

Contract Doctrine, Theory & Practice

Second Edition
Principal Cases



J H VERKERKE

PROFESSOR OF LAW
UNIVERSITY OF VIRGINIA
SCHOOL OF LAW



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J.H. Verkerke

Professor of Law

University of Virginia School of Law

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ABOUT THE AUTHOR

J.H. (Rip) Verkerke is a professor of law and director of the Program for Employment and Labor Law Studies at the University of Virginia School of Law. He earned an M.Phil. in economics and a J.D. from Yale University. He joined the UVA Law School faculty in 1991 after clerking for Judge Ralph K. Winter, Jr. of the U.S. Court of Appeals for the Second Circuit. Verkerke teaches contracts, several employment law courses, and a seminar on conservation planning and law.

A pioneer in the use of technology to support legal education, Verkerke was selected as an inaugural member of the University Academy of Teaching and won an All-University Teaching Award in 2007. In 2012, he received a Hybrid Challenge Grant for Technology-Enhanced Teaching to transform his first-year contracts class using the flipped classroom model of instruction. He previously chaired the University Committee on Information Technology.

Verkerke's published research focuses on employment discrimination law, employment contracts, vicarious liability, the economics of discrimination, and contract theory. He has co-authored an empirical study of law school teaching practices and how those methods affect student experiences and outcomes.

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Bailey v. West

Supreme Court of Rhode Island
105 R.I. 61, 249 A.2d 414 (1969)

PAOLINO, Justice.

1. This is a civil action wherein the plaintiff [Bailey] alleges that the defendant [West] is indebted to him for the reasonable value of his services rendered in connection with the feeding, care and maintenance of a certain race horse named "Bascom's Folly" from May 3, 1962 through July 3, 1966. The case was tried before a justice of the superior court sitting without a jury, and resulted in a decision for the plaintiff for his cost of boarding the horse for the five months immediately subsequent to May 3, 1962, and for certain expenses incurred by him in trimming its hoofs. The cause is now before us on the plaintiff's appeal and defendant's cross appeal from the judgment entered pursuant to such decision.
2. The facts material to a resolution of the precise issues raised herein are as follows. In late April 1962, defendant, accompanied by his horse trainer, went to Belmont Park in New York to buy race horses. On April 27, 1962, defendant purchased Bascom's Folly from a Dr. Strauss and arranged to have the horse shipped to Suffolk Downs in East Boston, Massachusetts. Upon its arrival defendant's trainer discovered that the horse was lame, and so notified defendant, who ordered him to reship the horse by van to the seller at Belmont Park. The seller refused to accept delivery at Belmont on May 3, 1962, and thereupon, the van driver, one Kelly, called defendant's trainer and asked for further instructions. Although the trial testimony is in conflict as to what the trainer told him, it is not disputed that on the same day Kelly brought Bascom's Folly to plaintiff's farm where the horse remained until July 3, 1966, when it was sold by plaintiff to a third party.
3. While Bascom's Folly was residing at his horse farm, plaintiff sent bills for its feed and board to defendant at regular intervals. According to testimony elicited from defendant at the trial, the first such bill was received by him some two or three months after Bascom's Folly was placed on plaintiff's farm. He also stated that he immediately returned the bill to plaintiff with the notation that he was not the owner of the horse nor was it sent to plaintiff's farm at his request. The plaintiff testified that he sent bills monthly to defendant and that the first notice he received from him

disclaiming ownership was “maybe after a month or two or so” subsequent to the time when the horse was left in plaintiff’s care.

4. In his decision the trial judge found that defendant's trainer had informed Kelly during their telephone conversation of May 3, 1962, that “he would have to do whatever he wanted to do with the horse, that he wouldn't be on any farm at the defendant's expense.” He also found, however, that when Bascom's Folly was brought to his farm, plaintiff was not aware of the telephone conversation between Kelly and defendant's trainer, and hence, even though he knew there was a controversy surrounding the ownership of the horse, he was entitled to assume that “there is an implication here that, ‘I am to take care of this horse.’” Continuing his decision, the trial justice stated that in view of the result reached by this court in a recent opinion¹ wherein we held that the instant defendant was liable to the original seller, Dr. Strauss, for the purchase price of this horse, there was a contract “implied in fact” between the plaintiff and defendant to board Bascom's Folly and that this contract continued until plaintiff received notification from defendant that he would not be responsible for the horse's board. The trial justice further stated that “I think there was notice given at least at the end of the four months, and I think we must add another month on there for a reasonable disposition of his property.”
5. In view of the conclusion we reach with respect to defendant's first two contentions, we shall confine ourselves solely to a discussion and resolution of the issues necessarily implicit therein, and shall not examine other subsidiary arguments advanced by plaintiff and defendant.

I

6. The defendant alleges in his brief and oral argument that the trial judge erred in finding a contract implied in fact between the parties. We agree.
7. The following quotation from 17 C.J.S. Contracts § 4 at pp. 557-560, illustrates the elements necessary to the establishment of a contract implied in fact:

A “contract implied in fact,” ... or an implied contract in the proper sense, arises where the intention of the parties is not expressed, but an agreement in fact, creating an obligation, is implied or presumed from their acts, or, as it has been otherwise stated, where there are circumstances which, according

¹ See *Strauss v. West*, 100 R.I. 388, 216 A.2d 366.

to the ordinary course of dealing and the common understanding of men, show a mutual intent to contract.

It has been said that a contract implied in fact must contain all the elements of an express contract. So, such a contract is dependent on mutual agreement or consent, and on the intention of the parties: and a meeting of the minds is required. A contract implied in fact is to every intent and purpose an agreement between the parties, and it cannot be found to exist unless a contract status is shown. Such a contract does not arise out of an implied legal duty or obligation, but out of facts from which consent may be inferred; there must be a manifestation of assent arising wholly or in part from acts other than words, and a contract cannot be implied in fact where the facts are inconsistent with its existence.

8. Therefore, essential elements of contracts implied in fact are mutual agreement, and intent to promise, but the agreement and the promise have not been made in words and are implied from the facts. *Power-Matics, Inc. v. Ligotti*, 191 A.2d 483 (N.J. Super. 1963); *St. Paul Fire & M. Ins. Co. v. Indemnity Ins. Co. of No. America*, 158 A.2d 825 (N.J. 1960); *St. John's First Lutheran Church v. Storsteen*, 84 N.W.2d 725 (S.D. 1957).²
9. In the instant case, plaintiff sued on the theory of a contract “implied in law.” There was no evidence introduced by him to support the establishment of a contract implied in fact, and he cannot now argue solely on the basis of the trial justice's decision for such a result.
10. The source of the obligation in a contract implied in fact, as in express contracts, is in the intention of the parties. We hold that there was no mutual agreement and intent to promise between the plaintiff and defendant so as to establish a contract implied in fact for defendant to pay plaintiff for the maintenance of this horse. From the time Kelly delivered the horse to him plaintiff knew there was a dispute as to its ownership, and his subsequent actions indicated he did not know with whom, if anyone, he had a contract. After he had accepted the horse, he made inquiries as to its ownership and, initially, and for some time thereafter, sent his bills to both defendant and Dr. Strauss, the original seller.

² Compare *Arden Engineering Co. v. E. Turgeon Constr. Co.*, 97 R.I. 342, 347, 197 A.2d 743, 746, and *George Spalt & Sons, Inc. v. Maiello*, 48 R.I. 223, 226, 136 A. 882, 883.

11. There is also uncontroverted testimony in the record that prior to the assertion of the claim which is the subject of this suit neither defendant nor his trainer had ever had any business transactions with plaintiff, and had never used his farm to board horses. Additionally, there is uncontradicted evidence that this horse, when found to be lame, was shipped by defendant's trainer not to plaintiff's farm, but back to the seller at Belmont Park. What is most important, the trial justice expressly stated that he believed the testimony of defendant's trainer that he had instructed Kelly that defendant would not be responsible for boarding the horse on any farm.
12. From our examination of the record we are constrained to conclude that the trial justice overlooked and misconceived material evidence which establishes beyond question that there never existed between the parties an element essential to the formulation of any true contract, namely, an intent to contract. Compare *Morrissey v. Piette*, R.I., 241 A.2d 302, 303.

II

13. The defendant's second contention is that, even assuming the trial justice was in essence predicating defendant's liability upon a quasi-contractual theory, his decision is still unsupported by competent evidence and is clearly erroneous.
14. The following discussion of quasi-contracts appears in 12 Am.Jur., Contracts, § 6 (1938) at pp. 503 to 504:

A quasi-contract has no reference to the intentions or expressions of the parties. The obligation is imposed despite, and frequently in frustration of, their intention. For a quasi contract neither promise nor privity, real or imagined, is necessary. In quasi contracts the obligation arises, not from consent of the parties, as in the case of contracts, express or implied in fact, but from the law of natural immutable justice and equity. The act, or acts, from which the law implies the contract must, however, be voluntary. Where a case shows that it is the duty of the defendant to pay, the law imputes to him a promise to fulfil that obligation. The duty, which thus forms the foundation of a quasi-contractual obligation, is frequently based on the doctrine of unjust enrichment. ... The law will not imply a promise against the express declaration of the party to be charged, made at the time of the supposed undertaking, unless such party is under legal obligation paramount to his will to perform some duty, and he is not under such legal obligation

unless there is a demand in equity and good conscience that he should perform the duty.

15. Therefore, the essential elements of a quasi-contract are a benefit conferred upon defendant by plaintiff, appreciation by defendant of such benefit, and acceptance and retention by defendant of such benefit under such circumstances that it would be inequitable to retain the benefit without payment of the value thereof. *Home Savings Bank v. General Finance Corp.*, 10 Wis.2d 417, 103 N.W.2d 117, 81 A.L.R.2d 580.
16. The key question raised by this appeal with respect to the establishment of a quasi-contract is whether or not plaintiff was acting as a “volunteer” at the time he accepted the horse for boarding at his farm. There is a long line of authority which has clearly enunciated the general rule that “if a performance is rendered by one person without any request by another, it is very unlikely that this person will be under a legal duty to pay compensation.” 1 A Corbin, Contracts § 234.
17. The Restatement of Restitution, § 2 (1937) provides: “A person who officiously confers a benefit upon another is not entitled to restitution therefor.” Comment a in the above-mentioned section states in part as follows:

Policy ordinarily requires that a person who has conferred a benefit...by way of giving another services...should not be permitted to require the other to pay therefor, unless the one conferring the benefit had a valid reason for so doing. A person is not required to deal with another unless he so desires and, ordinarily, a person should not be required to become an obligor unless he so desires.
18. Applying those principles to the facts in the case at bar it is clear that plaintiff cannot recover. The plaintiff's testimony on cross-examination is the only evidence in the record relating to what transpired between Kelly and him at the time the horse was accepted for boarding. The defendant's attorney asked plaintiff if he had any conversation with Kelly at that time, and plaintiff answered in substance that he had noticed that the horse was very lame and that Kelly had told him: “That's why they wouldn't accept him at Belmont Track.” The plaintiff also testified that he had inquired of Kelly as to the ownership of Bascom's Folly, and had been told that “Dr. Strauss made a deal and that's all I know.” It further appears from the record that plaintiff acknowledged receipt of the horse by signing a uniform livestock bill of lading, which clearly indicated on its face that the horse in question had been

consigned by defendant's trainer not to plaintiff, but to Dr. Strauss's trainer at Belmont Park. Knowing at the time he accepted the horse for boarding that a controversy surrounded its ownership, plaintiff could not reasonably expect remuneration from defendant, nor can it be said that defendant acquiesced in the conferment of a benefit upon him. The undisputed testimony was that defendant, upon receipt of plaintiff's first bill, immediately notified him that he was not the owner of Bascom's Folly and would not be responsible for its keep.

19. It is our judgment that the plaintiff was a mere volunteer who boarded and maintained Bascom's Folly at his own risk and with full knowledge that he might not be reimbursed for expenses he incurred incident thereto.
20. The plaintiff's appeal is denied and dismissed, the defendant's cross appeal is sustained, and the cause is remanded to the superior court for entry of judgment for the defendant.

Lucy v. Zehmer

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

BUCHANAN, J., delivered the opinion of the court.

1. This suit was instituted by W. O. Lucy and J. C. Lucy, complainants, against A. H. Zehmer and Ida S. Zehmer, his wife, defendants, to have specific performance of a contract by which it was alleged the Zehmers had sold to W. O. Lucy a tract of land owned by A. H. Zehmer in Dinwiddie county containing 471.6 acres, more or less, known as the Ferguson farm, for \$50,000. J. C. Lucy, the other complainant, is a brother of W. O. Lucy, to whom W. O. Lucy transferred a half interest in his alleged purchase.
2. The instrument sought to be enforced was written by A. H. Zehmer on December 20, 1952, in these words: "We hereby agree to sell to W. O. Lucy the Ferguson Farm complete for \$50,000.00, title satisfactory to buyer," and signed by the defendants, A. H. Zehmer and Ida S. Zehmer.
3. The answer of A. H. Zehmer admitted that at the time mentioned W. O. Lucy offered him \$50,000 cash for the farm, but that he, Zehmer, considered that the offer was made in jest; that so thinking, and both he and Lucy having had several drinks, he wrote out "the memorandum" quoted above and induced his wife to sign it; that he did not deliver the memorandum to Lucy, but that Lucy picked it up, read it, put it in his pocket, attempted to offer Zehmer \$5 to bind the bargain, which Zehmer refused to accept, and realizing for the first time that Lucy was serious, Zehmer assured him that he had no intention of selling the farm and that the whole matter was a joke. Lucy left the premises insisting that he had purchased the farm.
4. Depositions were taken and the decree appealed from was entered holding that the complainants had failed to establish their right to specific performance, and dismissing their bill. The assignment of error is to this action of the court.
5. W. O. Lucy, a lumberman and farmer, thus testified in substance: He had known Zehmer for fifteen or twenty years and had been familiar with the Ferguson farm for ten years. Seven or eight years ago he had offered Zehmer \$20,000 for the farm which Zehmer had accepted, but the agreement was verbal and Zehmer backed out.

On the night of December 20, 1952, around eight o'clock, he took an employee to McKenney, where Zehmer lived and operated a restaurant, filling station and motor court. While there he decided to see Zehmer and again try to buy the Ferguson farm. He entered the restaurant and talked to Mrs. Zehmer until Zehmer came in. He asked Zehmer if he had sold the Ferguson farm. Zehmer replied that he had not. Lucy said, "I bet you wouldn't take \$50,000.00 for that place." Zehmer replied, "Yes, I would too; you wouldn't give fifty." Lucy said he would and told Zehmer to write up an agreement to that effect. Zehmer took a restaurant check and wrote on the back of it, "I do hereby agree to sell to W. O. Lucy the Ferguson Farm for \$50,000 complete." Lucy told him he had better change it to "We" because Mrs. Zehmer would have to sign it too. Zehmer then tore up what he had written, wrote the agreement quoted above and asked Mrs. Zehmer, who was at the other end of the counter ten or twelve feet away, to sign it. Mrs. Zehmer said she would for \$50,000 and signed it. Zehmer brought it back and gave it to Lucy, who offered him \$5 which Zehmer refused, saying, "You don't need to give me any money, you got the agreement there signed by both of us."

6. The discussion leading to the signing of the agreement, said Lucy, lasted thirty or forty minutes, during which Zehmer seemed to doubt that Lucy could raise \$50,000. Lucy suggested the provision for having the title examined and Zehmer made the suggestion that he would sell it "complete, everything there," and stated that all he had on the farm was three heifers.
7. Lucy took a partly filled bottle of whiskey into the restaurant with him for the purpose of giving Zehmer a drink if he wanted it. Zehmer did, and he and Lucy had one or two drinks together. Lucy said that while he felt the drinks he took he was not intoxicated, and from the way Zehmer handled the transaction he did not think he was either.
8. December 20 was on Saturday. Next day Lucy telephoned to J. C. Lucy and arranged with the latter to take a half interest in the purchase and pay half of the consideration. On Monday he engaged an attorney to examine the title. The attorney reported favorably on December 31 and on January 2 Lucy wrote Zehmer stating that the title was satisfactory, that he was ready to pay the purchase price in cash and asking when Zehmer would be ready to close the deal. Zehmer replied by letter, mailed on January 13, asserting that he had never agreed or intended to sell.

9. Mr. and Mrs. Zehmer were called by the complainants as adverse witnesses. Zehmer testified in substance as follows:
10. He bought this farm more than ten years ago for \$11,000. He had had twenty-five offers, more or less, to buy it, including several from Lucy, who had never offered any specific sum of money. He had given them all the same answer, that he was not interested in selling it. On this Saturday night before Christmas it looked like everybody and his brother came by there to have a drink. He took a good many drinks during the afternoon and had a pint of his own. When he entered the restaurant around eight-thirty Lucy was there and he could see that he was "pretty high." He said to Lucy, "Boy, you got some good liquor, drinking, ain't you?" Lucy then offered him a drink. "I was already high as a Georgia pine, and didn't have any more better sense than to pour another great big slug out and gulp it down, and he took one too."
11. After they had talked a while Lucy asked whether he still had the Ferguson farm. He replied that he had not sold it and Lucy said, "I bet you wouldn't take \$50,000.00 for it." Zehmer asked him if he would give \$50,000 and Lucy said yes. Zehmer replied, "You haven't got \$50,000 in cash." Lucy said he did and Zehmer replied that he did not believe it. They argued "pro and con for a long time," mainly about "whether he had \$50,000 in cash that he could put up right then and buy that farm."
12. Finally, said Zehmer, Lucy told him if he didn't believe he had \$50,000, "you sign that piece of paper here and say you will take \$50,000.00 for the farm." He, Zehmer, "just grabbed the back off of a guest check there" and wrote on the back of it. At that point in his testimony Zehmer asked to see what he had written to "see if I recognize my own handwriting." He examined the paper and exclaimed, "Great balls of fire, I got 'Firgerson' for Ferguson. I have got satisfactory spelled wrong. I don't recognize that writing if I would see it, wouldn't know it was mine."
13. After Zehmer had, as he described it, "scribbled this thing off," Lucy said, "Get your wife to sign it." Zehmer walked over to where she was and she at first refused to sign but did so after he told her that he "was just needling him [Lucy], and didn't mean a thing in the world, that I was not selling the farm." Zehmer then "took it back over there...and I was still looking at the dern thing. I had the drink right there by my hand, and I reached over to get a drink, and he said, 'Let me see it.' He reached and picked it up, and when I looked back again he had it in his pocket and he dropped a five dollar bill over there, and he said, 'Here is five dollars payment on it.'...I said,

'Hell no, that is beer and liquor talking. I am not going to sell you the farm. I have told you that too many times before.'"

14. Mrs. Zehmer testified that when Lucy came into the restaurant he looked as if he had had a drink. When Zehmer came in he took a drink out of a bottle that Lucy handed him. She went back to help the waitress who was getting things ready for next day. Lucy and Zehmer were talking but she did not pay too much attention to what they were saying. She heard Lucy ask Zehmer if he had sold the Ferguson farm, and Zehmer replied that he had not and did not want to sell it. Lucy said, "I bet you wouldn't take \$50,000 cash for that farm," and Zehmer replied, "You haven't got \$50,000 cash." Lucy said, "I can get it." Zehmer said he might form a company and get it, "but you haven't got \$50,000.00 cash to pay me tonight." Lucy asked him if he would put it in writing that he would sell him this farm. Zehmer then wrote on the back of a pad, "I agree to sell the Ferguson Place to W. O. Lucy for \$50,000.00 cash." Lucy said, "All right, get your wife to sign it." Zehmer came back to where she was standing and said, "You want to put your name to this?" She said "No," but he said in an undertone, "It is nothing but a joke," and she signed it.
15. She said that only one paper was written and it said: "I hereby agree to sell," but the "I" had been changed to "We". However, she said she read what she signed and was then asked, "When you read 'We hereby agree to sell to W. O. Lucy,' what did you interpret that to mean, that particular phrase?" She said she thought that was a cash sale that night; but she also said that when she read that part about "title satisfactory to buyer" she understood that if the title was good Lucy would pay \$50,000 but if the title was bad he would have a right to reject it, and that that was her understanding at the time she signed her name.
16. On examination by her own counsel she said that her husband laid this piece of paper down after it was signed; that Lucy said to let him see it, took it, folded it and put it in his wallet, then said to Zehmer, "Let me give you \$5.00," but Zehmer said, "No, this is liquor talking. I don't want to sell the farm, I have told you that I want my son to have it. This is all a joke." Lucy then said at least twice, "Zehmer, you have sold your farm," wheeled around and started for the door. He paused at the door and said, "I will bring you \$50,000.00 tomorrow....No, tomorrow is Sunday. I will bring it to you Monday." She said you could tell definitely that he was drinking and she said to her husband, "You should have taken him home," but he said, "Well, I am just about as bad off as he is."

17. The waitress referred to by Mrs. Zehmer testified that when Lucy first came in “he was mouthy.” When Zehmer came in they were laughing and joking and she thought they took a drink or two. She was sweeping and cleaning up for next day. She said she heard Lucy tell Zehmer, “I will give you so much for the farm,” and Zehmer said, “You haven't got that much.” Lucy answered, “Oh, yes, I will give you that much.” Then “they jotted down something on paper ... and Mr. Lucy reached over and took it, said let me see it.” He looked at it, put it in his pocket and in about a minute he left. She was asked whether she saw Lucy offer Zehmer any money and replied, “He had five dollars laying up there, they didn't take it.” She said Zehmer told Lucy he didn't want his money “because he didn't have enough money to pay for his property, and wasn't going to sell his farm.” Both of them appeared to be drinking right much, she said.
18. She repeated on cross-examination that she was busy and paying no attention to what was going on. She was some distance away and did not see either of them sign the paper. She was asked whether she saw Zehmer put the agreement down on the table in front of Lucy, and her answer was this: “Time he got through writing whatever it was on the paper, Mr. Lucy reached over and said, ‘Let's see it.’ He took it and put it in his pocket,’ before showing it to Mrs. Zehmer.” Her version was that Lucy kept raising his offer until it got to \$50,000.
19. The defendants insist that the evidence was ample to support their contention that the writing sought to be enforced was prepared as a bluff or dare to force Lucy to admit that he did not have \$50,000; that the whole matter was a joke; that the writing was not delivered to Lucy and no binding contract was ever made between the parties.
20. It is an unusual, if not bizarre, defense. When made to the writing admittedly prepared by one of the defendants and signed by both, clear evidence is required to sustain it.
21. In his testimony Zehmer claimed that he “was high as a Georgia pine,” and that the transaction “was just a bunch of two doggoned drunks bluffing to see who could talk the biggest and say the most.” That claim is inconsistent with his attempt to testify in great detail as to what was said and what was done. It is contradicted by other evidence as to the condition of both parties, and rendered of no weight by the testimony of his wife that when Lucy left the restaurant she suggested that Zehmer drive him home. The record is convincing that Zehmer was not intoxicated to the

extent of being unable to comprehend the nature and consequences of the instrument he executed, and hence that instrument is not to be invalidated on that ground. 17 C.J.S., Contracts, § 133 b., p. 483; *Taliaferro v. Emery*, 124 Va. 674, 98 S.E. 627. It was in fact conceded by defendants' counsel in oral argument that under the evidence Zehmer was not too drunk to make a valid contract.

22. The evidence is convincing also that Zehmer wrote two agreements, the first one beginning "I hereby agree to sell." Zehmer first said he could not remember about that, then that "I don't think I wrote but one out." Mrs. Zehmer said that what he wrote was "I hereby agree," but that the "I" was changed to "We" after that night. The agreement that was written and signed is in the record and indicates no such change. Neither are the mistakes in spelling that Zehmer sought to point out readily apparent.
23. The appearance of the contract, the fact that it was under discussion for forty minutes or more before it was signed; Lucy's objection to the first draft because it was written in the singular, and he wanted Mrs. Zehmer to sign it also; the rewriting to meet that objection and the signing by Mrs. Zehmer; the discussion of what was to be included in the sale, the provision for the examination of the title, the completeness of the instrument that was executed, the taking possession of it by Lucy with no request or suggestion by either of the defendants that he give it back, are facts which furnish persuasive evidence that the execution of the contract was a serious business transaction rather than a casual, jesting matter as defendants now contend.
24. On Sunday, the day after the instrument was signed on Saturday night, there was a social gathering in a home in the town of McKenney at which there were general comments that the sale had been made. Mrs. Zehmer testified that on that occasion as she passed by a group of people, including Lucy, who were talking about the transaction, \$50,000 was mentioned, whereupon she stepped up and said, "Well, with the high-price whiskey you were drinking last night you should have paid more. That was cheap." Lucy testified that at that time Zehmer told him that he did not want to "stick" him or hold him to the agreement because he, Lucy, was too tight and didn't know what he was doing, to which Lucy replied that he was not too tight; that he had been stuck before and was going through with it. Zehmer's version was that he said to Lucy: "I am not trying to claim it wasn't a deal on account of the fact the price was too low. If I had wanted to sell \$50,000.00 would be a good price, in fact I think you would get stuck at \$50,000.00." A disinterested witness testified that what Zehmer

said to Lucy was that “he was going to let him up off the deal, because he thought he was too tight, didn't know what he was doing. Lucy said something to the effect that ‘I have been stuck before and I will go through with it.’”

25. If it be assumed, contrary to what we think the evidence shows, that Zehmer was jesting about selling his farm to Lucy and that the transaction was intended by him to be a joke, nevertheless the evidence shows that Lucy did not so understand it but considered it to be a serious business transaction and the contract to be binding on the Zehmers as well as on himself. The very next day he arranged with his brother to put up half the money and take a half interest in the land. The day after that he employed an attorney to examine the title. The next night, Tuesday, he was back at Zehmer's place and there Zehmer told him for the first time, Lucy said, that he wasn't going to sell and he told Zehmer, “You know you sold that place fair and square.” After receiving the report from his attorney that the title was good he wrote to Zehmer that he was ready to close the deal.
26. Not only did Lucy actually believe, but the evidence shows he was warranted in believing, that the contract represented a serious business transaction and a good faith sale and purchase of the farm.
27. In the field of contracts, as generally elsewhere, “We must look to the outward expression of a person as manifesting his intention rather than to his secret and unexpressed intention. ‘The law imputes to a person an intention corresponding to the reasonable meaning of his words and acts.’” *First Nat. Bank v. Roanoke Oil Co.*, 169 Va. 99, 114, 192 S.E. 764, 770.
28. At no time prior to the execution of the contract had Zehmer indicated to Lucy by word or act that he was not in earnest about selling the farm. They had argued about it and discussed its terms, as Zehmer admitted, for a long time. Lucy testified that if there was any jesting it was about paying \$50,000 that night. The contract and the evidence show that he was not expected to pay the money that night. Zehmer said that after the writing was signed he laid it down on the counter in front of Lucy. Lucy said Zehmer handed it to him. In any event there had been what appeared to be a good faith offer and a good faith acceptance, followed by the execution and apparent delivery of a written contract. Both said that Lucy put the writing in his pocket and then offered Zehmer \$5 to seal the bargain. Not until then, even under the defendants' evidence, was anything said or done to indicate that the matter was a joke. Both of the

Zehmers testified that when Zehmer asked his wife to sign he whispered that it was a joke so Lucy wouldn't hear and that it was not intended that he should hear.

29. The mental assent of the parties is not requisite for the formation of a contract. If the words or other acts of one of the parties have but one reasonable meaning, his undisclosed intention is immaterial except when an unreasonable meaning which he attaches to his manifestations is known to the other party. Restatement of the Law of Contracts, Vol. I, § 71, p. 74.

...The law, therefore, judges of an agreement between two persons exclusively from those expressions of their intentions which are communicated between them....

Clark on Contracts, 4 ed., § 3, p. 4.

30. An agreement or mutual assent is of course essential to a valid contract but the law imputes to a person an intention corresponding to the reasonable meaning of his words and acts. If his words and acts, judged by a reasonable standard, manifest an intention to agree, it is immaterial what may be the real but unexpressed state of his mind. 17 C.J.S., Contracts, § 32, p. 361; 12 Am. Jur., Contracts, § 19, p. 515.
31. So a person cannot set up that he was merely jesting when his conduct and words would warrant a reasonable person in believing that he intended a real agreement, 17 C.J.S., Contracts, § 47, p. 390; Clark on Contracts, 4 ed., § 27, at p. 54.
32. Whether the writing signed by the defendants and now sought to be enforced by the complainants was the result of a serious offer by Lucy and a serious acceptance by the defendants, or was a serious offer by Lucy and an acceptance in secret jest by the defendants, in either event it constituted a binding contract of sale between the parties.
33. Defendants contend further, however, that even though a contract was made, equity should decline to enforce it under the circumstances. These circumstances have been set forth in detail above. They disclose some drinking by the two parties but not to an extent that they were unable to understand fully what they were doing. There was no fraud, no misrepresentation, no sharp practice and no dealing between unequal parties. The farm had been bought for \$11,000 and was assessed for taxation at \$6,300. The purchase price was \$50,000. Zehmer admitted that it was a good price.

There is in fact present in this case none of the grounds usually urged against specific performance.

34. Specific performance, it is true, is not a matter of absolute or arbitrary right, but is addressed to the reasonable and sound discretion of the court. *First Nat. Bank v. Roanoke Oil Co., supra*, 169 Va. at p. 116, 192 S.E. at p. 771. But it is likewise true that the discretion which may be exercised is not an arbitrary or capricious one, but one which is controlled by the established doctrines and settled principles of equity; and, generally, where a contract is in its nature and circumstances unobjectionable, it is as much a matter of course for courts of equity to decree a specific performance of it as it is for a court of law to give damages for a breach of it. *Bond v. Crawford*, 193 Va. 437, 444, 69 S.E.2d 470, 475.
35. The complainants are entitled to have specific performance of the contracts sued on. The decree appealed from is therefore reversed and the cause is remanded for the entry of a proper decree requiring the defendants to perform the contract in accordance with the prayer of the bill.

Reversed and remanded.

Varney v. Ditmars

Court of Appeals of New York
217 N.Y. 223, 111 N.E. 822 (1916)

CHASE, Judge

1. This is an action brought for an alleged wrongful discharge of an employee. The defendant is an architect employing engineers, draftsmen and other assistants. The plaintiff is an architect and draftsman. In October, 1910, he applied to the defendant for employment and when asked what wages he wanted, replied that he would start for \$40 per week. He was employed at \$35 per week. A short time thereafter he informed the defendant that he had another position offered to him and the defendant said that if he would remain with him and help him through the work in his office he thought he could offer him a better future than anybody else. He continued in the employ of the defendant and became acquainted with a designer in the office and said designer and the plaintiff from time to time prior to the 1st of February, 1911, talked with the defendant about the work in his office. On that day by arrangement the two remained with the defendant after the regular office hours and the defendant said: "I am going to give you \$5 more a week; if you boys will go on and continue the way you have been and get me out of this trouble and get these jobs started that were in the office three years, on the first of next January I will close my books and give you a fair share of my profits. That was the result of the conversation. That was all of that conversation." The plaintiff was given charge of the drafting. Thereafter suggestions were made by the plaintiff and said designer about discharging many of the defendant's employees and employing new men and such suggestions were carried out and the two worked in the defendant's office over time and many Sundays and holidays. At least one piece of work that the defendant said had been in his office for three years was completed. The plaintiff on his cross-examination told the story of the employment of himself and said designer as follows: "And he says at that time 'I am going to give you \$5 more a week starting this week.' This was about Thursday. He says 'You boys go on and continue the work you are doing and the first of January next year I will close my books and give you a fair share of my profits.' Those were his exact words."
2. Thereafter the plaintiff was paid \$40 a week. On November 6, 1911, the night before the general election in this state, the defendant requested that all of his employees that

could do so, should work on election day. The plaintiff told the defendant that he wanted to remain at home to attend an election in the village where he lived. About four o'clock in the afternoon of election day he was taken ill and remained at his house ill until a time that as nearly as can be stated from the evidence was subsequent to December 1, 1911. On Saturday, November 11, the defendant caused to be delivered to the plaintiff a letter in which he said: "I am sending you herewith your pay for one day's work of seven hours, performed on Monday, the 6th inst. On Monday night, I made it my special duty to inform you that the office would be open all day Election Day and that I expected you and all the men to report for work. Much to my surprise and indignation, on Tuesday you made no appearance and all the men remained away, in obedience of your instructions to them of the previous evening. An act of this kind I consider one of extreme disloyalty and insubordination and I therefore am obliged to dispense with your services."

3. After the plaintiff had recovered from his illness and was able to do so he went to the defendant's office (the date does not appear) and told him that he was ready, willing and able to continue his services under the agreement. The defendant denied that he had any agreement with him and refused to permit him to continue in his service. Thereafter and prior to January 1, 1912, the plaintiff received for special work about \$50.
4. The plaintiff seeks to recover in this action for services from November 7, 1911, to December 31, 1911, inclusive, at \$40 per week and for a fair and reasonable percentage of the net profits of the defendant's business from February 1, 1911, to January 1, 1912, and demands judgment for \$1,680.
5. At the trial he was the only witness sworn as to the alleged contract and at the close of his case the complaint was dismissed.
6. The statement alleged to have been made by the defendant about giving the plaintiff and said designer a fair share of his profits is vague, indefinite and uncertain and the amount cannot be computed from anything that was said by the parties or by reference to any document, paper or other transaction. The minds of the parties never met upon any particular share of the defendant's profits to be given the employees or upon any plan by which such share could be computed or determined. The contract so far as it related to the special promise or inducement was never consummated. It was left subject to the will of the defendant or for further negotiation. It is urged that the

defendant by the use of the word "fair" in referring to a share of his profits, was as certain and definite as people are in the purchase and sale of a chattel when the price is not expressly agreed upon, and that if the agreement in question is declared to be too indefinite and uncertain to be enforced a similar conclusion must be reached in every case where a chattel is sold without expressly fixing the price therefor.

7. The question whether the words "fair" and "reasonable" have a definite and enforceable meaning when used in business transactions is dependent upon the intention of the parties in the use of such words and upon the subject-matter to which they refer. In cases of merchandising and in the purchase and sale of chattels the parties may use the words "fair and reasonable value" as synonymous with "market value." A promise to pay the fair market value of goods may be inferred from what is expressly agreed by the parties. The fair, reasonable or market value of goods can be shown by direct testimony of those competent to give such testimony. The competency to speak grows out of experience and knowledge. The testimony of such witnesses does not rest upon conjecture. The opinion of this court in *United Press v. N. Y. Press Co.* (164 N. Y. 406) was not intended to assert that a contract of sale is unenforceable unless the price is expressly mentioned and determined.
8. In the case of a contract for the sale of goods or for hire without a fixed price or consideration being named it will be presumed that a reasonable price or consideration is intended and the person who enters into such a contract for goods or service is liable therefor as on an implied contract. Such contracts are common, and when there is nothing therein to limit or prevent an implication as to the price, they are, so far as the terms of the contract are concerned, binding obligations.
9. The contract in question, so far as it relates to a share of the defendant's profits, is not only uncertain but it is necessarily affected by so many other facts that are in themselves indefinite and uncertain that the intention of the parties is pure conjecture. A fair share of the defendant's profits may be any amount from a nominal sum to a material part according to the particular views of the person whose guess is considered. Such an executory contract must rest for performance upon the honor and good faith of the parties making it. The courts cannot aid parties in such a case when they are unable or unwilling to agree upon the terms of their own proposed contract.
10. It is elementary in the law that, for the validity of a contract, the promise, or the agreement, of the parties to it must be certain and explicit and that their full intention

may be ascertained to a reasonable degree of certainty. Their agreement must be neither vague nor indefinite, and, if thus defective, parol proof cannot be resorted to. (*United Press v. N. Y. Press Co.*, *supra*, and cases cited; Ruling Case Law, vol. 6, 644.)

11. The courts in this state, in reliance upon and approval of the rule as stated in the *United Press* case, have decided many cases involving the same rule. Thus, in *Mackintosh v. Thompson* (58 App. Div. 25) and again in *Mackintosh v. Kimball* (101 App. Div. 494) the plaintiff sought to recover compensation in addition to a stated salary which he had received and which additional amount rested upon a claim by him that while he was employed by the defendants he informed them that he intended to leave their employ unless he was given an increase in salary, and that one of the defendants said to him that they would make it worth his while if he would stay on, and would increase his salary, and that his idea was to give him an interest in the profits on certain buildings that they were then erecting. The plaintiff further alleges that he asked what would be the amount of the increase and was told, "You can depend upon me; I will see that you get a satisfactory amount." The court held that the arrangement was too indefinite to form the basis of any obligation on the part of the defendants.
12. In *Bluemner v. Garvin* (120 App. Div. 29) the plaintiff and defendant were architects, and the plaintiff alleged that he drew plans for a public building in accordance with a contract held by the defendant and pursuant to a special agreement that if the plans were accepted the defendant would give him a fair share of the commissions to be received by him. The court held that a good cause of action was stated on *quantum meruit*, but that the contract was too vague and indefinite to be enforced.
13. A similar rule has been adopted in many other states. I mention a few of them. In *Fairplay School Township v. O'Neal* (127 Ind. 95) a verbal contract between a school trustee and a teacher, in which the latter undertook to teach school for a term in the district, and the trustee promised to pay her "good wages," it was held that the alleged contract was void for uncertainty as to compensation, and that the school township was not liable for its breach.
14. In *Dayton v. Stone* (111 Mich. 196) the plaintiff had sold to the defendant her stock of goods and fixtures, and by the contract of sale the undamaged goods were to be inventoried and taken at cost price, and the damaged goods at prices to be agreed

upon. In an action for breach of contract it was held that the contract was an entire one, and that so far as it left the price of the damaged goods to be fixed and determined it was uncertain and incomplete, and not one which could be enforced against the defendant.

15. In *Wittkowsky v. Wasson* (71 N. C. 451) it was held that where the price of certain property was to be fixed by agreement between the parties after the time of the agreement and they did not agree upon the price that the title to the property did not pass.
16. In *Adams v. Adams* (26 Ala. 272) a promise by a defendant for a valuable consideration to give his daughter a "full share of his property" which then and there was worth \$ 25,000 was held to be too indefinite and uncertain to support an action.
17. In *Van Slyke v. Broadway Ins. Co.* (115 Cal. 644) a contract between an insurance agent and the insurance company for a contingent commission of 5% which did not give the facts upon which the contingency depended nor state the sum on which the 5% was to be computed was held unenforceable and also that it could not be aided by parol.
18. In *Marvel v. Standard Oil Co.* (169 Mass. 553) a contract by which the defendant agreed to sell the plaintiff its oil on such reasonable terms as to enable him to compete successfully with other parties selling in the same territory was held to be too indefinite and too general to be enforceable as a contract.
19. In *Burks v. Stam* (65 Mo. App. 455) a contract for the sale of two race horses for a specified sum and providing for a further payment of a fixed sum by the purchaser if he did well and had no bad luck with the horses was held too vague to admit of enforcement.
20. In *Butler v. Kemmerer* (218 Pa. St. 242) the plaintiff was in the employ of the defendant at a regular salary and the defendant promised him that if there were any profits in the business he would divide them with the plaintiff "upon a very liberal basis." The action was brought to recover a part of the profits of the business and the court held that the contract was never made complete and that there was no standard by which to measure the degree of liberality with which the defendant should regard the plaintiff.

21. The only cases called to our attention that tend to sustain the appellant's position are *Noble v. Joseph Burnett Co.* (208 Mass. 75) and *Silver v. Graves* (210 Mass. 26). The first at least of such cases is distinguishable from the case under consideration, but in any event the decisions therein should not be held sufficient to sustain the plaintiff's contention in view of the authorities in this state.
22. The rule stated from the *United Press* case does not prevent a recovery upon *quantum meruit* in case one party to an alleged contract has performed in reliance upon the terms thereof, vague, indefinite and uncertain though they are. In such case the law will presume a promise to pay the reasonable value of the services. Judge Gray, who wrote the opinion in the *United Press* case, said therein: "I entertain no doubt that, where work has been done, or articles have been furnished, a recovery may be based upon *quantum meruit*, or *quantum valebat*; but, where a contract is of an executory character and requires performance over a future period of time, as here, and it is silent as to the price which is to be paid to the plaintiff during its term, I do not think that it possesses binding force. As the parties had omitted to make the price a subject of covenant, in the nature of things, it would have to be the subject of future agreement, or stipulation." (p. 412.)
23. In *Petze v. Morse Dry Dock & Repair Co.* (125 N.Y. App. Div. 267, 270) the court say: "There is no contract so long as any essential element is open to negotiation." In that case a contract was made by which an employee in addition to certain specified compensation was to receive 5% of the net distributable profits of a business and it was further provided that "the method of accounting to determine the net distributable profits is to be agreed upon later when the company's accounts have developed for a better understanding." The parties never agreed as to the method of determining the net profits and the plaintiff was discharged before the expiration of the term. The court in the opinion say that "the plaintiff could recover for what he had done on a *quantum meruit*, and the employment must be deemed to have commenced with a full understanding on the part of both parties that that was the situation." The judgment of the Appellate Division was unanimously affirmed without opinion in this court. (195 N. Y. 584.)
24. So, this case, while I do not think that the plaintiff can recover anything as extra work, yet if the work actually performed as stated was worth more than \$40 per week, he having performed until November 7, 1910, could, on a proper complaint, recover

its value less the amount received. (See *Bluemner v. Garvin*, *supra*; *S. C.*, 124 App. Div. 491; *King v. Broadhurst*, 164 App. Div. 689.)

25. The plaintiff claims that he at least should have been allowed to go to the jury on the question as to whether he was entitled to recover at the rate of \$40 per week from November 7, 1911, to December 31, 1911, inclusive. He did not perform any services for the defendant from November 6 until some time after December 1st, by reason of his illness. He has not shown just when he offered to return. It appears that between the time when he offered to return and January 1st he received \$50 for other services.
26. The amount that the plaintiff could recover, therefore, if any, based upon the agreement to pay \$40 per week would be very small, and he did not present to the court facts from which it could be computed. His employment by the defendant was conditional upon his continuing the way he had been working, getting the defendant out of his trouble and getting certain unenumerated jobs that were in the office three years, started. There was nothing in the contract specifying the length of service except as stated. It was not an unqualified agreement to continue the plaintiff in his service until the first of January, and it does not appear whether or not the special conditions upon which the contract was made had been performed. Even apart from the question whether the plaintiff's absence from the defendant's office by reason of his illness would permit the defendant to refuse to take him back into his employ, I do not think that on the testimony as it appears before us it was error to refuse to leave to the jury the question whether the plaintiff was entitled to recover anything [at] the rate of \$40 per week.
27. The judgment should be affirmed, with costs.

Cardozo, Judge ([concurring in the judgment in part and] dissenting [in part]).

28. I do not think it is true that a promise to pay an employee a fair share of the profits in addition to his salary is always and of necessity too vague to be enforced (*Noble v. Joseph Burnett Co.*, 208 Mass. 75; *Silver v. Graves*, 210 Mass. 26; *Brennan v. Employers Liability Assurance Corp., Ltd.*, 213 Mass. 365; *Joy v. St. Louis*, 138 U.S. 1, 43). The promise must, of course, appear to have been made with contractual intent (*Henderson Bridge Co. v. McGrath*, 134 U.S. 260, 275). But if that intent is present, it cannot be said from the mere form of the promise that the estimate of the reward is

inherently impossible. The data essential to measurement may be lacking in the particular instance, and yet they may conceivably be supplied. It is possible, for example, that in some occupations an employee would be able to prove a percentage regulated by custom. The difficulty in this case is not so much in the contract as in the evidence. Even if the data required for computation might conceivably have been supplied, the plaintiff did not supply them. He would not have supplied them if all the evidence which he offered, and which the court excluded, had been received. He has not failed because the nature of the contract is such that damages are of necessity incapable of proof. He has failed because he did not prove them.

29. There is nothing inconsistent with this view in *United Press v. N. Y. Press Co.* (164 N. Y. 406). The case is often cited as authority for the proposition that an agreement to buy merchandise at a fair and reasonable price is so indefinite that an action may not be maintained for its breach in so far as it is still executory. Nothing of the kind was decided, or with reason could have been. What the court did was to construe a particular agreement, and to hold that the parties intended to reserve the price for future adjustment. If instead of reserving the price for future adjustment, they had manifested an intent on the one hand to pay and on the other to accept a fair price, the case is far from holding that a jury could not determine what such a price would be and assess the damages accordingly. Such an intent, moreover, might be manifested not only through express words, but also through reasonable implication. It was because there was neither an express statement nor a reasonable implication of such an intent that the court held the agreement void to the extent that it had not been executed.
30. On the ground that the plaintiff failed to supply the data essential to computation, I concur in the conclusion that profits were not to be included as an element of damage. I do not concur, however, in the conclusion that he failed to make out a case of damage to the extent of his loss of salary. The amount may be small, but none the less it belongs to him. The hiring was not at will (*Watson v. Gugino*, 204 N. Y. 535; *Martin v. N. Y. Life Ins. Co.*, 148 N. Y. 117). The plain implication was that it should continue until the end of the year when the books were to be closed. The evidence would permit the jury to find that the plaintiff was discharged without cause, and he is entitled to damages measured by his salary for the unexpired term.
31. The judgment should be reversed and a new trial granted, with costs to abide the event.

D.R. Curtis, Co. v. Matthews

Court of Appeals of Idaho
103 Idaho 776; 653 P.2d 1188 (1982)

WALTERS, C.J.

1. This case involves the enforceability of a contract for the sale of goods where the parties left a factor in the price term to be agreed upon and failed to subsequently agree on the factor left open. Grant Mathews, a grain farmer, appeals a judgment holding him in breach of a contract for the sale of hard red spring wheat, and ordering him to pay \$12,450 damages to D.R. Curtis Company. We affirm the judgment.
2. The respondent, D.R. Curtis Company, is a brokerage firm in the farm commodity market. As a "middleman" between producers and exporters of farm commodities, Curtis Company buys crops directly from a farmer and then sells the crop to the exporter. Thus, for each contract to purchase grain from a producer, Curtis Company makes an interrelated, but independent, agreement to sell the grain to a grain exporter. When the company deals with hard red spring wheat for export, the grain is generally sold to large export companies in the Portland, Oregon ("North Coast"), exchange. Grain sold in this exchange is delivered to and shipped from Portland.
3. In April, 1978, Raleigh Curtis, a grain broker for Curtis Company, contacted Mathews by telephone to discuss the purchase of Mathews' hard red spring wheat crop. Mathews had never before sold his grain to Curtis Company, although he had sold other crops to the company. Nor had he ever before dealt in the Portland grain export market. His experience was limited to the procedures in the domestic grain market at Ogden, Utah. Raleigh Curtis informed Mathews that the then current price of hard red spring wheat at the Portland grain terminal was \$3.58 per bushel. That price was attractive, so Mathews orally agreed to sell 30,000 bushels to Curtis Company.
4. Both Mathews and Curtis Company, from prior dealings in the hard red spring wheat market, realized that although an express price per bushel is agreed upon, the price actually to be paid for the grain is not fixed until the grain is delivered to market. The actual price is determined, with respect to the expressed contract price term, by three factors: the protein content of the grain, the protein "basis" figure, and the protein

"scale." The protein content, i.e., the actual percentage of protein in the grain, is commonly determined in the grain market at the time of delivery. The protein "basis" is a figure ordinarily agreed upon between the broker and the exporter, at the time they contract, in advance of delivery. The protein "scale" is commonly determined by the grain exporter on the day the wheat is delivered to the grain terminal.

5. Protein "basis" is a standard against which the actual protein content is compared. If the protein content coincides with the fixed protein "basis" figure, then the price paid per bushel coincides with the price expressed in the contract. When protein content and protein "basis" do not coincide, the actual price paid for the grain is determined on the protein "scale," which runs up and down from the protein "basis." The "scale" is expressed as cents-per-bushel for each one-quarter-percent by which the protein content exceeds, or falls short of, the protein "basis" figure.
6. Mathews testified that he expected the "basis" figure in his agreement with Curtis Company to be established by mutual agreement with Curtis Company. Because Curtis was unable to ascertain a protein "basis" figure while negotiating with Mathews, and because protein "scale" was commonly set by the grain export company on the day the grain was delivered, protein "basis" and protein "scale" were left open, to be established later.
7. On the day after their oral agreement, Raleigh Curtis signed and mailed a written memorandum to Mathews. It stated the terms of the agreement as follows: "\$3.58 per bushel. Delivered Rail North Coast. . . . Hard Red Spring Wheat -- Protein scale to be established." No reference to a protein "basis" term or to a means of establishing the term was made. Mathews later testified that because protein "basis" was not mentioned he understood the written terms of the contract to mean that a protein "basis" figure was either not required or was still mutually to be agreed upon. He signed and returned the memorandum. Curtis Company sold the quantity of grain commensurate with this purchase to exporters within twenty-four hours of the purchase.
8. In September, at harvest time, Curtis Company informed Mathews that fourteen percent was the protein "basis" figure for the grain contract. The company had known that a "basis" of fourteen was required at the time they sold the grain to the grain export companies. It is not clear why Curtis Company waited until September to inform Mathews of the fourteen percent protein "basis" figure. Mathews replied he

could not meet that figure, and he disavowed any contract. Thereafter, the parties continued to communicate, with Curtis Company trying to assure itself that Mathews had arranged to deliver the grain to Portland.

9. Curtis Company employees went to Mathews' farm in November to test the protein content of his hard red spring wheat and to check his progress in arranging to deliver the grain. When they arrived, Mathews informed them that he had already sold his grain through the Ogden domestic market. Curtis Company then filed this suit for breach of contract.
10. The trial court determined that the parties had entered into the oral agreement and had executed the written memorandum with the intent to enter into a binding contract. Because Mathews failed to deliver the grain as required by the contract, the court concluded that Mathews breached the contract. Curtis Company was awarded \$12,450 as the cost of "cover."
11. On appeal, Mathews contends that the trial court erred in determining how price was to be determined under the contract. He further argues that the contract should fail because it is ambiguous and indefinite. Mathews asserts that Finding of Fact No. 11 is not supported by substantial and competent evidence. He alleges the error stems from a failure to distinguish between protein scale and protein basis. Assuming that no agreement was reached regarding protein basis, he urges that the contract is unenforceable because it is ambiguous and indefinite. He also asserts that the trial court applied an incorrect measure of damages.
12. We first address the alleged error in Finding of Fact No. 11. It appears undisputed that both Mathews and Curtis Company, from prior dealings in the grain market, knew that protein "scale" was established by the export purchaser on the date of delivery and at the place of delivery. It is not disputed that the parties expressly agreed that protein scale was to be established in this manner. On the other hand, the record does not show that Mathews and Curtis Company agreed to accept the "basis" figure fixed in the market. Consequently, we do not find substantial evidence in the record to support that part of Finding No. 11 which states "[that] the contract provided . . . [for] basis to be established on the date of delivery which is prevailing in the market at the place of delivery." We do not conclude, however, that this error materially affects the ultimate holding of the trial court.

13. The trial court found that the parties had the requisite intent to form a binding contract for sale at the time they entered into the contract. This finding is supported by competent and substantial evidence and we will not disturb it on appeal. I.R.C.P. 52(a); *Nesbitt v. Wolfkiel*, 100 Idaho 396, 598 P.2d 1046 (1979). Parties to a contract for the sale of goods may make a binding contract for sale even though the price is not settled, so long as they intend to enter into a binding contract. I.C. §§ 28-2-305, 28-2-204(3). That is, in the sale of goods, a contract will not fail on the grounds of indefiniteness when the price term is left open, *see* I.C. § 28-2-305, comment 1, so long as the agreement is entered with the mutual intent of the parties to make a binding contract.
14. If the price in such a binding contract is left open by the parties to be established by later agreement and they fail to reach later agreement, the parties are still bound to perform under the contract for the sale of goods. In such a case, the price is a reasonable price at the time for delivery. I.C. § 28-2-305(1)(b).
15. Here, the protein "basis" was a component of price; and, therefore it was an essential term of the contract for sale of the wheat. The term was left open to be established by the parties at a later date. The fact that this term was left open to be established, and the parties failed to reach an agreement on the figure, does not make the contract ambiguous or void for indefiniteness. It simply means that a reasonable figure remained to be determined. The record discloses no proof that a fourteen percent "basis" figure was unreasonable in the "North Coast" market. We hold that the trial court correctly determined that Mathews breached the contract for sale of grain.
16. In regard to the damages question, the trial court correctly determined that the proper standard for damages for nondelivery of the grain was the difference between the market price at the time the buyer learned of the breach and the contract price. I.C. § 28-2-713. The trial court found that Curtis Company learned of the breach on November 6 when Mathews refused to deliver the grain. The Portland market price for hard red spring wheat on this date was \$3.99½ per bushel. This was \$0.41½ more than the contract price of \$ 3.58 per bushel. Thus, \$0.41½ (damages per bushel) multiplied by 30,000 bushels gives a figure of \$12,450, which the trial court awarded as damages.

17. Mathews argues that Curtis Company first learned that the grain would not be delivered in September when he stated that he was not going to deliver his grain subject to a fourteen percent "basis" requirement. Thus, he argues, the trial court erred by using the November 6 market price instead of September market prices in the computation of damages. Determination of the date when the buyer learned of the breach is a question of fact. Conflicting evidence exists in the record concerning the date when Curtis Company first learned that Mathews did not intend to deliver his grain pursuant to the contract. Mathews did inform Curtis Company in September that he would not agree to the fourteen percent figure. However, after that time he continued to communicate by telephone with Curtis Company employees, and he was still apparently willing to load his grain on Curtis Company trucks. The trial court made no mention of the September date in its findings of fact. The finding of the trial court that the breach occurred on November 6 is supported by substantial and competent evidence. Although conflicting evidence does exist, we will not disturb this finding. *J.E.T. Development v. Dorsey Const. Co.*, 102 Idaho 863, 642 P.2d 954 (Ct.App.1982).
18. Finally, Curtis Company requests that it be allowed recovery of a reasonable attorney fee for defense of this appeal. The request is made pursuant to I.C. § 12-120(2), which provides that in any action to recover on a contract relating to the purchase or sale of goods, the prevailing party shall be allowed a reasonable attorney fee to be set by the court, to be taxed and collected as costs. Curtis Company is the prevailing party both at trial and on this appeal. The action involves recovery for breach of a contract for the sale of goods. The request is therefore proper and is granted, subject to I.A.R. 41. *McKee Bros., Ltd. v. Mesa Equipment, Inc.*, 102 Idaho 202, 628 P.2d 1036 (1981).
19. The judgment is affirmed; costs and attorney fees to respondent, Curtis Company. BURNETT and SWANSTROM, JJ., concur.

Hamer v. Sidway

Court of Appeals of New York
124 N.Y. 538, 27 N.E. 256 (1891)

1. APPEAL from order of the General Term of the Supreme Court in the fourth judicial department, made July 1, 1890, which reversed a judgment in favor of plaintiff entered upon a decision of the court on trial at Special Term and granted a new trial.
2. This action was brought upon an alleged contract.
3. The plaintiff presented a claim to the executor of William E. Story, Sr., for \$5,000 and interest from the 6th day of February, 1875. She acquired it through several mesne assignments from William E. Story, 2d. The claim being rejected by the executor, this action was brought. It appears that William E. Story, Sr., was the uncle of William E. Story, 2d; that at the celebration of the golden wedding [anniversary] of Samuel Story and wife, father and mother of William E. Story, Sr., on the 20th day of March, 1869, in the presence of the family and invited guests he promised his nephew that if he would refrain from drinking, using tobacco, swearing and playing cards or billiards for money until he became twenty-one years of age he would pay him a sum of \$5,000. The nephew assented thereto and fully performed the conditions inducing the promise. When the nephew arrived at the age of twenty-one years and on the 31st day of January, 1875, he wrote to his uncle informing him that he had performed his part of the agreement and had thereby become entitled to the sum of \$5,000. The uncle received the letter and a few days later and on the sixth of February, he wrote and mailed to his nephew the following letter:

BUFFALO, Feb. 6, 1875.

W. E. STORY, Jr.:

DEAR NEPHEW--Your letter of the 31st ult. came to hand all right, saying that you had lived up to the promise made to me several years ago. I have no doubt but you have, for which you shall have five thousand dollars as I promised you. I had the money in the bank the day you was 21 years old that I intend for you, and you shall have the money certain. Now, Willie I do not intend to interfere with this money in any way till I think you are capable of taking care of it and the sooner that time comes the better it will please me. I would hate very much to have you start out in some adventure that you thought all right and lose this money in one year. The first five thousand

dollars that I got together cost me a heap of hard work. You would hardly believe me when I tell you that to obtain this I shoved a jackplane many a day, butchered three or four years, then came to this city, and after three months' perseverance I obtained a situation in a grocery store. I opened this store early, closed late, slept in the fourth story of the building in a room 30 by 40 feet and not a human being in the building but myself. All this I done to live as cheap as I could to save something. I don't want you to take up with this kind of fare. I was here in the cholera season '49 and '52 and the deaths averaged 80 to 125 daily and plenty of small-pox. I wanted to go home, but Mr. Fisk, the gentleman I was working for, told me if I left then, after it got healthy he probably would not want me. I stayed. All the money I have saved I know just how I got it. It did not come to me in any mysterious way, and the reason I speak of this is that money got in this way stops longer with a fellow that gets it with hard knocks than it does when he finds it. Willie, you are 21 and you have many a thing to learn yet. This money you have earned much easier than I did besides acquiring good habits at the same time and you are quite welcome to the money; hope you will make good use of it. I was ten long years getting this together after I was your age. Now, hoping this will be satisfactory, I stop. One thing more. Twenty-one years ago I bought you 15 sheep. These sheep were put out to double every four years. I kept track of them the first eight years; I have not heard much about them since. Your father and grandfather promised me that they would look after them till you were of age. Have they done so? I hope they have. By this time you have between five and six hundred sheep, worth a nice little income this spring. Willie, I have said much more than I expected to; hope you can make out what I have written. To-day is the seventeenth day that I have not been out of my room, and have had the doctor as many days. Am a little better to-day; think I will get out next week. You need not mention to father, as he always worries about small matters.

Truly Yours,

W. E. STORY.

P. S.--You can consider this money on interest.

4. The nephew received the letter and thereafter consented that the money should remain with his uncle in accordance with the terms and conditions of the letters. The uncle died on the 29th day of January, 1887, without having paid over to his nephew any portion of the said \$5,000 and interest.

PARKER, J.

5. The question which provoked the most discussion by counsel on this appeal, and which lies at the foundation of plaintiff's asserted right of recovery, is whether by virtue of a contract defendant's testator William E. Story became indebted to his nephew William E. Story, 2d, on his twenty-first birthday in the sum of five thousand dollars. The trial court found as a fact that "on the 20th day of March, 1869, ... William E. Story agreed to and with William E. Story, 2d, that if he would refrain from drinking liquor, using tobacco, swearing, and playing cards or billiards for money until he should become 21 years of age then he, the said William E. Story, would at that time pay him, the said William E. Story, 2d, the sum of \$5,000 for such refraining, to which the said William E. Story, 2d, agreed," and that he "in all things fully performed his part of said agreement."
6. The defendant contends that the contract was without consideration to support it, and, therefore, invalid. He asserts that the promisee by refraining from the use of liquor and tobacco was not harmed but benefited; that that which he did was best for him to do independently of his uncle's promise, and insists that it follows that unless the promisor was benefited, the contract was without consideration. A contention, which if well founded, would seem to leave open for controversy in many cases whether that which the promisee did or omitted to do was, in fact, of such benefit to him as to leave no consideration to support the enforcement of the promisor's agreement. Such a rule could not be tolerated, and is without foundation in the law. The Exchequer Chamber, in 1875, defined consideration as follows: "A valuable consideration in the sense of the law may consist either in some right, interest, profit or benefit accruing to the one party, or some forbearance, detriment, loss or responsibility given, suffered or undertaken by the other." Courts "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." (Anson's Prin. of Con. 63.)
7. "In general a waiver of any legal right at the request of another party is a sufficient consideration for a promise." (Parsons on Contracts, 444.)
8. "Any damage, or suspension, or forbearance of a right will be sufficient to sustain a promise." (Kent, vol. 2, 465, 12th ed.)

9. Pollock, in his work on contracts, page 166, after citing the definition given by the Exchequer Chamber already quoted, says: “The second branch of this judicial description is really the most important one. Consideration means not so much that one party is profiting as that the other abandons some legal right in the present or limits his legal freedom of action in the future as an inducement for the promise of the first.”
10. Now, applying this rule to the facts before us, the promisee used tobacco, occasionally drank liquor, and he had a legal right to do so. That right he abandoned for a period of years upon the strength of the promise of the testator that for such forbearance he would give him \$5,000. We need not speculate on the effort which may have been required to give up the use of those stimulants. It is sufficient that he restricted his lawful freedom of action within certain prescribed limits upon the faith of his uncle's agreement, and now having fully performed the conditions imposed, it is of no moment whether such performance actually proved a benefit to the promisor, and the court will not inquire into it, but were it a proper subject of inquiry, we see nothing in this record that would permit a determination that the uncle was not benefited in a legal sense. Few cases have been found which may be said to be precisely in point, but such as have been support the position we have taken.
11. In *Shadwell v. Shadwell* (9 C. B. [N. S.] 159), an uncle wrote to his nephew as follows:

MY DEAR LANCEY

I am so glad to hear of your intended marriage with Ellen Nicholl, and as I promised to assist you at starting, I am happy to tell you that I will pay to you 150 pounds yearly during my life and until your annual income derived from your profession of a chancery barrister shall amount to 600 guineas, of which your own admission will be the only evidence that I shall require.

Your affectionate uncle,

CHARLES SHADWELL.

It was held that the promise was binding and made upon good consideration.

12. In *Lakota v. Newton*, an unreported case in the Superior Court of Worcester, Mass., the complaint averred defendant's promise that “if you (meaning plaintiff) will leave

off drinking for a year I will give you \$100,” plaintiff’s assent thereto, performance of the condition by him, and demanded judgment therefor. Defendant demurred on the ground, among others, that the plaintiff’s declaration did not allege a valid and sufficient consideration for the agreement of the defendant. The demurrer was overruled.

13. In *Talbott v. Stemmons*, 12 S. W. Rep. 297, (a Kentucky case not yet reported), the step-grandmother of the plaintiff made with him the following agreement: “I do promise and bind myself to give my grandson, Albert R. Talbott, \$500 at my death, if he will never take another chew of tobacco or smoke another cigar during my life from this date up to my death, and if he breaks this pledge he is to refund double the amount to his mother.” The executor of Mrs. Stemmons demurred to the complaint on the ground that the agreement was not based on a sufficient consideration. The demurrer was sustained and an appeal taken therefrom to the Court of Appeals, where the decision of the court below was reversed. In the opinion of the court it is said that “the right to use and enjoy the use of tobacco was a right that belonged to the plaintiff and not forbidden by law. The abandonment of its use may have saved him money or contributed to his health, nevertheless, the surrender of that right caused the promise, and having the right to contract with reference to the subject-matter, the abandonment of the use was a sufficient consideration to uphold the promise.” Abstinence from the use of intoxicating liquors was held to furnish a good consideration for a promissory note in *Lindell v. Rokes* (60 Mo. 249)....
14. The order appealed from should be reversed and the judgment of the Special Term affirmed, with costs payable out of the estate.

St. Peter v. Pioneer Theatre Corp.

Supreme Court of Iowa
227 Iowa 1391, 291 N.W. 164 (1940)

MILLER, Justice.

1. This controversy involves a drawing at a theatre under an arrangement designated as “bank night”, not identical with, but substantially similar to the arrangement involved in the controversy heretofore presented to this court by the case of *State v. Hundling*, 220 Iowa 1369, 264 N.W. 608, 103 A.L.R. 861. In that case, we held that the arrangement was not a lottery in violation of the provisions of Section 13218 of the Code, 1931, and that the proprietor of the theatre was not subject to criminal prosecution. In this case, we are confronted with the question whether the arrangement is such that one, to whom the prize is awarded, has a cause of action to enforce the payment thereof.
2. Plaintiff's petition alleges that the Pioneer Theatre Corporation operates a theatre at Jefferson, Iowa, known as the Iowa Theatre, and that the defendant Parkinson was at all times material herein manager of such theatre. The bank night drawing by defendants was conducted on Wednesday evening, at about 9 p.m. On December 21, 1938, the prize or purse was advertised by defendants in the amount of \$275. At about 9 p.m., plaintiff and her husband were outside the theatre when an agent of the defendants announced that plaintiff's name had been called. Plaintiff immediately went into the theatre and made demand upon the manager, who refused to pay her the prize or purse, although plaintiff made demand therefor within the three minutes allowed by defendants. Plaintiff demanded judgment for the \$275 and costs.
3. In count II of the plaintiff's petition, plaintiff alleged that her husband's name was drawn, he presented himself within three minutes, demanded the \$275 and payment was refused, if he was not within the allotted time it was due to acts of defendants, her husband assigned his claim to plaintiff and plaintiff demanded judgment as such assignee.
4. Defendants' answer admitted that the Pioneer Theatre Corporation is operating the Iowa Theatre at Jefferson, Iowa, and that the defendant Parkinson is and has been for more than five years manager of said Iowa Theatre for the corporate defendant. The answer denied all other allegations of both counts of the petition.

5. The only witnesses to testify at the trial were the plaintiff and her husband. Their testimony is not in conflict. Accordingly, no disputed question of fact is presented, only questions of law.
6. They testified that each had signed the bank night register, plaintiff's number was 6396, her husband's number 212. The husband signed the register at the express invitation and request of Parkinson. Plaintiff signed the register later at the theatre in the presence of an usher. Plaintiff attended every bank night, often accompanied by her husband. Sometimes they attended as patrons of the theatre. Other times they stood on the sidewalk outside. On the occasions when they remained on the sidewalk outside the theatre, one Alice Kafer habitually announced the name that had been drawn inside the theatre. The only other person seen by them to make such announcement was Parkinson.
7. On the evening of December 21, 1938, plaintiff and her husband were on the sidewalk in front of the theatre. They observed a sign reading "Bank Night \$275". About 9 o'clock Alice Kafer came out and said to plaintiff, "Hurry up Mrs. St. Peter, your name is called." Plaintiff entered the theatre and called to Parkinson. He came back and said, "I am sorry, but it was your husband's name that was called, where is your husband?" She said, "He is right behind me," turned around and motioned to him and said, "It's your name that was called." As he started toward them, the lights went out and in the darkness they lost track of Parkinson. They sent an usher to look for him. When Parkinson came out and approached them he said to plaintiff's husband, "You are too late, just one second too late." Mr. St. Peter said, "You have a pretty good watch." Parkinson replied, "One second is just as good as a week." Mr. St. Peter said, "Why don't you call the name outside like you do inside?" Parkinson replied, "I have a lady hired to call the name out." When asked who she was, he said, "It's none of your business." When told that Mr. St. Peter intended to see a lawyer, Parkinson stated, "That is what we want you to do; the law is backing us up on our side." Plaintiff and her husband then left the theatre. Plaintiff's husband testified that he assigned his claim to the plaintiff before the action was commenced.
8. At the close of plaintiff's evidence, which consisted solely of her testimony, that of her husband, and defendants' bank night register, defendants made a motion for a directed verdict on seven grounds, to wit: (1) there was no adequate or legal consideration for the claimed promise to give the alleged purse, (2) there was no evidence that Alice Kafer was employed by or in any manner authorized by

defendants to announce the winner of the drawing, and defendants were not bound by her statements, (3) the most that could be claimed for plaintiff's alleged cause of action was a mere executory agreement to make a gift upon the happening of certain events without legal or adequate consideration, and no recovery could be had, (4) if a verdict were returned for plaintiff under the evidence offered, it would be the duty of the court to set the same aside, (5) there was no evidence that either plaintiff or her husband claimed the purse within the time limit fixed by defendants, (6) there was no relevant, competent or material proof that the name of either plaintiff or her husband was drawn, (7) if there is any legal or sufficient consideration for the promise sought to be enforced, then such consideration would constitute the transaction a lottery and, therefore, an illegal transaction upon which no recovery could be had.

9. The court sustained the motion generally. A verdict for the defendants was returned accordingly and judgment was entered dismissing the action at plaintiff's costs. Plaintiff appeals, assigning as error the sustaining of the motion and the entry of judgment pursuant thereto.

I.

10. Since the motion was sustained generally, it is incumbent upon appellant, before she would be entitled to a reversal at our hands, to establish that the motion was not good upon any ground thereof. *People's Trust & Savings Bank v. Smith*, 212 Iowa 124, 126, 236 N.W. 30, 31; *Slippy Eng. Corp. v. City of Grinnell*, 226 Iowa 1293, 286 N.W. 508, 513. Realizing such burden, and undertaking to discharge the same, appellant has made seven assignments of error, each attacking a similarly numbered paragraph of the motion for directed verdict.

II.

11. Appellant's assignments of error Nos. 1, 3 and 7, attacking paragraphs 1, 3 and 7 of the motion for directed verdict, are definitely related to each other, and will be considered together. In such consideration, we are faced at the outset with our decision in the case of *State v. Hundling*, 220 Iowa 1369, 264 N.W. 608, 103 A.L.R. 861, heretofore referred to, wherein we held that an arrangement such as is involved herein does not constitute a lottery, and that the proprietor of the theatre is not subject to criminal prosecution on account thereof. In defining a lottery, we state at page 1370 of 220 Iowa, at page 609 of 264 N.W., 103 A.L.R. 861, as follows: "The giving away of property or prizes is not unlawful, nor is the gift made unlawful by the fact

that the recipient is determined by lot. Our statute provides that the recipient of a public office may be determined by lot in certain cases where there is a tie vote. Section 883, Code 1931. To constitute a lottery there must be a further element, and that is the payment of a valuable consideration for the chance to receive the prize. Thus, it is quite generally recognized that there are three elements necessary to constitute a lottery: First, a prize to be given; second, upon a contingency to be determined by chance; and, third, to a person who has paid some valuable consideration or hazarded something of value for the chance.”

12. In applying such definition to the facts presented in that case, we state at page 1371 of 220 Iowa, at page 609 of 264 N.W., 103 A.L.R. 861, as follows:

The term “lottery,” as popularly and generally used, refers to a gambling scheme in which chances are sold or disposed of for value and the sums thus paid are hazarded in the hope of winning a much larger sum. That is the predominant characteristic of lotteries which has become known to history and is the source of the evil which attends a lottery, in that it arouses the gambling spirit and leads people to hazard their substance on a mere chance. It is undoubtedly the evil against which our statute is directed. The provisions of the statute making it a crime to have possession of lottery tickets with intent to sell or dispose of them indicates not only what is regarded as characteristic of a lottery, but it indicates the particular incident of a lottery which is regarded as an evil. To have a lottery, therefore, he who has the chance to win the prize must pay, or agree to pay, something of value for that chance.

In the particular scheme under consideration here, there is no question but [that] two elements of a lottery are present, first, a prize, and, second, a determination of the recipient by lot. Difficulty arises in the third element, namely, the payment of some valuable consideration for the chance by the holder thereof. The holder of the chance to win the prize in the case at bar was required to do two things in order to be eligible to receive the prize, first, to sign his name in the book, and, second, be in such proximity to the theater as that he could claim the prize within two and one-half minutes after his name was announced. He was not required to purchase a ticket of admission to the theater either as a condition to signing the registration book or claiming the prize when his name was drawn. In other words, paying admission to the theater added nothing to the chance. Where then is the payment by the holder

of the chance of a valuable consideration for the chance, which is necessary in order to make the scheme a lottery?

13. In holding that there was not such a valuable consideration as would constitute the arrangement a lottery, we state at page 1372 of 220 Iowa, at page 610 of 264 N.W., 103 A.L.R. 861, as follows: “It is urged on behalf of the state that the defendant theater manager gained some benefit, or hoped to gain some benefit, from the scheme in the way of increased attendance at his theater, and that this would afford the consideration required. If it be conceded that the attendance at the theater on the particular night that the prize was to be given away was stimulated by reason of the scheme, it is difficult to see how that would make the scheme a lottery. The question is not whether the donor of the prize makes a profit in some remote and indirect way, but, rather, whether those who have a chance at the prize pay anything of value for that chance. Every scheme of advertising, including the giving away of premiums and prizes, naturally has for its object, not purely a philanthropic purpose, but increased business. . . . Profit accruing remotely and indirectly to the person who gives the prize is not a substitute for the requirement that he who has the chance to win the prize must pay a valuable consideration therefor, in order to make the scheme a lottery.”
14. Appellees rely upon the language above quoted to support their contention that the arrangement involved in both cases constitutes merely an offer to make a gift, which is not supported by a valuable consideration and is, therefore, unenforceable.
15. In 12 American Jurisprudence, pages 564 and 565, in Section 72, it is stated, “It is well settled, however, that ordinarily consideration is an essential element of a simple contract, and want or lack of consideration is an excuse for nonperformance of a promise.” It is also stated, “The policy of the courts in requiring a consideration for the maintenance of an action of assumpsit appears to be to prevent the enforcement of gratuitous promises.” Such principles have been recognized by this court. In the case of *Farlow v. Farlow*, 154 Iowa 647, 135 N.W. 1, we held that a promise to make a gift is without consideration and not enforceable. See also, *Lanfier v. Lanfier*, Iowa, 288 N.W. 104.
16. Appellees contend that the foregoing principles, considered with our statements in *State v. Hundling*, *supra*, show that this action is based upon a promise that cannot be enforced. In the *Hundling* case, we state, “The giving away of property or prizes is not unlawful,” and, “profit accruing remotely and indirectly to the person who gives

the prize is not a substitute for the requirement that he who has a chance to win the prize must pay a valuable consideration therefor.” Appellees contend that these pronouncements commit us to the proposition that the arrangement involved herein constituted nothing more than a promise to make a gift which is not supported by a legal consideration, and, accordingly, is not enforceable. We are unable to agree with the contentions of appellees.

17. At the outset, it is important to bear in mind that the plaintiff herein seeks to recover on a unilateral contract. A bilateral contract is one in which two promises are made; the promise of each party to the contract is consideration for the promise of the other party. In a unilateral contract, only one party makes a promise. If that promise is made contingent upon the other party doing some act, which he is not under legal obligation to do, or forbearing an action which he has a legal right to take, then such affirmative act or forbearance constitutes the consideration for and acceptance of the promise.
18. In discussing the difference between bilateral contracts and unilateral contracts, this court, in the case of *Port Huron Mach. Co. v. Wohlers*, 207 Iowa 826, 829, 221 N.W. 843, 844, states as follows:

The law recognizes, as a matter of classification, two kinds of contracts—unilateral and bilateral. In the case at bar a typical example of unilateral contract is found, since it is universally agreed that a “unilateral contract” is one in which no promisor receives a promise as consideration, whereas, in a “bilateral contract” there are mutual promises between the two parties to the contract. This matter of definition has recently received careful consideration by the American Law Institute and may be found in the Restatement of the Law of Contracts. Proposed Final Draft No. 1 (April 18, 1928) p. 17, § 12.

In the instant case the offer of the defendant must be viewed as a promise. It is promissory in terms. The rule is well stated by Prof. Williston: 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. See Williston on Contracts, vol. 1, § 139. Clearly the instant offer signed by the defendant was of this character. Appellant, however, contends that there was no acceptance of the offer. Words are not the only medium of expression of mutual assent. An offer may invite an acceptance to be made by merely an affirmative answer or by

performing a specific act. True, if an act other than a promise is requested, no contract exists until what is requested is performed or tendered in whole or in part. We are here dealing with a unilateral contract, and the act requested and performed as consideration for the contract indicates acceptance as well as furnishes the consideration.

19. The case of *Scott v. People's Monthly Co.*, 209 Iowa 503, 508, 228 N.W. 263, 265, 67 A.L.R. 413, involved an action for a \$1,000 prize offered in a "Word-building Contest". We there state:

In 34 Cyc. 1731, we find the following apt language:

"An offer of or promise to pay a reward is a proposal merely or a conditional promise, on the part of the offeror, and not a consummated contract. It may be said to be in effect the offer of a promise for an act, and the offer becomes a binding contract when the act is done or the service rendered in accordance with the terms of the offer."

It is the doing of the act in accordance with the terms and conditions of the offer which completes the contract. 34 Cyc. 1738. In other words, to make a binding and enforceable contract, the act must be done in accordance with the terms and conditions of the offer. 34 Cyc. 1742. See, also, 13 Corpus Juris 275; 13 C.J. 379; 13 C.J. 281-283; 13 C.J. 289; *Baker v. Johnson County*, 37 Iowa 186; *Breen v. Mayne*, 141 Iowa 399, 118 N.W. 441.

20. The principles applicable to the question of the adequacy of the consideration are clearly and concisely stated by Chief Justice Wright in the early case of *Blake v. Blake*, 7 Iowa 46, 51, as follows: "The essence and requisite of every consideration is, that it should create some benefit to the party promising, or some trouble, prejudice, or inconvenience to the party to whom the promise is made. Whenever, therefore, any injury to the one party, or any benefit to the other, springs from a consideration, it is sufficient to support a contract. Each party to a contract may, ordinarily, exercise his own discretion, as to the adequacy of the consideration; and if the agreement be made bona fide, it matters not how insignificant the benefit may apparently be to the promisor, or how slight the inconvenience or damage appear to be to the promisee, provided it be susceptible of legal estimation. Story on Contracts, section 431. Of course, however, if the inadequacy is so gross as to create a presumption of fraud, the contract founded thereon would not be enforced. But, even then, it is the fraud which

is thereby indicated, and not the inadequacy of consideration, which invalidates the contract.”

21. The principles announced in the above quotation have been recognized and applied by us in our later decisions. *State ex rel. v. American Bonding & Casualty Co.*, 213 Iowa 200, 206, 238 N.W. 726; *Edwards v. Foley*, 187 Iowa 5, 9, 173 N.W. 914; *Harlan v. Harlan*, 102 Iowa 701, 704, 72 N.W. 286.
22. Applying the principles above reviewed, it is readily apparent that, in this action on a unilateral contract, it was necessary for the plaintiff to show that a promise had been made which might be accepted by the doing of an act, which act would constitute consideration for the promise and performance of the contract. There is no basis for any claim of fraud herein. Plaintiff had nothing to do with inducing the defendants' promise. That promise was voluntarily and deliberately made. Defendants exercised their own discretion in determining the adequacy of the consideration for their promise. If the plaintiff did the acts called for by that promise, defendants cannot complain of the adequacy of the consideration.
23. Of course, it is fundamental that the act which is asserted as the consideration for acceptance and performance of a unilateral contract must be an act which the party sought to be bound bargained for, and the acts must have been induced by the promise made. Appellees contend that the facts are wholly insufficient to meet such requirements, contending as follows: “Although the action of Appellant in writing her name or standing in front of the theater might under some circumstances be such an act as would furnish a consideration for a promise, yet under the facts in the case at bar, . . . no reasonable person could say that the requested acts were actually bargained for in a legal sense so as to give rise to an enforceable promise.”
24. We are unable to concur in the contentions of counsel above quoted. We think that the requested acts were bargained for. We see nothing unreasonable in such holding. If there is anything unreasonable in this phase of the case, it would appear to be the contentions of counsel.
25. This brings us to the proposition raised by paragraph 7 of the motion for directed verdict, wherein it is asserted that, if there was a legal consideration for the promise sought to be enforced, then such consideration would constitute the transaction a lottery. To sustain such contention would require us to overrule *State v. Hundling*, *supra*, and to overrule such contention requires a differentiating of that case from this

case. We think that the two questions are different and may be logically distinguished.

26. In the *Hundling* case, we point out that the source of the evil which attends a lottery is that it arouses the gambling spirit and leads people to hazard their substance on a mere chance. Accordingly, it is vitally necessary to constitute a lottery that one who has the chance to win the prize must pay something of value for that chance. The value of the consideration, from a monetary standpoint, is the essence of the crime. However, in a civil action to enforce the promise to pay a prize, the monetary value of the consideration is in no wise controlling. It is only necessary that the act done be that which the promisor specified. The sufficiency of the consideration lies wholly within the discretion of the one who offers to pay the prize. "It matters not how insignificant the benefit may apparently be to the promisor, or how slight the inconvenience or damage appear to be to the promisee, provided it be susceptible of legal estimation." *Blake v. Blake, supra*. Accordingly, it is entirely possible that the act, specified by the promisor as being sufficient in his discretion to constitute consideration for and acceptance of his promise, might have no monetary value and yet constitute a legal consideration for the promise. Under such circumstances, the arrangement is not a lottery. The promoter of the scheme cannot be prosecuted criminally. But, if the act specified is done, the unilateral contract is supported by a consideration, and, having been performed by the party doing the act, can be enforced against the party making the promise. We hold that such is the situation here. There is no merit in grounds 1, 3 and 7 of the motion for directed verdict.

III.

27. Appellant's second assignment of error challenges paragraph 2 of the motion for directed verdict, which asserted that the evidence was insufficient to establish that Alice Kafer was employed by or authorized by defendants to announce the winner of the drawing, and that defendants were not bound by her statements. The answer admitted that Parkinson was manager of the theatre. As manager of the theatre, he asserted that he had a lady hired to call out the name outside the theatre. This assertion upon his part is binding upon the defendants. The evidence shows that the only person who called out the name other than Parkinson was Alice Kafer, and that she habitually announced the name that had been drawn on prior occasions. The evidence was sufficient to establish her agency and to make her announcement binding on defendants.

IV.

28. Appellants' fifth assignment of error challenges paragraph 5 of the motion for directed verdict, which asserts that there was no evidence that either plaintiff or her husband claimed the purse within the time limit fixed by defendants. The evidence shows that, when the plaintiff claimed the prize, Parkinson said, "I am sorry, but it was your husband's name that was called, where is your husband?" When her husband came, he said to him, "You are too late, just one second too late." Obviously, under Parkinson's statement, plaintiff claimed the prize in time. If her husband was the one entitled to it, the delay on his part was due to the defendants' act in permitting their agent, Alice Kafer, to announce the wrong name outside the theatre. Under such circumstances, defendants are estopped to claim the advantage of the one second delay. The basis for such estoppel was pleaded in the petition. It must be enforced against defendants.

V.

29. Appellant's sixth assignment of error challenges paragraph 6 of the motion for directed verdict, which asserted that no relevant, competent, or material proof tended to establish that the name of either the plaintiff or her husband was drawn. Plaintiff's name was announced by one agent, her husband's name by another agent, both of whom were in a position to bind the defendants. There is no merit in this ground of the motion.

VI.

30. Appellant's fourth assignment of error attacks paragraph 4 of the motion for directed verdict, which is a blanket statement that under the evidence it would be the duty of the court to set aside a verdict for the plaintiff. The disposition of the other propositions herein demonstrates that there is no merit in this ground of the motion.
31. All of appellant's assignments of error are well grounded. No ground of the motion for directed verdict was sufficient to warrant a sustaining of the motion. The court's ruling was erroneous.

The judgment entered pursuant thereto must be and it is reversed.

Kirksey v. Kirksey

Supreme Court of Alabama
8 Ala. 131 (1845)

1. Assumpsit by the defendant, against the plaintiff in error. The question is presented in this Court, upon a case agreed, which shows the following facts:
2. The plaintiff was the wife of defendant's brother, but had for some time been a widow, and had several children. In 1840, the plaintiff resided on public land, under a contract of lease, she had held over, and was comfortably settled, and would have attempted to secure the land she lived on. The defendant resided in Talladega county, some sixty, or seventy miles off. On the 10th October, 1840, he wrote to her the following letter:

Dear sister Antillico--Much to my mortification, I heard, that brother Henry was dead, and one of his children. I know that your situation is one of grief, and difficulty. You had a bad chance before, but a great deal worse now. I should like to come and see you, but cannot with convenience at present. ...I do not know whether you have a preference on the place you live on, or not. If you had, I would advise you to obtain your preference, and sell the land and quit the country, as I understand it is very unhealthy, and I know society is very bad. If you will come down and see me, I will let you have a place to raise your family, and I have more open land than I can tend; and on the account of your situation, and that of your family, I feel like I want you and the children to do well.
3. Within a month or two after the receipt of this letter, the plaintiff abandoned her possession, without disposing of it, and removed with her family, to the residence of the defendant, who put her in comfortable houses, and gave her land to cultivate for two years, at the end of which time he notified her to remove, and put her in a house, not comfortable, in the woods, which he afterwards required her to leave.
4. A verdict being found for the plaintiff, for two hundred dollars, the above facts were agreed, and if they will sustain the action, the judgment is to be affirmed, otherwise it is to be reversed.

ORMOND, J.

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

In re Greene

United States District Court, Southern District of New York
45 F.2d 428 (1930)

WOOLSEY, District Judge.

1. The petition for review is granted, and the order of the referee is reversed.
2. The claimant, a woman, filed proof of claim in the sum of \$375,700, based on an alleged contract, against this bankrupt's estate. The trustee in bankruptcy objected to the claim. A hearing was held before the referee in bankruptcy and testimony taken. The referee held the claim valid and dismissed the objections. The correctness of this ruling is raised by the trustee's petition to review and the referee's certificate.
3. For several years prior to April 28, 1926, the bankrupt, a married man, had apparently lived in adultery with the claimant. He gave her substantial sums of money. He also paid \$70,000 for a house on Long Island acquired by her, which she still owns. Throughout their relations the bankrupt was a married man, and the claimant knew it. The claimant was well over thirty years of age when the connection began. She testified that the bankrupt has promised to marry her as soon as his wife should get a divorce from him; this the bankrupt denied. The relations of intimacy between them were discontinued in April, 1926, and they then executed a written instrument under seal which is alleged to be a binding contract and which is the foundation of the claim under consideration.
4. In this instrument, which was made in New York, the bankrupt undertook (1) to pay to the claimant \$1,000 a month during their joint lives; (2) to assign to her a \$100,000 life insurance policy on his life and to keep up the premiums on it for life, the bankrupt to pay \$100,000 to the claimant in case the policy should lapse for nonpayment of premiums; and (3) to pay the rent for four years on an apartment which she had leased. It was declared in the instrument that the bankrupt had no interest in the Long Island house or in its contents, and that he should no longer be liable for mortgage interest, taxes, and other charges on this property. The claimant on her part released the bankrupt from all claims which she had against him. The preamble to the instrument recites as consideration the payment of \$1 by the claimant to the bankrupt, "and other good and valuable consideration." The bankrupt kept up

the several payments called for by the instrument until August, 1928, but failed to make payments thereafter.

5. In the proof of claim it is alleged that a total of \$375,700 was due because of breach of the agreement, made up as follows: \$250,000 for failure to pay \$1,000 a month; \$99,200 for failure to maintain the insurance policy; and \$26,500 for failure to pay the rent. The claim was sustained by the referee for the full amount.
6. It seems clear that the \$250,000 allowed as damages for failure to pay \$1,000 a month was excessive. The bankrupt's undertaking was to pay \$1,000 a month only so long as both he and the claimant should live; it was not an annuity for the claimant's life alone, as she seems to have assumed. There is nothing in the record to indicate the bankrupt's age, and consequently there is a failure of proof as to this element of damage. In view of my conclusion that the entire claim is void, however, the matter of damages is of no present importance.
7. A contract for future illicit cohabitation is unlawful. There is consideration present in such a case, but the law strikes the agreement down as immoral. Williston on Contracts, Sec. 1745. Here the illicit intercourse had been abandoned prior to the making of the agreement, so that the above rule is not infringed. This case is one where the motive which led the bankrupt to make the agreement on which the claim is based was the past illicit cohabitation between him and the claimant. The law is that a promise to pay a woman on account of cohabitation which has ceased is void, not for illegality, but for want of consideration. The consideration in such a case is past. The mere fact that past cohabitation is the motive for the promise will not of itself invalidate it, but the promise in such a case, to be valid, must be supported by some consideration other than past intercourse. Williston on Contracts, Secs. 148, 1745.
8. The problem in the present case, therefore, is one of consideration, not of illegality, and it is clear that the past illicit intercourse is not consideration. The cases dealing with situations where there is illegitimate offspring or where there has been seduction are of doubtful authority, for the doctrine that past moral obligation is consideration is now generally exploded. But these cases and others speaking of expiation of past wrong, cited by the referee, are not in point. Here there was not any offspring as a result of the bankrupt's union with the claimant; there was not any seduction shown in the sense in which that word is used in law. Cf. New York Penal Law, art. 195, Sec.

2175. There was not any past wrong for which the bankrupt owed the claimant expiation—*volenti non fit injuria*. Cases involving deeds, mortgages, and the like are not analogous, because no consideration is necessary in an executed transaction.

9. The question, therefore, is whether there was any consideration for the bankrupt's promises, apart from the past cohabitation. It seems plain that no such consideration can be found, but I will review the following points emphasized by the claimant as showing consideration:
10. (1) The \$1 consideration recited in the paper is nominal. It cannot seriously be urged that \$1, recited but not even shown to have been paid, will support an executory promise to pay hundreds of thousands of dollars.
11. (2) "Other good and valuable consideration" are generalities that sound plausible, but the words cannot serve as consideration where the facts show that nothing good or valuable was actually given at the time the contract was made.
12. (3) It is said that the release of claims furnishes the necessary consideration. So it would if the claimant had had any claims to release. But the evidence shows no vestige of any lawful claim. Release from imaginary claims is not valuable consideration for a promise. In this connection, apparently, the claimant testified that the bankrupt had promised to marry her as soon as he was divorced. Assuming that he did—though he denies it—the illegality of any such promise, made while the bankrupt was still married, is so obvious that no claim could possibly arise from it, and the release of such claim could not possibly be lawful consideration.
13. (4) The claimant also urges that by the agreement the bankrupt obtained immunity from liability for taxes and other charges on the Long Island house. The fact is that he was never chargeable for these expenses. He doubtless had been in the habit of paying them, just as he had paid many other expenses for the claimant; but such payments were either gratuitous or were the contemporaneous price of the continuance of his illicit intercourse with the claimant. It is absurd to suppose that, when a donor gives a valuable house to a donee, the fact that the donor need pay no taxes or upkeep thereafter on the property converts the gift into a contract upon consideration. The present case is even stronger, for the bankrupt had never owned the house and had never been liable for the taxes. He furnished the purchase price, but the conveyance was from the seller direct to the claimant.

14. (5) Finally, it is said that the parties intended to make a valid agreement. It is a non sequitur to say that therefore the agreement is valid. A man may promise to make a gift to another, and may put the promise in the most solemn and formal document possible; but, barring exceptional cases, such, perhaps, as charitable subscriptions, the promise will not be enforced. The parties may shout consideration to the housetops, yet, unless consideration is actually present, there is not a legally enforceable contract. What the bankrupt obviously intended in this case was an agreement to make financial contribution to the claimant because of his past cohabitation with her, and, as already pointed out, such an agreement lacks consideration.
15. The presence of the seal would have been decisive in the claimant's favor a hundred years ago. Then an instrument under seal required no consideration, or, to keep to the language of the cases, the seal was conclusive evidence of consideration. In New York, however, a seal is now only presumptive evidence of consideration on an executory instrument. Civil Practice Act, Sec. 342; *Harris v. Shorall*, 230 N.Y. 343, 348, 130 N.E. 572; *Alexander v. Equitable Life Assurance Society*, 233 N.Y. 300, 307, 135 N.E. 509. This presumption was amply rebutted in this case, for the proof clearly shows, I think, that there was not in fact any consideration for the bankrupt's promise contained in the executory instrument signed by him and the claimant.
16. An order in accordance with this opinion may be submitted for settlement on two days' notice.

Batsakis v. Demotsis

Court of Civil Appeals of Texas
226 S.W.2d 673 (1949)

McGILL, Justice.

1. This is an appeal from a judgment of the 57th judicial District Court of Bexar County. Appellant was plaintiff and appellee was defendant in the trial court. The parties will be so designated.
2. Plaintiff sued defendant to recover \$2,000 with interest at the rate of 8% per annum from April 2, 1942, alleged to be due on the following instrument, being a translation from the original, which is written in the Greek language:

Peiraeus

April 2, 1942

Mr. George Batsakis

Konstantinou Diadohou #7

Mr. Batsakis:

I state by my present (letter) that I received today from you the amount of two thousand dollars (\$2,000.00) of United States of America money, which I borrowed from you for the support of my family during these difficult days and because it is impossible for me to transfer dollars of my own from America.

The above amount I accept with the expressed promise that I will return to you again in American dollars either at the end of the present war or even before in the event that you might be able to find a way to collect them (dollars) from my representative in America to whom I shall write and give him an order relative to this you understand until the final execution (payment) to the above amount an eight per cent interest will be added and paid together with the principal.

I thank you and I remain yours with respects.

The recipient,

(Signed) Eugenia The. Demotsis.

3. Trial to the court without the intervention of a jury resulted in a judgment in favor of plaintiff for \$750.00 principal, and interest at the rate of 8% per annum from April 2, 1942 to the date of judgment, totaling \$1163.83, with interest thereon at the rate of 8% per annum until paid. Plaintiff has perfected his appeal.
4. The court sustained certain special exceptions of plaintiff to defendant's first amended original answer on which the case was tried, and struck therefrom paragraphs II, III and V. Defendant excepted to such action of the court, but has not cross-assigned error here. The answer, stripped of such paragraphs, consisted of a general denial contained in paragraph I thereof, and of paragraph IV, which is as follows:

IV. That under the circumstances alleged in Paragraph II of this answer, the consideration upon which said written instrument sued upon by plaintiff herein is founded, is wanting and has failed to the extent of \$1975.00, and defendant pleads specially under the verification hereinafter made the want and failure of consideration stated, and now tenders, as defendant has heretofore tendered to plaintiff, \$25.00 as the value of the loan of money received by defendant from plaintiff, together with interest thereon.

