245 A.2d 14.

PER CURIAM.

The issue here is whether plaintiff, Jasper C. Gould, has a cause of action for damages against defendant The Bernards Water Company in *quasi* or implied contract based upon alleged unjust enrichment resulting from defendant's appropriation and use of information developed through plaintiff's efforts and skill in locating underground water wells. The trial court decided that the evidence created a jury question on the subject and the jury found for plaintiff Jasper Gould. The complaint against defendant American Water Works Service Co., Inc. was dismissed and has not been appealed. The Appellate Division, in an unreported opinion, reversed, holding that plaintiff was a mere volunteer and that no legal basis existed for imposing a *quasi*-contractual liability on defendant. We granted certification. 51 N.J. 182, 238 A.2d 469 (1968).

Plaintiff Jasper C. Gould is an experienced well digger. Defendant is a public utility engaged in the business of selling water to the public in Bernards Township and other localities. In 1953 plaintiff learned from a friend of many years standing, one Burd, who was in defendant's employ as a superintendent, that the company was interested in developing an additional water supply. Upon Gould's inquiry, Burd indicated the company's interest was in wells which would yield 200 to 225 gallons of water a minute. Gould asked also what the company would be willing to pay for such a well. Burd replied he was not the "boss" but he knew it would pay a fair price. Nothing further was said. The friendship between Gould and Burd was purely social. They had had no business relationship. Some time later Burd asked Gould if he would be gracious enough to talk with defendant's geologist. Gould agreed and

spent two days with the geologist showing him wells Gould had dug on his own property and discussing conditions he encountered in doing so.

Thereafter, in the latter part of 1953 or early 1954, Gould spent some time drilling a well on five acres of land he owned in Bernards Township. At a depth of 365 feet the well delivered only 60 gallons a minute, so he abandoned it. He moved his equipment 80 feet farther in on his property and began to drill again. This time, after going down 670 feet, he located water and the well yielded over 200 gallons per minute. A short time later, at a social gathering, Gould told Burd he had a very good well and inquired as to whether the company would be interested in seeing a pump test on it. Burd said he would find out from his superiors, and a few days later he advised Gould his superiors would like to have such a test. In April 1954 the test was made. It revealed the well was yielding over 300 gallons a minute. In another conversation with Gould, Burd said the well was not large enough to admit defendant's pumping equipment and asked what it would cost to enlarge it from six to ten inches. It is undisputed that Gould never furnished a figure. Instead he proceeded to ream the well to a 10-inch diameter for a depth of 250 feet. He admitted that nobody connected with the water company asked him to do so.

Later in 1954, how much later does not appear, Gould met with Burd's superiors who offered \$12,000 for the well. There was no discussion about whether the offer was for title to the land or an easement. The conference was a short one because Gould asked for \$100,000. About a year later defendant offered \$12,000 to \$13,000. It was again rejected. Some time later in 1955 or in 1956 Gould reduced his asking price to \$50,000, but defendant was not interested. Finally about five years later, in 1960 or 1961, defendant offered \$16,000 and Gould lowered his figure to \$35,000. The negotiations ended on that note and no agreement was ever reached.

Gould conceded that no representative of defendant asked or authorized him to dig a well or to prospect for water in its behalf, or ever agreed that if he dug a well which produced water at the rate of 200 gallons a minute the company would buy it from him.

In August 1961 defendant acquired property on the south side of Route 202 opposite Gould's acreage and began to dig 490 feet from Gould's well. In March 1962, eight years after completion of Gould's second well, defendant's digging reached 1450 feet in depth and produced sufficient water to move defendant to obtain a permanent diversionary permit from the State Division of Water Policy and Supply to divert up to 500,000 gallons of water a day from the well. About a year later plaintiff brought this action seeking damages from the water company. He alleged that defendant had been unjustly enriched as the result of plaintiff's well-digging activity and the knowledge defendant acquired thereby that water was to be found in the immediate area to an extent which defendant, as a seller of water to the public, was interested in locating and acquiring. More specifically, plaintiff claimed that defendant had encouraged him to dig wells to locate water of the volume desired. Thus when he dug such a well, and informed defendant of the location, defendant's failure to buy it coupled with the subsequent use of the information as the incentive for acquiring nearby property and digging a sufficiently productive well of its own, unjustly enriched defendant at plaintiff's expense. Therefore, plaintiff contended, in order to do justice the law ought to impose an obligation on defendant to pay plaintiff for the expenses and losses resulting from defendant's inequitable conduct.

After consideration of the entire record, we agree with the Appellate Division that plaintiff's proof fails to establish a claim upon which relief can be granted. We concur in its declaration:

"The evidence is uncontradicted that what the plaintiff did was not done at the request of Bernards nor with any expectation at that time that he would be reimbursed by Bernards for his well digging expenses. Plaintiff * * * [Gould] dug the

two wells on his property on his own initiative in the hope that if he were successful in finding an adequate water supply, he would be able to negotiate for a sale of the well or an interest in his property to the water company. The fact that the drawn-out negotiations were unsuccessful because the parties did not agree on a price affords no basis for imposing a *quasi*-contractual liability on defendant, nor is such basis to be found in the fact that defendant thereafter dug its own well approximately 500 feet away to a depth almost twice that of plaintiff's well. See Restatement, Restitution, § 2, p. 15; § 112, p. 461; § 41, p. 162 (1937)."

In our judgment the plaintiff occupied the status of a volunteer who hoped that if his efforts produced a result which would interest defendant, an agreement to sell that result to defendant could be consummated. The fact that plaintiff knew defendant was interested generally in locating an additional water supply in the area would not transform his status from volunteer into an obligee when he found a source which defendant could use. Nor would the fact that defendant offered to buy the well at its price make it an obligor.

When the negotiations broke off, it meant that plaintiff's speculative venture had failed to achieve its ultimate purpose. If it is assumed that defendant had learned from plaintiff's unsolicited efforts that there was substantial underground water in the area, and to that extent was the recipient of a benefit, such enrichment should not be regarded as unjust enrichment creating a liability for plaintiff's expenses and losses simply because defendant, encouraged by plaintiff's experience, acquired nearby property, dug a well about 500 feet from that of plaintiff and more than twice as deep, and located an acceptable additional supply of water.

Accordingly the judgment of the Appellate Division is affirmed.

For affirmance: Chief Justice WEINTRAUB and Justices JACOBS, FRANCIS, PROCTOR, HALL, SCHETTINO and HANEMAN—7.

For reversal: None.



PARALEGAL CHECKLIST

The Acceptance Phase

- If the offer has not been revoked by the offeror, rejected by the offeree, or lapsed, check whether the offer has been accepted. Evaluate the following:
 1. Does the apparent acceptance have the necessary elements to be an acceptance?
 - If the offer was for a unilateral contract, the acceptance is: (1) the offeree's full performance; (2) consideration for the offeree's full performance (i.e., the offeror's promise); and (3) the offeree must have fully performed in order to obtain the offeror's promise.
 - If the offer was for a bilateral contract, the acceptance is: (1) the offeree's promise; (2) consideration for the offeree's promise (i.e., the offeror's promise); and (3) the offeree must be promising in order to obtain the offeror's promise.
 - a. The acceptance must be in response to the offer.
 - (1) If the offer is for a bilateral contract, the offeree must have knowledge of the offer before responding with a promise. Otherwise the offeror's promise is not inducing the offeree to respond and, therefore, the offeree's response is not an effective acceptance.

If the offer is for a unilateral contract, the Restatement (First) of Contracts § 53 would require the offeree to have knowledge of the offer before beginning the requested performance. The Restatement (Second) of Contracts § 51 requires only that the offeree learn of the offer sometime prior to completing the requested performance.

- (2) The offeror's promise must not be subject to a pre-existing duty. Otherwise, the offeror's promise cannot be consideration for the offeree's promise or performance.
 - b. The offeree must agree to the offeror's terms.
 - (1) Under the common law mirror image rule, the offeree must agree to all of the offeror's terms. Any deviation constitutes a rejection of the offeror's offer and is a counteroffer by the offeree. If the offeree's response is a counteroffer and the offeror begins performance of its promise, the performance may constitute an implied (in fact) promise to accept all of the offeree's terms and the contract is formed under the offeree's terms. This is known as the "last shot" doctrine. The party who makes the last express offer prior to performance by the other party is the party whose terms control the transaction.
 - (2) If the transaction is a sale of goods, Article 2 of the Uniform Commercial Code applies and a contract may be formed if the bargained for terms (the variable terms) coincide. An application of UCC § 2-207 determines what other terms, if any, are a part of the contract.
 - (3) If the offeror and offeree say the same thing but mean different things, the outcome is determined by the reasonable person's perception of what the parties said. If the reasonable person's perception coincides with the offeror's meaning, the contract was formed and the meaning would be the offeror's meaning. If the reasonable person's perception coincides with the offeree's meaning, the contract was formed and the meaning would be the offeree's meaning.
2. Did the offeree notify the offeror that the offer has been accepted?
 - a. If the offer was for a bilateral contract, the offeree must communicate acceptance to the offeror. The communication need not follow a special method unless the offeror has required a special method in the offer.
 - b. If the offer was for a unilateral contract, the offeree's communication of acceptance is normally obvious to the offeror by the offeree's performance. Where, however, the offeror would not see the offeree's performance, the offeree must communicate acceptance (the completion of performance) to the offeree.
 3. Who may accept the offer? The offeror controls who may accept the offer. An offer made to a specific party can be accepted only by that party. An offer, however, made to the general public can be accepted by anyone.
 4. Who sets the terms of the contract and establishes the method by which the offer must be accepted? The offeror, as the master of the offer, not only sets the terms of the contract but also establishes the method by which the offeree must accept the offer.
 - a. If the offeror mandates the method of acceptance, that method is the appropriate method.
 - b. If the offeror does not mandate a method of acceptance and the offer is for a unilateral contract, the offer must be accepted by full performance.
 - c. If the offeror does not mandate a method of acceptance and the offer is for a bilateral contract, the offer is accepted by a promise. The promise can, however, be implied from performance.
 - d. When an offeror specifies a method of acceptance, care must be exercised to determine whether the method stated is an optional method or the only method.
 5. When will the mailed acceptance be effective? If the offeror and offeree are dealing at a distance and are not in voice contact, each party will be unaware of the other's actions. If the offeree mails an acceptance, the acceptance is effective when posted.
 6. When will the offeree not be liable in a restitution cause of action for a benefit received? If the offeror confers a benefit on the offeree after making the offer but the offeree does not accept the offer, the offeree will not be liable in a restitution cause of action for the benefit received.

REVIEW QUESTIONS

DEFINE THE FOLLOWING NEW TERMS AND PHRASES

Acknowledgment form	Last shot doctrine
Additional term	Mailbox rule
Bargained for terms	Merchant
Between merchants	Mirror image
Boiler plate terms	Posting rule
Definite expression of acceptance	Purchase order
Different term	Seasonable expression of acceptance

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

1. T F An offeror can propose either a unilateral or bilateral contract.
2. T F The offer for a unilateral contract is a promise.
3. T F If the offer is for a bilateral contract, the offeree must have knowledge of the offer before responding with a promise.
4. T F If an offer is for a unilateral contract, the offeree's performance is acceptance of the offer even though the offeree performed without learning of the offer until after completing the requested performance.
5. T F The "pre-existing duty" rule which applies to consideration for the promisor's promise does not apply to consideration for the promisee's promise or performance.
6. T F Under the common law, the offeree need not agree to all of the offeror's terms for there to be an acceptance.
7. T F Alfred sent a letter promising to purchase Jan's 1965 T-Bird for Jan's promise to sell for \$5,500. Jan wrote Alfred that she would sell for \$5,500 if Alfred would let her drive it in one more road rally. Under the common law, the offer has been accepted.
8. T F The offeror is master of the offer and controls the terms of the contract.
9. T F Under the common law mirror image rule, the offeree cannot change the terms of the offer in the acceptance.
10. T F The preprinted terms on the forms used in commercial transactions are called "armor plate."
11. T F When the offeror and the offeree say the same thing but mean different things, a mistake in understanding the offer occurs.
12. T F A mistake in understanding the terms of the offer can be resolved by considering what the average person would have meant if he or she had been placed in this situation.

13. T F The seller wrote the buyer that she would sell her bean crop to him for \$3 a bushel. The buyer wrote back that he would be happy to buy her bean crop for \$3 a bushel. The seller has a crop of Kentucky Wonders. The buyer thinks the seller has a crop of Blue Lakes. The buyer has never seen the seller's crop. If both the buyer's and the seller's perception of the manifestation "bean" were reasonable, the buyer's letter would not be an acceptance of the seller's offer.
14. T F As a general rule, the offeree does not need to notify the offeror that the offer has been accepted.
15. T F If the offeree decides not to accept the offer, he or she may empower someone else to accept it.
16. T F An offer must be limited to one party.
17. T F The offeror establishes the method by which the offeree must accept the offer.
18. T F If the offeror does not mandate the method of acceptance, the general rules of contract law apply.
19. T F The "mailbox" rule is also known as the "posting" rule.
20. T F Under the "mailbox" rule, an acceptance is effective when it is received in the mail by the offeror.
21. T F If after an offer has been created, the offeror confers a benefit on the offeree and the offeree subsequently rejects the offer but retains the benefit, the offeror could successfully maintain a restitution cause of action against the offeree for unjust enrichment.
22. T F The restitution action is an alternative to a breach of contract action.

FILL-IN-THE-BLANK QUESTIONS

1. _____. The phase after the transaction passes through the post-offer/pre-acceptance phase.
2. _____. The type of contract that results when the offer is a promise for a performance.
3. _____. The type of contract that results when the offer is a promise for a promise.
4. _____. A common law rule which prevents the offeree from changing the terms of the offer in his or her acceptance.
5. _____. A rule which prevents a prior obligation from being consideration for a promise or performance.
6. _____. The master of the offer.
7. _____. Preprinted terms on the forms used in commercial transactions.

8. _____. A rule which provides that acceptance is effective when the offeree posts his or her acceptance.
9. _____. An action available only when a breach of contract action cannot be maintained.
10. _____. The last offer under the common law mirror image rule.
11. _____. A problem that occurs when the offeror and offeree say the same thing but mean different things.
12. _____. The party controlling who may accept the offer.
13. _____. A manifestation of assent to the terms of the offer.

MULTIPLE CHOICE QUESTIONS (CIRCLE ALL THE CORRECT ANSWERS)

1. One evening, Harry, a chimpanzee, escaped from the local zoo. WGAB, a local radio station, offered a reward of \$500 for the capture and return of Harry. That evening Carlos found a chimpanzee in his garage. Since it was too late to call the animal shelter, Carlos thought he would try to take the chimp to the zoo. Maybe they could take care of him. Carlos put the chimp in his van and began to drive to the zoo. As he drove he happened to hear an announcement on WGAB about Harry's escape and the information concerning the reward. Carlos continued to the zoo, left Harry, and then demanded his reward from WGAB.
 - (a) Carlos is not entitled to the reward because rewards are not offers
 - (b) Carlos is not entitled to the reward because he did not call WGAB to promise to capture Harry
 - (c) Carlos is not entitled to the reward because under Restatement (First) of Contracts § 53 (1932) he must have knowledge of the offer before beginning the requested performance
 - (d) Carlos is entitled to the reward because under Restatement (Second) of Contracts § 51 (1979) he must have knowledge of the offer only before completing the requested performance
 - (e) Carlos is not entitled to the reward because as a good citizen, he had a pre-existing duty to capture and return Harry to the zoo
2. ABC Company sent the XYZ Company a purchase order for 50,000 metal bracelets at \$.50 each. ABC's purchase order contained the following provision in its fine print: "all disputes will be settled by arbitration." XYZ sent its acknowledgment form to ABC and subsequently shipped the bracelets. XYZ's form stated in its fine print: "all disputes will be settled by mediation-arbitration." ABC accepted the shipment and paid.
 - (a) Under common law, XYZ's acknowledgment form constitutes the acceptance
 - (b) Under common law, XYZ's shipment constitutes the acceptance
 - (c) Under common law, ABC's acceptance of the shipment and payment constitutes the acceptance

- (d) Under UCC § 2-207 (1), XYZ's acknowledgment form constitutes the acceptance
 - (e) Under UCC § 2-207 (3), ABC's acceptance of the shipment and payment constitutes the acceptance
3. ABC Company sent the XYZ Company a purchase order for 50,000 metal bracelets at \$.50 each. ABC's purchase order contained the following provision in its fine print: "all disputes will be settled by arbitration." XYZ sent its acknowledgment form to ABC and subsequently shipped the bracelets. XYZ's form stated in its fine print: "all disputes will be settled by mediation-arbitration." XYZ's form also stated "this is not an acceptance unless the buyer assents to all of the seller's terms." ABC accepted the shipment and paid.
- (a) Under common law, XYZ's acknowledgment form constitutes the acceptance
 - (b) Under common law, XYZ's shipment constitutes the acceptance
 - (c) Under common law, ABC's acceptance of the shipment and payment constitutes the acceptance
 - (d) Under UCC § 2-207 (1), XYZ's acknowledgment form constitutes the acceptance
 - (e) Under UCC § 2-207 (3), ABC's acceptance of the shipment and payment constitutes the acceptance
4. ABC Company sent its purchase order form to XYZ Company for the purchase of 4,000 valves at \$32 each. ABC's form stated in its boilerplate "ABC reserves all express and implied warranties." XYZ responded with its acknowledgment form which stated in its boilerplate "all express and implied warranties are disclaimed." XYZ shipped the valves and ABC accepted the shipment and paid.
- (a) Under UCC § 2-207 (1), XYZ's acknowledgment form is the acceptance of ABC's offer, even though it states terms different from those in the offer
 - (b) Under UCC § 2-207(3), a contract has been formed by the conduct of the parties
 - (c) XYZ's disclaimer is a term in the first form but not in the second and therefore is a term in the contract
 - (d) XYZ's disclaimer is an additional term and under UCC § 2-207(2) may or may not be a term in the contract
 - (e) XYZ's disclaimer is a different term and may or may not be a term in the contract depending on whether the knockout, dropout, or the UCC § 2-207(2) approach is used
5. ABC Company sent its purchase order to XYZ Company for the purchase of 5,000 steel rods at \$1 each. XYZ sent its acknowledgment form which stated 4,500 steel rods at \$1 each. In the boilerplate of XYZ's acknowledgment form, XYZ disclaimed all express and implied warranties. XYZ shipped the rods and ABC accepted the shipment and paid.
- (a) Under UCC § 2-207(1), XYZ's acknowledgment form was the acceptance
 - (b) Under UCC § 2-207(2), XYZ's acknowledgment form was the acceptance
 - (c) Under UCC § 2-207(3), the shipping and accepting shipment and paying constituted a contract
 - (d) Under UCC § 2-207(3), the contract contains all implied warranties
 - (e) Under UCC § 2-207(3), all express and implied warranties are excluded from the contract

6. Alex wrote a letter to Sally promising to pay for a trip to Europe if Sally would promise to take Alex's daughter with her. When is this offer accepted?
 - (a) when Sally posts her acceptance
 - (b) when Alex receives Sally's acceptance
 - (c) when Alex posts his notice to Sally stating that he has received her acceptance
 - (d) when Sally posts her notice to Alex stating that she has received his notice that he has received her acceptance
 - (e) when she takes Alex's daughter to Europe

SHORT ANSWER QUESTIONS

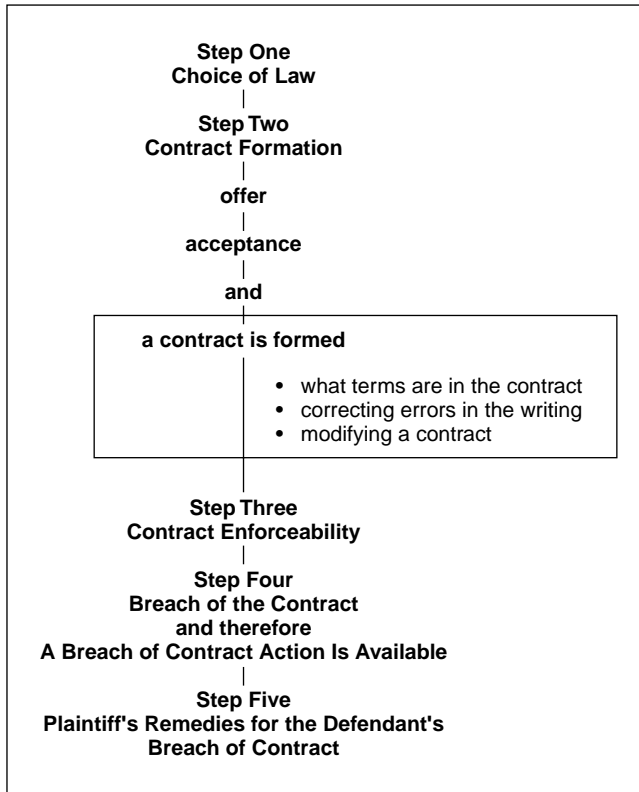
1. On March 1st, Bernadette mailed her cousin Agnes a letter stating that she would pay Agnes \$100 if Agnes would promise to sell her grandmother's antique cake stand. On March 2d, Agnes wrote to her cousin Bernadette stating that she would sell Bernadette her grandmother's cake stand if Bernadette would promise to pay \$100. Agnes received Bernadette's letter on March 4th. Bernadette received Agnes's letter on March 5th. Has a contract been formed?
2. Jose wrote Charlene, an artist, promising to pay her \$2,500 if she painted his daughter's portrait. As it happened, Charlene had already begun to paint the portrait when she received Jose's letter. Charlene completed the portrait. Has Jose's offer to pay \$2,500 been accepted by Charlene?
3. John had a statutory duty to support his daughter, Anne, until she became 18. John wrote his father promising to support Anne until she became 18 if his father would promise to leave her the family farm. John's father wrote John promising to leave the family farm to John's daughter for John's promise to support her until she became 18. At the time John's father made his promise, Anne was 7. Has John's father accepted John's offer?
4. When Sam was 17, Uncle Bob promised Sam, his nephew, that if Sam would refrain from smoking and drinking until he was 21, Uncle Bob would pay Sam \$5,000. Was a contract formed when Sam promised Uncle Bob that he would refrain?



The Post-Acceptance Phase

- ◆ What Are the Terms of the Contract?
 - Interpreting the Language of the Contract*
 - Identifying the Terms Included in the Contract*
 - Supplying Omitted Terms*
- ◆ Correcting Errors in the Written Contract: Mistake in Integration
- ◆ Modifying a Contract
- ◆ Ending a Contract Before It Has Been Fully Performed
 - Terminating a Contractual Duty When Neither Party Has Fully Performed*
 - Terminating a Contractual Duty When One Party Has Fully Performed*
 - Terminating a Noncontractual Duty*
 - Terminating a Contractual or Noncontractual Duty with a “Payment in Full” Check—The Accord and Satisfaction*

Chapter Five focuses on the contract after it comes into existence. This chapter begins with the terms of the contract. When the language of a contract may have more than one meaning, various rules of construction may be used to interpret that language. When a contract has been reduced to a

FIGURE 5-1 The Post-Acceptance Phase of the Road Map

final writing, the contract may consist of only those terms found in the final writing or those terms in the final writing plus additional terms. Also, some terms, such as “good faith,” may be added to the contract even though the parties had never discussed their inclusion.

The parties may sign a final writing only to discover later that the writing did not accurately capture their agreement. Chapter Five explores the problems that arise when parties attempt to correct errors in the written contract (the mistake in integration).

After the creation of a contract but before full performance, the needs of the contracting parties may change. The parties may attempt to modify their contract.

The parties may want to go beyond modification and terminate their contractual relationship without completing their contractual duties. Four topics are investigated: terminating a contractual duty when neither party has fully performed; terminating a contractual duty when one party has fully performed; terminating a noncontractual duty; and terminating a contractual or noncontractual duty with a “payment in full” check (the accord and satisfaction) (see Figure 5-1).

WHAT ARE THE TERMS OF THE CONTRACT?

Now that the parties have contracted, what have they agreed to do? The answer clearly comes from the contract, whether oral or written. The contract should contain their rights and duties. The parties, however, may interpret the language of the contract differently, or they may not agree as to which terms are included in the contract.

Interpreting the Language of the Contract

Words are vessels filled with ideas. Although words have standard meanings, these meanings may vary from time to time and region to region. Meanings may vary depending on whether the term is used in its general sense or as a trade term. **Trade usage**, as defined in UCC § 1-205(2), gives a term a special meaning when

any practice or method of dealing having such regularity of observance in a place, vocation or trade as to justify an expectation that it will be observed with respect to the transaction in question.

Lewis Carroll, in his classic *Through the Looking-Glass*, captures the full flavor in this go-around between Alice and Humpty Dumpty:

“But ‘glory’ doesn’t mean a nice knockdown argument,” Alice objected.

“When I use a word,” Humpty Dumpty said, in rather a scornful tone, “it means just what I choose it to mean—neither more nor less.”

“The question is,” said Alice, “whether you can make words mean so many different things.”

“The question is,” said Humpty Dumpty, “which is to be master—that’s all.”

Regardless of what Humpty Dumpty believes, a contract term is interpreted according to its “plain meaning.” **Plain meaning** is the meaning that reasonable people would give to that term. If a term has a plain meaning but one of the parties secretly attributes a special meaning to that term, the term will be interpreted according to its plain meaning. Because contracts are consensual, the parties may, at the time of contracting, agree to give the term a meaning other than its plain meaning.

A term may have two meanings, one known by the general population and the other used in a particular trade. If both parties to the contract are members of the trade, the term is interpreted according to its trade meaning. If only one party is a member of the trade, the nontrade meaning applies. If one party is a long-standing member of the trade and the other is new to the trade, the nontrade meaning will apply unless the party new to the trade has actual knowledge of the trade meaning or the trade meaning was so generally known that actual knowledge could be inferred.

Consider the interpretation of the term “50 percent protein” in *Hurst v. W.J. Lake & Co.* Hurst, the seller of horse meat scraps, contracted to give W.J. Lake & Co., the buyer, a \$5 discount for each ton analyzing less than 50 percent pro-

tein. When 140 tons of scraps contained protein varying from 49.53 percent to 49.96 percent, Lake claimed the discount. Hurst objected asserting that 50% was a trade term and in the trade 50% was really 49.5%. Therefore Lake was not entitled to the discount. Should the court use the plain meaning of 50% which is 50% or the trade meaning of 50% which is 49.5%?

What the parties said: Each ton below 50% will receive a \$5 discount.			
What the Seller (Hurst) meant	trade meaning 50% = 49.5% no discount	trade meaning 50% = 49.5% no discount	trade meaning 50% = 49.5% no discount
What the Buyer (Lake) meant	plain meaning 50% = 50% \$5 discount	plain meaning 50% = 50% \$5 discount	plain meaning 50% = 50% \$5 discount
What the reasonable person would have meant	if trade meaning 50% = 49.5% no discount	if plain meaning 50% = 50% \$5 discount	if either meaning 50% could = either 50% or 49.5%
Conclusion	contract with trade meaning 50% = 49.5% no discount	contract with plain meaning 50% = 50% \$5 discount	no contract



CASE

Hurst v. W.J. Lake & Co.

Supreme Court of Oregon, 1932. 141 Or. 306, 16 P.2d 627.

ROSSMAN, J.

From the portion of the pleadings which we are required to deem true, it appears that March 20, 1930, the plaintiff and the defendant entered into an agreement in writing, a copy of which follows:

“March 20, 1930.”

Messrs. Roscoe P. Hurst, Yeon Building, Portland, Oregon.

“Dear Sirs: We conform our purchase from you today as follows:

- Buyer: W.J. Lake & Co., Inc. Seattle, Washington.
- Commodity: Horse meat scraps.
- Quantity: 350 tons of 2000 lbs. each.
- Price: \$50.00 per ton f.o.b. cars Portland.

.....

Specifications: Minimum 50% protein, ground and sacked in 100 lb. net each.
Additional specifications on supplementary page.

"Yours truly,

"W.J. Lake & Company, Inc.,
"By L.E. Branchflower.

"Accepted by:

"Roscoe P. Hurst.

"March 20, 1930.

"Mr. Roscoe P. Hurst, Yeon Building, Portland, Oregon.

"Dear Sir: In case any of the Horse Meat Scraps, covered by our purchase order No. 1352 analyzes less than 50% of protein, it is understood that W.J. Lake & Company, Inc., the buyers, are to receive a discount of \$5.00 per ton.

. . . .

"Yours very truly,

"W.J. Lake & Co., Inc.,
"[Signed] L.E. Branchflower.

"LEB:G L.E. Branchflower.

"Accepted by:

"[Signed] Roscoe P. Hurst."

Pursuant to the contract, the plaintiff delivered to the defendant 349.25 tons of horse meat scraps. . . .

Based upon the contention [in] the complaint, admitted as true by the defendant, shows that the 140 tons with a protein content of 49.53 per cent. to 49.96 per cent. should have been regarded as within the 50 per cent. protein classification, the plaintiff argues that the circuit court erred when it sustained the defendant's motion for judgment on the pleadings.

It will be observed from the foregoing (1) that there is a group of dealers who trade in the commodity known as horse meat scraps; (2) that both plaintiff and defendant are members of that group; (3) that the terms "minimum 50% protein" and "less than 50% protein" are trade terms to which the group has attached meanings different from their common ones; (4) that this usage, prevalent among this group, demanded that, whenever those terms appeared in a contract for the sale of horse meat scraps, it became the duty of the buyer to accept all scraps containing 49.5 per cent. protein or more, and to pay for them at the rate provided for scraps containing full 50 per cent. protein; and (5) that the defendant was aware of all of the foregoing when it attached its signature to the aforementioned contract.

The flexibility of or multiplicity in the meaning of words is the principal source of difficulty in the interpretation of language. Words are the conduits by which thoughts are communicated, yet scarcely any of them have such a fixed and single meaning that they are incapable of denoting more than one thought. In addition to the multiplicity in meaning of words set forth in the dictionaries, there are the meanings imparted to them by trade customs, local uses, dialects, telegraphic codes, etc. One meaning crowds a word full of significance, while another almost empties the utterance of any import. The various groups above indicated are constantly amplifying our language; in fact, they are developing what may be called languages of their own. Thus one is justified in saying that the language of the dictionaries is not the only language spoken in America. For instance, the word "thousand" as commonly used has a very specific meaning; it denotes ten hundreds or fifty scores, but the language of the various trades and localities has assigned to it meanings quite different from

that just mentioned. Thus in the bricklaying trade a contract which fixes the bricklayer's compensation at "\$5.25 a thousand" does not contemplate that he need lay actually 1,000 bricks in order to earn \$5.25, but that he should build a wall of a certain size. *Brunold v. Glasser*, 25 Misc. 285, 52 N.Y.S. 1021; *Walker v. Syms*, 118 Mich. 183, 76 N.W. 320. In the lumber industry a contract requiring the delivery of 4,000 shingles will be fulfilled by the delivery of only 2,500 when it appears that by trade custom two packs of a certain size are regarded as 1,000 shingles, and that hence the delivery of eight packs fulfills the contract, even though they contain only 2,500 shingles by actual count. *Soutier v. Kellerman*, 18 Mo. 509. And, where the custom of a locality considers 100 dozen as constituting a thousand, one who has 19,200 rabbits upon a warren under an agreement for their sale at the price of 60 pounds for each thousand rabbits will be paid for only 16,000 rabbits. *Smith v. Wilson*, 3 Barn. & Adol. 728. Numerous other instances could readily be cited showing the manner in which the meaning of words has been contracted, expanded, or otherwise altered by local usage, trade custom, dialect influence, code agreement, etc. In fact, it is no novelty to find legislative enactments preceded by glossaries or brief dictionaries defining the meaning of the words employed in the act. Technical treatises dealing with aeronautics, the radio, engineering, etc., generally contain similar glossaries defining the meaning of many of the words employed by the craft. A glance at these glossaries readily shows that the different sciences and trades, in addition to coining words of their own, appropriate common words and assign to them new meanings. Thus it must be evident that one cannot understand accurately the language of such sciences and trades without knowing the peculiar meaning attached to the words which they use. It is said that a court in construing the language of the parties must put itself into the shoes of the parties. That alone would not suffice; it must also adopt their vernacular.

. . . .

Without setting forth herein our review of the many authorities cited in the briefs, all of which we have read with care, we state our conclusion that members of a trade or business group who have employed in their contracts trade terms are entitled to prove that fact in their litigation, and show the meaning of those terms to assist the court in the interpretation of their language.

Finally, it is suggested that the employment of the terms "minimum 50% protein" and "less than 50% of protein" indicates that the parties rejected the mercantile custom in effecting their contract. It will be recalled that under the state of the record we are compelled to regard these two terms as trade terms possessed of a special significance. We believe that it is safe to assume, in the absence of evidence to the contrary, that, when tradesmen employ trade terms, they attach to them their trade significance. If, when they write their trade terms into their contracts, they mean to strip the terms of their special significance and demote them to their common import, it would seem reasonable to believe that they would so state in their agreement. Otherwise they would refrain from using the trade term and express themselves in other language. We quote from *Nicoll v. Pittsvein Coal Co.* (C.C.A.) 269 F. 968, 971: "Indeed when tradesmen say or write anything, they are perhaps without present thought on the subject, writing on top of a mass of habits or usages which they take as matter of course. So (with Prof. Williston) we think that any one contracting with knowledge of a usage will naturally say nothing about the matter unless desirous of excluding its operation; if he does wish to exclude, he will say so in express terms. Williston, *Contracts*, § 653." Nothing in the contract repels the meaning assigned by the trade to the two above terms unless the terms themselves reject it. But, if these terms repel the meaning which usage has attached to them, then every trade term would deny its own meaning. We reject this contention as being without merit. We

have considered all other contentions presented by the respondent, but have found no merit in them.

It follows that, in our opinion, the circuit court erred when it sustained the defendant's motion for judgment on the pleadings.

Reversed.

BROWN, BELT, CAMPBELL, and KELLY, JJ., concur.

RAND, J., concurs in the result.

BEAN, C.J., dissents.

Identifying the Terms Included in the Contract

Not all contracts need to be in writing to be enforceable. Part III (contract enforceability) explores which contracts must be in writing and what constitutes the writing (Statute of Frauds). For contract formation purposes, the need for a writing is irrelevant unless the offeror mandates a writing as the last act of contracting.

If, however, the parties have reduced their agreement to writing (whether the writing was or was not required for the enforcement of the contract), the next question is whether the writing encompasses all the terms of the contract or only some. The answer is found in the parol evidence rule.

Parol Evidence Rule Although some contracts are created on the spur of the moment, often the contract is a product of negotiations between the parties prior to the actual time of contract formation. These negotiations may be brief or extended. If negotiations precede a written contract, the risk is that not all terms agreed upon in the negotiation will appear in the writing. Does failure to include all of the agreed-upon terms mean those terms not incorporated into the writing are not terms of the contract? Should the answer be that the contract consists of some written and some oral terms?

Under the parol evidence rule, the contract may consist of terms in the final writing and terms that are parol. **Parol terms** are terms that are oral or, if written, are not in the final writing.

In the absence of fraud in the inducement, duress, or mutual mistake of fact, extrinsic evidence, oral or written, made prior to or contemporaneous with the final writing cannot be used to add to or contradict the final writing.

Even though the parol evidence rule is exclusionary, making certain type of evidence inadmissible, the parol evidence rule is not a rule of evidence. The parol evidence rule is a rule of substantive law. At issue is what are the terms of the contract and not what type of evidence is admissible to demonstrate the terms of the contract. A rule of evidence would not bar the proof of the terms of the contract. It would bar a method of proving the terms of the contract. The fact could be established by a different method.

EXAMPLE 5-1

The Ventura Dance Company hired Bethany Alexander as its dance director. The contract was for one year and was in writing. After Ventura fired Bethany without cause, Bethany sued Ventura for breach of contract. Bethany attempted to prove the existence of the contract by oral testimony. Under the best evidence rule, the writing is required. The best evidence rule is a rule of evidence. As a general rule, oral testimony cannot be used to provide the existence of a contract when a writing exists. The writing must be produced.

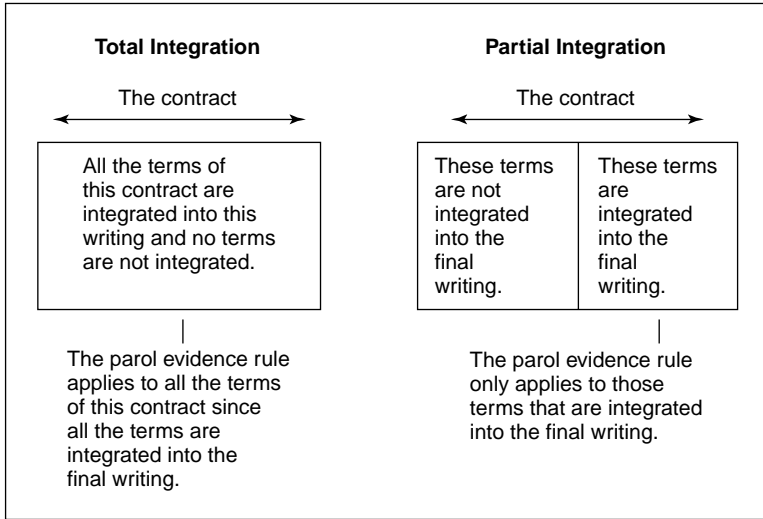
EXAMPLE 5-2

The Ventura Dance Company hired Bethany Alexander as its dance director. The contract was for one year and was in writing. After Ventura fired Bethany without cause, Bethany sued Ventura for breach of contract. Bethany submitted the writing into evidence and then attempted to prove additional contract terms by oral testimony. Under the parol evidence rule, if these terms were not a part of the contract, the oral testimony is inadmissible. If these terms were a part of the contract, the oral testimony is admissible.

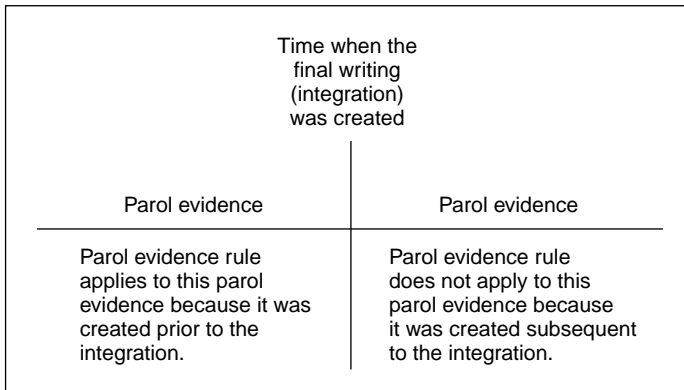
The parol evidence rule does not apply to all transactions, nor does it apply to all parol evidence. First, the parol evidence rule only comes into play when the terms of the contract have been set forth in a final writing. If the parties have a writing but it is not intended as the final writing, the parol evidence rule does not apply. The question that must be asked is “Has the contract been reduced to a final writing?” A final writing is called an **integration** because the final writing brings together the contract terms.

Second, the parol evidence rule does not apply to transactions where there has been fraud in the inducement, duress, or mutual mistake of fact. **Fraud in the inducement** is a false representation or concealment of fact, that should have been disclosed, that is intended to deceive and does deceive another party to the contract. **Duress** is the use of any wrongful act or threat to influence a party to contract. **Mutual mistake of fact** occurs when the parties to a contract have a common intention, but the writing does not reflect that intention due to their misconception of the facts. In those transactions, the parol evidence rule is inapplicable even though the contract has been integrated.

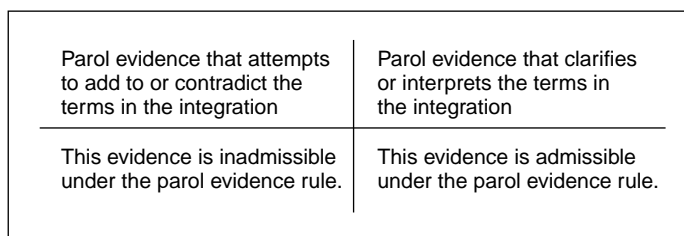
Third, the writing may be a final writing for all the terms of the contract (a total integration) or only some of the terms (a partial integration). The parol evidence rule will apply to the entire contract if the writing is a total integration. If the writing is a partial integration, the parol evidence rule will apply to only the final writing part of the contract.



Fourth, the parol evidence rule only excludes parol evidence made prior to or contemporaneous with (at the same time as) the final writing. The rule does NOT exclude evidence created after the parties entered into the final writing.



Fifth, the parol evidence rule only excludes evidence that adds to or contradicts those terms that appear in the final writing. The rule does not exclude evidence intended to clarify or interpret the terms in the final writing.



EXAMPLE 5-3

Geoquest produced a murder mystery videocassette program, *The Gold Key*, to be sold in home video stores and contacted Embassy, a distributor. The initial negotiations in July produced the following letter by Embassy.

We will in all likelihood submit a more formal contract letter later, but, in the meantime, I'd like to confirm our agreement regarding Embassy's video distribution of THE GOLD KEY on the following terms:

Geoquest did not sign this letter.

Additional negotiations produced an August letter by Embassy.

I've revised the July draft along the lines we discussed. This letter now serves to confirm our agreement regarding Embassy's video distribution of THE GOLD KEY on the following terms:

Geoquest did not sign this letter.

Another round of negotiations produced a third Embassy letter that was signed and returned by Geoquest in September.

If I've got the essential terms right, please indicate Geoquest's agreement by signing and returning the enclosed copy. . . . Until such time, if ever, that we execute a more formal agreement, this letter will serve to reflect the binding agreement between the parties.

Embassy distributed THE GOLD KEY and sales totaled only 5,700 copies. Geoquest sued Embassy for breach of contract contending that Embassy orally guaranteed minimum sales of 100,000 copies. Embassy has moved to bar this oral evidence under the parol evidence rule.

Step 1. Check for a final writing (an integration). If the contract has not been reduced to a final writing, there is no parol evidence rule problem, even though there may be parol evidence. Although not all writings are intended as final writings, Embassy's September letter was a final writing because it is the last in a series of writings, it states that it incorporates the "essential terms," it notes that there may not be a formal writing, and it is the first writing signed by both parties.

Step 2. Check the final writing for fraud in the inducement, duress, and mutual mistake of fact. None appears here.

Step 3. Check whether the integration was a final writing for all the terms of the contract (a total integration) or for only some of the terms (a partial integration). Embassy's September letter refers to the "essential terms," and therefore this is a total integration.

Step 4. Check whether the parol evidence was made prior to, or contemporaneous with, the final writing. If the parol evidence was made subsequent to the final writing, there is no parol evidence rule problem. The alleged oral guarantee was made prior to the final writing in September which means there is a parol evidence rule problem.

Step 5. Check whether the parol evidence was intended to add to, or contradict, that part of the contract that was reduced to a final writing. If the contract was only partially integrated and if the parol evidence attempts to add to, or contradict, the part of the contract that was *not* reduced to the final writing, there is no parol evidence rule problem. In this situation, the oral guarantee adds to the essential terms found in the final writing and therefore is inadmissible. *Geoquest Productions, Ltd. v. Embassy Home Entertainment, Inc.*, 593 N.E.2d 727 (IL Ct. App. 1992).

PARALEGAL EXERCISE 5.1 The Eldridge house needed exterior painting, so Eldridge telephoned the Quality Painting Company for an estimate. Quality looked at the house and on several occasions discussed the job with Eldridge by telephone. Finally, Eldridge agreed to pay Quality \$2,000 for painting her house. When Quality finished painting the house, Eldridge refused to pay until Quality painted the unattached garage.

Eldridge claims that during the negotiation they discussed the house and the garage and the contract was for both, even though they did not specifically talk about the garage during the final telephone conversation. Quality claims that they did not discuss the garage during the final telephone conversation and therefore the contract was for the house and not the garage.

Is whether the contract includes the garage a parol evidence rule problem?

PARALEGAL EXERCISE 5.2 Same facts as Paralegal Exercise 5.1, except the final telephone conversation was followed by a final writing that spoke of the house but was silent on the garage.

Is whether the contract includes the garage a parol evidence rule problem?

PARALEGAL EXERCISE 5.3 Same facts as Paralegal Exercise 5.2 but during the negotiation, no mention was made of the garage. The parties only discussed the house for \$2,000. After Quality began to paint the house, Eldridge asked Quality how much it would cost to paint the garage. Quality orally responded \$500, and they orally agreed.

When Quality finished painting the house and the garage, Eldridge would only pay \$2,000 because the writing only stated \$2,000.

Is whether the contract can be orally modified to include the garage a parol evidence rule problem?

PARALEGAL EXERCISE 5.4 After extended negotiations, Buyer and Seller contracted for \$50,000 of “chickens.” Their final writing contained only the term “chickens.” Upon uncrating the shipment Buyer was surprised to find “stewing chickens” instead of “fryers.”

Should any prior discussion between Seller and Buyer as to the type of chicken be excluded as a violation of the parol evidence rule?

Supplying Omitted Terms

Regardless of whether the contract is oral or written, or a bit of both, there are times when the courts will add a term to the contract that the parties never discussed. One such term is “good faith.” **Good faith** is defined as honesty in fact

(subjective honesty) in one's conduct. Courts have consistently supplied the "good faith" term to a contract. Therefore, the contracting parties must exercise good faith when performing their obligations under the contract.

Care, however, should be taken to distinguish the negotiation phase of contract formation from the post contract formation phase. Although both parties must perform the contract in good faith, neither is required to negotiate the contract in good faith. When the transaction is still in the precontract phase, no contractual relationship exists upon which to attach the reciprocal good faith promises.

PARALEGAL EXERCISE 5.5 Does Pluto Computers have a duty to deal in good faith in the following situations:

1. Pluto manufactures and distributes computers worldwide. Some of its products are unique and are, therefore, not available from any other company. Omni Unlimited, a data processing company, sought to buy several of Pluto's products, Pluto being the sole supplier of these products. Pluto refused to deal with Omni unless Omni would include in the contract its promise to buy all of its computer equipment from Pluto over the next five years.
2. Pluto and Omni have a contract for the purchase of sixteen computers. Omni has discussed buying an additional ten but is hesitant to finalize the contract until it uses the sixteen computers already ordered. Pluto will not ship these computers until Omni places the second order.

If the transaction is a sale of goods, Article 2 of the Uniform Commercial Code will supply some omitted terms. These terms, known as gap fillers, include provisions as to price (§ 2-305), place of delivery (§ 2-308), time for shipment or delivery (§ 2-309), payment or running of credit (§ 2-310), warranty of title (§ 2-312), warranty against infringement (§ 2-312), implied warranty of merchantability (§§ 2-314(1), (2)), implied warranty of usage of trade (§ 2-314(3)), and implied warranty of fitness for a particular purpose (§ 2-315).

EXAMPLE 5-4

The Uniform Commercial Code § 2-314. Implied Warranty: Merchantability; Usage of Trade.

- (1) Unless excluded or modified (Section 2-316), a warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind. Under this section the serving for value of food or drink to be consumed either on the premises or elsewhere is a sale.
- (2) Goods to be merchantable must be at least such as
 - (a) pass without objection in the trade under the contract description; and
 - (b) in the case of fungible goods, are of fair average quality within the description; and
 - (c) are fit for the ordinary purposes for which such goods are used; and

- (d) run, within the variations permitted by the agreement, of even kind, quality and quality within each unit and among all units involved; and
 - (e) are adequately contained, packaged, and labeled as the agreement may require; and
 - (f) conform to the promise or affirmation of fact made on the container or label if any.
- (3) Unless excluded or modified (Section 2-316) other implied warranties may arise from course of dealing or usage of trade.

CORRECTING ERRORS IN THE WRITTEN CONTRACT: MISTAKE IN INTEGRATION

Parties may orally contract with the understanding that one of the parties will later draft a writing to reflect the terms of the contract. Ultimately, both parties may sign this written confirmation of their oral contract. The parties may sign the writing without a thorough reading. Later, as the parties perform their duties, one party may be surprised to find that the writing fails to correspond to what he or she thought was agreed upon. A mistake occurred in the integration of the contract. When confronted by this alleged mistake in integration, the drafter may insist that the writing reflects the oral agreement. Can the non-drafting party have the writing reformed (altered) to correspond to the oral agreement?

A court has the power to reform the written evidence of a contract. **Reformation** is a judicial remedy designed to revise a writing to conform to the real agreement or intention of the parties. Reformation is appropriate only if clear and convincing evidence demonstrates that:

1. the parties' oral agreement expresses their real intentions;
2. the writing fails to express those intentions; and
3. the failure is due to a mutual mistake or a unilateral mistake accompanied by the other party's fraudulent conduct.

A **mutual mistake** is a mistake that both parties shared at the time they reduced their agreement to writing. The court will reform a writing only when the parties intended their written agreement to say one thing and, by mistake, it expressed something else. The fact that one party denies that a mistake occurred does not prevent the court from finding a mutual mistake.

In *Bollinger v. Central Pennsylvania Quarry Stripping & Construction Co.*, the Bollingers owned property near the Pennsylvania Turnpike. Central, a contractor working on the Turnpike, orally contracted with the Bollingers for permission to deposit construction waste on the Bollingers' property. Under the oral contract, Central promised to remove the topsoil, deposit the waste, and then replace the topsoil over the waste. Central reduced the oral contract to a writing. At some point in the performance of the contract, Central ceased reclaiming the land but instead began dumping the construction waste over the

top soil. The Bollingers asked the court to reform the writing to include their oral agreement regarding reclamation.

While reading the *Bollinger* case, answer the following:

1. What did the Bollingers allege was the mistake in the final writing (i.e., the integration)?
2. Did Central agree that the writing did not correspond to the oral agreement?
3. Would a reasonable person believe that the writing did not correspond to the oral agreement?
4. What would the reasonable person consider when making this determination?
5. If Central does not agree that a mistake was made in integrating the contract, on what basis does the court conclude that the mistake in integration was mutual?



CASE

Bollinger v. Central Pennsylvania Quarry Stripping & Construction Co.

Supreme Court of Pennsylvania, 1967. 425 Pa. 430, 229 A.2d 741.

OPINION OF THE COURT

MUSMANNO, Justice.

Mahlon Bollinger and his wife, Vinetta C. Bollinger, filed an action in equity against the Central Pennsylvania Quarry Stripping Construction Company asking that a contract entered into between them be reformed so as to include therein a paragraph alleged to have been omitted by mutual mistake and that the agreement, as reformed, be enforced.

The agreement, as executed, provided that the defendant was to be permitted to deposit on the property of the plaintiffs, construction waste as it engaged in work on the Pennsylvania Turnpike in the immediate vicinity of the plaintiffs' property. The Bollingers claimed that there had been a mutual understanding between them and the defendant that, prior to depositing such waste on the plaintiffs' property, the defendant would remove the topsoil of the plaintiffs' property, pile on it the waste material and then restore the topsoil in a way to cover the deposited waste. The Bollingers averred that they had signed the written agreement without reading it because they assumed that the condition just stated had been incorporated into the writing.

When the defendant first began working in the vicinity of the plaintiffs' property, it did first remove the topsoil, deposited the waste on the bare land, and then replaced the topsoil. After a certain period of time, the defendant ceased doing this and the plaintiffs remonstrated. The defendant answered there was nothing in the written contract which required it to make a sandwich of its refuse between the bare earth and the topsoil. It was at this point that the plaintiffs discovered that that feature of the oral understanding had been omitted from the written contract. The plaintiff husband renewed his protest and the defendant's superintendent replied he could not remove the topsoil because his equipment for that operation had been taken away. When he was reminded of the original understanding, the superintendent said, in effect, he couldn't help that.

The plaintiffs then filed their action for reformation of the contract, the Court granted the requested relief, and the defendant firm appealed. We said in *Bugen v. New York Life Insurance Co.*, 408 Pa. 472, 184 A.2d 499:

“A court of equity has the power to reform the written evidence of a contract and make it correspond to the understanding of the parties. * * * However, the mistake must be mutual to the parties to the contract.”

The fact, however, that one of the parties denies that a mistake was made does not prevent a finding of mutual mistake. *Kutsenkow v. Kutsenkow*, 414 Pa. 610, 612, 202 A.2d 68.

Once a person enters into a written agreement he builds around himself a stone wall, from which he cannot escape by merely asserting he had not understood what he was signing. However, equity would completely fail in its objectives if it refused to break a hole through the wall when it finds, after proper evidence, that there was a mistake between the parties, that it was real and not feigned, actual and not hypothetical.

The Chancellor, after taking testimony, properly concluded:

“We are satisfied that plaintiffs have sustained the heavy burden placed upon them. Their understanding of the agreement is corroborated by the undisputed evidence. The defendant did remove and set aside the top soil on part of the area before depositing its waste and did replace the top soil over such waste after such depositing. It follows it would not have done so had it not so agreed. Further corroboration is found in the testimony that it acted similarly in the case of plaintiffs’ neighbor Beltzner.”

Decree affirmed, costs on the appellant.

BELL, C.J., dissents.

COHEN, J., absent.

Care must be taken to distinguish a parol evidence rule problem from a mistake in integration problem. They share similarities in that both involve parol evidence (oral or non-final writings) and both involve an integration (a final writing). In a parol evidence rule problem, the issue is whether the contract consists of the integration and parol or only the integration. No attempt is made to reform the integration to include parol terms. In a mistake in integration problem, the issue is whether the integration should be reformed to include the parol terms. No attempt is made to limit the integration to only some of the terms in the contract. All of the terms of the contract are embodied in the integration.

EXAMPLE 5-5

Romaro leased space in an office building for the purpose of operating a snack bar. During the negotiations, Romaro agreed to refrain from selling tobacco products in exchange for the exclusive right to sell sandwiches. After the parties orally agreed to all the terms, the landlord drafted a final writing (an integration). Romaro signed the writing without noticing that it did not include his exclusive right to sell sandwiches. Several months later, Romaro noticed that another tenant had a snack bar and was selling sandwiches.

If Romaro wants to enforce his exclusive right to sell sandwiches, he must establish that the parties intended: (1) some contract terms would be in the written lease and some would remain oral and therefore the inclusion of the exclusivity term in the oral part of the contract would not violate the parol evidence rule; or (2) the exclusivity clause would be in the written lease which means there was a mutual mistake in the integration of the contract since the written lease did not include the exclusivity clause.

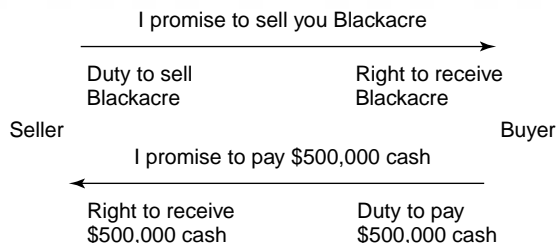
MODIFYING A CONTRACT

After the creation of a contract but before full performance, the needs of the contracting parties may change. Performance of the contract may no longer be in their best interest. The parties may desire to modify the terms of the contract to keep pace with their needs.

Once parties enter into a bilateral contract, each party's promise is consideration for the other's promise.

EXAMPLE 5-6

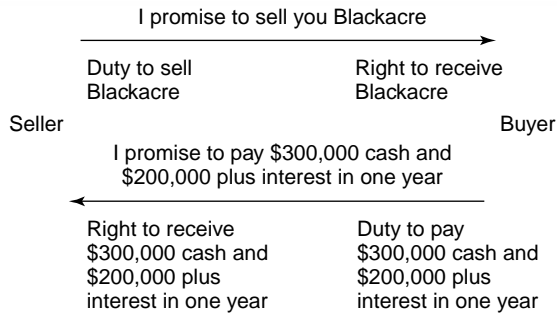
"I promise to sell you Blackacre for your promise to pay \$500,000 cash." "I promise to pay \$500,000 cash for your promise to sell me Blackacre." Buyer's promise to pay \$500,000 in cash is consideration for Seller's promise to sell Blackacre; Seller's promise to sell Blackacre is consideration for Buyer's promise to pay \$500,000 in cash.



Assume Buyer becomes a little short on cash and would like to modify the contract so she can pay \$300,000 cash and \$200,000 plus interest in one year. Seller, knowing that \$500,000 is a good price, is willing to modify the contract so Buyer has more time to pay. The dialogue, translated into offer format, might be something like this:

"I promise to sell you Blackacre for your promise to pay me \$300,000 cash and \$200,000 plus interest in one year."

The consideration for Seller's promise to sell Blackacre is Buyer's promise to pay \$300,000 cash and \$200,000 plus interest in one year.



Under the original contract, Buyer had the duty to pay \$500,000. Buyer's new promise adds the duty to pay interest on \$200,000 to the promise to pay \$500,000. Seller is asking for new consideration from Buyer. Seller has made a new offer.

Now analyze Buyer's attempted acceptance: "I promise to pay \$300,000 cash and \$200,000 plus interest in one year for your promise to sell me Blackacre." The consideration for Buyer's promise to pay \$300,000 cash and \$200,000 plus interest in one year is Seller's promise to sell Blackacre. Under the original contract, Seller had the duty to sell Blackacre to Buyer. Buyer is not asking for new consideration from Seller. Buyer, under the original contract, is already entitled to the original consideration. Seller has a pre-existing duty to sell Buyer Blackacre. Without new consideration for Buyer's promise, the attempted acceptance fails. The **modification** is a contract and must follow the same rules of contract formation required for the original contract. Because the offer to modify cannot be accepted (pre-existing duty precludes consideration), the attempt at modification fails.

PARALEGAL EXERCISE 5.6 The Bon Appetit Bakery Company contracted with Samantha Mills to host a fifteen-episode TV cooking show sponsored by Bon Appetit. The contract provided that Mills would receive \$200,000 per episode. Filming of all episodes would take place at the WFUN studios in Boston.

1. Before the filming began, Mills demanded that Bon Appetit increase her salary to \$250,000 an episode. Bon Appetit agreed. Bon Appetit paid Mills \$250,000 for the first fourteen episodes but only \$200,000 for the fifteenth. Was the contract successfully modified, thus entitling Mills to an additional \$50,000 for the last episode?
2. Same facts except in addition to increasing Mills's salary to \$250,000 an episode, Mills agreed to a sixteenth episode. Bon Appetit paid Mills \$250,000 for the first fifteen episodes but only \$200,000 for the sixteenth. Was the contract successfully modified, thus entitling Mills to an additional \$50,000 for the last episode?
3. Same facts except instead of adding an episode, Mills agreed to reduce the number to fourteen. Bon Appetit paid Mills \$250,000 for the first thirteen episodes but only \$200,000 for the fourteenth. Was the contract successfully modified, thus entitling Mills to an additional \$50,000 for the last episode?

4. Same facts as (1) except the attempted modification also called for the filming to be in southern France rather than in Boston. Bon Appetit paid Mills \$250,000 for the first fourteen episodes but only \$200,000 for the fifteenth. Was the contract successfully modified, thus entitling Mills to an additional \$50,000 for the last episode?

Recently, state legislatures have addressed the modification issue. The Uniform Commercial Code made the most uniform and sweeping changes for the sale of goods. Section 2-209(1) provides:

An agreement modifying a contract within this Article needs no consideration to be binding.

PARALEGAL EXERCISE 5.7 The Quality Glue Company contracted to sell to the Heirloom Furniture Company all of its glue requirements for the next year at \$10 a barrel. Three months into the contract, Quality raised its price to \$11 a barrel with Heirloom's consent. Has the contract price been successfully modified from \$10 to \$11 a barrel? Assume that this jurisdiction has enacted the UCC.

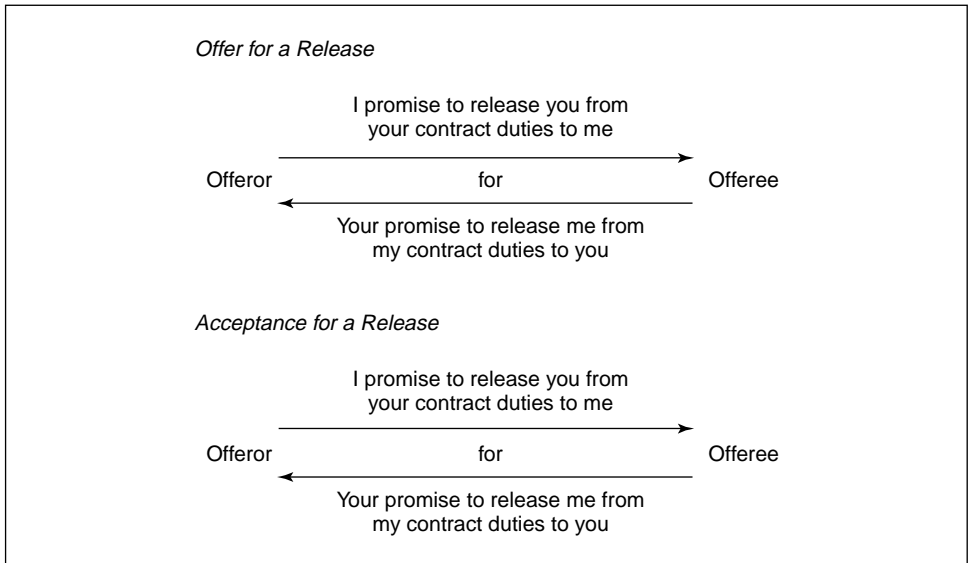
ENDING A CONTRACT BEFORE IT HAS BEEN FULLY PERFORMED

After a bilateral contract has been created but before it has been fully performed by both parties, the contracting parties may find that their needs have changed. They may discover that full performance of the contract is no longer in their best interests and may want to end their contractual duties without the contract being fully performed.

Terminating a Contractual Duty When Neither Party Has Fully Performed

The desire to end a contractual relationship may occur when *both* parties have duties to perform. Neither may have begun to perform, one may have begun to perform, or both may have begun to perform. A **mutual release** will terminate the parties' duties to perform their contractual duties. To create a mutual release, the parties must follow the same rules of contracts law used when they formed the original contract. The release has an offer and an acceptance. The offer consists of the offeror's promise and the consideration for the offeror's promise. "I promise to release you from your contract duties to me for your promise to release me from my contract duties to you." The acceptance consists of the offeree's promise and the consideration for the offeree's promise (the

mirror image of the offer). “I promise to release you from your contract duties to me for your promise to release me from my contract duties to you.” When the offeree promises, the offer is accepted and the release contract is formed. A mutual release absolves both parties from their contractual obligations. The duties of both parties under the original contract are terminated.



PARALEGAL EXERCISE 5.8 Tom, a stand-up comic, contracted with the Village Theatre of Victor, New York, to perform during the first two weeks of August. In mid-July, Tom received an offer to perform at a Las Vegas hotel that would substantially benefit his career. The Village Theatre does not want to lose Tom.

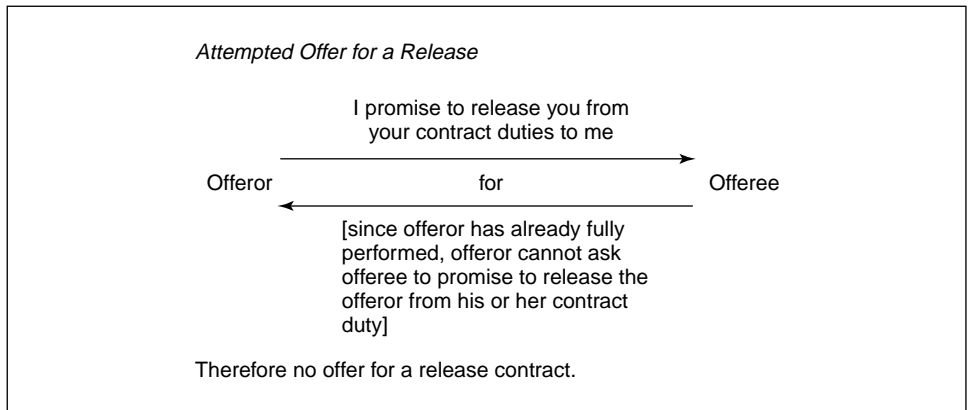
Can Tom rescind the contract?

PARALEGAL EXERCISE 5.9 Susan, an interior decorator, contracts to work for Design Today for one year at a salary of \$1,000 a week. After working for three months, Susan is invited to join another interior decorating firm with an increase in salary. Design Today has encouraged Susan to accept the new position because business at Design Today has been rather slow.

Draft a rescission that will free both Susan and Design Today from their duties under their contract.

Terminating a Contractual Duty When One Party Has Fully Performed

When one party has fully performed while the other party has either not begun to perform or has only partially performed, the party who has fully performed may want to release the other from his or her contractual duties. This release cannot follow contract form because the offeror has fully performed and no longer owes a duty to the offeree. Without a duty owed by the offeror, consideration for the offeror's promise to release is missing. "I promise to release you from your duty for your promise to release me from my duty" becomes "I promise to release you from your duty." Without consideration for the offeror's promise, the attempted offer fails. Without an offer, the attempted release contract fails.



PARALEGAL EXERCISE 5.10 Roberta, an artist, sold Jim a bronze sculpture for \$2,500. Roberta delivered the sculpture to Jim, and he paid her \$1,500. The next month Jim paid Roberta \$500.

Upon reflection, Jim decided \$2,500 was too high a price for the sculpture and he wanted to be released from his duty to pay the outstanding \$500. Jim presented Roberta with a writing that said "I, Roberta, promise to release Jim from his duty to pay me \$500 for Jim's promise to release me from my duties to him." The writing also stated, "I, Jim, promise to release Roberta from her duties to me for her promise to release me from my duty to pay her \$500."

If both parties sign the writing, has Roberta contracted to release Jim?

If one party has fully performed, that party can unilaterally release the other party. The transaction would not be a contract because the promise to release would lack consideration. The party who has fully performed can, however, confer a gift on the party who has contractual duties. The subject of the gift would be the right to that performance. The promisor's statement would be "I give you my right." The law of gifts would apply to the promisor's promise.

PARALEGAL EXERCISE 5.11 Could Roberta, in Paralegal Exercise 5.10, release Jim from his duty to pay \$500? Should the failed attempt to contract be treated as a gift?

Terminating a Noncontractual Duty

Not all duties arise from contract. A number of duties are noncontractual. Parties may release noncontractual duties by using a release that meets the requirements of contracts law. The release consists of an offer and an acceptance. The offer has the offeror's promise and consideration for the offeror's promise.

EXAMPLE 5-7

"I promise to pay you \$1,000 for your promise to release your claim against me." The "promise to release" is the consideration for the promisor's "promise to pay \$1,000."

PARALEGAL EXERCISE 5.12 Stephanie was walking on the sidewalk in a downtown business district when a bucket suddenly struck her head. A window washer on the twentieth floor of a local office building had been using the bucket. Pedestrians were not warned that someone was washing windows. Stephanie spent four days in the hospital and missed six weeks of work.

The window washer promised to pay Stephanie \$3,000 for her promise to release her claim against him.

Have they formed a contract?

PARALEGAL EXERCISE 5.13 While eating at the Pink Penguin, a local bar and grill, Erma began to choke on a piece of meat. A patron dislodged the obstruction and saved Erma's life. Erma threatened to sue the Pink Penguin, although she thought that her own carelessness could have caused the incident.

The Pink Penguin promises to pay Erma \$1,500 if she promises not to sue. Erma promises.

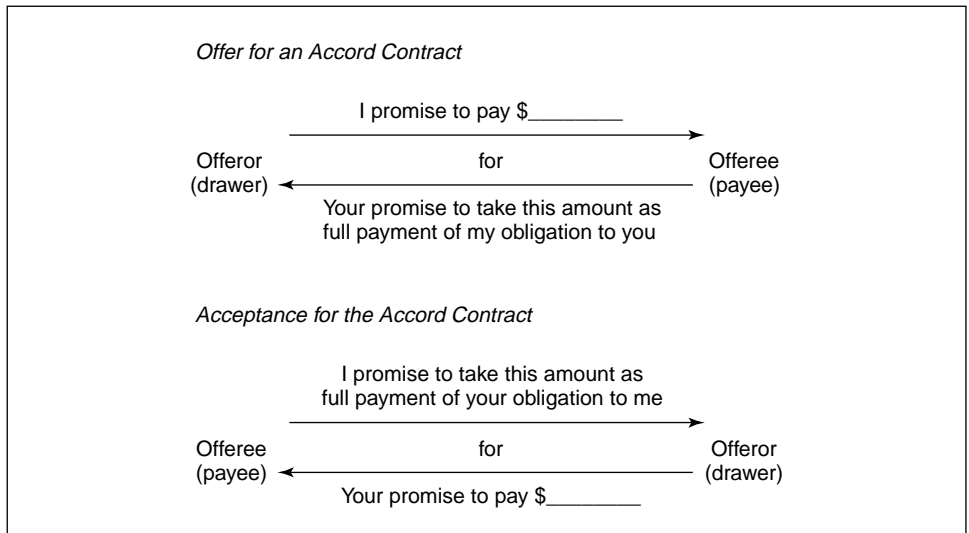
Have the parties formed a contract?

Terminating a Contractual or Noncontractual Duty with a "Payment in Full" Check—The Accord and Satisfaction

"Accord and satisfaction" is another variation on the theme of ending a contract before it has been fully performed. Although an accord and satisfaction can op-

erate without a check, generally it does involve a check. In an accord and satisfaction, one party writes a check to the other and states on the bottom or back of the check, “This check is taken in full payment of the obligation.” The “**accord**” is a contract to pay a stated amount to discharge a prior obligation.

Because the accord is simply a contract, the traditional rules of offer and acceptance, including the rules of consideration, apply. For an offer to exist under classical contracts law, there must be consideration for the drawer’s promise. The consideration for “the drawer’s promise to pay the stated amount” would be “the payee’s promise to take the amount as full payment.” The situation gives rise to an offer. For an acceptance to exist, there must be consideration for the payee’s promise. The consideration for the “payee’s promise to take the amount as full payment” would have to be (under the mirror image rule) “the drawer’s promise to pay the amount.”



If either the existence or the amount of the drawer’s obligation is in dispute, the notation “payment in full” is significant. When either the existence or the amount of the drawer’s duty under the original contract is in dispute, the drawer’s promise to pay a stated amount, by not reaffirming a pre-existing duty, can be consideration for the payee’s promise to take the stated amount as full payment. With this acceptance of the offer, an accord contract is created. **Satisfaction** is the performance of the accord contract. In the case of a check, satisfaction is the payee’s exercising dominion over the check which normally takes place when the payee cashes or deposits the check. Upon satisfaction, the original contract duty to pay is discharged.

EXAMPLE 5-8

The Quality Nursery contracted to landscape the Rainbow Mall to Rainbow's specifications. The contract provided that the price would be "a reasonable price."

After Quality landscaped the Mall according to Rainbow's specifications, Quality sent Rainbow a bill for \$20,000. Rainbow sent Quality a check for \$18,000. The check carried the notation "payment in full."

Rainbow's offer in the original contract was: "I promise to pay you a reasonable price for your promise to landscape the Mall according to my specifications." Quality's acceptance was: "I promise to landscape your Mall according to your specifications for your promise to pay me a reasonable price."

By sending the check for \$18,000, Rainbow made an offer for an accord contract: "I promise to pay you \$18,000 for your promise to accept this amount as full payment of my disputed obligation to you." The amount is in dispute because Quality claims the reasonable amount is \$20,000 and Rainbow claims the reasonable amount is \$18,000. If Quality cashes the check, it accepts the offer of the accord. Quality's actions would amount to saying, "I promise to accept \$18,000 as full payment of your disputed obligation to me for your promise to pay me \$18,000."

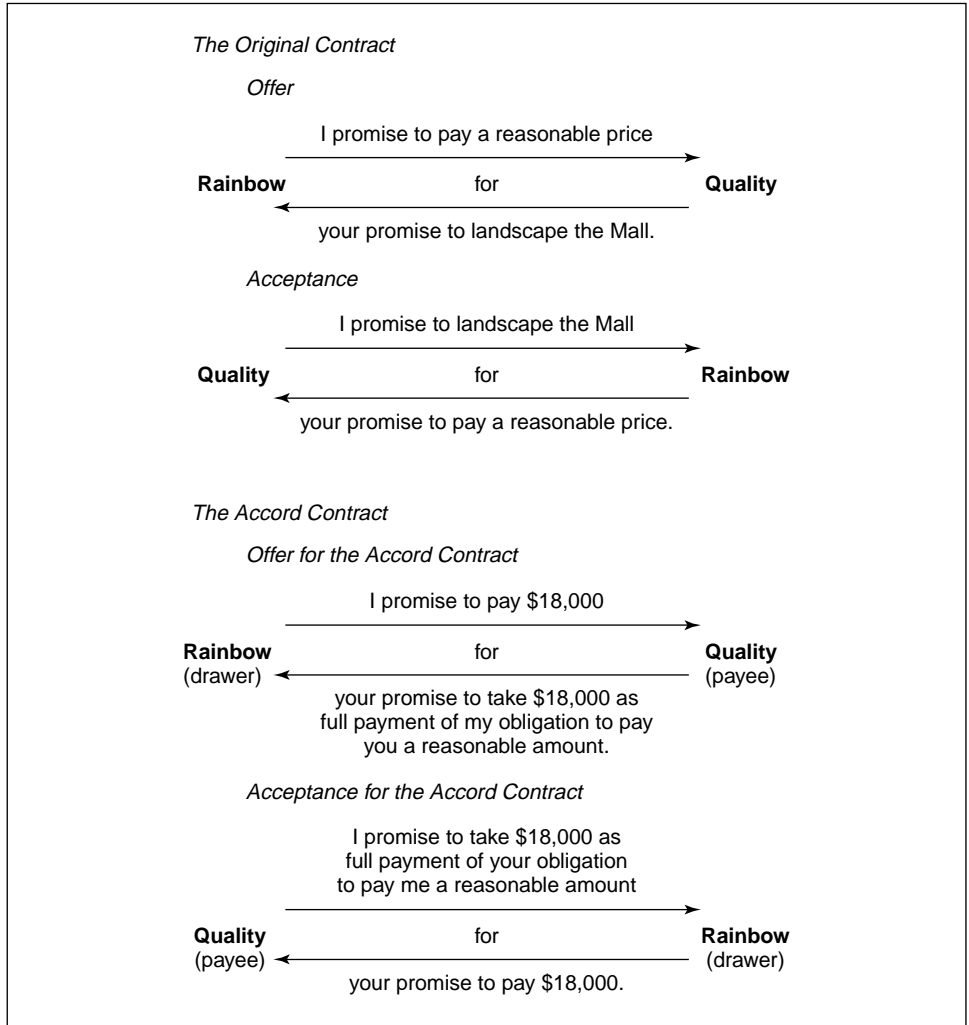
If neither the existence nor the amount of the drawer's obligation is in dispute, the drawer has a pre-existing duty to pay the undisputed higher amount. An attempt to promise to pay only a part of the undisputed amount cannot be a promise in the contractual sense. The attempted promise is not an unequivocal assurance that something will or will not occur. An unequivocal assurance already exists so the drawer has a pre-existing duty. Therefore, although the drawer has attempted a promise to pay, no offer for an accord contract is created. Also, the drawer's attempted promise to pay only a part of the undisputed amount will not be consideration for the payee's promise to take this amount as full payment. The drawer has a pre-existing duty. Therefore, the drawee's attempted acceptance is not an acceptance of an accord offer.

Without acceptance and thus without an accord contract, the drawer's notation on the check, "payment in full," is irrelevant, and the payee may exercise dominion over the check without losing his or her right to enforce the drawer's original promise to pay.

EXAMPLE 5-9

The Quality Nursery contracted to landscape the Rainbow Mall to Rainbow's specifications. The contract provided that the price would be \$20,000.

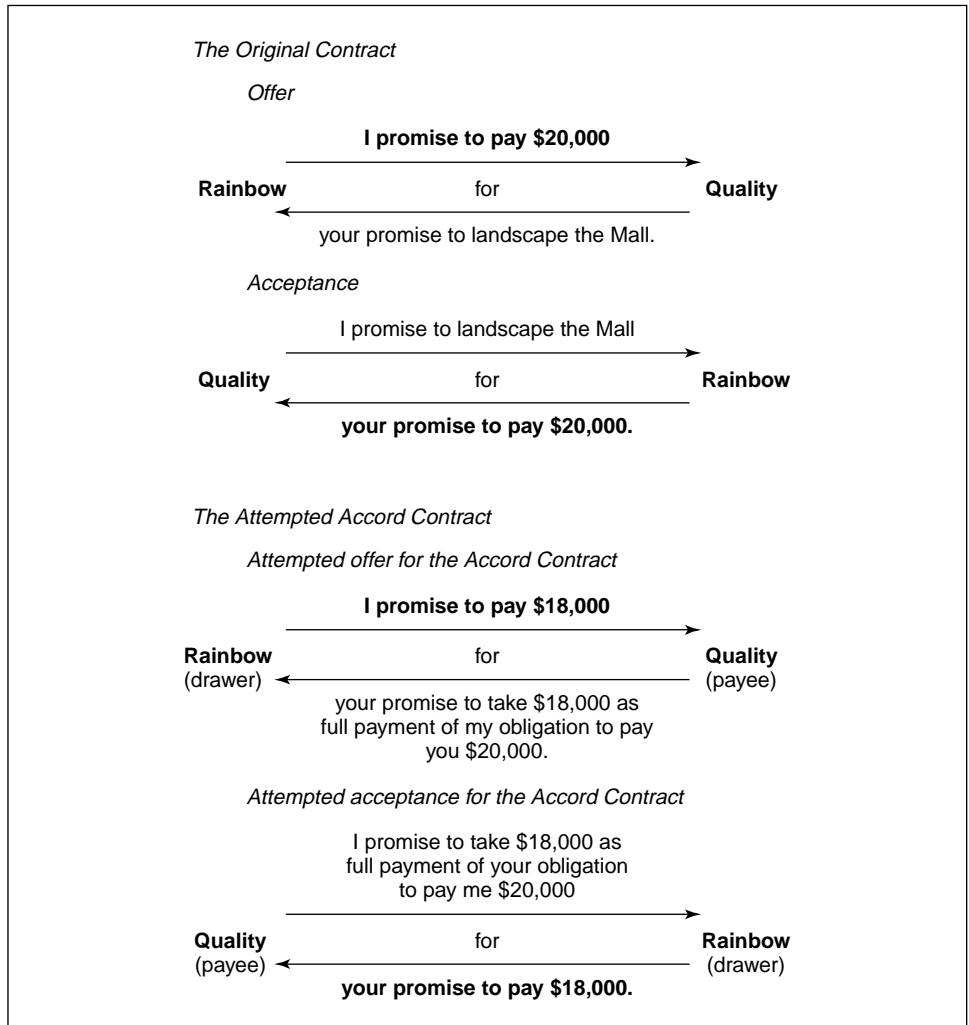
After Quality landscaped the Mall according to Rainbow's specifications, Quality sent Rainbow a bill for \$20,000. Rainbow sent Quality a check for \$18,000. The check carried the notation "payment in full."



Rainbow's offer in the original contract was: "I promise to pay you \$20,000 for your promise to landscape the Mall according to my specifications." Quality's acceptance was: "I promise to landscape your Mall according to your specifications for your promise to pay me \$20,000."

Although Rainbow sent a check for \$18,000, it did not make an offer for an accord contract. Neither Rainbow's obligation to pay nor the amount that it was obligated to pay was in dispute. The contract clearly established the amount of the obligation as \$20,000. Rainbow had a pre-existing duty to pay \$20,000, and therefore its promise to pay less could not be consideration for Quality's promise to take \$18,000 as full payment.

If Quality cashes the \$18,000 check, Rainbow is still obligated to Quality for \$2,000. An accord and satisfaction has not been made.



Even if the drawer's obligation is in dispute, new consideration for the payee's promise to do something that the drawer was not legally obligated to do already is consideration for the payee's promise to take the lesser amount as full payment. If, for example, the payee required the drawer to promise to pay a day or even an hour before the debt is due, pay at a different place, pay a third person, or pay in personal property or anything other than money, then the drawer's promise would be consideration for the payee's promise to take the lesser amount as full payment.

EXAMPLE 5–10

Jane borrowed \$2,000 from Sally and promised to repay her in one year at 6 percent interest. The amount due would be \$2,120. A week before the loan was due, Jane sent Sally a check for \$2,100 with the notation “payment in full.” If Sally accepts the check, she has accepted Jane’s offer for an accord contract. Although neither the existence of Jane’s obligation nor the amount of it was in dispute, Jane’s promise to pay before the due date would be consideration to support Sally’s promise to accept the lesser amount as full payment.

PARALEGAL EXERCISE 5.14 The Quality Print Company ordered 10,000 reams of paper from Excel Paper, Inc., at \$2 a ream. After the paper was delivered, Quality sent Excel a check for \$15,000 with the notation “payment in full.” If Excel cashes the check, does Excel still have a claim against Quality for \$5,000?

PARALEGAL EXERCISE 5.15 The Evertite Pool Company contracted to seal Jones’s leaking swimming pool for “a reasonable price.” After sealing the pool, Evertite sent Jones a bill for \$800. Jones, believing that a reasonable price was \$500, sent Evertite a check for \$500 with the notation “payment in full.” If Evertite cashes the check, does it still have a claim against Jones for \$300?

When a dispute exists, classical contracts law prevents the payee from rejecting the offer for the accord by altering the notation on the check. The payee, however, may negotiate the check without discharging the drawer if an accord cannot be proven or the payee does not see the obscure “payment in full” notation.

**PARALEGAL CHECKLIST****The Post-Acceptance Phase**

- After a contract has been formed, the paralegal and the supervising attorney can use the following analysis to determine the existence of problems that may arise after contract formation:
 1. Does the language of the contract require interpretation? The terms of the contract will be interpreted according to the reasonable person’s meaning. A term in the contract may have

different meanings for two different reasonable persons, one meaning known by the reasonable person in the general population and the other used by the reasonable person in a particular trade. The ordinary (nontrade or general) meaning will prevail unless both contracting parties are members of the trade and the term has a special meaning in the trade. If one of the parties is new to the trade, the trade meaning

will apply if he or she has actual knowledge of the trade meaning or the trade meaning is so generally known that actual knowledge could be inferred.

2. Has the contract been reduced to a final writing? The writing may encompass all or only some of the terms of the contract. Extrinsic evidence (oral or written) may not be introduced for the purpose of adding to or contradicting the final writing. Use the following line of inquiry to determine whether the extrinsic evidence creates a parol evidence rule problem. Some extrinsic evidence may be introduced without creating a parol evidence rule problem. Work through these steps to determine whether the extrinsic evidence creates a parol evidence rule problem. If there is no parol evidence rule problem, the evidence is not excluded.
 - a. Check whether the contract has been reduced to a final writing (an integration). Remember, not all writings are intended as final writings. If the contract has not been reduced to a final writing, there is no parol evidence rule problem even though there may be parol evidence (either oral or written).
 - b. Determine whether fraud, duress, or mutual mistake were involved in the final writing. If so, there is no parol evidence rule problem.
 - c. Analyze whether, if the contract has been reduced to a final writing, the writing is a final writing for all the terms of the contract (a total integration) or for only some of the terms (a partial integration).
 - d. Find out if the extrinsic evidence was made prior to or contemporaneous with the final writing. If the extrinsic evidence was made subsequent to the final writing, there is no parol evidence rule problem.
 - e. Consider whether the extrinsic evidence being presented intended to add to or contradict that part of the contract reduced to a final writing. There is no parol evidence rule problem if the contract was only partially integrated and if the extrinsic evidence attempts to add to or contradict only that part of the contract *not* reduced to a final writing. If, however, the extrinsic evidence attempts to add to or contradict the final writing (in either the partially integrated part or the totally integrated contract), there is a parol evidence rule problem. Remember, the test is “add to or contradict” the final writing and not merely “interpret” the final writing. An interpretation is not a parol evidence rule problem.
3. Have terms that the parties never discussed become part of the contract even if the contract is totally written, partially written, or completely oral? These terms include “good faith” and the UCC “gap fillers” if the contract is for a sale of goods.
4. If an oral contract has been reduced to writing, does the writing accurately reflect the terms of the oral contract? If a discrepancy is discovered after the fact, a court has the power to reform (alter) the writing to reflect the understanding of the parties.
 - a. Analyze whether the parties’ oral agreement expresses their real intentions.
 - b. Determine whether the writing fails to express those intentions.
 - c. Ascertain whether the failure is due to a mutual mistake or a unilateral mistake accompanied by the other party’s fraudulent conduct. Reformation is appropriate only if clear and convincing evidence demonstrates these three conditions.
5. Have the parties sought to modify the terms of the contract after it has been formed?
 - a. Analyze whether the modification involves an offer and an acceptance. As a general rule, the modification is itself a contract and requires an offer (a promise with consideration for that promise) and an acceptance (a promise or performance and consideration for that promise or performance).
 - b. Find out if the transaction involves a sale of goods. If it does, the Uniform Commercial Code provides that a modification can be effective without consideration.
6. Have the parties attempted to terminate the contract after it has been formed but before it has been fully performed?
 - a. If neither party has fully performed, a rescission contract may be made using the rules of contract formation (offer and acceptance).
 - b. If one party has fully performed, that party can unilaterally release the other party.
7. Has a release been used? Parties may settle noncontractual claims by using a release, if the release consists of an offer and an acceptance.

8. Has one contracting party attempted to terminate a contractual or noncontractual duty with a "payment in full" check (an accord and satisfaction)? The existence or the amount of the claim must be in dispute for an accord

contract to be created. The satisfaction is the performance of the accord contract. Once the accord contract has been performed, the original duty is terminated.

REVIEW QUESTIONS

DEFINE THE FOLLOWING NEW TERMS AND PHRASES

Accord

Duress

Fraud in the inducement

Good faith

Integration

Modification

Mutual mistake of fact

Mutual release

Parol terms

Plain meaning

Reformation

Satisfaction

Trade usage

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

1. T F A contract term is interpreted according to its "plain meaning."
2. T F Plain meaning is the meaning given to a contract term by the offeror.
3. T F The parties may, at the time of contracting, agree to give a term a meaning other than its plain meaning.
4. T F If a term has a trade meaning, it is always interpreted according to this trade meaning when both parties to the contract are members of the trade.
5. T F For contract formation purposes, a writing is required unless the offeror mandates that no writing is required.
6. T F Under the parol evidence rule, a contract may consist of both written and parol (including oral) terms.
7. T F The parol evidence rule applies to all transactions.
8. T F The parol evidence rule only comes into play when the terms of the contract have been set forth in a final writing.
9. T F The parol evidence rule does not apply to transactions where there has been fraud, duress, or mutual mistake.
10. T F If the writing is a partial integration, the parol evidence rule will apply to only the final writing part of the contract.
11. T F The parol evidence rule only excludes extrinsic evidence made prior to the final writing.
12. T F The parol evidence rule excludes extrinsic evidence made subsequent to the final writing.
13. T F The parol evidence rule only excludes evidence that is intended to clarify or interpret the terms in the final writing.
14. T F Both parties are required to negotiate a contract in good faith.

15. T F Both parties are required to perform a contract in good faith.
16. T F If the transaction is a sale of goods, Article 2 of the UCC will supply some terms omitted from the contract.
17. T F A mistake in integration occurs when the terms of the contract are inaccurately incorporated into the final writing.
18. T F A court has the power to reform the written evidence of a contract to reflect the understanding of the parties.
19. T F Reformation of a final writing is appropriate only if, by a preponderance of the evidence, the evidence demonstrates that:
 - (1) the parties' oral agreement expresses their real intentions;
 - (2) the writing fails to express those intentions; and
 - (3) the failure is due to a mutual mistake or a unilateral mistake accompanied by the other party's fraudulent conduct.
20. T F A mutual mistake is a mistake shared by both contracting parties at the time they reduced their agreement to writing.
21. T F If one of the contracting parties denies that a mistake occurred, the court will find that there is no mutual mistake.
22. T F Once a contract has been created it may not be modified.
23. T F Under classical contracts law, a modification is a contract and must follow the same rules of contract formation required for the original contract.
24. T F Under Article 2 of the UCC, an agreement modifying a contract for the sale of goods needs no consideration.
25. T F Parties may agree to end their contractual duties when the contract has been fully performed by neither party.
26. T F If parties want to rescind a contract which has been fully performed by neither party, they must follow the same rules of contracts law used to form the original contract.
27. T F The rescission of a contract has an offer and an acceptance.
28. T F When neither party has fully performed its contractual duties, the parties may rescind the contract by following the same rules of contracts law used when they formed the original contract.
29. T F When one party has fully performed but the other party has only partially performed, the party who has fully performed cannot unilaterally release the other party from its contractual duties.
30. T F The release parties use for terminating a noncontractual duty need not meet the requirements of contracts law.
31. T F An "accord and satisfaction" generally involves a check, written by one party to the other, stating "This check is taken in full payment of the obligation."
32. T F An "accord and satisfaction" can be used to discharge an obligation regardless of whether the existence of the obligation or the amount of the obligation is in dispute.
33. T F Constance Brown contracted to pay \$800 to Harvey Elliott for Harvey's promise to paint her house. After Harvey completed painting, Constance had second thoughts about the price and sent him a check for \$500 with the notation "Acceptance of this check constitutes payment in full." By

accepting the check, Harvey has no recourse against Constance for the remaining \$300.

34. T F An “accord and satisfaction” is a contract to pay a stated amount to discharge a prior obligation that is in dispute.
35. T F The traditional rules of offer and acceptance do not apply to the accord.
36. T F The “satisfaction” is the performance of the accord contract and discharges the original contractual duties.

FILL-IN-THE-BLANK QUESTIONS

- _____. The meaning that would be given to a contract term by a reasonable person.
- _____. The meaning that would be given to a contract term by members of a trade.
- _____. The correct spelling for the rule is payroll evidence rule, parole evidence rule, parol evidence rule.
- _____. A final writing between the contracting parties.
- _____. Extrinsic evidence whether written or oral.
- _____. A substantive rule of contracts law that may limit the terms of a contract in final written form to those in the writing.
- _____. The generic term used for those omitted terms supplied by Article 2 of the UCC.
- _____. The type of mistake that occurs when the integration of a contract does not accurately reflect the agreed upon terms.
- _____. The standard of proof necessary for the reformation of a contract due to a mistake in integration.
- _____. The process whereby the terms of a contract are changed to meet the changing needs of the parties.
- _____. The relinquishment of a right.
- _____. A contract to pay a stated amount to discharge a prior obligation that is in dispute and the performance of that contract.
- _____. A notation used on a check in an accord and satisfaction.

MULTIPLE CHOICE QUESTIONS (CIRCLE ALL THE CORRECT ANSWERS)

- Although words have standard meanings, these meanings may vary from time to time and region to region. Meanings may vary depending on whether the term is

used in its general sense or as a trade term with a special meaning. Circle the correct statements:

- (a) As a general rule, a contract term is interpreted according to its “plain meaning”
 - (b) If a term has a plain meaning but one of the parties (unknown to the other party) attributes a special meaning to that term, the term will be interpreted according to its special meaning
 - (c) The contracting parties may give a term a meaning other than its plain meaning
 - (d) If both contracting parties are members of a trade and the term has a trade and a nontrade meaning, the trade meaning will always prevail
 - (e) If both contracting parties are members of a trade and the term has a trade and a nontrade meaning, the trade meaning will always prevail unless one of the parties is new to the trade
2. The parol evidence rule does not apply to all transactions, nor does it apply to all parol (extrinsic) evidence. Circle the correct statements:
- (a) The parol evidence rule comes into play only when the terms of the contract have been set forth in a final writing (an integration)
 - (b) The parol evidence rule applies to transactions where there has been fraud, duress, or mutual mistake
 - (c) The parol evidence rule will apply to the entire contract if the writing is a total integration or to only the final writing part of the contract if the writing is a partial integration
 - (d) The parol evidence rule excludes only extrinsic evidence made subsequent to the final writing
 - (e) The parol evidence rule excludes only parol evidence that adds to or contradicts those terms that appear in the final writing
3. Benjamin Bickle, owner of a shopping center, leased space to Rita Pemberton so Rita could open a small sandwich shop. The agreement was reduced to a final writing. The writing was silent on whether Rita could sell tobacco products.
- (a) If Rita claims the writing was never intended to incorporate all the terms of the contract, the resolution of this dispute will involve the parol evidence rule
 - (b) If Rita claims that subsequent to the writing the parties agreed that she could sell tobacco products, the resolution of this dispute will involve the parol evidence rule
 - (c) If Rita claims the writing inaccurately omits the agreement as to tobacco products, the resolution of this dispute will involve a mistake in integration
 - (d) If Rita claims the writing inaccurately omits the agreement as to tobacco products, the resolution of this dispute will involve a mistake in understanding the terms of the contract
 - (e) If Rita claims the writing was not a final writing, the resolution of this dispute will involve the parol evidence rule
4. The Quality Glue Company contracted to sell to the Heirloom Furniture Company all of its glue requirements for the next year at \$10 a barrel. Three months into the contract, Quality raised its price to \$11 a barrel with Heirloom’s consent.

- (a) Under classical contracts law, the modification is ineffective since there is no new consideration for Heirloom's promise to pay \$11 a barrel
- (b) Under classical contracts law, the modification is ineffective since a contract cannot be modified
- (c) Under classical contracts law, the modification requires a peppercorn for Heirloom's promise to pay more per barrel
- (d) Under Article 2 of the UCC, the modification is ineffective since there is no new consideration for Heirloom's promise to pay \$11 a barrel
- (e) Under Article 2 of the UCC, the modification is ineffective since there is no new consideration for Quality's promise to continue to deliver

SHORT ANSWER QUESTIONS

1. A Seller of horse meat scraps contracted to give a Buyer of such scraps a \$5 discount for each ton analyzing less than 50% protein. When 140 tons of scraps contained protein varying from 49.53% to 49.96%, the Buyer demanded the discount. The Seller claimed that the trade meaning of 50% was 49.5%. Should the Buyer's meaning prevail?
2. Terri Fox orally contracted with a carpenter to have her house remodeled. The only writing was the carpenter's estimate. Is extrinsic evidence concerning this transaction inadmissible as a violation of the parol evidence rule?
3. Shelly Carter negotiated to purchase a home from Built Right Builders for \$150,000. During the negotiations, Built Right agreed to build a swimming pool for Shelly for an additional \$10,000. The final writing for the sale of the house for \$150,000 did not mention the swimming pool. Is the construction of the pool a term of the contract?
4. The Ponca City Police Department contracted to purchase ten police cars from the Ford Motor Company. When the cars arrived, they were black over white (top black, bottom white) rather than white over black (top white, bottom black). During the negotiations Ponca City had stated that they wanted white over black. The final writing merely said "black and white." Are the statements made during negotiations concerning the color of the cars admissible or does this extrinsic evidence violate the parol evidence rule?
5. The Bollingers owned property near the Pennsylvania Turnpike. Central, a contractor working on the Turnpike, orally contracted with the Bollingers for permission to deposit construction waste on the Bollingers' property. The oral contract provided that Central would reclaim the land after depositing the construction waste. The final writing did not mention soil reclamation. Should the integration be reformed to include soil reclamation?
6. When does a problem involve a mistake in integration rather than the parol evidence rule?



