Class 1: What Are Contracts?

Professor James Toomey

Restatement (Second) § 1

- “A contract is a promise or a set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty”

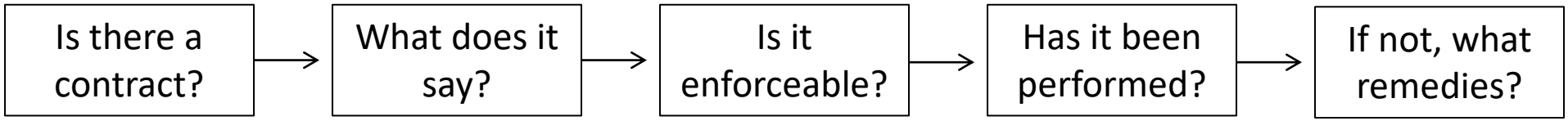
Where Does Contract Law Come From?

- State judge-made law (the "common law")
- The "Restatements"—not binding, but highly persuasive
  - Supposed to be a summary of common law
  - Sometimes self-consciously depart from traditional principles
- The Uniform Commercial Code—roughly identical state statutes governing sale of ***goods***

How To Read For This Course

- Read the textbook—including introductory materials and notes after cases
  - ***Google*** and make note of relevant provisions of the Restatement or UCC (where discussed in the book)
  - You can get a supplement containing these provisions if you want—but they are freely available online

The Story of a Contract—Organization of the Course



- Course tip—as you are reading cases, think about where they fit in this "story" or "lifecycle"
  - e.g.—*Hawkins v. McGee* is about both (1) whether there is a contract; and (2) what remedies

Hawkins v. McGee

- Dr. McGee promises to fix scarring on Hawkins's hand by grafting skin from his chest. He says:
  - "Three or four days, not over four; then the boy can go home and it will be just a few days when he will go back to work with a good hand." (in response to how long Hawkins will be in hospital)
  - "I will guarantee to make the hand a hundred per cent perfect hand or a hundred percent good hand."
  - Repeatedly solicits the father for the operation, because he wants to experiment.
- After operation, hand grows hair.
- Two questions:
  - Is there a contract here? [Trial court says yes]
  - If so, how should the court "measure damages"? (i.e., how should the contract *be enforced*?) [Trial court says—(1) pain and suffering due to operation, (2) negative effects of operation on hand]

Hawkins v. McGee—Is There a Contract?

- Held—yes.
  - Doctor made a promise *in exchange for* the father's consent—he got what he wanted only by promising a 100% good hand
    - Promise was *material* to Hawkins's behavior
    - Doctor repeatedly solicited the consent
  - Court admits that many of the doctor's statements taken alone (particularly about how long Hawkins would be in the hospital) would not be a contract

Hawkins v. McGee—What Damages?

- Held—"expectation damages"
  - "put the plaintiff in as good a position *as he would be in had the defendant kept his contract*"
  - Standard damages in breach of contract—payment of money as expectation damages from defendant to plaintiff
  - How to measure?
    - The "difference between the value to him of a perfect or a good hand, such as the jury found the defendant promised him, and the value of this hand in its present condition, including any incidental consequences fairly within the contemplation of the parties when they made their contract."
    - Why not pain and suffering?
      - These would have happened if operation had gone well—plaintiff "bargained" for it
    - Why not change for the worse?
      - Promise was to make the hand *better*

Hawkins v. McGee—Takeaways

- "Bargain" in contract law—a fundamental concept to which we'll return
  - Contracts are not *just* promises—they're bargains in which two parties each give up something to get something
- Expectation damages as the standard contract remedy
  - Typically, this is what we mean when we say the law "enforces" contracts

Sullivan v. O'Connor

- Similar facts to *Hawkins*—Dr. O'Connor promises Sullivan to make her nose smaller. Surgeries do not work.
  - Three operations—at this point further surgery will not help
- Question—what measure of damages?

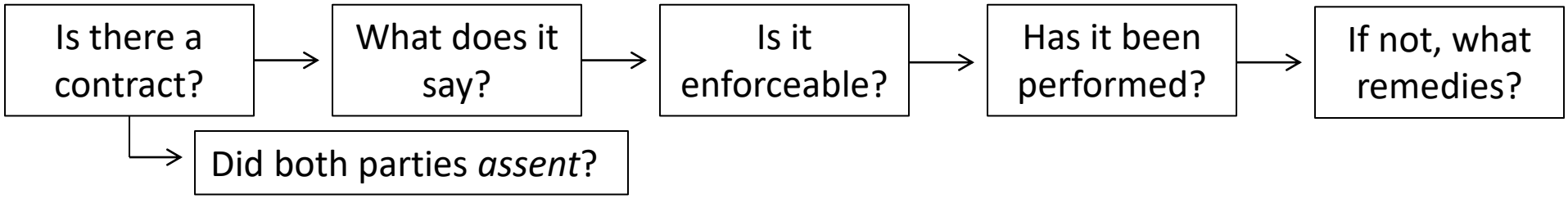
Sullivan v. O'Connor

- Held—*reliance* damages
  - Out of pocket expenses + damages flowing "directly, naturally, proximately, and foreseeably" from defendant's breach
  - Why not expectation damages? [disagreeing with *Hawkins v. McGee*]
    - Excessive, in a dubious class of contracts in the first place.
    - Doctor hasn't been negligent or committed malpractice.
    - Worried about turning everything doctors say into contracts with high and difficult-to-measure damages
  - Why not just give plaintiff her money back? ("*restitution*")
    - "Plainly too meager"

Sullivan v. O'Connor—Takeaways

- Two big alternative ways of measuring damages ("enforcing contracts"):
  - *Reliance*—damages incurred by plaintiff in relying on defendant's promises.
    - "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."
  - *Restitution*—return value that the defendant unfairly gained.
    - Money back—doctor keeping purchase price is unfair

The Story of a Contract



Restatement (Second) § 18. ***Manifestation of Mutual Assent***.

Manifestation of mutual assent to an exchange requires that each party make a promise or render a performance.

Lucy v. Zehmer

- Zehmers and Lucy are at a bar, talking about selling Zehmers' farm to Lucy for $50,000.
  - They discuss for 40 mins, draft a contract of sale, go through a couple of drafts, both Zehmers sign contract.
- A few days later, Lucy follows up and Zehmers say they were joking. "High as a Georgia pine."
- Was there a contract?
  - (Can Zehmer get out on the ground that he was joking, and never "agreed" to sell the farm?)

Lucy v. Zehmer

- Held—yes there's a contract; no, "joking" not a defense where no objective indication
  - "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 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."
- Doesn't matter even if Zehmer *actually was* joking at the time

Lucy v. Zehmer—Takeaways

- Contracts are consensual—require mutual assent
- Longstanding theoretical and legal debate about whether to measure assent *subjectively* (whether parties *actually internally agreed*) or *objectively* (whether someone would be reasonably understood to have agreed, externally)
  - *Lucy* stands for the majority view that law measures assent *objectively*

Specht v. Netscape Comms. Corp.

- Arbitration clause purportedly in terms of service for SmartDownload, but very hard to find.
  - SmartDownload often packaged with Communicator. If downloaded together, there's a terms of service for Communicator only, which says nothing about SmartDownload.
  - You *could* find SmartDownload terms of service if you scrolled to the bottom of the page and clicked through a series of links.
- Plaintiffs are alleging problems with SmartDownload. Question—is there an arbitration clause in SmartDownload license?
  - Did the plaintiffs "assent" to arbitrate issues with SmartDownload?

Specht v. Netscape Comms. Corp.

- Held—no arbitration clause; no mutual assent
  - "It is true that a party cannot avoid the terms of a contract on the ground that he or she failed to read it before signing."
  - Exception—"when the writing does not appear to be a contract and the terms are not called to the attention of the recipient"
  - Would a reasonably prudent person have known of the existence of the arbitration clause?

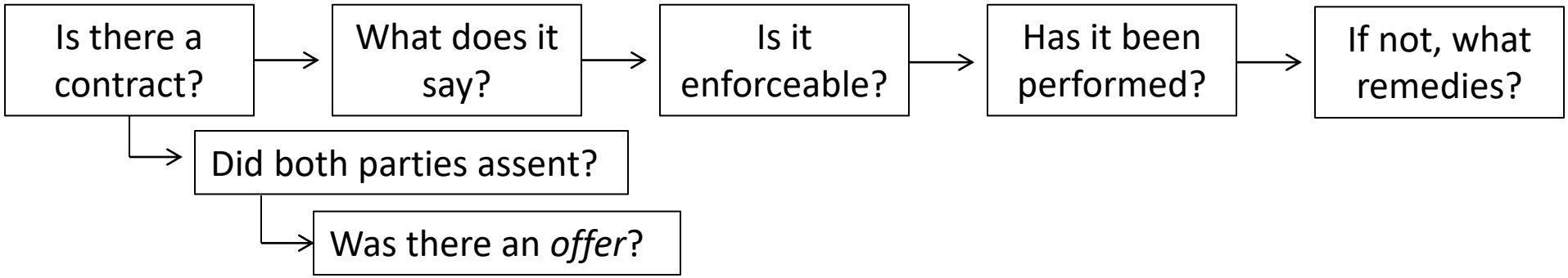
Specht v. Netscape Comms. Corp.— Takeaways

- Objective assent means that people generally held to terms of contracts they've signed/purportedly agreed to, even if they haven't read
- But it needs to objectively look like they agreed to it
  - Would a reasonably prudent person have actually seen and agreed to it?

Class 2: The Offer

Professor James Toomey

The Story of a Contract



Restatement (Second) § 24. ***Offer Defined.***

An offer is 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.

Some Generalizations About Offers

- An offer must, explicitly or implicitly:
  - be communicated to the offeree
  - be directed at a particular individual or specified group of persons
  - indicate a desire to enter into a contract with the offeree, specifying terms of the contract
  - invite acceptance (clarifying how it is to be accepted)
  - create the reasonable understanding that once the offer is accepted, the contract will be final and binding

Some Distinctions

- Offer vs. “invitation to bargain” (*Owen v. Tunison*)
- Offer vs. “quote” (*Fairmount v. Crunden-Martin*)
- Offer vs. “advertisement” (*Lefkowitz v. Great Minneapolis Surplus Store*)

Owen v. Tunison

- W.H. Owen asks R.H. Tunison if he would be willing to sell his store for $6,000
  - Tunison responds: “Because of improvements which have been added and an expenditure of several thousand dollars it would not be possible for me to sell it unless I was to receive $16,000 cash.”
  - Owen responds: “I accept your offer.”
- Was what Tunison said an offer?

Owen v. Tunison

- Held—no offer; no contract.
  - "May have been written with the intent to open negotiations that might lead to a sale" but was not "a proposal to sell"
  - Tunison's was an *invitation to bargain*

Owen v. Tunison—Takeaways

- Distinction between *offers* and *invitations to bargan*. Offers:
  - Indicate a desire to enter into a contract
  - Invite acceptance
  - And create a reasonable understanding that once the offer is accepted, the contract will be final and binding
- "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"

Fairmount Glass Works v. Crunden-Martin Woodenware Co.

- Crunden-Martin to Fairmount:
  - "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 . . . . State terms and cash discount."
- Fairmount to Crunden-Martin:
  - "We quote you Mason fruit jars, complete, in one-dozen boxes [at various prices] for immediate acceptance, [delivery specifications]"
- Crunden-Martin orders 10 car loads
- Fairmount says "Impossible to book the order. Output all sold."
- Was Fairmount's "quote" an offer that could immediately be accepted?

Fairmount Glass Works v. Crunden-Martin Woodenware Co.

- Held—yes; there was an offer, and there was a contract.
  - Distinction between *quotes* and *offers*
    - Quotes not generally offers
  - But this was *more* than a quote—"for immediate acceptance"
    - Context suggests Crunden-Martin reasonably believed it was soliciting a final offer of prices

Fairmount Glass Works v. Crunden-Martin Woodenware Co.—Takeaways

- Distinction between quotes and offers
  - Quotes generally are an invitation to bargain
  - But if specifically invites immediate acceptance, can become an offer

Lefkowitz v. Great Minneapolis Surplus Store

- Department store publishes two ads
  - "Saturday 9am sharp 3 brand new fur coats worth to $100.00. First come first served $1 each."
  - "Saturday 9am, 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."
- Man named Lefkovitz is first in line both Saturdays
- But store refuses to sell, saying there is a "house rule" that the offers are intended only for women
- Three questions:
  - Are the ads offers at all?
  - If so, can the department store apply its "house rule"?
  - If not, can Lefkowitz recover for both ads or just one? (lower court said that the value of the coats is too vague)

Lefkowitz v. Great Minneapolis Surplus Store

- Held—
  - Offers? Yes.
    - Distinction between *offers* and *advertisements*
      - Advertisements generally not offers
      - But "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"
  - House rule? No.
    - Offerors define the terms and conditions of offers and can restrict who can accept them
    - But offerors cannot "impose new or arbitrary conditions not contained in the published offer" *after* acceptance
  - Coats? No.
    - "worth to $100" too vague to assess damages

Lefkowitz v. Great Minneapolis Surplus Store—Takeaways

- Distinction between *advertisements* and *offers*
  - Advertisements not offers *unless* "clear, definite, and explicit, and leaves nothing open for negotiation"
- Conditions of acceptance
  - Offeror sets terms of acceptance and content of offer
  - And can vary the offer *before* acceptance
  - But not *after*

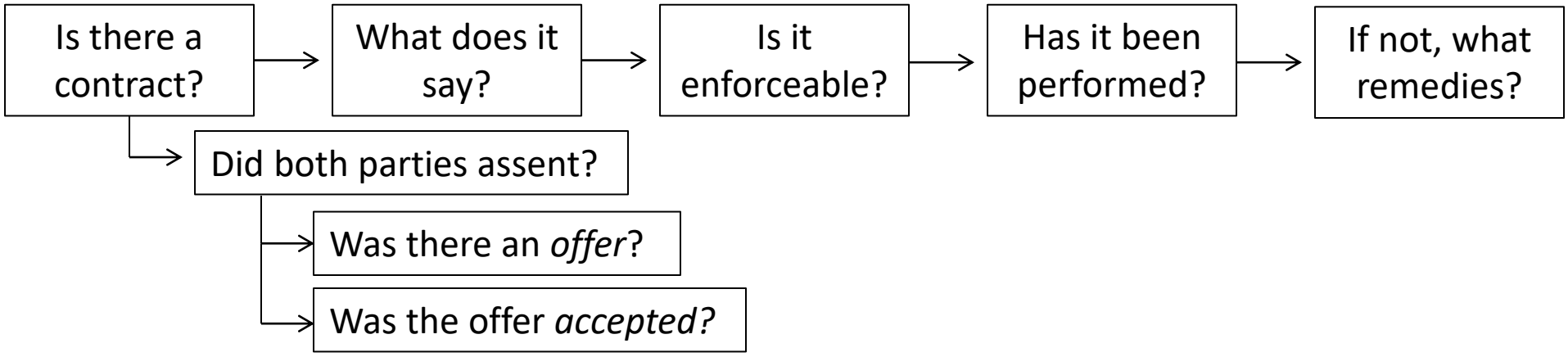
In Summary

- “An offer is 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.” Restatement (Second) § 24.
- Offer must be:
  - Definite and specific
  - Must communicate to the offeree exactly what is being offered
- But does not need words like “I offer”—can be found whenever definite and specific enough and invite performance

Class 3: Acceptance I

Professor James Toomey

The Story of a Contract



Restatement (Second) § 50 (1). ***Acceptance of Offer Defined.***

Acceptance of an offer is a manifestation of assent to the terms thereof made by the offeree in a manner invited or required by the offer.

Wucherpfennig v. Dooley

- Sister sends brother's attorney a letter:
  - "Now if Don [brother] wants to buy my share of real estate, I will sell it to him for $200 an acre, provided it is a cash deal & handled promptly."
- Brother's attorney says brother is interested, but nothing happens for a month
- A month later, attorney responds:
  - "Donald has made arrangements with the Federal Land Bank to secure funds to purchase your interest in the estate farmland and we are therefore ready to proceed with this transaction. Please let me know the exact dollar amount that you expect to receive for your interest in the land. I must know also if you are willing to sign the agreement relating to Special Use Valuation. Please let me hear from you regarding these matters."
- Sister withdraws offer.
- Question—was the attorney's letter an acceptance of the offer?

Wucherpfennig v. Dooley

- Held—no acceptance
  - "The acceptance of an offer must be absolute, unequivocal, and unconditional, and it may not introduce additional terms or conditions."
  - Here, "[t]he terms of the letter appear more in the nature of negotiations with a view toward reaching an agreement in the future."

Wucherpfennig v. Dooley—Takeaways

- At common law—
  - Acceptance must be unconditional
    - The offeror is in charge of the offer—offeror can change offer, offeree cannot
  - "Acceptance" that would vary terms is a counteroffer—common law "mirror image" rule

UCC § 2-207. Additional Terms in Acceptance or Confirmation. (“Battle of the Forms”)

(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 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 the 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 a 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.

International Filter Co. v. Conroe Gin, Ice & Light Co.

- Traveling salesman for International Filter gives Conroe Gin a form:
  - "[T]his proposal is made in duplicate and becomes a contract when accepted by the purchaser and approved by an executive officer of the International Filter Company, at its office in Chicago. Any modification can only be made by duly approved supplementary agreement signed by both parties."
- Conroe Gin writes "accepted" on form. Form goes to International Filter headquarters in Chicago.
  - President of International Filter writes "OK" on it
- International filter mails a separate letter to Conroe Gin thanking them for their order, but not saying anything about the approval by the President.
  - Conroe Gin tries to get out of contract arguing that they were not notified of the President's acceptance of the offer
- Did International Filter have to notify Conroe Gin of its acceptance?

International Filter Co. v. Conroe Gin, Ice & Light Co.

- Held—no.
  - The offeror gets to set the terms of acceptance of the offer.
  - The offer here did not require notification of acceptance.
    - "[T]he offeror said that the contract should be complete if approval be promptly given by the executive officer at Chicago; the court cannot properly restate the offer so as to make the offeror declare that a contract shall be made only when the approval shall have been promptly given at Chicago and that fact shall have been communicated to the offeror at Conroe."
  - Alternative holding—if necessary, the confirmation counts as notice.

International Filter Co. v. Conroe Gin, Ice & Light Co.—Takeaways

- The offeror gets to set the terms of acceptance
- Offer need not require notification of acceptance

White v. Corlies & Tift

- A Business and a Construction Company are in negotiations about fitting up offices.
- Construction Company submits an estimate that the business signs.
- Business sends note to Construction Company reading:
  - "Upon an agreement to finish the fitting up of offices 57 Broadway in two weeks from date, you can begin at once. The writer will call again, probably between 5 and 6 this pm."
- Construction Company doesn't reply but starts buying materials.
- Business wants to change terms, sends follow-up letter. Follow-up letter doesn't arrive for a few days; meanwhile, Construction Company has been preparing for project.
- Was the Construction Company's beginning to work on the project acceptance of an offer?

White v. Corlies & Tift

- Held—no; no acceptance.
  - "Where an offer is made by one party to another when they are not together, the acceptance of it by that other must be manifested by some appropriate act."
    - "A mental determination not indicated by speech, or put in the course of indication by act to the other party, is not an acceptance that will bind the other."
  - Here, Construction Company only bought materials it could have used for any project—no indication of acceptance to Business

White v. Corlies & Tift—Takeaways

- Although notice is not generally required for acceptance, it may be if the offeror has no reasonable way to know of acceptance in a reasonable time
  - Offeree must take some act that "in the usual course of events, in some reasonable time" will notify the offeror of acceptance

Restatement § 54. ***Acceptance by Performance; Necessity of Notification to Offeror***.

(1) Where an offer invites an offeree to accept by rendering performance, no notification is necessary to make such an acceptance effective unless the offer requests such a notification.

(2) If an offeree who accepts by rendering performance has reason to know that the offeror has no adequate means of learning of the performance with reasonable promptness and certainty, the contractual duty of the offeror is discharged unless

   (a) the offeree exercises reasonable diligence to notify the offeror of acceptance, or

   (b) the offeror learns of the performance within a reasonable time, or

   (c) the offer indicates that notification of acceptance is not required.

UCC § 2-206

- "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."

Corinthian Pharmaceutical Systems, Inc. v. Lederle Laboratories

- Lederle has been selling DTP vaccine for $60/vial for years, but is about to raise price to $170.
  - Price lists are not offers, and any price changes "take immediate effect and unfilled current orders and back orders will be invoiced at the price in effect at the time shipment is made"
- Corinthian orders 1000 vials the day before price increase is to go into effect, at then price of $64/vial.
- Lederle ships 50 vials at $64/vial. But includes note:
  - Normal policy is to invoice orders at price at the time of shipment, but "in light of the magnitude of the price increase, Lederle had decided to make an exception to its terms and conditions and ship a portion of the order at the lower price"
- But plans to send the rest of order at the $171/vial price.
- Do Corinthian and Lederle have a contract for the $64/vial price?
  - Did Lederle accept Corinthian's offer to sell at the $64/vial price by shipping 50 vials?

Corinthian Pharmaceutical Systems, Inc. v. Lederle Laboratories

- Held—no acceptance, no contract.
  - UCC § 2-206—"*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*"
  - Was shipment "non-conforming"?
    - Yes, only 50 of 1000 vials
  - Was shipment an accommodation?
    - Yes, because the letter explained they planned to send the rest at the higher price
  - Legal effect?
    - Counteroffer—Corinthian can accept the offer for 950 at $171, or reject, and no further contractual relationships

Corinthian Pharmaceutical Systems, Inc. v. Lederle Laboratories—Takeaways

- UCC § 2-206—shipment of goods counts as acceptance, unless non-conforming goods are an accommodation

Class 4: Acceptance II

Professor James Toomey

Corinthian Pharmaceutical Systems, Inc. v. Lederle Laboratories—Takeaways

- UCC § 2-206—shipment of goods counts as acceptance, unless non-conforming goods are an accommodation

Restatement (Second) § 69. ***Acceptance by Silence or Exercise of Dominion***.

(1) Where an offeree fails to reply to an offer, his silence and inaction operate as an acceptance in the following cases only:
   (a) Where an offeree takes the benefit of offered services with reasonable opportunity to reject them and reason to know that they were offered with the expectation of compensation.
   (b) Where the offeror has stated or given the offeree reason to understand that assent may be manifested by silence or inaction, and the offeree in remaining silent and inactive intends to accept the offer.
   (c) Where because of previous dealings or otherwise, it is reasonable that the offeree should notify the offeror if he does not intend to accept.

Termination of Power of Acceptance

(1) Offeree's rejection (*Wucherpfennig v. Dooley*; mirror image rule; battle of the forms)

(2) Lapse of the offer (Restatement § 41; *Ever-Tite Roofing)*

(3) Death or incapacity of offeror or offeree (Restatement § 48)

(4) Revocation by offeror (*Dickenson v. Dodds*; *Drennan v. Star Paving*; Restatement §§ 42, 43 45, 87; UCC § 2-205)

Restatement § 41. ***Lapse of Time.***

(1) An offeree's power of acceptance is terminated at the time specified in the offer; or, if no time is specified, at the end of a reasonable time.

(2) What is a reasonable time is a question of fact, depending on all the circumstances existing when the offer and attempted acceptance are made.

Ever-Tite Roofing Corporation v. Green

- Greens sign document with Ever-Tite for a new roof.
  - "This agreement shall become binding only upon written acceptance thereof, by the principal or authorized officer of the Contractor, or upon commencing performance of the work."
- Ever-Tite does not commence work immediately, pending credit check.
- The day after the credit approval comes through, Ever-Tite loads their truck and drives to the Greens'
- When they get there, there are already people working on the roof
- Did Ever-Tite successfully accept offer?

Ever-Tite Roofing Corporation v. Green

- Held—Yes, Ever-Tite accepted
  - An offer can specify the time within which acceptance must take place
  - But if it doesn't, the law implies a "reasonable" amount of time
    - Time here was reasonable because both parties knew about the necessity of a credit check
    - And there were no undue delays other than the credit check

Ever-Tite Roofing Corporation v. Green—Takeaways

- Offer can be withdrawn by offeror—but notice of this has to in some way reach the offeree
- Offers lapse after a ***reasonable*** period of time.
  - A fact-dependent inquiry
  - Takes into account what the parties knew would have to happen before acceptance

Restatement §42. ***Revocation by Communication From Offeror Received by Offeree.***

"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."