Further, in connection with this plea of want and failure of consideration defendant alleges that she at no time received from plaintiff himself or from anyone for plaintiff any money or thing of value other than, as hereinbefore alleged, the original loan of 500,000 drachmae. That at the time of the loan by plaintiff to defendant of said 500,000 drachmae the value of 500,000 drachmae in the Kingdom of Greece in dollars of money of the United States of America, was \$25.00, and also at said time the value of 500,000 drachmae of Greek money in the United States of America in dollars was \$25.00 of money of the United States of America.
5. The allegations in paragraph II which were stricken, referred to in paragraph IV, were that the instrument sued on was signed and delivered in the Kingdom of Greece on or about April 2, 1942, at which time both plaintiff and defendant were residents of and residing in the Kingdom of Greece, and

[Plaintiff] avers that on or about April 2, 1942 she owned money in the United States of America, but was then and there in the Kingdom of Greece in straitened financial circumstances due to the conditions produced by World War II and could not make use of her money and property and credit existing in the United States of America. That in the circumstances the plaintiff agreed to and did lend to defendant the sum of 500,000 drachmae, which at that time, on or about April 2, 1942, had the value of \$25.00 in money of the United States of America. That the said plaintiff, knowing defendant's financial distress and desire to return to the United States of America, exacted of her the written instrument plaintiff sues upon, which was a promise by her to pay to him the sum of \$2,000.00 of United States of America money.

6. Plaintiff specially excepted to paragraph IV because the allegations thereof were insufficient to allege either want of consideration or failure of consideration, in that it affirmatively appears therefrom that defendant received what was agreed to be delivered to her, and that plaintiff breached no agreement. The court overruled this exception, and such action is assigned as error. Error is also assigned because of the court's failure to enter judgment for the whole unpaid balance of the principal of the instrument with interest as therein provided.
7. Defendant testified that she did receive 500,000 drachmas from plaintiff. It is not clear whether she received all the 500,000 drachmas or only a portion of them before she signed the instrument in question. Her testimony clearly shows that the understanding of the parties was that plaintiff would give her the 500,000 drachmas if she would sign the instrument. She testified:

Q. who suggested the figure of \$2,000.00?

That was how he asked me from the beginning. He said he will give me five hundred thousand drachmas provided I signed that I would pay him \$2,000.00 American money.

8. The transaction amounted to a sale by plaintiff of the 500,000 drachmas in consideration of the execution of the instrument sued on, by defendant. It is not contended that the drachmas had no value. Indeed, the judgment indicates that the trial court placed a value of \$750.00 on them or on the other consideration which plaintiff gave defendant for the instrument if he believed plaintiff's testimony. Therefore the plea of want of consideration was unavailing. A plea of want of

consideration amounts to a contention that the instrument never became a valid obligation in the first place. *National Bank of Commerce v. Williams*, 125 Tex. 619, 84 S.W.2d 691.

9. Mere inadequacy of consideration will not void a contract. 10 Tex.Jur., Contracts, Sec. 89, p. 150; *Chastain v. Texas Christian Missionary Society*, Tex.Civ.App., 78 S.W.2d 728, loc. cit. 731(3), Wr. Ref.
10. Nor was the plea of failure of consideration availing. Defendant got exactly what she contracted for according to her own testimony. The court should have rendered judgment in favor of plaintiff against defendant for the principal sum of \$2,000.00 evidenced by the instrument sued on, with interest as therein provided. We construe the provision relating to interest as providing for interest at the rate of 8% per annum. The judgment is reformed so as to award appellant a recovery against appellee of \$2,000.00 with interest thereon at the rate of 8% per annum from April 2, 1942. Such judgment will bear interest at the rate of 8% per annum until paid on \$2,000.00 thereof and on the balance interest at the rate of 6% per annum. As so reformed, the judgment is affirmed.

Reformed and affirmed.

Feinberg v. Pfeiffer Co.

St. Louis Court of Appeals, Missouri
322 S.W.2d 163 (1959)

DOERNER, Commissioner.

1. This is a suit brought in the Circuit Court of the City of St. Louis by plaintiff, a former employee of the defendant corporation, on an alleged contract whereby defendant agreed to pay plaintiff the sum of \$200 per month for life upon her retirement. A jury being waived, the case was tried by the court alone. Judgment below was for plaintiff for \$5,100, the amount of the pension claimed to be due as of the date of the trial, together with interest thereon, and defendant duly appealed.
2. The parties are in substantial agreement on the essential facts. Plaintiff began working for the defendant, a manufacturer of pharmaceuticals, in 1910, when she was but 17 years of age. By 1947 she had attained the position of bookkeeper, office manager, and assistant treasurer of the defendant, and owned 70 shares of its stock out of a total of 6,503 shares issued and outstanding. Twenty shares had been given to her by the defendant or its then president, she had purchased 20, and the remaining 30 she had acquired by a stock split or stock dividend. Over the years she received substantial dividends on the stock she owned, as did all of the other stockholders. Also, in addition to her salary, plaintiff from 1937 to 1949, inclusive, received each year a bonus varying in amount from \$300 in the beginning to \$2,000 in the later years.
3. On December 27, 1947, the annual meeting of the defendant's Board of Directors was held at the Company's offices in St. Louis, presided over by Max Lippman, its then president and largest individual stockholder. The other directors present were George L. Marcus, Sidney Harris, Sol Flammer, and Walter Weinstock, who, with Max Lippman, owned 5,007 of the 6,503 shares then issued and outstanding. At that meeting the Board of Directors adopted the following resolution, which, because it is the crux of the case, we quote in full:

The Chairman thereupon pointed out that the Assistant Treasurer, Mrs. Anna Sacks Feinberg, has given the corporation many years of long and faithful service. Not only has she served the corporation devotedly, but with exceptional ability and skill. The President pointed out that although all of the officers and directors sincerely hoped and desired that Mrs. Feinberg

would continue in her present position for as long as she felt able, nevertheless, in view of the length of service which she has contributed provision should be made to afford her retirement privileges and benefits which should become a firm obligation of the corporation to be available to her whenever she should see fit to retire from active duty, however many years in the future such retirement may become effective. It was, accordingly, proposed that Mrs. Feinberg's salary which is presently \$350.00 per month, be increased to \$400.00 per month, and that Mrs. Feinberg would be given the privilege of retiring from active duty at any time she may elect to see fit so to do upon a retirement pay of \$200.00 per month for life, with the distinct understanding that the retirement plan is merely being adopted at the present time in order to afford Mrs. Feinberg security for the future and in the hope that her active services will continue with the corporation for many years to come. After due discussion and consideration, and upon motion duly made and seconded, it was—

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

4. At the request of Mr. Lippman his sons-in-law, Messrs. Harris and Flammer, called upon the plaintiff at her apartment on the same day to advise her of the passage of the resolution. Plaintiff testified on cross-examination that she had no prior information that such a pension plan was contemplated, that it came as a surprise to her, and that she would have continued in her employment whether or not such a resolution had been adopted. It is clear from the evidence that there was no contract, oral or written, as to plaintiff's length of employment, and that she was free to quit, and the defendant to discharge her, at any time.
5. Plaintiff did continue to work for the defendant through June 30, 1949, on which date she retired. In accordance with the foregoing resolution, the defendant began paying her the sum of \$200 on the first of each month. Mr. Lippman died on November 18, 1949, and was succeeded as president of the company by his widow. Because of an illness, she retired from that office and was succeeded in October, 1953, by her son-in-law, Sidney M. Harris. Mr. Harris testified that while Mrs. Lippman had been president she signed the monthly pension check paid plaintiff, but fussed about doing so, and considered the payments as gifts. After his election, he stated, a new

accounting firm employed by the defendant questioned the validity of the payments to plaintiff on several occasions, and in the Spring of 1956, upon its recommendation, he consulted the Company's then attorney, Mr. Ralph Kalish. Harris testified that both Ernst and Ernst, the accounting firm, and Kalish told him there was no need of giving plaintiff the money. He also stated that he had concurred in the view that the payments to plaintiff were mere gratuities rather than amounts due under a contractual obligation, and that following his discussion with the Company's attorney plaintiff was sent a check for \$100 on April 1, 1956. Plaintiff declined to accept the reduced amount, and this action followed. Additional facts will be referred to later in this opinion.

6. Appellant's first assignment of error relates to the admission in evidence of plaintiff's testimony over its objection, that at the time of trial she was sixty-five and a half years old, and that she was no longer able to engage in gainful employment because of the removal of a cancer and the performance of a colocholecystostomy operation on November 25, 1957. Its complaint is not so much that such evidence was irrelevant and immaterial, as it is that the trial court erroneously made it one basis for its decision in favor of plaintiff. As defendant concedes, the error (if it was error) in the admission of such evidence would not be a ground for reversal, since, this being a jury-waived case, we are constrained by the statutes to review it upon both the law and the evidence, Sec. 510.310 R.S. Mo. 1949, V.A.M.S., and to render such judgment as the court below ought to have given. Section 512.160, *Minor v. Lillard*, Mo., 289 S.W.2d 1; *Thumm v. Lohr*, Mo. App., 306 S.W.2d 604. We consider only such evidence as is admissible, and need not pass upon questions of error in the admission and exclusion of evidence. *Hussey v. Robinson*, Mo., 285 S.W.2d 603. However, in fairness to the trial court it should be stated that while he briefly referred to the state of plaintiff's health as of the time of the trial in his amended findings of fact, it is obvious from his amended grounds for decision and judgment that it was not, as will be seen, the basis for his decision.
7. Appellant's next complaint is that there was insufficient evidence to support the court's findings that plaintiff would not have quit defendant's employ had she not known and relied upon the promise of defendant to pay her \$200 a month for life, and the finding that, from her voluntary retirement until April 1, 1956, plaintiff relied upon the continued receipt of the pension installments. The trial court so found, and, in our opinion, justifiably so. Plaintiff testified, and was corroborated by Harris, defendant's witness, that knowledge of the passage of the resolution was

communicated to her on December 27, 1947, the very day it was adopted. She was told at that time by Harris and Flammer, she stated, that she could take the pension as of that day, if she wished. She testified further that she continued to work for another year and a half, through June 30, 1949; that at that time her health was good and she could have continued to work, but that after working for almost forty years she thought she would take a rest. Her testimony continued:

Q. Now, what was the reason-I'm sorry. Did you then quit the employment of the company after you-after this year and a half?

Yes.

Q. What was the reason that you left?

Well, I thought almost forty years, it was a long time and I thought I would take a little rest.

Q. Yes.

And with the pension and what earnings my husband had, we figured we could get along.

Q. Did you rely upon this pension?

We certainly did.

Q. Being paid?

Very much so. We relied upon it because I was positive that I was going to get it as long as I lived.

Q. Would you have left the employment of the company at that time had it not been for this pension?

No.

Mr. Allen: Just a minute, I object to that as calling for a conclusion and conjecture on the part of this witness.

The Court: It will be overruled.

Q. (Mr. Agatstein continuing): Go ahead, now. The question is whether you would have quit the employment of the company at that time had you not relied upon this pension plan?

No, I wouldn't.

Q. You would not have. Did you ever seek employment while this pension was being paid to you-

(interrupting): No.

Q. Wait a minute, at any time prior-at any other place?

No, sir.

Q. Were you able to hold any other employment during that time?

Yes, I think so.

Q. Was your health good?

My health was good.

8. It is obvious from the foregoing that there was ample evidence to support the findings of fact made by the court below.
9. We come, then, to the basic issue in the case. While otherwise defined in defendant's third and fourth assignments of error, it is thus succinctly stated in the argument in its brief: "...whether plaintiff has proved that she has a right to recover from defendant based upon a legally binding contractual obligation to pay her \$200 per month for life."
10. It is defendant's contention, in essence, that the resolution adopted by its Board of Directors was a mere promise to make a gift, and that no contract resulted either thereby, or when plaintiff retired, because there was no consideration given or paid by the plaintiff. It urges that a promise to make a gift is not binding unless supported by a legal consideration; that the only apparent consideration for the adoption of the foregoing resolution was the "many years of long and faithful service" expressed therein; and that past services are not a valid consideration for a promise. Defendant argues further that there is nothing in the resolution which made its effectiveness

conditional upon plaintiff's continued employment, that she was not under contract to work for any length of time but was free to quit whenever she wished, and that she had no contractual right to her position and could have been discharged at any time.

11. Plaintiff concedes that a promise based upon past services would be without consideration, but contends that there were two other elements which supplied the required element: First, the continuation by plaintiff in the employ of the defendant for the period from December 27, 1947, the date when the resolution was adopted, until the date of her retirement on June 30, 1949. And, second, her change of position, i. e., her retirement, and the abandonment by her of her opportunity to continue in gainful employment, made in reliance on defendant's promise to pay her \$200 per month for life.
12. We must agree with the defendant that the evidence does not support the first of these contentions. There is no language in the resolution predicating plaintiff's right to a pension upon her continued employment. She was not required to work for the defendant for any period of time as a condition to gaining such retirement benefits. She was told that she could quit the day upon which the resolution was adopted, as she herself testified, and it is clear from her own testimony that she made no promise or agreement to continue in the employ of the defendant in return for its promise to pay her a pension. Hence there was lacking that mutuality of obligation which is essential to the validity of a contract. *Middleton v. Holecraft*, Mo. App., 270 S.W.2d 90; *Solace v. T. J. Moss Tie Co.*, Mo. App., 142 S.W.2d 1079; *Aslin v. Stoddard County*, 341 Mo. 138, 106 S.W.2d 472; *Fuqua v. Lumbermen's Supply Co.*, 229 Mo. App. 210, 76 S.W.2d 715; *Hudson v. Browning*, 264 Mo. 58, 174 S.W. 393; *Campbell v. American Handle Co.*, 117 Mo. App. 19, 94 S.W. 815.
13. But as to the second of these contentions we must agree with plaintiff. By the terms of the resolution defendant promised to pay plaintiff the sum of \$200 a month upon her retirement. Consideration for a promise has been defined in the Restatement of the Law of Contracts, Section 75, as:

(1) Consideration for a promise is

(a) an act other than a promise, or

(b) a forbearance, or

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

(d) a return promise,

bargained for and given in exchange for the promise.

14. As the parties agree, the consideration sufficient to support a contract may be either a benefit to the promisor or a loss or detriment to the promisee. *Industrial Bank & Trust Co. v. Hesselberg*, Mo., 195 S.W.2d 470; *State ex rel. Kansas City v. State Highway Commission*, 349 Mo. 865, 163 S.W.2d 948; *Duvall v. Duncan*, 341 Mo. 1129, 111 S.W.2d 89; *Thompson v. McCune*, 333 Mo. 758, 63 S.W.2d 41.
15. Section 90 of the Restatement of the Law of Contracts states that: “A promise which the promisor should reasonably expect to induce action or forbearance of a definite and substantial character on the part of the promisee and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise.” This doctrine has been described as that of “promissory estoppel,” as distinguished from that of equitable estoppel or estoppel *in pais*, the reason for the differentiation being stated as follows:

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

WILLISTON ON CONTRACTS, Rev. Ed., Sec. 139, Vol. 1.

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

17. As pointed out by our Supreme Court in *In re Jamison's Estate*, Mo., 202 S.W.2d 879, 887, it is stated in the Missouri Annotations to the Restatement under Section 90 that: “There is a variance between the doctrine underlying this section and the theoretical justifications that have been advanced for the Missouri decisions.”

18. That variance, as the authors of the Annotations point out, is that:

This § 90, when applied with § 85, means that the promise described is a contract without any consideration. In Missouri the same practical result is reached without in theory abandoning the doctrine of consideration. In Missouri three theories have been advanced as ground for the decisions (1) *Theory of act for promise*. The induced “action or forbearance” is the consideration for the promise. *Underwood Typewriter Co. v. Century Realty Co.* (1909) 220 Mo. 522, 119 S.W. 400, 25 L.R.A., N.S., 1173. See § 76. (2) *Theory of promissory estoppel*. The induced “action or forbearance” works an estoppel against the promisor. (Citing *School District of Kansas City v. Sheidley* (1897) 138 Mo. 672, 40 S. W. 656 [37 L.R.A. 406]) ... (3) *Theory of bilateral contract*. When the induced ‘action or forbearance’ is begun, a promise to complete is implied, and we have an enforceable bilateral contract, the implied promise to complete being the consideration for the original promise.

19. Was there such an act on the part of plaintiff, in reliance upon the promise contained in the resolution, as will estop the defendant, and therefore create an enforceable contract under the doctrine of promissory estoppel? We think there was. One of the illustrations cited under Section 90 of the Restatement is: “2. A promises B to pay him an annuity during B's life. B thereupon resigns a profitable employment, as A expected that he might. B receives the annuity for some years, in the meantime becoming disqualified from again obtaining good employment. A's promise is binding.” This illustration is objected to by defendant as not being applicable to the case at hand. The reason advanced by it is that in the illustration B became “disqualified” from obtaining other employment *before* A discontinued the payments, whereas in this case the plaintiff did not discover that she had cancer and thereby became unemployable until *after* the defendant had discontinued the payments of \$200 per month. We think the distinction is immaterial. The only reason for the reference in the illustration to the disqualification of A is in connection with that part of Section 90 regarding the prevention of injustice. The injustice would occur regardless of when the disability occurred. Would defendant contend that the contract

would be enforceable if the plaintiff's illness had been discovered on March 31, 1956, the day before it discontinued the payment of the \$200 a month, but not if it occurred on April 2nd, the day after? Furthermore, there are more ways to become disqualified for work, or unemployable, than as the result of illness. At the time she retired plaintiff was 57 years of age. At the time the payments were discontinued she was over 63 years of age. It is a matter of common knowledge that it is virtually impossible for a woman of that age to find satisfactory employment, much less a position comparable to that which plaintiff enjoyed at the time of her retirement.

20. The fact of the matter is that plaintiff's subsequent illness was not the "action or forbearance" which was induced by the promise contained in the resolution. As the trial court correctly decided, such action on plaintiff's part was her retirement from a lucrative position in reliance upon defendant's promise to pay her an annuity or pension. In a very similar case, *Ricketts v. Scothorn*, 57 Neb. 51, 77 N.W. 365, 367, 42 L.R.A. 794, the Supreme Court of Nebraska said:

According to the undisputed proof, as shown by the record before us, the plaintiff was a working girl, holding a position in which she earned a salary of \$10 per week. Her grandfather, desiring to put her in a position of independence, gave her the note accompanying it with the remark that his other grandchildren did not work, and that she would not be obliged to work any longer. In effect, he suggested that she might abandon her employment, and rely in the future upon the bounty which he promised. He doubtless desired that she should give up her occupation, but, whether he did or not, it is entirely certain that he contemplated such action on her part as a reasonable and probable consequence of his gift. Having intentionally influenced the plaintiff to alter her position for the worse on the faith of the note being paid when due, it would be grossly inequitable to permit the maker, or his executor, to resist payment on the ground that the promise was given without consideration.

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

Hayes v. Plantations Steel Co.

Supreme Court of Rhode Island
438 A.2d 1091 (1982)

SHEA, Justice.

1. The defendant employer, Plantations Steel Company (Plantations), appeals from a Superior Court judgment for the plaintiff employee, Edward J. Hayes (Hayes). The trial justice, sitting without a jury, found that Plantations was obligated to Hayes on the basis of an implied-in-fact contract to pay him a yearly pension of \$5,000. The award covered three years in which payment had not been made. The trial justice ruled, also, that Hayes had made a sufficient showing of detrimental reliance upon Plantations's promise to pay to give rise to its obligation based on the theory of promissory estoppel. The trial justice, however, found in part for Plantations in ruling that the payments to Hayes were not governed by the Employee Retirement Income Security Act, 29 U.S.C.A. §§ 1001-1461 (West 1975), and consequently he was not entitled to attorney's fees under § 1132(g) of that act. Both parties have appealed.
2. We reverse the findings of the trial justice regarding Plantations's contractual obligation to pay Hayes a pension. Consequently we need not deal with the cross-appeal concerning the award of attorney's fees under the federal statute.
3. Plantations is a closely held Rhode Island corporation engaged in the manufacture of steel reinforcing rods for use in concrete construction. The company was founded by Hugo R. Mainelli, Sr., and Alexander A. DiMartino. A dispute between their two families in 1976 and 1977 left the DiMartinos in full control of the corporation. Hayes was an employee of the corporation from 1947 until his retirement in 1972 at age of sixty-five. He began with Plantations as an "estimator and draftsman" and ended his career as general manager, a position of considerable responsibility. Starting in January 1973 and continuing until January 1976, Hayes received the annual sum of \$5,000 from Plantations. Hayes instituted this action in December 1977, after the then company management refused to make any further payments.
4. Hayes testified that in January 1972 he announced his intention to retire the following July, after twenty-five years of continuous service. He decided to retire because he had worked continuously for fifty-one years. He stated, however, that he would not

have retired had he not expected to receive a pension. After he stopped working for Plantations, he sought no other employment.

5. Approximately one week before his actual retirement Hayes spoke with Hugo R. Mainelli, Jr., who was then an officer and a stockholder of Plantations. This conversation was the first and only one concerning payments of a pension to Hayes during retirement. Mainelli said that the company “would take care” of him. There was no mention of a sum of money or a percentage of salary that Hayes would receive. There was no formal authorization for payments by Plantations's shareholders and/or board of directors. Indeed, there was never any formal provision for a pension plan for any employee other than for unionized employees, who benefit from an arrangement through their union. The plaintiff was not a union member.
6. Mr. Mainelli, Jr., testified that his father, Hugo R. Mainelli, Sr., had authorized the first payment “as a token of appreciation for the many years of (Hayes's) service.” Furthermore, “it was implied that that check would continue on an annual basis.” Mainelli also testified that it was his “personal intention” that the payments would continue for “as long as I was around.”
7. Mainelli testified that after Hayes's retirement, he would visit the premises each year to say hello and renew old acquaintances. During the course of his visits, Hayes would thank Mainelli for the previous check and ask how long it would continue so that he could plan an orderly retirement.
8. The payments were discontinued after 1976. At that time a succession of several poor business years plus the stockholders' dispute, resulting in the takeover by the DiMartino family, contributed to the decision to stop the payments.
9. The trial justice ruled that Plantations owed Hayes his annual sum of \$5,000 for the years 1977 through 1979. The ruling implied that barring bankruptcy or the cessation of business for any other reason, Hayes had a right to expect continued annual payments.
10. The trial justice found that Hugo Mainelli, Jr.'s statement that Hayes would be taken care of after his retirement was a promise. Although no sum of money was mentioned in 1972, the four annual payments of \$5,000 established that otherwise unspecified term of the contract. The trial justice also found that Hayes supplied consideration for the promise by voluntarily retiring, because he was under no obligation to do so.

From the words and conduct of the parties and from the surrounding circumstances, the trial justice concluded that there existed an implied contract obligating the company to pay a pension to Hayes for life. The trial justice made a further finding that even if Hayes had not truly bargained for a pension by voluntarily retiring, he had nevertheless incurred the detriment of foregoing other employment in reliance upon the company's promise. He specifically held that Hayes's retirement was in response to the promise and held also that Hayes refrained from seeking other employment in further reliance thereon.

11. The findings of fact of a trial justice sitting without a jury are entitled to great weight when reviewed by this court. His findings will not be disturbed unless it can be shown that they are clearly wrong or that the trial justice misconceived or overlooked material evidence. *Lisi v. Marra*, R.I., 424 A.2d 1052 (1981); *Raheb v. Lemenski*, 115 R.I. 576, 350 A.2d 397 (1976). After careful review of the record, however, we conclude that the trial justice's findings and conclusions must be reversed.
12. Assuming for the purpose of this discussion that Plantations in legal effect made a promise to Hayes, we must ask whether Hayes did supply the required consideration that would make the promise binding? And, if Hayes did not supply consideration, was his alleged reliance sufficiently induced by the promise to estop defendant from denying its obligation to him? We answer both questions in the negative.
13. We turn first to the problem of consideration. The facts at bar do not present the case of an express contract. As the trial justice stated, the existence of a contract in this case must be determined from all the circumstances of the parties' conduct and words. Although words were expressed initially in the remark that Hayes "would be taken care of," any contract in this case would be more in the nature of an implied contract. Certainly the statement of Hugo Mainelli, Jr., standing alone is not an expression of a direct and definite promise to pay Hayes a pension. Though we are analyzing an implied contract, nevertheless we must address the question of consideration.
14. Contracts implied in fact require the element of consideration to support them as is required in express contracts. The only difference between the two is the manner in which the parties manifest their assent. *J. Koury Steel Erectors, Inc. v. San-Vel Concrete Corp.*, 387 A.2d 694 (R.I. 1978); *Bailey v. West*, 249 A.2d 414 (R.I. 1969). In this jurisdiction, consideration consists either in some right, interest, or benefit accruing to one party or some forbearance, detriment, or responsibility given,

suffered, or undertaken by the other. See *Dockery v. Greenfield*, 136 A.2d 682 (R.I. 1957); *Darcey v. Darcey*, 71 A. 595 (R.I. 1909). Valid consideration furthermore must be bargained for. It must induce the return act or promise. To be valid, therefore, the purported consideration must not have been delivered before a promise is executed, that is, given without reference to the promise. *Plowman v. Indian Refining Co.*, 20 F. Supp. 1 (E.D.Ill.1937). Consideration is therefore a test of the enforceability of executory promises, *Angel v. Murray*, 322 A.2d 630 (R.I. 1974), and has no legal effect when rendered in the past and apart from an alleged exchange in the present. *Zanturjian v. Boornazian*, 55 A. 199 (R.I. 1903).

15. In the case before us, Plantations's promise to pay Hayes a pension is quite clearly not supported by any consideration supplied by Hayes. Hayes had announced his intent to retire well in advance of any promise, and therefore the intention to retire was arrived at without regard to any promise by Plantations. Although Hayes may have had in mind the receipt of a pension when he first informed Plantations, his expectation was not based on any statement made to him or on any conduct of the company officer relative to him in January 1972. In deciding to retire, Hayes acted on his own initiative. Hayes's long years of dedicated service also is legally insufficient because his service too was rendered without being induced by Plantations's promise. See *Plowman v. Indian Refining Co.*, *supra*.
16. Clearly then this is not a case in which Plantations's promise was meant to induce Hayes to refrain from retiring when he could have chosen to do so in return for further service. 1 WILLISTON ON CONTRACTS § 130B (3d ed., Jaeger 1957). Nor was the promise made to encourage long service from the start of his employment. *Weesner v. Electric Power Board of Chattanooga*, 344 S.W.2d 766 (Tenn. App. 1961). Instead, the testimony establishes that Plantations's promise was intended "as a token of appreciation for (Hayes's) many years of service." As such it was in the nature of a gratuity paid to Hayes for as long as the company chose. In *Spickelmier Industries, Inc. v. Passander*, 359 N.E.2d 563 (Ind. App. 1977), an employer's promise to an employee to pay him a year-end bonus was unenforceable because it was made after the employee had performed his contractual responsibilities for that year.
17. The plaintiff's most relevant citations are still inapposite to the present case. *Bredemann v. Vaughan Mfg. Co.*, 188 N.E.2d 746 (Ill. App. 1963), presents similar yet distinguishable facts. There, the appellate court reversed a summary judgment

granted to the defendant employer, stating that a genuine issue of material fact existed regarding whether the plaintiff's retirement was in consideration of her employer's promise to pay her a lifetime pension. As in the present case, the employer made the promise one week prior to the employee's retirement, and in almost the same words. However, *Bredemann* is distinguishable because the court characterized that promise as a concrete offer to pay if she would retire immediately. In fact, the defendant wanted her to retire. *Id.* 188 N.E.2d at 749. On the contrary, Plantations in this case did not actively seek Hayes's retirement. DiMartino, one of Plantations's founders, testified that he did not want Hayes to retire. Unlike *Bredemann*, here Hayes announced his unsolicited intent to retire.

18. Hayes also argues that the work he performed during the week between the promise and the date of his retirement constituted sufficient consideration to support the promise. He relies on *Ulmann v. Sunset-McKee Co.*, 221 F.2d 128 (9th Cir. 1955), in which the court ruled that work performed during the one-week period of the employee's notice of impending retirement constituted consideration for the employer's offer of a pension that the employee had solicited some months previously. But there the court stated that its prime reason for upholding the agreement was that sufficient consideration existed in the employee's consent not to compete with his employer. These circumstances do not appear in our case. Hayes left his employment because he no longer desired to work. He was not contemplating other job offers or considering going into competition with Plantations. Although Plantations did not want Hayes to leave, it did not try to deter him, nor did it seek to prevent Hayes from engaging in other activity.
19. Hayes argues in the alternative that even if Plantations's promise was not the product of an exchange, its duty is grounded properly in the theory of promissory estoppel. This court adopted the theory of promissory estoppel in *East Providence Credit Union v. Geremia*, 239 A.2d 725, 727 (R.I. 1968) (quoting 1 RESTATEMENT CONTRACTS § 90 at 110 (1932)) stating:

“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 its promise.”

20. In *East Providence Credit Union* this court said that the doctrine of promissory estoppel is invoked “as a substitute for a consideration, rendering a gratuitous promise enforceable as a contract.” *Id.* To restate the matter differently, “the acts of reliance by the promisee to his detriment (provide) a substitute for consideration.” *Id.*
21. Hayes urges that in the absence of a bargained-for promise the facts require application of the doctrine of promissory estoppel. He stresses that he retired voluntarily while expecting to receive a pension. He would not have otherwise retired. Nor did he seek other employment.
22. We disagree with this contention largely for the reasons already stated. One of the essential elements of the doctrine of promissory estoppel is that the promise must induce the promisee's action or forbearance. The particular act in this regard is plaintiff's decision whether or not to retire. As we stated earlier, the record indicates that he made the decision on his own initiative. In other words, the conversation between Hayes and Mainelli which occurred a week before Hayes left his employment cannot be said to have induced his decision to leave. He had reached that decision long before.
23. An example taken from the Restatement provides a meaningful contrast:
2. A promises B to pay him an annuity during B's life. B thereupon resigns profitable employment, as A expected that he might. B receives the annuity for some years, in the meantime becoming disqualified from again obtaining good employment. A's promise is binding.
- 1 RESTATEMENT OF CONTRACTS § 90 at 111 (1932).
24. In *Feinberg v. Pfeiffer Co.*, 322 S.W.2d 163 (Mo. App.1959), the plaintiff-employee had worked for her employer for nearly forty years. The defendant corporation's board of directors resolved, in view of her long years of service, to obligate itself to pay “retirement privileges” to her. The resolution did not require the plaintiff to retire. Instead, the decision whether and when to retire remained entirely her own. The board then informed her of its resolution. The plaintiff worked for eighteen months more before retiring. She sued the corporation when it reduced her monthly checks seven years later. The court held that a pension contract existed between the parties. Although continued employment was not a consideration to her receipt of retirement benefits, the court found sufficient reliance on the part of the plaintiff to support her

claim. The court based its decision upon the above restatement example, that is, the defendant informed the plaintiff of its plan, and the plaintiff in reliance thereon, retired. *Feinberg* presents factors that also appear in the case at bar. There, the plaintiff had worked many years and desired to retire; she would not have left had she not been able to rely on a pension; and once retired, she sought no other employment.

25. However, the important distinction between *Feinberg* and the case before us is that in *Feinberg* the employer's decision definitely shaped the thinking of the plaintiff. In this case the promise did not. It is not reasonable to infer from the facts that Hugo R. Mainelli, Jr., expected retirement to result from his conversation with Hayes. Hayes had given notice of his intention seven months previously. Here there was thus no inducement to retire which would satisfy the demands of § 90 of the Restatement. Nor can it be said that Hayes's refraining from other employment was "action or forbearance of a definite and substantial character." The underlying assumption of Hayes's initial decision to retire was that upon leaving the defendant's employ, he would no longer work. It is impossible to say that he changed his position any more so because of what Mainelli had told him in light of his own initial decision. These circumstances do not lead to a conclusion that injustice can be avoided only by enforcement of Plantations's promise. Hayes received \$20,000 over the course of four years. He inquired each year about whether he could expect a check for the following year. Obviously, there was no absolute certainty on his part that the pension would continue. Furthermore, in the face of his uncertainty, the mere fact that payment for several years did occur is insufficient by itself to meet the requirements of reliance under the doctrine of promissory estoppel.
26. For the foregoing reasons, the defendant's appeal is sustained and the judgment of the Superior Court is reversed. The papers of the case are remanded to the Superior Court.

Dyno Construction Co. v. McWane, Inc.

United States Court of Appeals, Sixth Circuit
198 F.3d 567 (1999)

QUIST, District Judge.

1. Plaintiff, Dyno Construction Company, sued Defendant, McWane, Inc., alleging various breach of contract claims arising out of Dyno's purchase of ductile iron pipe from McWane that was later found to be defective. The district court denied the parties' cross-motions for summary judgment, and a jury returned a general verdict in favor of McWane. The district court denied Dyno's motion for a new trial. Dyno appeals the order denying its motion for summary judgment, the judgment entered after trial, and the order denying Dyno's motion for a new trial. We find no error and affirm.

I. FACTUAL AND PROCEDURAL BACKGROUND

2. Dyno is a company engaged in the business of constructing underground utility projects, specifically underground water and sewer lines. Dyno was purchased in the fall of 1995 by Frederick Harrah, Laymond Lewis, and a third party. Prior to purchasing Dyno, Harrah and Lewis were employees of Reynolds, Inc., a large underground pipeline construction company also in the business of installing underground water and sewer lines.
3. McWane is a manufacturer and seller of ductile iron pipe and fittings for underground utility projects. Harrah and Lewis frequently purchased pipe from McWane during their employment with Reynolds, as McWane was the exclusive supplier of certain types of ductile iron products to Reynolds.
4. Sometime shortly before November 6, 1995, Dyno submitted a bid to the City of Perrysburg, Ohio, for a multimillion dollar water and sewer system project. In order to prepare the bid, Lewis contacted various suppliers, including McWane, to obtain quotes for necessary materials. On November 6, 1995, Dyno learned that it was the low bidder on the project and would be awarded the contract.
5. On November 8, 1995, McWane's district sales manager, Kevin Ratcliffe, faxed Dyno a document containing quantities and prices for the materials Dyno requested for the

Perrysburg Project.¹ Ratcliffe sent a second fax to Lewis on November 13, 1995, which included handwritten prices and notes next to each item. On the fax cover sheet, Ratcliffe asked Lewis to “[p]lease call.”

6. On or prior to November 22, 1995, Lewis phoned Ratcliffe and told him to order the materials. Lewis testified at his deposition that he thought that there was a “done deal” when he got off the phone with Ratcliffe. However, after the phone call, Ratcliffe prepared and sent a package to Lewis via Federal Express. The Federal Express package included a purchase order, a credit application, and a cover letter in which Ratcliffe asked Lewis to review and sign the purchase order and credit application and return the originals to Ratcliffe. The purchase order and credit application each stated that the sale of the materials was subject to the terms and conditions printed on the reverse sides of those documents. The reverse side of each document contained additional terms and conditions, including a provision which limited McWane's liability for defective materials. The Federal Express invoice kept in McWane's files showed that Dyno received the package on November 24, 1995, at 8:53 a.m.
7. Lewis called Ratcliffe on December 1, 1995, to inquire about the status of Dyno's order. Lewis testified that Ratcliffe told him that “you have to sign our forms.” Lewis indicated both in his deposition and at trial that he was not surprised when Ratcliffe told him that the purchase order and credit application would have to be signed before McWane would ship the materials. Lewis told Ratcliffe that he had not received the forms Ratcliffe sent via Federal Express and could not find the package in his office. At Lewis' request, in order to expedite the transaction, Ratcliffe faxed Lewis copies of the documents that were sent on November 22, 1995. However, Ratcliffe did not fax the back sides of the documents which included, among other things, this provision limiting McWane's liability:

SELLER SHALL NOT BE LIABLE FOR EXEMPLARY, PUNITIVE, SPECIAL, INCIDENTAL, CONSEQUENTIAL DAMAGES OR EXPENSES, INCLUDING BUT NOT LIMITED TO, LOSS PROFIT REVENUES, LOSS OF USE OF THE GOODS, OR ANY ASSOCIATED GOODS OR EQUIPMENT, DAMAGE TO PROPERTY OF BUYER, COST OF CAPITAL, COST OF SUBSTITUTE GOODS, DOWNTIME,

¹ Ratcliffe was actually the district sales manager for Clow Water Systems, Co., a division of McWane. To avoid confusion, the Court will refer to the Clow division as McWane.

LIQUIDATED DAMAGES, OR THE CLAIMS OF BUYER'S CUSTOMERS FOR ANY OF THE AFORESAID DAMAGES, OR FROM ANY OTHER CAUSE RELATING THERETO, AND SELLER'S LIABILITY HEREUNDER IN ANY CASE IS EXPRESSLY LIMITED TO THE REPLACEMENT (IN THE FORM ORIGINALLY SHIPPED) OF GOODS NOT COMPLYING WITH THIS AGREEMENT, OR, AT SELLER'S ELECTION, TO THE REPAYMENT OF, OR CREDITING BUYER WITH, AN AMOUNT EQUAL TO THE PURCHASE PRICE OF SUCH GOODS PRIOR PAID TO AND RECEIVED BY SELLER, WHETHER SUCH CLAIMS ARE FOR BREACH OF WARRANTY OR NEGLIGENCE....

8. Dyno signed the faxed pages without the quoted damages limitation provision and returned them to Ratcliffe later that day.
9. Dyno had substantial problems with the pipes it purchased from McWane. Although McWane repaired and reinstalled the pipe to the satisfaction of Dyno, it refused to pay Dyno for consequential damages suffered as a result of the defects in the pipes on the basis of the limitation of damages provision on the back of the purchase order. Dyno filed this suit in an attempt to recover its consequential damages.
10. Both parties moved for summary judgment with respect to the question of whether the quoted provision limiting McWane's liability for consequential damages was a part of the Dyno/McWane contract.² In denying the motions, the district court rejected Dyno's contention that the two written quotations which Ratcliffe sent to Lewis were offers that Dyno accepted when Lewis informed Ratcliffe that Dyno wished to purchase the pipe from McWane because the quotations were part of preliminary negotiations between the parties. Instead, the court concluded that the contract was formed or, alternatively, modified, when Lewis signed the documents he received from Ratcliffe by fax on December 1, 1995. The district court also rejected as a matter of law McWane's arguments that Dyno's acceptance of documents containing the warranty limitation provision established a course of performance and that a course of dealing was established by Lewis' dealings with McWane while Lewis was employed at Reynolds. Instead, the district court found that McWane's argument that Lewis had knowledge of the disputed provision based upon his receipt

² McWane also sought summary judgment on the issue of whether the pipe was defective.

of the Federal Express package presented a genuine issue of material fact. Thus, the district court framed the issue for the jury with respect to the limitation of damages provision as whether Lewis knew or should have known about McWane's terms and conditions at the time he signed the fax copy.

11. At trial, during the conference on jury instructions, the district court rejected Dyno's proposed instruction number 7, which would have allowed the jury to find that the contract had been formed on or before November 22, 1995, on the basis of its ruling with respect to the summary judgment motions that the contract was formed on December 1, 1995.³ At the conclusion of trial, the jury returned a verdict in favor of McWane.

II. ANALYSIS

A. Summary Judgment

12. Dyno first contends that the district court erred when it found that the contract was formed on December 1, 1995, rather than on November 22, 1995. Although Dyno does not argue that the denial of its motion for summary judgment was erroneous, Dyno asserts that the determination made by the district court in ruling on the motion that the contract was made on December 1, 1995, when Lewis signed the fax documents, was erroneous.
13. Dyno asserted in its motion for summary judgment, and continues to argue to this Court, that the contract was actually entered into on November 22, 1995, when Lewis told Ratcliffe to go ahead and order the materials that Ratcliffe had listed in his November 8 and November 13 faxes. Dyno claims that the parties agreed to the essential terms of price, quantity, and description, and any other terms to the contract could be supplied by the “gap-filler” provisions of the Uniform Commercial Code, which do not limit the seller's liability for consequential damages.
14. In order to prove the existence of a contract, a plaintiff is required to demonstrate the essential requirements of an offer, acceptance, and consideration. *See Helle v. Landmark, Inc.*, 15 Ohio App.3d 1, 8, 472 N.E.2d 765, 773 (1984). A valid and binding contract comes into existence when an offer is accepted. *See Realty Dev., Inc.*

³ Judge James G. Carr, to whom the case was initially assigned, made the ruling on the parties' cross motions for summary judgment. The case was then reassigned to Senior Judge John W. Potter, who conducted the trial.

v. Kosydar, 322 N.E.2d 328, 332 (Ohio Ct.App.1974) (*per curiam*). Dyno contends that the written price quotations Ratcliffe faxed to Lewis on November 8, 1995, and November 13, 1995, constituted the offer, which Lewis accepted on behalf of Dyno on or about November 22, 1995, when Lewis told Ratcliffe to order the materials listed on the price quote.

15. “Typically, a price quotation is considered an invitation for an offer, rather than an offer to form a binding contract.” *White Consol. Indus., Inc. v. McGill Mfg. Co.*, 165 F.3d 1185, 1190 (8th Cir.1999) (citing *Litton Microwave Cooking Prods. v. Leviton Mfg. Co.*, 15 F.3d 790, 794 (8th Cir.1994)); *see also Realty Dev., Inc.*, 322 N.E.2d at 332 (finding that the price quotation furnished to the appellant was “susceptible to the interpretation that [it] was nothing more than an invitation to appellant to make an offer”). Instead, a buyer's purchase agreement submitted in response to a price quotation is usually deemed the offer. *See Master Palletizer Sys., Inc. v. T.S. Ragsdale Co.*, 725 F.Supp. 1525, 1531 (D.Colo.1989). However, a price quotation may suffice for an offer if it is sufficiently detailed and it “reasonably appear[s] from the price quotation that assent to that quotation is all that is needed to ripen the offer into a contract.” *Quaker State Mushroom Co. v. Dominick's Finer Foods, Inc., of Illinois*, 635 F.Supp. 1281, 1284 (N.D.Ill.1986); *see also Master Palletizer Sys.*, 725 F.Supp. at 1531. While the inclusion of a description of the product, price, quantity, and terms of payment may indicate that the price quotation is an offer rather than a mere invitation to negotiate, the determination of the issue depends primarily upon the intention of the person communicating the quotation as demonstrated by all of the surrounding facts and circumstances. *See Interstate Indus., Inc. v. Barclay Indus., Inc.*, 540 F.2d 868, 871 (7th Cir.1976) (quoting *R.E. Crummer & Co. v. Nuveen*, 147 F.2d 3, 5 (7th Cir.1945)); *Maurice Elec. Supply Co. v. Anderson Safeway Guard Rail Corp.*, 632 F.Supp. 1082, 1089 (D.D.C.1986) (mem.op.). Thus, to constitute an offer, a price quotation must “be made under circumstances evidencing the express or implied intent of the offeror that its acceptance shall constitute a binding contract.” *Maurice Elec. Supply*, 632 F.Supp. at 1087.
16. In *Interstate Industries, Inc. v. Barclay Industries, Inc.*, 540 F.2d 868 (7th Cir.1976), the court determined that a letter sent by the defendant to the plaintiff stating that the defendant would be able to manufacture fiberglass panels for the plaintiff pursuant to specified standards at certain prices did not constitute an offer. Among other things, the court found that the letter's use of the term “price quotation,” lack of language indicating that an offer was being made, and absence of terms regarding quantity,

time of delivery, or payment terms established that the letter was not intended as an offer. *See id.* at 873. *Thos. J. Sheehan Co. v. Crane Co.*, 418 F.2d 642 (8th Cir.1969), cited by the court in *Interstate Industries*, concluded that a price list for copper tubing which a supplier furnished to a subcontractor in connection with the latter's bid on a job was merely an invitation to engage in future negotiations. The court observed:

The only evidence of defendant's alleged September 1963 offer is the oral communication to plaintiff that Crane Company could supply copper for the Mansion House Project at a lower price than originally quoted. Reference was made to the new "Chase" price sheet concerning deliveries in minimum quantities of 5000 pounds or 5000 feet, and that prices for copper would be guaranteed for the "duration of the job." At this time nothing was stated by the defendant or plaintiff as to (1) the time in which plaintiff had to accept the "offer," (2) the quantity of copper tubing, fittings, or other supplies to be ordered, (3) the terms of payment or (4) the time when Crane Company promised to perform....

The "Chase" price sheet was nothing more than a circular sent to distributors by the manufacturer, Wolverine. Without other terms of commitment, we find that the proposal as to "price protection" was related only to the quoted price as a condition upon which the supplier would be willing *in the future* to negotiate a contract of shipment....

Prices and price factors quoted by suppliers to contractors for the purposes of aiding contractors to make bid estimates, without more specific terms, do not obligate the supplier to comply with any purchase order upon whatever terms and conditions the contractor may choose to offer at some undetermined date in the future. The fact that the prices quoted are not withdrawn or that a withdrawal of them is not communicated to the contractor is immaterial. No duty exists to revoke terms which without words of commitment merely quote an existing price at which a contract of purchase might be negotiated.

Thos. J. Sheehan, 418 F.2d at 645-46 (italics in original).

17. Similarly, in *Day v. Amax, Inc.*, 701 F.2d 1258 (8th Cir.1983), the Seventh Circuit affirmed the district court's grant of a directed verdict to the defendant on the issue of whether the defendant's description of mining equipment and a quotation of prices constituted an offer, reasoning that "[a]lthough questions of intent are usually for the

jury to decide ... the record discloses no evidence that any of the defendants manifested an intent to enter into a contract with [the plaintiff].” *Id.* at 1263. Thus, the plaintiff’s evidence that the defendant had given the plaintiff signed writings containing detailed descriptions of the mining equipment and the terms of sale and had set up an escrow account were insufficient to demonstrate the defendant’s intent to enter into a contract. *See id.* at 1264-65; *accord Maurice Elec. Supply*, 632 F.Supp. at 1088 (concluding that the defendant’s price quote “was simply a statement of price for three individual high mast poles of varying height” because “[i]t did not specify quality or quantity, time and place of delivery, or terms of payment” and “[t]here was no promise that the quote would remain open for a specified period of time”).

18. In contrast to the cases discussed above, the court in *Bergquist Co. v. Sunroc Corp.*, 777 F.Supp. 1236 (E.D.Pa.1991), found that the question of whether the price quotation at issue constituted an offer was a question of fact for the jury. Some of the factors cited by the court as creating an issue for the jury were: (i) the price quotation was developed by the defendant after the parties had engaged in substantial negotiations; (ii) the quotation included a description of the product, a list of various quantities at various prices, terms of payment, and delivery terms; (iii) the quotation contained the statement “This quotation is offered for your acceptance within 30 days”; and (iv) the price which the purchaser paid was the price listed in the price quotation rather than the price listed in the purchaser’s subsequent purchase order. *See id.* at 1249.
19. In this case, the facts before the district court furnished a sufficient basis for it to conclude as a matter of law that the contract was formed when Lewis signed the fax from Ratcliffe on December 1, 1995, rather than when Lewis told Ratcliffe to order the materials on November 22, 1995. In particular, neither the November 8 nor the November 13 price quotations contained words indicating that Ratcliffe intended to make an offer to Dyno. The word “Estimate” was printed at the top of the document faxed on November 8, and the message “Please call” was printed on the cover sheet for the document faxed on November 13. These words are indicative of an invitation to engage in future negotiations rather than an offer to enter into a contract. Although both price lists set forth descriptions of the materials, prices, and quantities, nothing was stated about the place of delivery, time of performance, or terms of payment. *See Litton Microwave Cooking Prods.*, 15 F.3d at 795 (rejecting the contention that the defendant’s price letters and catalogs, which failed to address the place of delivery, quantities, and availability of parts to be purchased were not offers). Finally, the fact

that Lewis voluntarily signed the December 1 fax demonstrated that he understood that a binding contract had not been formed as a result of the previous price quotations sent by Ratcliffe. In light of these facts, we agree with the district court that McWane's price quotations did not constitute offers and that the contract was formed on December 1, 1995.⁴

B. Motion for New Trial

[Students may wish to skim the rest of this opinion because it deals with issues that, though interesting, are peripheral to our discussion of offer.]

20. Dyno also contends that the trial court erred in denying its motion for a new trial. Dyno argued to the district court that it was entitled to a new trial because the district court made several erroneous rulings on evidentiary issues and jury instructions. Motions for a new trial are addressed to the sound discretion of the trial court. *See Hopkins v. Coen*, 431 F.2d 1055, 1059 (6th Cir.1970). We review a district court's denial of a motion for a new trial under an abuse of discretion standard. *See Holmes v. City of Massillon*, 78 F.3d 1041, 1045 (6th Cir.1996). An abuse of discretion occurs when this Court has “a definite and firm conviction that the trial court committed a clear error in judgment.” *Logan v. Dayton Hudson Corp.*, 865 F.2d 789, 790 (6th Cir.1989).

1. Evidentiary Issues

21. Dyno first argues that the district court erred in allowing testimony concerning Lewis' familiarity with McWane's standard purchase order, including its terms and conditions, based on Lewis' prior dealings with McWane as an employee of Reynolds. Dyno argues that Lewis' prior dealings with McWane as an employee of Reynolds are completely irrelevant to the issue of whether the contract between Dyno

⁴The cases cited by Dyno, *Reaction Molding Technologies, Inc. v. General Electric Co.*, 585 F.Supp. 1097 (E.D.Pa.1984), and *Loranger Plastics Corp. v. Incoe Corp.*, 670 F.Supp. 145 (W.D.Pa.1987), are both distinguishable from the instant case on their facts. In *Reaction Molding Technologies*, the quotations contained payment and delivery terms and thus were substantially more detailed than the price quotations at issue in this case. *See Reaction Molding Tech.*, 585 F.Supp. at 1099. In *Loranger Plastics*, the quotation stated that it was “subject to acceptance without modification within 30 days” from the date it was issued. *See Loranger Plastics*, 670 F.Supp. at 146. The language in the quotation therefore indicated that it was intended as an offer.

and McWane included a limitation of liability provision and that this evidence confused the jury and caused prejudicial error.

22. We agree with the district court that the evidence about Lewis' prior dealings with McWane, particularly as it related to Lewis' knowledge of McWane's standard terms and conditions, was relevant and properly admitted. The faxed copy of the purchase order signed by Lewis on December 1, 1995, stated on the front in large print directly above his signature that the purchase order was subject to the terms and conditions on the reverse side. There is no disputing that McWane intended those terms and conditions on the back of the purchase order to be part of the contract but that Ratcliffe inadvertently failed to fax the back of the purchase order to Lewis. Therefore, Lewis' knowledge of those terms or his knowledge that McWane used standard terms and conditions in its sales, based on his prior dealings with McWane, was particularly relevant to whether those terms and conditions became part of the contract. The jury could properly determine whether Lewis knew or should have known about the limitation of liability in McWane's standard terms and conditions, and therefore intended that the limitation of liability be part of the contract.
23. Dyno next contends that the district court abused its discretion and committed prejudicial error when it refused to admit Lewis' testimony that McWane had waived its limitation of liability for consequential damages on several occasions in its dealings with Reynolds while Lewis was an employee of that company. Dyno contends that if Lewis' prior dealings with McWane as an employee of Reynolds were relevant, McWane's waiver of its limitation of liability clause for Reynolds was also relevant.
24. We agree with the decision to exclude this evidence because its admission would have likely caused jury confusion. The issue for the jury was whether McWane's standard terms and conditions were part of the contract, not whether those terms and conditions would be enforced. Had the district court admitted the evidence, McWane would have been entitled to explore the circumstances under which consequential damages were allegedly paid and explain why those circumstances were different from those at issue in the case. The whole foray into the issue, which was collateral to the actual issues at trial, would have caused substantial prejudice to McWane. Furthermore, McWane's terms and conditions stated that any waiver of a right by McWane in a particular instance would not constitute a future waiver of that right.

25. Dyno's final evidentiary argument is that the district court erred in admitting Federal Express delivery records generated from Federal Express' computer system. McWane sought to lay the foundation for introduction of these records under the business records exception to the hearsay rule through the testimony of Fred Jacobs, the Operations Manager at the Federal Express office in Wauseon, Ohio. Jacobs explained that he was fully familiar with Federal Express' system for moving and tracking packages and testified that these records were generated and kept in the regular course of business by Federal Express in its centralized computer system in Memphis, Tennessee.
26. Dyno objected to the admission of the records, arguing that the records were not under Jacobs' "custody or control" because: (1) he was not responsible for the geographic area in Ohio where the package was shipped; and (2) the computer records were printed in Memphis. Dyno contends that because these records were not under Jacobs' custody or control, Jacobs could not lay a proper foundation for introduction of the records and they are therefore inadmissible as hearsay.
27. Federal Rule of Evidence 803(6) provides that the following evidence is not excluded by the hearsay rule:

A memorandum, report, record, or data compilation, in any form, of acts, events, conditions, opinions, or diagnoses, made at or near the time by, or from information transmitted by, a person with knowledge, if kept in the course of a regularly conducted business activity, and if it was the regular practice of that business activity to make the memorandum, report, record, or data compilation, all as shown by the testimony of the custodian or other qualified witness, unless the source of the information or the method or circumstances of preparation indicate lack of trustworthiness....

Fed. R. Evid. 803(6).

28. While Dyno is correct that Jacobs could not lay a foundation for introduction of the Federal Express records under Rule 803(6) as a "custodian" of the records, Jacobs would be a proper witness to lay a foundation as an "other qualified witness" as described in the Rule. To be an "other qualified witness," it is not necessary that the person laying the foundation for the introduction of the business record have personal knowledge of their preparation. *See United States v. Franks*, 939 F.2d 600, 602-03 (8th Cir.1991) (rejecting the defendant's contention that the district court erred in

admitting Federal Express records on the basis that the witness laying the foundation was unable to determine which employees prepared delivery records and airbills). All that is required of the witness is that he or she be familiar with the record-keeping procedures of the organization. *See United States v. Wables*, 731 F.2d 440, 449 (7th Cir.1984)(stating that “[i]t is clear that, in admitting documents under the business records exception to the hearsay rule, ‘the testimony of the custodian or otherwise qualified witness who can explain the record-keeping of his organization is ordinarily essential’ ”) (quoting 4 Weinstein, Evidence ¶ 803(6)[02] (1981)); *NLRB v. First Termite Control Co.*, 646 F.2d 424, 427 (9th Cir.1981) (noting that through the custodian or “other qualified witness” requirement, Rule 803(6) “insures the presence of some individual at trial who can testify to the methods of keeping the information”). Thus, in *United States v. Hathaway*, 798 F.2d 902 (6th Cir.1986), we stated that “[w]hen a witness is used to lay the foundation for admitting records under Rule 803(6), all that is required is that the witness be familiar with the record keeping system.” *Hathaway*, 798 F.2d at 906. In that case, we rejected the defendant's contention that the government could not lay a foundation through the testimony of an FBI agent for the admission of records seized from the defendant's business offices under the business records exception. We found “no reason why a proper foundation for application of Rule 803(6) cannot be laid, in part or in whole, by the testimony of a government agent or other person outside the organization whose records are sought to be admitted.” *Id.* at 906; *see also Zayre Corp. v. S.M. & R. Co.*, 882 F.2d 1145, 1150 (7th Cir.1989) (noting that a person qualified to lay the foundation under Rule 803(6) need not even be an employee of the entity keeping the records, as long as the witness understands the system by which they are made).

29. Jacobs testified in depth about his understanding of Federal Express' system for delivering and tracking documents, as well as its system for central storage of its voluminous computerized records in Memphis. That Jacobs was not involved in the preparation of the documents or that he did not know who prepared them were not matters that precluded the admission of the documents as business records. Therefore, the district court did not abuse its discretion in admitting the Federal Express records.
30. Furthermore, there was other evidence from which the jury could have concluded that Dyno received the Federal Express package by December 1, 1995. For instance, McWane also introduced into evidence a copy of a Federal Express invoice kept in its files as a business record, for which there is no dispute that a proper foundation was laid for admission at trial under the business records exception, through the testimony

of its custodian, Ratcliffe. The invoice showed that Dyno received the package on November 24, 1995, at 8:53 a.m. Accordingly, there was sufficient evidence for the jury to find that Dyno was or should have been aware of McWane's terms and conditions, including its limitation of liability, at the time it signed the faxed purchase order on December 1, 1995.

2. Jury Instructions

31. Dyno argues that the district court committed reversible error in refusing to give two of its proposed jury instructions. Jury instructions in civil cases are reviewed “as a whole to determine whether they adequately inform the jury of the relevant considerations and provide a basis in law for aiding the jury in reaching its decision. A judgment on a jury verdict may be vacated when the instructions, viewed as a whole, were confusing, misleading and prejudicial.” *Jones v. Consolidated Rail Corp.*, 800 F.2d 590, 592 (6th Cir.1986) (citation omitted).
32. Dyno first argues that the district court committed reversible error in refusing to give Dyno's proposed jury instruction number seven, which would have allowed the jury to find that the contract was formed on November 22, 1995, when Lewis told Ratcliffe by telephone to go ahead and order the materials. Because this Court has already affirmed the district court's conclusion that the contract was formed on December 1, 1995, when Lewis signed the document faxed by Ratcliffe, it would have been improper for the district court to instruct the jury that it could find that the contract was formed on November 22, 1995. Accordingly, the district court properly rejected Dyno's proposed instruction.
33. Dyno's final argument is that the district court committed reversible error in not giving its proposed instruction number twelve, which read:

McWane must show that the agent designated to receive such information as Federal Express packages actually received and had knowledge of the contents of the package before Dyno is deemed to have knowledge of the disputed terms.
34. We believe that this instruction is an erroneous statement of the law and would have placed an unwarranted burden on McWane at trial. The evidence presented at trial was sufficient to allow the jury to find that the Federal Express documents had been delivered to an authorized agent of Dyno because the Federal Express documents

were actually located in Dyno's job file for the Perrysburg project and contained Lewis' handwriting at the top of the documents. In addition, McWane's evidence showed that the documents were actually delivered to Dyno's offices on November 24, 1995. Moreover, McWane could demonstrate that Dyno had received and had knowledge of the contents of the package even if the "agent designated to receive such information" did not actually receive and have knowledge of the contents of the package. For example, if some agent of Dyno other than the "agent designated to receive such information" received the package, that knowledge could be imputed to Dyno. There was also evidence that Lewis had knowledge of the contents of the package, in that he had previous knowledge about McWane's credit application and terms and conditions, even though he testified that he never received the package. This instruction thus ignored other means by which McWane could have demonstrated Dyno's knowledge of McWane's terms and conditions and would have placed an unreasonable burden on McWane to prove actual receipt and review of the documents by the specified Dyno agent. That burden would have been extremely difficult to meet because no one at McWane specifically observed Dyno's handling and receipt of the November 22 documents. Thus, the failure to give this instruction does not render the instructions, "viewed as a whole, [] confusing, misleading and prejudicial..." *Jones*, 800 F.2d at 592.

35. Therefore, Dyno was not entitled to a new trial.

III. CONCLUSION

36. For the foregoing reasons, the judgment of the district court is **AFFIRMED**.

Lefkowitz v. Great Minneapolis Surplus Store

Supreme Court of Minnesota
251 Minn. 188, 86 N.W.2d 689 (1957)

MURPHY, Justice.

1. This is an appeal from an order of the Municipal Court of Minneapolis denying the motion of the defendant for amended findings of fact, or, in the alternative, for a new trial. The order for judgment awarded the plaintiff the sum of \$138.50 as damages for breach of contract.
2. This case grows out of the alleged refusal of the defendant to sell to the plaintiff a certain fur piece which it had offered for sale in a newspaper advertisement. It appears from the record that on April 6, 1956, the defendant published the following advertisement in a Minneapolis newspaper:

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

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

Saturday 9 A.M.
2 Brand New Pastel
Mink 3-Skin Scarfs
Selling for \$89.50
Out they go
Saturday. Each \$1.00

1 Black Lapin Stole
Beautiful
worth \$139.50 \$1.00

First Come -- First Served

4. The record supports the findings of the court that on each of the Saturdays following the publication of the above-described ads the plaintiff was the first to present himself at the appropriate counter in the defendant's store and on each occasion demanded the coat and the stole so advertised and indicated his readiness to pay the sale price of \$1. On both occasions, the defendant refused to sell the merchandise to the plaintiff, stating on the first occasion that by a 'house rule' the offer was intended for women only and sales would not be made to men, and on the second visit that plaintiff knew defendant's house rules.
5. The trial court properly disallowed plaintiff's claim for the value of the fur coats since the value of these articles was speculative and uncertain. The only evidence of value was the advertisement itself to the effect that the coats were "Worth to \$100.00," how much less being speculative especially in view of the price for which they were offered for sale. With reference to the offer of the defendant on April 13, 1956, to sell the "1 Black Lapin Stole...worth \$139.50..." the trial court held that the value of this article was established and granted judgment in favor of the plaintiff for that amount less the \$1 quoted purchase price.
6. The defendant contends that a newspaper advertisement offering items of merchandise for sale at a named price is a "unilateral offer" which may be withdrawn without notice. He relies upon authorities which hold that, where an advertiser publishes in a newspaper that he has a certain quantity or quality of goods which he wants to dispose of at certain prices and on certain terms, such advertisements are not offers which become contracts as soon as any person to whose notice they may come signifies his acceptance by notifying the other that he will take a certain quantity of them. Such advertisements have been construed as an invitation for an offer of sale on the terms stated, which offer, when received, may be accepted or rejected and which therefore does not become a contract of sale until accepted by the seller; and until a contract has been so made, the seller may modify or revoke such prices or terms. *Montgomery Ward & Co. v. Johnson*, 209 Mass. 89, 95 N.W. 290; *Nickel v. Theresa Farmers Co-op. Ass'n*, 247 Wis. 412, 20 N.W.2d 117; *Lovett v. Frederick Loeser & Co. Inc.*, 124 Misc. 81, 207 N.Y.S. 753; *Schenectady Stove Co. v. Holbrook*, 101 N.Y. 45, 4 N.E. 4; *Georgian Co. v. Bloom*, 27 Ga. App. 468, 108 S.E. 813; *Craft v. Elder & Johnson Co.*, 38 N.E.2d 416, 34 Ohio L.A. 603; Annotation, 157 A.L.R. 746.
7. The defendant relies principally on *Craft v. Elder & Johnston Co.*, *supra*. In that case, the court discussed the legal effect of an advertisement offering for sale, as a one-day

special, an electric sewing machine at a named price. The view was expressed that the advertisement was (38 N.E.2d 417, 34 Ohio L.A. 605) “not an offer made to any specific person but was made to the public generally. Thereby it would be properly designated as a unilateral offer and not being supported by any consideration could be withdrawn at will and without notice.” It is true that such an offer may be withdrawn before acceptance. Since all offers are by their nature unilateral because they are necessarily made by one party or on one side in the negotiation of a contract, the distinction made in that decision between a unilateral offer and a unilateral contract is not clear. On the facts before us we are concerned with whether the advertisement constituted an offer, and, if so, whether the plaintiff’s conduct constituted an acceptance.

8. There are numerous authorities which hold that a particular advertisement in a newspaper or circular letter relating to a sale of articles may be construed by the court as constituting an offer, acceptance of which would complete a contract. *J. E. Pinkham Lumber Co. v. C. W. Griffin & Co.*, 212 Ala. 341, 102 So. 689; *Seymour v. Armstrong & Kassebaum*, 62 Kan. 720, 64 P. 612; *Payne v. Lautz Bros. & Co.*, City Ct., 166 N.Y.S. 844, affirmed, 168 N.Y.S. 369, affirmed, 185 App.Div. 904, 171 N.Y.S. 1094; *Arnold v. Phillips*, 1 Ohio Dec. Reprint 195, 3 West. Law J. 448; *Oliver v. Henley*, Tex. Civ. App., 21 S.W.2d 576; Annotation, 157 A.L.R. 744, 746.
9. The test of whether a binding obligation may originate in advertisements addressed to the general public is “whether the facts show that some performance was promised in positive terms in return for something requested.” 1 WILLISTON, CONTRACTS (Rev. ed.) § 27.
10. The authorities above cited emphasize that, where the offer is clear, definite, and explicit, and leaves nothing open for negotiation, it constitutes an offer, acceptance of which will complete the contract. The most recent case on the subject is *Johnson v. Capital City Ford Co.*, La. App., 85 So.2d 75, in which the court pointed out that a newspaper advertisement relating to the purchase and sale of automobiles may constitute an offer, acceptance of which will consummate a contract and create an obligation in the offeror to perform according to the terms of the published offer.
11. Whether in any individual instance a newspaper advertisement is an offer rather than an invitation to make an offer depends on the legal intention of the parties and the surrounding circumstances. Annotation, 157 A.L.R. 744, 751; 77 C.J.S., SALES, §

25b; 17 C.J.S., CONTRACTS, § 389. We are of the view on the facts before us that the offer by the defendant of the sale of the Lapin fur was clear, definite, and explicit, and left nothing open for negotiation. The plaintiff having successfully managed to be the first one to appear at the seller's place of business to be served, as requested by the advertisement, and having offered the stated purchase price of the article, he was entitled to performance on the part of the defendant. We think the trial court was correct in holding that there was in the conduct of the parties a sufficient mutuality of obligation to constitute a contract of sale.

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

Affirmed.

Ever-Tite Roofing Corp. v. Green

Court of Appeals of Louisiana
83 So. 2d 449 (1955)

AYRES, Judge.

1. This is an action for damages allegedly sustained by plaintiff as the result of the breach by the defendants of a written contract for the re-roofing of defendants' residence. Defendants denied that their written proposal or offer was ever accepted by plaintiff in the manner stipulated therein for its acceptance, and hence contended no contract was ever entered into. The trial court sustained defendants' defense and rejected plaintiff's demands and dismissed its suit at its costs. From the judgment thus rendered and signed, plaintiff appealed.
2. Defendants executed and signed an instrument June 10, 1953, for the purpose of obtaining the services of plaintiff in re-roofing their residence situated in Webster Parish, Louisiana. The document set out in detail the work to be done and the price therefor to be paid in monthly installments. This instrument was likewise signed by plaintiff's sales representative, who, however, was without authority to accept the contract for and on behalf of the plaintiff. This alleged contract contained these provisions:

This agreement shall become binding only upon written acceptance hereof, by the principal or authorized officer of the Contractor, *or upon commencing performance of the work*. This contract is Not Subject to Cancellation. It is understood and agreed that this contract is payable at office of Ever-Tite Roofing Corporation, 5203 Telephone, Houston, Texas. It is understood and agreed that this Contract provides for attorney's fees and in no case less than ten per cent attorney's fees in the event same is placed in the hands of an attorney for collecting or collected through any court, and further provides for accelerated maturity for failure to pay any installment of principal or interest thereon when due.

This written agreement is the only and entire contract covering the subject matter hereof and no other representations have been made unto Owner except these herein contained. No guarantee on repair work, partial roof jobs, or paint jobs. (Emphasis supplied.)

3. Inasmuch as this work was to be performed entirely on credit, it was necessary for plaintiff to obtain credit reports and approval from the lending institution which was to finance said contract. With this procedure defendants were more or less familiar and knew their credit rating would have to be checked and a report made. On receipt of the proposed contract in plaintiff's office on the day following its execution, plaintiff requested a credit report, which was made after investigation and which was received in due course and submitted by plaintiff to the lending agency. Additional information was requested by this institution, which was likewise in due course transmitted to the institution, which then gave its approval.
4. The day immediately following this approval, which was either June 18 or 19, 1953, plaintiff engaged its workmen and two trucks, loaded the trucks with the necessary roofing materials and proceeded from Shreveport to defendants' residence for the purpose of doing the work and performing the services allegedly contracted for the defendants. Upon their arrival at defendants' residence, the workmen found others in the performance of the work which plaintiff had contracted to do. Defendants notified plaintiff's workmen that the work had been contracted to other parties two days before and forbade them to do the work.
5. Formal acceptance of the contract was not made under the signature and approval of an agent of plaintiff. It was, however, the intention of plaintiff to accept the contract by commencing the work, which was one of the ways provided for in the instrument for its acceptance, as will be shown by reference to the extract from the contract quoted hereinabove. Prior to this time, however, defendants had determined on a course of abrogating the agreement and engaged other workmen without notice thereof to plaintiff.
6. The basis of the judgment appealed was that defendants had timely notified plaintiff before "commencing performance of work." The trial court held that notice to plaintiff's workmen upon their arrival with the materials that defendants did not desire them to commence the actual work was sufficient and timely to signify their intention to withdraw from the contract. With this conclusion we find ourselves unable to agree.
7. Defendants' attempt to justify their delay in thus notifying plaintiff for the reason they did not know where or how to contact plaintiff is without merit. The contract itself, a copy of which was left with them, conspicuously displayed plaintiff's name, address

and telephone number. Be that as it may, defendants at no time, from June 10, 1953, until plaintiff's workmen arrived for the purpose of commencing the work, notified or attempted to notify plaintiff of their intention to abrogate, terminate or cancel the contract.

8. Defendants evidently knew this work was to be processed through plaintiff's Shreveport office. The record discloses no unreasonable delay on plaintiff's part in receiving, processing or accepting the contract or in commencing the work contracted to be done. No time limit was specified in the contract within which it was to be accepted or within which the work was to be begun. It was nevertheless understood between the parties that some delay would ensue before the acceptance of the contract and the commencement of the work, due to the necessity of compliance with the requirements relative to financing the job through a lending agency. The evidence as referred to hereinabove shows that plaintiff proceeded with due diligence.

9. The general rule of law is that an offer proposed may be withdrawn before its acceptance and that no obligation is incurred thereby. This is, however, not without exceptions. For instance, Restatement of the Law of Contracts stated:

(1) The power to create a contract by acceptance of an offer terminates at the time specified in the offer, or, if no time is specified, at the end of a reasonable time. What is a reasonable time is a question of fact depending on the nature of the contract proposed, the usages of business and other circumstances of the case which the offeree at the time of his acceptance either knows or has reason to know.

10. These principles are recognized in the Civil Code. LSA-C.C. Art. 1800 provides that an offer is incomplete as a contract until its acceptance and that before its acceptance the offer may be withdrawn. However, this general rule is modified by the provisions of LSA-C.C. Arts. 1801, 1802, 1804 and 1809, which read as follows:

Art. 1801. The party proposing shall be presumed to continue in the intention, which his proposal expressed, if, on receiving the unqualified assent of him to whom the proposition is made, he do not signify the change of his intention.

Art. 1802. He is bound by his proposition, and the signification of his dissent will be of no avail, if the proposition be made in terms, which evince a design to give the other party the right of concluding the contract by his assent; and

if that assent be given within such time as the situation of the parties and the nature of the contract shall prove that it was the intention of the proposer to allow....

Art. 1804. The acceptance needs (need) not be made by the same act, or in point of time, immediately after the proposition; if made at any time before the person who offers or promises has changed his mind, or may reasonably be presumed to have done so, it is sufficient....

Art. 1809. The obligation of a contract not being complete, until the acceptance, or in cases where it is implied by law, until the circumstances, which raise such implication, are known to the party proposing; *he may therefore revoke his offer or proposition before such acceptance, but not without allowing such reasonable time as from the terms of his offer he has given, or from the circumstances of the case he may be supposed to have intended to give to the party, to communicate his determination.* (Emphasis supplied.)

11. Therefore, since the contract did not specify the time within which it was to be accepted or within which the work was to have been commenced, a reasonable time must be allowed therefor in accordance with the facts and circumstances and the evident intention of the parties. A reasonable time is contemplated where no time is expressed. What is a reasonable time depends more or less upon the circumstances surrounding each particular case. The delays to process defendants' application were not unusual. The contract was accepted by plaintiff by the commencement of the performance of the work contracted to be done. This commencement began with the loading of the trucks with the necessary materials in Shreveport and transporting such materials and the workmen to defendants' residence. Actual commencement or performance of the work therefore began before any notice of dissent by defendants was given plaintiff. The proposition and its acceptance thus became a completed contract.
12. By their aforesaid acts defendants breached the contract. They employed others to do the work contracted to be done by plaintiff and forbade plaintiff's workmen to engage upon that undertaking. By this breach defendants are legally bound to respond to plaintiff in damages. LSA-C.C. Art. 1930 provides:

The obligations of contract (contracts) extending to whatsoever is incident to such contracts, the party who violates them, is liable, as one of the incidents

of his obligations, to the payment of the damages, which the other party has sustained by his default.

13. The same authority in Art. 1934 provides the measure of damages for the breach of a contract. This article, in part, states:

Where the object of the contract is anything but the payment of money, the damages due to the creditor for its breach are the amount of the loss he has sustained, and the profit of which he has been deprived,....

Plaintiff expended the sum of \$85.37 in loading the trucks in Shreveport with materials and in transporting them to the site of defendants' residence in Webster Parish and in unloading them on their return, and for wages for the workmen for the time consumed. Plaintiff's Shreveport manager testified that the expected profit on this job was \$226. None of this evidence is controverted or contradicted in any manner.

14. True, as plaintiff alleges, the contract provides for attorney's fees where an attorney is employed to collect under the contract, but this is not an action on the contract or to collect under the contract but is an action for damages for a breach of the contract. The contract in that respect is silent with reference to attorney's fees. In the absence of an agreement for the payment of attorney's fees or of some law authorizing the same, such fees are not allowed.
15. For the reasons assigned, the judgment appealed is annulled, avoided, reversed and set aside and there is now judgment in favor of plaintiff, Ever-Tite Roofing Corporation, against the defendants, G. T. Green and Mrs. Jessie Fay Green, for the full sum of \$311.37, with 5 per cent per annum interest thereon from judicial demand until paid, and for all costs.

Reversed and rendered.

Ciaramella v. Reader's Digest Association

United States Court of Appeals, Second Circuit
131 F.3d 320 (1997)

OAKES, Senior Circuit Judge:

1. Plaintiff filed suit against Reader's Digest Association ("RDA") alleging employment discrimination under the Americans with Disabilities Act, 42 U.S.C. §§ 12101-12213 (1994) ("ADA"), and article 15 of the New York State Executive Law, N.Y. Exec. Law §§ 290-301 (McKinney 1993), and also violations of the Employee Retirement Income Security Act, 29 U.S.C. §§ 1001-1461 (1994) ("ERISA"). Shortly after the commencement of the action, the parties negotiated a settlement which Ciaramella later refused to sign. RDA moved for an order to enforce the settlement agreement. The United States District Court for the Southern District of New York (Charles L. Briant, *J.*), granted the motion and dismissed the plaintiff's complaint with prejudice. Ciaramella argues that enforcement of the settlement agreement was improper because he had never signed the written agreement and the parties had specifically agreed that the settlement would not become binding until signed by all the parties. We agree, and reverse.

I. BACKGROUND

2. In November 1995, Ciaramella filed suit against his former employer, RDA, alleging that RDA failed to give him reasonable accommodations for his disability of chronic depression and subsequently terminated his employment in violation of the ADA and article 15 of New York State Executive Law. Ciaramella also raised a claim under ERISA for failure to pay severance benefits.
3. Before the exchange of any discovery, the parties entered into settlement negotiations. The negotiations resulted in an agreement in principle to settle the case in May, 1996. RDA prepared a draft agreement and sent it to Ciaramella's then attorney, Herbert Eisenberg, for review. This draft, as well as all subsequent copies, contained language indicating that the settlement would not be effective until executed by all the parties and their attorneys. Eisenberg explained the terms of the settlement to Ciaramella, who authorized Eisenberg to accept it. Eisenberg then made several suggestions for revision to RDA which were incorporated into a revised draft. After reviewing the revised draft, Eisenberg asked for a few final changes and then

allegedly stated to RDA's lawyer, "We have a deal." RDA forwarded several execution copies of the settlement to Eisenberg. However, before signing the agreement, Ciaramella consulted a second attorney and ultimately decided that the proposed settlement agreement was not acceptable to him and that he would not sign it. Eisenberg then moved to withdraw as plaintiff's counsel.

4. RDA, claiming that the parties had reached an enforceable oral settlement, filed a motion to enforce the settlement agreement on September 3, 1996. At a hearing on September 13, the district court granted Eisenberg's motion to withdraw, and stayed proceedings on the motion to enforce the settlement for thirty days to give Ciaramella time to obtain another attorney. On October 25, the district court heard RDA's motion to enforce the settlement agreement. Ciaramella had not yet obtained substitute counsel and appeared pro se at the hearing. The district court, after considering RDA's unopposed motion papers and questioning Ciaramella about the formation of the settlement agreement, granted RDA's motion to enforce the settlement by order dated October 28, 1996. The district court entered a judgment of dismissal on October 29, 1996. This Court has jurisdiction under 28 U.S.C. § 1291.

II. DISCUSSION

A. Choice of Law

5. An initial question presented is whether New York or federal common law determines whether the parties reached a settlement of claims brought under the ADA, ERISA, and state law. The district court analyzed the issue using federal common law and concluded that the parties had intended to enter into a binding oral agreement. We review the district court's findings of law under a de novo standard, and its factual conclusions under a clearly erroneous standard of review. *See Hirschfeld v. Spanakos*, 104 F.3d 16, 19 (2d Cir.1997).
6. Because we find that there is no material difference between the applicable state law or federal common law standard, we need not decide this question here. *See Bowden v. United States*, 106 F.3d 433, 439 (D.C.Cir.1997) (declining to decide whether state or federal common law governs the interpretation of a settlement agreement under Title VII where both sources of law dictate the same result); *Davidson Pipe Co. v. Laventhol & Horwath*, Nos. 84 Civ. 5192(LBS), 84 Civ. 6334(LBS), 1986 WL 2201, at *2 (S.D.N.Y. Feb. 11, 1986) (finding no federal rule that would differ critically from New York's rule governing the validity of oral settlement agreements). New

York relies on settled common law contract principles to determine when parties to a litigation intended to form a binding agreement.¹ See *Winston v. Mediafare Entertainment Corp.*, 777 F.2d 78, 80-81 (2d Cir.1985) (applying principles drawn from the Restatement (Second) of Contracts to determine whether a binding settlement agreement existed under New York law); see also *Jim Bouton Corp. v. William Wrigley Jr. Co.*, 902 F.2d 1074, 1081 (2d Cir.1990) (describing the New York rule of contract formation as “generally accepted”). Under New York law, parties are free to bind themselves orally, and the fact that they contemplate later memorializing their agreement in an executed document will not prevent them from being bound by the oral agreement. However, if the parties intend not to be bound until the agreement is set forth in writing and signed, they will not be bound until then. See *Winston*, 777 F.2d at 80; *V'Soske v. Barwick*, 404 F.2d 495, 499 (2d Cir.1968). The intention of the parties on this issue is a question of fact, to be determined by examination of the totality of the circumstances. See *International Telemeter Corp. v. Teleprompter Corp.*, 592 F.2d 49, 56 (2d Cir.1979). This same standard has been applied by courts relying on federal common law. See *Taylor v. Gordon Flesch Co.*, 793 F.2d 858, 862 (7th Cir.1986) (enforcing an oral settlement of a Title VII case where the parties had not specified the need for a final, signed document); *Board of Trustees of Sheet Metal Workers Local Union No. 137 Ins. Annuity & Apprenticeship Training Funds v. Vic Constr. Corp.*, 825 F.Supp. 463, 466 (E.D.N.Y.1993) (adopting the *Winston* analysis as based on “general contract principles” to uphold an oral settlement of an ERISA case); see also 1 Samuel Williston & Walter H.E. Jaeger, *A Treatise on the Law of Contracts* § 28 (3d ed. 1957) (“It is ... everywhere agreed that if the parties contemplate a reduction to writing of their agreement before it can be considered complete, there is no contract until the writing is signed.”).

¹ We note that New York Civil Practice Law and Rules 2104, N.Y. C.P.L.R. 2104 (McKinney 1997), which sets out technical requirements that must be met for a settlement agreement to be enforceable under New York law, may also apply. However, we need not address the issue whether section 2104 applies in federal cases or is consistent with federal policies favoring settlement. Cf. *Monaghan v. SZS 33 Assoc.*, 73 F.3d 1276, 1283 n. 3 (2d Cir.1996) (reserving decision on whether federal courts sitting in diversity must apply section 2104 when relying on New York law). Because we agree with Ciaramella that, under common law contract principles, Ciaramella never formed an agreement with RDA, we have no reason to rely on section 2104 in this case. See *Sears, Roebuck and Co. v. Sears Realty Co.*, 932 F.Supp. 392, 401-02 (N.D.N.Y.1996) (interpreting section 2104 as a defense to contract enforcement, and not as a rule of contract formation).

7. RDA urges us to fashion a federal rule of decision that would disregard this longstanding rule of contract interpretation and would hold parties to an oral settlement whenever their attorneys arrive at an agreement on all material terms.² We reject this suggestion. Even in cases where federal courts can choose the governing law to fill gaps in federal legislation, the Supreme Court has directed that state law be applied as the federal rule of decision unless it presents a significant conflict with federal policy. *See Atherton v. FDIC*, 519 U.S. 213 (1997); *O'Melveny & Myers v. FDIC*, 512 U.S. 79, 87 (1994) (noting that “cases in which judicial creation of a federal rule would be justified are ... ‘few and restricted’ ”) (quoting *Wheeldin v. Wheeler*, 373 U.S. 647, 651 (1963)).
8. We can find no federal objective contained in the ADA or ERISA that would be compromised by the application of the common law rules described above. RDA is correct that at least one of the federal statutes at issue expresses a preference for voluntary settlements of claims. *See* 42 U.S.C. § 12212 (1994) (encouraging the use of alternative means of dispute resolution, such as settlement, to resolve claims arising under the ADA). However, the common law rule does not conflict with this policy. The rule aims to ascertain and give effect to the intent of the parties at the time of contract. Such a rule promotes settlements that are truly voluntary. *See, e.g., Winston*, 777 F.2d at 80 (“Because of this freedom to determine the exact point at which an agreement becomes binding, a party can negotiate candidly, secure in the knowledge that he will not be bound until execution of what both parties consider to be final document [sic].”).
9. In fact, it is the rule suggested by RDA that would conflict with federal policy. Enforcing premature oral settlements against the expressed intent of one of the parties will not further a policy of encouraging settlements. People may hesitate to enter into negotiations if they cannot control whether and when tentative proposals become binding. We therefore decline to adopt a federal rule concerning the validity of oral agreements that is in conflict with federal policy and the settled common law principles of contract law.

² RDA relies on the Fifth Circuit's opinion in *Fulgence v. J. Ray McDermott & Co.*, 662 F.2d 1207 (5th Cir.1981) as support for this standard. However, RDA's reliance on *Fulgence* is misplaced because there was no suggestion in that case that the parties had ever explicitly reserved the right not to be bound until the execution of a written agreement.

B. Existence of a Binding Agreement

10. This court has articulated four factors to guide the inquiry regarding whether parties intended to be bound by a settlement agreement in the absence of a document executed by both sides. *Winston*, 777 F.2d at 80. We must consider (1) whether there has been an express reservation of the right not to be bound in the absence of a signed writing; (2) whether there has been partial performance of the contract; (3) whether all of the terms of the alleged contract have been agreed upon; and (4) whether the agreement at issue is the type of contract that is usually committed to writing. *Id.* No single factor is decisive, but each provides significant guidance. *See R.G. Group, Inc. v. Horn & Hardart Co.*, 751 F.2d 69, 74-75 (2d Cir.1984) (granting summary judgment where all four factors indicated that the parties had not intended to be bound by an oral franchise agreement). The district court did not explicitly rely on the *Winston* test, but concluded that based on the evidence the parties intended to enter into a binding oral agreement. Considering the above factors in the context of this case, we are left with the definite and firm conviction that the district court erred in concluding that the parties intended that the unexecuted draft settlement constitute a binding agreement. *See United States v. United States Gypsum Co.*, 333 U.S. 364, 395-97, 68 S.Ct. 525, 542-43, 92 L.Ed. 746 (1948) (finding clear error where trial court's findings conflicted with uncontroverted documentary evidence); *Winston*, 777 F.2d at 83 (finding clear error where the district court had enforced an unsigned settlement and three of the four factors indicated that the parties had not intended to be bound in the absence of a signed agreement).

1. Express Reservation

11. We find numerous indications in the proposed settlement agreement that the parties did not intend to bind themselves until the settlement had been signed. We must give these statements considerable weight, as courts should avoid frustrating the clearly-expressed intentions of the parties. *R.G. Group*, 751 F.2d at 75. For instance, in paragraph 10, the agreement states, “This Settlement Agreement and General Release shall not become effective (‘the Effective Date’) until it is signed by Mr. Ciaramella, Davis & Eisenberg, and Reader's Digest.”
12. RDA argues that the effect of paragraph 10 was simply to define the “Effective Date” of the agreement for the purpose of establishing the time period in which RDA was obligated to deliver payment and a letter of reference to Ciaramella. RDA further

urges that Ciaramella's obligation to dismiss the suit was not conditioned on paragraph 10. However, this interpretation is belied by the language of paragraph 2, which addresses RDA's payment obligation. Paragraph 2 states that RDA must proffer payment “[w]ithin ten (10) business days following the *later* of (a) the Effective Date of this Settlement Agreement and General Release (as defined by paragraph ten ...) or (b) entry by the Court of the Stipulation of Dismissal With Prejudice” (emphasis added). Under the terms of the proposed settlement, RDA had no obligation to pay Ciaramella until the agreement was signed and became effective. Likewise, under paragraph 12 of the final draft, RDA was not required to send the letter of reference until the agreement was signed. The interpretation that RDA advances, that Ciaramella had an obligation to dismiss the suit regardless of whether the settlement was signed, leaves Ciaramella no consideration for his promise to dismiss the suit. The more reasonable inference to be drawn from the structure of paragraph 2 is that it provided Ciaramella with an incentive to dismiss the suit quickly because he would receive no payment simply by signing the agreement, but that execution was necessary to trigger either parties' obligations. *See, e.g., Davidson Pipe Co.*, 1986 WL 2201, at *4 (finding that wording in a settlement agreement that placed great significance on the execution date evinced an intent not to create a binding settlement until some formal date of execution).

13. Similarly, several other paragraphs of the proposed agreement indicate that the parties contemplated the moment of signing as the point when the settlement would become binding. The agreement's first paragraph after the WHEREAS clauses reads, “NOW, THEREFORE, with the intent to be legally bound *hereby*, and in consideration of the mutual promises and covenants contained herein, Reader's Digest and Ciaramella agree to the terms and conditions *set forth below:*” (emphasis added). This language demonstrates that only the terms of the settlement agreement, and not any preexisting pact, would legally bind the parties. Read in conjunction with paragraph 10, which provides that the settlement agreement is effective only when signed, this paragraph explicitly signals the parties' intent to bind themselves only at the point of signature. *See, e. g., R.G. Group*, 751 F.2d at 71, 76 (finding an explicit reservation of the right not to be bound absent signature in the wording of an agreement that declared, “when duly executed, [this agreement] sets forth your rights and your

obligations”). In addition to the language of the first paragraph, paragraph 13 of the final draft³ contains a merger clause which states,

This Settlement Agreement and General Release constitutes the complete understanding between the parties, may not be changed orally and supersedes any and all prior agreements between the parties.... No other promises or agreements shall be binding unless in writing and signed by the parties.

14. The presence of such a merger clause is persuasive evidence that the parties did not intend to be bound prior to the execution of a written agreement. *See, e. g., R.G. Group*, 751 F.2d at 76; *McCoy v. New York City Police Dep't*, No. 95 Civ. 4508, 1996 WL 457312, at *2 (S.D.N.Y. Aug.14, 1996) (refusing to enforce a settlement of a § 1983 claim where a signed copy of the settlement agreement containing a merger clause had never been returned by the plaintiff).
15. Other parts of the agreement also emphasize the execution of the document. Paragraph 9 states, in relevant part,

Mr. Ciaramella represents and warrants that he ... has executed this Settlement Agreement and General Release after consultation with his ... legal counsel; ... that he voluntarily assents to all the terms and conditions contained therein; and that he is signing the Settlement Agreement and General Release of his own force and will.
16. Ciaramella's signature was meant to signify his voluntary and informed consent to the terms and obligations of the agreement. By not signing, he demonstrated that he withheld such consent.
17. The sole communication which might suggest that the parties did not intend to reserve the right to be bound is Eisenberg's alleged statement to RDA's counsel, “We have a deal.” However, nothing in the record suggests that either attorney took this statement to be an explicit waiver of the signature requirement. Eisenberg's statement followed weeks of bargaining over the draft settlement, which at all times clearly expressed the requirement that the agreement be signed to become effective. This Court has held in a similar situation that an attorney's statement that “a handshake deal” existed was insufficient to overcome “months of bargaining where there were repeated references to the need for a written and signed document, and where neither

³ This language was contained in paragraph 12 of earlier drafts.

party had ever ... even discussed dropping the writing requirement.” *R.G. Group*, 751 F.2d at 76; *see also Davidson Pipe Co.*, 1986 WL 2201, at *5 (holding that oral statement, “we have a deal,” made by one attorney to another did not in and of itself preclude a finding that the parties intended to be bound only by an executed contract).

2. Partial Performance

18. A second factor for consideration is whether one party has partially performed, and that performance has been accepted by the party disclaiming the existence of an agreement. *R.G. Group*, 751 F.2d at 75. No evidence of partial performance of the settlement agreement exists here. RDA paid no money to Ciaramella before the district court ordered the settlement enforced, nor did it provide Ciaramella with a letter of reference. These were the two basic elements of consideration that would have been due to Ciaramella under the settlement agreement.

3. Terms Remaining to be Negotiated

19. Turning to the third factor, we find that the parties had not yet agreed on all material terms. The execution copy of the settlement agreement contained a new provision at paragraph 12 that was not present in earlier drafts. That provision required RDA to deliver a letter of reference concerning Ciaramella to Eisenberg. The final draft of the settlement contained an example copy of the letter of reference annexed as Exhibit B. Ciaramella was evidently dissatisfied with the example letter. At the October 25, 1996, hearing at which Ciaramella appeared pro se, he attempted to explain to the court that the proposed letter of reference differed from what he had expected. He stated, “The original settlement that was agreed to, the one that was reduced to writing for me to sign had a discrepancy about letters of recommendation. I had requested one thing and the settlement in writing did not represent that.” Because Ciaramella's attorney resigned when Ciaramella refused to sign the settlement agreement, and RDA thereafter moved to enforce the agreement, Ciaramella never had an opportunity to finish bargaining for the letter he desired.
20. In *Winston*, this Court found that the existence of even “minor” or “technical” points of disagreement in draft settlement documents were sufficient to forestall the conclusion that a final agreement on all terms had been reached. *Winston*, 777 F.2d at 82-83. By contrast, the letter of reference from RDA was a substantive point of disagreement. It was also, from Ciaramella's perspective, a material term of the contract since it was part of Ciaramella's consideration for dismissing the suit. On this

basis, we find that the parties here had not yet reached agreement on all terms of the settlement.

4. Type of Agreement That Is Usually Reduced to a Writing

21. The final factor, whether the agreement at issue is the type of contract that is usually put in writing, also weighs in Ciaramella's favor. Settlements of any claim are generally required to be in writing or, at a minimum, made on the record in open court. *See, e.g.*, N.Y. C.P.L.R. § 2104; Cal.Civ.Proc.Code § 664.6 (West 1996). As we stated in *Winston*, “Where, as here, the parties are adversaries and the purpose of the agreement is to forestall litigation, prudence strongly suggests that their agreement be written in order to make it readily enforceable, and to avoid still further litigation.” *Winston*, 777 F.2d at 83.
22. We have also found that the complexity of the underlying agreement is an indication of whether the parties reasonably could have expected to bind themselves orally. *See R.G. Group*, 751 F.2d at 76; *Reprosystem, B.V. v. SCM Corp.*, 727 F.2d 257, 262-63 (2d Cir.1984) (finding that the magnitude and complexity of a four million dollar sale of six companies under the laws of five different countries reinforced the stated intent of the parties not to be bound until written contracts were signed). While this settlement agreement does not concern a complicated business arrangement, it does span eleven pages of text and contains numerous provisions that will apply into perpetuity. For instance, paragraph 6 determines how future requests for references would be handled, and also states that Ciaramella can never reapply for employment at RDA. Paragraph 7 states that Ciaramella will not publicly disparage RDA and agrees not to disclose the terms of the settlement agreement. In such a case, the requirement that the agreement be in writing and formally executed “simply cannot be a surprise to anyone.” *R.G. Group*, 751 F.2d at 77; *see also Winston*, 777 F.2d at 83 (finding a four page settlement agreement that contained obligations that would last over several years sufficiently complex to require reduction to writing).

CONCLUSION

23. In sum, we find that the totality of the evidence before us clearly indicates that Ciaramella never entered into a binding settlement agreement with his former employer. This conclusion is supported by the text of the proposed agreement and by Ciaramella's testimony at the October 25 hearing. Accordingly, the order enforcing

the settlement is vacated and the case remanded for further proceedings. Costs to appellant.

Pavel Enterprises v. A.S. Johnson Co.

Court of Appeals of Maryland
342 Md. 143, 674 A.2d 521 (1996)

Karwacki, Judge.

1. In this case we are invited to adapt the “modern” contractual theory of detrimental reliance,¹ or promissory estoppel, to the relationship between general contractors and their subcontractors. Although the theory of detrimental reliance is available to general contractors, it is not applicable to the facts of this case. For that reason, and because there was no traditional bilateral contract formed, we shall affirm the trial court.