Drafting a Contract

◆ Drafting a Better Contract

Draft from an Outline

Be Brief

Simplify the Language

Use Base Verbs and the Active Voice

Avoid Sexist Language

Check for Spelling, Punctuation, and Grammatical Errors

◆ Drafting Exercise

Chapters 2, 3, 4, and 5 have taken you through the evolution of a contract: offer, post-offer/pre-acceptance, acceptance, and post-acceptance. We now have a contract and we know its terms. Some types of contracts must be in writing to be enforceable. Other types are enforceable without a writing. Even contracts that do not need to be in writing often are written. Chapter 6 briefly discusses the art of drafting a written contract.

DRAFTING A BETTER CONTRACT

Drafting contracts involves skills that the paralegal can develop and hone. The ability to write well is the most valuable tool a paralegal can acquire. The fol-

lowing material provides some suggestions for drafting a well-written contract. These suggestions also apply to drafting well-written memoranda and briefs. Paralegals should reflect upon their own writing and determine whether some of these tips could improve it.

Draft from an Outline

Before drafting, develop an outline for the contract. An outline helps the drafter present the terms of the contract in a logical, orderly fashion. An outline prevents the omission or duplication of essential terms.

Begin the outlining process by defining the purpose of the contract. Next, following the organizational structure of the road map (see the Introduction to this text), develop a checklist of items that the contract might or should address.

EXAMPLE 6–1 The following is the beginning of a checklist.

- 1.** Choice of law
The applicable state law if the parties decide to select the applicable state law (that is, choice-of-law provision)
- 2.** Contract formation
 - a.** The offeror's duties
 - b.** The offeree's duties
 - c.** The timing and dependence of the performance of the duties to one another
 - d.** Events or conditions necessary to create the duty
 - e.** Events or conditions necessary to terminate the duty
 - f.** Whether all the terms of this contract will be set forth in this writing and, if so, whether the writing should so state (i.e., merger clause)
- 3.** Enforcement
 - a.** If the type of contract must be in writing to be enforceable, the terms the writing should contain and who must sign
 - b.** If the contract could be held unenforceable, the alternative course of action of the parties
- 4.** Breach
 - a.** Definition of breach
 - b.** Significance of breach
- 5.** Remedies for the aggrieved party
 - a.** The aggrieved party's remedies
 - b.** Alternative methods of dispute resolution in lieu of litigation (e.g., mediation or arbitration)
 - c.** A statement relating to costs and attorneys' fees
 - d.** The forum in which litigation would take place

PARALEGAL EXERCISE 6.1 Relate the items in the checklist in the previous example to the terms of the following contract. What would you change in the contract to improve upon it?

LEASE

This contract is between _____, the Lessor, and _____, the Lessee, for the rental of a residential house located at _____. The lease term will begin on _____ and will end on _____.

The Lessor promises:

1. to have the property available and ready for occupancy at the beginning of the lease term;
2. to have the appliances in good working order and to reimburse Lessee for any repairs made to the appliances during the lease term;
3. to pay all taxes on the property during the lease term;
4. to insure the physical structure and the Lessor's personal property within the structure during the lease term;
5. to provide exterior maintenance, including yard maintenance service, during the lease term; and
6. to refund the Lessee's deposit, less deductions for damage, within 10 days after the Lessee vacates the property.

The Lessee promises:

1. to pay the Lessor \$ ____ monthly by the fifth of the month during the term of the lease;
2. to have the property available and ready for occupancy by the Lessor, or the Lessor's designee, at the end of the lease term;
3. to leave the property clean when vacating the property;
4. to maintain the appliances in good working order and to notify the Lessor in the event repairs are necessary;
5. to insure the Lessor's personal property within the structure during the lease term;
6. to notify the Lessor when exterior maintenance, including yard maintenance service, is needed;
7. to maintain the decorum of the neighborhood;
8. to not have pets on the premises unless with written consent of the Lessor;
9. to not sublease the property without written consent by the Lessor; and
10. to be responsible for up to and exceeding the deposit all damage to the property, beyond normal wear and tear.

Failure of the Tenant to pay the monthly rent on time or breach of any other promise by the Tenant shall be a breach of this agreement and shall entitle the Lessor to evict the Lessee. Eviction of the Lessee does not terminate the Lessee's duty to pay the remaining monthly payments.

In the event of a dispute between Landlord and Tenant, the parties will attempt to resolve their dispute through mediation using Early Settlement. In

the event the parties cannot resolve their dispute through mediation, then the dispute shall be resolved by arbitration using the _____ Arbitration Services.

With the signing of this lease, the Lessee has paid \$_____ as a deposit.

In the event a part of this lease is deemed void, the remainder of the lease shall be enforceable.

This writing incorporates the terms agreed to by the parties. Terms not in this writing are not terms of the lease.

This lease shall be governed by the laws of _____ .

Lessor

Lessee

Address

Address

Date

Date

Be Brief

Omit surplus words. State the meaning clearly and concisely. More words do not make a better contract. Wordiness only creates an opportunity for ambiguity and confusion. Eliminate unnecessary paragraphs, sentences, phrases, and words. Good writing is concise.

A single word can often substitute for a verbose phrase:

afford an opportunity	allow, let
and/or	or
as to whether	whether
at that point in time	then
due to the fact that	because
during the period when	when
during the time that	during, while
file an action against	sue
force and effect	force, effect
for the reason that	because
free and clear	free, clear
full and complete	full, complete
from the point of view	from, or
good consideration	consideration
have an impact on	affect
have a tendency to	tend
insofar as . . . is concerned	(omit entirely and start with the subject)
null, void, and of no further effect	void

point in time	time
prior to	before
subsequent to	after
suffer and permit	permit
sufficient consideration	consideration
there is no doubt but that	doubtless, no doubt
the question as to whether	whether, the question whether
this is a topic that	this topic
void contract	no contract
written document	document
written instrument	instrument

EXAMPLE 6-2

The following paragraph contains unnecessary and verbose phrases. They are in brackets.

[By this written document], the seller, [the party of the first part], for [good and sufficient] consideration, [hereby] gives [and grants to] the buyer, [the party of the second part], her ownership interest in Blackacre. If [for any reason] this [written] document is held [null], void, [and of no further effect], the seller, [the party of the first part,] shall return the [good] consideration [paid by the party of the second part] to the buyer, [the party of the second part].

By either omitting unnecessary phrases or by substituting a single word for a verbose phrase, this paragraph could read:

The seller, for consideration, gives the buyer her ownership interest in Blackacre. If this document is held void, the seller shall return the consideration to the buyer.

Many such phrases are compound prepositions:

by means of	by
by reason of	because of
by virtue of	by, under
for the period of	for
for the purpose of	to
in accordance with	by, under
inasmuch as	since
in connection with	with, about, concerning
in favor of	for
in instances in which	when
in lieu thereof	instead
in order to	to
in regard to	about
in relation to	about, concerning
in spite of the fact that	although

in terms of	in
in the nature of	like
in view of	because
on the basis of	by, from
on the part of	by
until such time as	until
with the exception of	except
with reference to	about, concerning
with regard to	about, concerning
with respect to	on, about

EXAMPLE 6-3

The following sentence contains two compound prepositions. They are indicated by brackets.

[In spite of the fact that] the prisoner implicated his co-conspirators, the jury found that [inasmuch as] the prisoner was the instigator, he could not be acquitted.

By substituting one word for each compound preposition, the sentence becomes:

Although the prisoner implicated his co-conspirators, the jury found that *since* the prisoner was the instigator, he could not be acquitted.

PARALEGAL EXERCISE 6.2 Remove the unnecessary verbiage from the following paragraph.

1. The lessor, party of the first part, agrees
2. to lease, rent and/or otherwise allow the lessee,
3. party of the second part, to use, occupy and
4. hereafter during the term of this lease, make use
5. of lessor's, said party of the first part's premises.
6. The lessee, said party of the second part, shall
7. compensate, pay and/or remit to the lessor, said
8. party of the first part, for and in consideration
9. of the said agreement of lease, rent and/or
10. otherwise use lessor's, said party of the first
11. part's premises, the dollar sum of Two Thousand
12. Dollars (\$2,000.00).

Simplify the Language

Use clear, concise terms. Avoid synonyms. If writers mean “rooster,” they should use “rooster.” If they mean “hen,” they should use “hen.” If writers mean “rooster” but use “chicken,” a synonym, the reader might believe they mean “hen.” Do not confuse the reader by using different words to refer to the same object or idea.

Avoid legalese. Legalese does not make a writing “legal.” Legalese only makes a writing pompous and confusing.

EXAMPLE 6-4

Said Jack and said Jill went up the said hill to fetch a said pail of said water.

When paralegals remove “said” from their writing, they should also remove “heretofore,” “one,” “whereas,” and any other legalese that they might find.

Remove the following:

aforementioned
aforesaid
forthwith
hereafter
hereby
herein
hereinafter
heretofore
herewith
one
said
thence
whereas

Minimize confusion by referring to parties by name rather than designating them “the party of the first part” and “the party of the second part.”

Avoid indefinite pronouns such as “it, they, this, who, and which.” An indefinite pronoun only adds confusion. When possible, substitute a noun for a pronoun.

PARALEGAL EXERCISE 6.3 Rewrite the following sentences to eliminate the indefinite pronouns:

1. In this law review article, it states that paralegals are real assets.
2. They say that the program for legal assistants is one that benefits students.
3. This text is written so that it can be put together one chapter after another.
4. There is a house, it stands on a hill.

Avoid “etc.”; it gives the reader no new information.

EXAMPLE 6-5

“The bride received gifts from New York, Florida, California, etc.” Rewrite: “The bride received gifts from many states, including New York, Florida, and California.”

Paralegals can simplify their drafting style by grouping similar terms together.

EXAMPLE 6-6

The seller shall deliver the goods to buyer's store. The buyer shall pay the seller upon delivery. The seller will pay the cost of shipping. The buyer will inspect the goods upon delivery. The goods are sold "as is." The buyer shall insure the goods during transit.

The seller shall:

1. sell the goods "as is";
2. deliver the goods to the buyer's store; and
3. pay the cost of shipping.

The buyer shall:

1. pay the seller upon delivery;
2. inspect the goods upon delivery; and
3. insure the goods during transit.

PARALEGAL EXERCISE 6.4 Redraft the following by deleting the legalese and grouping the lessor's duties and lessee's duties.

1. WITNESSETH: that the party of the first
2. part, for and in consideration of the rents,
3. covenants and agreements hereinafter contained,
4. does, and by these presents, demise, lease and
5. rent, for a period of six months from the first
6. day of June, 1999, to the party of the second
7. part, the following described property, to-wit:
8. The party of the second part, for and in
9. consideration of the use and possession of said
10. premises for said period, does hereby agree to pay
11. unto the party of the first part, the sum of Three
12. Thousand Dollars (\$3,000.00), said sum to be paid
13. in the following amounts and at the time herein
14. designated, to-wit:
15. On the first day of June, 1999, the sum of
16. Five Hundred Dollars (\$500.00), and on the first
17. day of each and every month thereafter the sum of
18. Five Hundred Dollars (\$500.00), until the total
19. sum of Three Thousand Dollars (\$3,000.00) shall
20. have been fully paid.
21. THE PARTY OF THE SECOND PART further agrees to
22. keep and maintain all portions of the building let
23. to him by the terms of this contract in as good
24. state of repair as the same are turned over to him.

25. THE SECOND PARTY further agrees to be
26. responsible and pay for the repair of any damage
27. done to any of the buildings or grounds by any of
28. his family or guests.
29. THE SECOND PARTY agrees to hold said first
30. party free from any and all expenses for lights,
31. heat or any other expense incident to the
32. occupant of said property.
33. THE PARTY OF THE SECOND PART shall not engage,
34. or allow any other person, pet or animal to engage
35. in, any conduct that will disturb the quiet and
36. peaceful enjoyment of the other tenants, the party
37. of the first part, or the neighbors of second
38. party, or use the premises for any purpose
39. whatsoever which violates the laws of the
40. United States, the State of New Hampshire, or the
41. City of Concord.

Use Base Verbs and the Active Voice

Write in the active voice, replacing nouns with verbs. The purest verb form is the base verb (for example, collide, decide, pay). Verbs give sentences movement and life. Nouns do not. Use the base verb rather than its derivative noun.

collide	collision
decide	decision
pay	payment

PARALEGAL EXERCISE 6.5 Identify four additional base verbs and their derivative nouns.

PARALEGAL EXERCISE 6.6 Write four sentences, each using one of the four derivative nouns from Paralegal Exercise 6.5. Then rewrite each sentence changing the noun to a verb.

Replace forms of the verb “to be” (is, are, be) with active verbs (run, skip, jump).

EXAMPLE 6–7

“The ruling was made by the trial judge” becomes “The trial judge ruled.”

The active voice energizes the paralegal’s writing. Substitute active for passive verbs. With the active voice, the subject of the sentence acts.

EXAMPLE 6–8

“Tom called the police.”

With the passive voice, the subject of the sentence is acted upon.

EXAMPLE 6–9

“The police were called by Tom.”

The passive voice usually requires more words than the active voice. In our illustration, the passive voice requires a supporting verb (were) and a preposition (by).

The passive voice creates detached abstraction within the sentence. With the active voice, the reader readily understands who is doing what to whom. With the passive voice, who is doing what to whom is often unclear.

Avoid Sexist Language

“Every man for himself” is history. Paralegals should delete sexist language from their writing. Several tips are useful:

1. Avoid expressions that imply value judgments based on sex.

EXAMPLE 6–10

“Are you a man or a mouse?”
“A difficult task is a man’s work.”
“Don’t be such a weak sister.”
“He refused to do woman’s work.”

2. Change the wording of male-oriented expressions to include both men and women.

EXAMPLE 6–11

“reasonable man” becomes “reasonable person”
“gentlemen of the jury” becomes “members of the jury”
“Dear Sir” becomes “Dear Madam or Sir”

3. Replace sex-based descriptions and titles with non-sex-based descriptions and titles.

EXAMPLE 6–12

“workman” becomes “worker”
“newsman” becomes “journalist”
“fireman” becomes “firefighter”

4. Use parallel construction when referring to both sexes.

EXAMPLE 6–13

“man and wife” becomes “husband and wife.”

5. Avoid masculine singular pronouns when not referring to a male. While “he or she” can be used in moderation, it is often best to rewrite the sentence.
 - a. Omit the pronoun if it is unnecessary.

EXAMPLE 6–14

“The average citizen feels that he is doing his duty by voting” becomes “The average citizen feels a duty to vote.”

EXAMPLE 6–15

“Every person has his constitutional rights” becomes “Every person has constitutional rights.”

- b. Use the second person rather than the third person.

EXAMPLE 6–16

“Each voter must cast his own ballot” becomes “As a voter, you must cast your own ballot.”

- c. Use the plural rather than the singular.

EXAMPLE 6–17

“Every spring the farmer plows his fields” becomes “Every spring farmers plow their fields.”

EXAMPLE 6–18

“The policeman risks his life on a daily basis” becomes “Police officers risk their lives daily.”

Check for Spelling, Punctuation, and Grammatical Errors

Eliminate common spelling errors. Do not expect a secretary to correct the mistakes. Errors will reflect on the paralegal and not the secretary. Paralegals should keep a list of words they tend to misspell.

EXAMPLE 6–19

The following are common spelling errors:

accommodate	not accomodate
coming	not comming
defendant	not defendent
demurrer	not demurer
judgment	not judgement
occurred	not occurred or ocured

Check punctuation.

Eliminate grammatical errors. A common error is to write “it’s” for “its” and “its” for “it’s.” “It’s” is a contraction, meaning “it is.” “Its” is a possessive pronoun.

EXAMPLE 6–20

“It’s February 2d and the groundhog saw its shadow.”

“Irregardless” is improper. Use “regardless.” Use “could have” and “should have” rather than “could of” and “should of.” Check “to,” “too,” and “two,” as well as “accept” and “except,” “advice” and “advise,” “affect” and “effect,” “between” and “among,” and “principal” and “principle.”

These suggestions are but a brief introduction to better drafting. A number of helpful books are available. They include: G. Block, *Effective Legal Writing* (Foundation Press 4th ed. 1992); S. Brody, J. Rutherford, L. A. Vietzen, & J. C. Dearback, *Legal Drafting* (Aspen 1994); M. Cohen, *Creative Writing for Lawyers* (Carol Publishing Group 1991); B. Garner, *The Elements of Legal Style* (Oxford University Press 1991); L. Glorfeld, D. Lauerman, & N. Stageberg, *A Concise Guide for Writers* (Holt, Rinehart & Winston 6th ed. 1984); C. E. Good, *Mightier Than the Sword, Powerful Writing in the Legal Profession* (Blue Jeans Press 1989); D. Lambuth, *The Golden Book on Writing* (Viking Press 1964); D. Mellinkoff, *The Language of the Law* (Little, Brown & Co. 1963); C. Miller & K. Swift, *The Handbook of Nonsexist Writing* (Harper & Row 2d ed. 1988); L. C. Oates, A. Enquist, & K. Kunsch, *Legal Writing Handbook* (Little, Brown & Co. 1993); M. B. Ray & B. J. Cox, *Beyond the Basics, A Text for Advanced Legal Writing* (West Publishing Co. 1991); W. Strunk & E. B. White, *The Elements of Style* (MacMillan 3d ed. 1979); P. Tepper, *Basic Legal Writing* (Glencoe 1992); R. Wydick, *Plain English for Lawyers* (Carolina Academic Press 3d ed. 1994).

DRAFTING EXERCISE

PARALEGAL EXERCISE 6.7 Your supervising attorney has a client, Sarah Delbarton, who has four children (Amy, age 12; Clara, age 8; Reginald, age 6; and Hugo, age 5). Ms. Delbarton, a single mother, travels extensively on business. Ms. Delbarton is in the process of hiring a tutor to teach her children. The tutor will receive room and board, a salary, and insurance benefits. The tutor will have a three-month probationary period, after which will begin a one-year term. Ms. Delbarton would like an option to renew for an additional year. After the renewal year, the parties will be free to renegotiate the contract. The household staff includes a housekeeper, a nanny, a cook, and a gardener. Ms. Delbarton would like your law firm to identify the appropriate person, to conduct the initial interview to screen applicants, to complete the necessary background check, and to prepare the necessary documents. Ms. Delbarton, however, would conduct the final interview and make the selection. Ms. Delbarton would like to remain anonymous until the final interview.

1. Draft an advertisement for your local newspaper. Should this advertisement be an offer or only preliminary negotiation?
2. Draft an offer in letter form. Do you want this offer to be a total integration of the terms of the proposed contract or only a partial integration so some terms will be in the writing and others will be supplied orally?

You may want to explore various form books or the internet for sample employment contracts. They may give you ideas about format and content. You may want to check out such web sites as “Legal Forms,” “Lectric Law Library’s Legal Form Room” and “Sample Employment Contract.” When using such material, a number of points must be remembered. First, the forms may not be accurate in spite of the drafters’ best efforts. Second, the forms may not be current because the law is always changing. Third, the forms may be accurate for one situation but not for another.

3. Assume that Ms. Delbarton has interviewed and selected Gwenneth Lloyd-Jones for the position and your firm has, on Ms. Delbarton’s behalf, sent Ms. Lloyd-Jones your offer. Ms. Lloyd-Jones, however, has responded with the following letter:

Thank you for your letter of June 5th. While I find the position and the terms of your letter very enticing, I have been advised to request that the following be added to the contract.

1. In the event of a dispute, I would like us to attempt to resolve the dispute by negotiation. If that fails, I would like us to try mediation. Only if negotiation and mediation fail, would we resort to arbitration. Disputes would not be resolved by litigation. Also, disputes will be resolved in this state using the laws of this state.
2. Although this contract is for a stated term, I would like the opportunity to terminate the contract upon four weeks’ notice.
3. I would like the option to include an automatic increase in compensation of 10%.

4. I would also like to be assured that during the first and each successive year of my employment, a two-week paid vacation is provided.

Please let me hear from you at your earliest convenience if these requests are satisfactory. I have another offer and need to make a decision within the next two weeks.

Is Ms. Lloyd-Jones's letter an acceptance, a rejection and counteroffer, or merely an inquiry? Draft a response.

4. It is now six months later. Ms. Lloyd-Jones has accepted Ms. Delbarton's offer as you have drafted it in part 3 and has begun work. Ms. Delbarton and Ms. Lloyd-Jones have discussed modifying their contract in the following manner: (1) increasing the term of the option to five years; (2) adding a week of vacation for each two years of service; and (3) decreasing compensation by 15% as each child graduates from high school and leaves the family estate.

Draft a modification of the contract that you drafted in part 3. Remember to provide the appropriate consideration for both the offeror's promise and the offeree's promise.

If additional facts are necessary for any part of this question, you may create these facts (including compensation) as you draft.



PARALEGAL CHECKLIST

Drafting a Contract

Paralegals can develop their drafting skills by using the following ideas:

1. Construct an outline for the contract before drafting.
 - a. Begin the outlining process by defining the purposes of the contract.
 - b. Prepare a checklist of items that the contract should address by following the organizational structure of the road map.
2. Be brief when drafting. Omit surplus words.
 - a. Can a single word substitute for a verbose phrase?
 - b. Can a compound preposition be eliminated?
3. Simplify the language. Use clear, concise terms.
 - a. Avoid synonyms.
 - b. Avoid legalese.
 - c. Refer to the parties by name rather than "the party of the first part."
 - d. Avoid indefinite pronouns.
 - e. Avoid "etc."
 - f. Simplify the drafting style by grouping similar terms together.
4. Use base verbs and the active voice.
 - a. Write in the active voice by replacing nouns with verbs.
 - b. Replace forms of the verb "to be" (is, are, be) with active verbs (run, skip, jump).
 - c. Substitute active for passive verbs.
5. Avoid sexist language.
 - a. Avoid expressions that imply value judgments based on sex.
 - b. Change the wording of male-oriented expressions to include both men and women.
 - c. Replace sex-based descriptions and titles with non-sex-based descriptions and titles.
 - d. Use parallel construction when referring to both sexes.
 - e. Avoid masculine singular pronouns when not referring to a male.
 - (1) Avoid pronouns if unnecessary.
 - (2) Use second person rather than third person.
 - (3) Use plural rather than singular.
6. Review for spelling, punctuation, and grammatical errors.

REVIEW QUESTIONS

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

1. T F Preparing an outline before drafting a contract is a waste of time.
2. T F Begin the outlining process by defining the purpose of the contract.
3. T F Good writing stresses conciseness.
4. T F Never use a single word when an important sounding phrase has the same meaning.
5. T F The longer the contract, the better the contract.
6. T F The use of “legalese” makes a contract look professional.
7. T F Avoid the use of synonyms in drafting a contract.
8. T F Indefinite pronouns make writing less confusing.
9. T F Always use the base verb rather than its derivative noun.
10. T F Do not worry about sexist language. Everyone knows that male-oriented expressions include both men and women.
11. T F Paralegals are responsible for correct spelling, punctuation, and grammar.
12. T F The use of “etc.” gives the reader no new information.
13. T F Synonyms add interest to an otherwise dull contract.
14. T F The use of ambiguous terms will add clarity and precision to a contract.
15. T F Always use “party of the first part” and “party of the second part” to distinguish between the parties.
16. T F Using different words to refer to the same object or idea will confuse the reader.

FILL-IN-THE-BLANK QUESTIONS

1. Substitute a single word for the verbose phrase:
 - a. _____ afford an opportunity
 - b. _____ and/or
 - c. _____ as to whether
 - d. _____ at that point in time
 - e. _____ due to the fact that
 - f. _____ during the period when
 - g. _____ during the time that
 - h. _____ file an action against
 - i. _____ force and effect
 - j. _____ for the reason that
 - k. _____ free and clear
 - l. _____ full and complete

- m. _____ . from the point of view
- n. _____ . good consideration
- o. _____ . have an impact on
- p. _____ . have a tendency to
- q. _____ . insofar as . . . is concerned
- r. _____ . null, void, and of no further effect
- s. _____ . point in time
- t. _____ . prior to
- u. _____ . subsequent to
- v. _____ . suffer and permit
- w. _____ . sufficient consideration
- x. _____ . the question as to whether
- y. _____ . this is a topic that
- z. _____ . void contract
2. Change each compound preposition to a single word:
- a. _____ . by means of
- b. _____ . by reason of
- c. _____ . by virtue of
- d. _____ . for the period of
- e. _____ . for the purpose of
- f. _____ . in accordance with
- g. _____ . inasmuch as
- h. _____ . in connection with
- i. _____ . in favor of
- j. _____ . in instances in which
- k. _____ . in lieu thereof
- l. _____ . in order to
- m. _____ . in regard to
- n. _____ . in relation to
- o. _____ . in spite of the fact that
- p. _____ . in terms of
- q. _____ . in the nature of
- r. _____ . in view of
- s. _____ . on the basis of
- t. _____ . on the part of
- u. _____ . until such time as
- v. _____ . with the exception of

- w. _____ with reference to
- x. _____ with regard to
- y. _____ with respect to
3. Change each noun to its base verb:
- a. _____ collision
- b. _____ decision
- c. _____ payment
- d. _____ elimination
- e. _____ rejection
- f. _____ disapproval
- g. _____ isolation
- h. _____ possession
- i. _____ affiliation
- j. _____ application
- k. _____ abduction
4. Correct the spelling of these words.
- a. _____ acomodate
- b. _____ comming
- c. _____ defendent
- d. _____ demurer
- e. _____ occurred
- f. _____ definate
- g. _____ existance
- h. _____ seperate
- i. _____ suprise
- j. _____ truely
- k. _____ untill
- l. _____ writting
- m. _____ writen
- n. _____ payroll evidence
- o. _____ Statue of Frauds

SHORT ANSWER QUESTIONS

1. Rewrite the following sentences replacing forms of the verb “to be” (is, are, be) with active verbs (run, skip, jump). The subject of an active verb is the doer of the action. A passive verb generally has two parts. The first part is a form of “be” such

as “be,” “been,” “is,” “are,” “was,” “were,” and “am.” The second part is a past participle (a verbal generally ending in “d,” “ed,” “n,” “en,” or “t”) such as “discussed” and “broken.” Therefore, “was discussed” and “were broken” are passive verbs. All other verb forms are active.

- a. The ruling was made by the trial judge.

- b. The race was won by Stacey Jackson.

- c. The biggest lie was told by my brother.

- d. The bus was towed by the wrecker.

- e. The game was won by a shot at the buzzer.

- f. The work had been done by the same few people.

2. Rewrite the following sentences using clear, concise terms.

- a. The aforementioned clock, hereinafter referred to as said clock, is a valuable antique.

- b. The aforesaid lessor will furnish all utilities to said lessee.

- c. Whereas said plumber, the party of the first part, had performed services heretofore on behalf of the customer, the party of the second part, the party of the first part presented a bill to the party of the second part.

d. Please respond to all inquiries hereafter forthwith.

e. We hereby request your cooperation in this matter.

f. Your timely response will afford an opportunity to file an action against the breaching party.

g. Please let us know as to whether you wish to pursue aforesaid matter.

h. You had problems at that point in time due to the fact that you failed to complete the work.

i. During the period when the aforesaid problems arose, they were ignored for the reason that all of the parties were out of town.

j. The promisee's promise was good consideration for the promisor's promise.

k. What you do at this point in time will have an impact on the entire case.

l. There is no doubt but that small problems have a tendency to grow larger until such time as they are resolved.

- m. In connection with your letter in regard to the written instrument enclosed herein, please call our office for an appointment.

- n. We received further information in relation to the matter subsequent to the time that we thought there had been full and complete disclosure.

- o. It will be unnecessary for you to contact us until such time as we notify you of further developments in the case inasmuch as there is nothing that can be done at this point in time.

3. Rewrite the following sentences using nonsexist language.

- a. The cook served man-sized portions.

- b. Now is the time for all good men to come to the aid of their country.

- c. Newsmen fly around the world covering interesting stories.

- d. Men and their wives often share a similar sense of humor.

- e. Firemen wear highly specialized protective clothing.

- f. Policemen directing traffic use reflective vests for safety.

g. The gentlemen of the jury often engage in lengthy deliberations.

h. The reasonable man will consider a question in an objective manner.

i. Nursing is a job for compassionate women.

j. Ordinary men may perform heroic actions under stress.

PART
III

Step Three: Contract Enforceability

INTRODUCTION

Contracts That Are Not Enforceable

CHAPTER 7

Contract Enforceability: Protecting a Class

CHAPTER 8

Contract Enforceability: Protecting a Party Against Overreaching

CHAPTER 9

Contract Enforceability: Protecting the Judicial Process

INTRODUCTION

Contracts That Are Not Enforceable

Although parties are free to create contracts, public interest may override the parties' freedom to contract. When this occurs, a court will refuse to enforce the contract brought before it. A balance must be struck between freedom *to* contract and freedom *from* contract. The identification of overriding public interest may come from the legislatures through statute or from the courts through the evolution of common law.

When contractual duties are not enforced by the courts, the overriding public interest may be classified into three categories depending on whether a class is being protected, a party is being protected against overreaching, or the judicial process is being protected.

Chapter 7 considers precluding enforcement of a contract to protect a class, such as minors, the mentally incapacitated, and persons incapacitated due to alcohol or other drugs. Chapter 8 explores precluding enforcement of a contract to protect a party against another party's overreaching through unconscionability, fraud, duress, or mistake in a basic assumption of fact. Chapter 9 investigates precluding enforcement of a contract to protect the judicial process from involvement in nonjudicial type activity, such as illegality, perjury, and inappropriate forum shopping.



Contract Enforceability: Protecting a Class

- ◆ **Minority (Infancy)**

 - Minority as a Defense to a Breach of Contract Action (Minority as a Shield)*

 - Minority as an Offensive Weapon (Minority as a Sword)*

 - Liability of the Minor for Necessaries*

 - Statutory Variations*

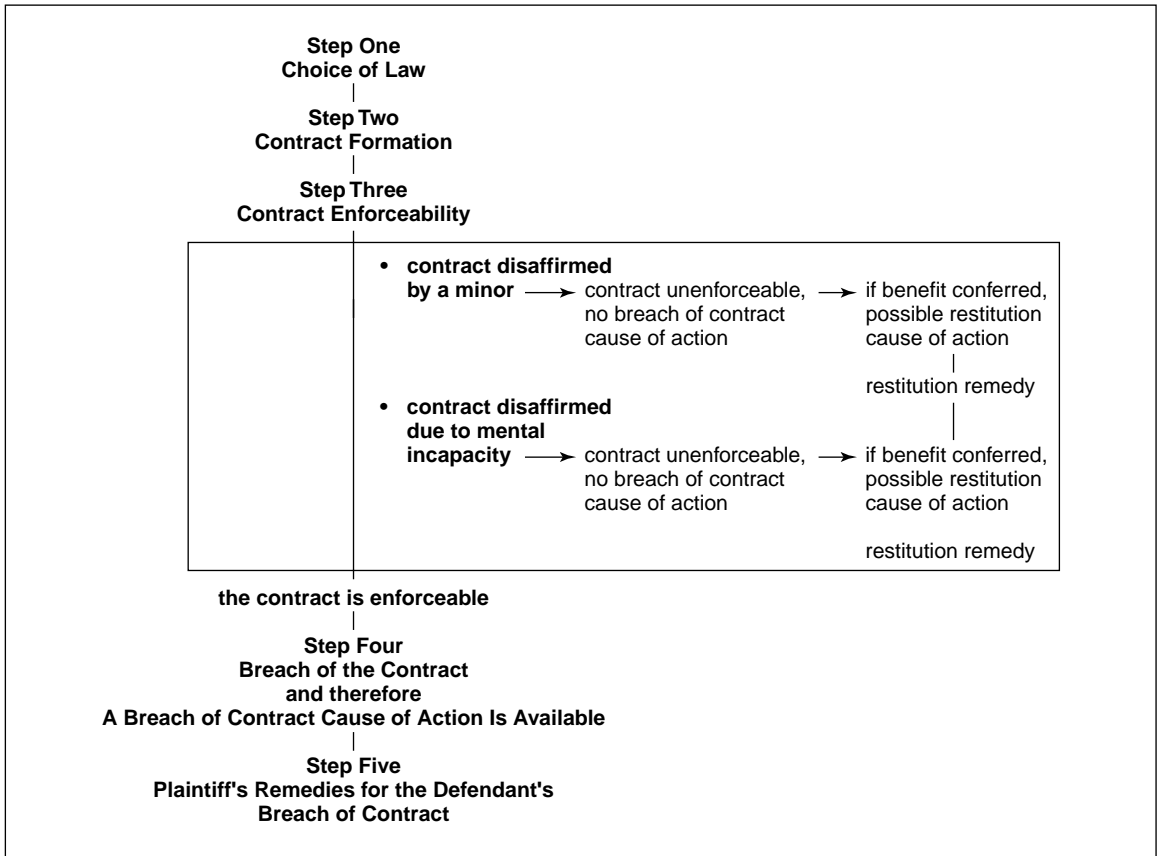
- ◆ **Mental Incapacity**

- ◆ **Incapacity Due to Alcohol or Other Drugs**

At times either the legislature or the court will find a class of people particularly vulnerable. Without some protection, members of these classes may contract when it is not in their own best interest. Rather than deal with each transaction as it arises, the law protects all members of the class in all their contract transactions. Instead of all members of the vulnerable class being precluded from contracting, they are permitted to contract as are others who are not members of these classes. The members of the protected class, however, are given the power to unilaterally disaffirm their contracts. When a contracting party disaffirms a contract, the party sets aside (**repudiates**) the contract.

Chapter 7 investigates three protected classes, the minor (infant), the mentally incapacitated, and the person lacking capacity due to alcohol or other drugs (see Figure 7–1).

FIGURE 7-1 The Contract Enforceability (Protecting a Class) Phase of the Road Map



MINORITY (INFANCY)

Minors have long been a protected class. Early contracts law, which was based on the meeting of the minds, viewed minors as mindless and, therefore, unable to contract. Their “contracts” were “void.” Modern contracts law, which is based on the manifestation of assent, gives minors the power to contract and the power to disaffirm a contract, even after the other party has fully performed. Early contracts law established the age of protection for minority as under twenty-one, but most modern statutes have rolled this age back to eighteen.

Minority as a Defense to a Breach of Contract Action (Minority as a Shield)

As a general rule, a minor may disaffirm a contract made during minority if the disaffirmance occurs during minority or within a reasonable time after reaching

the age of majority. The power to disaffirm is one-sided, giving only the minor the power to disaffirm. Disaffirmance ends the minor's duty to perform. Once the minor exercises the power to disaffirm, the other party may not enforce the contract. Minority, therefore, acts as a shield to an action of breach of contract.

EXAMPLE 7-1

When Charlene was 16, she entered into a four-year contract to model for Universal Modeling, Inc. Under the contract, Charlene promised to give Universal the exclusive rights to her services as a model. The contract also provided that in the event Charlene breached the contract, she would pay Universal \$5,000. A year later, Charlene was approached by Super Modeling, Inc., to model for them.

Since Charlene is still a minor, she could disaffirm her contract with Universal. If Charlene disaffirms her contract with Universal, she is not breaching the contract so she owes no duty to Universal to pay \$5,000 damages. Universal could not successfully sue Charlene for breach of contract because when Charlene disaffirmed the contract, it became unenforceable against her.

A minor need not disaffirm a contract during minority but may disaffirm within a reasonable time after reaching the age of majority. A reasonable time will vary depending on the circumstances. Some factors that may shed light on "reasonable time" include performance by either side, the nature of that performance, the ability of the minor to disaffirm, and the prejudice to be suffered by the minor's delay in disaffirming.

PARALEGAL EXERCISE 7.1 Just before going to college, Belinda, age seventeen, entered into three contracts. Should she have the same length of time after reaching majority (age eighteen) to disaffirm each?

1. Belinda contracts to model for an agency after she graduates from college.
2. Belinda buys a VCR from Quality Electronics and takes it to college.
3. Belinda buys a registered setter from Doctor Pets and takes it to college.

In each of these situations, would it matter whether Belinda was going to college near home or far away?

When a minor disaffirms a contract, whether during minority or within a reasonable time after reaching the age of majority, the contract is unenforceable and the other party has no cause of action for breach of contract. The other party is also precluded from successfully maintaining a restitution cause of action for unjust enrichment. If a restitution action could be maintained, it would erode the minor's absolute right to disaffirm. The minor would no longer be a

member of a protected group and would be easy prey for people who take advantage of those who are unable to protect themselves.

If the minor does not disaffirm the contract within a reasonable time after reaching the age of majority, the court will conclude that the minor, who has now reached the age of majority, has ratified the contract. **Ratification** is the confirmation of the contract.

The fact that the minor willfully misrepresented his or her age at the time of contract formation does not preclude the minor from disaffirming. The minor may, however, be liable in a separate tort action for misrepresentation.

EXAMPLE 7–2

When Alexander was sixteen, he purchased a Harley from Over-the-Road Motors. At the time of the purchase, Alexander represented his age as 18. When Alexander was seventeen, he disaffirmed the contract and discontinued his payments. Over-the-Road Motors could not successfully sue Alexander for breach of contract since the contract is not enforceable. Over-the-Road Motors could successfully sue Alexander for misrepresentation.

Minority as an Offensive Weapon (Minority as a Sword)

Minority may be the shield in an action for breach of contract brought by the other party against the minor. Minority may also act as a sword if the minor seeks to be returned to the time when the contract was formed. The minor must not only disaffirm the contract but must also seek a restitution cause of action for the return of what he or she has given the other party under the contract. As has been discussed previously, a restitution cause of action is based on unjust enrichment. The enrichment is the benefit conferred by the minor on the other party.

EXAMPLE 7–3

The minor may disaffirm the contract and seek a restitution cause of action for the reasonable value of the benefit conferred on the other party if:

- the minor has paid for the item (the benefit conferred is the payment)
- the minor has conveyed real or personal property (the benefit conferred is the real or personal property)

If the minor disaffirms the contract and seeks a restitution cause of action, the minor must return to the other party *only* what the minor received under

the contract *and* still has in his or her possession. The minor need not compensate the other person for something that he or she no longer has.

PARALEGAL EXERCISE 7.2 Lucy, age sixteen, contracted to buy an encyclopedia from the publisher for \$1,000. Lucy paid the purchase price and received her encyclopedia. Six months later, Lucy decided that she did not want the encyclopedia.

Could Lucy disaffirm the contract, return the used encyclopedia, and get her money back?

PARALEGAL EXERCISE 7.3 Jennifer, age sixteen, contracted to buy an heirloom gold pendant from Sly's Jewelry Store for \$200. She paid the purchase price and received the pendant. Over the next six months, the price of gold increased dramatically, and the pendant increased in value. Could Sly disaffirm the contract, return Jennifer's \$200, and get the pendant back?

If the price of gold decreased dramatically and the pendant decreased in value, could Jennifer disaffirm the contract, return the pendant, and get her \$200 back?

Upon disaffirmance, the minor will be restored to the position he or she was in before contracting. If, however, the minor has conveyed property to another party, that party may have conveyed the property to a third party. If real property has been conveyed to a subsequent purchaser who purchased in good faith and without notice of the fact that the original seller was a minor, the minor may still reclaim the real property. Personal property, however, may not be reclaimed by a minor from a subsequent bona fide purchaser for value.

PARALEGAL EXERCISE 7.4 Jeremy, age seventeen, purchased a used Ford Truck from Friendly Motors for \$1,500. He paid for his truck with \$1,000 in cash and the trade-in of his old Chevy. Shortly after delivering his Chevy to Friendly, paying the money, and taking delivery of the truck, Jeremy was involved in an accident in which his truck was totaled.

Can Jeremy disaffirm the contract and recover \$1,000 from Friendly? Can he recover the Chevy from Friendly?

If Friendly has sold the Chevy to Alice, who purchased it for value, in good faith, and without notice that it had been previously owned by a minor, can Jeremy recover his Chevy from her?

Prior to the time a minor disaffirms a contract and seeks restitution for the benefit he or she has conferred on the other contracting party, the minor may have used what the other contracting party has exchanged and it may have de-

preciated. Should the minor compensate the other contracting party for the value of the use and the depreciation of what the minor has received prior to the time of disaffirmance? Courts are divided on this issue. Some reason that the minor's right to disaffirm would no longer be absolute if the minor was required to compensate the other party for use and depreciation. Other courts reason that the minority doctrine should protect minors but not go so far as to give them a windfall.

If a minor is liable for the use and depreciation of what he or she received, the charge will be in the form of an offset. And **offset** is a deduction of the amount awarded to the defendant from the amount awarded to the plaintiff. In the case of a minor's disaffirmance, the offset is the deduction of the amount awarded to the defendant (non-minor) for use and depreciation from the amount of restitution awarded to the plaintiff (minor).

EXAMPLE 7-4

Teresa, a minor, purchased a motorcycle from Quality Motors for \$1,500. When Teresa disaffirmed the contract and returned the motorcycle to Quality, the motorcycle had depreciated \$500. Teresa is entitled to restitution of \$1,500 less an offset of \$500.

PARALEGAL EXERCISE 7.5 Is there a difference in whether the minor should be restored to the position she was in before contracting and, if so, how much she should receive in the following two situations:

1. Mary Alice, age sixteen, purchased a used Pinto from Friendly Ford for \$1,500. She took delivery of the Pinto and financed it over twenty-four months. After driving the Pinto for a year, Mary Alice disaffirmed the contract, ceased making payments, and returned the Pinto to Friendly Ford. Friendly Ford sued Mary Alice for breach of contract claiming that she breached the contract by not continuing to pay her installments.
What, if anything, should be restored to Mary Alice?
2. Using the same facts, assume that instead of financing the car, Mary Alice paid cash. Mary Alice sued Friendly Ford in a restitution action seeking the return of her money.
What, if anything, should be restored to Mary Alice?
Should the answers to these problems be the same or different? Why?

Liability of the Minor for Necessaries

A minor is liable for necessaries. Although the term necessaries generally consists of food, clothing, shelter, medical services, and education, the term necessaries varies with the facts. What may be considered necessaries for one minor

may not be considered necessities for another. **Necessaries**, as defined by the courts, are those articles that the minor actually needs and must supply for himself or herself because the person who has the duty to provide these articles either cannot or will not provide them.

In *Webster Street Partnership, Ltd. v. Sheridan*, two minors signed a lease, paid a security deposit, and paid rent for a period of time. After the landlord brought an action against the two minor tenants for back rent, one minor cross-petitioned seeking return of the security deposit and the other minor cross-petitioned seeking return of all monies paid to the landlord. The landlord claimed that the minors could not disaffirm the lease since the contract was for a necessary.



CASE

Webster Street Partnership, Ltd. v. Sheridan

Supreme Court of Nebraska, 1985. 220 Neb. 9, 368 N.W.2d 439.

KRIVOSHA, C. J., and BOSLAUGH, WHITE, HASTINGS, CAPORALE, SHANAHAN, and GRANT, JJ.

KRIVOSHA, Chief Justice.

Just what are necessities, however, has no exact definition. The term is flexible and varies according to the facts of each individual case. In *Cobbey v. Buchanan*, 48 Neb. 391, 397, 67 N.W. 176, 178 (1896), we said: "The meaning of the term "necessaries" cannot be defined by a general rule applicable to all cases; the question is a mixed one of law and fact, to be determined in each case from the particular facts and circumstances in such case." A number of factors must be considered before a court can conclude whether a particular product or service is a necessary. As stated in *Schoenung v. Gallet*, 206 Wis. 52, 54, 238 N.W. 852, 853 (1931):

"The term 'necessaries,' as used in the law relating to the liability of infants therefor, is a relative term, somewhat flexible, except when applied to such things as are obviously requisite for the maintenance of existence, and depends on the social position and situation in life of the infant, as well as upon his own fortune and that of his parents. The particular infant must have an actual need for the articles furnished; not for mere ornament or pleasure. The articles must be useful and suitable, but they are not necessities merely because useful or beneficial. Concerning the general character of the things furnished, to be necessities the articles must supply the infant's personal needs, either those of his body or those of his mind. However, the term 'necessaries' is not confined to merely such things as are required for a bare subsistence. There is no positive rule by means of which it may be determined what are or what are not necessities, for what may be considered necessary for one infant may not be necessities for another infant whose state is different as to rank, social position, fortune, health, or other circumstances, the question being one to be determined from the particular facts and circumstances of each case."

(Citation omitted.) This appears to be the law as it is generally followed throughout the country.

In *Ballinger v. Craig*, 95 Ohio App. 545, 121 N.E.2d 66 (1953), the defendants were husband and wife and were 19 years of age at the time they purchased a house trailer. Both were employed. However, prior to the purchase of the trailer, the defendants were living with the parents of the husband. The Court of Appeals for the State of Ohio held that under the facts presented the trailer was not a necessary. The court stated:

“To enable an infant to contract for articles as necessities, he must have been in actual need of them, and obliged to procure them for himself. They are not necessities as to him, however necessary they may be in their nature, if he was already supplied with sufficient articles of the kind, or if he had a parent or guardian who was able and willing to supply them. The burden of proof is on the plaintiff to show that the infant was destitute of the articles, and had no way of procuring them except by his own contract.”

(Citation omitted.) *Id.* at 547, 121 N.E.2d at 67. Under Ohio law the marriage of the parties did not result in their obtaining majority.

In 42 Am.Jur.2d *Infants* § 67 at 68–69 (1969), the author notes:

Thus, articles are not necessities for an infant if he has a parent or guardian who is able and willing to supply them, and an infant residing with and being supported by his parent according to his station in life is not absolutely liable for things which under other circumstances would be considered necessities.

The undisputed testimony is that both tenants were living away from home, apparently with the understanding that they could return home at any time. Sheridan testified:

Q. During the time that you were living at 3007 Webster, did you at any time, feel free to go home or anything like that?

A. Well, I had a feeling I could, but I just wanted to see if I could make it on my own.

Q. Had you been driven from your home?

A. No.

Q. You didn't have to go?

A. No.

Q. You went freely?

A. Yes.

Q. Then, after you moved out and went to 3417 for a week or so, you were again to return home, is that correct?

A. Yes, sir.

It would therefore appear that in the present case neither Sheridan nor Wilwerding was in need of shelter but, rather, had chosen to voluntarily leave home, with the understanding that they could return whenever they desired. One may at first blush believe that such a rule is unfair. Yet, on further consideration, the wisdom of the rule is apparent. If, indeed, landlords may not contract with minors, except at their peril, they may refuse to do so. In that event, minors who voluntarily leave home but who are free to return will be compelled to return to their parents' home—a result which is desirable. We therefore find that both the municipal court and the district court erred in finding that the apartment, under the facts in this case, was a necessary.

. . . .

Even when a minor is liable for necessities, the question remains whether the minor's liability is in a breach of contract action or in a restitution action. The courts are divided on this issue.

If the minor's liability is in a breach of contract action, the doctrine of necessities becomes an exception to the general rule that a minor has an absolute right to disaffirm a contract. The other party may then seek expectation damages. **Expectation damages** places the nonbreaching party in the position he or she would have been in had the contract been fully performed. This means that the other party would receive the full contract price.

If, however, the minor's liability is in a restitution action, the general rule that a minor has a right to disaffirm remains absolute. The minor may disaffirm a contract made for necessities. However, once the contract has been disaffirmed, the other party may pursue a cause of action in restitution for unjust enrichment. The other party may then seek restitution damages. **Restitution damages**, in the case of a minor's disaffirmance of a contract for necessities, returns the minor to the position he or she was in prior to the time when the minor received the benefit conferred under the contract.

This distinction may be important to the minor. Under the contract, the minor is liable for the contract price. Under a restitution action, the minor is only liable for the reasonable value to him or her. While the contract price and the reasonable value to the minor are often the same, instances may exist when they differ.

PARALEGAL EXERCISE 7.6 Donald, age sixteen, was involved in an automobile accident and was charged with leaving the scene of an accident. Donald hired the law firm of Ambrose & Pete to defend him. Through the firm's efforts, the charge was reduced to failure to yield the right of way, and Donald pleaded guilty, paying a small fine. The bill from Ambrose & Pete was \$1,000. After discovering that most other law firms charge \$700 for this service, Donald disaffirmed the contract and refused to pay.

Were the services of the law firm necessities?

If the services are not necessities, does Donald have the power to disaffirm the contract?

What damages will Ambrose & Pete recover if Donald disaffirms the contract?

If the services are necessities, does Donald have the power to disaffirm the contract?

What damages will Ambrose & Pete recover if Donald cannot disaffirm the contract even though the services were necessities?

What damages will Ambrose & Pete recover if Donald can disaffirm the contract and the services were necessities?

Statutory Variations

Although the minority doctrine began as a common law doctrine, a number of states now have statutes that deal with the minor's right to disaffirm a contract. Some statutes may establish the time after reaching majority in which the minor must disaffirm.

EXAMPLE 7-5

In all cases other than those specified herein, the contract of a minor may be disaffirmed by the minor himself, either before his majority or within one (1) year's time afterwards.

Some statutes address the issue of necessities.

EXAMPLE 7-6

(a) Contracts not disaffirmable. A contract, otherwise valid, entered into during minority, cannot be disaffirmed upon that ground either during the actual minority of the person entering into such contract, or at any time thereafter in the following cases:

1. Necessaries. A contract to pay the reasonable value of things necessary for his support, or that of his family, entered into by him when not under the care of a parent or guardian able to provide for him or them; provided, that these things have been actually furnished to him or to his family.

Other statutes may provide for judicially determined emancipation that includes the loss of the right to disaffirm. **Emancipation** means that the court no longer considers a person a minor even though the chronological age would fall within the definition of a minor.

EXAMPLE 7-7

A minor ordered emancipated under this Act shall have the right to enter into valid legal contracts, and shall have such other rights and responsibilities as the court may order that are not inconsistent with the specific age requirements of the State or federal constitution or any State or federal law.

In any event, when an issue of minority arises, the paralegal must check the appropriate state statutes to determine whether the governing state has codified or modified the common law rules.

MENTAL INCAPACITY

Early contracts law, under the meeting of the minds theory, denied the power to contract to the mentally incapacitated. A “contract” by a party who was mentally incapacitated was “void.” Modern contracts law (manifestation of assent) gives the mentally incapacitated the power to contract and the power to disaffirm the contract. Only the mentally incapacitated party has the power to disaffirm. The other party to the contract does not have this power.

Although a person suffering from mental incapacity may disaffirm the contract, the definition of what constitutes mental incapacity varies from state to state. Traditionally, the legislatures and courts measured contractual mental capacity by what is largely a “cognitive” test. Under the **cognitive test**, the court inquired whether the mind was so affected as to render the contracting party wholly and absolutely unable to comprehend and understand the nature of the transaction. This standard governing competency to contract evolved when psychiatric knowledge was primitive. This standard failed to account for those who by reason of mental illness were unable to control their conduct even though their cognitive ability seemed unimpaired.

Some courts and the drafters of the Restatement of Contracts have modernized the standard. The Restatement (Second) of Contracts § 15 provides the following version:

- (1) A person incurs only voidable contractual duties by entering into a transaction if by reason of mental illness or defect
 - (a) he is unable to understand in a reasonable manner the nature and consequence of the transaction, or
 - (b) he is unable to act in a reasonable manner in relation to the transaction and the other party has reason to know of his condition.
- (2) Where the contract is made on fair terms and the other party is without knowledge of the mental illness or defect, the power of avoidance under Subsection (1) terminates to the extent that the contract has been so performed in whole or in part or the circumstances have so changed that avoidance would be unjust. In such a case a court may grant relief as justice requires.

Subsection (1)(a) retains the cognitive test, the inability to understand. Subsection (1)(b) includes a “volitional” test. The **volitional test** recognizes an inability to act in a reasonable manner. The cognitive and volitional tests are alternatives. A person can disaffirm if by reason of mental illness or defect that person cannot understand OR cannot act in a reasonable manner. This permits people who understand but cannot control their actions to disaffirm their contracts. It should be noted that the power to disaffirm under subsection (1)(b) is limited to those situations where the other party had reason to know of the mental disease or defect.

EXAMPLE 7–8

Napoleon Westerville suffered from an insane delusion that he was Napoleon Bonaparte. During one of his delusionary episodes, Napoleon, dressed as Napoleon Bonaparte, purchased a Citroen from Import Motors and paid in cash.

Under the Restatement (Second) of Contracts § 15, Napoleon will be able to disaffirm the contract, return the Citroen, and recover his money. His demeanor and dress will establish that he contracted while he was suffering from mental illness—the delusion. If he cannot prove that he was “unable to understand in a reasonable manner the nature and consequences of the transaction,” because of the delusion, he could prove that he was “unable to act in a reasonable manner in relation to the transaction” because of the delusion. For the latter, Napoleon must also prove that Import Motors had reason to know of his condition, which could be established by his demeanor and dress.

PARALEGAL EXERCISE 7.7 Thelma Simmons, a sixty-year-old Medville schoolteacher, suffered a nervous breakdown and was placed on medical leave. Her illness was diagnosed as involving involuntional psychosis, melancholia type, and her psychiatrist suspected that she suffered from cerebral arteriosclerosis. While on disability, she contracted with her teachers’ retirement system to provide her the maximum retirement benefits during her lifetime with no benefits to her beneficiaries upon her death. She did not tell her husband, who was relying on the continuation of her retirement benefits as his sole means of support if she predeceased him.

Four months after contracting with the retirement system, Mrs. Simmons died, leaving her husband penniless.

Can Mrs. Simmons’s executor disaffirm her contract with the retirement system?

INCAPACITY DUE TO ALCOHOL OR OTHER DRUGS

The degree of incapacity due to alcohol or other drugs may vary. A person who is totally incapacitated due to alcohol or other drugs may, from an objective standard (the reasonable person), not even have the capacity to assent. In these instances, without a “manifestation of assent,” a contract cannot be formed.

A person who suffers from compulsive alcoholism or drug addiction may have diminished capacity to contract. Such a condition may constitute mental illness, and therefore, mental incompetency as grounds for disaffirmance of the

contract may be available. If the mental illness test of the Restatement (Second) of Contracts § 15 is followed, the person must, to incur only voidable contractual duties by reason of mental illness, be unable “to understand in a reasonable manner the nature and consequence of the transaction” or “to act in a reasonable manner in relation to the transaction and the other party has reason to know of his condition.” Even if a person qualifies under this test for the power to disaffirm a contract, the Restatement (Second) of Contracts § 15(2) places limitations on the power to disaffirm.

(2) Where the contract is made on fair terms and the other party is without knowledge of the mental illness or defect, the power of avoidance . . . terminates to the extent that the contract has been so performed in whole or in part or the circumstances have so changed that avoidance would be unjust. In such a case a court may grant relief as justice requires.

A person who voluntarily diminished his or her capacity to contract through the use of alcohol or other drugs may not be considered to have a mental illness. The Restatement (Second) of Contracts § 16, however, provides such a party with grounds to disaffirm a contract. Although the Restatement’s language is in terms of intoxication, it could be argued that the use of other drugs should be similarly treated.

A person incurs only voidable contractual duties by entering into a transaction if the other party has reason to know that by reason of intoxication

- (a) he is unable to understand in a reasonable manner the nature and consequences of the transaction, or
- (b) he is unable to act in a reasonable manner in relation to the transaction.

Under the Restatement’s test, if the intoxication does not constitute mental illness, an intoxicated person’s power to disaffirm is severely restricted. The other contracting party must have had reason to know that he or she was intoxicated and that, by reason of the intoxication, was unable “to understand in a reasonable manner the nature and consequences of the transaction” or “to act in a reasonable manner in relation to the transaction.”

PARALEGAL EXERCISE 7.8 In the case of *Lucy v. Zehmer*, the Zehmers, owners of the Ferguson Farm, operated a local restaurant. One evening, their old friend W. O. Lucy met them at the restaurant, and after a few drinks and a lot of talk, the Zehmers signed a writing saying they promised to sell W. O. Lucy the Ferguson Farm for \$50,000 cash. Review *Lucy v. Zehmer*, pages 46-49, in light of the incapacity due to alcohol and other drugs. Did Zehmer have the power to claim an incapacity and preclude the enforcement of the contract?



PARALEGAL CHECKLIST

Unenforceable Contracts—Protecting a Class

- ❑ The fact that a contract has been formed does not necessarily lead to the conclusion that it can be enforced in court by a nonbreaching party. The paralegal must evaluate whether one of the parties has the power to disaffirm the contract making it unenforceable. The supervising attorney will, of course, always make the final determination in all such matters and will advise the client. Enforcement problems can be divided into three broad categories:
 1. precluding enforcement of a contract to protect a class, such as minors, the mentally incapacitated, and persons incapacitated due to alcohol and other drugs;
 2. precluding enforcement of a contract to protect a party against another party's overreaching through unconscionability, fraud, duress, or mistake in a basic assumption of fact; and
 3. precluding enforcement of a contract to protect the judicial process from involvement in nonjudicial type activity, such as illegality, perjury, and inappropriate forum shopping.
- ❑ The following material deals with the first category, protecting a class.
 1. Was one of the parties a member of a protected class? If, at the time of contract formation, one of the parties was a minor, suffered from a mental disease or defect, or was under the influence of alcohol or other drugs, that party may be a member of a protected class and could possibly have the power to disaffirm the contract and claim unjust enrichment for any benefit conferred.
 2. Was the party a minor at the time of contract formation? If so, he or she may disaffirm the contract during minority or within a reasonable time thereafter.
 - a. Determine whether the minor has exercised the power to disaffirm. To do so, the minor must return to the other party only what the minor received under the contract and still has in his or her possession.
 - b. Find out if the minor has been restored to the position he or she was in before contracting. Upon disaffirmance, the minor is entitled to be restored to that position.
 - c. Evaluate whether the minor is liable for the necessaries. The minor may disaffirm a contract for necessaries but is still liable for the necessaries in a restitution action (reasonable value to the minor and not necessarily the contract price).
 - d. Check whether these general rules have been altered by statute or judicial decision.
 3. Was the party suffering from a mental illness or defect at the time of contract formation? If so, he or she may (if the Restatement (Second) of Contracts § 15 is followed by your court) disaffirm the contract if by reason of the mental illness or defect he or she was unable to understand in a reasonable manner the nature and consequence of the transaction or to act in a reasonable manner in relation to the transaction and the other party had reason to know of his or her condition. If the contract was made on fair terms and the other party was without knowledge of the mental illness or defect, the power to disaffirm may cease to the extent that the contract has been performed or the circumstances have changed causing disaffirmance to be unjust. In such a case, a court could grant relief as justice requires.
 4. Was the party incapacitated due to alcohol or another drug at the time of contract formation? If so, he or she may:
 - a. Determine whether the party was totally lacking the capacity to assent (using an objective standard). If so, the party may assert that the contract was not formed (no manifestation of assent);
 - b. Check whether the party was suffering diminished capacity due to compulsive alcoholism or drug addiction. If so, the party may assert the condition constitutes mental

- illness, thus rendering the contract unenforceable under the mental illness test;
- c. Analyze whether the party was suffering voluntarily diminished capacity due to alcohol or other drugs. If so, the party may assert that the contract was unenforceable: (1) if the other contracting party had reason to know of

his or her condition; and (2) that by reason of the alcohol or other drugs, he or she was unable to understand in a reasonable manner the nature and consequences of the transaction or to act in a reasonable manner in relation to the transaction.

REVIEW QUESTIONS

DEFINE THE FOLLOWING NEW TERMS AND PHRASES

Cognitive test

Disaffirm

Emancipation

Expectation damages

Necessaries

Offset

Ratification

Repudiation

Restitution damages

Volitional test

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

1. T F Certain classes of people are protected by law in their contract transactions.
2. T F The members of a protected class are given the power to unilaterally rescind their contracts.
3. T F Modern contracts law prevents minors from entering into contracts and thus their "contracts" are void.
4. T F Minors may disaffirm contracts made during minority if they disaffirm while still in minority or within a reasonable time after reaching majority.
5. T F Both parties involved in a contract in which one is a minor have the power to disaffirm.
6. T F A minor has the power to decide not to disaffirm a contract and may continue to perform and demand performance under the contract.
7. T F The minor who willfully misrepresents his or her age at the time of contract formation may not disaffirm.
8. T F Once a minor disaffirms a contract, the minor no longer has outstanding duties to perform and the other party may not enforce the contract against him or her.
9. T F The minor who willfully misrepresents his or her age at the time of contract formation may be liable in a tort action for misrepresentation.
10. T F A minor who disaffirms a contract will be restored to the position he or she was in before contracting.

11. T F A minor who disaffirms a contract may reclaim personal property but not real property from a subsequent bona fide purchaser for value.
12. T F The minor must restore to the other party what the minor received under the contract. If the minor no longer has what was given, then he or she cannot disaffirm the contract.
13. T F If the minor disaffirms the contract, discontinues performing, and files a restitution action to recover the benefit conferred on the other contracting party, many courts will charge the minor for the use and depreciation of what he or she received.
14. T F A minor who disaffirms a contract for necessities may still be liable for the reasonable value of the necessities.
15. T F If a minor disaffirms a contract for necessities, the minor will be liable in a breach of contract cause of action.
16. T F Under a restitution action a minor is only liable for the reasonable value of the necessities to him or her rather than the contract price.
17. T F A minor's liability for necessities is based on a restitution cause of action rather than breach of contract.
18. T F Early contracts law, based on the meeting of the minds theory, denied the mentally incapacitated the power to contract.
19. T F Modern contracts law allows both the mentally incapacitated party and the other party to disaffirm.
20. T F A person who is totally incapacitated due to alcohol or other drugs may not have the capacity to assent which is necessary to contract formation.
21. T F A person who suffers from mental illness due to compulsive alcoholism or drug addiction has an unlimited power to disaffirm a contract.
22. T F If voluntary intoxication does not constitute mental illness, the intoxicated person has no power to disaffirm a contract.

FILL-IN-THE-BLANK QUESTIONS

1. _____. A class of people protected by law in their contract transactions because of their age.
2. _____. The action that may be brought to allow the other contracting party to collect from a minor for necessities.
3. _____. The inability to understand or the inability to act in a reasonable manner due to mental illness or defect.
4. _____. A measure of contractual mental capacity to determine if a person is unable to understand the nature of the transaction.
5. _____. A measure of contractual mental capacity to determine if a person is unable to act in a reasonable manner.

MULTIPLE CHOICE QUESTIONS (CIRCLE ALL THE CORRECT ANSWERS)

1. A minor who enters into a contract has the power:
 - (a) to disaffirm the contract during minority
 - (b) to disaffirm the contract within a reasonable time after reaching majority
 - (c) to disaffirm the contract only if he or she still has what was received under the contract
 - (d) to disaffirm the contract and continue to retain what he or she received under the contract
 - (e) to ratify the contract after reaching majority
2. A minor, who has exercised his or her right to disaffirm the contract, cannot successfully maintain a restitution action to be restored to the position he or she was in before contracting if:
 - (a) the minor has ratified the contract
 - (b) the minor conferred no benefit on the other party
 - (c) the minor has conveyed real property and the other contracting party had already conveyed the property to a subsequent purchaser who purchased in good faith and without notice of the fact that the preceding vendor was a minor
 - (d) the minor no longer has what was given to him or her
 - (e) the subject of the contract was necessaries

SHORT ANSWER QUESTIONS

1. Albert, age seventeen, contracted to buy an automobile from Friendly Motors for \$4,500. Albert paid \$1,500 down and promised to pay the balance in monthly installments over three years. Two months after Albert turned eighteen, he was involved in an automobile accident and his car received \$4,000 in damage. Could Albert disaffirm the contract and recover the money that he paid.
2. How might a minor use minority (disaffirmance of a contract) as a defensive as well as an offensive weapon?



Contract Enforceability: Protecting a Party Against Overreaching

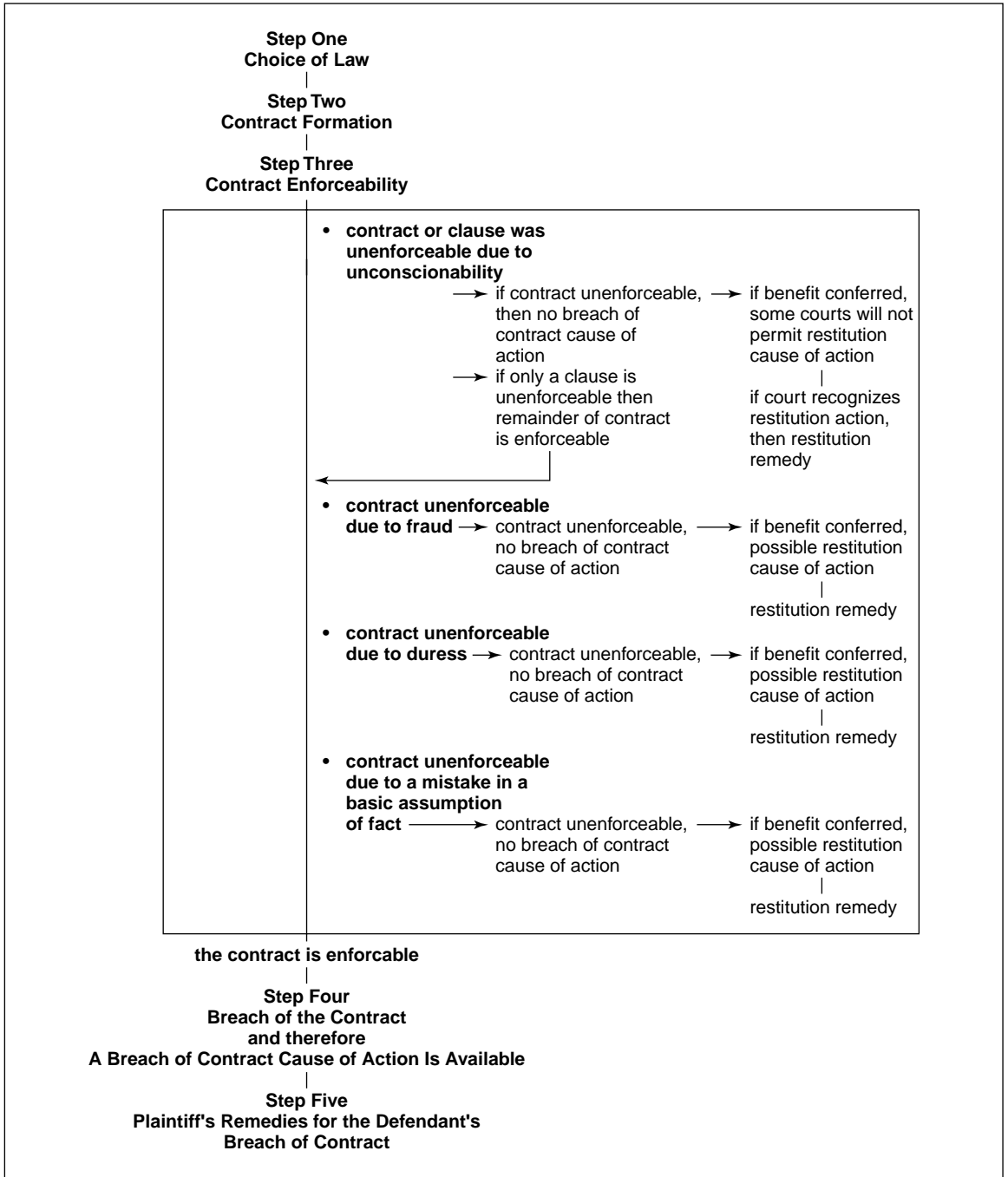
- ◆ Unconscionability and Adhesion Contracts

 - Unconscionability as a Defense to a Breach of Contract Action*
 - Restitution as a Cause of Action*

- ◆ Fraud and Misrepresentation
- ◆ Duress and Undue Influence
- ◆ Mistake in a Basic Assumption of Fact

Chapter 8, the second of three chapters dealing with contract enforceability, discusses governmental regulations (legislative and judicial) when one party overreaches another during contract formation. Rather than define a class and uniformly protect every member of the class (Chapter 7), a legislature or court may narrow its approach and protect the contracting party on a transaction-by-transaction basis. Chapter 8 explores four situations of overreaching: unconscionability and adhesion contracts; fraud and misrepresentation; duress and undue influence; and a mistake in a basic assumption of fact (see Figure 8–1).

FIGURE 8-1 The Contract Enforceability (Protecting a Party from Overreaching)
Phase of the Road Map



UNCONSCIONABILITY AND ADHESION CONTRACTS

An **adhesion contract** is a contract that was offered on a “take it or leave it” basis. The terms of a contract of adhesion are not negotiable. An offeree who receives such an offer has two choices: adherence to the terms of the offer or rejection of the offer. Adhesion contracts are commonplace and are found, for example, in the standardized forms produced by insurance companies, automobile dealerships, shipping companies, and airlines. As with any other document, an adhesion contract is strictly construed against its drafter.

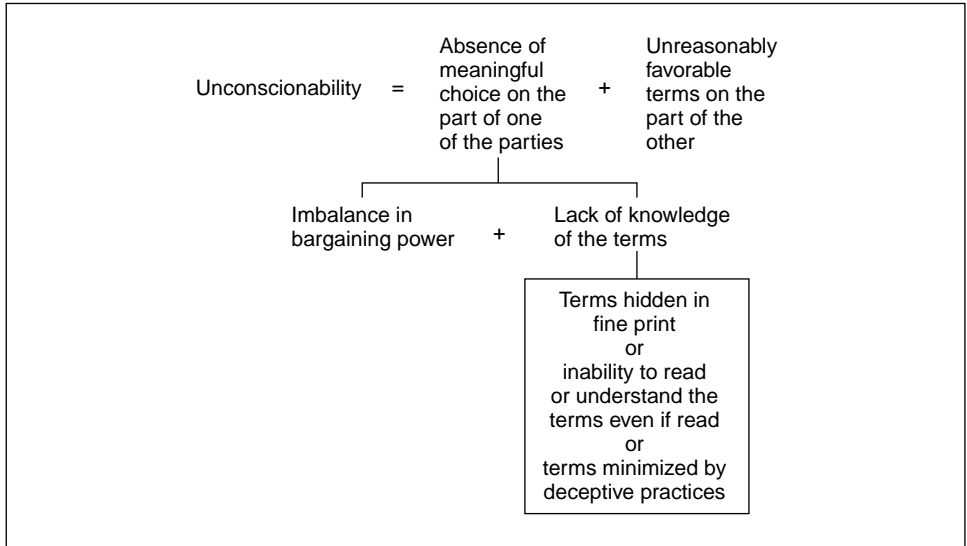
While standardized contracts illustrate adhesion contracts, nonstandardized contracts can be adhesion contracts as well. Nonstandardized contracts could involve a party with superior bargaining power who dictates the terms on a take it or leave it basis.

Adhesion contracts are not unenforceable because they are offered on a take it or leave it basis and are therefore one sided. An adhesion contract or a clause in an adhesion contract may be unenforceable if it is unconscionable. **Unconscionability** is characterized by the absence of meaningful choice on the part of one party together with terms that are unreasonably favorable to the other party. Therefore, an adhesion contract or clause in an adhesion contract is unconscionable if one party takes advantage of the other party’s lack of bargaining power by imposing *unreasonably* favorable terms.

Unconscionability as a Defense to a Breach of Contract Action

The contract or contract term must be unconscionable at the time of contract formation. If events subsequent to contract formation make the performance of the contract a severe hardship, the contract cannot be challenged as unconscionable.

Courts generally recognize unconscionability as an absence of meaningful choice on the part of one of the parties together with contract terms that are unreasonably favorable to the other party. Whether the first element of the test, “an absence of meaningful choice on the part of one of the parties,” is present in a particular case can only be determined once all the circumstances surrounding the transactions are considered. Absence of meaningful choice has two components: the imbalance in bargaining power and a lack of knowledge of the terms. A gross inequality of bargaining power will lead to the conclusion of absence of meaningful choice even if the other party had knowledge of the terms. If, however, the inequality of bargaining power is not gross, there still might be an absence of meaningful choice if the other party had little or no knowledge of the contract’s terms. This lack of knowledge may occur when the terms are hidden in a maze of fine print or minimized by deceptive sales practices. Even with a term that is clearly set forth, a party must be given a reasonable opportunity to become acquainted with the term.



For example, a contract written in English does not inform a buyer who can read only Spanish.

Absence of meaningful choice alone does not produce an unconscionable contract. The absence of meaningful choice must be coupled with a contract term that unreasonably favors the other party. If the term is not unreasonably favorable, it is not unconscionable even though there was a gross inequality of bargaining power, because the party with superior bargaining power has not taken advantage of that power.

Deciding whether the term is “reasonable” or “fair” cannot be done in a vacuum. The term must be considered in light of the circumstances existing when the contract was made. The general commercial background and the commercial needs of the particular trade or case shed light on reasonableness.

EXAMPLE 8-1

Brandi Pratt leased a BMW from Luxury Motors. The lease provided that at the end of the lease term, Pratt could purchase the vehicle for \$16,800, the estimated end-of-term wholesale value of the vehicle, or return it and pay a charge of 15 cents for each mile the vehicle had been driven over 85,000. Pratt chose not to purchase the BMW and returned it with an odometer reading of 180,400 miles. When she refused to pay for the excess mileage (\$14,310), Luxury Motors brought a breach of contract action. Pratt contended that the excess mileage provision of the lease was unconscionable because the charge was almost as much as the projected end-of-term value of the car. Luxury Motors responded that the excess mileage provision was not unreasonably favorable in light of commercial needs.

In the context of a corporation leasing a luxury vehicle, an excess mileage charge of 15 cents per mile is not unreasonable and certainly does not shock the conscience.

Such a charge serves the necessary commercial function of compensating for out-of-the-ordinary usage which will affect the residual value of the car. If at the end of the term defendants discovered the excess mileage charge was too high relative to the value of the car, they could have exercised their option to purchase it. But they did not do so, and now they cannot complain about a charge they agreed to pay. *BMW Financial Services, N.A., Inc. v. Smoke Rise Corp.*, 226 Ga. App. 469, 486 S.E.2d 629 (1997).

When a transaction involves a sale of goods, the Uniform Commercial Code simplifies the court's inquiry when the issue of unconscionability arises. Section 2-302 provides:

(1) 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.

(2) 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.

If section 2-302 applies, the courts may refuse to enforce the contract, delete the unconscionable term and enforce the remainder of the contract, or reform the unconscionable term so it no longer produces unconscionable results. Under section 2-302(2), the court may, of its own accord, raise the issue of unconscionability. Also, if the issue of unconscionability is raised, the court *must* hold a hearing to determine the issue. Unconscionability is a question for the court (the judge) to resolve. It is not a question for the jury.

PARALEGAL EXERCISE 8.1 Homer and Felicia Oakley, who are welfare recipients, contracted to purchase a used Chevy Suburban from A-1 Used Cars for \$7,000. With the addition of the time credit charges, credit life insurance, credit property insurance, and sales tax, the purchase price totaled \$12,300. After the Oakleys paid \$6,000, they ceased paying. A-1 brought a breach of contract action against the Oakleys seeking the remaining contract price. The Oakleys claimed that since the Suburban had a blue book price of \$3,500 at the time of contract formation, the contract price was unconscionable.

Should the court reform the contract price to the amount paid so the Oakley's will not be in breach of contract?

Unconscionability has not been a panacea for all disappointed contracting parties. A survey of the cases would indicate that a party claiming unconscionability will generally not prevail. *Fotomat Corporation of Florida v. Chanda* explores why findings of unconscionability should be meted out judiciously.



CASE

Fotomat Corporation of Florida v. Chanda

District Court of Appeal of Florida, 1985. 464 So. 2d 626.

ORFINGER, Judge.

The defendant appeals from a final judgment awarding damages of \$9,500 to plaintiff, resulting from the loss of film which plaintiff has delivered to defendant for processing. We reverse.

Plaintiff Chanda, a medical doctor, after reading a magazine article indicating that the deterioration of movie film could be avoided by transferring the images on the film to videotape, and having read a flyer distributed by defendant which advertised the availability of such service, delivered 28 rolls of already developed Super-8 movie film to one of defendant's outlets in Melbourne, Florida in April of 1980. Defendant's clerk prepared an order form which contained information necessary to identify the customer, type of film and type of videocassette ordered, and other matters incidental to the transaction, and which also contained in a conspicuous place on the sheet and in bold type, the following language:

IMPORTANT

THE WARRANTY BELOW GIVES YOU SPECIFIC LEGAL RIGHTS AND LIMITATIONS. PLEASE READ IT CAREFULLY.

By depositing film or other material with Fotomat, customer acknowledges and agrees that Fotomat's liability for any loss, damage, or delay to film during the processing service will be limited to the replacement cost of a non-exposed roll of film and/or a blank cassette of similar size. Except for such replacement, Fotomat shall not be liable for any other loss or damage, direct, consequential, or incidental, arising out of customer's use of Fotomat's service.

Customer Signature

Dr. Chanda read this clause, asked the clerk about it, and then signed it.

The film was lost and never made its way back to the plaintiff. Despite every effort on the part of defendant to locate it, it was never found nor could anyone account for its disappearance. Dr. Chanda testified that the film was of great sentimental value to him and to his family because it contained depictions of his honeymoon, the graduation ceremony at his medical school, movies of his son's birth and early life, and many memorable vacations which he and his wife had taken. In proving his damages, he was permitted to testify, over objection, on how much time and expense would be involved in duplicating so much of the lost film as was capable of duplication. This claim included travel expenses, lodging, meals, child care for his two children at home, and the overhead expense he would incur in his medical practice while he was away.

At an in-camera hearing prior to the commencement of the jury trial, the court determined that the limitation of liability clause was unconscionable at the time it was made. See section 672.302, Florida Statutes (1981). At the conclusion of the evidentiary portion of the trial, the court instructed the jury to disregard the loss limitation provision of the agreement in arriving at their verdict. Defendant contends that the trial court erred in permitting evidence as to plaintiff's consequential damages, and in its ruling that the limitation of liability clause was invalid as unconscionable. Because we agree that the court erred in holding the limitation of liability provision to be invalid, we need not discuss the damage issue.

Florida has adopted the Uniform Commercial Code in dealing with commercial transactions. Section 672.2–302 of the Florida Statutes (1979) states:

(1) 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.

(2) 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.

The code does not attempt to define “unconscionability.” Consequently, those courts which have dealt with the problem have often looked to the common law of their respective jurisdictions because, in most, this code provision is, in reality, a codification of the common law rules. In the seminal case of *Williams v. Walker-Thomas Furniture Company*, 350 F.2d 445 (C.A.D.C.1965), the court was faced with a contract entered into before the adoption by Congress of the Uniform Commercial Code for the District of Columbia, but decided after its adoption. First determining that the code provision followed the common law of the District, the court discussed unconscionability in terms of its elements:

Unconscionability has generally been recognized to include an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party. Whether a meaningful choice is present in a particular case can only be determined by consideration of all the circumstances surrounding the transaction. In many cases the meaningfulness of the choice is negated by a gross inequality of bargaining power. The manner in which the contract was entered is also relevant to this consideration. Did each party to the contract, considering his obvious education or lack of it, have a reasonable opportunity to understand the terms of the contract, or were the important terms hidden in a maze of fine print and minimized by deceptive sales practices? Ordinarily, one who signs an agreement without full knowledge of its terms might be held to assume the risk that he has entered a one-sided bargain. But when a party of little bargaining power, and hence little real choice, signs a commercially unreasonable contract with little or no knowledge of its terms, it is hardly likely that his consent, or even an objective manifestation of his consent, was ever given to all the terms. In such a case the usual rule that the terms of the agreement are not to be questioned should be abandoned and the court should consider whether the terms of the contract are so unfair that enforcement should be withheld. (Footnotes omitted).

Id. at 449–450.

Florida has long recognized the principle that the courts are not concerned with the wisdom or folly of contracts, *Duvall v. Walton*, 107 Fla. 60, 144 So. 318 (1932), but where it is perfectly plain to the court that one party has overreached the other and has gained an unjust and undeserved advantage which it would be inequitable to permit him to enforce, a court will grant relief even though the victimized parties owe their predicament largely to their own stupidity. *Peacock Hotel, Inc. v. Shipman*, 103 Fla. 633, 138 So. 44 (1931). Decisions in Florida since the adoption of the Uniform Commercial Code appear to follow the principles espoused in the earlier cases.

In *Kohl v. Bay Colony Club Condominium, Inc.*, 398 So.2d 865 (Fla. 4th DCA), *review denied*, 408 So.2d 1094 (Fla.1981), the court reviewed the authorities on the subject and concluded that:

The authorities appear to be virtually unanimous in declaring (or assuming) that two elements must coalesce before a case for unconscionability is made out. The first is referred to as substantive unconscionability and the other procedural unconscionability.

A case is made out for substantive unconscionability by alleging and proving that the terms of the contract are unreasonable and unfair.

Procedural unconscionability, on the other hand, speaks to the individualized circumstances surrounding each contracting party at the time the contract was entered into. This is thoughtfully discussed by the court in *Johnson v. Mobil Oil Corp.*, 415 F.Supp. 264, 268 (E.D.Mich.1967):

The various factors considered by the courts in deciding questions of unconscionability have been divided by the commentators into "procedural" and "substantive" categories. See J. White & R. Summers, *supra*, at 118–30. Under the "procedural" rubric come those factors bearing upon what in the *Weaver* case was called the "real and voluntary meeting of the minds" of the contracting parties: 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. The "substantive" heading embraces the contractual terms themselves, and requires a determination whether they are commercially reasonable. According to J. White & R. Summers, *supra*, at 128:

Most courts take a "balancing approach" to the unconscionability question, and to tip the scales in favor of unconscionability, most courts seem to require a certain quantum of procedural plus a certain quantum of substantive unconscionability.

Id. at 867–68. See also, *Bennett v. Behring Corp.*, 466 F.Supp. 689, 696 (S.D.Fla.1979).

This court has approved the "procedural-substantive" analysis in determining the question of unconscionability, and has approved *Kohl*. *State v. De Anza Corporation*, 416 So.2d 1173 (Fla. 5th DCA), *review denied*, 424 So.2d 763 (Fla.1982). Although rejecting the notion that the *Kohl* analysis is a rule of law, the court in *Steinhardt v. Rudolph*, 422 So.2d 884 (Fla. 3d DCA 1982), *review denied*, 434 So.2d 889 (Fla.1983), found it "generally helpful" and applied it to the facts of that case. The *Steinhardt* court nevertheless recognized the long standing principle of law that:

All of this does not mean, however, that a court will relieve a party of his obligations under a contract because he has made a bad bargain containing contractual terms which are unreasonable or impose an onerous hardship on him. Indeed, the entire law of contracts, as well as the commercial value of contractual arrangements, would be substantially undermined if parties could back out of their contractual undertakings on that basis. "People should be entitled to contract on their own terms without the indulgence of paternalism by courts in the alleviation of one side or another from the effects of a bad bargain. Also, they should be permitted to enter into contracts that actually may be unreasonable or which may lead to hardship on one side. It is only where it turns out that one side or the other is to be penalized

by the enforcement of the terms of a contract so unconscionable that no decent, fairminded person would view the ensuing result without being possessed of a profound sense of injustice, that equity will deny the use of its good offices in the enforcement of such unconscionability.' " (Citations omitted). (Emphasis added).

Id. at 890.

Applying the substantive prong of the test here, it cannot be said, as a matter of law, that the limitation clause here was unreasonable, when viewed in its commercial setting and when considering its purpose and effect. The charge for the processing service here was \$31.00. The videocassette was priced at \$18.95, and there was an additional \$2.00 charge for an item not identified. There was un rebutted defense testimony that the limitation of liability provision was standard in the industry because, although loss and damage of film was relatively low in view of the tremendous volume of work done, no film processor would expose itself to liability for the unknown content of film without having to so greatly increase the cost to the public as to price the service out of the market. This is clearly a commercially reasonable consideration. As one court has aptly put it,

To put the company . . . in that type of situation in which it rides every tiger that a person with a camera can imagine and carry out seems to be unconscionable. That is not to say that this limitation of liability is a perfect one, but it seems a fairly reasonable one.

Aetna Casualty & Surety Co. v. Eastman Kodak Co., District of Columbia Superior Court, 10 U.C.C.Rep.Serv. 53 (1972).

Other courts have examined similar limitation clauses in film transactions and have refused to declare these provisions unconscionable. In a commercial film transaction, the court in *Posttape Associates v. Eastman Kodak Co.*, 450 F.Supp. 407 (1978) (E.D.Pa.1978) considered a clause similar to the one here, and commented:

It is the "unknown or undeterminable risks" which justify the utilization of a limitation in the film industry. Not only are the risks difficult to access because of the latent nature of any film defect, but also because usually the seller is not aware of the scope of the commercial film maker's undertaking.

Id. at 412. The same principle has been applied in cases where the work was noncommercial, as where an amateur photographer leaves his vacation films with a photo supply shop for processing. *Carr v. Hoosier Photo Supplies, Inc.*, 441 N.E.2d 450 (Ind.1982).

The reasonableness of the clause is demonstrated by the huge loss claimed by Dr. Chanda, compared to the cost of the service. Without a doubt the film had peculiar value to the plaintiff. Some of it was irreplaceable and all of it was of great sentimental value, but that unknown "tiger" is the very reason for the inclusion of the limitation of liability provision in the transaction. There is no way the processor can conceive of the risk it takes in accepting film for processing absent an explicit agreement to accept such risk. When the customer is made aware of the provision for limitation of liability and nevertheless proceeds with the transaction he has assented to an agreement for which there is a commercial need, if the cost of the service is to be made reasonable.

Neither can we perceive that plaintiff satisfied the procedural prong of the test. The evidence reflects that Dr. Chanda saw and read the clause in question, asked a question about it and was apparently satisfied with the answer because he signed it. He had previously suffered the loss of film at a different place of business, and it had been replaced by new film. He was a doctor, well educated, experienced in business transactions, and well aware of what he was signing. While he was given no opportunity to negotiate the terms of this agreement,

he did not attempt to determine if anyone else could provide this service. Thus the evidence falls short of showing procedural unconscionability. If, as indicated by the official comment to Section 2-302 of the Uniform Commercial Code, the principle involved in the section "is one of the prevention of oppression and unfair surprise . . . and not of disturbance of allocation of risks because of superior bargaining power," no such oppression or unfair surprise is shown here.

Appellee's reliance on *Mieske v. Bartell Drug Co.*, 92 Wash.2d 40, 593 P.2d 1308 (1979) is misplaced. Although the scenario in that case is much like the one here, there is one very salient and important distinction. In *Mieske*, the plaintiff's wife, who brought the already developed film to the drug store for splicing and placing onto larger reels, was given a receipt for the film which contained a brief limitation of liability clause. It was not called to her attention nor discussed, she was not aware of it, and she had had no prior experience with or knowledge of any custom of the trade to include such provision in film transactions. The clerk who accepted the film did not recall discussing the clause with her, nor was he even sure what it meant. The court found that:

As to course of dealings, the record is clear that Mrs. Mieske and the Bartell manager never discussed the exclusionary clause. Mrs. Mieske had never read it, she viewed the numbered slip as merely a receipt. The manager was not "too clear on what it said." There was no showing what was the language on any other receipt given in prior dealings between the parties. In summary, defendants' proof fell short of that required by the express language of [the statute].

Id. at 1313.

It is clear from the record here that the trial court refused to consider and apply the procedural/substantive test to determine the issue of unconscionability. Neither was any other objective analysis applied, but instead, the court appeared to view the unfairness of the agreement in retrospect, because of the result. The contract should have been reviewed in the light of the circumstances that existed when it was made. The judgment for plaintiff is reversed, and the cause is remanded to the trial court with directions to enter judgment for plaintiff for the cost of 28 rolls of unexposed Super-8 movie film.

REVERSED and REMANDED.

COWART, J., and POWELL, R. W., Associate Judge, concur.

Restitution as a Cause of Action

The previous discussion portrayed unconscionability as a defense to a breach of contract action (a shield). The defendant in a breach of contract action has an opportunity to claim that the contract or a critical contract term is unconscionable and therefore unenforceable. If the court finds the contract or term unconscionable, the plaintiff's breach of contract action will be dismissed.

Unconscionability also may support an action and therefore become a sword. In *Jones v. Star Credit Corp.*, the Joneses were visited at their home by a sales representative from Your Shop At Home Service, Inc. During the visit, the Joneses purchased a \$300 home freezer for \$900 plus credit life insurance, credit property insurance, and sales tax. After paying over \$600, the Joneses brought an action to reform the contract. In reading *Jones*, answer the following:

1. Who is the plaintiff, who is the defendant, what is the plaintiff's cause of action, and what relief is the plaintiff seeking from the court?
2. Did the Joneses and Your Shop At Home Service create a contract?
3. Could the Joneses seek reformation of the price term by claiming the price term was unconscionable?
 - a. Was the price term unreasonably favorable toward the Your Shop At Home Service?
 - b. Did the Joneses lack a meaningful choice?
 1. What was the relative bargaining power between the parties?
 2. What knowledge did the Joneses have about the price term?



CASE

Jones v. Star Credit Corp.

Supreme Court of New York, 1969. 59 Misc. 2d 198, 298 N.Y.S.2d 264.

SOL M. WACHTLER, Justice.

On August 31, 1965 the plaintiffs, who are welfare recipients, agreed to purchase a home freezer unit for \$900 as the result of a visit from a salesman representing Your Shop At Home Service, Inc. With the addition of the time credit charges, credit life insurance, credit property insurance, and sales tax, the purchase price totaled \$1,234.80. Thus far the plaintiffs have paid \$619.88 toward their purchase. The defendant claims that with various added credit charges paid for an extension of time there is a balance of \$819.81 still due from the plaintiffs. The uncontroverted proof at the trial established that the freezer unit, when purchased, had a maximum retail value of approximately \$300. The question is whether this transaction and the resulting contract could be considered unconscionable within the meaning of Section 2-302 of the Uniform Commercial Code which provides in part:

(1) 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.

(2) 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. L.1962, c. 553, eff. Sept. 27, 1964.

There was a time when the shield of "caveat emptor" would protect the most unscrupulous in the marketplace—a time when the law, in granting parties unbridled latitude to make their own contracts, allowed exploitive and callous practices which shocked the conscience of both legislative bodies and the courts.

The effort to eliminate these practices has continued to pose a difficult problem. On the one hand it is necessary to recognize the importance of preserving the integrity of agreements and the fundamental right of parties to deal, trade, bargain, and contract. On the other hand there is the concern for the uneducated and often illiterate individual who is the victim of gross inequality of bargaining power, usually the poorest members of the community.

Concern for the protection of these consumers against overreaching by the small but hardy breed of merchants who would prey on them is not novel. The dangers of inequality of bargaining power were vaguely recognized in the early English common law when Lord Hardwicke wrote of a fraud, which "may be apparent from the intrinsic nature and subject of the bargain itself; such as no man in his senses and not under delusion would make." The English authorities on this subject were discussed in *Hume v. United States*, 132 U.S. 406, 411, 10 S.Ct. 134, 136, 33 L.Ed. 393 (1889) where the United States Supreme Court characterized (p. 413, 10 S.Ct. p. 137) these as "cases in which one party took advantage of the other's ignorance of arithmetic to impose upon him, and the fraud was apparent from the face of the contracts."

The law is beginning to fight back against those who once took advantage of the poor and illiterate without risk of either exposure or interference. From the common law doctrine of intrinsic fraud we have, over the years, developed common and statutory law which tells not only the buyer but also the seller to beware. This body of laws recognizes the importance of a free enterprise system but at the same time will provide the legal armor to protect and safeguard the prospective victim from the harshness of an unconscionable contract.

Section 2-302 of the Uniform Commercial Code enacts the moral sense of the community into the law of commercial transactions. It authorizes the court to find, as a matter of law, that a contract or a clause of a contract was "unconscionable at the time it was made", and upon so finding the court may refuse to enforce the contract, excise the objectionable clause or limit the application of the clause to avoid an unconscionable result. "The principle", states the Official Comments to this section, "is one of the prevention of oppression and unfair surprise". It permits a court to accomplish directly what heretofore was often accomplished by construction of language, manipulations of fluid rules of contract law and determinations based upon a presumed public policy.

There is no reason to doubt, moreover, that this section is intended to encompass the price term of an agreement. In addition to the fact that it has already been so applied (State by *Lefkowitz v. ITM, Inc.*, 52 Misc. 2d 39, 275 N.Y.S.2d 303; *Frostifresh Corp. v. Reynoso*, 52 Misc.2d 26, 274 N.Y.S.2d 757, revd. 54 Misc.2d 119, 281 N.Y.S.2d 964; *American Home Improvement, Inc. v. Maclver*, 105 N.H. 435, 201 A.2d 886, 14 A.L.R.3d 324), the statutory language itself makes it clear that not only a clause of the contract, but the contract in toto, may be found unconscionable as a matter of law. Indeed, no other provision of an agreement more intimately touches upon the question of unconscionability than does the term regarding price.

Fraud, in the instant case, is not present; nor is it necessary under the statute. The question which presents itself is whether or not, under the circumstances of this case, the sale of a freezer unit having a retail value of \$300 for \$900 (\$1,439.69 including credit charges and \$18 sales tax) is unconscionable as a matter of law. The court believes it is.