Restatement §43. ***Indirect Communication of Revocation.***

"An offeree's power of acceptance is terminated when the offeror takes definite action inconsistent with an intention to enter into the proposed contract and the offeree acquires reliable information to that effect."

Dickerson v. Dodds

- John Dodds writes and signs offer to George Dickerson to sell property for 800 pounds. It says:
  - "This offer to be left over until Friday, 9 o'clock a.m. June 12th, 1874"
- Dickerson decides by Thursday evening he wants it but can't get to Dodds until Friday at 7am.
- At which time Dodds tells him he's already sold the property to a third party
- Can Dickerson sue Dodds for breach of contract in not holding the offer open?

Dickerson v. Dodds

- Held—no
  - Offers can be revoked at any time before acceptance
  - Promises to hold offers open are generally unenforceable—unless "consideration" (money or something of value) is paid in exchange for promise

Dickerson v. Dodds—Takeaways

- Common law rules—
  - Offers generally revocable before acceptance—and can be impliedly revoked if the offeree learns of revocation
  - Promises to hold open offer for specified period of time ("option contract") generally unenforceable unless supported by "consideration"

Restatement § 87. ***Option Contract***

(1) An offer is binding as an option contract if it

(a) is in writing and signed by the offeror, recites a purported consideration for the making of the offer, and proposes an exchange on fair terms within a reasonable time; or

(b) is made irrevocable by statute

UCC § 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.

Restatement § 45. ***Option Contract Created by Part Performance of Tender.***

(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.

Drennan v. Star Paving Co.

- General contractor uses the offer of a subcontractor in compiling its bid for a school project, but doesn't accept the offer
- After the bid is submitted subcontractor tells general contract it made a mistake and can't do the job at that price
- Can the subcontractor revoke its bid before acceptance?

Drennan v. Star Paving Co.

- Held—no; offer had to be held open
  - Restatement (First) § 90—"A promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise."
    - Because sub *knew* and *wanted* general to rely on its bid, injustice would result if it could revoke the offer
    - Question is whether the general's reliance was *reasonable*, and what the sub's *expectations* are

Drennan v. Star Paving Co.— Takeaways

- Restatement § 90 can provide another way in which option contracts must be held open.
- Where reliance before acceptance is:
  - Reasonable, and
  - Expected
- This principle is explicitly codified in Restatement (Second) § 87(2)

Restatement § 87. ***Option 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

“Mailbox Rule”

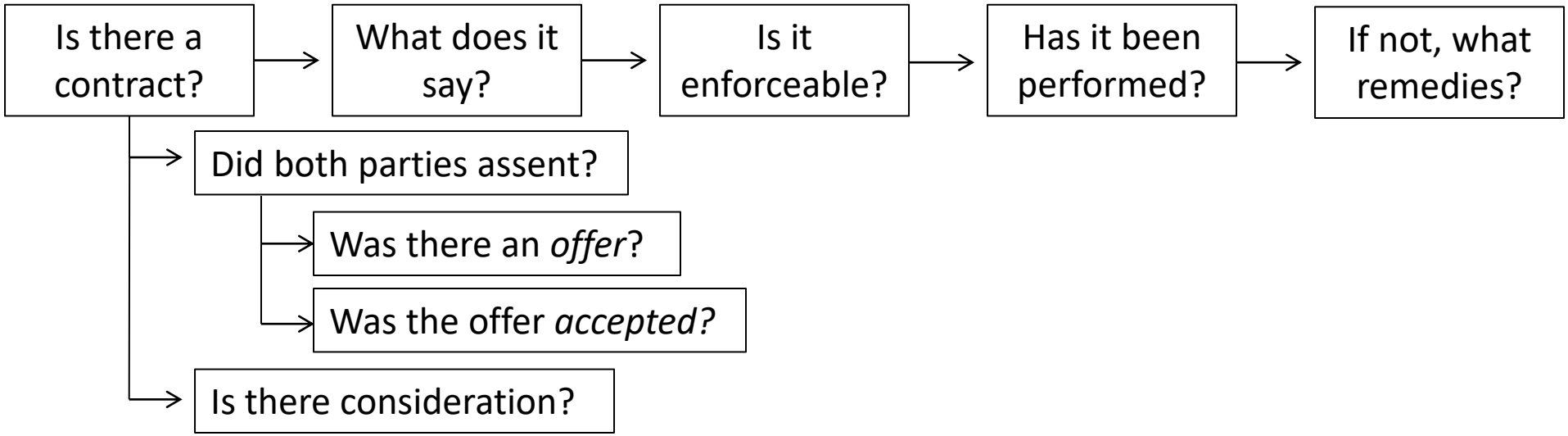
(1) Acceptance is valid upon ***dispatch*** by the offeree

(2) Rejection is valid upon ***receipt*** by the offeror

Class 5: Consideration I

Professor James Toomey

The Story of a Contract



What is Consideration?

- "Consideration" is *something of value*
  - Money
  - Goods
  - Promise to do something valuable
  - Promise not to do something one otherwise could
- The law only enforces promises where *both* parties *give up something to get something*
  - Contracts are *bargained for exchanges*—quid pro quo
  - Consideration is the *price* each party pays to get something from the other

Why is consideration required?

- *Both* parties can sue for breach?
  - Consideration ensures some *mutuality* of obligation—each has a potential cause of action against the other
  - Quid pro quo
- Formality?
  - Replacement for the seal
  - May serve "channeling" (marking this promise as one the parties want the law to enforce), "evidentiary" (proving the existence of a real agreement) and "cautionary" (getting people to think carefully before entering contracts) functions
  - "Peppercorn"—some jurisdictions enforce contracts with nominal consideration, some do not
- Historical?
  - Arose in complicated history of the requirements of forms of action (that originally didn't have to do with contracts *per se*)
  - Civil law countries don't require consideration

Restatement (Second) § 71. ***Requirement of Exchange; Types of Exchange.***

(1) To constitute consideration, a performance or a return promise must be bargained for.

(2) A performance or return promise is bargained for if it is sought by the promisor in exchange for his promise and is given by the promisee in exchange for that promise.

(3) The performance may consist of

  (a) an act other than a promise, or

  (b) a forbearance, or

  (c) the creation, modification, or destruction of a legal relation.

(4) The performance or return promise may be given to the promisor or to some other person. It may be given by the promisee or by some other person.

Restatement (Second) § 79. ***Adequacy of Consideration; Mutuality of Obligation.***

If the requirement of consideration is met, there is no additional requirement of

(a) a gain, advantage, or benefit to the promisor or a loss, disadvantage, or detriment to the promisee; or

(b) equivalence in the values exchanged; or

(c) "mutuality of obligation."

Hamer v. Sidway

- Uncle promises nephew—"if [nephew] would refrain from drinking, using tobacco, swearing, and playing cards or billiards for money until he became 21 years of age, [uncle] would pay him $5000."
- Nephew successfully refrains these activities until 21
- Executor of uncle's estate does not want to pay
- Q—Is there consideration?

Hamer v. Sidway

- Held—yes; contract enforceable
  - "[A] waiver of any legal right at the request of another party is sufficient consideration for a promise."
  - The court "will not ask whether the thing which forms the consideration does in fact benefit the promisee or a third party, or is of any substantial value to anyone. It is enough that something is promised, done, forborne, or suffered by the party to whom the promise is made as consideration for the promise made to him."

Hamer v. Sidway—Takeaways

- Consideration can take many forms—does not need to have an obvious monetary value
  - Promising to forgo a legal right generally qualifies
- Courts will not (generally) second-guess the adequacy of consideration

Feinberg v. Pfeiffer Co.

- In recognition for 40 years of service, Pfeiffer Co. promises to pay Feinberg $200/month upon her retirement for the rest of her life
  - She could retire at anytime; not required to continue working at all (but did)
- New management wants to stop paying
- Was there consideration for this promise?

Feinberg v. Pfeiffer Co.

- Held—no; contract not enforceable for lack of consideration
  - Retirement money was in recognition of *past* service
  - Things of value given in the past generally not consideration
    - Cannot be bargained for
  - Feinberg *could* retire immediately after promise, so no consideration that she in fact did not

Feinberg v. Pfeiffer Co.—Takeaways

- Past consideration generally not consideration

Mills v. Wyman

- Daniel Mills takes care of ill sailor Levi Wyman without expectation of reward
- After, Wyman's father promises to pay Daniel—and then reneges
- Was there consideration for the father's promise to pay Mills?

Mills v. Wyman

- Held—no; promise not enforceable
  - *Past* consideration not consideration
  - *Moral* obligation not (generally) sufficient for *legal* obligation

Mills v. Wyman—Takeaways

- Moral obligations arising from past heroic behavior generally not consideration

Webb v. McGowin

- Webb injures himself in saving the life of McGowin—unable to work
- McGowin promises to pay Webb $15 every two weeks for the rest of his life
- McGowin's executor wants to stop payment
- Was there consideration for this promise?

Webb v. McGowin

- Held—yes; court enforces contract
- *Contra Mills*, court analogizes to cases in which promises to pay for past conduct *have* been enforced:
  - Professional services rendered in an emergency
  - Lost bull case—promise to pay for care to bull enforced

Webb v. McGowin—Takeaways

- Some courts have departed from the traditional rule that moral obligations arising from past consideration cannot sustain enforceable contract
- ***Important note***—this case remains an outlier/minority view
  - And it is applying a ***different rule*** than *Mills v. Wyman*

Harrington v. Taylor

- Defendant promised to pay plaintiff for injuries sustained in her saving his life while he was assaulting his wife in her house
- Defendant reneges
- Consideration?

Harrington v. Taylor

- Held—no; promise unenforceable.
- Court applies the traditional rule that moral obligations arising from past acts are not consideration

Harrington v. Taylor—Takeaways

- Even after *Webb*, the rule from *Mills* remains the majority approach

Kirksey v. Kirksey

- Brother-in-law writes widowed sister Antillico—"if you come down and see me, I will let you have a place to raise your family, and I have more open land than I can tend"
- Antillico moves to brother-in-law
- Brother-in-law eventually kicks her out
- Was there consideration for promise?

Kirksey v. Kirksey

- Held—no; promise unenforceable.
- Promise was to make a gift—"a mere gratuity"
  - Did brother-in-law "bargain for" Antillico coming to his land?
  - Was there value to him in her coming?
  - Did he *want* her to come?
- Close case—judge writing opinion admits he would have decided differently

Kirksey v. Kirksey—Takeaways

- Promises to make gifts unenforceable
  - If a condition for a gift is logistical (necessary to make the gift happen)—no consideration, no contract.
  - If a condition for a "gift" is something valuable to the person giving—consideration, contract.

Class 6: Consideration II

Professor James Toomey

Consideration Review

- Consideration is *something of value* given *in exchange for* something of value from the other party
  - A *bargained for exchange*; the *price* for what the other party gives up
- Today—promises as consideration?
  - When is a commitment to do something valuable?
  - When is it not really a commitment at all?

Strong v. Sheffield

- Strong sells business to nephew-in-law "Rard" on credit—entitled under the agreement to call on debt for payment anytime.
- Strong wants Rard's wife (his niece) to co-sign debt:
  - "Rard, I will give you my word as a man that if you will give me a note, with your wife's endorsement, I will not pay that note away; I will not put it in any bank for collection, but I will hold it until such time as I want my money."
  - Responds to Rard asking whether he will "pay this note away," Strong says—"No, I will keep it until such time as I want it"
- New note signed—Strong in fact does not call on the debt for two years
- Is Strong's promise consideration?

Strong v. Sheffield

- Held—no consideration; no contract.
- Strong's promise was ***"illusory"*** —no consideration
  - "It would have been no violation of the plaintiff's promise if, immediately on receiving the note, he had commenced suit upon it."
- Does it matter that Strong in fact refrained from calling the debt?
  - No—not bargained for
- Does it matter that the parties may have all understood that Strong wouldn't call the debt for a reasonable time?
  - No—that is not what he said

Strong v. Sheffield—Takeaways

- ***"Illusory" promises*** not consideration
  - A "promise" is "illusory" if it does not actually commit the "promisor" to do or not do anything
  - If the "promisor's" freedom of action has not been restrained by what they said, the "promise" is "illusory"

Mattei v. Hopper

- Plaintiff is trying to build a shopping center, and enters into a real estate purchase contract with defendant
  - Contract provides for closing 120 days from signing
  - Closing is contingent on realtor, in the meantime, "obtaining leases satisfactory to [plaintiff]"
- During 120 period, defendant no longer wants to go through with the sale
- Was the plaintiff's promise consideration?

Mattei v. Hopper

- Held—yes, consideration, enforceable contract
- Two categories of cases in which "satisfaction clauses" count as consideration:
  - "[W]here a contract calls for satisfaction as to commercial value or quality, operative fitness, or mechanical utility"
    - Law implies a reasonable person standard—not actual subjective satisfaction
  - Applicable here—"[T]he promisor's determination that he is not satisfied, when made in good faith, has been held to be a defense to an action on the contract"

Mattei v. Hopper—Takeaways

- Promises contingent on one party's "satisfaction" count as consideration (***not*** "illusory") where the law can imply a "good faith" or "reasonable person" standard

Structural Polymer Group, Ltd. v. Zoltek Corp.

- Zoltek (manufacturer of carbon fiber) agrees to manufacture and sell to SP all of SP's requirements for carbon fiber
  - SP promises to "obtain their total requirements for suitable quality, in the reasonable opinion of [SP], Carbon Fibers from [Zoltek]"
  - At "then-current market price"
  - Up to "the amount actually purchased by [SP] in the preceding Contract Year plus one million . . . pounds."
- SP puts in orders for two years; Zoltek fails to provide
- Question—is there consideration?

Structural Polymer Group, Ltd. v. Zoltek Corp.

- Held—yes
- ***Requirements contract***—buyer agrees to buy all of their requirements from a particular seller
  - Law implies duty of good faith (i.e., promise to order their *good faith* requirements)
  - And not void for lack of consideration
  - Exclusive promise to buy everything you need from one seller is valuable, even if someone indeterminate

Structural Polymer Group, Ltd. v. Zoltek Corp.—Takeaways

- ***Requirements contract***—buyer of goods agrees to order all of their requirements from a given supplier
- ***Output contract***—seller of goods agrees to sell of their output to a given seller
  - In both cases, the law implies a duty of good faith, and neither are void for lack of consideration

Wood v. Lucy, Lady Duff-Gordon

- Lady Duff-Gordon, “creator of fashions,” enters agreement with Wood giving him the “exclusive right” to market and endorse clothing in her name
  - Duff-Gordon and Wood split profits 50-50
- Duff-Gordon endorses clothing without telling Wood
- Did Wood give consideration here?

Wood v. Lucy, Lady Duff-Gordon

- Held—consideration; binding contract
- Wood made an ***implied promise*** to make "reasonable efforts" to endorse and market Duff-Gordon's clothing
  - "The law has outgrown its primitive stage of formalism when the precise word was the sovereign talisman, and every slip was fatal. It takes a broader view today. A promise may be lacking, and yet the whole writing may be instinct with obligation, imperfectly expressed."
  - Why?
    - Profit sharing implies efforts to obtain profits
    - "The acceptance of exclusive agency was an assumption of its duties."
    - Contract refers to the fact that Wood runs a professional agency
- Promise to make reasonable efforts is consideration

Wood v. Lucy, Lady Duff-Gordon— Takeaways

- Law can find ***implied promises*** to satisfy consideration requirement
- Under circumstances like these, the grant of a right may be found to come with reasonable duties

Consideration Review

- For a promise to be enforceable as a contract, it must have been given ***in exchange for consideration***
  - In addition to having been assented to
- Consideration is ***anything of value*** that is bargained for or given in exchange for a promise

Promises Consideration Requirement Makes Unenforceable

(1) Gift promises

(2) Promises given in recognition of moral obligation

(3) Promises of which the promisee was unaware

(4) Illusory promises

Class 7: Reliance & Restitution

Professor James Toomey

Promises Consideration Requirement Makes Unenforceable

(1) Gift promises

(2) Promises given in recognition of moral obligation

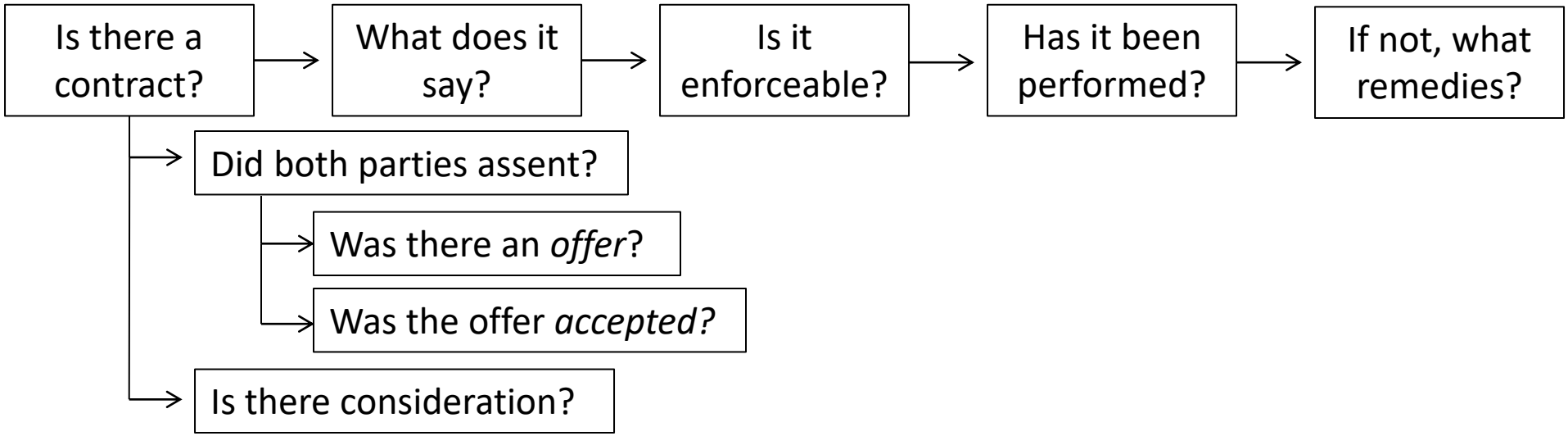
(3) Promises of which the promisee was unaware

(4) Illusory promises

Law vs. Equity

- Contract law is *“law”*
- Related “*equitable remedies*”?

The Story of a Contract



What if…

- A promise has no consideration?
  - *Reliance* or *promissory estoppel*
- There is no promise?
  - *Restitution*

Origins of Promissory Estoppel—Equitable Estoppel

- A party who asserts a *fact*, upon which another person detrimentally relied, will be later "*estopped*" from denying that fact

Ricketts v. Scothorn

- Ricketts (grandfather) walks into store where Scothorn (granddaughter) works:
  - Says “I have fixed out something that you have not got to work anymore. . . . None of my grandchildren work, and you don’t have to.”
  - Gives a note—”I promise to pay Katie Scothorn on demand, $2000 to be at 6 percent, per annum.”
- Ricketts dies a year later, executor wants to discontinue payment.
- Can Ricketts’s promise be enforced?

Ricketts v. Scothorn

- Held—yes; "applying the doctrine of equitable estoppel"
  - "Equitable estoppel is the effect of the voluntary conduct of a party whereby he is absolutely precluded, both at law and in equity, from asserting rights which might, perhaps, have otherwise existed, either of property, of contract, or of remedy, as against another person who in good faith relied upon such conduct, and has been led thereby to change his position for the worse, and who on his part acquires some corresponding right, either of property, or contract, or of remedy."

Ricketts v. Scothorn—Takeaways

- An expansion of equitable estoppel can be understood as a precursor to the development of promissory estoppel doctrine
  - Also, equitable estoppel generally—A party who asserts a *fact*, upon which another person detrimentally relied, will be later "*estopped*" from denying that fact

Restatement (First) § 90. ***Promise Reasonably Inducing Definite and Substantial Action.***

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 is binding if injustice can be avoided only by enforcement of the promise.

Restatement (Second) § 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 such breach may be limited as justice requires.

(2) A charitable subscription or a marriage settlement is binding under Subsection (1) without proof that the promise induced action or forbearance.

Feinberg v. Pfeiffer II

- Reminder—Pfeiffer Co. promised to pay Mrs. Feinberg $200 per month after her retirement
- If there is no contract for lack of consideration, can this promise be enforced under § 90?

Feinberg v. Pfeiffer II

- Held—yes; promise enforceable by promissory estoppel
- Would the promise be reasonably expected to induce action?
  - Yes, retirement stipend can reasonably be expected to induce retirement
- Did the promise induce action?
  - Yes, she retired relying on the stipend
- Can injustice only be avoided by enforcing the promise?
  - Yes—Feinberg is 63 and has cancer, unlikely that she can find alternative employment

Feinberg v. Pfeiffer II—Takeaways

- Restatement § 90 is a relatively novel equitable alternative way to enforce certain promises that cannot be contracts for lack of consideration
  - Read Restatement § 90 closely
  - Only applies if enforcing the promise avoids "injustice"
- § 90 was originally thought to be a move towards abolishing consideration requirement, but this hasn't happened

Restitution

- An equitable remedy to force someone to pay back benefits unfairly received
- Can apply even where there is no promise—where the law might find a “quasi-contract” or “implied contract”

Cotnam v. Wisdom

- Harrison killed in a street car accident, but cared for by doctors while unconscious but before death
- Doctors sue for payment for services
- Can the doctors recover?
  - If so, how much?

Cotnam v. Wisdom

- Held—yes, doctors entitled to compensation
  - "Quasi-contract," "implied contract," "constructive contract"
    - "[S]ervices rendered by physicians to persons unconscious or helpless by reason of injury or sickness are in the same situation as those rendered to persons incapable of contracting."
  - But the remedy is ***reasonable costs*** only
    - At this time, expectation damages would have taken into account Harrison's ability to pay
    - But expectation damages are a contract remedy—this is restitution
      - Return value unfairly gained to doctors

Cotnam v. Wisdom—Takeaways

- Professional services rendered in an emergency are a classic context for restitution
  - No promise—not a contract, no contract remedy
  - But return the value of the reasonable cost of services to those who gave them

Pyette v. Pyette

- Charles and Margrethe Pyette are married, work out an "agreement":
  - Margrethe will work for three years to put Charles through law school
  - Then he will work and she will go to grad school
- Margrethe puts Charles through law school; he dumps her
- Even if the "agreement" is unenforceable as a contract, can Margrethe recover?

Pyette v. Pyette

- Held—yes; "quasi-contract"
- Quasi-contract will be found "if the circumstances are such that it would be unjust to allow retention of the benefit without compensating the one who conferred it"
  - It is unjust to allow retention of the benefit where "there was an expectation of payment or compensation for services at the time they were rendered."
- Damages?
  - The value of what Margrethe gave Charles
  - *Not* the value of what Charles *would have* given Margrethe (expectation damages)

Pyette v. Pyette—Takeaways

- Restitution can be a remedy where there was a promise, but it fails to be an enforceable contract for some reason
- Restitution applies in cases in which benefits were rendered in expectation of compensation

Class 8: Pre-Contractual Liability

Professor James Toomey

Common Law Background

- No implied duty to negotiate in good faith
  - Historically, a sharp distinction in responsibility before and after a contract is entered into
  - *Before* contract, the parties have no duties towards one another
  - *After* contract parties have contractual duties, and implied duty of good faith
- *Contra* civil law countries, which imply duty to negotiate in good faith
- Today we're talking about *exceptions*, where there can be liability before contract

Hoffman v. Red Owl Stores

- Hoffman wants to run a Red Owl franchise. Red Owl's agent tells him he has enough money, but he has to take a number of steps first before they can enter into franchise agreement:
  - Buy and run a local grocery store for practice; then sell it
  - Put money down to buy land for Red Owl store
  - Move to another town
  - Ends up working the night shift at a bakery to support his family
- The deal falls through—Red Owl wants more money than Hoffman can put up.
- Hoffman sues—no contract, but can Red Owl still be liable to him anyway?