I

2. The National Institutes of Health [hereinafter, “NIH”], solicited bids for a renovation project on Building 30 of its Bethesda, Maryland campus. The proposed work entailed some demolition work, but the major component of the job was mechanical, including heating, ventilation and air conditioning [“HVAC”]. Pavel Enterprises Incorporated [hereinafter, “PEI”], a general contractor from Vienna, Virginia and appellant in this action, prepared a bid for the NIH work. In preparing its bid, PEI solicited sub-bids from various mechanical subcontractors. The A.S. Johnson Company [hereinafter, “Johnson”], a mechanical subcontractor located in Clinton, Maryland and the appellee here, responded with a written scope of work proposal on July 27, 1993.² On the morning of August 5, 1993, the day NIH opened the general contractors' bids, Johnson verbally submitted a quote of \$898,000 for the HVAC

¹ We prefer to use the phrase detrimental reliance, rather than the traditional nomenclature of “promissory estoppel,” because we believe it more clearly expresses the concept intended. Moreover, we hope that this will alleviate the confusion which until now has permitted practitioners to confuse promissory estoppel with its distant cousin, equitable estoppel. *See Note, The “Firm Offer” Problem in Construction Bids and the Need for Promissory Estoppel*, 10 WM & MARY L.REV. 212, 214 n. 17 (1968) [hereinafter, “*The Firm Offer Problem*”].

² The scope of work proposal listed all work that Johnson proposed to perform, but omitted the price term. This is a standard practice in the construction industry. The subcontractor's bid price is then filled in immediately before the general contractor submits the general bid to the letting party.

component.³ Neither party disputes that PEI used Johnson's sub-bid in computing its own bid. PEI submitted a bid of \$1,585,000 for the entire project.

3. General contractors' bids were opened on the afternoon of August 5, 1993. PEI's bid was the *second* lowest bid. The government subsequently disqualified the apparent low bidder,⁴ however, and in mid-August, NIH notified PEI that its bid would be accepted.
4. With the knowledge that PEI was the lowest responsive bidder, Thomas F. Pavel, president of PEI, visited the offices of A.S. Johnson on August 26, 1993, and met with James Kick, Johnson's chief estimator, to discuss Johnson's proposed role in the work. Pavel testified at trial to the purpose of the meeting:

I met with Mr. Kick. And the reason for me going to their office was to look at their offices, to see their facility, to basically sit down and talk with them, as I had not done, and my company had not performed business with them on a direct relationship, but we had heard of their reputation. I wanted to go out and see where their facility was, see where they were located, and basically just sit down and talk to them. Because if we were going to use them on a project, I wanted to know who I was dealing with.

Pavel also asked if Johnson would object to PEI subcontracting directly with Powers for electric controls, rather than the arrangement originally envisioned in which Powers would be Johnson's subcontractor.⁵ Johnson did not object.

5. Following that meeting, PEI sent a fax to all of the mechanical subcontractors from whom it had received sub-bids on the NIH job. The text of that fax is reproduced:

Pavel Enterprises, Inc.

TO: PROSPECTIVE MECHANICAL SUBCONTRACTORS

³ PEI alleged at trial that Johnson's bid, as well as the bids of the other potential mechanical subcontractors contained a fixed cost of \$355,000 for a sub-sub-contract to "Landis and Gear Powers" [hereinafter, "Powers"]. Powers was the sole source supplier of the electric controls for the project.

⁴ The project at NIH was part of a set-aside program for small business. The apparent low bidder, J.J. Kirlin, Inc. was disqualified because it was not a small business.

⁵ Pavel testified at trial that restructuring the arrangement in this manner would reduce the amount PEI needed to bond and thus reduce the price of the bond.

FROM: ESTIMATING DEPARTMENT

REFERENCE: NIH, BLDG 30 RENOVATION

We herewith respectfully request that you review your bid on the above referenced project that was bid on 8/05/93. PEI has been notified that we will be awarded the project as J.J. Kirlin, Inc. [the original low bidder] has been found to be nonresponsive on the solicitation. We anticipate award on or around the first of September and therefor request that you supply the following information.

1. Please break out your cost for the "POWERS" supplied control work as we will be subcontracting directly to "POWERS".

Please resubmit your quote deleting the above referenced item.

We ask this in an effort to allow all prospective bidders to compete on an even playing field.

Should you have any questions, please call us immediately as time is of the essence.

6. On August 30, 1993, PEI informed NIH that Johnson was to be the mechanical subcontractor on the job. On September 1, 1993, PEI mailed and faxed a letter to Johnson formally accepting Johnson's bid. That letter read:

Pavel Enterprises, Inc.

September 1, 1993

Mr. James H. Kick, Estimating Mngr.

A.S. Johnson Company

8042 Old Alexandria Ferry Road

Clinton, Maryland 20735

Re: NIH Bldg 30 HVAC Modifications

RC: IFB # 263-93-B (CM)-0422

Subject: Letter of Intent to Award Subcontract

Dear Mr. Kick:

We herewith respectfully inform your office of our intent to award a subcontract for the above referenced project per your quote received on 8/05/93 in the amount of \$898,000.00. This subcontract will be forwarded upon receipt of our contract from the NIH, which we expect any day. A preconstruction meeting is currently scheduled at the NIH on 9/08/93 at 10 AM which we have been requested that your firm attend.

As discussed with you, a meeting was held between NIH and PEI wherein PEI confirmed our bid to the government, and designated your firm as our HVAC Mechanical subcontractor. This action was taken after several telephonic and face to face discussions with you regarding the above referenced bid submitted by your firm.

We look forward to working with your firm on this contract and hope that this will lead to a long and mutually beneficial relationship

Sincerely,
/s/ Thomas F. Pavel

President

7. Upon receipt of PEI's fax of September 1, James Kick called and informed PEI that Johnson's bid contained an error, and as a result the price was too low. According to Kick, Johnson had discovered the mistake earlier, but because Johnson believed that PEI had not been awarded the contract, they did not feel compelled to correct the error. Kick sought to withdraw Johnson's bid, both over the telephone and by a letter dated September 2, 1993:

A.S. Johnson Co.

September 2, 1993

PEI Construction
780 West Maples Avenue, Suite 101
Vienna, Virginia 22180

Attention: Thomas Pavel, President

Reference: NIH Building 30 HVAC Modifications

Dear Mr. Pavel,

We respectfully inform you of our intention to withdraw our proposal for the above referenced project due to an error in our bid.

As discussed in our telephone conversation and face to face meeting, the management of A.S. Johnson Company was reviewing this proposal, upon which we were to confirm our pricing to you.

Please contact Mr. Harry Kick, General Manager at [telephone number deleted] for any questions you may have.

Very truly yours,

/s/ James H. Kick

Estimating Manager

8. PEI responded to both the September 1 phone call, and the September 2 letter, expressing its refusal to permit Johnson to withdraw.
9. On September 28, 1993, NIH formally awarded the construction contract to PEI. PEI found a substitute subcontractor to do the mechanical work, but at a cost of \$930,000.⁶ PEI brought suit against Johnson in the Circuit Court for Prince George's County to recover the \$32,000 difference between Johnson's bid and the cost of the substitute mechanical subcontractor.
10. The case was heard by the trial court without the aid of a jury. The trial court made several findings of fact, which we summarize:

1. PEI relied upon Johnson's sub-bid in making its bid for the entire project;

⁶ The record indicates that the substitute mechanical subcontractor used "Powers" as a sub-subcontractor and did not "break out" the "Powers" component to be directly subcontracted by PEI.

2. The fact that PEI was not the low bidder, but was awarded the project only after the apparent low bidder was disqualified, takes this case out of the ordinary;

3. Prior to NIH awarding PEI the contract on September 28, Johnson, on September 2, withdrew its bid; and

4. PEI's letter to all potential mechanical subcontractors, dated August 26, 1993, indicates that there was no definite agreement between PEI and Johnson, *and* that PEI was not relying upon Johnson's bid.

11. The trial court analyzed the case under both a traditional contract theory and under a detrimental reliance theory. PEI was unable to satisfy the trial judge that under either theory a contractual relationship had been formed.
12. PEI appealed to the Court of Special Appeals, raising both traditional offer and acceptance theory, and "promissory estoppel." Before our intermediate appellate court considered the case, we issued a writ of certiorari on our own motion.

II

13. The relationships involved in construction contracts have long posed a unique problem in the law of contracts. A brief overview of the mechanics of the construction bid process, as well as our legal system's attempts to regulate the process, is in order.

A. CONSTRUCTION BIDDING.

14. Our description of the bid process in *Maryland Supreme Corp. v. Blake Co.*, 279 Md. 531, 369 A.2d 1017 (1977) is still accurate:

In such a building project there are basically three parties involved: the letting party, who calls for bids on its job; the general contractor, who makes a bid on the whole project; and the subcontractors, who bid only on that portion of the whole job which involves the field of its specialty. The usual procedure is that when a project is announced, a subcontractor, on his own initiative or at the general contractor's request, prepares an estimate and submits a bid to one or more of the general contractors interested in the project. The general contractor evaluates the bids made by the subcontractors in each field and uses them to compute its total bid to the letting party. After

receiving bids from general contractors, the letting party ordinarily awards the contract to the lowest reputable bidder.

Id. at 533-34, 369 A.2d at 1020-21 (citing [Franklin M. Schulz, *The Firm Offer Puzzle: A Study of Business Practice in the Construction Industry*, 19 U. CHI. L. REV. 237 (1952)])

B. THE CONSTRUCTION BIDDING CASES-AN HISTORICAL OVERVIEW

15. The problem the construction bidding process poses is the determination of the precise points on the timeline that the various parties become bound to each other. The early landmark case was *James Baird Co. v. Gimbel Bros., Inc.*, 64 F.2d 344 (2d Cir.1933). The plaintiff, James Baird Co., [“Baird”] was a general contractor from Washington, D.C., bidding to construct a government building in Harrisburg, Pennsylvania. Gimbel Bros., Inc., [“Gimbel”], the famous New York department store, sent its bid to supply linoleum to a number of bidding general contractors on December 24, and Baird received Gimbel's bid on December 28. Gimbel realized its bid was based on an incorrect computation and notified Baird of its withdrawal on December 28. The letting authority awarded Baird the job on December 30. Baird formally accepted the Gimbel bid on January 2. When Gimbel refused to perform, Baird sued for the additional cost of a substitute linoleum supplier. The Second Circuit Court of Appeals held that Gimbel's initial bid was an offer to contract and, under traditional contract law, remained open only until accepted or withdrawn. Because the offer was withdrawn before it was accepted there was no contract. Judge Learned Hand, speaking for the court, also [rejected two alternative theories of the case: unilateral contract and promissory estoppel. He held that Gimbel's bid was not an offer of a unilateral contract⁷ that Baird could accept by performing, *i.e.*, submitting the bid as part of the general bid; and second, he held that the theory of promissory estoppel was limited to cases involving charitable pledges.
16. Judge Hand's opinion was widely criticized, *see Note, Contracts-Promissory Estoppel*, 20 VA. L. REV. 214 (1933) [hereinafter, “*Promissory Estoppel*”]; *Note, Contracts-Revocation of Offer Before Acceptance-Promissory Estoppel*, 28 ILL. L. REV. 419 (1934), but also widely influential. The effect of the *James Baird* line of cases, however, is an “obvious injustice without relief of any description.”

⁷ A unilateral contract is a contract which is accepted, not by traditional acceptance, but by performance. 2 *Williston on Contracts* § 6:2 (4th ed.).

Promissory Estoppel, at 215. The general contractor is bound to the price submitted to the letting party, but the subcontractors are not bound, and are free to withdraw.⁸ As one commentator described it, “If the subcontractor revokes his bid before it is accepted by the general, any loss which results is a deduction from the general's profit and conceivably may transform overnight a profitable contract into a losing deal.” Franklin M. Schultz, *The Firm Offer Puzzle: A Study of Business Practice in the Construction Industry*, 19 U. Chi. L. Rev. 237, 239 (1952).

17. The unfairness of this regime to the general contractor was addressed in *Drennan v. Star Paving*, 333 P.2d 757, 51 Cal.2d 409 (1958). Like *James Baird*, the *Drennan* case arose in the context of a bid mistake.⁹ Justice Traynor, writing for the Supreme Court of California, relied upon § 90 of the *Restatement (First) of Contracts*:

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.

RESTATEMENT (FIRST) OF CONTRACTS § 90 (1932).¹⁰

18. Justice Traynor reasoned that the subcontractor's bid contained an implied subsidiary promise not to revoke the bid. As the court stated:

⁸ Note that under the *Baird* line of cases, the general contractor, while bound by his offer to the letting party, is not bound to any specific subcontractor, and is free to “bid shop” prior to awarding the subcontract. Michael L. Cloisen & Donald G. Weiland, *The Construction Industry Bidding Cases: Application of Traditional Contract, Promissory Estoppel, and Other Theories to the Relations Between General Contractors and Subcontractors*, 13 J. Marshall L.Rev. 565, 583 (1980). At least one commentator argues that although potentially unfair, this system creates a necessary symmetry between general and subcontractors, in that neither party is bound. Note, *Construction Contracts-The Problem of Offer and Acceptance in the General Contractor-Subcontractor Relationship*, 37 U.Cinn.L.Rev. 798 (1980) [hereinafter, “*The Problem of Offer and Acceptance*”].

⁹ Commentators have suggested that the very fact that many of these cases have arisen from bid mistake, an unusual subspecies, rather than from more typical cases, has distorted the legal system's understanding of these cases. Comment, *Bid Shopping and Peddling in the Subcontract Construction Industry*, 18 UCLA L.Rev. 389, 409 (1970) [hereinafter, “*Bid Shopping*”]. See also note, *Once Around the Flag Pole: Construction Bidding and Contracts at Formation*, 39 N.Y.U.L.Rev. 816, 818 (1964) [hereinafter, “*Flag Pole*”] (bid mistake cases generally portray general contractor as victim, but market reality is that subs are usually in weaker negotiating position).

¹⁰ This section of the Restatement has been supplanted by the Restatement (Second) of Contracts § 90(1) (1979). That provision will be discussed, *infra*.

When plaintiff [, a General Contractor,] used defendant's offer in computing his own bid, he bound himself to perform in reliance on defendant's terms. Though defendant did not bargain for the use of its bid neither did defendant make it idly, indifferent to whether it would be used or not. On the contrary it is reasonable to suppose that defendant submitted its bid to obtain the subcontract. It was bound to realize the substantial possibility that its bid would be the lowest, and that it would be included by plaintiff in his bid. It was to its own interest that the contractor be awarded the general contract; the lower the subcontract bid, the lower the general contractor's bid was likely to be and the greater its chance of acceptance and hence the greater defendant's chance of getting the paving subcontract. Defendant had reason not only to expect plaintiff to rely on its bid but to want him to. Clearly defendant had a stake in plaintiff's reliance on its bid. Given this interest and the fact that plaintiff is bound by his own bid, it is only fair that plaintiff should have at least an opportunity to accept defendant's bid after the general contract has been awarded to him.

Drennan, 51 Cal.2d at 415, 333 P.2d at 760.

19. The *Drennan* court however did not use “promissory estoppel” as a substitute for the entire contract, as is the doctrine's usual function. Instead, the *Drennan* court, applying the principle of § 90, interpreted the subcontractor's bid to be irrevocable. Justice Traynor's analysis used promissory estoppel as consideration for an implied promise to keep the bid open for a reasonable time. Recovery was then predicated on traditional bilateral contract, with the sub-bid as the offer and promissory estoppel serving to replace acceptance.
20. The *Drennan* decision has been very influential. Many states have adopted the reasoning used by Justice Traynor. See, e.g., *Debron Corp. v. National Homes Constr. Corp.*, 493 F.2d 352 (8th Cir.1974) (applying Missouri law); *Reynolds v. Texarkana Constr. Co.*, 237 Ark. 583, 374 S.W.2d 818 (1964); *Mead Assocs. Inc. v. Antonsen*, 677 P.2d 434 (Colo.1984); *Illinois Valley Asphalt v. J.F. Edwards Constr. Co.*, 45 Ill.Dec. 876, 413 N.E.2d 209, 90 Ill.App.3d 768 (Ill.Ct.App.1980); *Lichtefeld-Massaró, Inc. v. R.J. Manteuffel Co.*, 806 S.W.2d 42 (Ky.App.1991); *Constructors Supply Co. v. Bostrom Sheet Metal Works, Inc.*, 291 Minn. 113, 190 N.W.2d 71 (1971); *E.A. Coronis Assocs. v. M. Gordon Constr. Co.*, 90 N.J. Super 69, 216 A.2d 246 (1966).

21. Despite the popularity of the *Drennan* reasoning, the case has subsequently come under some criticism.¹¹ The criticism centers on the lack of symmetry of detrimental reliance in the bid process, in that subcontractors are bound to the general, but the general is not bound to the subcontractors.¹² The result is that the general is free to bid shop,¹³ bid chop,¹⁴ and to encourage bid peddling,¹⁵ to the detriment of the subcontractors. One commentator described the problems that these practices create:

Bid shopping and peddling have long been recognized as unethical by construction trade organizations. These ‘unethical,’ but common practices have several detrimental results. First, as bid shopping becomes common within a particular trade, the subcontractors will pad their initial bids in order to make further reductions during post-award negotiations. This artificial inflation of subcontractor's offers makes the bid process less effective. Second, subcontractors who are forced into post-award negotiations with the general often must reduce their sub-bids in order to avoid losing the award. Thus, they will be faced with a Hobson's choice between doing the job at a loss or doing a less than adequate job. Third, bid shopping and peddling tend to increase the risk of loss of the time and money used in preparing a bid. This occurs because generals and subcontractors who engage in these practices use, without expense, the bid estimates prepared by others. Fourth, it is often impossible for a general to obtain bids far enough in advance to have sufficient time to properly prepare his own bid because of the practice, common among many subcontractors, of holding sub-bids until the last

¹¹ *Home Elec. Co. v. Underdown Heating & Air Conditioning Co.*, 86 N.C.App. 540, 358 S.E.2d 539 (1987). See also, *The Problem of Offer and Acceptance*.

¹² See *Williams v. Favret*, 161 F.2d 822, 823 n. 1 (5th Cir.1947); *Merritt-Chapman & Scott Corp. v. Gunderson Bros. Eng'g Corp.*, 305 F.2d 659 (9th Cir.1962). But see *Electrical Constr. & Maintenance Co. v. Maeda Pac. Corp.*, 764 F.2d 619 (9th Cir.1985) (subcontractor rejected by general contractor could maintain an action in both traditional contract or promissory estoppel). See *Bid Shopping*, at 405-09 (suggesting using “promissory estoppel” to bind generals to subcontractors, as well as subs to generals, in appropriate circumstances).

¹³ Bid shopping is the use of the lowest subcontractor's bid as a tool in negotiating lower bids from other subcontractors post-award.

¹⁴ “The general contractor, having been awarded the prime contract, may pressure the subcontractor whose bid was used for a particular portion of the work in computing the overall bid on the prime contract to reduce the amount of the bid.” *Closen & Weiland*, at 566 n. 6.

¹⁵ An unscrupulous subcontractor can save estimating costs, and still get the job by not entering a bid or by entering an uncompetitive bid. After bid opening, this unscrupulous subcontractor, knowing the price of the low sub-bid, can then offer to perform the work for less money, precisely because the honest subcontractor has already paid for the estimate and included that cost in the original bid. This practice is called bid peddling.

possible moment in order to avoid pre-award bid shopping by the general. Fifth, many subcontractors refuse to submit bids for jobs on which they expect bid shopping. As a result, competition is reduced, and, consequently, construction prices are increased. Sixth, any price reductions gained through the use of post-award bid shopping by the general will be of no benefit to the awarding authority, to whom these price reductions would normally accrue as a result of open competition before the award of the prime contract. Free competition in an open market is therefore perverted because of the use of post-award bid shopping.

Bid Shopping, at 394-96 (citations omitted). *See also Flag Pole*, at 818 (bid mistake cases generally portray general contractor as victim, but market reality is that subs are usually in weaker negotiating position); Jay M. Feinman, *Promissory Estoppel and Judicial Method*, 97 HARV. L. REV. 678, 707-08 (1984). These problems have caused at least one court to reject promissory estoppel in the contractor-subcontractor relationship. *Home Elec. Co. v. Underdown Heating & Air Conditioning Co.*, 86 N.C.App. 540, 358 S.E.2d 539 (1987). *See also Note, Construction Contracts-The Problem of Offer and Acceptance in the General Contractor-Subcontractor Relationship*, 37 U. CINN. L. REV. 798 (1980). But other courts, while aware of the limitations of promissory estoppel, have adopted it nonetheless. *See, e.g., Alaska Bussell Elec. Co. v. Vern Hickel Constr. Co.*, 688 P.2d 576 (Alaska 1984).¹⁶

22. The doctrine of detrimental reliance has evolved in the time since *Drennan* was decided in 1958. The American Law Institute, responding to *Drennan*, sought to make detrimental reliance more readily applicable to the construction bidding scenario by adding § 87. This new section was intended to make subcontractors' bids binding:

§ 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

¹⁶ The critical literature also contains numerous suggestions that might be undertaken by the legislature to address the problems of bid shopping, chopping, and peddling. *See Note, Construction Bidding Problem: Is There a Solution Fair to Both the General Contractor and Subcontractor?*, 19 St. Louis L.Rev. 552, 568-72 (1975) (discussing bid depository and bid listing schemes); *Flag Pole*, at 825-26.

acceptance and which does induce such action or forbearance is binding as an option contract to the extent necessary to avoid injustice.”

RESTATEMENT (SECOND) OF CONTRACTS § 87 (1979).¹⁷

23. Despite the drafter's intention that § 87 of the *Restatement (Second) of Contracts* (1979) should replace *Restatement (First) of Contracts* § 90 (1932) in the construction bidding cases, few courts have availed themselves of the opportunity. *But see, Arango Constr. Co. v. Success Roofing, Inc.*, 46 Wash.App. 314, 321-22, 730 P.2d 720, 725 (1986). Section 90(1) of the *Restatement (Second) of Contracts* (1979) modified the first restatement formulation in three ways, by: 1) deleting the requirement that the action of the offeree be “definite and substantial;” 2) adding a cause of action for third party reliance; and 3) limiting remedies to those required by justice.¹⁸
24. Courts and commentators have also suggested other solutions intended to bind the parties without the use of detrimental reliance theory. The most prevalent suggestion¹⁹ is the use of the firm offer provision of the Uniform Commercial Code. Maryland Code (1992 Repl.Vol.), § 2-205 of the Commercial Law Article. That statute provides:

¹⁷ This provision was derived from *Restatement (Second) of Contracts* § 89B(2) (Tent.Drafts Nos. 1-7, 1973). There are cases that refer to the tentative drafts. *See Loranger Constr. Corp. v. E.F. Hauserman Co.*, 384 N.E.2d 176, 179, 376 Mass. 757, 763 (1978). *See also* Closen & Weiland, at 593-97.

¹⁸ Section 90 of the *Restatement (First) of Contracts* (1932) explains detrimental reliance as follows:

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.

Section 90(1) of the *Restatement (Second) Contracts* (1979) defines the doctrine of detrimental reliance as follows:

A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce such action or forbearance is binding if injustice can be avoided only by enforcement of the promise. The remedy granted for breach may be limited as justice requires.

¹⁹ *See Bid Shopping and Peddling* at 399-401; *Firm Offer Problem* at 215; Closen & Weiland, at 604 n. 133.

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.

25. In this manner, subcontractor's bids, made in writing and giving some assurance of an intent that the offer be held open, can be found to be irrevocable.
26. The Supreme Judicial Court of Massachusetts has suggested three other traditional theories that might prove the existence of a contractual relationship between a general contractor and a sub: conditional bilateral contract analysis; unilateral contract analysis; and unrevoked offer analysis. *Loranger Constr. Corp. v. E.F. Hauserman Co.*, 384 N.E.2d 176, 376 Mass. 757 (1978). If the general contractor could prove that there was an exchange of promises binding the parties to each other, and that exchange of promises was made before bid opening, that would constitute a valid bilateral promise conditional upon the general being awarded the job. *Loranger*, 384 N.E.2d at 180, 376 Mass. at 762. This directly contrasts with Judge Hand's analysis in *James Baird*, that a general's use of a sub-bid constitutes acceptance conditional upon the award of the contract to the general. *James Baird*, 64 F.2d at 345-46.
27. Alternatively, if the subcontractor intended its sub-bid as an offer to a unilateral contract, use of the sub-bid in the general's bid constitutes part performance, which renders the initial offer irrevocable under the *Restatement (Second) of Contracts* § 45 (1979). *Loranger*, 384 N.E.2d at 180, 376 Mass. at 762. This resurrects a second theory dismissed by Judge Learned Hand in *James Baird*.
28. Finally, the *Loranger* court pointed out that a jury might choose to disbelieve that a subcontractor had withdrawn the winning bid, meaning that acceptance came before withdrawal, and a traditional bilateral contract was formed. *Loranger*, 384 N.E.2d at 180, 376 Mass. at 762-63.²⁰
29. Another alternative solution to the construction bidding problem is no longer seriously considered—revitalizing the common law seal. William Noel Keyes, *Consideration Reconsidered—The Problem of the Withdrawn Bid*, 10 STAN. L. REV.

²⁰ For an excellent analysis of the *Loranger* case, see Closen & Weiland at 597-603.

441, 470 (1958). Because a sealed option contract remains firm without consideration this alternative was proposed as a solution to the construction bidding problem.²¹

III

30. If PEI is able to prove by any of the theories described that a contractual relationship existed, but Johnson failed to perform its end of the bargain, then PEI will recover the \$32,000 in damages caused by Johnson's breach of contract. Alternatively, if PEI is unable to prove the existence of a contractual relationship, then Johnson has no obligation to PEI. We will test the facts of the case against the theories described to determine if such a relationship existed.
31. The trial court held, and we agree, that Johnson's sub-bid was an offer to contract and that it was sufficiently clear and definite. We must then determine if PEI made a timely and valid acceptance of that offer and thus created a traditional bilateral contract, or in the absence of a valid acceptance, if PEI's detrimental reliance served to bind Johnson to its sub-bid. We examine each of these alternatives, beginning with traditional contract theory.²²

A. TRADITIONAL BILATERAL CONTRACT

32. The trial judge found that there was not a traditional contract binding Johnson to PEI. A review of the record and the trial judge's findings make it clear that this was a close

²¹ Of course, general contractors could require their subcontractors to provide their bids under seal. The fact that they do not is testament to the lack of appeal this proposal holds. It is here that the state of the law rests.

²² Because they were not raised, either below or in this Court, we need not address the several methods in which a court might interpret a subcontractor's bid as a firm, and thus irrevocable, offer. Nevertheless, for the benefit of bench and bar, we review those theories as applied to this case. First, PEI could have purchased an option, thus supplying consideration for making the offer irrevocable. This did not happen. Second, Johnson could have submitted its bid as a sealed offer. Md.Code (1995 Repl. Vol.), § 5-102 of the Courts & Judicial Proceedings Article. An offer under seal supplants the need for consideration to make an offer firm. This did not occur in the instant case. The third method of Johnson's offer becoming irrevocable is by operation of Md.Code (1992 Repl. Vol.), § 2-205 of the Commercial Law Article. We note that Johnson's sub-bid was made in the form of a signed writing, but without further evidence we are unable to determine if the offer "by its terms gives assurance that it will be held open" and if the sub-bid is for "goods" as that term is defined by Md.Code (1994 Repl. Vol.), § 2-105(1) of the Commercial Law Article and by decisions of this Court, including *Anthony Pools v. Sheehan*, 295 Md. 285, 455 A.2d 434 (1983) and *Burton v. Artery Co.*, 279 Md. 94, 367 A.2d 935 (1977).

question. On appeal however, our job is to assure that the trial judge's findings were not clearly erroneous. Maryland Rule 8-131(c). This is an easier task.

33. The trial judge rejected PEI's claim of bilateral contract for two separate reasons: 1) that there was no meeting of the minds; and 2) that the offer was withdrawn prior to acceptance. Both need not be proper bases for decision; if either of these two theories is not clearly erroneous, we must affirm.
34. There is substantial evidence in the record to support the judge's conclusion that there was no meeting of the minds. PEI's letter of August 26, to all potential mechanical subcontractors, reproduced *supra* [¶ 5], indicates, as the trial judge found, that PEI and Johnson “did not have a definite, certain meeting of the minds on a certain price for a certain quantity of goods...” Because this reason is itself sufficient to sustain the trial judge's finding that no contract was formed, we affirm.
35. Alternatively, we hold, that the evidence permitted the trial judge to find that Johnson revoked its offer prior to PEI's final acceptance. We review the relevant chronology. Johnson made its offer, in the form of a sub-bid, on August 5. On September 1, PEI accepted. Johnson withdrew its offer by letter dated September 2. On September 28, NIH awarded the contract to PEI. Thus, PEI's apparent acceptance came one day *prior* to Johnson's withdrawal.
36. The trial court found, however, “that before there was ever a final agreement reached with the contract awarding authorities, that Johnson made it clear to [PEI] that they were not going to continue to rely on their earlier submitted bid.” Implicit in this finding is the judge's understanding of the contract. Johnson's sub-bid constituted an offer of a contingent contract. PEI accepted that offer subject to the condition precedent of PEI's receipt of the award of the contract from NIH. Prior to the occurrence of the condition precedent, Johnson was free to withdraw. *See 2 Williston on Contracts* § 6:14 (4th ed.). On September 2, Johnson exercised that right to revoke.²³ The trial judge's finding that withdrawal proceeded valid final acceptance

²³ We have also considered the possibility that Johnson's offer was not to enter into a contingent contract. This is unlikely because there is no incentive for a general contractor to accept a non-contingent contract prior to contract award but it would bind the general to purchase the subcontractor's services even if the general did not receive the award. Moreover, PEI's September 1 letter clearly “accepted” Johnson's offer subject to the award from NIH. If Johnson's bid was for a non-contingent contract, PEI's response substantially varied the offer and was therefore a counter-offer, not an acceptance. *Post v. Gillespie*, 219 Md. 378, 385-86, 149 A.2d 391, 395-96 (1959); *2 Williston on Contracts* § 6:13 (4th ed.).

is therefore logical and supported by substantial evidence in the record. It was not clearly erroneous, so we shall affirm.

B. DETRIMENTAL RELIANCE

37. PEI's alternative theory of the case is that PEI's detrimental reliance binds Johnson to its bid. We are asked, as a threshold question, if detrimental reliance applies to the setting of construction bidding. Nothing in our previous cases suggests that the doctrine was intended to be limited to a specific factual setting. The benefits of binding subcontractors outweigh the possible detriments of the doctrine.²⁴
38. This Court has decided cases based on detrimental reliance as early as 1854,²⁵ and the general contours of the doctrine are well understood by Maryland courts. The historical development of promissory estoppel, or detrimental reliance, in Maryland has mirrored the development nationwide. It was originally a small exception to the general consideration requirement, and found in “cases dealing with such narrow problems as gratuitous agencies and bailments, waivers, and promises of marriage settlement.” Jay M. Feinman, *Promissory Estoppel and Judicial Method*, 97 HARV. L. REV. 678, 680 (1984). The early Maryland cases applying “promissory estoppel” or detrimental reliance primarily involve charitable pledges.
39. The leading case is *Maryland Nat'l Bank v. United Jewish Appeal Fed'n of Greater Washington*, 286 Md. 274, 407 A.2d 1130 (1979), where this Court's opinion was authored by the late Judge Charles E. Orth, Jr. In that case, a decedent, Milton Polinger, had pledged \$200,000 to the United Jewish Appeal [“UJA”]. The UJA sued Polinger's estate in an attempt to collect the money promised them. Judge Orth reviewed four prior decisions of this Court²⁶ and determined that RESTATEMENT (FIRST) OF CONTRACTS § 90 (1932) applied. *Id.* at 281, 407 A.2d at 1134. Because the Court found that the UJA had not acted in a “definite or substantial” manner in reliance on the contribution, no contract was found to have been created. *Id.* at 289-90, 407 A.2d at 1138-39.

²⁴ General contractors, however, should not assume that we will also adopt the holdings of our sister courts who have refused to find general contractors bound to their subcontractors. *See, e.g., N. Litterio & Co. v. Glassman Constr. Co.*, 319 F.2d 736 (D.C.Cir.1963).

²⁵ *Gittings v. Mayhew*, 6 Md. 113 (1854).

²⁶ The cases reviewed were *Gittings v. Mayhew*, 6 Md. 113 (1854); *Erdman v. Trustees Eutaw M.P. Ch.*, 129 Md. 595, 99 A. 793 (1917); *Sterling v. Cushwa & Sons*, 170 Md. 226, 183 A. 593 (1936); and *American University v. Collings*, 190 Md. 688, 59 A.2d 333 (1948).

40. Detrimental reliance doctrine has had a slow evolution from its origins in disputes over charitable pledges, and there remains some uncertainty about its exact dimensions.²⁷ Two cases from the Court of Special Appeals demonstrate that confusion.
41. The first, *Snyder v. Snyder*, 79 Md.App. 448, 558 A.2d 412 (1989), arose in the context of a suit to enforce an antenuptial agreement. To avoid the statute of frauds, refuge was sought in the doctrine of “promissory estoppel.”²⁸ The court held that “promissory estoppel” requires a finding of *fraudulent* conduct on the part of the promisor. See also *Friedman & Fuller v. Funkhouser*, 107 Md.App. 91, 666 A.2d 1298 (1995).
42. The second, *Kiley v. First Nat'l Bank*, 102 Md.App. 317, 649 A.2d 1145 (1994), the court stated that “[i]t is unclear whether Maryland continues to adhere to the more stringent formulation of promissory estoppel, as set forth in the original RESTATEMENT OF CONTRACTS, or now follows the more flexible view found in the RESTATEMENT (SECOND) CONTRACTS.” *Id.* at 336, 649 A.2d at 1154.

²⁷ Other cases merely acknowledged the existence of a doctrine of “promissory estoppel,” but did not comment on the standards for the application of this doctrine. See, e.g., *Chesapeake Supply & Equip. Co. v. Manitowoc Eng'g Corp.*, 232 Md. 555, 566, 194 A.2d 624, 630 (1963).

²⁸ Section 139 of the *Restatement (Second) of Contracts* (1979) provides that detrimental reliance can remove a case from the statute of frauds:

Enforcement by Virtue of Action in Reliance

(1) A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a third person and which does induce the action or forbearance is enforceable notwithstanding the Statute of Frauds if injustice can be avoided only by enforcement of the promise. The remedy granted for breach is to be limited as justice requires.

(2) In determining whether injustice can be avoided only by enforcement of the promise, the following circumstances are significant:

- (a) the availability and adequacy of other remedies, particularly cancellation and restitution;
- (b) the definite and substantial character of the action or forbearance in relation to the remedy sought;
- (c) the extent to which the action or forbearance corroborates evidence of the making and terms of the promise, or the making and terms are otherwise established by clear and convincing evidence;
- (d) the reasonableness of the action or forbearance;
- (e) the extent to which the action or forbearance was foreseeable by the promisor.

43. To resolve these confusions we now clarify that Maryland courts are to apply the test of the RESTATEMENT (SECOND) OF CONTRACTS § 90(1) (1979), which we have recast as a four-part test:
1. a clear and definite promise;
 2. where the promisor has a reasonable expectation that the offer will induce action or forbearance on the part of the promisee;
 3. which does induce actual and reasonable action or forbearance by the promisee; and
 4. causes a detriment which can only be avoided by the enforcement of the promise.²⁹
44. We have adopted language of the RESTATEMENT (SECOND) OF CONTRACTS (1979) because we believe each of the three changes made to the previous formulation were for the better. As discussed earlier, the first change was to delete the requirement that the action of the offeree be “definite and substantial.” Although the Court of Special Appeals in *Kiley v. First Nat'l Bank*, 102 Md.App. 317, 336, 649 A.2d 1145, 1154 (1994) apparently presumed this to be a major change from the “stringent” first restatement to the “more flexible” second restatement, we perceive the language to have always been redundant. If the reliance is not “substantial and definite” justice will not compel enforcement.
45. The decisions in *Snyder v. Snyder*, 79 Md.App. 448, 558 A.2d 412 (1989) and *Friedman & Fuller v. Funkhouser*, 107 Md.App. 91, 666 A.2d 1298 (1995) to the extent that they required a showing of fraud on the part of the offeree are therefore disapproved.
46. In a construction bidding case, where the general contractor seeks to bind the subcontractor to the sub-bid offered, the general must first prove that the subcontractor's sub-bid constituted an offer to perform a job at a given price. We do not express a judgment about how precise a bid must be to constitute an offer, or to what degree a general contractor may request to change the offered scope before an

²⁹ This comports with the formulation given by the United States District Court for the District of Maryland in *Union Trust Co. of Md. v. Charter Medical Corp.*, 663 F.Supp. 175, 178 n. 4 (D.Md.1986) *aff'd w/o opinion*, 823 F.2d 548 (4th Cir.1987).

acceptance becomes a counter-offer. That fact-specific judgment is best reached on a case-by-case basis. In the instant case, the trial judge found that the sub-bid was sufficiently clear and definite to constitute an offer, and his finding was not clearly erroneous.

47. Second, the general must prove that the subcontractor reasonably expected that the general contractor would rely upon the offer. The subcontractor's expectation that the general contractor will rely upon the sub-bid may dissipate through time.³⁰
48. In this case, the trial court correctly inquired into Johnson's belief that the bid remained open, and that consequently PEI was not relying on the Johnson bid. The judge found that due to the time lapse between bid opening and award, "it would be unreasonable for offers to continue." This is supported by the substantial evidence. James Kick testified that although he knew of his bid mistake, he did not bother to notify PEI because J.J. Kirlin, Inc., and not PEI, was the apparent low bidder. The trial court's finding that Johnson's reasonable expectation had dissipated in the span of a month is not clearly erroneous.
49. As to the third element, a general contractor must prove that he actually and reasonably relied on the subcontractor's sub-bid. We decline to provide a checklist of potential methods of proving this reliance, but we will make several observations. First, a showing by the subcontractor, that the general contractor engaged in "bid shopping," or actively encouraged "bid chopping," or "bid peddling" is strong evidence that the general did *not* rely on the sub-bid. Second, prompt notice by the general contractor to the subcontractor that the general intends to use the sub on the job, is weighty evidence that the general *did* rely on the bid.³¹ Third, if a sub-bid is so low that a reasonably prudent general contractor would not rely upon it, the trier of fact may infer that the general contractor did not in fact rely upon the erroneous bid.
50. In this case, the trial judge did not make a specific finding that PEI failed to prove its reasonable reliance upon Johnson's sub-bid. We must assume, however, that it was his conclusion based on his statement that "the parties did not have a definite, certain meeting of the minds on a certain price for a certain quantity of goods and wanted to

³⁰ We expect that evidence of "course of dealing" and "usage of the trade," *see Restatement (Second) of Contracts* §§ 219-223 (1979), will provide strong indicies of the reasonableness of a subcontractor's expectations.

³¹ Prompt notice and acceptance also significantly dispels the possibility of bid shopping, bid chopping, and bid peddling.

renegotiate....” The August 26, 1993, fax from PEI to all prospective mechanical subcontractors, is evidence supporting this conclusion. Although the finding that PEI did not rely on Johnson's bid was indisputably a close call, it was not clearly erroneous.

51. Finally, as to the fourth prima facie element, the trial court, and not a jury, must determine that binding the subcontractor is necessary to prevent injustice. This element is to be enforced as required by common law equity courts—the general contractor must have “clean hands.” This requirement includes, as did the previous element, that the general did not engage in bid shopping, chopping or peddling, but also requires the further determination that justice compels the result. The fourth factor was not specifically mentioned by the trial judge, but we may infer that he did not find this case to merit an equitable remedy.
52. Because there was sufficient evidence in the record to support the trial judge's conclusion that PEI had not proven its case for detrimental reliance, we must, and hereby do, affirm the trial court's ruling.

IV

53. In conclusion, we emphasize that there are different ways to prove that a contractual relationship exists between a general contractor and its subcontractors. Traditional bilateral contract theory is one. Detrimental reliance can be another. However, under the evidence in this case, the trial judge was not clearly erroneous in deciding that recovery by the general contractor was not justified under either theory.

JUDGMENT AFFIRMED, WITH COSTS.

Dataserv Equipment v. Technology Finance Leasing Corp.

Court of Appeals of Minnesota
364 N.W.2d 838 (1985)

WOZNIAK, Judge.

1. This is an appeal from a judgment entered after trial to the district court determining that appellant was subject to the jurisdiction of Minnesota courts and that appellant breached a contract to purchase certain computer equipment. We ... reverse on the question of contract formation.

FACTS

2. Appellant Technology Finance Group, Inc. (Technology), a Nevada corporation with its principal place of business in Connecticut, and Respondent Dataserv Equipment, Inc. (Dataserv), a Minnesota corporation with its principal place of business in Minneapolis, are dealers in new and used computer equipment.
3. On or about August 29, 1979, Dataserv's Jack Skjonsby telephoned Technology's Ron Finerty in Connecticut and proposed to sell to Technology, for the price of \$100,000, certain IBM computer "features" which Dataserv had previously purchased in Canada.
4. As a result of long distance telephone conversations between Skjonsby and Finerty, on August 30, 1979, Finerty sent Skjonsby a written offer to purchase the features and on September 6, 1979, Dataserv sent to Technology a proposed form of contract. Dataserv's proposed contract form included a nonstandard provision, appearing in the contract form as clause 8 and referred to by the parties as the "Indepth Clause." The clause provided that installation of the features would be done by Indepth, a third party. The contract also provided that "[t]his agreement is subject to acceptance by the seller ... and shall only become effective on the date thereof," and "[t]his agreement is made subject to the terms and conditions included herein and Purchaser's acceptance is effective only to the extent that such terms and conditions are conditions herein. Any acceptance which contains conditions which are in addition to or inconsistent with the terms and conditions herein will be a counter offer and will not be binding unless agreed to in writing by the Seller."

5. On October 1, Finerty wrote Skjonsby that three changes “need to be made” in the contract, one of which was the deletion of clause 8. The letter closed with: “Let me know and I will make the changes and sign.” Two of the changes were thereafter resolved, but the resolution of clause 8 remained in controversy.
6. Later in October 1979, Dataserv offered to accept, in substitution for Indepth, any other third-party installation company Technology would designate. Technology never agreed to this.
7. On November 8, 1979, Dataserv by telephone offered to remove the Indepth clause from the contract form. Technology responded that it was “too late,” and that there was no deal.
8. On November 9, 1979, Finerty called Dataserv, and informed them that “the deal was not going to get done because they'd waited until too late a point in time.” During this period of time, the market value of the features was dropping rapidly and Dataserv was anxious to complete the deal. It is undisputed that the market for used computer equipment, including its features, is downwardly price volatile.
9. By telex dated November 12, 1979, Dataserv informed Technology that the features were ready for pickup and that the pickup and payment be no later than November 15, 1979.
10. On November 13, 1979, Finerty responded by telex stating:

[S]ince [Dataserv] had not responded in a positive fashion to Alanthus' [Alanthus is the former name of Technology Finance Group] letter requesting contract changes...its offer to purchase [the features] was withdrawn on 11/9/79 via telephone conversation with Jack Skjonsby. Ten to fifteen days prior, I made Jack aware that this deal was dead if Dataserv did not agree to contract changes prior to the “Eleventh Hour.”
11. On June 19, 1980, the features were sold by Dataserv to another party for \$26,000. It then sought a judgment against Technology for the difference between the sale price of the features and the contract price.
12. By its Answer and by way of pretrial motion, Technology claimed that the court lacked jurisdiction over the person of the defendant. The trial court denied the motion on February 20, 1981.

13. At trial the parties stipulated that as of November 8, 1979 Dataserv telephonically offered to take out the Indepth Clause. The trial court found that this telephone call operated as an acceptance of Technology's counteroffer of October 1, 1979, thereby establishing a contract between the parties embodying the terms of Dataserv's printed standard contract dated September 6, 1979, minus clause 8 thereof. The trial court found that as of November 15, 1979, Technology breached its contract to Dataserv's damage, and awarded Dataserv \$74,000 in damages, plus interest from the date of the breach.

ANALYSIS

14. Technology claims that the trial court erred in finding that the parties entered into a contract. It contends that Dataserv's response to its counteroffer operated, as a matter of law, as a rejection, terminating Dataserv's power to subsequently accept the counteroffer.
15. Under familiar principles of contract law, a party's rejection terminates its power of acceptance. Restatement (Second) of Contracts § 38 (1981). Once rejected, an offer is terminated and cannot subsequently be accepted without ratification by the other party. *Nodland v. Chirpich*, 240 N.W.2d 513, 307 Minn. 360 (1976).
16. The critical issue is whether Dataserv rejected Technology's October 1 counteroffer. Dataserv responded to Technology's October 1 counteroffer by agreeing to delete two of the three objectionable clauses, but insisting that the third be included. By refusing to accept according to the terms of the proposal, Dataserv rejected Technology's counteroffer and thus no contract was formed. Moreover, Dataserv's offer to substitute other third party installation companies, which Technology rejected, operated as a termination of its power to accept Technology's counteroffer. Dataserv's so-called "acceptance," when it offered to delete clause 8 on November 8, 1979, was without any legal effect whatsoever, except to create a new offer which Technology immediately rejected.
17. Dataserv's November 8 "acceptance" was also ineffective because it was not signed in accordance with the offer's conditions. While it is true that Minn.Stat. §336.2-204 does not require a signed agreement prior to formation of a contract, where the parties know that the execution of a written contract was a condition

precedent to their being bound, there can be no binding contract until the written agreement was executed. *Staley Manufacturing Co. v. Northern Cooperatives, Inc.*, 168 F.2d 892 (8th Cir.1948).

18. Having found that no contract was formed between the parties, it is unnecessary to address the question of mitigation of damages.

DECISION

19. Technology was subject to the jurisdiction of Minnesota courts. No contract was formed between the parties.

Affirmed in part, reversed in part.

Ionics, Inc. v. Elmwood Sensors, Inc.

United States Court of Appeals for the First Circuit
110 F.3d 184 (1997)

TORRUELLA, Chief Judge.

1. Ionics, Inc. (“Ionics”) purchased thermostats from Elmwood Sensors, Inc. (“Elmwood”) for installation in water dispensers manufactured by the former. Several of the dispensers subsequently caused fires which allegedly resulted from defects in the sensors. Ionics filed suit against Elmwood in order to recover costs incurred in the wake of the fires. Before trial, the district court denied Elmwood's motion for partial summary judgment. The District Court of Massachusetts subsequently certified to this court “the question whether, in the circumstances of this case, § 2-207 of M.G.L. c. 106 has been properly applied.”

I. Standard of Review

2. We review the grant or denial of summary judgment *de novo*. See *Borschow Hosp. & Medical Supplies v. Cesar Castillo, Inc.*, 96 F.3d 10, 14 (1st Cir.1996).

II. Background

3. The facts of the case are not in dispute. Elmwood manufactures and sells thermostats. Ionics makes hot and cold water dispensers, which it leases to its customers. On three separate occasions, Ionics purchased thermostats from Elmwood for use in its water dispensers.¹ Every time Ionics made a purchase of thermostats from Elmwood, it sent the latter a purchase order form which contained, in small type, various “conditions.” Of the 20 conditions on the order form, two are of particular relevance:

18. REMEDIES - The remedies provided Buyer herein shall be cumulative, and in addition to any other remedies provided by law or equity. A waiver of a breach of any provision hereof shall not constitute a waiver of any other breach. The laws of the state shown in Buyer's address printed on the masthead of this order shall apply in the construction hereof.

19. ACCEPTANCE - Acceptance by the Seller of this order shall be upon the terms and conditions set forth in items 1 to 17 inclusive, and elsewhere in this order. Said order can be so accepted only on the exact terms herein

¹ Orders were placed in March, June, and September 1990.

and set forth. No terms which are in any manner additional to or different from those herein set forth shall become a part of, alter or in any way control the terms and conditions herein set forth.

4. Near the time when Ionics placed its first order, it sent Elmwood a letter that it sends to all of its new suppliers. The letter states, in part:

The information preprinted, written and/or typed on our purchase order is especially important to us. Should you take exception to this information, please clearly express any reservations to us in writing. If you do not, we will assume that you have agreed to the specified terms and that you will fulfill your obligations according to our purchase order. If necessary, we will change your invoice and pay your invoice according to our purchase order.

5. Following receipt of each order, Elmwood prepared and sent an “Acknowledgment” form containing the following language in small type:

THIS WILL ACKNOWLEDGE RECEIPT OF BUYER'S ORDER AND STATE SELLER'S WILLINGNESS TO SELL THE GOODS ORDERED BUT ONLY UPON THE TERMS AND CONDITIONS SET FORTH HEREIN AND ON THE REVERSE SIDE HEREOF AS A COUNTEROFFER. BUYER SHALL BE DEEMED TO HAVE ACCEPTED SUCH COUNTEROFFER UNLESS IT IS REJECTED IN WRITING WITHIN TEN (10) DAYS OF THE RECEIPT HEREOF, AND ALL SUBSEQUENT ACTION SHALL BE PURSUANT TO THE TERMS AND CONDITIONS OF THIS COUNTEROFFER ONLY; ANY ADDITIONAL OR DIFFERENT TERMS ARE HEREBY OBJECTED TO AND SHALL NOT BE BINDING UPON THE PARTIES UNLESS SPECIFICALLY AGREED TO IN WRITING BY SELLER.

6. Although this passage refers to a “counteroffer,” we wish to emphasize that this language is not controlling. The form on which the language appears is labeled an “Acknowledgment” and the language comes under a heading that reads “Notice of Receipt of Order.” The form, taken as a whole, appears to contemplate an order's confirmation rather than an order's rejection in the form of a counteroffer.
7. It is undisputed that the Acknowledgment was received prior to the arrival of the shipment of goods. Although the district court, in its ruling on the summary judgment motion, states that “with each shipment of thermostats, Elmwood included an

Acknowledgment Form,” this statement cannot reasonably be taken as a finding in support of the claim that the Acknowledgment and the shipment arrived together. First, in its certification order, the court states that “[t]he purchaser, *after* receiving the Acknowledgment, accepted delivery of the goods without objection.” This language is clearer and more precise than the previous statement and suggests that the former was simply a poor choice of phrasing. Furthermore, Ionics has not disputed the arrival time of the Acknowledgment. In its Memorandum in Support of Defendant's Motion for Partial Summary Judgment Elmwood stated, under the heading of “Statements of Undisputed Facts,” that “for each of the three orders, Ionics received the Acknowledgment prior to receiving the shipment of thermostats.” In its own memorandum, Ionics argued that there existed disputed issues of material fact, but did not contradict Elmwood's claim regarding the arrival of the Acknowledgment Form. Furthermore, in its appellate brief, Ionics does not argue that the time of arrival of the Acknowledgment Form is in dispute. Ionics repeats language from the district court's summary judgment ruling that “with each shipment of thermostats, Elmwood included an Acknowledgment Form,” but does not argue that the issue is in dispute or confront the language in Elmwood's brief which states that “[i]t is undisputed that for each of the three orders, Ionics received the Acknowledgment prior to receiving the shipment of thermostats.”

8. As we have noted, the Acknowledgment Form expressed Elmwood's willingness to sell thermostats on “terms and conditions” that the Form indicated were listed on the reverse side. Among the terms and conditions listed on the back was the following:

WARRANTY. All goods manufactured by Elmwood Sensors, Inc. are guaranteed to be free of defects in material and workmanship for a period of ninety (90) days after receipt of such goods by Buyer or eighteen months from the date of manufacturer [sic] (as evidenced by the manufacturer's date code), whichever shall be longer. THERE IS NO IMPLIED WARRANTY OF MERCHANTABILITY AND NO OTHER WARRANTY, EXPRESSED OR IMPLIED, EXCEPT SUCH AS IS EXPRESSLY SET FORTH HEREIN. SELLER WILL NOT BE LIABLE FOR ANY GENERAL, CONSEQUENTIAL OR INCIDENTAL DAMAGES, INCLUDING WITHOUT LIMITATION ANY DAMAGES FROM LOSS OF PROFITS, FROM ANY BREACH OF WARRANTY OR FOR NEGLIGENCE, SELLER'S LIABILITY AND BUYER'S EXCLUSIVE REMEDY BEING EXPRESSLY LIMITED TO THE REPAIR OF DEFECTIVE GOODS F.O.B. THE SHIPPING POINT INDICATED ON

THE FACE HEREOF OR THE REPAYMENT OF THE PURCHASE PRICE UPON THE RETURN OF THE GOODS OR THE GRANTING OF A REASONABLE ALLOWANCE ON ACCOUNT OF ANY DEFECTS, AS SELLER MAY ELECT.

9. Neither party disputes that they entered into a valid contract and neither disputes the quantity of thermostats purchased, the price paid, or the manner and time of delivery. The only issue in dispute is the extent of Elmwood's liability.
10. In summary, Ionics' order included language stating that the contract would be governed exclusively by the terms included on the purchase order and that all remedies available under state law would be available to Ionics. In a subsequent letter, Ionics added that Elmwood must indicate any objections to these conditions in writing. Elmwood, in turn, sent Ionics an Acknowledgment stating that the contract was governed exclusively by the terms in the Acknowledgment, and Ionics was given ten days to reject this "counteroffer." Among the terms included in the Acknowledgment is a limitation on Elmwood's liability. As the district court stated, "the terms are diametrically opposed to each other on the issue of whether all warranties implied by law were reserved or waived."
11. We face, therefore, a battle of the forms. This is purely a question of law. The dispute turns on whether the contract is governed by the language after the comma in § 2-207(1) of the Uniform Commercial Code, according to the rule laid down by this court in *Roto-Lith, Ltd. v. F.P. Bartlett & Co.*, 297 F.2d 497 (1st Cir.1962), or whether it is governed by subsection (3) of the Code provision, as enacted by both Massachusetts, Mass. Gen. L. ch. 106, § 2-207 (1990 and 1996 Supp.), and Rhode Island, R.I. Gen. Laws § 6A-2-207 (1992).² We find the rule of *Roto-Lith* to be in conflict with the purposes of section 2-207 and, accordingly, we overrule *Roto-Lith* and find that subsection (3) governs the contract.³ Analyzing the case under section

² There is some uncertainty on the question of whether Massachusetts or Rhode Island law governs. We need not address this issue, however, because the two states have adopted versions of section 2-207 of the Uniform Commercial Code that are virtually equivalent.

³ Although panel decisions of this court are ordinarily binding on newly constituted panels, that rule does not obtain in instances where, as here, a departure is compelled by controlling authority (such as the interpreted statute itself). In such relatively rare instances, we have sometimes chosen to circulate the proposed overruling opinion to all active members of the court prior to publication even though the need to overrule precedent is reasonably clear. *See, e.g., Wright v. Park*, 5 F.3d 586, 591 n. 7 (1st Cir.1993); *Trailer Marine Transport Corp. v. Rivera Vazquez*, 977 F.2d 1, 9 n. 5 (1st Cir.1992). This procedure is, of course, informal, and does not preclude a suggestion of rehearing en banc on any

2-207, we conclude that Ionics defeats Elmwood's motion for partial summary judgment.

III. Legal Analysis

12. Our analysis begins with the statute. Section 2-207 reads as follows:

§ 2-207. Additional Terms in Acceptance or Confirmation

(1) A definite and seasonable expression of acceptance or a written confirmation which is sent within a reasonable time operates as an acceptance even though it states terms additional to or different from those offered or agreed upon, unless acceptance is expressly made conditional on assent to the additional or different terms.

(2) The additional or different terms are to be construed as proposals for addition to the contract. Between merchants such terms become part of the contract unless:

(a) the offer expressly limits acceptance to the terms of the offer;

(b) they materially alter it; or

(c) notification of objection to them has already been given or is given within a reasonable time after notice of them is received.

(3) Conduct by both parties which recognizes the existence of a contract is sufficient to establish a contract for sale although the writings of the parties do not otherwise establish a contract. In such case the terms of the particular contract consist of those terms on which the writings of the parties agree, together with any supplementary terms incorporated under any other provisions of this chapter.

Mass. Gen. L. ch. 106, § 2-207 (1990 and 1996 Supp.).

13. In *Roto-Lith*, Roto-Lith sent a purchase order to Bartlett, who responded with an acknowledgment that included language purporting to limit Bartlett's liability. Roto-

issue. We have followed that praxis here and can report that none of the active judges of this court has objected to the panel's analysis or to its conclusion that *Roto-Lith* has outlived its usefulness as circuit precedent.

Lith did not object. *Roto-Lith*, 297 F.2d at 498-99. This court held that “a response which states a condition materially altering the obligation solely to the disadvantage of the offeror is an ‘acceptance...expressly...conditional on assent to the additional...terms.’ ” *Id.* at 500. This holding took the case outside of section 2-207 by applying the exception after the comma in subsection (1). The court then reverted to common law and concluded that Roto-Lith “accepted the goods with knowledge of the conditions specified in the acknowledgment [and thereby] became bound.” *Id.* at 500. In other words, the *Roto-Lith* court concluded that the defendant's acceptance was conditional on assent, by the buyer, to the new terms and, therefore, constituted a counter offer rather than an acceptance. When Roto-Lith accepted the goods with knowledge of Bartlett's conditions, it accepted the counteroffer and Bartlett's terms governed the contract. Elmwood argues that *Roto-Lith* governs the instant appeal, implying that the terms of Elmwood's acknowledgment govern.

14. Ionics claims that the instant case is distinguishable because in *Roto-Lith* “the seller's language limiting warranties implied at law was proposed as an addition to, but was not in conflict with, the explicit terms of the buyer's form. [In the instant case] the explicit terms of the parties' forms conflict with and reject each other.” Appellee's Brief at 21.
15. We do not believe that Ionics' position sufficiently distinguishes *Roto-Lith*. It would be artificial to enforce language that conflicts with background legal rules while refusing to enforce language that conflicts with the express terms of the contract. Every contract is assumed to incorporate the existing legal norms that are in place. It is not required that every contract explicitly spell out the governing law of the jurisdiction. Allowing later forms to govern with respect to deviations from the background rules but not deviations from the terms in the contract would imply that only the terms in the contract could be relied upon. Aside from being an artificial and arbitrary distinction, such a standard would, no doubt, lead parties to include more of the background rules in their initial forms, making forms longer and more complicated. Longer forms would be more difficult and time consuming to read- implying that even fewer forms would be read than under the existing rules. It is the failure of firms to read their forms that has brought this case before us, and we do not wish to engender more of this type of litigation.
16. Our inquiry, however, is not complete. Having found that we cannot distinguish this case from *Roto-Lith*, we turn to the Uniform Commercial Code, quoted above. A

plain language reading of section 2-207 suggests that subsection (3) governs the instant case. Ionics sent an initial offer to which Elmwood responded with its “Acknowledgment.” Thereafter, the conduct of the parties established the existence of a contract as required by section 2-207(3).

17. Furthermore, the case before us is squarely addressed in comment 6, which states:

6. If no answer is received within a reasonable time after additional terms are proposed, it is both fair and commercially sound to assume that their inclusion has been assented to. Where clauses on confirming forms sent by both parties conflict, each party must be assumed to object to a clause of the other conflicting with one on the confirmation sent by himself. As a result, the requirement that there be notice of objection which is found in subsection (2) [of § 2-207] is satisfied and the conflicting terms do not become part of the contract. The contract then consists of the terms originally expressly agreed to, terms on which the confirmations agree, and terms supplied by this Act.

Mass. Gen. L. ch. 106, § 2-207, Uniform Commercial Code Comment 6. This Comment addresses precisely the facts of the instant case. Any attempt at distinguishing the case before us from section 2-207 strikes us as disingenuous.

18. We are faced, therefore, with a contradiction between a clear precedent of this court, *Roto-Lith*, which suggests that the language after the comma in subsection (1) governs, and the clear dictates of the Uniform Commercial Code, which indicate that subsection (3) governs. It is our view that the two cannot coexist and the case at bar offers a graphic illustration of the conflict. We have, therefore, no choice but to overrule our previous decision in *Roto-Lith, Ltd. v. F.P. Bartlett & Co.*, 297 F.2d 497 (1st Cir.1962). Our decision brings this circuit in line with the majority view on the subject and puts to rest a case that has provoked considerable criticism from courts and commentators and alike.⁴

⁴ See, e.g., *Step-Saver Data Systems, Inc. v. Wyse Technology*, 939 F.2d 91, 101 (3d Cir.1991); *St. Charles Cable TV, Inc. v. Eagle Comtronics, Inc.*, 687 F.Supp. 820, 828 & n. 19 (S.D.N.Y.1988); *Daitom v. Pennwalt Corp.*, 741 F.2d 1569, 1576-77 (10th Cir.1984); *Luria Bros. v. Piolet Bros. Scrap Iron & Metal*, 600 F.2d 103, 113 (7th Cir.1979); *Dorton v. Collins & Aikman Corp.*, 453 F.2d 1161, 1168 & n. 5 (6th Cir.1972); ; JAMES J. WHITE & ROBERT S. SUMMERS, 1 UNIFORM COMMERCIAL CODE, § 1-3, at 12, 16-17 (1995); Murray, *Intention over Terms: An Exploration of UCC 2-207 & New Section 60, Restatement of Contracts*, 37 FORDHAM L. REV. 317, 329 (1969).

19. We hold, consistent with section 2-207 and Official Comment 6, that where the terms in two forms are contradictory, each party is assumed to object to the other party's conflicting clause. As a result, mere acceptance of the goods by the buyer is insufficient to infer consent to the seller's terms under the language of subsection (1).⁵ Nor do such terms become part of the contract under subsection (2) because notification of objection has been given by the conflicting forms. *See* § 2-207(2)(c).
20. The alternative result, advocated by Elmwood and consistent with *Roto-Lith*, would undermine the role of section 2-207. Elmwood suggests that “a seller's expressly conditional acknowledgment constitutes a counteroffer where it materially alters the terms proposed by the buyer, and the seller's terms govern the contract between the parties when the buyer accepts and pays for the goods.” Appellant's Brief at 12. Under this view, section 2-207 would no longer apply to cases in which forms have been exchanged and subsequent disputes reveal that the forms are contradictory. That is, the last form would always govern.
21. The purpose of section 2-207, as stated in *Roto-Lith*, “was to modify the strict principle that a response not precisely in accordance with the offer was a rejection and a counteroffer.” *Roto-Lith*, 297 F.2d at 500; *see also Dorton v. Collins & Aikman Corp.*, 453 F.2d 1161, 1165-66 (6th Cir.1972) (stating that section 2-207 “was intended to alter the ‘ribbon-matching’ or ‘mirror’ rule of common law, under which the terms of an acceptance or confirmation were required to be identical to the terms of the offer”). Under the holding advocated by Elmwood, virtually any response that added to or altered the terms of the offer would be a rejection and a counteroffer. We do not think that such a result is consistent with the intent of section 2-207 and we believe it to be expressly contradicted by Comment 6.
22. Applied to this case, our holding leads to the conclusion that the contract is governed by section 2-207(3). Section 2-207(1) is inapplicable because Elmwood's acknowledgment is conditional on assent to the additional terms. The additional terms do not become a part of the contract under section 2-207(2) because notification of objection to conflicting terms was given on the order form and because the new terms materially alter those in the offer. Finally, the conduct of the parties demonstrates the existence of a contract, as required by section 2-207(3). Thus, section 2-207(3)

⁵ *See also* Official Comment 3 (“If [additional or different terms] are such as materially to alter the original bargain, they will not be included unless expressly agreed to by the other party.”).

applies and the terms of the contract are to be determined in accordance with that subsection.

23. We conclude, therefore, that section 2-207(3) prevails and “the terms of the particular contract consist of those terms on which the writings of the parties agree, together with any supplementary terms incorporated under any other provisions of this chapter.” Mass. Gen. L. ch. 106, § 2-207(3).
24. The reality of modern commercial dealings, as this case demonstrates, is that not all participants read their forms. *See James J. White & Robert S. Summers, Uniform Commercial Code* § 1-3 at 6-7 (4th ed.1995). To uphold Elmwood's view would not only fly in the face of Official Comment 6 to section 2-207 of the Uniform Commercial Code, and the overall purpose of that section, it would also fly in the face of good sense. The sender of the last form (in the instant case, the seller) could insert virtually any conditions it chooses into the contract, including conditions contrary to those in the initial form. The final form, therefore, would give its sender the power to re-write the contract. Under our holding today, we at least ensure that a party will not be held to terms that are directly contrary to the terms it has included in its own form. Rather than assuming that a failure to object to the offeree's conflicting terms indicates offeror's assent to those terms, we shall make the more reasonable inference that each party continues to object to the other's contradictory terms. We think it too much to grant the second form the power to contradict and override the terms in the first form.

IV. Conclusion

25. For the reasons stated herein, the district court's order denying Elmwood's motion for partial summary judgment is *affirmed* and the case is *remanded* to the district court for further proceedings.

Step-Saver Data Systems v. Wyse Technology

United States Court of Appeals, Third Circuit
939 F.2d 91 (1991)

WISDOM, Circuit Judge

1. The “Limited Use License Agreement” printed on a package containing a copy of a computer program raises the central issue in this appeal. The trial judge held that the terms of the Limited Use License Agreement governed the purchase of the package, and, therefore, granted the software producer, The Software Link, Inc. (“TSL”), a directed verdict on claims of breach of warranty brought by a disgruntled purchaser, Step-Saver Data Systems, Inc. We disagree with the district court's determination of the legal effect of the license, and reverse and remand the warranty claims for further consideration.
2. Step-Saver raises several other issues, but we do not find these issues warrant reversal. We, therefore, affirm in all other respects.

I. FACTUAL AND PROCEDURAL BACKGROUND

3. The growth in the variety of computer hardware and software has created a strong market for these products. It has also created a difficult choice for consumers, as they must somehow decide which of the many available products will best suit their needs. To assist consumers in this decision process, some companies will evaluate the needs of particular groups of potential computer users, compare those needs with the available technology, and develop a package of hardware and software to satisfy those needs. Beginning in 1981, Step-Saver performed this function as a value added retailer for International Business Machine (IBM) products. It would combine hardware and software to satisfy the word processing, data management, and communications needs for offices of physicians and lawyers. It originally marketed single computer systems, based primarily on the IBM personal computer.
4. As a result of advances in micro-computer technology, Step-Saver developed and marketed a multi-user system. With a multi-user system, only one computer is

required. Terminals are attached, by cable, to the main computer. From these terminals, a user can access the programs available on the main computer.¹

5. After evaluating the available technology, Step-Saver selected a program by TSL, entitled Multilink Advanced, as the operating system for the multi-user system. Step-Saver selected WY-60 terminals manufactured by Wyse, and used an IBM AT as the main computer. For applications software, Step-Saver included in the package several off-the-shelf programs, designed to run under Microsoft's Disk Operating System ("MS-DOS"),² as well as several programs written by Step-Saver. Step-Saver began marketing the system in November of 1986, and sold one hundred forty-two systems mostly to law and medical offices before terminating sales of the system in March of 1987. Almost immediately upon installation of the system, Step-Saver began to receive complaints from some of its customers.³
6. Step-Saver, in addition to conducting its own investigation of the problems, referred these complaints to Wyse and TSL, and requested technical assistance in resolving the problems. After several preliminary attempts to address the problems, the three companies were unable to reach a satisfactory solution, and disputes developed among the three concerning responsibility for the problems. As a result, the problems were never solved. At least twelve of Step-Saver's customers filed suit against Step-Saver because of the problems with the multi-user system.
7. Once it became apparent that the three companies would not be able to resolve their dispute amicably, Step-Saver filed suit for declaratory judgment, seeking indemnity from either Wyse or TSL, or both, for any costs incurred by Step-Saver in defending and resolving the customers' law suits. The district court dismissed this complaint, finding that the issue was not ripe for judicial resolution. We affirmed the dismissal

¹ In essence, the terminals are simply video screens with keyboards that serve as input-output devices for the main computer. The main computer receives data from all of the terminals and processes it appropriately, sending a return signal to the terminal. To someone working on one of the terminals of a properly operating multi-user system, the terminal appears to function as if it were, in fact, a computer. Thus, an operator could work with a word processing program on a terminal, and it would appear to the operator the same as would working with the word processing program on a computer. The difference is that, with a set of computers, the commands of each user are processed within each user's computer, whereas with a multi-user system, the commands of all of the users are sent to the main computer for processing.

² MS-DOS was the standard operating system for IBM and compatible personal computers.

³ According to the testimony of Jeffrey Worthington, an employee of Step-Saver, twenty to twenty-five of the purchasers of the multi-user system had serious problems with the system that were never resolved.

on appeal.⁴ Step-Saver then filed a second complaint alleging breach of warranties by both TSL and Wyse and intentional misrepresentations by TSL.⁵ The district court's actions during the resolution of this second complaint provide the foundation for this appeal.

8. On the first day of trial, the district court specifically agreed with the basic contention of TSL that the form language printed on each package containing the Multilink Advanced program (“the box-top license”) was the complete and exclusive agreement between Step-Saver and TSL under § 2-202 of the Uniform Commercial Code (UCC).⁶ Based on § 2-316 of the UCC, the district court held that the box-top license disclaimed all express and implied warranties otherwise made by TSL. The court therefore granted TSL's motion in limine to exclude all evidence of the earlier oral and written express warranties allegedly made by TSL. After Step-Saver presented its case, the district court granted a directed verdict in favor of TSL on the intentional misrepresentation claim, holding the evidence insufficient as a matter of law to establish two of the five elements of a prima facie case: (1) fraudulent intent on the part of TSL in making the representations; and (2) reasonable reliance by Step-Saver. The trial judge requested briefing on several issues related to Step-Saver's remaining express warranty claim against TSL. While TSL and Step-Saver prepared briefs on these issues, the trial court permitted Wyse to proceed with its defense. On the third day of Wyse's defense, the trial judge, after considering the additional briefing by Step-Saver and TSL, directed a verdict in favor of TSL on Step-Saver's remaining warranty claims, and dismissed TSL from the case.
9. The trial proceeded on Step-Saver's breach of warranties claims against Wyse. At the conclusion of Wyse's evidence, the district judge denied Step-Saver's request for rebuttal testimony on the issue of the ordinary uses of the WY-60 terminal. The district court instructed the jury on the issues of express warranty and implied

⁴ See *Step-Saver Data Sys., Inc. v. Wyse Tech.*, 912 F.2d 643 (3d Cir.1990).

⁵ Step-Saver also advanced claims under negligent misrepresentation and breach of contract theories. Step-Saver does not appeal these claims.

⁶ All three parties agree that the terminals and the program are “goods” within the meaning of UCC §§ 2-102 & 2-105. Cf. *Advent Sys. Ltd. v. Unisys Corp.*, 925 F.2d 670, 674-76 (3d Cir.1991). TSL and Step-Saver have disputed whether Pennsylvania or Georgia law governs the issues of contract formation and modification with regard to the Multilink programs. Because both Pennsylvania and Georgia have adopted, without modification, the relevant portions of Article 2 of the Uniform Commercial Code, see Ga. Code Ann. §§ 11-2-101 to 11-2-725 (1990); 13 Pa. Cons. Stat. Ann. §§ 2101-2725 (Purdon 1984), we will simply cite to the relevant UCC provision.

warranty of fitness for a particular purpose. Over Step-Saver's objection, the district court found insufficient evidence to support a finding that Wyse had breached its implied warranty of merchantability, and refused to instruct the jury on such warranty. The jury returned a verdict in favor of Wyse on the two warranty issues submitted.

10. Step-Saver appeals on four points. (1) Step-Saver and TSL did not intend the box-top license to be a complete and final expression of the terms of their agreement. (2) There was sufficient evidence to support each element of Step-Saver's contention that TSL was guilty of intentional misrepresentation. (3) There was sufficient evidence to submit Step-Saver's implied warranty of merchantability claim against Wyse to the jury. (4) The trial court abused its discretion by excluding from the evidence a letter addressed to Step-Saver from Wyse, and by refusing to permit Step-Saver to introduce rebuttal testimony on the ordinary uses of the WY-60 terminal.

II. THE EFFECT OF THE BOX-TOP LICENSE

11. The relationship between Step-Saver and TSL began in the fall of 1984 when Step-Saver asked TSL for information on an early version of the Multilink program. TSL provided Step-Saver with a copy of the early program, known simply as Multilink, without charge to permit Step-Saver to test the program to see what it could accomplish. Step-Saver performed some tests with the early program, but did not market a system based on it.
12. In the summer of 1985, Step-Saver noticed some advertisements in Byte magazine for a more powerful version of the Multilink program, known as Multilink Advanced. Step-Saver requested information from TSL concerning this new version of the program, and allegedly was assured by sales representatives that the new version was compatible with ninety percent of the programs available "off-the-shelf" for computers using MS-DOS. The sales representatives allegedly made a number of additional specific representations of fact concerning the capabilities of the Multilink Advanced program.
13. Based on these representations, Step-Saver obtained several copies of the Multilink Advanced program in the spring of 1986, and conducted tests with the program. After these tests, Step-Saver decided to market a multi-user system which used the Multilink Advanced program. From August of 1986 through March of 1987, Step-Saver purchased and resold 142 copies of the Multilink Advanced program. Step-

Saver would typically purchase copies of the program in the following manner. First, Step-Saver would telephone TSL and place an order. (Step-Saver would typically order twenty copies of the program at a time.) TSL would accept the order and promise, while on the telephone, to ship the goods promptly. After the telephone order, Step-Saver would send a purchase order, detailing the items to be purchased, their price, and shipping and payment terms. TSL would ship the order promptly, along with an invoice. The invoice would contain terms essentially identical with those on Step-Saver's purchase order: price, quantity, and shipping and payment terms. No reference was made during the telephone calls, or on either the purchase orders or the invoices with regard to a disclaimer of any warranties.

14. Printed on the package of each copy of the program, however, would be a copy of the box-top license. The box-top license contains five terms relevant to this action:

(1) The box-top license provides that the customer has not purchased the software itself, but has merely obtained a personal, non-transferable license to use the program.⁷

⁷ When these form licenses were first developed for software, it was, in large part, to avoid the federal copyright law first sale doctrine. Under the first sale doctrine, once the copyright holder has sold a copy of the copyrighted work, the owner of the copy could “sell or otherwise dispose of the possession of that copy” without the copyright holder's consent. *See Bobbs-Merrill Co. v. Straus*, 210 U.S. 339, 350, 28 S.Ct. 722, 726, 52 L.Ed. 1086 (1908); 17 U.S.C.A. § 109(a) (West 1977). Under this doctrine, one could purchase a copy of a computer program, and then lease it or lend it to another without infringing the copyright on the program. Because of the ease of copying software, software producers were justifiably concerned that companies would spring up that would purchase copies of various programs and then lease those to consumers. Typically, the companies, like a videotape rental store, would purchase a number of copies of each program, and then make them available for over-night rental to consumers. Consumers, instead of purchasing their own copy of the program, would simply rent a copy of the program, and duplicate it. This copying by the individual consumers would presumably infringe the copyright, but usually it would be far too expensive for the copyright holder to identify and sue each individual copier. Thus, software producers wanted to sue the companies that were renting the copies of the program to individual consumers, rather than the individual consumers. The first sale doctrine, though, stood as a substantial barrier to successful suit against these software rental companies, even under a theory of contributory infringement. By characterizing the original transaction between the software producer and the software rental company as a license, rather than a sale, and by making the license personal and non-transferable, software producers hoped to avoid the reach of the first sale doctrine and to establish a basis in state contract law for suing the software rental companies directly. Questions remained, however, as to whether the use of state contract law to avoid the first sale doctrine would be preempted either by the federal copyright statute (statutory preemption) or by the exclusive constitutional grant of authority over copyright issues to the federal government (constitutional preemption). *See generally Bonito Boats, Inc. v. Thunder Craft Boats, Inc.*, 489 U.S. 141, 109 S.Ct. 971, 103 L.Ed.2d 118 (1989); *Kewanee Oil Co. v. Bicron Corp.*, 416 U.S. 470, 94 S.Ct.

(2) The box-top license, in detail and at some length, disclaims all express and implied warranties except for a warranty that the disks contained in the box are free from defects.

(3) The box-top license provides that the sole remedy available to a purchaser of the program is to return a defective disk for replacement; the license excludes any liability for damages, direct or consequential, caused by the use of the program.

(4) The box-top license contains an integration clause, which provides that the box-top license is the final and complete expression of the terms of the parties' agreement.

(5) The box-top license states: "Opening this package indicates your acceptance of these terms and conditions. If you do not agree with them, you should promptly return the package unopened to the person from whom you purchased it within fifteen days from date of purchase and your money will be refunded to you by that person."

15. The district court, without much discussion, held, as a matter of law, that the box-top license was the final and complete expression of the terms of the parties's agreement. Because the district court decided the questions of contract formation and

1879, 40 L.Ed.2d 315 (1974); *Compco Corp. v. Day-Brite Lighting, Inc.*, 376 U.S. 234, 84 S.Ct. 779, 11 L.Ed.2d 669 (1964); *Sears, Roebuck & Co. v. Stiffel Co.*, 376 U.S. 225, 84 S.Ct. 784, 11 L.Ed.2d 661 (1964). Congress recognized the problem, and, in 1990, amended the first sale doctrine as it applies to computer programs and phonorecords. *See* Computer Software Rental Amendments Act of 1990, Pub.L. No. 101-650, 104 Stat. 5134 (codified at 17 U.S.C.A. § 109(b) (West Supp.1991)). As amended, the first sale doctrine permits only non-profit libraries and educational institutions to lend or lease copies of software and phonorecords. *See* 17 U.S.C.A. § 109(b)(1)(A) (West Supp.1991). (Under the amended statute, a purchaser of a copy of a copyrighted computer program may still sell his copy to another without the consent of the copyright holder.) This amendment renders the need to characterize the original transaction as a license largely anachronistic. While these transactions took place in 1986-87, before the Computer Software Rental Amendments were enacted, there was no need to characterize the transactions between Step-Saver and TSL as a license to avoid the first sale doctrine because both Step-Saver and TSL agree that Step-Saver had the right to resell the copies of the Multilink Advanced program.

interpretation as issues of law, we review the district court's resolution of these questions *de novo*.⁸

16. Step-Saver contends that the contract for each copy of the program was formed when TSL agreed, on the telephone, to ship the copy at the agreed price.⁹ The box-top license, argues Step-Saver, was a material alteration to the parties' contract which did not become a part of the contract under UCC § 2-207.¹⁰ Alternatively, Step-Saver argues that the undisputed evidence establishes that the parties did not intend the box-top license as a final and complete expression of the terms of their agreement, and, therefore, the parol evidence rule of UCC § 2-202 would not apply.¹¹

⁸ See *Diamond Fruit Growers, Inc. v. Krack Corp.*, 794 F.2d 1440, 1442 (9th Cir.1986).

⁹ See UCC § 2-206(1)(b) and comment 2. Note that under UCC § 2-201, the oral contract would not be enforceable in the absence of a writing or part performance because each order typically involved more than \$500 in goods. However, courts have typically treated the questions of formation and interpretation as separate from the question of when the contract becomes enforceable. See, e.g., *C. Itoh & Co. v. Jordan Int'l Co.*, 552 F.2d 1228, 1232-33 (7th Cir.1977); *Southeastern Adhesives Co. v. Funder America*, 89 N.C.App. 438, 366 S.E.2d 505, 507-08 (N.C.Ct.App.1988); *United Coal & Commodities Co. v. Hawley Fuel Coal, Inc.*, 363 Pa.Super. 106, 525 A.2d 741, 743 (Pa.Super.Ct.), *app. denied*, 517 Pa. 609, 536 A.2d 1333 (1987).

¹⁰ Section 2-207 provides:

Additional Terms in Acceptance or Confirmation.

(1) A definite and seasonable expression of acceptance or a written confirmation which is sent within a reasonable time operates as an acceptance even though it states terms additional to or different from those offered or agreed upon, unless acceptance is expressly made conditional on assent to the additional or different terms.

(2) The additional terms are to be construed as proposals for addition to the contract. Between merchants such terms become part of the contract unless:

- (a) the offer expressly limits acceptance to the terms of the offer;
- (b) they materially alter it; or
- (c) notification of objection to them has already been given or is given within a reasonable time after notice of them is received.

(3) Conduct by both parties which recognizes the existence of a contract is sufficient to establish a contract for sale although the writings of the parties do not otherwise establish a contract. In such case the terms of the particular contract consist of those terms on which the writings of the parties agree, together with any supplementary terms incorporated under any other provisions of the Act.

¹¹ Two other issues were raised by Step-Saver. First, Step-Saver argued that the box-top disclaimer is either unconscionable or not in good faith. Second, Step-Saver argued that the warranty disclaimer was inconsistent with the express warranties made by TSL in the product specifications. Step-Saver argues that interpreting the form language of the license agreement to override the specific warranties contained in the product specification is unreasonable, citing *Consolidated Data Terminals v. Applied*

17. TSL argues that the contract between TSL and Step-Saver did not come into existence until Step-Saver received the program, saw the terms of the license, and opened the program packaging. TSL contends that too many material terms were omitted from the telephone discussion for that discussion to establish a contract for the software. Second, TSL contends that its acceptance of Step-Saver's telephone offer was conditioned on Step-Saver's acceptance of the terms of the box-top license. Therefore, TSL argues, it did not accept Step-Saver's telephone offer, but made a counteroffer represented by the terms of the box-top license, which was accepted when Step-Saver opened each package. Third, TSL argues that, however the contract was formed, Step-Saver was aware of the warranty disclaimer, and that Step-Saver, by continuing to order and accept the product with knowledge of the disclaimer, assented to the disclaimer.
18. In analyzing these competing arguments, we first consider whether the license should be treated as an integrated writing under UCC § 2-202, as a proposed modification under UCC § 2-209, or as a written confirmation under UCC § 2-207. Finding that UCC § 2-207 best governs our resolution of the effect of the box-top license, we then consider whether, under UCC § 2-207, the terms of the box-top license were incorporated into the parties's agreement.

A. Does UCC § 2-207 Govern the Analysis?

19. As a basic principle, we agree with Step-Saver that UCC § 2-207 governs our analysis. We see no need to parse the parties's various actions to decide exactly when the parties formed a contract. TSL has shipped the product, and Step-Saver has accepted and paid for each copy of the program. The parties's performance demonstrates the existence of a contract. The dispute is, therefore, not over the existence of a contract, but the nature of its terms.¹² When the parties' conduct establishes a contract, but the parties have failed to adopt expressly a particular writing as the terms of their agreement, and the writings exchanged by the parties do not agree, UCC § 2-207 determines the terms of the contract.

As stated by the official comment to § 2-207:

Digital Data Sys., 708 F.2d 385 (9th Cir.1983). *See also Northern States Power Co. v. ITT Meyer Indus.*, 777 F.2d 405 (8th Cir.1985). Because of our holding that the terms of the box-top license were not incorporated into the contract, we do not address these issues.

¹² *See McJunkin Corp. v. Mechanicals, Inc.*, 888 F.2d 481, 488 (6th Cir.1989).

1. This section is intended to deal with two typical situations. The one is the written confirmation, where an agreement has been reached either orally or by informal correspondence between the parties and is followed by one or more of the parties sending formal memoranda embodying the terms so far as agreed upon and adding terms not discussed....

2. Under this Article a proposed deal which in commercial understanding has in fact been closed is recognized as a contract. Therefore, any additional matter contained in the confirmation or in the acceptance falls within subsection (2) and must be regarded as a proposal for an added term unless the acceptance is made conditional on the acceptance of the additional or different terms.

20. Although UCC § 2-202 permits the parties to reduce an oral agreement to writing, and UCC § 2-209 permits the parties to modify an existing contract without additional consideration, a writing will be a final expression of, or a binding modification to, an earlier agreement only if the parties so intend.¹³ It is undisputed that Step-Saver never expressly agreed to the terms of the box-top license, either as a final expression of, or a modification to, the parties's agreement. In fact, Barry Greebel, the President of Step-Saver, testified without dispute that he objected to the terms of the box-top license as applied to Step-Saver. In the absence of evidence demonstrating an express intent to adopt a writing as a final expression of, or a modification to, an earlier agreement, we find UCC § 2-207 to provide the appropriate legal rules for determining whether such an intent can be inferred from continuing with the contract after receiving a writing containing additional or different terms.¹⁴
21. To understand why the terms of the license should be considered under § 2-207 in this case, we review briefly the reasons behind § 2-207. Under the common law of sales, and to some extent still for contracts outside the UCC,¹⁵ an acceptance that varied any term of the offer operated as a rejection of the offer, and simultaneously made a counteroffer.¹⁶ This common law formality was known as the mirror image

¹³ See, e.g., *Sierra Diesel Injection Serv., Inc. v. Burroughs Corp.*, 890 F.2d 108, 112-13 (9th Cir.1989) (UCC § 2-202). By its terms, UCC § 2-209 extends only to “[a]n agreement to modify”.

¹⁴ See *Mead Corp. v. McNally-Pittsburgh Mfg. Corp.*, 654 F.2d 1197, 1206 (6th Cir.1981).

¹⁵ See, e.g., *Learning Works, Inc. v. Learning Annex, Inc.*, 830 F.2d 541, 543 (4th Cir.1987).

¹⁶ See, e.g., *Diamond Fruit Growers, Inc.*, 794 F.2d at 1443; J. White & R. Summers, *Handbook of the Law Under the Uniform Commercial Code*, § 1-2 at 34 (2d ed. 1980).

rule, because the terms of the acceptance had to mirror the terms of the offer to be effective.¹⁷ If the offeror proceeded with the contract despite the differing terms of the supposed acceptance, he would, by his performance, constructively accept the terms of the “counteroffer”, and be bound by its terms. As a result of these rules, the terms of the party who sent the last form, typically the seller, would become the terms of the parties's contract. This result was known as the “last shot rule”.

22. The UCC, in § 2-207, rejected this approach. Instead, it recognized that, while a party may desire the terms detailed in its form if a dispute, in fact, arises, most parties do not expect a dispute to arise when they first enter into a contract. As a result, most parties will proceed with the transaction even if they know that the terms of their form would not be enforced.¹⁸ The insight behind the rejection of the last shot rule is that it would be unfair to bind the buyer of goods to the standard terms of the seller, when neither party cared sufficiently to establish expressly the terms of their agreement, simply because the seller sent the last form. Thus, UCC § 2-207 establishes a legal rule that proceeding with a contract after receiving a writing that purports to define the terms of the parties's contract is not sufficient to establish the party's consent to the terms of the writing to the extent that the terms of the writing either add to, or differ from, the terms detailed in the parties's earlier writings or discussions.¹⁹ In the absence of a party's express assent to the additional or different terms of the writing, section 2-207 provides a default rule that the parties intended, as

¹⁷ See, e.g., *Daitom, Inc. v. Pennwalt Corp.*, 741 F.2d 1569, 1578 (10th Cir.1984).

¹⁸ As Judge Engel has written:

Usually, these standard terms mean little, for a contract looks to its fulfillment and rarely anticipates its breach. Hope springs eternal in the commercial world and expectations are usually, but not always, realized.

McJunkin Corp. v. Mechanicals, Inc., 888 F.2d at 482.

¹⁹ As the *Mead* Court explained:

Absent the [UCC], questions of contract formation and intent remain factual issues to be resolved by the trier of fact after careful review of the evidence. However, the [UCC] provides rules of law, and section 2-207 establishes important legal principles to be employed to resolve complex contract disputes arising from the exchange of business forms. Section 2-207 was intended to provide some degree of certainty in this otherwise ambiguous area of contract law. In our view, it is unreasonable and contrary to the policy behind the [UCC] merely to turn the issue over to the uninformed speculation of the jury left to apply its own particular sense of equity.

Mead Corp., 654 F.2d at 1206 (citations omitted).

the terms of their agreement, those terms to which both parties have agreed,²⁰ along with any terms implied by the provisions of the UCC.

23. The reasons that led to the rejection of the last shot rule, and the adoption of section 2-207, apply fully in this case. TSL never mentioned during the parties' negotiations leading to the purchase of the programs, nor did it, at any time, obtain Step-Saver's express assent to, the terms of the box-top license. Instead, TSL contented itself with attaching the terms to the packaging of the software, even though those terms differed substantially from those previously discussed by the parties. Thus, the box-top license, in this case, is best seen as one more form in a battle of forms, and the question of whether Step-Saver has agreed to be bound by the terms of the box-top license is best resolved by applying the legal principles detailed in section 2-207.

B. Application of § 2-207

24. TSL advances several reasons why the terms of the box-top license should be incorporated into the parties' agreement under a § 2-207 analysis. First, TSL argues that the parties' contract was not formed until Step-Saver received the package, saw the terms of the box-top license, and opened the package, thereby consenting to the terms of the license. TSL argues that a contract defined without reference to the specific terms provided by the box-top license would necessarily fail for indefiniteness. Second, TSL argues that the box-top license was a conditional acceptance and counter-offer under § 2-207(1). Third, TSL argues that Step-Saver, by continuing to order and use the product with notice of the terms of the box-top license, consented to the terms of the box-top license.

1. Was the contract sufficiently definite?

25. TSL argues that the parties intended to license the copies of the program, and that several critical terms could only be determined by referring to the box-top license. Pressing the point, TSL argues that it is impossible to tell, without referring to the box-top license, whether the parties intended a sale of a copy of the program or a license to use a copy. TSL cites *Bethlehem Steel Corp. v. Litton Industries* in support

²⁰ The parties may demonstrate their acceptance of a particular term either “orally or by informal correspondence”, UCC 2-207, comment 1, or by placing the term in their respective form.

of its position that any contract defined without reference to the terms of the box-top license would fail for indefiniteness.²¹

26. From the evidence, it appears that the following terms, at the least, were discussed and agreed to, apart from the box-top license: (1) the specific goods involved; (2) the quantity; and (3) the price. TSL argues that the following terms were only defined in the box-top license: (1) the nature of the transaction, sale or license; and (2) the warranties, if any, available. TSL argues that these two terms are essential to creating a sufficiently definite contract. We disagree.

Section 2-204(3) of the UCC provides:

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

27. Unlike the terms omitted by the parties in *Bethlehem Steel Corp.*, the two terms cited by TSL are not “gaping holes in a multi-million dollar contract that no one but the parties themselves could fill.”²² First, the rights of the respective parties under the federal copyright law if the transaction is characterized as a sale of a copy of the program are nearly identical to the parties's respective rights under the terms of the box-top license.²³ Second, the UCC provides for express and implied warranties if the seller fails to disclaim expressly those warranties.²⁴ Thus, even though warranties are an important term left blank by the parties, the default rules of the UCC fill in that blank.

²¹ 488 A.2d 581 (Pa. 1985).

²² 488 A.2d at 591.

²³ The most significant difference would be that, under the terms of the license, Step-Saver could not transfer the copies without TSL's consent, while Step-Saver could do so under the federal copyright law if it had purchased the copy. Even if we assume that federal law would not preempt state law enforcement of this aspect of the license, this difference is not material to this case in that both parties agree that Step-Saver had the right to transfer the copies to purchasers of the Step-Saver multi-user system.

²⁴ See UCC §§ 2-312, 2-313, 2-314, & 2-315.

28. We hold that contract was sufficiently definite without the terms provided by the box-top license.²⁵

2. The box-top license as a counter-offer?

29. TSL advances two reasons why its box-top license should be considered a conditional acceptance under UCC § 2-207(1). First, TSL argues that the express language of the box-top license, including the integration clause and the phrase “opening this product indicates your acceptance of these terms”, made TSL's acceptance “expressly conditional on assent to the additional or different terms”.²⁶ Second, TSL argues that the box-top license, by permitting return of the product within fifteen days if the purchaser²⁷ does not agree to the terms stated in the license (the “refund offer”), establishes that TSL's acceptance was conditioned on Step-Saver's assent to the terms of the box-top license, citing *Monsanto Agricultural Products Co. v. Edenfield*.²⁸ While we are not certain that a conditional acceptance analysis applies when a contract is established by performance,²⁹ we assume that it does and consider TSL's arguments.

30. Under this Article a proposed deal which in commercial understanding has in fact been closed is recognized as a contract. Therefore, any additional matter contained in the confirmation or in the acceptance falls within subsection (2) and must be regarded as a proposal for an added term *unless the acceptance is made conditional on the acceptance of the additional or different terms*.

31. To determine whether a writing constitutes a conditional acceptance, courts have established three tests. Because neither Georgia nor Pennsylvania has expressly

²⁵ See, e.g., *City University of New York v. Finalco, Inc.*, 514 N.Y.S.2d 244, 129 A.D.2d 494 (N.Y.App.Div.1987); *URSA Farmers Coop. Co. v. Trent*, 58 Ill.App.3d 930, 16 Ill.Dec. 348, 374 N.E.2d 1123 (Ill. App. Ct. 1978).

²⁶ UCC § 2-207(1).

²⁷ In the remainder of the opinion, we will refer to the transaction as a sale for the sake of simplicity, but, by doing so, do not mean to resolve the sale-license question.

²⁸ 426 So.2d 574 (Fla. Dist. Ct. App.1982).