Concededly, deciding the issue is substantially easier than explaining it. No doubt, the mathematical disparity between \$300, which presumably includes a reasonable profit margin, and \$900, which is exorbitant on its face, carries the greatest weight. Credit charges alone exceed by more than \$100 the retail value of the freezer. These alone, may be sufficient to sustain the decision. Yet, a caveat is warranted lest we reduce the import of Section 2-302 solely to a mathematical ratio formula. It may, at times, be that; yet it may also be much more. The very limited financial resources of the purchaser, known to the sellers at the time of the sale, is entitled to weight in the balance. Indeed, the value disparity itself leads inevitably to the felt conclusion that knowing advantage was taken of the plaintiffs. In addition, the meaningfulness of choice essential to the making of a contract, can be negated by a gross inequality of bargaining power. (*Williams v. Walker-Thomas Furniture Co.*, 121 U.S.App.D.C. 315, 350 F.2d 445.)

There is no question about the necessity and even the desirability of instalment sales and the extension of credit. Indeed, there are many, including welfare recipients, who would

be deprived of even the most basic conveniences without the use of these devices. Similarly, the retail merchant selling on installment or extending credit is expected to establish a pricing factor which will afford a degree of protection commensurate with the risk of selling to those who might be default prone. However, neither of these accepted premises can clothe the sale of this freezer with respectability.

Support for the court's conclusion will be found in a number of other cases already decided. In *American Home Improvement, Inc. v. MacIver*, supra, the Supreme Court of New Hampshire held that a contract to install windows, a door and paint, for the price of \$2,568.60, of which \$809.60 constituted interest and carrying charges and \$800 was a salesman's commission was unconscionable as a matter of law. In *State by Lefkowitz v. ITM, Inc.*, supra, a deceptive and fraudulent scheme was involved, but standing alone, the court held that the sale of a vacuum cleaner, among other things, costing the defendant \$140 and sold by it for \$749 cash or \$920.52 on time purchase was unconscionable as a matter of law. Finally, in *Frostifresh Corp. v. Reynoso*, supra, the sale of a refrigerator costing the seller \$348 for \$900 plus credit charges of \$245.88 was unconscionable as a matter of law.

Having already paid more than \$600 toward the purchase of this \$300 freezer unit, it is apparent that the defendant has already been amply compensated. In accordance with the statute, the application of the payment provision should be limited to amounts already paid by the plaintiffs and the contract be reformed and amended by changing the payments called for therein to equal the amount of payment actually so paid by the plaintiffs.

In *Jones*, the plaintiffs asked the court to reform the price term in the contract to allow them to keep the freezer without making further payments. Could the Joneses have asked the court to reform the price term to an amount less than what they had paid and to award them a judgment for what they paid over that amount? Some courts have expressed reluctance to go this far. One such court was the United States Court of Appeals, Eleventh Circuit, in *Cowin Equipment Co. v. General Motors Corp.* Cowin and other dealers contracted with General Motors for the purchase of heavy equipment. Although the contract required written notice of cancellation 90 days before the date of scheduled assembly, General Motors had permitted liberal cancellation. Subsequently the contract was modified to require noncancellation of orders. Cowin placed an order and then canceled. General Motors ignored the cancellation and shipped. Cowin sued General Motors for breach of the original modification seeking damages. General Motors defended by raising the modification. Cowin countered that the noncancellation term in the modification was unconscionable under section 2-302 of the UCC. The district court viewed the case as a Uniform Commercial Code unconscionability action for damages, held the terms unconscionable as a matter of law, and denied GM's motion for summary judgment. The Eleventh Circuit reversed and granted GM's motion for summary judgment.

While reading *Cowin*, consider the following:

1. What was Cowin's cause of action?
2. On what basis did the court deny Cowin's cause of action?
3. While the *Cowin* court was reluctant to open a new avenue of recovery for the plaintiff, should an injured party be able to maintain a restitution action for damages independent of section 2-302 of the UCC?



CASE

Cowin Equipment Co. v. General Motors Corp.

Eleventh Circuit, United States Court of Appeals 1984. 734 F.2d 1581.

Before GODBOLD, Chief Judge, RONEY and KRAVITCH, Circuit Judges.

RONEY, Circuit Judge:

Plaintiff Cowin Equipment Co., Inc. sued General Motors Corporation (GMC) for damages on the ground that the terms of its dealer sales and service agreement were unconscionable under § 2-302 of the Uniform Commercial Code. The district court held the provision was unconscionable as a matter of law and denied defendant's motion for summary judgment. We granted leave to appeal on the district court's 1292(b) certificate. 28 U.S.C.A. § 1292(b). We reverse on the ground that U.C.C. § 2-302, which concerns unconscionable contracts, does not create a cause of action for damages.

This is a diversity case. The agreement indicated that Ohio law would apply. The district court applied Alabama law. The parties do not contend there is any difference between Ohio law and Alabama law. Alabama and Ohio have adopted substantially identical versions of the Uniform Commercial Code (U.C.C.) provisions which are cited in this opinion. See Ala. Code § 7-2-302; Ohio Rev.Code Ann. § 1302.15. Consequently, we will refer to the applicable U.C.C. provisions without additional reference to their Alabama or Ohio statutory counterparts.

Briefly, the facts are as follows: In early 1978, GMC and its dealers anticipated an increase in demand for Terex heavy equipment, which GMC manufactured and Cowin sold. GMC responded by instituting a "Planned Distribution Program" (PDP), which modified the former agreement between the parties by requiring Cowin and other dealers handling Terex equipment to place non-cancellable orders in advance for equipment to be shipped between September 1, 1978 and August 1, 1979. Formerly GMC had permitted liberal cancellation, although the terms of its agreement with its dealers provided for cancellation only upon written notice received ninety days prior to the date of scheduled assembly "unless otherwise agreed at the time an order is submitted by dealer and accepted by Terex."

Cowin ordered forty-four machines in the months following. Due to a downturn in the economy, however, Cowin later attempted to cancel some of the orders. GMC refused to permit cancellation and delivered all of the machines as ordered, leaving Cowin with excess inventory. Cowin sued in December, 1980 seeking damages on grounds that the PDP terms were unconscionable. Specifically, plaintiff sought compensation for (1) interest incurred on loans necessary in order to buy equipment which defendant would not allow cancellation on; (2) insurance on the equipment; (3) storage and maintenance fees on the equipment; (4) loss incurred from sale of certain equipment sold for less than its purchase price.

The district court viewed the case as a "Uniform Commercial Code unconscionability action for damages" based on what it found to be unconscionable terms in the sales and service agreement between the parties. Our review of the Code provisions and the relevant cases persuades us that U.C.C. § 2-302 was not intended to create a cause of action, and cannot be used as a basis for damages in the instant case.

The language of § 2-302 and the Official Comment which follows it make no mention of damages as an available remedy for an unconscionable contract. This is consistent with traditional common law unconscionability theory. When the equity courts found contracts to be unconscionable, they refused specific enforcement. See J. White and R. Summers, *Uniform Commercial Code*, § 4-2 at 113, and § 4-8 at 130 (1972) (citing *Earl of Chesterfield v. Janssen*, 28 Eng.Rep. 82 (Ch.1750)). The remedies available to modern courts under § 2-302 are of similar equitable nature:

(1) 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.

U.C.C. § 2–302 (1983).

No case has been cited in which a damage award was based on an unconscionable contract. Although apparently not decided in either Alabama or Ohio courts, the cases which have addressed the issue have consistently rejected the theory that damages may be collected for an unconscionable contract provision, citing the language of § 2–302 and its common law precursor to demonstrate that § 2–302 was not intended to provide a basis for damage recovery. *See, e.g., Bennett v. Behring Corp.*, 466 F.Supp. 689, 700 (S.D.Fla.1979).

(the equitable theory of unconscionability has never been utilized to allow for the affirmative recovery of money damages. The Court finds that neither the common law of Florida, nor that of any other state, empowers a court addressing allegations of unconscionability to do more than refuse *enforcement* of the unconscionable section or sections of the contract so as to avoid an unconscionable result.)

(citations omitted); *Whitman v. Connecticut Bank and Trust Co.*, 400 F.Supp. 1341, 1346 (D.Conn.1975) (“The ‘unconscionability’ provision of the Uniform Commercial Code . . . carries no provision for damages; the remedy it provides is express.”); *Pearson v. National Budgeting Systems, Inc.*, 297 N.Y.S.2d 59, 31 A.D.2d 792 (N.Y.App.Div.1969) (“Section 2–302 of the Uniform Commercial Code does not provide any damages to a party who enters into an unconscionable contract.”); *Vom Lehn v. Astor Art Galleries, Ltd.*, 86 Misc.2d 1, 380 N.Y.S.2d 532, 541 (N.Y.Sup.Ct.1976) (“U.C.C. § 2–302 . . . makes no provision for damages, and none may be recovered thereunder.”). *See also* 2 R. Anderson, *Uniform Commercial Code* § 2–302:102 (3d ed.1982) (“[t]he unconscionability section of the Code does not authorize the recovery of any damages by the buyer, the relief obtainable being limited to that stated by the Code, namely, that the court may refuse to enforce the contract or the unconscionable provision”); 15 *Williston on Contracts* § 1763A at 215 (3d ed.1972) (“a court under [§ 2–302] may not award damages to the party who enters into an unconscionable agreement”).

Cowin contends that the damages requested were granted not on grounds of unconscionability of the Planned Distribution Program, but rather under the terms of the former agreement between the parties. Under Cowin’s theory, unconscionability simply provides a basis for striking the “clause” containing the Planned Distribution Program which GMC asserts as an affirmative defense, rendering the former agreement applicable. Cowin thus claims that the district court’s holding did not award damages under U.C.C. § 2–302.

The language used by the district court in its opinion, however, does not support this conclusion. The opinion opens by characterizing this case as “a Uniform Commercial Code unconscionability action for damages,” and closes with the observation that

[w]hile unconscionability has normally been used as a shield against oppressive and unfairly surprising terms of contracts, that shield can equitably be beaten into a sword of restitution attacking those terms. The court, therefore, finds that the terms implementing the Planned Distribution Program are unconscionable as a matter of law.

Our decision on this point forecloses Cowin’s attempt to recover damages on grounds of the unconscionability of the non-cancellation clause. GMC’s motion for summary judgment should have been granted. The district court’s denial of defendant’s motion for summary judgment is reversed and the case is remanded for entry of an appropriate judgment in accord with this opinion.

REVERSED and REMANDED.

FRAUD AND MISREPRESENTATION

Although courts often use the terms “fraud” and “misrepresentation” interchangeably, a distinction exists. The Restatement (Second) of Contracts provides that an assertion does not have to be fraudulent to be a misrepresentation. The Restatement (Second) of Contracts § 159 provides:

A **misrepresentation** is an assertion that is not in accord with the facts.

A statement the speaker intends as truthful may be a misrepresentation because of ignorance or carelessness.

EXAMPLE 8-2

Jerry's Electric Company, seeking to induce Bernard to buy a particular generator, wrote Bernard a letter with the intention of describing its output correctly as “1200 kilowatts.” Due to a typist's error, unnoticed by Jerry's, the letter stated that the generator's output was “2100 kilowatts.” When Bernard accepted Jerry's offer, a contract was formed. After Jerry's shipped the generator and Bernard accepted delivery and paid, Bernard discovered the generator's output was only “1200 kilowatts.” Jerry's statement is a misrepresentation as to the output of the generator. Bernard, the party relying on the misrepresentation, may assert that the contract is unenforceable (disaffirm), return the generator, and seek restitution of his purchase price.

A misrepresentation may be fraudulent. A fraudulent misrepresentation may be either fraud in the “factum” (fraud in the “essence”) or fraud in the “inducement.” **Fraud in the “factum”** involves the very character of the proposed contract. If the deceived party neither knows nor has reason to know of the character of the proposed contract, the effect of the misrepresentation is that the parties never contracted.

EXAMPLE 8-3

Rebecca visited Import Motors, Inc., to look at used BMWs. While there Rebecca noticed that Import Motors was giving a free trip to the Bahamas for the winner of a drawing. Quincy, a salesperson, encouraged Rebecca to sign her name to the entry form without reading the fine print. Had she read the fine print she would have discovered that she had purchased the used BMW on display. Since Rebecca did not know that what she had signed was the acceptance of an Import Motors's offer, the effect of the misrepresentation is that she never accepted the offer.

Fraud in the “inducement” involves a misrepresentation that entices a party to accept an offer. We will focus our attention on this latter type of fraud, fraud in the “inducement.” Whenever a party fraudulently induces another to enter into a transaction, the deceived party may disaffirm the contract and, in those cases where the defrauded party has conferred a benefit on the defrauding party, claim restitution. This power to disaffirm protects innocent parties from deliberately dishonest statements.

EXAMPLE 8-4

Marshall induces Betty to purchase a horse by making a statement that the horse is a stallion, when in fact it is a gelding. Betty can disaffirm the contract. Betty can return the gelding and, in a restitution action, recover the purchase price. She may also recover for food, maintenance, and veterinary care as measured by their reasonable value to Marshall.

The court will find the contract unenforceable when a deceived party can establish the following elements of fraud in the inducement:

1. The misrepresentation must be a statement of fact and must be false.
2. The party making the statement must know or believe the statement to be false and, by making the false statement of fact, must intend to influence the other party to act or refrain from acting.
3. The person to whom the statement is made must believe and rely on the statement.
4. The statement must be sufficiently material to induce the party relying on the statement to accept the offer.

PARALEGAL EXERCISE 8.2 Sylvia, of Sylvia’s A-1 Used Cars, while attempting to sell Brad a car made statements to him that a particular used car had only 40,000 miles on it. After Brad expressed concern over a lit dashboard warning light indicating faulty brakes, Sylvia further stated that the brakes had been fixed. Relying on these assurances, Brad purchased the car and later discovered that Sylvia had intentionally changed the odometer reading from its prior reading of 85,000 miles and had disconnected the warning light, making it inoperative.

Can Brad disaffirm the contract on the ground that Sylvia’s fraudulent conduct precludes enforcement of the contract?

PARALEGAL EXERCISE 8.3 Treeland, Inc., represented to Lynn that its grape vines were healthy, free of disease, and suitable for producing wine grapes. Lynn relied on these representations in deciding to purchase the vines. The vines, however, carried a latent disease that had gone undetected by either party prior to purchase. The disease devastated the grape vines soon after purchase, rendering the grape vines incapable of bearing fruit of adequate quality or quantity for Lynn's commercial wine production. Answer the following:

1. Can Lynn disaffirm the contract on the ground that Treeland's fraudulent conduct precludes enforcement of the contract?
2. Would it make any difference whether Lynn acted as a novice gardener or as the experienced owner of a winery?

DURESS AND UNDUE INFLUENCE

Duress is the use of any wrongful act or threat as a means of influencing a party to contract. Duress takes away a contracting party's "free will." Duress has two forms: duress by actual physical force and duress by threat. In **duress by actual physical force**, a person using physical force compels a party to "assent" to the "contract," even though that party did not intend to contract.

EXAMPLE 8-5

George presented a document in contract form to Clint for Clint's signature. When Clint refused to sign, George, who was physically stronger, grabbed Clint by the neck and forced him to sign his name. Clint's signature is an ineffective manifestation of assent, and no contract is formed. Clint literally was no more than a mere "mechanical instrument" at the hands of George.

Assent may be induced by someone who is not a party to the contract. The party subject to the duress may disaffirm the contract when the third party uses duress by physical force.

Duress encompasses more than physical force. In **duress by threat**, one party improperly threatens another party to assent to a contract, and the threatened party has no reasonable alternative but to assent. Duress by threat includes "economic duress." In **economic duress**, a party is wrongfully threatened with severe economic loss if the threatened party does not enter the proposed contract.

EXAMPLE 8-6

Simmons delivered a large order of merchandise to Barnes under a contract for sale. Barnes, knowing that Simmons was in urgent need of cash and was unable to borrow money, refused to pay unless Simmons reduced the contract price by half. Simmons assented to the modification. Barnes's threat amounts to duress. Simmons may disaffirm the modification.

Duress by threat has four elements:

1. There must be a threat.
2. The threat must be improper. Improper threats include threats that are either so shocking that the court will not inquire into the fairness of the resulting exchange, such as the threat of a criminal act or criminal prosecution, or threats that in themselves necessarily involve some element of unfairness, such as a breach of the duty of good faith and fair dealing under a contract (often involved with economic duress).
3. The threat must be sufficiently grave to induce the victim to assent. This requires a subjective determination of the victim's perception of the seriousness of the threat.
4. The threat must induce the victim to assent to the contract. A threat does not induce assent if the threatened party has a reasonable alternative to assenting and fails to take advantage of that alternative. Reasonable alternatives may include legal remedies or the availability of similar goods or services in the market place.

PARALEGAL EXERCISE 8.4 Reese, a general contractor, was awarded a contract by the government to extend a runway at a military air base. Reese gave Hawkins a subcontract to supply the concrete. After the foundation for the runway had been prepared, Hawkins refused to deliver the concrete unless Reese not only paid more than the contract price for the concrete but awarded Hawkins a subcontract on another job that Reese had. Reese agreed to modify the price and give Hawkins the second contract.

Could Reese disaffirm the modification of the first subcontract due to duress? In evaluating whether Reese could disaffirm, consider:

1. whether Hawkins threatened Reese;
2. whether the threat was improper;
3. whether the threat was sufficiently grave to induce Reese to assent; and
4. whether the threat induced Reese to assent to the contract (whether Reese had a reasonable alternative to assenting).

PARALEGAL EXERCISE 8.5 Jill, who had contracted to sell goods to Ben, threatened to refuse to deliver the goods to him unless he modified the contract to increase the price. Ben did not attempt to purchase the goods elsewhere, although he knew that they were available. Being in urgent need of the goods, he agreed to the modification. Jill shipped the goods.

Could Ben disaffirm the modification due to duress? In evaluating whether Ben could disaffirm, consider:

1. whether Jill threatened Ben;
2. whether the threat was improper;
3. whether the threat was sufficiently grave to induce Ben to assent; and
4. whether the threat induced Ben to assent to the contract (whether Ben had a reasonable alternative to assenting).

When a third party uses duress by threat, the victim of the duress may disaffirm the contract unless the other contracting party has begun performance in good faith and without reason to know of the duress.

Undue influence involves unfair persuasion by a party who is either in a position of dominance or in a position of trust and confidence. Undue influence differs from duress in two ways.

1. Undue influence requires neither threats nor deception, although often one or the other is present.
2. Undue influence requires a special relationship between the parties.

Undue influence often includes the following:

1. the susceptibility of the party influenced, such as the presence of mental or physical weakness;
2. the opportunity to exercise undue influence, such as a confidential relationship (including parent-child, husband-wife, attorney-client, or trustee-beneficiary); and
3. a resulting transaction that enriches the party exercising the influence at the expense of the party being influenced.

A victim of undue influence may disaffirm the contract unless a third party induces the assent and the other contracting party has begun performance in good faith and without reason to know of the undue influence.

PARALEGAL EXERCISE 8.6 Johnson, an elderly and illiterate man, lived with his nephew, Barker, and was dependent on him for support. Barker told Johnson that he would no longer support him unless Johnson sold Barker a tract of land called Greenacre. Johnson signed a contract selling Greenacre to Barker.

Could Johnson disaffirm the contract due to undue influence? In evaluating whether Johnson could disaffirm, consider:

1. whether Johnson was susceptible to Barker's influence;
2. whether Barker had the opportunity to exercise undue influence over Johnson; and
3. whether Barker was enriched at the expense of Johnson.

Could Johnson disaffirm the contract due to duress?

PARALEGAL EXERCISE 8.7 Tom, inexperienced in business, had for years relied on his local banker, Samantha, for business advice. Samantha constantly urged Tom to sell Jean, Samantha's business associate, a tract of land called Blackacre at a price well below its fair market value. Based on this advice, Tom contracted to sell Blackacre to Jean.

Could Tom disaffirm the contract due to undue influence? In evaluating whether Tom could disaffirm, consider:

1. whether Tom was susceptible to Samantha's influence;
2. whether Samantha had the opportunity to exercise undue influence on Tom; and
3. whether Samantha was enriched at the expense of Tom.

Could Tom disaffirm the contract due to duress?

MISTAKE IN A BASIC ASSUMPTION OF FACT

A **mistake in a basic assumption of fact** involves a situation where the contracting parties believe they were bargaining for something different from what they actually did contract for. Typically, these mistakes involve the existence or identity of the subject matter of the contract.

A mistake in a basic assumption of fact problem can be identified by considering five questions: what did the contract say; what did the offeror perceive the contract to mean at the time of contract formation; what did the offeree perceive the contract to mean at the time of contract formation; what would the reasonable person have perceived the contract to mean at the time of contract formation; and what were the true facts. If the issue is mistake in a basic assumption of fact, the offeror, offeree, and reasonable person will all perceive the contract to mean the same thing at the time of contract formation. Their perceptions will coincide. Their perceptions at the time of contract formation, however, will not coincide with the true facts.

EXAMPLE 8-7

In the famous case of *Sherwood v. Walker*, 66 Mich. 568, 33 N.W. 919 (1887), the mistake involved the sale of Rose 2d of Aberlone. At the time of contract formation both Walker, the seller, and Sherwood, the buyer, believed that Rose was a sterile cow. Therefore, Rose was sold at a sterile cow price. After the contract but before delivery, Walker discovered that Rose was with calf and worth about ten times the contract price. Walker, therefore, refused to deliver Rose claiming a mistake in a basic assumption of fact.

The following charts the facts in *Sherwood v. Walker*.

The contract term	Rose, a sterile cow
At the time of contracting, the seller perceived the contract to be for—	Rose, a sterile cow
At the time of contracting, the buyer perceived, the contract to be for—	Rose, a sterile cow
At the time of contracting, the reasonable person would have perceived the contract to be for—	Rose, a sterile cow
The subject of the contract ultimately turned out to be	Rose, a pregnant cow

The comments to the Restatement (Second) of Contracts suggest three requirements a party must meet before disaffirming a contract for a mistake in a basic assumption of fact.

1. The mistake must relate to a “basic assumption on which the contract was made,” such as the existence or identity of the subject matter.
2. The party seeking to disaffirm must show how the mistake had a material effect on the agreed exchange of performances.
3. The mistake must not involve a risk that the party seeking relief has agreed to bear (as provided in the contract or by implication arising from the party’s greater expertise).

EXAMPLE 8-8

In *Sherwood v. Walker*, the mistake (whether Rose was sterile or able to conceive) involved the very nature of the thing for which he bargained, the subject matter of the contract. The mistake had a material effect on the agreed exchange of performances because Rose with calf was worth about ten times the contract price. Although Walker assumed the risk of undervaluing Rose, the sterile cow, he did not assume the risk of undervaluing Rose, the cow with calf. Therefore, the court permitted Walker, the seller, to disaffirm the contract.

PARALEGAL EXERCISE 8.8 Kitty contracted to sell Northridge Lumber Company a tract of timberland. The high contract price reflected the quantity and quality of the standing timber. At the time of contracting, both parties believed the timber was standing. Unknown to the parties, the timber had recently been destroyed by fire.

Answer the following:

1. Did a mistake as to a basic assumption of fact exist when the parties contracted?
2. Could Northridge show that the mistake had a material effect on the agreed exchange of performances?
3. Did Northridge agree to bear the risk?
4. Could Northridge disaffirm the contract by claiming a mistake in a basic assumption of fact?

Generally, courts allow disaffirmance of only those contracts in which the mistake involves the “identity” or “existence” of the subject matter, rather than mere “quality” or “value.”

EXAMPLE 8-9

Costello sold Sykes ten shares of stock for \$316 a share. In fact, employees of the corporation had altered the corporation’s books, and the actual value of the stock was \$60 a share, rather than \$316 a share. Sykes could not successfully sue Costello for breach of contract to recover the contract price based on a mistake in a basic assumption of fact. The mistake relates to “attributes, quality, or value” and not to the “existence or identity” of the stocks sold.

Attorneys who have worked in this area know that this distinction is not always clear, and the application of the law to a set of facts is often difficult.

PARALEGAL EXERCISE 8.9 Wood found a pretty stone and offered to sell it to Boynton. The parties expressed their ignorance as to the nature of the stone and guessed it to be a topaz. Wood sold the stone to Boynton for one dollar. Later the stone was identified as an uncut diamond worth \$1,000. Could Wood rescind the contract due to a mistake in a basic assumption of fact?

Answer the following:

1. Did the mistake relate to a basic assumption on which the contract was made?
2. Could Wood show that the mistake had a material effect on the agreed exchange of performances?

3. What risks did Wood agree to bear in entering into the contract with Boynton?
4. Would it be surprising to learn that the court in *Wood v. Boynton*, 64 Wis. 265, 25 N.W. 42 (1885), held that Wood could not disaffirm?

The only reasons we know of for rescinding a sale and revesting the title in the vendor so that he may maintain an action at law for the recovery of the possession against his vendee are (1) that the vendee was guilty of some fraud in procuring a sale to be made to him; (2) that there was a mistake made by the vendor in delivering an article which was not the article sold,—a mistake in fact as to the identity of the thing sold with the thing delivered upon the sale. . . . There is no pretense of any mistake as to the identity of the thing sold. It was produced by the plaintiff and exhibited to the vendee before the sale was made, and the thing sold was delivered to the vendee when the purchase price was paid. *Kennedy v. Panama, etc., Mail Co.*, supra., 587; *Street v. Blay*, 2 Barn. & Adol. 456; *Gompertz v. Bartlett*, 2 El. & Bl. 849; *Gurney v. Womersley*, 4 El. & Bl. 133; *Ship's Case*, 2 De G. J. & S. 544. Suppose the appellant had produced the stone, and said she had been told it was a diamond, and she believed it was, but had no knowledge herself as to its character or value, and Mr. Boynton had given her \$500 for it. Could he have rescinded the sale if it had turned out to be a topaz or any other stone of very small value? Could Mr. Boynton have rescinded the sale on the ground of mistake? Clearly not, nor could he rescind it on the ground that there had been a breach of warranty, because there was no warranty, nor could he rescind it on the ground of fraud, unless he could show that she falsely declared that she had been told it was a diamond, or, if she had been so told, still she knew it was not a diamond. See *Street v. Blay*, supra.

The following cases show that, in the absence of fraud or warranty, the value of the property sold, as compared with the price paid, is no ground for a rescission of a sale. *Wheat v. Cross*, 31 Md. 99; *Lambert v. Heath*, 15 Mees. & W. 487; *Bryant v. Pember*, 45 Vt. 487; *Kuelkamp v. Hidding*, 31 Wis. 503–511. However unfortunate the plaintiff may have been in selling this valuable stone for a mere nominal sum, she has failed entirely to make out a case either of fraud or mistake in the sale such as will entitle her to a rescission of such sale so as to recover the property sold in an action at law.

5. Can the result in *Wood* be reconciled with the illustration given about Rose 2d of Aberlone?



PARALEGAL CHECKLIST

Unenforceable Contracts—Protecting a Party against Overreaching

- The fact that a contract has been formed does not necessarily lead to the conclusion that it can be enforced in court by a nonbreaching party. The paralegal and the supervising attorney must evaluate

whether one of the parties has the power to disaffirm the contract making it unenforceable. The supervising attorney will, of course, always make the final determination in all such matters and will advise the client. The previous chapter dealt with the first category of enforcement problems—protecting a

class. This chapter deals with the second category—protecting a party against another party’s overreaching. If at the time of contract formation, one of the parties took unconscionable advantage of the other party, procured a contract through fraud or duress, or entered a contract where there was a mistake in a basic assumption of fact, enforcement of the contract may be precluded.

1. Was one party’s will imposed upon an unwilling, or even unwitting, party during contract formation? If so, the contract is a “contract of adhesion.” A contract of adhesion may be standardized or nonstandardized. Not all contracts of adhesion are unenforceable. A contract of adhesion may be unconscionable and unenforceable in its entirety or in one term only.
 - a. Ascertain unconscionability by finding out whether superior bargaining power was used to force unreasonably favorable terms on a party (i.e., absence of meaningful choice on the part of one of the parties together with contract terms that are unreasonably favorable to the other party).
 - (1) Check for the two components of absence of meaningful choice:
 - (a) the imbalance in bargaining power; and
 - (b) knowledge of the terms (e.g., terms hidden in a maze of fine print or minimized by deceptive sales practices).
 - (2) Analyze whether the contract term unreasonably favors the other party. The term must be considered in light of the circumstances existing when the contract was made. The general commercial background and the commercial needs of the particular trade or case shed light on reasonableness.
 - b. Consider whether the court might permit unconscionability as support for an action for breach of contract. While courts may permit a party to bring an action using unconscionability as the mechanism for reformation of the contract (so the plaintiff owes no more), some courts are reluctant to permit a party to actually recover for unconscionability as a cause of action.
2. How are the terms “fraud” and “misrepresentation” distinguishable? An assertion does not have to be fraudulent to be a misrepresentation.
 - a. Determine whether there was an assertion that is not in accordance with the facts. A statement intended as truthful may be a misrepresentation if made in ignorance or carelessness.
 - b. Evaluate whether the misrepresentation was fraudulent. A fraudulent misrepresentation may be either:
 - (1) fraud in the factum (fraud in the essence); or
 - (2) fraud in the inducement.
 - c. Find out if a party fraudulently induced another to enter into the transaction. If it did, the deceived party may disaffirm the contract and, in those cases where the defrauded party has conferred a benefit on the defrauding party, claim restitution. The elements of fraud are:
 - (1) the misrepresentation must be a statement of fact and must be false;
 - (2) the party making the statement must know or believe the statement to be false and, by making the false statement of fact, must intend to influence the other party to act or refrain from acting;
 - (3) the person to whom the statement is made must believe and rely on the statement; and
 - (4) the statement must be sufficiently material to induce the party relying on the statement to accept the offer.
3. Was there duress? Duress is the use of any wrongful act or threat as a means of influencing a party to contract. Duress takes away a contracting party’s “free will.” Duress has two forms:
 - (1) duress by actual physical force; and (2) duress by threat.
 - a. Find out if there was duress by actual physical force. Did a person using physical force compel a party to “assent” to the “contract,” even though that party did not intend to contract? If assent was induced by a third party, the party subject to the duress may disaffirm the contract.

- b. Determine if there was duress by threat.
Duress by threat (including economic duress) has four elements:
- (1) a threat;
 - (2) the threat must be improper;
 - (3) the threat must be sufficiently grave to induce the victim to assent; and
 - (4) the threat must induce the victim to assent to the contract.
- When a third party uses duress by threat, the party subject to the duress cannot disaffirm the contract if the other contracting party begins performance in good faith and without reason to know of the duress.
4. Was undue influence exerted by one of the parties? Undue influence differs from duress in two ways.
- a. Undue influence requires neither threats nor deception, although one or the other is often present.
 - b. Undue influence requires a special relationship between the parties.
5. Was there a mistake in a basic assumption of fact during contract formation? Courts allow

contracting parties adversely affected by a mistake in a basic assumption of fact to disaffirm the contract. This form of mistake pertains to a situation in which the parties believed they were bargaining for something different from the thing for which they actually contracted. Typically, these mistakes concern the existence or identity of the subject matter of the contract.

The following conditions must be met affirmatively for a party to disaffirm a contract for a mistake in a basic assumption of fact:

- a. Determine if the mistake relates to a “basic assumption on which the contract was made.”
 - b. Find out if the party seeking to disaffirm can show how the mistake had a material effect on the agreed exchange of performances.
 - c. Determine whether the mistake involves something other than a risk that the party seeking relief has agreed to bear.
- Each party bears the risk of a bad bargain that results from failure to investigate the value of the subject matter.

REVIEW QUESTIONS

DEFINE THE FOLLOWING NEW TERMS AND PHRASES

Adhesion contract

Duress

Duress by actual physical force

Duress by threat

Economic duress

Fraud in the factum

Fraud in the inducement

Misrepresentation

Mistake in a basic assumption of fact

Unconscionability

Undue influence

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

1. T F When a court or legislature protects a class, this protection extends to all members of that class.
2. T F A contracting party who is not in a protected class may still be protected from the overreaching of another party.
3. T F The terms of a “contract of adhesion” will be enforced because there was a manifestation of assent.

4. T F The “imposition of will” by one party upon another party during contract formation will result in a “contract of adhesion.”
5. T F The terms of an “adhesion contract” will not be enforced because of the “imposition of will” by one party upon another party during contract formation.
6. T F An adhesion contract may be a nonstandardized contract or a standardized contract.
7. T F All adhesion contracts are unconscionable.
8. T F To determine whether a contract or a contract term is unconscionable, evaluate it as of the time of the allegation of unconscionability.
9. T F Unconscionability has been defined by the UCC as an absence of meaningful choice on the part of one of the parties together with contract terms that are unreasonably favorable to the other party.
10. T F Absence of meaningful choice has two components:
(1) the imbalance in bargaining power; and
(2) lack of knowledge of the terms.
11. T F A gross inequality of bargaining power will not lead to the conclusion of absence of meaningful choice if the other party had knowledge of the terms.
12. T F A party could lack knowledge of the terms of a contract if the contract is written in English and the buyer can read only Spanish.
13. T F A contract is unconscionable if one party lacked meaningful choice and the other party had no knowledge of that fact.
14. T F Determining whether a contract term is reasonable or fair will be done without considering the circumstances at the time the contract was made.
15. T F If a case involves a sale of goods, the court must consider whether or not UCC § 2–302 applies when the issue of unconscionability arises.
16. T F UCC § 2–302 is never used by courts in nonsale-of-goods transactions.
17. T F Unconscionability is a question for the jury.
18. T F Under section 2–302(2) of the UCC, the court may, of its own accord, raise the issue of unconscionability.
19. T F Unconscionability may be used both as a defense to a breach of contract action and as an action for breach of contract.
20. T F Fraud and misrepresentation are interchangeable terms.
21. T F An assertion must be fraudulent to be a misrepresentation.
22. T F A misrepresentation is “an assertion that is not in accord with the facts.”
23. T F A statement a speaker intends as truthful may be a misrepresentation due to ignorance or carelessness.
24. T F A statement a speaker intends as truthful but which is a misrepresentation due to ignorance or carelessness is still fraud.
25. T F A fraudulent misrepresentation may be either fraud in the “factum” or fraud in the “essence.”

26. T F Fraud in the “factum” occurs when one party tricks the other into signing a promissory note that the other believes is merely a receipt.
27. T F A typical case of fraud in the “inducement” involves a seller’s misrepresentation of the quality of the goods.
28. T F A party who has relied on a misrepresentation made because of ignorance or carelessness may not disaffirm the contract.
29. T F The power to disaffirm a contract protects innocent parties from misrepresentations that are either careless or fraudulent.
30. T F Duress encompasses more than physical force.
31. T F Duress by threat has two elements:
(1) there must be a threat; and
(2) the threat must be sufficiently grave to induce the victim to assent.
32. T F Duress by threat includes “economic duress.”
33. T F Duress does not take away a contracting party’s “free will.”
34. T F Undue influence is the same thing as duress.
35. T F Undue influence requires a special relationship between the parties.
36. T F Undue influence requires threats and deception.
37. T F Undue influence involves unfair persuasion by a party who is in either a position of dominance or a position of trust and confidence.
38. T F A contracting party who has been adversely affected by a mistake in a basic assumption of fact may disaffirm the contract.
39. T F A contracting party may disaffirm a contract in which the mistake in a basic assumption of fact involves “quality” or “value.”
40. T F A contracting party may not disaffirm a contract in which the mistake in a basic assumption of fact involves the “identity” or “existence” of the subject matter.

FILL-IN-THE-BLANK QUESTIONS

- _____. A contract formed by one party imposing his or her will upon an unwilling, or even unwitting, party.
- _____. Occurs when contract negotiations are not between equals, when there is no opportunity to bargain over the terms, or when one party is unfamiliar with the terms.
- _____. The imposition by one party of an unreasonably favorable contract or term on the other party who lacked a meaningful choice.
- _____. The determiner of unconscionability.
- _____. The UCC section that pertains to unconscionability.
- _____. An assertion that is not in accord with the facts.

7. _____. A misrepresentation that is a statement of fact known or believed to be false by the party making the statement with the intent of influencing the other party, who believes and relies on the statement, to act or refrain from acting, and the statement is sufficiently material to induce the relying party to accept the offer.
8. _____. A fraudulent misrepresentation that involves the very character of the proposed contract.
9. _____. A fraudulent misrepresentation that typically involves the quality of the goods.
10. _____. Protects contracting parties from deliberately dishonest statements.
11. _____. The use of any wrongful act or threat as a means of influencing a party to contract.
12. _____. Wrongfully threatening a party with severe economic loss if the threatened party does not enter the proposed contract.
13. _____. Unfair persuasion by a party who is in either a position of dominance or a position of trust and confidence.
14. _____. A mistake that involves a situation where both parties believed they were bargaining for something different from the thing for which they actually contracted.

MULTIPLE CHOICE QUESTIONS (CIRCLE ALL THE CORRECT ANSWERS)

1. The definition of unconscionable is found in:
 - (a) Article 1 of the UCC
 - (b) Article 2 of the UCC
 - (c) case law
 - (d) both Article 2 of the UCC and case law
 - (e) Article 2A of the UCC
2. Unconscionability is defined as:
 - (a) absence of meaningful choice on the part of one of the parties
 - (b) gross inequality of bargaining power
 - (c) unreasonably favorable terms
 - (d) deceptive sales practices
 - (e) absence of meaningful choice on the part of one of the parties coupled with unreasonably favorable terms on the part of the other

3. Under UCC § 2–302, the court may:
 - (a) refuse to enforce the contract
 - (b) delete the unconscionable term and enforce the remaining terms of the contract
 - (c) reform the unconscionable term so it no longer produces an unconscionable result
 - (d) ask the jury to decide whether the contract was unconscionable
 - (e) award damages
4. The elements of fraud that must be established for a court to find a contract unenforceable are:
 - (a) the misrepresentation must be a statement of fact
 - (b) the statement must be false
 - (c) the party making the statement must know or believe the statement to be false and, by making the statement, must intend to influence the other party to act or refrain from acting
 - (d) the person to whom the statement is made must believe and rely on the statement
 - (e) the statement must be sufficiently material to induce the party relying on the statement to accept the offer
5. Undue influence differs from duress in that:
 - (a) undue influence requires neither threats nor deception
 - (b) undue influence requires deception but not threats
 - (c) undue influence requires threats and deception
 - (d) undue influence requires a special relationship between the parties
 - (e) undue influence requires the party influenced to be susceptible (i.e., the presence of either a mental or physical weakness)
6. Travers contracted to sell “Come from Behind,” a racehorse, to Bishop. At the time of contracting, both parties believed “Come from Behind” to be alive and well. Unknown to the parties, “Come from Behind” had recently been severely injured by a careless groom. Bishop could disaffirm the contract under the following theory:
 - (a) unconscionability
 - (b) fraud in the factum
 - (c) fraud in the inducement
 - (d) undue influence
 - (e) mistake in a basic assumption of fact
7. At birth, Simon suffered a brain injury which resulted in an IQ of 79. He lived with his brother, Larry, on the family farm that had been left to Simon by his parents. Larry told Simon that he would have to move to a group home if he did not sell the farm to Larry. Simon signed the documents conveying the farm to Larry. Simon could disaffirm the contract under the following theory:
 - (a) unconscionability
 - (b) fraud in the factum

- (c) fraud in the inducement
- (d) undue influence
- (e) mistake in a basic assumption of fact

SHORT ANSWER QUESTIONS

1. Unconscionability is defined as an absence of meaningful choice on the part of one party coupled with unreasonably favorable terms on the part of the other. Discuss what constitutes absence of meaningful choice.
2. State the four elements of duress by threat.



Contract Enforceability: Protecting the Judicial Process

- ◆ Statute of Frauds

- Contracts that Require a Writing and What Constitutes the Writing*
 - Circumventing the Statute of Frauds through Reliance*
 - Restitution as a Cause of Action*

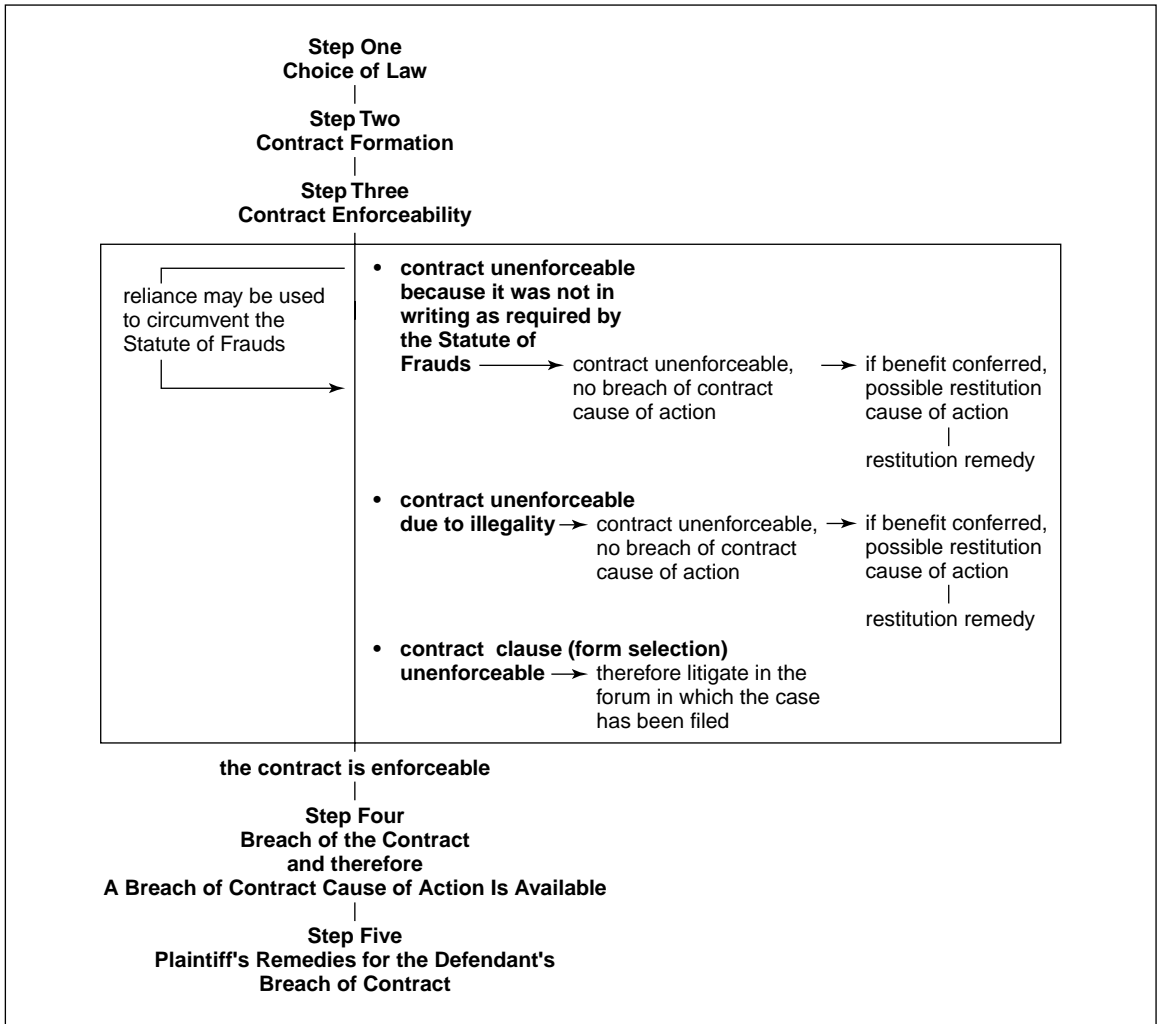
- ◆ Illegality

- Illegality as a Defense to a Breach of Contract Action*
 - Restitution as a Cause of Action*

- ◆ Forum Selection Provisions

Chapter 9, the third of three chapters dealing with contract enforceability, discusses protecting the judicial process. Rather than protecting a class (Chapter 7) or protecting a party from overreaching (Chapter 8), a legislature or court may protect the judicial process by not permitting disputants to use the courts to promote nonjudicial activity such as perjury, illegality, and inappropriate forum shopping (see Figure 9–1).

FIGURE 9-1 The Contract Enforceability (Protecting the Judicial Process) Phase of the Road Map



STATUTE OF FRAUDS

A common misconception is that a contract does not exist without a writing. Whether a contract is in writing has nothing to do with the formation of the contract (offer and acceptance) unless the offeror has mandated a writing as the method of acceptance.

Although as a general rule a writing is not required for contract formation, written evidence of the contract may be required for the enforcement of the contract.

EXAMPLE 9-1

Bradley Briggs offered to sell his comic book collection to Kathy Crawford for \$200. Bradley's offer also stated that Kathy must accept by registered mail within one week. Bradley has provided a mandatory method of acceptance—registered mail. Therefore, Kathy's written acceptance, sent by registered mail, is the acceptance.

In 1677, the British Parliament enacted a Statute of Frauds that required certain types of contracts to be in writing to be enforceable. The purpose of the statute was twofold: cautionary and evidentiary. The necessity of the writing cautioned the parties that this transaction was important and that they should pay attention to what they were doing. This was not a casual transaction without legal significance. The writing also was evidentiary. The terms in the writing were the terms the parties had to follow, even though their memories grew dim. Certainly the opportunity for perjury was reduced by the writing.

In the United States, each state legislature enacted its own Statute of Frauds. Although variations exist from state to state, most are similar. A typical Statute of Frauds may provide:

Promises or Agreements Not Binding Unless in Writing

No action shall be brought upon any of the following agreements or promises, unless the agreement or promise, upon which such action shall be brought or some memorandum or note thereof, shall be in writing, and signed by the party to be charged therewith, or by some other person thereunto by him lawfully authorized:

- a. A special promise of an executor or administrator to answer damages out of his own estate;
- b. A special promise to answer for the debt, default or mischarge of another person;
- c. An agreement made upon consideration of marriage;
- d. A contract for the sale of real estate, or any interest in or concerning the same; or
- e. An agreement that is not to be performed within one year from the making thereof.

While this Statute of Frauds provides a number of types of contracts that must be in writing to be enforceable, the list is incomplete. The Statute of Frauds dealing with the sale of goods is not found in the general Statute of Frauds but is in Article 2 of the Uniform Commercial Code. Other Statutes of Frauds may be scattered through a state's statutes.

In 1954, the British Parliament repealed all of its Statute of Frauds except promises to answer for the debt of another and contracts for the sale of land. American legislatures, however, have been reluctant to follow suit.

This section discusses three types of contracts that must be in writing to be enforceable:

- the contract that cannot be fully performed within one year
- the contract for the transfer of an interest in real property
- the contract for the sale of goods for the price of \$500 or more

Contracts That Require a Writing and What Constitutes the Writing

Although not all types of contracts must be in writing to be enforceable, many contracts are written, even though written evidence of the contract was not required for enforcement. A writing, even though not required, solves a number of problems. The act of writing a contract requires the parties to think about the terms that are to be a part of the writing. Therefore, a written contract may be more definite and refined than an oral contract, providing the parties document their promises.

If state statutes require a contract be in writing to be enforceable, what must the writing contain? The answer is found in the particular Statute of Frauds that requires the writing. Because the Statute of Frauds that requires a writing for the contract for sale of goods for the price of \$500 or more is not the same as the Statute of Frauds that requires a writing for a contract that cannot be fully performed within a year, the writing requirements are different.

Contract Not to Be Performed within One Year A contract that could be fully performed in less than a year from the time of contract formation need not be in writing to be enforceable. The one-year period runs from the time of contract formation and not from the time when performance begins.

EXAMPLE 9-2

A contract for a one-day concert recital that will take place fourteen months after the date of contracting is within the Statute of Frauds and must be in writing to be enforceable. The fact that the performance will only take one day is irrelevant because the critical time period is between the date of contract formation and the date of full performance. That period is fourteen months.

The probability that the contract will be fully performed within the year is irrelevant. What is necessary to bring a contract within the requirements of the Statute of Frauds (requiring a writing) is the lack of any possibility (no matter how slight) that performance will be completed within a year. Whether the contract could or could not be fully performed within a year is not made with 20/20 hindsight. The determination whether the contract could not be fully performed within one year is not made after the parties have performed but as of the date of contract formation.

PARALEGAL EXERCISE 9.1 The Airport Authority hired the All-Star Construction Company to build a new terminal. Although the normal construction time for such a project was eighteen months, All-Star finished the terminal eleven months from the date of contract.

Was this contract under the Statute of Frauds so a writing was required? Is either the normal construction time or the actual construction time relevant in this determination? At the time of contract formation, was there a possibility that performance could be completed within one year from the date of contract formation?

The Statute of Frauds requires a lack of any possibility of full performance of the contract within one year from the date of contract formation for written evidence of the contract to be necessary. A duty extinguished by full performance is distinguishable from a duty terminated prior to full performance. If a duty to perform is terminated, the duty has not been fully performed. Whether a duty to perform could be terminated within a year of contract formation is irrelevant when determining whether the contract must be evidenced by a writing to be enforceable.

EXAMPLE 9-3

Pauline Primrose, an actress, contracted to work exclusively for Universal Studios for five years. The contract provided that Universal could waive its rights before one year. Viewing the contract from the time of contract formation, it is possible that Pauline could die within one year, at which time her contract duties would terminate. She would not have fully performed. It is also possible that Universal could waive its rights within one year, at which time Universal's contract duties would be fully performed. Since Universal could fully perform within a year, the contract need not be evidenced by a writing to be enforceable by either party.

PARALEGAL EXERCISE 9.2 Atlas McBee contracts to play football for the Takoma Sasquatch, a professional football team.

1. If the contract is "for five years," must the contract be evidenced by writing to be enforceable?
2. If the contract is "for as long as McBee can play football," must the contract be evidenced by a writing to be enforceable?
3. If the contract is "for five years, but if McBee is injured, the contract is terminated," must this contract be evidenced by a writing to be enforceable?

PARALEGAL EXERCISE 9.3 Williams, an account executive, entered into a three-year employment contract with the High Profile Advertising Agency. After working for High Profile for six months, Williams was killed in a commercial airplane accident. The employment contract provided that the heirs of any employee would receive \$100,000 upon the death of the employee.

Must this contract be in writing to be enforceable?

What must be in the writing to satisfy the Statute of Frauds? The writing must state all the essential terms with reasonable certainty, and the party against whom the contract will be enforced must sign it.

PARALEGAL EXERCISE 9.4 Anna Aldrich, a realtor, was hired by Metro Realty to sell realty for Metro for two years at \$2,000 a month plus commissions. The writing was rather sketchy. While it stated the term, it did not state the salary. The writing was signed by both Aldrich and Metro. In six months, Aldrich is wrongfully (without cause) discharged. If Aldrich sues Metro for breach of contract, could Metro successfully assert that the contract was unenforceable under the Statute of Frauds?

PARALEGAL EXERCISE 9.5 Ava, a top model, contracts to pose for a high fashion magazine for two years at \$10,000 a month. The contract was reduced to writing, but only Ava signed it. After six months, Ava is discharged without cause. Ava brings a breach of contract action against the magazine.

Could the magazine successfully claim that the contract was unenforceable under the Statute of Frauds?

PARALEGAL EXERCISE 9.6 Based on the facts of Paralegal Exercise 9.5, draft a document that would satisfy the Statute of Frauds if Ava were to bring a breach of contract action against the magazine.

Contract for the Transfer of an Interest in Real Property In addition to the contract for the sale of land, the Statute of Frauds also covers the transfer of a lesser interest in real property. Therefore, to be enforceable, a lease, easement, or mortgage would be within the requirements of the statute and must be evidenced by a writing.

A number of states recognize a “part performance” exception to this category of the Statute of Frauds. If the buyer pays the seller and takes possession

of the realty or makes a valuable improvement on the realty with the consent of the seller, a writing is not required. The unequivocal acts of the buyer, in reliance on the seller's promise, leave little doubt that a contract for the sale of the interest in the land has been made. If other remedies are inadequate, it would be unjust to permit the seller to now claim that the contract was unenforceable because it was not in writing.

In *Elizondo v. Gomez*, Elizondo sought to enforce an oral agreement for the sale of real estate. In reading *Elizondo*, consider the following questions:

1. Was there a contract between Elizondo and Gomez?
2. Is written evidence of the contract needed for it to be enforceable?
3. Was the writing adequate to satisfy the writing requirement of the Statute of Frauds?
4. Could the contract be enforceable without any written evidence of the contract and, if so, why?



CASE

Elizondo v. Gomez

Court of Appeals of Texas, 1997.

957 S.W.2d 862.

Before RICKHOFF, LOPEZ and ANGELINI, JJ.
LOPEZ, Justice.

This appeal resulted from appellant's suit raising causes of action . . . for breach of contract. At trial, appellant sought damages and specific performance. Appellant sought to enforce an alleged oral agreement for the sale of real estate based on a "quasi-deed" and partial performance. The trial court found that the statute of frauds barred appellant's claims and ordered appellee to reimburse appellant for the amount of a down payment paid by appellant. . . . We reverse the judgment of the trial court, render in part and remand in part.

FACTS

Appellee, Aida Gomez, holds the deed to property described as three adjacent lots with addresses of 1206 Crystal, 1105 Ferndale, and 1105.5 Ferndale. This property consists of a non-business residence, a retail store, and an adjacent rear apartment, respectively. Appellant, Jesse Elizondo, contends that appellee orally agreed to sell the property for seventy-nine thousand dollars with a five thousand dollar down payment. In support of the oral contract, appellant offered a receipt for the alleged five thousand dollar down payment. The receipt, written on a restaurant "guest check" reads as follows:

I Jesse Elizondo have paid Mr. & Mrs. Leo Gomez \$5000.00 for the Real Estate property located on 1105 Ferndale city of San Antonio, Tex.

The written note contained the alleged signature of Mrs. Leo Gomez.

Appellant never received a deed for the property. At the subsequent trial for specific performance, appellant argued that the "guest check" receipt constitutes a quasi-deed establishing his right to the property as a matter of law. The trial court found the oral contract unenforceable and denied appellant's claims because the oral agreement violates the statute

of frauds. However, the trial court ordered appellee to refund the amount of the alleged down payment to appellant.

STATUTE OF FRAUDS

In points of error one through six, appellant argues that the trial court erred in determining that the statute of frauds barred enforcement of appellant's alleged oral agreement for the sale of real estate. The statute of frauds reads in pertinent part that a contract for the sale of real estate "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." Tex. Bus. & Com.Code Ann. § 26.01 (Vernon's 1987). In addition, the writing must adequately describe the property, and the written description must give an amount of information to identify the property with reasonable certainty. *Jones v. Kelley*, 614 S.W.2d 95, 99 (Tex.1981); *Hebisen v. Nassau Development Co.*, 754 S.W.2d 345, 351 (Tex.App.—Houston [14th Dist.] 1988, writ denied). Parol evidence may be used to explain or clarify the written agreement, but not to supply the essential terms. *Texas Builders v. Keller*, 928 S.W.2d 479, 481–82 (Tex.1996); *Morrow v. Shotwell*, 477 S.W.2d 538, 541 (Tex. 1972).

Appellant argues that the "guest-check" receipt of an alleged five thousand dollar down payment satisfies the statute of frauds. We disagree. The property in question consists of three parcels of land. Even though the parcels are adjacent to one another, each lot has a separate address; 1105 Ferndale; 1105.5 Ferndale; and 1206 Crystal. The "guest-check" merely identifies the "property located at 1105 Ferndale." Even a most liberal interpretation of the writing, without more, falls short of properly identifying all three lots in question. Therefore, on this basis alone, the writing fails to satisfy the identification requirement of the statute of frauds. Furthermore, the writing fails to properly recite the purchase price of the property. Even if we give the writing full effect, it merely illustrates five thousand dollars of consideration as a down payment. The writing fails to state the full amount of consideration given for the property. Thus, we find the trial court properly found that the writing fails to satisfy the statute of frauds. However, the equitable doctrine of partial performance serves as an exception to the statute of frauds. *Leon Ltd. V. Albuquerque Commons Partnership*, 862 S.W.2d 693, 702 (Tex.App.—El Paso 1993, no writ); *Wiley v. Bertelsen*, 770 S.W.2d 878, 882 (Tex.App.—Texarkana 1989, no writ).

In Texas, we may remove an oral contract for the sale of real estate from the statute of frauds when the promisee performs the contract to such a degree that application of the statute would defeat its true purpose. *Penwell v. Barrett*, 724 S.W.2d 902, 904 (Tex.App.—San Antonio 1987, no writ). The leading case of *Hooks v. Bridgewater*, 111 Tex. 122, 229 S.W. 1114, 1116 (1921), establishes the three elements required for exemption from the statute of frauds: (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. Each of the three elements is indispensable. *Penwell*, 724 S.W.2d at 904. The alleged oral agreement must unequivocally refer to the agreement and corroborate the fact that a contract actually was made. *Chevalier v. Lane's, Inc.*, 147 Tex. 106, 213 S.W.2d 530, 533–34 (1948). In essence, the performance must supply the key to what was promised. *Wiley*, 770 S.W.2d at 882.

In the case at bar, the record reveals that in December of 1994, both parties entered into an agreement for the sale of the land in question. The parties agreed to a purchase price of seventy-nine thousand dollars with a five thousand dollar down payment and monthly

mortgage payments of seven hundred and ninety five dollars per month for fifteen years at ten percent interest. On December 24, 1994, appellee delivered the keys to the property to appellant and appellant took possession of all three lots.

In accordance with the terms of the oral agreement, appellant made the agreed monthly payments for April, May, and June. Appellee accepted each payment and made multiple promises to transfer a proper deed. Appellant ceased making the mortgage payments only after appellee interfered with appellant's enjoyment of the property. Appellee misrepresented to the tenants of the property that appellant did not have legal right to the property.

When one party fully performs a contract, the statute of frauds is unavailable to the other who knowingly accepts the benefits and partly performs. *Enochs v. Brown*, 872 S.W.2d 312, 319 (Tex.App.—Austin 1994, no writ); *Estate of Kaiser v. Gifford*, 692 S.W.2d 525, 526 (Tex. App.—Houston [1st Dist.] 1985, writ ref'd n.r.e.) (oral installment agreement, payable in 300 monthly installments not barred by statute of frauds because deceased lender made full performance). We find that the facts of the present case fall within the equitable doctrine of partial performance making the oral contract enforceable. Therefore, we affirm appellant's points of error in that the trial court erred in denying appellant's claims based on the application of the statute of frauds.

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For the reasons recited herein, we reverse the judgment of the trial court, render judgment in favor of appellant, Jesse Elizondo, and remand the case for the determination of damages in accordance with this opinion.

Contract for the Sale of Goods for the Price of \$500 or More Section 2–201(1) of the Uniform Commercial Code mandates:

(1) Except as otherwise provided in this section 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. A writing is not insufficient because it omits or incorrectly states a term agreed upon but the contract is not enforceable under this paragraph beyond the quantity of goods shown in such writing.

To come within the requirements of this Statute of Frauds, there must be a contract for the sale of goods for the price of \$500 or more. Therefore, the following are not within this Statute of Frauds:

- a transaction for the lease of goods (because it is not a *sale* of goods)
- a transaction for the sale of services (because it is not a sale of *goods*)
- a transaction for the sale of goods for the price of \$499.99 (because it is not for the price of \$500.00 or more)

PARALEGAL EXERCISE 9.7 Julius orally contracted with the Overhead Door Company for the purchase and installation of overhead doors for his garage. The contract price was \$510 less 5 percent if paid by cash or check upon completion of

the installation. Prior to commencing work, Julius telephoned the Overhead Door Company and canceled the order. Overhead Door brought an action for breach of contract against Julius.

Could Julius claim that the contract was unenforceable under UCC § 2-201(1)?

After determining that the contract is for a sale of goods for a price of \$500 or more and therefore must be in writing under UCC § 2-201(1), what must the writing contain? Section 2-201(1) states only three requirements:

1. the writing must evidence a contract for the sale of goods;
2. the party against whom enforcement is sought must sign it; and
3. the writing must specify a quantity, even though the quantity is inaccurate. Recovery, however, is limited to the amount stated.

Other terms, although essential to the contract, such as price, time and place of payment or delivery, and warranty, need not be stated in the writing.

PARALEGAL EXERCISE 9.8 Mom & Pop's Hamburger Haven placed an oral order for 5,000 six ounce hamburger patties with the delivery person from Quality Meats, Inc. The delivery person completed the purchase order form and gave Mom & Pop's a copy. Mom & Pop's canceled the order before it was delivered.

Could Quality Meats successfully sue Mom & Pop's for breach of contract? Consider whether Mom & Pop's could successfully claim that the contract was unenforceable due to UCC § 2-201(1). What additional facts do you need to determine whether the contract was within the statute? If the contract was within the statute, what additional facts do you need to determine whether the order form would satisfy the writing required by section 2-201(1)?

PARALEGAL EXERCISE 9.9 Based on the facts in Paralegal Exercise 9.8, draft a document that would satisfy UCC § 2-201(1) if Quality Meats were to sue Mom & Pop's for breach of contract.

Section 2-201(1) begins with the phrase "Except as otherwise provided in this section." This means that if a contract must be in writing because it is a contract for the sale of goods for the price of \$500 or more, it may still be enforceable even though it does not satisfy the memorandum requirements of subsection (1). These exceptions are found in subsections (2) and (3) of 2-201:

(2) Between merchants if within a reasonable time a writing in confirmation of the contract and sufficient against the sender is received and the party receiving it

has reason to know its contents, it satisfies the requirements of subsection (1) against such party unless written notice of objection to its contents is given within 10 days after it is received.

(3) A contract which does not satisfy the requirements of subsection (1) but which is valid in other respects is enforceable

(a) if the goods are to be specially manufactured for the buyer and are not suitable for sale to others in the ordinary course of the seller's business and the seller, before notice of repudiation is received and under circumstances which reasonably indicate that the goods are for the buyer, has made either a substantial beginning of their manufacture or commitments for their procurement; or

(b) if the party against whom enforcement is sought admits in his pleading, testimony or otherwise in court that a contract for sale was made, but the contract is not enforceable under this provision beyond the quantity of goods admitted; or

(c) with respect to goods for which payment has been made and accepted or which have been received and accepted (Sec. 2-606).

Subsection (2) addresses the lack of signature in a contract between merchants. In some instances, a written confirmation sent by the party who is not being held liable under the contract may satisfy the signature requirement of the other party.

EXAMPLE 9-4

The Gotham Zoo telephoned the Pacific Meat Packing Company and placed an order for \$10,000 of meat scraps. The scraps were to be delivered in three installments, with the first due one month from the date of the telephone call. Pacific sent the Zoo a written confirmation of the order. The confirmation referenced the telephone call, the quantity, the price, and the delivery date and was signed by Pacific. Pacific sent the first shipment, which was rejected by the Zoo. The shipment was not defective.

Does section 2-201(1) preclude Pacific from enforcing this contract against the Zoo?

Does section 2-201(2) provide relief for Pacific?

Subsection (3)(a) exempts specially manufactured (custom-made) goods, from the writing requirement.

EXAMPLE 9-5

Billy orally contracted to manufacture a neon sign for Steven's bar and grill. When Billy tendered the sign, Steven refused to accept or pay for it.

Is this contract enforceable under section 2-201(1)?

If Billy sues Steven for breach of contract, is the contract enforceable under section 2-201(3)(a)?

Subsection (3)(b) eliminates the UCC § 2-201(1) written evidence of the contract when a party admits in court or in a court document the existence of the contract. The admission of the contract against interest is evidence that a contract did exist.

The contract, however, will not be enforced beyond the admitted quantity.

EXAMPLE 9-6

Meadowbrook Dairy orally contracted to sell three prize cows and one prize bull to Rolling Hills Farms, a livestock breeder, for \$2,500 for each cow and \$35,000 for the bull. Several days later, Meadowbrook sold the animals to another breeder for double the price.

Rolling Hills sued Meadowbrook for breach of contract. In its answer to Rolling Hills's petition, Meadowbrook denied the existence of the contract. During the trial, however, Meadowbrook was asked during cross-examination: "Didn't you agree to sell these three prize cows to Rolling Hills for \$2,500 each?" Meadowbrook replied: "Yes, sir." The admission of the existence of the oral contract precluded Meadowbrook from asserting the Statute of Frauds. Meadowbrook, however, was not cross-examined about the bull and did not admit the existence of the oral contract as to the bull. Under UCC § 2-201(3)(b), the contract is not enforceable as to the bull.

Subsection (3)(c) eliminates the writing requirement of UCC § 2-201(1) if the seller has accepted payment for the goods or if the buyer accepted shipment of the goods. The actions of the parties is evidence of the contract.

EXAMPLE 9-7

Garrison Equipment Company orally contracted to sell a used backhoe to Old McDonald Farms. The price was in excess of \$500. Old McDonald Farms sent a cashier's check to Garrison for the agreed purchase price. Garrison deposited the check in its account at First Bank. Several days later, Garrison sold the backhoe to Jonas Higginbotham, a local farmer, for twice the price paid by Old McDonald.

Old McDonald sued Garrison for breach of contract. Although there was no written evidence of the contract as required by UCC § 2-201(1), the fact that Garrison accepted payment evidenced a contract for the sale of the backhoe under UCC § 2-201(3)(c). Garrison could not rely on the Statute of Frauds.

Circumventing the Statute of Frauds through Reliance

In Chapter 2 we discussed reliance as a cause of action if no offer is made but one party relied on the other's "promise." Also in Chapter 2 we discussed reliance as a tool to circumvent the absence of consideration so the promise could be enforce-

able in a breach of contract action. In Chapter 3 we discussed reliance as the basis for creating an implied option contract which in turn would negate the offeror's power to revoke an offer. Once the offeror's power to revoke was negated, the offeree could accept the offer, form a contract, and sue for breach of contract.

This section takes reliance one step further. Some courts have begun to use reliance as a means for circumventing the lack of a writing as required by the Statute of Frauds. The Restatement (Second) of Contracts § 139 supports this circumvention.

§ 139. Enforcement by Virtue of Action in Reliance

- (1) A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce the action or forbearance is enforceable notwithstanding the Statute of Frauds if injustice can be avoided only by enforcement of the promise. The remedy granted for breach is to be limited as justice requires.
- (2) In determining whether injustice can be avoided only by enforcement of the promise, the following circumstances are significant:
 - (a) the availability and adequacy of other remedies, particularly cancellation and restitution;
 - (b) the definite and substantial character of the action or forbearance in relation to the remedy sought;
 - (c) the extent to which the action or forbearance corroborates evidence of the making and terms of the promise, or the making and terms are otherwise established by clear and convincing evidence;
 - (d) the reasonableness of the action or forbearance;
 - (e) the extent to which the action or forbearance was foreseeable by the promisor.

To circumvent the Statute of Frauds, a party must establish:

1. a promise by the promisee;
2. the promisor should reasonably expect the promise to induce action or forbearance on the part of the promisee or a third person;
3. the promise does induce the action or forbearance; and
4. injustice can be avoided only by enforcement of the promise notwithstanding the Statute of Frauds.

With the exception of the phrase "notwithstanding the Statute of Frauds," the Restatement (Second) of Contracts § 139(1) mirrors § 90(1).

§ 90. Promise Reasonably Inducing Action or Forbearance

- (1) A promise which the promisor 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 binding if injustice can be avoided only by enforcement of the promise. The remedy granted for breach may be limited as justice requires.

If reliance is to circumvent the Statute of Frauds under section 2-201, one obstacle that must be overcome is the language of section 2-201(1) itself. Subsection (1) begins with the phrase "Except as otherwise provided in this section. . . ." The "in this section" refers to 2-201. Therefore, if the exception is not found in subsection 2-201(2) or (3), the exception does not exist. Since reliance

is not found in either subsection (2) or (3), reliance is not an exception to section 2-201(1) for sale of goods.

The following case of *Warder & Lee Elevator, Inc. v. Britten*, illustrates the use of reliance to circumvent the Statute of Frauds. *Warder & Lee* is particularly interesting because it has a strong dissent that illustrates judicial reluctance to use reliance for this purpose. On July 4th, Britten, a farmer, orally contracted to sell 4,000 bushels of corn and 2,000 bushels of beans to the Warder & Lee Elevator for October-November delivery. Warder & Lee, acting in its normal capacity as a broker, immediately sold the corn and beans to a third party. When grain prices increased substantially during July, Britten called Lee and said he wished to “call the deal off.” Lee responded, “You cannot call it off. We sold this grain, and we expect delivery this fall.” When it became clear that Britten would not deliver, Warder & Lee purchased grain at a higher price to cover its contract with the third person. When Warder & Lee sued Britten for breach of contract, Britten raised the Statute of Frauds as a defense. Identify the reasons that the court and the dissent give for either using or not using reliance to circumvent the Statute of Frauds. Evaluate each reason.

Note in the first paragraph of the court’s opinion, Justice McCormick used the phrase “promissory estoppel.” Promissory estoppel is an early reference to what we refer to as reliance. A number of courts continue to use the phrase “promissory estoppel” although the Restatement (Second) of Contracts uses the phrase “reliance” instead. Therefore, the word “reliance” can be substituted for “promissory estoppel.”

CASE

Warder & Lee Elevator, Inc. v. Britten

Supreme Court of Iowa, 1979. 274 N.W.2d 339.

McCORMICK, Justice.

The question in this action for breach of an oral contract to sell grain is whether the trial court erred in holding defendant’s statute of frauds defense under the Uniform Commercial Code was defeated by promissory estoppel. We affirm the trial court.

This case was tried to the court at law. The trial court’s findings of fact have the effect of a special verdict and we examine the evidence in the light most favorable to the judgment. We are not bound by trial court determinations of law. *Kurtenbach v. TeKippe*, 260 N.W.2d 53, 54–55 (Iowa 1977).

Plaintiff Warder & Lee Elevator, Inc., operates a grain elevator in the town of Webster. The corporation president, Francis Lee, managed the elevator for many years until he suffered a slight stroke in November 1974. He was succeeded as manager by his son James who had been an elevator employee since 1964. The Lees were the only witnesses at trial.

We recite the evidence in the light most favorable to the judgment. Francis Lee was alone in the elevator office on July 4, 1974. Defendant John W. Britten, a farmer in the area, came to the office during the morning with a friend. The elevator had purchased Britten’s grain for years, and he and Lee were well acquainted. At Britten’s request Lee quoted him the price the elevator would pay for new-crop corn and soybeans for fall delivery based on market prices of the prior day.



Britten offered to sell and Lee agreed for the elevator to purchase from Britten 4000 bushels of corn at \$2.60 per bushel and 2000 bushels of beans at \$5.70 per bushel for October-November delivery.

The elevator did not at that time require a seller to sign a memorandum or other writing to show the agreement. Instead, the only writing consisted of notes showing the terms of sale made by Lee for internal bookkeeping purposes. All of the elevator's prior purchases from Britten had been upon oral agreement, and Britten had kept his promises on each occasion. In fact, no seller had previously refused to perform an oral agreement with the elevator.

It was the custom of the elevator not to speculate in grain but to act essentially as a broker. Thus on July 5, 1974, the elevator sold the same quantities of corn and beans as were involved in the Britten purchase for fall delivery to terminal elevators at Muscatine for a few cents more per bushel.

Grain prices increased substantially during July. On July 29, 1974, Britten called Francis Lee and said he wished to "call the deal off". Lee told him: "You cannot call it off. We sold this grain, and we expect delivery this fall." Britten said he would not deliver the grain.

In an effort to mitigate its loss and to enable it to meet its commitment to sell the grain, the elevator purchased appropriate quantities of new-crop corn and beans from other farmers on and shortly after July 29.

In August 1974, James Lee met Britten on a street in Webster. Britten initiated a conversation in which he said he would not fulfill his agreement and offered \$500 in settlement. Although counsel for Britten objected to the admissibility of the evidence at trial, the objection was untimely and no motion to strike was made. Lee rejected the offer. He told Britten the elevator had sold the grain and expected him to perform under his contract.

Britten sold his 1974 crop elsewhere.

The elevator brought this action against Britten for breach of the oral agreement, seeking as damages the loss it sustained in covering its delivery obligation under the July 5 contracts by which it sold the quantity of grain purchased from Britten. See § 554.2712, The Code. That loss was \$6478.34, which was the amount, plus interest, for which the trial court entered judgment.

Britten offered no evidence at trial. He relied solely on the statute of frauds in § 554.2201, The Code. The elevator urged promissory estoppel in bar of the defense.

The statute of frauds applicable to the sale of crops is § 554.2201. Under this statute an oral contract for the sale of goods for a price of \$500 or more is unenforceable, with certain stated exceptions. The elevator does not contend any of those exceptions is applicable. Promissory estoppel is not among them.

Authority for use of promissory estoppel to defeat the statute of frauds, if it exists, must be found under § 554.1103. It provides:

Unless displaced by the particular provisions of this chapter, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions.

We have not had occasion to decide whether the provisions of § 554.2201 displace the doctrine of estoppel which would otherwise be available in accordance with § 554.1103. However, other courts which have considered the question have held the doctrine is available. Several of those decisions involved grain sales in circumstances analogous to those in the present case. See *Decatur Cooperative Association v. Urban*, 219 Kan. 171, 547 P.2d 323 (1976); *Jamestown Terminal Elevator, Inc. v. Hieb*, 246 N.W.2d 736 (N.D. 1976); *Farmers Elevator Company of Elk Point v. Lyles*, 238 N.W.2d 290 (S.D.1976).

When other courts have refused to apply the doctrine they have done so because of a different view of the doctrine of promissory estoppel rather than because of any perceived

statutory bar to its use. See *Cox v. Cox*, 292 Ala. 106, 289 So.2d 609 (1974); *Del Hayes & Sons, Inc. v. Mitchell*, 304 Minn. 275, 230 N.W.2d 588 (1975); *Farmland Service Coop. v. Klein*, 196 Neb. 538, 244 N.W.2d 86 (1976).

We have long recognized promissory estoppel as a means of defeating the general statute of frauds in § 622.32, The Code. See *Miller v. Lawlor*, 245 Iowa 1144, 66 N.W.2d 267 (1954); *Shell Oil Co. v. Kelinson*, 158 N.W.2d 724 (Iowa 1968); *Johnson v. Pattison*, 185 N.W.2d 790 (Iowa 1971). We see nothing in § 554.2201 which purports to require a different rule under the Uniform Commercial Code.

The listing of exceptions to the statute of frauds in § 554.2201 is plainly definitional. The provision does not purport to eliminate equitable and legal principles traditionally applicable in contract actions. Therefore it does not affect the viability of defenses to application of the rule of evidence which it defines. See White and Summers, *Handbook of the Law Under the Uniform Commercial Code* § 2-6 at 59 (1972) ("There is every reason to believe these remain good law, post-Code.").

If § 554.2201 were construed as displacing principles otherwise preserved in § 554.1103, it would mean that an oral contract coming within its terms would be unenforceable despite fraud, deceit, misrepresentation, dishonesty or any other form of unconscionable conduct by the party relying upon the statute. No court has taken such an extreme position. Nor would we be justified in doing so. Despite differences relating to the availability of an estoppel defense, courts uniformly hold "that the Statute of Frauds, having been enacted for the purpose of preventing fraud, shall not be made the instrument of shielding, protecting, or aiding the party who relies upon it in the perpetration of a fraud or in the consummation of a fraudulent scheme." 3 *Williston on Contracts* § 553A at 796 (Third Ed. Jaeger, 1960). The estoppel defense, preserved on the same basis as the fraud defense by § 554.1103, developed from this principle. "The Statute was designed as the weapon of the written law to prevent frauds; the doctrine of estoppel is that of the unwritten law to prevent a like evil." *Id.* at 797-798.

We have found no reported decision in any jurisdiction holding that the statute of frauds in the Uniform Commercial Code, defined as it is in § 554.2203, displaces principles preserved in § 554.1103. We do not believe that our legislature intended for it to do so.

We hold that the provisions of § 554.2201 do not displace the doctrine of estoppel in relation to the sale of goods in Iowa.

We recently discussed the elements of promissory estoppel in *Merrifield v. Troutner*, 269 N.W.2d 136, 137 (Iowa 1978). Those elements are (1) a clear and definite oral agreement, (2) proof that the party urging the doctrine acted to his detriment in relying on the agreement, and (3) finding that the equities support enforcement of the agreement.

Specific circumstances which justify use of the doctrine as a means of avoiding a statute of frauds defense are now expressed in Restatement (Second) of Contracts § 217A (Tent. Draft 1-7, 1973), as follows:

- (1) A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce the action or forbearance is enforceable notwithstanding the Statute of Frauds if injustice can be avoided only by enforcement of the promise. The remedy granted for breach is to be limited as justice requires.
- (2) In determining whether injustice can be avoided only by enforcement of the promise, the following circumstances are significant:
 - (a) the availability and adequacy of other remedies particularly cancellation and restitution;
 - (b) the definite and substantial character of the action or forbearance in relation to the remedy sought;

- (c) the extent to which the action or forbearance corroborates evidence of the making and terms of the promise, or the making and terms are otherwise established by clear and convincing evidence;
- (d) the reasonableness of the action or forbearance;
- (e) the extent to which the action or forbearance was foreseeable by the promisor.

This section complements Restatement (Second) of Contracts § 90, the predecessor of which we previously approved. See *Miller v. Lawlor*, supra. We now approve and adopt the standard in § 217A.

. . . .

In order to obtain the benefit of the doctrine of promissory estoppel to defeat a statute of frauds defense, the promisee must show more than the nonperformance of an oral contract. See 3 Williston on Contracts § 553A (Third Ed. Jaeger, 1960). Under § 217A the defense cannot be overcome, when it is otherwise applicable, unless the promisee proves (1) the promisor should reasonably have expected the agreement to induce action or forbearance, (2) such action or forbearance was induced, and (3) enforcement is necessary to prevent injustice.

In determining whether injustice can be avoided only by enforcement of the promise, the circumstances listed in § 217A(2) must be considered. In this manner, § 217A provides a means of deciding whether the equities support enforcement of the agreement.

We must now decide whether the trial court erred in applying the doctrine of promissory estoppel in this case.

. . . .

Although Britten's second contention presents a closer question, we also find it is without merit. We do so because we believe substantial evidence supports the inference he expected or reasonably should have expected the agreement to induce action by the elevator. It was not necessary for the elevator to prove he actually knew it would rely on his promise. He should have known his prior dealings with the elevator gave the elevator manager every reason to believe he would keep his word. Furthermore, it is reasonable to believe that a farmer who sells grain regularly to country elevators knows they may immediately sell the grain which they purchase. In this case, Britten expressed no surprise when the elevator refused to allow him to rescind because of its sales in reliance on the agreement. Instead he sought to buy his way out of the transaction.

We conclude that the elements of promissory estoppel were supported by substantial evidence. In keeping with the standard in Restatement § 217A, we hold that injustice could be avoided only by enforcement of Britten's promise. The trial court did not err in holding the agreement was enforceable despite the statute of frauds defense.

AFFIRMED.

All Justices concur except REYNOLDSON, C. J., and ALLBEE, J., who dissent.

REYNOLDSON, Chief Justice (dissenting).

I respectfully dissent. The contract in issue falls squarely within the language and intent of the statute of frauds, § 554.2201, The Code 1973. The majority opinion, in my view, misapprehends and misapplies our rules relating to promissory estoppel. Further, the facts in this case do not bring it within the new principles pioneered in this decision.

I. In 1965 the Iowa legislature enacted the "Uniform Commercial Code—Sales." Sixty-First General Assembly, ch. 413, § 2101. It was "a complete revision and modernization of the Uniform Sales Act." D. Stanley & C. Coulter, Iowa Code Comment, 35 I.C.A. § 554.2101 at 118 (1967). Section 554.2201, the UCC's statute of frauds, underwent a substantial liberaliz-

ing overhaul designed to eliminate undesirable and overly technical features of the former law. See D. Stanley & C. Coulter, *supra*, at 145–48; 3 R. Dusenberg & L. King, *Sales & Bulk Transfers under the UCC § 2.05* (1978); R. Hudson, *Contracts In Iowa Revisited*, 15 Drake L.Rev. 61, 75–77 (1966); A. Squillante, *Sales Law In Iowa Under The UCC—Article 2*, 20 Drake L.Rev. 1, 61–65 (1970).

At the same time the statute was modified to clarify that its exceptions were limited to those contained in its provisions. Before 1919 the predecessor to § 622.32, our general statute of frauds, covered “sale[s] of personal property.” See § 4625, The Code 1897. In 1919 the Uniform Sales Act and its statute of frauds were enacted and the general statute was correspondingly revised. Compare §§ 554.4 and 622.32, The Code 1962. The catch-all exception in § 622.33, “or when there is any other circumstance which, by the law heretofore in force, would have taken the case out of the statute of frauds,” ceased to be applicable to sales of goods. Retained as applicable, however, were the “failure to deny” and “oral evidence of the maker” exceptions contained in § 622.34 and .35 respectively. See § 554.5, The Code 1962.

The lead sentence in § 554.2201 now provides:

Except as otherwise provided *in this section* a contract for the sale of goods for the price of five hundred dollars 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. (Emphasis provided.)

The § 622.34 and .35 exceptions are now incorporated in (3)(b) of the section. The specific limitation of exceptions to those contained “in this section” reflects a marked change from former § 554.4.

With exceptions to the statute of frauds now specifically limited by the terms of the statute to those enumerated in its provisions, the majority’s claim that promissory estoppel may be engrafted as simply another exception by virtue of § 554.1103 loses viability. Section 554.1103 permits application of other legal principles, including estoppel, “unless displaced by the particular provisions of this chapter.” Plainly, the limiting language of § 554.2201 constitutes such a displacement. Had the legislature intended the concepts of §§ 90 and 217A of the tentative draft of the Restatement (Second) of Contracts to serve as an exception to its statute of frauds, it would have incorporated them as an exception in the act.

Displacing § 554.1103 with the exceptions in § 554.2201 does not render ineffectual the common-law principles contained in the former. First, they supplement other sections of the UCC except those, like § 554.2201, which provide otherwise. Second, the victim of fraud who has no legal remedy because § 554.2201 prevents proof of the oral contract is not left out in the cold. The equitable remedy of restitution is not dependent upon proof of a contract. The basic elements of equitable estoppel and fraud are (1) intentional misrepresentation, (2) innocent, reasonable and foreseeable reliance, and (3) injury. See *Walters v. Walters*, 203 N.W.2d 376, 379 (Iowa 1973), quoted in *Merrifield v. Troutner*, 269 N.W.2d 136, 137 (Iowa 1978) (equitable estoppel); *Grefe v. Ross*, 231 N.W.2d 863, 864 (Iowa 1975) (fraud). Nor is a contract enforced in those situations. Recovery is based on the injury suffered in the course of reliance. As we stated in *Grefe*, the liability is predicated on the fraud, not on any contract. 231 N.W.2d at 868. With these remedies available, the statute of frauds gives a fraudulent party little protection.

The limiting language of § 554.2201 at least ought to displace a doctrine which would gut the legislative intent of the statute. Distilled to its essence, § 217A, as interpreted by the majority, provides that if one contracting party should know the other contracting party will rely on the contract and injustice will result if the oral contract is not enforced, the statute of frauds will be ignored. It is a rare case when either promisor in a bilateral contract does not

rely on the contract. *Del Hayes & Sons, Inc. v. Mitchell*, 304 Minn. 275, 284, 230 N.W.2d 588, 594 (1975). Any party to a contract should realize such reliance occurs. Most situations in which such an oral contract is breached result in injustice.

But the § 554.2201 statute of frauds obviously is designed to suffer these injustices in isolated oral contract cases in favor of the general public policy to reduce fraud and perjury, curtail litigation and controversy, and encourage written contracts in sales of goods for a price of \$500 or more. It is significant that by trial time the plaintiff corporation in the case at bar was using written sales contracts with its customers.

Adopting §§ 90 and 217A as an unwritten exception to § 554.2201 will not only encourage oral contracts, it will bring a massive infusion of litigation to our overloaded courts. Trial courts will be compelled to determine, on an *ad hoc* basis, whether there was a contract, whether the promisor could "reasonably expect" the other party to rely on it, whether reasonable action or forbearance resulted, whether "justice requires" a remedy, and otherwise engage in the delicate balancing maneuvers mandated by § 217A(2).

In the final analysis, the majority opinion means written contracts are unnecessary in initial purchases or agricultural products, probably Iowa's largest economic marketplace and involving almost three billion dollars worth of goods each year. We should proceed down that road with great caution.

It is just as clear the majority is moving against a long-time trend:

This attitude [to extend exceptions to the statute of frauds] has given way gradually, and from quite an early period the statute of frauds has frequently been spoken of as a most beneficial statute which should be liberally construed to effect its object. The wisdom of the statute is a matter within the control of the legislature, not the judiciary, but it has been said to be justified by long experience. The tendency has long been to restrict rather than to enlarge and multiply the cases of exceptions to the statute, and the right to invoke the statute as a defense is no longer regarded with disfavor. The courts should not be tempted to turn aside from its plain provisions merely because of the hardship of the particular case. They should not be controlled by the consequences following upon an application of the statute, or deem obnoxious a law which the legislature has placed in the statutes and allowed to remain for many years, and they cannot disregard the statute. They certainly should refuse to sanction such a construction as would permit the evils that the statute was intended to prevent.

73 Am.Jur.2d Statute of Frauds § 511 (1974).

II. Aside from the above factors, I am convinced promissory estoppel is not an appropriate device to serve as an exception to the statute of frauds.

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The effect of promissory estoppel on § 554.2201 under the majority opinion is devastating. If the statute is to be repealed the policy decision should be left with the legislature.

III. Finally, it should be noted the facts in this case would not warrant application of § 217A of the Restatement Tentative Draft.

Imposition of § 217A would require proof the defendant seller in this case "should reasonably expect" that the plaintiff corporation would promptly resell the grain. There is no evidence in the transcript in this case to show defendant either knew this was plaintiff's practice or that it was a custom in the industry.

Majority seeks to supply this crucial missing proof by asserting "it is reasonable to believe a farmer who sells grain regularly to country elevators knows they may immediately sell the grain which they purchase."

Majority seems to be judicially noting not only what defendant knew about elevator operations but also the sales practices in a private industry. I doubt these matters qualify for judicial notice as being within common knowledge or capable of certain verification. *Motor Club of Iowa v. Department of Transp.*, 251 N.W.2d 510, 517 (Iowa 1977). Plaintiff corporation's operating officer did not assume defendant had this knowledge. He felt compelled to tell defendant the grain had been resold. This, of course, was long after the event and had no bearing on whether defendant should have "reasonably expected" such action.

I would reverse and remand for a new trial, during which proof of the alleged contract would be regulated by § 554.2201 undiluted by promissory estoppel.

Restitution as a Cause of Action

If an oral contract is unenforceable by reason of the Statute of Frauds, a restitution action may be available to prevent unjust enrichment.

Contract That Cannot Be Fully Performed within a Year Under the Statute of Frauds, a contract that is not to be performed within one year from the date of its making is unenforceable unless it is in writing and signed by the person who made the promise. Part performance does not take the contract out of the statute. Therefore, an employee rendering services in part performance of an oral employment contract cannot maintain an action on the contract when the employer repudiates. Courts, however, generally recognize that the employee may recover in a restitution action for the value of services rendered when the party receiving the services repudiates (refuses to recognize) the contract.

EXAMPLE 9-8

Weaver contracted in writing to work for the General Chemical Company for two years at \$60,000 a year. His salary was to be paid in monthly installments of \$5,000. Shortly after Weaver began work, General Chemical Company became insolvent. Weaver, General Chemical, and General Metals entered into an oral contract whereby Weaver would work for General Metals under the same arrangements he had with General Chemical and General Chemical would be discharged. After working for General Metals for several months, Weaver quit because he was not being paid.

Weaver could successfully sue General Metals in a restitution action. Weaver's recovery would be measured by the reasonable value of his services to General Metals.

Contract for the Transfer of an Interest in Real Property Courts generally hold that the vendee who pays money, renders services, or transfers personal property under an oral contract to transfer an interest in real property may recover in restitution if the vendor repudiates the agreement.

EXAMPLE 9-9

A vendee makes a \$1,000 down payment to the vendor under an oral contract for the purchase of a farm. Subsequently, the vendee tenders the balance of the purchase price to the vendor, but the vendor refuses to accept the tender of the price and refuses to convey the farm. The vendee may recover the \$1,000 down payment in a restitution action.

If the vendor has conferred a benefit on the vendee, the vendor may recover in a restitution action the reasonable value of the benefit conferred.

EXAMPLE 9-10

If the vendee, who has been in possession of the land, repudiates the oral contract for the sale of the land, the vendor may recover in a restitution action for the use and occupation of the land.

If the vendor has not conferred a benefit on the vendee, the vendor cannot maintain a restitution action.

PARALEGAL EXERCISE 9.10 Sammy orally contracted to sell his hot dog stand on Coney Island to Cassandra for \$50,000. Several days later, Cassandra backed out of the deal. Sammy then sold his hot dog stand to Tony for \$45,000.

Could Sammy successfully maintain a restitution action against Cassandra?

ILLEGALITY**Illegality as a Defense to a Breach of Contract Action**

A contract may be unenforceable due to illegality. The illegality may take different forms. The contract in its entirety may be illegal or the contract may have an illegal term. The contract may be legal but an illegal act may have been used to procure the legal contract or an illegal act may have been committed during the performance of the legal contract.

EXAMPLE 9–11

- An illegal contract: A contract to commit murder.
- A legal contract with an illegal term: An employment contract that contains an unreasonable covenant not to compete.
- A legal contract procured by an illegal act: A contract for the sale of goods that was procured by the seller's bribe of the buyer's agent.
- A legal contract performed in an illegal manner: A contract for the sale of real estate where the buyer robs a bank to make the down payment.

Illegal Contract and Illegal Terms A contract that violates the law is illegal and therefore unenforceable. The court will not aid either party when the contract is illegal, regardless of whether the contract has been performed by either. The court will not become the paymaster for an illegal contract but will leave the parties where it finds them.

EXAMPLE 9–12

Henry Moran hired Peter Brooks to transport a dozen cases of illegal whiskey from one county in the state to another. Moran gave Brooks \$500 and promised to give him another \$500 after the job was done. After Brooks transported the whiskey, Moran refused to pay him the additional \$500.

If Brooks were to sue Moran for breach of contract, the court would find the contract unenforceable due to illegality. The purpose of the contract was to perform an illegal act.

PARALEGAL EXERCISE 9.11 James, an employee of Vernon Calhoun Packing Company, was injured on the job. Shortly after the injury, James and the Packing Company entered into a contract whereby the Packing Company promised James lifetime employment for his promise to waive his worker's compensation claim. Five years later, the Packing Company fired James without cause. A state statute provides, "No agreement by an employee to waive his or her rights to compensation under the worker's compensation law shall be valid."

Could James enforce this contract for lifetime employment against the Packing Company?

PARALEGAL EXERCISE 9.12 Hope, a livestock hauler, entered into a three-year contract with Cox Feedlots that provided that Cox would act as a broker, arranging hauling contracts for Hope. In return, Hope would haul all of Cox's livestock to and from the Cox Feedlot, haul all livestock owned by third parties to and from the Cox Feedlot, and pay Cox 10 percent of the gross income for the brokerage services. When Cox discovered that the brokerage fee was, in reality, a rebate in violation of law, he stopped arranging the hauling contracts with third persons for Hope. Could Hope enforce this contract against Cox?

Because the law of the jurisdiction in which performance of the contract occurs usually governs the contract, the issue of the illegality of a contract is ordinarily determined in accordance with the law of the place where the contract is performed.

PARALEGAL EXERCISE 9.13 Alex and Carrie contracted in Michigan to sell Michigan lottery tickets in Oklahoma. The contract provided that Alex would buy tickets in Michigan and Carrie would sell them in Oklahoma at a 10 percent markup. The sale of lottery tickets is legal in Michigan but illegal in Oklahoma.

Alex bought the tickets and gave them to Carrie. Having sold them in Oklahoma, Carrie refused to give Alex the proceeds from the sale.

If Michigan law governs, could Alex enforce this contract against Carrie? If Oklahoma law governs, could Alex enforce this contract against Carrie? Should the law of Michigan or Oklahoma apply?

A covenant not to compete may be illegal as an impermissible restraint on trade when it sweeps too broadly. Parties often use a covenant not to compete in a contract for the sale of a business. This covenant protects the buyer's purchase of the business's goodwill. A covenant may extend only to what is reasonably necessary in terms of subject matter, geography, and duration to protect the buyer's legitimate interest in the enjoyment of the asset purchased.

PARALEGAL EXERCISE 9.14 Rhodes, a minority shareholder and president of SIS, a security guard business, sold his shares to SIS and left the company. The contract for sale contained the following covenant:

Covenant by Seller not to Solicit Buyer's Customers. Seller covenants and agrees that for a period of two years from the date of this agreement, Rhodes will not, within a radius of fifty miles of City Hall, Philadelphia, Pennsylvania, directly or indirectly, as a corporation or as an individual, nor will any business entity or corporation of which he is an owner, shareholder, officer, employee, representative, or otherwise, either directly or indirectly, own,

manage, operate, control or participate in the ownership, management, operation of or control of or be connected in any manner with or assist others in, the security guard business.

After leaving SIS, Rhodes organized and became associated with Rhodes Investigative Services, a detective agency, and with Hahn Security Service, a security guard business. Both were located in Philadelphia.

Can SIS enforce the covenant against Rhodes as it pertains to his detective agency? Can SIS enforce the covenant against Rhodes as it pertains to his security guard business?

An employer hiring a new employee may also use a covenant not to compete when it is either necessary to prevent the disclosure of the employer's trade secrets or confidential lists or the employee's services are special, unique, or extraordinary. In light of the interests the employer is seeking to protect, the covenant must be reasonable in terms of the activities it prohibits the employee from doing, the geographic area in which the employee's activity is prohibited, and the length of time which the employee is prohibited from doing the activity.