Hoffman v. Red Owl Stores

- Held—yes; Red Owl liable to Hoffman
- § 90—promissory estoppel
  - Red Owl promised if you do these things, we will give you a store
  - That would be reasonably expected to induce him to do those things
  - He did them
  - And injustice can only be avoided by enforcing the contract
- Damages—reliance damages
  - Not expectation damages, so no lost profits from selling the grocery store

Hoffman v. Red Owl Stores—Takeaways

- Promises made during negotiations, reasonably relied on, can give rise to liability under promissory estoppel theory
- ***Note*—**this case is an exception; of more academic than practical interest

Dixon v. Wells Fargo

- In mortgage renegotiations, Wells Fargo tells Dixons to stop making monthly mortgage payments so they can restructure the loan when they reach an agreement
- Dixons stop paying
- Wells Fargo, ignoring Dixons' efforts to renegotiate, attempts to foreclose
- Before reaching a new contract, can Wells Fargo be held to its promise?

Dixon v. Wells Fargo

- Held—yes; Dixons cannot be foreclosed upon for not making mortgage payments
- Historically, promissory estoppel used as a consideration substitute for enforcing definite promises
  - No definite promise here—just a promise to negotiate
  - But promissory estoppel can also be used where one party is unfairly stringing the other along in the bargaining process
    - Something more like fraud or misrepresentation
- Wells Fargo's behavior was unfair and put Dixons in unfair position—Wells Fargo cannot take advantage
- Damages—reliance damages; just put Dixons in the position they would have been in before reliance

Dixon v. Wells Fargo—Takeaways

- Promissory estoppel can by used to police certain kinds of unfairness or manipulation in the bargaining process
  - Even where promise is not otherwise sufficiently definite to be enforced

Cyberchron Corp. v. Calldata Systems Development, Inc.

- Grumman is negotiating to buy a computer from Cyberchron
  - No contract because the parties cannot agree on weight
- Grumman keeps telling Cyberchron to build the computer anyway and they'll agree on the weight later
- Grumman goes out and buys a worse computer from another company in the meantime; refuses to pay Cyberchron
- Can Cyberchron recover expenses incurred in starting work on the computer?

Cyberchron Corp. v. Calldata Systems Development, Inc.

- Held—yes; Cyberchron can recover under promissory estoppel
- Promise induced reasonable reliance
  - And Grumman's treatment of Cyberchron was unjust
- Damages—reliance damages
  - But court allows Cyberchron to include overhead costs to the extent they could show they were related to this particular project

Cyberchron Corp. v. Calldata Systems Development, Inc.—Takeaways

- § 90 can provide pre-contractual liability between sophisticated commercial actors
- Compare *Dixon*—promissory estoppel as policing the bargaining process

Channel Home Centers v. Grossman

- Channel and Grossman sign a "letter of intent"
  - Channel—says it is interested in leasing, and negotiate in good faith the specifics of a lease agreement
  - Grossmans—say they will take the storefront at issue off the market and negotiate only with Channel
- Negotiations continue; Channel spends money preparing to move forward
- Grossmans lease store to Channel competitor Mr. Good Buys before final agreement
- Can Channel sue for breach of contract?

Channel Home Centers v. Grossman

- Held—yes; letter of intent is a binding, enforceable contract
- Definiteness?
  - Promise to negotiate in good faith sufficiently definite for a contract
- Consideration?
  - Grossman agreed to lock in space for Channel; negotiate exclusively
  - Channel gave Grossmans proof of interest they could use to get financing
- [Court sends back down for fact-finding]

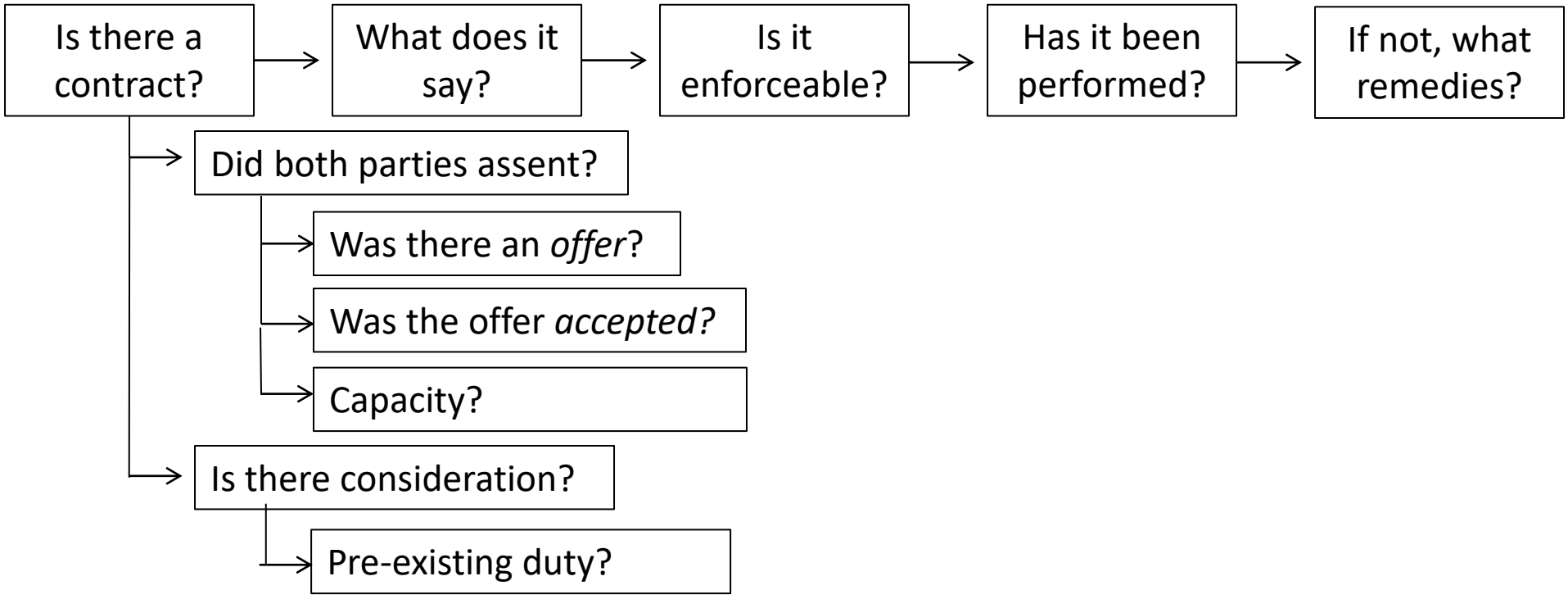
Channel Home Centers v. Grossman—Takeaways

- Two traditional common law rules:
  - No implied duty to negotiate in good faith
  - "Agreements to agree" are unenforceable (lack of definiteness; lack of consideration)
- *But* American courts increasingly enforce *contracts* to negotiate *in good faith*
  - Opposite default rule to civil law countries
  - English courts still generally invalidate these contracts as "agreements to agree"

Class 9: Capacity & Overreaching

Professor James Toomey

The Story of a Contract



Capacity

- *Void* contractual obligations—entirely unenforceable; no contract at all
- Void*able* contractual obligations:
  - Incapacitated party can renounce contract
  - Other party bound unless renounced

Restatement § 12. ***Capacity to Contract***.

(1) …

(2) A natural person who manifests assent to a transaction has full legal capacity to incur contractual duties thereby unless he is

(a) under guardianship, or

(b) an infant, or

(c) mentally ill or defective, or

(d) intoxicated

Restatement § 13. ***Persons Affected by Guardianship***.

A person has no capacity to incur contractual duties if his property is under guardianship by reason of an adjudication of mental illness or defect.

Restatement § 14. ***Infants***.

Unless a statute provides otherwise, a natural person has the capacity to incur only voidable contractual duties until the beginning of the day before the person's eighteenth birthday.

Restatement § 15. ***Mental Illness or Defect***.

(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 consequences 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.

Ortelere v. Teachers Retirement Bd.

- Retired teacher has "involutional psychosis, melancholia type," maybe cerebral arteriosclerosis
  - She seems able to *understand*, maybe unable to control herself. Expert—"Everything is impossible to decide."
- Two months before death—elects to take a higher monthly payment from pension, foregoing husband's remainder after her death
- After her death, husband sues to avoid decision on grounds of incapacity.
- Question—is this contract voidable?

Ortelere v. Teachers Retirement Bd.

- Held—yes
- People lack contractual capacity if they are "unable to act in a reasonable manner in relation to the transaction and the other party has reason to know of his condition"
  - "Of course, nothing less serious than medically classified psychosis should suffice or else few contracts would be invulnerable to some kind of psychological attack."

Ortelere v. Teachers Retirement Bd.—Dissent

- Contractual capacity requires just the ability to understand the decision one is making
  - Ortelere clearly did here

Ortelere v. Teachers Retirement Bd.— Takeaways

- Contracts made with insufficient mental capacity voidable
- Difficult, much-litigated area:
  - Split decisions
  - Competing medical experts and testimony from family and friends
  - Courts considering whether the decision was a "good" one

Cundick v. Broadbent

- Cundick ("confused and befuddled man with very poor judgment;" later diagnosed with arteriosclerosis) sells Broadbent his ranch and business for far below market value.
- Negotiations:
  - Take places over several months
  - Involve an attorney
  - Contract re-drafted several times
  - Cundick's wife is involved
- Wife (as Cundick's guardian ad litem) sues to avoid contract for lack of capacity
- Question—did Cundick have the mental capacity to sell?

Cundick v. Broadbent

- Held—yes
- "[M]ental capacity to contract depends upon whether the allegedly disabled person possessed sufficient reason to enable him to understand the nature and effect of the act in issue."
  - "It seems incredible that Cundick could have been utterly incapable of transacting his business affairs, yet such condition be unknown on this record to his family and friends, especially his wife who lived and worked with him and participated in the months-long transaction which she now contends was fraudulently conceived and perpetrated."

Cundick v. Broadbent—Dissent

- Medical testimony of incapacity undisputed
  - Majority inappropriately relying on circumstantial testimony from non-experts

Cundick v. Broadbent—Takeaways

- Capacity cases often involve disputes about comparative weight of expert and non-expert testimony

Kenai Chrysler Center, Inc. v. Denison

- David Denison, young man with developmental disabilities, is subject to guardianship of his parents
- Denison attempts to buy car with his debit card
- Parent-guardians want to avoid transaction
- Question—is Denison's purchase of the car void, voidable, or enforceable?

Kenai Chrysler Center, Inc. v. Denison

- Held—void
- Contracts entered into by individuals subject to guardianship are ***void***
- Guardianship (public record) furnishes constructive notice of person's incapacity

Kenai Chrysler Center, Inc. v. Denison—Takeaways

- Guardianship transfers contractual capacity guardian
  - Purported contracts entered into by persons subject to guardianship are ***void***
  - Regardless of other party's knowledge

Restatement § 73. ***Performance of Legal Duty***.

Performance of a legal duty owed to a promisor which is neither doubtful nor the subject of honest dispute is not consideration; but a similar performance is consideration if it differs from what was required by the duty in a way which reflects more than a pretense of bargain.

Alaska Packers' Ass'n v. Domenico

- In San Francisco, workers sign a contract to catch salmon in Alaska for $50 for the season
- In Alaska, workers refuse to work for less than $100 for the season
  - Superintendent agrees
- Upon returning to San Francisco, company only pays $50 for the season
- Question—is the "revised" contract for $100 enforceable?

Alaska Packers' Ass'n v. Domenico

- Held—no; "revised" agreement not a contract for lack of consideration
- Pre-existing duty rule—agreeing to do something one was already contractually obligated to do is not consideration
  - Purpose—avoid something like extortion or duress
  - Court emphasizes that once in Alaska, company could not get alternative workers and was under a time-crunch

Alaska Packers' Ass'n v. Domenico—Takeaways

- Pre-existing duty rule—agreeing to do something already contractually obligated is not consideration
  - Purpose—avoid extortion and duress
  - Controversial—may prevent reasonable, consensual modifications or adjustments
    - Cabined or abrogated by decision or statute in many jurisdictions

Watkins & Son v. Carrig

- Plaintiff agrees to build cellar under defendant's house
  - Contract provides that "all material" shall be removed from site; plaintiff to "excavate" cellar
- Shortly after starting, plaintiff finds a large boulder
- Plaintiff and defendant orally agree to raise the price to 9x original
- Defendant pays initially-agreed to price
- Question—is the oral modification enforceable?

Watkins & Son v. Carrig

- Held—yes
- "Changes to meet changes in circumstances and conditions should be valid if the law is to carry out its function and service by rules conformable with reasonable practices and understandings in matters of business and commerce."
  - "The contract being freely surrendered, the issue of contract law whether the new promise is valid is not doubtful."
- Theory—parties mutually rescinded original contract; entered into a new one

Watkins & Son v. Carrig—Takeaways

- Notwithstanding pre-existing duty rule, courts often find ways to enforce reasonable modifications in changed circumstances
  - Pre-existing duty rule controversial and widely limited

UCC § 2-209. ***Modification, Rescission and Waiver***.

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

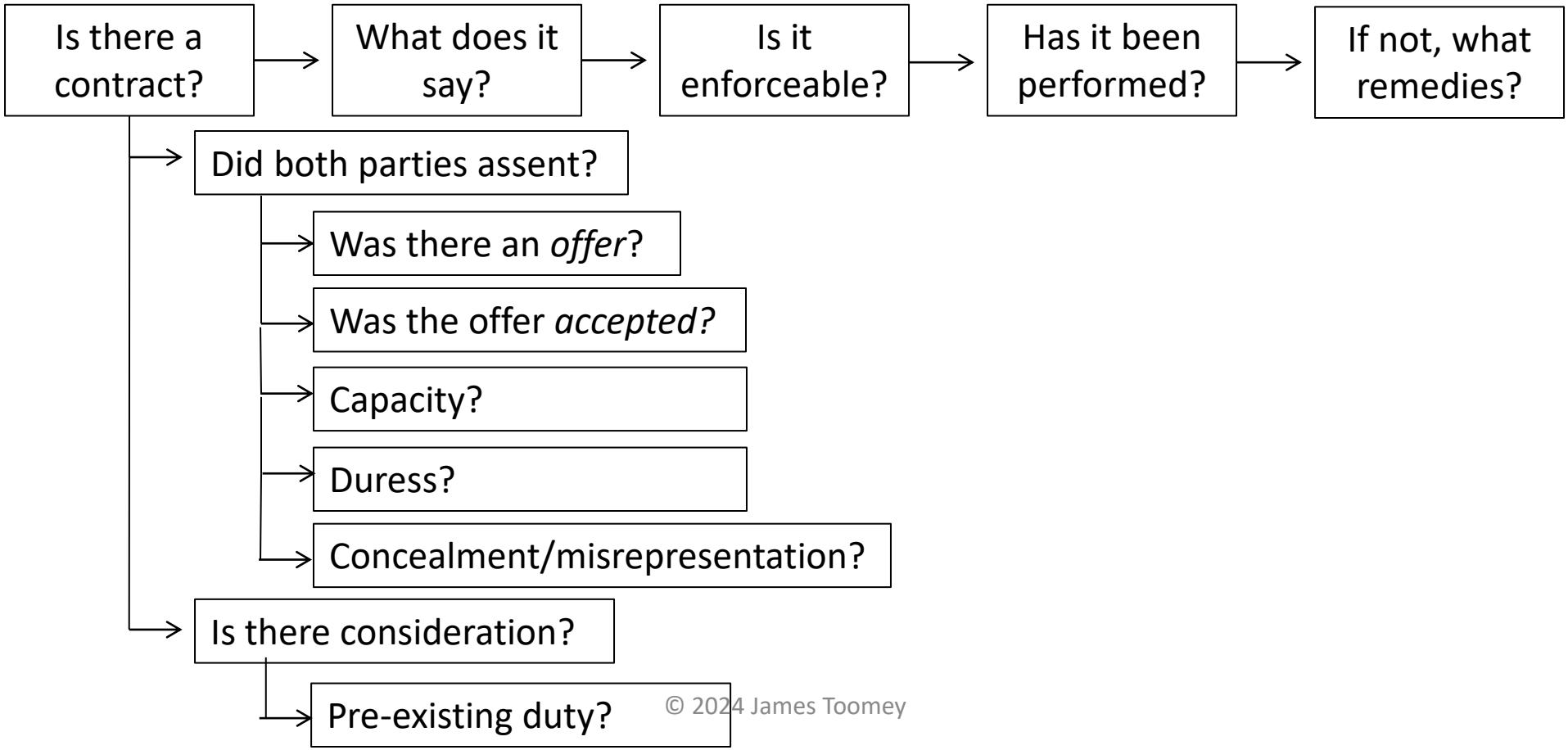
Other Eliminations of Pre-Existing Duty Rule

- *Winegardner v. Burns*, 361 So. 2d 1054 (Ala. 1978)
  - "[A]n executory contract may be modified by the parties without any new consideration other than mutual consent."
- NY Code § 5-1103
  - "An agreement, promise, or undertaking to change or modify, or to discharge in whole or in part, any contract . . . shall not be invalid because of the absence of consideration, provided that the agreement, promise or undertaking changing, modifying, or discharging such contract . . . shall be in writing and signed by the party against whom it is sought to enforce the change."

Class 10: Duress and Fraud

Professor James Toomey

The Story of a Contract



Restatement § 174. ***When Duress by Physical Compulsion Prevents Formation of a Contract.***

If conduct that appears to be a manifestation of assent by a party who does not intend to engage in that conduct is physically compelled by duress, the conduct is not effective as a manifestation of assent.

Restatement § 175. ***When Duress By Threat Makes a Contract Voidable.***

(1) If a party's manifestation of assent is induced by an improper threat by the other party that leaves the victim no reasonable alternative, the contract is voidable by the victim.

Restatement § 176. ***When a Threat Is Improper.***

(1) A threat is improper if
   (a) what is threatened is a crime or a tort, or the threat itself would be a crime or a tort if it resulted in obtaining property,
   (b) what is threatened is a criminal prosecution,
   (c) what is threatened is the use of civil process and the threat is made in bad faith, or
   (d) the threat is a breach of the duty of good faith and fair dealing under a contract with the recipient.

(2) A threat is improper if the resulting exchange is not on fair terms, and
   (a) the threatened act would harm the recipient and would not significantly benefit the party making the threat,
   (b) The effectiveness of the threat in inducing the manifestation of assent is significantly increased by prior unfair dealing by the party making the threat, or
   (c) what is threatened is otherwise a use of power for illegitimate ends.

Austin Instrument v. Loral Corporation

- Loral has contract with Navy to produce radars, for which it needs 40 parts
  - Subject to strict schedule that includes stiff penalties for missing deadlines
- Loral initially contracts with Austin for 23/40 parts
- For the next year, Loral opens bidding on all 40. Austin submits bid for all 40.
  - Austin threatens to stop shipping parts it already contracted for unless (1) Loral agrees to contract with it for all 40 parts next year, and (2) Loral pays substantially increased prices on current parts.
  - Loral explores alternatives with some other suppliers but can't find any.
- Loral agrees to Austin's demands. At the end of the contract period, Austin sues for full price under "re-negotiated" contract; Loral countersues for money it believes it overpaid under that contract.
- Question—were price increases unenforceable on grounds of economic duress?

Austin Instrument v. Loral Corporation

- Held—yes
- "A contract is voidable on ground of duress when it is established that the party making the claim was forced to agree to it by means of a wrongful threat precluding the exercise of his free will."
  - "The existence of economic duress or business compulsion is demonstrated by proof that immediate possession of needful goods is threatened or, more particularly, in cases such as the one before us, by proof that one party to a contract has threatened to breach the agreement by withholding goods unless the other party agrees to some further demand."
  - "It must also appear that the threatened party could not obtain the goods from another source of supply and that the ordinary remedy of an action for breach of contract would not be adequate."

Austin Instrument v. Loral Corporation—Dissent

- Duress is a fact-issue to be decided by jury, and—
  - Austin had an explanation for why renegotiation was reasonable
  - Loral had alternatives—other suppliers; could have asked for an extension from the government

Austin Instrument v. Loral Corporation—Takeaways

- Economic duress can (rarely) render contracts voidable in dealings between sophisticated commercial actors. Look for:
  - Time crunch
  - Lack of reasonable alternatives

Swinton v. Whitinsville Sav. Bank

- Defendant sells house to plaintiff
  - Defendant knows house is infested with termites
  - Says nothing about termites to plaintiff
- Plaintiff sues defendant for ***damages***
- Question—is plaintiff entitled to contract/expectation damages for failure to disclose termites?

Swinton v. Whitinsville Sav. Bank

- Held—no
- Mere failure to disclose facts not actionable for damages—”concealment and nothing more”

Swinton v. Whitinsville Sav. Bank—Takeaways

- Common law *caveat emptor*—no damages/contract liability for mere failure to disclose, absent:
  - Special duty to reveal
  - Affirmative false statement
  - Half-truth tantamount to falsehood
  - Affirmative concealment
- ***Note***—this suit is for ***damages***. More likely to get rescission at equity.
  - ***Note also***—in real estate and many consumer contexts, common law rule superseded by statute.

Kannavos v. Annino

- Annino lists property—"Income gross $9,600 yr. in lg. single house, converted to 8 lovely, completely furn. (include. TV and china) apts. 8 baths, ideal for couple to live free with excellent income. By apt. only. Foote Realty."
  - Property is in fact zoned only for single-family residences
- Kannavos, unaware of zoning requirements, purchases property with intent to rent.
- Shortly after the sale the authorities start proceedings against Kannavos. He wants out of sale.
- Kannavos sues in equity to ***rescind*** contract.
- Question—is not telling Kannavos about zoning problem grounds for rescission?

Kannavos v. Annino

- Held—yes
- More than bare nondisclosure—ad affirmatively implies legal ability to rent
  - But discovering zoning issue easier than discovering termites.
  - For rescission, court says due diligence not required

Kannavos v. Annino—Takeaways

- Rescission for failure to disclose more likely than damages
- Half-truths/statements implying the absence of a condition may require disclosure of condition under common law
  - Today, statutes play a major role in disclosure requirements in particular contexts

Restatement § 164. ***When a Misrepresentation Makes a Contract Voidable.***

(1) If a party's manifestation of assent is induced by either a fraudulent or a material misrepresentation by the other party upon which the recipient is justified in relying, the contract is voidable by the recipient.

Restatement § 161. ***When Non-Disclosure Is Equivalent to an Assertion.***

A person's non-disclosure of a fact known to him is equivalent to an assertion that the fact does not exist in the following cases only:

(a) where he knows that disclosure of the fact is necessary to prevent some previous assertion from being a misrepresentation or from being fraudulent or material.

(b) where he knows that disclosure of the fact would correct a mistake of the other party as to a basic assumption on which that party is making the contract and if non-disclosure of the fact amounts to a failure to act in good faith and in accordance with reasonable standards of fair dealing.

(c) where he knows that disclosure of the fact would correct a mistake of the other party as to the content or effect of a writing, evidencing or embodying an agreement in whole or in part.

(d) where the other person is entitled to know the fact because of a relationship of trust and confidence between them.

Speakers of Sport v. ProServ

- Ivan Rodriguez initially signed with Speakers of Sport
  - ProServ promises to get him between $2 million and $4 million in endorsements if he switches to them
  - Rodriguez switches; ProServ gets no significant endorsements
- Speakers of Sport sues ProServ, alleging promissory fraud (never intended to fulfill promise)
- Question—was there promissory fraud here?

Speakers of Sport v. ProServ

- Held—no; ProServ's statements were permissible "puffery"
  - "[A] reasonable person in the position of the 'promisee' would understand [the 'promise'] to be aspirational rather than enforceable—an expression of hope rather than a commitment"
  - Not fraud or misrepresentation because no statement of fact

Speakers of Sport v. ProServ—Takeaways

- "Puffery"—sales techniques characterized by statements reasonably understood to be aspirational—is permissible and not actionable
- For promissory fraud, there must at least be a concrete, definitive promise

Vokes v. Arthur Murray, Inc.