²⁹ Even though a writing sent after performance establishes the existence of a contract, courts have analyzed the effect of such a writing under UCC § 2-207. See *Herzog Oil Field Serv. v. Otto Torpedo Co.*, 391 Pa. Super. 133, 570 A.2d 549, 550 (Pa. Super. Ct. 1990); *McJunkin Corp. v. Mechanicals, Inc.*, 888 F.2d at 487. The official comment to UCC 2-207 suggests that, even though a proposed deal has been closed, the conditional acceptance analysis still applies in determining which writing's terms will define the contract.

adopted a test to determine when a written confirmation constitutes a conditional acceptance, we consider these three tests to determine which test the state courts would most likely apply.³⁰

32. Under the first test, an offeree's response is a conditional acceptance to the extent it states a term “materially altering the contractual obligations solely to the disadvantage of the offeror”.³¹ Pennsylvania, at least, has implicitly rejected this test. In *Herzog Oil Field Service, Inc.*,³² a Pennsylvania Superior Court analyzed a term in a written confirmation under UCC § 2-207(2), rather than as a conditional acceptance even though the term materially altered the terms of the agreement to the sole disadvantage of the offeror.³³
33. Furthermore, we note that adopting this test would conflict with the express provision of UCC § 2-207(2)(b). Under § 2-207(2)(b), additional terms in a written confirmation that “materially alter [the contract]” are construed “as proposals for addition to the contract”, not as conditional acceptances.
34. A second approach considers an acceptance conditional when certain key words or phrases are used, such as a written confirmation stating that the terms of the confirmation are “the only ones upon which we will accept orders”.³⁴ The third approach requires the offeree to demonstrate an unwillingness to proceed with the transaction unless the additional or different terms are included in the contract.³⁵

³⁰ See *Daitom, Inc.*, 741 F.2d at 1574-75.

³¹ *Daitom, Inc.*, 741 F.2d at 1576. See, e.g., *Roto-Lith Ltd. v. F.P. Bartlett & Co.*, 297 F.2d 497 (1st Cir.1962).

³² 570 A.2d 549 (Pa.Super.Ct.1990).

³³ The seller/offeree sent a written confirmation that contained a term that provided for attorney's fees of 25 percent of the balance due if the account was turned over for collection. 570 A.2d at 550

³⁴ *Ralph Shrader, Inc. v. Diamond Int'l Corp.*, 833 F.2d 1210, 1214 (6th Cir.1987); see *McJunkin Corp.*, 888 F.2d at 488. Note that even though an acceptance contains the key phrase, and is conditional, these courts typically avoid finding a contract on the terms of the counteroffer by requiring the offeree/counterofferor to establish that the offeror assented to the terms of the counteroffer. Generally, acceptance of the goods, alone, is not sufficient to establish assent by the offeror to the terms of the counteroffer. See, e.g., *Ralph Shrader, Inc.*, 833 F.2d at 1215; *Diamond Fruit Growers, Inc.*, 794 F.2d at 1443-44; *Coastal Indus. v. Automatic Steam Prods. Corp.*, 654 F.2d 375, 379 (5th Cir. Unit B Aug.1981). If the sole evidence of assent to the terms of the counteroffer is from the conduct of the parties in proceeding with the transaction, then the courts generally define the terms of the parties's agreement under § 2-207(3). See, e.g., *Diamond Fruit Growers, Inc.*, 794 F.2d at 1444.

³⁵ See, e.g., *Daitom, Inc.*, 741 F.2d at 1576; *Idaho Power Co. v. Westinghouse Elec. Corp.*, 596 F.2d 924, 926 (9th Cir.1979).

35. Although we are not certain that these last two approaches would generate differing answers,³⁶ we adopt the third approach for our analysis because it best reflects the understanding of commercial transactions developed in the UCC. Section 2-207 attempts to distinguish between: (1) those standard terms in a form confirmation, which the party would like a court to incorporate into the contract in the event of a dispute; and (2) the actual terms the parties understand to govern their agreement. The third test properly places the burden on the party asking a court to enforce its form to demonstrate that a particular term is a part of the parties' commercial bargain.³⁷
36. Using this test, it is apparent that the integration clause and the “consent by opening” language is not sufficient to render TSL's acceptance conditional. As other courts have recognized,³⁸ this type of language provides no real indication that the party is willing to forego the transaction if the additional language is not included in the contract.
37. The second provision provides a more substantial indication that TSL was willing to forego the contract if the terms of the box-top license were not accepted by Step-Saver. On its face, the box-top license states that TSL will refund the purchase price if the purchaser does not agree to the terms of the license.³⁹ Even with such a refund term, however, the offeree/counterofferor may be relying on the purchaser's investment in time and energy in reaching this point in the transaction to prevent the purchaser from returning the item. Because a purchaser has made a decision to buy a particular product and has actually obtained the product, the purchaser may use it despite the refund offer, regardless of the additional terms specified after the contract

³⁶ Under the second approach, the box-top license might be considered a conditional acceptance, but Step-Saver, by accepting the product, would not be automatically bound to the terms of the box-top license. See *Diamond Fruit Growers, Inc.*, 794 F.2d at 1444. Instead, courts have applied UCC § 2-207(3) to determine the terms of the parties' agreement. The terms of the agreement would be those “on which the writings of the parties agree, together with any supplementary terms incorporated under any other provisions of this Act.” UCC § 2-207(3). Because the writings of the parties did not agree on the warranty disclaimer and limitation of remedies terms, the box-top license version of those terms would not be included in the parties' contract; rather, the default provisions of the UCC would govern.

³⁷ See *Diamond Fruit Growers, Inc.*, 794 F.2d at 1444-45; cf. *Ralph Shrader, Inc.*, 833 F.2d at 1215.

³⁸ See, e.g., *Idaho Power Co.*, 596 F.2d at 926-27.

³⁹ One Florida Court of Appeals has accepted such an offer as a strong indication of a conditional acceptance. *Monsanto Agricultural Prods. Co.*, 426 So.2d at 575-76. Note that the *Monsanto* warranty label was conspicuous and available to the purchaser before the contract for the sale of the herbicide was formed. When an offeree proceeds with a contract with constructive knowledge of the terms of the offer, the offeree is typically bound by those terms, making the conditional acceptance finding unnecessary to the result reached in *Monsanto*.

formed. But we need not decide whether such a refund offer could ever amount to a conditional acceptance; the undisputed evidence in this case demonstrates that the terms of the license were not sufficiently important that TSL would forego its sales to Step-Saver if TSL could not obtain Step-Saver's consent to those terms.

38. As discussed, Mr. Greebel testified that TSL assured him that the box-top license did not apply to Step-Saver, as Step-Saver was not the end user of the Multilink Advanced program. Supporting this testimony, TSL on two occasions asked Step-Saver to sign agreements that would put in formal terms the relationship between Step-Saver and TSL. Both proposed agreements contained warranty disclaimer and limitation of remedy terms similar to those contained in the box-top license. Step-Saver refused to sign the agreements; nevertheless, TSL continued to sell copies of Multilink Advanced to Step-Saver.
39. Additionally, TSL asks us to infer, based on the refund offer, that it was willing to forego its sales to Step-Saver unless Step-Saver agreed to the terms of the box-top license. Such an inference is inconsistent with the fact that both parties agree that the terms of the box-top license *did not represent the parties's agreement* with respect to Step-Saver's right to transfer the copies of the Multilink Advanced program. Although the box-top license prohibits the transfer, by Step-Saver, of its copies of the program, both parties agree that Step-Saver was entitled to transfer its copies to the purchasers of the Step-Saver multi-user system. Thus, TSL was willing to proceed with the transaction despite the fact that one of the terms of the box-top license was not included in the contract between TSL and Step-Saver. We see no basis in the terms of the box-top license for inferring that a reasonable offeror would understand from the refund offer that certain terms of the box-top license, such as the warranty disclaimers, were essential to TSL, while others such as the non-transferability provision were not.
40. Based on these facts, we conclude that TSL did not clearly express its unwillingness to proceed with the transactions unless its additional terms were incorporated into the parties' agreement. The box-top license did not, therefore, constitute a conditional acceptance under UCC § 2-207(1).

3. Did the parties' course of dealing establish that the parties had excluded any express or implied warranties associated with the software program?
41. TSL argues that because Step-Saver placed its orders for copies of the Multilink Advanced program with notice of the terms of the box-top license, Step-Saver is bound by the terms of the box-top license. Essentially, TSL is arguing that, even if the terms of the box-top license would not become part of the contract if the case involved only a single transaction, the repeated expression of those terms by TSL eventually incorporates them within the contract.
42. Ordinarily, a “course of dealing” or “course of performance” analysis focuses on the actions of the parties with respect to a particular issue.⁴⁰ If, for example, a supplier of asphaltic paving material on two occasions gives a paving contractor price protection, a jury may infer that the parties have incorporated such a term in their agreement by their course of performance.⁴¹ Because this is the parties' first serious dispute, the parties have not previously taken any action with respect to the matters addressed by the warranty disclaimer and limitation of liability terms of the box-top license. Nevertheless, TSL seeks to extend the course of dealing analysis to this case where the only action has been the repeated sending of a particular form by TSL. While one court has concluded that terms repeated in a number of written confirmations eventually become part of the contract even though neither party ever

⁴⁰ A “course of performance” refers to actions with respect to the contract taken after the contract has formed. UCC § 2-208(1). “A course of dealing is a sequence of previous conduct between the parties to a particular transaction which is fairly to be regarded as establishing a common basis of understanding for interpreting their expressions and other conduct.” UCC § 1-205.

⁴¹ See *Nanakuli Paving & Rock Co. v. Shell Oil Co.*, 664 F.2d 772 (9th Cir.1981).

takes any action with respect to the issue addressed by those terms,⁴² most courts have rejected such reasoning.⁴³

43. For two reasons, we hold that the repeated sending of a writing which contains certain standard terms, without any action with respect to the issues addressed by those terms, cannot constitute a course of dealing which would incorporate a term of the writing otherwise excluded under § 2-207. First, the repeated exchange of forms by the parties only tells Step-Saver that TSL *desires* certain terms. Given TSL's failure to obtain Step-Saver's express assent to these terms before it will ship the program, Step-Saver can reasonably believe that, while TSL desires certain terms, it has agreed to do business on other terms—those terms expressly agreed upon by the parties. Thus, even though Step-Saver would not be surprised⁴⁴ to learn that TSL desires the terms of the box-top license, Step-Saver might well be surprised to learn that the terms of the box-top license have been incorporated into the parties's agreement.

44. Second, the seller in these multiple transaction cases will typically have the opportunity to negotiate the precise terms of the parties's agreement, as TSL sought to do in this case. The seller's unwillingness or inability to obtain a negotiated agreement reflecting its terms strongly suggests that, while the seller would like a court to incorporate its terms if a dispute were to arise, those terms are not a part of the parties's commercial bargain. For these reasons, we are not convinced that TSL's unilateral act of repeatedly sending copies of the box-top license with its product can

⁴² See *Schulze & Burch Biscuit Co. v. Tree Top, Inc.*, 831 F.2d 709, 714-15 (7th Cir.1987). As support for its position, the *Schulze* Court cites *Barliant v. Follett Corp.*, 138 Ill.App.3d 756, 91 Ill.Dec. 677, 483 N.E.2d 1312 (Ill.App.Ct.1985). Yet, the facts and result in *Barliant* do not support the reasoning in *Schulze*. In *Barliant*, the buyer had paid some twenty-four invoices, which included charges for freight and warehousing even though the agreement specified charges were F.O.B. The court found that the buyer had paid the invoices with knowledge of the additional charge for freight and warehousing. Because of this *conduct with respect to the term in question*, the buyer waived any right to complain that the charges should not have been included. 91 Ill.Dec. at 679-80, 483 N.E.2d at 1314-15. In contrast, in *Schulze*, neither party had taken any action with respect to the arbitration provision. Because no disputes had arisen, there was no conduct by either party indicating how disputes were to be resolved. Nevertheless, the *Schulze* Court held that, because the provision had been repeated in nine previous invoices, it became part of the parties's bargain. 831 F.2d at 715. We note that the Seventh Circuit refused to follow *Schulze* in a more recent case raising the same issue. See *Trans-Aire Int'l v. Northern Adhesive Co.*, 882 F.2d 1254, 1262-63 & n. 9 (7th Cir.1989).

⁴³ See, e.g., *Trans-Aire Int'l v. Northern Adhesive Co.*, 882 F.2d at 1262-63 & n. 9; *Diamond Fruit Growers, Inc.*, 794 F.2d at 1445; *Tuck Industries v. Reichhold Chemicals, Inc.*, 542 N.Y.S.2d 676, 678, 151 A.D.2d 566 (N.Y.App.Div.1989); *Southeastern Adhesives Co.*, 366 S.E.2d at 507-08.

⁴⁴ Cf. UCC § 2-207, comment 4 (suggesting that terms that “materially alter” a contract are those that would result in “surprise or hardship if incorporated without express awareness by the other party”).

establish a course of dealing between TSL and Step-Saver that resulted in the adoption of the terms of the box-top license.

45. With regard to more specific evidence as to the parties' course of dealing or performance, it appears that the parties have not incorporated the warranty disclaimer into their agreement. First, there is the evidence that TSL tried to obtain Step-Saver's express consent to the disclaimer and limitation of damages provision of the box-top license. Step-Saver refused to sign the proposed agreements. Second, when first notified of the problems with the program, TSL spent considerable time and energy attempting to solve the problems identified by Step-Saver.
46. Course of conduct is ordinarily a factual issue. But we hold that the actions of TSL in repeatedly sending a writing, whose terms would otherwise be excluded under UCC § 2-207, cannot establish a course of conduct between TSL and Step-Saver that adopted the terms of the writing.

4. Public policy concerns.

47. TSL has raised a number of public policy arguments focusing on the effect on the software industry of an adverse holding concerning the enforceability of the box-top license. We are not persuaded that requiring software companies to stand behind representations concerning their products will inevitably destroy the software industry. We emphasize, however, that we are following the well-established distinction between conspicuous disclaimers made available before the contract is formed and disclaimers made available only after the contract is formed.⁴⁵ When a disclaimer is not expressed until after the contract is formed, UCC § 2-207 governs the interpretation of the contract, and, between merchants, such disclaimers, to the extent they materially alter the parties' agreement, are not incorporated into the parties' agreement.

⁴⁵ Compare *Hill v. BASF Wyandotte Corp.*, 696 F.2d 287, 290-91 (4th Cir.1982). In that case, a farmer purchased seventy-three five gallon cans of a herbicide from a retailer. Because the disclaimer was printed conspicuously on each can, the farmer had constructive knowledge of the terms of the disclaimer before the contract formed. As a result, when he selected each can of the herbicide from the shelf and purchased it, the law implies his assent to the terms of the disclaimer. See also *Bowdoin v. Showell Growers, Inc.*, 817 F.2d 1543, 1545 (11th Cir.1987) (disclaimers that were conspicuous before the contract for sale has formed are effective; post-sale disclaimers are ineffective); *Monsanto Agricultural Prods. Co. v. Edenfield*, 426 So.2d at 575-76.

48. If TSL wants relief for its business operations from this well-established rule, their arguments are better addressed to a legislature than a court. Indeed, we note that at least two states have enacted statutes that modify the applicable contract rules in this area,⁴⁶ but both Georgia and Pennsylvania have retained the contract rules provided by the UCC.

C. The Terms of the Contract

49. Under section 2-207, an additional term detailed in the box-top license will not be incorporated into the parties' contract if the term's addition to the contract would materially alter the parties' agreement.⁴⁷ Step-Saver alleges that several representations made by TSL constitute express warranties, and that valid implied warranties were also a part of the parties' agreement. Because the district court considered the box-top license to exclude all of these warranties, the district court did not consider whether other factors may act to exclude these warranties. The existence and nature of the warranties is primarily a factual question that we leave for the district court,⁴⁸ but assuming that these warranties were included within the parties' original agreement, we must conclude that adding the disclaimer of warranty and limitation of remedies provisions from the box-top license would, as a matter of law, substantially alter the distribution of risk between Step-Saver and TSL.⁴⁹ Therefore, under UCC § 2-207(2)(b), the disclaimer of warranty and limitation of remedies terms of the box-top license did not become a part of the parties' agreement.⁵⁰

⁴⁶ Louisiana Software License Enforcement Act, La.R.S. §§ 51:1961-1966 (1987); Illinois Software Enforcement Act, Ill. Ann. Stat. ch. 29, para. 801-808 (Smith-Hurd 1987).

⁴⁷ UCC § 2-207(2)(b).

⁴⁸ For example, questions exist as to: (1) whether the statements by TSL were representations of fact, or mere statements of opinion; (2) whether the custom in the trade is to exclude warranties and limit remedies in contracts between a software producer and its dealer; (3) whether Step-Saver relied on TSL's alleged representations, or whether these warranties became a basis of the parties' bargain; and (4) whether Step-Saver's testing excluded some or all of these warranties. From the record, it appears that most of these issues are factual determinations that will require a trial, as did the warranty claims against Wyse. But we leave these issues open to the district court on remand.

⁴⁹ See *Valtrol, Inc. v. General Connectors Corp.*, 884 F.2d 149, 155 (4th Cir. 1989); *Trans-Aire Int'l v. Northern Adhesive Co.*, 882 F.2d at 1262-63; UCC § 2-207, official comment 4.

⁵⁰ The following recent cases reach a similar conclusion concerning indemnity or warranty disclaimers contained in writings exchanged after the contract had formed: *McJunkin Corp.*, 888 F.2d at 488-89; *Valtrol, Inc. v. General Connectors Corp.*, 884 F.2d at 155; *Trans-Aire Int'l v. Northern Adhesive Co.*, 882 F.2d at 1262-63; *Bowdoin*, 817 F.2d at 1545-46; *Diamond Fruit Growers, Inc.*, 794 F.2d at 1445; *Tuck Industries*, 542 N.Y.S.2d at 678; *Southeastern Adhesives Co.*, 366 S.E.2d at 507-08.

50. Based on these considerations, we reverse the trial court's holding that the parties intended the box-top license to be a final and complete expression of the terms of their agreement. Despite the presence of an integration clause in the box-top license, the box-top license should have been treated as a written confirmation containing additional terms.⁵¹ Because the warranty disclaimer and limitation of remedies terms would materially alter the parties' agreement, these terms did not become a part of the parties' agreement. We remand for further consideration the express and implied warranty claims against TSL.

[Students may wish to skim the following material which is not essential to understanding the issue of contract formation.]

III. THE INTENTIONAL MISREPRESENTATION CLAIM AGAINST TSL

51. We review the trial court's decision to grant a directed verdict on the intentional misrepresentation claim *de novo*.⁵² We ask whether, considering the evidence in the light most favorable to Step-Saver, a reasonable jury could find, by clear and convincing evidence,⁵³ each essential element of Step-Saver's fraud claim: (1) a material misrepresentation; (2) an intention to deceive; (3) an intention to induce reliance; (4) justifiable reliance by the recipient upon the representation; and (5) damage to the recipient proximately caused by the misrepresentation.⁵⁴
52. To support its intentional misrepresentation claim, Step-Saver argues that TSL made specific claims, in its advertisement and in statements by its sales representatives, that the Multilink Advanced program was compatible with various MS-DOS application programs and with the Wyse terminal. To demonstrate that TSL made these compatibility representations with an intent to deceive, Step-Saver refers to several statements made in deposition testimony by the co-founders of TSL, and argues that these statements are sufficient to establish that TSL knew these compatibility representations were false at the time they were made. In particular, Step-Saver points

⁵¹ See *Idaho Power Co.*, 596 F.2d at 925-27 (applying UCC § 2-207 despite presence of integration clause in written confirmation).

⁵² See, e.g., *Indian Coffee Corp. v. Proctor & Gamble Co.*, 752 F.2d 891, 894 (3d Cir.), cert. denied, 474 U.S. 863 (1985).

⁵³ See *Beardshall v. Minuteman Press Int'l, Inc.*, 664 F.2d 23, 26 (3d Cir.1981); *Snell v. State Examining Bd.*, 416 A.2d 468, 470 (Pa. 1980).

⁵⁴ See *Kinnel v. Mid-Atlantic Mausoleums, Inc.*, 850 F.2d 958, 963-64 (3d Cir.1988); *Scaife Co. v. Rockwell-Standard Corp.*, 285 A.2d 451, 454 (Pa. 1971), cert. denied, 407 U.S. 920 (1972).

to the statement by Mr. Robertson, one of TSL's co-founders, that he did not know of any programs “completely compatible” with Multilink Advanced.

53. In determining whether Mr. Robertson's testimony will support an inference of fraudulent intent, we, like the experts at trial, distinguish between compatibility, or practical compatibility, and complete, absolute, or theoretical compatibility. If two products are completely compatible, they will work properly together in every possible situation, every time. As Mr. Robertson explained, “complete compatibility is almost virtually impossible to obtain.” On the other hand, two products are compatible, within the standards of the computer industry, if they work together almost every time in almost every possible situation.⁵⁵
54. It is undisputed that the representations made by the sales representatives referred to practical compatibility, while Mr. Robertson's testimony referred to complete compatibility. Because of the differences between practical and complete compatibility, as those terms are used in the industry, we agree with the district court that Mr. Robertson's testimony about “complete compatibility” will not support a finding, under the clear and convincing standard, that TSL knew its representations concerning practical compatibility were false. In context, Mr. Robertson's statement was simply an expression of technical fact, not an indication that he knew that Multilink Advanced failed to satisfy industry standards for practical compatibility.

IV. THE IMPLIED WARRANTY OF MERCHANTABILITY CLAIM AGAINST WYSE

55. Step-Saver argues that there was sufficient evidence in the record to support a jury finding that the Wyse terminal was not “fit for the ordinary purposes for which such goods are used.”⁵⁶ and that the trial judge should have permitted the jury to decide the implied warranty of merchantability issue.
56. The only evidence introduced by Step-Saver on this issue was that certain features on the WY-60 terminal were not compatible with the Multilink Advanced operating environment. For example, the WY-60 terminal originally had repeatable, instead of

⁵⁵ We disagree with the holding by the district court that a representation of compatibility is a statement of opinion, rather than fact. Compatibility between two computer products can be tested and determined. While two computer products are not likely to be perfectly compatible, the question of whether the degree of compatibility is consistent with industry standards is a question generally for the jury, not the judge.

⁵⁶ UCC § 2-314(2)(c).

toggle,⁵⁷ NUM LOCK and CAPS LOCK keys. The combination of repeatable keys and the Multilink Advanced program caused the NUM LOCK or CAPS LOCK indicated by the terminal to become out of synchronicity with the actual setting followed by the computer. As a result, a terminal's screen and keyboard might indicate that CAPS LOCK was on, when in fact it was off. Because of this, a user might type an entire document believing that the document was in all capital letters, only to discover upon printing that the document was in all lower case letters.

57. While this evidence demonstrates some compatibility problems between the WY-60 terminal and the Multilink Advanced program, Wyse introduced undisputed testimony that a user would encounter the same compatibility problems when using the Multilink Advanced operating environment on either a Kimtron KT-7 terminal, or a Link terminal, the terminals offered by Wyse's two primary competitors. Undisputed testimony also established that Wyse had sold over one million WY-60 terminals since the terminal's introduction in April of 1986, and that the WY-60 was the top-selling terminal in its class.
58. Furthermore, undisputed testimony by Wyse engineers established that the WY-60 terminals were built to industry-standard specifications for terminals designed to work with a multi-user system based on the IBM AT or XT. It is apparent that when the pieces of a system intended to work together are designed and built independently, each piece must conform to certain specifications if the pieces are to work together properly. Just as a nut and bolt must be built in a certain manner to insure their fit, so too the components of a multi-user system. Just as a bolt, built to industry standards for a certain size and thread, cannot be considered unfit for its ordinary use simply because a particular nut does not fit it, so too the WY-60 terminal.
59. Under a warranty of merchantability, the seller warrants only that the goods are of acceptable quality "when compared to that generally acceptable in the trade for goods

⁵⁷ If a user presses and holds a repeatable NUM LOCK key, the terminal will switch back and forth between NUM LOCK on and NUM LOCK off as long as the user holds down the key. In contrast, if a user presses and holds a toggle key, the terminal will switch from the present setting to the other setting. Even if the user continues to hold the key, the setting will not change but once. In order to change the setting back to the prior setting, the user must release the key and press it again.

of the kind.”⁵⁸ Because the undisputed testimony established that the WY-60 terminal conformed to the industry standard for terminals designed to operate in conjunction with an IBM AT, the evidence of incompatibility with the Multilink Advanced operating system is not sufficient to support a finding that Wyse breached the implied warranty of merchantability.⁵⁹

V. EVIDENTIARY RULINGS

60. We have carefully reviewed the record regarding the evidentiary rulings. For the reasons given on these two issues in the district court's memorandum opinion rejecting Step-Saver's motion for a new trial,⁶⁰ we hold that the exclusion of the unsent letter and the refusal to permit rebuttal testimony on the issue of the ordinary uses of the WY-60 terminal did not constitute an abuse of discretion.

VI.

61. We will reverse the holding of the district court that the parties intended to adopt the box-top license as the complete and final expression of the terms of their agreement. We will remand for further consideration of Step-Saver's express and implied warranty claims against TSL. Finding a sufficient basis for the other decisions of the district court, we will affirm in all other respects.

⁵⁸ *Price Bros. Co. v. Philadelphia Gear Corp.*, 649 F.2d 416, 424 (6th Cir.), *cert. denied*, 454 U.S. 1099 (1981); *see also Dugan & Meyers Constr. Co. v. Worthington Pump Corp. (USA)*, 746 F.2d 1166, 1176 (6th Cir.1984), *cert. denied*, 471 U.S. 1135 (1985).

⁵⁹ *See In re Franklin Computer Corp.*, 57 B.R. 155, 157 (Bankr.E.D.Pa.1986).

⁶⁰ *Step-Saver Data Sys., Inc. v. Wyse Tech.*, 752 F.Supp. 181, 192-93 (E.D.Pa.1990).

Hill v. Gateway 2000

United States Court of Appeals, Seventh Circuit
105 F.3d 1147 (1997)

Easterbrook, Circuit Judge.

1. A customer picks up the phone, orders a computer, and gives a credit card number. Presently a box arrives, containing the computer and a list of terms, said to govern unless the customer returns the computer within 30 days. Are these terms effective as the parties' contract, or is the contract term-free because the order-taker did not read any terms over the phone and elicit the customer's assent?
2. One of the terms in the box containing a Gateway 2000 system was an arbitration clause. Rich and Enza Hill, the customers, kept the computer more than 30 days before complaining about its components and performance. They filed suit in federal court arguing, among other things, that the product's shortcomings make Gateway a racketeer (mail and wire fraud are said to be the predicate offenses), leading to treble damages under RICO for the Hills and a class of all other purchasers. Gateway asked the district court to enforce the arbitration clause; the judge refused, writing that “[t]he present record is insufficient to support a finding of a valid arbitration agreement between the parties or that the plaintiffs were given adequate notice of the arbitration clause.” Gateway took an immediate appeal, as is its right. 9 U.S.C. § 16(a)(1)(A).
3. The Hills say that the arbitration clause did not stand out: they concede noticing the statement of terms but deny reading it closely enough to discover the agreement to arbitrate, and they ask us to conclude that they therefore may go to court. Yet an agreement to arbitrate must be enforced “save upon such grounds as exist at law or in equity for the revocation of any contract.” 9 U.S.C. § 2. *Doctor's Associates, Inc. v. Casarotto*, 517 U.S. 681 (1996), holds that this provision of the Federal Arbitration Act is inconsistent with any requirement that an arbitration clause be prominent. A contract need not be read to be effective; people who accept take the risk that the unread terms may in retrospect prove unwelcome. *Carr v. CIGNA Securities, Inc.*, 95 F.3d 544, 547 (7th Cir.1996); *Chicago Pacific Corp. v. Canada Life Assurance Co.*, 850 F.2d 334 (7th Cir.1988). Terms inside Gateway's box stand or fall together. If they constitute the parties' contract because the Hills had an opportunity to return the computer after reading them, then all must be enforced.

4. *ProCD, Inc. v. Zeidenberg*, 86 F.3d 1447 (7th Cir.1996), holds that terms inside a box of software bind consumers who use the software after an opportunity to read the terms and to reject them by returning the product. Likewise, *Carnival Cruise Lines, Inc. v. Shute*, 499 U.S. 585 (1991), enforces a forum-selection clause that was included among three pages of terms attached to a cruise ship ticket. *ProCD* and *Carnival Cruise Lines* exemplify the many commercial transactions in which people pay for products with terms to follow; *ProCD* discusses others. 86 F.3d at 1451-52. The district court concluded in *ProCD* that the contract is formed when the consumer pays for the software; as a result, the court held, only terms known to the consumer at that moment are part of the contract, and provisos inside the box do not count. Although this is one way a contract could be formed, it is not the only way: “A vendor, as master of the offer, may invite acceptance by conduct, and may propose limitations on the kind of conduct that constitutes acceptance. A buyer may accept by performing the acts the vendor proposes to treat as acceptance.” *Id.* at 1452. Gateway shipped computers with the same sort of accept-or-return offer *ProCD* made to users of its software. *ProCD* relied on the Uniform Commercial Code rather than any peculiarities of Wisconsin law; both Illinois and South Dakota, the two states whose law might govern relations between Gateway and the Hills, have adopted the UCC; neither side has pointed us to any atypical doctrines in those states that might be pertinent; *ProCD* therefore applies to this dispute.
5. Plaintiffs ask us to limit *ProCD* to software, but where's the sense in that? *ProCD* is about the law of contract, not the law of software. Payment preceding the revelation of full terms is common for air transportation, insurance, and many other endeavors. Practical considerations support allowing vendors to enclose the full legal terms with their products. Cashiers cannot be expected to read legal documents to customers before ringing up sales. If the staff at the other end of the phone for direct-sales operations such as Gateway's had to read the four-page statement of terms before taking the buyer's credit card number, the droning voice would anesthetize rather than enlighten many potential buyers. Others would hang up in a rage over the waste of their time. And oral recitation would not avoid customers' assertions (whether true or feigned) that the clerk did not read term X to them, or that they did not remember or understand it. Writing provides benefits for both sides of commercial transactions. Customers as a group are better off when vendors skip costly and ineffectual steps such as telephonic recitation, and use instead a simple approve-or-return device. Competent adults are bound by such documents, read or unread. For what little it is

worth, we add that the box from Gateway was crammed with software. The computer came with an operating system, without which it was useful only as a boat anchor. See *Digital Equipment Corp. v. Uniq Digital Technologies, Inc.*, 73 F.3d 756, 761 (7th Cir.1996). Gateway also included many application programs. So the Hills' effort to limit *ProCD* to software would not avail them factually, even if it were sound legally—which it is not.

6. For their second sally, the Hills contend that *ProCD* should be limited to executory contracts (to licenses in particular), and therefore does not apply because both parties' performance of this contract was complete when the box arrived at their home. This is legally and factually wrong: legally because the question at hand concerns the *formation* of the contract rather than its *performance*, and factually because both contracts were incompletely performed. *ProCD* did not depend on the fact that the seller characterized the transaction as a license rather than as a contract; we treated it as a contract for the sale of goods and reserved the question whether for other purposes a “license” characterization might be preferable. 86 F.3d at 1450. All debates about characterization to one side, the transaction in *ProCD* was no more executory than the one here: Zeidenberg paid for the software and walked out of the store with a box under his arm, so if arrival of the box with the product ends the time for revelation of contractual terms, then the time ended in *ProCD* before Zeidenberg opened the box. But of course *ProCD* had not completed performance with delivery of the box, and neither had Gateway. One element of the transaction was the warranty, which obliges sellers to fix defects in their products. The Hills have invoked Gateway's warranty and are not satisfied with its response, so they are not well positioned to say that Gateway's obligations were fulfilled when the motor carrier unloaded the box. What is more, both *ProCD* and Gateway promised to help customers to use their products. Long-term service and information obligations are common in the computer business, on both hardware and software sides. Gateway offers “lifetime service” and has a round-the-clock telephone hotline to fulfil this promise. Some vendors spend more money helping customers use their products than on developing and manufacturing them. The document in Gateway's box includes promises of future performance that some consumers value highly; these promises bind Gateway just as the arbitration clause binds the Hills.
7. Next the Hills insist that *ProCD* is irrelevant because Zeidenberg was a “merchant” and they are not. Section 2-207(2) of the UCC, the infamous battle-of-the-forms section, states that “additional terms [following acceptance of an offer] are to be

construed as proposals for addition to a contract. Between merchants such terms become part of the contract unless ...”. Plaintiffs tell us that *ProCD* came out as it did only because Zeidenberg was a “merchant” and the terms inside ProCD's box were not excluded by the “unless” clause. This argument pays scant attention to the opinion in *ProCD*, which concluded that, when there is only one form, “sec. 2-207 is irrelevant.” 86 F.3d at 1452. The question in *ProCD* was not whether terms were added to a contract after its formation, but how and when the contract was formed—in particular, whether a vendor may propose that a contract of sale be formed, not in the store (or over the phone) with the payment of money or a general “send me the product,” but after the customer has had a chance to inspect both the item and the terms. *ProCD* answers “yes,” for merchants and consumers alike. Yet again, for what little it is worth we observe that the Hills misunderstand the setting of *ProCD*. A “merchant” under the UCC “means a person who deals in goods of the kind or otherwise by his occupation holds himself out as having knowledge or skill peculiar to the practices or goods involved in the transaction”, § 2-104(1). Zeidenberg bought the product at a retail store, an uncommon place for merchants to acquire inventory. His corporation put ProCD's database on the Internet for anyone to browse, which led to the litigation but did not make Zeidenberg a software merchant.

8. At oral argument the Hills propounded still another distinction: the box containing ProCD's software displayed a notice that additional terms were within, while the box containing Gateway's computer did not. The difference is functional, not legal. Consumers browsing the aisles of a store can look at the box, and if they are unwilling to deal with the prospect of additional terms can leave the box alone, avoiding the transactions costs of returning the package after reviewing its contents. Gateway's box, by contrast, is just a shipping carton; it is not on display anywhere. Its function is to protect the product during transit, and the information on its sides is for the use of handlers (“Fragile!” “This Side Up!”) rather than would-be purchasers.
9. Perhaps the Hills would have had a better argument if they were first alerted to the bundling of hardware and legal-ware after opening the box and wanted to return the computer in order to avoid disagreeable terms, but were dissuaded by the expense of shipping. What the remedy would be in such a case—could it exceed the shipping charges?—is an interesting question, but one that need not detain us because the Hills knew before they ordered the computer that the carton would include *some* important terms, and they did not seek to discover these in advance. Gateway's ads state that their products come with limited warranties and lifetime support. How limited was

the warranty—30 days, with service contingent on shipping the computer back, or five years, with free onsite service? What sort of support was offered? Shoppers have three principal ways to discover these things. First, they can ask the vendor to send a copy before deciding whether to buy. The Magnuson-Moss Warranty Act requires firms to distribute their warranty terms on request, 15 U.S.C. § 2302(b)(1)(A); the Hills do not contend that Gateway would have refused to enclose the remaining terms too. Concealment would be bad for business, scaring some customers away and leading to excess returns from others. Second, shoppers can consult public sources (computer magazines, the Web sites of vendors) that may contain this information. Third, they may inspect the documents after the product's delivery. Like Zeidenberg, the Hills took the third option. By keeping the computer beyond 30 days, the Hills accepted Gateway's offer, including the arbitration clause.

10. The Hills' remaining arguments, including a contention that the arbitration clause is unenforceable as part of a scheme to defraud, do not require more than a citation to *Prima Paint Corp. v. Flood & Conklin Mfg. Co.*, 388 U.S. 395, 87 S.Ct. 1801, 18 L.Ed.2d 1270 (1967). Whatever may be said pro and con about the cost and efficacy of arbitration (which the Hills disparage) is for Congress and the contracting parties to consider. Claims based on RICO are no less arbitrable than those founded on the contract or the law of torts. *Shearson/American Express, Inc. v. McMahon*, 482 U.S. 220, 238-42, 107 S.Ct. 2332, 2343-46, 96 L.Ed.2d 185 (1987). The decision of the district court is vacated, and this case is remanded with instructions to compel the Hills to submit their dispute to arbitration.

Steas v. Leonard

Supreme Court of Minnesota
20 Minn. 494 (1874)

1. Appeal by defendants from an order of the district court, Ramsey county, denying a new trial.
2. The action was brought to recover damages for a failure of defendants to erect and complete a building on a lot of plaintiffs, on Minnesota street, between Third and Fourth streets, in the city of St. Paul, which, by an agreement under seal between them and plaintiffs, the defendants had agreed to build, erect, and complete, according to plans and specifications annexed to and made part of the agreement. The defendants commenced the construction of the building, and had carried it to the height of three stories, when it fell to the ground. The next year, 1869, they began again and carried it to the same height as before, when it again fell to the ground, whereupon defendants refused to perform the contract. They claimed that in their attempts to erect the building they did the work in all respects according to the plans and specifications, and that the failure to complete the building and its fall on the two occasions was due to the fact that the soil upon which it was to be constructed was composed of quicksand, and when water flowed into it, was incapable of sustaining the building. The offers of proof by defendants, and the character of the allegations in the answer, under which the court held some of the offers inadmissible, are sufficiently indicated in the opinion.

YOUNG, J.

3. The general principle of law which underlies this case is well established. 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. This doctrine may sometimes seem to bear heavily upon contractors; but, in such cases, the hardship is attributable, not to the law, but to the contractor himself, who has improvidently assumed an absolute, when he might have undertaken only a qualified, liability. The law does no more than enforce the contract as the parties themselves have made it. Many cases illustrating the application of the doctrine to

every variety of contract are collected in the note to *Cutter v. Powell*, 2 Smith, Lead. Cas. 1.

4. The rule has been applied in several recent cases, closely analogous to the present in their leading facts. In *Adams v. Nichols*, 19 Pick. 275, the defendant, Nichols, contracted to erect a dwelling-house for plaintiff on plaintiff's land. The house was nearly completed, when it was destroyed by accidental fire. It was held that the casualty did not relieve the contractor from his obligation to perform the contract he had deliberately entered into. The court clearly state and illustrate the rule, as laid down in the note to *Walton v. Waterhouse*, 2 Wms. Saunders, 422, and add: "In these and similar cases, which seem hard and oppressive, the law does no more than enforce the exact contract entered into. If there be any hardship, it arises from the indiscretion or want of foresight of the suffering party. It is not the province of the law to relieve persons from the improvidence of their own acts."
5. In *School District v. Dauchy*, 25 Conn. 530, the defendant contracted to build and complete a school-house. When nearly finished, the building was struck by lightning, and consumed by the consequent fire, and the defendant refused to rebuild, although plaintiffs offered to allow him such further time as should be necessary. It was held that this non-performance was not excused by the destruction of the building. The court thus state the rule: "If a person promise absolutely, without exception or qualification, that a certain thing shall be done by a given time, or that a certain event shall take place, and the thing to be done, or the event, is neither impossible nor unlawful at the time of the promise, he is bound by his promise, unless the performance, before that time, becomes unlawful."
6. *School Trustees v. Bennett*, 3 Dutcher, 513, is almost identical, in its material facts, with the present case. The contractors agreed to build and complete a school-house, and find all materials therefor, according to specifications annexed to the contract; the building to be located on a lot owned by plaintiff, and designated in the contract. When the building was nearly completed it was blown down by a sudden and violent gale of wind. The contractors again began to erect the building, when it fell, solely on account of the soil on which it stood having become soft and miry, and unable to sustain the weight of the building; although, when the foundations were laid, the soil was so hard as to be penetrated with difficulty by a pickax, and its defects were latent. The plaintiff had a verdict for the amount of the installments paid under the contract as the work progressed. The verdict was sustained by the supreme court, which held

that the loss, although arising solely from a latent defect in the soil, and not from a faulty construction of the building, must fall on the contractor.

7. In the opinion of the court, the question is fully examined, many cases are cited, and the rule is stated “that where a party by his own contract creates a duty or charge upon himself he is bound to make it good if he may, notwithstanding any accident by inevitable necessity, because he might have provided against it by his contract.... If, before the building is completed or accepted, it is destroyed by fire or other casualty, the loss falls upon the builder; he must rebuild. The thing may be done, and he has contracted to do it....No matter how harsh and apparently unjust in its operation the rule may occasionally be, it cannot be denied that it has its foundations in good sense and inflexible honesty. He that agrees to do an act should do it, unless absolutely impossible. He should provide against contingencies in his contract. Where one of two innocent persons must sustain a loss, the law casts it upon him who has agreed to sustain it; or, rather, the law leaves it where the agreement of the parties has put it....Neither the destruction of the incomplete building by a tornado, nor its falling by a latent softness of the soil, which rendered the foundation insecure, *necessarily* prevented the performance of the contract to build, erect, and complete this building for the specified price. It can still be done, for aught that was opened to the jury as a defense, and overruled by the court.”
8. In *Dermott v. Jones*, 2 Wall. 1, the foundation of the building sank, owing to a latent defect in the soil, and the owner was compelled to take down and rebuild a portion of the work. The contractor having sued for his pay, it was held that the owner might recoup the damages sustained by his deviation from the contract. The court refer with approval to the cases cited, and say: “The principle which controlled them rests upon a solid foundation of reason and justice. It regards the sanctity of contracts. It requires a party to do what he has agreed to do. If unexpected impediments lie in the way, and a loss ensue, it leaves the loss where the contract places it. If the parties have made no provision for a dispensation, the rule of law gives none. It does not allow a contract fairly made to be annulled, and it does not permit to be interpolated what the parties themselves have not stipulated.”
9. Nothing can be added to the clear and cogent arguments we have quoted in vindication of the wisdom and justice of the rule which must govern this case, unless it is in some way distinguishable from the cases cited.

10. It is argued that the spot on which the building is to be erected is not designated with precision in the contract, but is left to be selected by the owner; that, under the contract, the right to designate the particular spot being reserved to plaintiffs, they must select one that will sustain the building described in the specifications, and if the spot they select is not, in its natural state, suitable, they must make it so; that in this respect the present case differs from *School Trustees v. Bennett*.
11. The contract does not, perhaps, designate the site of the proposed building with absolute certainty; but in this particular it is aided by the pleadings. The complaint states that defendants contracted to erect the proposed building on “*a certain piece* of land, of which the plaintiffs then were, and now are, the owners in fee, fronting on Minnesota street, between Third and Fourth streets, in the city of St. Paul.” The answer expressly admits that the defendants entered into a contract to erect the building, according to the plans, etc., “on that certain piece of land in said complaint described,” and that they “entered upon the performance of said contract, and proceeded with the erection of said building,” etc. This is an express admission that the contract was made with reference to the identical piece of land on which the defendants afterwards attempted to perform it, and leaves no foundation in fact for the defendants' argument.
12. It is no defense to the action that the specifications directed that “footings” should be used as the foundation of the building, and that the defendants, in the construction of these footings, as well as in all other particulars, conformed to the specifications. The defendants contracted to “erect and complete the building.” Whatever was necessary to be done in order to complete the building, they were bound by the contract to do. If the building could not be completed without other or stronger foundations than the footings specified, they were bound to furnish such other foundations. If the building could not be erected without draining the land, then they must drain the land, “because they have agreed to do everything necessary to erect and complete the building.” 3 Dutcher 520; and, see *Dermott v. Jones, supra*, where the same point was made by the contractor, but ruled against him by the court.
13. As the draining of the land was, in fact, necessary to the erection and completion of the building, it was a thing to be done, under the contract, by the defendants. The prior parol agreement that plaintiffs should drain the land, related, therefore, to a matter embraced within the terms of the written contract, and was not, as claimed by defendants' counsel, collateral thereto. It was, accordingly, under the familiar rule,

inadmissible in evidence to vary the terms of the written contract, and was properly excluded.

14. In their second and third offers the defendants proposed to prove that after the making of the written contract, and when the defendants, in the course of their excavation for the cellar and foundation, first discovered that the soil, being porous and spongy, would not sustain the building, unless drained, the plaintiffs proposed and promised to keep the soil well drained during the construction of the building; that, in consequence, the defendants did not drain the same; that plaintiffs for a time kept the soil drained, but afterwards, and just before the fall of the building, they neglected to drain, in consequence of which neglect the soil became saturated with water, and the building fell; and that a like promise was made by defendants at the beginning of the erection of the second building, followed by like part performance and neglect, and subsequent, and consequent, fall of the building.
15. The rule that a sealed contract cannot be varied by a subsequent parol agreement, is of great antiquity, the maxim on which it rests, *unumquodque dissolvitur eodem modo, quo ligatur*, being one of the most ancient in our law. Broom, Leg. Max. 877; 5 Rep. 26 *a*, citing Bracton, lib. 2, fol. 28; and, see Bracton, fol. 101. In early days the rigor with which it was enforced in the courts of law, led to the interference of chancery to prevent injustice. Per Lord ELLESMERE, *Earl of Oxford's Case*, 2 Lead. Cas. in Eq. 508*; 1 Spence, Eq. Jur. 636. In later times that rigor has become much relaxed, although the English courts of law have refused to permit sealed contracts to be varied by parol in cases of great hardship. *Littler v. Holland*, 3 Term R. 590; *Gwynne v. Davy*, 1 Man. & Gr. 857; *West v. Blakeway*, 2 Man. & Gr. 729; and, see *Albert v. Grosvenor Investment Co.* L. R. 3 Q. B. 123.
16. But, in this country, it has become a well-settled exception to the rule, that a sealed contract may be modified by a subsequent parol agreement, if the latter has been executed, or has been so acted on that the enforcing of the original contract would be inequitable. *Munroe v. Perkins*, 9 Pick. 298; *Mill-dam Foundry v. Hovey*, 21 Pick. 417; *Blasdell v. Souther*, 6 Gray 149; *Foster v. Dawber*, 6 Exch. 854, and note; *Thurston v. Ludwig*, 6 Ohio St. 1; *Delacroix v. Bulkley*, 13 Wend. 71; *Allen v. Jaquish*, 21 Wend. 628; *Vicary v. Moore*, 2 Watts, 451; *Lawall v. Rader*, 24 Pa. St. 283; *Carrier v. Dilworth*, 59 Pa. St. 406; *Richardson v. Cooper*, 25 Me. 450; *Lawrence v. Dole*, 11 Vt. 549; *Patrick v. Adams*, 29 Vt. 376; *Seibert v. Leonard*, 17 Minn. 436, (Gil. 410;); *Very v. Levy*, 13 How. 345; 1 Smith, Lead. Cas. (6th Ed.) 576.

17. Whether the evidence offered shows a valid consideration for the plaintiff's promise, or whether it shows that such promise, though without consideration, has been so acted on as to inure, by way of estoppel or otherwise, to release defendants from their obligation to drain, are questions that were fully discussed at the bar, but which we are not called upon to determine; for the objection is well taken by counsel for the plaintiffs, that the evidence embraced in the second and third offers is inadmissible under the pleadings.
18. In their answer, the defendants allege an offer and promise by plaintiffs (made after the defendants had commenced work under the contract) to keep the land drained during the erection of the building. No consideration is alleged for this promise, and, as *nudum pactum*, it could of itself have no effect to vary the obligations imposed on the defendants by the sealed contract. The answer proceeds to allege "that the plaintiffs wholly and wrongfully failed and neglected to drain or cause to be drained the said piece of land, or any part of the same." It is clear that the defendants would have no right to rely on this naked promise, followed by no acts of plaintiffs in part performance. If the defendants went on with the building, without taking the precaution to drain the land, they proceeded at their own risk. The answer sets up no facts on which an estoppel can be founded, and shows no defense to the action.
19. But the defendants, at the trial, offered to prove, not only that the plaintiffs offered to drain the land, but also "that the plaintiffs did, for a time, keep the same drained,...but afterwards they neglected to do so," etc. Assuming that the facts offered to be proved would constitute a defense, (and we are not prepared to say they would not,) no such defense is pleaded in the answer.
20. The tendency of this proof was to establish a new defense, not pleaded, and to contradict, rather than to sustain, the allegations of the answer. For this reason it was inadmissible, even if the facts offered to be proved would, if admissible constitute a defense to the action. If the proof offered would have no such tendency, it was immaterial, and for this reason also was rightly excluded. And as all the evidence embraced in each offer was offered as a whole, and a part thereof was inadmissible, the entire offers were properly rejected.
21. The objection that the evidence offered was "incompetent, irrelevant, and immaterial," was sufficiently specific. The defendants' counsel must know the

contents of the answer, and that evidence inconsistent therewith is inadmissible, if objected to.

22. There was, therefore, no error in the exclusion of the evidence offered, and the order appealed from is affirmed.

Taylor v. Caldwell

King's Bench

3 B. & S. 826, 112 Eng. Rep. 309 (1863)

BLACKBURN J.

1. In this case the plaintiffs and defendants had, on the 27th May, 1861, entered into a contract by which the defendants agreed to let the plaintiffs have the use of The Surrey Gardens and Music Hall on four days then to come, viz., the 17th June, 15th July, 5th August and 19th August, for the purpose of giving a series of four grand concerts, and day and night fetes at the Gardens and Hall on those days respectively; and the plaintiffs agreed to take the Gardens and Hall on those days, and pay 100£ for each day. The parties inaccurately call this a "letting," and the money to be paid a "rent;" but the whole agreement is such as to shew that the defendants were to retain the possession of the Hall and Gardens so that there was to be no demise of them, and that the contract was merely to give the plaintiffs the use of them on those days. Nothing however, in our opinion, depends on this. The agreement then proceeds to set out various stipulations between the parties as to what each was to supply for these concerts and entertainments, and as to the manner in which they should be carried on. The effect of the whole is to shew that the existence of the Music Hall in the Surrey Gardens in a state fit for a concert was essential for the fulfilment of the contract—such entertainments as the parties contemplated in their agreement could not be given without it. After the making of the agreement, and before the first day on which a concert was to be given, the Hall was destroyed by fire. This destruction, we must take it on the evidence, was without the fault of either party, and was so complete that in consequence the concerts could not be given as intended. And the question we have to decide is whether, under these circumstances, the loss which the plaintiffs have sustained is to fall upon the defendants. The parties when framing their agreement evidently had not present to their minds the possibility of such a disaster, and have made no express stipulation with reference to it, so that the answer to the question must depend upon the general rules of law applicable to such a contract.
2. There seems no doubt that where there is a positive contract to do a thing, not in itself unlawful, the contractor must perform it or pay damages for not doing it, although in consequence of unforeseen accidents, the performance of his contract has become unexpectedly burthensome or even impossible. The law is so laid down in 1

Roll. Abr. 450, Condition (G), and in the note (2) to *Walton v. Waterhouse* (2 Wms. Saund. 421 a. 6th ed.), and is recognised as the general rule by all the Judges in the much discussed case of *Hall v. Wright* (E. B. & E. 746). But this rule is only applicable when the contract is positive and absolute, and not subject to any condition either express or implied: and there are authorities which, as we think, establish the principle that where, from the nature of the contract, it appears that the parties must from the beginning have known that it could not be fulfilled unless when the time for the fulfilment of the contract arrived some particular specified thing continued to exist, so that, when entering into the contract, they must have contemplated such continuing existence as the foundation of what was to be done; there, in the absence of any express or implied warranty that the thing shall exist, the contract is not to be construed as a positive contract, but as subject to an implied condition that the parties shall be excused in case, before breach, performance becomes impossible from the perishing of the thing without default of the contractor. There seems little doubt that this implication tends to further the great object of making the legal construction such as to fulfil the intention of those who entered into the contract. For in the course of affairs men in making such contracts in general would, if it were brought to their minds, say that there should be such a condition. Accordingly, in the Civil law, such an exception is implied in every obligation of the class which they call *obligatio de certo corpore*. The rule is laid down in the Digest, lib. xLv., tit. 1, de *verborum obligationibus*, l. 33. "*Si Stichus certo die dari promissus, ante diem moriatur: non tenetur promissor.*" The principle is more fully developed in l. 23. "*Si ex legati causa, aut ex stipulatii hominem certum mihi debeas: non aliter post mortem ejus tenearis mihi, quam si per te steterit, quominus vivo eo eum mihi dares: quod ita fit, si aut interpellatus non dedisti, aut occidisti eum.*" The examples are of contracts respecting a slave, which was the common illustration of a certain subject used by the Roman lawyers, just as we are apt to take a horse; and no doubt the propriety, one might almost say necessity, of the implied condition is more obvious when the contract relates to a living animal, whether man or brute, than when it relates to some inanimate thing (such as in the present case a theatre) the existence of which is not so obviously precarious as that of the live animal, but the principle is adopted in the Civil law as applicable to every obligation of which the subject is a certain thing. The general subject is treated of by Pothier, who in his *Traite des Obligations*, partie 3, chap. 6, art. 3, § 668 states the result to be that the debtor *corporis certi* is freed from his obligation when the thing has perished, neither by his act, nor his neglect, and

before he is in default, unless by some stipulation he has taken on himself the risk of the particular misfortune which has occurred.

3. Although the Civil law is not of itself authority in an English Court, it affords great assistance in investigating the principles on which the law is grounded. And it seems to us that the common law authorities establish that in such a contract the same condition of the continued existence of the thing is implied by English law.
4. There is a class of contracts in which a person binds himself to do something which requires to be performed by him in person; and such promises, e.g. promises to marry, or promises to serve for a certain time, are never in practice qualified by an express exception of the death of the party; and therefore in such cases the contract is in terms broken if the promisor dies before fulfilment. Yet it was very early determined that, if the performance is personal, the executors are not liable; *Hyde v. The Dean of Windsor* (Cro. Eliz. 552, 553). See 2 Wms. Exors. 1560, 5th ed., where a very apt illustration is given. "Thus," says the learned author, "if an author undertakes to compose a work, and dies before completing it, his executors are discharged from this contract: for the undertaking is merely personal in its nature, and, by the intervention of the contractor's death, has become impossible to be performed." For this he cites a dictum of Lord Lyndhurst in *Marshall v. Broadhurst* (1 Tyr. 348, 349), and a case mentioned by Patteson J. in *Wentworth v. Cock* (10 A. & E. 42, 45-46). In *Hall v. Wright* (E. B. & E. 746, 749), Crompton J., in his judgment, puts another case. "Where a contract depends upon personal skill, and the act of God renders it impossible, as, for instance, in the case of a painter employed to paint a picture who is struck blind, it may be that the performance might be excused."
5. It seems that in those cases the only ground on which the parties or their executors, can be excused from the consequences of the breach of the contract is, that from the nature of the contract there is an implied condition of the continued existence of the life of the contractor, and, perhaps in the case of the painter of his eyesight. In the instances just given, the person, the continued existence of whose life is necessary to the fulfilment of the contract, is himself the contractor, but that does not seem in itself to be necessary to the application of the principle; as is illustrated by the following example. In the ordinary form of an apprentice deed the apprentice binds himself in unqualified terms to "serve until the full end and term of seven years to be fully complete and ended," during which term it is covenanted that the apprentice his master "faithfully shall serve," and the father of the apprentice in equally unqualified

terms binds himself for the performance by the apprentice of all and every covenant on his part. (See the form, 2 Chitty on Pleading, 370, 7th ed. by Greening.) It is undeniable that if the apprentice dies within the seven years, the covenant of the father that he shall perform his covenant to serve for seven years is not fulfilled, yet surely it cannot be that an action would lie against the father? Yet the only reason why it would not is that he is excused because of the apprentice's death.

6. These are instances where the implied condition is of the life of a human being, but there are others in which the same implication is made as to the continued existence of a thing. For example, where a contract of sale is made amounting to a bargain and sale, transferring presently the property in specific chattels, which are to be delivered by the vendor at a future day; there, if the chattels, without the fault of the vendor, perish in the interval, the purchaser must pay the price and the vendor is excused from performing his contract to deliver, which has thus become impossible.
7. That this is the rule of the English law is established by the case of *Rugg v. Minett* (11 East, 210), where the article that perished before delivery was turpentine, and it was decided that the vendor was bound to refund the price of all those lots in which the property had not passed; but was entitled to retain without deduction the price of those lots in which the property had passed, though they were not delivered, and though in the conditions of sale, which are set out in the report, there was no express qualification of the promise to deliver on payment. It seems in that case rather to have been taken for granted than decided that the destruction of the thing sold before delivery excused the vendor from fulfilling his contract to deliver on payment.
8. This also is the rule in the Civil law, and it is worth noticing that Pothier, in his celebrated *Traite du Contrat de Vente* (see Part. 4, § 307, etc.; and Part. 2, ch. 1, sect. 1, art. 4, § 1), treats this as merely an example of the more general rule that every obligation de certo corpore is extinguished when the thing ceases to exist. See Blackburn on the Contract of Sale, p. 173.
9. The same principle seems to be involved in the decision of *Sparrow v. Sowyate* (W. Jones, 29), where, to an action of debt on an obligation by bail, conditioned for the payment of the debt or the render of the debtor, it was held a good plea that before any default in rendering him the principal debtor died. It is true that was the case of a bond with a condition, and a distinction is sometimes made in this respect between a condition and a contract. But this observation does not apply to *Williams v. Lloyd* (W.

Jones, 179). In that case the count, which was in assumpsit, alleged that the plaintiff had delivered a horse to the defendant, who promised to redeliver it on request. Breach, that though requested to redeliver the horse he refused. Plea, that the horse was sick and died, and the plaintiff made the request after its death; and on demurrer it was held a good plea, as the bailee was discharged from his promise by the death of the horse without default or negligence on the part of the defendant. "Let it be admitted," say the Court, "that he promised to deliver it on request, if the horse die before, that is become impossible by the act of God, so the party shall be discharged, as much as if an obligation were made conditioned to deliver the horse on request, and he died before it." And Jones, adds the report, cited 22 Ass. 41, in which it was held that a ferryman who had promised to carry a horse safe across the ferry was held chargeable for the drowning of the animal only because he had overloaded the boat, and it was agreed, that notwithstanding the promise no action would have lain had there been no neglect or default on his part. It may, we think, be safely asserted to be now English law, that in all contracts of loan of chattels or bailments if the performance of the promise of the borrower or bailee to return the things lent or bailed, becomes impossible because it has perished, this impossibility (if not arising from the fault of the borrower or bailee from some risk which he has taken upon himself) excuses the borrower or bailee from the performance of his promise to redeliver the chattel. The great case of *Coggs v. Bernard* (1 Smith's L. C. 171, 5th ed.; 2 L. Raym. 909) is now the leading case on the law of bailments, and Lord Holt, in that case, referred so much to the Civil law that it might perhaps be thought that this principle was there derived direct from the civilians, and was not generally applicable in English law except in the case of bailments; but the case of *Williams v. Lloyd* (W. Jones, 179), above cited, shews that the same law had been already adopted by the English law as early as The Book of Assizes. The principle seems to us to be that, in contracts in which the performance depends on the continued existence of a given person or thing, a condition is implied that the impossibility of performance arising from the perishing of the person or thing shall excuse the performance. In none of these cases is the promise in words other than positive, nor is there any express stipulation that the destruction of the person or thing shall excuse the performance; but that excuse is by law implied, because from the nature of the contract it is apparent that the parties contracted on the basis of the continued existence of the particular person or chattel. In the present case, looking at the whole contract, we find that the parties contracted on the basis of the continued existence of the Music Hall at the time when the concerts were to be given; that being essential to their performance.

10. We think, therefore, that the Music Hall having ceased to exist, without fault of either party, both parties are excused, the plaintiffs from taking the gardens and paying the money, the defendants from performing their promise to give the use of the Hall and Gardens and other things. Consequently the rule must be absolute to enter the verdict for the defendants.
11. Rule absolute.

Sherwood v. Walker

Supreme Court of Michigan
66 Mich. 568, 33 N.W. 919 (1887)

MORSE, J.

1. Replevin for a cow. Suit commenced in justice's court; judgment for plaintiff; appealed to circuit court of Wayne county, and verdict and judgment for plaintiff in that court. The defendants bring error, and set out 25 assignments of the same.
2. The main controversy depends upon the construction of a contract for the sale of the cow. The plaintiff claims that the title passed, and bases his action upon such claim. The defendants contend that the contract was executory, and by its terms no title to the animal was acquired by plaintiff. The defendants reside at Detroit, but are in business at Walkerville, Ontario, and have a farm at Greenfield, in Wayne county, upon which were some blooded cattle supposed to be barren as breeders. The Walkers are importers and breeders of polled Angus cattle. The plaintiff is a banker living at Plymouth, in Wayne county. He called upon the defendants at Walkerville for the purchase of some of their stock, but found none there that suited him. Meeting one of the defendants afterwards, he was informed that they had a few head upon their Greenfield farm. He was asked to go out and look at them, with the statement at the time that they were probably barren, and would not breed. May 5, 1886, plaintiff went out to Greenfield, and saw the cattle. A few days thereafter, he called upon one of the defendants with the view of purchasing a cow, known as "Rose 2d of Aberlone." After considerable talk, it was agreed that defendants would telephone Sherwood at his home in Plymouth in reference to the price. The second morning after this talk he was called up by telephone, and the terms of the sale were finally agreed upon. He was to pay five and one-half cents per pound, live weight, fifty pounds shrinkage. He was asked how he intended to take the cow home, and replied that he might ship her from King's cattle-yard. He requested defendants to confirm the sale in writing, which they did by sending him the following letter:

WALKERVILLE, May 15, 1886.

T.C. Sherwood, President, etc.-DEAR SIR: We confirm sale to you of the cow Rose 2d of Aberlone, lot 56 of our catalogue, at five and half cents per pound, less fifty pounds shrink. We inclose herewith order on Mr. Graham

for the cow. You might leave check with him, or mail to us here, as you prefer.

Yours, truly, HIRAM WALKER & SONS.

The order upon Graham inclosed in the letter read as follows:

WALKERVILLE, May 15, 1886.

George Graham: You will please deliver at King's cattle-yard to Mr. T.C. Sherwood, Plymouth, the cow Rose 2d of Aberlone, lot 56 of our catalogue. Send halter with the cow, and have her weighed.

Yours truly, HIRAM WALKER & SONS.

3. On the twenty-first of the same month the plaintiff went to defendants' farm at Greenfield, and presented the order and letter to Graham, who informed him that the defendants had instructed him not to deliver the cow. Soon after, the plaintiff tendered to Hiram Walker, one of the defendants, \$80, and demanded the cow. Walker refused to take the money or deliver the cow. The plaintiff then instituted this suit. After he had secured possession of the cow under the writ of replevin, the plaintiff caused her to be weighed by the constable who served the writ, at a place other than King's cattle-yard. She weighed 1,420 pounds.
4. When the plaintiff, upon the trial in the circuit court, had submitted his proofs showing the above transaction, defendants moved to strike out and exclude the testimony from the case, for the reason that it was irrelevant and did not tend to show that the title to the cow passed, and that it showed that the contract of sale was merely executory. The court refused the motion, and an exception was taken. The defendants then introduced evidence tending to show that at the time of the alleged sale it was believed by both the plaintiff and themselves that the cow was barren and would not breed; that she cost \$850, and if not barren would be worth from \$750 to \$1,000; that after the date of the letter, and the order to Graham, the defendants were informed by said Graham that in his judgment the cow was with calf, and therefore they instructed him not to deliver her to plaintiff, and on the twentieth of May, 1886, telegraphed plaintiff what Graham thought about the cow being with calf, and that consequently they could not sell her. The cow had a calf in the month of October following. On the nineteenth of May, the plaintiff wrote Graham as follows:

PLYMOUTH, May 19, 1886.

Mr. George Graham, Greenfield-DEAR SIR: I have bought Rose or Lucy from Mr. Walker, and will be there for her Friday morning, nine or ten o'clock. Do not water her in the morning.

Yours, etc., T.C. SHERWOOD.

5. Plaintiff explained the mention of the two cows in this letter by testifying that, when he wrote this letter, the order and letter of defendants was at his home, and, writing in a hurry, and being uncertain as to the name of the cow, and not wishing his cow watered, he thought it would do no harm to name them both, as his bill of sale would show which one he had purchased. Plaintiff also testified that he asked defendants to give him a price on the balance of their herd at Greenfield, as a friend thought of buying some, and received a letter dated May 17, 1886, in which they named the price of five cattle, including Lucy, at \$90, and Rose 2d at \$80. When he received the letter he called defendants up by telephone, and asked them why they put Rose 2d in the list, as he had already purchased her. They replied that they knew he had, but thought it would make no difference if plaintiff and his friend concluded to take the whole herd.
6. The foregoing is the substance of all the testimony in the case.
7. The circuit judge instructed the jury that if they believed the defendants, when they sent the order and letter to plaintiff, meant to pass the title to the cow, and that the cow was intended to be delivered to plaintiff, it did not matter whether the cow was weighed at any particular place, or by any particular person; and if the cow was weighed afterwards, as Sherwood testified, such weighing would be a sufficient compliance with the order. If they believed that defendants intended to pass the title by writing, it did not matter whether the cow was weighed before or after suit brought, and the plaintiff would be entitled to recover. The defendants submitted a number of requests which were refused. The substance of them was that the cow was never delivered to plaintiff, and the title to her did not pass by the letter and order; and that under the contract, as evidenced by these writings, the title did not pass until the cow was weighed and her price thereby determined; and that, if the defendants only agreed to sell a cow that would not breed, then the barrenness of the cow was a condition precedent to passing title, and plaintiff cannot recover. The court also charged the jury that it was immaterial whether the cow was with calf or not. It will

therefore be seen that the defendants claim that, as a matter of law, the title of this cow did not pass, and that the circuit judge erred in submitting the case to the jury, to be determined by them, upon the intent of the parties as to whether or not the title passed with the sending of the letter and order by the defendants to the plaintiff.

[Paragraphs 8-13 discuss the comparatively arcane (and now archaic) issue of passing legal title to the cow. This portion of the opinion is not central to understanding mistake doctrine and thus you may feel free to skim until you reach paragraph 14.]

8. This question as to the passing of title is fraught with difficulties, and not always easy of solution. An examination of the multitude of cases bearing upon this subject, with their infinite variety of facts, and at least apparent conflict of law, oftentimes tends to confuse rather than to enlighten the mind of the inquirer. It is best, therefore, to consider always, in cases of this kind, the general principles of the law, and then apply them as best we may to the facts of the case in hand.
9. The cow being worth over \$50, the contract of sale, in order to be valid, must be one where the purchaser has received or accepted part of the goods, or given something in earnest, or in part payment, or where the seller has signed some note or memorandum in writing. How.St. § 6186. Here there was no actual delivery, nor anything given in payment or in earnest, but there was a sufficient memorandum signed by the defendants to take the case out of the statute, if the matter contained in such memorandum is sufficient to constitute a completed sale. It is evident from the letter that the payment of the purchase price was not intended as a condition precedent to the passing of the title. Mr. Sherwood is given his choice to pay the money to Graham at King's cattle-yards, or to send check by mail.
10. Nor can there be any trouble about the delivery. The order instructed Graham to deliver the cow, upon presentation of the order, at such cattle-yards. But the price of the cow was not determined upon to a certainty. Before this could be ascertained, from the terms of the contract, the cow had to be weighed; and, by the order inclosed with the letter, Graham was instructed to have her weighed. If the cow had been weighed, and this letter had stated, upon such weight, the express and exact price of the animal, there can be no doubt but the cow would have passed with the sending and receipt of the letter and order by the plaintiff. Payment was not to be a concurrent act with the delivery, and therein this case differs from *Case v. Dewey*, 55 Mich. 116,

20 N.W.Rep. 817, and 21 N.W.Rep. 911. Also, in that case, there was no written memorandum of the sale, and a delivery was necessary to pass the title of the sheep; and it was held that such delivery could only be made by a surrender of the possession to the vendee, and an acceptance by him. Delivery by an actual transfer of the property from the vendor to the vendee, in a case like the present, where the article can easily be so transferred by a manual act, is usually the most significant fact in the transaction to show the intent of the parties to pass the title, but it never has been held conclusive. Neither the actual delivery, nor the absence of such delivery, will control the case, where the intent of the parties is clear and manifest that the matter of delivery was not a condition precedent to the passing of the title, or that the delivery did not carry with it the absolute title. The title may pass, if the parties so agree, where the statute of frauds does not interpose without delivery, and property may be delivered with the understanding that the title shall not pass until some condition is performed.

11. And whether the parties intended the title should pass before delivery or not is generally a question of fact to be determined by a jury. In the case at bar the question of the intent of the parties was submitted to the jury. This submission was right, unless from the reading of the letter and the order, and all the facts of the oral bargaining of the parties, it is perfectly clear, as a matter of law, that the intent of the parties was that the cow should be weighed, and the price thereby accurately determined, before she should become the property of the plaintiff. I do not think that the intent of the parties in this case is a matter of law, but one of fact. The weighing of the cow was not a matter that needed the presence or any act of the defendants, or any agent of theirs, to be well or accurately done. It could make no difference where or when she was weighed, if the same was done upon correct scales, and by a competent person. There is no pretense but what her weight was fairly ascertained by the plaintiff. The cow was specifically designated by this writing, and her delivery ordered, and it cannot be said, in my opinion, that the defendants intended that the weighing of the animal should be done before the delivery even, or the passing of title. The order to Graham is to deliver her, and then follows the instruction, not that he shall weigh her himself, or weigh her, or even have her weighed, before delivery, but simply, "Send halter with the cow, and have her weighed."
12. It is evident to my mind that they had perfect confidence in the integrity and responsibility of the plaintiff, and that they considered the sale perfected and completed when they mailed the letter and order to plaintiff. They did not intend to

place any conditions precedent in the way, either of payment of the price, or the weighing of the cow, before the passing of the title. They cared not whether the money was paid to Graham, or sent to them afterwards, or whether the cow was weighed before or after she passed into the actual manual grasp of the plaintiff. The refusal to deliver the cow grew entirely out of the fact that, before the plaintiff called upon Graham for her, they discovered she was not barren, and therefore of greater value than they had sold her for.

13. The following cases in this court support the instruction of the court below as to the intent of the parties governing and controlling the question of a completed sale, and the passing of title: *Lingham v. Eggleston*, 27 Mich. 324; *Wilkinson v. Holiday*, 33 Mich. 386; *Grant v. Merchants' & Manufacturers' Bank*, 35 Mich. 527; *Carpenter v. Graham*, 42 Mich. 194, 3 N.W.Rep. 974; *Brewer v. Michigan Salt Ass'n*, 47 Mich. 534, 11 N.W.Rep. 370; *Whitcomb v. Whitney*, 24 Mich. 486; *Byles v. Colier*, 54 Mich. 1, 19 N.W.Rep. 565; *Scotten v. Sutter*, 37 Mich. 527, 532; *Ducey Lumber Co. v. Lane*, 58 Mich. 520, 525, 25 N.W.Rep. 568; *Jenkinson v. Monroe*, 28 N.W.Rep. 663.
14. It appears from the record that both parties supposed this cow was barren and would not breed, and she was sold by the pound for an insignificant sum as compared with her real value if a breeder. She was evidently sold and purchased on the relation of her value for beef, unless the plaintiff had learned of her true condition, and concealed such knowledge from the defendants. Before the plaintiff secured the possession of the animal, the defendants learned that she was with calf, and therefore of great value, and undertook to rescind the sale by refusing to deliver her. The question arises whether they had a right to do so. The circuit judge ruled that this fact did not avoid the sale and it made no difference whether she was barren or not. I am of the opinion that the court erred in this holding. I know that this is a close question, and the dividing line between the adjudicated cases is not easily discerned. But it must be considered as well settled that a party who has given an apparent consent to a contract of sale may refuse to execute it, or he may avoid it after it has been completed, if the assent was founded, or the contract made, upon the mistake of a material fact—such as the subject-matter of the sale, the price, or some collateral fact materially inducing the agreement; and this can be done when the mistake is mutual. 1 Benj. Sales, §§ 605, 606; Leake, Cont. 339; Story, Sales, (4th Ed.) §§ 377, 148. See, also, *Cutts v. Guild*, 57 N.Y. 229; *Harvey v. Harris*, 112 Mass. 32; *Gardner v. Lane*, 9 Allen, 492, 12 Allen, 44; *Huthmacher v. Harris' Adm'rs*, 38 Pa.St. 491; *Byers v.*

Chapin, 28 Ohio St. 300; *Gibson v. Pelkie*, 37 Mich. 380, and cases cited; *Allen v. Hammond*, 11 Pet. 63-71.

15. If there is a difference or misapprehension as to the substance of the thing bargained for; if the thing actually delivered or received is different in substance from the thing bargained for, and intended to be sold—then there is no contract; but if it be only a difference in some quality or accident, even though the mistake may have been the actuating motive to the purchaser or seller, or both of them, yet the contract remains binding. “The difficulty in every case is to determine whether the mistake or misapprehension is as to the substance of the whole contract, going, as it were, to the root of the matter, or only to some point, even though a material point, an error as to which does not affect the substance of the whole consideration.” *Kennedy v. Panama, etc., Mail Co.*, L.R. 2 Q.B. 580, 587. It has been held, in accordance with the principles above stated, that where a horse is bought under the belief that he is sound, and both vendor and vendee honestly believe him to be sound, the purchaser must stand by his bargain, and pay the full price, unless there was a warranty.
16. It seems to me, however, in the case made by this record, that the mistake or misapprehension of the parties went to the whole substance of the agreement. If the cow was a breeder, she was worth at least \$750; if barren, she was worth not over \$80. The parties would not have made the contract of sale except upon the understanding and belief that she was incapable of breeding, and of no use as a cow. It is true she is now the identical animal that they thought her to be when the contract was made; there is no mistake as to the identity of the creature. Yet the mistake was not of the mere quality of the animal, but went to the very nature of the thing. A barren cow is substantially a different creature than a breeding one. There is as much difference between them for all purposes of use as there is between an ox and a cow that is capable of breeding and giving milk. If the mutual mistake had simply related to the fact whether she was with calf or not for one season, then it might have been a good sale, but the mistake affected the character of the animal for all time, and for its present and ultimate use. She was not in fact the animal, or the kind of animal, the defendants intended to sell or the plaintiff to buy. She was not a barren cow, and, if this fact had been known, there would have been no contract. The mistake affected the substance of the whole consideration, and it must be considered that there was no contract to sell or sale of the cow as she actually was. The thing sold and bought had in fact no existence. She was sold as a beef creature would be sold; she is in fact a breeding cow, and a valuable one. The court should have instructed the jury that if

they found that the cow was sold, or contracted to be sold, upon the understanding of both parties that she was barren, and useless for the purpose of breeding, and that in fact she was not barren, but capable of breeding, then the defendants had a right to rescind, and to refuse to deliver, and the verdict should be in their favor.

17. The judgment of the court below must be reversed, and a new trial granted, with costs of this court to defendants.

CAMPBELL, C.J., and CHAMPLIN, J., concurred.

SHERWOOD, J., [*who, despite his name, is unrelated to the plaintiff*] (dissenting)

18. I do not concur in the opinion given by my brethren in this case. I think the judgments before the justice and at the circuit were right. I agree with my Brother MORSE that the contract made was not within the statute of frauds, and the payment for the property was not a condition precedent to the passing of the title from the defendants to the plaintiff. And I further agree with him that the plaintiff was entitled to a delivery of the property to him when the suit was brought, unless there was a mistake made which would invalidate the contract, and I can find no such mistake. There is no pretense there was any fraud or concealment in the case, and an intimation or insinuation that such a thing might have existed on the part of either of the parties would undoubtedly be a greater surprise to them than anything else that has occurred in their dealings or in the case.
19. As has already been stated by my brethren, the record shows that the plaintiff is a banker and farmer as well, carrying on a farm, and raising the best breeds of stock, and lived in Plymouth, in the county of Wayne, 23 miles from Detroit; that the defendants lived in Detroit, and were also dealers in stock of the higher grades; that they had a farm at Walkerville, in Canada, and also one in Greenfield in said county of Wayne, and upon these farms the defendants kept their stock. The Greenfield farm was about 15 miles from the plaintiff's. In the spring of 1886 the plaintiff, learning that the defendants had some "polled Angus cattle" for sale, was desirous of purchasing some of that breed, and meeting the defendants, or some of them, at Walkerville, inquired about them, and was informed that they had none at Walkerville, "but had a few head left on their farm in Greenfield, and asked the plaintiff to go and see them, stating that in all probability they were sterile and would not breed." In accordance with said request, the plaintiff, on the fifth day of May,

went out and looked at the defendants' cattle at Greenfield, and found one called "Rose, Second," which he wished to purchase, and the terms were finally agreed upon at five and a half cents per pound, live weight, 50 pounds to be deducted for shrinkage. The sale was in writing, and the defendants gave an order to the plaintiff directing the man in charge of the Greenfield farm to deliver the cow to plaintiff. This was done on the fifteenth of May. On the twenty-first of May plaintiff went to get his cow, and the defendants refused to let him have her; claiming at the time that the man in charge at the farm thought the cow was with calf, and, if such was the case, they would not sell her for the price agreed upon. The record further shows that the defendants, when they sold the cow, believed the cow was not with calf, and barren; that from what the plaintiff had been told by defendants (for it does not appear he had any other knowledge or facts from which he could form an opinion) he believed the cow was farrow, but still thought she could be made to breed. The foregoing shows the entire interview and treaty between the parties as to the sterility and qualities of the cow sold to the plaintiff. The cow had a calf in the month of October.

20. There is no question but that the defendants sold the cow representing her of the breed and quality they believed the cow to be, and that the purchaser so understood it. And the buyer purchased her believing her to be of the breed represented by the sellers, and possessing all the qualities stated, and even more. He believed she would breed. There is no pretense that the plaintiff bought the cow for beef, and there is nothing in the record indicating that he would have bought her at all only that he thought she might be made to breed. Under the foregoing facts—and these are all that are contained in the record material to the contract—it is held that because it turned out that the plaintiff was more correct in his judgment as to one quality of the cow than the defendants, and a quality, too, which could not by any possibility be positively known at the time by either party to exist, the contract may be annulled by the defendants at their pleasure. I know of no law, and have not been referred to any, which will justify any such holding, and I think the circuit judge was right in his construction of the contract between the parties.
21. It is claimed that a mutual mistake of a material fact was made by the parties when the contract of sale was made. There was no warranty in the case of the quality of the animal. When a mistaken fact is relied upon as ground for rescinding, such fact must not only exist at the time the contract is made, but must have been known to one or both of the parties. Where there is no warranty, there can be no mistake of fact when no such fact exists, or, if in existence, neither party knew of it, or could know of it;

and that is precisely this case. If the owner of a Hambletonian horse had speeded him, and was only able to make him go a mile in three minutes, and should sell him to another, believing that was his greatest speed, for \$300, when the purchaser believed he could go much faster, and made the purchase for that sum, and a few days thereafter, under more favorable circumstances, the horse was driven a mile in 2 min. 16 sec., and was found to be worth \$20,000, I hardly think it would be held, either at law or in equity, by any one, that the seller in such case could rescind the contract. The same legal principles apply in each case.

22. In this case neither party knew the actual quality and condition of this cow at the time of the sale. The defendants say, or rather said, to the plaintiff, “they had a few head left on their farm in Greenfield, and asked plaintiff to go and see them, stating to plaintiff that in all probability they were sterile and would not breed.” Plaintiff did go as requested, and found there these cows, including the one purchased, with a bull. The cow had been exposed, but neither knew she was with calf or whether she would breed. The defendants thought she would not, but the plaintiff says that he thought she could be made to breed, but believed she was not with calf. The defendants sold the cow for what they believed her to be, and the plaintiff bought her as he believed she was, after the statements made by the defendants. No conditions whatever were attached to the terms of sale by either party. It was in fact as absolute as it could well be made, and I know of no precedent as authority by which this court can alter the contract thus made by these parties in writing—interpolate in it a condition by which, if the defendants should be mistaken in their belief that the cow was barren, she could be returned to them and their contract should be annulled. It is not the duty of courts to destroy contracts when called upon to enforce them, after they have been legally made. There was no mistake of any material fact by either of the parties in the case as would license the vendors to rescind. There was no difference between the parties, nor misapprehension, as to the substance of the thing bargained for, which was a cow supposed to be barren by one party, and believed not to be by the other. As to the quality of the animal, subsequently developed, both parties were equally ignorant, and as to this each party took his chances. If this were not the law, there would be no safety in purchasing this kind of stock.
23. I entirely agree with my brethren that the right to rescind occurs whenever “the thing actually delivered or received is different in substance from the thing bargained for, and intended to be sold; but if it be only a difference in some quality or accident, even though the misapprehension may have been the actuating motive” of the parties in

making the contract, yet it will remain binding. In this case the cow sold was the one delivered. What might or might not happen to her after the sale formed no element in the contract. The case of *Kennedy v. Panama Mail Co.*, L.R. 2 Q.B. 587, and the extract cited therefrom in the opinion of my brethren, clearly sustains the views I have taken. See, also, *Smith v. Hughes*, L.R. 6 Q.B. 597; *Carter v. Crick*, 4 Hurl. & N. 416.

24. According to this record, whatever the mistake was, if any, in this case, it was upon the part of the defendants, and while acting upon their own judgment. It is, however, elementary law, and very elementary, too, “that the mistaken party, without any common understanding with the other party in the premises as to the quality of an animal, is remediless if he is injured through his own mistake.” Leake, Cont. 338; *Torrance v. Bolton*, L.R. 8 Ch. 118; *Smith v. Hughes*, L.R. 6 Q.B. 597.
25. The case cited by my brethren from 37 Mich. I do not think sustains the conclusion reached by them. In that case the subject-matter about which the contract was made had no existence, and in such case Mr. Justice GRAVES held there was no contract; and to the same effect are all the authorities cited in the opinion. That is certainly not this case. Here the defendants claim the subject-matter not only existed, but was worth about \$800 more than the plaintiff paid for it.
26. The case of *Huthmacher v. Harris*, 38 Pa. St. 491, is this: A party purchased at an administrator's sale a drill-machine, which had hid away in it by the deceased a quantity of notes, to the amount of \$3,000, money to the amount of over \$500, and two silver watches and a pocket compass of the value of \$60.25. In an action of trover for the goods, it was held that nothing but the machine was sold or passed to the purchasers, neither party knowing that the machine contained any such articles.
27. In *Cutts v. Guild*, 57 N.Y. 229, the defendant, as assignee, recovered a judgment against D. & H. He also recovered several judgments in his own name on behalf of the T. Co. The defendant made an assignment of and transferred the first judgment to an assignee of the plaintiff—both parties supposing and intending to transfer one of the T. Co. judgments—and it was held that such contract of assignment was void, because the subject-matter contained in the assignment was not contracted for.
28. In the case of *Byers v. Chapin*, 28 Ohio St. 300, the defendant sold the plaintiffs 5,000 oil barrels. The plaintiffs paid \$5,000 upon their purchase, and took some of the barrels. The barrels proved to be unfit for use, and the contract was rescinded by

consent of the parties. The defendant, instead of returning all the money paid to the purchaser, retained a portion and gave plaintiffs his note for the remainder. The plaintiffs brought suit upon this note. The defendant claimed that, under the contract of sale of the barrels, they were to be glued by the plaintiffs, which the plaintiffs properly failed to do, and this fact was not known to defendant when he agreed to rescind, and gave the note, and therefore the note was given upon a mistaken state of facts, falsely represented to the defendant, and which were known to the plaintiffs. On the proofs, the jury found for the defendant, and the verdict was affirmed.

29. In *Gardner v. Lane*, 9 Mass. 492, it is decided that if, upon a sale of No. 1 mackerel, the vendor delivers No. 3 mackerel, and some barrels of salt, no title to the articles thus delivered passes.
30. *Allen v. Hammond*, 11 Pet. 63, decides that if a life-estate in land is sold, and at the time of the sale the estate is terminated by the death of the person in whom the right vested, a court of equity will rescind the purchase.
31. In *Harvey v. Harris*, 112 Mass. 32, at an auction, two different grades of flour were sold, and a purchaser of the second claimed to have bought a quantity of the first grade, under a sale made of the second, and this he was not allowed to do, because of the mutual mistake; the purchaser had not in fact bought the flour he claimed. In this case, however, it is said it is true that, if there is a mutual agreement of the parties for the sale of particular articles of property, a mistake of misapprehension as to the quality of the articles will not enable the vendor to repudiate the sale.
32. The foregoing are all the authorities relied on as supporting the positions taken by my brethren in this case. I fail to discover any similarity between them and the present case; and I must say, further, in such examination as I have been able to make, I have found no adjudicated case going to the extent, either in law or equity, that has been held in this case. In this case, if either party had superior knowledge as to the qualities of this animal to the other, certainly the defendants had such advantage. I understand the law to be well settled that “there is no breach of any implied confidence that one party will not profit by his superior knowledge as to facts and circumstances” actually within the knowledge of both, because neither party reposes in any such confidence unless it be specially tendered or required, and that a general sale does not imply warranty of any quality, or the absence of any; and if the seller represents to the purchaser what he himself believes as to the qualities of an animal, and the purchaser

buys relying upon his own judgment as to such qualities, there is no warranty in the case, and neither has a cause of action against the other if he finds himself to have been mistaken in judgment.

33. The only pretense for avoiding this contract by the defendants is that they erred in judgment as to the qualities and value of the animal. I think the principles adopted by Chief Justice CAMPBELL in *Williams v. Spurr* completely cover this case, and should have been allowed to control in its decision. See 24 Mich. 335. See, also, Story, Sales, §§ 174, 175, 382, and Benj. Sales, § 430. The judgment should be affirmed.

Anderson Brothers Corp. v. O'Meara

United States Court of Appeals, Fifth Circuit
306 F.2d 672 (1962)

JONES, Circuit Judge.

1. The appellant, Anderson Brothers Corporation, a Texas corporation engaged in the business of constructing pipelines, sold a barge dredge to the appellee, Robert W. O'Meara, a resident of Illinois who is an oil well driller doing business in several states and Canada. The appellee brought this suit seeking rescission of the sale or, in the alternative, damages. After trial without a jury, the appellee's prayer of rescission was denied, but damages were awarded. The court denied the appellant's counterclaim for the unpaid purchase price of the dredge. Both parties have appealed.¹ Appellant contends that no relief should have been given to the appellee, and the appellee contends that the damages awarded to him were insufficient.
2. The dredge which the appellant sold to the appellee was specially designed to perform the submarine trenching necessary for burying a pipeline under water. In particular it was designed to cut a relatively narrow trench in areas where submerged rocks, stumps and logs might be encountered. The dredge could be disassembled into its larger component parts, moved over land by truck, and reassembled at the job site. The appellant built the dredge from new and used parts in its own shop. The design was copied from a dredge which appellant had leased and successfully used in laying a pipeline across the Mississippi River. The appellant began fabrication of the dredge in early 1955, intending to use it in performing a contract for laying a pipeline across the Missouri River. A naval architect testified that the appellant was following customary practice in pipeline operations by designing a dredge for a specific use. Dredges so designed can be modified, if necessary, to meet particular situations. For some reason construction of the dredge was not completed in time for its use on the job for which it was intended, and the dredge was never used by the appellant. After it was completed, the dredge was advertised for sale in a magazine. This advertisement came to the appellee's attention in early December, 1955. The appellee wanted to acquire a dredge capable of digging canals fifty to seventy-five or eighty feet wide

¹ Anderson Brothers Corporation will be referred to as the appellant and O'Meara as the appellee.

and six to twelve feet deep to provide access to off-shore oil well sites in southern Louisiana.

3. On December 8, 1955, the appellee or someone employed by him contacted the appellant's Houston, Texas, office by telephone and learned that the price of the dredge was \$45,000. Terms of sale were discussed, and later that day the appellant sent a telegram to the appellee who was then in Chicago, saying it accepted the appellee's offer of \$35,000 for the dredge to be delivered in Houston. The appellee's offer was made subject to an inspection. The next day Kennedy, one of the appellee's employees, went to Houston from New Orleans and inspected the dredge. Kennedy, it appears, knew nothing about dredges but was familiar with engines. After inspecting the engines of the dredge, Kennedy reported his findings to the appellee by telephone and then signed an agreement with the appellant on behalf of the appellee. In the agreement, the appellant acknowledged receipt of \$17,500. The agreement made provision for payment of the remaining \$17,500 over a period of seventeen months. The dredge was delivered to the appellee at Houston on December 11, 1955, and from there transported by the appellee to his warehouse in southern Louisiana. The barge was transported by water, and the ladder, that part of the dredge which extends from the barge to the stream bed and to which the cutting devices are attached, was moved by truck. After the dredge arrived at his warehouse the appellee executed a chattel mortgage in favor of the appellant and a promissory note payable to the order of the appellant. A bill of sale dated December 17, 1955, was given the appellee in which the appellant warranted only title and freedom from encumbrances. Both the chattel mortgage and the bill of sale described the dredge and its component parts in detail.
4. The record contains much testimony concerning the design and capabilities of the dredge including that of a naval architect who, after surveying the dredge, reported "I found that the subject dredge...had been designed for the purpose of dredging a straight trench over a river, lake or other body of water." The testimony shows that a dredge designed to perform sweep dredging, the term used to describe the dredging of a wide channel, must be different in several respects from one used only for trenching operations. The naval architect's report listed at least five major items to be replaced, modified, or added before the dredge would be suited to the appellee's intended use. It is clear that the appellee bought a dredge which, because of its design, was incapable, without modification, of performing sweep dredging.

5. On July 10, 1956, about seven months after the sale and after the appellee had made seven monthly payments pursuant to the agreement between the parties, the appellee's counsel wrote the appellant stating in part that "Mr. O'Meara has not been able to put this dredge in service and it is doubtful that it will ever be usable in its present condition." After quoting at length from the naval architect's report, which was dated January 28, 1956, the letter suggested that the differences between the parties could be settled amicably by the appellant's contributing \$10,000 toward the estimated \$12,000 to \$15,000 cost of converting the trenching dredge into a sweep dredge. The appellant rejected this offer and on July 23, 1956, the appellee's counsel wrote the appellant tendering return of the dredge and demanding full restitution of the purchase price. This suit followed the appellant's rejection of the tender and demand.
6. In his complaint the appellee alleged breaches of expressed and implied warranty and fraudulent representations as to the capabilities of the dredge. By an amendment he alleged as an alternative to the fraud count that the parties had been mistaken in their belief as to the operations of which the dredge was capable, and thus there was a mutual mistake which prevented the formation of a contract. The appellee sought damages of over \$29,000, representing the total of principal and interest paid the appellant and expenses incurred in attempting to operate the dredge. In the alternative, the appellee asked for rescission and restitution of all money expended by him in reliance on the contract. The appellant answered denying the claims of the appellee and counterclaiming for the unpaid balance.
7. The district court found that:

At the time the dredge was sold by the defendant to the plaintiff, the dredge was not capable for performing sweep dredging operations in shallow water, unless it was modified extensively. Defendant had built the dredge and knew the purpose for which it was designed and adapted. None of the defendant's officers or employees knew that plaintiff intended to use the dredge for shallow sweep dredging operations. Gier (an employee of the appellant who talked with the appellee or one of his employees by telephone) mistakenly assumed that O'Meara intended to use the dredge within its designed capabilities.

At the time the plaintiff purchased this dredge he mistakenly believed that the dredge was capable without modification of performing sweep dredging operations in shallow water.

8. The court further found that the market value of the dredge on the date of sale was \$24,000, and that the unpaid balance on the note given for part of the purchase price was \$10,500. Upon its findings the court concluded that:

The mistake that existed on the part of both plaintiff and defendant with respect to the capabilities of the subject dredge is sufficient to and does constitute mutual mistake, and the plaintiff is entitled to recover the damages he has suffered as a result thereof.

9. These damages were found to be “equal to the balance due on the purchase price” plus interest, and were assessed by cancellation of the note and chattel mortgage and vesting title to the barge in the appellee free from any encumbrance in favor of the appellant. The court also concluded that the appellee was “not entitled to rescission of this contract.” Further findings and conclusions, which are not challenged in this Court, eliminate any considerations of fraud or breach of expressed or implied warranties. The judgment for damages rests entirely upon the conclusion of mutual mistake.² The district court's conclusion that the parties were mutually mistaken “with respect to the capabilities of the subject dredge” is not supported by its findings. “A mutual mistake is one common to both parties to the contract, each laboring under the same misconception.” *St. Paul Fire & Marine Insurance Co. v. Culwell*, Tex.Com.App., 62 S.W.2d 100; *Hayman v. Dowda*, Tex.Civ.App., 233 S.W.2d 466; *Bryan v. Dallas National Bank*, Tex.Civ.App., 135 S.W.2d 249; 58 C.J.S. Mistake, p. 832. The appellee's mistake in believing that the dredge was capable, without modification, of performing sweep dredging was not a mistake shared by the appellant, who had designed and built the dredge for use in trenching operations and knew its capabilities. The mistake on the part of the appellant's employee in assuming that the appellee intended to use the dredge within its designed capabilities was certainly not one shared by the appellee, who acquired the dredge for use in sweep dredging operations. The appellee alone was mistaken in assuming that the dredge was adapted, without modification, to the use he had in mind.
10. The appellee insists that even if the findings do not support a conclusion of mutual mistake, he is entitled to relief under the well-established doctrine that knowledge by one party to a contract that the other is laboring under a mistake concerning the

² The disposition of this appeal does not require a review of the district court's action in awarding damages as a remedy for mutual mistake rather than granting rescission and attempting restoration of the *status quo ante*.

subject matter of the contract renders it voidable by the mistaken party.³ See 3 Corbin, Contracts 692, § 610. As a predicate to this contention, the appellee urges that the trial court erred in finding that “None of defendant's officers or employees knew that plaintiff intended to use the dredge for shallow sweep dredging operations.” Moreover, the appellee contends that the appellant's knowledge of his intended use of the dredge was conclusively established by the testimony of two of the appellant's employees, because, on the authority of *Griffin v. Superior Insurance Co.*, 161 Tex. 195, 338 S.W.2d 415, this testimony constitutes admissions, conclusive against the appellant. In the *Griffin* case, it was held that a party's testimony must be “deliberate, clear and unequivocal” before it is conclusive against him. The testimony on which the appellee relies falls short of being “clear and unequivocal.” If the statement of one witness were taken as conclusive, it would not establish that he knew the appellee intended to use the dredge as a sweep dredge,⁴ and the other witness spoke with incertitude.⁵ The testimony is not conclusive and is only one factor to be considered by the finder of facts. See 9 Wigmore, Evidence (3d Ed.) 397, 2594a.