PARALEGAL EXERCISE 9.15 Apex Sales & Service is in the business of selling and servicing fire protection equipment. When Peters applied for a job with Apex, he executed a written application that contained the following paragraph:

I further agree that if employed and after working for the company six months or more, I elect to quit, I will not participate in the sale or service of fire protection and/or safety equipment in the Counties of Harris and/or Galveston in the State of Texas for a period of two years.

After working for Apex for more than three years, Peters quit and went to work for Delta Safety and Supply Company, a direct competitor of Apex. While at Apex, Peters had been engaged in inspecting, maintaining, testing, and repairing fire protection equipment in various business establishments, particularly in restaurants. At Delta, Peters is the shop manager and oversees Delta's service personnel.

By working at Delta, has Peters breached his covenant not to compete with Apex? Peters will not be in breach of contract if the covenant not to compete is unenforceable. Determining whether the covenant not to compete is unenforceable requires doing the following:

1. Identify the interest Apex was seeking to protect when it had Peters sign the covenant. Was the covenant necessary:
 - a. to prevent disclosure of Apex's trade secrets or confidential lists; or
 - b. to retain the services of a special, unique, or extraordinary employee?
2. Ascertain, in light of the interest Apex is protecting, whether the covenant is reasonable in terms of:
 - a. the activities that Peters is prohibited from doing;
 - b. the geographic area in which Peters is prohibited from acting; and
 - c. the length of time Peters is prohibited from doing such activities.

Illegal Conduct to Procure a Legal Contract Even if the subject of the contract does not involve illegal conduct, illegal conduct may be present in the procurement of the contract. Such cases often involve bribery.

EXAMPLE 9-13

Sirkin bribed an employee of the Fourteenth Street Store to have the Store purchase merchandise from him. Sirkin delivered the merchandise, but the Fourteenth Street Store refused to pay. When Sirkin sought to use the court to collect on its contract with the Store, the court refused. The illegality—bribery—led to the formation of the legal contract for sale of goods. The court said:

Nothing could be more corrupting, nor have a greater tendency to lead to disloyalty and dishonesty on the part of servants, agents, and employees, and to a betrayal of the confidence and trust reposed in them, than these practices which the Legislature has endeavored to stamp out; and I think nothing will be more effective in stopping the growth and spread of this corrupting, and now criminal, custom than a decision that the courts will refuse their aid to a guilty vendor or vendee, or to anyone who has obtained a contract by secretly bribing the servant, agent, or employee of another to purchase or sell property, or to place the contract with him.

Sirkin v. Fourteenth Street Store, 124 A.D. 384, 108 N.Y.S. 830, 834 (N.Y. Sup. Ct. 1908).

Illegal Conduct in the Performance of a Legal Contract Although a contract may not contemplate illegal activities, one of the parties may act illegally when performing the contract. Not all illegal activity in the performance of a legal contract will preclude the enforcement of the contract. The illegality must be significant and must directly relate to the performance of the contract.

EXAMPLE 9-14

Commonwealth Pictures wanted the distribution rights to certain Universal films. McConnell promised to get Commonwealth the distribution rights if Commonwealth would promise to pay McConnell a commission on the gross receipts as the films are distributed.

McConnell bribed a representative of Universal to negotiate the Commonwealth/Universal contract. Upon discovering the bribery, Commonwealth refused to pay McConnell the commission.

The Commonwealth/McConnell contract was not illegal at its inception, nor did it contemplate that McConnell would use bribery to procure the Commonwealth/Universal contract. In the performance of the contract, however, McConnell engaged in an act of bribery (committed a significant illegal act) that directly related to his performance of the contract. Therefore, McConnell is not entitled to enforce his contract with Commonwealth for the commission.

Restitution as a Cause of Action

As a general rule, parties who enter into illegal contracts are not only unable to enforce their bargains, they also are unable to obtain restitution for any benefits they have conferred under the contract. Although the courts have created a number of exceptions, judicial opinions are unclear whether they entitle the party who conferred the benefit to a breach of contract or a restitution action.

If an exception were to permit a breach of contract action, the party who conferred the benefit would have a choice among expectation, reliance, and restitution remedies. Expectation remedies would place the party who conferred the benefit into the position he or she would have been in if the contract had been fully performed. Expectation remedies would give the party who conferred the benefit the “benefit of his or her bargain.” Reliance remedies would place the party who conferred the benefit back in the position he or she was in prior to conferring the benefit. Reliance remedies would reimburse the party who conferred the benefit for his or her expenditures. Restitution remedies would place the party who received the benefit back in the position he or she was in prior to receiving the benefit. Restitution remedies would require the party who received the benefit to pay what the benefit was worth to him or her. For the purpose of discussion, the exceptions will be treated as permitting a restitution action, not a breach of contract action. This denies the party who conferred the benefit “the benefit of his or her bargain” and limits recovery to disgorging the benefit from the receiver. Therefore, the receiver who is a wrongdoer does not benefit from the contract.

Three exceptions will be explored: *in pari delicto*, collateral illegality, and repentance. ***Pari delicto*** means equal fault. When parties are not *in pari delicto*, they do not share fault equally. When the parties are *in pari delicto* (in equal fault), the court will find for the defendant and leave the parties in the position they were in prior to litigating. As between two equally guilty parties, the concept makes sense because there is no reason to shift the loss from one guilty party to the other.

When the parties are not *in pari delicto*, the exception comes into play. A court may allow restitution to the party with less fault.

EXAMPLE 9–15

Jones, Lindsey and Mydland organized the AVTA Corporation for the manufacture, sale and distribution of audiovisual teaching aids. AVTA applied for and received the right to issue not more than 100 shares to AVTA's corporate officers as personal stock holdings. Of the 100 shares, Jones was issued 80 shares.

Bennett purchased five shares of AVTA stock from Jones's personal stock holdings with payment being made to the corporation. Since this stock was from an officer's personal stock holdings with payment being made to the corporation, a permit was required under state statute. No permit was acquired and therefore this sale was illegal. Bennett sued Jones, Lindsey and Mydland to recover his investment in the stock promotion. The trial court held against Bennett on the ground the contract was illegal and the parties were *in pari delicto*. The California Court of Appeals, in *Maner v. Mydland*, 58 Cal. Rptr. 740 (1967), reversed.



CASE

Maner v. Mydland

Court of Appeal of California, 1967. 58 Cal. Rptr. 740.

FOX, Associate Justice.¹

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We come now to the question: Was Bennett *in pari delicto* with defendants? We have concluded that he was not.

It must be borne in mind that the purpose of the Corporate Securities Law is to protect the investing public. And the penalties therein provided are leveled against the seller and not the buyer. (Robbins v. Pac. Eastern Corp., 8 Cal.2d 241, 278, 65 P.2d 42.) Therefore a purchaser of stock is not *in pari delicto* with the corporation and its directors unless he is equally culpable with them. If such purchaser is not *in pari delicto*, the law accords him relief against the corporation and against any person who aided the corporation in making the sale or participated in the scheme to sell the securities without the requisite permit or consent. (Randall v. Beber, 107 Cal.App.2d 692, 701, 237 P.2d 994.) Mere knowledge that no permit or consent had been issued does not place a purchaser *in pari delicto*. (Randall v. Calif. L.B. Syndicate, 217 Cal. 594, 598, 20 P.2d 331; Taormina v. Antelope Mining Corp., 110 Cal.App.2d 314, 320–321, 242 P.2d 665.)

In *Tri-Q, Inc. v. Sta-Hi Corp.*, 63 Cal.2d 199, at pages 218–219, 45 Cal.Rptr. 878, at page 889, 404 P.2d 486, at page 497, the court elaborated on the applicability of the principle expressed in the phrase *in pari delicto*. The court stated:

“There is no doubt that the general rule requires the courts to withhold relief under the terms of an illegal contract or agreement which is violative of public policy. [Citations.] It is also true that whatever the state of the pleadings, ‘when the evidence shows that . . . [a party] in substance seeks to enforce an illegal contract or recover compensation for an illegal act, the court has both the power and duty to ascertain the true facts in order that it may not unwittingly lend its assistance to the consummation or encouragement of what public policy forbids.’ (Lewis & Queen v. N.M. Ball Sons, 48 Cal. 2d 141, 147–148, 308 P.2d 713, 717.) These rules are intended to prevent the guilty party from reaping the benefit of his wrongful conduct, or to protect the public from the future consequences of an illegal contract. They do not necessarily apply to both parties to the agreement unless *both are truly* [emphasis added] *in pari delicto*. In *Norwood v. Judd*, 93 Cal.App.2d 276, at pp. 288–289, 209 P.2d 24, at p. 31, it was said: ‘The rule that the courts will not lend their aid to the enforcement of an illegal agreement or one against public policy is fundamentally sound. The rule was conceived for the purposes of protecting the public and the courts from imposition. It is a rule predicated upon sound public policy. But the courts should not be so enamored with the Latin phrase “*in pari delicto*” that they blindly extend the rule to every case where illegality appears somewhere in the transaction. The fundamental purpose of the rule must always be kept in mind, and the realities of the situation must be considered. . . . where the defendant is the one guilty of the greatest moral fault, and where to apply the rule will be to permit the defendant to be unjustly enriched at the expense of the plaintiff, the rule should not be applied.’ ”

It is quite apparent that plaintiffs and defendants were not “equally culpable” in this transaction. Bearing in mind that the Corporate Securities Law is for the protection of the

public and that the penalties run against the sellers of securities, it would appear clear that it was the duty of defendants to take the steps necessary to make the sale in conformity with the law. This they did not do. It is thus apparent that the defendants are “guilty of the greatest moral fault” and that the plaintiff Bennett and defendants are not “truly” *in pari delicto*. In such circumstances the rule should not be applied. (Norwood v. Judd, supra, 93 Cal.App.2d, at p. 289, 209 P.2d 24; Tri-Q, Inc. v. Sta-Hi Corp., supra, 63 Cal.2d, at p. 219, 45 Cal.Rptr. 878, 404 P.2d 486.)

The portion of the judgment in favor of defendants and against plaintiff Bennett must be reversed.

Collateral illegality is the second exception to the illegality doctrine. **Collateral illegality** arises when the illegality is not closely related to the plaintiff’s cause of action. Collateral illegality should not pose an obstacle to either a breach of contract or restitution cause of action.

EXAMPLE 9–16

Blackcrow, a Native American, conveyed Blackacre to Smithfield, who was not a Native American. Under state law, Indians could sell tobacco on tribal land without paying state tax. The deed provided that Smithfield could also sell tobacco on Blackacre without paying state tax.

The conveyance of Blackacre is legal, although the provision permitting the sale of tobacco without paying state tax is illegal. The provision permitting the sale of tobacco without paying state tax is collateral to the sale of Blackacre. The court will enforce the contract for sale of the land although the collateral provision is unenforceable.

“Repentance” is the third exception to the illegality doctrine. **Repentance** is a feeling of remorse or regret concerning one’s actions. If a contracting party repents before the illegal objective of the contract is accomplished, some courts will permit this party a restitution action to recover the benefit he or she has conferred on the party who has not repented. This encourages a contracting party to back away from the performance of an illegal transaction. Restitution may be available when:

1. the illegal purpose of the contract has not been accomplished and can be avoided by allowing the repenting party restitution; and
2. the illegality must not have been so serious or shamefully wicked in itself that the court regards the mere making of the contract as a substantial offense.

EXAMPLE 9–17

Mary Melody contracted to sing and play the piano at My Place Lounge for the week of July 1st (Monday through Sunday). Mary sang and played Monday through Saturday but refused to perform on Sunday because state law made it illegal for bars to be open on Sunday. My Place Lounge violates state law and is open on Sundays.

Although the contract between Mary and My Place is illegal, Mary has repented before the illegal purpose has been accomplished (open on Sunday) and the illegality is not an act so serious or shamefully wicked as to make the mere making of the contract a substantial offense. Therefore Mary can maintain an action for restitution to recover the value of her service for Monday through Saturday.

FORUM SELECTION PROVISIONS

At the time of contract formation, the contracting parties may select the forum that will hear any dispute that may arise as the contract is being performed. The parties will actually state their selection in the contract. Because a court is often referred to as a forum, this provision is known as a “forum selection clause.”

EXAMPLE 9–18

The Spanish Mission of Santa Fe, New Mexico, contracted to sell silver jewelry made by Native American artisans to the Old Country Store of Montpelier, Vermont. The contract contained the following forum selection clause: “All disputes arising from this contract shall be decided by the courts of New Mexico.” If a dispute arises during the performance of this contract, the dispute will be heard in a New Mexico forum.

The fact that a contract has a forum selection clause does not guarantee that all future disputes will be heard only by the named courts. If the plaintiff files an action in a court other than the court the contract named, the defendant may request the court to enforce the forum selection clause. Enforcement would require the court to transfer the action to the forum named in the contract.

A court will transfer the action only if the selection clause satisfies several criteria.

1. The forum selection provision must not violate the public policy of the named forum.
2. The forum selection provision must not be unjust and unreasonable.

3. The forum selection provision must be free from fraud, undue influence and unequal bargaining power that subverts the parties' free will at the time of contract formation.
4. The forum selection must be the exclusive forum and not merely a suggested forum for dispute resolution.

A forum selection provision that violates the public policy of the named forum will not be enforced.

EXAMPLE 9–19

If a breach of contract action is filed in Utah, even though the forum selection provision named New Mexico as the proper state for filing the action, the Utah court will refuse to transfer to New Mexico if the public policy in New Mexico condemns forum selection provisions.

An unjust and an unreasonable forum selection clause will not be enforced. A provision is unjust and unreasonable if a trial in the named forum would create a serious inconvenience to any of the participants. The problems of holding a trial in the selected forum must be so great that they would effectively deny a party his or her day in court. Generally, this degree of inconvenience is extremely difficult to prove.

EXAMPLE 9–20

Ronar, a New York Corporation, and F & C, a West German corporation, contracted for F & C to manufacture buttons in West Germany and Ronar to distribute them in North America. The contract contained the following forum selection provision:

The courts at Tirschenreuth, Federal Republic of Germany, shall have jurisdiction and venue.

A dispute arose and Ronar sued F & C in New York. F & C moved to dismiss on the ground that the forum selection provision in their contract conferred venue exclusively on a court in West Germany. The United States District Court for the Southern District of New York, in *Ronar, Inc. v. Wallace*, 649 F. Supp. 319 (S.D.N.Y. 1986) sustained F & C's motion

Interpretation of this clause, like that of any other contract provision, begins in familiar territory. The court's goal is to honor the legitimate expectations of the parties to the contract. See *The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 12, 92 S.Ct. 1907, 1914, 32 L.Ed.2d 513 (1972). To do so the court generally must enforce the specific terms that the parties have chosen because those terms reflect the agreement they have freely reached. See *id.* To be sure, courts are not always bound by contractual language. Most notably, the terms of an agree-

ment are not enforceable when evidence of “fraud, undue influence, or overweening bargaining power” undercuts the premise that the agreement was freely negotiated. *Id.* But absent a “strong showing” of such impinging circumstances, or some other reason why enforcement would be “unreasonable and unjust,” a forum-selection clause is controlling. *Id.* at 15, 92 S.Ct. at 1916; see *Mitsubishi Motors Corp. v. Soler Chrysler-Plymouth, Inc.*, 473 U.S. 614, _____, 105 S.Ct. 3346, 3356, 87 L.Ed.2d 444 (1985) (freely negotiated forum-selection clause enjoys a “strong presumption in favor of enforcement”).

Ronar does not allege that fraud, undue influence, or overweening bargaining power subverted the parties’ free negotiation. Instead it argues simply that enforcement of their agreement would be unfair, unjust, or unreasonable. Ronar explains that it might have difficulty getting personal jurisdiction over the British defendants in West Germany, pretrial discovery would be restricted in a West German proceeding, and many of the parties and prospective witnesses reside in the United States rather than West Germany.

These questions of convenience are hardly different from the ones the Supreme Court considered in *The Bremen*, which like this case involved a dispute between a German corporation and an American one. The Court noted that the inconvenience the plaintiff might suffer by being held to its bargain clearly could have been foreseen. *The Bremen*, *supra*, 407 U.S. at 17–18, 92 S.Ct. at 1917–18, and in order to escape the forum-selection provision on the ground that enforcement would be unjust and unreasonable, the American party would have to sustain the heavy burden of showing that “trial in the contractual forum will be so gravely difficult and inconvenient that he will for all practical purposes be deprived of his day in court.” *Id.* at 18–19, 92 S.Ct. at 1917–18.

None of the possible sources of inconvenience mentioned by Ronar strikes the court as grave. See, e.g., *Clinton v. Janger*, 583 F.Supp. 284, 288 (N.D.Ill.1984) (plaintiff’s inconvenience in suing in multiple forums because one forum does not assert jurisdiction over all defendants is not unreasonable); *Karlberg European Tanspa, Inc. v. JK-Josef Kratz Vertriebsgesellschaft mbH*, 618 F.Supp. 344, 348 (N.D.Ill.1985) (neither the restricted scope of discovery in West Germany, nor the fact that most of the witnesses reside in the United States rather than West Germany, is an unreasonable inconvenience). Each inconvenience was foreseeable when the parties agreed to the West German forum. In fact, the court assumes that because Ronar freely entered the agreement, it not only was aware of the potential disadvantages of the German forum but received consideration for them as part of the bargain. See *Full-Sight Contact Lens Corp. v. Soft Lenses, Inc.*, 466 F.Supp. 71, 73 (S.D. N.Y.1978) (Pierce, J.). Judge Friendly’s warning applies here: “There can be nothing ‘unreasonable and unjust’ in enforcing such an agreement; what would be unreasonable and unjust would be to allow one of the [parties] to disregard it.” *AVC Nederland B.V. v. Atrium Investment Partnership*, 740 F.2d 148, 156 (2d Cir. 1984) (footnote omitted), *quoted in Luce v. Edelstein*, 802 F.2d 49, 57 (2d Cir. 1986), *aff’d in pertinent part and rev’g in part on other grounds*, No. 85 Civ. 4064 (S.D.N.Y. Aug. 7, 1985) (Carter, J.).

Unequal bargaining power at the time of contract formation is also a factor. If one party held such a powerful bargaining position that the other was unable to effectively resist the inclusion of the forum selection provision, a court, on the grounds of fairness, may refuse to enforce the clause.

A final criterion is whether the forum selection clause is exclusive. A court will transfer a case to the named forum only if that forum is the exclusive site for litigation.

EXAMPLE 9–21

Exclusive language is “the courts of Arizona shall have exclusive jurisdiction to hear any and all disputes arising out of this contract.” Under this clause, the parties obviously have agreed that the courts of Arizona and no other courts were to hear the action.

EXAMPLE 9–22

If the clause had read, “The parties, with regard to the resolution of any dispute arising under this agreement, shall submit themselves to the jurisdiction of the courts of Arizona,” and if the action were brought in a court outside Arizona, that court could refuse to transfer the action. The clause merely authorized the Arizona courts to hear the claim. The clause did not designate the Arizona courts as the only courts that could hear the case.

PARALEGAL EXERCISE 9.16 Jane and Bill Anderson, residents of Atlantic, Iowa, decided it was time to buy a new car. They found a great deal at Freeway Motors in Omaha, Nebraska, only fifty miles away. They were so excited about the car that they did not notice the clause in the sales contract that said, “All disputes arising from this agreement shall be litigated in the proper court of Nebraska.”

Unfortunately, the car was a lemon, and Freeway Motors refused to make the repairs as the warranty required. The Andersons filed a breach of contract action in Iowa.

Should the Iowa court grant Freeway Motors’ request to transfer the action to Nebraska? If you were the Iowa judge, what additional facts would you need before you could make your decision and why?

If Freeway Motors had its main office in Kansas City, Missouri, and the contract provided that “all disputes arising from this agreement shall be litigated in the proper courts of Missouri,” would the Iowa judge transfer to Missouri?

The term “shall,” however, does not guarantee that the named forum will be the exclusive forum.

EXAMPLE 9–23

In *Sterling Forest Associates, Ltd. v. Barnett-Range Corp.*, 643 F. Supp. 530 (E.D.N.C. 1986), the contract between Sterling and Barnett-Range provided:

This Agreement shall be construed and enforced in accordance with the law of the State of California and the parties agree that in any dispute jurisdiction and venue shall be in California.

A dispute arose and Sterling sued Barnett-Range in North Carolina. Barnett-Range moved to transfer the case to California.

Defendants ask this court to decline to exercise jurisdiction, arguing that plaintiff waived the right to sue in North Carolina when it agreed to the forum-selection clause noted above. Defendants would claim that, instead of establishing California as one possible forum for adjudication, the Agreement creates exclusive jurisdiction over the contract in California. Plaintiff argues that, while the clause assures jurisdiction in California, it tolerates jurisdiction wherever it may otherwise be found by operation of law.

Defendants contend that, even if this court should find that it has jurisdiction, it should use its discretion to transfer the case in the interests of justice and convenience to the parties and witnesses. Plaintiff opposes this contention and asserts that North Carolina is the more convenient situs for this action. This court will first address the interpretation of the forum-selection clause and will then decide which forum offers the greater convenience.

Defendants rely on the Supreme Court decision of *The Bremen v. Zapata Off-Shore Co.*, 407 U.S. 1, 92 S.Ct. 1907, 32 L.Ed.2d 513 (1972). In that case, the Court held that a forum-selection clause which specified the court where cases would be heard would be enforced unless enforcement would be "unreasonable and unjust, or that the clause was invalid for such reasons as fraud or overreaching." 407 U.S. at 15, 92 S.Ct. at 1916. While this court appreciates the considerable impact of the *Bremen* on the validity of forum-selection clauses, it does not find that case to be controlling here.

In *Bremen*, the wording of the forum-selection clause differed in a critical respect from the clause in this case. The contract in *Bremen* stated that "[a]ny dispute arising *must* be treated before the London Court of Justice." 407 U.S. at 2, 92 S.Ct. at 1909 (emphasis added). The disputed clause in this case does not use such mandatory language. The phrase employed here is far more equivocal: "jurisdiction and venue *shall* be in California." (emphasis added). The contract contains no indication as to whether this language is meant to be exclusive or merely permissive. When confronted with a similarly ambiguous clause in *Keaty v. Freeport Indonesia, Inc.*, 503 F.2d 955 (1974), the Fifth Circuit found both interpretations to be reasonable. Faced with two opposing yet reasonable interpretations of the same contract, that court invoked the traditional rule that any ambiguities should be construed against the drafter of the clause. 503 F.2d at 957.

Because the forum-selection clause does not unambiguously give exclusive jurisdiction to California, this court cannot find that the clause is mandatory. Rather, it may fairly be interpreted as having no influence on the appropriateness of other fora where actions could otherwise be properly brought. *First National City Bank v. Nanz, Inc.*, 437 F.Supp. 184, 187 (S.D.N.Y., 1975).

. . . .

No persuasive proof has been offered either that the language of the clause is mandatory or that it is permissive. The defendants, in advancing this choice of forum clause as a bar to proceedings here, have the burden of proving this defense. The defendants have failed on this point. Because the defendants have not shown that their interpretation of the clause is any more plausible than plaintiff's, defendants have not sustained their burden of proof. The court is unable to find that the clause is mandatory and therefore declines to grant relief on this ground.

For the foregoing reasons, it is hereby ORDERED that defendants' motion for change of venue is DENIED.

PARALEGAL EXERCISE 9.17 Your law firm represents the Panhandle Oil Company, a Texas corporation. Panhandle is negotiating with the Euro ship company, a West German corporation, for Euro to tow an oil rig from Galveston, Texas, to Venezuela. Your senior attorney has asked you to draft a forum selection provision so all disputes would be resolved in Texas. She has given you the following forum selection provisions as a starting point.

Any dispute arising under this contract shall be decided in the state where the Carrier has its principal place of business.

Any action arising out of or relating to any of the provisions of this Agreement may, at the election of the Employer, be brought and prosecuted only in the courts of the Commonwealth of Pennsylvania, and in the event of such election the parties hereto consent to the jurisdiction and venue of said courts.

Any and all claims or causes of action which cannot be mutually settled and agreed to by the parties shall and must be brought or asserted by Purchaser only in the U.S. District Court for the Western District of North Carolina or the Northern Carolina General Court of Justice, Superior Court Division, in Charlotte, North Carolina, and Purchaser hereby expressly agrees, consents and stipulates to the exercise of personal jurisdiction over it and subject matter jurisdiction over any such controversy with respect to such claims or actions being only with such courts.



PARALEGAL CHECKLIST

Contract Enforceability—Protecting the Judicial Process

- ❑ In addition to protecting a class or a party against overreaching, a paralegal must be concerned with aiding the supervising attorney in protecting the court against nonjudicial activities, such as perjury, illegality, and inappropriate forum shopping.
 1. Must the contract be evidenced by a writing to be enforceable? Many contracts are written even though there is no requirement that they be in writing to be enforceable. Some types of contracts, however, must be evidenced by a writing to be enforceable and the writing signed by the person against whom enforcement of the contract is sought. A contract that must be evidenced by a writing that is not, violates the Statute of Frauds.
 - a. Is the contract one that could not be fully performed in less than a year from the time of contract formation? If so, it must be evidenced by a writing to be enforceable.
 - (1) Evaluate the possibility of performance. The probability that the contract will be fully performed within the year is irrelevant. What is relevant is whether there is a lack of any possibility (no matter how slight) that performance will be completed within a year from the date of contract formation. The determination is made as of the date of contract formation and not after the contract has been performed.
 - (2) Determine whether there is full performance. The test is full performance, not termination of the duty (which implies something less than full performance).
 - (3) Check the terms in the writing and the signatures on the contract. The writing must state all essential terms of the contract with reasonable certainty, and the party against whom the contract will be enforced must sign it.

- b. Is the contract for the transfer of an interest in real property? If so, the contract must be evidenced by a writing to be enforceable. A number of states recognize a “part performance” exception.
- c. Is the contract for the sale of goods for the price of \$500 or more? If so, the contract must be evidenced by a writing to be enforceable. The Statute of Frauds provision is UCC § 2-201.
- (1) Determine if the contract satisfies the Statute of Frauds by answering the following questions affirmatively:
 - (a) Does the writing evidence a contract for the sale of goods?
 - (b) Has the party against whom enforcement is sought signed it? and
 - (c) Is a quantity specified?
 - (2) Analyze whether the contract may still be enforceable. Even if these three requirements have not been met, the contract may still be enforceable if one of the following questions can be answered affirmatively:
 - (a) Are the requirements of UCC § 2-201(2) met (between merchants provision with an oral contract followed by a written confirmation)? or
 - (b) Is one of the requirements of UCC § 2-201(3) met (i.e., specially manufactured goods; admission in pleading, testimony, or otherwise in court; or payment made and accepted or goods received and accepted)?
- d. A party may circumvent the Statute of Frauds by relying on an oral promise.
- (1) Was there an oral promise that the promisor should have reasonably expected to induce action or forbearance on the part of the promisee?
 - (2) Did the oral promise induce the promisee to rely? and
 - (3) Is enforcement of the oral promise necessary to prevent injustice notwithstanding the Statute of Frauds?
- e. Even if a party cannot circumvent the Statute of Frauds, a restitution action may be available to prevent unjust enrichment.
2. The paralegal will assist the attorney in determining that a contract may be unenforceable due to illegality by going through the following analysis.
- a. Does the illegality involve the contract itself?
 - (1) Does the contract violate the law? A contract that violates the law is illegal and unenforceable in a breach of contract action. A restitution action is also not available. Some exceptions to the general rule exist.
 - (a) Were the parties *in pari delicto* (in equal fault) at the time of contracting?
 - (b) Is the illegality not closely related to the plaintiff’s cause of action (collateral illegality)?
 - (c) Has the claimant “repented” before the illegal objective was accomplished?
 - (2) Does the contract contain a covenant not to compete that may be illegal? A covenant not to compete may be illegal as an impermissible restraint on trade when it sweeps too broadly.
 - (a) A sale of a business’s goodwill may include a covenant not to compete. Such a covenant may extend only to what is reasonably necessary in terms of subject matter, geography, and duration to protect the buyer’s legitimate interest in the enjoyment of the asset purchased.
 - (b) An employment contract may include a covenant not to compete. Such a covenant must be evaluated in light of the interests the employer is seeking to protect (either to prevent disclosure of the employer’s trade secrets or confidential lists or the employee’s special, unique, or extraordinary services). The covenant must be reasonable in terms of the activities it prohibits, the geographic area in which the employee’s activities are prohibited, and the length of time during which the employee is prohibited for engaging in those activities.
 - b. Did illegal conduct occur in the procurement of a legal contract? Illegal conduct (e.g.,

bribery) may occur in the procurement of a contract. Such conduct may render the otherwise legal contract unenforceable.

- c. Did illegal conduct occur in the performance of a legal contract? Such conduct may render the otherwise legal contract unenforceable if the illegality is significant and is directly related to the performance of the contract.
3. Does the contract provide a selected forum for hearing future disputes? The inquiry is *which forum* and not *whose law*. The fact that a contract has a forum selection clause does not guarantee that all future disputes will be heard only by the named courts.

If a case is filed in a forum not named in the contract, that forum will refuse to transfer the

action to the forum named in the contract if one of the following questions can be answered affirmatively:

- a. Was the forum selection clause unreasonable (e.g., if a trial in the named forum would create a serious inconvenience to any of the participants)?
- b. Was the forum selection clause unfair (e.g., if one party held such a powerful bargaining position at the time of contract formation that the other was unable to effectively resist the inclusion of the forum selection provision)? or
- c. Was the forum selection clause not exclusive?
- d. A party may circumvent the Statute of Frauds by relying on an oral promise.

REVIEW QUESTIONS

DEFINE THE FOLLOWING NEW TERMS AND PHRASES

Collateral illegality

Pari delicto

Repentance

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

1. T F The Statute of Frauds is a common law doctrine.
2. T F Statutes of Frauds require certain types of contracts to be evidenced by a writing to be enforceable.
3. T F There are three major types of contracts that must be evidenced by a writing to be enforceable.
4. T F All contracts must be evidenced by a writing to be enforceable.
5. T F A contract that could be fully performed in less than a year from the time of contract formation does not have to be evidenced by a writing to be enforceable.
6. T F The determination of whether a contract could not be fully performed within one year is made after the parties have performed.
7. T F The Statute of Frauds covers a contract for the sale of land but does not apply to the transfer of a lesser interest in land such as a lease, easement, or mortgage.
8. T F Some states recognize a “part performance” exception to the transfer of an interest in the real property category of the Statute of Frauds.
9. T F A “part performance” exception covers unwritten contracts in which the buyer pays the seller and takes possession of the realty or makes a valuable improvement to the realty with the consent of the seller.

10. T F UCC § 2-201(1) provides that a contract for the sale of goods for a price over \$500 must be evidenced by a writing.
11. T F Section 2-201(1) of the UCC requires that a contract for the sale of goods for the price of \$250 or more must be evidenced by a writing.
12. T F Section 2-201(1) of the UCC requires that any transaction for the lease of goods or for the sale of services must be evidenced by a writing.
13. T F Some courts use reliance to circumvent the Statute of Frauds.
14. T F A restitution action may be available to prevent unjust enrichment if an oral contract is unenforceable because of the Statute of Frauds.
15. T F Illegality may be a defense to a breach of contract action.
16. T F An illegality used as a defense to a breach of contract action must involve the subject matter of the contract.
17. T F An illegality used as a defense to a breach of contract action may involve the subject matter of the contract, the illegal procurement of a legal contract, or the illegal performance of a legal contract.
18. T F A contract that violates the law is unenforceable.
19. T F When the subject matter about which the parties have contracted is illegal, the court will come to the aid of the party who has performed.
20. T F When the subject matter about which the parties have contracted is illegal, the court will leave the parties where it finds them.
21. T F The issue of the illegality of a contract is usually determined in accordance with the law of the place where the contract was formed.
22. T F A covenant not to compete may be illegal as an impermissible restraint on trade when it sweeps too broadly.
23. T F Whether a covenant not to compete is unreasonably broad can only be determined in light of the legitimate interest that the party is seeking to protect with the covenant.
24. T F A covenant not to compete used by an employer hiring an employee must be reasonable in terms of scope, geography, and duration.
25. T F If an employee does not deal with the employer's trade secrets or confidential lists or if the employee's services are not special, unique, or extraordinary, the employee cannot be the subject of an enforceable covenant not to compete.
26. T F Even if the subject of the contract does not involve illegal conduct, illegal conduct may be present in the procurement of the contract.
27. T F Illegal conduct in the procurement of a contract often involves bribery.
28. T F Any illegal activity in the performance of a legal contract will preclude enforcement of the contract.
29. T F Illegal activity in the performance of a legal contract must be significant and must directly relate to the performance of the contract in order to preclude enforcement.
30. T F There are no exceptions to the rule that a party who enters into an illegal contract can neither enforce the bargain nor obtain restitution for any benefit conferred.

31. T F As a general rule, a party who enters into an illegal contract is not only unable to enforce the bargain, he or she is also unable to obtain restitution for any benefits conferred under the contract.
32. T F When parties are *in pari delicto* in an illegal contract, the court will not shift the loss from one party to the other.
33. T F When parties are not *in pari delicto* in an illegal contract, the court may allow restitution to the party with less fault.
34. T F As a general rule collateral illegality (illegality not closely related to the plaintiff's claim) will not permit a restitution claim.
35. T F Collateral illegality will be an obstacle to a breach of contract claim.
36. T F Restitution may be available to the plaintiff who has "repented" and wants to back away from performance of an illegal transaction.
37. T F A "forum selection clause" in a contract is a statement naming the courts in which any dispute arising during the performance of the contract will be heard.
38. T F The fact that a contract has a forum selection clause guarantees that all future disputes will be heard only by the named courts.
39. T F A court must enforce a forum selection provision even if it violates the public policy of the named forum.
40. T F A court will refuse to enforce an unreasonable forum selection clause.
41. T F A court may refuse to enforce a forum selection provision on the grounds of fairness if one party held such a powerful bargaining position that the other was unable to resist inclusion of the provision.
42. T F Forum selection clauses do not apply to international contract disputes.
43. T F Contracting parties from different nations may designate the courts of either of their nations or of a third nation to hear their disputes.

FILL-IN-THE-BLANK QUESTIONS

- _____. Subject matter about which the parties have contracted which makes the contract unenforceable.
- _____. A type of covenant which may be illegal as an impermissible restraint on trade when it sweeps too broadly.
- _____. The asset of a business that a new buyer of the business may seek to protect with a covenant not to compete.
- _____ or _____
The interests that an employer may seek to protect with a covenant not to compete.
- _____, _____, _____
Three exceptions to the general rule that a party who enters into an illegal

contract is not only unable to enforce the bargain, but is also unable to obtain restitution for any benefits conferred under the contract.

6. _____. A Latin expression meaning in equal fault.
7. _____. Illegality not closely related to the plaintiff's claim.
8. _____. Action by the claimant before accomplishing the illegal objective that may permit a court to give the claimant a remedy.
9. _____. A statute forbidding enforcement of certain types of contracts unless they are evidenced by a writing.
10. _____. A cause of action that may be available to prevent unjust enrichment if an oral contract is unenforceable by reason of the Statute of Frauds.
11. _____. A provision in a contract providing for the forum in which any dispute arising as the contract is being performed will be heard.

MULTIPLE CHOICE QUESTIONS (CIRCLE ALL THE CORRECT ANSWERS)

1. Christy Carson, when hired by the Gotham Advertising Agency as an account manager, signed a covenant not to compete. The covenant stated that Christy could not work for any advertising agency in the United States for 10 years from the date of her termination of employment with Gotham.
This covenant not to compete, as applied to Christy Carson, is unenforceable because:
 - (a) Gotham has no legitimate interest to protect
 - (b) the covenant is unreasonable as to subject matter since there may be positions in an advertising agency that are not related to the legitimate interest that Gotham needs to protect
 - (c) the covenant is unreasonable as to duration because Gotham may not need a 10-year prohibition to protect its legitimate interest
 - (d) the covenant is unreasonable as to geographic inclusion because Gotham may not be doing business in the entire United States but only in a limited regional area
 - (e) the covenant is unreasonable as to duration and geographic inclusion but not as to subject matter.
2. Wilson bribed Amy, a buyer for the Kelleyville Super Store, to have the Store purchase merchandise from him. The Store contracted with Wilson and he shipped the merchandise. The Store accepted the shipment but refused to pay.
 - (a) the illegality occurred in the Wilson/Amy contract and not in the Wilson/Store contract and therefore the Wilson/Store contract was enforceable
 - (b) even though the illegality occurred in the Wilson/Amy contract and not in the Wilson/Store contract, the Wilson/Store contract was unenforceable because it was procured through an illegal act (bribery)

- (c) even if the Wilson/Store contract was unenforceable under the general rule, Wilson could maintain a cause of action for breach of contract because the parties were not *in pari delicto*
- (d) even if the Wilson/Store contract was unenforceable under the general rule, Wilson could maintain a cause of action for breach of contract because of the doctrine of collateral illegality
- (e) even if the Wilson/Store contract was unenforceable under the general rule, Wilson could maintain a cause of action for breach of contract because of the repentance doctrine

SHORT ANSWER QUESTIONS

1. John Franklin, the owner of the Ben Franklin Print Shop, sold the shop to Ellen Dewey. Could Ellen include a covenant not to compete in the contract for sale and, if so, how should the covenant be drafted to be enforceable?
2. Are all employees subject to an enforceable covenant not to compete?

PART
IV

Step Four: Breach of the Contract

INTRODUCTION

Types of Breach and Responses

CHAPTER 10

*The Defendant's Response to the Plaintiff's
Allegation of Breach*

INTRODUCTION

Types of Breach and Responses

Step one of the analysis required the finding of the applicable law (federal vs. state, state A vs. state B, common law vs. statute or code). Step two focused on contract formation (offer and acceptance). Step three raised issues of contract enforceability (e.g., minority, mental incapacity, unconscionability, fraud, duress, mistake in a basic assumption of fact, Statute of Frauds, and illegality). Step four (breach of the contract) completes the requirements for a cause of action for breach of contract. Step four has two parts. First the party who has a right to receive performance (the promisee-plaintiff) alleges that the party who has a duty to perform (the promisor-defendant) has breached the contract. Next the defendant will have an opportunity to respond to the plaintiff's allegation of breach by demonstrating that he or she has not breached the contract.

The promisee may allege that the contract has been breached when the promisor either: (1) has not performed when the performance was due; or (2) has notified the promisee that performance will not be forthcoming. A **breach by failure to perform** is the usual breach and arises when the time for the promisor's performance has come and gone without the promisor performing.

EXAMPLE

The House of Gems, a jewelry store, contracted with Quality Printing for the printing of its Christmas catalogs. Quality promised to deliver the catalogs on November 1. The date passed without the catalogs being delivered. Quality has breached the contract by failing to perform when the performance was due.

The promisee may allege that the promisor has breached a contractual duty by notifying the promisee that performance will not be forthcoming. A **breach by anticipatory repudiation** is a notice that the promisor will not perform in the future. The notice itself is a breach. Some refer to this as an "anticipatory breach." When the promisee receives notice that the promisor will not perform in the future, the promisee need not wait for the date performance is due but may rely on the notification, make other plans, and seek an appropriate remedy in a breach of contract action.

EXAMPLE

The House of Gems, a jewelry store, contracted with Quality Printing for the printing of its Christmas catalogs. Quality promised to deliver the catalogs on November 1. On October 15, Quality notified the House of Gems that the catalogs could not be delivered on November 1. Quality's notice that it will not perform on the promised date is a breach by anticipatory repudiation.

Just because the plaintiff-promisee alleges that the defendant-promisor has breached the contract does not make it so. The defendant has an arsenal of four responses to the plaintiff's allegation of breach, any of which, if successful, will cause the plaintiff's cause of action to fail. These responses can be reduced to shorthand phrases:

1. No breach, compliance
2. No breach, excuse
3. No breach, justification
4. No breach, terminated duty

In the first response ("No breach, I am complying with the terms of the contract"), the defendant denies that he or she is not performing in accordance with the terms of the contract.

Although the plaintiff alleges that I have breached the contract, I have complied with the terms of the contract. I am not in breach.

If the defendant is in compliance with the terms of the contract, the defendant has not breached the contract, and the plaintiff has no cause of action for breach.

In the second response ("No breach, although I am not complying with the terms of the contract, my nonperformance was excused"), the defendant admits not performing the contract but asserts that this nonperformance was excused by a supervening external event (that is, an event not referenced in the contract) and therefore not a breach.

I may not be performing the contract, but there is an outside event that prevents my performance. I am excused from performing, and I am not in breach.

Unlike the first response ("No breach, compliance"), the supervening external event in the second response ("No breach, excuse") was not an express term in the contract. Even though this supervening external event (an act of God or a governmental regulation) was not an express term, it may excuse the defendant's nonperformance. If the defendant's performance is excused, the defendant is not in breach, and the plaintiff cannot maintain a cause of action for breach of contract.

In the third response to the plaintiff's allegation of breach ("No breach, although I am not complying with the terms of the contract, my nonperformance

was justified by your breach of this contract”), the defendant admits nonperformance but claims that the nonperformance was justified by a breach by the plaintiff.

My nonperformance of the contract was justified by your breach of the contract. Therefore, you are the breaching party and not I.

The defendant’s nonperformance is not a breach—it is a justified nonperformance much like self-defense in criminal law. Because the plaintiff rather than the defendant is the breaching party, the plaintiff cannot maintain a cause of action for breach of contract against the defendant.

In the fourth response (“No breach, although I am not complying with the terms of the contract, my duty to perform the contract has been terminated”), the defendant admits nonperformance but claims that his or her contractual duty has ended either by agreement or by law and that, therefore, he or she has not breached the contract.

I no longer have to perform according to the contract. My obligation no longer exists due to some duty terminating occurrence. I am not in breach.

The terminating occurrence may be consensual (substitute contract, accord and satisfaction, or novation), unilateral (release or waiver), or by operation of law (statute of limitations). Because the defendant is not a breaching party, the plaintiff cannot maintain a breach of contract action.

If the defendant is unsuccessful in using these four responses, he or she has little alternative but to admit as true the plaintiff’s allegation of breach.

Yes, I admit I breached the contract.

Whether the defendant’s breach is intentional or unintentional is irrelevant. The law of contracts does not evaluate the mental state accompanying nonperformance. The relevant factor is whether the defendant did not perform his or her contractual duty.



10

The Defendant's Response to the Plaintiff's Allegation of Breach

- ◆ No Breach, Compliance

- Finding the Terms of the Contract*

- Performing the Terms of the Contract*

- Determining Whether the Condition Precedent Has Occurred*

- Restitution as an Action When a No Breach, Compliance Response Prevails*

- ◆ No Breach, Excuse

- Impossibility*

- Impracticability*

- Frustration of Purpose*

- Restitution as a Course of Action When Nonperformance of the Contract Is Excused*

- ◆ No Breach, Justification

- The Plaintiff and the Defendant Have Duties to Perform*

- The Plaintiff's Performance Was a Condition Precedent to the Defendant's Performance*

- The Plaintiff Was in Breach*

- The Magnitude of the Plaintiff's Breach Justified the Defendant's Nonperformance*

- Restitution as an Action for the Breaching Plaintiff*

◆ No Breach, Terminated Duty

Condition Subsequent Terminates the Duty

Consensual Termination of a Duty

Unilateral Termination of a Duty

Termination of a Duty by Operation of Law

◆ Breach

Now that a contract has been formed (Chapters 2 through 5) and no impediment to its enforcement exists (Chapters 7 through 9), Chapter 10 shifts the focus to the breach of contractual duties. The allegation of breach may be either that the promisor did not perform (breach by failure to perform) or notified the promisee that performance would not be forthcoming (breach by anticipatory repudiation) (see Figure 10–1).

After the plaintiff has alleged the defendant's breach, the defendant has an opportunity to respond to the plaintiff's allegation. The defendant has four responses that will negate plaintiff's allegation of breach:

1. no breach, compliance ("no breach, I am complying with the terms of the contract");
2. no breach, excuse ("no breach, although I am not complying with the terms of the contract, my nonperformance was excused");
3. no breach, justification ("no breach, although I am not complying with the terms of the contract, my nonperformance was justified by your breach of the contract"); and
4. no breach, terminated duty ("no breach, although I am not complying with the terms of the contract, my duty to perform the contract has been terminated").

If the defendant's response to the plaintiff's allegation of breach is successful and therefore the plaintiff could not maintain a breach of contract action and if the plaintiff has conferred a benefit on the defendant, the plaintiff may consider a restitution cause of action. A restitution cause of action would be available if it would be unjust to permit the defendant to retain the benefit without compensating the plaintiff.

If the defendant's response to the plaintiff's allegation of breach is unsuccessful, the defendant has breached the contract and the plaintiff has established his or her cause of action for breach of contract. Now the plaintiff is entitled to proceed to the final step in the analysis—the plaintiff's selection of remedies for the defendant's breach of contract (see Figure 10–2).

NO BREACH, COMPLIANCE

The defendant's first response to the plaintiff's allegation of breach is "No breach, I am complying with the terms of the contract" (see Figure 10–3). The defendant

FIGURE 10-1 Complaint—Plaintiff’s Allegation of Defendant’s Breach

IN THE DISTRICT COURT OF [NAME] COUNTY		
STATE OF [NAME]		
[NAME], dba [Name])	
)	
Plaintiff,)	
)	
v.)	Case No. _____
)	
[NAME], a [Name of State])	
corporation)	
)	
Defendant.)	

COMPLAINT FOR BREACH OF CONTRACT

1. Plaintiff is an individual residing in [Name] County, [Name of State], doing business as [Name].
2. Defendant is a corporation incorporated under the laws of the State of [Name of State].
3. On or about [date], Plaintiff and Defendant entered into a written contract whereby Plaintiff promised to design a marketing plan for Defendant and Defendant promised to pay [\$ dollars] and 1% of Defendant’s net profits earned during the first year after the marketing plan was implemented. The contract also provided that in the event of litigation, reasonable attorney fees could be awarded to the prevailing party. A copy of the contract is attached as Exhibit A.
4. On or about [date], Plaintiff presented the completed marketing plan to the Defendant.
5. All conditions precedent have been performed by Plaintiff or have occurred and Defendant has not been excused from performance.
6. Defendant has breached the contract by failing to pay the Plaintiff for the services rendered.
7. As a result of Defendant’s breach of contract, Plaintiff has sustained damages in the sum of \$ [dollars].

Accordingly, Plaintiff demands judgment against Defendant for the sum of \$ [dollars], interest, and costs, including reasonable attorney fees.

[Attorney’s name signed]
 [Attorney’s name typed]
 Attorney for plaintiff
 [Bar membership number]
 [Address]
 [Telephone number]

FIGURE 10-2 The Breach Phase of the Road Map

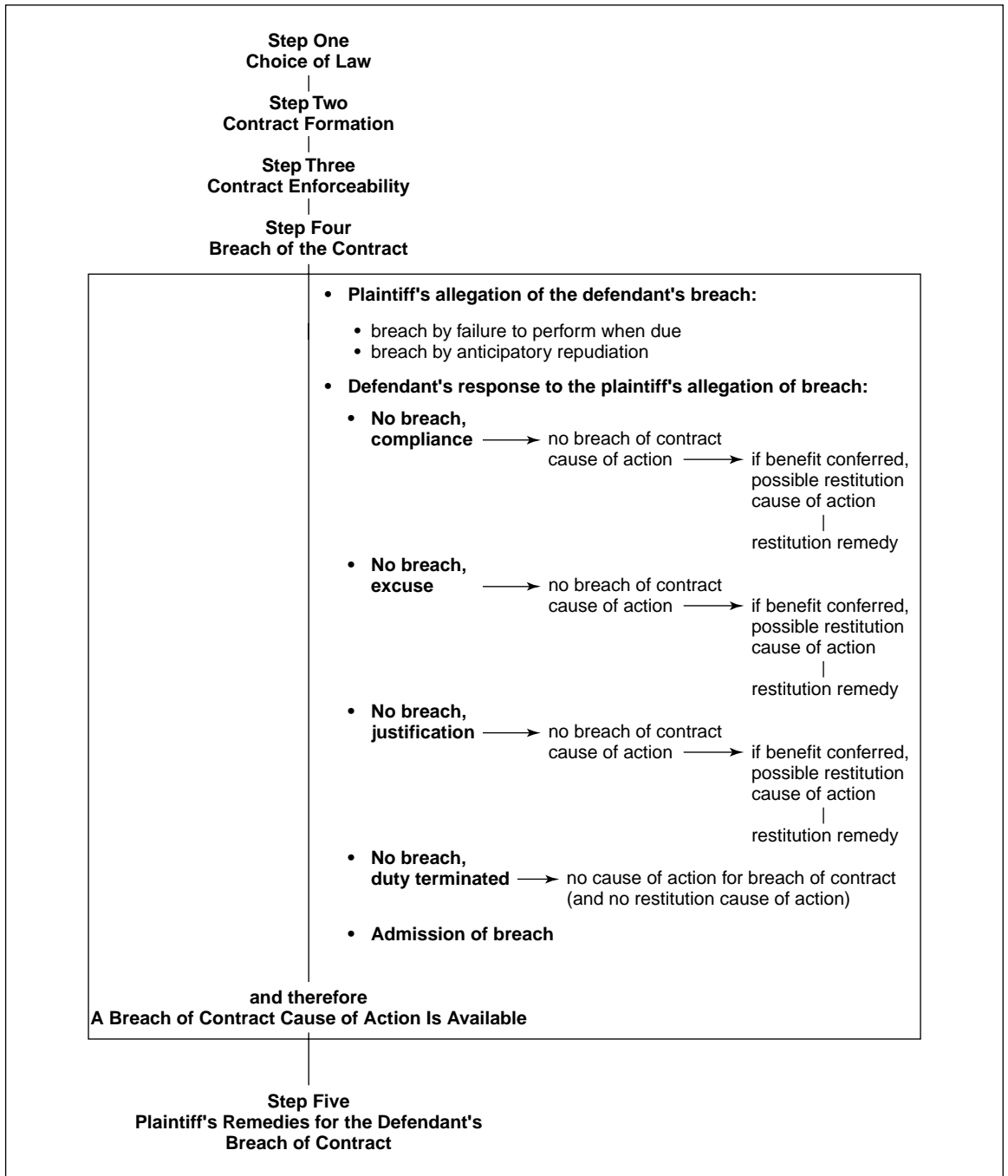


FIGURE 10-3 Answer—Defendant’s “No Breach, Compliance” Response to the Plaintiff’s Allegation of Defendant’s Breach

IN THE DISTRICT COURT OF [NAME] COUNTY
STATE OF [NAME]

[NAME], dba [Name])	
)	
Plaintiff,)	
)	
v.)	Case No. _____
)	
[NAME], a [Name of State])	
corporation)	
)	
Defendant.)	

ANSWER OF DEFENDANT [NAME]

Defendant [name] alleges the following in response to the complaint:

1. Defendant admits the allegations of paragraph 1 of the complaint.
2. Defendant admits the allegations of paragraph 2 of the complaint.
3. Defendant admits the allegations of paragraph 3 of the complaint.
4. Defendant admits the allegations of paragraph 4 of the complaint.
5. Defendant denies that all conditions precedent have occurred as alleged in paragraph 5 of the complaint in that payment was conditioned on the marketing plan improving sales by 50% over the next twelve months and twelve months have not yet passed.
6. Defendant denies the allegations of paragraph 6 that it breached the contract.
7. The complaint fails to state a claim against Defendant upon which relief can be granted.

Accordingly, Defendant demands that Plaintiff take nothing by this Action, and that Defendant be awarded costs including reasonable attorney fees.

[Attorney’s name signed]
 [Attorney’s name typed]
 Attorney for plaintiff
 [Bar membership number]
 [Address]
 [Telephone number]

denies that he or she has failed to comply with the terms of the contract. If the defendant is in compliance with the terms of the contract, the contract has not been breached, and the plaintiff has no cause of action for breach of contract.

The defendant-promisor may contend that he or she is complying with the terms of the contract because: (1) the contract does not include the duty the promisee alleges the promisor has breached; or (2) even if the contract does include such a duty, the promisor did not breach this duty.



If the terms of the contract are in writing, the parties will refer to the writing to determine each party's obligation. It is helpful when the writing clearly states the duties of the parties and there is no dispute, but writings are seldom perfect.

Finding the Terms of the Contract

Whether the contract includes the duty the promisee alleges the promisor breached raises two topics discussed in Chapter Five: the parol evidence rule and the mistake in integration.

The Parol Evidence Rule Revisited When a contract has been reduced to a final writing, the contract may consist of only those terms found in the final writing or those terms in the final writing plus additional terms.

Under the parol evidence rule, in the absence of fraud in the inducement, duress, or mutual mistake of fact, extrinsic evidence, oral or written, made prior to or contemporaneous with the final writing cannot be used to add to or contradict the final writing (the integration).

If under the parol evidence rule the term is not in the contract, the defendant-promisor will have no duty and can respond to the plaintiff-promisee's allegation of breach—"No breach, compliance."

A Mistake in Integration Revisited When a contract has been reduced to a final writing, the parties may discover that the writing did not accurately capture their agreement.

EXAMPLE 10–1

Buyer telephoned Seller to inquire about the price of 2,000 crates of oranges. After negotiating, the parties settled on 2,000 crates at \$10 a crate. Seller told Buyer that she would send a written confirmation of their oral contract. In typing up the confirmation, Seller erroneously typed 3,000 crates.

Seller sent the confirmation to Buyer, who did not bother to read it until an extra 1,000 crates of oranges arrived. When Seller typed the confirmation with a quantity that differed from the quantity orally agreed upon, she made a mistake in the integration of the contract.

Under the mistake in integration doctrine, a court has the power to reform the final writing to reflect the contract if parties' oral agreement expresses their real intentions; the writing fails to express those intentions; and the failure is due to a mutual mistake or a unilateral mistake accompanied by the other party's fraudulent conduct. If no mistake in integration is found and the final writing is not reformed, the defendant-promisor's duty will be only that found in the final writing and not what the plaintiff-promisee alleges is the duty. The defendant-promisor can respond to the plaintiff-promisee's allegation of breach—"No breach, compliance."

Performing the Terms of the Contract

If the contract includes the duty alleged by the promisee to have been breached by the promisor, there remains the question whether the defendant-promisor breached this duty. This raises the topic of the interpretation of contract language.

If the terms of the contract are in writing, the parties will refer to the writing to determine each party's obligations. It is helpful when the writing clearly states the duties of the parties and there is no dispute, but writings are seldom perfect.

In 20/20 hindsight, the terms of the writing may not have been as carefully drafted as they should have been. The parties may dispute each other's meaning. They are left with an ambiguity that needs resolution. Ambiguities may be patent or latent. A **patent ambiguity** is apparent from the face of the writing. A **latent ambiguity** is apparent when information beyond the writing demonstrates that the term has a double meaning.

Patent Ambiguities Patent ambiguities are often created by inexact pronoun reference or misleading modifiers.

EXAMPLE 10–2

The attorney told her client she needs more information. Who needs more information, the attorney or the client?

EXAMPLE 10–3

I said when I have finished my research, I will write the brief. Does this mean: I have finished my research and I will write the brief; or, I will write the brief when I have finished my research?

Latent Ambiguities—Miscommunications between the Promisor and the Promisee Revisited An ambiguity may not always be apparent from the face of the writing. Latent ambiguities are often created when the term has a double meaning. These miscommunications between the promisor and the promisee are discussed in Chapter Four.

EXAMPLE 10–4

Buyer purchased 125 bales of cotton from Seller to be shipped from Bombay to Liverpool on the ship *Peerless*. Buyer met the ship *Peerless* (which sailed from Bombay) when it docked in Liverpool in October, but there was no cotton. Buyer, believing Seller had breached the contract, purchased substitute cotton on the open market.

In December, a second ship named *Peerless* (which also sailed from Bombay) docked in Liverpool. Although this ship carried cotton Seller was sending to the Buyer, Buyer no longer needed the cotton and rejected the shipment.

The ambiguity—two ships with the same name sailing from and to the same ports—was not apparent from the face of the contract. The ambiguity became apparent only when Buyer discovered the existence of two ships with the same name. The ambiguity was latent.

Latent ambiguities are resolved by examining what the term means to a reasonable person. If the term is a trade term, the reasonable person will be a reasonable person in the trade.

The term: Peerless		
Promisor's perception of the term	October Peerless	October Peerless
Promisee's perception of the term	December Peerless	December Peerless
Reasonable person's perception of the term	October Peerless	December Peerless
Conclusion	October Peerless	December Peerless
Explanation	if the reasonable person's perception is the same as the promisor's perception, the term carries the promisor's meaning.	if the reasonable person's perception is the same as the promisee's perception, the term carries the promisee's meaning.

Differing Opinions as to the Duty The promisor and promisee may simply have differing opinions as to the promisor's duty. Differing opinions are also resolved by examining what the term means to a reasonable person. If the term is a trade term, the reasonable person will be a reasonable person in the trade.

A number of maxims and rules of construction provide some assistance, although for every maxim or rule, a contradictory one can be found. Some common phrases are:

- The terms of the contract should be strictly construed against the drafter (*contra proferentem*).
- The contract should follow the intent of the parties.
- Contract terms should be given their plain meaning (plain meaning rule).
- General words that follow specific words should be limited to the same general kind or class as the specific words (*ejusdem generis*).
- The enumeration of one thing implies the exclusion of those things not enumerated (*expressio unius est exclusio alterius*).

If the parties had prior contractual relationships, the course of their dealings under those contracts could shed light on the current dispute. Additionally, if the parties have partially performed under the contract in dispute, the prior performances of the parties may provide assistance in resolving the dispute.

Determining Whether the Condition Precedent Has Occurred

Some promises need not be performed until the occurrence of an express condition. A **condition** is a contingency. It is a premise upon which the fulfillment

of the promise depends. A condition may be based on the occurrence of an external event.

EXAMPLE 10-5

"I promise to come home when the sun goes down." The sun going down is a condition to the promise to come home.

A **condition precedent** is a duty creating event.

EXAMPLE 10-6

"I promise to pay for damages to your home if it is struck by lightning." Being struck by lightning is the event that creates the duty to pay. The promisor has no duty to pay until the event occurs.

EXAMPLE 10-7

A fire insurance policy presents a classic illustration of a "no breach, compliance" response. Triplett contracted with the Lone Star Insurance Company for homeowner's insurance. Triplett promised to pay the premiums for Lone Star's promise to pay for repairs to Triplett's house for damage caused by natural disaster. Because Triplett's house was located in a flood plain, the policy excluded damage due to flooding. Several months after Triplett paid the premium, his house was damaged by a 100-year flood.

Triplett filed a claim with Lone Star, but Lone Star denied the claim on the ground that the policy did not cover loss by flooding.

If Triplett filed an action against Lone Star for breach of contract, he would allege that Lone Star breached the contract by not paying the claim. Lone Star's response would be "no breach, compliance. Because the contract states that we do not have to pay for losses caused by flooding and because this loss was caused by flooding, we have no duty under the contract to pay for this loss. We are complying with the terms of the contract."

Restitution as an Action When a No-Breach, Compliance Response Prevails

The "no breach, compliance" response is a denial of breach. "I am not breaching, I am complying." Without a breach of the contract, the remedies for breach of contract are unavailable. Situations may exist in which both the promisor and

promisee are complying with the terms of the contract, although the contract will require neither to perform further, because a condition in the contract has terminated their duties to perform. Although neither is in breach, the promisee has at least partially performed.

Situations may arise in which the contract calls for the promisee to begin performance first. The promisee begins to perform his or her respective duties under the contract. Suddenly an event that is necessary for the continued performance of the contract does not occur, and the promisee's duty to continue performance is terminated. The contract does not call upon the promisor to perform because the promisor must perform after the promisee fully performs. The performance of the contract comes to a standstill. Neither party has breached the contract. If the promisee has partially performed the contract, further complications occur. By performing, did the promisee confer a benefit on the promisor? If the promisor retains this benefit without compensating the promisee, is the promisor unjustly enriched?

PARALEGAL EXERCISE 10.1 Lewis contracted to purchase Blackacre from Roberts for \$85,000. The contract was subject to Lewis's obtaining a twenty-year mortgage for \$60,000 at 9 percent from a lending institution. The contract also called for an \$8,500 deposit. The contract does not address who gets the deposit if Lewis makes a good faith attempt to secure financing but is unsuccessful.

Lewis paid Roberts the \$8,500 deposit. After exercising due diligence, Lewis was unable to find a twenty-year mortgage for \$60,000 at 9 percent from a lending institution.

Could Lewis maintain a breach of contract action against Roberts for return of the \$8,500 deposit? If Lewis could not maintain a breach of contract action, could Lewis maintain a restitution cause of action against Roberts for return of the \$8,500 deposit?

NO BREACH, EXCUSE

The defendant's second response (see Figure 10–4) to the plaintiff's allegation of breach is "No breach, excuse."

Although the promisee alleges that I have breached the contract, I have not performed the contract because a supervening external event has prevented my performance. I am excused from performing, and I am not in breach.

Unlike the first response ("No breach, compliance") where the defendant claims that he or she *is* performing the contract, in the second response ("No breach, excuse"), the defendant admits that he or she *is not* performing the contract. The defendant, however, claims that a supervening external event (an act of God or a governmental regulation) has excused his or her performance. A **supervening external event** is an event that occurs after contract formation and before full performance of the contract. In the "no breach, excuse" response,

FIGURE 10-4 Answer—Defendant’s “No Breach, Excuse” Response to the Plaintiff’s Allegation of Defendant’s Breach

IN THE DISTRICT COURT OF [NAME] COUNTY STATE OF [NAME]		
[NAME], dba [Name])	
)	
Plaintiff,)	
)	
v.)	Case No. _____
)	
[NAME], a [Name of State])	
corporation)	
)	
Defendant.)	
ANSWER OF DEFENDANT [NAME]		
Defendant [name] alleges the following in response to the complaint:		
1. Defendant admits the allegations of paragraph 1 of the complaint.		
2. Defendant admits the allegations of paragraph 2 of the complaint.		
3. Defendant admits the allegations of paragraph 3 of the complaint.		
4. Defendant admits the allegations of paragraph 4 of the complaint.		
5. Defendant alleges that it has been excused from performance as alleged in paragraph 5 of the complaint in that a tornado on [date] destroyed Defendant’s offices.		
6. Defendant denies the allegations of paragraph 6 that it breached the contract.		
7. The complaint fails to state a claim against Defendant upon which relief can be granted.		
Accordingly, Defendant demands that Plaintiff take nothing by this Action, and that Defendant be awarded costs including reasonable attorney fees.		
		[Attorney’s name signed] [Attorney’s name typed] Attorney for plaintiff [Bar membership number] [Address] [Telephone number]

the contract does not refer to the occurrence of the supervening external event. Therefore, the risk of the occurrence of the supervening external event is not allocated by contract. If the promisor is excused, the promisor is not in breach, and the promisee cannot maintain a breach of contract cause of action.

The “no breach, excuse” response has three variations. In some situations, the supervening external event renders the contract impossible to perform. In others, the supervening external event does not render the contract impossible to perform, but renders the performance of the contract commercially impracticable. In still others, although the supervening external event does not render the contract impossible or commercially impracticable to perform, the supervening external event renders the performance of the contract to be without purpose and therefore there is a frustration of purpose.

Impossibility

Cases of impossibility often involve destruction or unavailability of the subject matter of the contract. A leading case is *Taylor v. Caldwell*, 3 B. & S. 826, 122 Eng. Rep. 309, 314-15 (K.B. 1863), an old English case. Taylor, an impresario, contracted to rent the Surrey Gardens and Music Hall from Caldwell for four days for the purpose of presenting four “grand concerts” and “day and night fetes” in the hall. Shortly after the parties signed a lease and before the concert dates, fire destroyed the music hall. Taylor brought a breach of contract action against Caldwell alleging that Caldwell breached the contract by failing to provide the music hall. Caldwell responded that although he did not provide the hall, his not providing the hall was excused due to the fire. The court in *Taylor v. Caldwell*, held that the destruction of the music hall did excuse Caldwell from performing the contract:

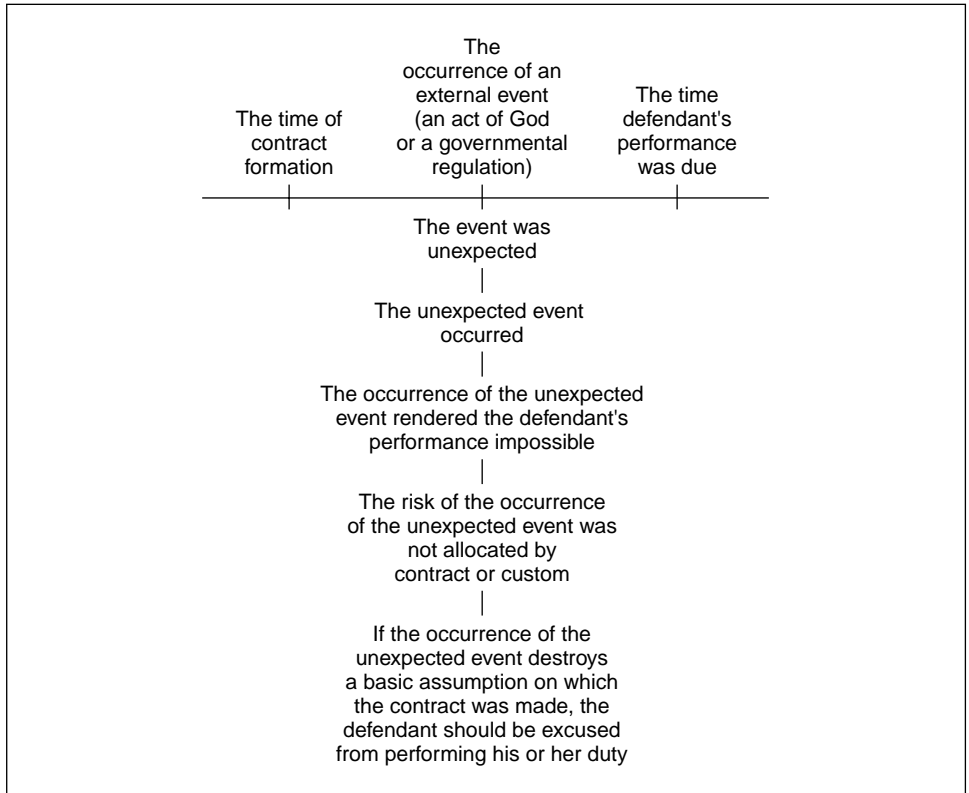
The principle seems to us to be that, in contracts in which the performance depends on the continued existence of a given person or thing, a condition is implied that the impossibility of performance arising from the perishing of the person or thing shall excuse the performance.

In none of these cases is the promise in words other than positive, nor is there any express stipulation that the destruction of the person or thing shall excuse the performance; but that excuse is by law implied, because from the nature of the contract it is apparent that the parties contracted on the basis of the continued existence of the particular person or chattel. In the present case, looking at the whole contract, we find that the parties contracted on the basis of the continued existence of the Music Hall at the time when the concerts were to be given; that being essential to their performance.

We think, therefore, that the Music Hall having ceased to exist, without fault of either party, both parties are excused, the plaintiffs from taking the gardens and paying the money, the defendants from performing their promise to give the use of the Hall and Gardens and other things.

The doctrine of implied conditions ultimately gave way to a more direct analysis of risk allocation. The following series of questions may be helpful in understanding impossibility cases:

1. Did an unexpected event occur after the contract was formed?
2. Did the occurrence of the unexpected event render the promisor's performance of the contract impossible?
3. Was the risk of the promisor's nonperformance due to the occurrence of the unexpected event allocated either by contract or by custom?
4. Was the nonoccurrence of this unexpected event a basic assumption on which the contract was made and therefore the promisor should be excused from performing?



The first three questions sort those cases that are impossibility cases from those that are not. In *Taylor v. Caldwell*, the destruction of the hall due to fire was an unexpected event and did take place after the contract to lease was formed. Without the music hall, Caldwell could not provide the space and therefore his performance was impossible. Neither the contract nor custom allocated the risk of Caldwell's nonperformance due to the destruction of the music hall by fire.

The fourth question is simply risk allocation. Should Caldwell, the lessor, bear the risk of any loss suffered by the lessee when the unexpected fire

prevents the lease of the hall? Which of the two innocent parties should bear the risk of the unexpected event and, ultimately, the risk of nonperformance? If the parties had thought about the possibility of nonperformance due to an unexpected supervening event, which party would have assumed the risk of the nonperformance? When answering this question, all the surrounding circumstances and equities are considered, including commercial practices and mores.

Suppose the parties are reversed in the lawsuit. Caldwell, the lessor, sued Taylor, the lessee, alleging that Taylor did not finish paying on the contract. Could Taylor respond that he was excused from paying because the music hall burned down? Should Taylor, the lessee, bear the risk of any loss suffered by the lessor when the unexpected fire prevents his using the hall?

PARALEGAL EXERCISE 10.2 In June, the Browning Agency, a creative advertising agency, contracted with Edith Edwards to send a hot air balloon over Chicago on the Fourth of July as part of an advertising campaign for Edith's Ice Cream Shoppe. High winds on the Fourth of July prevented Browning from sending up the balloon.

Edith sued Browning for breach of contract alleging that Browning breached by not sending up the balloon. Could Browning successfully maintain that its nonperformance was excused?

1. What was the event that led to Browning's failure to perform the contract, was this event expected or unexpected, and did it occur after contract formation?
2. Did the occurrence of the unexpected event render Browning's performance of the contract impossible?
3. Was the risk of Browning's nonperformance due to the occurrence of the unexpected event allocated either by contract or by custom?
4. Was the nonoccurrence of this unexpected event a basic assumption on which the contract was made?

PARALEGAL EXERCISE 10.3 Rona contracted to create a sculpture of a moose for Andy for Christmas. Shortly before Christmas, Rona completed the sculpture and arranged for it to be delivered to Andy. Before the sculpture could be delivered, a thief broke into Rona's studio and stole the sculpture. An extensive search by the police did not locate the sculpture.

Andy sued Rona for breach of contract alleging that Rona breached by not delivering the sculpture. Could Rona successfully maintain that her nonperformance was excused?

1. What was the event that led to Rona's failure to perform the contract, was this event expected or unexpected, and did it occur after contract formation?
2. Did the occurrence of this event render Rona's performance of the contract impossible?

3. Was the risk of Rona's nonperformance due to the occurrence of the unexpected event allocated either by contract or by custom?
4. Was the nonoccurrence of this unexpected event a basic assumption on which the contract was made?

PARALEGAL EXERCISE 10.4 Gateway Industries of St. Louis contracted to buy twelve new pick-up trucks from Good Deal Motors of Detroit. Good Deal contracted with Express Railway to deliver the trucks to St. Louis. Enroute, the train derailed and the trucks were damaged.

Gateway sued Good Deal for breach of contract alleging that Good Deal breached by not delivering the trucks. Could Good Deal successfully maintain that its nonperformance was excused?

1. What was the event that led to Good Deal's failure to perform the contract, was this event expected or unexpected, and did it occur after the contract was formed?
2. Did the occurrence of this event render Good Deal's performance of the contract impossible?
3. Was the risk of Good Deal's nonperformance due to the occurrence of the unexpected event allocated either by contract or by custom?
4. Was the nonoccurrence of this unexpected event a basic assumption on which the contract was made?

PARALEGAL EXERCISE 10.5 Baldwin contracted to sell Cox 2,000 tons of potatoes to be grown on Baldwin's farm in Boise, Idaho. Without any fault on Baldwin's part, a disease destroyed his entire potato crop. Cox sued Baldwin for breach of contract alleging that Baldwin breached by not delivering the potatoes. Could Baldwin successfully maintain that his nonperformance was excused?

1. What was the event that led to Baldwin's failure to perform the contract, was this event expected or unexpected, and did it occur after contract formation?
2. Did the occurrence of this event render Baldwin's performance of the contract impossible?
3. Was the risk of Baldwin's nonperformance due to the occurrence of the unexpected event allocated either by contract or by custom?
4. Was the nonoccurrence of this unexpected event a basic assumption on which the contract was made?

Would it make any difference if the contract had not specified that the potatoes were to be raised on Baldwin's farm?

Unexpected events making performance of the contract impossible may take the form of illness, physical incapacity, or death.

PARALEGAL EXERCISE 10.6 In January, Howard contracted to perform in Roxy's motorcycle stunt show. The first show was scheduled for the end of February. In early February, Howard broke both his legs in a skiing accident. Roxy sued Howard for breach of contract alleging that Howard breached by not performing in her stunt show. Could Howard successfully maintain that his nonperformance was excused?

1. What was the event that led to Howard's failure to perform the contract, was this event expected or unexpected, and did it occur after the contract was formed?
2. Did the occurrence of this event render Howard's performance of the contract impossible?
3. Was the risk of Howard's nonperformance due to the unexpected event allocated either by contract or by custom?
4. Was the nonoccurrence of this unexpected event a basic assumption on which the contract was made?

Death or serious illness excuses performance when a contract specifically calls for personal performance by the party who is unable to perform. When a contracting party's death or illness does not affect the performance of the contract, the failure to perform will be a breach and not an excused nonperformance.

PARALEGAL EXERCISE 10.7 Brent contracted to sell his car to Susan, who made a \$500 down payment. Brent died in a boating accident before the date he was to deliver his car to Susan. When Susan tendered Brent's executor the total purchase price under the contract, the executor refused to deliver Brent's car to Susan.

Susan sued Brent's estate for breach of contract alleging that Brent breached by not delivering the car. Could Brent's executor successfully maintain that his nonperformance was excused?

1. What was the event that led to Brent's failure to perform the contract, was this event expected or unexpected, and did it occur after the contract was formed?
2. Did the occurrence of this event render Brent's performance of the contract impossible?
3. Was the risk of Brent's nonperformance due to the unexpected event allocated either by contract or by custom?
4. Was the nonoccurrence of this unexpected event a basic assumption on which the contract was made?

A change in law may excuse both parties to the contract. Where a previously lawful contractual duty has become illegal after contracting, both contracting parties are excused so long as the nonperforming party did not contract to bear the risk of loss.

PARALEGAL EXERCISE 10.8 On January 15, Hudson Bay Pelts Company of Toronto, Canada, contracted to sell 2,400 lamb pelts to American Woolen Company of Philadelphia, Pennsylvania. The contract required Hudson Bay to ship the pelts by railroad from Toronto to Philadelphia on February 20. On February 1, a United States agency outlawed the importation of lamb pelts.

American sued Hudson Bay for breach of contract alleging that Hudson Bay breached by not delivering the pelts. Could Hudson Bay successfully maintain that its nonperformance was excused?

1. What was the event that led to Hudson Bay's failure to perform the contract, was this event expected or unexpected, and did it occur after the contract was formed?
2. Did the occurrence of this event render Hudson Bay's performance of the contract impossible?
3. Was the risk of Hudson Bay's nonperformance due to the unexpected event allocated either by contract or by custom?
4. Was the nonoccurrence of this unexpected event a basic assumption on which the contract was made?

Impracticability

The Restatement (Second) of Contracts does not include a provision entitled "impossibility" but uses the term "impracticability" as inclusive of impossibility. Restatement (Second) of Contracts § 261, Discharge by Supervening Impracticability, provides:

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.

Therefore, because this section uses the term "impracticability" rather than "impossibility," a party may be excused from the performance of his or her duty even though the unexpected event has not made performance impossible. Restatement (Second) of Contracts § 261, comment d, explains its use of the term "impracticability."

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.

Impracticability will excuse nonperformance only when the event is so unusual and unexpected that the performance under the new conditions is entirely different from the performance anticipated at the time of contract formation. The analysis set forth in the preceding section on impossibility, with only slight modification, also applies to impracticability. The modification must take into consideration that the performance in an impracticability case need not be impossible.

PARALEGAL EXERCISE 10.9 Mason Company contracted with Brady to take all the gravel needed for a construction project from Brady’s land. After taking 50,000 cubic yards of gravel from Brady’s land, the Mason Company discovered that there was not enough gravel on Brady’s land without having to dredge and dry gravel that was underwater. Because the cost of dredging and drying the gravel would have been twelve times the cost of buying dry gravel elsewhere, the Mason Company purchased 57,000 cubic yards of gravel from a third party.

Brady sued the Mason Company for breach of contract alleging that Mason breached by not taking all its gravel requirements from Brady’s land. Could Mason successfully maintain that its nonperformance was excused?

1. What was the event that led to Mason’s failure to perform the contract, was this event expected or unexpected, and did it occur after the contract was formed?
2. Did the occurrence of this event render Mason’s performance of the contract impracticable?
3. Was the risk of Mason’s nonperformance due to the unexpected event allocated either by contract or by custom?
4. Was the nonoccurrence of this unexpected event a basic assumption on which the contract was made?

PARALEGAL EXERCISE 10.10 Weebo Manufacturing Company, a firm specializing in space-age technological equipment, contracted with the Army to develop a heat-sensitive device designed to locate nuclear-powered submarines. Midway through the project, Weebo encountered technical difficulties resulting in unexpectedly heavy production costs far in excess of any profits it would make under the contract. Weebo notified the Army that it could not develop the heat-sensitive

device. The Army then contracted with the Space Age Corporation for the development of the heat-sensitive device at a contract price of five times the Weebo contract.

The Army sued the Weebo Company for breach of contract alleging that Weebo breached by not producing the heat-sensitive device. Could Weebo successfully maintain that its nonperformance was excused?

1. What was the event that led to Weebo's failure to perform the contract, was this event expected or unexpected, and did it occur after the contract was formed?
2. Did the occurrence of this event render Weebo's performance of the contract impracticable?
3. Was the risk of Weebo's nonperformance due to the unexpected event allocated either by contract or by custom?
4. Was the nonoccurrence of this unexpected event a basic assumption on which the contract was made?

Frustration of Purpose

Frustration of purpose cases involve an unexpected event that destroys the whole reason for the contract. Even though performance of the contract is still possible, courts may excuse nonperformance on the theory of failure of consideration.

EXAMPLE 10-8

An illustration is the famous English case of *Krell v. Henry*, [1903] 2 K.B. 740 (C.A.). Krell owned a suite of rooms overlooking the parade route for the coronation procession of King Edward VII. Krell contracted to lease his suite to Henry for the purpose of viewing the coronation procession. Shortly before the coronation, the King became ill and the coronation was indefinitely postponed. When Henry refused to pay Krell the balance due on the lease, Krell sued Henry. The court excused Henry's nonperformance. Although the nonhappening of the coronation did not prevent either Krell from renting the suite or Henry from paying Krell the contract price, the postponement of the coronation destroyed the value of the use of Krell's rooms to Henry during the contract period.

With a few minor variations, the analysis used for impossibility and impracticability can be useful in understanding the frustration of purpose cases:

1. Did an unexpected event occur after the contract was formed?
2. Did the occurrence of the unexpected event frustrate the purpose of the contract, destroying the value of performance to the promisee?
3. Was the risk of the promisee's frustration due to the unexpected event allocated either by contract or by custom?

4. Was the nonoccurrence of this unexpected event, which frustrated the promisee's purpose of the contract, a basic assumption on which the contract was made?

PARALEGAL EXERCISE 10.11 The summer Olympic games were scheduled for the week of July 1 in Dallas, Texas. On May 1, in anticipation of the summer Olympic games, the California T-Shirt Company contracted to purchase 500,000 T-shirts bearing the Olympic logo from Channing Enterprises. On May 20, a multinational boycott resulted in cancellation of the summer games. The California T-Shirt Company notified Channing not to ship the T-shirts.

Channing sued California for breach of contract alleging that California breached by canceling its order. Could California successfully maintain that its nonperformance was excused?

1. What was the event that led to California's failure to perform the contract, was this event expected or unexpected, and did it occur after the contract was formed?
2. Did the occurrence of the unexpected event frustrate the purpose of the contract, destroying the value of the performance to California?
3. Was the risk of California's frustration of purpose due to the unexpected event allocated either by contract or by custom?
4. Was the nonoccurrence of this unexpected event, which frustrated California's purpose of the contract, a basic assumption on which the contract was made?

PARALEGAL EXERCISE 10.12 In June, XYZ Communications contracted to lease a building from Jackson for five years for the purpose of selling satellite dishes. On December 1, the FCC declared the use of satellite dishes by homeowners illegal. XYZ ceased operating and moved out of the building.

Jackson sued XYZ for breach of contract alleging that XYZ breached by canceling its lease. Could XYZ successfully maintain that its nonperformance was excused?

1. What was the event that led to XYZ's failure to perform the contract, was this event expected or unexpected, and did it occur after the contract was formed?
2. Did the occurrence of the unexpected event frustrate the purpose of the contract, destroying the value of performance to XYZ?
3. Was the risk of XYZ's frustration of purpose due to the unexpected event allocated either by contract or by custom?
4. Was the nonoccurrence of this unexpected event, which frustrated XYZ's purpose of the contract, a basic assumption on which the contract was made?

Restitution as a Cause of Action When Nonperformance of the Contract Is Excused

The “no breach, excuse” response is an admission of nonperformance and a denial of breach. “I am not performing, but my nonperformance is excused.” Without a breach of the contract, the plaintiff’s remedies for the defendant’s breach of contract are unavailable.

Situations may arise in which the contract calls for the plaintiff to perform first. The plaintiff begins performance when suddenly an event occurs that terminates the plaintiff’s duty to continue performance. The defendant is not called upon to perform because the plaintiff must fully perform first. The performance of the contract comes to a standstill. Neither party has breached the contract. What about the performance the plaintiff has already conferred on the defendant? If the defendant is able to retain this benefit without compensating the plaintiff, will the defendant be unjustly enriched?

As a general rule when a contractor finds it impossible to complete performance under a construction contract due to the destruction of the structure, the contractor may be entitled to an action of restitution for the value of the work that had been done prior to the destruction.

EXAMPLE 10–9

Bell owned a building used as a cafe. He hired Carver Air Conditioning Company to install a heating and air conditioning unit in the building. Before Carver could complete the installation, Bell’s building was destroyed by fire. The heating and air conditioning unit also was destroyed. Bell refused to pay the contract price.

If Carver sued Bell for breach of contract alleging that Bell breached by not paying, Bell could successfully respond that his nonperformance was excused due to the fire. Therefore, Carver could not maintain a breach of contract cause of action.

Carver could successfully sue Bell in a restitution cause of action for unjust enrichment. Carver conferred a benefit on Bell (the heating and air conditioning unit and the labor involved in the installation) and it would be unjust for Bell to retain the unit and labor without compensating Carver.

In *Stein v. Shaw*, an attorney contracted with a client to file a negligence action on her behalf to recover damages for personal injuries. The client agreed to pay the attorney one-third of any recovery. After the attorney instituted suit and began negotiating a settlement, he was disbarred. The disbarment action was unrelated to this client. The client found herself another attorney, and her suit was ultimately settled for \$4,950. Is the disbarred attorney entitled to recover in a breach of contract action? If not, why? Is the disbarred attorney entitled to recover in a restitution action and, if so, how much?



CASE

Stein v. Shaw

Supreme Court of New Jersey, 1951.
6 N.J. 525, 79 A.2d 310.

Vanderbilt, C. J.

The plaintiff, an attorney at law, entered into a verbal agreement with the defendant to institute a suit in her behalf for the recovery of damages for personal injuries allegedly sustained by another's negligence. Under this agreement the plaintiff was to receive one-third of any recovery. He instituted suit and opened negotiations for a settlement, both of which were pending at the time he was disbarred from the practice of law for reasons not connected in anywise with the prosecution of the defendant's suit. After the plaintiff's disbarment other attorneys were substituted for him and the defendant's suit was subsequently settled for \$4,950. The defendant refused to pay the plaintiff and he then commenced this action against her, seeking in the first count to recover \$1,028 as the reasonable value of his services and disbursements, and in the second count to recover on his contingent fee contract one-third of the amount of the settlement. On the defendant's motion the trial court dismissed the complaint for failure to state a cause of action. From this judgment the plaintiff appealed to the Appellate Division of the Superior Court and we have certified the appeal here on our own motion.

We are of the opinion that the plaintiff should be permitted to recover in quasi contract for the reasonable value of his services rendered and disbursements made prior to his disbarment, for otherwise the defendant will be unjustly enriched at the expense of the plaintiff. To deprive an attorney of his claim for any and all compensation for services rendered prior to his disbarment when the services are not involved in the unprofessional conduct occasioning disciplinary action, would be inequitable. There is no sound reason in law or morals for permitting the defendant to use the plaintiff's disbarment as an escape from paying him for services rendered or necessary disbursements made by him in her behalf. Article VI, Section II, paragraph 3 of the Constitution imposes on this court the duty to discipline members of the bar for the protection of society, the legal profession and the courts in preserving the due administration of justice in the State, but its exercise does not affect either civil or criminal actions by or against the attorney disciplined by the court.

If the rule were otherwise, the effect of disciplinary action would inevitably be retroactive, which is not the intent or purpose in imposing discipline. The court, moreover, would never know the extent of such retroactive punishment without an undesirable inquiry as to the extent of the attorney's pending business and the monetary value thereof. It is unthinkable that punishment should be inflicted by a court so unintelligently. There are matters, however, which should not be considered by the committees on ethics and grievances appointed by us in the several counties to aid us by investigating complaints against members of the bar and by making presentments to us where the situation requires, nor should such matters be before us in imposing discipline. Our duty of safeguarding the integrity of the bar and of keeping the fountain of justice unpolluted is sufficiently difficult and delicate as it is without further complicating it with any such extraneous matters which should in all fairness be considered in imposing discipline, if the attorney's right to bring suit for services rendered is to be impaired by us. Disbarment is not a form of outlawry. To bring economic considerations into disciplinary proceedings would not only needlessly complicate them, but would in many instances serve to defeat the essential purpose thereof.

We are aware of *Davenport v. Waggoner*, 49 S.D. 592, 207 N.W. 972, 45 A.L.R. 1126 (S.Dak.1926) and *In re Woodworth*, 85 F.2d 50 (2nd Cir.1936) which hold to the contrary, but we cannot subscribe to the theory on which they are premised, that withdrawal from a suit by reason of disbarment constitutes a voluntary abandonment of the contract without just cause. Such is actually not the fact in those cases. The contract was not voluntarily abandoned, it was automatically terminated by operation of law, when the order of the court made further performance impossible. While the plaintiff was disbarred because of his own wrongful acts, so far as this defendant is concerned he is guiltless. It is pure fiction to say that he has intentionally and without cause abandoned his contract with her. While the analogy is not complete, the effect on the client of an attorney's disbarment is the same as that in the case of *Justice v. Lairy*, 19 Ind.App. 272, 49 N.E. 459 (Ind.App.1898), where an attorney accepted appointment to the bench and was thereby prohibited from the further practice of law. In either situation the attorney's disability is the result of conduct wholly unrelated to his client's case. In our opinion the situation resulting here from the plaintiff's disbarment is not dissimilar to that when an attorney is incapacitated by reason of death, illness or insanity. In such cases it has been uniformly held that because of his inability to perform the contract is discharged, but that the attorney may nevertheless recover in quasi contract for the reasonable value of the services rendered, 45 A.L.R. 1135, 1158. Nor is recovery in quasi contract here barred by virtue of the express contract for a contingent fee, for as we have indicated that contract was discharged by operation of law when its performance was rendered impossible by the plaintiff's disbarment.

The fact that the defendant was compelled by virtue of the plaintiff's disbarment to retain other counsel to prosecute her claim is, of course, to be considered in determining the reasonable value of the plaintiff's services. In no event, however, should the plaintiff's recovery exceed the amount stipulated for in his express agreement less whatever reasonable sum the defendant paid other counsel to complete the case. While the express contract has been discharged and cannot serve as the measure of recovery, it does operate as a limit on the amount of the recovery in quasi contract, 6 Williston on Contracts (Rev.Ed.1938) § 1977, p. 5557; Woodward, *The Law of Quasi Contracts* (1913) § 125, p. 197.

In view of the conclusions we have reached, it becomes unnecessary to consider the other questions raised by the plaintiff. The judgment appealed from is reversed and the cause remanded for further proceedings in accordance with this opinion.

For reversal: Chief Justice VANDERBILT, and Justices CASE, HEHER, OLIPHANT, BURLING and ACKERSON—6.

For affirmance: Justice WACHENFELD—1.

WACHENFELD, J. (dissenting).

In *In re Woodworth*, D.C., 15 F.Supp. 291, 293, affirmed 85 F.2d 50 (C.C.A. 2, 1936), the court held: "On principle it cannot be doubted that when an attorney makes an agreement to prosecute a case for a fee contingent on success and is disbarred before the fee is earned, he may not collect compensation from his client for the work done. The agreed fee he cannot have, because he has not performed his engagement and the contingency on which the compensation was to rest has not happened. Reasonable compensation in lieu of the fee he cannot have, because his inability to complete his contract has been brought about by his own wrongful conduct."

I subscribe to this reasoning and conclusion and am therefore to affirm.

Adopting this rule would not complicate or bring economic considerations into disciplinary proceedings nor would it defeat their purpose. It would, in my opinion, be an added incentive to professional conduct, which is foreign to disciplinary complaints.

Admittedly, the plaintiff was disbarred because of his own wrongful act, and whether it was with reference to this particular case or not, the result, in my opinion, is the same.

The penalty falls and he can no longer represent his client because of his wrongful conduct. The result of that misconduct should be uniform, not varying with the degree of culpability or its relationship to any particular case.

“His inability to complete his contract has been brought about by his own wrongful conduct.”

I would affirm the judgment.

NO BREACH, JUSTIFICATION

The defendant’s third response to the plaintiff’s allegation of breach is “No breach, although I am not complying with the terms of the contract, my nonperformance was justified by your breach of this contract (see Figure 10–5).” (“Your breach justified my nonperformance.”)

My nonperformance of the contract was justified by your breach of the contract. Therefore, you are the breaching party and not I.

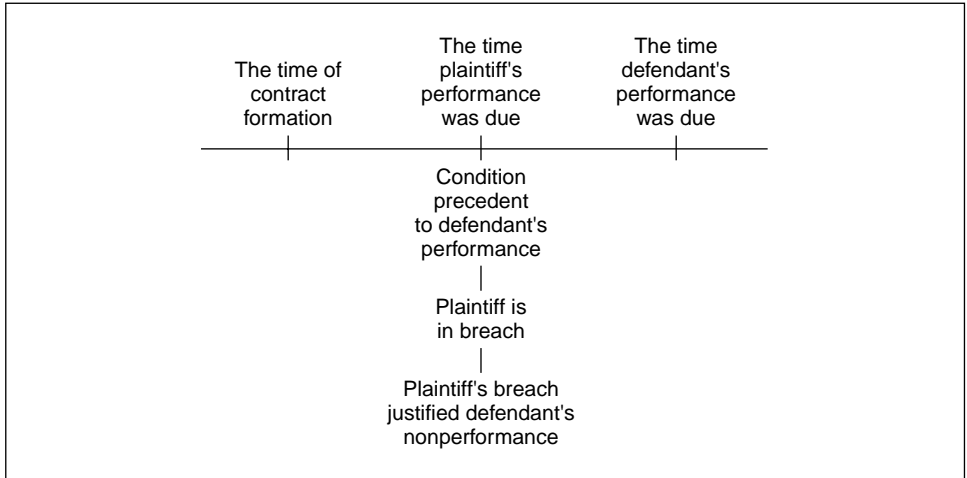
This response couples the defendant’s admission of nonperformance with the claim that the nonperformance was justified by a breach by the plaintiff. Unlike the “no breach, excuse” response, which was based on a supervening external event (an act of God or a governmental regulation), the “no breach, justification” response is based on the action of the other contracting party. The defendant is *not* responding “My breach is justified by your breach.” The defendant, although not admitting breach, is only admitting nonperformance. An admission of nonperformance is not the same as an admission of breach. *The defendant’s nonperformance is not a breach.* Because the plaintiff rather than the defendant is the breaching party, the plaintiff cannot maintain a breach of contract action against the defendant.

A careful analysis of the justification response reveals that the defendant must prove the following:

1. Both the plaintiff and the defendant had duties to perform.
2. The plaintiff’s performance was a condition precedent to the defendant’s performance.
3. The plaintiff was in breach of his or her duty to perform.
4. The magnitude of the plaintiff’s breach of his or her duty justified the defendant’s nonperformance of his or her duty.

FIGURE 10-5 Answer—Defendant's "No Breach, Justification" Response to the Plaintiff's Allegation of Defendant's Breach

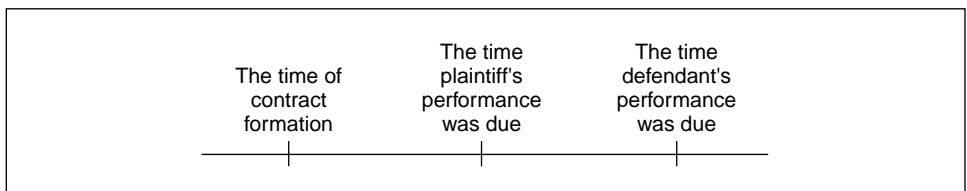
IN THE DISTRICT COURT OF [NAME] COUNTY STATE OF [NAME]		
[NAME], dba [Name])	
)	
Plaintiff,)	
)	
v.)	Case No. _____
)	
[NAME], a [Name of State])	
corporation)	
)	
Defendant.)	
ANSWER OF DEFENDANT [NAME]		
Defendant [name] alleges the following in response to the complaint:		
<ol style="list-style-type: none"> 1. Defendant admits the allegations of paragraph 1 of the complaint. 2. Defendant admits the allegations of paragraph 2 of the complaint. 3. Defendant admits the allegations of paragraph 3 of the complaint. 4. Defendant admits the allegations of paragraph 4 of the complaint. 5. Defendant denies that all conditions precedent have occurred as alleged in paragraph 5 of the complaint in that payment was conditioned on the Defendant presenting a completed marketing plan and the presented marketing plan was substantially incomplete. 6. Defendant denies the allegations of paragraph 6 that it breached the contract in that Plaintiff's breach by presenting an incomplete marketing plan justified Defendant's not paying. 7. The complaint fails to state a claim against Defendant upon which relief can be granted. 		
Accordingly, Defendant demands that Plaintiff take nothing by this Action, and that Defendant be awarded costs including reasonable attorney fees.		
	[Attorney's name signed] [Attorney's name typed] Attorney for defendant [Bar membership number] [Address] [Telephone number]	



This section explores these four elements of the justification response. If the defendant established these elements, he or she was justified in not performing the contract and was not in breach. Therefore, the plaintiff cannot maintain a breach of contract action. Even if the plaintiff cannot maintain a breach of contract cause of action, The plaintiff, who has conferred a benefit on the nonbreaching defendant could maintain a restitution action against the nonbreaching defendant. This section considers restitution as an action for the breaching plaintiff.