- 51-year-old widow Audrey Vokes is persuaded to sign up for $31k worth of dancing lessons at Arthur Murray dancing studio
  - They tell her she has "grace and poise"
  - That she's "rapidly improving and developing in her dancing skill"
  - She would "make . . . a beautiful dancer, capable of dancing with the most accomplished dancers
  - Etc.
- Vokes alleges that in fact she is very bad at dancing and wasn't getting any better
- Question—can these contracts be rescinded?

Vokes v. Arthur Murray, Inc.

- Held—yes
- At issue in this case are expressions of opinion, which are not generally a basis for rescission
  - But can be "where there is a fiduciary relationship between parties, or where there has been some artifice or trick employed by the representor, or where the parties do not in general deal at 'arm's length' as we understand the phrase, or where the representee does not have equal opportunity to become apprised of the truth or falsity of the fact represented."
  - Vokes was not in an "arm's length" position with Arthur Murray, and didn't have equal opportunity to assess the truth of what they were saying
  - Persuasion "went beyond the unsavory, yet legally permissible, perimeter of 'sales puffing' and intruded well into the forbidden area of undue influence, the suggestion of falsehood, the suppression of truth, and the free exercise of rational judgment"

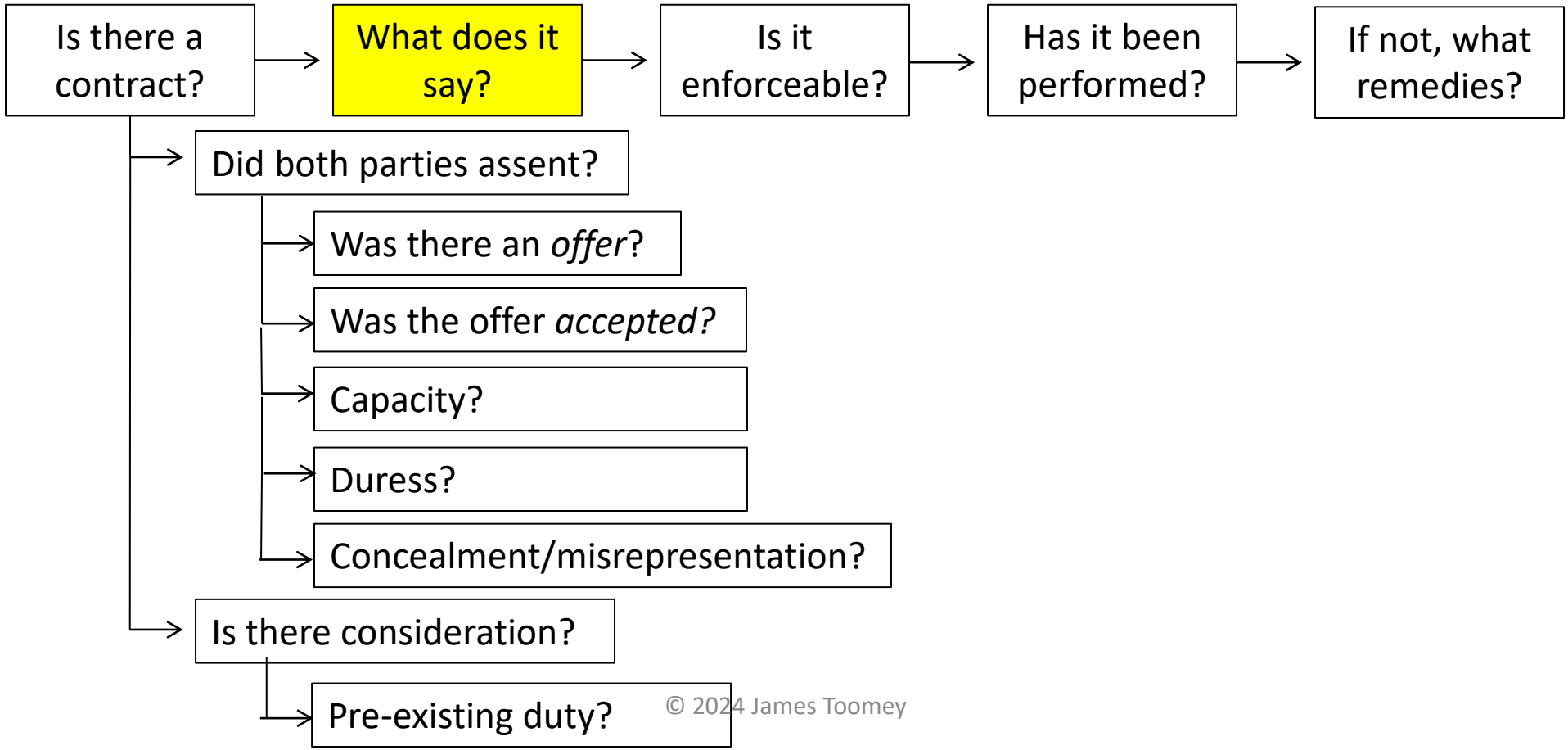
Vokes v. Arthur Murray, Inc.— Takeaways

- Expressions of opinion and persuasive sales tactics ***may*** be grounds for rescission
  - Where they go "too far"
    - Variation among courts as to how far is too far
    - Lines not always clear
  - Vulnerability (or perceived vulnerability) of the buyer is relevant

Class 11: Parol Evidence Rule and Extrinsic Evidence

Professor James Toomey

The Story of a Contract



Two Questions Today

- What text/language is the contract?
  - Parol evidence rule
  - *Mitchell v. Lath*, *Masterson v. Sine*, *Bollinger v. Central Pennsylvania Quarry*
- How do we interpret that text/language?
  - Plain meaning rule
  - *Pacific Gas & Electric*, *Greenfield v. Philles*

“Parol Evidence Rule”

- “Parol”—old French for “oral”
- The basic rule—a *written* document, *intended* to be the *final and complete* agreement between the parties, cannot be contradicted by evidence of *prior* agreements, documents, understandings, or statements
  - Does not only bar “oral” evidence
  - Is a substantive rule that goes to the nature of the contract, not a rule of admissible evidence

Mitchell v. Lath

- Laths own farm and ugly icehouse across the street on someone else's land
- Mrs. Mitchell is looking to buy farm
  - In negotiations, Laths and Mitchell make an oral agreement that the Laths will tear down the icehouse
- Mrs. Mitchell enter into written sale contract—standard real estate sale contract says nothing about icehouse
- Question—is the promise to take down the icehouse part of the contract?

Mitchell v. Lath

- Held—no; agreement about icehouse barred by parol evidence rule, superseded by written contract
- Parol evidence rule prevents "attempts to modify written contracts by parol"
- But does not bar "a collateral contract distinct and independent of the written agreement." Agreement "collateral" if:
  - Collateral *in form*—met here
  - Does not contradict the written contract—maybe met here
  - One that parties would not ordinarily be expected to embody in the writing—not met here

Mitchell v. Lath—Dissent

- Disagrees on third prong—thinks agreement was not of the sort expected to be included in the writing
  - "[T]o determine what the writing was intended to cover, the document alone will not suffice. What it was intended to cover cannot be known till we know what there was to cover."

Mitchell v. Lath—Takeaways

- NY parol evidence rule relatively traditional
- Parol evidence rule bars prior agreements *within the contract's domain*
- But does not necessarily bar separate *collateral* or *distinct* agreements.
- The domain of a written contract is often where the dispute is in parol evidence rule cases. In the Restatement's terms:
  - ***"Completely integrated contracts"***—intended to be the final and complete agreement on a subject between parties. Bars any prior evidence. Generally shown today with a "merger clause."
  - ***"Partially integrated contracts"***—intended to settle some but not all issues between the parties. Bars prior inconsistent evidence, but can be supplemented by non-contradictory prior agreements.

Masterson v. Sine

- Mastersons sell ranch to Sines (family)
- Under the deed, Mastersons:
  - "reserve an option to purchase the above described property on or before February 25, 1968" for the "same consideration as being paid heretofore . . . "
- In bankruptcy, Mastersons' trustee wants to exercise option. Masterson argues that the option was non-transferable, because intended to keep the property in the family.
- Can the court consider evidence of the alleged agreement that the option was non-transferable?

Masterson v. Sine

- Held—yes, evidence of non-transferability not barred by parol evidence rule
- "When the parties to a written contract have agreed to it as an 'integration'—a complete and final embodiment of the terms of an agreement—parol evidence cannot be used to add to or vary its terms. When only part of the agreement is integrated, the same rule applies to that part, but parol evidence may be used to prove elements of the agreement not reduced to writing."
  - Court finds this to be a partially integrated agreement
  - And concludes that an agreement to assign the contract could have been a separate agreement that would not be part of the writing.
- Narrowing parol evidence rule—"evidence of oral collateral agreements should be excluded only when the fact finder is likely to be misled"
  - Test from Restatement—whether the alleged separate agreement "might naturally be made as a separate agreement by parties situated as were the parties to the written contract"
  - Test from the UCC—whether "the additional terms are such that, if agreed upon, they would certainly have been included in the document in the view of the court"

Masterson v. Sine—Dissent

- Parol evidence rule prohibits evidence of agreements that *contradict* the text—this is true for both partially and completely integrated agreements
- Legal default rule is that an option, unless specifically made non-transferrable, is transferable
  - Therefore, the alleged agreement that this one was not *contradicts* rather than *supplements* the text
- This may well be a classic case of the kind of difficult-to-police fraud the parol evidence rule is designed to prevent
  - Party in bankruptcy now claiming unwritten terms to their benefit

Masterson v. Sine—Takeaways

- California has narrowed the parol evidence rule
  - Motivated by a concern that strict application may violate the expectations of unsophisticated parties
  - But may raise the risk of post-facto fraud?
- Whether an alleged term “supplements” or “contradicts” the written terms another area of dispute

Bollinger v. Central Pennsylvania Quarry

- Central Pennsylvania Quarry wants to store waste on Bollingers' land
- Written contract says nothing about waste storage
  - Bollingers testify that there was an oral understanding that Central Pennsylvania would bury waste and restore land
  - Bollingers did not read written contract. They believe that the agreement about disposal should have been in there and it is just a mistake if not.
- Question—is the oral agreement to dispose of waste and restore property part of the contract?

Bollinger v. Central Pennsylvania Quarry

- Held—yes
- If a term is omitted by *mistake*, court can (*in equity*) *reform* contract to include term
  - Central Pennsylvania was complying with this term for a while—no reason to do this unless it thought it had to
  - Question is whether term was omitted by mistake when the contract was written, so Central Pennsylvania's denial now is not dispositive
- "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."

Bollinger v. Central Pennsylvania Quarry—Takeaways

- Parol evidence rule may not bar equitable reformation where a term actually agreed to is omitted from writing by mistake

Plain Meaning Rule

- Courts traditionally enforce the *plain meaning* of written contracts. Two steps:
  - If the contract is unambiguous, enforce its unambiguous meaning. If it is ambiguous:
  - Extrinsic evidence may be admitted to resolve ambiguities.

Pacific Gas & Electric Co. v. G.W. Thomas Drayage & Rigging Co.

- Contract says that defendant will "indemnify" plaintiff "against all loss, damage, expense, and liability resulting from injury to property, arising out of or in any way connected with the performance of the contract."
- Plaintiff has a loss, sues defendant for indemnification.
- Defendant claims that indemnity clause was meant to cover only injury to the property of third parties, not plaintiff
  - And offers to prove this with evidence from similar contracts and prior conduct
- Can the court hear extrinsic evidence on the meaning of indemnity clause?

Pacific Gas & Electric Co. v. G.W. Thomas Drayage & Rigging Co.

- Held—yes.
- California test:
  - Step one: "A preliminary consideration of all credible evidence offered to prove the intention of the parties."
  - Step two: "If the court decides, after considering this evidence, that the language of the contract, in light of all the circumstances, is fairly susceptible of either one of the two interpretations contended, extrinsic evidence relevant to prove either of such meanings is admissible."

Pacific Gas & Electric Co. v. G.W. Thomas Drayage & Rigging Co.—Takeaways

- As with the parol evidence rule, California has modified the traditional plain meaning rule to allow in more extrinsic evidence, and considers extrinsic evidence at step one to determine whether an agreement is ambiguous
  - Motivated by goal of getting at the parties' true intent
  - But risk of post-facto manipulation?

Greenfield v. Philles Records

- Ronettes enter into NY contract with label Philles Records—Philles ownership of Ronettes' recordings and can license them "by any method now or hereafter known," pays the Ronettes royalties.
- Ronettes and Philles get divorced—CA divorce settlement agreement release all claims their respective companies may have against each other.
- Philles starts licensing Ronettes' music in new mediums, and is not paying royalties.
- Three questions:
  - Can Philles license Ronettes' music in new mediums?
  - If so, does Philles owe Ronettes royalties?
  - If so, does the divorce agreement preclude such a claim?

Greenfield v. Philles Records

- Held—
  - Yes—NY contract unambiguously grants Philles ownership and the right to license in any format
    - NY rule—"the best evidence of what the parties to a written agreement intend is what they say in their writing"
      - "extrinsic evidence of the parties' intent may be considered only if the agreement is ambiguous"
  - Yes—NY contract also unambiguously requires Philles to pay royalties
  - No—text of CA agreement unambiguously precludes any claims of Ronettes against Philles
    - *But* under CA law we can look to extrinsic evidence anyway, and court says that extrinsic evidence shows divorce settlement not intended to bar claims for royalties

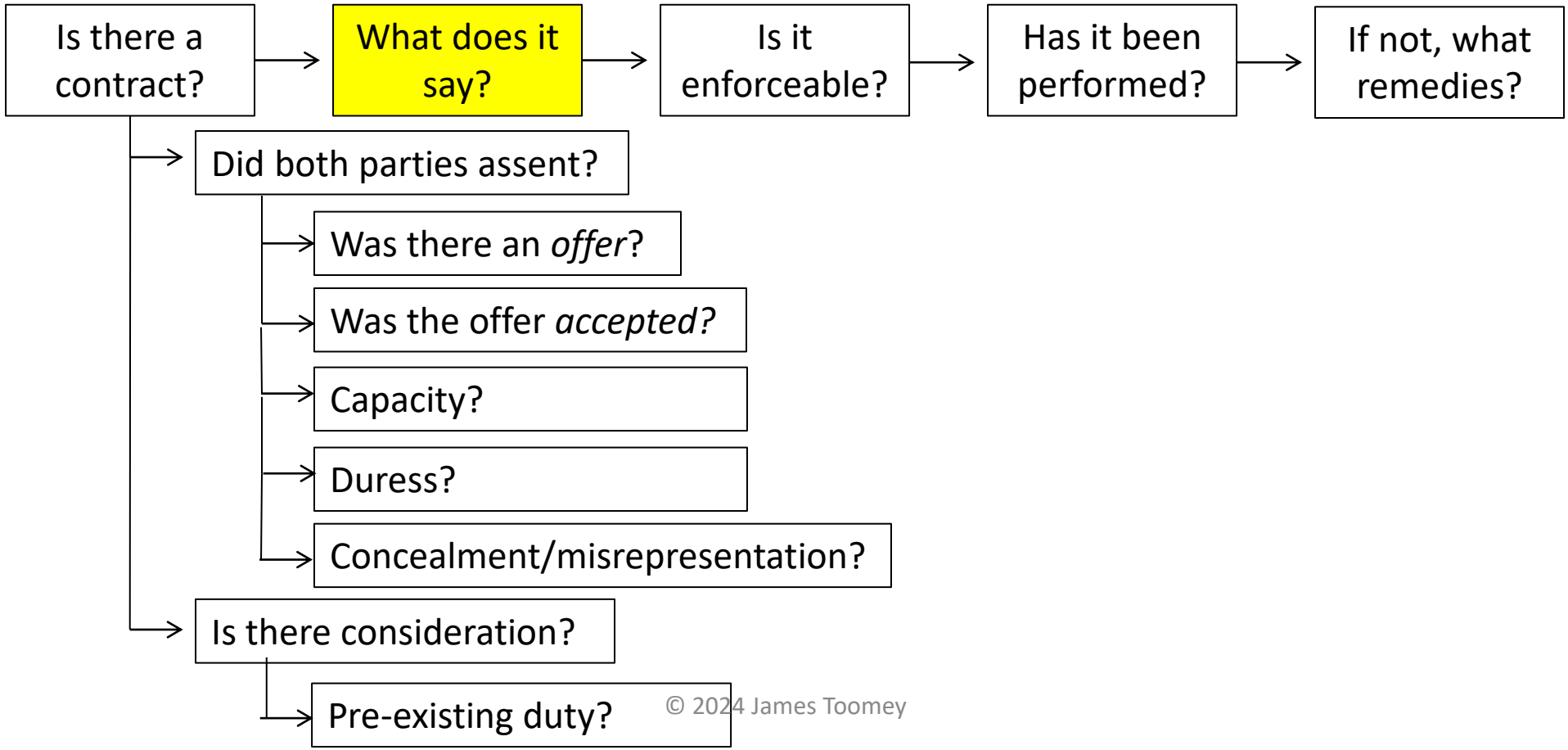
Greenfield v. Philles Records—Takeaways

- NY sticks to the traditional understanding of the plain meaning rule
  - Extrinsic evidence only relevant to contract interpretation if text is initially found to be ambiguous

Class 12: Context and Ambiguity

Professor James Toomey

The Story of a Contract



Frigaliment Importing Co. v. B.N.S. International Sales Corp.

- Plaintiff—Swiss company
- Defendant—American poultry company
- Contract requires defendant provide plaintiff with "US Fresh Frozen Chicken, Grade A, Government Inspected, Eviscerated"
  - Of different weights at specified prices
- Defendant ships "stewing chicken"—lower quality chicken
- Plaintiff sues for breach, argues that contract required defendant to send "broilers"—higher quality chicken
- Question—does "chicken" (for purposes of the contract) require "broilers"?

Frigaliment Importing Co. v. B.N.S. International Sales Corp.

- Held—no; defendant not held in breach for sending stewing chicken
  - Plaintiff has not *carried burden* of showing "chicken" means "broilers"
- Objective theory of contract interpretation (*cf. Lucy v. Zehmer*)—"the making of a contract depends not on the agreement of two minds in one intention, but on the agreement of two sets of external signs."
- "Chicken" is ambiguous. Extrinsic evidence:
  - Plaintiff—stewing chicken doesn't come in larger size (contract requires two sizes)
  - Plaintiff—parties used English "chicken" in negotiations otherwise in German to refer specifically to broilers (disputed)
  - Plaintiff—"chicken" in this trade means "broilers"
    - Defendant—disputes this, and notes they are new to the trade
  - Defendant—contract refers to Department of Agriculture regulations, which define "chicken" broadly
  - Defendant—plaintiff's conduct after the first shipment suggested it was OK with stewing chicken (disputed)
  - Defendant—contract would have been unreasonably low for "broilers"

Frigaliment Importing Co. v. B.N.S. International Sales Corp.—Takeaways

- Review "plain meaning rule"—courts look to extrinsic evidence to interpret ambiguous terms
  - Generally guided by the "objective" meaning of terms, though this can be controversial
- Some kinds of extrinsic evidence
  - General use of language
  - Trade usage
  - Subsequent conduct

Restatement § 201. ***Whose Meaning Prevails.***

(1) Where the parties have attached the same meaning to a promise or agreement or a term thereof, it is interpreted in accordance with that meaning.

(2) Where the parties have attached different meanings to a promise or agreement or a term thereof, it is interpreted in accordance with the meaning attached by one of them if at the time the agreement was made

  (a) that party did not know of any different meaning attached by the other, and the other knew the meaning attached by the first party; or

  (b) that party had no reason to know of any different attached by the other, and the other had reason to know the meaning attached by the first party

UCC § 1-303. ***Course of Performance, Course of Dealing, and Usage of Trade***.

(a) A "course of performance" is a sequence of conduct between the parties to a particular transaction that exists if: (1) the agreement of the parties with respect to the transaction involves repeated occasions for performance by a party; and (2) the other party, with knowledge of the nature of the performance and opportunity for objection to it, acceptance the performance or acquiesces in it without objection.

(b) A "course of dealing" is a sequence of conduct concerning previous transactions between the parties to a particular transaction that is fairly to be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct.

(c) 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 must be proved as facts. If it is established that such a usage is embodied in a trade code or similar record, the interpretation of the record is a question of fact.

(d) A course of performance or course of dealing between the parties or a usage of trade in the vocation or trade in which they are engaged or of which they are or should be aware is relevant in ascertaining the meaning of the parties' agreement, may give particular meaning to specific terms of the agreement, and may supplement or qualify the terms of the agreement. A usage of trade applicable in the place in which part of the performance under the agreement is to occur may be so utilized as to that part of the performance.

(e) Except as otherwise provided . . . the express terms of an agreement and any applicable course of performance, course of dealing, or usage of trade must be construed whenever reasonable as consistent with each other. If such a construction is unreasonable: (1) express terms prevail over course of performance, course of dealing, and usage of trade; (2) course of performance prevails over course of dealing and usage of trade; and (3) course of dealing prevails over usage of trade.

(f) …

Hurst v. W.V. Lake & Co.

- Parties contract for horse meat "minimum 50% protein," with a discount if it ends up having less protein than that
- Plaintiff provides horse meat between 49.53% and 49.96% protein
- Defendant pays discounted price
- Plaintiff sues for breach of contract, arguing that there is a trade usage under which "minimum 50% percent protein" is understood to mean more than 49.5% protein
- Question—can the court hear extrinsic evidence of trade usage?

Hurst v. W.V. Lake & Co.

- Held—yes
- Trade usage can help *interpret* the words—help us understand what the words mean in a particular context
- Court unpersuaded by arguments about post-facto manipulation of terms
  - The goal is to understand what the parties actually meant or would reasonably have understood

Hurst v. W.V. Lake & Co.—Takeaways

- Trade usage can aid in interpreting contractual terms, even where they *appear* unambiguous on their face

Nanakuli Paving & Rock Co. v. Shell Oil Co.

- Nanakuli (paving company) has longstanding requirements contract with Shell for asphalt supplies
  - Written contract provides for price of asphalt to be "Shell's Posted Price at the time of delivery"
- After a substantial price increase, Shell bills at higher new price rather than old price, on which Nanakuli had relied in negotiating paving contracts that cannot be re-negotiated on grounds of supply price-increase
  - Nanakuli argues Shell had a duty to "price protect"—bill at initial price where Nanakuli has committed to do paving based on that price
    - Trade usage—price protection seems to be assumed in paving industry in Hawaii
    - Course of performance (Shell price protected twice before in their contract)
    - Good faith
- Question—did Nanakuli have a duty to "price protect," notwithstanding the express language of the contract?

Nanakuli Paving & Rock Co. v. Shell Oil Co.

- Held—yes
  - UCC supplants common law parol evidence rule and allows extrinsic evidence to "explain" and "supplement" contract terms
  - "Since the agreement of the parties is broader than the express terms and includes usages, which may even add terms to the agreement . . . we follow the Code's mandate to proceed on the assumption that the parties have included those usages unless they cannot reasonably be construed as consistent with the express terms."
  - Price protection isn't a "total negation" of pricing term, just an "exception at times of price increases"
- Trade usage, course of performance, and good faith point in the same direction here
  - Trade usage—price protection ubiquitous in this industry, and even if Shell didn't actually know (and was only engaged in one part of it), should have known, because they transact in the industry all the time
  - Course of performance—Shell price protected twice before, apparently on the view it had to. It was not "waiving" a right to charge the higher price that it thought it had
  - Good faith—given the trade understanding, Shell had a duty to price protect implied in the duty of good faith performance
    - Special Concurrence—this holding turns on the trade understanding; no general duty to price protect implied in the duty of good faith everywhere

Nanakuli Paving & Rock Co. v. Shell Oil Co.—Takeaways

- Trade usage & course of performance can "supplement or qualify"
  - So long as the alleged agreement can "reasonably be construed as consistent" with the express terms
  - Not a total or unambiguous contradiction
- Broad reliance on trade usage and course of performance evidence in interpreting contracts under the UCC

Raffles v. Wichelhaus

- Plaintiff and defendant have a contract for cotton, at a certain price, to arrive on a ship named *Peerless* to arrive from Bombay
- There are two ships named *Peerless*—one leaving in October and other in December.
- When December ship arrives, plaintiff wants defendant to take delivery and pay
- Defendant refuses, and says they meant the October-*Peerless*
- Question—is defendant required to accept cotton from December-*Peerless*?