³The appellee does not complain of the district court's conclusion that he was not entitled to rescission. He urges, without citation of authority, that the relief to which he is entitled is by way of damages.

⁴Gier, the appellant's shop foreman, testified:

Q. Did Mr. O'Meara in the telephone conversation tell you what business he was in?

A. No, he didn't.

Q. He didn't. Mr. Gier, I suppose you have already answered this. Did he say what he wanted that dredge for?

Q. Now, did he (Kennedy) discuss with you what the dredge was going to be used for?

A. Other than he just said they was going to pump some channels out for some oil wells. That's all he said. He didn't tell me how deep or how wide or anything.

⁵Smith, the appellant's office manager, testified:

Q.Did you all discuss anything about the dredge itself?

A. No, not that I recall.

Q. In other words-

A. I do vaguely remember him (Kennedy) mentioning to me that O'Meara had an island over there and had some oil wells on it. He was going to use this dredge to they had been hiring someone else to do the dredging into well locations, and that's what he intended using this one for, to dredge into his well locations, and I don't remember now how much he said it cost, but as well as I remember, it was rather expensive for a subcontractor just to dredge back to one well location, but by owning their own dredge they would have a considerable saving there.

Q. In other words, he said they had to dredge out a channel so their drilling barge could get by?

A. Yes. So they could get the drilling barge or equipment in there. There wasn't any roads there. That's the impression I got.

11. There is a conflict in the evidence on the question of the appellant's knowledge of the appellee's intended use, and it cannot be held that the district court's finding is clearly erroneous. *Smith v. United States*, 5th Cir. 1961, 287 F.2d 299; *Levine v. Johnson*, 5th Cir. 1961, 287 F.2d 623; *Horton v. U.S. Steel Corp.*, 5th Cir. 1961, 286 F.2d 710. It is to be noted that the trial court before whom the appellee testified, did not credit his testimony that he had made a telephone call in which, he said, he personally informed an employee of the appellant of his plans for the use of the dredge.
12. The appellee makes a further contention that when he purchased the dredge he was laboring under a mistake so grave that allowing the sale to stand would be unconscionable. The ground urged is one which has apparently been recognized in some circumstances. *Edwards v. Trinity & B.V.R. Co.*, 54 Tex. Civ.App. 334, 118 S.W. 572; 13 Tex.Jur.2d 481, Contracts § 257; Annot., 59 A.L.R. 809. However, the Texas courts have held that when unilateral mistake is asserted as a ground for relief, the care which the mistaken complainant exercised or failed to exercise in connection with the transaction sought to be avoided is a factor for consideration. *Wheeler v. Holloway*, Tex.Com.App. 276 S.W. 653; *Ebberts v. Carpenter Production Co.*, Tex.Civ.App., 256 S.W.2d 601; *American Maid Flour Mills v. Lucia*, Tex.Civ.App., 285 S.W. 641; *Cole v. Kjellberg*, Tex.Civ.App., 141 S.W. 120; *Edwards v. Trinity & B.V.R. Co.*, supra; 13 Tex.Jur.2d 482, Contracts § 258. It has been stated that “though a court of equity will relieve against mistake, it will not assist a man whose condition is attributable to the want of due diligence which may be fairly expected from a reasonable person.” *American Maid Flour Mills v. Lucia*, supra. This is consistent with the general rule of equity that when a person does not avail himself of an opportunity to gain knowledge of the facts, he will not be relieved of the consequences of acting upon supposition. Annot., 1 A.L.R.2d 9, 89; see 30 C.J.S. Equity § 47, p. 376. Whether the mistaken party's negligence will preclude relief depends to a great extent upon the circumstances in each instance. *Edwards v. Trinity & B.V.R. Co.*, supra.
13. The appellee saw fit to purchase the dredge subject to inspection, yet he sent an employee to inspect it who he knew had no experience with or knowledge of dredging equipment. It was found that someone familiar with such equipment could have seen that the dredge was then incapable of performing channel type dredging. Although, according to his own testimony, the appellee was conscious of his own lack of knowledge concerning dredges, he took no steps, prior to purchase, to learn if the dredge which he saw pictured and described in some detail in the advertisement,

was suited to his purpose. Admittedly he did not even inquire as to the use the appellant had made or intended to make of the dredge, and the district court found that he did not disclose to the appellant the use he intended to make of the dredge. The finding is supported by evidence. The appellee did not attempt to obtain any sort of warranty as to the dredge's capabilities. The only conclusion possible is that the appellee exercised no diligence, prior to the purchase, in determining the uses to which the dredge might be put. Had he sent a qualified person, such as the naval architect whom he later employed, to inspect the dredge he would have learned that it was not what he wanted, or had even made inquiry, he would have been informed as to the truth or have had a cause of action for misrepresentation if he had been given misinformation and relied upon it. The appellee chose to act on assumption rather than upon inquiry or information obtained by investigation, and, having learned his assumption was wrong, he asks to be released from the resulting consequences on the ground that, because of his mistaken assumption, it would be unconscionable to allow the sale to stand. The appellee seeks this, although the court has found that the appellant was not guilty of any misrepresentation or fault in connection with the transaction.

14. The appellant is in the same position as the party seeking relief on the grounds of mistake in *Wheeler v. Holloway, supra*, and the same result must follow. In the *Wheeler* case it was held that relief should be denied where the mistaken party exercised 'no diligence whatever' in ascertaining the readily accessible facts before he entered into a contract.
15. The appellee should have taken nothing on his claim; therefore, it is unnecessary to consider the question raised by the cross-appeal. The other questions raised by the appellant need not be considered. The case must be reversed and remanded for further proceeding consistent with what we have here held.

Reversed and remanded.

Jacob & Youngs v. Kent

Court of Appeals of New York
230 N.Y. 239, 129 N.E. 889 (1921)

CARDOZO, J.

1. The plaintiff built a country residence for the defendant at a cost of upwards of \$77,000, and now sues to recover a balance of \$3,483.46, remaining unpaid. The work of construction ceased in June, 1914, and the defendant then began to occupy the dwelling. There was no complaint of defective performance until March, 1915. One of the specifications for the plumbing work provides that "all wrought iron pipe must be well galvanized, lap welded pipe of the grade known as 'standard pipe' of Reading manufacture." The defendant learned in March, 1915, that some of the pipe, instead of being made in Reading, was the product of other factories. The plaintiff was accordingly directed by the architect to do the work anew. The plumbing was then encased within the walls except in a few places where it had to be exposed. Obedience to the order meant more than the substitution of other pipe. It meant the demolition at great expense of substantial parts of the completed structure. The plaintiff left the work untouched, and asked for a certificate that the final payment was due. Refusal of the certificate was followed by this suit.
2. The evidence sustains a finding that the omission of the prescribed brand of pipe was neither fraudulent nor willful. It was the result of the oversight and inattention of the plaintiff's subcontractor. Reading pipe is distinguished from Cohoes pipe and other brands only by the name of the manufacturer stamped upon it at intervals of between six and seven feet. Even the defendant's architect, though he inspected the pipe upon arrival, failed to notice the discrepancy. The plaintiff tried to show that the brands installed, though made by other manufacturers, were the same in quality, in appearance, in market value and in cost as the brand stated in the contract—that they were, indeed, the same thing, though manufactured in another place. The evidence was excluded, and a verdict directed for the defendant. The Appellate Division reversed, and granted a new trial.
3. We think the evidence, if admitted, would have supplied some basis for the inference that the defect was insignificant in its relation to the project. The courts never say that one who makes a contract fills the measure of his duty by less than full performance.

They do say, however, that an omission, both trivial and innocent, will sometimes be atoned for by allowance of the resulting damage, and will not always be the breach of a condition to be followed by a forfeiture (*Spence v. Ham*, 163 N. Y. 220; *Woodward v. Fuller*, 80 N. Y. 312; *Glacius v. Black*, 67 N. Y. 563, 566; *Bowen v. Kimbell*, 203 Mass. 364, 370). The distinction is akin to that between dependent and independent promises, or between promises and conditions (Anson on Contracts [Corbin's ed.], sec. 367; 2 Williston on Contracts, sec. 842). Some promises are so plainly independent that they can never by fair construction be conditions of one another. (*Rosenthal Paper Co. v. Nat. Folding Box & Paper Co.*, 226 N. Y. 313; *Bogardus v. N. Y. Life Ins. Co.*, 101 N. Y. 328). Others are so plainly dependent that they must always be conditions. Others, though dependent and thus conditions when there is departure in point of substance, will be viewed as independent and collateral when the departure is insignificant (2 Williston on Contracts, secs. 841, 842; *Eastern Forge Co. v. Corbin*, 182 Mass. 590, 592; *Robinson v. Mollett*, L. R., 7 Eng. & Ir. App. 802, 814; *Miller v. Benjamin*, 142 N. Y. 613). Considerations partly of justice and partly of presumable intention are to tell us whether this or that promise shall be placed in one class or in another. The simple and the uniform will call for different remedies from the multifarious and the intricate. The margin of departure within the range of normal expectation upon a sale of common chattels will vary from the margin to be expected upon a contract for the construction of a mansion or a "skyscraper." There will be harshness sometimes and oppression in the implication of a condition when the thing upon which labor has been expended is incapable of surrender because united to the land, and equity and reason in the implication of a like condition when the subject-matter, if defective, is in shape to be returned. From the conclusion that promises may not be treated as dependent to the extent of their uttermost minutiae without a sacrifice of justice, the progress is a short one to the conclusion that they may not be so treated without a perversion of intention. Intention not otherwise revealed may be presumed to hold in contemplation the reasonable and probable. If something else is in view, it must not be left to implication. There will be no assumption of a purpose to visit venial faults with oppressive retribution.

4. Those who think more of symmetry and logic in the development of legal rules than of practical adaptation to the attainment of a just result will be troubled by a classification where the lines of division are so wavering and blurred. Something, doubtless, may be said on the score of consistency and certainty in favor of a stricter standard. The courts have balanced such considerations against those of equity and

fairness, and found the latter to be the weightier. The decisions in this state commit us to the liberal view, which is making its way, nowadays, in jurisdictions slow to welcome it (*Dakin & Co. v. Lee*, 1916, 1 K. B. 566, 579). Where the line is to be drawn between the important and the trivial cannot be settled by a formula. "In the nature of the case precise boundaries are impossible" (2 Williston on Contracts, sec. 841). The same omission may take on one aspect or another according to its setting. Substitution of equivalents may not have the same significance in fields of art on the one side and in those of mere utility on the other. Nowhere will change be tolerated, however, if it is so dominant or pervasive as in any real or substantial measure to frustrate the purpose of the contract (*Crouch v. Gutmann*, 134 N. Y. 45, 51). There is no general license to install whatever, in the builder's judgment, may be regarded as "just as good" (*Easthampton L. & C. Co., Ltd., v. Worthington*, 186 N. Y. 407, 412). The question is one of degree, to be answered, if there is doubt, by the triers of the facts (*Crouch v. Gutmann*; *Woodward v. Fuller, supra*), and, if the inferences are certain, by the judges of the law (*Easthampton L. & C. Co., Ltd., v. Worthington, supra*). We must weigh the purpose to be served, the desire to be gratified, the excuse for deviation from the letter, the cruelty of enforced adherence. Then only can we tell whether literal fulfilment is to be implied by law as a condition. This is not to say that the parties are not free by apt and certain words to effectuate a purpose that performance of every term shall be a condition of recovery. That question is not here. This is merely to say that the law will be slow to impute the purpose, in the silence of the parties, where the significance of the default is grievously out of proportion to the oppression of the forfeiture. The willful transgressor must accept the penalty of his transgression (*Schultze v. Goodstein*, 180 N. Y. 248, 251; *Desmond-Dunne Co. v. Friedman-Doscher Co.*, 162 N. Y. 486, 490). For him there is no occasion to mitigate the rigor of implied conditions. The transgressor whose default is unintentional and trivial may hope for mercy if he will offer atonement for his wrong (*Spence v. Ham, supra*).

5. In the circumstances of this case, we think the measure of the allowance is not the cost of replacement, which would be great, but the difference in value, which would be either nominal or nothing. Some of the exposed sections might perhaps have been replaced at moderate expense. The defendant did not limit his demand to them, but treated the plumbing as a unit to be corrected from cellar to roof. In point of fact, the plaintiff never reached the stage at which evidence of the extent of the allowance became necessary. The trial court had excluded evidence that the defect was

unsubstantial, and in view of that ruling there was no occasion for the plaintiff to go farther with an offer of proof. We think, however, that the offer, if it had been made, would not of necessity have been defective because directed to difference in value. It is true that in most cases the cost of replacement is the measure (*Spence v. Ham, supra*). The owner is entitled to the money which will permit him to complete, unless the cost of completion is grossly and unfairly out of proportion to the good to be attained. When that is true, the measure is the difference in value. Specifications call, let us say, for a foundation built of granite quarried in Vermont. On the completion of the building, the owner learns that through the blunder of a subcontractor part of the foundation has been built of granite of the same quality quarried in New Hampshire. The measure of allowance is not the cost of reconstruction. "There may be omissions of that which could not afterwards be supplied exactly as called for by the contract without taking down the building to its foundations, and at the same time the omission may not affect the value of the building for use or otherwise, except so slightly as to be hardly appreciable." (*Handy v. Bliss*, 204 Mass. 513, 519. *Cf. Foeller v. Heintz*, 137 Wis. 169, 178; *Oberlies v. Bullinger*, 132 N. Y. 598, 601; 2 Williston on Contracts, sec. 805, p. 1541) The rule that gives a remedy in cases of substantial performance with compensation for defects of trivial or inappreciable importance, has been developed by the courts as an instrument of justice. The measure of the allowance must be shaped to the same end.

6. The order should be affirmed, and judgment absolute directed in favor of the plaintiff upon the stipulation, with costs in all courts.

MCLAUGHLIN, J. (dissenting).

7. I dissent. The plaintiff did not perform its contract. Its failure to do so was either intentional or due to gross neglect which, under the uncontradicted facts, amounted to the same thing, nor did it make any proof of the cost of compliance, where compliance was possible.
8. Under its contract it obligated itself to use in the plumbing only pipe (between 2,000 and 2,500 feet) made by the Reading Manufacturing Company. The first pipe delivered was about 1,000 feet and the plaintiff's superintendent then called the attention of the foreman of the subcontractor, who was doing the plumbing, to the fact that the specifications annexed to the contract required all pipe used in the plumbing to be of the Reading Manufacturing Company. They then examined it for the purpose

of ascertaining whether this delivery was of that manufacture and found it was. Thereafter, as pipe was required in the progress of the work, the foreman of the subcontractor would leave word at its shop that he wanted a specified number of feet of pipe, without in any way indicating of what manufacture. Pipe would thereafter be delivered and installed in the building, without any examination whatever. Indeed, no examination, so far as appears, was made by the plaintiff, the subcontractor, defendant's architect, or any one else, of any of the pipe except the first delivery, until after the building had been completed. Plaintiff's architect then refused to give the certificate of completion, upon which the final payment depended, because all of the pipe used in the plumbing was not of the kind called for by the contract. After such refusal, the subcontractor removed the covering or insulation from about 900 feet of pipe which was exposed in the basement, cellar and attic, and all but 70 feet was found to have been manufactured, not by the Reading Company, but by other manufacturers, some by the Cohoes Rolling Mill Company, some by the National Steel Works, some by the South Chester Tubing Company, and some which bore no manufacturer's mark at all. The balance of the pipe had been so installed in the building that an inspection of it could not be had without demolishing, in part at least, the building itself.

9. I am of the opinion the trial court was right in directing a verdict for the defendant. The plaintiff agreed that all the pipe used should be of the Reading Manufacturing Company. Only about two-fifths of it, so far as appears, was of that kind. If more were used, then the burden of proving that fact was upon the plaintiff, which it could easily have done, since it knew where the pipe was obtained. The question of substantial performance of a contract of the character of the one under consideration depends in no small degree upon the good faith of the contractor. If the plaintiff had intended to, and had complied with the terms of the contract except as to minor omissions, due to inadvertence, then he might be allowed to recover the contract price, less the amount necessary to fully compensate the defendant for damages caused by such omissions. (*Woodward v. Fuller*, 80 N. Y. 312; *Nolan v. Whitney*, 88 N. Y. 648.) But that is not this case. It installed between 2,000 and 2,500 feet of pipe, of which only 1,000 feet at most complied with the contract. No explanation was given why pipe called for by the contract was not used, nor was any effort made to show what it would cost to remove the pipe of other manufacturers and install that of the Reading Manufacturing Company. The defendant had a right to contract for what he wanted. He had a right before making payment to get what the contract called for.

It is no answer to this suggestion to say that the pipe put in was just as good as that made by the Reading Manufacturing Company, or that the difference in value between such pipe and the pipe made by the Reading Manufacturing Company would be either “nominal or nothing.” Defendant contracted for pipe made by the Reading Manufacturing Company. What his reason was for requiring this kind of pipe is of no importance. He wanted that and was entitled to it. It may have been a mere whim on his part, but even so, he had a right to this kind of pipe, regardless of whether some other kind, according to the opinion of the contractor or experts, would have been “just as good, better, or done just as well.” He agreed to pay only upon condition that the pipe installed were made by that company and he ought not to be compelled to pay unless that condition be performed. (*Schultze v. Goodstein*, 180 N. Y. 248; *Spence v. Ham, supra*; *Steel S. & E. C. Co. v. Stock*, 225 N. Y. 173; *Van Clief v. Van Vechten*, 130 N. Y. 571; *Glacius v. Black*, 50 N. Y. 145; *Smith v. Brady*, 17 N. Y. 173, and authorities cited on p. 185.) The rule, therefore, of substantial performance, with damages for unsubstantial omissions, has no application. (*Crouch v. Gutmann*, 134 N. Y. 45; *Spence v. Ham*, 163 N. Y. 220.)

What was said by this court in *Smith v. Brady* (*supra*) is quite applicable here:

I suppose it will be conceded that everyone has a right to build his house, his cottage or his store after such a model and in such style as shall best accord with his notions of utility or be most agreeable to his fancy. The specifications of the contract become the law between the parties until voluntarily changed. If the owner prefers a plain and simple Doric column, and has so provided in the agreement, the contractor has no right to put in its place the more costly and elegant Corinthian. If the owner, having regard to strength and durability, has contracted for walls of specified materials to be laid in a particular manner, or for a given number of joists and beams, the builder has no right to substitute his own judgment or that of others. Having departed from the agreement, if performance has not been waived by the other party, the law will not allow him to allege that he has made as good a building as the one he engaged to erect. He can demand payment only upon and according to the terms of his contract, and if the conditions on which payment is due have not been performed, then the right to demand it does not exist. To hold a different doctrine would be simply to make another contract, and would be giving to parties an encouragement to violate their engagements, which the just policy of the law does not permit.

10. I am of the opinion the trial court did not err in ruling on the admission of evidence or in directing a verdict for the defendant.
11. For the foregoing reasons I think the judgment of the Appellate Division should be reversed and the judgment of the Trial Term affirmed.

Williams v. Walker-Thomas Furniture Co. I

District of Columbia Court of Appeals
198 A.2d 914 (1964)

QUINN, Associate Judge.

1. Appellant, a person of limited education separated from her husband, is maintaining herself and her seven children by means of public assistance. During the period 1957-1962 she had a continuous course of dealings with appellee from which she purchased many household articles on the installment plan. These included sheets, curtains, rugs, chairs, a chest of drawers, beds, mattresses, a washing machine, and a stereo set. In 1963 appellee filed a complaint in replevin for possession of all the items purchased by appellant, alleging that her payments were in default and that it retained title to the goods according to the sales contracts. By the writ of replevin appellee obtained a bed, chest of drawers, washing machine, and the stereo set. After hearing testimony and examining the contracts, the trial court entered judgment for appellee.
2. Appellant's principal contentions on appeal are (1) there was a lack of meeting of the minds, and (2) the contracts were against public policy.
3. Appellant signed fourteen contracts in all. They were approximately six inches in length and each contained a long paragraph in extremely fine print. One of the sentences in this paragraph provided that payments, after the first purchase, were to be prorated on all purchases then outstanding. Mathematically, this had the effect of keeping a balance due on all items until the time balance was completely eliminated. It meant that title to the first purchase, remained in appellee until the fourteenth purchase, made some five years later, was fully paid.
4. At trial appellant testified that she understood the agreements to mean that when payments on the running account were sufficient to balance the amount due on an individual item, the item became hers. She testified that most of the purchases were made at her home; that the contracts were signed in blank; that she did not read the instruments; and that she was not provided with a copy. She admitted, however, that she did not ask anyone to read or explain the contracts to her.

5. We have stated that “one who refrains from reading a contract and in conscious ignorance of its terms voluntarily assents thereto will not be relieved from his bad bargain.” *Bob Wilson, Inc. v. Swann*, D.C.Mun.App., 168 A.2d 198, 199 (1961). “One who signs a contract has a duty to read it and is obligated according to its terms.” *Hollywood Credit Clothing Co. v. Gibson*, D.C.App., 188 A.2d 348, 349 (1963). “It is as much the duty of a person who cannot read the language in which a contract is written to have someone read it to him before he signs it, as it is the duty of one who can read to peruse it himself before signing it.” *Stern v. Moneyweight Scale Co.*, 42 App.D.C. 162, 165 (1914).
6. A careful review of the record shows that appellant's assent was not obtained “by fraud or even misrepresentation falling short of fraud.” *Hollywood Credit Clothing Co. v. Gibson*, *supra*. This is not a case of mutual misunderstanding but a unilateral mistake. Under these circumstances, appellant's first contention is without merit.
7. Appellant's second argument presents a more serious question. The record reveals that prior to the last purchase appellant had reduced the balance in her account to \$164. The last purchase, a stereo set, raised the balance due to \$678. Significantly, at the time of this and the preceding purchases, appellee was aware of appellant's financial position. The reverse side of the stereo contract listed the name of appellant's social worker and her \$218 monthly stipend from the government. Nevertheless, with full knowledge that appellant had to feed, clothe and support both herself and seven children on this amount, appellee sold her a \$514 stereo set.
8. We cannot condemn too strongly appellee's conduct. It raises serious questions of sharp practice and irresponsible business dealings. A review of the legislation in the District of Columbia affecting retail sales and the pertinent decisions of the highest court in this jurisdiction disclose, however, no ground upon which this court can declare the contracts in question contrary to public policy. We note that were the Maryland Retail Installment Sales Act, Art. 83 §§ 128-153, or its equivalent, in force in the District of Columbia, we could grant appellant appropriate relief. We think Congress should consider corrective legislation to protect the public from such exploitive contracts as were utilized in the case at bar.

Williams v. Walker-Thomas Furniture Co. II

United States Court of Appeals, District of Columbia Circuit
121 U.S. App. D.C. 315, 350 F.2d 445 (1965)

WRIGHT, Circuit Judge.

1. Appellee, Walker-Thomas Furniture Company, operates a retail furniture store in the District of Columbia. During the period from 1957 to 1962 each appellant in these cases purchased a number of household items from Walker-Thomas, for which payment was to be made in installments. The terms of each purchase were contained in a printed form contract which set forth the value of the purchased item and purported to lease the item to appellant for a stipulated monthly rent payment. The contract then provided, in substance, that title would remain in Walker-Thomas until the total of all the monthly payments made equaled the stated value of the item, at which time appellants could take title. In the event of a default in the payment of any monthly installment, Walker-Thomas could repossess the item.
2. The contract further provided that “the amount of each periodical installment payment to be made by (purchaser) to the Company under this present lease shall be inclusive of and not in addition to the amount of each installment payment to be made by (purchaser) under such prior leases, bills or accounts; and all payments now and hereafter made by (purchaser) shall be credited pro rata on all outstanding leases, bills and accounts due the Company by (purchaser) at the time each such payment is made.” The effect of this rather obscure provision was to keep a balance due on every item purchased until the balance due on all items, whenever purchased, was liquidated. As a result, the debt incurred at the time of purchase of each item was secured by the right to repossess all the items previously purchased by the same purchaser, and each new item purchased automatically became subject to a security interest arising out of the previous dealings.
3. On May 12, 1962, appellant Thorne purchased an item described as a Daveno, three tables, and two lamps, having total stated value of \$391.10. Shortly thereafter, he defaulted on his monthly payments and appellee sought to replevy all the items purchased since the first transaction in 1958. Similarly, on April 17, 1962, appellant

Williams bought a stereo set of stated value of \$514.95.¹ She too defaulted shortly thereafter, and appellee sought to replevy all the items purchased since December, 1957. The Court of General Sessions granted judgment for appellee. The District of Columbia Court of Appeals affirmed, and we granted appellants' motion for leave to appeal to this court.

4. Appellants' principal contention, rejected by both the trial and the appellate courts below, is that these contracts, or at least some of them, are unconscionable and, hence, not enforceable. In its opinion in *Williams v. Walker-Thomas Furniture Company*, 198 A.2d 914, 916 (1964), the District of Columbia Court of Appeals explained its rejection of this contention as follows:

Appellant's second argument presents a more serious question. The record reveals that prior to the last purchase appellant had reduced the balance in her account to \$164. The last purchase, a stereo set, raised the balance due to \$678. Significantly, at the time of this and the preceding purchases, appellee was aware of appellant's financial position. The reverse side of the stereo contract listed the name of appellant's social worker and her \$218 monthly stipend from the government. Nevertheless, with full knowledge that appellant had to feed, clothe and support both herself and seven children on this amount, appellee sold her a \$514 stereo set.

We cannot condemn too strongly appellee's conduct. It raises serious questions of sharp practice and irresponsible business dealings. A review of the legislation in the District of Columbia affecting retail sales and the pertinent decisions of the highest court in this jurisdiction disclose, however, no ground upon which this court can declare the contracts in question contrary to public policy. We note that were the Maryland Retail Installment Sales Act, Art. 83 §§ 128-153, or its equivalent, in force in the District of Columbia, we could grant appellant appropriate relief. We think Congress should consider corrective legislation to protect the public from such exploitive contracts as were utilized in the case at bar.

5. We do not agree that the court lacked the power to refuse enforcement to contracts found to be unconscionable. In other jurisdictions, it has been held as a matter of

¹ At the time of this purchase her account showed a balance of \$164 still owing from her prior purchases. The total of all the purchases made over the years in question came to \$1,800. The total payments amounted to \$1,400.

common law that unconscionable contracts are not enforceable.² While no decision of this court so holding has been found, the notion that an unconscionable bargain should not be given full enforcement is by no means novel. In *Scott v. United States*, 79 U.S. (12 Wall.) 443, 445 (1870), the Supreme Court stated:

...If a contract be unreasonable and unconscionable, but not void for fraud, a court of law will give to the party who sues for its breach damages, not according to its letter, but only such as he is equitably entitled to....³

Since we have never adopted or rejected such a rule,⁴ the question here presented is actually one of first impression.

6. Congress has recently enacted the Uniform Commercial Code, which specifically provides that the court may refuse to enforce a contract which it finds to be unconscionable at the time it was made. 28 D.C.CODE § 2-302 (Supp. IV 1965). The enactment of this section, which occurred subsequent to the contracts here in suit, does not mean that the common law of the District of Columbia was otherwise at the time of enactment, nor does it preclude the court from adopting a similar rule in the exercise of its powers to develop the common law for the District of Columbia. In fact, in view of the absence of prior authority on the point, we consider the congressional adoption of § 2-302 persuasive authority for following the rationale of the cases from which the section is explicitly derived.⁵ Accordingly, we hold that

² *Campbell Soup Co. v. Wentz*, 3 Cir., 172 F.2d 80 (1948); *Indianapolis Morris Plan Corporation v. Sparks*, 132 Ind.App. 145, 172 N.E.2d 899 (1961); *Henningsen v. Bloomfield Motors, Inc.*, 32 N.J. 358, 161 A.2d 69, 84-96, 75 A.L.R.2d 1 (1960). Cf. 1 CORBIN, CONTRACTS § 128 (1963).

³ See *Luing v. Peterson*, 143 Minn. 6, 172 N.W. 692 (1919); *Greer v. Tweed*, N.Y.C.P., 13 Abb.Pr., N.S., 427 (1872); *Schnell v. Nell*, 17 Ind. 29 (1861); and see generally the discussion of the English authorities in *Hume v. United States*, 132 U.S. 406 (1889).

⁴ While some of the statements in the court's opinion in *District of Columbia v. Harlan & Hollingsworth Co.*, 30 App. D.C. 270 (1908), may appear to reject the rule, in reaching its decision upholding the liquidated damages clause in that case the court considered the circumstances existing at the time the contract was made, see 30 App. D.C. at 279, and applied the usual rule on liquidated damages. See 5 CORBIN, CONTRACTS §§ 1054-1075 (1964); Note, 72 YALE L.J. 723, 746-755 (1963). Compare *Jaeger v. O'Donoghue*, 57 App.D.C. 191, 18 F.2d 1013 (1927).

⁵ See Comment, § 2-302, Uniform Commercial Code (1962). Compare Note, 45 VA. L. REV. 583, 590 (1959), where it is predicted that the rule of § 2-302 will be followed by analogy in cases which involve contracts not specifically covered by the section. Cf. 1 STATE OF NEW YORK LAW REVISION COMMISSION, REPORT AND RECORD OF HEARINGS ON THE UNIFORM COMMERCIAL CODE 108-110 (1954) (remarks of Professor Llewellyn).

where the element of unconscionability is present at the time a contract is made, the contract should not be enforced.

7. 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.⁶ Whether a meaningful choice is present in a particular case can only be determined by consideration of all the circumstances surrounding the transaction. In many cases the meaningfulness of the choice is negated by a gross inequality of bargaining power.⁷ The manner in which the contract was entered is also relevant to this consideration. Did each party to the contract, considering his obvious education or lack of it, have a reasonable opportunity to understand the terms of the contract, or were the important terms hidden in a maze of fine print and minimized by deceptive sales practices? Ordinarily, one who signs an agreement without full knowledge of its terms might be held to assume the risk that he has entered a one-sided bargain.⁸ But when a party of little bargaining power, and hence little real choice, signs a commercially unreasonable contract with little or no knowledge of its terms, it is hardly likely that his consent, or even an objective manifestation of his consent, was ever given to all the terms. In such a case the usual rule that the terms of the agreement are not to be questioned⁹ should be abandoned

⁶ See *Henningsen v. Bloomfield Motors, Inc.*, *supra* Note 2; *Campbell Soup Co. v. Wentz*, *supra* Note 2.

⁷ See *Henningsen v. Bloomfield Motors, Inc.*, *supra* Note 2, 161 A.2d at 86., and authorities there cited. Inquiry into the relative bargaining power of the two parties is not an inquiry wholly divorced from the general question of unconscionability, since a one-sided bargain is itself evidence of the inequality of the bargaining parties. This fact was vaguely recognized in the common law doctrine of intrinsic fraud, that is, fraud which can be presumed from the grossly unfair nature of the terms of the contract. See the oft-quoted statement of Lord Hardwicke in *Earl of Chesterfield v. Janssen*, 28 Eng. Rep. 82, 100 (1751): "... (Fraud) may be apparent from the intrinsic nature and subject of the bargain itself; such as no man in his senses and not under delusion would make...." And *cf. Hume v. United States*, *supra* Note 3, 132 U.S. at 413, where the Court characterized the English cases as 'cases in which one party took advantage of the other's ignorance of arithmetic to impose upon him, and the fraud was apparent from the face of the contracts.' See also *Greer v. Tweed*, *supra* Note 3.

⁸ See RESTATEMENT, CONTRACTS § 70 (1932); Note, 63 HARV. L. REV. 494 (1950). See also *Daley v. People's Building, Loan & Savings Ass'n*, 178 Mass. 13, 59 N.E. 452, 453 (1901), in which Mr. Justice Holmes, while sitting on the Supreme Judicial Court of Massachusetts, made this observation: "... Courts are less and less disposed to interfere with parties making such contracts as they choose, so long as they interfere with no one's welfare but their own.... It will be understood that we are speaking of parties standing in an equal position where neither has any oppressive advantage or power...."

⁹ This rule has never been without exception. In cases involving merely the transfer of unequal amounts of the same commodity, the courts have held the bargain unenforceable for the reason that "in such a case, it is clear, that the law cannot indulge in the presumption of equivalence between the consideration and the promise." 1 WILLISTON, CONTRACTS § 115 (3d ed. 1957).

and the court should consider whether the terms of the contract are so unfair that enforcement should be withheld.¹⁰

8. In determining reasonableness or fairness, the primary concern must be with the terms of the contract considered in light of the circumstances existing when the contract was made. The test is not simple, nor can it be mechanically applied. The terms are to be considered “in the light of the general commercial background and the commercial needs of the particular trade or case.”¹¹ Corbin suggests the test as being whether the terms are ‘so extreme as to appear unconscionable according to the mores and business practices of the time and place.’¹² We think this formulation correctly states the test to be applied in those cases where no meaningful choice was exercised upon entering the contract.
9. Because the trial court and the appellate court did not feel that enforcement could be refused, no findings were made on the possible unconscionability of the contracts in these cases. Since the record is not sufficient for our deciding the issue as a matter of law, the cases must be remanded to the trial court for further proceedings.

So ordered.

DANAHER, Circuit Judge (dissenting):

10. The District of Columbia Court of Appeals obviously was as unhappy about the situation here presented as any of us can possibly be. Its opinion in the *Williams* case, quoted in the majority text, concludes: “We think Congress should consider corrective legislation to protect the public from such exploitive contracts as were utilized in the case at bar.”
11. My view is thus summed up by an able court which made no finding that there had actually been sharp practice. Rather the appellant seems to have known precisely where she stood.

¹⁰ See the general discussion of ‘Boiler-Plate Agreements’ in LLEWELLYN, *THE COMMON LAW TRADITION* 362-371 (1960).

¹¹ Comment, *Uniform Commercial Code* § 2-307.

¹² See *Henningsen v. Bloomfield Motors, Inc.*, *supra* Note 2; *Mandel v. Liebman*, 303 N.Y. 88, 100 N.E.2d 149 (1951). The traditional test as stated in *Greer v. Tweed*, *supra* Note 3, 13 Abb. Pr., N.S., at 429, is “such as no man in his senses and not under delusion would make on the one hand, and as no honest or fair man would accept, on the other.”

12. There are many aspects of public policy here involved. What is a luxury to some may seem an outright necessity to others. Is public oversight to be required of the expenditures of relief funds? A washing machine, e.g., in the hands of a relief client might become a fruitful source of income. Many relief clients may well need credit, and certain business establishments will take long chances on the sale of items, expecting their pricing policies will afford a degree of protection commensurate with the risk. Perhaps a remedy when necessary will be found within the provisions of the "Loan Shark" law, D.C.Code §§ 26-601 et seq. (1961).
13. I mention such matters only to emphasize the desirability of a cautious approach to any such problem, particularly since the law for so long has allowed parties such great latitude in making their own contracts. I dare say there must annually be thousands upon thousands of installment credit transactions in this jurisdiction, and one can only speculate as to the effect the decision in these cases will have.¹³
14. I join the District of Columbia Court of Appeals in its disposition of the issues.

¹³ However the provision ultimately may be applied or in what circumstances, D.C. Code § 28-2-301 (Supp. IV, 1965) it did not become effective until January 1, 1965.

Alaska Packers' Ass'n v. Domenico

United States Court of Appeals, Ninth Circuit
117 F. 99 (1902)

ROSS, Circuit Judge.

1. The libel in this case was based upon a contract alleged to have been entered into between the libelants and the appellant corporation on the 22d day of May, 1900, at Pyramid Harbor, Alaska, by which it is claimed the appellant promised to pay each of the libelants, among other things, the sum of \$100 for services rendered and to be rendered. In its answer the respondent denied the execution, on its part, of the contract sued upon, averred that it was without consideration, and for a third defense alleged that the work performed by the libelants for it was performed under other and different contracts than that sued on, and that, prior to the filing of the libel, each of the libelants was paid by the respondent the full amount due him thereunder, in consideration of which each of them executed a full release of all his claims and demands against the respondent.
2. The evidence shows without conflict that on March 26, 1900, at the city and county of San Francisco, the libelants entered into a written contract with the appellants, whereby they agreed to go from San Francisco to Pyramid Harbor, Alaska, and return, on board such vessel as might be designated by the appellant, and to work for the appellant during the fishing season of 1900, at Pyramid Harbor, as sailors and fishermen, agreeing to do "regular ship's duty, both up and down, discharging and loading; and to do any other work whatsoever when requested to do so by the captain or agent of the Alaska Packers' Association." By the terms of this agreement, the appellant was to pay each of the libelants \$50 for the season, and two cents for each red salmon in the catching of which he took part.
3. On the 15th day of April, 1900, 21 of the libelants signed shipping articles by which they shipped as seamen on the Two Brothers, a vessel chartered by the appellant for the voyage between San Francisco and Pyramid Harbor, and also bound themselves to perform the same work for the appellant provided for by the previous contract of March 26th; the appellant agreeing to pay them therefor the sum of \$60 for the season, and two cents each for each red salmon in the catching of which they should respectively take part. Under these contracts, the libelants sailed on board the Two Brothers for Pyramid Harbor, where the appellants had about \$150,000 invested in a

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

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

The contention of libelants that the nets provided them were rotten and unserviceable is not sustained by the evidence. The defendants' interest required that libelants should be provided with every facility necessary to their success as fishermen, for on such success depended the profits

defendant would be able to realize that season from its packing plant, and the large capital invested therein. In view of this self-evident fact, it is highly improbable that the defendant gave libelants rotten and unserviceable nets with which to fish. It follows from this finding that libelants were not justified in refusing performance of their original contract.

112 Fed. 554.

5. The evidence being sharply conflicting in respect to these facts, the conclusions of the court, who heard and saw the witnesses, will not be disturbed. *The Alijandro*, 6 C.C.A. 54, 56 Fed. 621; *The Lucy*, 20 C.C.A. 660, 74 Fed. 572; *The Glendale*, 26 C.C.A. 500, 81 Fed. 633. *The Coquitlam*, 23 C.C.A. 438, 77 Fed. 744; *Gorham Mfg. Co. v. Emery-Bird-Thayer Dry Goods Co.*, 43 C.C.A. 511, 104 Fed. 243.
6. The real questions in the case as brought here are questions of law, and, in the view that we take of the case, it will be necessary to consider but one of those. Assuming that the appellant's superintendent at Pyramid Harbor was authorized to make the alleged contract of May 22d, and that he executed it on behalf of the appellant, was it supported by a sufficient consideration? From the foregoing statement of the case, it will have been seen that the libelants agreed in writing, for certain stated compensation, to render their services to the appellant in remote waters where the season for conducting fishing operations is extremely short, and in which enterprise the appellant had a large amount of money invested; and, after having entered upon the discharge of their contract, and at a time when it was impossible for the appellant to secure other men in their places, the libelants, without any valid cause, absolutely refused to continue the services they were under contract to perform unless the appellant would consent to pay them more money. Consent to such a demand, under such circumstances, if given, was, in our opinion, without consideration, for the reason that it was based solely upon the libelants' agreement to render the exact services, and none other, that they were already under contract to render. The case shows that they willfully and arbitrarily broke that obligation. As a matter of course, they were liable to the appellant in damages, and it is quite probable, as suggested by the court below in its opinion, that they may have been unable to respond in damages. But we are unable to agree with the conclusions there drawn, from these facts, in these words:

Under such circumstances, it would be strange, indeed, if the law would not permit the defendant to waive the damages caused by the libelants' breach,

and enter into the contract sued upon—a contract mutually beneficial to all the parties thereto, in that it gave to the libelants reasonable compensation for their labor, and enabled the defendant to employ to advantage the large capital it had invested in its canning and fishing plant.

7. Certainly, it cannot be justly held, upon the record in this case, that there was any voluntary waiver on the part of the appellant of the breach of the original contract. The company itself knew nothing of such breach until the expedition returned to San Francisco, and the testimony is uncontradicted that its superintendent at Pyramid Harbor, who, it is claimed, made on its behalf the contract sued on, distinctly informed the libelants that he had no power to alter the original or to make a new contract, and it would, of course, follow that, if he had no power to change the original, he would have no authority to waive any rights thereunder. The circumstances of the present case bring it, we think, directly within the sound and just observations of the supreme court of Minnesota in the case of *King v. Railway Co.*, 61 Minn. 482, 63 N.W. 1105:

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

8. In *Lingenfelder v. Brewing Co.*, 103 Mo. 578, 15 S.W. 844, the court, in holding void a contract by which the owner of a building agreed to pay its architect an additional sum because of his refusal to otherwise proceed with the contract, said:

It is urged upon us by respondents that this was a new contract. New in what? Jungenfeld was bound by his contract to design and supervise this building. Under the new promise, he was not to do anything more or anything different. What benefit was to accrue to Wainwright? He was to receive the same service from Jungenfeld under the new, that Jungenfeld was bound to tender

under the original, contract. What loss, trouble, or inconvenience could result to Jungenfeld that he had not already assumed? No amount of metaphysical reasoning can change the plain fact that Jungenfeld took advantage of Wainwright's necessities, and extorted the promise of five per cent. on the refrigerator plant as the condition of his complying with his contract already entered into. Nor had he even the flimsy pretext that Wainwright had violated any of the conditions of the contract on his part. Jungenfeld himself put it upon the simple proposition that "if he, as an architect, put up the brewery, and another company put up the refrigerating machinery, it would be a detriment to the Empire Refrigerating Company," of which Jungenfeld was president.

To permit plaintiff to recover under such circumstances would be to offer a premium upon bad faith, and invite men to violate their most sacred contracts that they may profit by their own wrong. That a promise to pay a man for doing that which he is already under contract to do is without consideration is conceded by respondents. The rule has been so long imbedded in the common law and decisions of the highest courts of the various states that nothing but the most cogent reasons ought to shake it. (Citing a long list of authorities.) But it is "carrying coals to Newcastle" to add authorities on a proposition so universally accepted, and so inherently just and right in itself.

The learned counsel for respondents do not controvert the general proposition. [Their] contention is, and the circuit court agreed with them, that, when Jungenfeld declined to go further on his contract, the defendant then had the right to sue for damages, and not having elected to sue Jungenfeld, but having acceded to his demand for the additional compensation defendant cannot now be heard to say his promise is without consideration. While it is true Jungenfeld became liable in damages for the obvious breach of his contract, we do not think it follows that defendant is estopped from showing its promise was made without consideration. It is true that as eminent a jurist as Judge Cooley, in *Goebel v. Linn*, 47 Mich. 489, 11 N.W. 284, 41 Am.Rep. 723, held that an ice company which had agreed to furnish a brewery with all the ice they might need for their business from November 8, 1879, until January 1, 1881, at \$1.75 per ton, and afterwards in May, 1880, declined to deliver any more ice unless the brewery would give it \$3 per ton, could recover on a promissory note given for the increased price.

Profound as is our respect for the distinguished judge who delivered the opinion, we are still of the opinion that his decision is not in accord with the almost universally accepted doctrine, and is not convincing; and certainly so much of the opinion as holds that the payment, by a debtor, of a part of his debt then due, would constitute a defense to a suit for the remainder, is not the law of this state, nor, do we think, of any other where the common law prevails. ... What we hold is that, when a party merely does what he has already obligated himself to do, he cannot demand an additional compensation therefor; and although, by taking advantage of the necessities of his adversary, he obtains a promise for more, the law will regard it as *nudum pactum*, and will not lend its process to aid in the wrong.

9. The case of *Goebel v. Linn*, 47 Mich. 489, 11 N.W. 284, is one of the eight cases relied upon by the court below in support of its judgment in the present case, five of which are by the supreme court of Massachusetts, one by the supreme court of Vermont, and one other Michigan case, that of *Moore v. Locomotive Works*, 14 Mich. 266. The Vermont case referred to is that of *Lawrence v. Davey*, 28 Vt. 264, which was one of the three cases cited by the court in *Moore v. Locomotive Works*, 14 Mich. 272, 273, as authority for its decision. In that case there was a contract to deliver coal at specified terms and rates. A portion of it was delivered, and plaintiff then informed the defendant that he could not deliver at those rates, and, if the latter intended to take advantage of it, he should not deliver any more; and that he should deliver no more unless the defendant would pay for the coal independent of the contract. The defendant agreed to do so, and the coal was delivered. On suit being brought for the price, the court said:

Although the promise to waive the contract was after some portion of the coal sought to be recovered had been delivered, and so delivered that probably the plaintiff, if the defendant had insisted upon strict performance of the contract, could not have recovered anything for it, yet, nevertheless, the agreement to waive the contract, and the promise, and, above all, the delivery of coal after this agreement to waive the contract, and upon the faith of it, will be a sufficient consideration to bind the defendant to pay for the coal already received.

10. The doctrine of that case was impliedly overruled by the supreme court of Vermont in the subsequent case of *Cobb v. Cowdery*, 40 Vt. 25, where it was held that:

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

11. The Massachusetts cases cited by the court below in support of its judgment commence with the case of *Munroe v. Perkins*, 9 Pick. 305, 20 Am. Dec. 475, which really seems to be the foundation of all of the cases in support of that view. In that case, the plaintiff had agreed in writing to erect a building for the defendants. Finding his contract a losing one, he had concluded to abandon it, and resumed work on the oral contract of the defendants that, if he would do so, they would pay him what the work was worth without regard to the terms of the original contract. The court said that whether the oral contract was without consideration:

[d]epends entirely on the question whether the first contract was waived. The plaintiff having refused to perform that contract, as he might do, subjecting himself to such damages as the other parties might show they were entitled to recover, he afterward went on, upon the faith of the new promise, and finished the work. This was a sufficient consideration. If Payne and Perkins were willing to accept his relinquishment of the old contract, and proceed on a new agreement, the law, we think, would not prevent it.

12. The case of *Goebel v. Linn*, 47 Mich. 489, 11 N.W. 284, presented some unusual and extraordinary circumstances. But, taking it as establishing the precise rule adopted in the Massachusetts cases, we think it not only contrary to the weight of authority, but wrong on principle.
13. In addition to the Minnesota and Missouri cases above cited, the following are some of the numerous authorities holding the contrary doctrine: *Vanderbilt v. Schreyer*, 91 N.Y. 392; *Ayres v. Railroad Co.*, 52 Iowa, 478, 3 N.W. 522; *Harris v. Carter*, 3 Ellis & B. 559; *Frazer v. Hatton*, 2 C.B.(N.S.) 512; *Conover v. Stillwell*, 34 N.J. Law, 54;

Reynolds v. Nugent, 25 Ind. 328; *Spencer v. McLean* (Ind. App.) 50 N.E. 769, 67 Am.St.Rep. 271; *Harris v. Harris* (Colo. App.) 47 Pac. 841; *Moran v. Peace*, 72 Ill.App. 139; *Carpenter v. Taylor* (N.Y.) 58 N.E. 53; *Westcott v. Mitchell* (Me.) 50 Atl. 21; *Robinson v. Jewett*, 116 N.Y. 40, 22 N.E. 224; *Sullivan v. Sullivan*, 99 Cal. 187, 33 Pac. 862; *Blyth v. Robinson*, 104 Cal. 230, 37 Pac. 904; *Skinner v. Mining Co.* (C.C.) 96 Fed. 735; 1 Beach, Cont. § 166; Langd. Cont. § 54; 1 Pars.Cont. (5th Ed.) 457; *Ferguson v. Harris* (S.C.) 17 S.E. 782.

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

Reed v. King

Court of Appeal of California
145 Cal. App. 3d 261 (1983)

BLEASE, J.

1. In the sale of a house, must the seller disclose it was the site of a multiple murder?
2. Dorris Reed purchased a house from Robert King. Neither King nor his real estate agents (the other named defendants) told Reed that a woman and her four children were murdered there 10 years earlier. However, it seems “truth will come to light; murder cannot be hid long.” (Shakespeare, Merchant of Venice, act II, scene II.) Reed learned of the gruesome episode from a neighbor after the sale. She sues seeking rescission and damages. King and the real estate agent defendants successfully demurred to her first amended complaint for failure to state a cause of action. Reed appeals the ensuing judgment of dismissal. We will reverse the judgment.

Facts

3. We take all issuable facts pled in Reed's complaint as true. (See 3 WITKIN, CAL. PROCEDURE (2d ed. 1971) Pleading, § 800.) King and his real estate agent knew about the murders and knew the event materially affected the market value of the house when they listed it for sale. They represented to Reed the premises were in good condition and fit for an “elderly lady” living alone. They did not disclose the fact of the murders. At some point King asked a neighbor not to inform Reed of that event. Nonetheless, after Reed moved in neighbors informed her no one was interested in purchasing the house because of the stigma. Reed paid \$76,000, but the house is only worth \$65,000 because of its past.
4. The trial court sustained the demurrers to the complaint on the ground it did not state a cause of action. The court concluded a cause of action could only be stated “if the subject property, by reason of the prior circumstances, were *presently* the object of community notoriety” (Original italics.) Reed declined the offer of leave to amend.

Discussion

5. Does Reed's pleading state a cause of action? Concealed within this question is the nettlesome problem of the duty of disclosure of blemishes on real property which are not physical defects or legal impairments to use.
6. Reed seeks to state a cause of action sounding in contract, i.e. rescission, or in tort, i.e., deceit. In either event her allegations must reveal a fraud. (See Civ. Code, §§ 1571-1573, 1689, 1709-1710.) “The elements of actual fraud, whether as the basis of the remedy in contract or tort, may be stated as follows: There must be (1) a *false representation* or concealment of a material fact (or, in some cases, an opinion) susceptible of knowledge, (2) made with *knowledge* of its falsity or without sufficient knowledge on the subject to warrant a representation, (3) with the *intent* to induce the person to whom it is made to act upon it; and such person must (4) act in *reliance* upon the representation (5) to his *damage*.”¹ (Original italics.) (1 WITKIN, SUMMARY OF CAL. LAW (8th ed. 1973) Contracts, § 315.)
7. The trial court perceived the defect in Reed's complaint to be a failure to allege concealment of a material fact. “Concealment” and “material” are legal conclusions concerning the effect of the issuable facts pled. As appears, the analytic pathways to these conclusions are intertwined.
8. Concealment is a term of art which includes mere nondisclosure when a party has a duty to disclose. (See, e.g., *Lingsch v. Savage* (1963) 213 Cal.App.2d 729, 738 [29 Cal.Rptr. 201, 8 A.L.R.3d 537]; Rest.2d Contracts, § 161; Rest.2d Torts, § 551; Rest., Restitution, § 8, esp. com. b.) Reed's complaint reveals only nondisclosure despite the allegation King asked a neighbor to hold his peace. There is no allegation the attempt at suppression was a cause in fact of Reed's ignorance.² (See Rest.2d Contracts, §§ 160, 162-164; Rest.2d Torts, § 550; Rest., Restitution, § 9.) Accordingly, the critical question is: does the seller have a duty to disclose here? Resolution of this question depends on the materiality of the fact of the murders.

¹Proof of damage, i.e. specific pecuniary loss, is not essential to obtain rescission alone. (See 1 WITKIN, *op. cit. supra.*, §§ 324-325; see also *Earl v. Saks & Co.* (1951) 36 Cal.2d 602 [226 P.2d 340].)

²Reed elsewhere in the complaint asserts defendants “actively concealed” the fact of the murders and this in part misled her. However, no connection is made or apparent between the legal conclusion of active concealment and any issuable fact pled by Reed. Accordingly, the assertion is insufficient. (See *Bacon v. Soule* (1912) 19 Cal. App. 428, 438 [126 P. 384].)

9. Similarly we do not view the statement the house was fit for Reed to inhabit as transmuting her case from one of nondisclosure to one of false representation. To view the representation as patently false is to find “elderly ladies” uniformly susceptible to squeamishness. We decline to indulge this stereotypical assumption. To view the representation as misleading because it conflicts with a duty to disclose is to beg that question.
10. In general, a seller of real property has a duty to disclose: “where the seller knows of facts *materially* affecting the value or desirability of the property which are known or accessible only to him and also knows that such facts are not known to, or within the reach of the diligent attention and observation of the buyer, the seller is under a duty to disclose them to the buyer.”³ [Italics added, citations omitted.]” (*Lingsch v. Savage, supra.*, 213 Cal. App. 2d at p. 735.) This broad statement of duty has led one commentator to conclude: “The ancient maxim *caveat emptor* ('let the buyer beware.') has little or no application to California real estate transactions.” (1 Miller & Starr, *Current Law of Cal. Real Estate* (rev. ed. 1975) § 1:80.)
11. Whether information “is of sufficient materiality to affect the value or desirability of the property ... depends on the facts of the particular case.” (*Lingsch, supra.*, 213 Cal. App. 2d at p. 737.) Materiality “is a question of law, and is part of the concept of right to rely or justifiable reliance.” (3 WITKIN, *CAL. PROCEDURE* (2d ed. 1971) Pleading, § 578, p. 2217.) Accordingly, the term is essentially a label affixed to a normative conclusion.⁴ Three considerations bear on this legal conclusion: the gravity of the harm inflicted by nondisclosure; the fairness of imposing a duty of discovery on the buyer as an alternative to compelling disclosure, and the impact on the stability of contracts if rescission is permitted.

³The real estate agent or broker representing the seller is under the same duty of disclosure. (*Lingsch v. Savage, supra.*, 213 Cal.App.2d at p. 736.)

⁴This often subsumes a policy analysis of the effect of permitting rescission on the stability of contracts. (See fn. 6, *ante.*) “In the case law of fraud, the word 'material' has become a sort of talisman. It is suggested that it has no meaning when undefined other than to the user since the word actually means no more than that the fraud is the sort which will justify rescission or damages in deceit. However, courts continue to use materiality as a test without explanatory reference to the varying standards of reliance, damage, etc. they are following.” (Note, *Rescission: Fraud as Ground: Contracts* (1951) 39 Cal.L.Rev. 309, 310-311, fn. 4.)

12. Numerous cases have found nondisclosure of physical defects and legal impediments to use of real property are material. (See 1 Miller & Starr, *supra.*, § 181.)⁵ However, to our knowledge, no prior real estate sale case has faced an issue of nondisclosure of the kind presented here. (Compare *Earl v. Saks & Co.*, *supra.*, 36 Cal.2d 602; *Kuhn v. Gottfried* (1951) 103 Cal.App.2d 80, 85-86 [229 P.2d 137].) Should this variety of ill-repute be required to be disclosed? Is this a circumstance where “non-disclosure of the fact amounts to a failure to act in good faith and in accordance with reasonable standards of fair dealing[?]” (Rest. 2d Contracts, § 161, subd. (b).)
13. The paramount argument against an affirmative conclusion is it permits the camel's nose of unrestrained irrationality admission to the tent. If such an “irrational” consideration is permitted as a basis of rescission the stability of all conveyances will be seriously undermined. Any fact that might disquiet the enjoyment of some segment of the buying public may be seized upon by a disgruntled purchaser to void a bargain.⁶ In our view, keeping this genie in the bottle is not as difficult a task as these arguments assume. We do not view a decision allowing Reed to survive a demurrer in these unusual circumstances as indorsing the materiality of facts predicating peripheral, insubstantial, or fancied harms.
14. The murder of innocents is highly unusual in its potential for so disturbing buyers they may be unable to reside in a home where it has occurred. This fact may foreseeably deprive a buyer of the intended use of the purchase. Murder is not such a common occurrence that *buyers* should be charged with anticipating and discovering

⁵ For example, the following have been held of sufficient materiality to require disclosure: the home sold was constructed on filled land (*Burkett v. J.A. Thompson & Son* (1957) 150 Cal.App.2d 523, 526 [310 P.2d 56]); improvements were added without a building permit and in violation of zoning regulations (*Barder v. McClung* (1949) 93 Cal.App.2d 692, 697 [209 P.2d 808]) or in violation of building codes (*Curran v. Heslop* (1953) 115 Cal.App.2d 476, 480-481 [252 P.2d 378]); the structure was condemned (*Katz v. Department of Real Estate* (1979) 96 Cal.App.3d 895, 900 [158 Cal.Rptr. 766]); the structure was termite-infested (*Godfrey v. Steinpress* (1982) 128 Cal.App.3d 154 [180 Cal.Rptr. 95]); there was water infiltration in the soil (*Barnhouse v. City of Pinole* (1982) 133 Cal.App.3d 171, 187-188 [183 Cal.Rptr. 881]); the amount of net income a piece of property would yield was overstated (*Ford v. Cournale* (1973) 36 Cal.App.3d 172, 179-180 [111 Cal.Rptr. 334, 81 A.L.R.3d 704].)

⁶ Concern for the effects of an overly indulgent rescission policy on the stability of bargains is not new. Our Supreme Court early on quoted with approval the sentiment: “The power to cancel a contract is a most extraordinary power. It is one which should be exercised with great caution—nay, I may say, with great reluctance—unless in a clear case. A too free use of this power would render all business uncertain, and, as has been said, make the length of a chancellor's foot the measure of individual rights. The greatest liberty of making contracts is essential to the business interests of the country. In general, the parties must look out for themselves.” (*Colton v. Stanford* (1980) 82 Cal. 351, 398 [23 P. 16].)

this disquieting possibility. Accordingly, the fact is not one for which a duty of inquiry and discovery can sensibly be imposed upon the buyer.

15. Reed alleges the fact of the murders has a quantifiable effect on the market value of the premises.⁷ We cannot say this allegation is inherently wrong and, in the pleading posture of the case, we assume it to be true. If information known or accessible only to the seller has a significant and measurable effect on market value and, as is alleged here, the seller is aware of this effect, we see no principled basis for making the duty to disclose turn upon the character of the information. Physical usefulness is not and never has been the sole criterion of valuation. Stamp collections and gold speculation would be insane activities if utilitarian considerations were the sole measure of value. (See also Civ. Code, § 3355 [deprivation of property of peculiar value to owner]; Annot. (1950) 12 A.L.R.2d 902 [Measure of Damages for Conversion or Loss of, or Damage to, Personal Property Having No Market Value].)
16. Reputation and history can have a significant effect on the value of realty. “George Washington slept here” is worth something, however physically inconsequential that consideration may be. Ill-repute or “bad will” conversely may depress the value of property. Failure to disclose such a negative fact where it will have a foreseeably depressing effect on income expected to be generated by a business is tortious. (See Rest.2d Torts, § 551, illus. 11.) Some cases have held that *unreasonable* fears of the potential buying public that a gas or oil pipeline may rupture may depress the market value of land and entitle the owner to incremental compensation in eminent domain. (See Annot., Eminent Domain: Elements and Measure of Compensation for Oil or Gas Pipeline Through Private Property (1954) 38 A.L.R.2d 788, 801-804.)
17. Whether Reed will be able to prove her allegation the decade-old multiple murder has a significant effect on market value we cannot determine.⁸ If she is able to do so by competent evidence she is entitled to a favorable ruling on the issues of materiality

⁷ See Evidence Code section 810 et seq. We note the traditional formulation of market value assumes a buyer “with knowledge of all the issues and purposes to which [the realty] is adapted.” (See e.g. *South Bay Irr. Dist. v. California-American Water Co.* (1976) 61 Cal. App. 3d 944, 961 and 970 [133 Cal. Rptr. 166].)

⁸ [In]determining what factors would motivate [buyers and sellers] in reaching an agreement as to price, and in weighing the effect of their motivation, [the trier of fact] may rely upon the opinion of experts in the field and also upon its knowledge and experience shared in common with people in general.“ (*South Bay Irr. Dist.*, *supra.*, 61 Cal.App.3d at p. 970; see also 3 Wigmore, Evidence (Chadbourn rev.ed. 1970) § 711 et seq.)

and duty to disclose.⁹ Her demonstration of objective tangible harm would still the concern that permitting her to go forward will open the floodgates to rescission on subjective and idiosyncratic grounds.

18. A more troublesome question would arise if a buyer in similar circumstances were unable to plead or establish a significant and quantifiable effect on market value. However, this question is not presented in the posture of this case. Reed has not alleged the fact of the murders has rendered the premises useless to her as a residence. As currently pled, the gravamen of her case is pecuniary harm. We decline to speculate on the abstract alternative.
19. The judgment is reversed.

⁹ The ruling of the trial court requiring the additional element of notoriety, i.e. widespread public knowledge, is unpersuasive. Lack of notoriety may facilitate resale to yet another unsuspecting buyer at the "market price" of a house with no ill-repute. However, it appears the buyer will learn of the possibly unsettling history of the house soon after moving in. Those who suffer no discomfort from the specter of residing in such quarters per se, will nonetheless be discomforted by the prospect they have bought a house that may be difficult to sell to less hardy souls. Nondisclosure must be evaluated as fair or unfair regardless of the ease with which a buyer may escape this discomfort by foisting it upon another.

Stamovsky v. Ackley

New York Supreme Court, Appellate Division
169 A.D.2d 254 (1991)

RUBIN, Justice.

1. Plaintiff, to his horror, discovered that the house he had recently contracted to purchase was widely reputed to be possessed by poltergeists, reportedly seen by defendant seller and members of her family on numerous occasions over the last nine years. Plaintiff promptly commenced this action seeking rescission of the contract of sale. Supreme Court reluctantly dismissed the complaint, holding that plaintiff has no remedy at law in this jurisdiction.
2. The unusual facts of this case, as disclosed by the record, clearly warrant a grant of equitable relief to the buyer who, as a resident of New York City, cannot be expected to have any familiarity with the folklore of the Village of Nyack. Not being a “local,” plaintiff could not readily learn that the home he had contracted to purchase is haunted. Whether the source of the spectral apparitions seen by defendant seller are parapsychic or psychogenic, having reported their presence in both a national publication (“Readers' Digest”) and the local press (in 1977 and 1982, respectively), defendant is estopped to deny their existence and, as a matter of law, the house is haunted. More to the point, however, no divination is required to conclude that it is defendant's promotional efforts in publicizing her close encounters with these spirits which fostered the home's reputation in the community. In 1989, the house was included in a five-home walking tour of Nyack and described in a November 27th newspaper article as “a riverfront Victorian (with ghost).” The impact of the reputation thus created goes to the very essence of the bargain between the parties, greatly impairing both the value of the property and its potential for resale. The extent of this impairment may be presumed for the purpose of reviewing the disposition of this motion to dismiss the cause of action for rescission (*Harris v. City of New York*, 147 A.D.2d 186, 188-189, 542 N.Y.S.2d 550) and represents merely an issue of fact for resolution at trial.
3. While I agree with Supreme Court that the real estate broker, as agent for the seller, is under no duty to disclose to a potential buyer the phantasmal reputation of the premises and that, in his pursuit of a legal remedy for fraudulent misrepresentation against the seller, plaintiff hasn't a ghost of a chance, I am nevertheless moved by the

spirit of equity to allow the buyer to seek rescission of the contract of sale and recovery of his downpayment. New York law fails to recognize any remedy for damages incurred as a result of the seller's mere silence, applying instead the strict rule of caveat emptor. Therefore, the theoretical basis for granting relief, even under the extraordinary facts of this case, is elusive if not ephemeral.

4. “Pity me not but lend thy serious hearing to what I shall unfold” (WILLIAM SHAKESPEARE, *HAMLET*, Act I, Scene V [Ghost]).
5. From the perspective of a person in the position of plaintiff herein, a very practical problem arises with respect to the discovery of a paranormal phenomenon: “Who you gonna' call?” as the title song to the movie “Ghostbusters” asks. Applying the strict rule of caveat emptor to a contract involving a house possessed by poltergeists conjures up visions of a psychic or medium routinely accompanying the structural engineer and Terminix man on an inspection of every home subject to a contract of sale. It portends that the prudent attorney will establish an escrow account lest the subject of the transaction come back to haunt him and his client—or pray that his malpractice insurance coverage extends to supernatural disasters. In the interest of avoiding such untenable consequences, the notion that a haunting is a condition which can and should be ascertained upon reasonable inspection of the premises is a hobgoblin which should be exorcised from the body of legal precedent and laid quietly to rest.
6. It has been suggested by a leading authority that the ancient rule which holds that mere non-disclosure does not constitute actionable misrepresentation “finds proper application in cases where the fact undisclosed is patent, or the plaintiff has equal opportunities for obtaining information which he may be expected to utilize, or the defendant has no reason to think that he is acting under any misapprehension” (PROSSER, *LAW OF TORTS* § 106, at 696 [4th ed., 1971]). However, with respect to transactions in real estate, New York adheres to the doctrine of caveat emptor and imposes no duty upon the vendor to disclose any information concerning the premises (*London v. Courduff*, 141 A.D.2d 803, 529 N.Y.S.2d 874) unless there is a confidential or fiduciary relationship between the parties (*Moser v. Spizzirro*, 31 A.D.2d 537, 295 N.Y.S.2d 188, *affd.*, 25 N.Y.2d 941, 305 N.Y.S.2d 153, 252 N.E.2d 632; *IBM Credit Fin. Corp. v. Mazda Motor Mfg. (USA) Corp.*, 152 A.D.2d 451, 542 N.Y.S.2d 649) or some conduct on the part of the seller which constitutes “active concealment” (see, *17 East 80th Realty Corp. v. 68th Associates*, 173 A.D.2d 245,

569 N.Y.S.2d 647 [dummy ventilation system constructed by seller]; *Haberman v. Greenspan*, 82 Misc.2d 263, 368 N.Y.S.2d 717 [foundation cracks covered by seller]). Normally, some affirmative misrepresentation (e.g., *Tahini Invs., Ltd. v. Bobrowsky*, 99 A.D.2d 489, 470 N.Y.S.2d 431 [industrial waste on land allegedly used only as farm]; *Jansen v. Kelly*, 11 A.D.2d 587, 200 N.Y.S.2d 561 [land containing valuable minerals allegedly acquired for use as campsite]) or partial disclosure (*Junius Constr. Corp. v. Cohen*, 257 N.Y. 393, 178 N.E. 672 [existence of third unopened street concealed]; *Noved Realty Corp. v. A.A.P. Co.*, 250 App.Div. 1, 293 N.Y.S. 336 [escrow agreements securing lien concealed]) is required to impose upon the seller a duty to communicate undisclosed conditions affecting the premises (contra, *Young v. Keith*, 112 A.D.2d 625, 492 N.Y.S.2d 489 [defective water and sewer systems concealed]).

7. Caveat emptor is not so all-encompassing a doctrine of common law as to render every act of non-disclosure immune from redress, whether legal or equitable. “In regard to the necessity of giving information which has not been asked, the rule differs somewhat at law and in equity, and while the law courts would permit no recovery of damages against a vendor, because of mere concealment of facts under certain circumstances, yet if the vendee refused to complete the contract because of the concealment of a material fact on the part of the other, equity would refuse to compel him so to do, because equity only compels the specific performance of a contract which is fair and open, and in regard to which all material matters known to each have been communicated to the other” (*Rothmiller v. Stein*, 143 N.Y. 581, 591-592, 38 N.E. 718 [emphasis added]). Even as a principle of law, long before exceptions were embodied in statute law (see, e.g., UCC §§ 2-312, 2-313, 2-314, 2-315; 3-417[2][e]), the doctrine was held inapplicable to contagion among animals, adulteration of food, and insolvency of a maker of a promissory note and of a tenant substituted for another under a lease (see, *Rothmiller v. Stein, supra*, at 592-593, 38 N.E. 718 and cases cited therein). Common law is not moribund. Ex facto jus oritur (law arises out of facts). Where fairness and common sense dictate that an exception should be created, the evolution of the law should not be stifled by rigid application of a legal maxim.
8. The doctrine of caveat emptor requires that a buyer act prudently to assess the fitness and value of his purchase and operates to bar the purchaser who fails to exercise due care from seeking the equitable remedy of rescission (see, e.g., *Rodas v. Manitaras*, 159 A.D.2d 341, 552 N.Y.S.2d 618). For the purposes of the instant motion to

dismiss the action pursuant to CPLR 3211(a)(7), plaintiff is entitled to every favorable inference which may reasonably be drawn from the pleadings (*Arrington v. New York Times Co.*, 55 N.Y.2d 433, 442, 449 N.Y.S.2d 941, 434 N.E.2d 1319; *Rovello v. Orofino Realty Co.*, 40 N.Y.2d 633, 634, 389 N.Y.S.2d 314, 357 N.E.2d 970), specifically, in this instance, that he met his obligation to conduct an inspection of the premises and a search of available public records with respect to title. It should be apparent, however, that the most meticulous inspection and the search would not reveal the presence of poltergeists at the premises or unearth the property's ghoulish reputation in the community. Therefore, there is no sound policy reason to deny plaintiff relief for failing to discover a state of affairs which the most prudent purchaser would not be expected to even contemplate (see, *Da Silva v. Musso*, 53 N.Y.2d 543, 551, 444 N.Y.S.2d 50, 428 N.E.2d 382).

9. The case law in this jurisdiction dealing with the duty of a vendor of real property to disclose information to the buyer is distinguishable from the matter under review. The most salient distinction is that existing cases invariably deal with the physical condition of the premises (e.g., *London v. Courduff*, supra [use as a landfill]; *Perin v. Mardine Realty Co.*, 5 A.D.2d 685, 168 N.Y.S.2d 647 *aff'd*, 6 N.Y.2d 920, 190 N.Y.S.2d 995, 161 N.E.2d 210 [sewer line crossing adjoining property without owner's consent]), defects in title (e.g., *Sands v. Kissane*, 282 App. Div. 140, 121 N.Y.S.2d 634 [remainderman]), liens against the property (e.g., *Noved Realty Corp. v. A.A.P. Co.*, supra), expenses or income (e.g., *Rodas v. Manitaras*, supra [gross receipts]) and other factors affecting its operation. No case has been brought to this court's attention in which the property value was impaired as the result of the reputation created by information disseminated to the public by the seller (or, for that matter, as a result of possession by poltergeists).
10. Where a condition which has been created by the seller materially impairs the value of the contract and is peculiarly within the knowledge of the seller or unlikely to be discovered by a prudent purchaser exercising due care with respect to the subject transaction, nondisclosure constitutes a basis for rescission as a matter of equity. Any other outcome places upon the buyer not merely the obligation to exercise care in his purchase but rather to be omniscient with respect to any fact which may affect the bargain. No practical purpose is served by imposing such a burden upon a purchaser. To the contrary, it encourages predatory business practice and offends the principle that equity will suffer no wrong to be without a remedy.

11. Defendant's contention that the contract of sale, particularly the merger or "as is" clause, bars recovery of the buyer's deposit is unavailing. Even an express disclaimer will not be given effect where the facts are peculiarly within the knowledge of the party invoking it (*Danann Realty Corp. v. Harris*, 5 N.Y.2d 317, 322, 184 N.Y.S.2d 599, 157 N.E.2d 597; *Tahini Invs., Ltd. v. Bobrowsky*, *supra*). Moreover, a fair reading of the merger clause reveals that it expressly disclaims only representations made with respect to the physical condition of the premises and merely makes general reference to representations concerning "any other matter or things affecting or relating to the aforesaid premises". As broad as this language may be, a reasonable interpretation is that its effect is limited to tangible or physical matters and does not extend to paranormal phenomena. Finally, if the language of the contract is to be construed as broadly as defendant urges to encompass the presence of poltergeists in the house, it cannot be said that she has delivered the premises "vacant" in accordance with her obligation under the provisions of the contract rider.
12. To the extent New York law may be said to require something more than "mere concealment" to apply even the equitable remedy of rescission, the case of *Junius Construction Corporation v. Cohen*, 257 N.Y. 393, 178 N.E. 672, *supra*, while not precisely on point, provides some guidance. In that case, the seller disclosed that an official map indicated two as yet unopened streets which were planned for construction at the edges of the parcel. What was not disclosed was that the same map indicated a third street which, if opened, would divide the plot in half. The court held that, while the seller was under no duty to mention the planned streets at all, having undertaken to disclose two of them, he was obliged to reveal the third (*see also, Rosenschein v. McNally*, 17 A.D.2d 834, 233 N.Y.S.2d 254).
13. In the case at bar, defendant seller deliberately fostered the public belief that her home was possessed. Having undertaken to inform the public at large, to whom she has no legal relationship, about the supernatural occurrences on her property, she may be said to owe no less a duty to her contract vendee. It has been remarked that the occasional modern cases which permit a seller to take unfair advantage of a buyer's ignorance so long as he is not actively misled are "singularly unappetizing" (PROSSER, LAW OF TORTS § 106, at 696 [4th ed. 1971]). Where, as here, the seller not only takes unfair advantage of the buyer's ignorance but has created and perpetuated a condition about which he is unlikely to even inquire, enforcement of the contract (in whole or in part) is offensive to the court's sense of equity. Application of the remedy of rescission, within the bounds of the narrow exception to the doctrine of caveat

emptor set forth herein, is entirely appropriate to relieve the unwitting purchaser from the consequences of a most unnatural bargain.

14. Accordingly, the judgment of the Supreme Court, New York County (Edward H. Lehner, J.), entered April 9, 1990, which dismissed the complaint pursuant to CPLR 3211(a)(7), should be modified, on the law and the facts and in the exercise of discretion, and the first cause of action seeking rescission of the contract reinstated, without costs.

All concur except MILONAS, J.P. and SMITH, J., who dissent in an opinion by SMITH, J.

SMITH, Justice (dissenting).

15. I would affirm the dismissal of the complaint by the motion court.
16. Plaintiff seeks to rescind his contract to purchase defendant Ackley's residential property and recover his down payment. Plaintiff alleges that Ackley and her real estate broker, defendant Ellis Realty, made material misrepresentations of the property in that they failed to disclose that Ackley believed that the house was haunted by poltergeists. Moreover, Ackley shared this belief with her community and the general public through articles published in Reader's Digest (1977) and the local newspaper (1982). In November 1989, approximately two months after the parties entered into the contract of sale but subsequent to the scheduled October 2, 1989 closing, the house was included in a five-house walking tour and again described in the local newspaper as being haunted.
17. Prior to closing, plaintiff learned of this reputation and unsuccessfully sought to rescind the \$650,000 contract of sale and obtain return of his \$32,500 down payment without resort to litigation. The plaintiff then commenced this action for that relief and alleged that he would not have entered into the contract had he been so advised and that as a result of the alleged poltergeist activity, the market value and resaleability of the property was greatly diminished. Defendant Ackley has counterclaimed for specific performance.
18. "It is settled law in New York that the seller of real property is under no duty to speak when the parties deal at arm's length. The mere silence of the seller, without some act or conduct which deceived the purchaser, does not amount to a concealment that is

actionable as a fraud (see *Perin v. Mardine Realty Co., Inc.*, 5 A.D.2d 685, 168 N.Y.S.2d 647, *aff'd.*, 6 N.Y.2d 920, 190 N.Y.S.2d 995, 161 N.E.2d 210; *Moser v. Spizzirro*, 31 A.D.2d 537, 295 N.Y.S.2d 188, *aff'd.*, 25 N.Y.2d 941, 305 N.Y.S.2d 153, 252 N.E.2d 632). The buyer has the duty to satisfy himself as to the quality of his bargain pursuant to the doctrine of *caveat emptor*, which in New York State still applies to real estate transactions.” *London v. Courduff*, 141 A.D.2d 803, 804, 529 N.Y.S.2d 874, *app. disp'd.*, 73 N.Y.2d 809, 537 N.Y.S.2d 494, 534 N.E.2d 332 (1988).

19. The parties herein were represented by counsel and dealt at arm's length. This is evidenced by the contract of sale which, inter alia, contained various riders and a specific provision that all prior understandings and agreements between the parties were merged into the contract, that the contract completely expressed their full agreement and that neither had relied upon any statement by anyone else not set forth in the contract. There is no allegation that defendants, by some specific act, other than the failure to speak, deceived the plaintiff. Nevertheless, a cause of action may be sufficiently stated where there is a confidential or fiduciary relationship creating a duty to disclose and there was a failure to disclose a material fact, calculated to induce a false belief. *County of Westchester v. Welton Becket Assoc.*, 102 A.D.2d 34, 50-51, 478 N.Y.S.2d 305, *aff'd.*, 66 N.Y.2d 642, 495 N.Y.S.2d 364, 485 N.E.2d 1029 (1985). However, plaintiff herein has not alleged and there is no basis for concluding that a confidential or fiduciary relationship existed between these parties to an arm's length transaction such as to give rise to a duty to disclose. In addition, there is no allegation that defendants thwarted plaintiff's efforts to fulfill his responsibilities fixed by the doctrine of *caveat emptor*. See *London v. Courduff*, *supra*, 141 A.D.2d at 804, 529 N.Y.S.2d 874.
20. Finally, if the doctrine of *caveat emptor* is to be discarded, it should be for a reason more substantive than a poltergeist. The existence of a poltergeist is no more binding upon the defendants than it is upon this court.
21. Based upon the foregoing, the motion court properly dismissed the complaint.

Obde v. Schlemeyer

Supreme Court of Washington
56 Wash. 2d 449, 353 P.2d 672

FINLEY, Judge.

1. Plaintiffs, Mr. and Mrs. Fred Obde, brought this action to recover damages for the alleged fraudulent concealment of termite infestation in an apartment house purchased by them from the defendants, Mr. and Mrs. Robert Schlemeyer. Plaintiffs assert that the building was infested at the time of the purchase; that defendants were well apprised of the termite condition, but fraudulently concealed it from the plaintiffs.
2. After a trial on the merits, the trial court entered findings of fact and conclusions of law sustaining the plaintiffs' claim, and awarded them a judgment for damages in the amount of \$3,950. The defendants appealed. Their assignments of error may be compartmentalized, roughly, into two categories: (1) those going to the question of liability, and (2) those relating to the amount of damages to be awarded if liability is established.
3. First, as to the question of liability: The Schlemeyers concede that, shortly after they purchased the property from a Mr. Ayars on an installment contract in April 1954, they discovered substantial termite infestation in the premises. The Schlemeyers contend, however, that they immediately took steps to eradicate the termites, and that, at the time of the sale to the Obdes in November 1954, they had no reason to believe that these steps had not completely remedied the situation. We are not convinced of the merit of this contention.
4. The record reveals that when the Schlemeyers discovered the termite condition they engaged the services of a Mr. Senske, a specialist in pest control. He effected some measures to eradicate the termites, and made some repairs in the apartment house. Thereafter, there was no easily apparent or surface evidence of termite damage. However, portions of the findings of fact entered by the trial court read as follows:

Senske had advised Schlemeyer that in order to obtain a complete job it would be necessary to drill the holes and pump the fluid into all parts of the basement floors as well as the basement walls. Part of the basement was used

as a basement apartment. Senske informed Schlemeyer that the floors should be taken up in the apartment and the cement flooring under the wood floors should be treated in the same manner as the remainder of the basement. Schlemeyer did not care to go to the expense of tearing up the floors to do this and therefore this portion of the basement was not treated.

Senske also told Schlemeyer even though the job were done completely, including treating the portion of the basement which was occupied by the apartment, to be sure of success, it would be necessary to make inspections regularly for a period of a year. Until these inspections were made for this period of time the success of the process could not be determined. Considering the job was not completed as mentioned, Senske would give Schlemeyer no assurance of success and advised him that he would make no guarantee under the circumstances.

5. No error has been assigned to the above findings of fact. Consequently, they will be considered as the established facts of the case, *Lewis v. Scott*, 1959, 154 Wash. Dec. 509, 341 P.2d 488. The pattern thus established is hardly compatible with the Schlemeyers' claim that they had no reason to believe that their efforts to remedy the termite condition were not completely successful.
6. The Schlemeyers urge that, in any event, as sellers, they had no duty to inform the Obdes of the termite condition. They emphasize that it is undisputed that the purchasers asked no questions respecting the possibility of termites. They rely on a Massachusetts case involving a substantially similar factual situation, *Swinton v. Whitinsville Savings Bank*, 1942, 311 Mass. 677, 42 N.E.2d 808, 141 A.L.R. 965. Applying the traditional doctrine of *caveat emptor*—namely, that, as between parties dealing at arms length (as vendor and purchaser), there is no duty to speak, in the absence of a request for information—the Massachusetts court held that a vendor of real property has no duty to disclose to a prospective purchaser the fact of a latent termite condition in the premises.
7. Without doubt, the parties in the instant case were dealing at arms length. Nevertheless, and notwithstanding the reasoning of the Massachusetts court above noted, we are convinced that the defendants had a duty to inform the plaintiffs of the termite condition. In *Perkins v. Marsh*, 1934, 179 Wash. 362, 37 P.2d 689, 690, a case involving parties dealing at arm's length as landlord and tenant, we held that,

Where there are concealed defects in demised premises, dangerous to the property, health, or life of the tenant, which defects are known to the landlord when the lease is made, but unknown to the tenant, and which a careful examination on his part would not disclose, it is the landlord's duty to disclose them to the tenant before leasing, and his failure to do so amounts to a fraud.

8. We deem this rule to be equally applicable to the vendor-purchaser relationship. See Keeton, *Fraud-Concealment and Non-Disclosure*, 15 TEX. L. REV. 1, 14-16 (1936). In this article Professor Keeton also aptly summarized the modern judicial trend away from a strict application of *caveat emptor* by saying:

It is of course apparent that the content of the maxim "caveat emptor," used in its broader meaning of imposing risks on both parties to a transaction, has been greatly limited since its origin. When Lord Cairns stated in *Peek v. Gurney* that there was no duty to disclose facts, however morally censurable their non-disclosure may be, he was stating the law as shaped by an individualistic philosophy based upon freedom of contract. It was not concerned with morals. In the present stage of the law, the decisions show a drawing away from this idea, and there can be seen an attempt by many courts to reach a just result in so far as possible, but yet maintaining the degree of certainty which the law must have. The statement may often be found that if either party to a contract of sale conceals or suppresses a material fact which he is in good faith bound to disclose then his silence is fraudulent.

The attitude of the courts toward non-disclosure is undergoing a change and contrary to Lord Cairns' famous remark it would seem that the object of the law in these cases should be to impose on parties to the transaction a duty to speak whenever justice, equity, and fair dealing demand it.

9. A termite infestation of a frame building, such as that involved in the instant case, is manifestly a serious and dangerous condition. One of the Schlemeyers' own witnesses, Mr. Hoefer, who at the time was a building inspector for the city of Spokane, testified that "...if termites are not checked in their damage, they can cause a complete collapse of a building, ... they would simply eat up the wood." Further, at the time of the sale of the premises, the condition was clearly latent—not readily observable upon reasonable inspection. As we have noted, all superficial or surface evidence of the condition had been removed by reason of the efforts of Senske, the

pest control specialist. Under the circumstances, we are satisfied that “justice, equity, and fair dealing,” to use Professor Keeton's language, demanded that the Schlemeyers speak—that they inform prospective purchasers, such as the Obdes, of the condition, regardless of the latter's failure to ask any questions relative to the possibility of termites.

10. Error has been assigned to the trial court's finding that Mrs. Schlemeyer knew of the termite condition and participated with her husband in the sale to the Obdes. However, this assignment of error has not been argued in the appeal brief. Thus, it must be deemed to have been abandoned. *Winslow v. Mell*, 1956, 48 Wash.2d 581, 295 P.2d 319, and cases cited therein.
11. Schlemeyers' final contentions, relating to the issue of liability, emphasize the Obdes' conduct after they discovered the termite condition. Under the purchase agreement with the Schlemeyers, the Obdes paid \$5,000 in cash, and gave their promissory note for \$2,250 to the Schlemeyers. In addition, they assumed the balance due on the installment contract, under which the Schlemeyers had previously acquired the property from Ayars. This amounted to \$34,750. After they discovered the termites (some six weeks subsequent to taking possession of the premises in November 1954), the Obdes continued for a time to make payments on the Ayars contract. They then called in Senske to examine the condition—not knowing that he had previously worked on the premises at the instance of the Schlemeyers. From Senske the Obdes learned for the first time that the Schlemeyers had known of the termite infestation prior to the sale. Obdes then ceased performance of the Ayars contract, and allowed the property to revert to Ayars under a forfeiture provision in the installment contract.
12. The Schlemeyers contend that by continuing to make payments on the Ayars contract after they discovered the termites the Obdes waived any right to recovery for fraud. This argument might have some merit if the Obdes were seeking to rescind the purchase contract. *Salter v. Heiser*, 1951, 39 Wash. 2d 826, 239 P.2d 327. However, this is not an action for rescission; it is a suit for damages, and thus is not barred by conduct constituting an affirmation of the contract. *Salter v. Heiser, supra*.
13. Contrary to the Schlemeyers final argument relative to the question of liability, the Obdes' ultimate default and forfeiture on the Ayars contract does not constitute a bar to the present action. The rule governing this issue is well stated in 24 Am.Jur. 39, Fraud and Deceit, § 212, as follows:

Since the action of fraud or deceit in inducing the entering into a contract or procuring its execution is not based upon the contract, but is independent thereof, although it is regarded as an affirmance of the contract, it is a general rule that a vendee is entitled to maintain an action against the vendor for fraud or deceit in the transaction even though he has not complied with all the duties imposed upon him by the contract. His default is not a bar to an action by him for fraud or deceit practiced by the vendor in regard to some matter relative to the contract.

See, also, Annotation, 74 A.L.R. 169; *cf. Conaway v. Co-Operative Homebuilders*, 1911, 65 Wash. 39, 117 P. 716.

14. For the reasons hereinbefore set forth, we hold that the trial court committed no error in determining that the respondents (Obdes) were entitled to recover damages against the appellants (Schlemeyers) upon the theory of fraudulent concealment. However, there remains the question of the proper amount of damages to be awarded. The trial court found that,

...because of the termite condition the value [of the premises] has been reduced to the extent of \$3950.00 and the plaintiffs have been damaged to that extent, and in that amount.

15. As hereinbefore noted, judgment was thereupon entered for the respondents in that amount.
16. The appellants concede that the measure of damages in a case of this type is the difference between the actual value of the property and what the property would have been worth had the misrepresentations been true. *Salter v. Heiser, supra*, and cases cited therein. However, they urge that the only evidence introduced to show the diminution in value of the premises on account of the termite condition—namely, the testimony of one Joseph P. Wieber—was incompetent. Wieber qualified as an expert witness on the basis of substantial experience as a realtor and appraiser. He examined the premises in question, and estimated that the termite condition had reduced the value of the property by some thirty per cent. Applying this estimate to an assumption (as posed in a hypothetical question propounded by respondents' counsel) that the property had been purchased twice during the year 1954 by persons who were unaware of the termite condition for approximately \$40,000, Wieber rendered an

opinion that the actual value of the premises (taking into account the termite condition) was about \$25,000.

17. Appellants' sole objection to Wieber's testimony is based upon a claim that the facts (two purchases in 1954 for approximately \$40,000, by persons who were unaware of the termite condition) supporting the hypothetical question were never supplied. We find no merit in this claim. The record fully discloses the two purchases in question: namely, the Obdes' purchase from the Schlemeyers in November 1954; and the Schlemeyers' purchase from Ayars in April 1954.
18. The judgment awarding damages of \$3,950 is well within the limits of the testimony in the record relating to damages. The Obdes have not cross-appealed. The judgment of the trial court should be affirmed in all respects. It is so ordered.

WEAVER, C. J., and ROSELLINI and FOSTER, JJ., concur. HILL, J., concurs in the result.

L&N Grove v. Chapman

District Court of Appeal of Florida
291 So. 2d 217 (1974)

BOARDMAN, Judge.

1. Appellants/defendants, Paul L. Curtis and his wife and L & N Grove, Inc. (hereinafter Curtis) seeks this timely review of an adverse final judgment of the trial judge in which Curtis was declared to be constructive trustee of the real property in question for appellees/plaintiffs, Robert L. Chapman, Jr., et al. (hereinafter Chapman).
2. The second amended complaint was filed by Chapman on November 5, 1970, to rescind the contract and deed and to impose a constructive trust on the property in favor of Chapman, alleging therein, *inter alia*, that Curtis was the real estate broker for Chapman and that he breached the fiduciary relationship by failing to disclose certain material facts, principally the impact of Walt Disney World on the value of the property involved here.
3. The basic facts are not in serious dispute. During the summer of 1966 Curtis, who was an active real estate broker with offices in Orlando, contacted Chapman concerning the purchase of a 10-acre tract of land located in Lake County and legally described as:

That part West of U.S. #27 of the South Half of the NE 1/4 of the SE 1/4 of Section 35, Township 24 South Range 26 East, less the northerly 15 feet thereof, being 10 acres more or less.

The property is situated north of and contiguous to a 22-acre tract that Curtis had purchased previously. Both parcels of land are located on U.S. Highway 27 near what was designated as State Road #530, now U.S. Highway 192.

4. Chapman is also a real estate broker with offices in St. Petersburg and was a member of the partnership that owned the subject property and spokesman for the partnership in this transaction.
5. After a period of negotiations between the parties concerning the purchase of the real property, on or about August 1, 1966, an agreement was reached and Chapman agreed, after submitting Curtis' offer to the other members of the partnership, to sell

the land involved to Curtis. The said agreement was confirmed by letter dated August 3, 1966, from Curtis to Dr. Pollard, a member of the partnership, with copy of said letter being mailed to Chapman. In addition, the letter advised that Curtis was acting “. . . as a Broker and a principal and would look to (his) group for a commission compensation.” The contract for sale and purchase of the land was subsequently prepared and, in due course, executed by Chapman on August 23, 1966, and by Curtis on August 16, 1966. We call attention at this point to the fact that the buyer designated in the contract was Paul L. Curtis, or assigns.

6. The purchase price agreed upon was \$47,500, which appears to have been one and one half times the then market value of the land for grove purposes. The contract provided that Chapman would maintain the grove and be entitled to the fruit crop under the conditions set forth in ‘SCHEDULE A’ which was attached to the said contract.
7. In August, 1966, Curtis had formed L & N Grove, Inc., with one other person named Odell Warren, each owning 50% of the corporation. The corporation was organized for the purpose of acquiring title to the real property involved here and the 22-acre tract of land referred to above. The corporation was dissolved on August 20, 1970. The warranty deed, mortgage and note were recorded among the public records of Lake County on December 14, 1966. L & N Grove, Inc. was the grantee named in the deed. The mortgage and note were signed by Curtis as president of the corporation.
8. The complete terms and conditions of the sale are not necessarily pertinent. We mention that the mortgage was payable annually, covering a period of seven years. The mortgage payments due in June of 1967, 1968, 1969, and 1970, were paid to Chapman or his assignee. The payment due in June of 1971 was refused by Chapman's assignee.
9. This is the third appearance of this cause before this court.¹ This appeal followed from entry of the final judgment.

¹This court reversed the trial court's holding that a bond was required in connection with the lis pendens because plaintiffs/appellees were claiming against their own deed stating that the claim was ‘founded on a duly recorded instrument.’ 244 So.2d 154. After trial, final judgment in favor of appellees was entered and appellants filed several post-trial motions, including a motion to vacate and set aside judgment for want of indispensable parties, which the trial court granted. This holding resulted in another interlocutory appeal wherein this court held that L & N Grove, Inc., was not dissolved until August 20, 1970, that the cause did not abate, and that the trustees of the corporation

10. It is, of course, necessary to prove the existence of a constructive trust by clear and convincing evidence. *Carberry v. Foley*, Fla.App.3rd, 1968, 213 So.2d 635. The doctrine of constructive trust is well established in Florida law and the courts of this state will impose the same where ‘ . . . through actual fraud, abuse of confidence reposed and accepted, to through other questionable means gains something for himself which in equity and good conscience he should not be permitted to hold. . . .’ *Quinn v. Phipps*, 93 Fla. 805, 113 So. 419, 422 (1927). We also are aware that it is not within the province of this court to substitute its judgment for that of the trier of the facts unless the record clearly reflects that the findings and conclusions by the trial court are erroneous. *Old Equity Life Insurance Co. v. Levenson*, Fla.App.3rd, 1965, 177 So.2d 50; *In re Estate of Hobein*, Fla.App.1st, 1970, 238 So.2d 497; *Griffith Services, Inc. v. Walter Kidde Constructors, Inc.*, Fla.App.1st, 1972, 262 So.2d 240. Against this background of general and accepted principles, we turn then to the particular situation presented in the case sub judice.

11. We have carefully considered the records, briefs, the authorities cited and discussed therein and arguments of respective counsel and conclude, for reasons delineated hereinafter, that reversible error has been demonstrated.

12. The trial court made a finding of fact in the final judgment as follows:

It is beyond question that Paul Curtis had knowledge of the impact which Walt Disney World would have on the value of this property...

The trial court further found that Curtis failed to disclose that fact to Chapman. This is the finding of fact that has caused us great concern. We submit that after many readings of the record this finding of fact is not supported by substantial competent evidence.

13. The central and perhaps the sole question for our decision is what inside information does the record disclose that Curtis had that he did not disclose to Chapman and that he had a duty to disclose to him. There is not a scintilla of evidence in the record that we have been able to find that shows Curtis knew in 1966 what effect the Disney project would have on the value of the property. It is, of course, Chapman's contention that Curtis knew said property was immediately adjacent to the proposed

were not indispensable parties and ordered the trial court to reinstate the final judgment and to hear and rule on the pending post-decretal motions. 265 So.2d 725. Thereafter, final judgment was entered and the post-decretal motions denied.

widening and reconstruction of U.S. Highway 27 and that a cloverleaf exchange was to be constructed on said highway with its intersection with State Road #530.