The Plaintiff and the Defendant Have Duties to Perform

The first step in the “justification response” is establishing that both the plaintiff and the defendant had duties to perform. The plaintiff must have a duty to perform and must have failed to perform this duty to justify the defendant’s claim that his or her nonperformance was justified by the plaintiff’s nonperformance of a contractual duty.



The Plaintiff's Performance Was a Condition Precedent to the Defendant's Performance

For the defendant to claim a justification response, its performance must be dependent on the plaintiff's performance. If the defendant's performance is independent of the plaintiff's performance, the justification response will fail. Under modern contracts law, performances are presumed to be dependent.

PARALEGAL EXERCISE 10.13 Dwayne contracted to paint Robin's portrait for Robin's promise to pay Dwayne \$1,000, with \$200 down and the balance in \$100 weekly installments. Although the painting would take about three weeks, a time was not set for its completion.

Are painting and paying independent or dependent performances?

The defendant's performance must be dependent not only on the plaintiff's performance, but the plaintiff's performance must occur first. The plaintiff's performance must be a condition precedent to the defendant's performance.

EXAMPLE 10-10

Tom contracted with Gary for the remodeling of Tom's kitchen. The contract required Tom to purchase the materials and Gary to do the carpentry. Tom's buying of the materials is a condition precedent to Gary's duty to remodel. If Tom does not buy materials, Gary will be unable to remodel the kitchen.

PARALEGAL EXERCISE 10.14 Karen hired Stacy to tutor her in Latin. Is Karen's duty to pay a condition precedent to Stacy's tutoring, or is Stacy's tutoring a condition precedent to Karen's duty to pay?

The Plaintiff Was in Breach

The third step in the "justification response" is establishing that the plaintiff has breached the contract. If the plaintiff has not breached, the defendant's justification response will not succeed.

PARALEGAL EXERCISE 10.15 The Ace Painting Company contracted to paint Erica's apartment for \$1,500. Erica contracted to supply the paint. When Ace arrived to paint Erica's apartment, Erica refused to provide Ace with the paint and demanded that Ace supply the paint. Ace refused and ultimately did not paint Erica's apartment. Erica then hired Russell to paint and paid Russell \$2,000.

Erica sued Ace for breach of contract alleging Ace breached by not painting her apartment. Ace responded, "No breach, justification. My nonperformance—not painting—was justified by your breach—not supplying the paint."

Did Erica breach the contract by not supplying the paint? Will Ace's justification response succeed?

Entire and Divisible Performances A contract may require one performance or a number of performances. An **entire contract** is a contract with a single performance.

EXAMPLE 10-11

"I promise to sell you Flora, the elephant, for your promise to pay \$1,500."

A **divisible contract** is a contract with separate or installment performances.

EXAMPLE 10-12

"I promise to sell you Flora, the elephant, for your promise to pay \$1,500, in two monthly payments of \$750 each."

EXAMPLE 10-13

"I promise to sell you two elephants, Flora and Sally, one to be delivered this fall and the other next spring, for your promise to pay \$1,500 each."

Whether a performance of a contract is entire (one performance) or divisible (multiple performances) may affect when the plaintiff breached the contract. If the performance is divisible, the plaintiff may have breached some of the later performances, although not some of the earlier ones. If the plaintiff has not breached an early performance, the defendant may not withhold the performance that corresponds to the plaintiff's performance.

EXAMPLE 10–14

Consider the last elephant example. Suppose Seller delivered the first elephant in the fall but refused to deliver the second in the spring. Seller did not breach the fall delivery, but Seller did breach the spring delivery. If each elephant was to be paid for separately, Buyer could not refuse to pay for the first elephant because Seller had not breached delivery of the first elephant.

PARALEGAL EXERCISE 10.16 The Orion Timber Company contracted to sell the Juniper Lumber Company twenty truckloads of freshly harvested trees (five truckloads of oak, five of maple, and ten of white pine). The contract provided that Juniper would pay \$20,000 for each truckload of oak, \$15,000 for maple, and \$10,000 for pine. Orion delivered the maple and pine but did not deliver the oak. Juniper accepted the delivery of the maple and pine but subsequently refused to pay for the maple and pine because it did not receive the oak.

Orion sued Juniper for breach of contract. Answer the following:

1. What did Orion allege was Juniper's breach?
2. If Juniper responded with a "justification response," what specifically did it say?
3. Did Orion breach the contract?
4. Was Orion's performance entire or divisible?
5. What difference to the question of breach does the answer to the previous question make?

Waiver of a Breach Even if the plaintiff has breached the contract, the defendant might not be able to use the plaintiff's breach in its justification response if the defendant has waived the breach.

EXAMPLE 10–15

Albert hired the Countryside Landscape Company to landscape Blackacre for \$2,400. When Countryside finished the job after a week, Albert was dissatisfied with what it had done. Countryside offered to redo some of the work, but Albert said that he was so disgusted, he would take it as it was. When Albert received Countryside's bill for \$2,400, he refused to pay it.

Countryside sued Albert for breach of contract alleging that Albert did not pay. Albert responded, "No breach, justification. My not paying was justified by your breach—not performing the work satisfactorily." Countryside responded by claiming that Albert waived Countryside's breach by accepting the work.

PARALEGAL EXERCISE 10.17 The Horizon Construction Company received the prime contract to build a government building in Baltimore. The contract called for facing the building in Vermont marble. Horizon contracted with the Old Maine Stone Company for all of the Vermont marble that Horizon would need. Old Maine delivered New Hampshire, instead of Vermont, marble. The marbles were similar, and Horizon knew when it accepted the shipment that it was New Hampshire and not Vermont marble. Horizon incorporated the marble into the structure. When the building was completed, the government refused to accept it unless the marble was changed to Vermont marble. Horizon refused to pay Old Maine.

When evaluating whether Old Maine could successfully sue Horizon for breach of contract, consider:

1. What would Old Maine allege as Horizon's breach?
2. What would Horizon respond to Old Maine's allegation of breach (i.e., complete the details for a "no breach, justification" response)?
3. What would Old Maine respond to Horizon's "no breach, justification" response (i.e., has Horizon waived Old Maine's breach)?

Estoppel In addition to waiver, the defendant may be estopped (precluded) from claiming that the plaintiff has breached. Unlike waiver, which requires no action by the breaching party, estoppel requires that the breaching party rely on the nonbreaching party's actions.

EXAMPLE 10-16

Suppose in the landscape example, Albert had watched Countryside perform the work and had stated dissatisfaction only after the work had been completed. Even if Countryside had been in breach, Albert had said nothing. Countryside relied on Albert's inaction. Albert is estopped from later raising Countryside's breach.

PARALEGAL EXERCISE 10.18 Paralegal Exercise 10.17, suppose that Old Maine had notified Horizon before shipping that it was New Hampshire rather than Vermont marble and Horizon did not object. Should Horizon be estopped from objecting after the government refuses to accept the building?

The Magnitude of the Plaintiff's Breach Justified the Defendant's Nonperformance

The defendant may not use just any breach by the plaintiff to justify his or her nonperformance. The plaintiff's breach must be of sufficient magnitude. If the contract is a construction contract, the plaintiff's performance must be less than

“substantial performance.” If the contractor has substantially performed but did not fully perform, the owner will not be justified in nonperforming (not paying).

PARALEGAL EXERCISE 10.19 Beautiful Homes, Inc., contracted to build a house for the Culvers. Beautiful Homes promised to complete the home in ninety days, and the Culvers were to pay in four installments—25 percent at the time of signing the contract and 25 percent at the end of each month thereafter. At the end of ninety days, Beautiful Homes had the house completed except for exterior painting. Has Beautiful Homes substantially performed the contract?

If the contract is for employment rather than for construction, the language changes from “substantial performance” to “immaterial breach.” An employee’s immaterial breach will not justify the employer’s nonperformance (nonpayment), even though the employee has not fully performed.

PARALEGAL EXERCISE 10.20 The Modern Sign Company hired Alvin to solicit sign orders from businesses in town. The contract provided that Alvin would be paid \$500 a month plus commissions. The salary was to be paid at the end of each month. After working for Modern Sign for three weeks, Alvin quit without giving the two weeks’ notice required in his contract.

Was Alvin’s breach material or immaterial?

If the contract is for the sale of goods, the Uniform Commercial Code governs. If the performance under evaluation relates to the goods and not to the payment and if the goods are not authorized to be shipped in several deliveries, the Code (UCC § 2–601) authorizes the buyer to reject the goods that fail to conform to the contract in any respect. This is known as the perfect tender rule. UCC § 2–601 states the consequences when goods do not comply with the perfect tender rule:

- ... if the goods or the tender of delivery fail in any respect to conform to the contract, the buyer may
- (a) reject the whole; or
 - (b) accept the whole; or
 - (c) accept any commercial unit or units and reject the rest.

EXAMPLE 10–17

John and Carol ordered a \$200 wedding cake from the Elite Bakery to be delivered on April 19 at 5 P.M. Elite prepared the cake and delivered it to John and Carol’s reception at 5 P.M. on April 19. As the cake was being placed on the table by Elite, the bride’s mother noticed that the inscription read “John and Alice.”

The cake fails to conform to the contract and can be rejected.

Although the buyer's right to reject nonconforming goods appears absolute in section 2-601, the buyer's right is subject to a number of limitations. First, if the contract is an installment contract, then section 2-612 rather than section 2-601 applies. Perfect tender of goods in an installment is no longer required. UCC § 2-612 states:

(1) An "installment contract" is one which requires or authorizes the delivery of goods in separate lots to be separately accepted, even though the contract contains a clause "each delivery is a separate contract" or its equivalent.

(2) The buyer may reject any installment which is non-conforming if the non-conformity substantially impairs the value of that installment and cannot be cured or if the non-conformity is a defect in the required documents; but if the non-conformity does not fall within subsection (3) and the seller gives adequate assurance of its cure the buyer must accept the installment.

(3) Whenever non-conformity or default with respect to one or more installments substantially impairs the value of the whole contract there is a breach of the whole. But the aggrieved party reinstates the contract if he accepts a non-conforming installment without seasonably notifying of cancellation or if he brings an action with respect only to past installments or demands performance as to future installments.

EXAMPLE 10-18

Buyer contracts to buy 300,000 tons of coal to be delivered in three shipments of 100,000 tons each on the first day of three consecutive months. The first shipment is only 75,000 tons. Because this was an installment contract (three deliveries), Buyer cannot reject the shipment unless the shortage substantially impairs the value of that installment and the shortage cannot be cured. Furthermore, if the shortage does not substantially impair the value of the whole contract and if Seller gives adequate assurance of its cure, Buyer must accept the shipment even though it is 25,000 tons short.

Second, if the buyer exercises his or her power under section 2-601 and rejects a nonconforming tender, the seller may have a right to correct the non-conformity. This is known in the Code as the seller's right to "cure." The seller does not have a right to cure in all situations but only in the following situations discussed in section 2-508:

(1) Where any tender or delivery by the seller is rejected because non-conforming and the time for performance has not yet expired, the seller may seasonably notify the buyer of his intention to cure and may then within the contract time make a conforming delivery.

(2) Where the buyer rejects a non-conforming tender which the seller had reasonable grounds to believe would be acceptable with or without money allowance the seller may if he seasonably notifies the buyer have a further reasonable time to substitute a conforming tender.

EXAMPLE 10–19

Buyer contracted to purchase steel I beams from Seller with delivery by November 1. Seller delivered the beams on October 7. Buyer inspected, found the beams did not conform to the contract specifications, and rejected them (UCC § 2–601). Because the time for performance has not yet expired (time for performance expires on November 1), Seller could seasonably notify Buyer of its intention to cure (UCC § 2–508(1)) and would have until November 1 to make a conforming delivery.

Consider the following case of *Wilson v. Scampoli*:

1. Is this a UCC § 2–508(1) or a UCC § 2–508(2) case?
2. What is the difference?
3. If the seller decides to cure, must the seller replace the goods delivered?

**CASE*****Wilson v. Scampoli***

United States Court of Appeals, District of Columbia Circuit, 1967.
228 A.2d 848.

Before HOOD, Chief Judge, MYERS, Associate Judge, and QUINN (Associate Judge, Retired).

MYERS, Associate Judge.

This is an appeal from an order of the trial court granting rescission of a sales contract for a color television set and directing the return of the purchase price plus interest and costs.

Appellee purchased the set in question on November 4, 1965, paying the total purchase price in cash. The transaction was evidenced by a sales ticket showing the price paid and guaranteeing ninety days' free service and replacement of any defective tube and parts for a period of one year. Two days after purchase the set was delivered and uncrated, the antennae adjusted and the set plugged into an electrical outlet to "cook out."¹ When the set was turned on however, it did not function properly, the picture having a reddish tinge. Appellant's delivery man advised the buyer's daughter, Mrs. Kolley, that it was not his duty to tune in or adjust the color but that a service representative would shortly call at her house for that purpose. After the departure of the delivery men, Mrs. Kolley unplugged the set and did not use it.²

On November 8, 1965, a service representative arrived, and after spending an hour in an effort to eliminate the red cast from the picture advised Mrs. Kolley that he would have to remove the chassis from the cabinet and take it to the shop as he could not determine

1. Such a "cook out," usually over several days, allows the set to magnetize itself and to heat up the circuit in order to indicate faulty wiring.

2. Appellee, who made his home with Mrs. Kolley, had been hospitalized shortly before delivery of the set. The remaining negotiations were carried on by Mrs. Kolley, acting on behalf of her father.

the cause of the difficulty from his examination at the house. He also made a written memorandum of his service call, noting that the television "Needs Shop Work (Red Screen)." Mrs. Kolley refused to allow the chassis to be removed, asserting she did not want a "repaired" set but another "brand new" set. Later she demanded the return of the purchase price, although retaining the set. Appellant refused to refund the purchase price, but renewed his offer to adjust, repair, or, if the set could not be made to function properly, to replace it. Ultimately, appellee instituted this suit against appellant seeking a refund of the purchase price. After a trial, the court ruled that "under the facts and circumstances the complaint is justified. Under the equity powers of the Court I will order the parties put back in their original status, let the \$675 be returned, and the set returned to the defendant."

Appellant does not contest the jurisdiction of the trial court to order rescission in a proper case, but contends the trial judge erred in holding that rescission here was appropriate. He argues that he was always willing to comply with the terms of the sale either by correcting the malfunction by minor repairs or, in the event the set could not be made thereby properly operative, by replacement; that as he was denied the opportunity to try to correct the difficulty, he did not breach the contract of sale or any warranty thereunder, expressed or implied.³

D.C.Code § 28:2-508 (Supp. V, 1966) provides:

(1) Where any tender or delivery by the seller is rejected because non-conforming and the time for performance has not yet expired, the seller may seasonably notify the buyer of his intention to cure and may then within the contract time make a conforming delivery.

(2) Where the buyer rejects a non-conforming tender which the seller had reasonable grounds to believe would be acceptable with or without money allowance the seller may if he seasonably notifies the buyer have a further reasonable time to substitute a conforming tender.

A retail dealer would certainly expect and have reasonable grounds to believe that merchandise like color television sets, new and delivered as crated at the factory, would be acceptable as delivered and that, if defective in some way, he would have the right to substitute a conforming tender. The question then resolves itself to whether the dealer may conform his tender by adjustment or minor repair or whether he must conform by substituting brand new merchandise. The problem seems to be one of first impression in other jurisdictions adopting the Uniform Commercial Code as well as in the District of Columbia.

Although the Official Code Comments do not reach this precise issue, there are cases and comments under other provisions of the Code which indicate that under certain circumstances repairs and adjustments are contemplated as remedies under implied warranties. In *L & N Sales Co. v. Little Brown Jug, Inc.*, 12 Pa. Dist. & Co. R. 2d 469 (Phila. County Ct. 1957), where the language of a disclaimer was found insufficient to defeat warranties under §§ 2-314 and 2-315, the court noted that the buyer had notified the seller of defects in the merchandise, and as the seller was unable to remedy them and later refused to accept return of the articles, it was held to be a breach of warranty.

...

3. Appellee maintains that the delivery of a color television set with a malfunctioning color control is a breach of both an implied warranty of merchantability (D.C.Code § 28:2-314 (Supp. V, 1966)) and of an implied warranty of fitness for a particular purpose (D.C.Code § 28:2-315 (Supp. V, 1966)) and as such is a basis for the right to rescission of the sale. We find it unnecessary to determine whether a set sold under the circumstances of this case gives rise to an implied warranty of fitness for a particular purpose or whether, as appellant contends, the remedial provisions of the express warranties bind the buyer to accept these same remedial provisions as sole remedies under an implied warranty.

While these cases provide no mandate to require the buyer to accept patchwork goods or substantially repaired articles in lieu of flawless merchandise, they do indicate that minor repairs or reasonable adjustments are frequently the means by which an imperfect tender may be cured.

Removal of a television chassis for a short period of time in order to determine the cause of color malfunction and ascertain the extent of adjustment or correction needed to effect fully operational efficiency presents no great inconvenience to the buyer. In the instant case, appellant's expert witness testified that this was not infrequently necessary with new televisions. Should the set be defective in workmanship or parts, the loss would be upon the manufacturer who warranted it free from mechanical defect. Here the adamant refusal of Mrs. Kolley, acting on behalf of appellee, to allow inspection essential to the determination of the cause of the excessive red tinge to the picture defeated any effort by the seller to provide timely repair or even replacement of the set if the difficulty could not be corrected. The cause of the defect might have been minor and easily adjusted or it may have been substantial and required replacement by another new set—but the seller was never given an adequate opportunity to make a determination.

We do not hold that appellant has no liability to appellee,⁴ but as he was denied access and a reasonable opportunity to repair, appellee has not shown a breach of warranty entitling him either to a brand new set or to rescission. We therefore reverse the judgment of the trial court granting rescission and directing the return of the purchase price of the set.

Reversed.

4. Appellant on appeal has renewed his willingness to remedy any defect in the tender, and thus there is no problem of expiration of his warranties. He should be afforded the right to inspect and correct any malfunction. If appellee refuses to allow appellant an opportunity to do so, then no cause of action can lie for breach of warranty, express or implied, and the loss must be borne by appellee.

Third, the buyer's right to reject nonconforming goods under section 2-601 can be contracted away by the buyer. Section 2-601 expressly authorizes this consensual release of the power:

Subject to the provisions of this Article on breach in installment contracts (Section 2-612) and *unless otherwise agreed under the sections on contractual limitations of remedy (Sections 2-718 and 2-719)*, if the goods or the tender of delivery fail in any respect to conform to the contract, the buyer may

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

In these cases, the contracting parties will, at the time of contract, agree on what remedies will be available in the event the goods do not conform to the contract. Section 2-718(1) provides for liquidated damages:

(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.

Section 2–719 discusses the contractual modification and limitation of remedies:

- (1) Subject to the provisions of subsections (2) and (3) of this section and of the preceding section on liquidation and limitation of damages,
 - (a) the agreement may provide for remedies in addition to or in substitution for those provided in this Article and may limit or alter the measure of damages recoverable under this Article, as by limiting the buyer's remedies to return of the goods and repayment of the price or to repair and replacement of non-conforming goods or parts; and
 - (b) resort to a remedy as provided is optional unless the remedy is expressly agreed to be exclusive, in which case it is the sole remedy.
- (2) Where circumstances cause an exclusive or limited remedy to fail of its essential purpose, remedy may be had as provided in this Act.
- (3) Consequential damages may be limited or excluded unless the limitation or exclusion is unconscionable. Limitation of consequential damages for injury to the person in the case of consumer goods is prima facie unconscionable but limitation of damages where the loss is commercial is not.

Restitution as an Action for the Breaching Plaintiff

Because a breach of contract action is an action against a breaching party and since the plaintiff rather than the defendant is the breaching party, if the defendant is successful in its “no breach, justification” response, the plaintiff has no cause of action against the defendant for breach of contract. The breaching plaintiff may, however, maintain a cause of action in restitution against the nonbreaching defendant if the plaintiff has conferred a benefit on the defendant and it would be unjust to permit the defendant to retain that benefit without compensating the plaintiff.

PARALEGAL EXERCISE 10.21 Bradley, incarcerated for murder, hired Murphy as his legal counsel. Bradley paid Murphy \$4,000 as an advance for legal services to be rendered in his defense. Before Murphy could render any legal services, Bradley committed suicide. Bradley's estate demanded that Murphy return the \$4,000, and Murphy refused.

If Bradley's estate sues Murphy for breach of contract, what would be the allegation of breach? What would be Murphy's response to this allegation of breach? Could the estate recover in a breach of contract action?

Could Bradley's estate successfully sue Murphy in a restitution action? What benefit did Bradley confer on Murphy? Would it be unjust to permit Murphy to retain this benefit without compensating Bradley's estate?

Today, one of the more important questions dealing with the breaching plaintiff is whether the breaching purchaser of real property can recover payments made to the seller before the purchaser's breach. Although the majority position is that restitution will not be granted, a number of jurisdictions have

adopted a minority view allowing recovery and the perceptible trend is away from the rigidity of the majority rule.

If the contract were for the sale of goods, the courts would give restitutionary relief to a breaching seller. Before the enactment of the UCC, the majority of courts treated a breaching buyer of goods the same as a breaching purchaser of real property. In both cases, a majority of courts refused to give the breaching buyer restitutionary relief. Under section 2-718 of the UCC, the breaching buyer has gained some rights. Section 2-718 requires the seller to return to the buyer so much of the deposit or down payment as exceeds the damages that the seller in fact sustains. This reverses pre-Code authority, which generally regarded a buyer's willful refusal to take proper goods as forfeiting the right to the return of the down payment.

Courts are split three ways over whether a contractor who has not substantially performed may recover in a restitution action for benefits conferred on the nonbreaching owner.

- Some courts apparently reject restitution as a cause of action in these cases.
- Some courts permit restitution but only if the contractor's breach was not willful or "voluntary."
- Some courts permit restitution even where the contractor is guilty of a willful breach of court.

If a court does permit the breaching contractor to maintain a restitution action and the contractor's costs exceed the value conferred, the contractor's recovery will be limited to the actual value to the defendant rather than the contractor's cost of construction.

NO BREACH, TERMINATED DUTY

The defendant's fourth response to the plaintiff's allegation of breach is "No breach, although I am not complying with the terms of the contract, my duty to perform the contract has been terminated" (see Figure 10-6).

I am not in breach. I no longer have to perform according to the contract. My obligation no longer exists due to some duty terminating occurrence.

The "no breach, terminated duty" response couples the defendant's admission of nonperformance with a claim that his or her contractual duty has ended either by agreement or by law and therefore the defendant is not in breach of contract. The terminating event may be a part of the contract (condition subsequent) or external to the contract. If external, the terminating occurrence may be consensual (substitute contract, accord and satisfaction, or novation), unilateral (waiver), or by operation of law (statute of limitations). Because the defendant is not the breaching party, the plaintiff cannot maintain a breach of contract action against the defendant.

FIGURE 10-6 Answer—Defendant’s “No Breach, Duty Terminated” Response to the Plaintiff’s Allegation of Defendant’s Breach

IN THE DISTRICT COURT OF [NAME] COUNTY
STATE OF [NAME]

[NAME], dba [Name])	
)	
Plaintiff,)	
)	
v.)	Case No. _____
)	
[NAME], a [Name of State])	
corporation)	
)	
Defendant.)	

ANSWER OF DEFENDANT [NAME]

Defendant [name] alleges the following in response to the complaint:

1. Defendant admits the allegations of paragraph 1 of the complaint.
2. Defendant admits the allegations of paragraph 2 of the complaint.
3. Defendant admits the allegations of paragraph 3 of the complaint.
4. Defendant admits the allegations of paragraph 4 of the complaint.
5. Defendant admits the allegations of paragraph 5 of the complaint.
6. Defendant denies the allegations of paragraph 6 and alleges that after the alleged breach of the agreement and before the filing of this action, Defendant delivered to Plaintiff and Plaintiff accepted \$ [dollars] in full satisfaction of Plaintiff’s claim.
7. The complaint fails to state a claim against Defendant upon which relief can be granted.

Accordingly, Defendant demands that Plaintiff take nothing by this Action, and that Defendant be awarded costs including reasonable attorney fees.

[Attorney’s name signed]
 [Attorney’s name typed]
 Attorney for defendant
 [Bar membership number]
 [Address]
 [Telephone number]

Unlike with the “no breach, compliance,” “no breach, justification,” and “no breach, excuse” responses, a restitution action is not available with the “no breach, terminated duty” response.

Condition Subsequent Terminates the Duty

A duty may be terminated by the occurrence of a condition subsequent. A **condition subsequent** is a duty terminating event.

EXAMPLE 10–20

“I promise to play tennis with you today unless it rains.” Rain is the event that ends the duty to play tennis. The promisor has a duty to play tennis up until the time it rains.

Consensual Termination of a Duty

A contractual duty may be terminated by the consent of the contracting parties. Consent will involve a contractual relationship with all the trappings of consideration. Such contracts as the substitute contract, the accord and satisfaction, and the novation illustrate termination by consent, we have or will discuss each in detail in another part of this text: substitute contract (see Chapter 5); accord and satisfaction (see Chapter 5); and novation (see Chapter 12).

Unilateral Termination of a Duty

A contractual duty may also be terminated by a unilateral act by the party to whom the duty is owed, the promisee. Such a termination may take the form of a waiver.

Termination of a Duty by Operation of Law

A contractual duty may also be terminated by operation of law. An illustration is the statute of limitations.

PARALEGAL EXERCISE 10.22 Ultrasound Electronics Company contracted to purchase twenty-five TVs from Sound Warehouse, a wholesaler, for the 1996 Christmas season. Although the TVs were to be delivered by November 1, 1996, they were actually delivered on January 15, 1997, too late for Christmas.

On March 1, 2000, Ultrasound filed a breach of contract action against Sound Warehouse, alleging as breach the late delivery. If the statute of limitations for breach of contract actions is three years, could Sound Warehouse answer the allegation of breach with the “no breach, terminated duty” response?

BREACH

If the defendant is unsuccessful in using any of the four responses discussed in this chapter, he or she has little alternative but to admit the plaintiff’s allegation that the contract has been breached is true (see Figure 10–7).

Yes, I admit I breached the contract.

The law of contracts does not evaluate the mental state accompanying non-performance. Because an intentional breach will have the same significance as an unintentional breach, a contracting party may intentionally breach a contract if not performing the contract is in his or her best economic interest.

PARALEGAL EXERCISE 10.23 Johnson, a fashion designer, contracted to work for Top Line Fashions for one year at \$20,000 a month. After working for Top Line for two months, Johnson received an offer to work for The Ultra, another fashion designer, for \$25,000 a month. Top Line replaced Johnson with Swanson at a salary of \$22,000 a month.

Was Johnson’s breach of contract financially beneficial to her? Did it matter whether her breach was intentional or unintentional?

If the conclusion from the Fourth Step of the analysis is “breach,” the plaintiff has established a cause of action against the defendant for breach of contract. The plaintiff may now consider an appropriate remedy for the defendant’s breach.

If the defendant has breached the contract, the plaintiff may not seek an action in restitution even though he or she has conferred a benefit on the defendant. The plaintiff does not have the power to choose between a breach of contract action and a restitution action. The party who has conferred a benefit on the other is never in a position to elect which cause of action to pursue. A restitution action is not an alternative to a breach of contract action.

FIGURE 10-7 Answer—Defendant’s “Admission of Breach” Response to the Plaintiff’s Allegation of the Defendant’s Breach

IN THE DISTRICT COURT OF [NAME] COUNTY STATE OF [NAME]		
[NAME], dba [Name])	
)	
Plaintiff,)	
)	
v.)	Case No. _____
)	
[NAME], a [Name of State])	
corporation)	
)	
Defendant.)	
ANSWER OF DEFENDANT [NAME]		
Defendant [name] alleges the following in response to the complaint:		
1. Defendant admits the allegations of paragraph 1 of the complaint.		
2. Defendant admits the allegations of paragraph 2 of the complaint.		
3. Defendant admits the allegations of paragraph 3 of the complaint.		
4. Defendant admits the allegations of paragraph 4 of the complaint.		
5. Defendant admits the allegations of paragraph 5 of the complaint.		
6. Defendant denies the allegations of paragraph 6 of the complaint.		
7. Defendant denies the allegations of paragraph 7 of the complaint and alleges that Plaintiff did not sustain damages of any amount in excess of \$ [dollars] by reason of Defendant’s breach.		
Accordingly, Defendant demands that Plaintiff take nothing by this Action, and that Defendant be awarded costs including reasonable attorney fees.		
		[Attorney’s name signed] [Attorney’s name typed] Attorney for defendant [Bar membership number] [Address] [Telephone number]

PARALEGAL EXERCISE 10.24 The White Star Canning Company hired the Quality Paving Company to resurface its parking lots for \$12,000. After Quality had completed one half of the work (which was worth more to White Star than one half of the contract price), White Star terminated the contract without cause, thus breaching the contract. Could Quality successfully maintain a *restitution cause of action* against White Star, or would Quality have to maintain a *breach of contract action* against White Star?

The plaintiff, however, may seek a restitution remedy in a breach of contract action. The restitution sought in a breach of contract action is to protect a restitution interest, which is one of the three interests protected in a breach of contract action. This restitution remedy in a breach of contract action is not the same as a restitution remedy in a restitution action. The restitution remedy for a breach of contract action will be discussed in Chapter 11.



PARALEGAL CHECKLIST

The Defendant's Response to the Plaintiff's Allegation of Breach

- ❑ Once a contract has been formed and is enforceable, the supervising attorney will want the paralegal to focus on the alleged breach of the contract.
 1. What is the plaintiff-promisee alleging that the defendant-promisor did wrong?
 - a. Did the promisor fail to perform? or
 - b. Did the promisor notify the promisee that performance would not be forthcoming when it was due (i.e., breach by anticipatory repudiation)?

Whether the promisor's breach is intentional or unintentional is irrelevant. The law of contracts does not evaluate the mental state accompanying nonperformance.
 2. The fact that the plaintiff-promisee alleges the defendant-promisor breached the contract does not make it so. The defendant-promisor may respond: (a) no breach, compliance; (b) no breach, excuse; (c) no breach, justification; (d) no breach, terminated duty; or (e) yes, breach.
 - a. If the defendant-promisor responds no breach, compliance, he or she is saying "no breach, I am complying with the terms of the contract." Whether the defendant is in fact complying with the terms of the contract may

depend on whether: (1) the contract includes the duty the promisee alleges the promisor has breached (may raise parol evidence rule or mistake in integration problems); (2) the contract is interpreted according to the promisee's perception (patent and latent ambiguities and differing opinions as to the duty); or (3) the contractual duty has a condition precedent that has yet to occur. If the defendant has not breached the contract, the plaintiff has no cause of action for breach. A restitution action may be available if the plaintiff has unjustly enriched the defendant.

- b. If the defendant-promisor responds no breach, excuse, he or she is saying "no breach, although I am not complying with the terms of the contract, my nonperformance was excused." Unlike the "no breach, compliance" response, the defendant-promisor admits nonperformance. An event (an act of God or a third party) that was not an express term in the contract occurred and excused the nonperformance. The defendant's performance may be excused when performance is impossible or impracticable. The defendant's performance may also be excused if an unexpected supervening event destroyed the whole

- reason for the contract (frustration of purpose). If the defendant is not in breach, the plaintiff cannot maintain an action for breach of contract. A restitution action may be available if the defendant has been unjustly enriched at the plaintiff's expense.
- c. If the defendant-promisor responded no breach, justification, he or she is saying "no breach, although I am not complying with the terms of the contract, my nonperformance was justified by your breach of the contract." As with the "no breach, excuse" response, the defendant-promisor admits nonperformance. Unlike the "no breach, excuse" response, the defendant-promisor in this instance is not alleging an external event (act of God or a third party) but rather an act (or omission) of the other party as the reason for nonperformance. The allegation is, therefore, that the roles should be reversed. The plaintiff is actually the breaching party, and the defendant is the nonbreaching party. Carefully analyze the justification response to determine whether the defendant can prove:
- (1) Both the plaintiff and the defendant had duties to perform.
 - (2) The plaintiff's performance was a condition precedent to the defendant's performance.
 - (3) The plaintiff was in breach of his or her duty to perform.
 - (4) The magnitude of the plaintiff's breach of his or her duty justified the defendant's nonperformance of his or her duty.
- If the plaintiff, rather than the defendant, is the breaching party, the plaintiff cannot maintain a cause of action for breach of contract. A restitution action may be available if the defendant has been unjustly enriched at the plaintiff's expense.
- d. If the defendant-promisor responded no breach, terminated duty, he or she is saying "no breach, although I am not complying with the terms of the contract, my duty to perform the contract has been terminated." The terminating event may be a part of the contract (condition subsequent) or arise after the contract was formed. In the latter case, the terminating event may be consensual (substitute contract, accord and satisfaction or novation), unilateral (waiver), or by operation of law (statute of limitations). If the defendant is not a breaching party, the plaintiff cannot maintain an action for breach of contract.
- e. If the defendant-promisor responded, "Yes, I admit I breached my contractual duty," the plaintiff may proceed to the next step in the analysis—selection of remedies.

REVIEW QUESTIONS

DEFINE THE FOLLOWING NEW TERMS AND PHRASES

Breach by anticipatory repudiation	Divisible contract
Breach by failure to perform	Entire contract
Condition	Latent ambiguity
Condition precedent	Patent ambiguity
Condition subsequent	Supervening external event

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

1. T F The party who is alleged to have breached the contract is the promisee.
2. T F Sophia promised to teach Janet a new dance step for Janet's promise to pay Sophia \$40. Janet in turn promised to pay Sophia \$40 for Sophia's promise to teach Janet the new dance step. When the date of the first

- lesson came and went without Janet showing up for her lesson, Janet committed a breach by anticipatory repudiation.
3. T F A successful “no breach” response by the defendant to the plaintiff’s allegation of breach concludes the breach of contract action in the defendant’s favor.
 4. T F Although the no breach, compliance; no breach, excuse; and no breach, justification responses end the breach of contract action, a possibility of relief for unjust enrichment in a restitution action still exists.
 5. T F Even though a plaintiff has conferred a benefit on the defendant, the plaintiff may never pursue a restitution action.
 6. T F In a no breach, compliance response, the promisor admits to not performing according to the terms of the contract.
 7. T F A patent ambiguity becomes apparent only when information beyond the writing demonstrates that the terms have a double meaning.
 8. T F A latent ambiguity is apparent from the face of the writing.
 9. T F Patent ambiguities are often created by inexact pronoun references or misleading modifiers.
 10. T F The two ships *Peerless* case involved a patent ambiguity.
 11. T F A mistake made by the drafter in reducing the oral agreement to writing is called a mistake in the integration of the contract.
 12. T F If the writing is unambiguous it will always reflect the agreed upon terms.
 13. T F The writing should be reformed to reflect the true intent of the parties if their intent is clear and the writing was in error.
 14. T F A contingency is a condition that must be based on an external event.
 15. T F Conditions can be classified into four types.
 16. T F The performance of a promise that is a condition to the performance of another promise is called a “promissory condition.”
 17. T F A condition precedent is a duty terminating event.
 18. T F A condition subsequent is a duty creating event.
 19. T F Concurrent conditions occur when each promise is conditioned on the other and both must be performed simultaneously.
 20. T F The statement “I promise to pay you \$500 when my horse wins the race” contains a condition subsequent.
 21. T F Even if there has been no breach of contract, the remedies for breach of contract may still be available in certain situations.
 22. T F Even if there has been no breach of contract, restitution remedies in a restitution action may still be available in certain situations.
 23. T F If an external event prevents the promisor from performing, this nonperformance may be excused even though the external event was not an express term in the contract.
 24. T F Unexpected events making performance of the contract impossible may involve illness, physical incapacity, death, or destruction or unavailability of the subject matter of the contract.

25. T F Mohammed Marzook contracted to rent The Golden Pyramid, a restaurant, from Patsy Bennett for the purpose of having a wedding dinner. Shortly after the contract was signed and before the date of the dinner, lightning struck the restaurant damaging the interior. If Marzook sued Bennett for breach of contract alleging Bennett's failure to provide the restaurant, Bennett could respond "no breach, justification."
26. T F Under the Restatement (Second) of Contracts § 261 (1979), a party may be excused from nonperformance of his or her duty if it is impracticable to perform.
27. T F Impracticability means the same thing as impracticality.
28. T F A mere change in the degree or difficulty or expense will render performance impracticable.
29. T F Frustration of purpose involves an unexpected event that destroys the reason for the contract.
30. T F Courts may excuse nonperformance in frustration of purpose cases on the theory of failure of consideration even though performance of the contract is actually possible.
31. T F Restitution as a cause of action is not available when nonperformance of the contract is excused.
32. T F The "no breach, justification" response by the defendant is based on the action of the other contracting party rather than on an external event.
33. T F A restitution action is not available to the breaching plaintiff even if he or she has conferred a benefit on the nonbreaching defendant.
34. T F An admission of nonperformance is the same thing as an admission of breach.
35. T F Under the no breach, justification response, the defendant responds that my breach was justified by your breach.
36. T F The defendant's nonperformance may be justified by the plaintiff's breach of the contract.
37. T F An "entire contract" is a contract with a single performance while a "divisible contract" requires multiple performances.
38. T F The defendant may not be able to use the plaintiff's breach in its justification response if the defendant has waived the breach.
39. T F The defendant's performance must be independent of the plaintiff's performance for the defendant to claim a justification response.
40. T F The defendant may use any breach by the plaintiff, however small, to justify his or her nonperformance.
41. T F The plaintiff's performance in a construction contract must be less than "substantial performance" to justify the defendant's nonperformance.
42. T F An employee's "immaterial breach" will not justify the employer's nonperformance in an employment contract.
43. T F If the contract is for the sale of goods, UCC § 2-601 authorizes the buyer to reject the goods that fail to conform to the contract in any respect (the perfect tender rule).

44. T F Perfect tender of goods in an installment contract is not required by the UCC.
45. T F In some situations the seller of goods may have a right to “cure” (correct the nonconformity) if the buyer rejects a nonconforming tender.
46. T F The buyer may not contract away its right to reject nonconforming goods under UCC § 2-601.
47. T F The buyer’s right to reject goods is limited if the nonconformity deals with tender through a substitute carrier or in a substitute manner.
48. T F The buyer has an unlimited right to reject when the seller is required or authorized to send the goods to the buyer under a contract that does not require the seller to deliver the goods at a particular destination.
49. T F The breaching plaintiff may maintain a cause of action in restitution against the nonbreaching defendant if the plaintiff has conferred a benefit on the defendant, and it would be unjust to permit retention of that benefit without compensation.
50. T F A restitution action is available with the “no breach, terminated duty” response.
51. T F A contractual duty may be terminated by the consent of the contracting parties.
52. T F Consensual termination of a contractual duty will involve a contractual relationship with all the trappings of consideration.
53. T F A contractual duty may not be terminated by a unilateral act by the party to whom the duty is owed, the promisee.
54. T F A contractual duty may be terminated by operation of law such as by the statute of limitations.
55. T F The law of contracts evaluates the mental state accompanying nonperformance.
56. T F A contracting party may intentionally breach a contract if not performing the contract is in his or her best economic interest.
57. T F If the defendant has breached the contract, the plaintiff may not seek an action in restitution even though he or she has conferred a benefit on the defendant.
58. T F A restitution action can be an alternative to a breach of contract action.

FILL-IN-THE-BLANK QUESTIONS

1. _____. The defendant’s denial that he or she is not complying with the terms of the contract.
2. _____. An ambiguity that is sometimes apparent from the face of the writing.
3. _____. Does the following statement contain a patent or latent ambiguity? “The attorney told her paralegal that she needs more information concerning a certain client’s problem.”

4. _____. An ambiguity that may become apparent when information beyond the writing demonstrates that the term has a double meaning.
5. _____. Does the following statement contain a patent or latent ambiguity? "Buyer purchased 100 hogs from Seller." Buyer expected Tamworths but Seller sent Berkshires.
6. _____. A Latin term meaning that the terms of the contract should be strictly construed against the drafter.
7. _____. A rule that contract terms should be given their plain meaning.
8. _____. A Latin term meaning that general words that follow specific words should be limited to the same general kind or class as the specific words.
9. _____. A Latin term meaning that the enumeration of one thing implies the exclusion of those things not enumerated.
10. _____. The performance of a promise may be a condition to the performance of another promise.
11. _____. A duty creating event.
12. _____. A duty terminating event.
13. _____. Each promise is conditioned on the other and both must be performed simultaneously.
14. _____. Defendant admits not complying with the terms of the contract but asserts the nonperformance was excused and therefore not a breach.
15. _____. The result of the occurrence of an unexpected event that renders a party incapable of performing his or her contractual duties.
16. _____. The result of the occurrence of an unexpected event that renders performance of a contractual duty extremely difficult or expensive.
17. _____. The result of the occurrence of an unexpected event that destroys the whole reason for the contract.
18. _____. Defendant admits nonperformance but asserts the nonperformance was justified by the breach of the plaintiff.
19. _____. A contract with a single performance.
20. _____. A contract that requires multiple performances.
21. _____. Requires that the breaching party rely on the nonbreaching party's actions.
22. _____. A rule set forth in UCC § 2-601 authorizing the buyer to reject goods that fail to conform to the contract in any respect if the performance under evaluation relates to the goods and not to the payment and the contract is not an installment contract.
23. _____. Defendant admits not complying with the terms of the contract but asserts his or her duty to perform the contract has been terminated.

MULTIPLE CHOICE QUESTIONS (CIRCLE ALL THE CORRECT ANSWERS)

1. The following are maxims and rules of construction:
 - (a) *Contra perferentem*
 - (b) *Pari delicto*
 - (c) *Ejusdem generis*
 - (d) *E pluribus unum*
 - (e) *Expressio unius est exclusio alterius*
2. B.K. Georgescu contracted to purchase “Run Away,” a racehorse, from Jimmy WhiteEagle. “Run Away” was to be delivered after he competed in the Claremore Downs Futurity. During that race, “Run Away” was injured and was destroyed. If Georgescu sued WhiteEagle for breach of contract alleging that WhiteEagle breached by not delivering “Run Away,” WhiteEagle could respond:
 - (a) no breach, compliance
 - (b) no breach, excuse
 - (c) no breach, justification
 - (d) no breach, terminated duty
 - (e) admission of breach
3. Carter entered into a three-year contract to teach at Gotham University, beginning when the first-year class reached 1,000. Gotham notified Carter to begin teaching during the fall semester even though the first-year class reached only 950. When Carter did not show up for fall semester, Gotham filed a breach of contract action alleging that Carter breached by not showing up to teach. Carter’s response to Gotham’s allegation of breach is:
 - (a) no breach, compliance
 - (b) no breach, excuse
 - (c) no breach, justification
 - (d) no breach, terminated duty
 - (e) admission of breach
4. A-1 Electronics contracted to build a superconducting supercollider for the United States government. The contract provided that the U.S. could cancel the contract by giving 30 days notice and paying 10% of the contract price. Before A-1 could begin performance, the U.S. sent notice along with a check for 10% of the contract price. If A-1 sued the U.S. alleging that the U.S. breached the contract by sending notice, the U.S. could respond:
 - (a) no breach, compliance
 - (b) no breach, excuse
 - (c) no breach, justification
 - (d) no breach, terminated duty
 - (e) admission of breach
5. A-1 Electronics contracted to build a superconducting supercollider for the United States government. The contract provided that the U.S. could cancel the contract by giving 30 days notice and paying 10% of the contract price. A-1 began to build

the supercollider but found that it would cost twenty times what had been expected. If A-1 notified the U.S. that it could not continue to build and the U.S. sued A-1 alleging that A-1 breached by discontinuing building, A-1 could respond:

- (a) no breach, compliance
 - (b) no breach, excuse
 - (c) no breach, justification
 - (d) no breach, terminated duty
 - (e) admission of breach
6. The Brighton High School contracted to rent the Grand Hotel's ballroom for its Senior Prom. Several days before the night of the prom, a flu epidemic spread through the high school and the prom was canceled. If the Hotel sued the High School alleging it breached by canceling the contract, the High School could respond:
- (a) no breach, compliance
 - (b) no breach, excuse
 - (c) no breach, justification
 - (d) no breach, terminated duty
 - (e) admission of breach
7. Hiram Novak contracted with Quality Builders for the construction of a family room to be added to his house. After about a third of the construction had been completed, Quality left the job. When Quality demanded pro rata payment, Novak refused. If Quality sued Novak for breach of contract alleging nonpayment, Novak could respond:
- (a) no breach, compliance
 - (b) no breach, excuse
 - (c) no breach, justification
 - (d) no breach, terminated duty
 - (e) admission of breach

SHORT ANSWER QUESTIONS

1. Explain how a condition precedent, a condition subsequent, and a concurrent condition differ.
2. Describe the steps to be taken when evaluating a "no breach, justification" response.
3. Distinguish a "no breach, compliance" from a "no breach, justification" response.

PART

V

**Step Five: Plaintiff's Remedies for
the Defendant's Breach of Contract**

INTRODUCTION

Compensation for Breach

CHAPTER 11

Plaintiff's Remedies for the Defendant's Breach of Contract

INTRODUCTION

Compensation for Breach

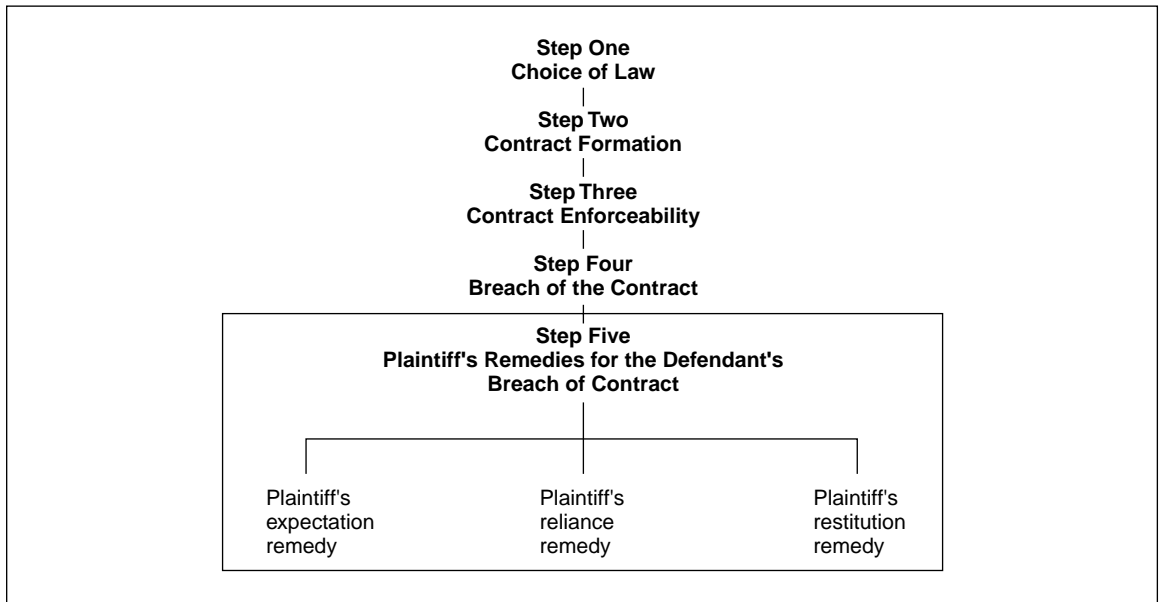
Once an enforceable contract has been breached, the nonbreaching party may successfully maintain an action for breach of contract and is entitled to a remedy for the breach. The nonbreaching party may seek redress for the breach but may not seek punitive damages. In most cases, the nonbreaching party will receive a judgment awarding money damages as a substitute for what was promised. The nonbreaching party will seldom be awarded specific goods or services. Also in most cases, the nonbreaching party will be compensated for what he or she expected to receive under the contract (expectation damages). This places the nonbreaching party in the position he or she would have been in had the contract been fully performed. Although the nonbreaching party generally fares best with compensation based on lost expectation, compensation based on reliance or restitution may, at times, exceed compensation based on contract expectations. The reliance remedy for breach of contract will compensate the nonbreaching party for his or her costs incurred while relying on the breaching party's promise. The reliance remedy returns the nonbreaching party to the position he or she was in prior to relying on the breaching party's promise. The restitution remedy for breach of contract will compensate the nonbreaching party for any benefit that he or she conferred on the breaching party for which it would be unjust to permit the breaching party to retain without compensating the nonbreaching party. The restitution remedy returns the breaching party to the position he or she was in prior to receiving the benefit from the nonbreaching party. Chapter 11 explores the nonbreaching party's expectation, reliance, and restitution remedies for a breach of contract cause of action.



Plaintiff's Remedies for the Defendant's Breach of Contract

- ◆ Plaintiff's Expectation, Reliance, and Restitution Remedies for the Defendant's Breach of Contract
 - Expectation Remedy for Breach of Contract*
 - Reliance Remedy for Breach of Contract*
 - Restitution Remedy for Breach of Contract*
- ◆ The Unavailability of Restitution as a Cause of Action for the Nonbreaching Plaintiff
 - When the Defendant Has Breached the Contract

If an enforceable contract is breached, the nonbreaching party is entitled to a remedy for the breach. This remedy may involve expectation, reliance, or restitution. These three remedies are examined in this chapter. Also considered is the question of why the nonbreaching party may not pursue a restitution cause of action when a breach of contract action is available (see Figure 11-1).

FIGURE 11–1 The Plaintiff's Remedies for Defendant's Breach Phase of the Road Map

PLAINTIFF'S EXPECTATION, RELIANCE, AND RESTITUTION REMEDIES FOR THE DEFENDANT'S BREACH OF CONTRACT

Expectation Remedy for Breach of Contract

When parties contract, they have expectations about what their net gains will be once the contract is performed. The parties have perceptions of the value of what they had promised to give and the value of what they had been promised in return. Protecting the nonbreaching party's **expectation interest** places the nonbreaching party in the position he or she would have been in had the contract been fully performed by *both parties* according to its terms.

To move the nonbreaching party to the position he or she would have been in had the contract been fully performed requires two calculations. First, the nonbreaching party must receive what he or she expected to receive. Second, the nonbreaching party must give what he or she expected to give in return. These two calculations represent both elements of an offer and both elements of an acceptance.

EXAMPLE 11-1

Offer: "I promise to work for your promise to pay."
 Acceptance: "I promise to pay for your promise to work."

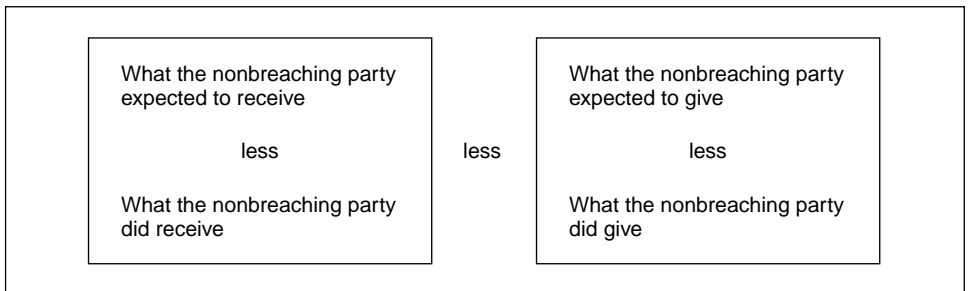
If the offeror completes the work but the offeree does not pay, the offeree has breached the contract. Under the expectation remedy, the offeror is moved to the point of full performance when he or she receives the pay that the offeree had promised. Nothing need be subtracted from the offeror's recovery because the offeror has fully performed.

If the offeror completes almost all the work and the offeree does not pay, the offeree has breached the contract. Under the expectation remedy, the offeror is moved to the point of full performance when he or she receives the pay that the offeree had promised less the value of the work left unperformed.

If, on the other hand, the offeree prepays but the offeror does not work, the offeror has breached the contract. Under the expectation remedy, the offeree is moved to the point of full performance when he or she receives the value of the offeror's work. Nothing need be subtracted from the offeree's recovery because the offeree has fully performed.

If the offeree prepays most of what he or she was obligated to pay and the offeror does not work, the offeror has breached the contract. Under the expectation remedy, the offeree is moved to the point of full performance when he or she receives the value of the offeror's work less the payment he or she has not paid.

The formula for an expectation reads: *[(what the nonbreaching party expected to receive) less (what the nonbreaching party did receive)] less [(what the nonbreaching party expected to give) less (what the nonbreaching party did give)]*.

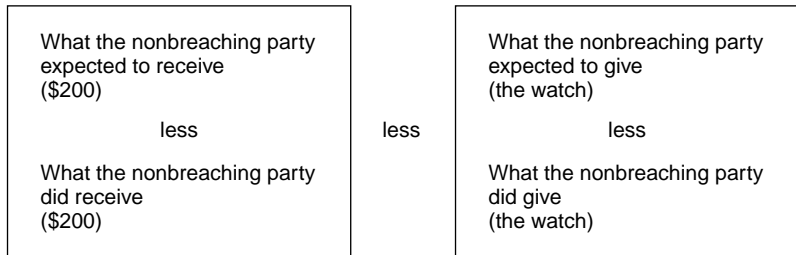


The diagram is useful in visualizing the expectation remedy formula. The left-hand box is the "receiving" box. What the nonbreaching party expected to receive and what the nonbreaching party did receive. The difference between "what the nonbreaching party expected to receive" and "what the nonbreaching party did receive" is what the nonbreaching party must receive to be brought

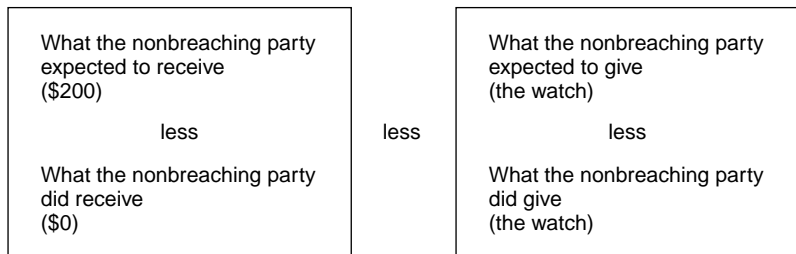
to full performance on the receiving side. The right-hand box is the “giving” box. What the nonbreaching party expected to give and what the nonbreaching party did give. The difference between “what the nonbreaching party expected to give” and “what the nonbreaching party did give” is what the nonbreaching party must give to full performance on the giving side. The expectation remedy requires the nonbreaching party to receive what he or she expected to receive and to give what he or she expected to give in return.

EXAMPLE 11-2

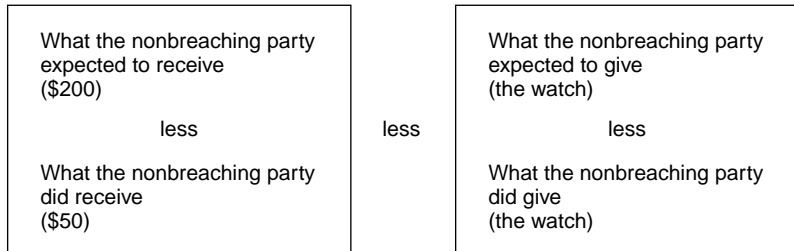
Suppose Andrew contracted to sell his watch to Bently for Bently’s promise to pay Andrew \$200. Andrew expected to receive \$200 and to give Bently his watch. If Andrew receives \$200 and gives Bently the watch, the contract is fully performed.



If Andrew receives \$0 but gives Bently the watch, it would take \$200 to place Andrew where he would have been had the contract been fully performed by Bently.

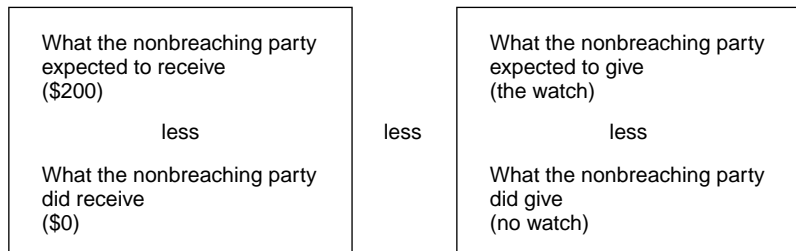


If Andrew receives \$50 but gives the watch, it would take \$150 to place him at the point of full performance.



Andrew also must give what he expected to give. If he expected to give the watch and does give Bently the watch, then Andrew has given what he expected to give. But if Andrew did not give Bently the watch, Andrew must compensate Bently for the nondelivery of the watch.

Andrew would need to compensate Bently for the difference between what Andrew expected to give and what he did give.



Compensatory Damages The nonbreaching party's damages are compensatory damages. **Compensatory damages** are intended to compensate the nonbreaching party for not receiving his or her expectation under the contract. The nonbreaching party will be brought up to full performance, no more and no less. Therefore, punitive damages are not awarded in breach of contract actions. **Punitive damages** are monetary awards that punish the breaching party. The breaching party is not held up to the public as an example of what might happen if a party breaches.

The fact that damages for breach of contract do not include punitive damages is consistent with the fact that the intentions of the breaching party are irrelevant. Intentional and unintentional breaches will result in the same measure of expectation damages. Therefore, a contracting party may find

breaching a contract to be in his or her best economic interest. Breaching a contract and paying expectation damages may place the breaching party in a better economic position than performing the contract.

EXAMPLE 11-3

The ABC Painting Company contracted to paint Smith's house for \$3,000. Before beginning to paint, ABC breached the Smith contract so it could paint the First Bank Building. First Bank contract is for \$12,000. Smith hired Quality Painters for \$3,500. If Smith sues ABC for breach of contract, she will recover \$500, the additional amount it would cost her to have her house painted. ABC may be more than willing to pay Smith \$500 if it can make substantially more on the First Bank contract.

In some situations, it may be difficult to decide what will place the injured party in the position he or she would have been in had the contract been fully performed. In construction contracts, the issue is whether the injured party is entitled to the cost to replace (or to repair) or to only the diminished value of the subject of the contract.

EXAMPLE 11-4

Contractor built Owner a house but mislocated an interior wall by one foot. After the house was completed, Owner discovered Contractor's error. The mislocation does not change the value of the house. Contractor has breached the contract by not building according to the blueprints.

Is Owner entitled to the cost to relocate the wall or to only the diminished value of the house with the mislocated wall? Unless there was some overriding reason why the house was unacceptable with the mislocated wall, a relocation of the wall would have created "economic waste." A court will generally award Owner only the diminished value of the house attributable to the mislocation.

PARALEGAL EXERCISE 11.1 The Allegheny Coal Company leased ranch land from the Bar Z Ranch for the purpose of strip mining coal. The contract provided that Allegheny would reclaim the land (restore the surface) after it had completed strip mining. At the end of the lease term, Allegheny left the mining site without reclaiming the land. The value of the land would be \$50 an acre if not reclaimed and \$600 an acre if reclaimed. Reclaiming the land would cost \$900 an acre. Should the Bar Z Ranch be entitled to the diminished value of the land or the cost to reclaim? Consider the policy arguments supporting each position.

Damages for breach of contract are limited to those that the breaching party could reasonably foresee at the time of the making of the contract as the probable result of such a breach. Foreseeable damages are either general or special damages. The classic case of *Hadley v. Baxendale*, 9 Ex. 341, 156 Eng. Rep. 145 (1854), stated the rule of foreseeability as:

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.

General damages “arise naturally, i.e., according to the usual course of things, from such breach of contract itself.” In a contract for the sale of goods:

1. What are the buyer’s normal damages if the seller breaches by refusing to deliver the goods?
2. What are the seller’s normal damages if the buyer breaches by refusing to accept delivery of the goods?

In a contract for employment:

1. What are the employee’s normal damages if the employer breaches by wrongfully discharging her?
2. What are the employer’s normal damages if the employee breaches by wrongfully leaving the job?

Special damages do not “arise naturally, i.e., according to the usual course of things, from such breach of contract itself.” **Special damages** are those that “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.” Because they may reasonably be supposed to have been in the contemplation of both parties, they are foreseeable.

PARALEGAL EXERCISE 11.2 The Hunter Hotel Corporation contracted with Apex Construction Company for renovation of the hotel. The contract provided September 1 as the completion date for the renovation. Apex did not complete the renovation until October 1, and as a result, the hotel lost a convention that it scheduled during the week of September 15. Is the Hunter Hotel entitled to recover the lost profits for the convention?

Whether a nonbreaching party can recover damages for pain and suffering and emotional distress in a breach of contract action is a question of foreseeability. Generally, damages for pain and suffering or for emotional distress are not available in a breach of contract action. In some instances, recovery can be awarded for pain and suffering or emotional distress if they were the natural

result of the breach (i.e., within the contemplation of the parties at the time the contract was made).

Damages for breach of contract must be shown with reasonable certainty. Damages that are speculative and incapable of being ascertained with reasonable certainty are not recoverable. Although damages must be certain, mathematical exactness is not required.

PARALEGAL EXERCISE 11.3 Assume in Paralegal Exercise 11.2 that Apex knew at the time of contracting that the Hunter had a convention scheduled for September 15 and that if the renovation was not completed before that date, the Hunter would lose the convention and the accompanying profits. Is the Hunter entitled to recover the lost profits for the convention?

In the event of breach, the nonbreaching party has a duty to mitigate the damages. **Mitigation** requires the nonbreaching party to use reasonable means to avoid or minimize damages. Mitigation may take different forms. In some situations, the doctrine prevents the nonbreaching party from increasing the amount the breaching party must pay.

In a construction contract, the contractor is entitled to the contract price upon completion of the structure. If the owner breaches the contract before the contractor begins to build, the contractor is entitled to its profits (contract price less the expected cost to build the structure). If the owner breaches after the contractor begins to build but before the structure is complete, the contractor is entitled to the contract price less the amount it saved by not having to complete the structure. If the contractor ignores the owner's notice not to complete the structure, the contractor cannot increase the amount due on the contract by continuing to build.

PARALEGAL EXERCISE 11.4 Broken Arrow Construction Company contracted to build a school building for the Oologah School District for \$4,500,000. At the time of contract formation, the contractor estimated that it would cost \$4 million in labor and materials to complete the work.

1. Calculate the Construction Company's damages if the School District breaches the contract before the Construction Company begins to build.
2. Calculate the Construction Company's damages if the School District breaches the contract after the Construction Company has begun to build. At this time, the contractor has spent \$1,500,000 on labor and materials and anticipates spending another \$2,750,000 to complete the work.
3. Calculate the Construction Company's damages if instead of stopping the work when the School District wrongfully ordered it to do so, the Construction Company completed the school.

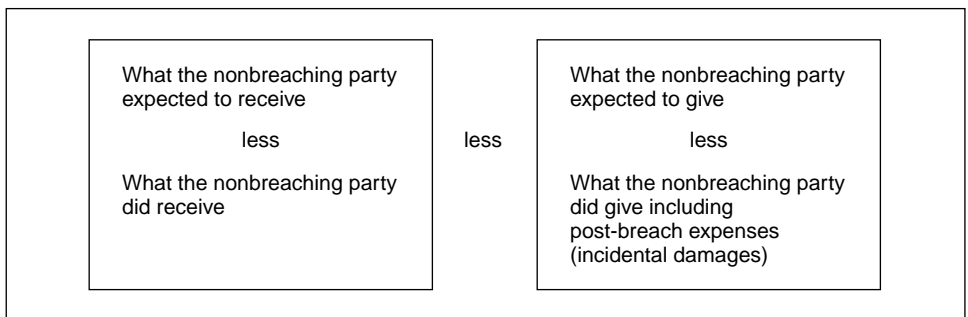
In other situations, the doctrine of mitigation requires the nonbreaching party to decrease the amount of damages the breaching party must pay. In an employment contract, a wrongfully terminated employee must attempt to use his or her saved time productively by seeking substitute employment. If the employee does use this saved time by taking another job, the money earned from the new job will be subtracted from the money the employee expected to earn under the original contract. If the employee does not take another job but should have taken it, the money that could have been earned from the new job will be subtracted from the money the employee expected to earn under the original contract.

PARALEGAL EXERCISE 11.5 The *Daily News* hired Brenda under a one-year contract to write the local news. After three months, Brenda was wrongfully discharged. The *Chronicle*, a rival newspaper, learned of Brenda's discharge and offered her a nine-month contract at 90 percent of her salary with the *Daily News*.

In determining Brenda's damages for the *Daily News*'s breach of contract, must her salary with the *Chronicle* be subtracted from her expected salary with the *Daily News* if she accepts the *Chronicle*'s offer?

Must the salary offered by the *Chronicle* be subtracted from Brenda's expected salary with the *Daily News* if she does not accept the *Chronicle*'s offer?

Incidental Damages The bottom portion of the right-hand box includes that which has been given pursuant to the contract and post-breach expenses incurred by the nonbreaching party to salvage the contract, retrieve or protect the goods, or otherwise mitigate damages. **Incidental damages** are post-breach expenses.



In a contract for the sale of goods, the seller's incidental damages (UCC § 2-710) include:

any commercially reasonable charges, expenses or commissions incurred in stopping delivery, in the transportation, care and custody of goods after the buyer's breach, in connection with return or resale of the goods or otherwise resulting from the breach.

The buyer's incidental damages (UCC § 2-715) include:

expenses reasonably incurred in inspection, receipt, transportation and care and custody of goods rightfully rejected, and commercially reasonable charges, expenses or commissions in connection with effecting cover and any other reasonable expense incident to the delay or other breach.

Nominal Damages If the nonbreaching party establishes a breach of contract but is unable to prove damages, it is entitled to nominal damages. **Nominal damages** are a trifling sum awarded when the plaintiff does not prove actual damages. A judgment for nominal damages, while not compensating the nonbreaching party in dollars and cents, clarifies the rights and duties of the parties and may include an award of court costs.

Injunction At times, damages may not totally compensate the nonbreaching party for his or her injury. The circumstances may be such that future injuries will occur. An **injunction** orders the breaching party to refrain from further action.

EXAMPLE 11-5

A research chemist is hired by Green Farm, a farm fertilizer company, and as a part of the employment contract, she promises not to work for another farm fertilizer company for two years after she ends her employment with Green Farm. After working for Green Farm for several years, the chemist quits and begins to work for another farm fertilizer company. While Green Farm is entitled to damages for the chemist's breach of her covenant not to compete, damages will not protect Green Farm from loss of its secrets that the chemist could reveal to her new employer. If the court precludes the chemist from working for her new employer for the remainder of the covenant's term, Green Farm would be better protected. This court order precluding the chemist from working for her new employer is known as an injunction.

Specific Performance **Specific performance** mandates delivery of the thing. Specific performance is available only when the remedy of damages would be inadequate. If the seller, in a contract for the sale of goods, refuses to deliver, specific performance may be available if the goods are unique and thus are not easily replaceable on the market.

What the nonbreaching party
expected to receive
(goods)

less

What the nonbreaching party
did receive
(no goods)

less

What the nonbreaching party
expected to give
(the contract price)

less

What the nonbreaching party
did give
(nothing)

PARALEGAL EXERCISE 11.6 Blue Grass Stables contracted to sell Neal's Diamond, an outstanding three-year-old thoroughbred and winner of the triple crown, to California Meadows, a breeding syndicate. Prior to the delivery date, Blue Grass notified California Meadows that it had decided to race Neal's Diamond for another year and would not deliver him to the syndicate.

1. Could California Meadows find a substitute horse on the market to replace Neal's Diamond?
2. Would damages (money) be an adequate remedy for California Meadows?
3. Would specific performance be an appropriate remedy?

Specific performance is not available when the breach is the failure to pay money. Money is interchangeable and not unique. Specific performance is also not available in personal service contracts. Involuntary servitude violates the Thirteenth Amendment to the United States Constitution.

PARALEGAL EXERCISE 11.7 Sylvia, a female acid rock group, contracted to give a Fourth of July concert at Woodstock. Early in June, Woodstock notified Sylvia that its services were no longer needed. Should Sylvia be entitled to the remedy of specific performance for Woodstock's breach of contract?

Cover **Cover** is a substitute. In a sale of goods, the nonbreaching buyer may need the goods and can attempt to purchase substitutes from a third party. Section 2-712(2) of the Uniform Commercial Code defines the buyer's damages:

(2) The buyer may recover from the seller as damages the difference between the cost of cover and the contract price together with any incidental or consequential damages as hereinafter defined (Section 2-715), but less expenses saved in consequence of the seller's breach.

What the nonbreaching party
expected to receive
(goods from the breaching
party)

less

What the nonbreaching party
did receive
(cover — goods from a third
party)

less

What the nonbreaching party
expected to give
(contract price)

less

What the nonbreaching party
did give
(cover price — price paid
to third party)

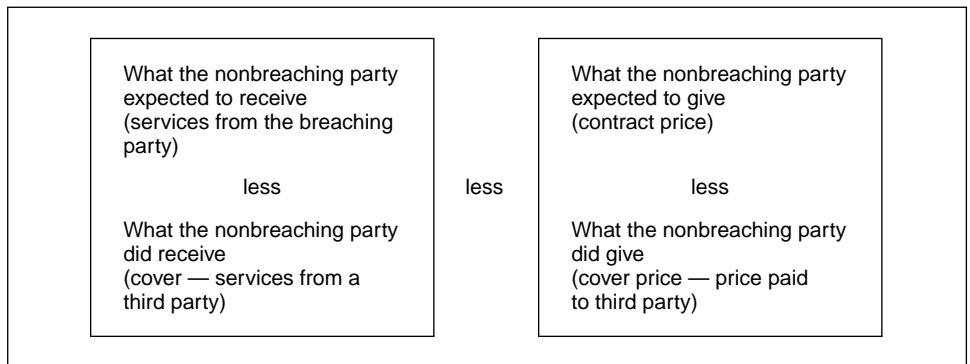
EXAMPLE 11-6

In early March, Farmer Jones contracted to sell his cotton crop to the ABC Cotton Gin for fifty cents a pound. Farmer Jones normally expects to harvest 100 tons of cotton. Later in March, ABC contracted to resell Farmer Jones's cotton to Quality Mills.

During the summer, when the price of cotton rose to seventy-five cents a pound, Farmer Jones notified ABC that he would not deliver his cotton to ABC. ABC then purchased cotton on the open market to meet its commitment with Quality Mills. ABC paid seventy-five cents a pound for the substitute cotton.

ABC has "covered" by buying substitute cotton and is entitled to damages of twenty-five cents a pound plus costs in finding the substitute cotton.

In an employment contract, the nonbreaching employer may need certain services and can attempt to find a substitute employee. Even though the nonbreaching party has found a substitute, he or she may still be entitled to damages. These damages include the difference in cost between what the nonbreaching party expected to pay for the services and what the nonbreaching party did pay, in addition to any expenses incurred in finding the substitute.

**EXAMPLE 11-7**

The Pink Panther Lounge hired Irma LaRue to sing at the Lounge on Friday and Saturday nights. The contract was for the month of December at a salary of \$500 an evening. After appearing for one weekend, Irma quit to perform in Atlantic City. Because this was the Christmas season and most entertainers had engagements, the Lounge hired Melody Layne, who appeared through the month of December at a salary of \$700 an evening.

The Lounge is entitled to \$200 for each of the remaining Friday and Saturday evenings in December. The Lounge is also entitled to any costs incurred in finding Melody.

Liquidated Damages **Liquidated damages** are damages included in the contract by the parties that will be due at the time of contract formation in the event of breach. Not all such clauses are enforceable. When one of the parties challenges such a clause, the court will evaluate whether the clause is in fact a liquidated damage provision or merely a penalty. Clauses that are classified as penalties are unenforceable.

A clause is a liquidated damage provision and not a penalty if:

1. at the time of contract formation the damages in the event of a breach would be impossible or very difficult to estimate accurately;
2. there was a reasonable endeavor by the parties to fix a fair compensation; and
3. the amount stipulated bears a reasonable relation to probable damages and is not disproportionate to any damages reasonably anticipated.

PARALEGAL EXERCISE 11.8 Reliable Property Company owned a fifty-unit apartment complex. Reliable hired Felix to repaint apartments as they became vacant, for \$300 each. The contract provided that Felix would have five days from the date of notice of vacancy to paint each apartment. The contract further provided that Felix would pay Reliable 10 percent of the contract price for each day he was late. Felix finished painting the first apartment in eight days and was paid \$210.

Could Felix successfully sue Reliable for breach of contract and, if so, for how much? Would the following facts be relevant?

1. The apartment rents for \$400 a month.
2. The apartment complex has an 85 percent occupancy rate.
3. The apartment was ready by the first of the month.

Costs and Attorney Fees In anticipation of litigation, parties might stipulate in the contract who will pay costs. **Costs** generally include filing fees, service of process, jury fees, and court officer charges, but not attorney fees. To pre-determine who will pay these expenses, the contract might contain a term stating, “the party initiating litigation will pay all costs.” Such a term will cause a court to levy the costs against the named party.

If the contract does not include a provision for costs, most courts will allocate costs to the losing party. Some states, however, place various limitations on this rule. For example, in Illinois, the court may apportion costs to the parties if the case is not decided on all of the issues presented. Because the rules on costs may vary from jurisdiction to jurisdiction, contracting parties must determine prior to drafting a contract which state’s law will apply in the event of a breach and who will be assessed costs if the contract does not allocate costs.

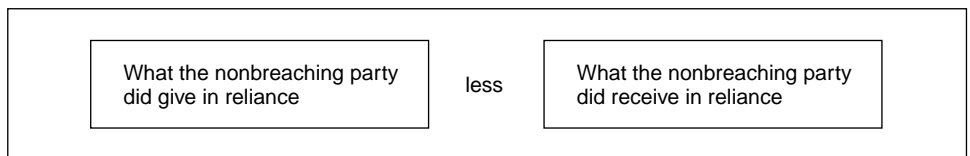
Unlike costs, the nonbreaching party in a breach of contract action generally cannot recover its attorney fees from the other, even after winning the judgment. This rule has two general exceptions. First, attorney fees can be recovered if suit is brought under a statute allowing the nonbreaching party to

recover attorney fees. A statute might include the clause, "Anyone bringing a cause of action under this statute may recover attorney fees, if that party has obtained a favorable judgment."

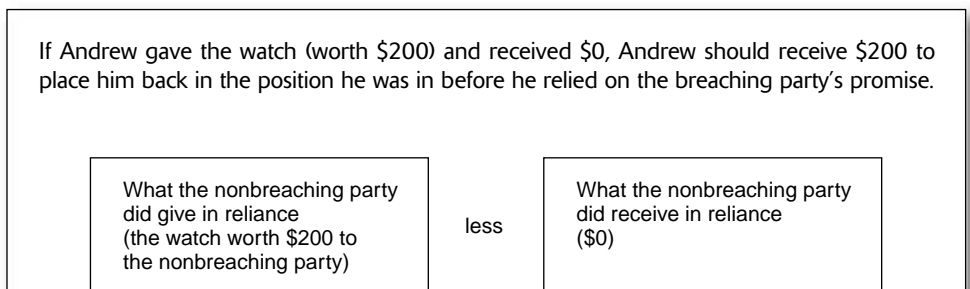
Second, the parties may allocate attorney fees by contract. The agreement may state, "if litigation arises from this contract, the party obtaining a favorable judgment in such litigation may recover his or her attorney fees from the opposing party." Although most states allow the parties to allocate attorney fees, some, such as California, limit the attorney fees recoverable to "reasonable attorney fees." Because the rules on attorney fees vary from jurisdiction to jurisdiction, the parties contemplating a contract must determine prior to drafting the contract which state's law will apply in the event of a breach, whether that state will enforce an allocation of attorney fees, and whether limitation will be placed on the allocation.

Reliance Remedy for Breach of Contract

The reliance remedy is not concerned with the nonbreaching party's expectations. Therefore, what the nonbreaching party expected to receive and what the nonbreaching party expected to give are irrelevant when computing damages based on reliance. The important factors are what the nonbreaching party did give and did receive in reliance on the breaching party's promise. The formula for the reliance remedy reads: *(what the nonbreaching party gave in reliance on the breaching party's promise) less (what the nonbreaching party received in reliance on the breaching party's promise).*



EXAMPLE 11-8



If the watch were worth \$250 rather than \$200 and he received \$0, Andrew should receive \$250 to place him back in the position he was in before he relied on the breaching party's promise.

What the nonbreaching party did give in reliance (the watch worth \$250 to the nonbreaching party)	less	What the nonbreaching party did receive in reliance (\$0)
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On the other hand, if the watch were only worth \$150, Andrew should receive \$150 if his reliance interest, rather than his expectation interest, were to be protected.

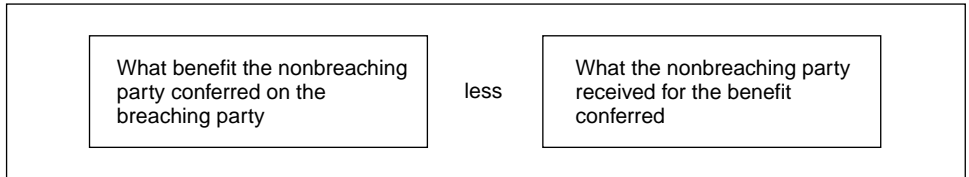
What the nonbreaching party did give in reliance (the watch worth \$150 to the nonbreaching party)	less	What the nonbreaching party did receive in reliance (\$0)
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PARALEGAL EXERCISE 11.9 Mary Oliver, a financial consultant in New York City, was hired by the Golden Gate Investment Company of San Francisco for \$80,000 a year for three years. Mary stayed for a week in San Francisco at her own expense finding a place to live. She also spent \$5,000 moving her household goods. When she reported to work, she found that new management had taken over the investment company and her services were no longer needed. Fortunately for Mary, she was able to return to her old job in New York City at \$78,000 a year.

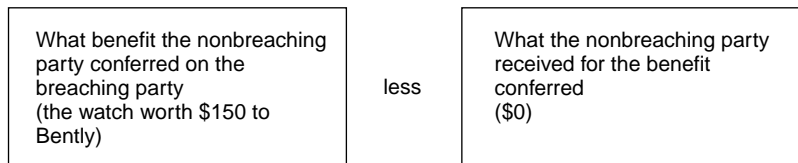
Could Mary successfully sue Golden Gate for breach of contract and, if so, for how much? Consider both Mary's expectation and reliance remedies.

Restitution Remedy for Breach of Contract

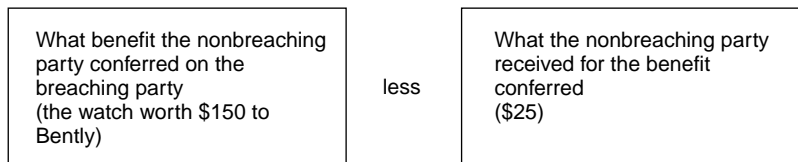
The restitution remedy, like the reliance remedy, is not concerned with what the nonbreaching party expected to receive and what that party expected to give. The restitution remedy also is not concerned with what the nonbreaching party gave or received in reliance on the breaching party's promise. Rather, the restitution remedy is concerned with the benefit that the nonbreaching party conferred on the breaching party and what the nonbreaching party received for conferring that benefit. The measure of damages is the reasonable value to the party receiving the benefit, that is, the breaching party.

**EXAMPLE 11-9**

If Andrew gave Bently the watch worth \$200 to Andrew but worth only \$150 to Bently and Bently did not pay Andrew the \$200 contract price, Andrew's restitution remedy is only \$150, the reasonable value of the watch to Bently.



If Bently had paid Andrew \$25 for the watch, Andrew could recover \$125, the reasonable value of the watch to Bently (\$150) less the amount Bently already paid Andrew for the watch (\$25).



Although the expectation remedy generally is greater than the restitution remedy, instances do exist in which the restitution remedy exceed expectation. This will occur when the breaching party breaches a contract that was unfavorable to the nonbreaching party. The nonbreaching party is taken off the hook.

EXAMPLE 11–10

The Sunset Nursery Company contracted to landscape the Zenith Mall for \$50,000. Sunset spent several weeks grading the land for trees and sod. The work took longer than Sunset had expected, due to the lack of spring rains and the hot summer that baked the soil. Zenith grew impatient and fired Sunset without cause. At the time of the termination, Sunset had spent the equivalent of \$40,000 on the job and would have spent an additional \$20,000 to complete it. The reasonable value of Sunset's work to Zenith was also \$40,000.

Zenith breached the contract by firing Sunset without cause. Sunset is entitled to a restitution remedy for Zenith's breach of contract. Sunset's measure of damages is the reasonable value of its work to Zenith, that is, \$40,000. Had Sunset sought to protect its expectation interest, it would have recovered two-thirds of the contract price (\$33,333) (two-thirds of the work was completed), or less than the value of its work.

In determining a restitution recovery, two factors come into play.

1. Was the nonbreaching party to pay money?
2. Did the nonbreaching party fully perform?

If the nonbreaching party was to pay money and has partially performed (i.e., has paid some money), the nonbreaching party is entitled to restitution of the money paid.

PARALEGAL EXERCISE 11.10 Alexander contracted to build a barn for Herman for \$30,000. Herman paid Alexander \$15,000 in advance. Alexander, however, did not begin to build the barn. If the barn had been built, it would have been worth only \$25,000.

When Herman sues Alexander for breach of contract, how much should he recover to protect his expectation interest?

How much should he recover to protect his restitution interest?

If the nonbreaching party was to perform services and did partially perform, then the nonbreaching party is entitled to the value of the services performed as measured by the reasonable value of the services to the breaching party. The nonbreaching party may recover the reasonable value of the services to the breaching party even though the reasonable value exceeds the prorated contract price.

EXAMPLE 11–11

A Client hired an Attorney to handle his divorce for \$750. The divorce turned out to be more complicated than the Attorney originally thought, and the Attorney devoted substantial time to the case. Before the Attorney could procure the divorce, the Client wrongfully discharged the Attorney. Had the Attorney computed his time in billable hours, he would have charged \$1,000 as of the time of his discharge.

The Attorney is entitled to a restitution remedy for breach of contract of \$1,000, the reasonable value of his services even though this exceeds the \$750 contract price.

If the nonbreaching party has fully performed the services, then the contract price limits recovery.

EXAMPLE 11–12

If the Client discharged the Attorney after the Attorney procured the divorce, the Attorney would be entitled to only the contract price, \$750, even though the reasonable value of his services was \$1,500.

This rule contains an anomaly. The nonbreaching party may recover more than the contract price for less than full performance but no more than the contract price for full performance.

PARALEGAL EXERCISE 11.11 Fields, seeking a divorce from her husband, hired Bailey as her attorney. The parties agreed upon a flat legal fee of \$2,500 for the completed property settlement and the divorce decree. After Bailey had spent substantial time preparing the case, Fields reconciled with her husband and refused to pay Bailey. The case turned out to be more complicated than Bailey had originally thought, and had she charged by billable hour, her fee for work performed prior to the reconciliation would easily have been \$4,000.

How much should Bailey recover from Fields in an action for breach of contract? Consider both Bailey's expectation and restitution interests.

In *Sullivan v. O'Connor*, the court discusses the injured party's expectation, reliance, and restitution remedies. Ms. Sullivan, a patient, contracted with Dr. O'Connor, a surgeon, for plastic surgery on her nose. The surgery failed to enhance her beauty and improve her appearance. The surgery in fact disfigured and deformed her nose and caused her pain and suffering beyond what she expected. Ms. Sullivan sued Dr. O'Connor for both breach of contract and negligence. The jury did not find Dr. O'Connor negligent but did find that he breached his contract with Ms. Sullivan.

1. What did each party promise in the contract?
2. Was the contract enforceable?
3. Did Dr. O'Connor breach the contract?
4. Referring to the following diagrams on damages, answer the following questions.
 - a. What did Ms. Sullivan expect to give?
 - b. What did Ms. Sullivan give?
 - c. What did Ms. Sullivan expect to receive?
 - What kind of nose?
 - Pain and suffering for how many operations?
 - Emotional distress for how many operations?
 - Loss of income associated with how many operations?
 - d. What did Ms. Sullivan receive?
 - What kind of nose?
 - Pain and suffering for how many operations?
 - Emotional distress for how many operations?
 - Loss of income associated with how many operations?
5. What were Ms. Sullivan's expectation damages?
6. What were Ms. Sullivan's reliance damages?
7. What were Ms. Sullivan's restitution damages?
8. Were the expectation, reliance, and restitution damages theoretically the same?
9. Did Ms. Sullivan's attorney ask for all the damages to which she was entitled?

Expectation Remedy

What the nonbreaching party expected to receive
 (_____ Nose)
 (Pain and suffering associated with _____ operations)
 (Emotional distress associated with _____ operations)
 (Loss of income associated with _____ operations)

less

What the nonbreaching party did receive
 (_____ Nose)
 (Pain and suffering associated with _____ operations)
 (Emotional distress associated with _____ operations)
 (Loss of income associated with _____ operations)

What the nonbreaching party expected to give
 (Dr's fees for _____ operations)
 (Clinic's fees for _____ operations)

less

What the nonbreaching party expected to give
 (Dr's fees for _____ operations)
 (Clinic's fees for _____ operations)

less

Reliance Remedy

What the nonbreaching party did give in reliance
 (Dr's fees for _____ operations)
 (Clinic's fees for _____ operations)

less

What the nonbreaching party did receive
 (_____ Nose)
 (Pain and suffering associated with _____ operations)
 (Emotional distress associated with _____ operations)
 (Loss of income associated with _____ operations)

Restitution Remedy

What benefit the nonbreaching party conferred on the breaching party
 (Dr's fees for _____ operations)
 (Clinic's fees for _____ operations)

less

What the nonbreaching party received for the benefit conferred
 (_____ Nose)
 (Pain and suffering associated with _____ operations)
 (Emotional distress associated with _____ operations)
 (Loss of income associated with _____ operations)

**CASE*****Sullivan v. O'Connor***

*Supreme Judicial Court of Massachusetts, 1973.
363 Mass. 579, 296 N.E.2d 183.*

Before TAURO, C. J., and REARDON, QUIRICO, KAPLAN and WILKINS, JJ.
KAPLAN, Justice.

The plaintiff patient secured a jury verdict of \$13,500 against the defendant surgeon for breach of contract in respect to an operation upon the plaintiff's nose. The substituted consolidated bill of exceptions presents questions about the correctness of the judge's instructions on the issue of damages.

The declaration was in two counts. In the first count, the plaintiff alleged that she, as patient, entered into a contract with the defendant, a surgeon, wherein the defendant promised to perform plastic surgery on her nose and thereby to enhance her beauty and improve her appearance; that he performed the surgery but failed to achieve the promised result; rather the result of the surgery was to disfigure and deform her nose, to cause her pain in body and mind, and to subject her to other damage and expense. The second count, based on the same transaction, was in the conventional form for malpractice, charging that the defendant had been guilty of negligence in performing the surgery. Answering, the defendant entered a general denial.

On the plaintiff's demand, the case was tried by jury. At the close of the evidence, the judge put to the jury, as special questions, the issues of liability under the two counts, and instructed them accordingly. The jury returned a verdict for the plaintiff on the contract count, and for the defendant on the negligence count. The judge then instructed the jury on the issue of damages.

As background to the instructions and the parties' exceptions, we mention certain facts as the jury could find them. The plaintiff was a professional entertainer, and this was known to the defendant. The agreement was as alleged in the declaration. More particularly, judging from exhibits, the plaintiff's nose had been straight, but long and prominent; the defendant undertook by two operations to reduce its prominence and somewhat to shorten it, thus making it more pleasing in relation to the plaintiff's other features. Actually the plaintiff was obliged to undergo three operations, and her appearance was worsened. Her nose now had a concave line to about the midpoint, at which it became bulbous; viewed frontally, the nose from bridge to midpoint was flattened and broadened, and the two sides of the tip had lost symmetry. This configuration evidently could not be improved by further surgery. The plaintiff did not demonstrate, however, that her change of appearance had resulted in loss of employment. Payments by the plaintiff covering the defendant's fee and hospital expenses were stipulated at \$622.65.

The judge instructed the jury, first, that the plaintiff was entitled to recover her out-of-pocket expenses incident to the operations. Second, she could recover the damages flowing directly, naturally, proximately, and foreseeably from the defendant's breach of promise. These would comprehend damages for any disfigurement of the plaintiff's nose—that is, any change of appearance for the worse—including the effects of the consciousness of such disfigurement on the plaintiff's mind, and in this connection the jury should consider the nature of the plaintiff's profession. Also consequent upon the defendant's breach, and compensable, were the pain and suffering involved in the third operation, but not in the first two. As there was no proof that any loss of earnings by the plaintiff resulted from the breach, that element should not enter into the calculation of damages.

By his exceptions the defendant contends that the judge erred in allowing the jury to take into account anything but the plaintiff's out-of-pocket expenses (presumably at the stipulated amount). The defendant excepted to the judge's refusal of his request for a general charge to that effect, and, more specifically, to the judge's refusal of a charge that the plaintiff could not recover for pain and suffering connected with the third operation or for impairment of the plaintiff's appearance and associated mental distress.

The plaintiff on her part excepted to the judge's refusal of a request to charge that the plaintiff could recover the difference in value between the nose as promised and the nose as it appeared after the operations. However, the plaintiff in her brief expressly waives this exception and others made by her in case this court overrules the defendant's exceptions; thus she would be content to hold the jury's verdict in her favor.

We conclude that the defendant's exceptions should be overruled.

[The court found Dr. O'Connor had contracted to provide Ms. Sullivan with a beautiful nose and had breached his contract.]

If an action on the basis of contract is allowed, we have next the question of the measure of damages to be applied where liability is found. Some cases have taken the simple view that the promise by the physician is to be treated like an ordinary commercial promise, and accordingly that the successful plaintiff is entitled to a standard measure of recovery for breach of contract—"compensatory" ("expectancy") damages, an amount intended to put the plaintiff in the position he would be in if the contract had been performed, or, presumably, at the plaintiff's election, "restitution" damages, an amount corresponding to any benefit conferred by the plaintiff upon the defendant in the performance of the contract disrupted by the defendant's breach. See Restatement: Contracts § 329 and comment a, §§ 347, 384(1). Thus in *Hawkins v. McGee*, 84 N.H. 114, 146 A. 641, the defendant doctor was taken to have promised the plaintiff to convert his damaged hand by means of an operation into a good or perfect hand, but the doctor so operated as to damage the hand still further. The court, following the usual expectancy formula, would have asked the jury to estimate and award to the plaintiff the difference between the value of a good or perfect hand, as promised, and the value of the hand after the operation. (The same formula would apply, although the dollar result would be less, if the operation had neither worsened nor improved the condition of the hand.) If the plaintiff had not yet paid the doctor his fee, that amount would be deducted from the recovery. There could be no recovery for the pain and suffering of the operation, since that detriment would have been incurred even if the operation had been successful; one can say that this detriment was not "caused" by the breach. But where the plaintiff by reason of the operation was put to more pain than he would have had to endure, had the doctor performed as promised, he should be compensated for that difference as a proper part of his expectancy recovery. It may be noted that on an alternative count for malpractice the plaintiff in the *Hawkins* case had been nonsuited; but on ordinary principles this could not affect the contract claim, for it is hardly a defense to a breach of contract that the promisor acted innocently and without negligence. The New Hampshire court further refined the *Hawkins* analysis in *McQuaid v. Michou*, 85 N.H. 299, 157 A. 881, all in the direction of treating the patient-physician cases on the ordinary footing of expectancy. See *McGee v. United States Fid. & Guar. Co.*, 53 F.2d 953 (1st Cir.) (later development in the *Hawkins* case); *Cloutier v. Kasheta*, 105 N.H. 262, 197 A.2d 627; *Lakeman v. LaFrance*, 102 N.H. 300, 305, 156 A.2d 123.

Other cases, including a number in New York, without distinctly repudiating the *Hawkins* type of analysis, have indicated that a different and generally more lenient measure of damages is to be applied in patient-physician actions based on breach of alleged special agreements to effect a cure, attain a stated result, or employ a given medical method. This measure is expressed in somewhat variant ways, but the substance is that the plaintiff is to

recover any expenditures made by him and for other detriment (usually not specifically described in the opinions) following proximately and foreseeably upon the defendant's failure to carry out his promise. *Robins v. Finestone*, 308 N.Y. 543, 546, 127 N.E.2d 330; *Frankel v. Wolper*, 181 App.Div. 485, 488, 169 N.Y.S. 15, affd., 228 N.Y. 582, 127 N.E. 913; *Frank v. Maliniak*, 232 App.Div. 278, 280, 249 N.Y.S. 514; *Colvin v. Smith*, 276 App.Div. 9, 10, 92 N.Y.S.2d 794; *Stewart v. Rudner*, 349 Mich. 459, 465–473, 84 N.W.2d 816. Cf. *Carpenter v. Moore*, 51 Wash.2d 795, 322 P.2d 125. This, be it noted, is not a "restitution" measure, for it is not limited to restoration of the benefit conferred on the defendant (the fee paid) but includes other expenditures, for example, amounts paid for medicine and nurses; so also it would seem according to its logic to take in damages for any worsening of the plaintiff's condition due to the breach. Nor is it an "expectancy" measure, for it does not appear to contemplate recovery of the whole difference in value between the condition as promised and the condition actually resulting from the treatment. Rather the tendency of the formulation is to put the plaintiff back in the position he occupied just before the parties entered upon the agreement, to compensate him for the detriments he suffered in reliance upon the agreement. This kind of intermediate pattern of recovery for breach of contract is discussed in the suggestive article by Fuller and Perdue, *The Reliance Interest in Contract Damages*, 46 *Yale L.J.* 52, 373, where the authors show that, although not attaining the currency of the standard measures, a "reliance" measure has for special reasons been applied by the courts in a variety of settings, including noncommercial settings. See 46 *Yale L.J.* at 396–401.