Raffles v. Wichelhaus

- Held—no.
- (Apparently) *no contract*—no mutual assent.
  - Parties used the same words but meant different things. Neither had reason to know of the others meaning. No mutual assent; no contract.

Raffles v. Wichelhaus—Takeaways

- Ambiguity is not only a matter of contract interpretation—
  - If essential ambiguous term is understood by parties in different reasonable ways ("latent ambiguity"), there may be no contract at all

Restatement § 20. ***Effect of Misunderstanding***.

(1) There is no manifestation of mutual assent to an exchange if the parties attach materially different meanings to their manifestations and
   (a) neither party knows or has reason to know the meaning attached by the other; or
   (b) each party knows or each party has reason to know the meaning attached by the other.

(2) The manifestations of the parties are operative in accordance with the meaning attached to them by on of the parties if
   (a) that party does not know of any different meaning attached by the other, and the other knows the meaning attached by the first party; or
   (b) that party has no reason to know of any different meaning attached by the other, and the other has reason to know the meaning attached by the first party.

Colfax Envelope Corp. v. Local No. 458-3m

- Colfax Envelope has a few employees manning 78-inch printers, governed by periodically re-negotiated agreement between trade association and general printers' union
- In past years, agreement has required 4 employees for 78 inch printers
- This year, summary of agreement says "4C 60 Press-3 men"
  - And President of Colfax told that he would "really like" changes
- Colfax thinks this means printers *more than* 60" only need 3 employees. He agrees. Later full agreement contains a typo supporting this interpretation
- Later corrected agreement clarified that printers *under* 60" could have 3 employees, but more required 4
- Colfax argues there is no contract. Union argues that Colfax agreed to summary as contract (which at least requires arbitration)
- Question—is there no contract? Or can Colfax be compelled to arbitrate interpretation question?

Colfax Envelope Corp. v. Local No. 458-3m

- Held—parties have a contract; Colfax to arbitration.
- If parties agree to an *obviously* ambiguous term, they agree to that term being interpreted by the court (not reserving a power to back out if the other party has a different meaning)
  - "4C 60 Press-3 men" is *obviously* ambiguous.
  - "Colfax had a right to *hope* that its interpretation would prevail but it had no right to accept the offer constituted by the summary on the premise that either its interpretation was correct or it could walk away from the contract."
- *Contra Raffles*—no reason there for the parties to have known the contract was ambiguous ("latent" vs. "patent" ambiguity)

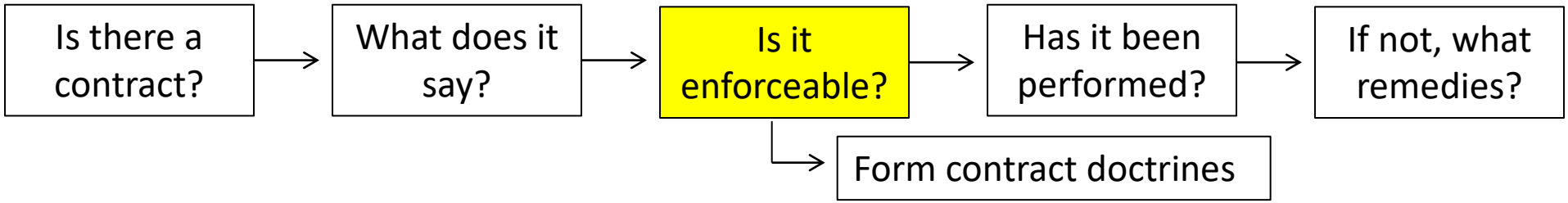
Colfax Envelope Corp. v. Local No. 458-3m—Takeaways

- If party agrees to a contract with an obviously ("patently") ambiguous term, *Raffles*/§20(1) is not an escape

Class 13: Form Contracts

Professor James Toomey

The Story of a Contract



O'Callaghan v. Waller & Beckwith Realty Co.

- O'Callaghan signs a form lease provided by landlord
  - Lease includes an "exculpation clause" disclaiming liability for any negligence in maintaining the premises
- O'Callaghan injures herself on property and sues for negligence
- Question—is the exculpatory clause in the form contract enforceable?

O'Callaghan v. Waller & Beckwith Realty Co.

- Held—yes
- Background principle of freedom of contract—"The use of a form contract does not itself establish disparity of bargaining power."
  - Not a public relationship
  - Functioning market
  - Allow contracting for lower rents
  - Legislative question

O'Callaghan v. Waller & Beckwith Realty Co.—Dissent

- Exculpatory clause unenforceable as against public policy
  - Disparity in bargaining power
  - Courts have a role in declining to enforce contractual provisions against public policy

O'Callaghan v. Waller & Beckwith Realty Co.—Takeaways

- Enforcing provisions in form contracts is controversial and different courts take different approaches. Particularly challenging when—
  - Provision would relieve liability or is otherwise one-sided in a defendant's favor
  - Particularly acute disparity of bargaining power
- Form leases (and other consumer contracts) also often regulated by statute or regulation today

Graham v. Scissor-Tail

- Bill Graham (promoter) and Scissor-Tail (music agent) have a contract dispute involving Leon Russell's tour
  - Form contract, required by the American Federation of Musicians, includes an arbitration clause
- Question—is the arbitration clause enforceable as a clause in the form contract?

Graham v. Scissor-Tail

- Held—yes (but unenforceable on other grounds—unconscionable)
  - Court describes contract as "contract of adhesion"—"a standardized contract, which, imposed and drafted by the party of superior bargaining strength, relegates to the subscribing party only the opportunity to adhere to the contract or reject it."
- Provisions of contracts of adhesion will not be enforced where—
  - They "do[] not fall within the reasonable expectations of the weaker or 'adhering' party"
  - They are unconscionable
- There is evidence that in fact Graham knew about the provision

Graham v. Scissor-Tail—Takeaways

- "Reasonable expectations" doctrine—probably the most common way courts consider enforceability of provisions in form contracts
  - If a provision falls outside the "reasonable expectations" of the party signing the form contract, it generally will not be enforced

Restatement § 211. ***Standardized Agreements.***

(1) Except as stated in Subsection (3), where a party to an agreement signs or otherwise manifests assent to a writing and has reason to believe that like writings are regularly used to embody terms of agreements of the same type, he adopts the writing as an integrated agreement with respect to the terms included in the writing.

(2) Such a writing is interpreted wherever reasonable as treating alike all those similarly situated, without regard to their knowledge or understanding of the standard terms of the writing.

(3) Where the other party has reason to believe that the party manifesting such assent would not do so if he knew that the writing contained a particular term, the term is not part of the agreement.

Doe v. Great Expectations

- Doe and Roe pay for Great Expectations dating service
  - Contract does not set them up with anyone specifically; puts their profile up on website
  - Costs more than $25
  - Doe and Roe never provided with the “Bill of Rights” dating services are required to provide
- Doe and Roe sue Great Expectations under New York Dating Services Law
- Question—is Great Expectations liable, and for how much?

Doe v. Great Expectations

- Held—Great Expectations liable
  - Dating Services law applies to profile-sharing companies
  - Must guarantee clients will be set up with a certain number of people
  - Must provide Bill of Rights
  - Doe and Roe entitled to full "actual damages"—restitution
  - Great Expectations referred to executive authorities

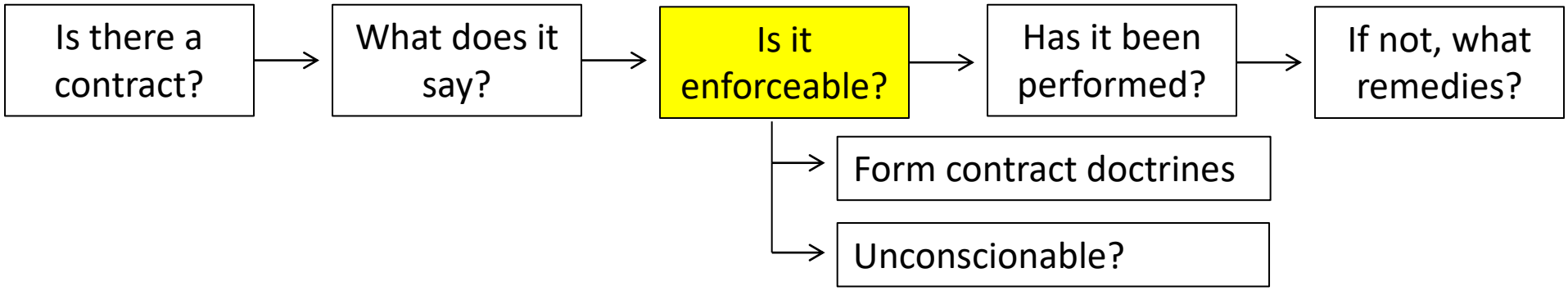
Doe v. Great Expectations—Takeaways

- Much consumer protection law with respect to form contracts covered by statute
  - Which often provide private causes of action with civil penalties as an alternative to damages

Class 14: Unconscionability

Professor James Toomey

The Story of a Contract



Restatement § 208. ***Unconscionable Contract or Term.***

If a contract or term thereof is unconscionable at the time the contract is made a court may refuse to enforce the contract, or may enforce the remainder of the contract without the unconscionable term, or may so limit the application of any unconscionable term as to avoid any unconscionable result.

UCC § 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 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.

Two Ways of Thinking About Unconscionability

- ***Procedural*** unconscionability—some unfairness or defect in the bargaining process
  - That doesn't fall into the traditional categories of duress, fraud, etc.
  - But courts have long policed with equitable powers
- ***Substantive*** unconscionability—term in contract, however arrived at, simply goes too far and is unfair
  - *Much* more controversial than procedural unconscionability
- This distinction is more descriptive than legal
  - Both kinds have the same legal effect (invalidate contract/term)
  - And often, contracts found unconscionable implicate aspects of both

Williams v. Walker-Thomas Furniture Co.

- Walker-Thomas Furniture Co. sells furniture on credit, and the contract purports to permit it to repossess everything a particular buyer has purchased for default on the amount owed on any piece of furniture
- Williams is a poor woman who purchased, among other things, a stereo set from Walker-Thomas, defaulted, and Walker-Thomas is trying to repossess all goods it has sold her
- Question—is the Walker-Thomas credit payment structure unconscionable?

Williams v. Walker-Thomas Furniture Co.

- Held—yes; contract unconscionable
- "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."
  - "[W]hether the terms are 'so extreme as to appear unconscionable according to the mores and business practices of the time and place'"
- Court finds that Walker-Thomas knowingly took advantage of Williams's financial situation, getting her to "agree" to unfair terms with little real choice

Williams v. Walker-Thomas Furniture Co.—Dissent

- Condemns Walker-Thomas's business practices but would defer to Congress for resolution
  - "There are many aspects of public policy here involved."

Williams v. Walker-Thomas Furniture Co.—Takeaways

- Unconscionability can void contracts or terms. Look for:
  - "Gross" inequality of bargaining power
  - Lack of real choice
  - Terms hidden in contract
  - Inability on the part of one party to see or understand the terms
  - Deceptive sales practices
  - Characteristics of the "weaker" party and "stronger" party's knowledge
- Controversial whether courts are good at/ought to be engaged in the kind of policy reasoning unconscionability doctrine often relies on

Stoll v. Xiong

- Stoll sells farm to immigrants Xiong and Yang, who have limited fluency in English
  - Basic headline terms—$130,000 for 60 acres; that's $2,000/acre plus $10,000 for Stoll building an access road
  - Paragraph 10—"Buyers shall be obligated to construct a poultry litter shed on the property . . . Buyer shall place the litter from their poultry houses in the litter shed at the end of the growing cycle. Seller shall have all rights to the litter for a period of 30 years from the date of closing. Seller shall empty the litter shed completely between growing cycles so that the shed will be available for use by Buyers as needed."
- Stoll put Paragraph 10 in the contract; Xiong and Yang testify they did not know about it
- Chicken litter is very valuable
- Question—is Paragraph 10 enforceable or unconscionable?

Stoll v. Xiong

- Held—unconscionable
- "An unconscionable contract is one which no person in his senses not under delusion would make, on the one hand, and which no fair and honest man would accept on the other. The basic test of unconscionability of a contract is whether under the circumstances existing at the time of the making of the contract, and in light of the general commercial background and commercial need of a particular case, clauses are so one-sided as to oppress or unfairly surprise one of the parties."
  - "[N]o fair and honest person would propose and no rational person would enter into a contract containing a clause imposing a premium for land and which, without any consideration to them, imposes additional costs in the hundreds of thousands over a thirty-year period that both are unrelated to the land itself and exceed the value of the land."

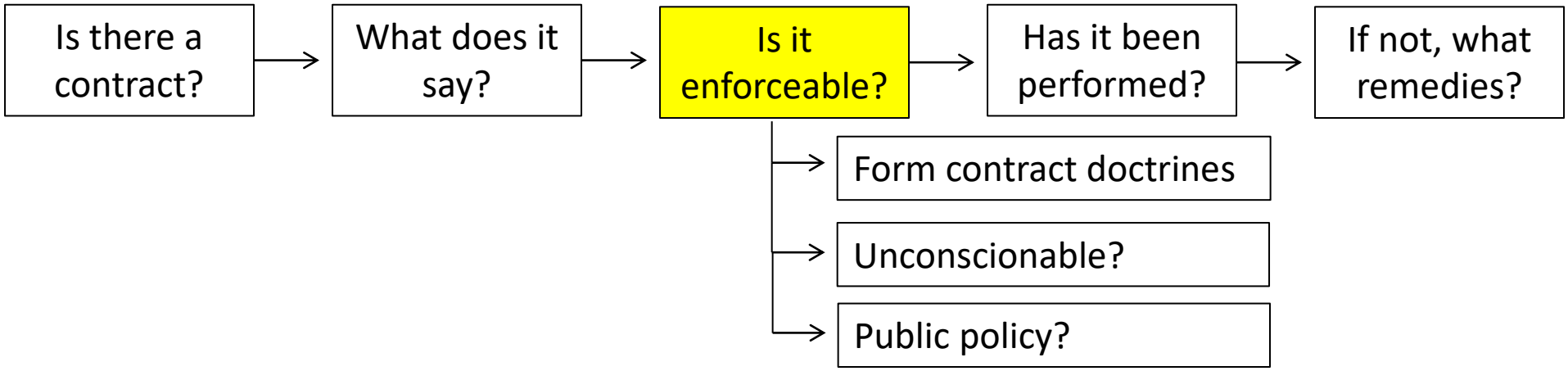
Stoll v. Xiong—Takeaways

- In extreme cases, dramatic mismatch of consideration can render a contract or term unconscionable
  - More likely where there are irregularities in bargaining that, although they do not neatly fit into doctrines like misrepresentation, undue influence, capacity, etc., resemble those doctrines

Class 15: Public Policy

Professor James Toomey

The Story of a Contract



Two Categories of Public Policy Constraints

- Illegal contracts
  - Contracts that are illegal to perform
  - Contracts tied up with illegal activity (*Blossom*)
- Contracts against public policy
  - Policy derived from statute (*Sheets*; *Baby M*)
  - Judicial policy (*Sheets*; *Baby M*)

Blossom Farm Products Co. v. Kasson Cheese Co.

- Kasson is purchasing Isokappacase from Blossom
  - In small quantities, Isokappacase can be used legally to make cheese
  - In large quantities, isokappacase creates what must be labeled as “imitation cheese” under federal regulations
- Kasson is using isokappacase in large quantities and selling it as “real cheese” (this is illegal)
- Kasson refuses to pay for final shipment of isokappacase. Blossom sues for breach of contract.
- Question—is this contract void as an illegal contract?

Blossom Farm Products Co. v. Kasson Cheese Co.

- Held—yes; illegal contract
- Blossom *knowingly facilitated* Kasson's illegal behavior
  - "If the conduct to be engaged in by the promisor is deemed improper conduct because it is against public policy, the promisee's doing of specific acts to facilitate the improper use is a bar to recovery."
- Parties *in pari delicto* (equal fault)—let the losses lie where they have fallen

Blossom Farm Products Co. v. Kasson Cheese Co.—Takeaways

- Contracts can be void as illegal even where performance is not itself illegal, so long as the contract is intimately tied up with illegal activity
  - Totality of the circumstances inquiry
  - Look for knowing facilitation of illegal conduct
- *In pari delicto*/unclean hands—courts are reluctant to enforce contracts where both parties are at fault, which can give one party but not the other the benefit of the bargain

Restatement § 182. ***Effect of Performance if Intended Use is Improper.***

If the promisee has substantially performed, enforcement of a promise is not precluded on grounds of public policy because of some improper use that the promisor intends to make of what he obtains unless the promisee

(a) acted for the purpose of furthering the improper use, or

(b) knew of the use and the use involves grave social harm.

Restatement § 178. ***When a Term is Unenforceable on Grounds of Public Policy***

(1) A promise or other term of an agreement is unenforceable on grounds of public policy if legislation provides that it is unenforceable or the interest in its enforcement is clearly outweighed in the circumstances by a public policy against the enforcement of such terms.

(2) In weighing the interest in the enforcement of a term, account is taken of

  (a) the parties' justified expectations,

  (b) any forfeiture that would result if enforcement were denied, and

  (c) any special public interest in the enforcement of a particular term.

(3) In weighing a public policy against enforcement of a term, account is taken of

  (a) the strength of that policy as manifested by legislation or judicial decisions,

  (b) the likelihood that a refusal to enforce the term will further that policy,

  (c) the seriousness of any misconduct involved and the extent to which it was deliberate, and

  (d) the directness of the connection between that misconduct and the term.

Restatement § 179. ***Bases of Public Policies Against Enforcement.***

A public policy against the enforcement of promises or other terms may be derived by the court from

(a) legislation relevant to such a policy, or

(b) the need to protect some aspect of the public welfare, as is the case for the judicial policies against, for example

(i) restraint of trade,

(ii) impairment of family relations, and

(iii) interference with other protected interests.

Sheets v. Teddy's Frosted Foods

- Sheets is an at-will employee (quality control manager -> operations manager) at Teddy's Frozen Foods
  - Sheets raises issues of deviation from CT state food regulations to Teddy's management
  - Teddy's fires him a few weeks later for "unsatisfactory performance"
- Sheets sues Teddy's for tort of wrongful discharge
- Question—can an at-will employee state a claim for wrongful discharge in retaliation for raising unlawful conduct to employer?

Sheets v. Teddy's Frosted Foods

- Held—yes; exception to at-will for wrongful discharge in these circumstances
- "The argument that contract rights which are inherently legitimate may yet give rise to liability in tort if they are exercised improperly is not a novel one."
- Other cases where at-will employees have been permitted to bring wrongful discharge claims, retaliation for
  - Refusing to commit perjury
  - Filing a workmen's comp. claim
  - Engaging in union activity
  - Performing jury duty
- Court derives public policy from CT Food, Drug, and Cosmetics Act
- Suggests that this is a narrow exception—it matters that he was Quality Control Manager

Sheets v. Teddy's Frosted Foods—Dissent

- At-will employees can be fired for any or no reason
- Courts role in policing contracts for public policy is limited to *direct violations of statutes*
- Dissent skeptical of majority's framing of the facts—
  - The alleged violations were not very serious
  - Sheets may be fabricating them
  - Sheets could have anonymously notified the authorities

Sheets v. Teddy's Frosted Foods—Takeaways

- Most courts have read "public policy" exceptions into at-will employment contracts
  - Prohibiting employers from terminating at-will employees in retaliation for certain conduct (usually reporting or refusing to participate in illegal activity)
- Scope of these exceptions, and their relationship to statutory employment/whistleblower protections, is controversial

In the Matter of Baby M

- William Stern (married to Elizabeth Stern) enters into "commercial surrogacy contract" with Mary Beth Whitehead
  - Whitehead is to be artificially inseminated with William's semen
  - Carry to term a baby genetically the child of William and herself
  - And immediately surrender parental rights upon child's birth to William and Elizabeth Stern
  - In exchange for $10,000
- Upon "Baby M's" birth, Whitehead refuses to surrender parental rights and attempts to keep baby
- William sues for breach of contract
- Question—is this "commercial surrogacy contract" enforceable?

In the Matter of Baby M

- Held—no; commercial surrogacy contracts unenforceable under New Jersey law as a matter of public policy
- Two sources of policy—
  - Policy derived from statutes
    - Paid private adoption ("baby selling") is illegal in NJ
    - Contract violates "laws requiring proof of parental unfitness or abandonment before termination of parental rights"
    - And "laws that make surrender of custody and consent to adoption revocable in private placement adoptions"
  - Judicial/general principles of public policy
    - *Money* cannot be used in this context
      - Coercive
      - Corrosive—"There are, in a civilized society, some things that money cannot buy."
    - Degrading to women—"dignity"
    - Bad for children

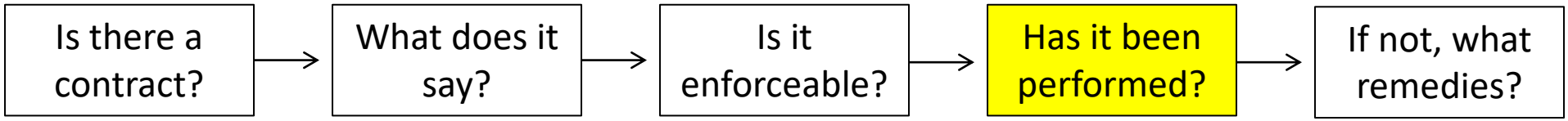
In the Matter of Baby M—Takeaways

- Common law courts retain prerogative to decline to enforce contracts on public policy grounds
  - Controversial the extent to which this power must be tied to specific statutory law
- Enforcement of commercial surrogacy contracts is *extremely* controversial
  - Many jurisdictions disagree with *Baby M*, but still good law in NJ
  - Active area of statutory reform
  - Raises questions of the fundamentals of contract law (promise, assent, consideration) and bioethics (dignity, the role of money, the value of genetic relationships)

Class 16: Substantial Performance and Breach

Professor James Toomey

The Story of a Contract



Breach After Performance

- "Breach"—*any* deviation from behavior promised in contract. ***After*** performance, ask:
  - *Condition* ("performance to be exchanged under an exchange of promises")
    - Breach may relieve other party of obligations conditional on that performance
  - *"Duty"* ("duty under a promise of which the injured party's promise is independent")
    - Breach gives rise to ***damages*** in breach of contract action, but so long as there has been ***substantial*** performance, ***does not*** relieve other party of performance

Jacob & Youngs v. Kent

- Contract for construction of a house for $77,000, paid in installments
  - "all wrought iron pipe must be well galvanized, lap welded pipe of the grade known as 'standard pipe' of Reading manufacture"
- House constructed, but 50%-66% of pipe used was not Reading pipe—"same in quality, in appearance, in market value, and in cost"
- A year after living in the house, defendant discovers pipe non-compliance, and refuses to keep paying
- Construction company sues for payment of the remaining contract price
- Three questions—
  - Was this really a breach of contract?
  - If so, was it a *condition*? (relieving defendant of obligation to pay)
  - If not, what is the measure of damages?

Jacob & Youngs v. Kent

- Was there a breach?
  - Yes—"The courts never say that one who makes a contract fills the measure of his duty by less than full performance."
  - Contract calls for Reading pipe; performance did not use Reading pipe
- Was the use of Reading pipe a condition of payment?
  - No—"Considerations partly of justice and partly of presumable intention are to tell us whether this or that promise shall be placed in one class or another."
- What is the measure of damages?
  - *Not* cost of repair—doctrine of ***substantial performance***—"The rule that gives a remedy in cases of substantial performance with compensation for defects of trivial or inappreciable importance has been developed by the courts as an instrument of justice."
  - Breach here was both ***innocent*** and ***trivial***
  - "In the circumstances of this case, we think the measure of the allowance is not the cost of replacement, which would be great, but the difference in value, which would be either nominal or nothing."