14. In 1966 it is extremely doubtful that anyone knew if Walt Disney World would ever be developed into a reality. It was only on the drawing boards at that particular time. There can be no serious doubt that the Walt Disney World project was announced sometime in the fall of 1965, many months prior to the sale of the property involved here. Perhaps it is not significant that Curtis testified that the Disney announcement was the biggest announcement in the history of Florida real estate and resounded around the world. We believe it highly plausible and reasonable to glean from the record that Chapman likewise had this knowledge, or by the exercise of reasonable diligence could have acquired it. We believe the announcement was one of general public knowledge. The alleged information that Curtis is charged with having withheld was speculative in nature and clearly available to the parties involved here.
15. It was not until 1970 that construction of Walt Disney World had actually been commenced and the Central Florida real estate boom hit with full impact that this present action was filed by Chapman. In the interim period of time the record shows that Chapman accepted the terms of the mortgage and payments made thereon.
16. Notwithstanding the above-recited matters, the trial judge found breach of duty even if the broker-employer relationship did not exist. In this connection, the trial court found that that relationship at one time did exist between the parties. As Curtis concedes, this finding is not assailable. We submit that the record definitely shows that at the time the contract of sale was executed Chapman was advised of the fact that Curtis was acting as a principal in the transaction. The trial judge found, however:

Irrespective of any technical brokerage relationship, defendant Curtis, as a registered real estate broker, owed plaintiffs the duty of acting honestly and fairly in his dealings with them.

17. It is agreed that there is an abundance of case law supporting this finding, as well as learned treatises, but, the question is, is the finding supported by competent evidence. We cannot find wherein Curtis failed to act honestly and fairly with Chapman. Here the transaction from its conception to its consummation was negotiated between Curtis and Chapman. Both parties, as stated, are real estate brokers and must be

considered as being fully aware of the duties, responsibilities and ethics of their time-honored profession.

18. Lest it be overlooked, Chapman cannot be thought of as a stranger to this area of the state. It would be naiveté to reach such a conclusion. The record shows that he has an interest in over 600 acres of land in the immediate vicinity of the subject property—433 acres on the west side of U.S. Highway 27, which lands had been in possession of Chapman and relatives for approximately 20 years, about 180 acres of which have been used for citrus purposes and, additionally, had an interest in approximately 178 acres immediately across the highway and west of the 433 acres. The latter tract was purchased by the partnership, of which Chapman was a member, in 1962. Furthermore, Chapman is a real estate broker and a housing consultant accredited by the U.S. Department of Housing and Urban Development.
19. The remedy of rescission requires that the reliance be justified. A representee who has expert knowledge of the general subject matter, and is peculiarly fitted and qualified, by knowledge and experience, to evaluate that which he sees and appreciate the obvious falsity of the claimed representation does not have the right to rely on a representation. *Puget Sound National Bank v. McMahon*, 53 Wash.2d 51, 330 P.2d 559 (1958).
20. In view of this fact, perhaps standing alone, it is difficult to reconcile the trial judge's finding that Curtis had all the alleged information and withheld it from Chapman, who is depicted as being completely ignorant and innocent of the land market in this area.
21. Chapman asserts that he believed that Curtis purchased the land for grove purposes. The testimony of the parties and the documentary evidence indicate to us that the land in issue was purchased for speculative purposes and it is not unreasonable for us to conclude that Chapman was aware of this fact. We point out again that the contract documents provide that Chapman was to retain possession of the fruit under the conditions provided in the contract.
22. Now, it is true that during the negotiations for the purchase of this land Curtis had hoped that State Road #530 would be the entrance to Walt Disney World and that he attempted to ascertain this information. He had a dream and some five years later it became a reality. This case appears to be a classic example of the old cliché that hindsight is better than foresight. As Chapman testified on cross-examination:

... If I had fully realized the effect of Disney World on that property, I would not have sold it. If I had had adequate information to make a judgment, we-I would not have been a party to its sale.

23. Chapman further testified that in 1968 he attempted to make inquiries of the State Road Department, “. . . Smith, Reynolds & Hill,” (sic) engineers, concerning a certain configuration taking place on the highway and he got enough conflicting stories as to what was and wasn't planned to be at a loss to understand or even if anything was definite. It appears that Chapman was negotiating an option with Humble Oil Company for a lease on some other property Chapman owned and was attempting to find out if U.S. Highway 27 would be widened and four-laned and the interchange constructed in the area. The property Chapman owned abutting U.S. Highway 27 is a relatively short distance from the intersection of U.S. Highway 27 and State road #530.

24. The case of *Chisman v. Moylan*, Fla. App. 2d, 1958, 105 So. 2d 186, is cited in the final judgment and by both parties in their briefs. We agree with that decision and the cases cited therein. We are impressed by the language in the court's opinion where it is held:

... Neither a judgment nor a decree, however, should be entered in favor of an employer or a principal who complains that he has been injured by breach of duty by a broker where the complaint appears to be founded on conjecture, suspicion, or speculation. (105 So. 2d 186, 189).

25. Chapman's testimony amounts to just that, for he does not testify or prove by other witnesses or documentary evidence that Curtis had specific inside information that State Road #530 would either be four-laned or become the entrance to Walt Disney World. His testimony in this regard is based purely on conjecture, suspicion, or speculation.

26. In the light of our decision we do not think it necessary to discuss the remaining points raised by Curtis on appeal. We do mention that it is quite apparent from the record that cancellation and rescission, returning the parties to their original position, due to the passage of time, intervening probable equities, would make a just settlement of the transaction a very difficult, if not an impossible task.

27. Lastly, but importantly, the court truly expresses its appreciation to the trial judge and attorneys representing the parties litigant for the exemplary manner in which this case was litigated in the trial court. The briefs of counsel filed in support of their respective contentions were superbly presented and oral argument to this court was presented most ably and was of invaluable assistance.
28. Accordingly, for the reasons above stated, the order appealed from is reversed and the trial court directed to enter judgment in favor of Curtis. Each party is required to bear his own cost and expenses incurred in this litigation.

Reversed.

Monetti, S.P.A. v. Anchor Hocking Corporation

United States Court of Appeals, Seventh Circuit
931 F.2d 1178 (1991)

POSNER, Circuit Judge.

1. This is a diversity suit for breach of contract; the parties agree that Illinois law governs the substantive issues. The district judge dismissed the suit, on the defendant's motion for summary judgment, as barred by the statute of frauds, and also refused to allow the plaintiffs to amend their complaint to add a claim of promissory estoppel. The appeal, which challenges both rulings, presents difficult and important questions concerning both the general Illinois statute of frauds, Ill.Rev.Stat. ch. 59, ¶ 1, and the statute of frauds in the Uniform Commercial Code, UCC § 2-201, adopted by Illinois in Ill.Rev.Stat. ch. 26, ¶ 2-201.
2. The plaintiffs are Monetti, an Italian firm that makes decorative plastic trays and related products for the food service industry, and a wholly owned subsidiary, Melform U.S.A., which Monetti set up in 1981 to market its products in the U.S. In 1984, Monetti began negotiations with a father-and-son team, the Schneiders, importers of food service products, to grant the Schneiders the exclusive right to distribute Monetti's products in the United States and in connection with this grant to turn over to them Melform's tangible and intangible assets. While these negotiations were proceeding, the Schneiders sold their importing firm to Anchor Hocking, the defendant, and their firm became a division of Anchor Hocking, though—at first—the Schneiders remained in charge. In the fall of 1984, the younger Schneider, who was handling the negotiations with Monetti for his father and himself, sent Monetti a telex requesting preparation of an agreement “formalizing our [i.e., Anchor Hocking's] exclusive for the United States.” In response, Monetti terminated all of Melform's distributors and informed all of Melform's customers that Anchor would become the exclusive U.S. distributor of Monetti products on December 31, 1984.
3. On December 18, the parties met, apparently for the purpose of making a final agreement. Monetti—which incidentally was not represented by counsel at the meeting—submitted a draft the principal provisions of which were that Anchor Hocking would be the exclusive distributor of Monetti products in the U.S., the contract would last for ten years, and during each of these years Anchor Hocking would make specified minimum purchases of Monetti products, adding up to \$27

million over the entire period. No one from Anchor Hocking signed this or any other draft of the agreement. However, the record contains a memo, apparently prepared for use at the December 18 meeting, entitled “Topics of Discussion With Monetti.” The memo's first heading is “Exclusive Agreement-Attachment # 1”—a reference to an attached draft which is identical to the Monetti draft except for two additional, minor paragraphs added in handwriting. Under the heading appears the notation “Agree” beside each of the principal paragraphs of the agreement, with one exception: beside the first paragraph, the provision for exclusivity, the notation is “We want Canada” (i.e., exclusive distribution rights in Canada as well as in the U.S.). On the bottom of the left-hand side of the last page appears the legend “SS/mh”—indicating that the younger Schneider (Steve Schneider) had dictated the memo to a secretary.

4. Shortly after the December 18 meeting, Monetti—which had already, remember, terminated Melform's distributors and informed Melform's customers that Anchor Hocking would be the exclusive distributor of Monetti products in the United States as of the last day of 1984—turned over to Anchor Hocking all of Melform's inventory, records, and other physical assets, together with Melform's trade secrets and know-how.
5. Several months later, in May 1985, Anchor Hocking abruptly fired the Schneiders. Concerned about the possible implications of this *démarche* for its relationship with Anchor Hocking, Monetti requested a meeting between the parties, and it was held on May 19. Reviewing the events up to and including that meeting, a memo dated June 12, 1985, from Raymond Davis, marketing director of Anchor Hocking's food services division, to the law department of Anchor Hocking, states that “In the middle to latter part of 1984 Irwin Schneider and his company were negotiating an agreement with [Monetti and Melform] to obtain exclusive distribution rights on Melform's plastic tray product line in the United States”; “later, this distribution agreement was expanded to also include Canada, the Caribbean and Central and South America”; there had been many meetings between the parties, including the meeting of May 19 (at which Davis had been present); “Exhibit A (attached) represents the summary agreement that was reached in the meeting. You will notice that I have added some handwritten changes which I believe represents more clearly our current position regarding the agreement.... Now that we have had our ‘New Management’ [i.e., the management team that had replaced the Schneiders] meeting with Monetti, both parties would like to have a written and signed agreement to guide this new relationship.” Exhibit A to the Davis memo is identical to Attachment # 1 to Steve

Schneider's memo, except that it contains the handwritten changes to which the Davis memo refers. Shortly after this memo was written, the parties' relationship began to deteriorate, and eventually Monetti sued for breach of contract.

6. Illinois' general statute of frauds forbids a suit upon an agreement that is not to be performed within a year "unless the promise or agreement upon which such action shall be brought, or some memorandum or note thereof, shall be in writing, and signed by the party to be charged therewith, or some other person thereunto by him lawfully authorized." The statute of frauds in Article 2 of the Uniform Commercial Code makes a contract for the sale of goods worth at least \$500 unenforceable "unless there is some writing sufficient to indicate that a contract for sale has been made between the parties and signed by the party against whom enforcement is sought or by his authorized agent or broker." The differences between these formulations are subtle but important. The Illinois statute requires that the writing "express the substance of the contract with reasonable certainty." *Frazer v. Howe*, 106 Ill. 564, 574 (1883); see also *Holsz v. Stephen*, 362 Ill. 527, 532, 200 N.E. 601, 603 (1936); *Mariani v. School Directors*, 154 Ill.App.3d 404, 407, 107 Ill.Dec. 90, 92, 506 N.E.2d 981, 983 (1987). The UCC statute of frauds does not require that the writing contain the terms of the contract. Ill.Code Comment 1 to UCC § 2-201. In fact it requires no more than written corroboration of the alleged oral contract. Even if there is no such signed document, the contract may still be valid "with respect to goods ... which have been received and accepted." § 2-201(3)(c). This provision may appear to narrow the statute of frauds still further, but if anything it curtails a traditional exception, and one applicable to Illinois' general statute: the exception for partial performance, on which see, for example, *Payne v. Mill Race Inn*, 152 Ill.App.3d 269, 277-78, 105 Ill.Dec. 324, 330-331, 504 N.E.2d 193, 199-200 (1987); *Grundy County National Bank v. Westfall*, 13 Ill.App.3d 839, 845, 301 N.E.2d 28, 32 (1973). The Uniform Commercial Code does not treat partial delivery by the party seeking to enforce an oral contract as a partial performance of the *entire* contract, allowing him to enforce the contract with respect to the undelivered goods.
7. Let us postpone the question of partial performance for a moment and focus on whether there was a signed document of the sort that the statutes of frauds require. The judge, over Monetti's objection, refused to admit oral evidence on this question. He was right to refuse. The use of oral evidence to get round the requirement of a writing would be bootstrapping, would sap the statute of frauds of most of its force, and is therefore forbidden. *Western Metals Co. v. Hartman Co.*, 303 Ill. 479, 485, 135

N.E. 744, 746 (1922); *R.S. Bennett & Co. v. Economy Mechanical Industries, Inc.*, 606 F.2d 182, 186 n. 4 (7th Cir.1979); *Bazak International Corp. v. Mast Industries, Inc.*, 73 N.Y.2d 113, 117-18, 538 N.Y.S.2d 503, 505, 535 N.E.2d 633, 635 (1989). *The Hip Pocket, Inc. v. Levi Strauss & Co.*, 144 Ga.App. 792, 793, 242 S.E.2d 305, 306 (1978), is *contra*, but does not discuss the question and is, we think, wrong; while *Impossible Electronic Techniques, Inc. v. Wackenhut Protective Systems, Inc.*, 669 F.2d 1026, 1034 (5th Cir.1982), on which Monetti also relies, is distinguishable from our case because there the writing was first held to satisfy the statute of frauds and only then was oral evidence admitted to clear up a detail, albeit a vital one—the identity of one of the parties!

8. Although we have cited cases from different jurisdictions, the question whether oral evidence is admissible to show that an ambiguous document satisfies the requirements of the statute of frauds is ultimately one of state law. So far as we have been able to discover, the question is uniformly assumed to be substantive rather than procedural for purposes of determining, in accordance with the *Erie* doctrine, whether state or federal law applies, though direct authority on the question is sparse. *Lehman v. Dow, Jones & Co.*, 606 F.Supp. 1152, 1156 (S.D.N.Y.1985); *McInnis v. A.M.F., Inc.*, 765 F.2d 240, 245 (1st Cir. 1985) (dictum); 19 Charles Alan Wright, Arthur R. Miller & Edward H. Cooper, *Federal Practice and Procedure* § 4512, at pp. 194-95 (1982). We think the assumption is well founded, although the point is not crucial in this case because neither party questions the applicability of Illinois law. It is true that a statute of frauds is procedural in form and that its main proximate goal is evidentiary; it is largely based on distrust of the ability of juries to determine the truth of testimony that there was or was not a contract. 2 E. Allan Farnsworth, *Farnsworth on Contracts* § 6.1, at p. 85 (1990). But it is usually and we think correctly regarded as a part of contract law, not of general procedural law. Cf. *Harbor Ins. Co. v. Continental Bank Corp.*, 922 F.2d 357, 364 (7th Cir.1990). It is designed to make the contractual process cheaper and more certain by encouraging the parties to contracts to memorialize their agreement. The end of the statute of frauds thus is substantive (albeit the means is procedural), which makes essential aspects of the administration of the statute, such as the admissibility of oral evidence to disambiguate an ambiguous document that is contended to satisfy the statute of frauds, a matter of primary concern to the states rather than to the federal government. So Illinois law applies to the issue; and *Western Metals* indicates that Illinois courts would not allow oral evidence to be used to enable a vague document to satisfy the statute of frauds.

9. Because oral evidence was inadmissible on the question whether the documents meet the requirements of the statutes of frauds, it was proper for the judge to resolve it on motion for summary judgment. The parties agree that, if this was proper, our review is plenary. This does not follow, however, from the documentary character of the issue, *Anderson v. City of Bessemer City*, 470 U.S. 564, 105 S.Ct. 1504, 84 L.Ed.2d 518 (1985), as the parties may believe. But in view of the parties' agreement concerning the proper scope of our review, we need not resolve the matter, beyond noting that there is authority, illustrated by the *Bazak* case, for regarding the issue as one of law, not fact—and if it is an issue of law, then our review is indeed plenary.
10. We have two documents (really, two pairs of documents) to consider. The first is Steve Schneider's "Topics for Discussion" memo with its "Attachment ## 1." Since "signed" in statute-of-frauds land is a term of art, meaning executed or adopted by the defendant, *Weston v. Myers*, 33 Ill. 424, 433 (1864); UCC § 1-201(39) and Ill.Code Comment thereto; 2 *Farnsworth on Contracts, supra*, § 6.8, at p. 144, Schneider's typed initials are sufficient. The larger objection is that the memo was written before the contract—any contract—was made. The memo indicates that Schneider (an authorized representative of the defendant) agrees to the principal provisions in the draft agreement prepared by Monetti, but not to all the provisions; further negotiations are envisaged. There was no contract when the memo was prepared and signed, though it is fair to infer from the memo that a contract much like the draft attached to it would be agreed upon—if Monetti agreed to Anchor Hocking's demand for Canada, as Monetti concedes (and the Davis memo states) it did.
11. Can a memo that precedes the actual formation of the contract ever constitute the writing required by the statute of frauds? Under the Uniform Commercial Code, why not? Its statute of frauds does not require that any contracts "be in writing." All that is required is a document that provides solid evidence of the existence of a contract; the contract itself can be oral. Three cases should be distinguished. In the first, the precontractual writing is merely one party's offer. We have held, interpreting Illinois' version of the Uniform Commercial Code, that an offer won't do. *R.S. Bennett & Co. v. Economy Mechanical Industries, Inc., supra*, 606 F.2d at 186. Otherwise there would be an acute danger that a party whose offer had been rejected would nevertheless try to use it as the basis for a suit. The second case is that of notes made in preparation for a negotiating session, and this is another plausible case for holding the statute unsatisfied, lest a breakdown of contract negotiations become the launching pad for a suit on an alleged oral contract. Third is the case—arguably this

case—where the precontractual writing—the Schneider memo and the attachment to it—indicates the promisor's (Anchor Hocking's) acceptance of the promisee's (Monetti's) offer; the case, in other words, where all the essential terms are stated in the writing and the only problem is that the writing was prepared before the contract became final. The only difficulty with holding that such a writing satisfies the statute of frauds is the use of the perfect tense by the draftsmen of the Uniform Commercial Code: the writing must be sufficient to demonstrate that “a contract for sale *has been made*.... The ‘futuristic’ nature of the writing disqualifies it.” *Micromedia v. Automated Broadcast Controls*, 799 F.2d 230, 234 (5th Cir.1986) (emphasis in original); see also *American Web Press, Inc. v. Harris Corp.*, 596 F.Supp. 1089, 1093 (D.Colo.1983). Yet under a general statute of frauds, “it is well settled that a memorandum satisfying the Statute may be made before the contract is concluded.” *Farrow v. Cahill*, 663 F.2d 201, 209 (D.C.Cir.1980) (footnote omitted). And while merely because the UCC's draftsmen relaxed one requirement of the statute of frauds—that there be a writing containing all the essential terms of the contract—doesn't exclude the possibility that they wanted to stiffen another, by excluding writings made before the contract itself was made, the choice of tenses is weak evidence. No doubt they had in mind, as the typical case to be governed by section 2-201, a deal made over the phone and evidenced by a confirmation slip. They may not have foreseen a case like the present, or provided for it. The distinction between what is assumed and what is prescribed is critical in interpretation generally.

12. In both of the decisions that we cited for the narrow interpretation, the judges' concern was with our first two classes of case; and judicial language, like other language, should be read in context. *Micromedia* involved an offer; in *American Web*, negotiations were continuing. We agree with Professor Farnsworth that in appropriate circumstances a memorandum made before the contract is formed can satisfy the statute of frauds, 2 *Farnsworth on Contracts, supra*, § 6.7, at p. 132 and n. 16, including the UCC statute of frauds. This case illustrates why a rule of strict temporal priority is unnecessary to secure the purposes of the statute of frauds. Farnsworth goes further. He would allow a written *offer* to satisfy the statute, provided of course that there is oral evidence it was accepted. *Id.*, n. 16. We needn't decide in this case how far we would go with him, and therefore needn't reexamine *Bennett*.
13. Nor need we decide whether the first memo (Schneider's) can be linked with the second (Davis's) —probably not, since they don't refer to each other, *Poulos v. Reda*, 165 Ill.App.3d 793, 800, 117 Ill.Dec. 465, 471, 520 N.E.2d 816, 822 (1987);

Southmark Corp. v. Life Investors, Inc., 851 F.2d 763, 767 n. 5 (5th Cir.1988) —to constitute a post-contract writing and eliminate the issue just discussed. For, shortly after the Schneider memo was prepared, Monetti gave dramatic evidence of the existence of a contract by turning over its entire distribution operation in the United States to Anchor Hocking. (In fact it had started to do this even earlier.) Monetti was hardly likely to do that without a contract—without in fact a contract requiring Anchor Hocking to purchase a minimum of \$27 million worth of Monetti's products over the next ten years, for that was a provision to which Schneider in the memo had indicated agreement, and it is the only form of compensation to Monetti for abandoning its distribution business that the various drafts make reference to and apparently the only one the parties ever discussed.

14. This partial performance took the contract out of the general Illinois statute of frauds. Unilateral performance is pretty solid evidence that there really was a contract—for why else would the party have performed unilaterally? Almost the whole purpose of contracts is to protect the party who performs first from being taken advantage of by the other party, so if a party performs first there is some basis for inferring that he had a contract. The inference of contract from partial performance is especially powerful in a case such as this, since while the nonenforcement of an oral contract leaves the parties free to pursue their noncontractual remedies, such as a suit for quantum meruit (a form of restitution), *Farash v. Sykes Datatronics, Inc.*, 59 N.Y.2d 500, 503, 465 N.Y.S.2d 917, 918, 452 N.E.2d 1245, 1246 (1983); *Robertus v. Candee*, 205 Mont. 403, 407, 670 P.2d 540, 542 (1983); 2 *Farnsworth on Contracts, supra*, § 6.11, at p. 171, once Monetti turned over its trade secrets and other intangible assets to Anchor Hocking it had no way of recovering these things. (Of course, Monetti may just have been foolish.) The partial-performance exception to the statute of frauds is often explained (and its boundaries fixed accordingly) as necessary to protect the reliance of the performing party, so that if he can be made whole by restitution the oral contract will not be enforced. This is the Illinois rationale, *Payne v. Mill Race Inn, supra*, 152 Ill.App.3d at 277-78, 105 Ill.Dec. at 330-331, 504 N.E.2d at 199-200, and it is not limited to Illinois. 2 *Farnsworth on Contracts, supra*, § 6.9. It supports enforcement of the oral contract in this case.
15. This discussion assumes, however, that the contract is governed by the general Illinois statute of frauds rather than, as the district judge believed, by the UCC's statute of frauds (or in addition to it—for both might apply, as we shall see), with its arguably narrower exception for partial performance. The UCC statute of frauds at

issue in this case appears in Article 2, the sale of goods article of the Code, and, naturally therefore, is expressly limited to contracts for the sale of goods. That is a type of transaction in which a partial performance exception to a writing requirement would make no sense if the seller were seeking payment for more than the goods he had actually delivered. Suppose A delivers 1,000 widgets to B, and later sues B for breach of an alleged oral contract for 100,000 widgets and argues that the statute of frauds is not a bar because he performed his part of the contract in part. In such a case partial performance just is not indicative of the existence of an oral contract for any quantity greater than that already delivered, so it is no surprise that the statute of frauds provides that an oral contract cannot be enforced in a quantity greater than that received and accepted by the buyer. § 2-201(3)(c); cf. § 2-201(1). The present case is different. The partial performance here consisted not of a delivery of goods alleged to be part of a larger order but the turning over of an entire business. *That* kind of partial performance *is* evidence of an oral contract and also shows that this is not the pure sale of goods to which the UCC's statute of frauds was intended to apply.

16. This is not to say that the *contract* is outside the Uniform Commercial Code. It is a contract for the sale of goods plus a contract for the sale of distribution rights and of the assets associated with those rights. Courts forced to classify a mixed contract of this sort ask, somewhat unhelpfully perhaps, what the predominant purpose of the contract is. *Yorke v. B.F. Goodrich Co.*, 130 Ill.App.3d 220, 223, 85 Ill.Dec. 606, 608, 474 N.E.2d 20, 22 (1985), and cases cited there. And, no doubt, they would classify this contract as one for the sale of goods, therefore governed by the UCC, because the \$27 million in sales contemplated by the contract (if there was a contract, as we are assuming) swamped the goodwill and other intangibles associated with Melform's very new, very small operation. Distributorship agreements, such as this one was in part, and even sales of businesses as going concerns, are frequently though not always classified as UCC contracts under the predominant-purpose test. Compare *De Filippo v. Ford Motor Co.*, 516 F.2d 1313, 1323 (3d Cir.1975); *Hudson v. Town & Country True Value Hardware, Inc.*, 666 S.W.2d 51, 53 (Tenn.1984); *Cavalier Mobile Homes, Inc. v. Liberty Homes, Inc.*, 53 Md.App. 379, 394, 454 A.2d 367, 376 (1983); and *WICO Corp. v. Willis Industries*, 567 F.Supp. 352, 355 (N.D.Ill.1983) (applying Illinois law), with *Lorenz Supply Co. v. American Standard, Inc.*, 419 Mich. 610, 615, 358 N.W.2d 845, 847 (1984).
17. We may assume that the UCC applies to this contract; but must *all* of the UCC apply? We have difficulty seeing why. It is not a matter of holding the contract partly

enforceable and partly unenforceable, a measure disapproved in *Distribu-Dor, Inc. v. Karadanis*, 11 Cal.App.3d 463, 468, 90 Cal.Rptr. 231, 234 (1970). Because of the contract's mixed character, the UCC statute of frauds doesn't make a nice fit; it's designed for a pure sale of goods. The general statute works better. The fact that Article 2, which we have been loosely referring to as the sale of goods article, in fact applies not to the sale of goods as such but rather to “transactions in goods,” § 2-102, while its statute of frauds is limited to “contract[s] for the sale of goods,” § 2-201(1), could be thought to imply that the statute of frauds does not cover every transaction that is otherwise within the scope of Article 2. 2 *Farnsworth on Contracts, supra*, § 6.6, at p. 126 and n. 5. Perhaps the contract in this case is better described as a transaction in goods than as a contract for the sale of goods, since so much more than a mere sale of goods was contemplated.

18. Another possibility is to interpret the UCC statute of frauds flexibly (an approach endorsed in *Meyer v. Logue*, 100 Ill.App.3d 1039, 1044-46, 56 Ill.Dec. 707, 710-12, 427 N.E.2d 1253, 1256-58 (1981)) in consideration of the special circumstances of the class of cases represented by this case, so that it does make a smooth fit. There is precedent for doing this. When the partial performance is not the delivery of some of the goods but part payment for all the goods, most courts will enforce oral contracts under the UCC. *Sedmak v. Charlie's Chevrolet, Inc.*, 622 S.W.2d 694, 698-99 (Mo.App.1981); *W.I. Snyder Corp. v. Caracciolo*, 373 Pa. Super. 486, 494-95, 541 A.2d 775, 779 (1988); *The Press, Inc. v. Fins & Feathers Publishing Co.*, 361 N.W.2d 171, 174 (Minn.App.1985). Such cases do not present the danger at which the limitation on using partial performance to take the entire contract outside of the statute of frauds was aimed, that of the seller's unilaterally altering the quantity ordered by the buyer, although they could be thought to present the analogous danger of the seller's unilaterally altering the price the buyer had agreed to pay—by claiming that full payment was actually part payment. *This* case, at all events, presents no dangers of the sort the provision in question was designed to eliminate. The semantic lever for the interpretation we are proposing is that the UCC does not abolish the partial-performance exception. It merely limits the use of partial delivery as a ground for insisting on the full delivery allegedly required by the oral contract. That is not what Monetti is trying to do.
19. We need not pursue these interesting questions about the applicability and scope of the UCC statute of frauds any further in this case, because our result would be unchanged no matter how they were answered. For we have said nothing yet about

the second writing in the case, the Davis memorandum of June 12. It was a writing on Anchor Hocking's letterhead, so satisfied the writing and signature requirements of the UCC statute of frauds, and it was a writing sufficient to evidence the existence of the contract upon which Anchor Hocking is being sued. It is true that "Exhibit A" does not contain all the terms of the contract; it makes no reference to the handing over of Melform's assets. But, especially taken together with the Davis memo itself (and we are permitted to connect them provided that the connections are "apparent from a comparison of the writings themselves," *Western Metals Co. v. Hartman Co.*, *supra*, 303 Ill. at 483, 135 N.E. at 746, and they are, since the Davis memo refers explicitly to Exhibit A), Exhibit A is powerful evidence that there was a contract and that its terms were as Monetti represents. Remember that the UCC's statute of frauds does not require that the contract be in writing, but only that there be a sufficient memorandum to indicate that there really was a contract. The Davis memorandum fits this requirement to a t. So even if the partial-performance doctrine is not available to Monetti, the UCC's statute of frauds was satisfied. And since the general Illinois statute was satisfied as well, we need not decide whether, since the contract in this case both was (we are assuming) within the UCC *and* could not be performed within one year, it had to satisfy both statutes of frauds. 2 *Farnsworth on Contracts*, *supra*, § 6.2, at pp. 90-91.

20. Our conclusion that Monetti's suit for breach of contract is not barred by the statute(s) of frauds makes the district judge's second ruling, refusing to allow Monetti to add a claim for promissory estoppel, academic. The only reason Monetti wanted to add the claim was as a backstop should it lose on the statute of frauds. In light of our decision today, he does not need a backstop.
21. Can promissory estoppel be used to avoid the limitations that the statute of frauds places on the enforcement of oral promises? It can be argued that a party to a contract for the sale of goods should not be allowed to get around the statute of frauds merely by alleging promissory estoppel and using partial performance to establish the necessary reliance in circumstances in which the requirements for the exception in the statute of frauds for partial performance would for one reason or another not be satisfied. It can further be argued that since promissory estoppel unlike equitable estoppel is a method of establishing contractual liability, the statute of frauds should be no less applicable than if the contract were supported by consideration or a seal rather than by promissory estoppel. *A/S Apothekernes Laboratorium for Specialpraeparater v. I.M.C. Chemical Group, Inc.*, 725 F.2d 1140, 1142 (7th

Cir.1984). On the other side it can be argued that promissory estoppel is deliberately open-ended, and should therefore remain available to overcome, in appropriate cases, possible rigidities in the statute of frauds. *Hoffman v. Red Owl Stores, Inc.*, 26 Wis. 2d 683, 133 N.W.2d 267 (1965). Consistent with this counterargument, we held in *R.S. Bennett & Co. v. Economy Mechanical Industries, Inc.*, *supra*, 606 F.2d at 187-89, that Illinois' version of the UCC statute of frauds was inapplicable to promissory estoppel cases. *Janke Construction Co. v. Vulcan Materials Co.*, 386 F.Supp. 687, 697 (W.D.Wis.1974), *aff'd*, 527 F.2d 772 (7th Cir.1976), reached a similar conclusion under Wisconsin's general statute of frauds, and in affirming we cut loose promissory estoppel from contract law, thus answering the second argument in favor of applying the statute of frauds in promissory estoppel cases. *Id.* at 777. See also 2 *Farnsworth on Contracts*, *supra*, § 6.12, at p. 185 n. 26. We have been having second thoughts lately. *Goldstick v. ICM Realty*, 788 F.2d 456, 464-66 (7th Cir.1986); *Evans v. Fluor Distribution Cos.*, 799 F.2d 364, 367-68 (7th Cir.1986). But as in *Goldstick* and *Evans*, so in this case, we need not and do not decide whether *Bennett* was an accurate forecast of Illinois law. Not only is the issue moot in view of our decision that the statute of frauds does not bar Monetti from enforcing the contract, but *Bennett* was not a case in which the plaintiff was using promissory estoppel to avoid the UCC's provision disallowing a defense to the statute of frauds for partial performance consisting of the delivery of some but not all of the quantity allegedly contracted for orally. It is in such a case that the "end run" character of promissory estoppel appears most strongly; yet we need not and do not decide whether the appearance is so strong as to preclude resort to promissory estoppel.

Reversed and Remanded.

Mitchill v. Lath

Court of Appeals of New York
247 N.Y. 377, 160 N.E. 646 (1928)

ANDREWS, J.

1. In the fall of 1923 the Laths owned a farm. This they wished to sell. Across the road, on land belonging to Lieutenant-Governor Lunn, they had an ice house which they might remove. Mrs. Mitchill looked over the land with a view to its purchase. She found the ice house objectionable. Thereupon "the defendants orally promised and agreed, for and in consideration of the purchase of their farm by the plaintiff, to remove the said ice house in the spring of 1924." Relying upon this promise, she made a written contract to buy the property for \$8,400, for cash and a mortgage and containing various provisions usual in such papers. Later receiving a deed, she entered into possession and has spent considerable sums in improving the property for use as a summer residence. The defendants have not fulfilled their promise as to the ice house and do not intend to do so. We are not dealing, however, with their moral delinquencies. The question before us is whether their oral agreement may be enforced in a court of equity.
2. This requires a discussion of the parol evidence rule—a rule of law which defines the limits of the contract to be construed. (*Glackin v. Bennett*, 226 Mass. 316.) It is more than a rule of evidence and oral testimony even if admitted will not control the written contract (*O'Malley v. Grady*, 222 Mass. 202), unless admitted without objection. (*Brady v. Nally*, 151 N. Y. 258.) It applies, however, to attempts to modify such a contract by parol. It does not affect a parol collateral contract distinct from and independent of the written agreement. It is, at times, troublesome to draw the line. Williston, in his work on Contracts (sec. 637) points out the difficulty. "Two entirely distinct contracts," he says, "each for a separate consideration may be made at the same time and will be distinct legally. Where, however, one agreement is entered into wholly or partly in consideration of the simultaneous agreement to enter into another, the transactions are necessarily bound together. ... Then if one of the agreements is oral and the other is written, the problem arises whether the bond is sufficiently close to prevent proof of the oral agreement." That is the situation here. It is claimed that the defendants are called upon to do more than is required by their written contract in connection with the sale as to which it deals. The principle may be clear, but it can be

given effect by no mechanical rule. As so often happens, it is a matter of degree, for as Professor Williston also says where a contract contains several promises on each side it is not difficult to put any one of them in the form of a collateral agreement. If this were enough written contracts might always be modified by parol. Not form, but substance is the test.

3. In applying this test the policy of our courts is to be considered. We have believed that the purpose behind the rule was a wise one not easily to be abandoned. Notwithstanding injustice here and there, on the whole it works for good. Old precedents and principles are not to be lightly cast aside unless it is certain that they are an obstruction under present conditions. New York has been less open to arguments that would modify this particular rule, than some jurisdictions elsewhere. Thus in *Eighmie v. Taylor* (98 N. Y. 288) it was held that a parol warranty might not be shown although no warranties were contained in the writing.
4. Under our decisions before such an oral agreement as the present is received to vary the written contract at least three conditions must exist, (1) the agreement must in form be a collateral one; (2) it must not contradict express or implied provisions of the written contract; (3) it must be one that parties would not ordinarily be expected to embody in the writing; or put in another way, an inspection of the written contract, read in the light of surrounding circumstances must not indicate that the writing appears "to contain the engagements of the parties, and to define the object and measure the extent of such engagement." Or again, it must not be so clearly connected with the principal transaction as to be part and parcel of it.
5. The respondent does not satisfy the third of these requirements. It may be, not the second. We have a written contract for the purchase and sale of land. The buyer is to pay \$8,400 in the way described. She is also to pay her portion of any rents, interest on mortgages, insurance premiums and water meter charges. She may have a survey made of the premises. On their part the sellers are to give a full covenant deed of the premises as described, or as they may be described by the surveyor if the survey is had, executed and acknowledged at their own expense; they sell the personal property on the farm and represent they own it; they agree that all amounts paid them on the contract and the expense of examining the title shall be a lien on the property; they assume the risk of loss or damage by fire until the deed is delivered; and they agree to pay the broker his commissions. Are they to do more? Or is such a claim inconsistent with these precise provisions? It could not be shown that the plaintiff was to pay \$500

additional. Is it also implied that the defendants are not to do anything unexpressed in the writing?

6. That we need not decide. At least, however, an inspection of this contract shows a full and complete agreement, setting forth in detail the obligations of each party. On reading it one would conclude that the reciprocal obligations of the parties were fully detailed. Nor would his opinion alter if he knew the surrounding circumstances. The presence of the ice house, even the knowledge that Mrs. Mitchill thought it objectionable would not lead to the belief that a separate agreement existed with regard to it. Were such an agreement made it would seem most natural that the inquirer should find it in the contract. Collateral in form it is found to be, but it is closely related to the subject dealt with in the written agreement—so closely that we hold it may not be proved.
7. Where the line between the competent and the incompetent is narrow the citation of authorities is of slight use. Each represents the judgment of the court on the precise facts before it. How closely bound to the contract is the supposed collateral agreement is the decisive factor in each case. But reference may be made to *Johnson v. Oppenheim* (55 N. Y. 280, 292); *Thomas v. Scutt* (127 N. Y. 133); *Eighmie v. Taylor* (98 N. Y. 288); *Stowell v. Greenwich Ins. Co.* (163 N. Y. 298); *Newburger v. American Surety Co.* (242 N. Y. 134); *Love v. Hamel* (59 App. Div. 360); *Daly v. Piza* (105 App. Div. 496); *Seitz v. Brewers Refrigerating Co.* (141 U. S. 510); *American Locomotive Co. v. Nat. Grocery Co.* (226 Mass. 314); *Doyle v. Dixon* (12 Allen, 576). Of these citations, *Johnson v. Oppenheim* and the two in the Appellate Division relate to collateral contracts said to have been the inducing cause of the main contract. They refer to leases. A similar case is *Wilson v. Deen* (74 N. Y. 531). All hold that an oral stipulation, said to have been the inducing cause for the subsequent execution of the lease itself, concerning some act to be done by the landlord, or some condition as to the leased premises, might not be shown. In principle they are not unlike the case before us. Attention should be called also to *Taylor v. Hopper* (62 N. Y. 649), where it is assumed that evidence of a parol agreement to remove a barn, which was an inducement to the sale of lots, was improper.
8. We do not ignore the fact that authorities may be found that would seem to support the contention of the appellant. Such are *Erskine v. Adeane* (L. R. 8 Ch. App. 756) and *Morgan v. Griffith* (L. R. 6 Exch. 70), where although there was a written lease a collateral agreement of the landlord to reduce the game was admitted. In this State

Wilson v. Deen might lead to the contrary result. Neither are they approved in New Jersey (*Naumberg v. Young*, 15 Vroom, 331). Nor in view of later cases in this court can *Batterman v. Pierce* (3 Hill, 171) be considered an authority. A line of cases in Massachusetts, of which *Durkin v. Cobleigh* (156 Mass. 108) is an example, have to do with collateral contracts made before a deed is given. But the fixed form of a deed makes it inappropriate to insert collateral agreements, however closely connected with the sale. This may be cause for an exception. Here we deal with the contract on the basis of which the deed to Mrs. Mitchill was given subsequently, and we confine ourselves to the question whether its terms may be modified.

9. Finally there is the case of *Chapin v. Dobson* (78 N. Y. 74, 76). This is acknowledged to be on the border line and is rarely cited except to be distinguished. Assuming the premises, however, the court was clearly right. There was nothing on the face of the written contract, it said, to show that it intended to express the entire agreement. And there was a finding, sustained by evidence, that there was an entire contract, only part of which was reduced to writing. This being so, the contract as made might be proved.
10. It is argued that what we have said is not applicable to the case as presented. The collateral agreement was made with the plaintiff. The contract of sale was with her husband and no assignment of it from him appears. Yet the deed was given to her. It is evident that here was a transaction in which she was the principal from beginning to end. We must treat the contract as if in form, as it was in fact, made by her.
11. Our conclusion is that the judgment of the Appellate Division and that of the Special Term should be reversed and the complaint dismissed, with costs in all courts.

LEHMAN, J. (dissenting).

12. I accept the general rule as formulated by Judge Andrews. I differ with him only as to its application to the facts shown in the record. The plaintiff contracted to purchase land from the defendants for an agreed price. A formal written agreement was made between the sellers and the plaintiff's husband. It is on its face a complete contract for the conveyance of the land. It describes the property to be conveyed. It sets forth the purchase price to be paid. All the conditions and terms of the conveyance to be made are clearly stated. I concede at the outset that parol evidence to show additional conditions and terms of the conveyance would be inadmissible. There is a conclusive

presumption that the parties intended to integrate in that written contract every agreement relating to the nature or extent of the property to be conveyed, the contents of the deed to be delivered, the consideration to be paid as a condition precedent to the delivery of the deeds, and indeed all the rights of the parties in connection with the land. The conveyance of that land was the subject-matter of the written contract and the contract completely covers that subject.

13. The parol agreement which the court below found the parties had made was collateral to, yet connected with, the agreement of purchase and sale. It has been found that the defendants induced the plaintiff to agree to purchase the land by a promise to remove an ice house from land not covered by the agreement of purchase and sale. No independent consideration passed to the defendants for the parol promise. To that extent the written contract and the alleged oral contract are bound together. The same bond usually exists wherever attempt is made to prove a parol agreement which is collateral to a written agreement. Hence "the problem arises whether the bond is sufficiently close to prevent proof of the oral agreement." See Judge Andrews' citation from *WILLISTON ON CONTRACTS*, section 637.
14. Judge Andrews has formulated a standard to measure the closeness of the bond. Three conditions, at least, must exist before an oral agreement may be proven to increase the obligation imposed by the written agreement. I think we agree that the first condition that the agreement "must in form be a collateral one" is met by the evidence. I concede that this condition is met in most cases where the courts have nevertheless excluded evidence of the collateral oral agreement. The difficulty here, as in most cases, arises in connection with the two other conditions.
15. The second condition is that the "parol agreement must not contradict express or implied provisions of the written contract." Judge Andrews voices doubt whether this condition is satisfied. The written contract has been carried out. The purchase price has been paid; conveyance has been made, title has passed in accordance with the terms of the written contract. The mutual obligations expressed in the written contract are left unchanged by the alleged oral contract. When performance was required of the written contract, the obligations of the parties were measured solely by its terms. By the oral agreement the plaintiff seeks to hold the defendants to other obligations to be performed by them thereafter upon land which was not conveyed to the plaintiff. The assertion of such further obligation is not inconsistent with the written contract unless the written contract contains a provision, express or implied, that the

defendants are not to do anything not expressed in the writing. Concededly there is no such express provision in the contract, and such a provision may be implied, if at all, only if the asserted additional obligation is "so clearly connected with the principal transaction as to be part and parcel of it," and is not "one that the parties would not ordinarily be expected to embody in the writing." The hypothesis so formulated for a conclusion that the asserted additional obligation is inconsistent with an implied term of the contract is that the alleged oral agreement does not comply with the third condition as formulated by Judge Andrews. In this case, therefore, the problem reduces itself to the one question whether or not the oral agreement meets the third condition.

16. I have conceded that upon inspection the contract is complete. "It appears to contain the engagements of the parties, and to define the object and measure the extent of such engagement;" it constitutes the contract between them and is presumed to contain the whole of that contract. (*Eighmie v. Taylor*, 98 N. Y. 288.) That engagement was on the one side to convey land; on the other to pay the price. The plaintiff asserts further agreement based on the same consideration to be performed by the defendants after the conveyance was complete, and directly affecting only other land. It is true, as Judge Andrews points out, that "the presence of the ice house, even the knowledge that Mrs. Mitchill thought it objectionable, would not lead to the belief that a separate agreement existed with regard to it;" but the question we must decide is whether or not, assuming an agreement was made for the removal of an unsightly ice house from one parcel of land as an inducement for the purchase of another parcel, the parties would ordinarily or naturally be expected to embody the agreement for the removal of the ice house from one parcel in the written agreement to convey the other parcel. Exclusion of proof of the oral agreement on the ground that it varies the contract embodied in the writing may be based only upon a finding or presumption that the written contract was intended to cover the oral negotiations for the removal of the ice house which lead up to the contract of purchase and sale. To 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. The question being whether certain subjects of negotiation were intended to be covered, we must compare the writing and the negotiations before we can determine whether they were in fact covered." (WIGMORE ON EVIDENCE [2d ed.], section 2430.)

17. The subject-matter of the written contract was the conveyance of land. The contract was so complete on its face that the conclusion is inevitable that the parties intended to embody in the writing all the negotiations covering at least the conveyance. The promise by the defendants to remove the ice house from other land was not connected with their obligation to convey, except that one agreement would not have been made unless the other was also made. The plaintiff's assertion of a parol agreement by the defendants to remove the ice house was completely established by the great weight of evidence. It must prevail unless that agreement was part of the agreement to convey and the entire agreement was embodied in the writing.
18. The fact that in this case the parol agreement is established by the overwhelming weight of evidence is, of course, not a factor which may be considered in determining the competency or legal effect of the evidence. Hardship in the particular case would not justify the court in disregarding or emasculating the general rule. It merely accentuates the outlines of our problem. The assumption that the parol agreement was made is no longer obscured by any doubts. The problem then is clearly whether the parties are presumed to have intended to render that parol agreement legally ineffective and non-existent by failure to embody it in the writing. Though we are driven to say that nothing in the written contract which fixed the terms and conditions of the stipulated conveyance suggests the existence of any further parol agreement, an inspection of the contract, though it is complete on its face in regard to the subject of the conveyance, does not, I think, show that it was intended to embody negotiations or agreements, if any, in regard to a matter so loosely bound to the conveyance as the removal of an ice house from land not conveyed.
19. The rule of integration undoubtedly frequently prevents the assertion of fraudulent claims. Parties who take the precaution of embodying their oral agreements in a writing should be protected against the assertion that other terms of the same agreement were not integrated in the writing. The limits of the integration are determined by the writing, read in the light of the surrounding circumstances. A written contract, however complete, yet covers only a limited field. I do not think that in the written contract for the conveyance of land here under consideration we can find an intention to cover a field so broad as to include prior agreements, if any such were made, to do other acts on other property after the stipulated conveyance was made.

20. In each case where such a problem is presented, varying factors enter into its solution. Citation of authority in this or other jurisdictions is useless, at least without minute analysis of the facts. The analysis I have made of the decisions in this State leads me to the view that the decision of the courts below is in accordance with our own authorities and should be affirmed.

CARDOZO, Ch. J., POUND, KELLOGG and O'BRIEN, JJ., concur with ANDREWS, J.; LEHMAN, J., dissents in opinion in which CRANE, J., concurs.

Masterson v. Sine

Supreme Court of California
68 Cal. 2d. 222, 436 P.2d 561 (1968)

TRAYNOR, Chief Justice.

1. Dallas Masterson and his wife Rebecca owned a ranch as tenants in common. On February 25, 1958, they conveyed it to Medora and Lu Sine by a grant deed “Reserving unto the Grantors herein an option to purchase the above described property on or before February 25, 1968” for the “same consideration as being paid heretofore plus their depreciation value of any improvements Grantees may add to the property from and after two and a half years from this date.” Medora is Dallas' sister and Lu's wife. Since the conveyance Dallas has been adjudged bankrupt. His trustee in bankruptcy and Rebecca brought this declaratory relief action to establish their right to enforce the option.
2. The case was tried without a jury. Over defendants' objection the trial court admitted extrinsic evidence that by “the same consideration as being paid heretofore” both the grantors and the grantees meant the sum of \$50,000 and by “depreciation value of any improvements” they meant the depreciation value of improvements to be computed by deducting from the total amount of any capital expenditures made by defendants grantees the amount of depreciation allowable to them under United States income tax regulations as of the time of the exercise of the option.
3. The court also determined that the parol evidence rule precluded admission of extrinsic evidence offered by defendants to show that the parties wanted the property kept in the Masterson family and that the option was therefore personal to the grantors and could not be exercised by the trustee in bankruptcy.
4. The court entered judgment for plaintiffs, declaring their right to exercise the option, specifying in some detail how it could be exercised, and reserving jurisdiction to supervise the manner of its exercise and to determine the amount that plaintiffs will be required to pay defendants for their capital expenditures if plaintiffs decide to exercise the option.
5. Defendants appeal. They contend that the option provision is too uncertain to be enforced and that extrinsic evidence as to its meaning should not have been admitted.

The trial court properly refused to frustrate the obviously declared intention of the grantors to reserve an option to repurchase by an overly meticulous insistence on completeness and clarity of written expression. (See *California Lettuce Growers v. Union Sugar Co.* (1955) 45 Cal.2d 474, 481, 289 P.2d 785, 49 A.L.R.2d 496; *Rivers v. Beadle* (1960) 183 Cal.App.2d 691, 695-697, 7 Cal.Rptr. 170.) It properly admitted extrinsic evidence to explain the language of the deed (*Nofziger v. Holman* (1964) 61 Cal.2d 526, 528, 39 Cal.Rptr. 384, 393 P.2d 696; *Barham v. Barham* (1949) 33 Cal.2d 416, 422-423, 202 P.2d 289; *Union Oil Co. v. Union Sugar Co.* (1948) 31 Cal.2d 300, 306, 188 P.2d 470; *Schmidt v. Macco Construction Co.* (1953) 119 Cal.App.2d 717, 730, 260 P.2d 230; see Farnsworth, 'Meaning' in the Law of Contracts (1967) 76 YALE L.J. 939, 959-965; Corbin, *The Interpretation of Words and the Parol Evidence Rule* (1965) 50 CORNELL L.Q. 161) to the end that the consideration for the option would appear with sufficient certainty to permit specific enforcement (see *McKeon v. Santa Claus of California, Inc.* (1964) 230 Cal.App.2d 359, 364, 41 Cal.Rptr. 43; *Burrow v. Timmsen* (1963) 223 Cal.App.2d 283, 288, 35 Cal.Rptr. 668, 100 A.L.R.2d 544). The trial court erred, however, in excluding the extrinsic evidence that the option was personal to the grantors and therefore nonassignable.

6. 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. (*Pollyanna Homes, Inc. v. Berney* (1961) 56 Cal.2d 676, 679-680, 16 Cal.Rptr. 345, 365 P.2d 401; *Hale v. Bohannon* (1952) 38 Cal.2d 458, 465, 241 P.2d 4; see 3 CORBIN, CONTRACTS (1960) § 573, p. 357; REST., CONTRACTS (1932) §§ 228 (and com. a), 237; Code Civ.Proc., § 1856; Civ.Code, § 1625.) 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. (*Hulse v. Juillard Fancy Foods Co.* (1964) 61 Cal.2d 571, 573, 39 Cal.Rptr. 529, 394 P.2d 65; *Schwartz v. Shapiro* (1964) 229 Cal.App.2d 238, 250, 40 Cal.Rptr. 189; *Mangini v. Wolfschmidt, Ltd.* (1958) 165 Cal.App.2d 192, 200-201, 331 P.2d 728; REST., CONTRACTS (1932) § 239.)
7. The crucial issue in determining whether there has been an integration is whether the parties intended their writing to serve as the exclusive embodiment of their agreement. The instrument itself may help to resolve that issue. It may state, for example, that “there are no previous understandings or agreements not contained in the writing,” and thus express the parties' “intention to nullify antecedent

understandings or agreements.” (See 3 CORBIN, CONTRACTS (1960) § 578, p. 411.) Any such collateral agreement itself must be examined, however, to determine whether the parties intended the subjects of negotiation it deals with to be included in, excluded from, or otherwise affected by the writing. Circumstances at the time of the writing may also aid in the determination of such integration. (See 3 CORBIN, CONTRACTS (1960) §§ 582-584; MCCORMICK, EVIDENCE (1954) § 216, p. 441; 9 WIGMORE, EVIDENCE (3d ed. 1940) § 2430, p. 98, § 2431, pp. 102-103; WITKIN, CAL. EVIDENCE (2d ed. 1966) § 721; *Schwartz v. Shapiro*, *supra*, 229 Cal.App.2d 238, 251, fn. 8, 40 Cal.Rptr. 189; *contra*, 4 WILLISTON, CONTRACTS (3d ed. 1961) § 633, pp. 1014-1016.)

8. California cases have stated that whether there was an integration is to be determined solely from the face of the instrument (e.g., *Thoroman v. David* (1926) 199 Cal. 386, 389-390, 249 P. 513; *Heffner v. Gross* (1919) 179 Cal. 738, 742-743, 178 P. 860; *Gardiner v. McDonogh* (1905) 147 Cal. 313, 318-321, 81 P. 964; *Harrison v. McCormick* (1891) 89 Cal. 327, 330, 26 P. 830), and that the question for the court is whether it ‘appears to be a complete...agreement....’ (See *Ferguson v. Koch* (1928) 204 Cal. 342, 346, 268 P. 342, 344, 58 A.L.R. 1176; *Harrison v. McCormick*, *supra*, 89 Cal. 327, 330, 26 P. 830.) Neither of these strict formulations of the rule, however, has been consistently applied. The requirement that the writing must appear incomplete on its face has been repudiated in many cases where parol evidence was admitted “to prove the existence of a separate oral agreement as to any matter on which the document is silent and which is not inconsistent with its terms”—even though the instrument appeared to state a complete agreement. (E.g., *American Industrial Sales Corp. v. Airscope, Inc.* (1955) 44 Cal.2d 393, 397, 282 P.2d 504, 506, 49 A.L.R.2d 1344; *Stockburger v. Dolan* (1939) 14 Cal.2d 313, 317, 94 P.2d 33, 128 A.L.R. 83; *Crawford v. France* (1933) 219 Cal. 439, 443, 27 P.2d 645; *Buckner v. A. Leon & Co.* (1928) 204 Cal. 225, 227, 267 P. 693; *Sivers v. Sivers* (1893) 97 Cal. 518, 521, 32 P. 571; *cf. Simmons v. California Institute of Technology* (1949) 34 Cal.2d 264, 274, 209 P.2d 581.) Even under the rule that the writing alone is to be consulted, it was found necessary to examine the alleged collateral agreement before concluding that proof of it was precluded by the writing alone. (See 3 CORBIN, CONTRACTS (1960) § 582, pp. 444-446.) It is therefore evident that “The conception of a writing as wholly and intrinsically self-determinative of the parties' intent to make it a sole memorial of one or seven or twenty-seven subjects of negotiation is an impossible one.” (9 WIGMORE, EVIDENCE (3d ed. 1940) § 2431, p. 103.) For example, a

promissory note given by a debtor to his creditor may integrate all their present contractual rights and obligations, or it may be only a minor part of an underlying executory contract that would never be discovered by examining the face of the note.

9. In formulating the rule governing parol evidence, several policies must be accommodated. One policy is based on the assumption that written evidence is more accurate than human memory. (*Germain Fruit Co. v. J. K. Armsby Co.* (1908) 153 Cal. 585, 595, 96 P. 319.) This policy, however, can be adequately served by excluding parol evidence of agreements that directly contradict the writing. Another policy is based on the fear that fraud or unintentional invention by witnesses interested in the outcome of the litigation will mislead the finder of facts. (*Germain Fruit Co. v. J. K. Armsby Co.*, *supra*, 153 Cal. 585, 596, 96 P. 319; *Mitchill v. Lath* (1928) 247 N.Y. 377, 388, 160 N.E. 646, 68 A.L.R. 239 (dissenting opinion by Lehman, J.); see 9 WIGMORE, EVIDENCE (3d ed. 1940) § 2431, p. 102; Murray, *The Parol Evidence Rule: A Clarification* (1966) 4 DUQUESNE L. REV. 337, 338-339.) McCormick has suggested that the party urging the spoken as against the written word is most often the economic underdog, threatened by severe hardship if the writing is enforced. In his view the parol evidence rule arose to allow the court to control the tendency of the jury to find through sympathy and without a dispassionate assessment of the probability of fraud or faulty memory that the parties made an oral agreement collateral to the written contract, or that preliminary tentative agreements were not abandoned when omitted from the writing. (See MCCORMICK, EVIDENCE (1954) § 210.) He recognizes, however, that if this theory were adopted in disregard of all other considerations, it would lead to the exclusion of testimony concerning oral agreements whenever there is a writing and thereby often defeat the true intent of the parties. See MCCORMICK, *op. cit. supra*, § 216, p. 441.)
10. Evidence of oral collateral agreements should be excluded only when the fact finder is likely to be misled. The rule must therefore be based on the credibility of the evidence. One such standard, adopted by section 240(1)(b) of the Restatement of Contracts, permits proof of a collateral agreement if it “is such an agreement as might *naturally* be made as a separate agreement by parties situated as were the parties to the written contract.” (Italics added; see MCCORMICK, EVIDENCE (1954) § 216, p. 441; see also 3 CORBIN, CONTRACTS (1960) § 583, p. 475, § 594, pp. 568-569; 4 WILLISTON, CONTRACTS (3d ed. 1961) § 638, pp. 1039-1045.) The draftsmen of the Uniform Commercial Code would exclude the evidence in still fewer instances: “If the additional terms are such that, if agreed upon, they would *certainly* have been

included in the document in the view of the court, then evidence of their alleged making must be kept from the trier of fact.” (Com. 3, § 2-202, italics added.)¹

11. The option clause in the deed in the present case does not explicitly provide that it contains the complete agreement, and the deed is silent on the question of assignability. Moreover, the difficulty of accommodating the formalized structure of a deed to the insertion of collateral agreements makes it less likely that all the terms of such an agreement were included.² (See 3 CORBIN, CONTRACTS (1960) § 587; 4 WILLISTON, CONTRACTS (3d ed. 1961) § 645; 70 A.L.R. 752, 759 (1931); 68 A.L.R. 245 (1930).) The statement of the reservation of the option might well have been placed in the recorded deed solely to preserve the grantors' rights against any possible future purchasers and this function could well be served without any mention of the parties' agreement that the option was personal. There is nothing in the record to indicate that the parties to this family transaction, through experience in land transactions or otherwise, had any warning of the disadvantages of failing to put the whole agreement in the deed. This case is one, therefore, in which it can be said that a collateral agreement such as that alleged “might naturally be made as a separate agreement.” A fortiori, the case is not one in which the parties ‘would certainly’ have included the collateral agreement in the deed.
12. It is contended, however, that an option agreement is ordinarily presumed to be assignable if it contains no provisions forbidding its transfer or indicating that its performance involves elements personal to the parties. (*Mott v. Cline* (1927) 200 Cal. 434, 450, 253 P. 718; *Altman v. Blewett* (1928) 93 Cal. App. 516, 525, 269 P. 751.) The fact that there is a written memorandum, however, does not necessarily preclude parol evidence rebutting a term that the law would otherwise presume. In *American Industrial Sales Corp. v. Airscope, Inc.*, *supra*, 44 Cal.2d 393, 397-398, 282 P.2d 504,

¹ Corbin suggests that, even in situations where the court concludes that it would not have been natural for the parties to make the alleged collateral oral agreement, parol evidence of such an agreement should nevertheless be permitted if the court is convinced that the unnatural actually happened in the case being adjudicated. (3 Corbin, Contracts, § 485, pp. 478, 480; cf. Murray, *The Parol Evidence Rule: A Clarification* (1966) 4 *Duquesne L. Rev.* 337, 341-342.) This suggestion may be based on a belief that judges are not likely to be misled by their sympathies. If the court believes that the parties intended a collateral agreement to be effective, there is no reason to keep the evidence from the jury.

² See *Goble v. Dotson* (1962) 203 Cal.App.2d 272, 21 Cal. Rptr. 769, where the deed given by a real estate developer to the plaintiffs contained a condition that grantees would not build a pier or boathouse. Despite this reference in the deed to the subject of berthing for boats, the court allowed plaintiffs to prove by parol evidence that the condition was agreed to in return for the developer's oral promise that plaintiffs were to have the use of two boat spaces nearby.

we held it proper to admit parol evidence of a contemporaneous collateral agreement as to the place of payment of a note, even though it contradicted the presumption that a note, silent as to the place of payment, is payable where the creditor resides. (For other examples of this approach, see *Richter v. Union Land etc. Co.* (1900) 129 Cal. 367, 375, 62 P. 39 (presumption of time of delivery rebutted by parol evidence); *Wolters v. King* (1897) 119 Cal. 172, 175-176, 51 P. 35 (presumption of time of payment rebutted by parol evidence); *Mangini v. Wolfschmidt, Ltd., supra*, 165 Cal.App.2d 192, 198-201, 331 P.2d 728 (presumption of duration of an agency contract rebutted by parol evidence); *Zinn v. Ex-Cell-O Corp.* (1957) 148 Cal.App.2d 56, 73-74, 306 P.2d 1017; see also REST., CONTRACTS, § 240, com. c.)³ Of course a statute may preclude parol evidence to rebut a statutory presumption. (E.g., *Neff v. Ernst* (1957) 48 Cal.2d 628, 635, 311 P.2d 849 (commenting on Civ.Code, § 1112); *Kilfoy v. Fritz* (1954) 125 Cal.App.2d 291, 293-294, 270 P.2d 579 (applying Deering's Gen.Laws 1937, Act 652, § 15a; see also Com.Code, § 9-318, subd. (4).) Here, however, there is no such statute. In the absence of a controlling statute the parties may provide that a contract right or duty is nontransferable. (*La Rue v. Groezinger* (1890) 84 Cal. 281, 283, 24 P. 42; *Benton v. Hofmann Plastering Co.* (1962) 207 Cal.App.2d 61, 68, 24 Cal.Rptr. 268; *Parkinson v. Caldwell* (1954) 126 Cal.App.2d 548, 552-553, 272 P.2d 934; see 4 CORBIN, CONTRACTS (1951) §§ 872-873.) Moreover, even when there is no explicit agreement—written *or* oral—that contractual duties shall be personal, courts will effectuate presumed intent to that effect if the circumstances indicate that performance by [a] substituted person would be different from that contracted for. (*Farmland Irrigation Co. v. Dopplmaier* (1957)

³ Counsel for plaintiffs direct our attention to numerous cases that they contend establish that parol evidence may never be used to show a collateral agreement contrary to a term that the law presumes in the absence of an agreement. In each of these cases, however, the decision turned upon the court's belief that the writing was a complete integration and was no more than an application of the rule that parol evidence cannot be used to vary the terms of a completely integrated agreement. (Cf. discussion in *Mangini v. Wolfschmidt, Ltd., supra*, 165 Cal.App.2d 192, 203, 331 P.2d 728.) In *Gardiner v. McDonogh, supra*, 147 Cal. 313, 319, 81 P. 964, defendants sought to prove a collateral agreement that beams sold them were to conform to a sample earlier given. The court purportedly looked only to the face of the writing to decide whether parol evidence was admissible, and such evidence would be excluded if the writing was 'clear and complete.' Defendants argued that the written order was not complete because it did not fix a time and place of delivery, but the court answered that the failure to state those terms did not result in incompleteness because the law would supply them by implication. This decision was based on the belief that the question of admissibility had to be decided from that face of the instrument alone. Virtually every writing leaves some terms to be implied and almost none would qualify as integrations without implying some terms. The decision was therefore a product of an outmoded approach to the parol evidence rule, not of any compulsion to give conclusive effect to presumptions of implied terms.

- 48 Cal.2d 208, 222, 308 P.2d 732, 66 A.L.R.2d 590; *Prichard v. Kimball* (1923) 190 Cal. 757, 764-765, 214 P. 863; *Simmons v. Zimmerman* (1904) 144 Cal. 256, 260-261, 79 P. 451; *La Rue v. Groezinger, supra*, 84 Cal. 281, 285, 24 P. 42; *Coykendall v. Jackson* (1936) 17 Cal.App.2d 729, 731, 62 P.2d 746; see 4 CORBIN, CONTRACTS (1951) § 865; 3 WILLISTON, CONTRACTS (3d ed. 1960) § 412, pp. 32-33; REST., CONTRACTS (Tent. Draft No. 3, 1967) § 150(2).)
13. In *Standard Box Co. v. Mutual Biscuit Co.* (1909) 10 Cal.App. 746, 750, 103 P. 938, 940, the rationale of *Gardiner v. McDonogh* was extended to exclude evidence of an agreement for a time of performance other than the “reasonable time” implied by law in a situation where the writing, although stating no time of performance, was “clear and complete when aided by that which is imported into it by legal implication.” This decision was simply an application of the then-current theory regarding integration. The court regarded the instrument as a complete integration, and it therefore precluded proof of collateral agreements. Since it is now clear that integration cannot be determined from the writing alone, the decision is not authoritative insofar as it finds a complete integration. There is no reason to believe that the court gave any independent significance to implied terms. Had the court found from the writing alone that there was no integration, there is nothing to indicate that it would have excluded proof contrary to terms it would have otherwise presumed.
 14. In *Buffalo Arms, Inc. v. Remler Co.* (1960) 179 Cal.App.2d 700, 710, 4 Cal.Rptr. 103, the court refused to admit parol evidence showing a collateral oral agreement that a buyer would have more than the ‘reasonable time’ presumed by law to refuse goods, but the decision is based on a conclusion that the writing on its face was a complete expression of the agreement. In *La France v. Kashishian* (1928) 204 Cal. 643, 645, 269 P. 655, and *Fogler v. Purkiser* (1932) 127 Cal.App. 554, 559-560, 16 P.2d 305, there are no clear findings concerning the completeness of the writings; but the argument in each case is borrowed from the *Standard Box Co.* decision and thus implies a finding of a complete integration. *Calpetro Producers Syndicate v. C. M. Woods Co.* (1929) 206 Cal. 246, 247-248, 252, 274 P. 65, relies on *Standard Box Co.* and expressly finds a complete integration.
 15. In the present case defendants offered evidence that the parties agreed that the option was not assignable in order to keep the property in the Masterson family. The trial court erred in excluding that evidence.

16. The judgment is reversed.

PETERS, TOBRINER, MOSK, and SULLIVAN, JJ., concur.

DISSENTING OPINION

BURKE, Justice

17. I dissent. The majority opinion:

(1) Undermines the parol evidence rule as we have known it in this state since at least 1872¹ by declaring that parol evidence should have been admitted by the trial court to show that a written option, absolute and unrestricted in form, was intended to be limited and nonassignable;

(2) Renders suspect instruments of conveyance absolute on their face;

(3) Materially lessens the reliance which may be placed upon written instruments affecting the title to real estate; and

(4) Opens the door, albeit unintentionally to a new technique for the defrauding of creditors.

18. The opinion permits defendants to establish by parol testimony that their grant² to their brother (and brother-in-law) of a written option, absolute in terms, was nevertheless agreed to be nonassignable by the grantee (now a bankrupt), and that therefore the right to exercise it did not pass, by operation of the bankruptcy laws, to the trustee for the benefit of the grantee's creditors.

19. And how was this to be shown? By the proffered testimony of the bankrupt optionee himself! Thereby one of his assets (the option to purchase defendants' California ranch) would be withheld from the trustee in bankruptcy and from the bankrupt's creditors. Understandably the trial court, as required by the parol evidence rule, did

¹ In that year the Legislature set forth the rule in sections 1625 of the Civil Code and 1856 of the Code of Civil Procedure.

² The option was in the form of a reservation in a deed; however, in legal effect it is the same as if it had been contained in a separate document.

not allow the bankrupt by parol to so contradict the unqualified language of the written option.

20. The court properly admitted parol evidence to explain the intended meaning of the “same consideration” and “depreciation value” phrases of the written option to purchase defendants' land, as the intended meaning of those phrases was not clear. However, there was nothing ambiguous about the *granting* language of the option and not the slightest suggestion in the document that the option was to be nonassignable. Thus, to permit such words of limitation to be added by parol is to *contradict* the absolute nature of the grant, and to directly violate the parol evidence rule.
21. Just as it is unnecessary to state in a deed to “lot X” that the house located thereon goes with the land, it is likewise unnecessary to add to “I grant an option to Jones” the words “and his assigns” for the option to be assignable. As hereinafter emphasized in more detail, California statutes expressly declare that it is assignable, and only if I add language in writing showing my intent to withhold or restrict the right of assignment may the grant be so limited. Thus, to seek to restrict the grant by parol is to contradict the written document in violation of the parol evidence rule.
22. The majority opinion arrives at its holding via a series of false premises which are not supported either in the record of this case or in such California authorities as are offered.

[The remainder of the dissent presents a point-by-point refutation of the majority's reasoning. Although I have elected to reprint these pages for the benefit of those students who might find the analysis interesting, you should feel free to skim this material if you are at all pressed for time (or prone to drowsiness). To say that Justice Burke's writing style is somewhat soporific would be to dramatically understate its likely effect on your level of alertness. Forewarned is forearmed.]

23. The parol evidence rule is set forth in clear and definite language in the statutes of this state. (Civ.Code, § 1625; Code Civ.Proc., § 1856.) It “is not a rule of evidence but is one of substantive law....The rule as applied to contracts is simply that as a matter of substantive law, a certain act, the act of embodying the complete terms of an agreement in a writing (the ‘integration’), Becomes the contract of the parties.” (Hale v. Bohannon (1952) 38 Cal.2d 458, 465, 241 P.2d 4, 7(1, 2), quoting from In re Estate of Gaines (1940) 15 Cal.2d 255, 264-265, 100 P.2d 1055.) The rule is based upon the sound principle that the parties to a written instrument, after committing

their agreement to or evidencing it by the writing, are not permitted to add to, vary or contradict the terms of the writing by parol evidence. As aptly expressed by the author of the present majority opinion, speaking for the court in *Parsons v. Bristol Development Co.* (1965) 62 Cal.2d 861, 865(2), 44 Cal.Rptr. 767, 402 P.2d 839, and in *Coast Bank v. Minderhout* (1964) 61 Cal.2d 311, 315, 38 Cal.Rptr. 505, 507, 392 P.2d 265, 267, such evidence is “admissible to *interpret* the instrument, but not to give it a meaning to which it is not reasonably susceptible.” (Italics added.) Or, as stated by the same author, concurring in *Laux v. Freed* (1960) 53 Cal.2d 512, 527, 2 Cal.Rptr. 265, 273, 348 P.2d 873, 881, “extrinsic evidence is not admissible to add to, *detract* from, or vary its terms.” (Italics added.)

24. At the outset the majority in the present case reiterate³ that the rule against contradicting or varying the terms of a writing remains applicable when only part of the agreement is contained in the writing, and parol evidence is used to prove elements of the agreement not reduced to writing. But having restated this established rule, the majority opinion inexplicably proceeds to subvert it.
25. Each of the three cases cited by the majority (fn. 3, Ante) holds that although parol evidence is admissible to prove the parts of the contract not put in writing, it is *not* admissible to vary or *contradict* the writing or prove collateral agreements which are *inconsistent* therewith. The meaning of this rule (and the application of it found in the cases) is that if the asserted unwritten elements of the agreement would contradict, add to, detract from, vary or be inconsistent with the written agreement, then such elements may not be shown by parol evidence.
26. The contract of sale and purchase of the ranch property here involved was carried out through a title company upon written escrow instructions executed by the respective parties after various preliminary negotiations. The deed to defendant grantees, in which the grantors expressly reserved an option to repurchase the property within a ten-year period and upon a specified consideration, was issued and delivered in consummation of the contract. In neither the written escrow instructions nor the deed containing the option is there any language even suggesting that the option was agreed or intended by the parties to be personal to the grantors, and so nonassignable.

³ Citing three California cases (p. 547); *Hulse v. Juillard Fancy Foods Co.* (1964) 61 Cal.2d 571, 573, 39 Cal.Rptr. 529, 394 P.2d 65; *Schwartz v. Shapiro* (1964) 229 Cal.App.2d 238, 250, 40 Cal.Rptr. 189; *Mangini v. Wolfschmidt, Ltd.* (1958) 165 Cal.App.2d 192, 200-201, 331 P.2d 728.

The trial judge, on at least three separate occasions, correctly sustained objections to efforts of defendant optionors to get into evidence the testimony of Dallas Masterson (the bankrupt holder of the option) that a part of the agreement of sale of the parties was that the option to repurchase the property was personal to him, and therefore unassignable for benefit of creditors. But the majority hold that that testimony should have been admitted, thereby permitting defendant optionors to limit, detract from and contradict the plain and unrestricted terms of the written option in clear violation of the parol evidence rule and to open the door to the perpetration of fraud.

27. Options are property, and are widely used in the sale and purchase of real and personal property. One of the basic incidents of property ownership is the right of the owner to sell or transfer it. The author of the present majority opinion, speaking for the court in *Farmland Irrigation Co. v. Dopplmaier* (1957) 48 Cal.2d 208, 222, 308 P.2d 732, 740, 66 A.L.R.2d 590, put it this way: “The statutes in this state clearly manifest a policy in favor of the free transferability of all types of property, including rights under contracts.”⁴ (Citing Civ.Code, §§ 954, 1044, 1458;⁵ see also 40 Cal.Jur.2d 289-291, and cases there cited.) These rights of the owner of property to transfer it, confirmed by the cited code sections, are elementary rules of substantive law and not the mere disputable presumptions which the majority opinion in the present case would make of them. Moreover, the right of transferability applies to an option to purchase, unless there are words of limitation in the option forbidding its assignment or showing that it was given because of a peculiar trust or confidence reposed in the optionee. (*Mott v. Cline* (1927) 200 Cal. 434, 450(11), 253 P. 718; *Prichard v. Kimball* (1923) 190 Cal. 757, 764-765(4, 5), 214 P. 867; *Altman v. Blewett* (1928) 93 Cal.App. 516, 525(3), 269 P. 751; see also 5 Cal.Jur.2d 393, 395-396, and cases there cited.) Thus, in *Prichard* the language of the *document* itself (a written, *expressly* nonassignable lease, with option to buy) was held to establish the

⁴ The opinion continues: ‘The terms and purpose of a contract may show, however, that it was intended to be nonassignable.’ With this qualification of the general rule I am in accord, but here it is inapplicable as language indicating any intention whatever to restrict assignability is completely nonexistent.

⁵ Section 1044: ‘Property of any kind may be transferred, except as otherwise provided by this Article.’ The *only* property the article provides cannot be transferred is ‘A mere possibility, not coupled with an interest.’ (s 1045.)

Section 1458: ‘A right arising out of an obligation is the property of the person to whom it is due, and may be transferred as such.’

trust or confidence reposed in the optionee and so to negate assignability of the option.

28. The right of an optionee to transfer his option to purchase property is accordingly one of the basic rights which accompanies the option unless limited under the language of the option itself. To allow an optionor to resort to parol evidence to support his assertion that the written option is not transferable is to authorize him to limit the option by attempting to restrict and reclaim rights with which he has already parted. A clearer violation of two substantive and basic rules of law—the parol evidence rule and the right of free transferability of property—would be difficult to conceive.
29. The majority opinion attempts to buttress its approach by asserting that “California cases have stated that whether there was an integration is to be determined solely from the face of the instrument (citations), and that the question for the court is whether it ‘appears to be a complete...agreement....’” (citations), but that “Neither of these strict formulations of the rule...has been consistently applied.”
30. The majority's claim of inconsistent application of the parol evidence rule by the California courts fails to find support in the examples offered. First, the majority opinion asserts that “The requirement that the writing must appear incomplete on its face has been repudiated in many cases where parol evidence was admitted ‘to prove the existence of a separate oral agreement as to any matter on which the document is silent and which is not inconsistent with its terms’—even though the instrument appeared to state a complete agreement. (Citations.)” But an examination of the cases cited in support of the quoted statement discloses that on the contrary in every case which is pertinent here (with a single exception) the writing was obviously incomplete on its face.⁶ In the one exception (*Stockburger v. Dolan* (1939) 14 Cal.2d 313, 317, 94 P.2d 33, 128 A.L.R. 83) it was held that lessors under a lease to drill for oil in an area zoned against such drilling should be permitted to show by parol that

⁶ Thus in *American Industrial Sales Corp. v. Airscope, Inc.* (1955) 44 Cal.2d 393, 397, 282 P.2d 504, 49 A.L.R.2d 1344, the contract was silent as to the place of payment for property purchased; in *Crawford v. France* (1933) 219 Cal. 439, 443, 27 P.2d 645, a contract for an architect's fee based upon the cost of a building was silent as to such cost; in *Buckner v. A. Leon & Co.* (1928) 204 Cal. 225, 227, 267 P. 693, a contract for sale and purchase of grapes was silent as to which party was to furnish the lug boxes required for delivery; in *Sivers v. Sivers* (1893) 97 Cal. 518, 521, 32 P. 571, a written agreement to repay money loaned was silent as to the time for payment; and *Simmons v. California Institute of Technology* (1949) 34 Cal.2d 264, 274(9), 209 P.2d 581, was a case of fraud in the inducement and not one of parol evidence to show a promise or agreement inconsistent with the written contract.

the lessee had contemporaneously agreed orally to seek a variance—an agreement which, as the opinion points out, did not contradict the written contract. But what is additionally noteworthy in *Stockburger*, and controlling here, is the further holding that lessors could not show by parol that lessee had orally agreed that a lease provision suspending payment of rental under certain circumstances would not apply during certain periods of time—as “evidence to that effect would vary the terms of the contract in that particular....” (P. 317(5) of 14 Cal.2d p. 35 of 94 P.2d.)

31. In further pursuit of what would appear to be nonexistent support for its assertions of inconsistency in California cases, the majority opinion next declares (p. 548) that “Even under the rule that the writing alone is to be consulted, it was found necessary to examine the alleged collateral agreement before concluding that proof of it was precluded by the writing alone. (See 3 Corbin, Contracts (1960) § 582, pp. 444-446.)” Not only are *no* California cases cited by the majority in supposed support for the quoted declaration (offered by the majority as an example of inconsistent applications of the parol evidence rule by California courts), but 3 Corbin, Contracts, which the majority do cite, likewise refers to *no* California cases, and makes but scanty citation to any cases whatever. In any event, in what manner other than by “examining” an alleged collateral agreement is it possible for a court to rule upon the admissibility of testimony or upon an offer of proof with respect to such agreement?
32. The majority opinion has thus demonstrably failed to substantiate its next utterance (p. 548) that “The conception of a writing as wholly and intrinsically self-determinative of the parties' intent to make it a sole memorial of one or seven or twenty-seven subjects of negotiation is an impossible one,” citing 9 Wigmore, Evidence (3d ed. 1940) section 2431, page 103, whose views on the subject were Rejected by this court as early as 1908 in *Germain Fruit Co. v. J. K. Armsby Co.*, 153 Cal. 585, 595, 96 P. 319, which, indeed, is also cited by the majority in the present case. And the example given, that of a promissory note, is obviously specious. Rarely, if ever, does a promissory note given by a debtor to his creditor integrate all their agreements (that is not the purpose it serves); it may or it may not integrate all their present contractual rights and obligations; but relevant to the parol evidence rule, at least until the advent of the majority opinion in this case, alleged collateral agreements which would vary or contradict the terms and conditions of a promissory note may *not* be shown by parol. (*Bank of America etc. Ass'n v. Pendergrass* (1935) 4 Cal.2d 258, 263-264(6), 48 P.2d 659.)

33. Upon this structure of incorrect premises and unfounded assertions the majority opinion arrives at its climax: The pronouncement of “several policies [to] be accommodated...*[i]n formulating the rule governing parol evidence.*” (Italics added.)⁷ Two of the “policies” as declared by the majority are: Written evidence is more accurate than human memory⁸ fraud or unintentional invention by interested witnesses may well occur.
34. I submit that these purported “policies” are in reality two of the basic and obvious reasons for adoption by the legislature of the parol evidence rule as the policy in this state. Thus the speculation of the majority concerning the views of various writers on the subject and the advisability of following them in this state is not only superfluous but flies flatly in the face of established California law and policy. It serves only to introduce uncertainty and confusion in a field of substantive law which was codified and made certain in this state a century ago.
35. However, despite the law which until the advent of the present majority opinion has been firmly and clearly established in California and relied upon by attorneys and courts alike, that parol evidence may *not* be employed to vary or contradict the terms of a written instrument, the majority now announce (p. 548) that such evidence “should be excluded only when the fact finder is *likely* to be misled,” and that “The rule must therefore be based on the *credibility* of the evidence.” (Italics added.) But was it not, inter alia, to avoid misleading the fact finder, and to further the introduction of only the evidence which is most likely to *be* credible (the written document), that the Legislature adopted the parol evidence rule as a part of the substantive law of this state?
36. Next, in an effort to implement this newly promulgated “credibility” test, the majority opinion offers a choice of two “standards”: one, a “certainty” standard, quoted from

⁷ It is the Legislature of this state which did the formulating of the rule governing parol evidence nearly a century ago when in 1872, as previously noted, sections 1625 of the Civil Code and 1856 of the Code of Civil Procedure were adopted. And as already shown herein, the rule has since been consistently applied by the courts of this state. The parol evidence rule as thus laid down by the Legislature and applied by the courts is the policy of this state.

⁸ Although the majority declare that this first ‘policy’ may be served by excluding parol evidence of agreements that directly contradict the writing, such contradiction is precisely the effect of the agreement sought to be shown by parol in this case.

the Uniform Commercial Code,⁹ and the other a “natural” standard found in the Restatement of Contracts,¹⁰ and concludes that at least for purposes of the present case the “natural” viewpoint should prevail.

37. This new rule, not hitherto recognized in California, provides that proof of a claimed collateral oral agreement is admissible if it is such an agreement as might *naturally* have been made a separate agreement by the parties under the particular circumstances. I submit that this approach opens the door to uncertainty and confusion. Who can know what its limits are? Certainly I do not. For example, in its application to this case who could be expected to divine as “natural” a separate oral agreement between the parties that the assignment, absolute and unrestricted on its face, was intended by the parties to be limited to the Masterson family?
38. Or, assume that one gives to his relative a promissory note and that the payee of the note goes bankrupt. By operation of law the note becomes an asset of the bankruptcy. The trustee attempts to enforce it. Would the relatives be permitted to testify that by a separate oral agreement made at the time of the execution of the note it was understood that should the payee fail in his business the maker would be excused from payment of the note, or that, as here, it was intended that the benefits of the note would be personal to the payee? I doubt that trial judges should be burdened with the task of conjuring whether it would have been ‘natural under those circumstances for such a separate agreement to have been made by the parties. Yet, under the application of the proposed rule, this is the task the trial judge would have, and in essence the situation presented in the instant case is no different.
39. Under the application of the codes and the present case law, proof of the existence of such an agreement would not be permitted, “natural” or “unnatural.” But conceivably, as loose as the new rule is, one judge might deem it natural and another judge unnatural.¹¹ And in each instance the ultimate decision would have to be made (“naturally”) on a case-by-case basis by the appellate courts.

⁹ ‘If the additional terms are such that, if agreed upon, they would certainly have been included in the document in the view of the court, then evidence of their alleged making must be kept from the trier of fact.’ (Comment 3, § 2-202; italics added.)

¹⁰ Viz., proof of a collateral agreement should be permitted if it ‘is such an agreement as might naturally be made as a separate agreement by parties situated as were the parties to the written contract.’ Restatement of Contracts, § 240, subd. (1)(b); italics added.)

¹¹ Or perhaps application of the new rule will turn upon the opinion of the court (trial or appellate) that it is “natural” for one family group to agree that in case of unfriendly approach by a creditor of any of

40. In an effort to provide justification for applying the newly pronounced “natural” rule to the circumstances of the present case, the majority opinion next attempts to account for the silence of the writing in this case concerning assignability of the option, by asserting that “the difficulty of accommodating the formalized structure of a deed to the insertion of collateral agreements makes it less likely that all the terms of such an agreement were included.” What difficulty would have been involved here, to add the words “this option is nonassignable”? The asserted “formalized structure of a deed” is no formidable barrier. The Legislature has set forth the requirements in simple language in section 1092 of the Civil Code. It is this: “I, A B, grant to C D all that real property situated in (naming county), State of California...described as follows: (describing it).” To this the grantor desiring to reserve an option to repurchase need only so state, as was done here. It is a matter of common knowledge that collateral agreements (such as the option clause here involved, or such as deed restrictions) are frequently included in deeds, without difficulty of any nature.
41. To support further speculation, that “the reservation of the option might well have been placed in the recorded deed solely to preserve the grantors' rights against any possible future purchasers, and this function could well be served without any mention of the parties' agreement that the option was personal,” the majority assert that “There is nothing in the record to indicate that the parties to this family transaction, through experience in land transactions or otherwise, had any warning of the disadvantages of failing to put the whole agreement in the deed.” (*Italics added.*) The facts of this case, however, do not support such claim of naivete. The grantor husband (the bankrupt businessman) testified that as none of the parties were attorneys “we wanted to contact my attorney...which we did...The wording in the option was obtained from (the attorney). ...I told him what my discussion was with the Sines (defendant grantees) and he wanted...a little time... And, then this (the wording provided by the attorney) was taken to the title company at the time Mr. and Mrs. Sine and I went in to complete the transaction.” (*Italics added.*) The witness was an experienced businessman who thus demonstrated awareness of the wisdom of seeking legal guidance and advice in this business transaction, and who did so. Wherein lies the naive family transaction postulated by the majority?

them, then the debtor's property will be transferable or assignable only to other members of the family, whereas such a scheme might be considered less than “natural” for other families to pursue.

42. The majority opinion then proceeds on the fallacious assertion that the right to transfer or to assign an option, if it contains no provisions forbidding transfer or indicating that performance involves elements personal to the parties, is a mere disputable presumption, and in purported support cites cases not one of which involves an option and in each of which the presumption which was invoked served to supply a missing but essential element of a complete agreement.¹² As already emphasized hereinabove, the right of free transferability of property, including options, is one of the most fundamental tenets of substantive law, and the crucial distinction would appear self-evident between such a basic right on the one hand, and on the other hand the disputable evidentiary presumptions which the law has developed to supply terms lacking from a written instrument but essential to making it whole and complete. There is no such lack in the deed and the option reservation now at issue.
43. The statement of the majority opinion that in the absence of a controlling statute the parties may provide that a contract right or duty is nontransferable, is of course true. Equally true is the next assertion that “even when there is no explicit agreement—written *or* oral—that contractual duties shall be personal, courts will effectuate a presumed intent to that effect if the circumstances indicate that performance by a substituted person would be different from that contracted for.” But to apply the law of contracts for the rendering of personal services to the reservation of an option in a deed of real estate calls for a misdirected use of the rule, particularly in an instrument containing not one word from which such “a presumed intent to that effect” could be gleaned. Particularly is the holding objectionable when the result is to upset established statutory and case law in this state that “circumstances” shown by parol may not be employed to contradict, add to or detract from, the agreement of the parties as expressed by them in writing. And once again the quoted pronouncement of the majority concerning the showing of “circumstances” by parol fails to find support in the cases they cite,¹³ which relate to a patent license agreement, held to be

¹² Thus in *American Industrial Sales Corp. v. Airscope, Inc.*, supra (1955) 44 Cal.2d 393, 397, 282 P.2d 504, the missing element was the place of payment of a note; in *Richter v. Union Land etc. Co.* (1900) 129 Cal. 367, 375, 62 P. 39, the missing element was the time of delivery; in *Wolters v. King* (1897) 119 Cal. 172, 175-176, 51 P. 35, it was the time of payment; and in *Mangini v. Wolfschmidt, Ltd.*, supra (1958) 165 Cal.App.2d 192, 200, 331 P.2d 728, and *Zinn v. Ex-Cell-O Corp.* (1957) 148 Cal.App.2d 56, 73-74, 306 P.2d 1017, it was the duration of an agency contract.

¹³ In *Farmland Irrigation Co. v. Dopplmaier*, supra (1957) 48 Cal.2d 208, 222, 308 P.2d 732, 740, the court in holding that a patent license agreement was assignable pursuant to the policy “clearly manifested” by “the statutes in this state ... in favor of the free transferability of all types of property,

assignable absent terms indicating a contrary intent; a contract to sell grapes, also held assignable; a contract which included language showing the intent that it be nonassignable; a contract to buy land held to be assignable because approval of title by the buyer was held not to be a personal privilege attaching only to the assignor; and to contracts for personal services.

44. In *Prichard v. Kimball*, supra (1923) 190 Cal. 757, 764-765, 214 P. 863, next cited by the majority, the *written* contract contained language showing the intent that it be nonassignable (as already pointed out hereinabove). *Simmons v. Zimmerman* (1904) 144 Cal. 256, 260-261, 79 P. 451, held that a contract to buy land *was* assignable, as approval of title by the buyer is *not* a personal privilege attaching only to the assignor (the party to whom the seller agreed to sell). *La Rue v. Groezinger* has already been shown not to support the majority's proposition here. And the last case which the majority cite, *Coykendall v. Jackson* (1936) 17 Cal.App.2d 729, 731, 62 P.2d 746, involved a contract for *personal* services, almost uniformly held to be nonassignable; it did *not* deal with a contract or an option to buy property, which ordinarily imposes no other obligation on the buyer than to make payment, as does the option now before this court.
45. Neither personal skill nor personal qualities can be conjured as a requirement for the exercise of the option reserved in the deed here, regardless of how ardent may be the desire of the parties (the bankrupt husband-optionee and his sister), "to keep the property in the ... family." Particularly is this true when a contrary holding would permit the property to be acquired by plaintiff referee in bankruptcy for the benefit of the creditors of the bankrupt husband.
46. Comment hardly seems necessary on the convenience to a bankrupt of such a device to defeat his creditors. He need only produce parol testimony that any options (or other property, for that matter) which he holds are subject to an oral "collateral agreement" with family members (or with friends) that the property is nontransferable

including rights under contracts," stated "The terms and purpose of a contract may show, however, that it was intended to be nonassignable. Thus the duties imposed upon one party may be of such a personal nature that their performance by someone else would in effect deprive the other party of that for which he bargained. The duties in such a situation cannot be delegated." (Citing *La Rue v. Groezinger* (1890) 84 Cal. 281, 283-285, 286, 24 P. 42, which held that a contract to sell grapes from a certain vineyard was assignable to the purchaser of the vineyard, as nothing in the contract language excluded the "idea of performance by another," and (p. 287, 24 P. p. 44) there was "nothing in the nature or circumstances ... which shows that the skill or other personal quality of the party was a distinctive characteristic of the thing stipulated for, or a material inducement to the contract.")

“in order to keep the property in the family” or in the friendly group. In the present case the value of the ranch which the bankrupt and his wife held an option to purchase has doubtless increased substantially during the years since they acquired the option. The initiation of this litigation by the trustee in bankruptcy to establish his right to enforce the option indicates his belief that there is substantial value to be gained for the creditors from this asset of the bankrupt. Yet the majority opinion permits defeat of the trustee and of the creditors through the device of an asserted collateral oral agreement that the option was “personal” to the bankrupt and nonassignable “in order to keep the property in the family”!¹⁴

47. It also seems appropriate to inquire as to the rights of plaintiff wife in the option which she holds with her bankrupt husband. Is her interest therein also subject to being shown to be personal and not salable or assignable? And, what are her rights and those of her husband in the ranch land itself, if they exercise their option to purchase it? Will they be free to then sell the land? Or, if they prefer, may they hold it beyond the reach of creditors? Or can other members of “the family” claim some sort of restriction on it in perpetuity, established by parol evidence?
48. And if defendants sell the land subject to the option, will the new owners be heard to assert that the option is “personal” to the optionees, “in order to keep the property in the Masterson family”? Or is that claim “personal” to defendants only?
49. These are only a few of the confusions and inconsistencies which will arise to plague property owners and, incidentally, attorneys and title companies, who seek to counsel and protect them.
50. I would hold that the trial court ruled correctly on the proffered parol evidence, and would affirm the judgment.

McCOMB, J., concurs.

¹⁴ As noted at the outset of this dissent, it was by means of the bankrupt's own testimony that defendants (the bankrupt's sister and her husband) sought to show that the option was personal to the bankrupt and thus not transferable to the trustee in bankruptcy.

Hunt Foods & Industries v. Doliner

Supreme Court of New York, Appellate Division

26 A.D.2d 41, 270 N.Y.S.2d 937, *aff'd*, 272 N.Y.S.2d 686 (1966)

Steuer, J.

1. In February, 1965 plaintiff corporation undertook negotiations to acquire the assets of Eastern Can Company. The stock of the latter is owned by defendant George M. Doliner and his family to the extent of 73%. The balance is owned by independent interests. At a fairly early stage of the negotiations agreement was reached as to the price to be paid by plaintiff (\$5,922,500 if in cash, or \$5,730,000 in Hunt stock), but several important items, including the form of the acquisition, were not agreed upon. At this point it was found necessary to recess the negotiations for several weeks. The Hunt negotiators expressed concern over any adjournment and stated that they feared that Doliner would use their offer as a basis for soliciting a higher bid from a third party. To protect themselves they demanded an option to purchase the Doliner stock. Such an option was prepared and signed by George Doliner and the members of his family and at least one other person associated with him who were stockholders. It provides that Hunt has the option to buy all of the Doliner stock at \$5.50 per share. The option is to be exercised by giving notice on or before June 1, 1965, and if notice is not given the option is void. If given, Hunt is to pay the price and the Doliners to deliver their stock within seven days thereafter. The agreement calls for Hunt to pay \$1,000 for the option, which was paid. To this point there is substantial accord as to what took place.
2. Defendant claims that when his counsel called attention to the fact that the option was unconditional in its terms, he obtained an understanding that it was only to be used in the event that he solicited an outside offer; and that plaintiff insisted that unless the option was signed in unconditional form negotiations would terminate. Plaintiff contends there was no condition. Concededly, on resumption of negotiations the parties failed to reach agreement and the option was exercised. Defendants declined the tender and refused to deliver the stock.
3. Plaintiff moved for summary judgment for specific performance. We do not believe that summary judgment lies. Plaintiff's position is that the condition claimed could

not be proved under the parol evidence rule and, eliminating that, there is no defense to the action.

4. The parol evidence rule, at least as that term refers to contracts of sale,¹ is now contained in section 2-202 of the Uniform Commercial Code, which reads:

Terms with respect to which the confirmatory memoranda of the parties agree or which are otherwise set forth in a writing intended by the parties as a final expression of their agreement with respect to such terms as are included therein may not be contradicted by evidence of any prior agreement or of a contemporaneous oral agreement but may be explained or supplemented ...

(b) by evidence of consistent additional terms unless the court finds the writing to have been intended also as a complete and exclusive statement of the terms of the agreement.