For breach of the patient-physician agreements under consideration, a recovery limited to restitution seems plainly too meager, if the agreements are to be enforced at all. On the other hand, an expectancy recovery may well be excessive. The factors, already mentioned, which have made the cause of action somewhat suspect, also suggest moderation as to the breadth of the recovery that should be permitted. Where, as in the case at bar and in a number of the reported cases, the doctor has been absolved of negligence by the trier, an expectancy measure may be thought harsh. We should recall here that the fee paid by the patient to the doctor for the alleged promise would usually be quite disproportionate to the putative expectancy recovery. To attempt, moreover, to put a value on the condition that would or might have resulted, had the treatment succeeded as promised, may sometimes put an exceptional strain on the imagination of the fact finder. As a general consideration, Fuller and Perdue argue that the reasons for granting damages for broken promises to the extent of the expectancy are at their strongest when the promises are made in a business context, when they have to do with the production or distribution of goods or the allocation of functions in the market place; they become weaker as the context shifts from a commercial to a noncommercial field. 46 *Yale L.J.* at 60–63.

There is much to be said, then, for applying a reliance measure to the present facts, and we have only to add that our cases are not unreceptive to the use of that formula in special situations. We have, however, had no previous occasion to apply it to patient-physician cases.

The question of recovery on a reliance basis for pain and suffering or mental distress requires further attention. We find expressions in the decisions that pain and suffering (or the like) are simply not compensable in actions for breach of contract. The defendant seemingly espouses this proposition in the present case. True, if the buyer under a contract for the purchase of a lot of merchandise, in suing for the seller's breach, should claim damages for mental anguish caused by his disappointment in the transaction, he would not succeed; he would be told, perhaps, that the asserted psychological injury was not fairly foreseeable by the defendant as a probable consequence of the breach of such a business contract. See *Restatement: Contracts*, § 341, and comment a. But there is no general rule barring such items of damage in actions for breach of contract. It is all a question of the subject matter and background of the contract, and when the contract calls for an operation on the person of the

plaintiff, psychological as well as physical injury may be expected to figure somewhere in the recovery, depending on the particular circumstances. The point is explained in *Stewart v. Rudner*, 349 Mich. 459, 469, 84 N.W.2d 816. Cf. *Frewen v. Page*, 238 Mass. 499, 131 N.E. 475; *McClellan v. University Club*, 327 Mass. 68, 97 N.E.2d 174. Again, it is said in a few of the New York cases, concerned with the classification of actions for statute of limitations purposes, that the absence of allegations demanding recovery for pain and suffering is characteristic of a contract claim by a patient against a physician, that such allegations rather belong in a claim for malpractice. See *Robins v. Finestone*, 308 N.Y. 543, 547, 127 N.E.2d 330; *Budoff v. Kessler*, 2 A.D.2d 760, 153 N.Y.S.2d 654. These remarks seem unduly sweeping. Suffering or distress resulting from the breach going beyond that which was envisaged by the treatment as agreed, should be compensable on the same ground as the worsening of the patient's condition because of the breach. Indeed it can be argued that the very suffering or distress "contracted for"—that which would have been incurred if the treatment achieved the promised result—should also be compensable on the theory underlying the New York cases. For that suffering is "wasted" if the treatment fails. Otherwise stated, compensation for this waste is arguably required in order to complete the restoration of the status quo ante.

In the light of the foregoing discussion, all the defendant's exceptions fail: the plaintiff was not confined to the recovery of her out-of-pocket expenditures; she was entitled to recover also for the worsening of her condition, and for the pain and suffering and mental distress involved in the third operation. These items were compensable on either an expectancy or a reliance view. We might have been required to elect between the two views if the pain and suffering connected with the first two operations contemplated by the agreement, or the whole difference in value between the present and the promised conditions, were being claimed as elements of damage. But the plaintiff waives her possible claim to the former element, and to so much of the latter as represents the difference in value between the promised condition and the condition before the operations.

Plaintiff's exceptions waived.

Defendant's exceptions overruled.

THE UNAVAILABILITY OF RESTITUTION AS A CAUSE OF ACTION FOR THE NONBREACHING PLAINTIFF WHEN THE DEFENDANT HAS BREACHED THE CONTRACT

A nonbreaching party does not have the luxury of selecting between a breach of contract action and a restitution action. (The restitution action should not be confused with the restitution remedy for a breach of contract action.) If a contract has been formed and is enforceable and if the defendant has breached, the nonbreaching party has no choice but to pursue a breach of contract action. If the nonbreaching party ignores the breach of contract action and pleads a restitution action, the breaching party can defend the restitution action by claiming the existence of an enforceable contract that has been breached.

But why would a breaching party want to defend a restitution action by stating that he or she breached the contract? The answer may be found in the baggage that accompanies each cause of action. Each cause of action has its own attributes. The difference may include: the statute of limitations, costs and attorney fees, and the simplicity of the issues to be litigated.

EXAMPLE 11–13

The ABC Corporation contracted with the Washington County Sheriff's Department to provide video cameras in all deputy sheriff patrol vehicles. ABC installed the cameras, but the Sheriff's Department refused to pay. The contract provides that in the event of breach, the breaching party will pay one-half of the nonbreaching party's attorney's fees. Under a state statute, attorney fees may be awarded by the court in a restitution cause of action.

Although ABC would like to sue the Sheriff's Department in a restitution cause of action and seek all of its attorney's fees, it would be unsuccessful because a cause of action for breach of contract could be maintained. A contract existed between ABC and the Sheriff's Department. The contract was enforceable. The Sheriff's Department breached the contract and ABC has a cause of action for breach of contract. A restitution cause of action can only be maintained when a breach of contract cause of action cannot be maintained. Therefore, ABC has no choice but to claim its remedies under a breach of contract cause of action. ABC could recover only one-half of its attorney's fees.

ABC may, however, plead both breach of contract and restitution as alternative causes of action. If the breach of contract cause of action survives the trial, the restitution cause of action ceases to exist. If the breach of contract cause of action does not survive trial, the restitution cause of action could be maintained.

**PARALEGAL CHECKLIST****Plaintiff's Remedies for the Defendant's Breach of Contract**

- Once an enforceable contract has been breached, the nonbreaching party may successfully maintain an action for breach of contract and *seek a remedy for the breach*. The remedies for breach of contract may compensate the nonbreaching party: (1) for what it expected to receive under the contract (expectation); (2) for costs incurred while relying on the contract (reliance); or (3) for any benefit conferred by the nonbreaching party on the breaching party that would cause an unjust result if retained by the breaching party without compensating the nonbreaching party (restitution).
 - Although the nonbreaching party generally fares best when seeking compensation based on lost expectations, compensation based on reliance or restitution may exceed compensation based on contract expectations. The paralegal must, therefore, analyze for the supervising attorney what the nonbreaching party could receive under each remedy to produce the largest award.
1. Evaluate the expectation remedy to determine how the nonbreaching party will be placed at the point of full performance by considering the following questions:
 - a. What will it take: (1) to give the nonbreaching party what he or she expected to receive; and (2) to have the nonbreaching party give what he or she expected to give?
 - (1) What has the nonbreaching party already received? Anything that has been received must be subtracted from what the nonbreaching party expected to receive. Otherwise, the nonbreaching party will get more than he or she expected to receive.
 - (2) What has the nonbreaching party already given? Anything that has been given must be subtracted from what the nonbreaching party expected to give. Otherwise, the nonbreaching party will be required to give more than he or she expected to give. Incidental damages are

- included as something that the nonbreaching party gave.
- b. How can the injured party be brought up to full performance, no more and no less (compensatory damages)? Punitive damages are not awarded in breach of contract actions.
 - c. What damages could the breaching party reasonably foresee at the time of contract formation as the probable result of such a breach? Damages are limited to those foreseeable. Foreseeable damages are either general or special damages.
 - (1) General damages arise naturally from a breach of contract itself. These damages can be expected to occur when the contract is breached. The damages will vary depending on how the contract is breached.
 - (2) Special damages do not arise naturally when a contract is breached but may reasonably be supposed to have been in the contemplation of both parties to the contract and are, therefore, foreseeable.
 - d. How can damages for breach of contract be shown with reasonable certainty? Damages that are speculative and incapable of being ascertained with reasonable certainty are not recoverable. Although damages must be certain, mathematical exactness is not required.
 - e. How can the nonbreaching party meet the duty to mitigate the damages? The nonbreaching party must use reasonable means to avoid or minimize damages (mitigation).
 - (1) The mitigation doctrine prevents the nonbreaching party from increasing the amount the breaching party must pay.
 - (2) The nonbreaching party is required, under the mitigation doctrine, to decrease the amount of damages the breaching party must pay.
 - f. Can the nonbreaching party establish that a breach of contract has occurred but is unable to prove damages? If so, it is entitled to nominal damages. Nominal damages may clarify the rights and duties under the contract.
 - g. What other protection is available if damages do not totally compensate the nonbreaching party for his or her injury?
 - (1) Consider an injunction, which may protect the nonbreaching party from future injuries.
 - (2) Look at the availability of specific performance if the performance is unique and therefore not easily replaceable on the market.
 - (a) Specific performance is not available when the breach is the failure to pay money. Money is interchangeable and therefore not unique.
 - (b) Specific performance is not available in a personal service contract. Involuntary servitude is unconstitutional.
 - h. How does cover place the nonbreaching party at the point of full performance? Cover is a substitute. Cover may be replacement goods or a substitute employee. The nonbreaching party is entitled to the difference between the cost of the substitute and the contract price.
 - i. At the time of contract formation, did the parties agree upon a liquidated damages provision, i.e., a stipulation of what the damages will be in the event of breach? Such a provision will be enforceable as a liquidated damage provision and not as a penalty if:
 - (1) at the time of contract formation the damages in the event of a breach would be impossible or very difficult to estimate accurately;
 - (2) there was a reasonable endeavor by the parties to fix a fair compensation; and
 - (3) the amount stipulated bears a reasonable relation to probable damages and is not disproportionate to any damages reasonably anticipated.
 - j. Did the contracting parties stipulate in the contract who will pay costs. Costs generally include filing fees, service of process, jury fees, and court officer charges, but not attorney fees. If the parties have not allocated costs in the contract, the court may allocate costs to the losing party. Contracting parties may allocate attorney fees by contract. Limitations may be placed on both the allocation of costs and attorney fees, depending on the jurisdiction.
2. Remember that the court, when evaluating the reliance remedy, will place the nonbreaching

party back to the time prior to his or her reliance on the promisor's promise.

- a. Therefore, ask:
 - (1) what did the nonbreaching party give in reliance on the promise? and
 - (2) what did the nonbreaching party receive in reliance on the promise?
 - b. Keep in mind that the nonbreaching party's expectations (what would have been given or received) are irrelevant because the nonbreaching party is not being moved forward to the time when performance would have been completed by both sides.
3. Be aware that the court, when evaluating the restitution remedy, will place the nonbreaching party back to the time prior to conferring the benefit on the breaching party.
- a. Therefore, ask:
 - (1) what benefit did the nonbreaching party confer on the breaching party? and
 - (2) what did the nonbreaching party receive for conferring this benefit?
 - b. Recall that the nonbreaching party's expectations (what he or she would give or receive) are irrelevant because the nonbreaching party is not being moved forward to the time when performance would have been completed by both sides.
 - c. Which two factors come into play in determining a restitution remedy?
 - (1) whether the nonbreaching party was to pay money, and
 - (2) whether the nonbreaching party fully performed.
- (a) Determine if the nonbreaching party was to pay money and has partially performed. If so, he or she is entitled to restitution of the money paid.
 - (b) Find out if the nonbreaching party was to perform services and has partially performed. If so, he or she is entitled to the value of the services performed (measured by the reasonable value of the services to the breaching party). The nonbreaching party may recover the reasonable value of the services to the breaching party even though the reasonable value exceeds the prorated contract price.

If the nonbreaching party has fully performed the services, the contract price limits recovery. Therefore, the nonbreaching party may recover more than the contract price for less than full performance but no more than the contract price for full performance.
4. Bear in mind that a nonbreaching party may not choose between breach of contract and restitution actions. If an enforceable contract has been breached, the nonbreaching party has no choice but to pursue a breach of contract action. If the nonbreaching party ignores the breach of contract action and pleads a restitution action, the breaching party can defend the restitution action by claiming the existence of an enforceable contract. Whether a defendant finds this strategy beneficial may depend on the statute of limitations, costs and attorney fees, and other issues to be litigated.

REVIEW QUESTIONS

DEFINE THE FOLLOWING NEW TERMS AND PHRASES

Compensatory Damages

Costs

Cover

Expectation Damages

General Damages

Incidental Damages

Injunction

Liquidated Damages

Mitigation

Nominal Damages

Punitive Damages

Special Damages

Specific Performance

Reliance Damages

Restitution Damages

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

1. T F The nonbreaching party is entitled to a remedy for the breaching party's nonperformance of an enforceable contract.
2. T F A remedy for breach of contract may involve expectation, reliance, or restitution interests.
3. T F Courts give the breaching party what he or she expected to receive when an expectation interest is being protected.
4. T F Courts require the nonbreaching party to give what he or she expected to give when an expectation interest is being protected.
5. T F The reliance interest concerns the nonbreaching party's expectations.
6. T F What the nonbreaching party expected to receive and to give must be considered when computing damages based on the reliance interest.
7. T F The restitution interest is not concerned with what the nonbreaching party expected to receive and to give.
8. T F The restitution interest is concerned with what the nonbreaching party gave or received in reliance on the breaching party's promise.
9. T F The restitution interest is concerned with the benefit that the nonbreaching party conferred on the breaching party and what the nonbreaching party received for conferring that benefit.
10. T F The measure of damages to the restitution interest is the reasonable value to the breaching party.
11. T F When the expectation interest is protected, the nonbreaching party will be placed in the position he or she would have been in had the contract been fully performed according to its terms.
12. T F The damages awarded to the nonbreaching party to protect his or her expectation interest are intended as compensation for not receiving that expectation under the contract.
13. T F Damages for breach of contract include punitive damages.
14. T F The intentions of the breaching party are relevant to the damages for breach of contract.
15. T F Intentional and unintentional breaches will result in the same measure of expectation damages.
16. T F A contracting party will never find that breaching a contract will be in his or her best economic interest.
17. T F The breaching party is held up to the public as an example of what might happen to a party who breaches.
18. T F Determining what will place the injured party in the position he or she would have been in had the contract been fully performed may be difficult.
19. T F Damages for breach of contract are limited to those that the breaching party could reasonably foresee, when the contract was made, as a probable result of breach.
20. T F Only general damages are foreseeable.

21. T F General damages arise naturally while special damages do not.
22. T F Damages for pain and suffering or for emotional distress are never available in a breach of contract action.
23. T F Damages that are speculative and incapable of being ascertained with reasonable certainty are not recoverable for breach of contract.
24. T F The nonbreaching party has a duty to mitigate the damages in the event of a breach.
25. T F Although the nonbreaching party is required by the doctrine of mitigation to prevent increasing damages, he or she is not required to decrease the damages the breaching party must pay.
26. T F A nonbreaching party who establishes a breach of contract but is unable to prove damages is entitled to nominal damages.
27. T F A judgment for nominal damages compensates the nonbreaching party in dollars and cents.
28. T F A judgment for nominal damages clarifies the rights and duties of the parties and may include an award of court costs.
29. T F An injunction is a court order directing the breaching party to refrain from a specified act and is designed to prevent future injuries to the nonbreaching party.
30. T F Specific performance is available to a nonbreaching party who prefers it as compensation for his or her injury rather than accepting damages.
31. T F Specific performance may be available in a contract for the sale of goods if the goods are unique.
32. T F Specific performance is not available when the breach is a failure to pay money.
33. T F Specific performance is available in personal service contracts if the service is unique.
34. T F Cover is a substitute for contractual performance and is often used by the nonbreaching buyer in contracts for the sale of goods.
35. T F The nonbreaching employer in an employment contract may still be entitled to damages even though he or she has found a substitute employee.
36. T F Liquidated damages are those imposed on the parties by the court.
37. T F Parties to a contract may agree upon what damages will be in the event of a breach and incorporate this agreement in a provision known as a liquidated damage clause.
38. T F All liquidated damage clauses are enforceable.
39. T F Liquidated damage clauses that are classified by the court as penalties are unenforceable.
40. T F Parties to a contract may not include a provision regarding who will pay costs if litigation ensues.
41. T F Most courts will allocate costs to the losing party in a contractual dispute in which the contract does not include a provision for costs.
42. T F Costs in a breach of contract case usually include attorney fees.

43. T F Attorney fees may not be allocated by contract.
44. T F A nonbreaching party may choose between a breach of contract action and a restitution action.
45. T F A restitution action is the same thing as a restitution remedy for a breach of contract action.

FILL-IN-THE-BLANK QUESTIONS

- _____. Damages that place the nonbreaching party in a position he or she would have been in had both parties fully performed according to the terms of the contract.
- _____. Damages based on what the nonbreaching party did give and did receive in reliance on the breaching party's promise.
- _____. Damages based on the benefit that the nonbreaching party conferred on the breaching party and what the nonbreaching party received for conferring that benefit.
- _____. Damages intended to compensate the nonbreaching party for not receiving his or her expectation under the contract.
- _____. Damages that the breaching party could reasonably foresee, at the time of the making of the contract, as a probable result of the breach.
- _____. Damages that "arise naturally, i.e., according to the usual course of things, from such breach of contract itself"
- _____. Damages that "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."
- _____. Action that the aggrieved party must take after a breach of contract to limit the damages that will arise due to the breach.
- _____. Damages that clarify the rights and duties of the parties but do not compensate the nonbreaching party in dollars and cents.
- _____. A court order directing the breaching party to refrain from a specified act.
- _____. A remedy whereby a court directs a party to do a specified act.
- _____. A substitute for contractual performance.
- _____. Damages agreed to by the parties, at the time of contract formation, that will apply to the transaction if a breach occurs.
- _____. Expenses incurred in litigation that generally include filing fees, service of process, jury fees, and court officer charges, but not attorney fees.

MULTIPLE CHOICE QUESTIONS (CIRCLE ALL THE CORRECT ANSWERS)

1. Naomi contracted to sell a computer to Watson for \$1,500. Watson paid Naomi \$100, and Naomi delivered the computer. The reasonable value of the computer to Naomi was \$1,300. The reasonable value of the computer on the open market was \$1,600. Watson refused to pay the balance. In a breach of contract action, Naomi is entitled to recover:
 - (a) \$1,600
 - (b) \$1,500
 - (c) \$1,400
 - (d) \$1,300
 - (e) \$1,200
2. Naomi contracted to sell a computer to Watson for \$1,500. Watson paid Naomi \$100 and was to pay an additional \$400 before Naomi had a duty to deliver the computer. Watson never paid the \$400 so Naomi never delivered the computer. The reasonable value of the computer to Naomi was \$1,300. The reasonable value of the computer on the open market was \$1,600. Watson refused to pay the balance. In a breach of contract action, Naomi is entitled to recover:
 - (a) \$1,600
 - (b) \$1,400
 - (c) \$1,300
 - (d) \$1,200
 - (e) \$ 0
3. Naomi contracted to sell a computer to Watson for \$1,500. Watson paid Naomi \$100, and Naomi delivered the computer. The reasonable value of the computer to Naomi was \$1,300. The reasonable value of the computer on the open market was \$1,600. Watson refused to pay the balance. If Naomi seeks to protect her reliance interest in a breach of contract action, she is entitled to recover:
 - (a) \$1,600
 - (b) \$1,500
 - (c) \$1,400
 - (d) \$1,300
 - (e) \$1,200
4. Naomi contracted to sell a computer to Watson for \$1,500. Watson paid Naomi \$100, and Naomi delivered the computer. The reasonable value of the computer to Naomi was \$1,300. The reasonable value of the computer on the open market was \$1,600. The reasonable value of the computer to Watson was \$1,700. Watson refused to pay the balance. If Naomi seeks to protect her restitution interest in a breach of contract action, she is entitled to recover:
 - (a) \$1,600
 - (b) \$1,500
 - (c) \$1,400
 - (d) \$1,300
 - (e) \$1,200

5. Cornelia contracted to refinish an antique dining room table for Delana for \$950. After Cornelia made a \$200 down payment, Delana refused to work on the table. Cornelia found another furniture restorer to refinish the table, but it cost her \$1,500. The restoration increased the value of the table by \$2,000. It will cost \$1,000 in attorney's fees for Cornelia to successfully maintain her breach of contract action. If Cornelia sues Delana for breach of contract, she could recover:
- (a) \$2,500
 - (b) \$2,400
 - (c) \$1,750
 - (d) \$ 750
 - (e) \$ 200

SHORT ANSWER QUESTIONS

1. Complete the diagram for expectation damages.
2. Complete the diagram for reliance damages.
3. Complete the diagram for restitution damages.

PART
VI

Third Party Interests

INTRODUCTION

Beyond the Two Contracting Parties

CHAPTER 12

Third Party Interests

INTRODUCTION

Beyond the Two Contracting Parties

The first five parts of this book have explored the consensual relationship between the two contracting parties. Part Six (Chapter 12) moves beyond the two parties to the contract.



Third Party Interests

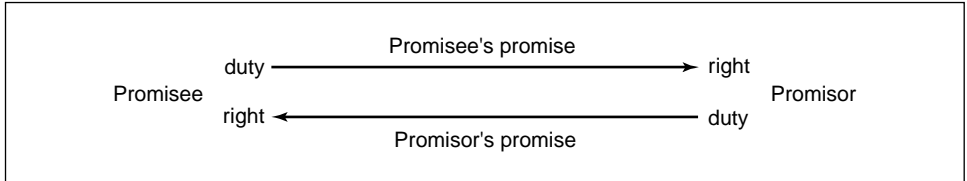
- ◆ Third Party Beneficiary Contracts
- ◆ The Assignment of Contract Rights and Delegation of Contract Duties
 - Assignment*
 - Delegation*
 - Assignment and Delegation*
 - Substituting and Releasing a Contracting Party: The Novation*
- ◆ Third Party's Interference with Existing Contract Rights

Chapter 12 moves beyond the two parties to the contract to explore three types of third party interests: third party beneficiary contracts; assignment of contract rights and delegation of contract duties (including the novation); and tortious interference with existing contract rights.

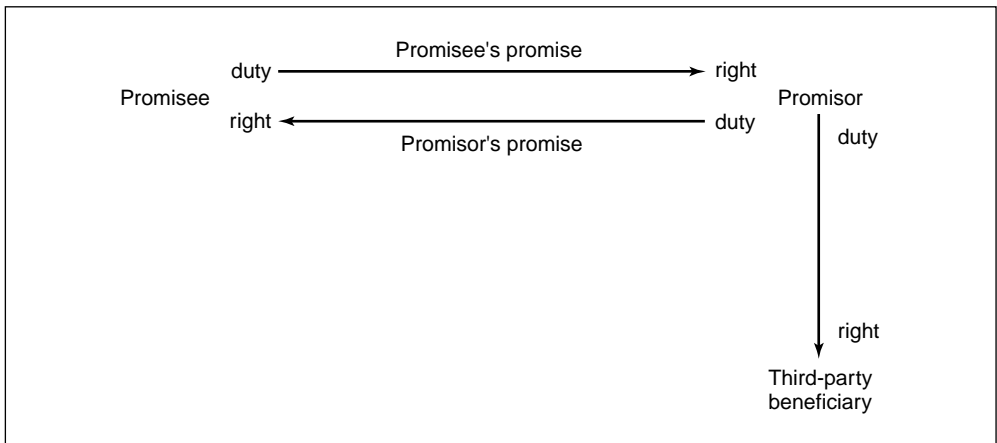
THIRD PARTY BENEFICIARY CONTRACTS

A **third party beneficiary contract**, as its name suggests, is a contract for the benefit of a third party who is not a contracting party. Courts agree that a contract made for the benefit of a third party beneficiary may be enforced by that third party if that party is more than an incidental beneficiary.

In a bilateral contract, each contracting party has a duty associated with his or her promise and a right associated with the other party's promise.



In a third party beneficiary contract, the two contracting parties have duties and rights. The third party beneficiary has only contractual rights but no contractual duties.

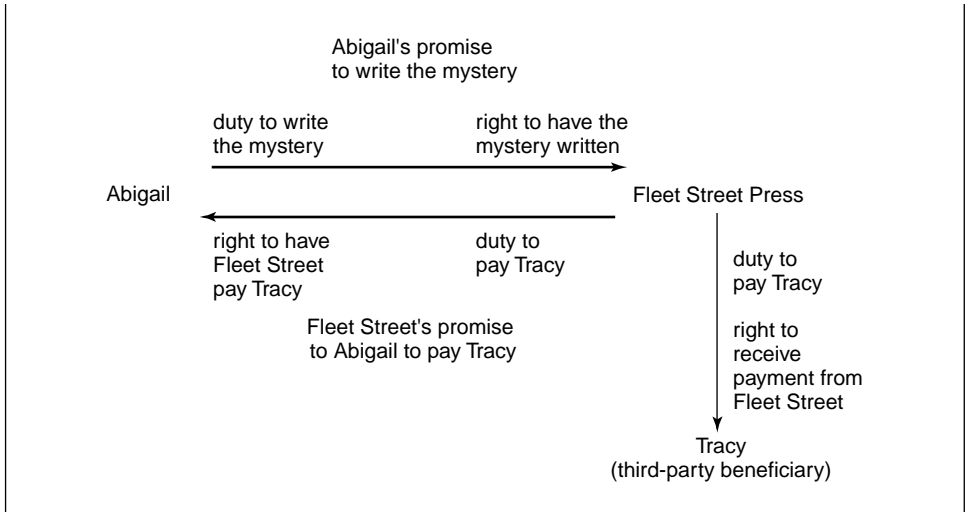


The following contract between Abigail and Fleet Street Press illustrates a typical third party beneficiary contract.

EXAMPLE 12-1

Abigail, a mystery writer, promises to write a new mystery for her publisher, Fleet Street Press, if Fleet Street promises to put the royalties in trust for her godchild, Tracy, the third party beneficiary, owes no duty to either Abigail or to Fleet Street. Abigail owes a duty to Fleet Street to write, and Fleet Street owes both Abigail and Tracy a duty to pay Tracy. Because Fleet Street owes a duty to Tracy, Tracy has a right to have Fleet Street perform this duty.

The following diagram illustrates the parties' rights and duties:



A third party beneficiary contract is subject to the same rules of contract formation as any other contract. The consideration for Abigail's promise to write is Fleet Street's promise to pay Tracy. The consideration for Fleet Street's promise to pay Tracy is Abigail's promise to write.

Third party beneficiaries come in three forms: donee, creditor, and incidental. A **donee beneficiary** receives a gift.

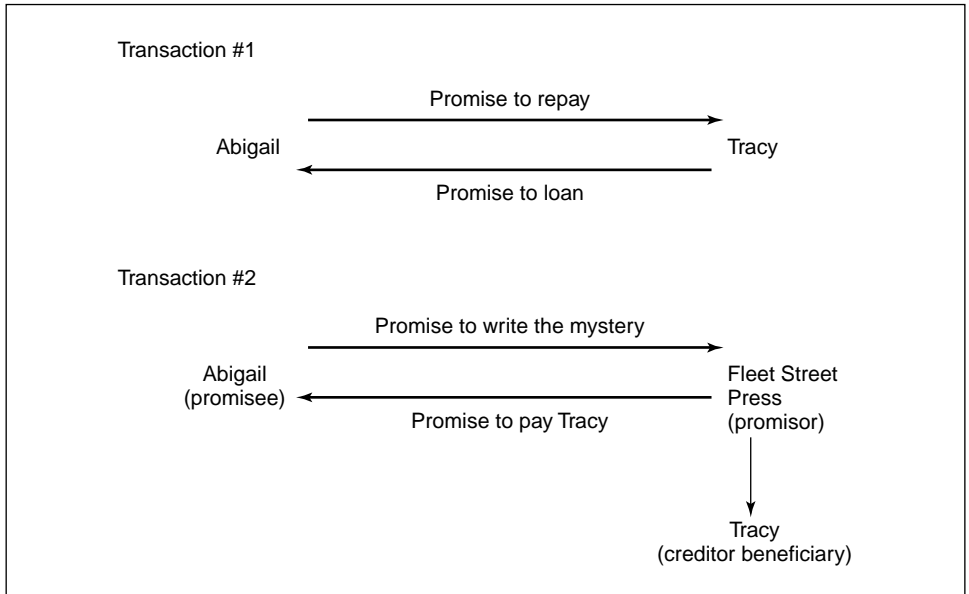
EXAMPLE 12-2

In the Abigail/Fleet Street example, Tracy is a donee beneficiary. Prior to the third party beneficiary contract, neither Abigail nor Fleet Street had a duty to give Tracy Abigail's royalties.

A **creditor beneficiary** has a right to receive something that arose prior to the third party beneficiary contract. The promisor's performance of his or her duty extinguishes the third party beneficiary prior right.

EXAMPLE 12-3

Change the Abigail/Fleet Street example. Add the fact that Tracy had lent Abigail money in a prior transaction. Now add the third party beneficiary transaction so Abigail promises to write the mystery for Fleet Street Press for Fleet Street's promise to Abigail to pay Tracy to satisfy Abigail's debt. Tracy would be a creditor beneficiary of the Abigail/Fleet Street Contract.



The Restatement (Second) of Contracts has moved away from the creditor-donee beneficiary distinction. **Intended beneficiary** is the Restatement's term for a third party beneficiary who has an enforceable right.

An **incidental beneficiary** is a third party beneficiary who is neither a creditor nor a donee, and therefore has no enforceable rights under the contract. To determine whether a beneficiary has a right to enforce the contract, use the "intent to benefit" test, which examines who the promisee intended to receive the performance of the contract. If the *promisee* intended to benefit the third party, the third party is a protected beneficiary with enforceable contractual rights.

PARALEGAL EXERCISE 12.1 Uncle Bill promised his nephew, George, that if George would quit smoking cigarettes for one year, Uncle Bill would buy George a new Corvette. George quit smoking for a year.

1. What are the rights and duties between Uncle Bill and George?
2. Is the Chevrolet Motor Company a donee, creditor, or incidental beneficiary of this contract?
3. What are the rights and duties between Uncle Bill and the third party beneficiary?

PARALEGAL EXERCISE 12.2 Alan contracted to sell Greenacre to Graham for Graham's promise to pay \$250,000 according to the following plan: \$10,000 to Alan's nephew Calvin as a graduation gift; \$100,000 to Charge-It Credit Company

as full payment of Alan's last month's charges; and \$140,000 to Benton, a broker, to invest for the benefit of Alan's mother, Margaret.

1. What are the rights and duties between Alan and Graham?
2. Are Calvin, Charge-It Credit Company, and Margaret donee, creditor, or incidental beneficiaries?
3. What are the rights and duties between Graham and the third party beneficiaries?

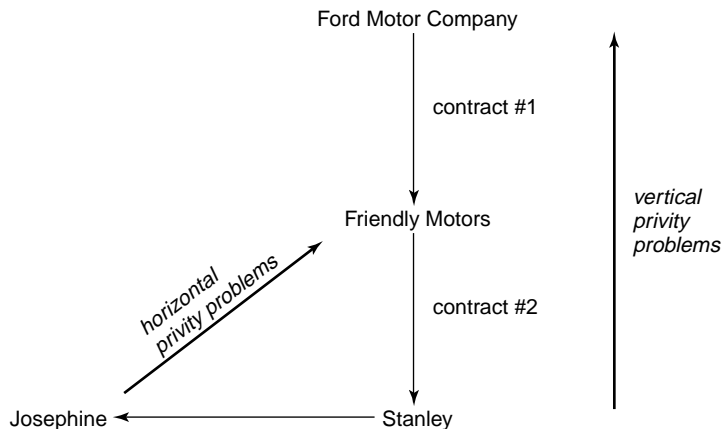
The distinction between intended (creditor and donee) beneficiaries and incidental beneficiaries is important when considering breach of implied warranties in a contract for the sale of goods.

EXAMPLE 12-4

An automobile with a defective wheel was manufactured by Ford Motor Company and sold to Friendly Motors, a dealership. Friendly sold the Ford to Stanley. When Stanley was out on a Sunday drive with his girlfriend, Josephine, the wheel collapsed and the car crashed. Both Josephine and Stanley were injured.

Although Stanley could sue Friendly on his contract with Friendly, could Stanley sue Ford, the deep pocket up the distribution chain? Was Stanley a third party beneficiary of the Ford Motor Company/Friendly Motors contract? Because the three parties are in the distribution chain (as either buyers or sellers), the question is whether Stanley will be barred from suing Ford Motor on the ground that he was not in vertical privity of contract with the Ford Motor Company. The **vertical nonprivity plaintiff** is a buyer in the distribution chain who did not buy directly from the defendant.

Unlike Stanley, who was a buyer, Josephine was not contractually related to either Friendly or Ford. She was not in the distribution chain. The question is whether Josephine is in horizontal privity of contract with Friendly Motors. The **horizontal nonprivity plaintiff** is not a buyer in the distribution chain but one who consumes, uses, or is affected by the goods.



The “privity of contract” language can be translated into donee and incidental beneficiary. A third party who is in privity of contract is a donee beneficiary and has contractual rights. A third party who is not in privity of contract is an incidental beneficiary and has no contractual rights.

Because the subject matter of this illustration is a sale of goods, the Uniform Commercial Code applies. Unfortunately, the Code is silent as to the first question—whether Stanley can sue up the distribution chain. After the enactment of the Code, many courts viewed this legislative silence as an indication that such a suit is prohibited due to a lack of vertical privity of contract.

Recently, a number of courts have abrogated at least a part of the vertical privity requirement. The abrogation has been piecemeal based on the injury sustained by the aggrieved party. Products can cause three different types of injury: personal injury, property damage, and economic loss. Personal injury and property damage have traditionally been compensated under the tort actions of strict liability and negligence. Economic loss has traditionally been compensated in a breach of contract action. Some courts, therefore, found the abrogation of vertical privity for breach of warranty cases involving economic loss a reasonable evolutionary step. Other courts have gone further and have abrogated vertical privity for breach of warranty cases involving personal injury.

The second question—whether Josephine can sue the last seller in the distribution chain—is addressed in the Code. Section 2-318 offers the states a selection among three alternatives. Alternative A extends a seller’s express and implied warranty liability to family and household members and guests in the buyer’s home if it is reasonable to expect that such person may use, consume, or be affected by the goods.

Alternative A

A seller’s warranty whether express or implied extends to any natural person who is in the family or household of his buyer or who is a guest in his home if it is reasonable to expect that such person may use, consume or be affected by the goods and who is injured in person by breach of the warranty. A seller may not exclude or limit the operation of this section.

Alternative B extends the seller’s express and implied warranty liability to any person who may reasonably be expected to use the goods. Alternative B expands coverage to persons beyond the buyer’s family, household, or guests.

Alternative B

A seller’s warranty whether express or implied extends to any natural person who may reasonably be expected to use, consume or be affected by the goods and who is injured in person by breach of the warranty. A seller may not exclude or limit the operation of this section.

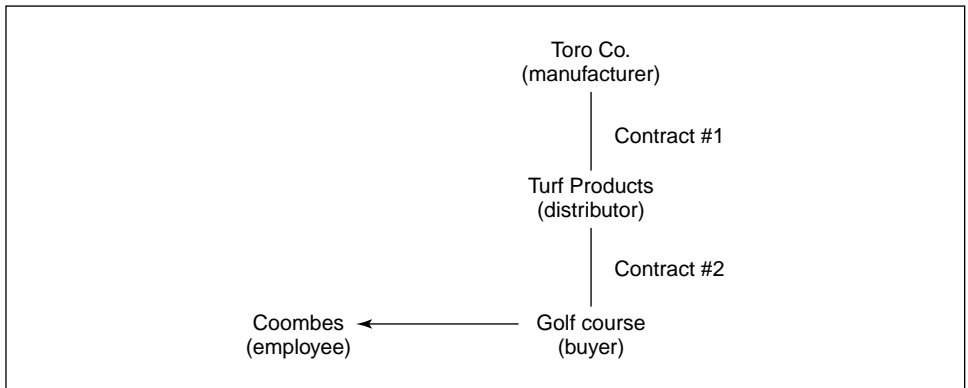
Alternative C is the broadest of the three and expands coverage to business entities.

Alternative C

A seller’s warranty whether express or implied extends to any person who may reasonably be expected to use, consume or be affected by the goods and who is injured by breach of the warranty. A seller may not exclude or limit the operation of this section with respect to injury to the person of an individual to whom the warranty extends.

PARALEGAL EXERCISE 12.3 Is Josephine a donee or incidental beneficiary in the Stanley/Friendly Motors contract? Is the answer the same under the three alternatives of UCC § 2-318?

In *Coombes v. Toro Co.*, The Toro Company manufactured a three-wheel utility vehicle which was distributed by Turf Products Corporation and purchased by a golf course. Coombes, an employee of a golf course sued The Toro Company, the manufacturer, and Turf Products Corporation, the seller, for personal injuries incurred when he was using the vehicle.



1. Does Coombes have a horizontal or vertical privity problem when he sues Turf and Toro?
2. Is Coombes a donee, creditor, or incidental beneficiary of the Toro/Turf contract and of the Turf/golf course contract?
3. Why did the court use UCC § 2-318?
4. Which alternative of UCC § 2-318 was enacted in Connecticut?
5. Did the court correctly apply the facts to the law?
6. Would the result have been the same if Connecticut had enacted either of the other alternatives to section 2-318?

CASE

Coombes v. Toro Co.

Superior Court of Connecticut, 1979. 28 UCC Rep.Serv. 391.

DUPONT, J. Plaintiff is bringing this action to recover for personal injuries allegedly incurred when, in the course of his employment, the engine of a “three wheel utility vehicle”



which he was operating stalled and the brakes failed. As a result, the vehicle rolled backwards down an incline and the plaintiff was thrown to the ground and struck by the vehicle when it overturned. The defendants are The Toro Company which manufactures this model and the Turf Products Corporation which distributes and sells it. The plaintiff-employee was a member of the maintenance crew of a golf course which purchased the vehicle for use by its workers. The action is grounded in negligence, strict tort, and breach of warranty. The defendants have moved to strike that part of the third count which sounds in breach of statutory warranty. The parties have agreed that those portions of the Motion to Strike relating to other counts need not be addressed by the court.

Defendants argue that the complaint does not state a claim upon which relief can be granted because, *inter alia*, count three does not allege that plaintiff is within the category of individuals protected by § 42a-2-318. Resolution of this issue in favor of the defendants is dispositive of the other claims of the Motion to Strike.

The provision governing third-party beneficiaries, CGS § 42a-2-318, was adopted in 1959 and amended in 1965. It is significant to note that although more expansive alternatives to the statute have existed since 1966,¹ the Connecticut legislature has maintained its adherence to Alternative A. The sentence pertaining to the neutrality in the statute apparently refers to developing tort law. See J. White & R. Summers, *Uniform Commercial Code* § 11-3 at 330-31 (1972 ed).

The Supreme Court has not yet considered whether an employee is covered by § 42a-2-318. However, in the only Superior Court case on point, *Chen v. Reliable Rubber & Plastic Machinery Co.*, 5 CLT # 7 at 13 [25 UCC Rep 1274], September 18, 1978, the court held that an employee is not an intended beneficiary. The court relied heavily on the availability of a cause of action in strict tort. Furthermore, the majority of states which like Connecticut, have adopted Alternative A and which have considered the issue at hand have decided that the section does not extend to employees.²

The plaintiff urges that the spirit of various Connecticut warranty decisions should encourage the court to extend coverage to employees. The cases cited were decided under tort principles, however. It has been recognized that "an action based on strict liability is to be distinguished from liability on breach of warranty or simple negligence." *De Felice v. Ford Motor Co.*, 28 Conn Supp 164, 168, 255 A2d 636 (1969), citing *Rossignol v. Danbury School of Aeronautics, Inc.*, 154 Conn 549, 227 A2d 418 [4 UCC Rep 305] (1967). As a result, the import of plaintiff's cited decisions is limited.

Plaintiff also suggests that the *Chen* decision concerning employee coverage is not well reasoned because it is not in accord with the Connecticut decisions extending warranties and does not follow the rationale of jurisdictions which have included employees. As indicated above, however, the warranty decisions were made in accord with tort principles and the majority of Alternative A jurisdictions have denied coverage.

Motion to strike that portion of Count 3 relating to a cause of action in breach of warranty under § 42a-2-318 granted.

1. Alternative B extends warranties to "any natural person who may reasonably be expected to use, consume or be affected by the goods and who is injured in person by the breach of warranty." Alternative C extends to "any person who may reasonably be expected to use, consume or be affected by the goods and who is injured by the breach of warranty." 1A Uniform Laws Annotated 52-53 (1976).

2. The following Alternative A states have not extended the warranties to employees: Alaska, Georgia, Maryland, North Carolina, Ohio, Oklahoma, Tennessee, and West Virginia. The following Alternative A states have extended the warranties to employees: Arkansas, Florida, Maine, and Pennsylvania. 1A Uniform Laws Annotated 74-77 (1976) and 10-11 (Supp 1979).

Third party beneficiary's rights depend on the existence and enforceability of a contract between the contracting parties. If a contract has not been formed, a third party beneficiary does not exist. If a contract exists but the contract is unenforceable, the third party beneficiary cannot enforce the contract.

EXAMPLE 12-5

Mickie contracted to sell Brent her car for Brent's promise to pay the purchase price to Mickie's debtor, Kathy. Mickie misrepresented the car's mileage as 50,000, instead of the correct mileage of 150,000. If Brent disaffirms the contract due to the misrepresentation, Brent no longer has a duty to pay Kathy.

Contracting parties are generally free to make a subsequent agreement to discharge or modify duties to the beneficiary if the beneficiary consents. If, however, the beneficiary does not consent, he or she may still be able to enforce the contract despite efforts by the contracting parties to discharge or modify their duties. The trend is to allow both creditor and donee beneficiaries to enforce the contract when the beneficiary has learned of the contract and has relied on it or brought suit to enforce the contract before receiving notification of the discharge or modification. The equal treatment of creditor and donee beneficiaries in the Restatement (Second) of Contracts supports this trend.

EXAMPLE 12-6

Sneed owed Sanders \$200. Sneed contracted with Johnson for Johnson to pay Sanders the \$200 Sneed owed Sanders. Sneed notified Sanders that Johnson would pay his debt. Later Sneed, in exchange for Johnson's loaning Sneed his lake cabin over Labor Day weekend, released Johnson from his duty to pay Sanders. Ignorant of Sneed's attempted discharge of Johnson's duty, Sanders sued Johnson for \$200. Johnson remained liable to Sanders because Sanders learned of the contract and brought suit to enforce it before receiving notice of the attempted discharge.

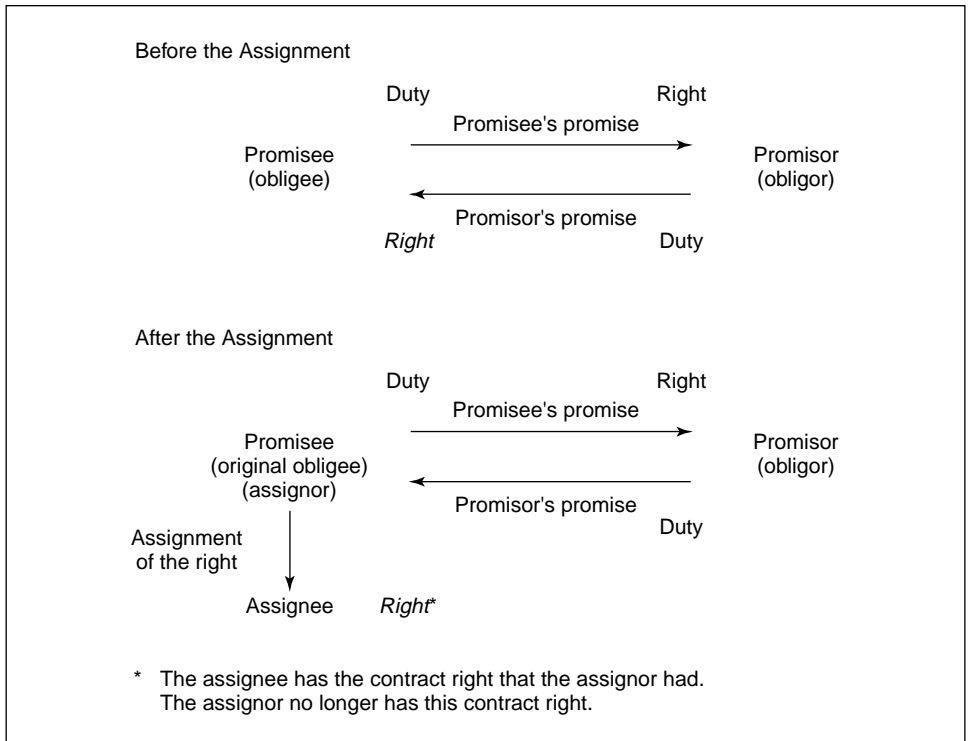
THE ASSIGNMENT OF CONTRACT RIGHTS AND DELEGATION OF CONTRACT DUTIES

After a contract has been formed, it may become advantageous for one of the parties to either sell his or her contractual rights or delegate his or her contractual duties. This section introduces assignment and delegation. Rights are assigned. Duties are delegated.

Assignment

An **assignment** is the transfer of a contract right. The **assignor** is the original promisee and is the party who transfers the contract right. The **assignee** is the party to whom the contract right is transferred.

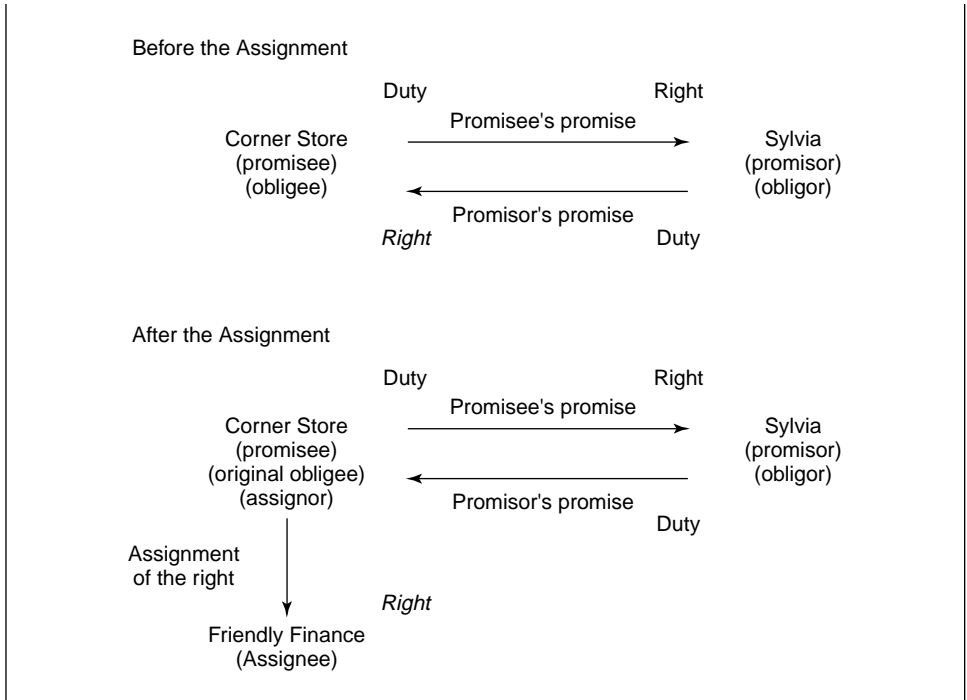
The promisor may also be called an obligor. The **obligor** (promisor) is the party who owes the contract duty associated with the contract right. The promisee may be called the original obligee. The **original obligee** (promisee) is the party to whom the contract right was originally owed.



EXAMPLE 12-7

Corner Store sells a VCR to Sylvia on \$300 credit. Under this contract, Corner Store has a duty to deliver the VCR to Sylvia and a right to have Sylvia pay \$300. Sylvia has a duty to pay Corner Store \$300 and a right to receive delivery of the VCR. Because Corner Store lacks the assets to finance its credit sales, it sells its right to payment to Friendly Finance Company. Friendly pays Corner Store in exchange for Corner Store's right to have Sylvia pay \$300. Once Sylvia is notified of the assignment, she will have a duty to pay Friendly Finance. She will no longer have a duty to pay Corner Store.

In this transaction, Corner Store, the promisee, is the original obligor and the assignor. Sylvia is the obligor. Friendly Finance is the assignee.



Although many rights can be assigned, not all rights may be assigned. Whether a right is assignable depends on whether the transfer of the right will materially alter the duty of the obligor (promisor), the party who must perform the duty associated with that right.

PARALEGAL EXERCISE 12.4 The law firm of Peabody, Anderson & Grable, hired Samantha Stevenson as their legal assistant. The contract had a one-year term. After working for the Peabody firm for several months, Samantha was notified that the firm had transferred its right to her work to O'Sullivan & Mead. Was Samantha's contract assignable?

Whether the transfer of the right will materially alter the duty of the obligor is not the only factor determining whether a contract right can be assigned. A court may place great weight on a well-drafted term in the contract prohibiting the assignment of a contract right. A court may also refuse to enforce an assignment where a special relationship exists between parties. Also many states have statutes that prohibit or limit certain types of assignments.

An assignee takes the assigned rights subject to any defense which the obligor could have set up against the assignor-obligee at the time of the as-

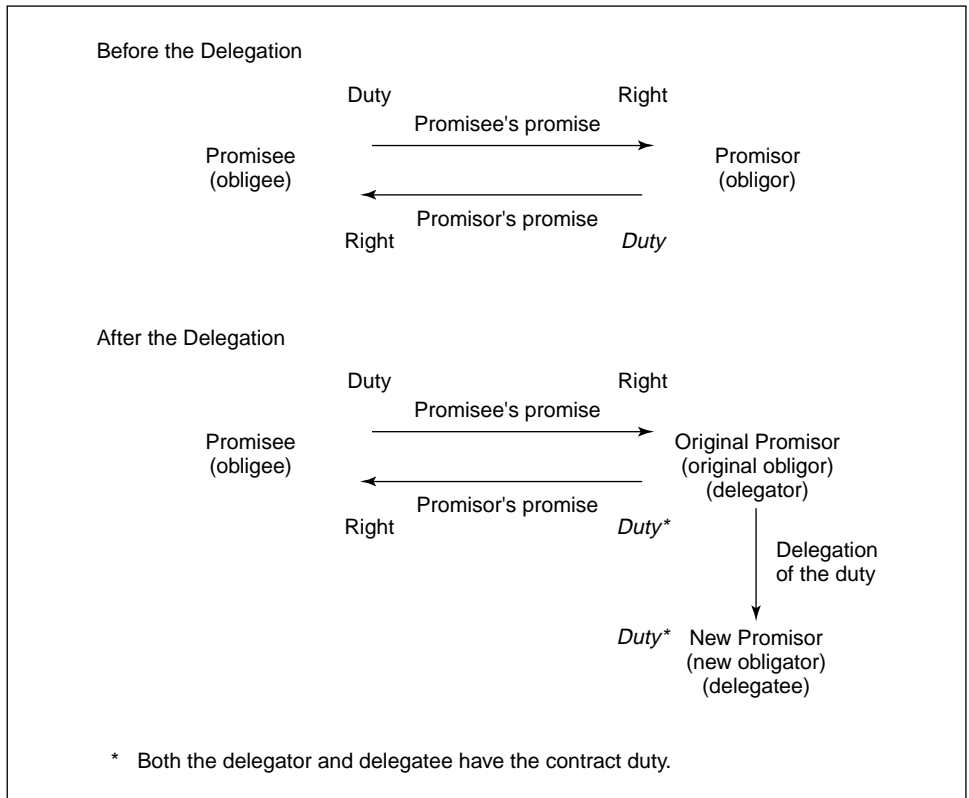
signment. Common defenses include lack of consideration, misrepresentation, fraud, and duress.

PARALEGAL EXERCISE 12.5 A-1 Motors sold a used Volvo to Andre for \$4,500. The sale was a credit sale. A-1 assigned its right to Andre's payment to Consumer Credit. Several days after Andre took possession of the Volvo, he discovered that it had a cracked block and therefore was in breach of the implied warranties of merchantability. The seriousness of this defect in the vehicle would have justified Andre in withholding his time payments.

Must Andre pay Consumer Credit?

Delegation

A **delegation of a contract duty** is an authorization to another party to perform the contract duty. The **delegator** is the original promisor and is the party who delegates the contract duty. The original promisor is also called the original obligor. The **delegatee** is the party who is authorized by the delegator to perform the contract duty. The delegatee is the new promisor and is the new obligor. The promisee is the obligee.



EXAMPLE 12–8

Tony had a contract with the *Evening Gazette* to deliver newspapers. Because Tony's paper route was quite lucrative, he sold it to Michael. Tony delegated his duty to deliver newspapers to Michael.

The act of delegating a duty does not terminate the duty on the part of the delegator. Delegation only increases the number of parties who have the duty.

EXAMPLE 12–9

Barnes delegated his duty to clean Dell's garage to Roberts. If Roberts fails to perform, Dell could receive performance from Barnes.

As was the case with assignment, not all duties may be delegated. Whether a duty is delegable depends on whether the delegation of the duty will materially alter the right of the obligee (the promisee), the party who has the right associated with that duty. The obligee may have a substantial interest in requiring the original obligor to perform, especially when the performance is "personal," involving such qualities as character, reputation, taste, or skill.

EXAMPLE 12–10

Showtime hired the Blue Notes to perform at its club. The Blue Notes could not delegate their duty to perform. Their performance is "personal" because it involves unique talent.

PARALEGAL EXERCISE 12.6 Under Paralegal Exercise 12.4, could Samantha delegate her duty to work for the firm?

Even general rules have exceptions. In *Rossetti v. City of New Britain*, the architectural firm of Rossetti, DiCorcia, and Mileto, a partnership, contracted with the city of New Britain to design a police station and circuit court building. DiCorcia left the partnership and assigned all of his rights and delegated all of his duties to the new partnership, Rossetti and Mileto. This included the contract to design the New Britain police station and circuit court building.

The City ultimately terminated the contract with Rossetti and Mileto and hired another architect for the project. Rossetti and Mileto sued the City for breach of contract. In *Rossetti v. City of New Britain*, 163 Conn. 283, 303 A.2d

714, 718-19 (1972), the court addressed the City's claim that the original partnership's duty was not delegable.

As to the defendant's claim concerning the nonassignability of personal service contracts, it is indeed the general rule that contracts for personal services cannot be assigned. To be technically accurate, it is not the benefits that are nonassignable; rather, it is the duties which are nondelegable. Performance, in other words, cannot be delegated to another. 4 Corbin, Contracts, p. 439; 6 Am.Jur.2d, Assignments, § 11. Thus if a specific artist is hired to paint a picture, the artist cannot delegate his duty of performing. See *LaRue v. Groezinger*, 84 Cal. 281, 24 P. 42; 6 Am.Jur.2d, Assignments, § 13. Personal performance is of the essence. Agreements to render professional services as a physician or lawyer fall within this rule. *Deaton v. Lawson*, 40 Wash. 486, 82 P. 879; *Corson v. Lewis*, 77 Neb. 446, 109 N.W. 735. Whether a duty is personal such that it cannot be delegated, however, is a question of the intention of the parties to be ascertained from the contract, its nature, and the attending circumstances. Clearly, a contract to render architectural services could be one where personal performance is of the essence. *Smith v. Board of Education*, 115 Kan. 155, 222 P. 101. The claims of proof, by which the charge is to be tested, do not support such a conclusion in the case at bar. The defendant's contention is that the contract was personal to the Rossetti, DiCorcia and Mileto partnership. From the claims of proof, however, it is clear that all dealings were with the plaintiff. He was the person in charge of and responsible for the contract. There was nothing offered to show an intent that the plaintiff's partners could not delegate whatever duties they had to the plaintiff. We cannot say that the court erred in its charge in this respect.

Assignment and Delegation

Contracting parties often assign and delegate in one transaction.

EXAMPLE 12-11

Kelly Collins, a professional photographer, has a contract to photograph all of the Fashion Statement's models for one year. Six months into the contract, Kelly decided to move to Milano, Italy. Kelly delegated her duty to photograph all of the Fashion Statement's models for the remainder of the year to Amanda Campbell. Kelly also assigned her right to payment to Amanda. Assuming that Fashion Statement has no objection to the delegation, the Kelly/Amanda transaction is both an assignment and a delegation.

When an assignment and a delegation take place in the same transaction, the transaction is termed an assignment. When analyzing a transaction labeled an assignment, care must be taken to determine whether the transaction also includes a delegation. Note in an assignment, the assignor (original promisee) no longer has the right to receive the promisor's performance. However, in a delegation, the delegator (original promisor) still has the duty to perform.

Substituting and Releasing a Contracting Party: The Novation

A time may come when one of the original contracting parties would like to be replaced by a party who had not been a party to the original contract. This transaction is called a “novation.” A **novation** is a contract between one or both of the original contracting parties and a third party that substitutes the third party in the place of one of the original contracting parties and discharges that party. Often parties attempt a novation but fail to discharge the original contracting party. Substitution without discharge is not a novation.

If the new party is a substitute for the promisor (obligor), the new promisor’s duties may be the same as, or different from, those of the original promisor. If the new party is a substitute for the promisee (obligee), the new promisee’s rights may be the same as, or different from, those of the original promisee.

As a substituted contract, a novation replaces the original contract. The end result of a novation is the immediate discharge of one of the original contracting parties and the creation of a new duty. A novation does not exist until the discharge has been accomplished. Because the novation is substituted for the original contract and the duties in the original contract are terminated, a party is unable to maintain a breach of contract action under the original contract.

A novation may be a simple novation or a compound novation. A simple novation begins with one original contract. In a simple novation (the substitute contract) a new promisor (obligor) is substituted for an original promisor or a new promisee (obligee) is substituted for an original promisee.

EXAMPLE 12–12

Bank One loaned Amanda \$10,000. Subsequently, Stephanie, Amanda’s aunt, promised Bank One that she would pay the bank the amount owed by Amanda if Bank One promised to discharge Amanda’s debt. Bank One promised.

The original contract was between Bank One and Amanda. Bank One promised to loan for Amanda’s promise to repay. As to Amanda’s promise to repay, Amanda is the promisor (has a duty to repay) and Bank One is the promisee (has a right to repayment).

The novation (the substitute contract) was between Bank One and Stephanie. Bank One promised Stephanie to substitute Stephanie for Amanda and to discharge Amanda. Stephanie promised Bank One to pay Amanda’s debt. Under this simple novation, Stephanie is substituted for Amanda as the promisor (has a duty to repay).

EXAMPLE 12–13

Adam loaned Megan \$10,000. Subsequently, Adam married Sarah. Adam promised Megan that he would discharge her debt to him if she promised to pay Sarah the amount she owed him. Megan promised Adam.

The original contract was between Adam and Megan. Adam promised to loan for Megan's promise to repay. As to Megan's promise to repay, Megan is the promisor (has a duty to repay) and Adam is the promisee (has a right to repayment).

The novation (the substitute contract) was between Adam and Megan. Adam promised Megan to discharge her from her duty to pay him. Megan promised Adam that she would pay Sarah. Under this simple novation, Sarah is substituted for Adam as the promisee (has a right to repayment).

The compound novation may begin with one original contract, which is executory on both sides. That is, at the time of making the novation, both parties had duties outstanding and both parties were promisors and promisees. As with the case of a simple novation, a third party becomes involved. The third party assumes both the duties and rights of one of the original contracting parties.

EXAMPLE 12–14

Adam promised to deliver a tractor to Ben for Ben's promise to pay Adam \$1,000. Subsequently, Adam promises Ben and Carol to deliver a bulldozer to Carol and to discharge Ben's duty to pay him \$1,000 if Ben promises to discharge Adam's duty to deliver the tractor to him and if Carol promises to pay \$2,000 to Adam. Ben and Carol promise.

The original contract was between Adam and Ben. Adam promised to deliver a tractor to Ben for Ben's promise to pay \$1,000. As to Adam's promise to deliver, Adam is the promisor (has the duty to deliver) and Ben is the promisee (has the right to receive delivery). As to Ben's promise to pay, Ben is the promisor (has the duty to pay) and Adam is the promisee (has the right to receive payment).

The novation (the substitute contract) was among Adam, Ben and Carol. Adam promised both Ben and Carol to deliver the bulldozer to Carol in exchange for Ben's promise to discharge him from his duty to deliver the tractor to him and for Carol's promise to pay him \$2,000. Under this compound novation, Carol is substituted for Ben as both promisor (promise to pay) and promisee (right to receive the bulldozer). Adam is discharged from his duty to deliver the tractor to Ben and Ben is discharged from his duty to pay Adam.

The compound novation may also begin with two original contracts with one party being common to both. In the novation (the substitute contract), the three parties to the original contracts agree that the party common to both contracts shall drop out.

EXAMPLE 12–15

Anthony contracted with Best Construction for Best to provide materials and remodel Anthony's restaurant. Best subcontracted with the Century Lumber Company for Century to

supply the materials. Century supplied the materials and Best incorporated some of these materials into Anthony's restaurant. For some reason, the construction halted. Anthony promised Best and Century that he would discharge Best from its duty to complete the remodeling and he would pay Century what Best owed Century for the materials if Best promised to discharge Anthony from his duty to pay Best and Century promised to discharge Best from Best's duty to pay Century. When Anthony, Best, and Century promised, a novation was formed, Anthony's duty to pay Best was discharged, and Best's duties to Anthony and Century were discharged. Anthony now has a duty to pay Century for the materials supplied.

THIRD PARTY'S INTERFERENCE WITH EXISTING CONTRACT RIGHTS

In most states, one who interferes with the contractual relationship of others may be liable for harming their contractual relationship. The cause of action is known as "tortious interference with a contract."

The party claiming interference can maintain this cause of action by demonstrating the following elements:

1. an enforceable contract existed;
2. the party inducing the breach knew of the contract;
3. the interfering party intentionally induced the breach;
4. the interfering party induced the breach unjustifiably; and
5. the party claiming interference was damaged by the breach of contract.

The first element, an enforceable contract, is demonstrated by the information in Chapters 2 through 5 and 7 through 9.

The second element, knowledge of the contract, can be established by proving that the interfering party had either actual or constructive knowledge of the contract. Constructive knowledge means that the party who interfered knew facts that would cause a reasonable person to believe that a contract existed.

The third element, that the interfering party intentionally induced the breach, requires a showing that the interfering party acted intentionally to induce a breach. The inducement may include threats, coercion, or economic persuasion. Some jurisdictions do not require actual breach of contract. These jurisdictions require only that the party somehow disrupt the contractual relationship. Generally, a party acts intentionally if he or she acts with the purpose of bringing about a particular result. Some courts reject the intent requirement and demand only a showing that the party interfering knew his or her acts would result in a breach.

The fourth element is a showing that the party inducing the breach was unjustified in his or her actions. Generally, courts do not consider the breaching of a contract for personal gain to be "justified." Some courts go a bit further and require that the act be wrongful, malicious, or unjust, which indicates an interpretation stronger than "unjustified."

The fifth and final element is a showing that the party complaining of the interference was damaged by the interference. The most traditional aspects of harm are those damages related to the breaching of a contract.

The courts have applied various remedies in tortious interference of contract cases. One remedy is injunctive relief. The injunction forces a party to cease any activities that are designed to result in breach of a contract. If a breach has already occurred, an injunction may be of little consequence. Courts, however, will frequently award a traditional measure of contract damages. Some courts will also award punitive damages.

PARALEGAL EXERCISE 12.7 Carriers, Inc., delivered the *Times* newspaper to subscribers. The *Post*, a rival newspaper, liked the job that Carriers was doing so much that it hired Carriers to deliver its newspaper to its subscribers. The Carriers/*Post* contract stated that Carriers must deliver all the newspapers that the *Post* printed.

Recently, the *Post* doubled its production, thereby placing a heavy burden on Carriers. Because of the increased burden, Carriers informed the *Times* that it might have to cancel its contract with them. Unfortunately, Carriers was the only delivery company in town and the *Times* did not have its own delivery system.

Will the *Times* be successful in its suit against the *Post* for tortiously interfering with its contract? If so, what should be the remedy?

The following cases, *R. C. Hilton Associates, Inc. v. Stan Musial & Biggie's, Inc.* and *Ahern v. Boeing Co.*, add perspective on how courts deal with the tortious interference issue. Check each case for the five elements necessary for maintaining the action.

CASE

R. C. Hilton Associates, Inc. v. Stan Musial & Biggie's, Inc.
United States Court of Appeals, Eleventh Circuit, 1983. 702 F.2d 907.

Before GODBOLD, Chief Judge, RONEY, Circuit Judge, and PITTMAN*, District Judge.

GODBOLD, Chief Judge:

A real estate broker, R. C. Hilton Associates, Inc., brought this action to recover a commission on the sale of a hotel. Initially Hilton's agent visited the hotel to determine whether it was for sale. An agent of Stan Musial & Biggie's, Inc. (Musial), the owner, advised Hilton that the hotel might be for sale for \$4.25 million, net to owner. Musial stated that it did not intend to pay any sales commission and that Hilton would have to make arrangements for

*Honorable Virgil Pittman, U.S. District Judge for the Southern District of Alabama, sitting by designation.



its commission with the buyer. Hilton subsequently initiated discussions between Musial and Edward Stern. After a short period of negotiations (in which Hilton did not participate) Stern agreed to purchase the hotel for \$4.12 million. No commission was paid to Hilton.

Hilton brought suit against Musial and Stern in Florida state court. The defendants removed the case to federal court based on diversity.

The complaint contains three counts: (1) a breach of contract action against Musial; (2) a claim of tortious interference with a business contract against Stern; and (3) an unjust enrichment claim against Musial for the value of services rendered. The case was referred to a United States Magistrate acting as a special master pursuant to Fed.R.Civ.P. 53. After a non-jury trial the magistrate made findings of fact and conclusions of law and recommended that judgment be entered against Hilton on all counts. The district court adopted and confirmed the magistrate's findings and conclusions. We affirm.

The district court ruled that Hilton had neither an express nor implied contract with Musial. Hilton argues that the district court's conclusion that no contract existed is inconsistent with its findings of fact. The court found that Musial told Hilton that "anything over \$4.25 million is yours." Hilton contends that in making this statement Musial agreed to pay a commission. To support this contention Hilton relies on the court's statement that "since the sale price was less than [\$4.25 million] there is no basis for a claim predicated upon an express agreement." According to Hilton, the court concluded that an agreement would have existed had the price exceeded \$4.25 million. This argument, however, is expressly refuted in both the findings of fact and conclusions of law where the district court explicitly stated that no contract existed.

Hilton next argues that, even if no formal agreement existed, a broker is entitled to recover a commission for services rendered in the sale of real estate.

[I]n the absence of any special agreement, when a seller places property with a broker for sale, he impliedly agrees to pay a customary commission to the broker.

Kerdyk v. Hammock Oaks Estates, Inc., 342 So.2d 833, 835 (Fla.App.1977).

The authorities cited by Hilton are inapposite. In the case before us Musial did not place the property with Hilton for sale; Hilton obtained no listing. Also, Musial explicitly informed Hilton that it did not intend to pay a sales commission. "A broker cannot recover for his services unless they were rendered at the express or implied request of his employer. . . ." *City Builders' Finance Co. v. Stahl*, 90 Fla. 357, 106 So. 77, 78 (Fla.1925); *George G. Massey & Assoc. v. Borgemeister*, 297 So.2d 577 (Fla.App.1977). The finding of no contractual liability should be affirmed.

Hilton seeks recovery from Stern for malicious interference with a "business contract." The district court concluded: "Although a claim for tortious interference may be based upon a contractual agreement which is not legally enforceable, no recovery is allowed if there is no contractual relationship at all." On appeal Hilton argues that the existence of a contract is not necessary in order to recover for tortious interference with a "business relationship." Even assuming that the court should have liberally interpreted Hilton's claim for tortious interference with contract as a claim for tortious interference with business relationship, see *Smith v. Ocean State Bank*, 335 So.2d 641 (Fla.App.1976), Hilton has failed to establish its right to recover.

To establish a claim for tortious interference with business relationship the plaintiff must prove:

the existence of a business relationship under which the plaintiff has legal rights;
an intentional and unjustified interference with that relationship by the defendant;
and damage to the plaintiff as a result of the breach of the business relationship.

Fearick v. Smugglers Cove, Inc., 379 So.2d 400, 403 (Fla.App.1980).

Initially, the broker had the burden of establishing an advantageous relationship with the seller. A broker can not recover for his services unless they were rendered at the express or implied request of his employer and a contract for services will not be implied unless the vendor knows or has reasonable grounds to believe that they were rendered with the expectation of receiving payment therefor.

Retzky v. J. A. Cantor Associates, Inc., 192 So.2d 24, 26 (Fla.App.1966). Hilton failed to prove that its services were rendered at the express or implied request of Musial. Having failed to establish an advantageous relationship with the seller, Hilton's tort claim against Stern fails.

Hilton also seeks recovery from Musial under an unjust enrichment theory. The district court denied relief, concluding:

the Florida cases discussing broker's commissions state quite emphatically that a broker is not entitled to a commission for his services unless there is either an express contract, or one that is implied from the factual situation. The authorities thus negate the theory of unjust enrichment as a basis for the recovery of a broker's commission.

The parties did not cite, nor did our research reveal, any precedent inconsistent with the district court's decision. Even assuming that a broker could recover under an unjust enrichment theory, Hilton's claim would still fail. In *Yeats v. Moody*, 128 Fla. 658, 175 So. 719, 720 (Fla.1937), the Florida Supreme Court stated:

It is well settled that where services are rendered by one person for another which are knowingly and voluntarily accepted, without more, the law presumes that such services are given and received in the expectation of being paid for, and will imply a promise to pay what they are reasonably worth.

In the present case Musial clearly informed Hilton that it did not intend to pay a sales commission. Thus, Hilton's services could not reasonably be "given and received in the expectation of being paid for. . . ."

AFFIRMED.

CASE

Ahern v. Boeing Co.

United States Court of Appeals, Eleventh Circuit, 1983. 701 F.2d 142.

Before HILL, KRAVITCH and HENDERSON, Circuit Judges.

KRAVITCH, Circuit Judge:

Appellants appeal from summary judgment granted to appellee by the district court. We conclude that the district court, 539 F.Supp. 1210, applied an incorrect legal standard to the facts of this case; therefore we reverse and remand for trial on the merits.

In 1976, "A & O," a partnership in which appellants were partners, entered into an agreement with Scientific Energy Engineering, Inc., ("SEE") covering the testing, production, sales, and leasing aspects of an incinerator device. A prototype of the incinerator was installed for testing on appellants' property. In May 1977, the agreement was modified to grant



appellants the exclusive marketing rights to the incinerator. The agreement as modified did not contain an express durational provision, but did contain references to termination upon default of either of the parties.

SEE and A & O subsequently experienced some difficulties in their relationship, and SEE filed a state court action in September 1978, seeking declaratory relief and damages. While the state action was pending, SEE entered into negotiations with Boeing Company regarding the incinerator. On June 7, 1979, Boeing executed an option agreement with SEE and its principals, which gave Boeing an option to acquire the marketing rights to the incinerator and other products. Boeing exercised the option and on February 14, 1980, Boeing, SEE, and its principals entered into a marketing agreement. Appellants contend that this agreement directly interfered with the exclusive marketing rights that SEE had granted them.

On April 24, 1980, the state trial court entered a final declaratory judgment and declined to award SEE damages. The court found that the joint venture agreement granted certain marketing rights to the appellants, but that the contract was terminable at will by either party upon thirty days notice. Shortly after the state court judgment was entered and after the contract with Boeing had taken effect, SEE notified the appellants that it was terminating the marketing agreement with A & O. Appellants then filed this action in Florida state court seeking compensatory and punitive damages against Boeing for alleged tortious interference with the business relationship between A & O and SEE. The case was removed to federal district court pursuant to 28 U.S.C. §§ 1332 and 1441. After discovery was concluded, Boeing moved for summary judgment, and the district court granted the motion.

Under Florida law, to establish a cause of action for tortious interference, a party must demonstrate:

1. the existence of an advantageous business relationship under which that party has legal rights;
2. an intentional and unjustified interference with that relationship by the defendant; and
3. damage to the plaintiff as a result of the interference with the business relationship.

Unistar Corporation v. Child, 415 So.2d 733, 734 (Fla.3d Dist.Ct.App.1982); *Wackenhut Corporation v. Maimone*, 389 So.2d 656, 657 (Fla. 4th Dist.Ct.App.1980); *Lake Gateway Motor Inn v. Matt's Sunshine Gift Shops, Inc.*, 361 So.2d 769, 771 (Fla.4thDist.Ct.App.1978). The Florida courts have determined that "an action will lie where a party tortiously interferes with a contract terminable at will." *Unistar Corporation*, 415 So.2d at 734. Thus, where the plaintiff shows "an intentional and unjustified interference with an existing business relationship which causes damage to the plaintiff," a prima facie case is established, and the burden then shifts to the defendant to justify its actions. *Id.* at 734-35. "If the defendant can prove that the interference was lawful competition—a privilege which the courts recognize when the contract is terminable at will—the defendant will not be found to have committed the tort of wrongful business interference." *Id.* at 735 (citing *Insurance Field Services, Inc. v. White & White Inspection and Audit Service, Inc.*, 384 So.2d 303 (Fla.5th Dist.Ct.App.1980); W. Prosser, *Handbook of the Law of Torts* § 129, at 932, 946 (4th ed. 1971)).

The district court focused upon this privilege of competition in granting Boeing's motion for summary judgment. The court found that Boeing was motivated by no ill will toward A & O, but only by competitive interests, a finding we do not dispute. The court, however, concluded that Florida law protects interference with at-will contracts as long as the motivation for that interference is deemed "proper." The trial court in its opinion and order granting summary judgment, stated:

that where, as here, there is a contract terminable at will and part of defendant's motivation for interfering with that contract was to advance defendant's business interests, the interference is privileged as competition and is therefore justified as a matter of law.

We believe that the judge erred in her reading of the Florida case law. In the recent trilogy of cases cited above, the Florida courts ruled that the plaintiffs had not established the requisite unjustified interference with their business relationships. In none of the cases did the defendant actually enter into a contract that interfered with the existing at-will contract of the plaintiff. In *Lake Gateway Motor Inn*, the plaintiff was a gift shop operator who had an at-will contract with the motel. The motel notified the plaintiff that it was exercising its rights to terminate the contract upon thirty days notice. The gift shop operator then negotiated with a possible successor, but that successor also held discussions with the motel. The successor found that the motel would contract with him if he paid the motel the amount due the gift shop operator under the “buy-out” clause of the at-will contract. The court found no tortious interference because the successor and the motel had not entered into a contract interfering with the gift shop’s operation. The privilege of competition, the court held, protects solicitation for future business, not interference with existing contracts. The court summarized its reasoning as follows:

Assuming all alleged actions of the successor were as bad as the appellee paints them, (although this is disputed) said successor went to the motel and solicited a take over of the gift shop, having heard it was to be available. Such competition seems to us to be par for the course in the free enterprise system. Can not the IBM salesman solicit this court to change over from a Xerox copier? *Of course he can, unless he suggests to us that we violate a contract with Xerox in so doing.*

In the case at bar, there is no proof that the successor operator sought to persuade the motel to break a contract or strip his predecessor of some legal rights.

Lake Gateway Motor Inn, 361 So.2d at 772 (emphasis added).

The district court concluded that the determining factor under Florida law is the motivation of the alleged tortfeasor. Motivation is *not*, however, the guiding star in the constellation of Florida’s common law of tortious interference. The case law clearly demonstrates that mere self-interested and competitive solicitation will not constitute tortious interference with an at-will contract, so long as the third party does not induce the breach of or interference with that existing contract.

Viewing the facts in the light most favorable to the nonmoving party as we must in reviewing a grant of summary judgment, *Northwest Power Prods., Inc. v. Omark Indus., Inc.*, 576 F.2d 83, 85 (5th Cir.1978), cert. denied, 439 U.S. 1116, 99 S.Ct. 1021, 59 L.Ed.2d 75 (1979), we conclude that appellants have alleged a prima facie case showing that Boeing went much further than the mere solicitation that would be protected under Florida’s privilege of competition. We hold, therefore, that appellants are entitled to present their case to a jury. The order of the district court granting summary judgment is REVERSED, and the case REMANDED for trial.



PARALEGAL CHECKLIST

Third Party Interests

- A paralegal must sometimes be concerned with parties other than those contracting. These parties include third party beneficiaries, assignees, delegates, and third parties who interfere with existing contract rights (tortfeasors). Regardless of

the situation, the first step in an analysis requires the paralegal, with the supervision of an attorney, to determine the existence of a contract. Without a contract, there can be no third party beneficiary, assignee, delegatee, or tortfeasor. Use the following guidelines to evaluate whether a contract exists.

1. Who does the contract benefit? A third party beneficiary contract is a contract for the benefit of a third party.
 - a. Is the third party a donee or a creditor beneficiary? A donee or a creditor beneficiary has enforceable contractual rights. An incidental beneficiary has no enforceable contractual rights. The Restatement (Second) of Contracts does not distinguish between donee and creditor beneficiaries but identifies both as intended beneficiaries. Focus on the intent of promisor to determine whether a beneficiary is an intended beneficiary.
 - b. Does the third party have rights and duties under the contract? A third party beneficiary has only contractual rights (no duties) under the contract.
 - c. Is there a third party beneficiary who can enforce the contract? A third party beneficiary's rights depend on the existence and enforceability of a contract between the contracting parties.
 - (1) If a contract has not been formed, a third party beneficiary does not exist.
 - (2) If a contract exists but is unenforceable, the third party beneficiary cannot enforce the contract.
 - d. Can the beneficiary enforce the contract? Contracting parties are generally free to make a subsequent agreement to discharge or modify duties to the beneficiary if the beneficiary consents. If the beneficiary does not consent, he or she may be able to enforce the contract despite efforts by the contracting parties to discharge or modify their duties. The trend is to allow both creditor and donee beneficiaries to enforce the contract when the beneficiary has learned of the contract and has relied on it or has brought suit to enforce the contract before receiving notification of the discharge or modification.
2. Did the parties retain their contractual rights and duties? After a contract has been formed, the parties may either sell contractual rights or delegate contractual duties.
 - a. Was there an assignment of contract rights? An assignment of a contract is the transfer to another of the rights due under the terms of the contract.
 - (1) Many, although not all, rights can be assigned. Whether a right is assignable depends on whether the transfer of the right will materially alter the duty of the obligor—the party who must perform the duty associated with that right.
 - (2) An assignee takes the assigned right subject to any defense that the obligor could have raised against the assignor-obligee at the time of the assignment.
 - b. Was there a delegation of a duty? A delegation of a duty is an authorization to another party to perform the duty.
 - (1) The party who delegates the duty is the delegator and the party who is authorized to perform the duty is the delegatee. The party who has the right to receive performance of the duty is the obligee.
 - (2) The act of delegating a duty does not terminate the duty on the part of the delegator. Delegation only increases the number of parties who have the duty.
 - (3) Not all duties may be delegated. Whether a duty is delegable depends on whether the delegation of the duty will materially alter the right of the obligee. The obligee may have a substantial interest in requiring the original obligor to perform.
 - c. Has there been a novation? A novation occurs when one of the original contracting parties is replaced by a party who was not a party to the original contract. A novation is a contract that discharges a party to the contract, sometimes an obligor and sometimes an obligee, and substitutes a new party in his or her place.
 - (1) If the new party is an obligor, the obligor may have the same or different duties as the original obligor. If the new party is an obligee, the new obligee may have the same or different rights as the original obligee.
 - (2) Although novations come in different forms, what is critical is that a third party, one who was not a party to the original contract, must be added and either the original obligor or the original obligee must be discharged.

- (3) As a substitute contract, a novation replaces the original contract. Because the novation is substituted for the original contract and the duties in the original contract are terminated, a party is unable to maintain a breach of contract action under the original contract.
3. Has there been interference in the contract by a third party? One who interferes with the contractual relationship of others may be liable for harming this relationship. The cause of action is known as "tortious interference with a contract." A party claiming interference must be able to answer the following questions affirmatively:
- Did an enforceable contract exist?
 - Did the party inducing the breach know of the contract?
 - Did the interfering party intentionally induce the breach?
 - Did the interfering party induce the breach unjustifiably? and
 - Was the party claiming interference damaged by the breach of contract?

REVIEW QUESTIONS

DEFINE THE FOLLOWING NEW TERMS AND PHRASES

Assignee	Horizontal privity
Assignment	Incidental beneficiary
Assignor	Intended beneficiary
Creditor beneficiary	Novation
Delegatee	Obligee
Delegation	Obligor
Delegator	Third party beneficiary contract
Donee beneficiary	Vertical privity

TRUE/FALSE QUESTIONS (CIRCLE THE CORRECT ANSWER)

- T F A third party beneficiary contract is a contract made for the benefit of a third party.
- T F A contract made for the benefit of a third party beneficiary may not be enforced by that third party.
- T F In a third party beneficiary contract all three parties have both rights and duties.
- T F A third party beneficiary contract is subject to the same rules of contract formation as any other contract.
- T F Under classical common law and the Restatement (First) of Contracts (1932), there are three types of third party beneficiaries.
- T F If a party contracts to give a third party a gift, the third party is an incidental beneficiary.
- T F If a party contracts to discharge a prior obligation that the promisee had with a third party, the third party is a creditor beneficiary.

8. T F A beneficiary who is neither a creditor nor a donee beneficiary is an incidental beneficiary.
9. T F An incidental beneficiary has enforceable rights under the contract.
10. T F There is no distinction between intended and incidental beneficiaries when considering breach of implied warranties in a contract for the sale of goods.
11. T F The “vertical” nonprivity plaintiff is a buyer in the distribution chain who did not buy directly from the defendant.
12. T F The “horizontal” nonprivity plaintiff is not a buyer in the distribution chain but one who consumes, uses, or is affected by the goods.
13. T F A third party who is in privity of contract is a donee beneficiary and has contractual rights.
14. T F A third party who is not in privity of contract is an incidental beneficiary and has no contractual rights.
15. T F Even if the contracting parties cannot enforce the contract, the third party beneficiary can enforce it.
16. T F Contracting parties are free to make a subsequent agreement to discharge or modify duties to the beneficiary without consent of the beneficiary.
17. T F Contracting parties may delegate their rights and assign their duties.
18. T F An assignment of a contract is a transfer to another of the rights due under the terms of the contract.
19. T F All rights may be assigned.
20. T F A right will not be assignable if the transfer of the right will materially alter the duty of the obligor, the party who must perform the duty associated with that right.
21. T F A court may refuse to enforce an assignment when there is a well-drafted term in the contract prohibiting the assignment of a contract right.
22. T F A court will not take into account a special relationship between the parties when deciding whether to enforce an assignment.
23. T F A delegation of a duty is an authorization to another party to perform the duty.
24. T F Not all duties may be delegated.
25. T F Whether a duty is delegable depends on whether the delegation of the duty will materially alter the right of the obligee, the party who has the right associated with that duty.
26. T F A party who was not a party to the original contract may not replace one of the original contracting parties.
27. T F A novation is a contract that discharges a party to the contract and substitutes a new party in place of the original party.
28. T F A party may still maintain a breach of contract action under the original contract when a novation has been substituted for the original contract.

29. T F Novations may be simple or compound.
30. T F A novation is not created if the new contract merely adds the third party without discharging the original obligor.
31. T F In most states, one who interferes with the contractual relationship of others will not be liable for harming their contractual relationship.
32. T F In most states, one who interferes with the contractual relationship of others may be sued for tortious interference with a contract.
33. T F Courts may offer injunctive relief in tortious interference of contract cases in which a third party is engaged in activities designed to result in breach of a contract.
34. T F Courts frequently award a traditional measure of contract damages in tortious interference of contract cases.
35. T F Courts never award punitive damages in tortious interference of contract cases.

FILL-IN-THE-BLANK QUESTIONS

1. _____. A contract made for the benefit of a party other than the two contracting parties.
2. _____. The party who has contractual rights but no contractual duties in a third party beneficiary contract.
3. _____. The party who will receive a gift under a third party beneficiary contract.
4. _____. The third party who benefits when a party contracts to discharge a prior obligation that the promisee had with the third party.
5. _____. The term used by the Restatement (Second) of Contracts for the third party beneficiary who has an enforceable right.
6. _____. A beneficiary who is neither a creditor nor a donee beneficiary.
7. _____. A nonprivity plaintiff who is a buyer in the distribution chain who did not buy directly from his or her seller's seller.
8. _____. A nonprivity plaintiff who is not a party in the distribution chain but who consumed, used, or was affected by the goods.
9. _____. The transfer to another of the rights due under the terms of the contract.
10. _____. An authorization to another party by the obligor to perform the obligor's contractual duty.

11. _____. A contract between one or both of the original contracting parties and a third party.
12. _____. A novation that substitutes a new obligor for the original obligor or a new obligee for the original obligee.
13. _____. A novation that may involve one original contract in which a new contract replaces an executory contract where one party to the new contract was a party to the original contract, or two original contracts with one party being common to both contracts.
14. _____. The cause of action that may be filed against one who interferes with the contractual relationship of others.

MULTIPLE CHOICE QUESTIONS (CIRCLE ALL THE CORRECT ANSWERS)

1. Aunt Jean promised to give her car to Tommy if Tommy would promise to drive his sister Charlotte to school every morning. This transaction illustrates:
 - (a) a donee beneficiary
 - (b) a creditor beneficiary
 - (c) an incidental beneficiary
 - (d) an assignment
 - (e) a delegation
2. Harvey borrowed \$500 from Charlie. Sarah borrowed \$500 from Harvey and promised him that she would repay the \$500 to Charlie. The second transaction illustrates:
 - (a) a donee beneficiary
 - (b) a creditor beneficiary
 - (c) an incidental beneficiary
 - (d) an assignment
 - (e) a delegation
3. Adam promised to loan \$10,000 to Bridget for Bridget's promise to repay the loan at 8% interest. Cary promised Bridget to loan her the \$10,000 if she would promise to substitute Cary for Adam and to release Adam from his obligation to loan her the \$10,000. Bridget promised Cary.

The second transaction illustrates:

 - (a) a donee beneficiary contract
 - (b) a creditor beneficiary contract
 - (c) an assignment of a right
 - (d) a simple novation with substitution of promisors (obligors)
 - (e) a simple novation with substitution of promisees (obligees)

SHORT ANSWER QUESTIONS

1. Discuss how courts determine whether a third party beneficiary has a right to enforce the contract (i.e., whether the beneficiary is a donee or incidental beneficiary).
2. Describe the difference between a party who is a vertical nonprivity plaintiff and one who is a horizontal nonprivity plaintiff.
3. Describe the difference between an assignment and a delegation.
4. List four basic variations of novations.
5. Define the two essential elements of a novation.
6. List the elements that a party claiming interference with a contractual relationship must demonstrate.



Briefing Cases and Analyzing Statutes

Textbooks used by paralegals include a number of court decisions. Reported cases will generally be at the appellate level because most states do not report trial court decisions for publication. Although trial court decisions resolve both factual and legal issues, appellate decisions will generally consider only legal issues. Appellate decisions are rendered in cases that originated at the trial court level. One of the disputants, unhappy with the trial court's decision, has asked a higher court to review the decision of the lower court.

Textbooks for paralegal courses usually include not only cases but statutes as well. Both of these forms of the law will be used extensively in preparing clients' cases.

HOW TO BRIEF A CASE

Students must dissect assigned cases to be able to participate in and follow the class discussion. One outline form for dissecting judicial opinions is called a "brief." Some faculty members will require students to read their written briefs in class. Most assume that students have written a brief prior to class. The information generated in a brief is usually the focal point for classroom discussion.

Many faculty members will give students guidance on how they want them to brief for their classes. Students may find it convenient to use the following

briefing format as the starting point, refining it to conform to each faculty member's suggestions. This format uses the headings: "Case Name," "Pre-Trial Facts," "Action," "Decision(s)," "Issue," "Rule," "Application," and "Conclusion."

Case Name

The case name, jurisdiction, court, year, and page in the casebook are written in this order.

EXAMPLE A-1

Laredo Hides Co. v. H&H Meat Prods. Co. (TX Civ. App. 1974) p. 2
Use *A Uniform System of Citation* as the guide to case names.

Pre-Trial Facts

State the key facts. Omit non-key facts.

"A fact in an opinion is a key fact when the result in the opinion would have been different if that fact had been altered."

W. Statsky & R. Wernet, *Case Analysis and Fundamentals of Legal Writing* 164 (1977).

For many courses, the key facts will include only pre-litigation facts—those facts that led to the lawsuit. The filing of the lawsuit will be discussed under "Action," and the various judicial decisions will be discussed under "Decisions." The brief, under this format, will follow events in chronological order.

At the pre-litigation stage, neither a plaintiff nor a defendant exists. Do not, therefore, refer to a plaintiff or to a defendant in the statement of the facts. Refer to the disputants by name. Referring to the disputants as plaintiff and defendant at the pre-litigation stage violates **Cardinal Rule #1** (see Figure A-1).

The statement of facts should be long enough to trigger an accurate recollection of the case but short enough to represent a substantial condensation of the court's statement of the facts. The entire brief should be no longer than one page (if at all possible). An excessively long brief violates **Cardinal Rule #2**.

Action

This step covers who is suing whom, the name of the action, and the nature of the relief requested.

EXAMPLE A-2

Laredo Hides sued H&H for breach of contract seeking specific performance and damages.

The “who is suing whom” should designate the disputants by name rather than “plaintiff sued defendant.”

The “name of the action” or “cause of action” should be separated from the “remedy.” For example, breach of contract is a cause of action, damages is a remedy; negligence is a cause of action, damages is a remedy.

Remember that the “Action” step in the brief is the entry into the trial court. This is the court where the lawsuit is initiated (by petition or complaint) and the trial held. Including extraneous material in “Action” violates **Cardinal Rule #3**.

Decision(s)

This step involves highly technical material that should flow in chronological order.

Look ahead to the appellant’s alleged error. The appellant will complain that the trial court erroneously sustained the opposing counsel’s demurrer, motion for summary judgment, motion for judgment notwithstanding the verdict (judgment n.o.v.), or motion for a new trial, or erroneously overruled his or her own demurrer or motion. Begin the “Decision(s)” section of the brief with a statement regarding this procedural move (that is, error asserted). Follow with the trial court’s resolution of this procedural move. Finally, state the trial court’s finding in the case and who appealed.

Next, consider the first appellate court and state how the case was resolved on appeal. If the case has been appealed to a still higher court, state who appealed and how the case was resolved.

Begin each sentence with the name of the court followed by what that court did. Do this for each court.

EXAMPLE A-3

The District Court (without a jury) sustained Smith’s motion for summary judgment. Jones appealed. The Texas Court of Civil Appeals reversed and remanded the case for trial.

Issue

The issue must have two components:

- (1) the key facts to which the rule is being applied, and
- (2) the rule of law being applied. (Statsky & Wernet 216.)

An issue that omits either the fact or rule component violates **Cardinal Rule #4**.

State the issue in one sentence in question form. An issue not stated in one sentence violates **Cardinal Rule #5**.

Work enough facts into the issue so that the brief will still mean something two weeks after the case has been briefed.

If the case involves several issues, state the issue, rule, application, and conclusion for the first issue. Repeat these steps for subsequent issues.

Rule

The rule is the legal statement that governs the resolution of the issue.

The rule may emanate from the United States or a State Constitution or the Bill of Rights, a statute, ordinance, administrative regulation, or a prior case (case law). Because the rules form the structure for the substantive or procedural area being studied, students must think about how these rules relate to one another.

Application

Apply the facts to the rule.

By the time this step is reached (because this is an appellate case, it will by nature emphasize the law rather than the facts), the application in most cases will be straightforward.

Conclusion

The conclusion returns to the issue and states how the issue was resolved based on this set of facts.

A brief that states only a conclusion and omits the rule and application violates **Cardinal Rule #6**.

In briefing, students should not merely rewrite the court's opinion. They should think about what is said and put it into the briefing format in their own words. Some judicial opinions have shortcomings. Astute briefing identifies

these shortcomings. A brief that merely restates the court's opinion violates **Cardinal Rule #7**.

Do not rewrite the court's opinion to the extent that the brief no longer follows the court's rationale. (If the opinion is resolved by common law, for example, do not use the Uniform Commercial Code in the brief.) A brief that disregards the court's rationale and goes its own merry way violates **Cardinal Rule #8**.

Once the brief is completed, students should consider what they would have done if they had been the court. Specifically:

1. Is the court deciding the appropriate issue?
2. Is the court using the appropriate rule?
3. Is the application of facts to rule correct?
4. Based on social and economic needs of the community, is the rule sound? Should a different rule be promoted? If so, what would it be and why?

FIGURE A-1 Cardinal Rules

Cardinal Rule #1.	During the pre-litigation stage, do not refer to the disputants as plaintiff and defendant.
Cardinal Rule #2.	Do not write an excessively long brief.
Cardinal Rule #3.	Do not include extraneous material in the "Action."
Cardinal Rule #4.	An "Issue" must contain both fact and rule components.
Cardinal Rule #5.	An "Issue" must be stated in a single sentence.
Cardinal Rule #6.	A brief must contain the rule and application and not just a conclusion.
Cardinal Rule #7.	Do not just restate the court's opinion.
Cardinal Rule #8.	Do not disregard the court's rationale and go your own merry way.

Postscript

A memorandum could be organized around the "Issue," "Rule," "Application," "Conclusion" format of briefs. Begin with the issue. The issue would be followed by the rule, the application of rule to facts, and the conclusion for that issue.