Jacob & Youngs v. Kent—Dissent

- "The defendant had a right to contract for what he wanted. He had a right before making payment to get what the contract called for."
  - "What his reason was for requiring this kind of pipe is of no importance. He wanted it and was entitled to it."
- Using Reading pipe *was* a condition of payment
  - Defendant is entitled to withhold payment until plaintiff repairs (or can sue for breach)
- Defendant is entitled to be put in the actual position he would have been in had the contract been performed, and majority's damages measure does not do that

Jacob & Youngs v. Kent—Takeaways

- Breach of duties that are not conditions compensated for with damages; they do not relieve the other party of obligation
  - Whether a requirement is a "duty" or a "condition" is a question "partly of justice and partly of presumable intention"
  - Consider adjustment of damage measurement where breach of non-conditional duty is ***trivial*** and ***innocent***, and where cost of repair greatly outweighs diminution of value
  - Usual expectation damages are cost of repair, but diminution of value is an alternative metric

Breach During Performance ("Restatement Analysis")

- Is there a breach?
  - Y: Is the breach as to a duty of performance that was part of an exchange of promises (i.e., a "condition")?
    - Y: Is the breach to a performance that was to take place before that of the aggrieved party?
      - Y: Was the breach ***material***?
        - » Y: ***Choice***—treat breach as ***total*** and suspend performance; ***or*** treat breach as ***partial***, continue performance and sue for damages
          - ***Note***—treating breach as total is itself a material breach justifying other party in suspending performance. (If aggrieved party was wrong about materiality of breach, they have now materially breached the contract themselves).
        - » N: Breach is ***partial***, keep performing but can sue for damages
      - N: Keep performing, but can sue for damages
    - N: Keep performing, but can sue for damages
  - N: Keep performing

Restatement § 232. ***When It Is Presumed That Performances Are to Be Exchanged Under an Exchange of Promises.***

Where the consideration given by each party to a contract consists in whole or in part of promises, all the performances to be rendered by each party taken collectively are treated as performances to be exchanged under an exchange of promises, unless a contrary intention is clearly manifested.

Restatement § 241. ***Circumstances Significant in Determining Whether a Failure is Material.***

In determining whether a failure to render or to offer performance is material, the following circumstances are significant:

(a) the extent to which the injured party will be deprived of the benefit which he reasonably expected;

(b) the extent to which the injured party can be adequately compensated for the part of that benefit of which he will be deprived;

(c) the extent to which the party failing to perform or to offer to perform will suffer forfeiture;

(d) the likelihood that the party failing to perform or to offer to perform will cure his failure, taking account of all the circumstances including any reasonable assurances;

(e) the extent to which the behavior of the party failing to perform or to offer to perform comports with standards of good faith and fair dealing.

Walker & Co. v. Harrison

- Walker & Co. leases a billboard to Harrison (laundromat) for 36 months, at specified rent
  - "Lessor at his expense agrees to maintain and service the sign together with such equipment as supplied and installed by the lessor to operate in conjunction with said sign under the terms of this lease; this service is to include cleaning and repainting of sign in original color scheme as often as deemed necessary by lessor to keep sign in first class advertising condition and make all necessary repairs to sign and equipment installed by lessor."
- "[S]hortly after the sign was installed, someone hit it with a tomato. Rust, also, was visible on the chrome . . . and in its corners were 'little spider cobwebs.' In addition, there were some children's sayings written down there."
- Harrison repeatedly calls Walker & Co., who ignores him.
  - Follows up with telegraph—"You have continually voided our rental contract by not maintaining signs as agreed as we no longer have a contract with you do not expect any further remuneration."
- Walker sues for breach of contract under acceleration clause that makes the full balance of rental payments due upon breach
- Question—was Walker's breach ***material***?

Walker & Co. v. Harrison

- Held—no; Walker's breach not material. Therefore, Harrison is in breach for failure to pay/repudiation.
- "[R]epudiation is one of the weapons available to an injured party in the event the other contractor has committed a material breach."
  - "But the injured party's determination that there has been material breach, justifying his own repudiation, is fraught with peril, for should such determination, as viewed by a later court in calm contemplation, be unwarranted, the repudiator himself will have been guilty of material breach and himself have become the aggressor, not an innocent victim."
- Multi-factorial test—at the end of the day "when a tomato has been splashed all over your clock, you don't like it. But . . . I really can't find that that was such a material breach of the contract as to justify rescission."

Walker & Co. v. Harrison—Takeaways

- The victim of a material breach may terminate their own performance.
- ***But*** this is a risky path, because if a court disagrees that the breach was material, the terminating party is themselves in material breach.
- Whether a breach is material is a multi-factorial test—
  - "The extent to which the injured party will obtain the substantial benefit which he could have reasonably anticipated"
  - "The extent to which the injured party may be adequately compensated in damages for lack of complete performance"
  - "The extent to which the party failing to perform has already partly performed or made preparation for performance"
  - "The greater or less hardship on the party failing to perform in terminating the contract"
  - "The willful, negligent, or innocent behavior of the party failing to perform."
  - "The greater or less uncertainty that the party failing to perform will perform the remainder of the contract"

K&G Construction Co. v. Harris

- K&G is general contractor; Harris sub.
  - Sub accidentally bulldozes contractor's house
    - Refuses to fix or pay damage, as does insurer
  - Sub submits monthly invoice
  - General refuses to pay until sub fixes house
  - Sub works a little more and then refuses to work until paid
  - General hires another sub who completes work for $450 more than initial sub would have
- K&G sues Harris, seeking $450 as expectation damages. Harris countersues for amount owed under submitted invoice & lost profits.
- Question—who gets damages here?
  - "Did the contractor have a right, under the circumstances, to refuse to make the progress payment due on August 10, 1958?"

K&G Construction Co. v. Harris

- Held—general gets expectation damages; had a right to terminate contract after material breach
- Was there a breach?
  - Yes, “when the subcontractor’s employee negligently damaged the contractor’s wall, this constituted a breach of the subcontractor’s promise to perform his work in a workmanlike manner”
  - Was this a promise part of an exchange of promises?
    - Yes—presumption that monthly payments dependent on care and quality of work.
    - Did this breach go to performance that was supposed to happen before performance by K&G?
      - Yes—payment supposed to be for work completed
      - Was this breach material?
        - » Yes—”[T]here can be little doubt that the breach was material: the damage to the wall amounted to more than double the payment due on August 10.”
        - » Does K&G treat this breach as total or partial?
          - Partial—invites sub to continue performance if they fix the house
          - But then sub totally breaches the contract by refusing to continue
- Bottom line—sub breached contract, general gets $450 expectation damages

K&G Construction Co. v. Harris—Takeaways

- A case study in applying the "Restatement analysis" for breach in the course of performance
- Find where the contract was totally breached/repudiated and work backwards to whether that was justified

New England Structures v. Loranger

- Loranger (general) has a lot of issues with New England Structure's (sub) work on roof of school project
  - Loranger to New England—"Because of your repeated refusal or inability to provide enough properly skilled workmen to maintain satisfactory progress, we terminated your right to proceed with work at the school . . . In accordance with Article 5 of our contract"
- Factual disputes over breach goes to court—Loranger has a lot of problems with New England
- Question—having blamed New England's breach initially on lack of workmen, can Loranger raise other ways in which New England breached in court?

New England Structures v. Loranger

- Held—yes
- “Our cases . . . require reliance or change of position based upon the assertion of the particular reason or defense before treating a person, giving one reason for his action, as estopped later to give a different reason.”

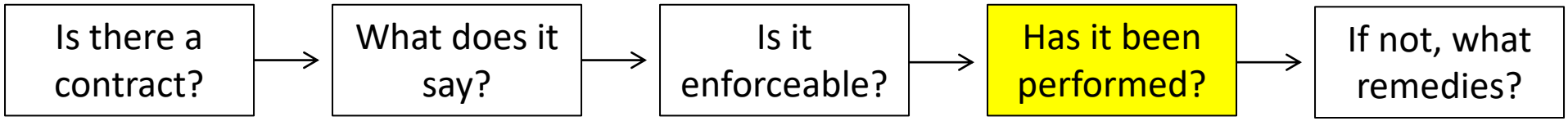
New England Structures v. Loranger—Takeaways

- Asserting specific grounds for breach *can* later confine evidence of breach to those grounds
- But courts are relatively sympathetic to new grounds of breach, especially if there hasn't been reliance or the evidence supporting the theory is new

Class 17: Mistake

Professor James Toomey

The Story of a Contract



Restatement § 151. ***Mistake Defined.***

A mistake is a belief that is not in accord with the facts.

Restatement § 152. ***When Mistake of Both Parties Makes a Contract Voidable.***

(1) Where a mistake of both parties at the time a contract was made as to a basic assumption on which the contract was made has a material effect on the agreed exchange of performances, the contract is voidable by the adversely affected party unless he bears the risk of mistake under the rule stated in § 154.

(2) In determining whether the mistake has a material effect on the agreed exchange of performances, account is taken of any relief by way of reformation, restitution, or otherwise.

Restatement § 154. ***When a Party Bears the Risk of Mistake.***

A party bears the risk of mistake when

(a) the risk is allocated to him by agreement of the parties, or

(b) he is aware, at the time the contract is made, that he has only limited knowledge with respect to the facts to which the mistake relates but treats his limited knowledge as sufficient, or

(c) the risk is allocated to him by the court on the ground that it is reasonable in the circumstances to do so.

Stees v. Leonard

- Defendants contract to construct building on plaintiff's lot
- Land is waterlogged, and defendants twice construct up to three stories before it collapses
- Defendants refuse to keep trying; plaintiffs sue for breach of contract
- Question—can defendants be relieved of contractual duties on grounds of mutual mistake?

Stees v. Leonard

- Held—defendants held to contract; "mistake" not a defense
- "If a man bind himself, by a positive, express contract, to do an act in itself possible, he must perform his engagement, unless prevented by the act of God, the law, or the other party to the contract."
  - "No hardship, no unforeseen hindrance, no difficulty short of absolute impossibility, will excuse him from doing what he has expressly agreed to do."
- Court awards (on plaintiff's demand) more like reliance rather than expectation damages

Stees v. Leonard—Takeaways

- Mutual mistake defense requires showing one party did not contract to bear the risk
  - Courts historically have been skeptical of mistake defenses

Renner v. Kehl

- Renner, looking to grow jojoba, contracts to buy tract of undeveloped land from Kehls. Both parties know Renner's plan and think the land is good for jojoba.
- After making a down payment and getting ownership of land, Renner drills test wells, and discovers there is insufficient groundwater for jojoba.
- Renner sues for rescission
- Question—can Renner be relieved of contractual obligations on grounds of mutual mistake?

Renner v. Kehl

- Held—yes; contract can be rescinded
- "[A] contract maybe rescinded when there is a mutual mistake of material fact which constitutes an essential part of the condition of the contract."
  - Remedy—rescission; restitution on both sides

Renner v. Kehl—Takeaways

- Rescission available for mutual mistake
  - Both parties
  - Make a mistake about a basic assumption
  - Which has a material effect on the agreed exchange of performances

Restatement § 153. ***When Mistake of One Party Makes a Contract Voidable.***

Where a mistake of one party at the time a contract was made as to a basic assumption on which he made the contract has a material effect on the agreed exchange of performances that is adverse to him, the contract is voidable by him if he does not bear the risk of the mistake under the rule stated in § 154, and

(a) the effect of the mistake is such that enforcement of the mistake would be unconscionable, or

(b) the other party had reason to know of the mistake or his fault caused the mistake.

Sumerel v. Goodyear Tire & Rubber Co.

- Plaintiff's attorneys win judgment against Goodyear, and are finalizing damages award
  - Jury held Goodyear only partially liable
- Goodyear's attorney sends email—"Here are our charts providing the numbers that Goodyear believes are appropriate. Please review these, then let's discuss."
  - Figures in charts mistakenly calculated as though Goodyear were fully liable
- Plaintiff's attorneys notice mistake
  - But purport to "accept" the "offer" by calling someone else at Goodyear
- Goodyear discovers error shortly before the documents are finalized. Plaintiff's attorneys insist they will hold Goodyear to higher price.
- Question—can plaintiff's attorneys hold Goodyear to mistakenly high damages figures?

Sumerel v. Goodyear Tire & Rubber Co.

- Held—no; no contract because no offer.
  - Not sufficiently definite, says "please review these, then let's discuss"
- In the alternative, contract is voidable because of Goodyear's unilateral mistake
  - "There is practically universal agreement that, if the material mistake of one party was known by the other or was of such character and accompanied by such circumstances that the other had reason to know of it, the mistaken party has the power to avoid the contract."
  - Mistake went to a basic assumption of the contract; had material effect on agreed exchange; and (at least) plaintiff's attorneys had reason to know of it

Sumerel v. Goodyear Tire & Rubber Co.—Takeaways

- Unilateral mistake requires:
  - One party to have made
  - A mistake about a basic assumption
  - Which has a material effect on the agreed exchange of performances
  - And *either*—
    - Enforcement would be ***unconscionable***, or
    - The other party ***had reason to know of mistake***

Class 18: Impracticability

Professor James Toomey

Mineral Park Land v. Howard

- Mineral Park contracts with Howard to get gravel from Howard's land for use on a bridge project
  - Contract provides Mineral Park will get all gravel it needs from Howard's land
  - And pay 5 cents per cubic yard
- Mineral Park gets only about half of the gravel for the project from Howard
  - Remaining gravel was below waterline and not cost-effective for Mineral Park to collect
- Howard sues for breach, asking for damages of the 5 cents per cubic yard for all cubic yards Mineral Park ultimately used
- Question—can Mineral Park be excused on grounds of impracticability?

Mineral Park Land v. Howard

- Held—yes; contract for below-waterline gravel discharged
- "[W]here performance depends upon the existence of a given thing, and such existence was assumed as the basis of the agreement, performance is excused to the extent that the thing ceases to exist or turn out to be nonexistent."
  - "[D]etermining whether the earth and gravel were 'available,' we must view the conditions in a practical and reasonable way."

Mineral Park Land v. Howard—Takeaways

- ***Existing impracticability***—impracticability not known to the parties existing at the time they sign the contract *can* discharge obligation
  - Conceptual overlap with mistake ("In many of the cases that come under this Section, relief based on the rules relating to mistake . . . will also be appropriate." Restatement § 266 cmt. a)
  - *Mineral Park* is an outlier case where defendant relieved on grounds of existing impracticability, but probably wouldn't have succeeded on grounds of mistake
    - Cited more often in defendants' briefs than court opinions

Restatement § 266. ***Existing Impracticability or Frustration***

(1) Where, at the time a contract is made, a party's performance under it is impracticable without his fault because of a fact of which he has no reason to know and the non-existence of which is a basic assumption on which the contract is made, no duty to render that performance arises, unless language or circumstances indicate the contrary.

(2) . . .

Restatement § 261. ***Discharge by Supervening Impracticability.***

Where, after a contract is made, a party's performance is made impracticable without his fault by the occurrence of an event the non-occurrence of which was a basic assumption on which the contract was made, his duty to render that performance is discharged, unless the language or the circumstances indicate the contrary.

Taylor v. Caldwell

- Defendants contract to rent music hall to plaintiffs for the purpose of performances and fêtes on certain dates
- Music hall burns down after signing contract but before performances
- Plaintiffs sue defendants to recoup at least preparation and advertising costs
- Question—can defendants be held liable on contract after music hall burns down?

Taylor v. Caldwell

- Held—no; contract discharged by ***supervening impracticability*** (impossibility)
- "[I]n 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."
  - At least where there is no fault of the defendant

Taylor v. Caldwell—Takeaways

- ***Supervening impracticability***—the faultless later non-existence of a thing the existence of which was a basic assumption of the contract can discharge obligation
  - Codified in Restatement §§ 261; 263

Restatement § 263. ***Destruction, Deterioration or Failure to Come into Existence of Thing Necessary for Performance.***

If the existence of a specific thing is necessary for the performance of a duty, its failure to come into existence, destruction, or such deterioration as makes performance impracticable is an event the non-occurrence of which was a basic assumption on which the contract was made.

UCC § 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 to no longer 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.

UCC § 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.

Canadian Industrial Alcohol Co. v. Dunbar Molasses Co.

- Dunbar (distributor) has a contract with Alcohol Co.—
  - "approximately 1,500,000 wine gallons Refined Blackstrap (Molasses) of the usual run from the National Sugar Refinery"
- Refinery makes less molasses than anticipated, Dunbar delivers much less than 1,500,000 wine gallons
- Alcohol Co. sues Dunbar
- Question—can Dunbar be excused by Refinery's unanticipated underperformance?

Canadian Industrial Alcohol Co. v. Dunbar Molasses Co.

- Held—no
  - No implied term in contract between Dunbar and Alcohol Co. making performance depend on Refinery's output
  - Dunbar "put its faith in the mere chance that the output of the refinery would be the same from year to year"

Canadian Industrial Alcohol Co. v. Dunbar Molasses Co.—Takeaways

- "Implied term" defenses unlikely where contingency was reasonably foreseeable and the defendant could have avoided problem with proactive contracting
  - Consider "*force majeure*" clauses covering common causes of supply failures

Eastern Air Lines, Inc. v. Gulf Oil Corporation

- Eastern Air Lines has a contract with Gulf Oil for jet fuel supplies
  - Contract price based on "the average of posted prices for West Texas sour crude, posted in Platts Oilgram Service"
- As the result of OPEC oil embargo and US government regulations, the price for West Texas sour crude posted in Platts Oilgram Service is much lower than prevailing global crude prices
- Question—can Gulf be relieved of contractual obligations on ground of commercial impracticability?

Eastern Air Lines, Inc. v. Gulf Oil Corporation

- Held—no
  - UCC § 2-615 requires—
    - Hardship—"The party undertaking the burden of establishing 'commercial impracticability' by reason of allegedly increased raw material costs undertakes the obligation of showing the extent to which he has suffered, or will suffer, losses in performing his contract."
      - Because of Gulf's ability to transfer costs among subsidiaries, it is still making a profit overall, so no hardship
    - Unanticipated circumstances
      - Volatility in the middle east and government oil regulations "reasonably foreseeable"
      - The contract provides an unambiguous pricing mechanism nevertheless

Eastern Air Lines, Inc. v. Gulf Oil Corporation—Takeaways

- "Commercial impracticability" is a high bar. Look for—
  - Substantial hardship
  - From an unforeseeable event, for which the party seeking relief could not have feasibly contracted around initially

Class 19: Frustration of Purpose

Professor James Toomey

Krell v. Henry

- Henry signs a contract with Krell to rent rooms from which to watch coronation parade
- Coronation postponed due to King's illness
- Henry doesn't want rooms and refuses to pay
- Krell sues Henry for payment
- Question—can Henry avoid the contract because its essential purpose for him no longer exists?

Krell v. Henry

- Held—contract avoided; Henry not required to pay
- If the "substance of the contract . . . needs for its foundation the assumption of the existence of a particular state of affairs," and that state of affairs does not obtain, then contractual liability is relieved
  - Essential purpose of contract was to rent rooms *for the coronation*
  - Non-occurrence of the coronation was not foreseen or contracted for

Krell v. Henry—Takeaways

- ***Frustration of purpose***—if the contract was entered into for a specific, mutually understood purpose, which fails to occur, both parties may be relieved of contractual obligation

Restatement § 265. ***Discharge by Supervening Frustration.***

Where, after a contract is made, a party's principal purpose is substantially frustrated 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 remaining duties to render performance are discharged, unless the language or the circumstances indicate the contrary.

Swift Canadian Co. v. Banet

- Keystone Wool Pullers (Philadelphia) enters contract to purchase lamb pelts from Swift Canadian
  - "F.O.B. Toronto"
  - Neither party is liable for "orders or acts of any government or governmental agency"
  - "[W]hen pelts are sold F.O.B. seller's plant title and risk of loss shall pass to buyer when product is loaded on cars at seller's plant."
- Subsequent U.S. government regulations prohibit importation of lamb pelts
- Swift is ready to put pelts on train; Keystone says don't bother
- Swift sues for payment under the contract
- Question—can Keystone be discharged from contractual obligation?

Swift Canadian Co. v. Banet

- Held—no
  - *Even though* Keystone's purpose was frustrated by government regulation
  - It bore the risk from when Swift Canadian performed
    - And, as a matter of contract interpretation, Swift Canadian performed when it was ready to deliver the pelts to the shipper in Toronto—"title and risk of loss shall pass to buyer when product is loaded on cars at seller's plant"
  - "Even if the goods could not be imported into the United States under the then existing regulations, the rest of the world was free to the buyer, so far as we know, as destination for the shipment."

Swift Canadian Co. v. Banet— Takeaways

- Frustration of purpose generally requires the contract to become *valueless* (or near-valueless) to the payor
  - If a buyer's subjective goals for use of a product are frustrated, they are unlikely to be able to avoid the contract on frustration grounds if there are other valuable uses available

Chase Precast Corp. v. John J. Paonessa Co.

- Paonessa (general contractor) has contract with Chase (subcontractor) for concrete medians on highway project Paonessa is completing under contract with MA DPW
  - Paonessa's contract with DPW allows DPW to vary the work called for
- After protests, DPW doesn't want to use concrete medians on rest of project
- Paonessa tells Chase to stop making medians
- Chase sues Paonessa for anticipated profits on full order of medians
- Question—is Paonessa relieved of contractual obligation on grounds of DPW's revised order?

Chase Precast Corp. v. John J. Paonessa Co.

- Held—contract avoided on grounds of frustration of purpose
- Not impracticability, but very close conceptually
- Chase knew the purpose of the medians was for the DPW project
- "[E]ven if the parties were aware generally of the department's power to eliminate contract items, the judge could reasonably have concluded that they did not contemplate the cancellation for a major portion of the project of such a widely used item as concrete median barriers, and did not allocate the risk of such cancellation."

Chase Precast Corp. v. John J. Paonessa Co.—Takeaways

- In American law, frustration is understood as distinct from but closely related to impracticability
- If, for unanticipated reasons, the known purpose of a contractual exchange is defeated, the contract may be avoided

NIPSCO v. Carbon County Coal Co.

- NIPSCO (public utility) has a 20-year contract with Carbon County Coal
  - For specified amounts of coal
  - At prices calculated by an escalation mechanism in the contract
  - Contract has a *force majeure* clause—NIPSCO can stop taking delivery of coal "for any cause beyond [its] reasonable control . . . including but not limited to . . . orders or acts of civil . . . authority . . . which wholly or partly prevent . . . the utilizing . . . of the coal"
- The price NIPSCO is paying Carbon County by 1985 makes NIPSCO's electricity generation higher than the general market price
- NIPSCO wants to pass these costs to customers by raising the price of its electricity; consumers want the Indiana regulators to let them get electricity at cheaper prices from other sources
- Regulators say NIPSCO can only raise its prices to the extent it can't get electricity cheaper from other sources
- Question—can NIPSCO avoid its contractual requirement to buy and pay for coal from Carbon County?

NIPSCO v. Carbon County Coal Co.

- Held—no; no escape from contractual liability
- *Force majeure*?
  - Doesn't apply, NIPSCO not *prevented* from using coal
- Frustration/impracticability?
  - Contract allocated risk to NIPSCO, by building in a clear pricing mechanism on a 20-year commitment
  - Implied allocation of risk to buyer of price drops (corresponding allocation of risk to seller of price rise)

NIPSCO v. Carbon County Coal Co.— Takeaways

- Frustration (like mistake & impracticability) can only void a contract if the risk has not been allocated to the party seeking to avoid
- Pricing mechanisms on long-term contracts impliedly allocate risk of price drops to buyer; risk of price rises to seller

Class 20: Good Faith

Professor James Toomey

Restatement § 205. ***Duty of Good Faith and Fair Dealing.***

Every contract imposes upon each party a duty of good faith and fair dealing in its performance and its enforcement.

UCC § 1-203. ***Obligation of Good Faith.***

Every contract or duty within this Act imposes an obligation of good faith in its performance or enforcement.

UCC § 1-201. ***General Definitions.***

. . .

(19) “Good faith” means honesty in fact in the conduct or transaction concerned.

. . .