5. The term (that the option was not to be exercised unless Doliner sought outside bids), admittedly discussed but whose operative effect is disputed, not being set out in the writing, is clearly "additional" to what is in the writing. So the first question presented is whether that term is "consistent" with the instrument. In a sense any oral provision which would prevent the ripening of the obligations of a writing is inconsistent with the writing. But that obviously is not the sense in which the word is used (*Hicks v. Bush*, 10 N Y 2d 488, 491). To be inconsistent the term must contradict or negate a term of the writing. A term or condition which has a lesser effect is provable.
6. The Official Comment prepared by the drafters of the code contains this statement: "If the additional terms are such that, if agreed upon, they would certainly have been included in the document in the view of the court, then evidence of their alleged making must be kept from the trier of fact." (McKinney's Uniform Commercial Code, Part 1, p. 158.)
7. Special Term interpreted this language as not only calling for an adjudication by the court in all instances where proof of an "additional oral term" is offered, but making that determination exclusively the function of the court. We believe the proffered

¹ While article 2 of the Uniform Commercial Code which contains this section does not deal with the sale of securities, this section applies to article 8, dealing with securities. (Cf. *Agar v. Orda*, 264 N. Y. 248; Official Comment, McKinney's Cons. Laws of N. Y., Book 62 12, Part 1, Uniform Commercial Code, pp. 96-97; Note, 65 Col. L. Rev. 880, 890-891.) All parties and Special Term so regarded it.

evidence to be inadmissible only where the writing contradicts the existence of the claimed additional term (*Meadow Brook Nat. Bank v. Bzura*, 20 A D 2d 287, 290). The conversations in this case, some of which are not disputed, and the expectation of all the parties for further negotiations, suggest that the alleged oral condition precedent cannot be precluded as a matter of law or as factually impossible. It is not sufficient that the existence of the condition is implausible. It must be impossible (cf. *Millerton Agway Co-op. v. Briarcliff Farms*, 17 N Y 2d 57, 63-64).

8. The order should be reversed on the law and the motion for summary judgment denied, with costs and disbursements to abide the event.

Freund v. Washington Square Press, Inc.

Court of Appeals of New York
314 N.E.2d 419, 357 N.Y.S.2d 857 (1974)

RABIN, Judge.

1. In this action for breach of a publishing contract, we must decide what damages are recoverable for defendant's failure to publish plaintiff's manuscript. In 1965, plaintiff, an author and a college teacher, and defendant, Washington Square Press, Inc., entered into a written agreement which, in relevant part, provided as follows. Plaintiff ("author") granted defendant ("publisher") exclusive rights to publish and sell in book form plaintiff's work on modern drama. Upon plaintiff's delivery of the manuscript, defendant agreed to complete payment of a nonreturnable \$2,000 "advance." Thereafter, if defendant deemed the manuscript not "suitable for publication," it had the right to terminate the agreement by written notice within 60 days of delivery. Unless so terminated, defendant agreed to publish the work in hardbound edition within 18 months and afterwards in paperbound edition. The contract further provided that defendant would pay royalties to plaintiff, based upon specified percentages of sales. (For example, plaintiff was to receive 10% of the retail price of the first 10,000 copies sold in the continental United States.) If defendant failed to publish within 18 months, the contract provided that "this agreement shall terminate and the rights herein granted to the Publisher shall revert to the Author. In such event all payments therefore made to the Author shall belong to the Author without prejudice to any other remedies which the Author may have." The contract also provided that controversies were to be determined pursuant to the New York simplified procedure for court determination of disputes (CPLR 3031-3037, Consol. Laws, c. 8).
2. Plaintiff performed by delivering his manuscript to defendant and was paid his \$2,000 advance. Defendant thereafter merged with another publisher and ceased publishing in hardbound. Although defendant did not exercise its 60-day right to terminate, it has refused to publish the manuscript in any form.
3. Plaintiff commenced the instant action pursuant to the simplified procedure practice and initially sought specific performance of the contract. The Trial Term Justice denied specific performance but, finding a valid contract and a breach by defendant, set the matter down for trial on the issue of monetary damages, if any, sustained by the plaintiff. At trial, plaintiff sought to prove: (1) delay of his academic promotion;

(2) loss of royalties which would have been earned; and (3) the cost of publication if plaintiff had made his own arrangements to publish. The trial court found that plaintiff had been promoted despite defendant's failure to publish, and that there was no evidence that the breach had caused any delay. Recovery of lost royalties was denied without discussion. The court found, however, that the loss of hardcover publication to plaintiff was the natural and probable consequence of the breach and, based upon expert testimony, awarded \$10,000 to cover this cost. It denied recovery of the expenses of paperbound publication on the ground that plaintiff's proof was conjectural.

4. The Appellate Division, (3 to 2) affirmed, finding that the cost of publication was the proper measure of damages. In support of its conclusion, the majority analogized to the construction contract situation where the cost of completion may be the proper measure of damages for a builder's failure to complete a house or for use of wrong materials. The dissent concluded that the cost of publication is not an appropriate measure of damages and consequently, that plaintiff may recover nominal damages only.¹ We agree with the dissent. In so concluding, we look to the basic purpose of damage recovery and the nature and effect of the parties' contract.
5. It is axiomatic that, except where punitive damages are allowable, the law awards damages for breach of contract to compensate for injury caused by the breach—injury which was foreseeable, i.e., reasonably within the contemplation of the parties, at the time the contract was entered into. (*Swain v. Schieffelin*, 134 N.Y. 471, 473, 31 N.E. 1025, 1026.) Money damages are substitutional relief designed in theory “to put the injured party in as good a position as he would have been put by full performance of the contract, at the least cost to the defendant and without charging him with harms that he had no sufficient reason to foresee when he made the contract.” (5 CORBIN, CONTRACTS, § 1002, pp. 31-32; 11 WILLISTON, CONTRACTS (3d ed.), § 1338, p. 198.) In other words, so far as possible, the law attempts to secure to the injured party the benefit of his bargain, subject to the limitations that the injury—whether it be losses suffered or gains prevented—was foreseeable, and that the amount of damages claimed be measurable with a reasonable degree of certainty and, of course, adequately proven. (See, generally, DOBBS, LAW OF REMEDIES, p. 148; see, also,

¹ Plaintiff does not challenge the trial court's denial of damages for delay in promotion or for anticipated royalties.

Farnsworth, *Legal Remedies for Breach of Contract*, 70 COLUM. L. REV. 1145, 1159 [(1970)].) But it is equally fundamental that the injured party should not recover more from the breach than he would have gained had the contract been fully performed. (*Baker v. Drake*, 53 N.Y. 211, 217; see, generally, DOBBS, LAW OF REMEDIES, p. 810.)

6. Measurement of damages in this case according to the cost of publication to the plaintiff would confer greater advantage than performance of the contract would have entailed to plaintiff and would place him in a far better position than he would have occupied had the defendant fully performed. Such measurement bears no relation to compensation for plaintiff's actual loss or anticipated profit. Far beyond compensating plaintiff for the interests he had in the defendant's performance of the contract—whether restitution, reliance or expectation (see Fuller & Perdue, *Reliance Interest in Contract Damages*, 46 YALE L.J. 52, 53-56 [(1936)]) an award of the cost of publication would enrich plaintiff at defendant's expense.
7. Pursuant to the contract, plaintiff delivered his manuscript to the defendant. In doing so, he conferred a value on the defendant which, upon defendant's breach, was required to be restored to him. Special Term, in addition to ordering a trial on the issue of damages, ordered defendant to return the manuscript to plaintiff and plaintiff's restitution interest in the contract was thereby protected. (Cf. 5 CORBIN, CONTRACTS, § 996, p. 15.)
8. At the trial on the issue of damages, plaintiff alleged no reliance losses suffered in performing the contract or in making necessary preparations to perform. Had such losses, if foreseeable and ascertainable, been incurred, plaintiff would have been entitled to compensation for them. (Cf. *Bernstein v. Meech*, 130 N.Y. 354, 359, 29 N.E. 255, 257.)
9. As for plaintiff's expectation interest in the contract, it was basically two-fold—the “advance” and the royalties. (To be sure, plaintiff may have expected to enjoy whatever notoriety, prestige or other benefits that might have attended publication, but even if these expectations were compensable, plaintiff did not attempt at trial to place a monetary value on them.) There is no dispute that plaintiff's expectancy in the “advance” was fulfilled—he has received his \$2,000. His expectancy interest in the royalties—the profit he stood to gain from sale of the published book—while theoretically compensable, was speculative. Although this work is not plaintiff's first,

at trial he provided no stable foundation for a reasonable estimate of royalties he would have earned had defendant not breached its promise to publish. In these circumstances, his claim for royalties falls for uncertainty. (Cf. *Broadway Photoplay Co. v. World Film Corp.*, 225 N.Y. 104, 121 N.E. 756; *Hewlett v. Caplin*, 275 App. Div. 797, 88 N.Y.S.2d 428.)

10. Since the damages which would have compensated plaintiff for anticipated royalties were not proved with the required certainty, we agree with the dissent in the Appellate Division that nominal damages alone are recoverable. (Cf. *Manhattan Sav. Inst. v. Gottfried Baking Co.*, 286 N.Y. 398, 36 N.E.2d 637.) Though these are damages in name only and not at all compensatory, they are nevertheless awarded as a formal vindication of plaintiff's legal right to compensation which has not been given a sufficiently certain monetary valuation. (Cf. *Baker v. Hart*, 123 N.Y. 470, 474, 25 N.E. 948, 949; see, generally, DOBBS, LAW OF REMEDIES, p. 191; 11 WILLISTON, CONTRACTS (3d ed.), § 1339A, pp. 206-208.)
11. In our view, the analogy by the majority in the Appellate Division to the construction contract situation was inapposite. In the typical construction contract, the owner agrees to pay money or other consideration to a builder and expects, under the contract, to receive a completed building in return. The value of the promised performance to the owner is the properly constructed building. In this case, unlike the typical construction contract, the value to plaintiff of the promised performance—publication—was a percentage of sales of the books published and not the books themselves. Had the plaintiff contracted for the printing, binding and delivery of a number of hardbound copies of his manuscript, to be sold or disposed of as he wished, then perhaps the construction analogy, and measurement of damages by the cost of replacement or completion, would have some application.
12. Here, however, the specific value to plaintiff of the promised publication was the royalties he stood to receive from defendant's sales of the published book. Essentially, publication represented what it would have cost the defendant to confer that value upon the plaintiff, and, by its breach, defendant saved that cost. The error by the courts below was in measuring damages not by the value to plaintiff of the promised performance but by the cost of that performance to defendant. Damages are not measured, however, by what the defaulting party saved by the breach, but by the natural and probable consequences of the breach to the plaintiff. In this case, the consequence to plaintiff of defendant's failure to publish is that he is prevented from

realizing the gains promised by the contract—the royalties. But, as we have stated, the amount of royalties plaintiff would have realized was not ascertained with adequate certainty and, as a consequence, plaintiff may recover nominal damages only.

13. Accordingly, the order of the Appellate Division should be modified to the extent of reducing the damage award of \$10,000 for the cost of publication to six cents, but with costs and disbursements to the plaintiff.

Klein v. Pepsico, Inc.

United States Court of Appeals, Fourth Circuit
845 F.2d 76 (1988)

ERVIN, Circuit Judge:

1. This case turns on whether a contract was formed between Universal Jet Sales, Inc. (“UJS”) and PepsiCo, Inc., (“PepsiCo”) for the sale of a Gulfstream G-II corporate jet to UJS for resale to one Eugene V. Klein. If a contract was formed, the question remains whether the district court acted within his discretion by ordering specific performance of the contract. We believe the district court properly found that a contract was formed; however, we conclude that the remedy of specific performance is inappropriate. Accordingly, we affirm in part, reverse and remand in part.

I.

2. In March 1986, Klein began looking for a used corporate jet; specifically, he wanted a G-II. He contacted Patrick Janas, President of UJS, who provided information to Klein about several aircraft including the PepsiCo aircraft. Klein's pilot and mechanic, Mr. Sherman and Mr. Quaid, inspected the PepsiCo jet in New York. Mr. James Welsch served as the jet broker for PepsiCo.
3. Klein asked that the jet be flown to Arkansas for his personal inspection. On March 29, 1986, he inspected the jet. Mr. Rashid, PepsiCo Vice President for Asset Management and Corporate Service, accompanied the jet to Arkansas and met Mr. Klein. Janas also went to Arkansas. Klein gave Janas \$200,000 as a deposit on the jet, and told Janas to offer \$4.4 million for the aircraft.
4. On March 31, 1986, Janas telexed the \$4.4 million offer to Welsch. The telex said the offer was subject to a factory inspection satisfactory to the purchaser, and a definitive contract. On April 1, PepsiCo counteroffered with a \$4.7 million asking price. After some dickering, Welsch offered the jet for \$4.6 million. Janas accepted the offer by telex on April 3. Janas then planned to sell the aircraft to Klein for \$4.75 million. In Finding of Fact number 18, JA 85, Judge Williams declared that a contract had been formed at this point.
5. Judge Williams ruled that a contract was evidenced by Janas' confirming telex which “accepted” PepsiCo's offer to sell the jet, and noted that a \$100,000 down payment

would be wired. The telex also asked for the proper name of the company selling the aircraft. See JA 86 Finding of Fact number 22.

6. On April 3, Janas sent out copies of the Klein/UJS agreement and the UJS-PepsiCo agreement to the respective parties. Janas also sent a bill of sale to PepsiCo (to Rashid). PepsiCo sent the bill of sale to the escrow agent handling the deal on April 8. Mr. Rochoff, PepsiCo's corporate counsel, spoke with Janas about the standard contract sent by Janas to PepsiCo. He noted only that the delivery date should be changed.
7. On Monday, April 7, the aircraft was flown to Savannah, Georgia for the pre-purchase inspection. Quaid was present at the inspection for Klein. Archie Walker, PepsiCo's chief of maintenance, was present for the seller. Walker and Quaid discussed a list of repairs to be made to the jet. Most of the problems were cured during the inspection. However, one cosmetic problem was to be corrected in New York, and there were cracks in the engine blades of the right engine.
8. On April 8, a boroscopic examination conducted by Aviall revealed eight to eleven cracks on the turbine blades. Walker told Rashid that the cost of repairing the blades would be between \$25,000 to \$28,000. Judge Williams found in Finding of Fact numbers 34 through 37 that PepsiCo, through Walker and Rashid, agreed to pay for the repair to the engine.
9. On April 9, the plane was returned to New York. Rashid wanted the plane grounded; however, it was sent to retrieve the stranded PepsiCo Chairman of the Board from Dulles airport that same evening. Donald Kendall, the Chairman, on April 10, called Rashid and asked that the jet be withdrawn from the market. Rashid called Welsch who effected the withdrawal. On the 11th Janas told Klein that PepsiCo refused to tender the aircraft. The deal was supposed to close on Friday, April 11.
10. On April 14, Klein telexed UJS demanding delivery of the aircraft. That same day, UJS telexed PepsiCo demanding delivery and expressing satisfaction with the pre-purchase inspection. On April 15, PepsiCo responded with a telex to UJS saying that it refused to negotiate further because discussions had not reached the point of agreement; in particular, Klein was not prepared to go forward with the deal.
11. Judge Williams, in a lengthy opinion, made numerous findings of fact. Such findings are reviewed only for clear error. *Davis v. Food Lion*, 792 F.2d 1274, 1277 (4th

Cir.1986). If the findings are based on determinations of witness credibility, are consistent, and are corroborated by extrinsic evidence, they are virtually never clearly erroneous. *Brown v. Baltimore and Ohio R. Co.*, 805 F.2d 1133, 1140 (4th Cir.1986).

12. Judge Williams' decision to grant specific performance is reviewed only for an abuse of discretion. *Haythe v. May*, 223 Va. 359, 288 S.E.2d 487 (1982); *Horner v. Bourland*, 724 F.2d 1142, 1144-45 (5th Cir.1984). Keeping these standards in mind, we now turn to the first issue, whether the district court clearly erred in finding that a contract arose between PepsiCo and UJS.

II.

13. PepsiCo argues forcefully that no contract was formed between it and UJS. The soft drink dealer argues first that the parties did not intend to be bound until a complete integration was written in final form. Until that definitive written contract existed, PepsiCo maintains that no contract existed. The company argues that the March 31 and April 1 telexes explicitly stated that no contract would exist until a written agreement was executed. Because no written agreement had been executed (PepsiCo had not signed the sales agreement sent by Janas to PepsiCo) the company argues that it had the right to withdraw from the negotiations. PepsiCo cites *Reprosystem, B.V. v. SCM Corp.*, 727 F.2d 257, 262 (2d Cir.1984), *cert. denied*, 469 U.S. 828 (1984) and *Skycom Corp. v. Telstar Corp.*, 813 F.2d 810, 815-16 (7th Cir.1987) for the general proposition that either party can withdraw from negotiations for any reason.
14. Upon reviewing the facts, Judge Williams ruled that a contract was formed between the parties. He explains:

A contract was formed between UJS and PepsiCo for the sale of the GII aircraft, Serial No. 170, for \$4.6 million. The contract formation is based upon (1) UJS's April 3rd confirming telex; (2) the conduct of the parties, e.g., (a) PepsiCo's failure to communicate any objection to the terms of the April 3rd telex confirming the agreement reached between Welsch and Janas; (b) PepsiCo's directive to UJS to wire transfer a One Hundred Thousand Dollar (\$100,000.00) down payment, which money was received by PepsiCo; (c) PepsiCo's communication with UJS that the Sales Agreement, which served to memorialize the contract, appeared "fine"; (d) PepsiCo's execution of the Bill of Sale for the aircraft and its sending of the Bill of Sale to the escrow agent, as called for by Janas and in the Sales Agreement; (e) PepsiCo's sending the aircraft to Savannah, Georgia, for a prepurchase inspection as

called for in both the April 3rd confirming telex and the Sales Agreement; and (e) admissions of PepsiCo., through Rashid, that UJS's offer to purchase the airplane was accepted.

JA 103-04, Conclusion of Law # 6. Finally, Judge Williams expressly held that the intent to memorialize the contract in writing was not necessarily a condition to the existence of the contract itself. JA 104 (Conclusion of Law number 8).

15. PepsiCo offers no reason as to why Judge Williams' findings on this issue are clearly erroneous. They merely disagree with his characterizations of the facts. This court may disagree with his characterization too, but that does not amount to a firm and definite conviction that a mistake has been committed. *Anderson v. City of Bessemer City, N.C.*, 470 U.S. 564 (1985).
16. PepsiCo argues secondly, that no contract was formed because the condition of inspection satisfactory to the buyer had not been met. PepsiCo urges strongly that neither UJS nor Klein were willing to accept the aircraft “as is,” so the condition was unsatisfied. Judge Williams ruled that when PepsiCo agreed to make the repairs, the condition was satisfied. Furthermore, the court below ruled that the condition was excused by PepsiCo's refusal to tender the aircraft so that the buyer could express his dissatisfaction.
17. The district court's first ruling, that the condition was satisfied by PepsiCo's offers to pay for the repairs, resolves this issue. Judge Williams ruled that based on the conversations between Walker and Rashid, the seller had agreed to make the necessary repairs to market the plane. See Finding of Fact 34-37 at JA 89-90. Again, PepsiCo offers no suggestion that Judge Williams committed any error, much less clear error. Rather, PepsiCo urges its version of the facts on this court. Without more, the company loses.
18. Ultimately, then, a contract exists between PepsiCo and UJS for the sale of one G-II Gulfstream aircraft.¹ Because PepsiCo failed to deliver the aircraft, the district court

¹ PepsiCo argues that Klein has no right to sue on the PepsiCo/UJS contract because (1) the contract violates the statute of frauds, (2) Klein was not an intended beneficiary of the contract, and (3) the Klein/UJS contract, from which Klein derives his right to sue PepsiCo, was rescinded. The district court's discussion thoroughly and ably treats these claims and rejects them. Based on the district court's reasoning, this court affirms the disposition of those issues.

ordered relief in the form of specific performance. We now consider the appropriateness of the relief ordered.

III.

19. The Virginia Code § 8.2-716 permits a jilted buyer of goods to seek specific performance of the contract if the goods sought are unique, or in other proper circumstances. Judge Williams ruled that: 1) the G-II aircraft involved in this case is unique and 2) Klein's inability to cover with a comparable aircraft is strong evidence of "other proper circumstances." JA 111-112, Conclusions of Law No. 31 and No. 32. These conclusions are not supported in the record.
20. We note first that Virginia's adoption of the Uniform Commercial Code does not abrogate the maxim that specific performance is inappropriate where damages are recoverable and adequate. *Griscom v. Childress*, 183 Va. 42, 31 S.E.2d 309, 311 (1944). In this case Judge Williams repeatedly stated that money damages would make Klein whole. JA 668-9, 582. Klein argued that he wanted the plane to resell it for a profit. JA 669. Finally, an increase in the cost of a replacement does not merit the remedy of specific performance. *Hilmor Sales Co. v. Helen Neuschalfer Division of Supronics Corp.*, 6 U.C.C.Rep.Serv. 325 (N.Y.Sup.Ct.1969). There is no room in this case for the equitable remedy of specific performance.
21. Turning now to the specific rulings of the court below, Judge Williams explained that the aircraft was unique because only three comparable aircraft existed on the market. Therefore, Klein would have to go through considerable expense to find a replacement. JA 110. Klein's expert testified that there were twenty-one other G-II's on the market, three of which were roughly comparable. JA 838-9, 1284-88. Klein's chief pilot said that other G-II's could be purchased. JA 259. Finally, we should note that UJS bought two G-II's which they offered to Klein after this deal fell through, JA 796-7, and Klein made bids on two other G-II's after PepsiCo withdrew its aircraft from the market. JA 277, 666, 694. Given these facts, we find it very difficult to support a ruling that the aircraft was so unique as to merit an order of specific performance.
22. Judge Williams ruled further that Klein's inability to cover his loss is an "other proper circumstance" favoring specific performance. Klein testified himself that he didn't purchase another G-II because prices had started to rise. JA 693. Because of the price increase, he decided to purchase a G-III aircraft. As noted earlier, price increases

alone are no reason to order specific performance. Because money damages would clearly be adequate in this case, and because the aircraft is not unique within the meaning of the Virginia Commercial Code, we reverse the grant of specific performance and remand the case to the district court for a trial on damages.

AFFIRMED IN PART, REVERSED AND REMANDED IN PART.

Sedmak v. Charlie's Chevrolet

Missouri Court of Appeals
622 S.W.2d 694 (1981)

SATZ, Judge.

1. This is an appeal from a decree of specific performance. We affirm.
2. In their petition, plaintiffs, Dr. and Mrs. Sedmak (Sedmaks), alleged they entered into a contract with defendant, Charlie's Chevrolet, Inc. (Charlie's), to purchase a Corvette automobile for approximately \$15,000.00. The Corvette was one of a limited number manufactured to commemorate the selection of the Corvette as the Pace Car for the Indianapolis 500. Charlie's breached the contract, the Sedmaks alleged, when, after the automobile was delivered, an agent for Charlie's told the Sedmaks they could not purchase the automobile for \$15,000.00 but would have to bid on it.
3. The trial court found the parties entered into an oral contract and also found the contract was excepted from the Statute of Frauds. The court then ordered Charlie's to make the automobile "available for delivery" to the Sedmaks.
4. Charlie's raises three points on appeal: (1) the existence of an oral contract is not supported by the credible evidence; (2) if an oral contract exists, it is unenforceable because of the Statute of Frauds; and (3) specific performance is an improper remedy because the Sedmaks did not show their legal remedies were inadequate.
5. This was a court-tried case. The scope of our review is defined by the well-known principles set out in *Murphy v. Carron*, 536 S.W.2d 30 (Mo. 1976). We sustain the judgment of the trial court unless the judgment is not supported by substantial evidence, unless it is against the weight of the evidence or unless it erroneously declares or applies the law. *Id.* at 32. In conducting our review, we do not judge the credibility of witnesses. That task quite properly rests with the trial court. Rule 73.01(c)(2); *Kim Mfg., Inc. v. Superior Metal Treating, Inc.*, 537 S.W.2d 424, 428 (Mo.App.1976).
6. In light of these principles, the record reflects the Sedmaks to be automobile enthusiasts, who, at the time of trial, owned six Corvettes. In July, 1977, "Vette Vues," a Corvette fancier's magazine to which Dr. Sedmak subscribed, published an article announcing Chevrolet's tentative plans to manufacture a limited edition of the

Corvette. The limited edition of approximately 6,000 automobiles was to commemorate the selection of the Corvette as the Indianapolis 500 Pace Car. The Sedmaks were interested in acquiring one of these Pace Cars to add to their Corvette collection. In November, 1977, the Sedmaks asked Tom Kells, sales manager at Charlie's Chevrolet, about the availability of the Pace Car. Mr. Kells said he did not have any information on the car but would find out about it. Kells also said if Charlie's were to receive a Pace Car, the Sedmaks could purchase it.

7. On January 9, 1978, Dr. Sedmak telephoned Kells to ask him if a Pace Car could be ordered. Kells indicated that he would require a deposit on the car, so Mrs. Sedmak went to Charlie's and gave Kells a check for \$500.00. She was given a receipt for that amount bearing the names of Kells and Charlie's Chevrolet, Inc. At that time, Kells had a pre-order form listing both standard equipment and options available on the Pace Car. Prior to tendering the deposit, Mrs. Sedmak asked Kells if she and Dr. Sedmak were "definitely going to be the owners." Kells replied, "yes." After the deposit had been paid, Mrs. Sedmak stated if the car was going to be theirs, her husband wanted some changes made to the stock model. She asked Kells to order the car equipped with an L82 engine, four speed standard transmission and AM/FM radio with tape deck. Kells said that he would try to arrange with the manufacturer for these changes. Kells was able to make the changes, and, when the car arrived, it was equipped as the Sedmaks had requested.
8. Kells informed Mrs. Sedmak that the price of the Pace Car would be the manufacturer's retail price, approximately \$15,000.00. The dollar figure could not be quoted more precisely because Kells was not sure what the ordered changes would cost, nor was he sure what the "appearance package"—decals, a special paint job—would cost. Kells also told Mrs. Sedmak that, after the changes had been made, a "contract"—a retail dealer's order form—would be mailed to them. However, no form or written contract was mailed to the Sedmaks by Charlie's.
9. On January 25, 1978, the Sedmaks visited Charlie's to take delivery on another Corvette. At that time, the Sedmaks asked Kells whether he knew anything further about the arrival date of the Pace Car. Kells replied he had no further information but he would let the Sedmaks know when the car arrived. Kells also requested that Charlie's be allowed to keep the car in their showroom for promotional purposes until after the Indianapolis 500 Race. The Sedmaks agreed to this arrangement.

10. On April 3, 1978, the Sedmaks were notified by Kells that the Pace Car had arrived. Kells told the Sedmaks they could not purchase the car for the manufacturer's retail price because demand for the car had inflated its value beyond the suggested price. Kells also told the Sedmaks they could bid on the car. The Sedmaks did not submit a bid. They filed this suit for specific performance.
11. Mr. Kells' testimony about his conversations with the Sedmaks regarding the Pace Car differed markedly from the Sedmaks' testimony. Kells stated that he had no definite price information on the Pace Car until a day or two prior to its arrival at Charlie's. He denied ever discussing the purchase price of the car with the Sedmaks. He admitted, however, that after talking with the Sedmaks on January 9, 1978,¹ he telephoned the zone manager and requested changes be made to the Pace Car. He denied the changes were made pursuant to Dr. Sedmak's order. He claimed the changes were made because they were "more favorable to the automobile" and were changes Dr. Sedmak "preferred." In ordering the changes, Kells said he was merely taking Dr. Sedmak's advice because he was a "very knowledgeable man on the Corvette." There is no dispute, however, that when the Pace Car arrived, it was equipped with the options requested by Dr. Sedmak.
12. Mr. Kells also denied the receipt for \$500.00 given him by Mrs. Sedmak on January 9, 1978, was a receipt for a deposit on the Pace Car. On direct examination, he said he "accepted a five hundred dollar (\$500) deposit from the Sedmaks to assure them the first opportunity of purchasing the car." On cross-examination, he said: "We were accepting bids and with the five hundred dollar (\$500) deposit it was to give them the first opportunity to bid on the car." Then after acknowledging that other bidders had not paid for the opportunity to bid, he explained the deposit gave the Sedmaks the "last opportunity" to make the final bid. Based on this evidence, the trial court found the parties entered into an oral contract for the purchase and sale of the Pace Car at the manufacturer's suggested retail price.
13. Charlie's first contends the Sedmaks' evidence is "so wrought with inconsistencies and contradictions that a finding of an oral contract for the sale of a Pace Car at the manufacturer's suggested retail price is clearly against the weight of the evidence." We disagree. The trial court chose to believe the Sedmaks' testimony over that of Mr. Kells and the reasonableness of this belief was not vitiated by any real contradictions

¹ According to Kells' testimony, both Mr. and Mrs. Sedmak visited Charlie's on January 9, 1978. Mrs. Sedmak testified only she visited Charlie's on that date.

in the Sedmaks' testimony. Charlie's examples of conflict are either facially not contradictory or easily reconcilable.

14. Although not clearly stated in this point or explicitly articulated in its argument, Charlie's also appears to argue there was no contract because the parties did not agree to a price. The trial court concluded “(t)he price was to be the suggested retail price of the automobile at the time of delivery.” Apparently, Charlie's argues that if this were the agreed to price, it is legally insufficient to support a contract because the manufacturer's suggested retail price is not a mandatory, fixed and definite selling price but, rather, as the term implies, it is merely a suggested price which does not accurately reflect the market and the actual selling price of automobiles. Charlie's argument is misdirected and, thus, misses the mark.
15. Without again detailing the facts, there was evidence to support the trial court's conclusion that the parties agreed the selling price would be the price suggested by the manufacturer. Whether this price accurately reflects the market demands on any given day is immaterial. The manufacturer's suggested retail price is ascertainable and, thus, if the parties choose, sufficiently definite to meet the price requirements of an enforceable contract. Failure to specify the selling price in dollars and cents did not render the contract void or voidable. See, e. g., *Klaber v. Lahar*, 63 S.W.2d 103, 106-107 (Mo.1933); see also § 400.2-305 RSMo 1978. As long as the parties agreed to a method by which the price was to be determined and as long as the price could be ascertained at the time of performance, the price requirement for a valid and enforceable contract was satisfied. See *Burger v. City of Springfield*, 323 S.W.2d 777, 783-84 (Mo.1959); see also, *Allied Disposal, Inc. v. Bob's Home Service, Inc.*, 595 S.W.2d 417, 419-20 (Mo.App.1980) and § 400.2-305 RSMo 1978. This point is without merit.
16. Charlie's next complains that if there were an oral contract, it is unenforceable under the Statute of Frauds. The trial court concluded the contract was removed from the Statute of Frauds either by the written memoranda concerning the transaction or by partial payment made by the Sedmaks. We find the latter ground a sufficient answer to defendant's complaint. We discuss it and do not consider or address the former ground.
17. Prior to our adoption of the Uniform Commercial Code, part payment for goods was sufficient to remove the entire contract from the Statute of Frauds. § 432.020 RSMo

1949; *Woodburn v. Cogdal*, 39 Mo. 222, 228 (1866); See *Coffman v. Fleming*, 301 Mo. 313, 256 S.W. 731, 732-733 (1923). This result followed from the logical assumption that money normally moves from one party to another not as a gift but for a bargain. The basis of this rule is the probative value of the act—part payment shows the existence of an agreement. 3 SALES & BULK TRANSFERS UNDER U.C.C., (Bender), § 2.04(5) at 2-96. However, “[t]his view overlooks the fact that, although ... part payment of the price does indicate the existence of an agreement, [it does] not reveal [the agreement’s] quantity term, a key provision without which the court cannot reconstruct the contract fairly and provide against fraudulent claims.”¹ HAWKLAND, A TRANSACTIONAL GUIDE TO THE UNIFORM COMMERCIAL CODE (1964), § 1.1202 at 28. Thus, under this rule a buyer who orally purchased one commercial unit for \$10.00 could falsely assert he purchased 100 units and, then, by also asserting a \$10.00 payment was part payment on the 100 units, he could, in theory and in practice, convince the trier of fact that the contract entered into was for 100 units. The Code attempts to correct this defect by providing that part payment of an oral contract satisfies the Statute of Frauds only “with respect to goods for which payment has been made and accepted” § 400.2-201(3)(c) RSMo 1978. Under this provision, part payment satisfies the Statute of Frauds, not for the entire contract, but only for that quantity of goods to which part payment can be apportioned.² This change simply reflects the rationale that part payment alone does not establish the oral contract’s quantity term.

18. In correcting one problem, however, the change creates another problem when, as in the instant case, payment for a single unit sale has been less than full. Obviously, this part payment cannot be apportioned and, thus, the question arises how shall this subsection of the Code be applied. The few courts that have considered this question have used opposing logic and, thus, reached opposing answers. At least one court

² § 400.2-201(3)(c) provides:

- (3) A contract which does not satisfy the requirements (of a writing) but which is valid in other respects is enforceable
 - (c) with respect to goods for which payment has been made and accepted or which have been received and accepted.

Interpreting this section, U.C.C. Comment 2 states:

‘Partial performance’ as a substitute for the required memorandum can validate the contract only for the goods which have been accepted or for which payment has been made and accepted. If the Court can make a just apportionment, ..., the agreed price of any goods actually delivered can be recovered without a writing or, if the price has been paid, the seller can be forced to deliver an apportionable part of the goods.

reads and applies the changed provision literally and denies the enforcement of the oral contract because payment has not been received in full. *Williamson v. Martz*, 11 Pa. Dist. & Co. R.2d 33, 35 (1956). The *Williamson* Court reasoned:

Under the code, part payment takes the case out of the statute only to the extent for which payment has been made. The code therefore makes an important change by denying the enforcement of the contract where in the case of a single object the payment made is less than the full amount.

Id. at 35.

19. Charlie's argues for this view. Other courts infer that part payment for one unit is still sufficient evidence that a contract existed between the parties and enforce the oral contract. *Lockwood v. Smigel*, 18 Cal.App.3d 800, 96 Cal.Rptr. 289 (1971); *Starr v. Freeport Dodge, Inc.*, 54 Misc.2d 271, 282 N.Y.S.2d 58 (N.Y.Dist.1967); see also, *Paloukos v. Intermountain Chevrolet Company*, 99 Idaho 740, 588 P.2d 939, 944 (1978); *Bertram Yacht Sales, Inc. v. West*, 209 So.2d 677, 679 (Fla.App.1968); *Thomaier v. Hoffman Chevrolet, Inc.*, 64 A.D.2d 492, 410 N.Y.S.2d 645, 648-649 (1978). We are persuaded by the cogency of the logic supporting this view.
20. Admittedly, § 400.2-201(3)(c) does validate a divisible contract only for as much of the goods as has been paid for. However, this subsection was drafted to provide a method for enforcing oral contracts where there is a quantity dispute. See *Lockwood v. Smigel, supra*, 18 Cal.App.3d 800, 96 Cal.Rptr. at 291; see also, 1 HAWKLAND, *supra* at 28. The subsection does not necessarily resolve the Statute of Frauds problem where there is no quantity dispute. Neither the language of the subsection nor its logical dictates necessarily invalidate an oral contract for an indivisible commercial unit where part payment has been made and accepted. If there is no dispute as to quantity, the part payment still retains its probative value to prove the existence of the contract.
21. Moreover, where, as here, there is no quantity dispute, part payment evidences the existence of a contract as satisfactorily as would a written memorandum of agreement under the liberalized criteria of the Code. The Code establishes only three basic requirements for a written memorandum to take an oral contract out of the Statute of Frauds. "First, it must evidence a contract for the sale of goods; second it must be 'signed,' a word which includes any authentication which identifies the party to be charged; and third, it must specify a quantity." § 400.2-201 RSMo 1978, U.C.C.,

Comment 1. Here, part payment evidences the contract for the sale of goods—the car. The party to be charged—Charlie's—is identified as the one who received payment. The quantity is not in dispute because the Sedmaks are claiming to have purchased one unit—the car. Thus, part payment here evidences the existence of a contract as satisfactorily as would a written memorandum of agreement under the Code. *Lockwood v. Smigel*, 18 Cal.App.3d 800, 96 Cal.Rptr. 289, 291 (1971); see also *Paloukos v. Intermountain Chevrolet Co.*, 99 Idaho 740, 588 P.2d 939, 944 (1978).

22. Finally, the Code has not changed the basic policy of the Statute of Frauds.

The purpose of the Statute of Frauds is to prevent the enforcement of alleged promises that were never made; it is not, and never has been, to justify the contractors in repudiating promises that were in fact made.

Corbin, *The Uniform Commercial Code; Should It Be Enacted?* 59 YALE L.J. 821, 829 (1950). Enforcement of the oral contract here carries out the purpose of the Statute of Frauds. Denial of the contract's existence frustrates that purpose. The present contract could not have contemplated less than one car. If the part payment is believed, it must have been intended to buy the entire car not a portion of the car. Thus, denying the contract because part payment cannot be apportioned encourages fraud rather than discouraging it. “The Statute of Frauds would be used to cut down the trusting buyer rather than to protect the one who, having made his bargain, parted with a portion of the purchase price as an earnest of his good faith.” *Starr v. Freeport Dodge, Inc.*, *supra*, 54 Misc.2d 271, 282 N.Y.S.2d at 61.

23. We hold, therefore, that where, as here, there is no dispute as to quantity, part payment for a single indivisible commercial unit validates an oral contract under § 400.2-201(3)(c) RSMo 1978.
24. Finally, Charlie's contends the Sedmaks failed to show they were entitled to specific performance of the contract. We disagree. Although it has been stated that the determination whether to order specific performance lies within the discretion of the trial court, *Landau v. St. Louis Public Service Co.*, 273 S.W.2d 255, 259 (Mo.1954), this discretion is, in fact, quite narrow. When the relevant equitable principles have been met and the contract is fair and plain, “specific performance goes as a matter of right.” *Miller v. Coffeen*, 280 S.W.2d 100, 102 (Mo.1955). Here, the trial court ordered specific performance because it concluded the Sedmaks “have no adequate remedy at law for the reason that they cannot go upon the open market and purchase

an automobile of this kind with the same mileage, condition, ownership and appearance as the automobile involved in this case, except, if at all, with considerable expense, trouble, loss, great delay and inconvenience.” Contrary to defendant's complaint, this is a correct expression of the relevant law and it is supported by the evidence.

25. Under the Code, the court may decree specific performance as a buyer's remedy for breach of contract to sell goods “where the goods are unique or in other proper circumstances.” § 400.2-716(1) RSMo 1978. The general term “in other proper circumstances” expresses the drafters' intent to “further a more liberal attitude than some courts have shown in connection with the specific performance of contracts of sale.” § 400.2-716, U.C.C., Comment 1. This Comment was not directed to the courts of this state, for long before the Code, we, in Missouri, took a practical approach in determining whether specific performance would lie for the breach of contract for the sale of goods and did not limit this relief only to the sale of “unique” goods. *Boeving v. Vandover*, 240 Mo.App. 117, 218 S.W.2d 175 (1945). In *Boeving*, plaintiff contracted to buy a car from defendant. When the car arrived, defendant refused to sell. The car was not unique in the traditional legal sense but, at that time, all cars were difficult to obtain because of war-time shortages. The court held specific performance was the proper remedy for plaintiff because a new car “could not be obtained elsewhere except at considerable expense, trouble or loss, which cannot be estimated in advance and under such circumstances (plaintiff) did not have an adequate remedy at law.” *Id.* at 177-178. Thus, *Boeving*, presaged the broad and liberalized language of § 400.2-716(1) and exemplifies one of the “other proper circumstances” contemplated by this subsection for ordering specific performance. § 400.2-716, Missouri Code Comment 1. The present facts track those in *Boeving*.
26. The Pace Car, like the car in *Boeving*, was not unique in the traditional legal sense. It was not an heirloom or, arguably, not one of a kind. However, its “mileage, condition, ownership and appearance” did make it difficult, if not impossible, to obtain its replication without considerable expense, delay and inconvenience. Admittedly, 6,000 Pace Cars were produced by Chevrolet. However, as the record reflects, this is limited production. In addition, only one of these cars was available to each dealer, and only a limited number of these were equipped with the specific options ordered by plaintiffs. Charlie's had not received a car like the Pace Car in the previous two years. The sticker price for the car was \$14,284.21. Yet Charlie's received offers from individuals in Hawaii and Florida to buy the Pace Car for \$24,000.00 and \$28,000.00

respectively. As sensibly inferred by the trial court, the location and size of these offers demonstrated this limited edition was in short supply and great demand. We agree, with the trial court. This case was a “proper circumstance” for ordering specific performance.

Judgment affirmed.

Hadley v. Baxendale

Court of Exchequer

9 Exch. 341, 156 Eng. Rep. 145 (1854)

1. [Reporter's Headnote:] At the trial before Crompton, J., at the last Gloucester Assizes, it appeared that the plaintiffs carried on an extensive business as millers at Gloucester; and that, on the 11th of May, their mill was stopped by a breakage of the crank shaft by which the mill was worked. The steam-engine was manufactured by Messrs. Joyce & Co., the engineers, at Greenwich, and it became necessary to send the shaft as a pattern for a new one to Greenwich. The fracture was discovered on the 12th, and on the 13th the plaintiffs sent one of their servants to the office of the defendants, who are the well-known carriers trading under the name of Pickford & Co., for the purpose of having the shaft carried to Greenwich. The plaintiffs' servant told the clerk that the mill was stopped, and that the shaft must be sent immediately; and in answer to the inquiry when the shaft would be taken, the answer was, that if it was sent up by twelve o'clock any day, it would be delivered at Greenwich on the following day. On the following day the shaft was taken by the defendants, before noon, for the purpose of being conveyed to Greenwich, and the sum of 2£ 4s. was paid for its carriage for the whole distance; at the same time the defendants' clerk was told that a special entry, if required, should be made to hasten its delivery. The delivery of the shaft at Greenwich was delayed by some neglect; and the consequence was, that the plaintiffs did not receive the new shaft for several days after they would otherwise have done, and the working of their mill was thereby delayed, and they thereby lost the profits they would otherwise have received.
2. On the part of the defendants, it was objected that these damages were too remote, and that the defendants were not liable with respect to them. The learned Judge left the case generally to the jury, who found a verdict with 25£ damages beyond the amount paid into Court.
3. Whateley, in last Michaelmas Term, obtained a rule nisi for a new trial, on the ground of misdirection.

ALDERSON, B.

4. We think that there ought to be a new trial in this case; but, in so doing, we deem it to be expedient and necessary to state explicitly the rule which the Judge, at the next trial, ought, in our opinion, to direct the jury to be governed by when they estimate the damages.
5. Indeed, it is of the last importance that we should do this; for, if the jury are left without any definite rule to guide them, it will, in such cases as these, manifestly lead to the greatest injustice. The Courts have done this on several occasions; and in *Blake v. Midland Railway Company* (18 Q. B. 93), the Court granted a new trial on this very ground, that the rule had not been definitely laid down to the jury by the learned Judge at Nisi Prius.
6. "There are certain establishing rules", this Court says, in *Alder v. Keighley* (15 M. & W. 117), "according to which the jury ought to find". And the Court, in that case, adds: "and here there is a clear rule, that the amount which would have been received if the contract had been kept, is the measure of damages if the contract is broken."
7. Now we think the proper rule in such a case as the present is this:-- Where two parties have made a contract which one of them has broken, the damages which the other party ought to receive in respect of such breach of contract should be such as may fairly and reasonably be considered either arising naturally, i.e., according to the usual course of things, from such breach of contract itself, or such as may reasonably be supposed to have been in the contemplation of both parties, at the time they made the contract, as the probable result of the breach of it. Now, if the special circumstances under which the contract was actually made were communicated by the plaintiffs to the defendants, and thus known to both parties, the damages resulting from the breach of such a contract, which they would reasonably contemplate, would be the amount of injury which would ordinarily follow from a breach of contract under these special circumstances so known and communicated. But, on the other hand, if these special circumstances were wholly unknown to the party breaking the contract, he, at the most, could only be supposed to have had in his contemplation the amount of injury which would arise generally, and in the great multitude of cases not affected by any special circumstances, from such a breach of contract. For, had the special circumstances been known, the parties might have specially provided for the breach of contract by special terms as to the damages in that case; and of this

advantage it would be very unjust to deprive them. Now the above principles are those by which we think the jury ought to be guided in estimating the damages arising out of any breach of contract. It is said, that other cases such as breaches of contract in the nonpayment of money, or in the not making a good title of land, are to be treated as exceptions from this, and as governed by a conventional rule. But as, in such cases, both parties must be supposed to be cognizant of that well-known rule, these cases may, we think, be more properly classed under the rule above enunciated as to cases under known special circumstances, because there both parties may reasonably be presumed to contemplate the estimation of the amount of damages according to the conventional rule. Now, in the present case, if we are to apply the principles above laid down, we find that the only circumstances here communicated by the plaintiffs to the defendants at the time of 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 the mill.

8. But how do these circumstances shew reasonably that the profits of the mill must be stopped by an unreasonable delay in the delivery of the broken shaft by the carrier to the third person? Suppose the plaintiffs had another shaft in their possession put up or putting up at the time, and that they only wished to send back the broken shaft to the engineer who made it; it is clear that this would be quite consistent with the above circumstances, and yet the unreasonable delay in the delivery would have no effect upon the intermediate profits of the mill. Or, again, suppose that, at the time of the delivery to the carrier, the machinery of the mill had been in other respects defective, then, also, the same results would follow. Here it is true that the shaft was actually sent back to serve as a model for the new one, and that the want of a new one was the only cause of the stoppage of the mill, and that the loss of profits really arose from not sending down the new shaft in proper time, and that this arose from the delay in delivering the broken one to serve as a model. But it is obvious that, in the great multitude of cases of millers sending off broken shafts to third persons by a carrier under ordinary circumstances, such consequences would not, in all probability, have occurred; and these special circumstances were here never communicated by the plaintiffs to the defendants. It follows therefore, that the loss of profits here cannot reasonably be considered such a consequence of the breach of contract as could have been fairly and reasonably contemplated by both the parties when they made this contract. For such loss would neither have flowed naturally from the breach of this contract in the great multitude of such cases occurring under ordinary circumstances,

nor were the special circumstances, which, perhaps, would have made it a reasonable and natural consequence of such breach of contract, communicated to or known by the defendants. The Judge ought, therefore, to have told the jury that upon the facts then before them they ought not to take the loss of profits into consideration at all in estimating the damages. There must therefore be a new trial in this case.

Rule absolute.

Drews Company v. Ledwith-Wolfe Associates

Supreme Court of South Carolina
371 S.E.2d 532 (1988)

HARWELL, Justice:

1. This case involves the breach of a construction contract. We affirm the trial court's refusal to grant a new trial, but reverse the jury's award of lost profits.

FACTS

2. The Drews Company, Inc. ("Contractor") contracted to renovate a building owned by Ledwith-Wolfe Associates, Inc. ("Owner"). Owner intended to convert the building into a restaurant. From its inception, the project was plagued by construction delays, work change orders, and general disagreement over the quality of work performed. Contractor eventually pulled its workers off the project. Contractor later filed, then sued to foreclose, a mechanic's lien for labor and materials used in renovating the building. Owner counterclaimed, alleging Contractor breached the contract and forced Owner to rework part of the job. Owner also claimed that Contractor's delays in performance caused Owner to lose profits from the restaurant.
3. The jury returned an \$18,000 verdict for Contractor on its complaint. The jury awarded Owner \$22,895 on its counterclaim for re-doing and completing the work and \$14,000 in lost profits caused by Contractor's delays. The trial judge denied Contractor's new trial motion and awarded Owner attorney's fees and costs pursuant to S.C. Code Ann. § 29-5-10 (Supp.1987) (mechanics' liens).

A.

4. Contractor first argues that the trial court erred in admitting evidence of Owner's "delay damages" because the contract contained no completion date or statement that "time was of the essence." We disagree.
5. A contractor may be liable for delay damages regardless of whether time was of the essence of the contract. 17A C.J.S. CONTRACTS § 502(4)(a) (1963). Where a contract sets no date for performance, time is not of the essence of the contract and it must be performed within a reasonable time. *General Sprinkler Corp. v. Loris Industrial Developers, Inc.*, 271 F.Supp. 551, 557 (D.S.C.1967); *see Davis v. Cordell*, 115

S.E.2d 649 (S.C. 1960) (applying “reasonable time” rule to time for payment under contract); *Cloniger v. Cloniger*, 193 S.E.2d 647 (S.C. 1973) (applying “reasonable time” rule to agreement to repurchase property within an unspecified time); *Smith v. Spratt Machine Co.*, 24 S.E. 376 (S.C. 1896) (where manufacturing contract specified no time for performance, “reasonable time” implied); *see also* 17A C.J.S. CONTRACTS § 503(a)(1) (1963) (“reasonable time” for performance will be implied where no time therefor is fixed in building or construction contract). The timeliness of Contractor's performance here was a disputed factual issue properly reserved for jury determination.

B.

6. Contractor's next exception presents this Court with an opportunity to address a legal issue unsettled in South Carolina: Does the “new business rule” operate to automatically preclude the recovery of lost profits by a new business or enterprise? We hold that it does not.

1. Lost Profits in South Carolina

7. We begin our analysis of the lost profits issue by recognizing an elementary principle of contract law. The purpose of an award of damages for breach is “to give compensation, that is, to put the plaintiff in as good a position as he would have been in had the contract been performed.” 11 S. WILLISTON, A TREATISE ON THE LAW OF CONTRACTS, § 1338 (3d ed. 1968). The proper measure of that compensation, then, “is the loss actually suffered by the contractee as the result of the breach.” *South Carolina Finance Corp. v. West Side Finance Co.*, 113 S.E.2d 329, 335 (S.C. 1960).
8. “Profits” have been defined as “the net pecuniary gain from a transaction, the gross pecuniary gains diminished by the cost of obtaining them.” *Restatement of Contracts* § 331, Comment B (1932); *see Mali v. Odom*, 367 S.E.2d 166 (S.C. Ct. App. 1988) (defining “profits” as the net of income over expenditures during a given period). Profits lost by a business as the result of a contractual breach have long been recognized as a species of recoverable consequential damages in this state. *Hollingsworth on Wheels, Inc. v. Arkon Corp.*, 305 S.E.2d 71 (S.C. 1983); *South Carolina Finance Corp. v. West Side Finance Co.*, *supra*. The issue is more difficult, however, when a new or unestablished business is the aggrieved party seeking projected lost profits as damages.

9. The new business rule as a per se rule of nonrecoverability of lost profits was firmly established in this state in *Standard Supply Co. v. Carter & Harris*, 62 S.E. 150, 152 (S.C. 1907): “When a business is in contemplation, but not established or not in actual operation, profit merely hoped for is too uncertain and conjectural to be considered.” *McMeekin v. Southern Ry. Co.*, 64 S.E. 413 (S.C. 1909), like *Standard Supply Co.*, involved profits allegedly lost when a carrier failed to deliver machinery necessary for a new mill enterprise. The Court adhered to a strict application of the rule, stating that “[t]he plaintiff’s business had not been launched, and therefore he could not recover profits he expected to make.” 64 S.E. at 415; cited in *Currie v. Davis*, 126 S.E. 119 (S.C. 1923) (new business rule applied to preclude recovery of lost profits where carrier’s tort against passenger delayed production by passenger’s cotton gin “not yet in active operation”).
10. Modern cases, however, reflect the willingness of this Court and our Court of Appeals to view the new business rule as a rule of evidentiary sufficiency rather than an automatic bar to recovery of lost profits by a new business. See *Hollingsworth on Wheels, Inc. v. Arkon Corp.*, *supra* (holding that while aggrieved buyer’s projections of lost profits from new business enterprise introduced unreasonable amount of uncertainty into damages computation, evidence sufficient to permit Court itself to reach reasonable figure for profits lost); *Bryson v. Arcadian Shores, Inc.*, 257 S.E.2d 233 (S.C. 1979) (evidence of room revenues allegedly lost by hotel as result of construction delay held speculative and insufficient to allow recovery); *Mali v. Odom*, *supra* (attorney malpractice action-estimates of anticipated monthly income from new school held speculative and without reasonable basis where offered without reference to operational history or standard method for estimations); *Petty v. Weyerhaeuser Co.*, 288 S.C. 349, 342 S.E.2d 611 (S.C. Ct. App. 1986) (tort action-three month period business operated prior to debilitating effect of tort afforded basis for fairly and reasonably approximating lost profits). These cases have so eroded the new business rule as an absolute bar to recovery of lost profits that the rigid *Standard Supply Co.* rule is no longer good law.

2. A Multi-Jurisdictional Trend

11. South Carolina has not been alone in developing its evidentiary view of the new business rule. Numerous authorities and commentators have tracked a similar trend nationwide: “Courts are now taking the position that the distinction between established businesses and new ones is a distinction that goes to the weight of the

evidence and not a rule that automatically precludes recovery of profits by a new business.” D. DOBBS, HANDBOOK ON THE LAW OF REMEDIES, § 3.3, at 155 (1973). See R. DUNN, RECOVERY OF DAMAGES FOR LOST PROFITS, § 4.2 (3d ed. 1987) (trend of modern cases plainly toward replacing old rule of law with rule of evidence-reasonable certainty); Comment, *Remedies-Lost Profits as Contract Damages for an Unestablished Business: The New Business Rule Becomes Outdated*, 56 N.C.L. REV. 693, 695 (1978) (noting “increasing trend either to create exceptions and mitigating sub-doctrines to the new business rule or simply to recognize that its rationale is no longer persuasive”); Note, *The New Business Rule And The Denial Of Lost Profits*, 48 OHIO ST. L.J. 855, 859 (1987) (clear and growing majority of courts apply new business rule as rule delimiting sufficiency of evidence). Moreover, application of the rule in this manner has been applauded as fairer than mechanical application of the old rule. See D. DOBBS, *supra* (as a matter of evidence, new business/established business distinction makes sense; as a matter of setting an inflexible rule, it does not); R. DUNN, *supra*, at 227 (no worthwhile end achieved “by permitting one party to breach his contracts with impunity—giving him an option, as it were—because the other party has not yet commenced operation.”).

12. In light of the facts before us, we find particularly persuasive several cases involving lost profits flowing from breaches of contracts to construct and/or lease buildings for the operation of new business ventures. See, e.g., *Chung v. Kaonohi Center Co.*, 618 P.2d 283 (Haw. 1980) (rejecting per se nonrecoverability version of new business rule in favor of “reasonable certainty” evidentiary standard; lost profits award upheld for breach of contract to lease space for new restaurant); *Welch v. U.S. Bancorp Realty and Mortgage*, 596 P.2d 947 (Or. 1979) (breach of contract to advance funds for residential and commercial development on land tract; “reasonable certainty” standard applied); *Fera v. Village Plaza, Inc.*, 242 N.W.2d 372 (Mich. 1976) (breach of lease of shopping center space for new book store; per se rule of nonrecoverability rejected in favor of broad jury discretion in lost profits determinations); *Smith Dev. Corp. v. Bilow Enterprises, Inc.*, 308 A.2d 477 (R.I. 1973) (tortious interference with contractual right to erect “McDonald’s” restaurant; “reasonable certainty” rule applied and per se new business rule rejected); *S. Jon Kredman & Co. v. Meyer Bros. Parking-Western Corp.*, 58 Cal.App.3d 173, 130 Cal.Rptr. 41 (1976) (breach of contract to construct parking garage and lease it to operator; “hard and fast” new business rule rejected in favor of “reasonable certainty” test).

13. We believe South Carolina should now unequivocally join those jurisdictions applying the new business rule as a rule of evidentiary sufficiency and not as an automatic preclusion to recovery of lost profits by a new business or enterprise.

3. The Standard for Entitlement to Lost Profits

14. The same standards that have for years governed lost profits awards in South Carolina will apply with equal force to cases where damages are sought for a new business or enterprise. First, profits must have been prevented or lost “as a natural consequence of” the breach of contract. *South Carolina Finance Corp.*, *supra*, at 122, 113 S.E.2d at 335; *Charles v. Texas Co.*, 18 S.E.2d 719, 729 (S.C. 1942) (lost profits are proper elements of damages where they are “direct and necessary result” of defendant's breach).

The second requirement is foreseeability; a breaching party is liable for those damages, including lost profits, “which may reasonably be supposed to have been within the contemplation of the parties at the time the contract was made as a probable result of the breach of it.” *National Tire & Rubber Co. v. Hoover*, 122 S.E. 858, 859 (S.C. 1924); *see also Traywick v. Southern Ry. Co.*, 50 S.E. 549 (S.C. 1905); *Colvin v. McCormick Cotton Oil Co.*, 44 S.E. 380 (S.C. 1902); *Sitton v. MacDonald*, 60 Am.Rep. 484 (S.C. 1885) (lost profits cases citing the “knowledge of special circumstances” rule of *Hadley v. Baxendale*, 9 Ex. 341, 156 Eng. Rep. 154 (1854)).

15. The crucial requirement in lost profits determinations is that they be “established with reasonable certainty, for recovery cannot be had for profits that are conjectural or speculative.” *South Carolina Finance Corp.*, *supra*, 113 S.E.2d at 336. “The proof must pass the realm of conjecture, speculation, or opinion not founded on facts, and must consist of actual facts from which a reasonably accurate conclusion regarding the cause and the amount of the loss can be logically and rationally drawn.” 22 Am. Jur. 2d *Damages* § 641 (1988).
16. Numerous proof techniques have been discussed and accepted in different factual scenarios. *See, e.g., Upjohn v. Rachele Laboratories, Inc.*, 661 F.2d 1105, 1114 (6th Cir.1981) (proof of future lost profits based on marketing forecasts by employees specializing in economic forecasting); *Petty v. Weyerhaeuser Co.*, *supra* (skating rink's projected revenues compared to those of another arena in a nearby town); *see also* RESTATEMENT (SECOND) OF CONTRACTS § 352, at 146 (1981) (proof of lost

profits “may be established with reasonable certainty with the aid of expert testimony, economic and financial data, market surveys and analyses, business records of similar enterprises, and the like.”); Note, *supra*, 48 OHIO ST. L.J. at 872-3 (means of proving prospective profits include (1) “yardstick” method of comparison with profit performance of business similar in size, nature, and location; (2) comparison with profit history of plaintiff’s successor, where applicable; (3) comparison of similar businesses owned by plaintiff himself, and (4) use of economic and financial data and expert testimony). While the factual contexts in which new business/lost profits cases arise will undoubtedly vary, these methods of proof and the “reasonable certainty” requirement bear an inherent flexibility facilitating the just assessment of profits lost to a new business due to contractual breach.

4. Application of the Standard to the Present Facts

17. Applying this standard to the facts before us, we find that Owner's proof failed to clear the “reasonable certainty” hurdle. Owner's projections of the profits lost by the restaurant because of the breach were based on nothing more than a sheet of paper reflecting the gross profits the restaurant made in the first 11 months of operation after construction was completed. These figures were not supplemented with corresponding figures for overhead or operating expenditures, but only with Owner's testimony that he “would expect at least a third of that [gross figure] to be” net profit. Owner's expectations, unsupported by any particular standard or fixed method for establishing net profits, were wholly insufficient to provide the jury with a basis for calculating profits lost with reasonable certainty. *South Carolina Finance Corp., supra; Mali v. Odom, supra.*
18. The trial judge erred in failing to rule that, as a matter of law, Owner's proof was insufficient to merit submission to the jury. The \$14,000 award of lost profits must therefore be reversed.

C.

19. Contractor's remaining exceptions are disposed of pursuant to Supreme Court Rule 23. *See Talley v. South Carolina Higher Education Tuition Grants Committee*, 347 S.E.2d 99 (S.C. 1986) (issue neither presented to nor ruled upon by trial court not preserved for appeal); *Reid v. Hardware Mutual Insurance Co.*, 166 S.E.2d 317 (S.C. 1969) (questions not raised by proper exception will not be considered); Supreme

Court Rule 8, § 3; *Howell v. Pacific Columbia Mills*, 354 S.E.2d 384 (S.C. 1987)
(exceptions not argued in brief deemed abandoned on appeal).

20. Costs and attorneys' fees under Supreme Court Rule 38 shall be assessed against appellant.

AFFIRMED IN PART; REVERSED IN PART.

Rockingham County v. Luten Bridge Co.

Circuit Court of Appeals, Fourth Circuit
35 F.2d 301 (1929)

PARKER, Circuit Judge.

1. This was an action at law instituted in the court below by the Luten Bridge Company, as plaintiff, to recover [from] Rockingham County, North Carolina, an amount alleged to be due under a contract, but defendant contends that notice of cancellation was given the bridge company before the erection of the bridge was commenced, and that it is liable only for the damages which the company would have sustained, if it had abandoned construction at that time. The judge below refused to strike out an answer filed by certain members of the board of commissioners of the county, admitting liability in accordance with the prayer of the complaint, allowed this pleading to be introduced in evidence as the answer of the county, excluded evidence offered by the county in support of its contentions as to notice of cancellation and damages, and instructed a verdict for plaintiff for the full amount of its claim. From judgment on this verdict the county has appealed.
2. The facts out of which the case arises, as shown by the affidavits and offers of proof appearing in the record, are as follows: On January 7, 1924, the board of commissioners of Rockingham County voted to award to plaintiff a contract for the construction of the bridge in controversy. Three of the five commissioners favored the awarding of the contract and two opposed it. Much feeling was engendered over the matter, with the result that on February 11, 1924, W. K. Pruitt, one of the commissioners who had voted in the affirmative, sent his resignation to the clerk of the superior court of the county. The clerk received this resignation on the same day, and immediately accepted same and noted his acceptance thereon. Later in the day, Pruitt called him over the telephone and stated that he wished to withdraw the resignation, and later sent him written notice to the same effect. The clerk, however, paid no attention to the attempted withdrawal, and proceeded on the next day to appoint one W. W. Hampton as a member of the board to succeed him.
3. After his resignation, Pruitt attended no further meetings of the board, and did nothing further as a commissioner of the county. Likewise Pratt and McCollum, the other two members of the board who had voted with him in favor of the contract, attended no further meetings. Hampton, on the other hand, took the oath of office

immediately upon his appointment and entered upon the discharge of the duties of a commissioner. He met regularly with the two remaining members of the board, Martin and Barber, in the courthouse at the county seat, and with them attended to all of the business of the county. Between the 12th of February and the first Monday in December following, these three attended, in all, 25 meetings of the board.

4. At one of these meetings, a regularly advertised called meeting held on February 21st, a resolution was unanimously adopted declaring that the contract for the building of the bridge was not legal and valid, and directing the clerk of the board to notify plaintiff that it refused to recognize same as a valid contract, and that plaintiff should proceed no further thereunder. This resolution also rescinded action of the board theretofore taken looking to the construction of a hard-surfaced road, in which the bridge was to be a mere connecting link. The clerk duly sent a certified copy of this resolution to plaintiff.
5. At the regular monthly meeting of the board on March 3d, a resolution was passed directing that plaintiff be notified that any work done on the bridge would be done by it at its own risk and hazard, that the board was of the opinion that the contract for the construction of the bridge was not valid and legal, and that, even if the board were mistaken as to this, it did not desire to construct the bridge, and would contest payment for same if constructed. A copy of this resolution was also sent to plaintiff. At the regular monthly meeting on April 7th, a resolution was passed, reciting that the board had been informed that one of its members was privately insisting that the bridge be constructed. It repudiated this action on the part of the member and gave notice that it would not be recognized. At the September meeting, a resolution was passed to the effect that the board would pay no bills presented by plaintiff or anyone connected with the bridge. At the time of the passage of the first resolution, very little work toward the construction of the bridge had been done, it being estimated that the total cost of labor done and material on the ground was around \$1,900; but, notwithstanding the repudiation of the contract by the county, the bridge company continued with the work of construction.
6. On November 24, 1924, plaintiff instituted this action against Rockingham County, and against Pruitt, Pratt, McCollum, Martin, and Barber, as constituting its board of commissioners. Complaint was filed, setting forth the execution of the contract and the doing of work by plaintiff thereunder, and alleging that for work done up until November 3, 1924, the county was indebted in the sum of \$18,301.07. On November

27th, three days after the filing of the complaint, and only three days before the expiration of the term of office of the members of the old board of commissioners, Pruitt, Pratt, and McCollum met with an attorney at the county seat, and, without notice to or consultation with the other members of the board, so far as appears, had the attorney prepare for them an answer admitting the allegations of the complaint. This answer, which was filed in the cause on the following day, did not purport to be an answer of the county, or of its board of commissioners, but of the three commissioners named.

7. On December 1, 1924, the newly elected board of commissioners held its first meeting and employed attorneys to defend the action which had been instituted by plaintiff against the county. These attorneys immediately moved to strike out the answer which had been filed by Pruitt, Pratt, and McCollum, and entered into an agreement with opposing counsel that the county should have 30 days from the action of the court on the motion within which to file answer. The court denied the motion on June 2, 1927, and held the answer filed by Pruitt, Pratt, and McCollum to be the answer of the county. An order was then entered allowing the county until August 1st to file answer, pursuant to stipulation, within which time the answer of the county was filed. This answer denied that the contract sued on was legal or binding, and for a further defense set forth the resolutions of the commissioners with regard to the building of the bridge, to which we have referred, and their communication to plaintiff. A reply was filed to this, and the case finally came to trial.
8. At the trial, plaintiff, over the objection of the county, was allowed to introduce in evidence, the answer filed by Pruitt, Pratt, and McCollum, the contract was introduced, and proof was made of the value under the terms of the contract of the work done up to November 3, 1924. The county elicited on cross-examination proof as to the state of the work at the time of the passage of the resolutions to which we have referred. It then offered these resolutions in evidence, together with evidence as to the resignation of Pruitt, the acceptance of his resignation, and the appointment of Hampton; but all of this evidence was excluded, and the jury was instructed to return a verdict for plaintiff for the full amount of its claim. The county preserved exceptions to the rulings which were adverse to it, and contends that there was error on the part of the judge below in denying the motion to strike out the answer filed by Pruitt, Pratt, and McCollum; in allowing same to be introduced in evidence; in excluding the evidence offered of the resignation of Pruitt, the acceptance of his resignation, and the appointment of Hampton, and of the resolutions attempting to

cancel the contract and the notices sent plaintiff pursuant thereto; and in directing a verdict for plaintiff in accordance with its claim.

[From this point in the opinion through paragraph 21, the court embarks on a complex analysis of who had authority to act on behalf of the County. The discussion is included here to give you a sense of the uncertainty surrounding this crucial legal issue. However, the rules for identifying “de facto officers” are not central to our study of avoidability doctrine and you may therefore wish to skim this portion of the court’s opinion.]

9. As the county now admits the execution and validity of the contract, and the breach on its part, the ultimate question in the case is one as to the measure of plaintiff’s recovery, and the exceptions must be considered with this in mind. Upon these exceptions, three principal questions arise for our consideration, viz. (1) Whether the answer filed by Pruitt, Pratt, and McCollum was the answer of the county. If it was, the lower court properly refused to strike it out, and properly admitted it in evidence. (2) Whether, in the light of the evidence offered and excluded, the resolutions to which we have referred, and the notices sent pursuant thereto, are to be deemed action on the part of the county. If they are not, the county has nothing upon which to base its position as to minimizing damages, and the evidence offered was properly excluded. And (3) whether plaintiff, if the notices are to be deemed action by the county, can recover under the contract for work done after they were received, or is limited to the recovery of damages for breach of contract as of that date.
10. With regard to the first question the learned District Judge held that the answer of Pruitt, Pratt, and McCollum was the answer of the county, but we think that this holding was based upon an erroneous view of the law. It appears, without contradiction, not only that their answer purports to have been filed by them individually, and not in behalf of the county or of the board of commissioners, but also that it was not authorized by the board of commissioners, acting as a board at a meeting regularly held. It appears that Pruitt, Pratt, and McCollum merely met at the county seat to consider the filing of an answer to plaintiff’s complaint. This was not a “regular” meeting of the board, held on the first Mondays of December and June. It was not a “special” meeting held on the first Monday in some other month. It was not shown to be a meeting “called” by the chairman upon the written request of a member of the board, and advertised at the courthouse door and in a newspaper as provided by statute. Consol. St. Sec. 1296. And between the filing of the complaint and the filing

of the answer there was not sufficient time for the advertising of a called meeting of the board. Consequently any action taken by Pruitt, Pratt, and McCollum with regard to filing an answer was not taken at a meeting of the board in legal session. Even if it be assumed that Pruitt continued to be a member of the board, and that he, Pratt, and McCollum constituted a majority thereof, nevertheless such majority could bind the county only by action taken at a meeting regularly held. The rule is well settled that the governing board of a county can act only as a body and when in legal session as such. 7 R.C.L. 941; 15 C.J. 460 and cases cited; *O'Neal v. Wake County*, 196 N.C. 184, 145 S.E. 28, 29; *Grand Island & N.W.R. Co. v. Baker*, 6 Wyo. 369, 45 P. 494, 34 L.R.A. 835, 71 Am. St. Rep. 926; *Board of Com'rs of Jasper County v. Allman*, 142 Ind. 573, 42 N.E. 206, 39 L.R.A. 58, 68; *Campbell County v. Howard & Lee*, 133 Va. 19, 112 S.E. 876; *Paola, etc. R. Co. v. Anderson County Com'rs*, 16 Kan. 302, 310. As said in the case last cited: "...Commissioners casually meeting have no power to act for the county. There must be a session of the 'board.' This single entity, the 'board,' alone can by its action bind the county. And it exists only when legally convened."

11. The North Carolina case of *Cleveland Cotton-Mills v. Commissioners*, 108 N.C. 678, 13 S.E. 271, 274, established the rule in North Carolina. That case arose under the old law, which required bridge contracts involving more than \$500 to be made with the concurrence of a majority of the justices of the peace of the county. Such a contract was made, and a majority of the justices of the county, who were not then in session, executed a written instrument approving it. Afterwards, at a regular meeting of the justices with the board of commissioners, a majority of the quorum of the justices present voted to ratify the contract. A divided court held that this ratification at the regular meeting was sufficient, although the majority of the quorum which voted for ratification was less than a majority of all of the justices of the county; but all of the members of the court agreed that the execution of the instrument by a majority of the justices when not in session was without effect. As to this, it was said in the majority opinion:

We attach no importance to the paper signed by an actual majority of the whole number of justices of the peace of the county. The action contemplated by the law was that of the justices of the peace in a lawfully constituted meeting as a body, as in cases where the validity of an agreement made by the governing officials of any other corporation is drawn in question. *Duke v. Markham*, 105 N.C. 131, 10 S.E. 1017 (18 Am. St. Rep. 889).

12. It will be seen that the court applied to this case, where the validity of the action of the governing officials of a public corporation was drawn in question, the rule laid down in *Duke v. Markham*, which is, of course, the well-settled rule in the case of private corporation, viz. that such officials can exercise their powers as members of the governing board only at a meeting regularly held. See, also, *First National Bank v. Warlick*, 125 N.C. 593, 34 S.E. 687; *Everett v. Staton*, 192 N.C. 216, 134 S.E. 492.
13. But in the case of *O'Neal v. Wake County*, *supra*, decided in 1928, the Supreme Court of North Carolina set at rest any doubt which may have existed in that state as to the question here involved. In holding that the county could not be held liable on a contract made at a joint meeting of the county commissioners, the county board of education, and a representative of the insurance department, the court said:

A county makes its contracts through the agency of its board of commissioners; but to make a contract which shall be binding upon the county the board must act as a body convened in legal session, regular, adjourned, or special. A contract made by members composing the board when acting in their individual and not in their corporate capacity while assembled in a lawful meeting is not the contract of the county. As a rule authorized meetings are prerequisite to corporate action based upon deliberate conference and intelligent discussion of proposed measures. 7 R.C.L. 941; 15 C.J. 460; 43 C.J. 497; *P.&F.R. Ry. Co. v. Com'rs of Anderson County*, 16 Kan. 302; *Kirkland v. State*, 86 Fla. 84, 97 So. 502. The principle applies to corporations generally, and by the express terms of our statute, as stated above, every county is a corporate body.
14. We think, therefore, that Pruitt, Pratt, and McCollum, even if they constituted a majority of the board of commissioners, did not bind the county by their action in filing an answer admitting its liability, where no meeting of the board of commissioners was held according to law, and where, so far as appears, the other commissioners were not even notified of what was being attempted. It is unthinkable that the county should be held bound by such action, especially where the commissioners attempting to bind it had taken no part in its government for nearly 10 months, and where the answer filed did not defend it in any particular, but, on the contrary, asserted its liability. If, therefore, the answer be considered as an attempt to answer on behalf of the county, it must be stricken out, because not authorized by its governing board; if considered as to the answer of Pruitt, Pratt, and McCollum individually, it must go out because, having been sued in their official capacity, they

had no right to answer individually. And, of course, not having been authorized by the county, the answer was not admissible as evidence against it on the trial of the cause.

15. Coming to the second inquiry—i.e., whether the resolutions to which we have referred and the notices sent pursuant thereto are to be deemed the action of the county, and hence admissible in evidence on the question of damages— it is to be observed that, along with the evidence of the resolutions and notices, the county offered evidence to the effect that Pruitt's resignation had been accepted before he attempted to withdraw same, and that thereafter Hampton was appointed, took the oath of office, entered upon the discharge of the duties of the office, and with Martin and Barber transacted the business of the board of commissioners until the coming into office of the new board. We think that this evidence, if true, shows (1) that Hampton, upon his appointment and qualification, became a member of the board in place of Pruitt, and that he, Martin, and Barber constituted a quorum for the transaction of its business; and (2) that, even if this were not true, Hampton was a de factor commissioner, and that his presence at meetings of the board with that of the other two commissioners was sufficient to constitute a quorum, so as to give validity to its proceedings.
16. The North Carolina statutes make no provision for resignations by members of the boards of county commissioners. A public officer, however, has at common law the right to resign his office, provided his resignation is accepted by the proper authority. *Hoke v. Henderson*, 15 N.C. 1, 25 Am.Dec. 677; *U.S. v. Wright*, Fed. Cas. No. 16,775; *Rowe v. Tuck*, 149 Ga. 88, 99 S.E. 303, 5 A.L.R. 113; *Van Orsdall v. Hazard*, 3 Hill (N.Y.) 243; *Philadelphia v. Marcer*, 8 Phila. (Pa.) 319; *Gates v. Delaware County*, 12 Iowa, 405; 22 R.C.L. 556, 557; note, 19 A.L.R. 39, and cases there cited. And, in the absence of statute regulating the matter, his resignation should be tendered to the tribunal or officer having power to appoint his successor. 22 R.C.L. 558; *State v. Popejoy*, 165 Ind. 177, 74 N.E. 994, 6 Ann.Cas. 687, and note; *State ex rel. Conley v. Thompson*, 100 W.Va. 253, 130 S.E. 456; *State v. Huff*, 172 Ind. 1, 87 N.E. 141, 139 Am. St. Rep. 355; *State v. Augustine*, 113 Mo. 21, 20 S.W. 651, 35 Am. St. Rep. 696. In the case last cited it is said:

It is well-established law that, in the absence of express statutory enactment, the authority to accept the resignation of a public officer rests with the power to appoint a successor to fill the vacancy. The right to accept a resignation is

said to be incidental to the power of appointment. 1 Dillon on Municipal Corporations (3d Ed.) § 224; Mechem on Public Offices, Sec. 413; *Van Orsdall v. Hazard*, 3 Hill (N.Y.) 243; *State v. Boecker*, 56 Mo. 17.

In North Carolina, the officer having power to appoint the successor of a member of the board of county commissioners is the clerk of the superior court of the county. Consolidated Statutes of North Carolina, Sec. 1294. It is clear, therefore, that, when Pruitt tendered his resignation to the clerk of the superior court, he tendered it to the proper authority.

17. The mere filing of the resignation with the clerk of the superior court did not of itself vacate the office of Pruitt, it was necessary that his resignation be accepted. *Hoke v. Henderson*, *supra*; *Edwards v. U.S.*, 103 U.S. 471. But, after its acceptance, he had no power to withdraw it. *Mimmack v. U.S.*, 97 U.S. 426; *Murray v. State*, 115 Tenn. 303, 89 S.W. 101, 5 Ann.Cas. 687, and note; *State v. Augustine*, *supra*; *Gates v. Delaware County*, *supra*; 22 R.C.L. 559. If, as the offer of proof seems to indicate, the resignation of Pruitt was accepted by the clerk prior to his attempt to withdraw it, the appointment of Hampton was unquestionably valid, and the latter, with Martin and Barber, constituted a quorum of the board of commissioners, with the result that action taken by them in meetings of the board regularly held was action by the county.
18. But, irrespective of the validity of Hampton's appointment, we think that he must be treated as a de facto officer, and that the action taken by him, Martin, and Barber in meetings regularly held is binding upon the county and upon those dealing with it. Hampton was appointed by the lawful appointing power. He took the oath of office and entered upon the discharge of the duties of a commissioner. The only government which the county had for a period of nearly 10 months was that which he and his associates, Martin and Barber, administered. If their action respecting this contract is to be ignored, then, for the same reason, their tax levy for the year must be treated as void, and the many transactions carried through at their 25 meetings, which were not attended by Pruitt, Pratt, or McCollum, must be set aside. This cannot be the law. It ought not be the law anywhere; it certainly is not the law in North Carolina. Section 3204 of the Consolidated Statutes provides:

3204. Persons admitted to office deemed to hold lawfully. Any person who shall, by the proper authority, be admitted and sworn into any office, shall be held, deemed, and taken, by force of such admission, to be rightfully in such

office until, by judicial sentence, upon a proper proceeding, he shall be ousted therefrom, or his admission thereto be, in due course of law, declared void.

19. In the case of *State v. Lewis*, 107 N.C. 967, 12 S.E. 457, 458, 13 S.E. 247, 11 L.R.A. 105, the court quotes with approval the widely accepted definition and classification of de facto officers by Chief Justice Butler in the case of *State v. Carroll*, 38 Conn. 449, 9 Am. Rep. 409, as follows:

An officer de facto is one whose acts, though not those of a lawful officer, the law, upon principles of policy and justice, will hold valid so far as they involve the interests of the public and third persons, where the duties of the office were exercised—First, without a known appointment or election, but under such circumstances of reputation or acquiescence as were calculated to induce people, without inquiry, to submit to or invoke his action, supposing him to be the officer he assumed to be; second, under color of a known and valid appointment or election, but where the officer failed to conform to some precedent requirement or condition, as to take an oath, give a bond, or the like; third, under color of a known election or appointment, void because there was a want of power in the electing or appointing body, or by reason of some defect or irregularity in its exercise, such ineligibility, want of power, or defect being unknown to the public; fourth, under color of an election or appointment by or pursuant to a public unconstitutional law before the same is adjudged to be such.

20. It is clear that, if the appointment of Hampton be considered invalid, the case falls under the third class in the above classification; for Hampton was discharging the duties of a county commissioner under color of a known appointment, the invalidity of which, if invalid, arose from a want of power or irregularity unknown to the public. Other North Carolina cases supporting this conclusion are *Burke v. Elliott*, 26 N.C. 355, 42 Am.Dec. 142; *Burton v. Patton*, 47 N.C. 124, 62 Am.Dec. 194; *Norfleet v. Staton*, 73 N.C. 546, 21 Am.Rep. 479; *Markham v. Simpson*, 175 N.C. 135, 95 S.E. 106; *State v. Harden*, 177 N.C. 580, 98 S.E. 782; 22 R.C.L. 596, 597. This is not a case like *Baker v. Hobgood*, 126 N.C. 149, 35 S.E. 253, where there were rival boards, both attempting to discharge the duties of office; for, upon the appointment of Hampton, Pruitt attended no further meetings and left him in the unchallenged possession of the office.

21. The rule is well settled in North Carolina, as it is elsewhere, that the acts of a de facto officer will be held valid in respect to the public whom he represents and to third persons with whom he deals officially, notwithstanding there was a want of power to appoint him in the person or body which professed to do so. *Norfleet v. Staton, supra*; *Markham v. Simpson, supra*; 22 R.C.L. 601, 602, and cases cited.

[From this point to the end of the opinion, the court returns to the issues that are central to our discussion of mitigation and the avoidability doctrine.]

22. Coming, then, to the third question—i.e., as to the measure of plaintiff's recovery—we do not think that, after the county had given notice, while the contract was still executory, that it did not desire the bridge built and would not pay for it, plaintiff could proceed to build it and recover the contract price. It is true that the county had no right to rescind the contract, and the notice given plaintiff amounted to a breach on its part; but, after plaintiff had received notice of the breach, it was its duty to do nothing to increase the damages flowing therefrom. If A enters into a binding contract to build a house for B, B, of course, has no right to rescind the contract without A's consent. But if, before the house is built, he decides that he does not want it, and notifies A to that effect, A has no right to proceed with the building and thus pile up damages. His remedy is to treat the contract as broken when he receives the notice, and sue for the recovery of such damages, as he may have sustained from the breach, including any profit which he would have realized upon performance, as well as any other losses which may have resulted to him. In the case at bar, the county decided not to build the road of which the bridge was to be a part, and did not build it. The bridge, built in the midst of the forest, is of no value to the county because of this change of circumstances. When, therefore, the county gave notice to the plaintiff that it would not proceed with the project, plaintiff should have desisted from further work. It had no right thus to pile up damages by proceeding with the erection of a useless bridge.
23. The contrary view was expressed by Lord Cockburn in *Frost v. Knight*, L.R. 7 Ex. 111, but, as pointed out by Prof. Williston (*WILLISTON ON CONTRACTS*, vol. 3, p. 2347), it is not in harmony with the decisions in this country. The American rule and the reasons supporting it are well stated by Prof. Williston as follows:

There is a line of cases running back to 1845 which holds that, 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. This rule is only a particular application of the general rule of damages that 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. The application of this rule to the matter in question is obvious. If a man engages to have work done, and afterwards repudiates his contract before the work has been begun or when it has been only partially done, it is inflicting damage on the defendant without benefit to the plaintiff to allow the latter to insist on proceeding with the contract. The work may be useless to the defendant, and yet he would be forced to pay the full contract price. On the other hand, the plaintiff is interested only in the profit he will make out of the contract. If he receives this it is equally advantageous for him to use his time otherwise.

24. The leading case on the subject in this country is the New York case of *Clark v. Marsiglia*, 1 Denio (N.Y.) 317, 43 Am.Dec. 670. In that case defendant had employed plaintiff to paint certain pictures for him, but countermanded the order before the work was finished. Plaintiff, however, went on and completed the work and sued for the contract price. In reversing a judgment for plaintiff, the court said:

The plaintiff was allowed to recover as though there had been no countermand of the order; and in this the court erred. The defendant, by requiring the plaintiff to stop work upon the paintings, violated his contract, and thereby incurred a liability to pay such damages as the plaintiff should sustain. Such damages would include a recompense for the labor done and materials used, and such further sum in damages as might, upon legal principles, be assessed for the breach of the contract; but the plaintiff had no right, by obstinately persisting in the work, to make the penalty upon the defendant greater than it would otherwise have been.

And the rule as established by the great weight of authority in America is summed up in the following statement in 6 R.C.L. 1029, which is quoted with approval by the Supreme Court of North Carolina in the recent case of *Novelty Advertising Co. v. Farmers' Mut. Tobacco Warehouse Co.*, 186 N.C. 197, 119 S.E. 196, 198:

While a contract is executory a party has the power to stop performance on the other side by an explicit direction to that effect, subjecting himself to such damages as will compensate the other party for being stopped in the performance on his part at that stage in the execution of the contract. The

party thus forbidden cannot afterwards go on and thereby increase the damages, and then recover such damages from the other party. The legal right of either party to violate, abandon, or renounce his contract, on the usual terms of compensation to the other for the damages which the law recognizes and allows, subject to the jurisdiction of equity to decree specific performance in proper cases, is universally recognized and acted upon.

This is in accord with the earlier North Carolina decision of *Heiser v. Mears*, 120 N.C. 443, 27 S.E. 117, in which it was held that, where a buyer countermands his order for goods to be manufactured for him under an executory contract, before the work is completed, it is notice to the seller that he elects to rescind his contract and submit to the legal measure of damages, and that in such case the seller cannot complete the goods and recover the contract price. See, also, *Kingman & Co. v. Western Mfg. Co.* (C.C.A. 8th) 92 F. 486; *Davis v. Bronson*, 2 N.D. 300, 50 N.W. 836, 16 L.R.A. 655 and note, 33 Am.St.Rep. 783, and note; *Richards v. Manitowoc & Northern Traction Co.*, 140 Wis. 85, 121 N.W. 837, 133 Am.St.Rep. 1063.

25. We have carefully considered the cases of *Roehm v. Horst*, 178 U.S. 1, *Roller v. George H. Leonard & Co.* (C.C.A. 4th) 229 F. 607, and *McCoy v. Justices of Harnett County*, 53 N.C. 272, upon which plaintiff relies; but we do not think that they are at all in point. *Roehm v. Horst* merely follows the rule of *Hockster v. DeLaTour*, 2 El.& Bl. 678, to the effect that where one party to any executory contract refuses to perform in advance of the time fixed for performance, the other party, without waiting for the time of performance, may sue at once for damages occasioned by the breach. The same rule is followed in *Roller v. Leonard*. In *McCoy v. Justices of Harnett County* the decision was that mandamus to require the justices of a county to pay for a jail would be denied, where it appeared that the contractor in building same departed from the plans and specifications. In the opinions in all of these some language was used which lends support to plaintiff's position, but in none of them was the point involved which is involved here, *viz.* whether, in application of the rule which requires that the party to a contract who is not in default do nothing to aggravate the damages arising from breach, he should not desist from performance of an executory contract for the erection of a structure when notified of the other party's repudiation, instead of piling up damages by proceeding with the work. As stated above, we think that reason and authority require that this question be answered in the affirmative. It follows that there was error in directing a verdict for plaintiff for the full amount of its claim. The measure of plaintiff's damage, upon its appearing that

notice was duly given not to build the bridge, is an amount sufficient to compensate plaintiff for labor and materials expended and expense incurred in the part performance of the contract, prior to its repudiation, plus the profit which would have been realized if it had been carried out in accordance with its terms. *See Novelty Advertising Co. v. Farmers' Mut. Tobacco Warehouse Co., supra.*

26. Our conclusion, on the whole case, is that there was error in failing to strike out the answer of Pruitt, Pratt, and McCollum, and in admitting same as evidence against the county, in excluding the testimony offered by the county to which we have referred, and in directing a verdict for plaintiff. The judgment below will accordingly be reversed, and the case remanded for a new trial.

Reversed.

Parker v. Twentieth Century-Fox Film Corp.

Supreme Court of California

3 Cal. 3d 176, 474 P.2d 689, 89 Cal. Rptr. 737 (1970)

BURKE, J.

1. Defendant Twentieth Century-Fox Film Corporation appeals from a summary judgment granting to plaintiff the recovery of agreed compensation under a written contract for her services as an actress in a motion picture. As will appear, we have concluded that the trial court correctly ruled in plaintiff's favor and that the judgment should be affirmed.
2. Plaintiff [Shirley MacLaine] is well known as an actress, and in the contract between plaintiff and defendant is sometimes referred to as the "Artist." Under the contract, dated August 6, 1965, plaintiff was to play the female lead in defendant's contemplated production of a motion picture entitled "Bloomer Girl." The contract provided that defendant would pay plaintiff a minimum "guaranteed compensation" of \$53,571.42 per week for 14 weeks commencing May 23, 1966, for a total of \$750,000. Prior to May 1966 defendant decided not to produce the picture and by a letter dated April 4, 1966, it notified plaintiff of that decision and that it would not "comply with our obligations to you under" the written contract.
3. By the same letter and with the professed purpose "to avoid any damage to you," defendant instead offered to employ plaintiff as the leading actress in another film tentatively entitled "Big Country, Big Man" (hereinafter, "Big Country"). The compensation offered was identical, as were 31 of the 34 numbered provisions or articles of the original contract.¹ Unlike "Bloomer Girl," however, which was to have been a musical production, "Big Country" was a dramatic "western type" movie. "Bloomer Girl" was to have been filmed in California; "Big Country" was to be produced in Australia. Also, certain terms in the proffered contract varied from those of the original.² Plaintiff was given one week within which to accept; she did not and

¹ Among the identical provisions was the following found in the last paragraph of Article 2 of the original contract: "We [defendant] shall not be obligated to utilize your [plaintiff's] services in or in connection with the Photoplay hereunder, our sole obligation, subject to the terms and conditions of this Agreement, being to pay you the guaranteed compensation herein provided for."

² Article 29 of the original contract specified that plaintiff approved the director already chosen for "Bloomer Girl" and that in case he failed to act as director plaintiff was to have approval rights of any

the offer lapsed. Plaintiff then commenced this action seeking recovery of the agreed guaranteed compensation.

4. Defendant's letter of April 4 to plaintiff, which contained both defendant's notice of breach of the "Bloomer Girl" contract and offer of the lead in "Big Country," eliminated or impaired each of those rights. It read in part as follows: "The terms and conditions of our offer of employment are identical to those set forth in the 'BLOOMER GIRL' Agreement, Articles 1 through 34 and Exhibit A to the Agreement, except as follows:

1. Article 31 of said Agreement will not be included in any contract of employment regarding 'BIG COUNTRY, BIG MAN' as it is not a musical and it thus will not need a dance director.

2. In the 'BLOOMER GIRL' agreement, in Articles 29 and 32, you were given certain director and screenplay approvals and you had preapproved certain matters. Since there simply is insufficient time to negotiate with you regarding your choice of director and regarding the screenplay and since you already expressed an interest in performing the role in 'BIG COUNTRY, BIG MAN,' we must exclude from our offer of employment in 'BIG COUNTRY, BIG MAN' any approval rights as are contained in said Articles 29 and 32; however, we shall consult with you respecting the director to be selected to direct the photoplay and will further consult with you with respect to the screenplay and any revisions or changes therein, provided, however, that if we fail to agree ... the decision of ... [defendant] with respect to the selection of a director and to revisions and changes in the said screenplay shall be binding upon the parties to said agreement.

5. The complaint sets forth two causes of action. The first is for money due under the contract; the second, based upon the same allegations as the first, is for damages resulting from defendant's breach of contract. Defendant in its answer admits the existence and validity of the contract, that plaintiff complied with all the conditions, covenants and promises and stood ready to complete the performance, and that defendant breached and "anticipatorily repudiated" the contract. It denies, however, that any money is due to plaintiff either under the contract or as a result of its breach, and pleads as an affirmative defense to both causes of action plaintiff's allegedly

substitute director. Article 31 provided that plaintiff was to have the right of approval of the "Bloomer Girl" dance director, and Article 32 gave her the right of approval of the screenplay.

deliberate failure to mitigate damages, asserting that she unreasonably refused to accept its offer of the leading role in “Big Country.”

6. Plaintiff moved for summary judgment under Code of Civil Procedure section 437c, the motion was granted, and summary judgment for \$750,000 plus interest was entered in plaintiff's favor. This appeal by defendant followed.
7. The familiar rules are that the matter to be determined by the trial court on a motion for summary judgment is whether facts have been presented which give rise to a triable factual issue. The court may not pass upon the issue itself. Summary judgment is proper only if the affidavits or declarations³ in support of the moving party would be sufficient to sustain a judgment in his favor and his opponent does not by affidavit show facts sufficient to present a triable issue of fact. The affidavits of the moving party are strictly construed, and doubts as to the propriety of summary judgment should be resolved against granting the motion. Such summary procedure is drastic and should be used with caution so that it does not become a substitute for the open trial method of determining facts. The moving party cannot depend upon allegations in his own pleadings to cure deficient affidavits, nor can his adversary rely upon his own pleadings in lieu or in support of affidavits in opposition to a motion; however, a party can rely on his adversary's pleadings to establish facts not contained in his own affidavits. (*Slobojan v. Western Travelers Life Ins. Co.* (1969) 70 Cal.2d 432, 436-437 [74 Cal.Rptr. 895, 450 P.2d 271]; and cases cited.) Also, the court may consider facts stipulated to by the parties and facts which are properly the subject of judicial notice. (*Ahmanson Bank & Trust Co. v. Tepper* (1969) 269 Cal.App.2d 333, 342 [74 Cal.Rptr. 774]; *Martin v. General Finance Co.* (1966) 239 Cal. App.2d 438, 442 [48 Cal.Rptr. 773]; *Goldstein v. Hoffman* (1963) 213 Cal.App.2d 803, 814 [29 Cal.Rptr. 334]; *Thomson v. Honer* (1960) 179 Cal.App.2d 197, 203 [3 Cal.Rptr. 791].)
8. As stated, defendant's sole defense to this action which resulted from its deliberate breach of contract is that in rejecting defendant's substitute offer of employment plaintiff unreasonably refused to mitigate damages.
9. 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

³ In this opinion “affidavits” includes “declarations under penalty of perjury.” (See Code Civ. Proc., § 2015.5.)

might have earned from other employment. (*W. F. Boardman Co. v. Petch* (1921) 186 Cal. 476, 484 [199 P. 1047]; *De Angeles v. Roos Bros., Inc.* (1966) 244 Cal.App.2d 434, 441-442 [52 Cal.Rptr. 783]; *de la Falaise v. Gaumont-British Picture Corp.* (1940) 39 Cal.App.2d 461, 469 [103 P.2d 447], and cases cited; see also *Wise v. Southern Pac. Co.* (1970) 1 Cal.3d 600, 607-608 [83 Cal. Rptr. 202, 463 P.2d 426].)⁴ However, before projected earnings from other employment opportunities 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. (*Gonzales v. Internat. Assn. of Machinists* (1963) 213 Cal.App.2d 817, 822-824 [29 Cal.Rptr. 190]; *Harris v. Nat. Union etc. Cooks, Stewards* (1953) 116 Cal.App.2d 759, 761 [254 P.2d 673]; *Crillo v. Curtola* (1949) 91 Cal.App.2d 263, 275 [204 P.2d 941]; *de la Falaise v. Galumont-British Picture Corp., supra.*, 39 Cal.App.2d 461, 469; *Schiller v. Keuffel & Esser Co.* (1963) 21 Wis.2d 545 [124 N.W.2d 646, 651]; 28 A.L.R. 736, 749; 22 Am.Jur.2d, Damages, §§ 71- 72, p. 106.)