If the memorandum has more than one issue, begin the next section with the next issue, continuing in this manner until all issues are covered. As students develop their briefing technique, they are also developing their writing technique.

HOW TO ANALYZE CONSTITUTIONS, STATUTES, REGULATIONS, AND OTHER RULES

Law created to address existing or potential concerns includes constitutions, statutes, regulations, executive orders, and ordinances. It comes into existence focusing not on one dispute but on a number of pending and hypothetical disputes or concerns. It is created in a deliberate process. Hearings are often held to gain information to enable the drafter or drafters to fully comprehend the problem and write a law that will apply to a range of situations. As a result, the law often appears cumbersome because it aims not at one target but at multiple targets.

As students research the constitutional provisions, statutes, and other rules, they must dissect them to understand them thoroughly. The following outline uses a decision tree approach. This approach is helpful in identifying the various components of the law and how they relate to one another. Does all the language of a statute apply to each problem governed by the statute? If not, which phrases apply and which do not?

The student's initial task is to find the elements of the law that apply to the problem. The simplest form of law will have all the elements arranged linearly with no choice between elements.

EXAMPLE A-4

The Uniform Commercial Code § 2-201(2) provides:

(2) Between merchants if within a reasonable time a writing in confirmation of the contract and sufficient against the sender is received and the party receiving it has reason to know its contents, it satisfies the requirements of subsection (1) against such party unless written notice of objection to its contents is given within 10 days after it is received.

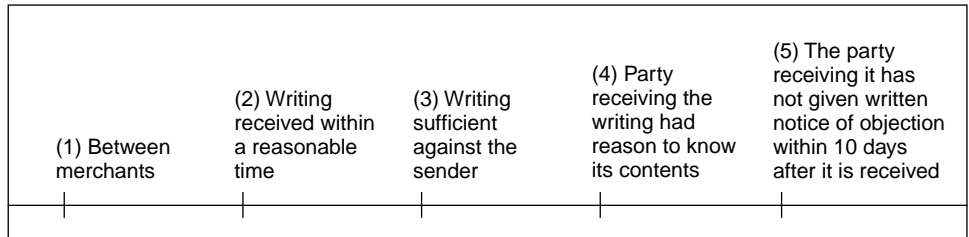
A writing satisfies the requirements of section (1) [2-201(1)] against the party receiving it if:

1. the writing was sent between merchants;
2. the writing was received within a reasonable time;
3. the writing is sufficient against the sender;

4. the party receiving the writing had reason to know its contents; and
5. the party receiving the writing has not given written notice of objection to the writing's contents within 10 days after receiving it.

A decision tree of 2–201(2) would be a straight line because there are no choices within the statute (see Figure A–2). All elements of the statute must be met for it to be applicable.

FIGURE A–2 Decision Tree of a Statute with No Disjunctives



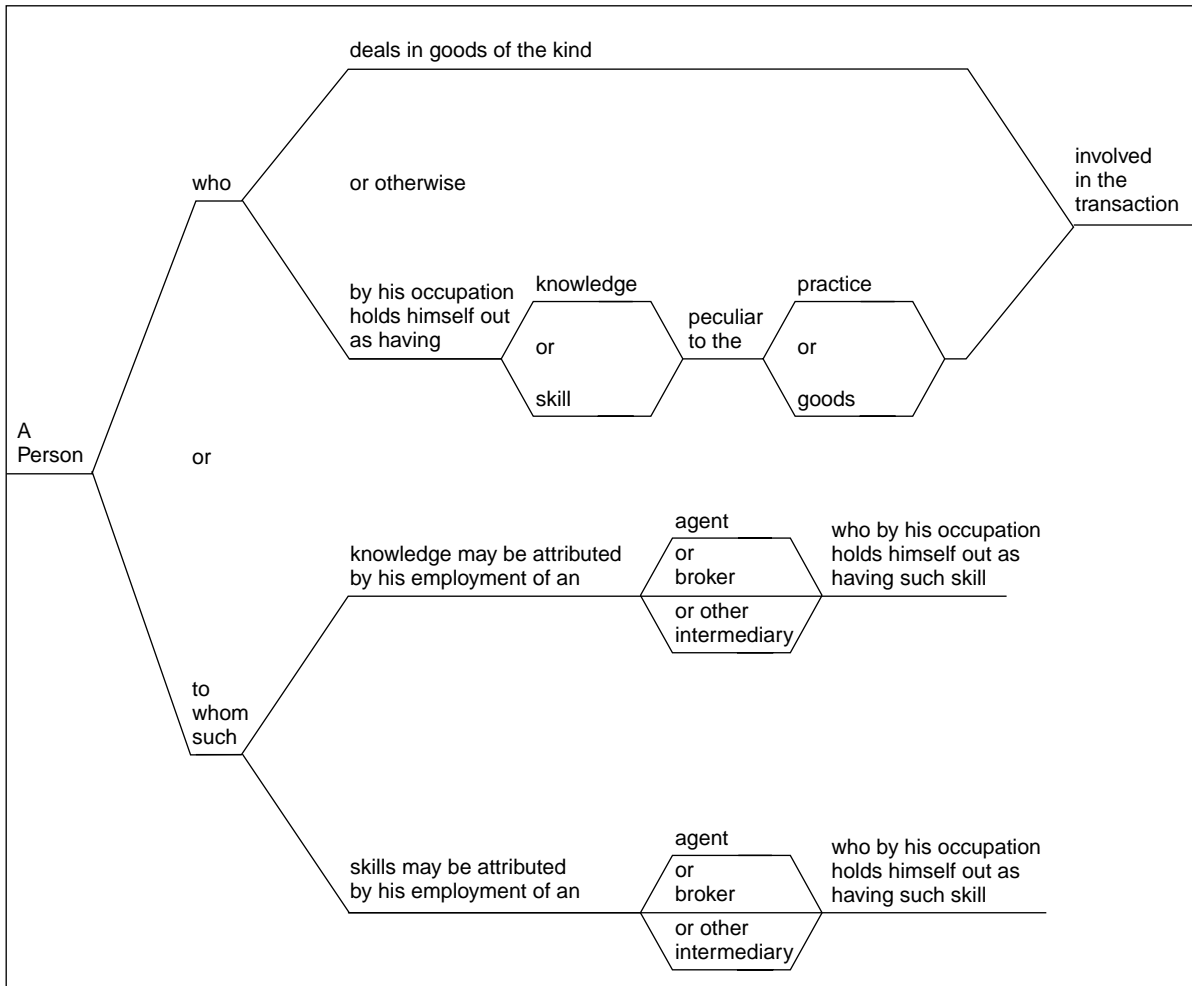
To develop a decision tree that has a number of choices, divide a statute using the word “or” as a starting point. Each “or” will indicate a choice in the decision tree. The reader must choose between one branch or the other. Since “or” is disjunctive, only one branch will need to be used when resolving a dispute. By applying the facts to each decision in the tree, students will select the appropriate avenue.

EXAMPLE A–5

The Uniform Commercial Code § 2–104(1) defines the term “merchant” when used in transactions that involve a sale of goods.

“Merchant” means a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction or to whom such knowledge or skill may be attributed by his employment of an agent or broker or other intermediary who by his occupation holds himself out as having such knowledge or skill.

This definition uses “or” eight times. Since “or” is disjunctive, some phrases in this statute will be applicable to some problems and some to others. The trick is to identify which phrases apply to which problems. Tracing the various branches in section 2–104(1) shows that a person could be a merchant if he or she fits into one of eleven different scenarios (see Figure A–3):

FIGURE A-3 Decision Tree of a Statute with Disjunctives

1. He or she is a person who deals in goods of the kind involved in the transaction;
2. He or she is a person who by his or her occupation holds himself or herself out as having knowledge peculiar to the practice involved in the transaction;
3. He or she is a person who by his or her occupation holds himself or herself out as having knowledge peculiar to the goods involved in the transaction;
4. He or she is a person who by his or her occupation holds himself or herself out as having skill peculiar to the practice involved in the transaction;

5. He or she is a person who by his or her occupation holds himself or herself out as having skill peculiar to the goods involved in the transaction;
6. He or she is a person to whom such knowledge may be attributed by his or her employment of an agent who by his or her occupation holds himself or herself out as having such knowledge;
7. He or she is a person to whom such knowledge may be attributed by his or her employment of a broker who by his or her occupation holds himself or herself out as having such knowledge;
8. He or she is a person to whom such knowledge may be attributed by his or her employment of another intermediary who by his or her occupation holds himself or herself out as having such knowledge;
9. He or she is a person to whom such skill may be attributed by his or her employment of an agent who by his or her occupation holds himself or herself out as having such skill;
10. He or she is a person to whom such skill may be attributed by his or her employment of a broker who by his or her occupation holds himself or herself out as having such skill; or
11. He or she is a person to whom such skill may be attributed by his or her employment of another intermediary who by his or her occupation holds himself or herself out as having such skill.



Answers to the Review Questions

Introduction. A Road Map for Analyzing the Law of Contracts

TRUE/FALSE QUESTIONS

- | | |
|-------|--|
| 1. T | 13. T |
| 2. T | 14. T |
| 3. T | 15. F |
| 4. T | (The defendant is saying “my nonperformance was justified by your breach,” not “my breach was justified by your breach.” An admission of breach (rather than just nonperformance) will permit the plaintiff to receive a breach of contract remedy.) |
| 5. T | 16. T |
| 6. F | 17. T |
| 7. F | 18. F |
| 8. T | |
| 9. F | |
| 10. T | |
| 11. F | |
| 12. T | |

FILL-IN-THE-BLANK QUESTIONS

- | | |
|------------------|------------------------------|
| 1. Choice of law | 5. Promise for a promise |
| 2. Offer | 6. Promise for a performance |
| 3. Offeror | 7. No breach, compliance |
| 4. Offeree | 8. No breach, excuse |

- | | |
|--------------------------------|----------------------------|
| 9. No breach, justification | 12. "Expectation interest" |
| 10. No breach, terminated duty | 13. "Reliance interest" |
| 11. Breach | 14. "Restitution interest" |

MULTIPLE CHOICE QUESTIONS

- | | |
|-------------------|--------|
| 1. (a) & (b) | 5. (b) |
| 2. (a), (b) & (c) | 6. (c) |
| 3. (e) | 7. (d) |
| 4. (a) | |

SHORT ANSWER QUESTIONS

- The five steps in the road map for the law of contracts are:
 - Step One: Determining the applicable law (choice of law)
 - Step Two: Contract formation
 - Step Three: Contract enforceability
 - Step Four: Breach of contract
 - Step Five: Plaintiff's remedies for the defendant's breach of contract
- The three settings in which a choice of law question may arise are:
 - when the transaction takes place in a number of states or nations;
 - when several sets of rules within a state appear to apply to the transaction;
 - when federal and state rules appear to be competing.
- the promisor's promise
 - the consideration for the promisor's promise
 - the fact that the promisor made a promise to induce the promisee to make a promise.
- In an offer for a bilateral contract, the consideration for the promisor's promise is the promisee's promise. In an offer for a unilateral contract, the consideration for the promisor's promise is the promisee's performance, not the promisee's promise.
- Since consideration is a crucial element of both offer and acceptance, the conclusion of offer could not be reached without determining the existence of consideration. Therefore, it would be redundant to list consideration as an element separate from offer. The same could be said about acceptance.
- the promisee's promise
 - the consideration for the promisee's promise
 - the fact that the promisee's promise was intended to secure the promisor's promise
- The offer may have lapsed
 - The offeror may have revoked the offer
 - The offeree may have rejected the offer
 - The offeror or offeree may have died or become incapacitated
- a selected class of people unable to protect themselves
 - a contracting party from the overreaching of the other contracting party
 - the integrity of the judicial process
- No breach, compliance
 - No breach, excuse
 - No breach, justification
 - No breach, terminated duty
 - Breach

Chapter 1 Determining the Rules Governing the Dispute

TRUE/FALSE QUESTIONS

- | | |
|------|-------|
| 1. T | 9. T |
| 2. F | 10. T |
| 3. T | 11. F |
| 4. F | 12. T |
| 5. F | 13. F |
| 6. T | 14. F |
| 7. T | 15. F |
| 8. F | 16. T |

FILL-IN-THE-BLANK QUESTIONS

- | | |
|-----------------------------------|--|
| 1. Choice of Law | 7. Federal Preemption Doctrine |
| 2. Common Law | 8. Forum state |
| 3. Statutory Law | 9. Party Autonomy Rule |
| 4. UCC or Uniform Commercial Code | 10. "Center of gravity," "grouping of contacts," or "most significant relationship theory" |
| 5. Article 2 | 11. Article 2A |
| 6. Hybrid transaction | |

MULTIPLE CHOICE QUESTIONS

- | | |
|------------------------|-------------------|
| 1. (a) & (d) | 4. (d) |
| 2. (a), (b) & (e) | 5. (b), (c) & (d) |
| 3. (a), (c), (d) & (e) | |

SHORT ANSWER QUESTIONS

- "This agreement shall be governed and interpreted in accordance with the laws of the State of California."
- (1) the chosen state has no substantial relationship to the parties or the transaction, or
(2) the result obtained from the applicability of the law of the chosen state would be contrary to the forum state's public policy.
- This is a hybrid transaction. The painting is a sale of a service. Supplying the paint is a sale of goods. Whether Article 2 applies depends on which is the predominant factor of this transaction, the sale of goods or the service. It could be argued that the purpose of the transaction was the painting of the house and the paint itself was incidental to the work. Therefore, the predominant factor would be the service and Article 2 of the UCC would be

inapplicable. The contract could be enforced without being in writing.

4. Under the federal preemption doctrine, state law must give way to federal law when

federal law either expressly regulates the matter or when a particular subject is regarded as being beyond the bounds of state action.

Chapter 2 The Offer Phase

TRUE/FALSE QUESTIONS

- | | |
|-------|-------|
| 1. T | 30. F |
| 2. T | 31. F |
| 3. F | 32. T |
| 4. T | 33. T |
| 5. T | 34. T |
| 6. T | 35. T |
| 7. T | 36. T |
| 8. T | 37. T |
| 9. T | 38. F |
| 10. T | 39. F |
| 11. T | 40. F |
| 12. F | 41. F |
| 13. T | 42. T |
| 14. F | 43. F |
| 15. F | 44. F |
| 16. F | 45. F |
| 17. T | 46. T |
| 18. T | 47. T |
| 19. F | 48. F |
| 20. F | 49. T |
| 21. F | 50. T |
| 22. T | 51. F |
| 23. F | 52. F |
| 24. F | 53. F |
| 25. T | 54. T |
| 26. T | 55. F |
| 27. F | 56. T |
| 28. T | 57. T |
| 29. T | 58. F |

59. T

60. T

61. T

62. T

63. F

64. T

FILL-IN-THE-BLANK QUESTIONS

- | | |
|----------------------------|---------------------------------|
| 1. The reasonable person | 13. Illusory promise |
| 2. Objective standard | 14. Indefinite promise |
| 3. Subjective standard | 15. Sham consideration |
| 4. Auction without reserve | 16. Pre-existing duty |
| 5. Auction with reserve | 17. Restitution cause of action |
| 6. Unilateral contract | 18. Promissory estoppel |
| 7. Bilateral contract | 19. Judicial construct |
| 8. Gap fillers | 20. Quantum meruit |
| 9. Consideration | 21. Unjust enrichment |
| 10. Reliance | 22. Implied by law promise |
| 11. Promise | 23. Implied in fact promise |
| 12. Illusory promise | |

MULTIPLE CHOICE QUESTIONS

- | | |
|------------------------|------------------------|
| 1. (a), (c), (d) & (e) | 6. (a) & (b) |
| 2. (b) or (c) | 7. (a), (b), (d) & (e) |
| 3. (b), (d) & (e) | 8. (b) |
| 4. (b) | 9. (b) & (d) |
| 5. (b) & (c) | 10. (e) |

SHORT ANSWER QUESTIONS

1. A subjective standard evaluates a communication in light of how the person making the communication would evaluate it. An objective standard evaluates a communication in light of how a reasonable person would interpret it. A subjective standard is the “meeting of the minds” standard. An objective standard is the “manifestation of assent” standard.
2. If the offer is for a unilateral contract, the offeree’s full performance is acceptance. If the offer is for a bilateral contract, the offeree’s promise is acceptance.
3. The problem of past services is a timing problem. The promisor must make his or her promise to induce the promisee to either promise or perform. If the promisee has already performed services, the promisor

- would not be making his or her promise to induce the promisee to perform. There would be no bargained for exchange.
4. To evaluate whether the son's moving back to town is consideration for the father's promise or only a condition is a question of inducement. Did the father make his promise to induce his son to move back to town? If not, then moving back to town would be only a condition to receiving the performance of the father's promise.
 5. Some legislatures have enacted statutes to eliminate the need for consideration if the promise is in writing. Others require a writing with an additional express statement whereby the promisor promises to be legally bound. Still others will shift the presumption so the promise is presumed to have been made for consideration.
 6. Some courts may imply a previously existing promise if timing is a problem. Courts may also use detrimental reliance (promissory estoppel) as an alternative for consideration.
 7. (1) Promise by the promisor; (2) promisor should reasonably expect the promisee to rely on his or her promise; (3) promisee does rely; and (4) injustice would occur if the promise were not enforced.
 8. (1) Promise by the promisor; (2) promisor should reasonably expect the promisee to rely on his or her promise; (3) promisee does rely; and (4) injustice would occur if the promise were not enforced.
 9. Ricketts's promise to give his granddaughter the note lacks consideration since he is not demanding that she do something in return for the note. She could stop working if she so desired. The note only placed her in the position to have the choice. Therefore, Katie could not maintain a breach of contract action under classical contract law.
 She could maintain a breach of contract action using the doctrine of reliance as an alternative to consideration. Grandfather promised to give her his note. He reasonably expected her to rely on his promise by his statement that she could stop work. His giving of the note was intended to afford her this opportunity. She did rely by quitting work. Injustice would occur if his promise were not enforced because she has lost not only her employment position but also the income while she relied. Therefore, detrimental reliance as found in the Restatement (Second) of Contracts § 90 could be used as an alternative to consideration. Thus a contract without consideration would be formed. Grandfather's estate breached by not paying and Katie would be entitled to a remedy.
 10. Because a contract is not formed in the pre-offer phase of the transaction, neither party has expectations based on a contract. Therefore, if the parties walk away without a contract being formed, neither could successfully claim injury to an expectation interest.
 11. In the pre-offer phase, if one party acts or refrains from acting because he or she is relying on the other party's encouragement, a reliance interest that courts may protect comes into being even though no offer has been made. The reliance interest is protected by means of a reliance cause of action and not by means of a breach of contract action.
 12. If one party confers a benefit on another, the courts may recognize a restitution cause of action, separate and apart from an action for breach of contract, to compensate the party who conferred the benefit. This action is based on unjust enrichment.
 13. An implied by law contract is the same as an implied contract and both are judicial constructs (i.e., figments of the courts' imagination). Implied by law contract and implied contract are other names for a restitution cause of action. An implied in fact contract is a real contract and forms the basis for a breach of contract action.
 14. A person is officious when he or she interferes in the affairs of another by conferring an unnecessary or unwanted benefit.

Chapter 3 The Post Offer/Pre-Acceptance Phase

TRUE/FALSE QUESTIONS

- | | |
|-------|-------|
| 1. F | 12. F |
| 2. T | 13. F |
| 3. F | 14. T |
| 4. T | 15. T |
| 5. F | 16. F |
| 6. F | 17. T |
| 7. T | 18. T |
| 8. T | 19. T |
| 9. T | 20. T |
| 10. T | 21. F |
| 11. F | 22. T |

FILL-IN-THE-BLANK QUESTIONS

- | | |
|----------------------|----------------------------|
| 1. A reasonable time | 6. Implied option contract |
| 2. Revocation | 7. Express option contract |
| 3. Rejection | 8. Section 45 |
| 4. Counteroffer | 9. Section 87(2) |
| 5. Option contract | 10. Section 87(2) |

MULTIPLE CHOICE QUESTIONS

- | | |
|------------------------|------------------------|
| 1. (a), (b), (c) & (d) | 6. (a), (b), (c) & (e) |
| 2. (b) & (e) | 7. (b) & (c) |
| 3. (e) | 8. (a) & (e) |
| 4. (b) & (e) | 9. (a), (b), (d) & (e) |
| 5. (a), (b) & (c) | 10. (c) & (e) |

SHORT ANSWER QUESTIONS

1. First consider the City's offer. Does the offer state how long it will remain open? If the offer does not state a termination date, it will remain open for a reasonable time. A reasonable time may be determined by such factors as the City's urgency in acquiring the property, the timetable established by the City to acquire property, the location of the property in relation to the schedule of the work to be done, the amount of the offer in relation to the value of the property, and the history of the City's acquisition of property for similar projects.
2. Katy's letter of March 1st was an inquiry about price and therefore was preliminary negotiation. A-1's letter of March 5th left nothing open for negotiation and therefore was an offer. Katy's letter of March 10th was a rejection because it stated a quantity different from that of the offer (100,000 rather than 50,000). Katy's letter of March 10th was also a counteroffer because it left nothing open for negotiation. A-1's letter of March 15th was a rejection since it turned down Katy's counteroffer. Katy's letter of March 20th was a new offer. A-1's response of March 25th was another rejection, this time a rejection of Katy's offer of March 20th. Without an acceptance of an offer, no contract was formed.
3. Martha made an offer for a unilateral contract to John, "I promise to pay if you perform." When Martha died, John's power of acceptance terminated so that when he performed his duties as executor, he could not exercise the power to accept her offer. Therefore, no contract was formed.
4. Charles not only offered to sell Mary Blackacre but also offered to enter into an option contract. Mary accepted the offer for the option contract thus preventing Charles from revoking for 60 days. Charles's attempted revocation was ineffective. When Mary attempted to accept Charles's offer to sell Blackacre, her acceptance was effective and a contract was formed.
5. Martina made an offer for a unilateral contract when she promised to pay Rachael for teaching Erica French during the summer. This offer could only be accepted by full performance, that is teaching Erica French during the summer. Under classical contract law, Martina could revoke her offer prior to full performance (prior to the end of the summer). Under classical contract law, the offer would be revoked and there would be no contract.
Under modern contract law, since there was no express option contract that would preclude Martina from revoking her offer, Restatement (Second) of Contracts § 45 must be consulted. Under this section of the Restatement, an implied option contract would be created when Rachael began her performance, that is, when she began teaching Erica French. Under the Restatement, however, Martina could not revoke her offer but Rachael must fully perform for a contract to be formed. The same result would be achieved under Restatement (Second) of Contracts § 87(2), which applies to offers for both unilateral and bilateral contracts.
6. Martina made an offer for a bilateral contract when she promised to pay Rachael for Rachael's promise to teach Erica French during the summer. This offer could only be accepted by Rachael's promise to teach Erica French during the summer. Under classical contract law, Martina could revoke her offer prior to Rachael's promise. Under classical contract law, the offer would be revoked and there would be no contract.
Under modern contract law, since there was no express option contract that would preclude Martina from revoking her offer, Restatement (Second) of Contracts § 87(2) must be consulted. Under this section of the Restatement, an implied option contract would be created when Rachael began her preparation, that is, when she began her lesson plans and purchases. Under the Restatement Martina could not revoke her offer but Rachael must promise to teach Erica French for a contract to be formed. Rachael did this and a contract was formed. Martina's attempted revocation would constitute a breach of contract.

Chapter 4 The Acceptance Phase

TRUE/FALSE QUESTIONS

1. T
2. F
3. T
4. F
5. F
6. F
7. F
8. T
9. T
10. F
11. T
12. T
13. T
14. F
15. F
16. F
17. T
18. T
19. T
20. F
21. F
22. F

FILL-IN-THE-BLANK QUESTIONS

1. Acceptance phase
2. Unilateral contract
3. Bilateral contract
4. Mirror image rule
5. Pre-existing duty rule
6. Offeror
7. Boilerplate
8. "Mailbox" rule
9. Restitution action
10. Last shot doctrine
11. A mistake in understanding the offer
12. Offeror
13. Acceptance

MULTIPLE CHOICE QUESTIONS

1. (c) & (d)
2. (c) & (d)
3. (c) & (e)
4. (a) & (e)
5. (c) & (d)
6. (a)

SHORT ANSWER QUESTIONS

- Bernadette's letter of March 1st was an offer. This offer, however, was not received by Agnes until March 4th. When Agnes wrote Bernadette on March 2d, she was not responding to Bernadette's offer and therefore could not accept that offer. An acceptance must be in response to an offer.

Agnes's letter of March 2d was an offer. Bernadette did not respond to this offer so she did not accept this offer and no contract was formed.
- Jose's letter was an offer for a unilateral contract (a promise to pay for painting the portrait). An offer for a unilateral contract is accepted by full performance (the completed portrait). To accept the offer, however, the offeree must have knowledge of the offer. Under the Restatement (First) of Contracts § 53 (1932), the offeree must have knowledge prior to the beginning of her performance. Therefore, since Charlene did not have knowledge prior to beginning to paint, her full performance would not be acceptance of Jose's offer. Under the Restatement (Second) of Contracts § 51 (1979), the offeree must have knowledge prior to completing her performance. Therefore, since Charlene did have knowledge prior to completing the portrait, her full performance would constitute acceptance and a contract was formed.
- John made an offer for a bilateral contract (John's promise for his father's promise). The acceptance would be John's father's promise for John's promise. John, however, had a pre-existing duty to support his daughter until she became 18. Therefore, his promise could not be consideration for his father's promise. Without consideration, there was no acceptance of John's offer. [Note that this question could be answered that there was no offer by John since he had a pre-existing duty and therefore his promise in the offer was ineffective.]
- Uncle Bob's offer is for a unilateral contract (Uncle Bob's promise to pay \$5,000 for Sam's refraining from smoking and drinking until he was 21). The method for accepting an offer for a unilateral contract is full performance. Therefore, Sam's promise is irrelevant and is not an acceptance.

Chapter 5 The Post-Acceptance Phase

TRUE/FALSE QUESTIONS

- | | |
|-------|-------|
| 1. T | 13. F |
| 2. F | 14. F |
| 3. T | 15. T |
| 4. F | 16. T |
| 5. F | 17. T |
| 6. T | 18. T |
| 7. F | 19. F |
| 8. T | 20. T |
| 9. T | 21. F |
| 10. T | 22. F |
| 11. F | 23. T |
| 12. F | 24. T |

- | | |
|-------|-------|
| 25. T | 31. T |
| 26. T | 32. F |
| 27. T | 33. F |
| 28. T | 34. T |
| 29. F | 35. F |
| 30. F | 36. T |

FILL-IN-THE-BLANK QUESTIONS

- | | |
|------------------------|--|
| 1. Plain meaning | 8. Mistake in integration |
| 2. Trade meaning | 9. Clear and convincing |
| 3. Parol evidence rule | 10. Modification |
| 4. An integration | 11. Release |
| 5. Parol evidence | 12. Accord and satisfaction |
| 6. Parol evidence rule | 13. The acceptance of this check constitutes payment in full |
| 7. Gap fillers | |

MULTIPLE CHOICE QUESTIONS

- | | |
|-------------------|--------------|
| 1. (a) & (c) | 3. (a) & (c) |
| 2. (a), (c) & (e) | 4. (a) & (c) |

SHORT ANSWER QUESTIONS

- The term 50% has two meanings. The plain meaning is that 50% is 50%. The trade meaning is that 50% is 49.5%. The Seller's meaning will prevail if both parties are members of the trade that equates 50% with 49.5%. The Buyer's meaning will prevail if the Buyer was new to the trade unless he or she had actual knowledge of the trade meaning or the trade meaning was so generally known that actual knowledge could be inferred.
- The parol evidence rule only applies if the contract was reduced to a final writing (an integration). In this transaction, the contract was never reduced to a final writing and the parol evidence rule is inapplicable.
- Are the terms of this contract limited to those in the final writing (the integration)? Under the parol evidence rule, evidence extrinsic to the final writing may be admitted to demonstrate that the contract included terms beyond the final writing. The extrinsic evidence (the agreement to build the pool) occurred prior to the final writing. The extrinsic evidence concerning the pool dealt with a subject that was not covered by the final writing (the integration was limited to the sale of the house). Therefore, the extrinsic evidence did not add to or contradict the final writing but dealt with a topic independent of the final writing. The parol evidence rule would not exclude this evidence and the agreement regarding the pool would be a part of the contract even though it was not the subject of the final writing.

4. Since there was a final writing (an integration), the parol evidence rule would apply to exclude prior or contemporaneous parol evidence that would add to or contradict terms in the final writing. The extrinsic evidence sought to be admitted was prior to the final writing. The extrinsic evidence dealt with the terms in the final writing. Unless the court held that the extrinsic evidence was admissible to interpret the terms in the final writing, it would be inadmissible as adding to or contradicting the final writing.
5. The oral agreement between the Bollingers and Central expressed their real intentions. The integration, by omitting reclamation, did not conform to the oral contract. This omission was due to a mutual mistake because at the time the oral contract was reduced to writing, both parties believed that the integration included soil reclamation. Since the evidence was clear and convincing that soil reclamation was omitted due to mutual mistake, the integration should be reformed.
6. A problem involves a mistake in integration when the final writing does not accurately reflect the agreement of the parties. One party seeks reformation of the final writing to accurately reflect the agreement. A problem involves the parol evidence rule when one party claims that the final writing does not include all the terms of the contract. This party does not intend to have the final writing reformed. Rather, this party would like the contract to be more encompassing than the final writing so that some terms of this contract are in the final writing and some are not.

Chapter 6 Drafting a Contract

TRUE/FALSE QUESTIONS

- | | |
|------|-------|
| 1. F | 9. T |
| 2. T | 10. F |
| 3. T | 11. T |
| 4. F | 12. T |
| 5. F | 13. F |
| 6. F | 14. F |
| 7. T | 15. F |
| 8. F | 16. T |

FILL-IN-THE-BLANK QUESTIONS

- | | |
|------------------|-------------------|
| 1. a. allow, let | i. force, effect |
| b. or | j. because |
| c. whether | k. free, clear |
| d. then | l. full, complete |
| e. because | m. from, or |
| f. when | n. consideration |
| g. during, while | o. affect |
| h. sue | p. tend |

- q. (omit entirely and start with the subject)
- r. void
- s. time
- t. before
- u. after
- v. permit
- w. consideration
- x. whether, the question whether
- y. this topic
- z. no contract
2. a. by
- b. because of
- c. by, under
- d. for
- e. to
- f. by, under
- g. since
- h. with, about, concerning
- i. for
- j. when
- k. instead
- l. to
- m. about
- n. about, concerning
- o. although
- p. in
- q. like
- r. because
- s. by, from
- t. by
- u. until
- v. except
- w. about, concerning
- x. about, concerning
- y. on, about
3. a. collide
- b. decide
- c. pay
- d. eliminate
- e. reject
- f. disapprove
- g. isolate
- h. possess
- i. affiliate
- j. apply
- k. abduct
4. a. accommodate
- b. coming
- c. defendant
- d. demurrer
- e. occurred
- f. definite
- g. existence
- h. separate
- i. surprise
- j. truly
- k. until
- l. writing
- m. written
- n. parole evidence
- o. Statute of Frauds

SHORT ANSWER QUESTIONS

1. a. The trial judge ruled.
- b. Stacey Jackson won the race.
- c. My brother told the biggest lie.
- d. The wrecker towed the bus.
- e. A shot at the buzzer won the game.
- f. The same few people did the work.
2. a. The clock is a valuable antique.
- b. The lessor will furnish all utilities to the lessee.

- c. The plumber presented a bill to the customer for services.
 - d. Please respond to all future inquiries promptly.
 - e. We request your cooperation in this matter.
 - f. Your timely response will allow us to sue the breaching party.
 - g. Please let us know whether you wish to pursue this matter.
 - h. You had problems then because you failed to complete the work.
 - i. The problems were ignored when they arose because all of the parties were out of town.
 - j. The promisee's promise was consideration for the promisor's promise.
 - k. What you do now will affect the entire case.
 - l. No doubt small problems tend to grow larger until they are resolved.
 - m. Please call our office for an appointment regarding your letter and the enclosed instrument.
 - n. We received further information about the matter after we thought there had been full disclosure.
 - o. It will be unnecessary for you to contact us until we notify you of further developments in the case since nothing can be done now.
- 3.
- a. The cook served large portions.
 - b. Now is the time for all good citizens to come to the aid of their country.
 - c. Journalists fly around the world covering interesting stories.
 - d. Husbands and wives often share a similar sense of humor.
 - e. Firefighters wear highly specialized protective clothing.
 - f. Police officers directing traffic use reflective vests for safety.
 - g. The members of the jury often engage in lengthy deliberations.
 - h. The reasonable person will consider a question in an objective manner.
 - i. Nursing is a job for compassionate people.
 - j. Ordinary people may perform heroic actions under stress.

Chapter 7 Contract Enforceability: Protecting a Class

TRUE/FALSE QUESTIONS

- | | |
|-------|-------|
| 1. T | 12. F |
| 2. T | 13. T |
| 3. F | 14. T |
| 4. T | 15. F |
| 5. F | 16. T |
| 6. T | 17. T |
| 7. F | 18. T |
| 8. T | 19. F |
| 9. T | 20. T |
| 10. T | 21. F |
| 11. F | 22. F |

FILL-IN-THE-BLANK QUESTIONS

- | | |
|-----------------------|--------------------|
| 1. Minors | 4. Cognitive test |
| 2. Restitution action | 5. Volitional test |
| 3. Mental incapacity | |

MULTIPLE CHOICE QUESTIONS

- | | |
|-------------------|--------------|
| 1. (a), (b) & (e) | 2. (a) & (b) |
|-------------------|--------------|

SHORT ANSWER QUESTIONS

1. Albert purchased the car while a minor (he was 17 at the time) and therefore could disaffirm the contract prior to reaching majority (18) or within a reasonable time thereafter. A reasonable time would be determined by such factors as prejudice suffered by Friendly Motors by a delay in disaffirmance, the nature of the subject matter, and the ability of Albert to disaffirm. Although the facts do not give extenuating circumstances, two months from reaching majority does not appear to be unreasonable because the subject matter is not perishable and its depreciation would be gradual since it was a used vehicle when purchased.

Assuming that Albert was not beyond a reasonable time after reaching majority, he

may exercise his power to disaffirm by returning to Friendly Motors what he currently has, that is, the wrecked automobile, certificate of title, and keys. Albert could then bring a restitution action to recover his down payment and any installments paid.

2. As a defensive weapon, the minor could disaffirm the contract, discontinue performance, and wait for the other contracting party to file a breach of contract action. As an offensive weapon, the minor could disaffirm the contract, discontinue performance, and bring a restitution action to recover the benefit he or she conferred on the other party.

Chapter 8 Contract Responsibility: Protecting a Party Against Overreaching**TRUE/FALSE QUESTIONS**

- | | |
|------|-------|
| 1. T | 8. F |
| 2. T | 9. F |
| 3. F | 10. T |
| 4. T | 11. F |
| 5. F | 12. T |
| 6. T | 13. F |
| 7. F | 14. F |

- | | |
|-------|-------|
| 15. T | 28. F |
| 16. F | 29. T |
| 17. F | 30. T |
| 18. T | 31. F |
| 19. T | 32. T |
| 20. F | 33. F |
| 21. F | 34. F |
| 22. T | 35. T |
| 23. T | 36. F |
| 24. F | 37. T |
| 25. F | 38. T |
| 26. T | 39. F |
| 27. T | 40. F |

FILL-IN-THE-BLANK QUESTIONS

- | | |
|-------------------------|---|
| 1. Contract of adhesion | 8. Fraud in the factum |
| 2. Imposition of will | 9. Fraud in the inducement |
| 3. Unconscionability | 10. Power to disaffirm |
| 4. Court | 11. Duress |
| 5. Section 2–302 | 12. Economic duress |
| 6. Misrepresentation | 13. Undue influence |
| 7. Fraud | 14. Mistake in a basic assumption of fact |

MULTIPLE CHOICE QUESTIONS

- | | |
|-----------------------------|--------------|
| 1. (c) | 5. (a) & (d) |
| 2. (e) | 6. (e) |
| 3. (a), (b) & (c) | 7. (d) |
| 4. (a), (b), (c), (d) & (e) | |

SHORT ANSWER QUESTIONS

1. Absence of meaningful choice has two components:
- (1) the imbalance in bargaining power; and
 - (2) a lack of knowledge of the terms.
- A gross inequality of bargaining power will negate the need for a lack of knowledge of the

terms. If the inequality of bargaining power is less than gross, the lack of knowledge of the terms may be demonstrated by the terms being hidden in a maze of fine print, being minimized by deceptive sales practices, or by the lack of a reasonable opportunity to become acquainted with the terms.

2. The four elements of duress by threat are:
- (a) there must be a threat;
 - (b) the threat must be improper;
 - (c) the threat must be sufficiently grave to induce the victim to assent; and
 - (d) the threat must induce the victim to assent to the contract.

Chapter 9 Contract Enforceability: Protecting the Judicial Process

TRUE/FALSE QUESTIONS

- | | |
|-------|-------|
| 1. F | 24. T |
| 2. T | 25. T |
| 3. T | 26. T |
| 4. F | 27. T |
| 5. T | 28. F |
| 6. F | 29. T |
| 7. F | 30. F |
| 8. T | 31. T |
| 9. T | 32. T |
| 10. F | 33. T |
| 11. F | 34. F |
| 12. F | 35. F |
| 13. T | 36. T |
| 14. T | 37. T |
| 15. T | 38. F |
| 16. F | 39. F |
| 17. T | 40. T |
| 18. T | 41. T |
| 19. F | 42. F |
| 20. T | 43. T |
| 21. F | |
| 22. T | |
| 23. T | |

FILL-IN-THE-BLANK QUESTIONS

- | | |
|-----------------------------|--|
| 1. Illegal subject matter | 4. Disclosure of the employer's trade secrets or confidential lists or an employee's services that are special, unique, or extraordinary |
| 2. Covenant not to compete | |
| 3. The business's good will | |

- | | |
|---|----------------------------|
| 5. Parties are not in pari delicto, collateral illegality, repentance | 8. Repentance |
| 6. In pari delicto | 9. Statute of Frauds |
| 7. Collateral illegality | 10. Restitution action |
| | 11. Forum selection clause |

MULTIPLE CHOICE QUESTIONS

- | | |
|-------------------|--------|
| 1. (b), (c) & (d) | 2. (b) |
|-------------------|--------|

SHORT ANSWER QUESTIONS

- | | |
|---|--|
| <p>1. Ellen could use a covenant not to compete in a contract for the sale of a business to protect her purchase of the business's goodwill. The covenant must be drafted to protect this goodwill and must not be overly broad. Therefore, the covenant will be enforceable so long as it does not extend beyond the subject matter, geography and duration necessary to protect the business's goodwill. For example, if the Print Shop operates in three states, an eight state prohibition would be overly broad.</p> | <p>2. For an employee to be subject to an enforceable covenant not to compete, the employer must have a legitimate interest to protect. If the employee does not have access to the employer's trade secrets or confidential lists or if the employee's services are not special, unique, or extraordinary, the employer has no interest to protect. Without a legitimate interest to protect, any covenant not to compete between this employer and employee would be unreasonable and therefore unenforceable.</p> |
|---|--|

Chapter 10 The Defendant's Response to the Plaintiff's Allegation of Breach

TRUE/FALSE QUESTIONS

- | | |
|-------|-------|
| 1. F | 13. T |
| 2. F | 14. F |
| 3. T | 15. F |
| 4. T | 16. T |
| 5. F | 17. F |
| 6. F | 18. F |
| 7. F | 19. T |
| 8. F | 20. F |
| 9. T | 21. F |
| 10. F | 22. T |
| 11. T | 23. T |
| 12. F | 24. T |

- | | |
|-------|-------|
| 25. F | 42. T |
| 26. T | 43. T |
| 27. F | 44. T |
| 28. F | 45. T |
| 29. T | 46. F |
| 30. T | 47. T |
| 31. F | 48. F |
| 32. T | 49. T |
| 33. F | 50. F |
| 34. F | 51. T |
| 35. F | 52. T |
| 36. T | 53. F |
| 37. T | 54. T |
| 38. T | 55. F |
| 39. F | 56. T |
| 40. F | 57. T |
| 41. T | 58. F |

FILL-IN-THE-BLANK QUESTIONS

- | | |
|--|--------------------------------|
| 1. No breach, compliance | 13. Concurrent conditions |
| 2. Patent ambiguity | 14. No breach, excuse |
| 3. Patent ambiguity | 15. Impossibility |
| 4. Latent ambiguity | 16. Impracticability |
| 5. Latent ambiguity | 17. Frustration of purpose |
| 6. Contra perferentem | 18. No breach, justification |
| 7. Plain meaning rule | 19. Entire contract |
| 8. Ejusdem generis | 20. Divisible contract |
| 9. Expressio unius est exclusio alterius | 21. Estoppel |
| 10. Promissory condition | 22. Perfect tender rule |
| 11. Condition precedent | 23. No breach, terminated duty |
| 12. Condition subsequent | |

MULTIPLE CHOICE QUESTIONS

- | | |
|-------------------|--------|
| 1. (a), (c) & (e) | 5. (b) |
| 2. (b) | 6. (b) |
| 3. (a) | 7. (c) |
| 4. (a) | |

SHORT ANSWER QUESTIONS

1. A condition precedent is a duty creating event. The promisor has no duty to perform until the event occurs. A condition subsequent is a duty terminating event. The promisor's duty to perform ends when the event occurs. Concurrent conditions exist when promises are conditioned on each other and both must be performed simultaneously.
2. The "no breach, justification" response states that the defendant's nonperformance was justified by the plaintiff's breach. First, the plaintiff must be in breach. Second, the defendant's performance must be dependent on the plaintiff's performance. Third, the plaintiff's performance must be a condition precedent to the defendant's performance. Fourth, the magnitude of the plaintiff's breach must justify the defendant's nonperformance.
3. In a "no breach, compliance" response, the defendant claims that he or she is performing according to the terms of the contract. This performance may in fact be waiting for a condition precedent to occur. In a "no breach, justification" response, the defendant claims that although he or she is not performing according to the terms of the contract, performance is unnecessary because of the plaintiff's breach.

Chapter 11 Plaintiff's Remedies for the Defendant's Breach of Contract

TRUE/FALSE QUESTIONS

- | | |
|-------|-------|
| 1. T | 21. T |
| 2. T | 22. F |
| 3. F | 23. T |
| 4. T | 24. T |
| 5. F | 25. F |
| 6. F | 26. T |
| 7. T | 27. F |
| 8. F | 28. T |
| 9. T | 29. T |
| 10. F | 30. F |
| 11. T | 31. T |
| 12. T | 32. T |
| 13. F | 33. F |
| 14. F | 34. T |
| 15. T | 35. T |
| 16. F | 36. F |
| 17. F | 37. T |
| 18. T | 38. F |
| 19. T | 39. T |
| 20. F | 40. F |

41. T
42. F
43. F

44. F
45. F

FILL-IN-THE-BLANK QUESTIONS

- | | |
|-------------------------|--------------------------|
| 1. Expectation damages | 8. Mitigation |
| 2. Reliance damages | 9. Nominal damages |
| 3. Restitution damages | 10. Injunction |
| 4. Compensatory damages | 11. Specific performance |
| 5. Foreseeable damages | 12. Cover |
| 6. General damages | 13. Liquidated damages |
| 7. Special damages | 14. Costs |

MULTIPLE CHOICE QUESTIONS

- | | |
|--------|--------|
| 1. (c) | 4. (c) |
| 2. (e) | 5. (d) |
| 3. (b) | |

SHORT ANSWER QUESTIONS

- | | |
|--|--|
| 1. what the nonbreaching party expected to receive | what the nonbreaching party expected to give |
| _____ | _____ |
| what the nonbreaching party did receive | what the nonbreaching party did give |
| 2. _____ | _____ |
| what the nonbreaching party did receive based on reliance | what the nonbreaching party did give based on reliance |
| 3. _____ | _____ |
| What the nonbreaching party did receive for conferring the benefit | What the nonbreaching party did give for the benefit conferred |

Chapter 12 Third Party Interests

TRUE/FALSE QUESTIONS

- | | |
|-------|-------|
| 1. T | 19. F |
| 2. F | 20. T |
| 3. F | 21. T |
| 4. T | 22. F |
| 5. T | 23. T |
| 6. F | 24. T |
| 7. T | 25. T |
| 8. T | 26. F |
| 9. F | 27. T |
| 10. F | 28. F |
| 11. T | 29. T |
| 12. T | 30. T |
| 13. T | 31. F |
| 14. T | 32. T |
| 15. F | 33. T |
| 16. F | 34. T |
| 17. F | 35. F |
| 18. T | |

FILL-IN-THE-BLANK QUESTIONS

- | | |
|-------------------------------------|---|
| 1. Third party beneficiary contract | 8. Horizontal nonprivity plaintiff |
| 2. Third party beneficiary | 9. Assignment |
| 3. Donee beneficiary | 10. Delegation |
| 4. Creditor beneficiary | 11. Novation |
| 5. Intended beneficiary | 12. Simple novation |
| 6. Incidental beneficiary | 13. Compound novation |
| 7. Vertical nonprivity plaintiff | 14. Tortious interference with a contract |

MULTIPLE CHOICE QUESTIONS

- | | |
|--------|--------|
| 1. (a) | 3. (d) |
| 2. (b) | |

SHORT ANSWER QUESTIONS

1. Courts often use the “intent to benefit” test which examines who is to receive the performance of the contract. The courts, however, are not in agreement in their application of the “intent to benefit” test. Some investigate whether both contracting parties intended to benefit the third party; others consider only the promisee’s intent; and still others emphasize the conferring of a right rather than a benefit.
2. A vertical nonprivity plaintiff is a buyer of goods. This buyer has a contract with his or her seller but not with his or her seller’s seller and therefore is not in privity of contract with his or her seller’s seller. A horizontal nonprivity plaintiff is not a buyer but rather a consumer, user, or someone affected by the goods. The party has no contractual relationship with the buyer or with the buyer’s seller.
3. An assignment is a transfer of a contractual right. A delegation is the authorization of another to perform a contractual duty.
4. (a) simple novation with substitution of obligors;
(b) simple novation with substitution of obligees;
(c) compound novation with one original contract;
(d) compound novation with two original contracts.
5. The two essential elements of a novation are:
 - (1) the discharge of a party to the original contract; and
 - (2) the substitution of a new party in his or her place.
6. The elements for an action for tortious interference with a contract are:
 - (1) the existence of an enforceable contract;
 - (2) the party inducing the breach knew of the contract;
 - (3) the interfering party intentionally induced the breach;
 - (4) the interfering party induced the breach unjustifiably; and
 - (5) the party claiming interference was damaged by the breach of contract.



ARTICLE 1 GENERAL PROVISIONS

Part 1. Short Title, Construction, Application and Subject Matter of the Act

Section

- 1-101. Short Title.
- 1-102. Purposes; Rules of Construction; Variation by Agreement.
- 1-103. Supplementary General Principles of Law Applicable.
- 1-104. Construction Against Implicit Repeal.
- 1-105. Territorial Application of the Act; Parties' Power to Choose Applicable Law.
- 1-106. Remedies to Be Liberally Administered.
- 1-107. Waiver or Renunciation of Claim or Right After Breach.
- 1-108. Severability.
- 1-109. Section Captions.

Part 2. General Definitions and Principles of Interpretation

- 1-201. General Definitions.
- 1-202. Prima Facie Evidence by Third Party Documents.
- 1-203. Obligation of Good Faith.
- 1-204. Time; Reasonable Time; "Seasonably".
- 1-205. Course of Dealing and Usage of Trade.

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- 1–206. Statute of Frauds for Kinds of Personal Property Not Otherwise Covered.
- 1–207. Performance or Acceptance Under Reservation of Rights.
- 1–208. Option to Accelerate at Will.
- 1–209. Subordinated Obligations.

Part 1 Short Title, Construction, Application and Subject Matter of the Act

§ 1–101. Short Title.

This Act shall be known and may be cited as Uniform Commercial Code.

§ 1–102. Purposes; Rules of Construction; Variation by Agreement.

- (1) This Act shall be liberally construed and applied to promote its underlying purposes and policies.
- (2) Underlying purposes and policies of this Act are
 - (a) to simplify, clarify and modernize the law governing commercial transactions;
 - (b) to permit the continued expansion of commercial practices through custom, usage and agreement of the parties;
 - (c) to make uniform the law among the various jurisdictions.
- (3) The effect of provisions of this Act may be varied by agreement, except as otherwise provided in this Act and except that the obligations of good faith, diligence, reasonableness and care prescribed by this Act may not be disclaimed by agreement but the parties may by agreement determine the standards by which the performance of such obligations is to be measured if such standards are not manifestly unreasonable.
- (4) The presence in certain provisions of this Act of the words “unless otherwise agreed” or words of similar import does not imply that the effect of other provisions may not be varied by agreement under subsection (3).
- (5) In this Act unless the context otherwise requires
 - (a) words in the singular number include the plural, and in the plural include the singular;
 - (b) words in the masculine gender include the feminine and the neuter, and when the sense so indicates words of the neuter gender may refer to any gender.

§ 1–103. Supplementary General Principles of Law Applicable.

Unless displaced by the particular provisions of this Act, the principles of law and equity, including the law merchant and the law relative to capacity to contract, principal and agent, estoppel, fraud, misrepresentation, duress, coercion, mistake, bankruptcy, or other validating or invalidating cause shall supplement its provisions.

§ 1-104. Construction Against Implicit Repeal.

This Act being a general act intended as a unified coverage of its subject matter, no part of it shall be deemed to be impliedly repealed by subsequent legislation if such construction can reasonably be avoided.

§ 1-105. Territorial Application of the Act; Parties' Power to Choose Applicable Law.

- (1) Except as provided hereafter in this section, when a transaction bears a reasonable relation to this state and also to another state or nation the parties may agree that the law either of this state or of such other state or nation shall govern their rights and duties. Failing such agreement this Act applies to transactions bearing an appropriate relation to this state.

- (2) Where one of the following provisions of this Act specifies the applicable law, that provision governs and a contrary agreement is effective only to the extent permitted by the law (including the conflict of laws rules) so specified:

Rights of creditors against sold goods. Section 2-402.

Applicability of the Article on Leases. Sections 2A-105 and 2A-106.

Applicability of the Article on Bank Deposits and Collections. Section 4-102.

Governing law in the Article on Funds Transfers. Section 4A-507.

Letters of Credit. Section 5-116.

Bulk sales subject to the Article on Bulk Sales. Section 6-103.

Applicability of the Article on Investment Securities. Section 8-110

Perfection provisions of the Article on Secured Transactions. Section 9-103.

As amended in 1972, 1987, 1988, 1989 and 1995.

§ 1-106. Remedies to be Liberally Administered.

- (1) The remedies provided by this Act shall be liberally administered to the end that the aggrieved party may be put in as good a position as if the other party had fully performed but neither consequential or special nor penal damage may be had except as specifically provided in this Act or by other rule of law.
- (2) Any right or obligation declared by this Act is enforceable by action unless the provision declaring it specifies a different and limited effect.

§ 1-107. Waiver or Renunciation of Claim or Right After Breach.

Any claim or right arising out of an alleged breach can be discharged in whole or in part without consideration by a written waiver or renunciation signed and delivered by the aggrieved party.

§ 1-108. Severability.

If any provision or clause of this Act or application thereof to any person or circumstances is held invalid, such invalidity shall not affect other provisions or applications of the Act which can be given effect without the

invalid provision or application, and to this end the provisions of this Act are declared to be severable.

§ 1-109. Section Captions.

Section captions are parts of this Act.

Part 2 General Definitions and Principles of Interpretation

§ 1-201. General Definitions.

Subject to additional definitions contained in the subsequent Articles of this Act which are applicable to specific Articles or Parts thereof, and unless the context otherwise requires, in this Act:

- (1) “Action” in the sense of a judicial proceeding includes recoupment, counterclaim, set-off, suit in equity and any other proceedings in which rights are determined.
- (2) “Aggrieved party” means a party entitled to resort to a remedy.
- (3) “Agreement” means the bargain of the parties in fact as found in their language or by implication from other circumstances including course of dealing or usage of trade or course of performance as provided in this Act (Sections 1-205, 2-208, and 2A-207). Whether an agreement has legal consequences is determined by the provisions of this Act, if applicable; otherwise by the law of contracts (Section 1-103). (Compare “Contract”.)
- (4) “Bank” means any person engaged in the business of banking.
- (5) “Bearer” means the person in possession of an instrument, document of title, or certificated security payable to bearer or indorsed in blank.
- (6) “Bill of lading” means a document evidencing the receipt of goods for shipment issued by a person engaged in the business of transporting or forwarding goods, and includes an airbill. “Airbill” means a document serving for air transportation as a bill of lading does for marine or rail transportation, and includes an air consignment note or air waybill.
- (7) “Branch” includes a separately incorporated foreign branch of a bank.
- (8) “Burden of establishing” a fact means the burden of persuading the triers of fact that the existence of the fact is more probable than its non-existence.
- (9) “Buyer in ordinary course of business” means a person who in good faith and without knowledge that the sale to him is in violation of the ownership rights or security interest of a third party in the goods buys in ordinary course from a person in the business of selling goods of that kind but does not include a pawnbroker. All persons who sell minerals or the like (including oil and gas) at wellhead or minehead shall be deemed to be persons in the business of selling goods of that kind. “Buying” may be for cash or by exchange of other property or on secured or unsecured credit and includes receiving goods or documents of title under a pre-existing contract for sale but does not include a transfer in bulk or as security for or in total or partial satisfaction of a money debt.

- (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: NON-NEGOTIABLE 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.
- (11) “Contract” means the total legal obligation which results from the parties’ agreement as affected by this Act and any other applicable rules of law. (Compare “Agreement”.)
- (12) “Creditor” includes a general creditor, a secured creditor, a lien creditor and any representative of creditors, including an assignee for the benefit of creditors, a trustee in bankruptcy, a receiver in equity and an executor or administrator of an insolvent debtor’s or assignor’s estate.
- (13) “Defendant” includes a person in the position of defendant in a cross-action or counterclaim.
- (14) “Delivery” with respect to instruments, documents of title, chattel paper, or certificated securities means voluntary transfer of possession.
- (15) “Document of title” includes bill of lading, dock warrant, dock receipt, warehouse receipt or order for the delivery of goods, and also any other document which in the regular course of business or financing is treated as adequately evidencing that the person in possession of it is entitled to receive, hold and dispose of the document and the goods it covers. To be a document of title a document must purport to be issued by or addressed to a bailee and purport to cover goods in the bailee’s possession which are either identified or are fungible portions of an identified mass.
- (16) “Fault” means wrongful act, omission or breach.
- (17) “Fungible” with respect to goods or securities means goods or securities of which any unit is, by nature or usage of trade, the equivalent of any other like unit. Goods which are not fungible shall be deemed fungible for the purposes of this Act to the extent that under a particular agreement or document unlike units are treated as equivalents.
- (18) “Genuine” means free of forgery or counterfeiting.
- (19) “Good faith” means honesty in fact in the conduct or transaction concerned.
- (20) “Holder” with respect to a negotiable instrument, means the person in possession if the instrument is payable to bearer or, in the case of an instrument payable to an identified person, if the identified person is in possession. “Holder” with respect to a document of title means the person in possession if the goods are deliverable to bearer or to the order of the person in possession.
- (21) To “honor” is to pay or to accept and pay, or where a credit so engages to purchase or discount a draft complying with the terms of the credit.
- (22) “Insolvency proceedings” includes any assignment for the benefit of creditors or other proceedings intended to liquidate or rehabilitate the estate of the person involved.

- (23) A person is “insolvent” who either has ceased to pay his debts in the ordinary course of business or cannot pay his debts as they become due or is insolvent within the meaning of the federal bankruptcy law.
- (24) “Money” means a medium of exchange authorized or adopted by a domestic or foreign government and includes a monetary unit of account established by an intergovernmental organization or by agreement between two or more nations.
- (25) A person has “notice” of a fact when
- (a) he has actual knowledge of it; or
 - (b) he has received a notice or notification of it; or
 - (c) from all the facts and circumstances known to him at the time in question he has reason to know that it exists.
- A person “knows” or has “knowledge” of a fact when he has actual knowledge of it. “Discover” or “learn” or a word or phrase of similar import refers to knowledge rather than to reason to know. The time and circumstances under which a notice or notification may cease to be effective are not determined by this Act.
- (26) A person “notifies” or “gives” a notice or notification to another by taking such steps as may be reasonably required to inform the other in ordinary course whether or not such other actually comes to know of it. A person “receives” a notice or notification when
- (a) it comes to his attention; or
 - (b) it is duly delivered at the place of business through which the contract was made or at any other place held out by him as the place for receipt of such communications.
- (27) Notice, knowledge or a notice or notification received by an organization is effective for a particular transaction from the time when it is brought to the attention of the individual conducting that transaction, and in any event from the time when it would have been brought to his attention if the organization had exercised due diligence. An organization exercises due diligence if it maintains reasonable routines for communicating significant information to the person conducting the transaction and there is reasonable compliance with the routines. Due diligence does not require an individual acting for the organization to communicate information unless such communication is part of his regular duties or unless he has reason to know of the transaction and that the transaction would be materially affected by the information.
- (28) “Organization” includes a corporation, government or governmental subdivision or agency, business trust, estate, trust, partnership or association, two or more persons having a joint or common interest, or any other legal or commercial entity.
- (29) “Party”, as distinct from “third party”, means a person who has engaged in a transaction or made an agreement within this Act.
- (30) “Person” includes an individual or organization (See Section 1–102).

- (31) “Presumption” or “presumed” means that the trier of fact must find the existence of the fact presumed unless and until evidence is introduced which would support a finding of its non-existence.
- (32) “Purchase” includes taking by sale, discount, negotiation, mortgage, pledge, lien, issue or reissue, gift or any other voluntary transaction creating an interest in property.
- (33) “Purchaser” means a person who takes by purchase.
- (34) “Remedy” means any remedial right to which an aggrieved party is entitled with or without resort to a tribunal.
- (35) “Representative” includes an agent, an officer of a corporation or association, and a trustee, executor or administrator of an estate, or any other person empowered to act for another.
- (36) “Rights” includes remedies.
- (37) “Security interest” means an interest in personal property or fixtures which secures payment or performance of an obligation. The retention or reservation of title by a seller of goods notwithstanding shipment or delivery to the buyer (Section 2–401) is limited in effect to a reservation of a “security interest”. The term also includes any interest of a buyer of accounts or chattel paper which is subject to Article 9. The special property interest of a buyer of goods on identification of those goods to a contract for sale under Section 2–401 is not a “security interest”, but a buyer may also acquire a “security interest” by complying with Article 9. Unless a consignment is intended as security, reservation of title thereunder is not a “security interest”, but a consignment in any event is subject to the provisions on consignment sales (Section 2–326).

Whether a transaction creates a lease or security interest is determined by the facts of each case; however, a transaction creates a security interest if the consideration the lessee is to pay the lessor for the right to possession and use of the goods is an obligation for the term of the lease not subject to termination by the lessee, and

- (a) the original term of the lease is equal to or greater than the remaining economic life of the goods,
- (b) the lessee is bound to renew the lease for the remaining economic life of the goods or is bound to become the owner of the goods,
- (c) the lessee has an option to renew the lease for the remaining economic life of the goods for no additional consideration or nominal additional consideration upon compliance with the lease agreement, or
- (d) the lessee has an option to become the owner of the goods for no additional consideration or nominal additional consideration upon compliance with the lease agreement.

A transaction does not create a security interest merely because it provides that

- (a) the present value of the consideration the lessee is obligated to pay the lessor for the right to possession and use of the goods is substantially equal to or is greater than the fair market value of the goods at the time the lease is entered into,

- (b) the lessee assumes risk of loss of the goods, or agrees to pay taxes, insurance, filing, recording, or registration fees, or service or maintenance costs with respect to the goods,
 - (c) the lessee has an option to renew the lease or to become the owner of the goods,
 - (d) the lessee has an option to renew the lease for a fixed rent that is equal to or greater than the reasonably predictable fair market rent for the use of the goods for the term of the renewal at the time the option is to be performed, or
 - (e) the lessee has an option to become the owner of the goods for a fixed price that is equal to or greater than the reasonably predictable fair market value of the goods at the time the option is to be performed. For purposes of this subsection (37):
 - (x) Additional consideration is not nominal if (i) when the option to renew the lease is granted to the lessee the rent is stated to be the fair market rent for the use of the goods for the term of the renewal determined at the time the option is to be performed, or (ii) when the option to become the owner of the goods is granted to the lessee the price is stated to be the fair market value of the goods determined at the time the option is to be performed. Additional consideration is nominal if it is less than the lessee's reasonably predictable cost of performing under the lease agreement if the option is not exercised;
 - (y) "Reasonably predictable" and "remaining economic life of the goods" are to be determined with reference to the facts and circumstances at the time the transaction is entered into; and
 - (z) "Present value" means the amount as of a date certain of one or more sums payable in the future, discounted to the date certain. The discount is determined by the interest rate specified by the parties if the rate is not manifestly unreasonable at the time the transaction is entered into; otherwise, the discount is determined by a commercially reasonable rate that takes into account the facts and circumstances of each case at the time the transaction was entered into.
- (38) "Send" in connection with any writing or notice means to deposit in the mail or deliver for transmission by any other usual means of communication with postage or cost of transmission provided for and properly addressed and in the case of an instrument to an address specified thereon or otherwise agreed, or if there be none to any address reasonable under the circumstances. The receipt of any writing or notice within the time at which it would have arrived if properly sent has the effect of a proper sending.
- (39) "Signed" includes any symbol executed or adopted by a party with present intention to authenticate a writing.
- (40) "Surety" includes guarantor.
- (41) "Telegram" includes a message transmitted by radio, teletype, cable, any mechanical method of transmission, or the like.

- (42) “Term” means that portion of an agreement which relates to a particular matter.
- (43) “Unauthorized” signature means one made without actual, implied, or apparent authority and includes a forgery.
- (44) “Value”. Except as otherwise provided with respect to negotiable instruments and bank collections (Sections 3–303, 4–210, and 4–211) a person gives “value” for rights if he acquires them
- (a) in return for a binding commitment to extend credit or for the extension of immediately available credit whether or not drawn upon and whether or not a charge-back is provided for in the event of difficulties in collection; or
 - (b) as security for or in total or partial satisfaction of a pre-existing claim; or
 - (c) by accepting delivery pursuant to a pre-existing contract for purchase; or
 - (d) generally, in return for any consideration sufficient to support a simple contract.
- (45) “Warehouse receipt” means a receipt issued by a person engaged in the business of storing goods for hire.
- (46) “Written” or “writing” includes printing, typewriting or any other intentional reduction to tangible form.
- As amended in 1962, 1972, 1977, 1987, 1990 and 1994.

§ 1–202. Prima Facie Evidence by Third Party Documents.

A document in due form purporting to be a bill of lading, policy or certificate of insurance, official weigher’s or inspector’s certificate, consular invoice, or any other document authorized or required by the contract to be issued by a third party shall be prima facie evidence of its own authenticity and genuineness and of the facts stated in the document by the third party.

§ 1–203. Obligation of Good Faith.

Every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement.

§ 1–204. Time; Reasonable Time; “Seasonably”.

- (1) Whenever this Act requires any action to be taken within a reasonable time, any time which is not manifestly unreasonable may be fixed by agreement.
- (2) What is a reasonable time for taking any action depends on the nature, purpose and circumstances of such action.
- (3) An action is taken “seasonably” when it is taken at or within the time agreed or if no time is agreed at or within a reasonable time.

§ 1–205. Course of Dealing and Usage of Trade.

- (1) A course of dealing is a sequence of previous conduct between the parties to a particular transaction which is fairly to be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct.

- (2) A usage of trade is any practice or method of dealing having such regularity of observance in a place, vocation or trade as to justify an expectation that it will be observed with respect to the transaction in question. The existence and scope of such a usage are to be proved as facts. If it is established that such a usage is embodied in a written trade code or similar writing the interpretation of the writing is for the court.
- (3) A course of dealing between parties and any usage of trade in the vocation or trade in which they are engaged or of which they are or should be aware give particular meaning to and supplement or qualify terms of an agreement.
- (4) The express terms of an agreement and an applicable course of dealing or usage of trade shall be construed wherever reasonable as consistent with each other; but when such construction is unreasonable express terms control both course of dealing and usage of trade and course of dealing controls usage of trade.
- (5) An applicable usage of trade in the place where any part of performance is to occur shall be used in interpreting the agreement as to that part of the performance.
- (6) Evidence of a relevant usage of trade offered by one party is not admissible unless and until he has given the other party such notice as the court finds sufficient to prevent unfair surprise to the latter.

§ 1-206. Statute of Frauds for Kinds of Personal Property Not Otherwise Covered.

- (1) Except in the cases described in subsection (2) of this section a contract for the sale of personal property is not enforceable by way of action or defense beyond five thousand dollars in amount or value of remedy unless there is some writing which indicates that a contract for sale has been made between the parties at a defined or stated price, reasonably identifies the subject matter, and is signed by the party against whom enforcement is sought or by his authorized agent.
- (2) Subsection (1) of this section does not apply to contracts for the sale of goods (Section 2-201) nor of securities (Section 8-113) nor to security agreements (Section 9-203).

As amended in 1994.

§ 1-207. Performance or Acceptance Under Reservation of Rights.

- (1) A party who, 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.
- (2) Subsection (1) does not apply to an accord and satisfaction.

§ 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 burden of establishing lack of good faith is on the party against whom the power has been exercised.

§ 1-209. Subordinated Obligations.

An obligation may be issued as subordinated to payment of another obligation of the person obligated, or a creditor may subordinate his right to payment of an obligation by agreement with either the person obligated or another creditor of the person obligated. Such a subordination does not create a security interest as against either the common debtor or a subordinated creditor. This section shall be construed as declaring the law as it existed prior to the enactment of this section and not as modifying it.
Added 1966.

ARTICLE 2 SALES

Part 1. Short Title, General Construction and Subject Matter

Section

- 2-101. Short Title.
- 2-102. Scope; Certain Security and Other Transactions Excluded From This Article.
- 2-103. Definitions and Index of Definitions.
- 2-104. Definitions: “Merchant”; “Between Merchants”; “Financing Agency”.
- 2-105. Definitions: Transferability; “Goods”; “Future” Goods; “Lot”; “Commercial Unit”.
- 2-106. Definitions: “Contract”; “Agreement”; “Contract for Sale”; “Sale”; “Present Sale”; “Conforming” to Contract; “Termination”; “Cancellation”.
- 2-107. Goods to Be Severed From Realty: Recording.

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- 2-201. Formal Requirements; Statute of Frauds.
- 2-202. Final Written Expression: Parol or Extrinsic Evidence.
- 2-203. Seals Inoperative,
- 2-204. Formation in General.
- 2-205. Firm Offers.
- 2-206. Offer and Acceptance in Formation of Contract.
- 2-207. Additional Terms in Acceptance or Confirmation.
- 2-208. Course of Performance or Practical Construction.
- 2-209. Modification, Rescission and Waiver.
- 2-210. Delegation of Performance; Assignment of Rights.

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- 2-303. Allocation or Division of Risks.
- 2-304. Price Payable in Money, Goods, Realty, or Otherwise.
- 2-305. Open Price Term.
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- 2-307. Delivery in Single Lot or Several Lots.
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- 2-310. Open Time for Payment or Running of Credit; Authority to Ship Under Reservation.
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- 2-312. Warranty of Title and Against Infringement; Buyer's Obligation Against Infringement.
- 2-313. Express Warranties by Affirmation, Promise, Description, Sample.
- 2-314. Implied Warranty: Merchantability; Usage of Trade.
- 2-315. Implied Warranty: Fitness for Particular Purpose.
- 2-316. Exclusion or Modification of Warranties.
- 2-317. Cumulation and Conflict of Warranties Express or Implied.
- 2-318. Third Party Beneficiaries of Warranties Express or Implied.
- 2-319. F.O.B. and F.A.S. Terms.
- 2-320. C.I.F. and C. & F. Terms.
- 2-321. C.I.F. or C. & F.: "Net Landed Weights"; "Payment on Arrival"; Warrant of Condition on Arrival.
- 2-322. Delivery "Ex-Ship".
- 2-323. Form of Bill of Lading Required in Overseas Shipment; "Overseas".
- 2-324. "No Arrival, No Sale" Term.
- 2-325. "Letter of Credit" Term; "Confirmed Credit".
- 2-326. Sale on Approval and Sale or Return; Consignment Sales and Rights of Creditors.
- 2-327. Special Incidents of Sale on Approval and Sale or Return.
- 2-328. Sale by Auction.

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- 2-401. Passing of Title; Reservation for Security; Limited Application of This Section.
- 2-402. Rights of Seller's Creditors Against Sold Goods.
- 2-403. Power to Transfer; Good Faith Purchase of Goods; "Entrusting".

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- 2-501. Insurable Interest in Goods; Manner of Identification of Goods.
- 2-502. Buyer's Right to Goods on Seller's Insolvency.

- 2-503. Manner of Seller's Tender of Delivery.
- 2-504. Shipment by Seller.
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- 2-506. Rights of Financing Agency.
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- 2-603. Merchant Buyer's Duties as to Rightfully Rejected Goods.
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- 2-606. What Constitutes Acceptance of Goods.
- 2-607. Effect of Acceptance; Notice of Breach; Burden of Establishing Breach After Acceptance; Notice of Claim or Litigation to Person Answerable Over.
- 2-608. Revocation of Acceptance in Whole or in Part.
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- 2-613. Casualty to Identified Goods.
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- 2-701. Remedies for Breach of Collateral Contracts Not Impaired.
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- 2-705. Seller's Stoppage of Delivery in Transit or Otherwise.
- 2-706. Seller's Resale Including Contract for Resale.
- 2-707. "Person in the Position of a Seller".
- 2-708. Seller's Damages for Non-acceptance or Repudiation.

- 2-709. Action for the Price.
- 2-710. Seller's Incidental Damages.
- 2-711. Buyer's Remedies in General; Buyer's Security Interest in Rejected Goods.
- 2-712. "Cover"; Buyer's Procurement of Substitute Goods.
- 2-713. Buyer's Damages for Non-delivery or Repudiation.
- 2-714. Buyer's Damages for Breach in Regard to Accepted Goods.
- 2-715. Buyer's Incidental and Consequential Damages.
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- 2-717. Deduction of Damages From the Price.
- 2-718. Liquidation or Limitation of Damages; Deposits.
- 2-719. Contractual Modification or Limitation of Remedy.
- 2-720. Effect of "Cancellation" or "Rescission" on Claims for Antecedent Breach.
- 2-721. Remedies for Fraud.
- 2-722. Who Can Sue Third Parties for Injury to Goods.
- 2-723. Proof of Market Price: Time and Place.
- 2-724. Admissibility of Market Quotations.
- 2-725. Statute of Limitations in Contracts for Sale.

Part 1. Short Title, General Construction and Subject Matter

§ 2-101. Short Title.

This Article shall be known and may be cited as Uniform Commercial Code—Sales.

§ 2-102. Scope; Certain Security and Other Transactions Excluded From This Article.

Unless the context otherwise requires, this Article applies to transactions in goods; it does not apply to any transaction which although in the form of an unconditional contract to sell or present sale is intended to operate only as a security transaction nor does this Article impair or repeal any statute regulating sales to consumers, farmers or other specified classes of buyers.

§ 2-103. Definitions and Index of Definitions.

- (1) In this Article unless the context otherwise requires
 - (a) "Buyer" means a person who buys or contracts to buy goods.
 - (b) "Good faith" in the case of a merchant means honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade.
 - (c) "Receipt" of goods means taking physical possession of them.
 - (d) Seller means a person who sells or contracts to sell goods.
- (2) Other definitions applying to this Article or to specified Parts thereof, and the sections in which they appear are:
"Acceptance". Section 2-606.

- “Banker’s credit”. Section 2–325.
 - “Between merchants”. Section 2–104.
 - “Cancellation”. Section 2–106(4).
 - “Commercial unit”. Section 2–105.
 - “Confirmed credit”. Section 2–325.
 - “Conforming to contract”. Section 2–106.
 - “Contract for sale”. Section 2–106.
 - “Cover”. Section 2–712.
 - “Entrusting”. Section 2–403.
 - “Financing agency”. Section 2–104.
 - “Future goods”. Section 2–105.
 - “Goods”. Section 2–105.
 - “Identification”. Section 2–501.
 - “Installment contract”. Section 2–612.
 - “Letter of Credit”. Section 2–325.
 - “Lot”. Section 2–105.
 - “Merchant”. Section 2–104.
 - “Overseas”. Section 2–323.
 - “Person in position of seller”. Section 2–707.
 - “Present Sale”. Section 2–106
 - “Sale”. Section 2–106.
 - “Sale on approval”. Section 2–326.
 - “Sale or return”. Section 2–326.
 - “Termination”. Section 2–106.
- (3) The following definitions in other Articles apply to this Article:
- “Check”. Section 3–104.
 - “Consignee”. Section 7–102.
 - “Consignor”. Section 7–102.
 - “Consumer goods”. Section 9–109.
 - “Dishonor”. Section 3–502.
 - “Draft”. Section 3–104.
- (4) In addition Article 1 contains general definitions and principles of construction and interpretation applicable throughout this Article. As amended in 1994.

§ 2-104. Definitions: “Merchant”; “Between Merchants”; “Financing Agency”.

- (1) “Merchant” means a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction or to whom such knowledge or skill may be attributed by his employment of an agent or broker or other intermediary who by his occupation holds himself out as having such knowledge or skill.
- (2) “Financing agency” means a bank, finance company or other person who in the ordinary course of business makes advances against goods or documents of title or who by arrangement with either the seller or the buyer intervenes in ordinary course to make or collect payment due or

claimed under the contract for sale, as by purchasing or paying the seller's draft or making advances against it or by merely taking it for collection whether or not documents of title accompany the draft.

"Financing agency" includes also a bank or other person who similarly intervenes between persons who are in the position of seller and buyer in respect to the goods (Section 2-707).

- (3) "Between merchants" means in any transaction with respect to which both parties are chargeable with the knowledge or skill of merchants.

Official Comment

Prior Uniform Statutory Provision: None. But see Sections 15(2), (5), 16(c), 45(2) and 71, Uniform Sales Act, and Sections 35 and 37, Uniform Bills of Lading Act for examples of the policy expressly provided for in this Article.

Purposes:

1. This Article assumes that transactions between professionals in a given field require special and clear rules which may not apply to a casual or inexperienced seller or buyer. It thus adopts a policy of expressly stating rules applicable "between merchants" and "as against a merchant", wherever they are needed instead of making them depend upon the circumstances of each case as in the statutes cited above. This section lays the foundation of this policy by defining those who are to be regarded as professionals or "merchants" and by stating when a transaction is deemed to be "between merchants."
2. The term "merchant" as defined here roots in the "law merchant" concept of a professional in business. The professional status under the definition may be based upon specialized knowledge as to the goods, specialized knowledge as to business practices, or specialized knowledge as to both and which kind of specialized knowledge may be sufficient to establish the merchant status is indicated by the nature of the provisions.

The special provisions as to merchants appear only in this Article and they are of three kinds. Sections 2-201(2), 2-205, 2-207 and 2-209 dealing with the statute of frauds, firm offers, confirmatory memoranda and modification rest on normal business practices which are or ought to be typical of and familiar to any person in business. For purposes of these sections almost every person in business would, therefore, be deemed to be a "merchant" under the language "who . . . by his occupation holds himself out as having knowledge or skill peculiar to the practices . . . involved in the transaction . . ." since the practices involved in the transaction are non-specialized business practices such as answering mail. In this type of provision, banks or even universities, for example, well may be "merchants." But even these sections only apply to a merchant in his mercantile capacity; a lawyer or bank president buying fishing tackle for his own use is not a merchant.

On the other hand, in Section 2-314 on the warranty of merchantability, such warranty is implied only "if the seller is a merchant with respect to

goods of that kind.” Obviously this qualification restricts the implied warranty to a much smaller group than everyone who is engaged in business and requires a professional status as to particular kinds of goods. The exception in Section 2–402(2) for retention of possession by a merchant-seller falls in the same class; as does Section 2–403(2) on entrusting of possession to a merchant “who deals in goods of that kind”.

A third group of sections includes 2–103(1)(b), which provides that in the case of a merchant “good faith” includes observance of reasonable commercial standards of fair dealing in the trade; 2–327(1)(c), 2–603 and 2–605, dealing with responsibilities of merchant buyers to follow seller’s instructions, etc.; 2–509 on risk of loss, and 2–609 on adequate assurance of performance. This group of sections applies to persons who are merchants under either the “practices” or the “goods” aspect of the definition of merchant.

3. The “or to whom such knowledge or skill may be attributed by his employment of an agent or broker . . .” clause of the definition of merchant means that even persons such as universities, for example, can come within the definition of merchant if they have regular purchasing departments or business personnel who are familiar with business practices and who are equipped to take any action required.

Cross References:

Point 1: See Sections 1–102 and 1–203.

Point 2: See Sections 2–314, 2–315 and 2–320 to 2–325 of this Article, and Article 9.

Definitional Cross References:

“Bank”. Section 1–201.

“Buyer”. Section 2–103.

“Contract for sale”. Section 2–106.

“Document for sale”. Section 2–201.

“Draft”. Section 3–104.

“Goods”. Section 2–105.

“Person”. Section 1–201.

“Purchase”. Section 1–201.

“Seller”. Section 2–103.

§ 2–105. Definitions: Transferability; “Goods”; “Future” Goods; “Lot”; “Commercial Unit”.

- (1) “Goods” means all things (including specially manufactured goods) 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. “Goods” also includes the unborn young of animals and growing crops and other identified things attached to realty as described in the section on goods to be severed from realty (Section 2–107).

- (2) Goods must be both existing and identified before any interest in them can pass. Goods which are not both existing and identified are “future” goods. A purported present sale of future goods or of any interest therein operates as a contract to sell.
- (3) There may be a sale of a part interest in existing identified goods.
- (4) An undivided share in an identified bulk of fungible goods is sufficiently identified to be sold although the quantity of the bulk is not determined. Any agreed proportion of such a bulk or any quantity thereof agreed upon by number, weight or other measure may to the extent of the seller’s interest in the bulk be sold to the buyer who then becomes an owner in common.
- (5) “Lot” means a parcel or a single article which is the subject matter of a separate sale or delivery, whether or not it is sufficient to perform the contract.
- (6) “Commercial unit” means such a unit of goods as by commercial usage is a single whole for purposes of sale and division of which materially impairs its character or value on the market or in use. A commercial unit may be a single article (as a machine) or a set of articles (as a suite of furniture or an assortment of sizes) or a quantity (as a bale, gross, or carload) or any other unit treated in use or in the relevant market as a single whole.

§ 2–106 Definitions: “Contract”; “Agreement”; “Contract for Sale”; “Sale”; “Present Sale”; “Conforming” to Contract; “Termination”; “Cancellation”.

- (1) In this Article unless the context otherwise requires “contract” and “agreement” are limited to those relating to the present or future sale of goods. “Contract for sale” includes both a present sale of goods and a contract to sell goods at a future time. A “sale” consists in the passing of title from the seller to the buyer for a price (Section 2–401). A “present sale” means a sale which is accomplished by the making of the contract.
- (2) Goods or conduct including any part of a performance are “conforming” or conform to the contract when they are in accordance with the obligations under the contract.
- (3) “Termination” occurs when either party pursuant to a power created by agreement or law puts an end to the contract otherwise than for its breach. On “termination” all obligations which are still executory on both sides are discharged but any right based on prior breach or performance survives.
- (4) “Cancellation” occurs when either party puts an end to the contract for breach by the other and its effect is the same as that of “termination” except that the cancelling party also retains any remedy for breach of the whole contract or any unperformed balance.

§ 2–107. Goods to Be Severed From Realty: Recording.

- (1) A contract for the sale of minerals or the like (including oil and gas) or a structure or its materials to be removed from realty is a contract for the sale of goods within this Article if they are to be severed by the seller but

until severance a purported present sale thereof which is not effective as a transfer of an interest in land is effective only as a contract to sell.

- (2) A contract for the sale apart from the land of growing crops or other things attached to realty and capable of severance without material harm thereto but not described in subsection (1) or of timber to be cut is a contract for the sale of goods within this Article whether the subject matter is to be severed by the buyer or by the seller even though it forms part of the realty at the time of contracting, and the parties can by identification effect a present sale before severance.
- (3) The provisions of this section are subject to any third party rights provided by the law relating to realty records, and the contract for sale may be executed and recorded as a document transferring an interest in land and shall then constitute notice to third parties of the buyer's rights under the contract for sale.

As amended in 1972.

Part 2 Form, Formation and Readjustment of Contract

§ 2-201. Formal Requirements; Statute of Frauds

- (1) Except as otherwise provided in this section 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. A writing is not insufficient because it omits or incorrectly states a term agreed upon but the contract is not enforceable under this paragraph beyond the quantity of goods shown in such writing.
- (2) Between merchants if within a reasonable time a writing in confirmation of the contract and sufficient against the sender is received and the party receiving it has reason to know its contents, it satisfies the requirements of subsection (1) against such party unless written notice of objection to its contents is given within 10 days after it is received.
- (3) A contract which does not satisfy the requirements of subsection (1) but which is valid in other respects is enforceable
 - (a) if the goods are to be specially manufactured for the buyer and are not suitable for sale to others in the ordinary course of the seller's business and the seller, before notice of repudiation is received and under circumstances which reasonably indicate that the goods are for the buyer, has made either a substantial beginning of their manufacture or commitments for their procurement; or
 - (b) if the party against whom enforcement is sought admits in his pleading, testimony or otherwise in court that a contract for sale was made, but the contract is not enforceable under this provision beyond the quantity of goods admitted; or

- (c) with respect to goods for which payment has been made and accepted or which have been received and accepted (Section 2–606).

Official Comment

Prior Uniform Statutory Provisions: Section 4, Uniform Sales Act (which was based on Section 17 of the Statute of 29 Charles II).

Changes: Completely rephrased; restricted to sale of goods. See also Sections 1–206, 8–319 and 9–203.

Purposes of Changes: The changed phraseology of this section is intended to make it clear that:

1. The required writing need not contain all the material terms of the contract and such material terms as are stated need not be precisely stated. All that is required is that the writing afford a basis for believing that the offered oral evidence rests on a real transaction. It may be written in lead pencil on a scratch pad. It need not indicate which party is the buyer and which the seller. The only term which must appear is the quantity term which need not be accurately stated but recovery is limited to the amount stated. The price, time and place of payment or delivery, the general quality of the goods, or any particular warranties may all be omitted.

Special emphasis must be placed on the permissibility of omitting the price term in view of the insistence of some courts on the express inclusion of this term even where the parties have contracted on the basis of a published price list. In many valid contracts for sale the parties do not mention the price in express terms, the buyer being bound to pay and the seller to accept a reasonable price which the trier of the fact may well be trusted to determine. Again, frequently the price is not mentioned since the parties have based their agreement on a price list or catalogue known to both of them and this list serves as an efficient safeguard against perjury. Finally, “market” prices and valuations that are current in the vicinity constitute a similar check. Thus if the price is not stated in the memorandum it can normally be supplied without danger of fraud. Of course if the “price” consists of goods rather than money the quantity of goods must be stated.

Only three definite and invariable requirements as to the memorandum are made by this subsection. First, it must evidence a contract for the sale of goods; second, it must be “signed”, a word which includes any authentication which identifies the party to be charged; and third, it must specify a quantity.

2. “Partial performance” as a substitute for the required memorandum can validate the contract only for the goods which have been accepted or for which payment has been made and accepted.

Receipt and acceptance either of goods or of the price constitutes an unambiguous overt admission by both parties that a contract actually exists. If the court can make a just apportionment, therefore, the agreed price of any goods actually delivered can be recovered without a writing or, if the price has been paid, the seller can be forced to deliver an apportionable part of the goods. The overt actions of the parties make

admissible evidence of the other terms of the contract necessary to a just apportionment. This is true even though the actions of the parties are not in themselves inconsistent with a different transaction such as a consignment for resale or a mere loan of money.

Part performance by the buyer requires the delivery of something by him that is accepted by the seller as such performance. Thus, part payment may be made by money or check, accepted by the seller. If the agreed price consists of goods or services, then they must also have been delivered and accepted.

3. Between merchants, failure to answer a written confirmation of a contract within ten days of receipt is tantamount to a writing under subsection (2) and is sufficient against both parties under subsection (1). The only effect, however, is to take away from the party who fails to answer the defense of the Statute of Frauds; the burden of persuading the trier of fact that a contract was in fact made orally prior to the written confirmation is unaffected. Compare the effect of a failure to reply under Section 2–207.
4. Failure to satisfy the requirements of this section does not render the contract void for all purposes, but merely prevents it from being judicially enforced in favor of a party to the contract. For example, a buyer who takes possession of goods as provided in an oral contract which the seller has not meanwhile repudiated, is not a trespasser. Nor would the Statute of Frauds provisions of this section be a defense to a third person who wrongfully induces a party to refuse to perform an oral contract, even though the injured party cannot maintain an action for damages against the party so refusing to perform.
5. The requirement of “signing” is discussed in the comment to Section 1–201.
6. It is not necessary that the writing be delivered to anybody. It need not be signed or authenticated by both parties but it is, of course, not sufficient against one who has not signed it. Prior to a dispute no one can determine which party’s signing of the memorandum may be necessary but from the time of contracting each party should be aware that to him it is signing by the other which is important.
7. If the making of a contract is admitted in court, either in a written pleading, by stipulation or by oral statement before the court, no additional writing is necessary for protection against fraud. Under this section it is no longer possible to admit the contract in court and still treat the Statute as a defense. However, the contract is not thus conclusively established. The admission so made by a party is itself evidential against him of the truth of the facts so admitted and of nothing more; as against the other party, it is not evidential at all.

Cross References:

See Sections 1–201, 2–202, 2–207, 2–209 and 2–304.

Definitional Cross References:

“Action”. Section 1–201.

“Between merchants”. Section 2–104.

“Buyer”. Section 2–103.
“Contract”. Section 1–201.
“Contract for sale”. Section 2–106.
“Goods”. Section 2–105.
“Notice”. Section 1–201.
“Party”. Section 1–201.
“Reasonable time”. Section 1–204.
“Sale”. Section 2–106.
“Seller”. Section 2–103.

§ 2–202. Final Written Expression: Parol or Extrinsic Evidence.

Terms with respect to which the confirmatory memoranda of the parties agree or which are otherwise set forth in a writing intended by the parties as a final expression of their agreement with respect to such terms as are included therein may not be contradicted by evidence of any prior agreement or of a contemporaneous oral agreement but may be explained or supplemented

- (a) by course of dealing or usage of trade (Section 1–205) or by course of performance (Section 2–208); and
- (b) by evidence of consistent additional terms unless the court finds the writing to have been intended also as a complete and exclusive statement of the terms of the agreement.

§ 2–203. Seals Inoperative.

The affixing of a seal to a writing evidencing a contract for sale or an offer to buy or sell goods does not constitute the writing a sealed instrument and the law with respect to sealed instruments does not apply to such a contract or offer.

§ 2–204. Formation in General.

- (1) 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.
- (2) An agreement sufficient to constitute a contract for sale may be found even though the moment of its making is undetermined.
- (3) Even though one or more terms are left open a contract for sale does not fail for indefiniteness if the parties have intended to make a contract and there is a reasonably certain basis for giving an appropriate remedy.

§ 2–205. Firm Offers.

An offer by a merchant to buy or sell goods in a signed writing which by its terms gives assurance that it will be held open is not revocable, for lack of consideration, during the time stated or if no time is stated for a reasonable time, but in no event may such period of irrevocability exceed three months; but any such term of assurance on a form supplied by the offeree must be separately signed by the offeror.

§ 2-206. Offer and Acceptance in Formation of Contract.

- (1) Unless otherwise unambiguously indicated by the language or circumstances
 - (a) an offer to make a contract shall be construed as inviting acceptance in any manner and by any medium reasonable in the circumstances;
 - (b) an order or other offer to buy goods for prompt or current shipment shall be construed as inviting acceptance either by a prompt promise to ship or by the prompt or current shipment of conforming or non-conforming goods, but such a shipment of non-conforming goods does not constitute an acceptance if the seller seasonably notifies the buyer that the shipment is offered only as an accommodation to the buyer.
- (2) Where the beginning of a requested performance is a reasonable mode of acceptance an offeror who is not notified of acceptance within a reasonable time may treat the offer as having lapsed before acceptance.

§ 2-207. Additional Terms in Acceptance or Confirmation.

- (1) A definite and seasonable expression of acceptance or a written confirmation which is sent within a reasonable time operates as an acceptance even though it states terms additional to or different from those offered or agreed upon, unless acceptance is expressly made conditional on assent to the additional or different terms.
- (2) The additional terms are to be construed as proposals for addition to the contract. Between merchants such terms become part of the contract unless:
 - (a) the offer expressly limits acceptance to the terms of the offer;
 - (b) they materially alter it; or
 - (c) notification of objection to them has already been or is given within a reasonable time after notice of them is received.
- (3) Conduct by both parties which recognizes the existence of a contract is sufficient to establish a contract for sale although the writings of the parties do not otherwise establish a contract. In such case the terms of the particular contract consist of those terms on which the writings of the parties agree, together with any supplementary terms incorporated under any other provisions of this Act.

Official Comment

Prior Uniform Statutory Provision: Sections 1 and 3, Uniform Sales Act.
Changes: Completely rewritten by this and other sections of this Article.

Purposes of Changes:

1. This section is intended to deal with two typical situations. The one is the written confirmation, where an agreement has been reached either orally or by informal correspondence between the parties and is followed by one or both of the parties sending formal memoranda embodying the terms so far as agreed upon and adding terms not discussed. The other situation is offer and acceptance, in which a wire or letter expressed and intended as an acceptance or the closing of an agreement adds further minor suggestions or proposals such as “ship by Tuesday,” “rush,” “ship

draft against bill of lading inspection allowed,” or the like. A frequent example of the second situation is the exchange of printed purchase order and acceptance (sometimes called “acknowledgment”) forms. Because the forms are oriented to the thinking of the respective drafting parties, the terms contained in them often do not correspond. Often the seller’s form contains terms different from or additional to those set forth in the buyer’s form. Nevertheless, the parties proceed with the transaction. [Comment 1 was amended in 1966.]

2. Under this Article a proposed deal which in commercial understanding has in fact been closed is recognized as a contract. Therefore, any additional matter contained in the confirmation or in the acceptance falls within subsection (2) and must be regarded as a proposal for an added term unless the acceptance is made conditional on the acceptance of the additional or different terms. [Comment 2 was amended in 1966.]
3. Whether or not additional or different terms will become part of the agreement depends upon the provisions of subsection (2). If they are such as materially to alter the original bargain, they will not be included unless expressly agreed to by the other party. If, however, they are terms which would not so change the bargain they will be incorporated unless notice of objection to them has already been given or is given within a reasonable time.
4. Examples of typical clauses which would normally “materially alter” the contract and so result in surprise or hardship if incorporated without express awareness by the other party are: a clause negating such standard warranties as that of merchantability or fitness for a particular purpose in circumstances in which either warranty normally attaches; a clause requiring a guaranty of 90% or 100% deliveries in case such as a contract by cannery, where the usage of the trade allows greater quantity leeways; a clause reserving to the seller the power to cancel upon the buyer’s failure to meet any invoice when due; a clause requiring that complaints be made in a time materially shorter than customary or reasonable.
5. Examples of clauses which involve no element of unreasonable surprise and which therefore are to be incorporated in the contract unless notice of objection is seasonably given are: a clause setting forth and perhaps enlarging slightly upon the seller’s exemption due to supervening causes beyond his control, similar to those covered by the provision of this Article on merchant’s excuse by failure of presupposed conditions or a clause fixing in advance any reasonable formula of proration under such circumstances; a clause fixing a reasonable time for complaints within customary limits, or in the case of a purchase for sub-sale, providing for inspection by the sub-purchaser; a clause providing for interest on overdue invoices or fixing the seller’s standard credit terms where they are within the range of trade practice and do not limit any credit bargained for; a clause limiting the right of rejection for defects which fall within the customary trade tolerances for acceptance “with

adjustment” or otherwise limiting remedy in a reasonable manner (see Sections 2–718 and 2–719).

6. If no answer is received within a reasonable time after additional terms are proposed, it is both fair and commercially sound to assume that their inclusion has been assented to. Where clauses on confirming forms sent by both parties conflict each party must be assumed to object to a clause of the other conflicting with one on the confirmation sent by himself. As a result the requirement that there be notice of objection which is found in subsection (2) is satisfied and the conflicting terms do not become a part of the contract. The contract then consists of the terms originally expressly agreed to, terms on which the confirmations agree, and terms supplied by this Act, including subsection (2). The written confirmation is also subject to Section 2–201. Under that section a failure to respond permits enforcement of a prior oral agreement; under this section a failure to respond permits additional terms to become part of the agreement. [Comment 6 was amended in 1966.]
7. In many cases, as where goods are shipped, accepted and paid for before any dispute arises, there is no question whether a contract has been made. In such cases, where the writings of the parties do not establish a contract, it is not necessary to determine which act or document constituted the offer and which the acceptance. See Section 2–204. The only question is what terms are included in the contract, and subsection (3) furnishes the governing rule. [Comment 7 was added in 1966.]

Cross References:

See generally Section 2–302.

Point 5: Sections 2–513, 2–602, 2–607, 2–609, 2–612, 2–614, 2–615, 2–616, 2–718 and 2–719.

Point 6: Sections 1–102 and 2–104.

Definitional Cross References:

“Between merchants”. Section 2–104.

“Contract”. Section 1–201.

“Notification”. Section 1–201.

“Reasonable time”. Section 1–204.