Dalton v. Educational Testing Service

- Brian Dalton took the SAT twice, scoring 410 points higher the second time
  - SAT administrator ETS investigated the disparity and determined there was “preliminary evidence of cheating” based on handwriting differences and suspects Dalton’s second test of impersonation
  - Dalton elects to respond under contract by providing additional information
    - Additional information supports that it was him at the second test, explains the disparity (sick during first test), and he has his own handwriting expert saying they are the same
- ETS ignores additional evidence and is focused solely on the handwriting issue
- Question—did ETS comply with its contractual obligations in good faith?

Dalton v. Educational Testing Service

- Held—no; breach for failing to perform in good faith
- "Implicit in all contracts is a covenant of good faith and fair dealing in the course of contract performance."
  - Contractually authorized discretion cannot be exercised arbitrarily or irrationally
- "ETS expressly framed the dispositive question as one of suspected impersonation. Because the statements from the classroom proctor and November test-takers corroborated Dalton's contention that he was present at and in fact took the November examination, they were relevant to this issue."
- Remedy—specific performance
  - *Not* releasing the November score, but considering the new evidence in good faith

Dalton v. Educational Testing Service—Takeaways

- Duty of good faith and fair dealing implied into contracts
  - A matter of contract interpretation?
  - A substantive, policy-based limit on contracting and performance?
- Duty of good faith doesn't require any particular outcome in using discretion; but requires genuine and open consideration

Northwest, Inc. v. Ginsburg

- Northwest Airlines cancels Platinum Elite status of Ginsburg on grounds of "abusing the program"
  - "abuse of the program . . . (including . . . improper conduct as determined by [Northwest] in its sole judgment may result in cancellation of the member's account"
  - Northwest Airlines accuses Ginsburg of repeatedly demanding compensation above their guidelines
- Ginsburg responds with a class action lawsuit alleging Northwest has breached duty of good faith and fair dealing
- Federal Airline Deregulation Act preempts state law, but doesn't preempt the content of private contracts
- Question—is the duty of good faith and fair dealing (under MN law) a state-imposed substantive principle or a presumption about parties' actual intent?

Northwest, Inc. v. Ginsburg

- Held—substantive, state-imposed limit on contracting
  - Therefore, this lawsuit is pre-empted
- Under Minnesota law, the duty of good faith and fair dealing
  - cannot be contracted out of, implied in every contract whatever they say
  - applies to all contracts except employment contracts (on policy grounds)

Northwest, Inc. v. Ginsburg— Takeaways

- There is a theoretical dispute across jurisdictions and commentators as to whether the duty of good faith is a substantive, state-imposed limit on contracting, or a presumption about the parties' intent. Consider—
  - Whether parties can contract out of the duty
  - Whether it is justified on policy grounds
- This theoretical dispute can have real implications in pre-emption cases

Market Street Associates v. Frey

- Market Street Associates has a contract with General Electric Pension Trust
  - Paragraph 34 says that Pension Trust will give "reasonable consideration" to Market Street's requests for additional financing for improvements
  - If Pension Trust does not give such consideration, Market Street is permitted to buy financed property for less than market value
- Timeline—
  - Orenstein (Market Street) sends letter to Erb (Pension Trust) with formal proposal for $4 million in financing
  - Erb is slow to respond but eventually rejects the proposal on the grounds that Pension Trust will not consider projects for less than $7 million
  - Orenstein responds saying Market Street wants to exercise option to purchase under Paragraph 34
- Question—was Orenstein's not reminding Erb about the option under Paragraph 34 a breach of the duty of good faith and fair dealing?

Market Street Associates v. Frey

- Held—maybe; depends on Orenstein's state of mind (court sends case back down for fact-finding)
- A party violates the covenant of good faith and fair dealing where it "take[s] deliberate advantage of an oversight by [their] contract partner concerning his rights under the contract"
  - *But* "[t]he duty of honesty, of good faith, even expansively conceived is not a duty of candor. You can make a binding contract to purchase something you know your seller undervalues"
  - *And* "even after you have signed the contract, you are not obliged to become an altruist toward the other party and relax the terms if he gets into trouble in performing his side of the bargain"

Market Street Associates v. Frey— Takeaways

- Duty of good faith and fair dealing implied into contracts
- *But* does not require subjecting one's own interests to the interests of another
- Look for—
  - Knowingly trying to take advantage of another party's misunderstanding or lack of knowledge about contract
  - Especially with sneaky behavior, concealment/misrepresentation/half-truths

Bloor v. Falstaff Brewing Co.

- Falstaff acquires Ballantine brand from Bloor, for a price + royalties on every Ballantine unit sold
  - Contract requires Falstaff to "use its best efforts to promote and maintain a high volume of sales," or pay liquidated damages if it decides it wants to stop promoting brand
- New Falstaff CEO pursues overall profit of the company rather than volume of any individual brand
  - Slashes Ballantine advertising
  - Closes Ballantine distribution center, requires buyers to pay for shipping
  - Discontinues illegal practices that Ballantine (and other Falstaff brands) were engaged in
- Falstaff profits go up; Ballantine volume sales go down dramatically
- Question—has Falstaff violated the "best efforts" clause in its purchase contract?

Bloor v. Falstaff Brewing Co.

- Held—yes; Falstaff breached contract by not using best efforts to promote sales volume
- Court is vague about what "best efforts" requires, and acknowledges that Falstaff didn't have to spend itself into bankruptcy promoting Ballantine
  - But "[i]t was sufficient to show that Falstaff simply didn't care about Ballantine's volume and was content to allow this to plummet so long as that course was best for Falstaff's overall profit picture . . . ."
  - And a number of choices demonstrated lack of best efforts to promote Ballantine volume—(1) closing distribution center, (2) using a distributor that owned a competing brand, (3) failure to consider an offer for Ballantine distribution, (4) no longer setting sales targets for Ballantine
- Damages—not liquidated damages clause; expectation damages based on comparison to sales of comparable beer

Bloor v. Falstaff Brewing Co.—Takeaways

- "Best efforts" clauses—contracts can elaborate on implied duty of good faith and fair dealing
- Generally enforceable by their terms, even if doing so leads to economically irrational results

Iron Trade Products Co. v. Wilkoff Co.

- Plaintiff buys railroad rails from defendant at $41/ton to be delivered to NY
  - While defendant was negotiating for rails, plaintiff goes out and buys more rails directly from manufacturers
  - In a tight market, plaintiff's buying additional rails dramatically raised the price of the rails for which defendant was negotiating
- Question—did plaintiff *prevent* defendant from performing, relieving defendant of expectation damages?

Iron Trade Products Co. v. Wilkoff Co.

- Held—no
- "The conduct of one party which *prevents* the other from performing his part is an excuse for nonperformance."
  - But "[m]ere difficulty of performance will not excuse a breach of contract."

Iron Trade Products Co. v. Wilkoff Co.—Takeaways

- One party's *preventing* the other's performance can relieve that party of damages for breach
  - Classic case—*United States v. Peck*—Peck had a contract to provide hay to U.S. from specified government lands, but the U.S. then has all hay removed from those lands by third parties
- But making the other party's performance more difficult (within reasonable commercial bounds) is not sufficient

Class 21: Repudiation and Assurance

Professor James Toomey

Hochster v. De La Tour

- Defendant hires plaintiff to accompany him as courier on trip around Europe
- Trip to begin June 1, followed by 3 months of travel
- Before June 1, defendant renounces the contract and says that he has no intention of taking trip
- Plaintiff, before June 1—
  - Enters into a new, substantially similar agreement with Lord Ashburton, doesn't start until July 4
  - Files suit, alleging breach of contract
- Question—
  - Can plaintiff enter into a new agreement in response to repudiation?
  - Can plaintiff maintain cause of action for breach of contract on basis of repudiation, before time to perform has arrived?

Hochster v. De La Tour

- Held—plaintiff was justified in entering into new contract; plaintiff can sue based on repudiation before June 1
- "[I]t is surely much more rational, and more for the benefit of both parties, that, after the renunciation of the agreement by the defendant, the plaintiff should be at liberty to consider himself absolved from any future performance on it, retaining his right to sue for any damage he has suffered from the breach of it."
  - "The declaration in the present case, in alleging a breach, states a great deal more than a passing intention on the part of the defendant which he may repent of, and could only be proved by evidence that he had utterly renounced the contract, or done some act which rendered it impossible for him to perform."

Hochster v. De La Tour—Takeaways

- Doctrine of ***anticipatory repudiation***—clear and definitive repudiation of contract before performance can give rise to immediate liability for total breach
  - Justifies the other party in making alternative arrangements

Restatement § 253. ***Effect of a Repudiation as a Breach and on Other Party's Duties***

(1) Where an obligor repudiates a duty before he has committed a breach by non-performance and before he has received all of the agreed exchange for it, his repudiation alone gives rise to a claim for damages for total breach.

(2) Where performances are to be exchanged under an exchange of promises, one party's repudiation of a duty to render performance discharges the other party's remaining duties to render performance.

Kanavos v. Hancock Bank & Trust Co.

- Kanavos has a right of first refusal on the sale of particular property by the bank, allows Kanavos to buy the property at the same price as any offer from a third party
- Bank sells the property to a third party for $760,000 in violation of the right of first refusal—does not notify Kanavos or give him opportunity to purchase for that price
- Bank's defense—Kanavos couldn't have afforded the property if offered
- Question—is Kanavos's inability to pay a defense?

Kanavos v. Hancock Bank & Trust Co.

- Held—yes
- In order to be entitled to damages, Kanavos needs to show he could have purchased the property if contract hadn't been breached
- Kanavos has burden of showing ability to pay—plaintiff has to prove damages as part of claim

Kanavos v. Hancock Bank & Trust Co.—Takeaways

- General rule—plaintiff has burden to prove that defendant's breach caused damages
  - Particularly relevant in anticipatory repudiation cases, where plaintiff has to show that but for defendant's breach, they could and would have performed themselves

UCC § 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.

Restatement § 251. ***When a Failure to Give Assurance May be Treated as a Repudiation.***

(1) Where reasonable grounds arise to believe that the obligor will commit a breach by non-performance that would itself give the obligee a claim for damages for total breach under § 243, the obligee may demand adequate assurance of due performance and may, if reasonable, suspend any performance for which he has not already received the agreed exchange until he receives such assurance.

(2) The obligee may treat as a repudiation the obligor's failure to provide within a reasonable time such assurance of due performance as is adequate in the circumstances of the particular case.

By-Lo Oil Co. v. ParTech, Inc.

- ParTech runs By-Lo's IT, under contract to provide continuing support for a monthly fee
- ByLo asks ParTech whether it will make sure its systems are Y2K compliant, first in September 1997, makes first serious demand January 1998
- ParTech can't give a definitive answer and says they will figure this out at a higher level and get back to By-Lo
- By-Lo demands further assurance
  - Attempts to sue ParTech
  - And purchases another computer system in June 1998
- In November 1998, ParTech realizes it actually does need to update the system by January 1, 1999—a quick turnaround but it assures that it can do it
- By-Lo sues ParTech, arguing that it was justified in buying new equipment because of ParTech's failure to provide assurances
- Question—did ParTech fail to give adequate assurances, justifying By-Lo's contracting with another company?

By-Lo Oil Co. v. ParTech, Inc.

- Held—no; By-Lo breached by contracting with another company
- Were there reasonable grounds to demand assurance?
  - No, Y2K was too far off when By-Lo started freaking out
  - It turns out the systems would have had problems sooner, but By-Lo didn't know that—the time under analysis is the time when By-Lo demanded assurance, not actual performance
- Were ParTech's assurances adequate?
  - Yes
  - General rule—assurances are inadequate whenever they are less than what the person seeking assurance sought
  - But can be adequate where less than that on a balancing test—and under these circumstances ParTech's assurances that it was looking into the issue were sufficient

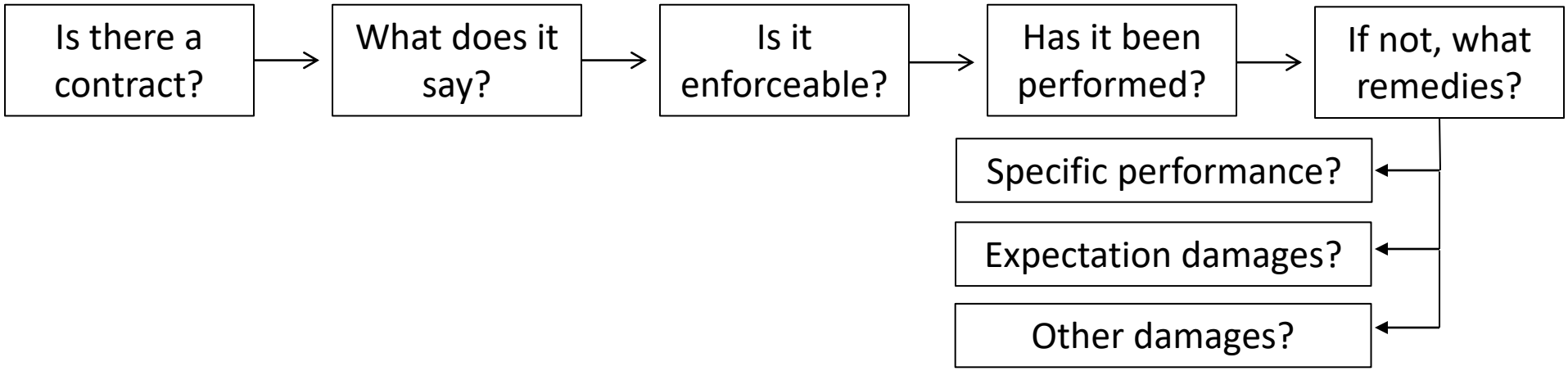
By-Lo Oil Co. v. ParTech, Inc.— Takeaways

- If reasonable grounds arise to doubt performance, the other party may demand assurance
  - And failure to give adequate assurance can count as repudiation/breach
- But grounds for doubting performance need to be ***reasonable*** (concrete, reasonably imminent), and any assurance provided ***inadequate*** (presumptively less than asked for, but look for whether a reasonable person would have accepted their answer for now)

Class 22: Remedies I

Professor James Toomey

The Story of a Contract



Remedying Breach

- Standard remedy—**expectation damages**
  - Monetary damages ***to put plaintiff in position they would have been in had the contract been performed***
- Maybe, alternative—specific performance
  - Order defendant to perform as promised
- Maybe, alternative—other damages
  - Restitution
  - Reliance

Specific Performance

- Discretionary equitable remedy
- ***Only*** available on a finding that monetary expectation damages are inadequate.
- Typically—
  - Land contracts
  - Contracts for “unique” goods—a specific painting, a racehorse, etc.
- Never—
  - Personal services contracts

Expectation Damages

- Put plaintiff in the (at least financial) position they would have been in had the contract been performed
- Basic formula—
  - Damages = loss in value + other loss – cost and loss avoided

Restatement § 347. ***Measure of Damages in General.***

Subject to the limitations stated in §§ 350-353, the injured party has a right to damages based on his expectation interest as measured by

(a) the loss in the value to him of the other party's performance caused by its failure or deficiency, plus

(b) any other loss, including incidental or consequential loss, caused by the breach, less

(c) any cost or other loss that he has avoided by not having to perform.

Vitex Manufacturing Corp. v. Caribtex Corp.

- Caribtex contracts to pay Vitex to process its wool for import into the U.S.
  - In preparing to perform, Vitex reopens a temporarily closed plant and recalls workers
- Caribtex repudiates contract before delivering the wool
- Vitex sues for breach, and wins
- Question—how should the court appropriately measure expectation damages?
  - Specifically, should "overhead," (fixed, ongoing) Vitex costs be included as "cost avoided" subtracted from damages?

Vitex Manufacturing Corp. v. Caribtex Corp.

- Held—overhead costs not generally "costs avoided"
  - "Although there is authority to the contrary, we feel that the better view is that normally, in a claim for lost profits, overhead should be treated as a part of gross profits and recoverable as damages, and should not be considered as part of the seller's costs."
  - "Since this overhead remained constant, in no way attributable to or affected by the Caribtex contract, it would be improper to consider it as a cost of Vitex's performance to be deducted from the gross proceeds of the Caribtex contract."
- Damages = loss in value + other loss – costs avoided
  - $21,114 (damages) = $31,250 (loss in value, contract price; court confusingly calls this "gross profits") + [no other loss] – $10,136 (costs avoided, estimate of costs of processing the wool, not including overhead costs in running the factory)
  - Caribtex's argument is that "costs avoided" should be increased by the overhead costs of running factory; court says no

Vitex Manufacturing Corp. v. Caribtex Corp.—Takeaways

- Expectation damages = loss in value (generally the consideration under the contract) + other loss ("incidental and consequential damages") – costs avoided (by not having to do work)
- Costs avoided generally not held to include fixed, "overhead" costs—paying property taxes, keeping the lights on in the factory, etc.

UCC 2-712. ***"Cover"; Buyer's Procurement of Substitute Goods.***

(1) After a breach within the preceding section the buyer may "cover" by making in 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 . . . 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.

Laredo Hides Co., Inc. v. H&H Meat Products Co., Inc.

- Laredo Hides (hide distributor, with contracts with Mexican tanneries) contracts for all of meat-company H&H's cattle hides produced in the year of 1972, for a per-hide price
  - Laredo's payment check gets delayed in the mail
  - Which H&H (unjustifiably) treats as a breach, repudiates contract, and stops delivery
- Laredo buys replacement hides on the open market, which are more expensive
  - Costs $142,254.48 + additional expenses
- Question—what is the appropriate measure of Laredo's damages?
  - Is Laredo's "cost of cover" (i.e., price at which it purchased replacement goods) the appropriate measure?

Laredo Hides Co., Inc. v. H&H Meat Products Co., Inc.

- Held—Laredo entitled to recover cost of cover + incidental expenses
- Burden on seller to show that cover purchase was not "reasonable"
  - The cover price *was* a lot more expensive than the contract price, because contract price was in bulk where Laredo ended up buying smaller lots on the open market
  - But that is not "unreasonable," and at the time of breach Laredo didn't really have an alternative opportunity to enter into a long-term output contract
- In addition to cover expenses, Laredo entitled to incidental damages
  - $1435.77 for increased transportation costs
  - $2013.18 for increased handling costs

Laredo Hides Co., Inc. v. H&H Meat Products Co., Inc.—Takeaways

- Buyer's right to "cover"—purchase replacement goods and recover the actual cost of purchase
  - Unless the cover was "unreasonable," which the seller has the burden of showing

UCC § 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 . . . 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 by this Article . . . 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 . . . , due allowance for costs reasonably incurred and due credit for payments or proceeds of resale.

R.E. Davis Chemical Corp. v. Diasonics, Inc.

- Davis contracts to buy an MRI machine from Diasonics
  - Paid for with a down payment ($300,000) and scheduled further payment
- After the doctors Davis had intended to use the machine back out, Davis repudiates contract
  - Diasonics sells the MRI machine to a third party for the same price it was going to sell to Davis (no loss)
- Davis sues Diasonics for return of downpayment; Diasonics countersues for damages for breach
- Question—what is the appropriate measure of damages?
  - Can Diasonics recover lost profits it would have made on Diasonics sale on the theory that it lost the opportunity to sell two MRI machines rather than one?

R.E. Davis Chemical Corp. v. Diasonics, Inc.

- Held—Diasonics may be entitled to recover lost profits on Davis-sale, on theory that it is a "lost volume seller"
  - "[A] lost volume seller [is] one that has a predictable and finite number of customers and that has the capacity either to sell to all new buyers or to make the one additional sale represented by the resale after the breach."
- Plaintiff has the burden to show—
  - That they *could* have made additional sale
  - And that they *would* have (at least, it wouldn't have been unprofitable for them to do so)—"Of course, Diasonics . . . must show that it probably would have made the second sale absent the breach"
- Incidentally, Davis is entitled to return of its downpayment under UCC § 718

R.E. Davis Chemical Corp. v. Diasonics, Inc.—Takeaways

- Damages for ***lost volume sellers***—
  - A seller is entitled to lost profits on a particular sale if it can show that, but for the defendant's breach, it would have made two sales rather than one
  - Seller has the burden of showing that it ***could*** have made a second sale and that it ***probably would have***

Restatement § 373. ***Restitution When Other Party is in Breach.***

(1) Subject to the rule stated in Subsection (2), on a breach by non-performance that gives rise to a claim for damages for total breach or on a repudiation, the injured party is entitled to restitution for any benefit that he has conferred on the other party by way of part performance or reliance.

(2) The injured party has no right to restitution if he has performed all of his duties under the contract and no performance by the other party remains due other than payment of a definite sum of money for that performance.

United States v. Algernon Blair, Inc.

- Subcontractor begins work on project—it is paying for cranes but believes general should be paying for cranes under the contract
  - Eventually sub stops work
  - And general completes work with another sub
  - Court holds that general breached the contract—the sub was right that the general was supposed to be paying for the cranes
- Sub sues general for breach of contract
  - But general can show that contract would have been a loss for sub
  - Contract price was $37,000, it would have cost more than $37,000 for sub to actually perform
- Question—is sub entitled to restitution as an alternative to expectation damages?

United States v. Algernon Blair, Inc.

- Held—sub entitled to restitution
- Even if the contract would have been a loss to sub, its partial performance conferred real benefit to general, for which sub is entitled to recovery
  - "The measure of recovery for quantum meruit is the reasonable value of the performance."
  - "Recovery is undiminished by any loss which would have been incurred by complete performance."
  - "The amount for which such services could have been purchased from one in the plaintiff's position at the time and place the services were rendered."

United States v. Algernon Blair, Inc.—Takeaways

- ***Restitution*** is an ***alternative*** to expectation damages for a ***non-breaching party, after part performance***
  - Return value of benefits actually conferred by part performance
  - Not available in breach after non-breaching party's complete performance
  - Puzzle—can provide compensation for work done on losing contracts; plaintiff can recover more than if the contract had been performed

Class 23: Remedies II

Professor James Toomey

Two Ways of Thinking About "Lost Value"

- Cost of repair
  - Give the plaintiff the money needed to actually put themselves in the position they would have been in had the contract been performed
- Diminution of value
  - Give the plaintiff the cash approximating the market value lost because of defendant's breach
  - Put the plaintiff in the *financial* position they would have been in had the contract been performed

Restatement § 348. ***Alternatives to Loss of Value in Performance.***

. . .

(2) If a breach results in defective or unfinished construction and the loss in value to the injured party is not proved with sufficient certainty, he may recover damages based on

(a) the diminution in the market price of the property caused by the breach, or

(b) the reasonable cost of completing performance or of remedying the defects if that cost is not clearly disproportionate to the probable loss in value to him.

. . .

Plante v. Jacobs

- Frank and Carol Jacobs hire Eugene Plante to build them a house, for $26,765, paid in installments
  - There are disputes about performance
  - But the house is mostly built and the Jacobses are living in it
    - Cabinets, etc., missing
    - Structural wall misplaced by one foot (larger kitchen; smaller living room)
    - Paint cracks, small issues
  - Jacobs have paid $20k, but refuse to pay more, and Plante stops work
- Plante sues, seeking contract price less value of work he admits he did not do ($1601.95)
- Question—was the contract substantially performed, and how do we measure damages?

Plante v. Jacobs

- Held—Plante substantially performed; is entitled to contract price less any damages caused by various breaches
- In construction cases, courts often measure loss of value by—
  - "[T]he difference between the value of the house as it stands with faulty and incomplete construction and the value of the house if it had been constructed in strict accordance with the plans and specifications."
- Contrast with *cost of repair* damages
- Diminution of value applied to misplaced wall; cost of repair awarded for smaller breaches
  - Awarding cost of repair damages for the misplaced wall would create "economic waste," and grants a windfall to the Jacobses if they decide not to have the wall moved

Plante v. Jacobs—Takeaways

- ***Cost of repair*** and ***diminution of value*** are two ways of measuring the non-breaching party's loss of value
- Cost of repair is the default in general (more closely approximates putting the non-breaching party in the actual position they would have been in had the contract been performed)
  - But where cost of repair is wildly out of proportion to diminution in value (especially in construction cases), courts often turn to diminution of value

Groves v. John Wunder Co.