“Seasonably”. Section 1–204.

“Send”. Section 1–201.

“Term”. Section 1–201.

“Written”. Section 1–201.

§ 2–208. Course of Performance or Practical Construction.

- (1) Where the contract for sale involves repeated occasions for performance by either party with knowledge of the nature of the performance and opportunity for objection to it by the other, any course of performance accepted or acquiesced in without objection shall be relevant to determine the meaning of the agreement.

- (2) The express terms of the agreement and any such course of performance, as well as any course of dealing and usage of trade, shall be construed whenever reasonable as consistent with each other; but when such construction is unreasonable, express terms shall control course of performance and course of performance shall control both course of dealing and usage of trade (Section 1–205).
- (3) Subject to the provisions of the next section on modification and waiver, such course of performance shall be relevant to show a waiver or modification of any term inconsistent with such course of performance.

§ 2–209. Modification, Rescission and Waiver.

- (1) An agreement modifying a contract within this Article needs no consideration to be binding.
- (2) A signed agreement which excludes modification or rescission except by a signed writing cannot be otherwise modified or rescinded, but except as between merchants such a requirement on a form supplied by the merchant must be separately signed by the other party.
- (3) The requirements of the statute of frauds section of this Article (Section 2–201) must be satisfied if the contract as modified is within its provisions.
- (4) Although an attempt at modification or rescission does not satisfy the requirements of subsection (2) or (3) it can operate as a waiver.
- (5) 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.

§ 2–210. Delegation of Performance; Assignment of Rights.

- (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. A right to damages for breach of the whole contract or a right arising out of the assignor's due performance of his entire obligation can be assigned despite agreement otherwise.
- (3) Unless the circumstances indicate the contrary a prohibition of assignment of "the contract" is to be construed as barring only the delegation to the assignee of the assignor's performance.
- (4) An assignment of "the contract" or of "all my rights under the contract" or an assignment in similar general terms is an assignment of rights and

unless the language or the circumstances (as in an assignment for security) indicate the contrary, it is a delegation of performance of the duties of the assignor and its acceptance by the assignee constitutes a promise by him to perform those duties. This promise is enforceable by either the assignor or the other party to the original contract.

- (5) The other party may treat any assignment which delegates performance as creating reasonable grounds for insecurity and may without prejudice to his rights against the assignor demand assurances from the assignee (Section 2-609).

Part 3 General Obligation and Construction of Contract

§ 2-301. General Obligations of Parties.

The obligation of the seller is to transfer and deliver and that of the buyer is to accept and pay in accordance with the contract.

§ 2-302. Unconscionable Contract or Clause.

- (1) 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.
- (2) 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.

§ 2-303. Allocation or Division of Risks.

Where this Article allocates a risk or a burden as between the parties “unless otherwise agreed”, the agreement may not only shift the allocation but may also divide the risk or burden.

§ 2-304. Price Payable in Money, Goods, Realty, or Otherwise.

- (1) The price can be made payable in money or otherwise. If it is payable in whole or in part in goods each party is a seller of the goods which he is to transfer.
- (2) Even though all or part of the price is payable in an interest in realty the transfer of the goods and the seller’s obligations with reference to them are subject to this Article, but not the transfer of the interest in realty or the transferor’s obligations in connection therewith.

§ 2-305. Open Price Term.

- (1) The parties if they so intend can conclude a contract for sale even though the price is not settled. In such a case the price is a reasonable price at the time for delivery if

- (a) nothing is said as to price; or
 - (b) the price is left to be agreed by the parties and they fail to agree; or
 - (c) the price is to be fixed in terms of some agreed market or other standard as set or recorded by a third person or agency and it is not so set or recorded.
- (2) A price to be fixed by the seller or by the buyer means a price for him to fix in good faith.
 - (3) When a price left to be fixed otherwise than by agreement of the parties fails to be fixed through fault of one party the other may at his option treat the contract as cancelled or himself fix a reasonable price.
 - (4) Where, however, the parties intend not to be bound unless the price be fixed or agreed and it is not fixed or agreed there is no contract. In such a case the buyer must return any goods already received or if unable so to do must pay their reasonable value at the time of delivery and the seller must return any portion of the price paid on account.

§ 2-306. Output, Requirements and Exclusive Dealings.

- (1) A term which measures the quantity by the output of the seller or the requirements of the buyer means such actual output or requirements as may occur in good faith, except that no quantity unreasonably disproportionate to any stated estimate or in the absence of a stated estimate to any normal or otherwise comparable prior output or requirements may be tendered or demanded.
- (2) A lawful agreement by either the seller or the buyer for exclusive dealing in the kind of goods concerned imposes unless otherwise agreed an obligation by the seller to use best efforts to supply the goods and by the buyer to use best efforts to promote their sale.

§ 2-307. Delivery in Single Lot or Several Lots.

Unless otherwise agreed all goods called for by a contract for sale must be tendered in a single delivery and payment is due only on such tender but where the circumstances give either party the right to make or demand delivery in lots the price if it can be apportioned may be demanded for each lot.

§ 2-308. Absence of Specified Place for Delivery.

Unless otherwise agreed

- (a) the place for delivery of goods is the seller's place of business or if he has none his residence; but
- (b) in a contract for sale of identified goods which to the knowledge of the parties at the time of contracting are in some other place, that place is the place for their delivery; and
- (c) documents of title may be delivered through customary banking channels.

§ 2-309. Absence of Specific Time Provisions; Notice of Termination.

- (1) The time for shipment or delivery or any other action under a contract if not provided in this Article or agreed upon shall be a reasonable time.

- (2) Where the contract provides for successive performances but is indefinite in duration it is valid for a reasonable time but unless otherwise agreed may be terminated at any time by either party.
- (3) Termination of a contract by one party except on the happening of an agreed event requires that reasonable notification be received by the other party and an agreement dispensing with notification is invalid if its operation would be unconscionable.

§ 2-310. Open Time for Payment or Running of Credit; Authority to Ship Under Reservation.

Unless otherwise agreed

- (a) payment is due at the time and place at which the buyer is to receive the goods even though the place of shipment is the place of delivery; and
- (b) if the seller is authorized to send the goods he may ship them under reservation, and may tender the documents of title, but the buyer may inspect the goods after their arrival before payment is due unless such inspection is inconsistent with the terms of the contract (Section 2-513); and
- (c) if delivery is authorized and made by way of documents of title otherwise than by subsection (b) then payment is due at the time and place at which the buyer is to receive the documents regardless of where the goods are to be received; and
- (d) where the seller is required or authorized to ship the goods on credit the credit period runs from the time of shipment but post-dating the invoice or delaying its dispatch will correspondingly delay the starting of the credit period.

§ 2-311. Options and Cooperation Respecting Performance.

- (1) An agreement for sale which is otherwise sufficiently definite (subsection (3) of Section 2-204) to be a contract is not made invalid by the fact that it leaves particulars of performance to be specified by one of the parties. Any such specification must be made in good faith and within limits set by commercial reasonableness.
- (2) Unless otherwise agreed specifications relating to assortment of the goods are at the buyer's option and except as otherwise provided in subsections (1)(c) and (3) of Section 2-319 specifications or arrangements relating to shipment are at the seller's option.
- (3) Where such specification would materially affect the other party's performance but is not seasonably made or where one party's cooperation is necessary to the agreed performance of the other but is not seasonably forthcoming, the other party in addition to all other remedies
 - (a) is excused for any resulting delay in his own performance; and
 - (b) may also either proceed to perform in any reasonable manner or after the time for a material part of his own performance treat the failure to specify or to cooperate as a breach by failure to deliver or accept the goods.

§ 2-312. Warranty of Title and Against Infringement; Buyer's Obligation Against Infringement.

- (1) Subject to subsection (2) there is in a contract for sale a warranty by the seller that
 - (a) the title conveyed shall be good, and its transfer rightful; and
 - (b) the goods shall be delivered free from any security interest or other lien or encumbrance of which the buyer at the time of contracting has no knowledge.
- (2) A warranty under subsection (1) will be excluded or modified only by specific language or by circumstances which give the buyer reason to know that the person selling does not claim title in himself or that he is purporting to sell only such right or title as he or a third person may have.
- (3) Unless otherwise agreed a seller who is a merchant regularly dealing in goods of the kind warrants that the goods shall be delivered free of the rightful claim of any third person by way of infringement or the like but a buyer who furnishes specifications to the seller must hold the seller harmless against any such claim which arises out of compliance with the specifications.

§ 2-313. Express Warranties by Affirmation, Promise, Description, Sample.

- (1) Express warranties by the seller are created as follows:
 - (a) Any affirmation of fact or promise made by the seller to the buyer which relates to the goods and becomes part of the basis of the bargain creates an express warranty that the goods shall conform to the affirmation or promise.
 - (b) Any description or model which is made part of the basis of the bargain creates an express warranty that the goods shall conform to the description.
 - (c) Any sample or model which is made part of the basis of the bargain creates an express warranty that the whole of the goods shall conform to the sample or model.
- (2) It is not necessary to the creation of an express warranty that the seller use formal words such as "warrant" or "guarantee" or that he have a specific intention to make a warranty, but an affirmation merely of the value of the goods or a statement purporting to be merely the seller's opinion or commendation of the goods does not create a warranty.

§ 2-314. Implied Warranty: Merchantability; Usage of Trade.

- (1) Unless excluded or modified (Section 2-316), a warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind. Under this section the serving for value of food or drink to be consumed either on the premises or elsewhere is a sale.
- (2) Goods to be merchantable must be at least such as

- (a) pass without objection in the trade under the contract description; and
 - (b) in the case of fungible goods, are of fair average quality within the description; and
 - (c) are fit for the ordinary purposes for which such goods are used; and
 - (d) run, within the variations permitted by the agreement, of even kind, quality and quantity within each unit and among all units involved; and
 - (e) are adequately contained, packaged, and labeled as the agreement may require; and
 - (f) conform to the promise or affirmations of fact made on the container or label if any.
- (3) Unless excluded or modified (Section 2–316) other implied warranties may arise from course of dealing or usage of trade.

§ 2–315. Implied Warranty: Fitness for Particular Purpose.

Where the seller at the time of contracting has reason to know any particular purpose for which the goods are required and that the buyer is relying on the seller's skill or judgment to select or furnish suitable goods, there is unless excluded or modified under the next section an implied warranty that the goods shall be fit for such purpose.

§ 2–316. Exclusion or Modification of Warranties.

- (1) Words or conduct relevant to the creation of an express warranty and words or conduct tending to negate or limit warranty shall be construed wherever reasonable as consistent with each other; but subject to the provisions of this Article on parol or extrinsic evidence (Section 2–202) negation or limitation is inoperative to the extent that such construction is unreasonable.
- (2) Subject to subsection (3), to exclude or modify the implied warranty of merchantability or any part of it the language must mention merchantability and in case of a writing must be conspicuous, and to exclude or modify any implied warranty of fitness the exclusion must be by a writing and conspicuous. Language to exclude all implied warranties of fitness is sufficient if it states, for example, that "There are no warranties which extend beyond the description on the face hereof."
- (3) Notwithstanding subsection (2)
 - (a) unless the circumstances indicate otherwise, all implied warranties are excluded by expressions like "as is", "with all faults" or other language which in common understanding calls the buyer's attention to the exclusion of warranties and makes plain that there is no implied warranty; and
 - (b) when the buyer before entering into the contract has examined the goods or the sample or model as fully as he desired or has refused to examine the goods there is no implied warranty with regard to defects which an examination ought in the circumstances to have revealed to him; and
 - (c) an implied warranty can also be excluded or modified by course of dealing or course of performance or usage of trade.

- (4) Remedies for breach of warranty can be limited in accordance with the provisions of this Article on liquidation or limitation of damages and on contractual modification of remedy (Sections 2–718 and 2–719).

§ 2–317. Cumulation and Conflict of Warranties Express or Implied.

Warranties whether express or implied shall be construed as consistent with each other and as cumulative, but if such construction is unreasonable the intention of the parties shall determine which warranty is dominant. In ascertaining that intention the following rules apply:

- (a) Exact or technical specifications displace an inconsistent sample or model or general language of description.
- (b) A sample from an existing bulk displaces inconsistent general language of description.
- (c) Express warranties displace inconsistent implied warranties other than an implied warranty of fitness for a particular purpose.

§ 2–318. Third Party Beneficiaries of Warranties Express or Implied.

Alternate A

A seller's warranty whether express or implied extends to any natural person who is in the family or household of his buyer or who is a guest in his home if it is reasonable to expect that such person may use, consume or be affected by the goods and who is injured in person by breach of the warranty. A seller may not exclude or limit the operation of this section.

Alternative B

A seller's warranty whether express or implied extends to any natural person who may reasonably be expected to use, consume or be affected by the goods and who is injured in person by breach of the warranty. A seller may not exclude or limit the operation of this section.

Alternative C

A seller's warranty whether express or implied extends to any person who may reasonably be expected to use, consume or be affected by the goods and who is injured by breach of the warranty. A seller may not exclude or limit the operation of this section with respect to injury to the person of an individual to whom the warranty extends.

As amended in 1966.

§ 2–319. F.O.B. and F.A.S. Terms.

- (1) Unless otherwise agreed the term F.O.B. (which means "free on board") at a named place, even though used only in connection with the stated price, is a delivery term under which
 - (a) when the term is F.O.B. the place of shipment, the seller must at that place ship the goods in the manner provided in this Article (Section 2–504) and bear the expense and risk of putting them into the possession of the carrier; or
 - (b) when the term is F.O.B. the place of destination, the seller must at his own expense and risk transport the goods to that place and there tender delivery of them in the manner provided in this Article (Section 2–503);

- (c) when under either (a) or (b) the term is also F.O.B. vessel, car or other vehicle, the seller must in addition at his own expense and risk load the goods on board. If the term is F.O.B. vessel the buyer must name the vessel and in an appropriate case the seller must comply with the provisions of this Article on the form of bill of lading (Section 2-323).
- (2) Unless otherwise agreed the term F.A.S. vessel (which means "free alongside") at a named port, even though used only in connection with the stated price, is a delivery term under which the seller must
 - (a) at his own expense and risk deliver the goods alongside the vessel in the manner usual in that port or on a dock designated and provided by the buyer; and
 - (b) obtain and tender a receipt for the goods in exchange for which the carrier is under a duty to issue a bill of lading.
- (3) Unless otherwise agreed in any case falling within subsection (1)(a) or (c) or subsection (2) the buyer must seasonably give any needed instructions for making delivery, including when the term is F.A.S. or F.O.B. the loading berth of the vessel and in an appropriate case its name and sailing date. The seller may treat the failure of needed instructions as a failure of cooperation under this Article (Section 2-311). He may also at his option move the goods in any reasonable manner preparatory to delivery or shipment.
- (4) Under the term F.O.B. vessel or F.A.S. unless otherwise agreed the buyer must make payment against tender of the required documents and the seller may not tender nor the buyer demand delivery of the goods in substitution for the documents.

§ 2-320. C.I.F. and C. & F. Terms.

- (1) The term C.I.F. means that the price includes in a lump sum the cost of the goods and the insurance and freight to the named destination. The term C. & F. or C.F. means that the price so includes cost and freight to the named destination.
- (2) Unless otherwise agreed and even though used only in connection with the stated price and destination, the term C.I.F. destination or its equivalent requires the seller at his own expense and risk to
 - (a) put the goods into the possession of a carrier at the port for shipment and obtain a negotiable bill or bills of lading covering the entire transportation to the named destination; and
 - (b) load the goods and obtain a receipt from the carrier (which may be contained in the bill of lading) showing that the freight has been paid or provided for; and
 - (c) obtain a policy or certificate of insurance, including any war risk insurance, of a kind and on terms then current at the port of shipment in the usual amount, in the currency of the contract, shown to cover the same goods covered by the bill of lading and providing for payment of loss to the order of the buyer or for the account of whom it may

- concern; but the seller may add to the price the amount of the premium for any such war risk insurance; and
- (d) prepare an invoice of the goods and procure any other documents required to effect shipment or to comply with the contract; and
 - (e) forward and tender with commercial promptness all the documents in due form and with any indorsement necessary to perfect the buyer's rights.
- (3) Unless otherwise agreed the term C. & F. or its equivalent has the same effect and imposes upon the seller the same obligations and risks as a C.I.F. term except the obligation as to insurance.
 - (4) Under the term C.I.F. or C. & F. unless otherwise agreed the buyer must make payment against tender of the required documents and the seller may not tender nor the buyer demand delivery of the goods in substitution for the documents.

§ 2-321. C.I.F. or C. & F.: “Net Landed Weights”; “Payment on Arrival”; Warranty of Condition on Arrival.

Under a contract containing a term C.I.F. or C. & F.

- (1) Where the price is based on or is to be adjusted according to “net landed weights”, “delivered weights”, “out turn” quantity or quality or the like, unless otherwise agreed the seller must reasonably estimate the price. The payment due on tender of the documents called for by the contract is the amount so estimated, but after final adjustment of the price a settlement must be made with commercial promptness.
- (2) An agreement described in subsection (1) or any warranty of quality or condition of the goods on arrival places upon the seller the risk of ordinary deterioration, shrinkage and the like in transportation but has no effect on the place or time of identification to the contract for sale or delivery or on the passing of the risk of loss.
- (3) Unless otherwise agreed where the contract provides for payment on or after arrival of the goods the seller must before payment allow such preliminary inspection as is feasible; but if the goods are lost delivery of the documents and payment are due when the goods should have arrived.

§ 2-322. Delivery “Ex-Ship”.

- (1) Unless otherwise agreed a term for delivery of goods “ex-ship” (which means from the carrying vessel) or in equivalent language is not restricted to a particular ship and requires delivery from a ship which has reached a place at the named port of destination where goods of the kind are usually discharged.
- (2) Under such a term unless otherwise agreed
 - (a) the seller must discharge all liens arising out of the carriage and furnish the buyer with a direction which puts the carrier under a duty to deliver the goods; and

- (b) the risk of loss does not pass to the buyer until the goods leave the ship's tackle or are otherwise properly unloaded.

§ 2-323. Form of Bill of Lading Required in Overseas Shipment; "Overseas".

- (1) Where the contract contemplates overseas shipment and contains a term C.I.F. or C. & F. or F.O.B. vessel, the seller unless otherwise agreed must obtain a negotiable bill of lading stating that the goods have been loaded in board or, in the case of a term C.I.F. or C. & F., received for shipment.
- (2) Where in a case within subsection (1) a bill of lading has been issued in a set of parts, unless otherwise agreed if the documents are not to be sent from abroad the buyer may demand tender of the full set; otherwise only one part of the bill of lading need be tendered. Even if the agreement expressly requires a full set
 - (a) due tender of a single part is acceptable within the provisions of this Article on cure of improper deliver (subsection (1) of Section 2-508); and
 - (b) even though the full set is demanded, if the documents are sent from abroad the person tendering an incomplete set may nevertheless require payment upon furnishing an indemnity which the buyer in good faith deems adequate.
- (3) A shipment by water or by air or a contract contemplating such shipment is "overseas" insofar as by usage of trade or agreement it is subject to the commercial, financing or shipping practices characteristic of international deep water commerce.

§ 2-324. "No Arrival, No Sale" Term.

Under a term "no arrival, no sale" or terms of like meaning, unless otherwise agreed,

- (a) the seller must properly ship conforming goods and if they arrive by any means he must tender them on arrival but he assumes no obligation that the goods will arrive unless he has caused the non-arrival; and
- (b) where without fault of the seller the goods are in part lost or have so deteriorated as no longer to conform to the contract or arrive after the contract time, the buyer may proceed as if there had been casualty to identified goods (Section 2-613).

§ 2-325. "Letter of Credit" Term; "Confirmed Credit".

- (1) Failure of the buyer seasonably to furnish an agreed letter of credit is a breach of the contract for sale.
- (2) The delivery to seller of a proper letter of credit suspends the buyer's obligation to pay. If the letter of credit is dishonored, the seller may on seasonable notification to the buyer require payment directly from him.
- (3) Unless otherwise agreed the term "letter of credit" or "banker's credit" in a contract for sale means an irrevocable credit issued by a financing agency of good repute and, where the shipment is overseas, a good international repute. The term "confirmed credit" means that the credit

must also carry the direct obligation of such an agency which does business in the seller's financial market.

§ 2-326. Sale on Approval and Sale or Return; Consignment Sales and Rights of Creditors.

- (1) Unless otherwise agreed, if delivered goods may be returned by the buyer even though they conform to the contract, the transaction is
 - (a) a "sale on approval" if the goods are delivered primarily for use, and
 - (b) a "sale or return" if the goods are delivered primarily for resale.
- (2) Except as provided in subsection (3), goods held on approval are not subject to the claims of the buyer's creditors until acceptance; goods held on sale or return are subject to such claims while in the buyer's possession.
- (3) Where goods are delivered to a person for sale and such person maintains a place of business at which he deals in goods of the kind involved, under a name other than the name of the person making delivery, then with respect to claims of creditor of the person conducting the business the goods are deemed to be on sale or return. The provisions of this subsection are applicable even though an agreement purports to reserve title to the person making delivery until payment or resale or uses such words as "on consignment" or "on memorandum". However, this subsection is not applicable if the person making delivery
 - (a) complies with an applicable law providing for a consignor's interest or the like to be evidenced by a sign, or
 - (b) establishes that the person conducting the business is generally known by his creditors to be substantially engaged in selling the goods of others, or
 - (c) complies with the filing provisions of the Article on Secured Transactions (Article 9).
- (4) Any "or return" term of a contract for sale is to be treated as a separate contract for sale within the statute of frauds section of this Article (Section 2-201) and as contradicting the sale aspect of the contract within the provisions of this Article on parol or extrinsic evidence (Section 2-202).

§ 2-327. Special Incidents of Sale on Approval and Sale or Return.

- (1) Under a sale on approval unless otherwise agreed
 - (a) although the goods are identified to the contract the risk of loss and the title do not pass to the buyer until acceptance; and
 - (b) use of the goods consistent with the purpose of trial is not acceptance but failure seasonably to notify the seller of election to return the goods is acceptance, and if the goods conform to the contract acceptance of any part is acceptance of the whole; and
 - (c) after due notification of election to return, the return is at the seller's risk and expense but a merchant buyer must follow any reasonable instructions.

- (2) Under a sale or return unless otherwise agreed
 - (a) the option to return extends to the whole or any commercial unit of the goods while in substantially their original condition, but must be exercised seasonably; and
 - (b) the return is at the buyer's risk and expense.

§ 2–328. Sale by Auction.

- (1) In a sale by auction if goods are put up in lots each lot is the subject of a separate sale.
- (2) A sale by auction is complete when the auctioneer so announces by the fall of the hammer or in other customary manner. Where a bid is made while the hammer is falling in acceptance of a prior bid the auctioneer may in his discretion reopen the bidding or declare the goods sold under the bid on which the hammer was falling.
- (3) Such a sale is with reserve unless the goods are in explicit terms put up without reserve. In an auction with reserve the auctioneer may withdraw the goods at any time until he announces completion of the sale. In an auction without reserve, after the auctioneer calls for bids on an article or lot, that article or lot cannot be withdrawn unless no bid is made within a reasonable time. In either case a bidder may retract his bid until the auctioneer's announcement of completion of the sale, but a bidder's retraction does not revive any previous bid.
- (4) If the auctioneer knowingly receives a bid on the seller's behalf or the seller makes or procures such a bid, and notice has not been given that liberty for such bidding is reserved, the buyer may at his option avoid the sale or take the goods at the price of the last good faith bid prior to the completion of the sale. This subsection shall not apply to any bid at a forced sale.

Part 4 Title, Creditors and Good Faith Purchasers

§ 2–401. Passing of Title; Reservation for Security; Limited Application of This Section.

Each provision of this Article with regard to the rights, obligations and remedies of the seller, the buyer, purchasers or other third parties applies irrespective of title to the goods except where the provision refers to such title. Insofar as situations are not covered by the other provisions of this Article and matters concerning title become material the following rules apply:

- (1) Title to goods cannot pass under a contract for sale prior to their identification to the contract (Section 2–501), and unless otherwise explicitly agreed the buyer acquires by their identification a special property as limited by this Act. Any retention or reservation by the seller of the title (property) in goods shipped or delivered to the buyer is limited in effect to a reservation of a security interest. Subject to these provisions and to the provisions of the Article on Secured Transactions

- (Article 9), title to goods passes from the seller to the buyer in any manner and on any conditions explicitly agreed on by the parties.
- (2) Unless otherwise explicitly agreed title passes to the buyer at the time and place at which the seller completes his performance with reference to the physical delivery of the goods, despite any reservation of a security interest and even though a document of title is to be delivered at a different time or place; and in particular and despite any reservation of a security interest by the bill of lading
 - (a) if the contract requires or authorizes the seller to send the goods to the buyer but does not require him to deliver them at destination, title passes to the buyer at the time and place of shipment; but
 - (b) if the contract requires delivery at destination, title passes on tender there.
 - (3) Unless otherwise explicitly agreed where delivery is to be made without moving the goods,
 - (a) if the seller is to deliver a document of title, title passes at the time when and the place where he delivers such documents; or
 - (b) if the goods are at the time of contracting already identified and no documents are to be delivered, title passes at the time and place of contracting.
 - (4) A rejection or other refusal by the buyer to receive or retain the goods, whether or not justified, or a justified revocation of acceptance revests title to the goods in the seller. Such revesting occurs by operation of law and is not a “sale”.

§ 2-402. Rights of Seller’s Creditors Against Sold Goods.

- (1) Except as provided in subsections (2) and (3), rights of unsecured creditors of the seller with respect to goods which have been identified to a contract for sale are subject to the buyer’s rights to recover the goods under this Article (Sections 2-502 and 2-716).
- (2) A creditor of the seller may treat a sale or an identification of goods to a contract for sale as void if as against him a retention of possession by the seller is fraudulent under any rule of law of the state where the goods are situated, except that retention of possession in good faith and current course of trade by a merchant-seller for a commercially reasonable time after a sale or identification is not fraudulent.
- (3) Nothing in this Article shall be deemed to impair the rights of creditors of the seller
 - (a) under the provisions of the Article on Secured Transactions (Article 9); or
 - (b) where identification to the contract or delivery is made not in current course of trade but in satisfaction of or as security for a pre-existing claim for money, security or the like and is made under circumstances which under any rule of law of the state where the goods are situated

would apart from this Article constitute the transaction of a fraudulent transfer or voidable preference.

§ 2-403. Power to Transfer; Good Faith Purchase of Goods; “Entrusting”.

- (1) A purchaser of goods acquires all title which his transferor had or had power to transfer except that a purchaser of a limited interest acquires rights only to the extent of the interest purchased. A person with voidable title has power to transfer a good title to a good faith purchaser for value. When goods have been delivered under a transaction of purchase the purchaser has such power even though
 - (a) the transferor was deceived as to the identity of the purchaser, or
 - (b) the delivery was in exchange for a check which is later dishonored, or
 - (c) it was agreed that the transaction was to be a “cash sale”, or
 - (d) the delivery was procured through fraud punishable as larcenous under the criminal law.
- (2) Any entrusting of possession of goods to a merchant who deals in goods of that kind gives him power to transfer all rights of the entruster to a buyer in ordinary course of business.
- (3) “Entrusting” includes any delivery and any acquiescence in retention of possession regardless of any condition expressed between the parties to the delivery or acquiescence and regardless of whether the procurement of the entrusting or the possessor’s disposition of the goods have been such as to be larcenous under the criminal law.
- (4) The rights of other purchasers of goods and of lien creditors are governed by the Articles on Secured Transactions (Article 9) and Documents of Title (Article 7).

As amended in 1988.

Part 5 Performance

§ 2-501. Insurable Interest in Goods; Manner of Identification of Goods.

- (1) The buyer obtains a special property and an insurable interest in goods by identification of existing goods as goods to which the contract refers even though the goods so identified are non-conforming and he has an option to return or reject them. Such identification can be made at any time and in any manner explicitly agreed to by the parties. In the absence of explicit agreement identification occurs
 - (a) when the contract is made if it is for the sale of goods already existing and identified;
 - (b) if the contract is for the sale of future goods other than those described in paragraph (c), when goods are shipped, marked or otherwise designated by the seller as goods to which the contract refers;
 - (c) when the crops are planted or otherwise become growing crops or the young are conceived if the contract is for the sale of unborn young to

be born within twelve months after contracting or for the sale of crops to be harvested within twelve months or the next normal harvest season after contracting whichever is longer.

- (2) The seller retains an insurable interest in goods so long as title to or any security interest in the goods remains in him and where the identification is by the seller alone he may until default or insolvency or notification to the buyer that the identification is final substitute other goods for those identified.
- (3) Nothing in this section impairs any insurable interest recognized under any other statute or rule of law.

§ 2-502. Buyer's Right to Goods on Seller's Insolvency.

- (1) Subject to subsection (2) and even though the goods have not been shipped a buyer who has paid a part or all of the price of goods in which he has a special property under the provisions of the immediately preceding section may on making and keeping good a tender of any unpaid portion of their price recover them from the seller if the seller becomes insolvent within ten days after receipt of the first installment on their price.
- (2) If the identification creating his special property has been made by the buyer he acquires the right to recover the goods only if they conform to the contract for sale.

§ 2-503. Manner of Seller's Tender of Delivery.

- (1) Tender of delivery requires that the seller put and hold conforming goods at the buyer's disposition and give the buyer any notification reasonably necessary to enable him to take delivery. The manner, time and place for tender are determined by the agreement and this Article, and in particular
 - (a) tender must be at a reasonable hour, and if it is of goods they must be kept available for the period reasonably necessary to enable the buyer to take possession; but
 - (b) unless otherwise agreed the buyer must furnish facilities reasonably suited to the receipt of the goods.
- (2) Where the case is within the next section respecting shipment tender requires that the seller comply with its provisions.
- (3) Where the seller is required to deliver at a particular destination tender requires that he comply with subsection (1) and also in any appropriate case tender documents as described in subsections (4) and (5) of this section.
- (4) Where goods are in the possession of a bailee and are to be delivered without being moved
 - (a) tender requires that the seller either tender a negotiable document of title covering such goods or procure acknowledgment by the bailee of the buyer's right to possession of the goods; but
 - (b) tender to the buyer of a non-negotiable document of title or of a written direction to the bailee to deliver is sufficient tender unless the

buyer seasonably objects, and receipt by the bailee of notification of the buyer's rights fixes those rights as against the bailee and all third persons; but risk of loss of the goods and of any failure by the bailee to honor the non-negotiable document of title or to obey the direction remains on the seller until the buyer has had a reasonable time to present the document or direction, and a refusal by the bailee to honor the document or to obey the direction defeats the tender.

- (5) Where the contract requires the seller to deliver documents.
 - (a) he must tender all such documents in correct form, except as provided in this Article with respect to bills of lading in a set (subsection (2) of Section 2-323); and
 - (b) tender through customary banking channels is sufficient and dishonor of a draft accompanying the documents constitutes non-acceptance or rejection.

§ 2-504. Shipment by Seller.

Where the seller is required or authorized to send the goods to the buyer and the contract does not require him to deliver them at a particular destination, then unless otherwise agreed he must

- (a) put the goods in the possession of such a carrier and make such a contract for their transportation as may be reasonable having regard to the nature of the goods and other circumstances of the case; and
- (b) obtain and promptly deliver or tender in due form any document necessary to enable the buyer to obtain possession of the goods or otherwise required by the agreement or by usage of trade; and
- (c) promptly notify the buyer of the shipment.

Failure to notify the buyer under paragraph (c) or to make a proper contract under paragraph (a) is a ground for rejection only if material delay or loss ensues.

§ 2-505. Seller's Shipment Under Reservation.

- (1) Where the seller has identified goods to the contract by or before shipment:
 - (a) his procurement of a negotiable bill of lading to his own order or otherwise reserves in him a security interest in the goods. His procurement of the bill to the order of a financing agency or of the buyer indicates in addition only the seller's expectation of transferring that interest to the person named.
 - (b) a non-negotiable bill of lading to himself or his nominee reserves possession of the goods as security but except in a case of conditional delivery (subsection (2) of Section 2-507) a non-negotiable bill of lading naming the buyer as consignee reserves no security interest even though the seller retains possession of the bill of lading.
- (2) When shipment by the seller with reservation of a security interest is in violation of the contract for sale it constitutes an improper contract for transportation within the preceding section but impairs neither the

rights given to the buyer by shipment and identification of the goods to the contract nor the seller's powers as a holder of a negotiable document.

§ 2-506. Rights of Financing Agency.

- (1) A financing agency by paying or purchasing for value a draft which relates to a shipment of goods acquires to the extent of the payment or purchase and in addition to its own rights under the draft and any document of title securing it any rights of the shipper in the goods including the right to stop delivery and the shipper's right to have the draft honored by the buyer.
- (2) The right to reimbursement of a financing agency which has in good faith honored or purchased the draft under commitment to or authority from the buyer is not impaired by subsequent discovery of defects with reference to any relevant document which was apparently regular on its face.

§ 2-507. Effect of Seller's Tender; Delivery on Condition.

- (1) Tender of delivery is a condition to the buyer's duty to accept the goods and, unless otherwise agreed, to his duty to pay for them. Tender entitles the seller to acceptance of the goods and to payment according to the contract.
- (2) Where payment is due and demanded on the delivery to the buyer of goods or documents of title, his right as against the seller to retain or dispose of them is conditioned upon his making the payment due.

§ 2-508. Cure by Seller of Improper Tender or Delivery; Replacement.

- (1) Where any tender or delivery by the seller is rejected because non-conforming and the time for performance as not yet expired, the seller may seasonably notify the buyer of his intention to cure and may then within the contract time make a conforming delivery.
- (2) Where the buyer rejects a non-conforming tender which the seller had reasonable grounds to believe would be acceptable with or without money allowance the seller may if he seasonably notifies the buyer have a further reasonable time to substitute a conforming tender.

§ 2-509. Risk of Loss in the Absence of Breach.

- (1) Where the contract requires or authorizes the seller to ship the goods by carrier
 - (a) if it does not require him to deliver them at a particular destination, the risk of loss passes to the buyer when the goods are duly delivered to the carrier even though the shipment is under reservation (Section 2-505); but
 - (b) if it does require him to deliver them at a particular destination and the goods are there duly tendered while in the possession of the carrier, the risk of loss passes to the buyer when the goods are there duly so tendered as to enable the buyer to take delivery.

- (2) Where the goods are held by a bailee to be delivered without being moved, the risk of loss passes to the buyer
 - (a) on his receipt of a negotiable document of title covering the goods; or
 - (b) on acknowledgment by the bailee of the buyer's right to possession of the goods; or
 - (c) after his receipt of a non-negotiable document of title or other written direction to deliver, as provided in subsection (4)(b) of Section 2-503.
- (3) In any case not within subsection (1) or (2), the risk of loss passes to the buyer on his receipt of the goods if the seller is a merchant; otherwise the risk passes to the buyer on tender of delivery.
- (4) The provisions of this section are subject to contrary agreement of the parties and to the provisions of this Article on sale on approval (Section 2-327) and on effect of breach on risk of loss (Section 2-510).

§ 2-510. Effect of Breach on Risk of Loss.

- (1) Where a tender or delivery of goods so fails to conform to the contract as to give a right of rejection the risk of their loss remains on the seller until cure or acceptance.
- (2) Where the buyer rightfully revokes acceptance he may to the extent of any deficiency in his effective insurance coverage treat the risk of loss as having rested on the seller from the beginning.
- (3) Where the buyer as to conforming goods already identified to the contract for sale repudiates or is otherwise in breach before risk of their loss has passed to him, the seller may to the extent of any deficiency in his effective insurance coverage treat the risk of loss as resting on the buyer for a commercially reasonable time.

§ 2-511. Tender of Payment by Buyer; Payment by Check.

- (1) Unless otherwise agreed tender of payment is a condition to the seller's duty to tender and complete any delivery.
- (2) Tender of payment is sufficient when made by any means or in any manner current in the ordinary course of business unless the seller demands payment in legal tender and gives any extension of time reasonably necessary to procure it.
- (3) Subject to the provisions of this Act on the effect of an instrument on an obligation (Section 3-310), payment by check is conditional and is defeated as between the parties by dishonor of the check on due presentment.

As amended in 1994.

§ 2-512. Payment by Buyer Before Inspection.

- (1) Where the control requires payment before inspection non-conformity of the goods does not excuse the buyer from so making payment unless
 - (a) the non-conformity appears without inspection; or

- (b) despite tender of the required documents the circumstances would justify injunction against honor under this Act (Section 5–109(b)).
- (2) Payment pursuant to subsection (1) does not constitute an acceptance of goods or impair the buyer's right to inspect or any of his remedies. As amended in 1995.

§ 2–513. Buyer's Right to Inspection of Goods.

- (1) Unless otherwise agreed and subject to subsection (3), where goods are tendered or delivered or identified to the contract for sale, the buyer has a right before payment or acceptance to inspect them at any reasonable place and time and in any reasonable manner. When the seller is required or authorized to send the goods to the buyer, the inspection may be after their arrival.
- (2) Expenses of inspection must be borne by the buyer but may be recovered from the seller if the goods do not conform and are rejected.
- (3) Unless otherwise agreed and subject to the provisions of this Article on C.I.F. contracts (subsection (3) of Section 2–321), the buyer is not entitled to inspect the goods before payment of the price when the contract provides
 - (a) for delivery "C.O.D." or on other like terms; or
 - (b) for payment against documents of title except where such payment is due only after the goods are to become available for inspection.
- (4) A place or method of inspection fixed by the parties is presumed to be exclusive but unless otherwise expressly agreed it does not postpone identification or shift the place for delivery or for passing the risk of loss. If compliance becomes impossible, inspection shall be as provided in this section unless the place or method fixed was clearly intended as an indispensable condition failure of which avoids the contract.

§ 2–514. When Documents Deliverable on Acceptance; When on Payment.

Unless otherwise agreed documents against which a draft is drawn are to be delivered to the drawee on acceptance of the draft if it is payable more than three days after presentment; otherwise, only on payment.

§ 2–515. Preserving Evidence of Goods in Dispute.

In furtherance of the adjustment of any claim or dispute

- (a) either party on reasonable notification to the other and for the purpose of ascertaining the facts and preserving evidence has the right to inspect, test and sample the goods including such of them as may be in the possession or control of the other; and
- (b) the parties may agree to a third party inspection or survey to determine the conformity or condition of the goods and may agree that the findings shall be binding upon them in any subsequent litigation or adjustment.

Part 6 Breach, Repudiation and Excuse

§2-601. Buyer's Rights on Improper Delivery.

Subject to the provisions of this Article on breach in installment contracts (Section 2-612) and unless otherwise agreed under the sections on contractual limitations of remedy (Sections 2-718 and 2-719), if the goods or the tender of delivery fail in any respect to conform to the contract, the buyer may

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

§ 2-602. Manner and Effect of Rightful Rejection.

- (1) Rejection of goods must be within a reasonable time after their delivery or tender. It is ineffective unless the buyer seasonably notifies the seller.
- (2) Subject to the provisions of the two following sections on rejected goods (Sections 2-603 and 2-604),
 - (a) after rejection any exercise of ownership by the buyer with respect to any commercial unit is wrongful as against the seller; and
 - (b) if the buyer has before rejection taken physical possession of goods in which he does not have a security interest under the provisions of this Article (subsection (3) of Section 2-711), he is under a duty after rejection to hold them with reasonable care at the seller's disposition for a time sufficient to permit the seller to remove them; but
 - (c) the buyer has no further obligations with regard to goods rightfully rejected.
- (3) The seller's rights with respect to goods wrongfully rejected are governed by the provisions of this Article on Seller's remedies in general (Section 2-703).

§ 2-603. Merchant Buyer's Duties as to Rightfully Rejected Goods.

- (1) Subject to any security interest in the buyer (subsection (3) of Section 2-711), when the seller has no agent or place of business at the market of rejection a merchant buyer is under a duty after rejection of goods in his possession or control to follow any reasonable instructions received from the seller with respect to the goods and in the absence of such instructions to make reasonable efforts to sell them for the seller's account if they are perishable or threaten to decline in value speedily. Instructions are not reasonable if on demand indemnity for expenses is not forthcoming.
- (2) When the buyer sells goods under subsection (1), he is entitled to reimbursement from the seller or out of the proceeds for reasonable expenses of caring for and selling them, and if the expenses include no selling commission then to such commission as is usual in the trade or if there is none to a reasonable sum not exceeding ten per cent on the gross proceeds.
- (3) In complying with this section the buyer is held only to good faith and good faith conduct hereunder is neither acceptance nor conversion nor the basis of an action for damages.

§ 2-604. Buyer's Options as to Salvage of Rightfully Rejected Goods.

Subject to the provisions of the immediately preceding section on perishables if the seller gives no instructions within a reasonable time after notification of rejection the buyer may store the rejected goods for the seller's account or reship them to him or resell them for the seller's account with reimbursement as provided in the preceding section. Such action is not acceptance or conversion.

§ 2-605. Waiver of Buyer's Objections by Failure to Particularize.

- (1) The buyer's failure to state in connection with rejection a particular defect which is ascertainable by reasonable inspection precludes him from relying on the unstated defect to justify rejection or to establish breach
 - (a) where the seller could have cured it if stated seasonably; or
 - (b) between merchants when the seller has after rejection made a request in writing for a full and final written statement of all defects on which the buyer proposes to rely.
- (2) Payment against documents made without reservation of rights precludes recovery of the payment for defects apparent on the face of the documents.

§ 2-606. What Constitutes Acceptance of Goods.

- (1) Acceptance of goods occurs when the buyer
 - (a) after a reasonable opportunity to inspect the goods signifies to the seller that the goods are conforming or that he will take or retain them in spite of their non-conformity; or
 - (b) fails to make an effective rejection (subsection (1) of Section 2-602), but such acceptance does not occur until the buyer has had a reasonable opportunity to inspect them; or
 - (c) does any act inconsistent with the seller's ownership; but if such act is wrongful as against the seller it is an acceptance only if ratified by him.
- (2) Acceptance of a part of any commercial unit is acceptance of that entire unit.

§ 2-607. Effect of Acceptance; Notice of Breach; Burden of Establishing Breach After Acceptance; Notice of Claim or Litigation to Person Answerable Over.

- (1) The buyer must pay at the contract rate for any goods accepted.
- (2) Acceptance of goods by the buyer precludes rejection of the goods accepted and if made with knowledge of a non-conformity cannot be revoked because of it unless the acceptance was on the reasonable assumption that the non-conformity would be seasonably cured but acceptance does not of itself impair any other remedy provided by this Article for non-conformity.
- (3) Where a tender has been accepted
 - (a) the buyer must within a reasonable time after he discovers or should have discovered any breach notify the seller of breach or be barred from any remedy; and

- (b) if the claim is one for infringement or the like (subsection (3) of Section 2-312), and the buyer is sued as a result of such a breach he must so notify the seller within a reasonable time after he receives notice of the litigation or be barred from any remedy over for liability established by the litigation.
- (4) The burden is on the buyer to establish any breach with respect to the goods accepted.
- (5) Where the buyer is sued for breach of a warranty or other obligation for which his seller is answerable over
 - (a) he may give his seller written notice of the litigation. If the notice states that the seller may come in and defend and that if the seller does not so do he will be bound in any action against him by his buyer by any determination of fact common to the two litigations, then unless the seller after reasonable receipt of the notice does come in and defend he is so bound.
 - (b) if the claim is one for infringement or the like (subsection (3) of Section 2-312) the original seller may demand in writing that his buyer turn over to him control of the litigation including settlement or else be barred from any remedy over and if he also agrees to bear all expense and to satisfy any adverse judgment, then unless the buyer after reasonable receipt of the demand does turn over control the buyer is so barred.
- (6) The provisions of subsections (3), (4) and (5) apply to any obligation of a buyer to hold the seller harmless against infringement or the like (subsection (3) of Section 2-312).

§ 2-608. Revocation of Acceptance in Whole or in Part.

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

§ 2-609. Right to Adequate Assurance of Performance.

- (1) A contract for sale imposes an obligation on each party that the other's expectation of receiving due performance will not be impaired. 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.

- (2) Between merchants the reasonableness of grounds for insecurity and the adequacy of any assurance offered shall be determined according to commercial standards.
- (3) Acceptance of any improper delivery or payment does not prejudice the aggrieved party's right to demand adequate assurance of future performance.
- (4) After receipt of a justified demand failure to provide within a reasonable time not exceeding thirty days such assurance of due performance as is adequate under the circumstances of the particular case is a repudiation of the contract.

§ 2-610. Anticipatory Repudiation.

When either party repudiates the contract with respect to a performance not yet due the loss of which will substantially impair the value of the contract to the other, the aggrieved party may

- (a) for a commercially reasonable time await performance by the repudiating party; or
- (b) resort to any remedy for breach (Section 2-703 or Section 2-711), even though he has notified the repudiating party that he would await the latter's performance and has urged retraction; and
- (c) in either case suspend his own performance or proceed in accordance with the provisions of this Article on the seller's right to identify goods to the contract notwithstanding breach or to salvage unfinished goods (Section 2-704).

§ 2-611. Retraction of Anticipatory Repudiation.

- (1) Until the repudiating party's next performance is due he can retract his repudiation unless the aggrieved party has since the repudiation cancelled or materially changed his position or otherwise indicated that he considers the repudiation final.
- (2) Retraction may be by any method which clearly indicates to the aggrieved party that the repudiating party intends to perform, but must include any assurance justifiably demanded under the provisions of this Article (Section 2-609).
- (3) Retraction reinstates the repudiating party's rights under the contract with due excuse and allowance to the aggrieved party for any delay occasioned by the repudiation.

§ 2-612. "Installment Contract"; Breach.

- (1) An "installment contract" is one which requires or authorizes the delivery of goods in separate lots to be separately accepted, even though the contract contains a clause "each delivery is a separate contract" or its equivalent.

- (2) The buyer may reject any installment which is non-conforming if the non-conformity substantially impairs the value of that installment and cannot be cured or if the non-conformity is a defect in the required documents; but if the nonconformity does not fall within subsection (3) and the seller gives adequate assurance of its cure the buyer must accept that installment.
- (3) Whenever non-conformity or default with respect to one or more installments substantially impairs the value of the whole contract there is a breach of the whole. But the aggrieved party reinstates the contract if he accepts a non-conforming installment without seasonably notifying of cancellation or if he brings an action with respect only to past installments or demands performance as to future installments.

§ 2-613. Casualty to Identified Goods.

Where the contract requires for its performance goods identified when the contract is made, and the goods suffer casualty without fault of either party before the risk of loss passes to the buyer, or in a proper case under a “no arrival, no sale” term (Section 2-324) then

- (a) if the loss is total the contract is avoided; and
- (b) if the loss is partial or the goods have so deteriorated as no longer to conform to the contract the buyer may nevertheless demand inspection and at his option either treat the contract as avoided or accept the goods with due allowance from the contract price for the deterioration or the deficiency in quantity but without further right against the seller.

§ 2-614. Substituted Performance.

- (1) Where without fault of either party the agreed berthing, loading, or unloading facilities fail or an agreed type of carrier becomes unavailable or the agreed manner of delivery otherwise becomes commercially impracticable but a commercially reasonable substitute is available, such substitute performance must be tendered and accepted.
- (2) If the agreed means or manner of payment fails because of domestic or foreign governmental regulation, the seller may withhold or stop delivery unless the buyer provides a means or manner of payment which is commercially a substantial equivalent. If delivery has already been taken, payment by the means or in the manner provided by the regulation discharges the buyer's obligation unless the regulation is discriminatory, oppressive, or predatory.

§ 2-615. Excuse by Failure of Presupposed Conditions.

Except so far as a seller may have assumed a greater obligation and subject to the preceding section on substituted performance:

- (a) Delay in delivery or non-delivery in whole or in part by a seller who complies with paragraphs (b) and (c) is not a breach of his duty under a contract for sale if performance as agreed has been made impracticable by the occurrence of a contingency the non-occurrence of which was a

basic assumption on which the contract was made or by compliance in good faith with any applicable foreign or domestic governmental regulation or order whether or not it later proves to be invalid.

- (b) Where the causes mentioned in paragraph (a) affect only a part of the seller's capacity to perform, he must allocate production and deliveries among his customers but may at his option include regular customers not then under contract as well as his own requirements for further manufacture. He may so allocate in any manner which is fair and reasonable.
- (c) The seller must notify the buyer seasonably that there will be delay or non-delivery and, when allocation is required under paragraph (b), of the estimated quota thus made available for the buyer.

§ 2-616. Procedure on Notice Claiming Excuse.

- (1) Where the buyer receives notification of a material or indefinite delay or an allocation justified under the preceding section he may by written notification to the seller as to any delivery concerned, and where the prospective deficiency substantially impairs the value of the whole contract under the provisions of this Article relating to breach of installment contracts (Section 2-612), then also as to the whole,
 - (a) terminate and thereby discharge any unexpected portion of the contract; or
 - (b) modify the contract by agreeing to take his available quota in substitution.
- (2) If after receipt of such notification from the seller the buyer fails so to modify the contract within a reasonable time not exceeding thirty days the contract lapses with respect to any deliveries affected.
- (3) The provisions of this section may not be negated by agreement except in so far as the seller has assumed a greater obligation under the preceding section.

Part 7 Remedies

§ 2-701. Remedies for Breach of Collateral Contracts Not Impaired.

Remedies for breach of any obligation or promise collateral or ancillary to a contract for sale are not impaired by the provisions of this Article.

§ 2-702. Seller's Remedies on Discovery of Buyer's Insolvency.

- (1) Where the seller discovers the buyer to be insolvent he may refuse delivery except for cash including payment for all goods theretofore delivered under the contract, and stop delivery under this Article (Section 2-705).
- (2) Where the seller discovers that the buyer has received goods on credit while insolvent he may reclaim the goods upon demand made within ten days after the receipt, but if misrepresentation of solvency has been made to the particular seller in writing within three months before

delivery the ten day limitation does not apply. Except as provided in this subsection the seller may not base a right to reclaim goods on the buyer's fraudulent or innocent misrepresentation of solvency or of intent to pay.

- (3) The seller's right to reclaim under subsection (2) is subject to the rights of a buyer in ordinary course or other good faith purchaser under this Article (Section 2-403). Successful reclamation of goods excludes all other remedies with respect to them.

As amended in 1966.

§ 2-703. Seller's Remedies in General.

Where the buyer wrongfully rejects or revokes acceptance of goods or fails to make a payment due on or before delivery or repudiates with respect to a part or the whole, then with respect to any goods directly affected and, if the breach is of the whole contract (Section 2-612), then also with respect to the whole undelivered balance, the aggrieved seller may

- (a) stop delivery of such goods;
- (b) stop delivery by any bailee as hereafter provided (Section 2-705);
- (c) proceed under the next section respecting goods still unidentified to the contract;
- (d) resell and recover damages as hereafter provided (Section 2-706);
- (e) recover damages for non-acceptance (Section 2-708) or in a proper case the price (Section 2-709);
- (f) cancel.

§ 2-704. Seller's Right to Identify Goods to the Contract Notwithstanding Breach or to Salvage Unfinished Goods.

- (1) An aggrieved seller under the preceding section may
 - (a) identify to the contract conforming goods not already identified if at the time he learned of the breach they are in his possession or control;
 - (b) treat as the subject of resale goods which have demonstrably been intended for the particular contract even though those goods are unfinished.
- (2) Where the goods are unfinished an aggrieved seller may in the exercise of reasonable commercial judgment for the purposes of avoiding loss and of effective realization either complete the manufacture and wholly identify the goods to the contract or cease manufacture and resell for scrap or salvage value or proceed in any other reasonable manner.

§ 2-705. Seller's Stoppage of Delivery in Transit or Otherwise.

- (1) The seller may stop delivery of goods in the possession of a carrier or other bailee when he discovers the buyer to be insolvent (Section 2-702) and may stop delivery of carload, truckload, planeload or larger shipments of express or freight when the buyer repudiates or fails to make a payment due before delivery or if for any other reason the seller has a right to withhold or reclaim the goods.

- (2) As against such buyer the seller may stop delivery until
 - (a) receipt of the goods by the buyer; or
 - (b) acknowledgment to the buyer by any bailee of the goods except a carrier that the bailee holds the goods for the buyer; or
 - (c) such acknowledgment to the buyer by a carrier by reshipment or as warehouseman; or
 - (d) negotiation to the buyer of any negotiable document of title covering the goods.
- (3)
 - (a) To stop delivery the seller must so notify as to enable the bailee by reasonable diligence to prevent delivery of the goods.
 - (b) After such notification the bailee must hold and deliver the goods according to the directions of the seller but the seller is liable to the bailee for any ensuing charges or damages.
 - (c) If a negotiable document of title has been issued for goods the bailee is not obliged to obey a notification to stop until surrender of the document.
 - (d) A carrier who has issued a non-negotiable bill of lading is not obliged to obey a notification to stop received from a person other than the consignor.

§ 2-706. Seller's Resale Including Contract for Resale.

- (1) Under the conditions stated in Section 2-703 on seller's remedies, the seller may resell the goods concerned or the undelivered balance thereof. Where the resale is made in good faith and in a commercially reasonable manner the seller may recover the difference between the resale price and the contract price together with any incidental damages allowed under the provisions of this Article (Section 2-710), but less expenses saved in consequence of the buyer's breach.
- (2) Except as otherwise provided in subsection (3) or unless otherwise agreed resale may be at public or private sale including sale by way of one or more contracts to sell or of identification to an existing contract of the seller. Sale may be as a unit or in parcels and at any time and place and on any terms but every aspect of the sale including the method, manner, time, place and terms must be commercially reasonable. The resale must be reasonably identified as referring to the broken contract, but it is not necessary that the goods be in existence or that any or all of them have been identified to the contract before the breach.
- (3) Where the resale is at private sale the seller must give the buyer reasonable notification of his intention to resell.
- (4) Where the resale is at public sale
 - (a) only identified goods can be sold except where there is a recognized market for a public sale of futures in goods of the kind; and
 - (b) it must be made at a usual place or market for public sale if one is reasonably available and except in the case of goods which are perishable or threaten to decline in value speedily the seller must give the buyer reasonable notice of the time and place of the resale; and

- (c) if the goods are not to be within the view of those attending the sale the notification of sale must state the place where the goods are located and provide for their reasonable inspection by prospective bidders; and
- (d) the seller may buy.
- (5) A purchaser who buys in good faith at a resale takes the goods free of any rights of the original buyer even though the seller fails to comply with one or more of the requirements of this section.
- (6) The seller is not accountable to the buyer for any profit made on any resale. A person in the position of a seller (Section 2-707) or a buyer who has rightfully rejected or justifiably revoked acceptance must account for any excess over the amount of his security interest, as hereinafter defined (subsection (3) of Section 2-711).

§ 2-707. “Person in the Position of a Seller”.

- (1) A “person in the position of a seller” includes as against a principal an agent who has paid or become responsible for the price of goods on behalf of his principal or anyone who otherwise holds a security interest or other right in goods similar to that of a seller.
- (2) A person in the position of a seller may as provided in this Article withhold or stop delivery (Section 2-705) and resell (Section 2-706) and recover incidental damages (Section 2-710).

§ 2-708. Seller’s Damages for Non-acceptance or Repudiation.

- (1) Subject to subsection (2) and to the provisions of this Article with respect to proof of market price (Section 2-723), the measure of damages for non-acceptance or repudiation by the buyer is the difference between the market price at the time and place for tender and the unpaid contract price together with any incidental damages provided in this Article (Section 2-710), but less expenses saved in consequence of the buyer’s breach.
- (2) If the measure of damages provided in subsection (1) is inadequate to put the seller in as good a position as performance would have done then the measure of damages is the profit (including reasonable overhead) which the seller would have made from full performance by the buyer, together with any incidental damages provided in this Article (Section 2-710), due allowance for costs reasonably incurred and due credit for payments or proceeds of resale.

§ 2-709. Action for the Price.

- (1) When the buyer fails to pay the price as it becomes due the seller may recover, together with any incidental damages under the next section, the price
 - (a) of goods accepted or of conforming goods lost or damaged within a commercially reasonable time after risk of their loss has passed to the buyer; and
 - (b) of goods identified to the contract if the seller is unable after reasonable effort to resell them at a reasonable price or the circumstances reasonably indicate that such effort will be unavailing.

- (2) Where the seller sues for the price he must hold for the buyer any goods which have been identified to the contract and are still in his control except that if resale becomes possible he may resell them at any time prior to the collection of the judgment. The net proceeds of any such resale must be credited to the buyer and payment of the judgment entitles him to any goods not resold.
- (3) After the buyer has wrongfully rejected or revoked acceptance of the goods or has failed to make a payment due or has repudiated (Section 2-610), a seller who is held not entitled to the price under this section shall nevertheless be awarded damages for non-acceptance under the preceding section.

§ 2-710. Seller's Incidental Damages.

Incidental damages to an aggrieved seller include any commercially reasonable charges, expenses or commissions incurred in stopping delivery, in the transportation, care and custody of goods after the buyer's breach, in connection with return or resale of the goods or otherwise resulting from the breach.

§ 2-711. Buyer's Remedies in General; Buyer's Security Interest in Rejected Goods.

- (1) Where the seller fails to make delivery or repudiates or the buyer rightfully rejects or justifiably revokes acceptance then with respect to any goods involved, and with respect to the whole if the breach goes to the whole contract (Section 2-612), the buyer may cancel and whether or not he has done so may in addition to recovering so much of the price as has been paid
 - (a) "cover" and have damages under the next section as to all the goods affected whether or not they have been identified to the contract; or
 - (b) recover damages for non-delivery as provided in this Article (Section 2-713).
- (2) Where the seller fails to deliver or repudiates the buyer may also
 - (a) if the goods have been identified recover them as provided in this Article (Section 2-502); or
 - (b) in a proper case obtain specific performance or replevy the goods as provided in this Article (Section 2-716).
- (3) On rightful rejection or justifiable revocation of acceptance a buyer has a security interest in goods in his possession or control for any payments made on their price and any expenses reasonably incurred in their inspection, receipt, transportation, care and custody and may hold such goods and resell them in like manner as an aggrieved seller (Section 2-706).

§ 2-712. "Cover"; Buyer's Procurement of Substitute Goods.

- (1) After a breach within the preceding section the buyer may "cover" by making a good faith and without unreasonable delay any reasonable purchase of or contract to purchase goods in substitution for those due from the seller.

- (2) The buyer may recover from the seller as damages the difference between the cost of cover and the contract price together with any incidental or consequential damages as hereinafter defined (Section 2-715), but less expenses saved in consequence of the seller's breach.
- (3) Failure of the buyer to effect cover within this section does not bar him from any other remedy.

§ 2-713. Buyer's Damages for Non-delivery or Repudiation.

- (1) Subject to the provisions of this Article with respect to proof of market price (Section 2-723), the measure of damages for non-delivery or repudiation by the seller is the difference between the market price at the time when the buyer learned of the breach and the contract price together with any incidental and consequential damages provided in this Article (Section 2-715), but less expenses saved in consequence of the seller's breach.
- (2) Market price is to be determined as of the place for tender or, in cases of rejection after arrival or revocation of acceptance, as of the place of arrival.

§ 2-714. Buyer's Damages for Breach in Regard to Accepted Goods.

- (1) Where the buyer has accepted goods and given notification (subsection (3) of Section 2-607) he may recover as damages for any non-conformity of tender the loss resulting in the ordinary course of events from the seller's breach as determined in any manner which is reasonable.
- (2) The measure of damages for breach of warranty is the difference at the time and place of acceptance between the value of the goods accepted and the value they would have had if they had been as warranted, unless special circumstances show proximate damages of a different amount.
- (3) In a proper case any incidental and consequential damages under the next section may also be recovered.

§ 2-715. Buyer's Incidental and Consequential Damages.

- (1) Incidental damages resulting from the seller's breach include expenses reasonably incurred in inspection, receipt, transportation and care and custody of goods rightfully rejected, any commercially reasonable charges, expenses or commissions in connection with effecting cover and any other reasonable expense incident to the delay or other breach.
- (2) Consequential damages resulting from the seller's breach include:
 - (a) any loss resulting from general or particular requirements and needs of which the seller at the time of contracting had reason to know and which could not reasonably be prevented by cover or otherwise; and
 - (b) injury to person or property proximately resulting from any breach of warranty.

§ 2-716. Buyer's Right to Specific Performance or Replevin.

- (1) Specific performance may be decreed where the goods are unique or in other proper circumstances.

- (2) The decree for specific performance may include such terms and conditions as to payment of the price, damages, or other relief as the court may deem just.
- (3) The buyer has a right of replevin for goods identified to the contract if after reasonable effort he is unable to effect cover for such goods or the circumstances reasonably indicate that such effort will be unavailing or if the goods have been shipped under reservation and satisfaction of the security interest in them has been made or tendered.

§ 2-717. Deduction of Damages from the Price.

The buyer on notifying the seller of his intention to do so may deduct all or any part of the damages resulting from the breach of the contract from any part of the price still due under the same contract.

§ 2-718. Liquidation or Limitation of Damages; Deposits.

- (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.
- (2) Where the seller justifiably withholds delivery of goods because of the buyer's breach, the buyer is entitled to restitution of any amount by which the sum of his payments exceeds
 - (a) the amount to which the seller is entitled by virtue of terms liquidating the seller's damages in accordance with subsection (1), or
 - (b) in the absence of such terms, twenty per cent of the value of the total performance for which the buyer is obligated under the contract or \$500, whichever is smaller.
- (3) The buyer's right to restitution under subsection (2) is subject to offset to the extent that the seller establishes
 - (a) a right to recover damages under the provisions of this Article other than subsection (1), and
 - (b) the amount or value of any benefits received by the buyer directly or indirectly by reason of the contract.
- (4) Where a seller has received payment in goods their reasonable value or the proceeds of their resale shall be treated as payments for the purposes of subsection (2); but if the seller has notice of the buyer's breach before reselling goods received in part performance, his resale is subject to the conditions laid down in this Article on resale by an aggrieved seller (Section 2-706).

§ 2-719. Contractual Modification or Limitation of Remedy.

- (1) Subject to the provisions of subsections (2) and (3) of this section and of the preceding section on liquidation and limitation of damages,
 - (a) the agreement may provide for remedies in addition to or in substitution for those provided in this Article and may limit or alter

the measure of damages recoverable under this Article, as by limiting the buyer's remedies to return of the goods and repayment of the price or to repair and replacement of non-conforming goods or parts; and

(b) resort to a remedy as provided is optional unless the remedy is expressly agreed to be exclusive, in which case it is the sole remedy.

(2) Where circumstances cause an exclusive or limited remedy to fail of its essential purpose, remedy may be had as provided in this Act.

(3) Consequential damages may be limited or excluded unless the limitation or exclusion is unconscionable. Limitation of consequential damages for injury to the person in the case of consumer goods is prima facie unconscionable but limitation of damages where the loss is commercial is not.

§2-720. Effect of “Cancellation” or “Rescission” on Claims for Antecedent Breach.

Unless the contrary intention clearly appears, expressions of “cancellation” or “rescission” of the contract or the like shall not be construed as a renunciation or discharge of any claim in damages for an antecedent breach.

§ 2-721. Remedies for Fraud.

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

§ 2-722. Who Can Sue Third Parties for Injury to Goods.

Where a third party so deals with goods which have been identified to a contract for sale as to cause actionable injury to a party to that contract

(a) a right of action against the third party is in either party to the contract for sale who has title to or a security interest or a special property or an insurable interest in the goods; and if the goods have been destroyed or converted a right of action is also in the party who either bore the risk of loss under the contract for sale or has since the injury assumed that risk as against the other;

(b) if at the time of the injury the party plaintiff did not bear the risk of loss as against the other party to the contract for sale and there is no arrangement between them for disposition of the recovery, his suit or settlement is, subject to his own interest, as a fiduciary for the other party to the contract;

(c) either party may with the consent of the other for the benefit of whom it may concern.

§ 2-723. Proof of Market Price: Time and Place.

(1) If an action based on anticipatory repudiation comes to trial before the time for performance with respect to some or all of the goods, any

damages based on market price (Section 2–708 or Section 2–713) shall be determined according to the price of such goods prevailing at the time when the aggrieved party learned of the repudiation.

- (2) If evidence of a price prevailing at the times and places described in this Article is not readily available the price prevailing within any reasonable time before or after the time described or at any other place which in commercial judgment or under usage of trade would serve as a reasonable substitute for the one described may be used, making any proper allowance for the cost of transporting the goods to or from such other place.
- (3) Evidence of a relevant price prevailing at a time or place other than the one described in this Article offered by one party is not admissible unless and until he has given the other party such notice as the court finds sufficient to prevent unfair surprise.

§ 2–724. Admissibility of Market Quotations.

Whenever the prevailing price or value of any goods regularly bought and sold in any established commodity market is in issue, reports in official publications or trade journals or in newspapers or periodicals of general circulation published as the reports of such market shall be admissible in evidence. The circumstances of the preparation of such a report may be shown to affect its weight but not its admissibility.

§ 2–725. Statute of Limitations in Contracts for Sale.

- (1) An action for breach of any contract for sale must be commenced within four years after the cause of action has accrued. By the original agreement the parties may reduce the period of limitation to not less than one year but may not extend it.
- (2) A cause of action accrues when the breach occurs, regardless of the aggrieved party's lack of knowledge of the breach. A breach of warranty occurs when tender of delivery is made, except that where a warranty explicitly extends to future performance of the goods and discovery of the breach must await the time of such performance the cause of action accrues when the breach is or should have been discovered.
- (3) Where an action commenced within the time limited by subsection (1) is so terminated as to leave available a remedy by another action for the same breach such other action may be commenced after the expiration of the time limited and within six months after the termination of the first action unless the termination resulted from voluntary discontinuance or from dismissal for failure or neglect to prosecute.
- (4) This section does not alter the law on tolling of the statute of limitations nor does it apply to causes of action which have accrued before this Act becomes effective.



Glossary

A

Abrogated An abrogated law has been repealed or nullified by a constitution, the legislature, or through the evolution of case law.

Acceptance An acceptance is the offeree's manifestation of assent to the terms of the offer.

Accord An accord is a contract to pay a stated amount to discharge a prior obligation that is either uncertain as to its existence or amount. Satisfaction (performance) of the accord contract is required before the duties under the original contract are terminated.

Account Stated An account stated is the debtor's and creditor's manifestation of assent to a stated sum as an accurate computation of an amount due the creditor.

Acknowledgment Form The acknowledgment form is the seller's acceptance form.

Action An action is a shorthand phrase for cause of action, that is, the theory upon which relief should be granted.

Actual Knowledge Actual knowledge is valid objective knowledge based upon known facts rather than guesses or theories.

Additional Term When two forms are exchanged, an additional term is a substantive boilerplate term that appears in the second form but not in the first form.

Adhesion Contract An adhesion contract (contract of adhesion) is a contract formed by one party

imposing his or her will upon an unwilling or even unwitting party.

Affirmance Affirmance is the manifestation, by a contracting party who has the power to avoid the contract, of a willingness to continue with the performance of the contract.

Agreement An agreement is the actual bargain of the parties as found in their language, course of dealing, usage of trade, and course of performance. Whether an agreement has legal consequences is determined by the law of contracts.

Ambiguity An ambiguity occurs when a word has two different meanings. The ambiguity may be patent (apparent on its face) or latent (apparent only in light of surrounding circumstances).

Anticipatory Repudiation Anticipatory repudiation is a shorthand phrase for "breach by anticipatory repudiation." It is a party's refusal to perform a contractual duty made prior to the time the performance is due.

Assignee The assignee is the third party (not one of the original contracting parties) to whom a contractual right is transferred.

Assignor The assignor is the promisee in the original contract who transfers his or her contractual right to a third person.

Assignment An assignment is the transfer of a contractual right.

Assumpsit Assumpsit, a common law form of action, was one of the forerunners to the modern

breach of contract and restitution actions. The term “assumpsit” meant an undertaking. Assumpsit was divided into Special Assumpsit and General (common or indebitatus) Assumpsit. An action of Special Assumpsit was brought on an express promise. An action of General Assumpsit was brought on an implied in fact or an implied by law promise.

Auction with Reserve In an auction with reserve, the auctioneer may withdraw the property at any time until he or she announces the completion of the sale. The potential bidders are the offerors.

Auction without Reserve In an auction without reserve, the auctioneer is the offeror and the bidders are the offerees.

Avoidability of Damages Avoidability of damages refers to the losses that occur after a breach of contract that are preventable by the nonbreaching party. A court ordinarily will not compensate an injured party for a loss that he or she could have prevented by an appropriate effort.

B

Bargain A bargain is an agreement between the parties.

Bargained for Terms The bargained for terms in a preprinted form are those terms that are supplied by the party on the form and have not been preprinted.

Beneficiary A beneficiary is the recipient of a contractual promise.

Bilateral Contract A bilateral contract is a contract consisting of a promise by the offeror and a reciprocal promise by the offeree.

Boiler Plate Terms Boiler plate terms are the fixed terms of a form offer or acceptance and are not bargained for. Boiler plate terms may be either substantive terms (warranty, disclaimer, credit, arbitration, risk of loss, choice of law, and choice of forum) or procedural terms (“only my terms shall apply” and “this is not an acceptance unless you agree to all of our terms”).

Breach by Anticipatory Repudiation A breach by anticipatory repudiation is a notice that the promisor will not perform in the future.

Breach by Failure to Perform A breach by failure to perform is the usual breach and arises when the time for the promisor’s performance has come and gone without the promisor performing.

C

Capacity Capacity is the legal ability a party has to contract. Some parties, such as minors and the mentally incapacitated, have only limited capacity and therefore have, under some circumstances, the right to disaffirm their contracts.

Cause of Action A cause of action is the theory upon which relief should be granted. The cause of action should be distinguished from the remedy sought if the cause of action could be maintained. Breach of contract is a cause of action; damages is a remedy for breach of contract.

Certainty Certainty is the requirement that contract terms must be discernible to provide the basis for determining breach and the appropriate remedy.

Choice of Law Choice of law is the determination of which law applies where more than one state is involved in a transaction, where conflicting laws exist within a state, or where federal law may preempt state law.

Cognitive Test The traditional common law test whereby a contracting party may disaffirm a contract if his or her mind was so affected by mental disease or defect as to render him or her wholly and absolutely unable to comprehend and understand the nature of the transaction.

Collateral Illegality Collateral illegality is an illegal act that occurred during the performance of the contract although not contemplated as a part of the performance of the contract when the contract was formed.

Common Law Common law has several meanings. The common law is the body of law and jurisprudential theory that originated and developed in England. Common law, as distinguished from law created by legislative enactment, is derived from custom and usage and from judicial decisions recognizing and enforcing custom and usage.

Compensatory Damages Compensatory damages are intended to compensate the nonbreaching party for not receiving his or her expectation under the contract.

Concealment Concealment is an act intended or known to be likely to keep another party from learning a fact.

Condition A condition is a contingency.

Condition Precedent A condition precedent is a duty creating event. An event external to the contract can be a condition precedent to the performance of a contracting party. An event internal to the contract, such as the performance by one party, can be a condition precedent to the performance by the other.

Condition Subsequent A condition subsequent is a duty terminating event.

Conditional Promise A conditional promise is another name for promise with a condition precedent. The promisee does not have a duty to perform until the event occurs.

Consequential Damages Consequential damages do not flow directly from an act but from the consequences or results of that act. See UCC § 2-715(2) (Buyer's Consequential Damages).

Consideration A contract has two "considerations"—consideration for the promisor's promise and consideration for the promisee's promise or performance. Consideration is the "price" sought by the promisor for his or her promise and the "price" sought by the promisee for his or her promise or performance.

Constructive Contract A constructive contract is not a contract because the transaction lacks the elements of a contract. A court, however, might use this terminology to impose recovery under a restitution cause of action.

Constructive Knowledge Constructive knowledge is inferred or deduced rather than based upon known facts.

Contract A contract is the total legal obligation that results from the parties' agreement. It may consist of an exchange of promises (bilateral contract) or an exchange of a promise for a performance (unilateral contract).

Costs Costs include filing fees, service of process, jury fees, and court officer charges, but not attorney fees.

Counterclaim A counterclaim is a claim the defendant has against the plaintiff that arises out of the same transaction that is the basis for the claim that the plaintiff has against the defendant.

Counteroffer A counteroffer is an offer made by the offeree to the offeror that deals with the subject matter of the original offer but with some variation in terms.

Course of Dealing A course of dealing is a sequence of previous acts and conduct between the contracting parties, which can be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct.

Cover Cover is a substitute performance.

Creditor Beneficiary A creditor beneficiary is a third party beneficiary to a contract who received a right under the contract when it was formed to discharge a prior obligation that the promisee had with the third party beneficiary.

Cure Cure is the correction of performance to meet contract specifications.

D

Damages Damages are compensation awarded by a court to a party who has suffered loss or injury to rights or property.

Deep Pocket Deep pocket is an expression used to designate a party with substantial assets or insurance.

Definite Expression of Acceptance When the offeree responds to the offeror's preprinted form with his or her own preprinted form, the offeree manifests a definite expression of acceptance when the offeree's form accepts the offeror's "bargained for" terms.

Delegatee The delegatee is the third party (not one of the original contracting parties) who is empowered by the delegator to perform the delegator's contractual duty.

Delegation A delegation is the empowering of another by the obligor to perform the obligor's contractual duty.

Delegator The delegator is the promisor in the original contract who delegates his or her duty to a third party.

Detrimental Reliance Detrimental reliance is conduct by a party that was induced by another party making a promise and would result in an injury if compensation is denied.

Different Term When two forms are exchanged, a different term is a substantive boiler plate term that appears in both forms but one is not the mirror image of the other.

Divisible Contract A divisible contract is a contract with separate or installment performances.

Donee Beneficiary A donee beneficiary is a third party beneficiary to a contract who receives a gift under the contract.

Duress Duress is the use of any wrongful act or threat to influence a party to contract. Duress has two forms: duress by actual physical force and duress by threat.

Duress by Actual Physical Force This form of duress occurs when a person using physical force compels a party to assent to the contract, even though that party did not intend to contract.

Duress by Threat This form of duress occurs when a person improperly threatens a party to induce assent to a contract, when the threatened party has no reasonable alternative but to assent. Duress by threat includes “economic duress.”

Duty “Duty” is the correlative of “right.” When one party has a duty, another will have a corresponding right. Duty means that which is owed to a party.

E

Economic Duress A party subjected to economic duress is wrongfully threatened with severe economic loss if he or she does not enter the proposed contract.

Emancipation Emancipation occurs when a court no longer considers the person a minor even though the person’s chronological age would fall within the definition of a minor.

Entire Contract An entire contract is a contract with a single performance.

Estoppel Estoppel is the judicial preclusion of a party’s assertion of a position inconsistent with his or her prior actions or promise.

Excuse Excuse is the term used to indicate that the promisor is exempted by an unforeseen external event from performing under a contract.

Executory Contract An executory contract is one that has not been fully performed by both parties.

Expectation Damages Expectation damages places the nonbreaching party in the position he or she would have been in had the contract been fully performed.

Expectation Interest Protecting the nonbreaching party’s expectation interest places the nonbreaching party in the position he or she would have been in had the contract been fully performed by both parties according to the contract.

Express Promise An express promise is a promise stated either orally or in writing.

F

Forbearance Forbearance means refraining from taking action.

Forfeiture Forfeiture is the loss of a right.

Forum State The forum state is the state in which the case is filed (the state hearing the case).

Fraud in the Factum Fraud in the factum involves the very character of the proposed contract.

Fraud in the Inducement Fraud in the inducement is a false representation or concealment of fact, that should have been disclosed, that deceives and is intended to deceive another party to the contract.

Frustration of Purpose Frustration of purpose occurs when an unexpected event destroys a party’s underlying reason for contracting. Even though performance of the contract is still possible, courts may excuse nonperformance on the theory of failure of consideration.

G

Gap Filers Those contract terms supplied by Article 2 of the UCC (sale of goods) that supplement the express terms of the contracting parties.

General Damages General damages arise naturally, that is, according to the usual course of events when a contract is breached. General damages are foreseeable.

Good Faith Good faith in the case of a merchant means honesty in fact and the observance of reasonable commercial standards of fair dealing in the trade. In the case of a nonmerchant, good faith means honesty in fact in the conduct or transaction concerned.

Gratuitous Promise (Gift Promise) If a promisor makes a gratuitous promise, the promisor does not seek consideration for his or her promise.

Guarantor A guarantor is a party whose duty is conditioned on the failure of another party’s performance.

H

Horizontal Privity Horizontal privity of contract is the relationship that must be established by a legislature or court before an injured user of

a product, although not contracting with the seller of the product, can successfully sue the seller in a breach of contract action for a breach of warranty.

Hybrid Transaction A contract that is for both the sale of goods and for the sale of services.

I

Illusory Promise An illusory promise is a statement that is less than a commitment to do or refrain from doing something. Therefore, an illusory promise is a misnomer because it is not a promise.

Implied by Law (Implied in Law) Promise The implied by law promise is neither express nor implied in fact. It is a legal fiction, not a promise, which represents the court's label attached to the set of facts to reach a desired result.

Implied in Fact Promise An implied in fact promise is a promise that is inferred from conduct rather than expressed orally or in writing.

Implied Promise An implied promise may be either an implied in fact or implied by law promise. The facts must be evaluated to determine whether the promise can be inferred from conduct or whether the promise is merely a legal fiction.

Impossibility Impossibility results from the occurrence of an unexpected event that renders a party incapable of performing his or her contractual duties.

Impracticability Impracticability results from the occurrence of an unexpected event that renders the performance of a contractual duty extremely difficult or expensive to perform.

Incidental Beneficiary An incidental beneficiary is a third party beneficiary to a contract who is neither a creditor nor a donee beneficiary. An incidental beneficiary receives a windfall if the contract is performed, but has no enforceable rights under the contract if it is not performed.

Incidental Damages Incidental damages are awarded to the nonbreaching party for expenses reasonably incurred as a result of the other contracting party's breach. See UCC § 2-710 (Seller's Incidental Damages) and UCC § 2-715(1) (Buyer's Incidental Damages).

Indefinite Promise An indefinite promise is a statement that appears to be a promise but omits terms essential to enable the courts to determine

an appropriate remedy in the event the "promise" is breached.

Injunction An injunction is a writ issued by a court directing a party to refrain from a specified act.

Insolvent Insolvent may be defined differently depending on the context. A person may be insolvent when he or she has ceased to pay his or her debts in the ordinary course of business; cannot pay his or her debts as they become due; or is insolvent within the meaning of the federal bankruptcy law (the sum of the debts is greater than the fair valuation of all of the debtor's property).

Installment Contract An installment contract is one that requires or authorizes the delivery of goods or services in separate lots or increments to be separately accepted.

Integration An integration is the final written form of a contract.

Intended Beneficiary An intended beneficiary is a third party donee or creditor beneficiary. The Restatement (First) of Contracts uses the terms "donee" and "creditor beneficiary." The Restatement (Second) of Contracts uses the term "intended beneficiary."

Interstate Transaction A transaction spanning several states. Also known as a multistate transaction.

J

Justification A promisor may be justified in not performing his or her contractual duties if the promisor was freed from performing due to a prior breach by the promisee.

K

Knowledge A person "knows" or has "knowledge" of a fact when he or she has actual knowledge of it.

L

Lapse Lapse is the termination of the offer through the offeree's failure to accept it within the time specified in the offer or, if no time is specified, then within a reasonable time.

Last Shot Doctrine A common law doctrine that provides where the acceptance of an express offer is implied from the offeree's performance (e.g.,

acceptance of the shipment and paying), the offeree, by performance, has accepted the offeror's terms.

Latent Ambiguity A latent ambiguity is a miscommunication between the promisor and the promisee and occurs when a term has a double meaning.

Liquidated Damages Liquidated damages are those damages agreed to by the parties at the time of contract formation that will apply to the transaction if a breach occurs.

M

Mailbox Rule The rule of determining when an acceptance sent from a distance is effective. Under the mailbox rule, acceptance is effective when sent.

Manifestation A manifestation is a demonstration that could be readily perceived by a third party.

Manifestation of Assent Manifestation of assent is the modern phrase that refers to the objective theory of contracts law.

Meeting of the Minds Meeting of the minds is an outdated phrase that refers to the subjective theory of contracts law.

Merchant A merchant as used in Article 2 of the UCC is defined in section 2-104 and its comment 2 and may be either a merchant who has specialized knowledge as to the goods, specialized knowledge as to the business practices, or specialized knowledge as to both the goods and the business practices. The business practices are those practices discussed in a specific code section. Therefore, a party may have specialized knowledge as to some business practices but not others or may have specialized knowledge as to the goods but not as to specialized business practices and therefore may be a merchant for one code section but not another.

Minors (Infants) A minor is a person under the legal age. In most states the legal age is eighteen. A minor may be referred to as an infant in older cases and statutes.

Mirror Image Mirror image means that the offeree must accept the offer without changing it.

Misrepresentation A misrepresentation is an assertion that is not in accord with the facts.

Mistake Mistake may take one of five forms: (1) mistake in judgment; (2) mistake in the performance of the contract; (3) mistake in understand-

ing the terms of the contract (mistake misunderstanding); (4) mistake in a basic assumption of fact; and (5) mistake in the integration of the contract.

Mistake in a Basic Assumption of Fact A mistake in a basic assumption of fact involves a situation where the contracting parties believe they were bargaining for something different from what they actually did contract for.

Mistake in Integration A mistake in integration occurs when a party makes a clerical error in writing the terms of the contract.

Mistake in Judgment A mistake in judgment occurs when a party makes an erroneous assessment regarding how beneficial the contract will be.

Mistake in the Performance of the Contract A mistake in the performance of the contract occurs when a party makes an error by overperforming his or her contractual duty. The overperformance may include an overpayment.

Mistake: Misunderstanding A mistake in understanding the terms of a contract occurs when, at the time of contract formation, both contracting parties use the same manifestations, but the parties do not attach the same meaning to these manifestations.

Mistake of Fact A mistake of fact is a belief that is not in accordance with the facts.

Mistake of Law A mistake of law is a belief that is not in accordance with the law.

Mitigation Mitigation requires the nonbreaching party to use reasonable means to avoid or minimize damages.

Modification Under classical contract theory, modification of a contract is itself a contract and must follow the same rules of contract formation required for the original contract.

Motion in Limine Motion in limine is a preliminary request to limit evidence or testimony as specified by agreement of the parties or by order of the court.

Mutual Mistake of Fact Mutual mistake of fact occurs when the parties to a contract have a common intention but the writing does not reflect that intention due to their misconception of the facts.

Mutual Releases Mutual releases will terminate the parties' duties to perform their contractual duties.

N

Necessaries Necessaries are those articles that the minor actually needs and must supply for himself or herself because the person who has the duty to provide these articles either cannot or will not provide them.

No Breach, Compliance The defendant responds to the plaintiff's allegation of breach—"I am complying with the terms of the contract."

No Breach, Excuse The defendant responds to the plaintiff's allegation of breach—"Although I am not complying with the terms of the contract, my nonperformance was excused, and therefore I have not breached the contract."

No Breach, Justification The defendant responds to the plaintiff's allegation of breach—"Although I am not complying with the terms of the contract, my nonperformance was justified by your breach of this contract, and therefore I have not breached the contract."

No Breach, Terminated Duty The defendant responds to the plaintiff's allegation of breach—"Although I am not complying with the terms of the contract, my duty to perform the contract has been terminated, and therefore I have not breached the contract."

Nominal Damages Nominal damages are a token award to the nonbreaching party, given more for clarification of the rights and duties of the parties than for actual monetary compensation. Court costs may be included.

Nondisclosure A nondisclosure occurs when one party withholds information from another.

Notice A person has "notice" of a fact when he or she has actual knowledge of a fact, has received a notice or notification of a fact, or, in light of all the facts and circumstances known to him or her at the time in question, has reason to know that a fact exists.

Novation A novation is a contract that discharges a party to the contract, sometimes an obligor and sometimes an obligee, and substitutes a new party in his or her place.

O

Objective Standard The objective standard is the reasonable person's standard. It is based on manifestations that could be reasonably inter-

preted by hypothetical third persons watching the transaction.

Obligee The obligee (promisee) is the contracting party with the contractual right to whom is owed the contractual duty.

Obligor The obligor (promisor) is the contracting party who owes the contractual duty associated with the contractual right.

Offer An offer is a manifestation of willingness to enter into a bargain, which justifies another person in understanding that his or her assent to that bargain is invited and will conclude it.

Offer for a Bilateral Contract In an offer for a bilateral contract, the offeror makes a promise to entice the offeree to make a promise (a promise for a promise).

Offer for a Unilateral Contract In an offer for a unilateral contract, the offeror makes a promise to entice the offeree to perform (a promise for a performance).

Offeree An offeree is the person whom the offeror invites to accept the offer.

Offeror An offeror is the person who extends the offer to the offeree.

Officious Officious means to act in a meddling manner, interfering in the affairs of another by conferring an unnecessary or unwanted benefit.

Offset An offset is a deduction of the amount awarded to the defendant from the amount awarded to the plaintiff.

Option Contract An option contract is a contract that negates the promisor's power to revoke the offer. An option contract has the same requirements as the main contract—promisor's promise, consideration for the promisor's promise, promisee's promise or performance, and consideration for the promisee's promise or performance.

P

Pari Delicto *Pari delicto* means equal fault. When parties are not *in pari delicto*, they do not share fault equally.

Parol Evidence Rule The parol evidence rule is a substantive rule of contracts law that limits the terms of a contract in final written form to those in the writing. Prior or contemporaneous parol evidence cannot be used to add to or contradict terms in the final writing. Parol evidence,

however, can be used to interpret terms in the final writing.

Parol Terms Parol terms are terms that are oral or, if written, are not in the final writing.

Partial Integration A partial integration is a contract that has only some of its terms in final written form.

Party Autonomy Rule The court deference to the parties' own choice of applicable law.

Patent Ambiguity A contract term suffers from a patent ambiguity when the ambiguity is apparent from the face of the writing.

Performance Performance must be distinguished from promise. A performance is an act or omission (doing or not doing something). A promise is the unequivocal assurance that something will or will not be done.

Person A person includes an individual and an organization. See UCC § 1-201(30).

Plain Meaning Plain meaning is the meaning that reasonable people would give to a word or phrase.

Posting Rule The rule of determining when an acceptance sent from a distance is effective. Under the posting rule, acceptance is effective when sent.

Predominant Factor Test The test used to resolve whether a hybrid transaction should be treated under Article 2 of the UCC (sale of goods) or under the common law (sale of a service).

Preemption Doctrine Under the federal preemption doctrine, state law must give way to federal law when federal law either expressly regulates the matter or when a particular subject is regarded as being beyond the bounds of state action.

Preliminary Negotiation Preliminary negotiations include all discussions of the parties that occur prior to the offer.

Privity Privity of contract is a relationship that must exist before a party can successfully maintain a breach of contract action. See **Horizontal Privity** and **Vertical Privity**.

Promise A promise is a manifestation of intention to act or refrain from acting in a specified way, which justifies a promisee's understanding that the promisor has made a commitment. A promise is an unequivocal assurance that something will or will not be done.

Promisee A promisee is the person to whom a promise is made.

Promisor A promisor is the person who makes the promise.

Promissory Estoppel Promissory estoppel is the preclusion of an assertion by the promisor that is inconsistent with a previously made promise upon which the promisee has relied.

Puffing Puffing is an expression of opinion by a seller not intended as a representation of fact.

Punitive Damages Monetary awards that are above and beyond compensation for injury and that would punish the breaching party.

Purchase Order The purchase order is the buyer's offer form.

Q

Quantum Meruit Quantum meruit is a common count (a standard allegation) in an action of assumpsit for work and labor. It is based on an implied assumpsit or promise on the part of the defendant to pay the plaintiff as much as is reasonably deserved for his or her labor.

Quasi Contract A quasi contract is an implied by law or constructive contract. A quasi contract is not a contract but is a restitution cause of action based on unjust enrichment.

R

Ratification Ratification is the confirmation (affirmation) of the contract.

Reasonable Person Standard (Reasonable Man Standard) The reasonable person standard is an objective rather than a subjective standard. The inquiry is how a reasonable person, having observed the transaction, perceived the transaction. The inquiry is not whether the parties mentally viewed the transaction in a common fashion. For example, if the parties dispute whether an offer was made, the legal conclusion will be that an offer was made if a reasonable person would conclude from the disputants' manifestations that an offer was made. The reasonable person standard is used in modern contracts law.

Reformation Reformation is a judicial remedy designed to revise a writing to conform to the real agreement or intention of the parties.

Rejection Rejection is the offeree's manifestation of nonacceptance of the offer.

Release A release is the relinquishment of a right.

Reliance Damages Reliance damages places the nonbreaching party back to the position he or she was in prior to relying on the breaching party's promise.

Remedy A remedy is the relief sought if a cause of action can be maintained.

Renunciation A renunciation is the abandonment of a right.

Repentance Repentance is a feeling of remorse or regret concerning one's actions.

Repudiation Repudiation is the refusal to accept a right or to perform a duty.

Rescission A rescission is the abrogation of a contract. Rescission usually involves returning the parties to their pre-contract positions.

Restatements of the Law The Restatements are an attempt by the American Law Institute (ALI) to codify the common law of the various states into black letter law with commentary and examples. At times, the Restatements go beyond the common law and present the ALI's view of what the law should be.

Restitution Restitution may be either a cause of action (the basis of a claim) or a remedy (the relief sought) for a breach of contract or restitution cause of action. Both forms of restitution are based on unjust enrichment.

Restitution Damages Restitution damages places the breaching party back to the position he or she was in prior to the time the breaching party received the benefit conferred upon him or her by the nonbreaching party. The measure of damages is the reasonable value of the benefit conferred to the breaching party.

Revocation Revocation is the offeror's manifestation to withdraw the offer.

Right "Right" is the correlative of "duty." When one party has a right, another will have a corresponding duty. Right means that which is due a party.

S

Satisfaction Satisfaction is the performance of the accord contract. Once the accord contract has been performed, the original contractual duties are terminated.

Seal An emblem or symbol affixed to a document to authenticate a signature.

Seasonable Expression of Acceptance When preprinted forms are exchanged, a seasonable expression of acceptance refers to the fact that the second form must have been sent within a reasonable time after receiving the first form.

Setoff Setoff is a claim the defendant has against the plaintiff that arises independent of the claim the plaintiff has against the defendant.

Sham Consideration Sham consideration is feigned or pretended consideration.

Signature A signature is any symbol made by a party with a present intention to authenticate the writing as that of the signer.

Special Damages Special damages do not naturally arise from a breach of contract. They are not within the usual course of events when a contract is breached. Special damages become foreseeable when they may reasonably be supposed to have been in the contemplation of both parties at the time of contract formation as the probable result of the breach.

Specific Performance Specific performance is a remedy whereby a court directs a party to do a specified act.

Statute of Frauds The Statute of Frauds is a statute forbidding enforcement of certain types of contracts unless they are in writing. Under the Statute of Frauds, for example, a contract for the sale of goods for the price of \$500 or more and a contract that cannot be fully performed within one year from the time of its formation must be in writing.

Statute of Limitations A Statute of Limitations provides for a specified period of time within which a cause of action must be brought.

Subjective Standard The subjective standard refers to a party's thinking or mental state rather than manifestations. The subjective standard is commonly referred to as the meeting of the minds.

Substitute Contract A contract between the original contracting parties that replaces the original contract.

Supervening External Event A supervening external event is an event that occurs after contract formation and before full performance of the contract.

Surety A surety is one who, by contract, is liable for the obligations of another.

T

Third Party Beneficiary A third party beneficiary is a party who will be benefited by the performance of a contract. A third party beneficiary may be a donee, creditor, or incidental beneficiary. An incidental beneficiary has no enforceable rights under the contract.

Third Party Beneficiary Contract A third party beneficiary contract is a contract for the benefit of a third party. This party is neither the offeror nor offeree.

Total Integration A contract is totally integrated if all of the contractual terms are in final written form.

Trade Usage Trade usage gives a word or phrase the meaning of the trade that is different from its plain meaning.

U

Unconscionable A contract or contract term is unconscionable if, at the time of contract formation, one party imposed an unreasonably favorable contract or term on the other party who lacked a meaningful choice.

Undue Influence Undue influence involves unfair persuasion by a party who is either in a position of dominance or in a position of trust and confidence. Undue influence requires neither threats nor deception, although one or the other is often present.

Unenforceable Contract An unenforceable contract is a contract that the court will not implement.

Uniform Commercial Code A comprehensive compilation of rules drafted by the American Law Institute and the National Conference of Commissioners on Uniform State Laws that includes a number of topics including sale of goods and which becomes the law of a given state upon enactment by that state's legislature and signature of the governor.

Unilateral Contract A unilateral contract is a contract consisting of a promise by the offeror and a reciprocal performance by the offeree.

Unjust Enrichment Unjust enrichment is the underlying theory for a restitution remedy for breach of contract or a restitution cause of action. Unjust enrichment occurs when the plaintiff has conferred a benefit on the defendant and it would be unfair to permit the defendant to retain the benefit without compensating the plaintiff.

Usage Usage is a habitual or customary practice.

V

Vagueness A term suffers from vagueness if it lacks a precise meaning.

Vertical Privity Vertical privity of contract is the relationship that must be established by a legislature or a court before an injured purchaser of a product can successfully sue a remote seller in a breach of contract action for a breach of warranty. The remote seller did not contract directly with the injured purchaser, but one or more intermediate sellers were involved in the distribution of the product.

Void Contract A void contract is an agreement that has no legal effect as a contract.

Voidable Contract A voidable contract is a contract in which one or both parties have the power to avoid the legal relationship created by the contract or to ratify the contract and thus extinguish the power of avoidance.

Volitional Test The more modern test which supplements the cognitive test so a person may disaffirm a contract when due to mental disease or defect, he or she is unable to act in a reasonable manner and the other party had reasons to know of the mental disease or defect.

W

Waiver Waiver is the intentional or voluntary relinquishment of a right.




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