- Groves leases industrial land on outskirts of Minneapolis to Wunder for 7 years
  - Wunder extracts gravel from land and processes it at its plant
  - Wunder promised in contract to return the property "at a uniform grade, substantially the same as the grade now existing at the roadway . . . on said premises, and that in stripping the overburden . . . it will use said overburden for the purpose of maintaining and establishing said grade."
- After removing "the richest and the best of the gravel," Wunder returns property "broken, rugged, and uneven," not at "any uniform grade"
- Evidence shows that—
  - It would cost $60,000 to grade the land, as promised
  - And if re-graded, the property would only be worth $12,000 total
- Question—should the plaintiff's loss of value be measured by cost of repair or diminution of value?

Groves v. John Wunder Co.

- Held—cost of repair
- Court argues that cost of repair is the only fair way to measure expectation damages—put Groves in position it would have been in had the contract been performed
  - Groves contracted for evenly graded land, not the market value of that land
  - Especially, the court thinks, where defendant's breach was "wilful" and "deliberate"—"the wilful transgressor must accept the penalty of his transgression"
- "The answer is that there can be no unconscionable enrichment, no advantage upon which the law will frown, when the result is but to give one party to a contract only what the other has promised; particularly where, as here, the delinquent has had full payment for the promised performance."

Groves v. John Wunder Co.— Takeaways

- Some (few) courts will award cost of repair damages even in construction cases where they are out of proportion to diminution of value
  - On the theory that they better approximate the purposes of expectation damages
  - But note the importance of moral condemnation of wilful breach

Peevyhouse v. Garland Coal & Mining Co.

- Willie and Lucille Peevyhouse lease their farm to Garland Coal & Mining to strip mine for 5 years
  - Contract requires Garland to complete specified remedial and restorative work (which the Peevyhouse's specifically bargained for)
  - Garland does not do any remedial work
- Evidence shows—
  - Promised remedial work would have cost $29,000
  - And the market price of the farm with remedial work would only be $300 more than without
- Question—is the appropriate measure of the Peevyhouses' damages cost of repair or diminution of value?

Peevyhouse v. Garland Coal & Mining Co.

- Held—diminution of value
  - "We hold that where, in a coal mining lease, lessee agrees to perform certain remedial work on the premises concerned at the end of the lease period, and thereafter the contract is fully performed by both parties except that the remedial work is not done, the measure of damages in an action by lessor against lessee for damages for breach of contract is ordinarily the reasonable cost of performance of the work; however, where the contract provision breached was merely incidental to the main purpose in view, and where the economic benefit which would result to lessor by full performance of the work is grossly disproportionate to the cost of performance, the damages which lessor may recover are limited to the diminution in value resulting to the premises of the non-performance."
- Court does not think *Groves* is strong authority

Peevyhouse v. Garland Coal & Mining Co.—Dissent

- Would have used cost of repair, or even awarded specific performance
  - "The defendant admitted in the trial of the action, that the plaintiffs insisted that the above provisions be included in the contract and that they would not agree to the coal mining lease unless the above provisions were included."

Peevyhouse v. Garland Coal & Mining Co.—Takeaways

- Most courts disagree with *Groves*, and use diminution of value to measure plaintiffs' loss of value where cost of repair is wildly disproportionate

Restatement § 350. ***Avoidability as a Limitation on Damages.***

(1) Except as stated in Subsection (2), damages are not recoverable for loss that the injured party could have avoided without undue risk, burden or humiliation.

(2) The injured party is not precluded from recovery by the rule stated in Subsection (1) to the extent that he has made reasonable but unsuccessful efforts to avoid loss.

Rockingham County v. Luten Bridge Co.

- Rockingham County hires Luten to build a bridge
  - Luten has started building the bridge
  - But, after considerable public opposition, the county repudiates the contract and tells Luten to stop work
  - But Luten keeps working and finishes the bridge
- Luten sues for breach of contract
- Question—can Luten recover the $18K contract price when it kept working after being told to stop?

Rockingham County v. Luten Bridge Co.

- Held—no; Luten can recover only what it could have recovered at time of repudiation
  - (Amounts spent constructing the bridge after repudiation is counted as "costs avoided" in damages calculation)
- "[A] plaintiff cannot hold a defendant liable for damages which need not have been incurred; or, as it is often stated, the plaintiff must, so far as he can without loss to himself, mitigate the damages caused by the defendant's wrongful act."
  - "After an absolute repudiation or refusal to perform by one party to a contract, the other party cannot continue to perform and recover damages based on full performance."

Rockingham County v. Luten Bridge Co.—Takeaways

- ***Duty to mitigate damages***—non-breaching parties cannot recover damages that, with reasonable effort, they could have avoided
  - Another way of thinking about duty to mitigate—defendant's breach didn't *cause* damages if plaintiff could have avoided them relatively easily

Cosden Oil & Chemical Co. v. Karl O. Helm Aktiengesellschaft

- Helm (German trader) contracts to buy large quantities of polystyrene from Cosden (Texas petrochemical company)
  - After part performance, Cosden repudiates
  - (Helm has some polystyrene it hasn't paid for)
- Helm does not cover
- Cosden sues for payment on unpaid polystyrene; Helm counterclaims for damages from repudiation
  - Helm wins—Cosden breached by repudiation
  - Buyer's damages = market price – contract price
- Question—*when* should court measure market price for damages?

Cosden Oil & Chemical Co. v. Karl O. Helm Aktiengesellschaft

- Held—from when Helm learned of repudiation + reasonable time
  - UCC—"at the time when the buyer learned of the breach"
- Theory—although UCC's text is incoherent on this point, goal is to emulate damages if buyer *had* covered (which is a kind of mitigation)
  - UCC allows buyer to cover within a "reasonable time" of learning of the repudiation
  - Not immediately
  - And not waiting until performance, when prices may have risen

Cosden Oil & Chemical Co. v. Karl O. Helm Aktiengesellschaft—Takeaways

- UCC cover remedy is a variation of duty to mitigate damages
- Where buyer does *not* cover, courts generally measure damages as if they had (from learning of repudiation + reasonable time)

Parker v. Twentieth Century-Fox Film Corp.

- Actress Shirley MacLaine contracts with Fox to star in a film called "Bloomer Girl," a
  - Musical
  - Shot in Los Angeles
  - For $750,000 for 14 weeks of shooting
- Fox decides not to go forward with "Bloomer Girl." They offer MacLaine the female lead role in another project, "Big Man, Big Country," a
  - Dramatic Western
  - Shot in Australia
  - Same compensation
  - Most contract terms the same; a few differences, including losing her ability to approve screenwriter and director
- MacLaine turns down "Big Man, Big Country," and sues for breach, seeking agreed compensation on "Bloomer Girl"
- Question—was turning down "Big Man, Big Country" a failure to mitigate, reducing damages (to zero, here)?

Parker v. Twentieth Century-Fox Film Corp.

- Held—no
- "The general rule is that the measure of recovery by a wrongfully discharged employee is the amount of salary agreed upon for the period of service, less the amount which the employer affirmatively proves the employee has earned or with reasonable effort might have earned from other employment."
  - "However, before projected earnings from other employment not sought or accepted by the discharged employee can be applied in mitigation, the employer must show that the other employment was comparable, or substantially similar, to that of which the employee has been deprived; the employee's rejection of or failure to seek other available employment of a ***different or inferior kind*** may not be resorted to in order to mitigate damages."
- Court says that proposed contract for "Big Man, Big Country" was "different or inferior"

Parker v. Twentieth Century-Fox Film Corp.—Dissent

- The rule is about whether the employment is of a different *kind*, not whether it is merely *different* in some way
  - "The question is, of course, intimately bound up in what I consider the ultimate issue: whether or not the employee acted reasonably."
- Whether the employment turned down was of a different kind is a factual question that should have been submitted to a jury

Parker v. Twentieth Century-Fox Film Corp.—Takeaways

- Duty to mitigate damages in employment contexts means that a wrongfully discharged employee cannot recover any amounts they obtained from similar employment, or would have, behaving reasonably
  - Expect disputes about what constitutes "similar" employment
  - And what "reasonableness" requires

Class 24: Severability

Professor James Toomey

Gill v. Johnstown Lumber Co.

- Gill contracts to deliver four million feet of logs to Johnstown Lumber Co.
  - Payment on a per-log basis
  - But due after delivery of *all* logs
- After delivery of some logs, a huge flood sweeps away the rest
- Johnstown refuses to pay for any
- Gill sues Johnstown for partial payment
- Question—"whether the contract upon which the plaintiff sued is entire or severable"

Gill v. Johnstown Lumber Co.

- Held—severable; Gill entitled to payment for logs actually delivered, *pro rata* under the contract
- "If the part to be performed by one party consists of several distinct items, and the price to be paid by the other is (1) apportioned to each item to be performed, or (2) is left to be implied by law, such a contract will generally be held to be severable. But if the consideration to be paid is single and entire the contract must be held to be entire, although the subject of the contract may consist of several distinct and wholly independent items."

Gill v. Johnstown Lumber Co.— Takeaways

- "Severability" of contracts can mitigate damages/provide partial compensation for partial performance
- Contracts will be found severable—as a matter of contract interpretation—where it appears separate consideration is being exchanged for distinct parts of performance

Restatement § 240. ***Part Performances as Agreed Equivalents.***

If the performances to be exchanged under an exchange of promises can be apportioned into corresponding pairs of part performances so that the parts of each pair are properly regarded as agreed equivalents, a party's performance of his part of such a pair has the same effect on the other's duties to render performance of the agreed equivalent as it would have if only that pair of performances had been promised.

Britton v. Turner

- Britton agrees to work for Turner for 1 year, March 1831-March 1832, for $120 for the full year
- Britton works for 9 and a half months and then quit, without Turner's consent or good reason
- Question—can Britton recover in restitution for work actually performed?

Britton v. Turner

- Held—yes; Britton can recover in restitution, *pro rata* share of the contract price
- Concerns of basic fairness relevant in equity—“That such rule in its operation may be very unequal, not to say unjust, is apparent”
- Default rule—”It is easy, if parties so choose, to provide by an express agreement that nothing shall be earned, if the laborer leaves his employer without having performed the whole service contemplated, and then there can be no pretense for a recovery if he voluntarily deserts the service before the expiration of the time.”
- Britton gets $95 as *pro rata* share of contract price

Britton v. Turner—Takeaways

- Restitution/unjust enrichment can provide partial payment for valuable partial performance even in “entire” contracts

Kirkland v. Archbold

- Plaintiff contracted with defendant to repair defendant's house—$6,000 for repairs
  - Paid in installments of $1,000, with the remainder after performance
  - "All outside walls are to be lined with rock wool and rock lathe, superimposed thereon"
- Plaintiff was completing work with *wood* lathe. Defendant prevents him from continuing work.
  - Defendant has paid only $800 (partial payment of first installment)
  - Plaintiff says that he has expended $2,985 in partial performance
- Plaintiff sues for $2,985 expended
- Question—is plaintiff entitled to recover, and, if so, how much?

Kirkland v. Archbold

- Held—yes; can recover in *restitution* for benefits conferred, not necessarily for costs expended, nor just on first installment
- Is this contract severable or entire?
  - "The plaintiff agreed to make certain repairs and improvements on the defendant's property for which he was to be paid $6,000. The total consideration was to be paid for the total work specified in the contract. The fact that a schedule of payments was set up based on the progress of the work does not change the character of the agreement."
- But does this mean the plaintiff can't recover at all?
  - No—restitution for benefits conferred
  - "An ever increasing number of decisions of courts of last resort now modify the severity of this rule and permit defaulting contractors, where their work has contributed substantial value to the other contracting party's property, to recover the value of the work and materials expended on a quantum meruit basis, the recovery being diminished, however, the extent of such damage as the contractor's breach causes the other party."

Kirkland v. Archbold—Takeaways

- The rule from *Britton v. Turner* commonly used to provide restitution for benefits conferred, even in entire contracts

McKenna v. Vernon

- McKenna contracts with Vernon to build a movie theater, for $8750
  - Paid in installments for 80% of the work, then final 20% after completion
  - Each payment is contingent on the architect certifying that work complies with contract
- Vernon makes 7 installment payments, but only 1 was based on the required certificate from the architect
- Vernon refuses to make final payments
- McKenna sues to recover amount due under contract
- Question—did Vernon waive architectural certificate as a condition of payment in making 6 installment payments without it?

McKenna v. Vernon

- Held—yes; Vernon waived certification requirement; McKenna *not* in breach for failing to provide
  - "With such constant and repeated disregard on the part of the owner to exact compliance with this provision in the contract, it is too late now for him to insist that failure on the part of the plaintiff to secure such certificate before suit defeats his right of action."
  - Vernon was actively involved in supervising the work and there was in fact nothing wrong with it

McKenna v. Vernon—Takeaways

- Waiver of conditions in contract can estop a party from later pointing to non-compliance as a breach
- Look for—
  - Clear and consistent acquiescence to non-compliance
  - Apparent acquiescence to a substitute condition
  - Explicit waiver
- Courts are reluctant to find waiver merely on a showing of some lenience in performance

Restatement § 84. ***Promise to Perform a Duty in Spite of Non-Occurrence of a Condition.***

(1) Except as stated in Subsection (2), a promise to perform all or part of a conditional duty under an antecedent contract in spite of the non-occurrence of the condition is binding, whether the promise is made before or after the time for the condition to occur, unless

  (a) occurrence of the condition was a material part of the agreed exchange for the performance of the duty and the promisee was under no duty that it occur; or

  (b) uncertainty of the occurrence of the condition was an element of the risk assumed by the promisor

(2) If the promise is made before the time for the occurrence of the condition has expired and the condition is within the control of the promisee or a beneficiary, the promisor can make his duty again subject to the condition by notifying the promisee or beneficiary of his intention to do so if

  (a) the notification is received while there is still a reasonable time to cause the condition to occur under the antecedent terms or an extension given by the promisor; and

  (b) reinstatement of the requirement of the condition is not unjust because of a material change of position by the promisee or beneficiary; and

  (c) the promise is not binding apart from the rule stated in Subsection (1).

Class 25: Foreseeability & Alternative Remedies

Professor James Toomey

Hadley v. Baxendale

- Plaintiff mill operators have broken crank shaft, with no backup available, and hire defendant common carrier to deliver broken shaft as sample (and new shaft) to/from manufacturer
  - ***Assume***—"[T]he only circumstances here communicated by the plaintiffs to the defendants at the time the contract was made, were, that the article to be carried was the broken shaft of a mill, and that the plaintiffs were the millers of that mill."
- Defendants' delivery was "delayed by some neglect" for an unreasonably long time
  - During the shipment the mill was shut down, because the plaintiffs had no backup
  - And the re-opening of the mill was delayed 5 days because of the defendant's delay
  - Leading to lost profits
- Plaintiffs sue for damages including lost profits for 5-day shutdown
- Question—are plaintiffs entitled to recover lost profits during the additional 5-day shutdown due to defendant's delay?

Hadley v. Baxendale

- Held—no; lost profits attributable to delay-caused shutdown not recoverable
  - Plaintiffs may only recover ***reasonably foreseeable*** consequential damages
    - "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 the 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."
  - Lost profits from plant shut-down do not usually arise from delay in crank-shaft delivery
    - Court assumes mills ordinarily have back-ups
  - And the defendants did not actually know that the mill was shut down pending shaft-replacement
    - "If the special circumstances under which the contract was actually made were communicated by the plaintiffs to the defendants, and thus known to both parties, the damages resulting from the breach of such contract, which they would reasonably contemplate, would be the amount of injury which would ordinarily follow from a breach of contract under these special circumstances so known and so communicated."
    - Court finds that plaintiffs did not tell defendants the circumstances (though there seems to have been a factual dispute)

Hadley v. Baxendale—Takeaways

- **"The rule of *Hadley v. Baxendale*"**—plaintiffs can only recover such damages as would be the ***reasonably foreseeable*** consequence of breach at the time the contract was made
- Damages can be reasonably foreseeable either because
  - They are the universal consequence of breach (basic expectation damages, extra incidental costs of shipping and storage, etc.)
  - ***Or*** special circumstances known to both parties

Restatement § 351. ***Unforeseeability and Related Limitations on Damages.***

(1) Damages are not recoverable for loss that the party in breach did not have reason to foresee as a probable result of the breach when the contract was made.

(2) Loss may be foreseeable as a probable result of a breach because it follows from the breach

  (a) in the ordinary course of events,

  (b) as a result of special circumstances, beyond the ordinary course of events, that the party in breach had reason to know.

(3) A court may limit damages for foreseeable loss by excluding recovery for loss of profits, by allowing recovery only for loss incurred in reliance, or otherwise if it concludes that in the circumstances justice so requires in order to avoid disproportionate compensation.

Delchi Carrier S.p.A. v. Rotorex Corp.

- Rotorex (NY company) contracts to send air compressors to Delchi (Italian company)
  - Across three shipments
  - First shipment is non-conforming
  - Delchi cancels contract and sues Rotorex
- Suit governed by Convention on Contracts for the International Sale of Goods (CISG)
- Question—does the rule of *Hadley v. Baxendale* apply to CISG suits?
  - (Can Delchi recover incidental damages for its efforts to comply with the contract?)

Delchi Carrier S.p.A. v. Rotorex Corp.

- Held—yes; (and yes)
- CISG—"Damages for breach of contract may not exceed the loss which the party in breach foresaw or ought to have foreseen at the time of the conclusion of the contract, in the light of the facts and matters of which he then knew or ought to have known, as a possible consequence of the breach of contract."
  - "The CISG requires that damages be limited by the familiar principle of foreseeability established in *Hadley v. Baxendale*."
  - Lost profits damages here were foreseeable—"It was objectively foreseeable that Delchi would take orders for sales based on the number of compressors it had ordered and expected to have ready for the season"
- (Delchi can also recover for incidental damages in additional shipping, customs, storage expenses, insulation, tubing & maybe labor materials)
  - This court finds overhead not recoverable under CISG

Delchi Carrier S.p.A. v. Rotorex Corp.—Takeaways

- Some rule of foreseeability of damages in contract actions (foreseeable? possible? probable?) is widely accepted across jurisdictions

Restatement § 356. ***Liquidated Damages and Penalties.***

(1) Damages for breach by either party may be liquidated in the agreement but only at an amount that is reasonable in light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss. A term fixing unreasonably large liquidated damages is unenforceable on grounds of public policy as a penalty.

. . .

Dave Gustafson & Co. v. State

- Contract between state and highway company to redo a particular highway
  - Provides for damages of $210/day for delay
- Construction delayed by 67 days
- Highway company sues to recover full contract price; state wants reduction of $14K under the liquidated damages clause for delay
- Question—is the liquidated damages clause enforceable?

Dave Gustafson & Co. v. State

- Held—yes; liquidated damages provision enforceable
  - "A provision for payment of a stipulated sum as liquidation of damages will ordinarily be sustained if it appears that at the time the contract was made the damages in the event of a breach will be incapable or very difficult of accurate estimation, that there was a reasonable endeavor by the parties as stated to fix fair compensation, and that the amount stipulated bears a reasonable relation to probable damages reasonably to be anticipated."
- Damages from delay of highway construction exist but are hard to measure
  - And court thinks $210/day is a reasonable estimate (doesn't really tell us why)

Dave Gustafson & Co. v. State—Takeaways

- Reasonable liquidated damages provisions are enforceable
  - Must be a reasonable estimate of actual damages
  - And it helps (required in many jurisdictions) to show that traditional ways of estimating damages *post facto* in court are unlikely to be adequate
- On the contrary, "penalties," or *unreasonable* estimates of actual damages are unenforceable

Lake River Corp. v. Carborundum Co.

- Lake River contracts to bag and ship ferro carbo for Carborundum
  - This requires Lake River to invest $89,000 in new equipment upfront
  - "In consideration of the special equipment to be acquired and furnished by LAKE-RIVER for handling the product, CARBORUNDUM shall, during the initial three-year term of this Agreement ship to LAKE-RIVER for bagging a minimum quantity of [22500 tons]. If, at the end of the three-year term this minimum quantity shall not have been shipped, LAKE-RIVER shall invoice CARBORUNDUM at the then prevailing rates for the difference between the quantity bagged and the minimum guaranteed."
- Carborundum ships only 55% of guaranteed amount
- Lake River demands payment under the guaranteed minimum clause of contract
  - And refuses to ship Carborundum's ferro carbo in its possession until paid
- Lake River sues for payment; Carborundum countersues for what it believes was Lake River's conversion of its ferro carbo
- Question—is the "guaranteed minimum" clause enforceable as liquidated damages?

Lake River Corp. v. Carborundum Co.

- Held—no; guaranteed minimum clause was an unenforceable penalty
- "To be valid under Illinois law a liquidation of damages must be a reasonable estimate at the time of contracting of the likely damages from breach, and the need for estimation at that time must be shown by reference to the likely difficulty of measuring the actual damages from a breach of contract after breach occurs."
  - "If damages would be easy to determine then, or if the estimate greatly exceeds a reasonable upper estimate of what the damages are likely to be, it is a penalty."
  - "Mindful that Illinois courts resolve doubtful cases in favor of classification as a penalty, we conclude that the damage formula in this case is a penalty and not a liquidation of damages, because it is designed always to assure Lake River more than its actual damages."
- The fundamental problem with this provision is that Carborundum saved Lake River a lot of money (high "costs avoided")
  - But the guaranteed minimum clause would grant the full contract price anyway
  - Meaning that Lake River would get compensated under the clause *more* than it would have made in profit had the contract been performed (by a lot in this case)

Lake River Corp. v. Carborundum Co.—Takeaways

- The traditional rule that "penalties" for breach are unenforceable is controversial, but governs in most jurisdictions
- A liquidated damages clause that would leave a non-breaching party better off than if the contract had been performed is generally unenforceable

Campbell Soup Co. v. Wentz

- Campbell Soup has contract with Wentzes (farmers) for all Chantenay red cored carrots from specified 15 acres for $30/ton
  - Market price of Chantenay red cored carrots is up to $90/ton by the time of performance
  - These carrots are "virtually unobtainable" on the open market
  - Wentzes refuse to perform
    - Instead, sell carrots to their neighbor, Lojeski, who is selling them for market price
    - Including to Campbell
- Campbell sues Wentzes and Lojeski to stop this scheme
- Question—would Campbell be entitled to specific performance?

Campbell Soup Co. v. Wentz

- Held—yes
  - "A party may have specific performance of a contract for the sale of chattels if the legal remedy is inadequate."
  - Campbell could fairly demand Chantenay red cored carrots, even if only aesthetically different from other carrots
    - "That the test for specific performance is not necessarily 'objective' is shown by the many cases in which equity has given it to enforce contracts for articles—family heirlooms and the like—the value of which was personal to the plaintiff."
  - And without specific performance, replacements were virtually unobtainable on the market

Campbell Soup Co. v. Wentz— Takeaways

- Specific performance is a discretionary, alternative equitable remedy where money expectation damages are for some specific reason inadequate

Van Wagner Advertising Corp. v. S&M Enterprises

- Van Wagner (billboard company) contracts with Barbara Michaels for billboard space on building visible from exit to Midtown Tunnel
- Michaels sells building to S&M, who purport to cancel the lease
  - Court holds this was a breach
    - This was the main issue in the lower court, because there was a clause that looked like it allowed cancelation in case of sale
    - But lower court holds and (appellate court affirms) clause didn't apply, and S&M breached
- Lower court awards expectation damages as an estimate of lost profits
- Question—can Van Wagner get specific performance?

Van Wagner Advertising Corp. v. S&M Enterprises

- Held—no
  - "Whether or not to award specific performance is a decision that rests in the sound discretion of the trial court, and here that discretion was not abused."
  - "The point at which breach of a contract will be redressable by specific performance thus must lie not in any inherent physical uniqueness of the property but instead in the uncertainty in valuing it."
  - Because there is a thick market for billboard advertising, it is possible here to estimate with "reasonable certainty" Van Wagner's lost profits

Van Wagner Advertising Corp. v. S&M Enterprises—Takeaways

- Specific performance is always discretionary
  - And may be justified as a better way to put the non-breaching party in the position they would have been in had the contract been performed where the value of performance is *particularly* difficult to estimate
- Expectation damages are the default remedy in breach of contract