10. In the present case defendant has raised no issue of *reasonableness of efforts* by plaintiff to obtain other employment; the sole issue is whether plaintiff's refusal of defendant's substitute offer of "Big Country" may be used in mitigation. Nor, if the "Big Country" offer was of employment different or inferior when compared with the original "Bloomer Girl" employment, is there an issue as to whether or not plaintiff acted reasonably in refusing the substitute offer. Despite defendant's arguments to the contrary, no case cited or which our research has discovered holds or suggests that reasonableness is an element of a wrongfully discharged employee's option to reject, or fail to seek, different or inferior employment lest the possible earnings therefrom be charged against him in mitigation of damages.⁵

⁴ Although it would appear that plaintiff was not *discharged* by defendant in the customary sense of the term, as she was not permitted by defendant to enter upon performance of the "Bloomer Girl" contract, nevertheless the motion for summary judgment was submitted for decision upon a stipulation by the parties that "plaintiff Parker was discharged."

⁵ Instead, in each case the reasonableness referred to was that of the *efforts* of the employee to obtain other employment that was not different or inferior; his right to reject the latter was declared as an unqualified rule of law. Thus, *Gonzales v. Internat. Assn. of Machinists, supra.*, 213 Cal.App.2d 817, 823-824, holds that the trial court correctly instructed the jury that plaintiff union member, a machinist, was required to make "such *efforts* as the average [member of his union] desiring employment would

11. In *Harris v. Nat. Union etc. Cooks, Stewards, supra.*, 116 Cal. App. 2d 759, 761, the issues were stated to be, inter alia, whether comparable employment was open to each plaintiff employee, and if so whether each plaintiff made a reasonable effort to secure such employment. It was held that the trial court properly sustained an objection to an offer to prove a custom of accepting a job in a lower rank when work in the higher rank was not available, as “The duty of mitigation of damages ... does not require the plaintiff 'to seek or to accept other employment of a different or inferior kind.’” (P. 764 [5].) See also: *Lewis v. Protective Security Life Ins. Co.* (1962) 208 Cal.App.2d 582, 584 [25 Cal.Rptr. 213]: “*honest effort* to find similar employment ...” (Italics added.) *de la Falaise v. Gaumont-British Picture Corp., supra.*, 39 Cal.App.2d 461, 469: “reasonable effort.” *Erler v. Five Points Motors, Inc.* (1967) 249 Cal.App.2d 560, 562 [57 Cal.Rptr. 516]: Damages may be mitigated “by a showing that the employee, by the exercise of *reasonable diligence and effort*, could have procured comparable employment ...” (Italics added.) *Savitz v. Gallaccio* (1955) 179 Pa.Super. 589 [118 A.2d 282, 286]; *Atholwood Dev. Co. v. Houston* (1941) 179 Md. 441 [19 A.2d 706, 708]; *Harcourt & Co. v. Heller* (1933) 250 Ky. 321 [62 S.W.2d 1056]; *Alaska Airlines, Inc. v. Stephenson* (1954) 217 F.2d 295, 299 [15 Alaska 272]; *United Protective Workers v. Ford Motor Co.* (7th Cir. 1955) 223 F.2d 49, 52 [48 A.L.R.2d 1285]; *Chisholm v. Preferred Bankers' Life Assur. Co.* (1897) 112 Mich. 50 [70 N.W. 415]; each of which held that the *reasonableness of the employee's efforts*, or his excuses for failure, to find other similar employment was properly submitted to the jury as a question of fact. NB: *Chisholm* additionally *approved* a jury instruction that a *substitute offer* of the employer to work for a lesser compensation was *not to be considered in mitigation*, as the employee was not required to accept it. *Williams v. National Organization, Masters, etc.* (1956) 384 Pa. 413 [120 A.2d 896, 901 [13]]: “Even assuming that plaintiff ... could have obtained employment in ports other than ... where he resided, *legally* he was not compelled to do so in order to mitigate his damages.” (Italics added.)
12. Applying the foregoing rules to the record in the present case, with all intendments in favor of the party opposing the summary judgment motion—here, defendant—it is clear that the trial court correctly ruled that plaintiff's failure to accept defendant's

make at that particular time and place” (italics added); but, further, that the court *properly rejected* defendant's *offer of proof of the availability of other kinds of employment* at the same or higher pay than plaintiff usually received and all outside the jurisdiction of his union, as plaintiff could not be required to accept different employment or a nonunion job.

tendered substitute employment could not be applied in mitigation of damages because the offer of the “Big Country” lead was of employment both different and inferior, and that no factual dispute was presented on that issue. The mere circumstance that “Bloomer Girl” was to be a musical review calling upon plaintiff’s talents as a dancer as well as an actress, and was to be produced in the City of Los Angeles, whereas “Big Country” was a straight dramatic role in a “Western Type” story taking place in an opal mine in Australia, demonstrates the difference in kind between the two employments; the female lead as a dramatic actress in a western style motion picture can by no stretch of imagination be considered the equivalent of or substantially similar to the lead in a song-and-dance production.

13. Additionally, the substitute “Big Country” offer proposed to eliminate or impair the director and screenplay approvals accorded to plaintiff under the original “Bloomer Girl” contract (see fn. 2, *ante*), and thus constituted an offer of inferior employment. No expertise or judicial notice is required in order to hold that the deprivation or infringement of an employee’s rights held under an original employment contract converts the available “other employment” relied upon by the employer to mitigate damages, into inferior employment which the employee need not seek or accept. (See *Gonzales v. Internal. Assn. of Machinists*, *supra.*, 213 Cal.App.2d 817, 823-824; and fn. 5, *post.*)
14. Statements found in affidavits submitted by defendant in opposition to plaintiff’s summary judgment motion, to the effect that the “Big County” offer was not of employment different from or inferior to that under the “Bloomer Girl” contract, merely repeat the allegations of defendant’s answer to the complaint in this action, constitute only conclusory assertions with respect to undisputed facts, and do not give rise to a triable factual issue so as to defeat the motion for summary judgment. (See *Colvig v. KSFO* (1964) 224 Cal.App.2d 357, 364 [36 Cal.Rptr. 701]; *Dashew v. Dashew Business Machines, Inc.* (1963) 218 Cal.App.2d 711, 715 [32 Cal.Rptr. 682]; *Hatch v. Bush* (1963) 215 Cal.App.2d 692, 707 [30 Cal. Rptr. 397, 13 A.L.R.3d 503]; *Barry v. Rodgers* (1956) 141 Cal.App.2d 340, 342 [296 P.2d 898].)
15. In view of the determination that defendant failed to present any facts showing the existence of a factual issue with respect to its sole defense—plaintiff’s rejection of its substitute employment offer in mitigation of damages—we need not consider plaintiff’s further contention that for various reasons, including the provisions of the

original contract set forth in footnote 1, *ante*, plaintiff was excused from attempting to mitigate damages.

16. The judgment is affirmed.

McComb, J., Peters, J., Tobriner, J., Kaus, J. (Assigned by the Acting Chairman of the Judicial Council) and Roth, J., (Assigned by the Acting Chairman of the Judicial Council) concurred.

SULLIVAN, Acting C. J., *dissenting*

17. The basic question in this case is whether or not plaintiff acted reasonably in rejecting defendant's offer of alternate employment. The answer depends upon whether that offer (starring in “Big Country, Big Man”) was an offer of work that was substantially similar to her former employment (starring in “Bloomer Girl”) or of work that was of a different or inferior kind. To my mind this is a factual issue, which the trial court should not have determined on a motion for summary judgment. The majority have not only repeated this error but have compounded it by applying the rules governing mitigation of damages in the employer-employee context in a misleading fashion. Accordingly, I respectfully dissent.
18. The familiar rule requiring a plaintiff in a tort or contract action to mitigate damages embodies notions of fairness and socially responsible behavior which are fundamental to our jurisprudence. Most broadly stated, it precludes the recovery of damages which, through the exercise of due diligence, could have been avoided. Thus, in essence, it is a rule requiring reasonable conduct in commercial affairs. This general principle governs the obligations of an employee after his employer has wrongfully repudiated or terminated the employment contract. Rather than permitting the employee simply to remain idle during the balance of the contract period, the law requires him to make a reasonable effort to secure other employment.¹ He is not

¹ The issue is generally discussed in terms of a duty on the part of the employee to minimize loss. The practice is long-established and there is little reason to change despite Judge Cardozo's observation of its subtle inaccuracy. “The servant is free to accept employment or reject it according to his uncensored pleasure. What is meant by the supposed duty is merely this, that if he unreasonably reject, he will not be heard to say that the loss of wages from then on shall be deemed the jural consequence of the earlier discharge. He has broken the chain of causation, and loss resulting to him thereafter is suffered through his own act.” (*McClelland v. Climax Hosiery Mills* (1930) 252 N.Y. 347, 359 [169 N.E. 605, 609], concurring opinion.)

obliged, however, to seek or accept any and all types of work which may be available. Only work which is in the same field and which is of the same quality need be accepted.²

19. Over the years the courts have employed various phrases to define the type of employment which the employee, upon his wrongful discharge, is under an obligation to accept. Thus in California alone it has been held that he must accept employment which is “substantially similar” (*Lewis v. Protective Security Life Ins. Co.* (1962) 208 Cal.App.2d 582, 584 [25 Cal.Rptr. 213]; *de la Falaise v. Gaumont-British Picture Corp.* (1940) 39 Cal.App.2d 461, 469 [103 P.2d 447]); “comparable employment” (*Erler v. Five Points Motors, Inc.* (1967) 249 Cal.App.2d 560, 562 [57 Cal.Rptr. 516]; *Harris v. Nat. Union etc. Cooks, Stewards* (1953) 116 Cal.App.2d 759, 761 [254 P.2d 673]); employment “in the same general line of the first employment” (*Rotter v. Stationers Corp.* (1960) 186 Cal.App.2d 170, 172 [8 Cal. Rptr. 690]); “equivalent to his prior position” (*De Angeles v. Roos Bros., Inc.* (1966) 244 Cal.App.2d 434, 443 [52 Cal.Rptr. 783]); “employment in a similar capacity” (*Silva v. McCoy* (1968) 259 Cal.App.2d 256, 260 [66 Cal.Rptr. 364]); employment which is “not ... of a different or inferior kind....” (*Gonzales v. Internat. Assn. of Machinists* (1963) 213 Cal.App.2d 817, 822 [29 Cal.Rptr. 190].)³
20. For reasons which are unexplained, the majority cite several of these cases yet select from among the various judicial formulations which they contain one particular phrase, “Not of a different or inferior kind,” with which to analyze this case. I have discovered no historical or theoretical reason to adopt this phrase, which is simply a negative restatement of the affirmative standards set out in the above cases, as the exclusive standard. Indeed, its emergence is an example of the dubious phenomenon of the law responding not to rational judicial choice or changing social conditions, but to unrecognized changes in the language of opinions or legal treatises.⁴ However, the

² This qualification of the rule seems to reflect the simple and humane attitude that it is too severe to demand of a person that he attempt to find and perform work for which he has no training or experience. Many of the older cases hold that one need not accept work in an inferior rank or position nor work which is more menial or arduous. This suggests that the rule may have had its origin in the bourgeois fear of resubmergence in lower economic classes.

³ See also 28 A.L.R. 736, 740-742; 15 Am.Jur. 431.

⁴ The earliest California case which the majority cite is *de la Falaise v. Gaumont-British Picture Corp.*, *supra.*, 39 Cal.App.2d at p. 469. *de la Falaise* states “The ‘other employment’ which the discharged employee is bound to seek is employment of a character substantially similar to that of which he has been deprived; he need not enter upon service of a different or inferior kind, ...” *de la Falaise* cites, in turn, two sources as authority for this proposition. The first is 18 R.C.L. (Ruling Case law) 529. That

phrase is a serviceable one and my concern is not with its use as the standard but rather with what I consider its distortion.

21. The relevant language excuses acceptance only of employment which is of a *different kind*. (*Gonzales v. Internat. Assn. of Machinists, supra.*, 213 Cal.App.2d 817, 822; *Harris v. Nat. Union etc. Cooks, Stewards, supra.*, 116 Cal.App.2d 759, 761; *de la Falaise v. Gaumont-British Picture Corp., supra.*, 39 Cal.App.2d 461, 469.) It has never been the law that the mere existence of *differences between two jobs in the same field* is sufficient, as a matter of law, to excuse an employee wrongfully discharged from one from accepting the other in order to mitigate damages. Such an approach would effectively eliminate any obligation of an employee to attempt to minimize damage arising from a wrongful discharge. The only alternative job offer an employee would be required to accept would be an offer of his former job by his former employer.
22. Although the majority appear to hold that there was a difference “in kind” between the employment offered plaintiff in “Bloomer Girl” and that offered in “Big Country” (*ante*, at p. 183), an examination of the opinion makes crystal clear that the majority merely point out differences between the two *films* (an obvious circumstance) and then apodically assert that these constitute a difference in the *kind of employment*. The entire rationale of the majority boils down to this; that the “*mere circumstances*” that “Bloomer Girl” was to be a musical review while “Big Country” was a straight drama “demonstrates the difference in kind” since a female lead in a western is not “the equivalent of or substantially similar to” a lead in a musical. This is merely attempting to prove the proposition by repeating it. It shows that the vehicles for the

digest, however, states only that the “discharged employee ... need not enter upon service of a *more menial kind*.” (Italics added.) It was in this form that the rule entered California law explicitly, *Gregg v. McDonald* (1925) 73 Cal. App. 748, 757 [239 P. 373], quoting the text verbatim. The second citation is to 28 A.L.R. 737. The author of the annotation states: “The principal question with which this annotation is concerned is the kind of employment which the employee is under a duty to seek or accept in order to reduce the damages caused by his wrongful discharge. Must one who is skilled in some special work he is employed to do, as an actor, musician, accountant, etc., seek or accept employment of an *entirely different nature*?” (Italics added.) (28 A.L.R. 736.) In answering that question in the negative, the annotation employs the language adopted by the majority: The employee is “not obliged to seek or accept other employment of a different or inferior kind,” (*Id.* at p. 737.) Rather than a restatement of a generally agreed upon rule, however, the phrase is an epitomization of the varied formulations found in the cases cited. (See 28 A.L.R. 740-742.)

display of the star's talents are different but it does not prove that her employment as a star in such vehicles is of necessity different *in kind* and either inferior or superior.

23. I believe that the approach taken by the majority (a superficial listing of differences with no attempt to assess their significance) may subvert a valuable legal doctrine.⁵ The inquiry in cases such as this should not be whether differences between the two jobs exist (there will always be differences) but whether the differences which are present are substantial enough to constitute differences in the *kind* of employment or, alternatively, whether they render the substitute work employment of an *inferior kind*.
24. It seems to me that *this* inquiry involves, in the instant case at least, factual determinations which are improper on a motion for summary judgment. Resolving whether or not one job is substantially similar to another or whether, on the other hand, it is of a different or inferior kind, will often (as here) require a critical appraisal of the similarities and differences between them in light of the importance of these differences to the employee. This necessitates a weighing of the evidence, and it is precisely this undertaking which is forbidden on summary judgment. (*Garlock v. Cole* (1962) 199 Cal. App. 2d 11, 14 [18 Cal.Rptr. 393].)
25. This is not to say that summary judgment would never be available in an action by an employee in which the employer raises the defense of failure to mitigate damages. No case has come to my attention, however, in which summary judgment has been granted on the issue of whether an employee was obliged to accept available alternate employment. Nevertheless, there may well be cases in which the substitute employment is so manifestly of a dissimilar or inferior sort, the declarations of the plaintiff so complete and those of the defendant so conclusionary and inadequate that no factual issues exist for which a trial is required. This, however, is not such a case.
26. It is not intuitively obvious, to me at least, that the leading female role in a dramatic motion picture is a radically different endeavor from the leading female role in a musical comedy film. Nor is it plain to me that the rather qualified rights of director and screenplay approval contained in the first contract are highly significant matters

⁵ The values of the doctrine of mitigation of damages in this context are that it minimizes the unnecessary personal and social (e.g., nonproductive use of labor, litigation) costs of contractual failure. If a wrongfully discharged employee can, through his own action and without suffering financial or psychological loss in the process, reduce the damages accruing from the breach of contract, the most sensible policy is to require him to do so. I fear the majority opinion will encourage precisely opposite conduct.

either in the entertainment industry in general or to this plaintiff in particular. Certainly, none of the declarations introduced by plaintiff in support of her motion shed any light on these issues.⁶ Nor do they attempt to explain why she declined the offer of starring in “Big Country, Big Man.” Nevertheless, the trial court granted the motion, declaring that these approval rights were “critical” and that their elimination altered “the essential nature of the employment.”

27. The declaration of Herman Citron, plaintiff's theatrical agent, alleges that prior to the formation of the “Bloomer Girl” contract he discussed with Richard Zanuck, defendant's vice president, the conditions under which plaintiff might be interested in doing “Big Country”; that it was Zanuck who informed him of Fox's decision to cancel production of “Bloomer Girl” and queried him as to plaintiff's continued interest in “Big Country”; that he informed Zanuck that plaintiff was shocked by the decision, had turned down other offers because of her commitment to defendant for “Bloomer Girl” and was not interested in “Big Country.” It further alleges that “Bloomer Girl” was to have been a musical review which would have given plaintiff an opportunity to exhibit her talent as a dancer as well as an actress and that “Big Country” was a straight dramatic role; the former to have been produced in California, the latter in Australia. Citron's declaration concludes by stating that he has not received any payment from defendant for plaintiff under the “Bloomer Girl” contract.
28. Benjamin Neuman's declaration states that he is plaintiff's attorney; that after receiving notice of defendant's breach he requested Citron to make every effort to obtain other suitable employment for plaintiff; that he (Neuman) rejected defendant's offer to settle for \$400,000 and that he has not received any payment from defendant for plaintiff under the “Bloomer Girl” contract. It also sets forth correspondence between Neuman and Fox which culminated in Fox's final rejection of plaintiff's demand for full payment.
29. The plaintiff's declarations were of no assistance to the trial court in its effort to justify reaching this conclusion on summary judgment. Instead, it was forced to rely on judicial notice of the definitions of “motion picture,” “screenplay” and “director” (Evid. Code, § 451, subd. (e)) and then on judicial notice of practices in the film

⁶ Plaintiff's declaration states simply that she has not received any payment from defendant under the “Bloomer Girl” contract and that the only persons authorized to collect money for her are her attorney and her agent.

industry which were purportedly of “common knowledge.” (Evid. Code, § 451, subd. (f) or § 452, subd. (g).) This use of judicial notice was error. Evidence Code section 451, subdivision (e) was never intended to authorize resort to the dictionary to solve essentially factual questions which do not turn upon conventional linguistic usage. More important, however, the trial court's notice of “facts commonly known” violated Evidence Code section 455, subdivision (a).⁷ Before this section was enacted there were no procedural safeguards affording litigants an opportunity to be heard as to the propriety of taking judicial notice of a matter or as to the tenor of the matter to be noticed. Section 455 makes such an opportunity (which may be an element of due process, see Evid. Code, § 455, Law Revision Com. Comment (a)) mandatory and its provisions should be scrupulously adhered to. “[J]udicial notice can be a valuable tool in the adversary system for the lawyer as well as the court” (Kongsgaard, *Judicial Notice* (1966) 18 Hastings L.J. 117, 140) and its use is appropriate on motions for summary judgment. Its use in this case, however, to determine on summary judgment issues fundamental to the litigation without complying with statutory requirements of notice and hearing is a highly improper effort to “cut the Gordian knot of involved litigation.” (*Silver Land & Dev. Co. v. California Land Title Co.* (1967) 248 Cal.App.2d 241, 242 [56 Cal.Rptr. 178].)

30. The majority do not confront the trial court's misuse of judicial notice. They avoid this issue through the expedient of declaring that neither judicial notice nor expert opinion (such as that contained in the declarations in opposition to the motion)⁸ is

⁷ Evidence Code section 455 provides in relevant part: “With respect to any matter specified in Section 452 or in subdivision (f) of Section 451 that is of substantial consequence to the determination of the action: (a) If the trial court has been requested to take or has taken or proposes to take judicial notice of such matter, the court shall afford each party reasonable opportunity, before the jury is instructed or before the cause is submitted for decision by the court, to present to the court information relevant to (1) the propriety of taking judicial notice of the matter and (2) the tenor of the matter to be noticed.”

⁸ Fox filed two declarations in opposition to the motion; the first is that of Frank Ferguson, Fox's chief resident counsel. It alleges, in substance, that he has handled the negotiations surrounding the “Bloomer Girl” contract and its breach; that the offer to employ plaintiff in “Big Country” was made in good faith and that Fox would have produced the film if plaintiff had accepted; that by accepting the second offer plaintiff was not required to surrender any rights under the first (breached) contract nor would such acceptance have resulted in a modification of the first contract; that the compensation under the second contract was identical; that the terms and conditions of the employment were substantially the same and not inferior to the first; that the employment was in the same general line of work and comparable to that under the first contract; that plaintiff often makes pictures on location in various parts of the world; that article 2 of the original contract which provides that Fox is not required to use the artist's services is a standard provision in artists' contracts designed to negate any implied covenant that the film producer promises to play the artist in or produce the film; that it is not intended to be an advance waiver by the producer of the doctrine of mitigation of damages.

necessary to reach the trial court's conclusion. *Something*, however, clearly *is* needed to support this conclusion. Nevertheless, the majority make no effort to justify the judgment through an examination of the plaintiff's declarations. Ignoring the obvious insufficiency of these declarations, the majority announce that “the deprivation or infringement of an employee's rights held under an original employment contract” changes the alternate employment offered or available into employment of an inferior kind.

31. The second declaration is that of Richard Zanuck. It avers that he is Fox's vice president in charge of production; that he has final responsibility for casting decisions, that he is familiar with plaintiff's ability and previous artistic history; that the offer of employment for “Big Country” was in the same general line and comparable to that of “Bloomer Girl”; that plaintiff would not have suffered any detriment to her image or reputation by appearing in it; that elimination of director and script approval rights would not injure plaintiff; that plaintiff has appeared in dramatic and western roles previously and has not limited herself to musicals; and that Fox would have complied with the terms of its offer if plaintiff had accepted it.
32. I cannot accept the proposition that an offer which eliminates *any* contract right, regardless of its significance, is, as a matter of law, an offer of employment of an inferior kind. Such an absolute rule seems no more sensible than the majority's earlier suggestion that the mere existence of differences between two jobs is sufficient to render them employment of different kinds. Application of such per se rules will severely undermine the principle of mitigation of damages in the employer-employee context.
33. I remain convinced that the relevant question in such cases is whether or not a particular contract provision is so significant that its omission creates employment of an inferior kind. This question is, of course, intimately bound up in what I consider the ultimate issue: whether or not the employee acted reasonably. This will generally involve a factual inquiry to ascertain the importance of the particular contract term and a process of weighing the absence of that term against the countervailing advantages of the alternate employment. In the typical case, this will mean that summary judgment must be withheld.
34. In the instant case, there was nothing properly before the trial court by which the importance of the approval rights could be ascertained, much less evaluated. Thus, in

order to grant the motion for summary judgment, the trial court misused judicial notice. In upholding the summary judgment, the majority here rely upon per se rules which distort the process of determining whether or not an employee is obliged to accept particular employment in mitigation of damages.

35. I believe that the judgment should be reversed so that the issue of whether or not the offer of the lead role in “Big Country, Big Man” was of employment comparable to that of the lead role in “Bloomer Girl” may be determined at trial.

American Standard, Inc. v. Schectman

Supreme Court of New York, Appellate Division
80 A.D.2d 318; 439 N.Y.S.2d 529 (1981)

HANCOCK, Jr.

1. Plaintiffs have recovered a judgment on a jury verdict of \$90,000 against defendant for his failure to complete grading and to take out certain foundations and other subsurface structures to one foot below the grade line as promised. Whether the court should have charged the jury, as defendant Schectman requested, that the difference in value of plaintiffs' property with and without the promised performance was the measure of the damage is the main point in his appeal.¹ We hold that the request was properly denied and that the cost of completion—not the difference in value—was the proper measure. Finding no basis for reversal, we affirm.
2. Until 1972, plaintiffs operated a pig iron manufacturing plant on land abutting the Niagara River in Tonawanda. On the 26-acre parcel were, in addition to various industrial and office buildings, a 60-ton blast furnace, large lifts, hoists and other equipment for transporting and storing ore, railroad tracks, cranes, diesel locomotives and sundry implements and devices used in the business. Since the 1870's plaintiffs' property, under several different owners, had been the site of various industrial operations. Having decided to close the plant, plaintiffs on August 3, 1973 made a contract in which they agreed to convey the buildings and other structures and most of the equipment to defendant, a demolition and excavating contractor, in return for defendant's payment of \$275,000 and his promise to remove the equipment, demolish the structures and grade the property as specified.
3. We agree with Trial Term's interpretation of the contract as requiring defendant to remove all foundations, piers, headwalls, and other structures, including those under the surface and not visible and whether or not shown on the map attached to the

¹ The judgment in the amount of \$122,434.60 including interest and costs is jointly and severally against both defendants, viz., Harold Schectman, the contracting party, and the company which issued the performance bond, United States Fire Insurance Company. Inasmuch as the interests of both defendants here are identical, for the purpose of this appeal and for the sake of simplicity we treat the defendants as one: i.e., the contracting party, Harold Schectman. A third-party action commenced by the bonding company on an indemnity agreement between it and defendant Schectman and others is not part of this appeal. The appeal is also taken from an order denying defendant's motion to set aside the verdict and for a new trial.

contract, to a depth of approximately one foot below the specified grade lines.² The proof from plaintiffs' witnesses and the exhibits, showing a substantial deviation from the required grade lines and the existence above grade of walls, foundations and other structures, support the finding, implicit in the jury's verdict, that defendant failed to perform as agreed. Indeed, the testimony of defendant's witnesses and the position he has taken during his performance of the contract and throughout this litigation (which the trial court properly rejected), *viz.*, that the contract did not require him to remove all subsurface foundations, allow no other conclusion.

4. We turn to defendant's argument that the court erred in rejecting his proof that plaintiffs suffered no loss by reason of the breach because it makes no difference in the value of the property whether the old foundations are at grade or one foot below grade and in denying his offer to show that plaintiffs succeeded in selling the property for \$183,000—only \$3,000 less than its full fair market value. By refusing this testimony and charging the jury that the cost of completion (estimated at \$110,500 by plaintiffs' expert), not diminution in value of the property, was the measure of damage the court, defendant contends, has unjustly permitted plaintiffs to reap a windfall at his expense. Citing the definitive opinion of Judge Cardozo in *Jacob & Youngs v Kent* (230 NY 239), he maintains that the facts present a case "of substantial performance" of the contract with omissions of "trivial or inappreciable importance" and that because the cost of completion was "grossly and unfairly out of proportion to the good to be attained," the proper measure of damage is diminution in value.
5. The general rule of damages for breach of a construction contract is that the injured party may recover those damages which are the direct, natural and immediate consequence of the breach and which can reasonably be said to have been in the contemplation of the parties when the contract was made (see 13 NY Jur, Damages, §§ 46, 56; *Chamberlain v Parker*, 45 NY 569; *Hadley v Baxendale*, 9 Exch [Welsby, Hurlstone & Gordon] 341; Restatement, Contracts, § 346). In the usual case where

² Paragraph 7 of the agreement states in pertinent part: "7. After the Closing Date, Purchaser shall demolish all of the Improvements on the North Tonawanda Property included in the sale to Purchaser, cap the water intake at the pumphouse end, and grade and level the property, all in accordance with the provisions of Exhibit 'C' and 'C1' attached hereto." Exhibit C (notes on demolition and grading) contains specifications for the grade levels for four separate areas shown on Map C1 and the following instruction: "Except as otherwise excepted all structures and equipment including foundations, piers, headwalls, etc. shall be removed to a depth approximately one foot below grade lines as set forth above. Area common to more than one area will be faired to provide reasonable transitions, it being intended to provide a reasonably attractive vacant plot for resale."

the contractor's performance has been defective or incomplete, the reasonable cost of replacement or completion is the measure (see *Bellizzi v Huntley Estates*, 3 NY2d 112; *Spence v Ham*, 163 NY 220; *Condello v Stock*, 285 App Div 861, mod on other grounds 1 NY2d 831; *Along-The-Hudson Co. v Ayres*, 170 App Div 218; 13 NY Jur, Damages, § 56, p 502; Restatement, Contracts, § 346). When, however, there has been a substantial performance of the contract made in good faith but defects exist, the correction of which would result in economic waste, courts have measured the damages as the difference between the value of the property as constructed and the value if performance had been properly completed (see *Jacob & Youngs v Kent*, *supra*; *Droher & Sons v Toushin*, 250 Minn 490; Restatement, Contracts, § 346, subd [1], par [a], cl [ii], p 573; comment *b*, p 574; 13 NY Jur, Damages, § 58; Ann., 76 ALR2d 805, § 4, pp 812-815). *Jacob & Youngs* is illustrative. There, plaintiff, a contractor, had constructed a house for the defendant which was satisfactory in all respects save one: the wrought iron pipe installed for the plumbing was not of Reading manufacture, as specified in the contract, but of other brands of the same quality. Noting that the breach was unintentional and the consequences of the omission trivial, and that the cost of replacing the pipe would be "grievously out of proportion" (*Jacob & Youngs v Kent*, *supra*, p 244) to the significance of the default, the court held the breach to be immaterial and the proper measure of damage to the owner to be not the cost of replacing the pipe but the nominal difference in value of the house with and without the Reading pipe.

6. Not in all cases of claimed "economic waste" where the cost of completing performance of the contract would be large and out of proportion to the resultant benefit to the property have the courts adopted diminution in value as the measure of damage. Under the Restatement rule, the completion of the contract must involve "unreasonable economic waste" and the illustrative example given is that of a house built with pipe different in name but equal in quality to the brand stipulated in the contract as in *Jacob & Youngs v Kent* (230 NY 239, *supra*) (Restatement, Contracts, § 346, subd [1], par [a], cl [ii], p 573; Illustration No. 2, p 576). In *Groves v Wunder Co.* (205 Minn. 163), plaintiff had leased property and conveyed a gravel plant to defendant in exchange for a sum of money and for defendant's commitment to return the property to plaintiff at the end of the term at a specified grade -- a promise defendant failed to perform. Although the cost of the fill to complete the grading was \$60,000 and the total value of the property, graded as specified in the contract, only \$12,160 the court rejected the "diminution in value" rule, stating: "The owner's right

to improve his property is not trammled by its small value. It is his right to erect thereon structures which will reduce its value. If that be the result, it can be of no aid to any contractor who declines performance. As said long ago in *Chamberlain v. Parker*, 45 N.Y. 569, 572: 'A man may do what he will with his own, ... and if he chooses to erect a monument to his caprice or folly on his premises, and employs and pays another to do it, it does not lie with a defendant who has been so employed and paid for building it, to say that his own performance would not be beneficial to the plaintiff.'" (*Groves v Wunder Co.*, *supra*, p 168.)

7. The "economic waste" of the type which calls for application of the "diminution in value" rule generally entails defects in construction which are irremediable or which may not be repaired without a substantial tearing down of the structure as in *Jacob & Youngs* (see *Bellizzi v Huntley Estates*, 3 NY2d 112, 115, *supra*; *Groves v Wunder Co.*, *supra*; *Slugg Seed & Fertilizer v Paulson Lbr.*, 62 Wis 2d 220; Restatement, Contracts, § 346, subd [1], Illustration Nos. 2, 4, pp 576-577; Ann., 76 ALR2d 805, § 4, pp 812-815).
8. Where, however, the breach is of a covenant which is only incidental to the main purpose of the contract and completion would be disproportionately costly, courts have applied the diminution in value measure even where no destruction of the work is entailed (see, e.g., *Peevyhouse v Garland Coal & Min. Co.*, 382 P2d 109 [Okla], *cert. denied*, 375 U.S. 906, holding [contrary to *Groves v Wunder Co.*, *supra*] that diminution in value is the proper measure where defendant, the lessee of plaintiff's lands under a coal mining lease, failed to perform costly remedial and restorative work on the land at the termination of the lease. The court distinguished the "building and construction" cases and noted that the breach was of a covenant incidental to the main purpose of the contract which was the recovery of coal from the premises to the benefit of both parties; and see *Avery v Fredericksen & Westbrook*, 67 Cal App 2d 334).
9. It is also a general rule in building and construction cases, at least under *Jacob & Youngs* (*supra*) in New York (see *Groves v Wunder Co.*, *supra*; Ann., 76 ALR2d 805, § 6, pp 823-826), that a contractor who would ask the court to apply the diminution of value measure "as an instrument of justice" must not have breached the contract intentionally and must show substantial performance made in good faith (*Jacob & Youngs v Kent*, *supra*, pp 244, 245).

10. In the case before us, plaintiffs chose to accept as part of the consideration for the promised conveyance of their valuable plant and machines to defendant his agreement to grade the property as specified and to remove the foundations, piers and other structures to a depth of one foot below grade to prepare the property for sale. It cannot be said that the grading and the removal of the structures were incidental to plaintiffs' purpose of "achieving a reasonably attractive vacant plot for resale" (cf. *Peevyhouse v Garland Coal & Min. Co.*, *supra*). Nor can defendant maintain that the damages which would naturally flow from his failure to do the grading and removal work and which could reasonably be said to have been in the contemplation of the parties when the contract was made would not be the reasonable cost of completion (see 13 NY Jur, Damages, §§ 46, 56; *Hadley v Baxendale*, 9 Exch [Welsby, Hurlstone & Gordon] 341, *supra*). That the fulfillment of defendant's promise would (contrary to plaintiffs' apparent expectations) add little or nothing to the sale value of the property does not excuse the default.
11. As in the hypothetical case, posed in *Chamberlain v Parker* (45 NY 569, *supra*) (cited in *Groves v Wunder Co.*, 205 Minn 163, *supra*), of the man who "chooses to erect a monument to his caprice or folly on his premises, and employs and pays another to do it", it does not lie with defendant here who has received consideration for his promise to do the work "to say that his own performance would not be beneficial to the [plaintiffs]" (*Chamberlain v Parker*, *supra*, p 572).
12. Defendant's completed performance would not have involved undoing what in good faith was done improperly but only doing what was promised and left undone (cf. *Jacob & Youngs v Kent*, 230 NY 239, *supra*; Restatement, Contracts, § 346, subd [1], Illustration No. 2, p 576). That the burdens of performance were heavier than anticipated and the cost of completion disproportionate to the end to be obtained does not, without more, alter the rule that the measure of plaintiffs' damage is the cost of completion. Disparity in relative economic benefits is not the equivalent of "economic waste" which will invoke the rule in *Jacob & Youngs v Kent* (*supra*) (see *Groves v Wunder Co.*, *supra*). Moreover, faced with the jury's finding that the reasonable cost of removing the large concrete and stone walls and other structures extending above grade was \$90,000, defendant can hardly assert that he has rendered substantial performance of the contract or that what he left unfinished was "of trivial or inappreciable importance" (*Jacob & Youngs v Kent*, *supra*, p 245). Finally, defendant, instead of attempting in good faith to complete the removal of the underground structures, contended that he was not obliged by the contract to do so

and, thus, cannot claim to be a "transgressor whose default is unintentional and trivial [and who] may hope for mercy if he will offer atonement for his wrong" (*Jacob & Youngs v Kent, supra*, p 244). We conclude, therefore, that the proof pertaining to the value of plaintiffs' property was properly rejected and the jury correctly charged on damages.

13. The judgment and order should be affirmed.

Peevyhouse v. Garland Coal & Mining Co.

Supreme Court of Oklahoma
382 P.2d 109 (1962)

JACKSON, Justice.

1. In the trial court, plaintiffs Willie and Lucille Peevyhouse sued the defendant, Garland Coal and Mining Company, for damages for breach of contract. Judgment was for plaintiffs in an amount considerably less than was sued for. Plaintiffs appeal and defendant cross-appeals.
2. In the briefs on appeal, the parties present their argument and contentions under several propositions; however, they all stem from the basic question of whether the trial court properly instructed the jury on the measure of damages.
3. Briefly stated, the facts are as follows: plaintiffs owned a farm containing coal deposits, and in November, 1954, leased the premises to defendant for a period of five years for coal mining purposes. A “stripmining” operation was contemplated in which the coal would be taken from pits on the surface of the ground, instead of from underground mine shafts. In addition to the usual covenants found in a coal mining lease, defendant specifically agreed to perform certain restorative and remedial work at the end of the lease period. It is unnecessary to set out the details of the work to be done, other than to say that it would involve the moving of many thousands of cubic yards of dirt, at a cost estimated by expert witnesses at about \$29,000.00. However, plaintiffs sued for only \$25,000.00.
4. During the trial, it was stipulated that all covenants and agreements in the lease contract had been fully carried out by both parties, except the remedial work mentioned above; defendant conceded that this work had not been done.
5. Plaintiffs introduced expert testimony as to the amount and nature of the work to be done, and its estimated cost. Over plaintiffs' objections, defendant thereafter introduced expert testimony as to the “diminution in value” of plaintiffs' farm resulting from the failure of defendant to render performance as agreed in the contract—that is, the difference between the present value of the farm, and what its value would have been if defendant had done what it agreed to do.

6. At the conclusion of the trial, the court instructed the jury that it must return a verdict for plaintiffs, and left the amount of damages for jury determination. On the measure of damages, the court instructed the jury that it might consider the cost of performance of the work defendant agreed to do, “together with all of the evidence offered on behalf of either party.”
7. It thus appears that the jury was at liberty to consider the “diminution in value” of plaintiffs' farm as well as the cost of “repair work” in determining the amount of damages.
8. It returned a verdict for plaintiffs for \$5000.00—only a fraction of the “cost of performance,” *but more than the total value of the farm even after the remedial work is done.*
9. On appeal, the issue is sharply drawn. Plaintiffs contend that the true measure of damages in this case is what it will cost plaintiffs to obtain performance of the work that was not done because of defendant's default. Defendant argues that the measure of damages is the cost of performance “limited, however, to the total difference in the market value before and after the work was performed.”
10. It appears that this precise question has not heretofore been presented to this court. In *Ardizonne v. Archer*, 72 Okl. 70, 178 P. 263, this court held that the measure of damages for breach of a contract to drill an oil well was the reasonable cost of drilling the well, but here a slightly different factual situation exists. The drilling of an oil well will yield valuable geological information, even if no oil or gas is found, and of course if the well is a producer, the value of the premises increases. In the case before us, it is argued by defendant with some force that the performance of the remedial work defendant agreed to do will add at the most only a few hundred dollars to the value of plaintiffs' farm, and that the damages should be limited to that amount because that is all plaintiffs have lost.
11. Plaintiffs rely on *Groves v. John Wunder Co.*, 205 Minn. 163, 286 N.W. 235, 123 A.L.R. 502. In that case, the Minnesota court, in a substantially similar situation, adopted the “cost of performance” rule as-opposed to the “value” rule. The result was to authorize a jury to give plaintiff damages in the amount of \$60,000, where the real estate concerned would have been worth only \$12,160, even if the work contracted for had been done.

12. It may be observed that *Groves v. John Wunder Co.*, *supra*, is the only case which has come to our attention in which the cost of performance rule has been followed under circumstances where the cost of performance greatly exceeded the diminution in value resulting from the breach of contract. Incidentally, it appears that this case was decided by a plurality rather than a majority of the members of the court.
13. Defendant relies principally upon *Sandy Valley & E. R. Co., v. Hughes*, 175 Ky. 320, 194 S.W. 344; *Bigham v. Wabash-Pittsburg Terminal Ry. Co.*, 223 Pa. 106, 72 A. 318; and *Sweeney v. Lewis Const. Co.*, 66 Wash. 490, 119 P. 1108. These were all cases in which, under similar circumstances, the appellate courts followed the “value” rule instead of the “cost of performance” rule. Plaintiff points out that in the earliest of these cases (*Bigham*) the court cites as authority on the measure of damages an earlier Pennsylvania *tort* case, and that the other two cases follow the first, with no explanation as to why a measure of damages ordinarily followed in cases sounding in *tort* should be used in contract cases. Nevertheless, it is of some significance that three out of four appellate courts have followed the diminution in value rule under circumstances where, as here, the cost of performance greatly exceeds the diminution in value.
14. The explanation may be found in the fact that the situations presented are artificial ones. It is highly unlikely that the ordinary property owner would agree to pay \$29,000 (or its equivalent) for the construction of “improvements” upon his property that would increase its value only about (\$300) three hundred dollars. The result is that we are called upon to apply principles of law theoretically based upon reason and reality to a situation which is basically unreasonable and unrealistic.
15. In *Groves v. John Wunder Co.*, *supra*, in arriving at its conclusions, the Minnesota court apparently considered the contract involved to be analogous to a building and construction contract, and cited authority for the proposition that the cost of performance or completion of the building as contracted is ordinarily the measure of damages in actions for damages for the breach of such a contract.
16. In an annotation following the Minnesota case beginning at 123 A.L.R. 515, the annotator places the three cases relied on by defendant (*Sandy Valley*, *Bigham* and *Sweeney*) under the classification of cases involving “grading and excavation contracts.”

17. We do not think either analogy is strictly applicable to the case now before us. The primary purpose of the lease contract between plaintiffs and defendant was neither “building and construction” nor “grading and excavation.” It was merely to accomplish the economical recovery and marketing of coal from the premises, to the profit of all parties. The special provisions of the lease contract pertaining to remedial work were incidental to the main object involved.
18. Even in the case of contracts that are unquestionably building and construction contracts, the authorities are not in agreement as to the factors to be considered in determining whether the cost of performance rule or the value rule should be applied. The American Law Institute's RESTATEMENT OF THE LAW, CONTRACTS, Volume 1, Sections 346(1)(a)(i) and (ii) submits the proposition that the cost of performance is the proper measure of damages “if this is possible and does not involve *unreasonable economic waste*,” and that the diminution in value caused by the breach is the proper measure “if construction and completion in accordance with the contract would involve *unreasonable economic waste*.” (Emphasis supplied.) In an explanatory comment immediately following the text, the Restatement makes it clear that the “economic waste” referred to consists of the destruction of a substantially completed building or other structure. Of course no such destruction is involved in the case now before us.
19. On the other hand, in MCCORMICK, DAMAGES, Section 168, it is said with regard to building and construction contracts that “...in cases where the defect is one that can be repaired or cured without *undue expense*” the cost of performance is the proper measure of damages, but where “...the defect in material or construction is one that cannot be remedied without *an expenditure for reconstruction disproportionate to the end to be attained*” (emphasis supplied) the value rule should be followed. The same idea was expressed in *Jacob & Youngs, Inc. v. Kent*, 230 N.Y. 239, 129 N.E. 889, 23 A.L.R. 1429, as follows:
- The owner is entitled to the money which will permit him to complete, unless the cost of completion is grossly and unfairly out of proportion to the good to be attained. When that is true, the measure is the difference in value.
20. It thus appears that the prime consideration in the Restatement was “economic waste;” and that the prime consideration in MCCORMICK, DAMAGES, and in *Jacob &*

Youngs, Inc. v. Kent, supra, was the relationship between the expense involved and the “end to be attained”—in other words, the “relative economic benefit.”

21. In view of the unrealistic fact situation in the instant case, and certain Oklahoma statutes to be hereinafter noted, we are of the opinion that the “relative economic benefit” is a proper consideration here. This is in accord with the recent case of *Mann v. Clowser*, 190 Va. 887, 59 S.E.2d 78, where, in applying the cost rule, the Virginia court specifically noted that “... the defects are remediable from a practical standpoint and the costs *are not grossly disproportionate to the results to be obtained*” (Emphasis supplied).

22. 23 O.S.1961 §§ 96 and 97 provide as follows:

§ 96. ...Notwithstanding the provisions of this chapter, no person can recover a greater amount in damages for the breach of an obligation, than he would have gained by the full performance thereof on both sides....

§ 97. ...Damages must, in all cases, be reasonable, and where an obligation of any kind appears to create a right to unconscionable and grossly oppressive damages, contrary to substantial justice no more than reasonable damages can be recovered.

Although it is true that the above sections of the statute are applied most often in tort cases, they are by their own terms, and the decisions of this court, also applicable in actions for damages for breach of contract. It would seem that they are peculiarly applicable here where, under the “cost of performance” rule, plaintiffs might recover an amount about nine times the total value of their farm. Such would seem to be “unconscionable and grossly oppressive damages, contrary to substantial justice” within the meaning of the statute. Also, it can hardly be denied that if plaintiffs here are permitted to recover under the “cost of performance” rule, they will receive a greater benefit from the breach than could be gained from full performance, contrary to the provisions of Sec. 96.

23. An analogy may be drawn between the cited sections, and the provisions of 15 O.S.1961 §§ 214 and 215. These sections tend to render void any provisions of a contract which attempt to fix the amount of stipulated damages to be paid in case of a breach, except where it is impracticable or extremely difficult to determine the actual damages. This results in spite of the agreement of the parties, and the obvious and

well known rationale is that insofar as they exceed the actual damages suffered, the stipulated damages amount to a penalty or forfeiture which the law does not favor.

24. 23 O.S.1961 §§ 96 and 97 have the same effect in the case now before us. *In spite of the agreement of the parties*, these sections limit the damages recoverable to a reasonable amount not “contrary to substantial justice;” they prevent plaintiffs from recovering a “greater amount in damages for the breach of an obligation” than they would have “gained by the full performance thereof.”
25. We therefore 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 because of the non-performance.
26. We believe the above holding is in conformity with the intention of the Legislature as expressed in the statutes mentioned, and in harmony with the better-reasoned cases from the other jurisdictions where analogous fact situations have been considered. It should be noted that the rule as stated does not interfere with the property owner's right to “do what he will with his own” *Chamberlain v. Parker*, 45 N.Y. 569), or his right, if he chooses, to contract for “improvements” which will actually have the effect of reducing his property's value. Where such result is in fact contemplated by the parties, and is a main or principal purpose of those contracting, it would seem that the measure of damages for breach would ordinarily be the cost of performance.
27. The above holding disposes of all of the arguments raised by the parties on appeal.
28. Under the most liberal view of the evidence herein, the diminution in value resulting to the premises because of non-performance of the remedial work was \$300.00. After a careful search of the record, we have found no evidence of a higher figure, and plaintiffs do not argue in their briefs that a greater diminution in value was sustained. It thus appears that the judgment was clearly excessive, and that the amount for which

judgment should have been rendered is definitely and satisfactorily shown by the record.

29. We are asked by each party to modify the judgment in accordance with the respective theories advanced, and it is conceded that we have authority to do so. 12 O.S.1961 § 952; *Busboom v. Smith*, 199 Okl. 688, 191 P.2d 198; *Stumpf v. Stumpf*, 173 Okl. 1, 46 P.2d 315.
30. We are of the opinion that the judgment of the trial court for plaintiffs should be, and it is hereby, modified and reduced to the sum of \$300.00, and as so modified it is affirmed.

WELCH, DAVISON, HALLEY, and JOHNSON, JJ., concur.

WILLIAMS, C. J., BLACKBIRD, V. C. J., and IRWIN and BERRY, JJ., dissent.

IRWIN, Justice (dissenting).

31. By the specific provisions in the coal mining lease under consideration, the defendant agreed as follows:

7b Lessee agrees to make fills in the pits dug on said premises on the property line in such manner that fences can be placed thereon and access had to opposite sides of the pits.

7c Lessee agrees to smooth off the top of the spoil banks on the above premises.

7d Lessee agrees to leave the creek crossing the above premises in such a condition that it will not interfere with the crossings to be made in pits as set out in 7b....

7f Lessee further agrees to leave no shale or dirt on the high wall of said pits....

Following the expiration of the lease, plaintiffs made demand upon defendant that it carry out the provisions of the contract and to perform those covenants contained therein.

32. Defendant admits that it failed to perform its obligations that it agreed and contracted to perform under the lease contract and there is nothing in the record which indicates that defendant could not perform its obligations. Therefore, in my opinion defendant's breach of the contract was wilful and not in good faith.
33. Although the contract speaks for itself, there were several negotiations between the plaintiffs and defendant before the contract was executed. Defendant admitted in the trial of the action, that 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.
34. In consideration for the lease contract, plaintiffs were to receive a certain amount as royalty for the coal produced and marketed and in addition thereto their land was to be restored as provided in the contract.
35. Defendant received as consideration for the contract, its proportionate share of the coal produced and marketed and in addition thereto, the *right to use* plaintiffs' land in the furtherance of its mining operations.
36. The cost for performing the contract in question could have been reasonably approximated when the contract was negotiated and executed and there are no conditions now existing which could not have been reasonably anticipated by the parties. Therefore, defendant had knowledge, when it prevailed upon the plaintiffs to execute the lease, that the cost of performance might be disproportionate to the value or benefits received by plaintiff for the performance.
37. Defendant has received its benefits under the contract and now urges, in substance, that plaintiffs' measure of damages for its failure to perform should be the economic value of performance to the plaintiffs and not the cost of performance.
38. If a peculiar set of facts should exist where the above rule should be applied as the proper measure of damages, (and in my judgment those facts do not exist in the instant case) before such rule should be applied, consideration should be given to the benefits received or contracted for by the party who asserts the application of the rule.
39. Defendant did not have the right to mine plaintiffs' coal or to use plaintiffs' property for its mining operations without the consent of plaintiffs. Defendant had knowledge of the benefits that it would receive under the contract and the approximate cost of performing the contract. With this knowledge, it must be presumed that defendant

thought that it would be to its economic advantage to enter into the contract with plaintiffs and that it would reap benefits from the contract, or it would have not entered into the contract.

40. Therefore, if the value of the performance of a contract should be considered in determining the measure of damages for breach of a contract, the value of the benefits received under the contract by a party who breaches a contract should also be considered. However, in my judgment, to give consideration to either in the instant action, completely rescinds and holds for naught the solemnity of the contract before us and makes an entirely new contract for the parties.

41. In *Goble v. Bell Oil & Gas Co.*, 97 Okl. 261, 223 P. 371, we held:

Even though the contract contains harsh and burdensome terms which the court does not in all respects approve, it is the province of the parties in relation to lawful subject matter to fix their rights and obligations, and the court will give the contract effect according to its expressed provisions, unless it be shown by competent evidence proof that the written agreement as executed is the result of fraud, mistake, or accident.

42. In *Cities Service Oil Co. v. Geologist Co. Inc.*, 208 Okl. 179, 254 P.2d 775, we said:

While we do not agree that the contract as presently written is an onerous one, we think the short answer is that the folly or wisdom of a contract is not for the court to pass on.

43. In *Great Western Oil & Gas Company v. Mitchell*, Okl., 326 P.2d 794, we held:

The law will not make a better contract for parties than they themselves have seen fit to enter into, or alter it for the benefit of one party and to the detriment of the others; the judicial function of a court of law is to enforce a contract as it is written.

44. I am mindful of Title 23 O.S.1961 § 96, which provides that no person can recover a greater amount in damages for the breach of an obligation than he could have gained by the full performance thereof on both sides, except in cases not applicable herein. However, in my judgment, the above statutory provision is not applicable here.

45. In my judgment, we should follow the case of *Groves v. John Wunder Company*, 205 Minn. 163, 286 N.W. 235, 123 A.L.R. 502, which defendant agrees “that the fact situation is apparently similar to the one in the case at bar”, and where the Supreme Court of Minnesota held:

The owner's or employer's damages for such a breach (i. e. breach hypothesized in 2d syllabus) are to be measured, not in respect to the value of the land to be improved, but by the reasonable cost of doing that which the contractor promised to do and which he left undone.

46. The hypothesized breach referred to states that where the contractor's breach of a contract is willful, that is, in bad-faith, he is not entitled to any benefit of the equitable doctrine of substantial performance.

47. In the instant action defendant has made no attempt to even substantially perform. The contract in question is not immoral, is not tainted with fraud, and was not entered into through mistake or accident and is not contrary to public policy. It is clear and unambiguous and the parties understood the terms thereof, and the approximate cost of fulfilling the obligations could have been approximately ascertained. There are no conditions existing now which could not have been reasonably anticipated when the contract was negotiated and executed. The defendant could have performed the contract if it desired. It has accepted and reaped the benefits of its contract and now urges that plaintiffs' benefits under the contract be denied. If plaintiffs' benefits are denied, such benefits would inure to the direct benefit of the defendant.

48. Therefore, in my opinion, the plaintiffs were entitled to specific performance of the contract and since defendant has failed to perform, the proper measure of damages should be the cost of performance. Any other measure of damage would be holding for naught the express provisions of the contract; would be taking from the plaintiffs the benefits of the contract and placing those benefits in defendant which has failed to perform its obligations; would be granting benefits to defendant without a resulting obligation; and would be completely rescinding the solemn obligation of the contract for the benefit of the defendant to the detriment of the plaintiffs by making an entirely new contract for the parties.

49. I therefore respectfully dissent to the opinion promulgated by a majority of my associates.

[Although none of what follows is strictly necessary for understanding the issues in Peevyhouse, the court's discussion of the testimony at trial may give us more insight into the facts underlying plaintiffs' claim for damages. You may also find grounds to question the competence of plaintiffs' counsel in developing the record and presenting arguments at trial.]

SUPPLEMENTAL OPINION ON REHEARING

JACKSON, Justice.

50. In a Petition for Rehearing, plaintiffs Peevyhouse have raised certain questions not presented in the original briefs on appeal.
51. They insist that the trial court excluded evidence as to the total value of the premises concerned, and, in effect, that they have not had their 'day in court'. This argument arises by reason of the fact that their farm consists not merely of the 60 acres covered by the coal mining lease, but includes other lands as well.
52. Plaintiffs originally pleaded two causes of action against the defendant mining company. The first one was for damages for breach of contract; the second one was for damages to the water well and home of plaintiffs, because of the use of excessively large charges of dynamite or blasting powder in close proximity to the home and well.
53. Numbered paragraph 2 of plaintiffs' petition alleges that they own and live upon 60 acres of land which are specifically described. *This is the only land described in the petition, and there is no allegation as to the ownership or leasing of any other lands.*
54. Page 4 of the transcript of evidence reveals that near the beginning of the trial, plaintiff Peevyhouse was asked a question concerning improvements he had made to his property. His answer was "For one thing I built a new home on the place in 1951, and along about that time I was building a pasture. And I would say *ninety percent of this 120 acres is in good grass.*" (Emphasis supplied.) Mr. Watts, defense counsel, then objected "to any testimony about the property, other than the 160 acres." (It is obvious that he means "60" instead of "160.") Further proceedings were as follows:

The Court: The objection will be sustained as to any other part. Go ahead.

Mr. McCornell (attorney for plaintiffs): Comes now the plaintiff and dismisses the second cause of action without prejudice.

It thus appears that plaintiffs made no complaint as to the court's exclusion of evidence concerning lands other than the 60 acres described in their petition.

55. Pages 7 and 8 of the transcript show that later during direct examination of Mr. Peevyhouse, the following occurred:

Q. (By Mr. McConnell) Now, Mr. Peevyhouse, I ask you to step down here and I ask you if you are familiar with this sketch or drawing?

....

A. Yes. I've got about 40 acres here, and here would be 20, and there would be 20 on this sketch. And I've got leased land lying in here, 80 acres.

Mr. Watts: If your Honor please, I object to anything except the 60 acres involved in this lawsuit.

The Court: Sustained.

Q. (By Mr. McConnell) Will you point out to the jury, the boundary line shown of your property?

....

A. That blue is where the water is actually standing at the present time. Up until a short time ago this area here came over that far. And this spring all of it would run, come in here out this way and through here, spreading over this land and all below it. And at the present time this is washed out here.

Mr. Watts: If your Honor please, I object to that as not the proper measure of damages.

The Court: The objection will be sustained.

This testimony of Mr. Peevyhouse is difficult for us to follow, even with the exhibits in the case before us. However, no complaint was made by plaintiffs, or any suggestion that the court was in error in excluding this testimony.

56. The defendant offered the testimony of five witnesses in the trial court; four of them testified as to “diminution in value.” They were not cross examined by plaintiffs.
57. In their motion for new trial, plaintiffs did not complain that they had been prevented from offering evidence as to the diminution in value of their lands; on the contrary, they affirmatively complained of the trial court's action in admitting evidence of the *defendant* on that point.
58. In the original brief of plaintiffs in error (Peevyhouse) filed in this court there appears the following language at page 4:

...Near the outset of the trial plaintiffs dismissed their second cause of action without prejudice: further, it was stipulated.... It was further stipulated that the *only issue remaining in the lawsuit* was the proof and *measure of damages* to which plaintiffs were entitled.... (Emphasis supplied.)

In the answer brief of Garland Coal & Mining Co., at page 3, there appears the following language:

Defendant offered evidence that the total value of the property involved before the mining operation would be \$60.00 per acre, and \$11.00 per acre after the mining operation (60 acres at \$49.00 per acre is \$2940.00). Other evidence was that the property was worth \$5.00 to \$15.00 per acre after the mining, but before the repairs; and would be worth an increase of \$2.00 to \$5.00 per acre after the repairs had been made (60 acres at \$5.00 per acre is \$300.00) (Tr. 96-97, 135, 137-138, 138-141, 143-145, 156, 158).

At page 18 of the same brief there is another statement to the effect that the ‘amount of diminution in value of the land’ was \$300.00.

59. About two months after the answer brief was filed in this court, plaintiffs filed a reply brief. The reply brief makes no reference at all to the language of the answer brief above quoted and *does not deny that the diminution in value shown by the record amounts to \$300.00*. On the contrary, it contains the following language at page 5:

...Plaintiffs in error pointed out in their initial brief that this evidence concerning land values was objectionable as being incompetent and refused to cross-examine or offer rebuttal for the reason that they did not choose to waive their objections to the competency of the evidence by disproving defendant in error's allegations as to land values. We strongly urged at the trial below, and still do, that market value of the land has no application....

60. Our extended reference to the pleadings, testimony and prior briefs in this case has not been solely for the purpose of showing that plaintiffs failed to complain of the court's rulings. Our purpose, rather, has been to demonstrate the plan and theory upon which plaintiffs tried their case below, and upon which they argued it in the prior briefs on appeal.
61. The whole record in this case justifies the conclusion that plaintiffs tried their case upon the theory that the "cost of performance" would be the sole measure of damages and that they would recognize no other. In view of the whole record in this case and the original briefs on appeal, we conclude that they so tried it *with notice* that defendant would contend for the "diminution in value" rule. The testimony to which they specifically refer in the petition for rehearing shows that the trial court properly excluded defendant's evidence concerning lands other than the 60 acres described in the petition because such evidence was *not within the scope of the pleadings*. At no time did plaintiffs ask permission to amend their petition, either with or without prejudice to trial, so as to describe *all* of the lands they own or lease, and no evidence was admitted which could broaden the scope of the petition.
62. Plaintiffs' petition described 60 acres of land only; plaintiffs offered no evidence on the question of "diminution in value" and objected to similar evidence offered by the defendant; their motion for new trial contained no allegation that they had been prevented from offering evidence on this question; in their reply brief they did not controvert the allegation in defendant's answer brief that the record showed a "diminution in value" of only \$300.00; and in view of the stipulation they admittedly made in the trial court, their statement in petition for rehearing that the court's instructions on the measure of damages came as a "complete surprise" and "did not afford them the opportunity to prepare and introduce evidence under the 'diminution in value' rule" is not supported by the record.
63. We think plaintiffs' present position is that of a plaintiff in any damage suit who has failed to prove his damages-opposed by a defendant who has proved plaintiff's

damages; and that plaintiffs' complaint that the record does not show the total "diminution in value" to their lands comes too late. It is well settled that a party will not be permitted to change his theory of the case upon appeal. *Knox v. Eason Oil Co.*, 190 Okl. 627, 126 P.2d 247.

64. Also, plaintiffs' expressed fear that by introducing evidence on the question of "diminution in value" they would have waived their objection to similar evidence by defendant was not justified. *Vogel v. Fisher et al.*, 203 Okl. 657, 225 P.2d 346; 53 Am. Jur. Trial § 144.
65. It is suggested in a brief of amici curiae that our decision in this case has resulted in an impairment of the obligation of the contract of the parties, in violation of Article 1, Section 10, of the Constitution of the United States, and in that connection the only case cited is *Sturges v. Crowninshield*, 4 Wheat 122, 17 U.S. 1229 (1819). In their brief, amici curiae quote language from the Lawyer's Edition notes of Mr. Stephen K. Williams, in which he summarized the "points and authorities" of one of the counsel appearing before the U. S. Supreme Court.
66. *Sturges v. Crowninshield* was an early case in which the Supreme Court considered the power of a state to enact bankruptcy laws, and the extent, if any, to which such power is limited by Article 1, Section 10 of the Constitution. The contracts concerned consisted of promissory notes executed in March, 1811, and the bankruptcy law under which the promisor claimed a discharge was not enacted until April 3, 1811. In a memorable opinion written by Chief Justice Marshall, the court held that insofar as the bankruptcy law purported to discharge the obligations of contracts executed *before its enactment*, it was unconstitutional and void.
67. The same situation does not exist here. 23 O.S.1961 §§ 96 and 97, cited in our original opinion, were a part of the Revised Laws of 1910 (R.L.1910) Sections 2889 and 2890) and have been in force in this state, in unchanged form, since that codification was adopted by the legislature in 1911. The lease contract concerned in the case now before us was not executed until 1954.
68. Nor do we agree that our decision itself (as opposed to the statutes cited therein as controlling) impairs the obligations of the contract concerned. It may be conceded that at one time there was respectable authority for the proposition that the "contract" clause was violated by a judicial decision which overruled prior decisions, upon the strength of which contract rights had been acquired. In this connection, it should be

noted that our decision overrules no prior holdings of this court upon which the contracting parties could be said to have relied. Even if it did,

... it is now definitely and authoritatively settled that such prohibition in federal and state constitutions relate to legislative action and not to judicial decisions. Thus, they do not apply to the decision of a state court, where such decision does not expressly, or by necessary implication, give effect to a subsequent law of the state whereby the obligation of the contract is impaired....

16 C.J.S. CONSTITUTIONAL LAW § 280. To the same effect, see 12 AM. JUR. CONSTITUTIONAL LAW § 398.

69. Our decision herein overrules no prior holdings of this court, and it does not give effect to a *subsequent* law of this state. It therefore cannot be said to impair the obligations of the contract of the parties here concerned.
70. The petition for rehearing is denied.

HALLEY, V. C. J., and WELCH, DAVISON and JOHNSON, JJ., concur.

BLACKBIRD, C. J., and WILLIAMS, IRWIN and BERRY, JJ., dissent.

Lake River Corp. v. Carborundum Co.

United States Court of Appeals for the Seventh Circuit
769 F.2d 1284 (1985)

POSNER, Circuit Judge.

1. This diversity suit between Lake River Corporation and Carborundum Company requires us to consider questions of Illinois commercial law, and in particular to explore the fuzzy line between penalty clauses and liquidated-damages clauses.
2. Carborundum manufactures “Ferro Carbo,” an abrasive powder used in making steel. To serve its midwestern customers better, Carborundum made a contract with Lake River by which the latter agreed to provide distribution services in its warehouse in Illinois. Lake River would receive Ferro Carbo in bulk from Carborundum, “bag” it, and ship the bagged product to Carborundum's customers. The Ferro Carbo would remain Carborundum's property until delivered to the customers.
3. Carborundum insisted that Lake River install a new bagging system to handle the contract. In order to be sure of being able to recover the cost of the new system (\$89,000) and make a profit of 20 percent of the contract price, Lake River insisted on the following minimum-quantity guarantee:

In consideration of the special equipment [i.e., the new bagging system] 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 [22,500 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.

4. If Carborundum had shipped the full minimum quantity that it guaranteed, it would have owed Lake River roughly \$533,000 under the contract.
5. After the contract was signed in 1979, the demand for domestic steel, and with it the demand for Ferro Carbo, plummeted, and Carborundum failed to ship the guaranteed amount. When the contract expired late in 1982, Carborundum had shipped only 12,000 of the 22,500 tons it had guaranteed. Lake River had bagged the 12,000 tons

and had billed Carborundum for this bagging, and Carborundum had paid, but by virtue of the formula in the minimum-guarantee clause Carborundum still owed Lake River \$241,000—the contract price of \$533,000 if the full amount of Ferro Carbo had been shipped, minus what Carborundum had paid for the bagging of the quantity it had shipped.

6. When Lake River demanded payment of this amount, Carborundum refused, on the ground that the formula imposed a penalty. At the time, Lake River had in its warehouse 500 tons of bagged Ferro Carbo, having a market value of \$269,000, which it refused to release unless Carborundum paid the \$241,000 due under the formula. Lake River did offer to sell the bagged product and place the proceeds in escrow until its dispute with Carborundum over the enforceability of the formula was resolved, but Carborundum rejected the offer and trucked in bagged Ferro Carbo from the East to serve its customers in Illinois, at an additional cost of \$31,000.
7. Lake River brought this suit for \$241,000, which it claims as liquidated damages. Carborundum counterclaimed for the value of the bagged Ferro Carbo when Lake River impounded it and the additional cost of serving the customers affected by the impounding. The theory of the counterclaim is that the impounding was a conversion, and not as Lake River contends the assertion of a lien. The district judge, after a bench trial, gave judgment for both parties. Carborundum ended up roughly \$42,000 to the good: $\$269,000 + \$31,000 - \$241,000 - \$17,000$, the last figure representing prejudgment interest on Lake River's damages. (We have rounded off all dollar figures to the nearest thousand.) Both parties have appealed.
8. The only issue that is not one of damages is whether Lake River had a valid lien on the bagged Ferro Carbo that it refused to ship to Carborundum's customers—that, indeed, it holds in its warehouse to this day. Although Ferro Carbo does not deteriorate with age, the domestic steel industry remains in the doldrums and the product is worth less than it was in 1982 when Lake River first withheld it. If Lake River did not have a valid lien on the product, then it converted it, and must pay Carborundum the \$269,000 that the Ferro Carbo was worth back then.
9. It might seem that if the minimum-guarantee clause was a penalty clause and hence unenforceable, the lien could not be valid, and therefore that we should discuss the penalty issue first. But this is not correct. If the contractual specification of damages is invalid, Lake River still is entitled to any actual damages caused by Carborundum's

breach of contract in failing to deliver the minimum amount of Ferro Carbo called for by the contract. The issue is whether an entitlement to damages, large or small, entitles the victim of the breach to assert a lien on goods that are in its possession though they belong to the other party.

10. Lake River has not been very specific about the type of lien it asserts. We think it best described as a form of artisan's lien, the “lien of the bailee, who does work upon or adds materials to chattels....” Restatement of Security § 61, comment on clause (a), at p. 165 (1941). Lake River was the bailee of the Ferro Carbo that Carborundum delivered to it, and it did work on the Ferro Carbo—bagging it, and also storing it (storage is a service, too). If Carborundum had refused to pay for the services that Lake River performed on the Ferro Carbo delivered to it, then Lake River would have had a lien on the Ferro Carbo in its possession, to coerce payment. Cf. *National Bank of Joliet v. Bergeron Cadillac, Inc.*, 66 Ill.2d 140, 143-44, 5 Ill. Dec. 588, 589, 361 N.E.2d 1116, 1117 (1977). But in fact, when Lake River impounded the bagged Ferro Carbo, Carborundum had paid in full for all bagging and storage services that Lake River had performed on Ferro Carbo shipped to it by Carborundum. The purpose of impounding was to put pressure on Carborundum to pay for services not performed, Carborundum having failed to ship the Ferro Carbo on which those services would have been performed.
11. Unlike a contractor who, having done the work contracted for without having been paid, may find himself in a box, owing his employees or suppliers money he does not have—money he was counting on from his customer—Lake River was the victim of a breach of a portion of the contract that remained entirely unexecuted on either side. Carborundum had not shipped the other 10,500 tons, as promised; but on the other hand Lake River had not had to bag those 10,500 tons, as it had promised. It is not as if Lake River had bagged those tons, incurring heavy costs that it expected to recoup from Carborundum, and then Carborundum had said, “Sorry, we won't pay you; go ahead and sue us.”
12. A lien is strong medicine; it clogs up markets, as the facts of this case show. Its purpose is to provide an effective self-help remedy for one who has done work in expectation of payment and then is not paid. The vulnerable position of such a person gives rise to “the artisan's privilege of holding the balance for *work done in the past.*” *United States v. Toys of the World Club, Inc.*, 288 F.2d 89, 94 (2d Cir.1961) (Friendly, J.) (emphasis added). A lien is thus a device for preventing unjust

enrichment—not for forcing the other party to accede to your view of a contract dispute. “The right to retain possession of the property to enforce a possessory lien continues until such time as the charges for such materials, labor and services are paid.” *Bull v. Mitchell*, 448 N.E.2d 1016, 1019 (Ill. App. 1983); cf. Ill.Rev.Stat. ch. 82, § 40. Since here the charges were paid before the lien was asserted, the lien was no good.

13. Lake River tries to compare its position to that of a conventional lien creditor by pointing out that it made itself particularly vulnerable to a breach of contract by buying specialized equipment at Carborundum's insistence, to the tune of \$89,000, before performance under the contract began. It says it insisted on the minimum guarantee in order to be sure of being able to amortize this equipment over a large enough output of bagging services to make the investment worthwhile. But the equipment was not completely useless for other contracts—Lake River having in fact used it for another contract; it was not the major cost of fulfilling the contract; and Lake River received almost \$300,000 during the term of the contract, thus enabling it to amortize much of the cost of the special equipment. Although Lake River may have lost money on the contract (but as yet there is no proof it did), it was not in the necessitous position of a contractor who completes his performance without receiving a dime and then is told by his customer to sue for the price. The recognition of a lien in such a case is based on policies akin to those behind the rule that a contract modification procured by duress will not be enforced. See, e.g., *Selmer Co. v. Blakeslee-Midwest Co.*, 704 F.2d 924 (7th Cir.1983). When as a practical matter the legal remedy may be inadequate because it operates too slowly, self-help is allowed. But we can find no case recognizing a lien on facts like these, no ground for thinking that the Illinois Supreme Court would be the first court to recognize such a lien if this case were presented to it, and no reason to believe that the recognition of such a lien would be a good thing. It would impede the marketability of goods without responding to any urgent need of creditors.
14. *Conrow v. Little*, 22 N.E. 346, 347 (N.Y. 1889), on which Lake River relies heavily because the lien allowed in that case extended to “money expended in the preparation of instrumentalities,” is not in point. The plaintiffs, dealers in paper, had made extensive deliveries to the defendants for which they had received no payment. See *id.* at 390-91, 22 N.E. at 346. If Lake River had bagged several thousand tons of Ferro Carbo without being paid anything, it would have had a lien on the Ferro Carbo; and maybe—if *Conrow* is good law in Illinois, a question we need not try to answer—the

lien would have included not only the contract price for the Ferro Carbo that Lake River had bagged but also the unreimbursed, unsalvageable cost of the special bagging system that Lake River had installed. But that is not this case. Carborundum was fully paid up and Lake River has made no effort to show how much if any money it stood to lose because the bagging system was not fully amortized. The only purpose of the lien was to collect damages which would have been unrelated to—and certainly exceeded—the investment in the bagging system.

15. It is no answer that the bagging system should be presumed to have been amortized equally over the life of the contract, and therefore to have been only half amortized when Carborundum broke the contract. Amortization is an accounting device; it need not reflect cash flows. There is no evidence that when the contract was broken, Lake River was out of pocket a cent in respect of the bagging system, especially when we consider that the bagging system was still usable, and was used to fulfill another contract.
16. The hardest issue in the case is whether the formula in the minimum-guarantee clause imposes a penalty for breach of contract or is merely an effort to liquidate damages. Deep as the hostility to penalty clauses runs in the common law, see Loyd, *Penalties and Forfeitures*, 29 HARV. L. REV. 117 (1915), we still might be inclined to question, if we thought ourselves free to do so, whether a modern court should refuse to enforce a penalty clause where the signator is a substantial corporation, well able to avoid improvident commitments. Penalty clauses provide an earnest of performance. The clause here enhanced Carborundum's credibility in promising to ship the minimum amount guaranteed by showing that it was willing to pay the full contract price even if it failed to ship anything. On the other side it can be pointed out that by raising the cost of a breach of contract to the contract breaker, a penalty clause increases the risk to his other creditors; increases (what is the same thing and more, because bankruptcy imposes “deadweight” social costs) the risk of bankruptcy; and could amplify the business cycle by increasing the number of bankruptcies in bad times, which is when contracts are most likely to be broken. But since little effort is made to prevent businessmen from assuming risks, these reasons are no better than makeweights.
17. A better argument is that a penalty clause may discourage efficient as well as inefficient breaches of contract. Suppose a breach would cost the promisee \$12,000 in actual damages but would yield the promisor \$20,000 in additional profits. Then there would be a net social gain from breach. After being fully compensated for his loss the

promisee would be no worse off than if the contract had been performed, while the promisor would be better off by \$8,000. But now suppose the contract contains a penalty clause under which the promisor if he breaks his promise must pay the promisee \$25,000. The promisor will be discouraged from breaking the contract, since \$25,000, the penalty, is greater than \$20,000, the profits of the breach; and a transaction that would have increased value will be forgone.

18. On this view, since compensatory damages should be sufficient to deter inefficient breaches (that is, breaches that cost the victim more than the gain to the contract breaker), penal damages could have no effect other than to deter some efficient breaches. But this overlooks the earlier point that the willingness to agree to a penalty clause is a way of making the promisor and his promise credible and may therefore be essential to inducing some value-maximizing contracts to be made. It also overlooks the more important point that the parties (always assuming they are fully competent) will, in deciding whether to include a penalty clause in their contract, weigh the gains against the costs—costs that include the possibility of discouraging an efficient breach somewhere down the road—and will include the clause only if the benefits exceed those costs as well as all other costs.
19. On this view the refusal to enforce penalty clauses is (at best) paternalistic—and it seems odd that courts should display parental solicitude for large corporations. But however this may be, we must be on guard to avoid importing our own ideas of sound public policy into an area where our proper judicial role is more than usually deferential. The responsibility for making innovations in the common law of Illinois rests with the courts of Illinois, and not with the federal courts in Illinois. And like every other state, Illinois, untroubled by academic skepticism of the wisdom of refusing to enforce penalty clauses against sophisticated promisors, *see, e.g.,* Goetz & Scott, *Liquidated Damages, Penalties and the Just Compensation Principle*, 77 COLUM. L. REV. 554 (1977), continues steadfastly to insist on the distinction between penalties and liquidated damages. *See, e.g.,* *Bauer v. Sawyer*, 134 N.E.2d 329, 333-34 (Ill. 1956); *Stride v. 120 West Madison Bldg. Corp.*, 477 N.E.2d 1318, 1321 (Ill. App. 1985); *Builder's Concrete Co. v. Fred Faubel & Sons, Inc.*, 373 N.E.2d 863, 869 (Ill. App. 1978). 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 the 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. See, e.g., *M.I.G. Investments, Inc. v. Marsala*, 414 N.E.2d 1381, 1386 (Ill. App. 1981).
20. The distinction between a penalty and liquidated damages is not an easy one to draw in practice but we are required to draw it and can give only limited weight to the district court's determination. Whether a provision for damages is a penalty clause or a liquidated-damages clause is a question of law rather than fact, *Weiss v. United States Fidelity & Guaranty Co.*, 132 N.E. 749, 751 (Ill. 1921); *M.I.G. Investments, Inc. v. Marsala*, *supra*, 414 N.E.2d 1381, 1386, and unlike some courts of appeals we do not treat a determination by a federal district judge of an issue of state law as if it were a finding of fact, and reverse only if persuaded that clear error has occurred, though we give his determination respectful consideration. See, e.g., *Morin Bldg. Products Co. v. Baystone Construction, Inc.*, 717 F.2d 413, 416-17 (7th Cir.1983); *In re Air Crash Disaster Near Chicago*, 701 F.2d 1189, 1195 (7th Cir.1983); 19 WRIGHT, MILLER & COOPER, FEDERAL PRACTICE AND PROCEDURE § 4507, at pp. 106-110 (1982).
21. Mindful that Illinois courts resolve doubtful cases in favor of classification as a penalty, see, e.g., *Stride v. 120 West Madison Bldg. Corp.*, *supra*, 477 N.E.2d at 1321; *Pick Fisheries, Inc. v. Burns Electronic Security Services, Inc.*, 342 N.E.2d 105, 108 (Ill. App. 1976), 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 formula—full contract price minus the amount already invoiced to Carborundum—is invariant to the gravity of the breach. When a contract specifies a single sum in damages for any and all breaches even though it is apparent that all are not of the same gravity, the specification is not a reasonable effort to estimate damages; and when in addition the fixed sum greatly exceeds the actual damages likely to be inflicted by a minor breach, its character as a penalty becomes unmistakable. See *M.I.G. Investments, Inc. v. Marsala*, *supra*, 414 N.E.2d at 1386; cf. *Arduini v. Board of Educ.*, 418 N.E.2d 104, 109-10 (Ill. App. 1981), *rev'd on other grounds*, 441 N.E.2d 73 (Ill. 1982); 5 CORBIN ON CONTRACTS § 1066 (1964). This case is within the gravitational field of these principles even though the minimum-guarantee clause does not fix a single sum as damages.
22. Suppose to begin with that the breach occurs the day after Lake River buys its new bagging system for \$89,000 and before Carborundum ships any Ferro Carbo. Carborundum would owe Lake River \$533,000. Since Lake River would have

incurred at that point a total cost of only \$89,000, its net gain from the breach would be \$444,000. This is more than four times the profit of \$107,000 (20 percent of the contract price of \$533,000) that Lake River expected to make from the contract if it had been performed: a huge windfall.

23. Next suppose (as actually happened here) that breach occurs when 55 percent of the Ferro Carbo has been shipped. Lake River would already have received \$293,000 from Carborundum. To see what its costs then would have been (as estimated at the time of contracting), first subtract Lake River's anticipated profit on the contract of \$107,000 from the total contract price of \$533,000. The difference—Lake River's total cost of performance—is \$426,000. Of this, \$89,000 is the cost of the new bagging system, a fixed cost. The rest ($\$426,000 - \$89,000 = \$337,000$) presumably consists of variable costs that are roughly proportional to the amount of Ferro Carbo bagged; there is no indication of any other fixed costs. Assume, therefore, that if Lake River bagged 55 percent of the contractually agreed quantity, it incurred in doing so 55 percent of its variable costs, or \$185,000. When this is added to the cost of the new bagging system, assumed for the moment to be worthless except in connection with the contract, the total cost of performance to Lake River is \$274,000. Hence a breach that occurred after 55 percent of contractual performance was complete would be expected to yield Lake River a modest profit of \$19,000 ($\$293,000 - \$274,000$). But now add the “liquidated damages” of \$241,000 that Lake River claims, and the result is a total gain from the breach of \$260,000, which is almost two and a half times the profit that Lake River expected to gain if there was no breach. And this ignores any use value or salvage value of the new bagging system, which is the property of Lake River—though admittedly it also ignores the time value of money; Lake River paid \$89,000 for that system before receiving any revenue from the contract.
24. To complete the picture, assume that the breach had not occurred till performance was 90 percent complete. Then the “liquidated damages” clause would not be so one-sided, but it would be one-sided. Carborundum would have paid \$480,000 for bagging. Against this, Lake River would have incurred its fixed cost of \$89,000 plus 90 percent of its variable costs of \$337,000, or \$303,000. Its total costs would thus be \$392,000, and its net profit \$88,000. But on top of this it would be entitled to “liquidated damages” of \$53,000, for a total profit of \$141,000—more than 30 percent more than its expected profit of \$107,000 if there was no breach.

25. The reason for these results is that most of the costs to Lake River of performing the contract are saved if the contract is broken, and this saving is not reflected in the damage formula. As a result, at whatever point in the life of the contract a breach occurs, the damage formula gives Lake River more than its lost profits from the breach—dramatically more if the breach occurs at the beginning of the contract; tapering off at the end, it is true. Still, over the interval between the beginning of Lake River's performance and nearly the end, the clause could be expected to generate profits ranging from 400 percent of the expected contract profits to 130 percent of those profits. And this is on the assumption that the bagging system has no value apart from the contract. If it were worth only \$20,000 to Lake River, the range would be 434 percent to 150 percent.
26. Lake River argues that it would never get as much as the formula suggests, because it would be required to mitigate its damages. This is a dubious argument on several grounds. First, mitigation of damages is a doctrine of the law of court-assessed damages, while the point of a liquidated-damages clause is to substitute party assessment; and that point is blunted, and the certainty that liquidated-damages clauses are designed to give the process of assessing damages impaired, if a defendant can force the plaintiff to take less than the damages specified in the clause, on the ground that the plaintiff could have avoided some of them. It would seem therefore that the clause in this case should be read to eliminate any duty of mitigation, that what Lake River is doing is attempting to rewrite the clause to make it more reasonable, and that since actually the clause is designed to give Lake River the full damages it would incur from breach (and more) even if it made no effort to find a substitute use for the equipment that it bought to perform the contract, this is just one more piece of evidence that it is a penalty clause rather than a liquidated-damages clause. See *Northwest Collectors, Inc. v. Enders*, 446 P.2d 200, 206 (Wash. 1968).
27. But in any event mitigation would not mitigate the penal character of this clause. If Carborundum did not ship the guaranteed minimum quantity, the reason was likely to be—the reason was—that the steel industry had fallen on hard times and the demand for Ferro Carbo was therefore down. In these circumstances Lake River would have little prospect of finding a substitute contract that would yield it significant profits to set off against the full contract price, which is the method by which it proposes to take account of mitigation. At argument Lake River suggested that it might at least have been able to sell the new bagging equipment to someone for something, and the figure \$40,000 was proposed. If the breach occurred on the first day when

performance under the contract was due and Lake River promptly sold the bagging equipment for \$40,000, its liquidated damages would fall to \$493,000. But by the same token its costs would fall to \$49,000. Its profit would still be \$444,000, which as we said was more than 400 percent of its expected profit on the contract. The penal component would be unaffected.

28. With the penalty clause in this case compare the liquidated-damages clause in *Arduini v. Board of Education, supra*, which is representative of such clauses upheld in Illinois. The plaintiff was a public school teacher whose contract provided that if he resigned before the end of the school year he would be docked 4 percent of his salary. This was a modest fraction of the contract price. And the cost to the school of an untimely resignation would be difficult to measure. Since that cost would be greater the more senior and experienced the teacher was, the fact that the liquidated damages would be greater the higher the teacher's salary did not make the clause arbitrary. Even the fact that the liquidated damages were the same whether the teacher resigned at the beginning, the middle, or the end of the school year was not arbitrary, for it was unclear how the amount of actual damages would vary with the time of resignation. Although one might think that the earlier the teacher resigned the greater the damage to the school would be, the school might find it easier to hire a replacement for the whole year or a great part of it than to bring in a replacement at the last minute to grade the exams left behind by the resigning teacher. Here, in contrast, it is apparent from the face of the contract that the damages provided for by the “liquidated damages” clause are grossly disproportionate to any probable loss and penalize some breaches much more heavily than others regardless of relative cost.
29. We do not mean by this discussion to cast a cloud of doubt over the “take or pay” clauses that are a common feature of contracts between natural gas pipeline companies and their customers. Such clauses require the customer, in consideration of the pipeline's extending its line to his premises, to take a certain amount of gas at a specified price—and if he fails to take it to pay the full price anyway. The resemblance to the minimum-guarantee clause in the present case is obvious, but perhaps quite superficial. Neither party has mentioned take-or-pay clauses, and we can find no case where such a clause was even challenged as a penalty clause—though in one case it was argued that such a clause made the damages unreasonably low. See *National Fuel Gas Distribution Corp. v. Pennsylvania Public Utility Comm'n*, 464 A.2d 546, 558 n. 8 (Pa. Comm.1983). If, as appears not to be the case here but would often be the case in supplying natural gas, a supplier's fixed costs

were a very large fraction of his total costs, a take-or-pay clause might well be a reasonable liquidation of damages. In the limit, if *all* the supplier's costs were incurred before he began supplying the customer, the contract revenues would be an excellent measure of the damages from breach. But in this case, the supplier (Lake River, viewed as a supplier of bagging services to Carborundum) incurred only a fraction of its costs before performance began, and the interruption of performance generated a considerable cost saving that is not reflected in the damage formula.

30. The fact that the damage formula is invalid does not deprive Lake River of a remedy. The parties did not contract explicitly with reference to the measure of damages if the agreed-on damage formula was invalidated, but all this means is that the victim of the breach is entitled to his common law damages. See, e.g., Restatement, Second, Contracts § 356, comment a (1981). In this case that would be the unpaid contract price of \$241,000 minus the costs that Lake River saved by not having to complete the contract (the variable costs on the other 45 percent of the Ferro Carbo that it never had to bag). The case must be remanded to the district judge to fix these damages.
31. Two damage issues remain. The first concerns Carborundum's expenses of delivering bagged Ferro Carbo to its customers to replace that impounded by Lake River. The district judge gave Carborundum the full market value of the bagged Ferro Carbo. Lake River argues that it should not have to pay for Carborundum's expense of selling additional Ferro Carbo—additional in the sense that Carborundum is being given credit for the full retail value of the product that Lake River withheld. To explain, suppose that Carborundum had an order for \$1,000 worth of bagged Ferro Carbo, which Lake River was supposed to deliver; and because it refused, Carborundum incurred a transportation cost of \$100 to make a substitute shipment of bagged Ferro Carbo to the customer. Carborundum would still get \$1,000 from the customer, and if that price covered the transportation cost it would still make a profit. In what sense, therefore, is that cost a separate item of damage, of loss? On all Ferro Carbo (related to this case) sold by Carborundum in the Midwest, Carborundum received the full market price, either from its customers in the case of Ferro Carbo actually delivered to them, or from Lake River in the case of the Ferro Carbo that Lake River refused to deliver. Having received a price designed to cover all expenses of sale, a seller cannot also get an additional damage award for any of those expenses.
32. If, however, the additional Ferro Carbo that Carborundum delivered to its midwestern customers in substitution for Ferro Carbo previously delivered to, and impounded by,

Lake River would have been sold in the East at the same price but lower cost, Carborundum would have had an additional loss, in the form of reduced profits, for which it could recover additional damages. But it made no effort to prove such a loss. Maybe it had no unsatisfied eastern customers, and expanded rather than shifted output to fulfill its midwestern customers' demand. The damages on the counterclaim must be refigured also.

33. Finally, Lake River argues that Carborundum failed to mitigate its damages by accepting Lake River's offer to deliver the bagged product and place the proceeds in escrow. But a converter is not entitled to retain the proceeds of the conversion even temporarily. Lake River had an opportunity to limit its exposure by selling the bagged product on Carborundum's account and deducting what it claimed was due it on its "lien." Its failure to follow this course reinforces our conclusion that the assertion of the lien was a naked attempt to hold Carborundum hostage to Lake River's view—an erroneous view, as it has turned out—of the enforceability of the damage formula in the contract.
34. The judgment of the district court is affirmed in part and reversed in part, and the case is returned to that court to redetermine both parties' damages in accordance with the principles in this opinion. The parties may present additional evidence on remand, and shall bear their own costs in this court. Circuit Rule 18 shall not apply on remand.

California and Hawaiian Sugar Co. v. Sun Ship, Inc.

United States Court of Appeals for the Ninth Circuit
794 F.2d 1433 (1986)

NOONAN, Circuit Judge.

1. Jurisdiction in this case is based on the diversity of citizenship of California and Hawaiian Sugar company (C and H), a California corporation; Sun Ship, Inc. (Sun), a Pennsylvania corporation; and Halter Marine, Inc. (Halter), a Louisiana corporation. Interpreting a contract which provides for construction by the law of Pennsylvania, we apply Pennsylvania law. The appeal is from a judgment of the district court in favor of C and H and Halter on the main issues. Reviewing the district court's interpretation of the contract anew as a matter of law and respecting the findings of fact of the district court when not clearly erroneous, we affirm the judgment in all respects.

BACKGROUND

2. C and H is an agricultural cooperative owned by fourteen sugar plantations in Hawaii. Its business consists in transporting raw sugar—the crushed cane in the form of coarse brown crystal—to its refinery in Crockett, California. Roughly one million tons a year of sugar are harvested in Hawaii. A small portion is refined there; the bulk goes to Crockett. The refined sugar—the white stuff—is sold by C and H to groceries for home consumption and to the soft drink and cereal companies that are its industrial customers.
3. To conduct its business, C and H has an imperative need for assured carriage for the raw sugar from the islands. Sugar is a seasonal crop, with 70 percent of the harvest occurring between April and October, while almost nothing is harvestable during December and January. Consequently, transportation must not only be available, but seasonably available. Storage capacity in Hawaii accommodates not more than a quarter of the crop. Left stored on the ground or left unharvested, sugar suffers the loss of sucrose and goes to waste. Shipping ready and able to carry the raw sugar is a priority for C and H.
4. In 1979 C and H was notified that Matson Navigation Company, which had been supplying the bulk of the necessary shipping, was withdrawing its services as of

January 1981. While C and H had some ships at its disposal, it found a pressing need for a large new vessel, to be in service at the height of the sugar season in 1981. It decided to commission the building of a kind of hybrid—a tug of catamaran design with two hulls and, joined to the tug, a barge with a wedge which would lock between the two pontoons of the tug, producing an “integrated tug barge.” In Hawaiian, the barge and the entire vessel were each described as a Mocababoo or push boat.

5. C and H relied on the architectural advice of the New York firm, J.J. Henry. It solicited bids from shipyards, indicating as an essential term a “preferred delivery date” of June 1981. It decided to accept Sun's offer to build the barge and Halter's offer to build the tug.
6. In the fall of 1979 C and H entered into negotiations with Sun on the precise terms of the contract. Each company was represented by a vice-president with managerial responsibility in the area of negotiation; each company had a team of negotiators; each company had the advice of counsel in drafting the agreement that was signed on November 14, 1979. This agreement was entitled “Contract for the Construction of One Oceangoing Barge for California and Hawaiian Sugar Company By Sun Ship, Inc.” The “Whereas” clause of the contract identified C and H as the Purchaser, and Sun as the Contractor; it identified “one non-self-propelled oceangoing barge” as the Vessel that Purchaser was buying from Contractor. Article I provided that Contractor would deliver the Vessel on June 30, 1981. The contract price was \$25,405,000.
7. Under Article I of the agreement, Sun was entitled to an extension of the delivery date for the usual types of force majeure and for “unavailability of the Tug to Contractor for joining to the Vessel, where it is determined that Contractor has complied with all obligations under the Interface Agreement.” (The Interface Agreement, executed the same day between C and H, Sun, and Halter provided that Sun would connect the barge with the tug.) Article 17 “Delivery” provided that “the Vessel shall be offered for delivery fully and completely connected with the Tug.” Article 8, “Liquidated Damages for Delay in Delivery” provided that if “Delivery of the Vessel” was not made on “the Delivery Date” of June 30, 1981, Sun would pay C and H “as per-day liquidated damages, and not as a penalty” a sum described as “a reasonable measure of the damages”—\$17,000 per day.
8. On the same date C and H entered into an agreement with Halter to purchase “one oceangoing catamaran tug boat” for \$20,350,000. The tug (the “Vessel” of that

contract) was to be delivered on April 30, 1981 at Sun's shipyard. Liquidated damages of \$10,000 per day were provided for Halter's failure to deliver.

9. Halter did not complete the tug until July 15, 1982. Sun did not complete the barge until March 16, 1982. Tug and barge were finally connected under C and H's direction in mid-July 1982 and christened the Moku Pahu. C and H settled its claim against Halter. Although Sun paid C and H \$17,000 per day from June 30, 1981 until January 10, 1982, it ultimately denied liability for any damages, and this lawsuit resulted.

ANALYSIS

10. Sun contends that its obligation was to deliver the barge connected to the tug on the delivery date of June 30, 1981 and that only the failure to deliver the integrated hybrid would have triggered the liquidated damage clause. It is true that Article 17 creates some ambiguity by specifying that the Vessel is to be “offered for delivery completely connected with the Tug.” The case of the barge being ready while the tug was not, is not explicitly considered. Nonetheless, the meaning of “Vessel” is completely unambiguous. From the “Whereas” clause to the articles of the agreement dealing with insurance, liens, and title, “the Vessel” is the barge. It would require the court to rewrite the contract to find that “the Vessel” in Article 8 on liquidated damages does not mean the barge. The article takes effect on failure to deliver “the Vessel”—that is, the barge.
11. Sun contends, however, that on such a reading of the contract, the \$17,000 per day is a penalty, not to be enforced by the court. The barge, Sun points out, was useless to C and H without the tug. Unconnected, the barge was worse than useless—it was an expensive liability. C and H did not want the barge by itself. To get \$17,000 per day as “damages” for failure to provide an unwanted and unusable craft is, Sun says, to exact a penalty. C and H seeks to be “paid according to the tenour of the bond”; it “craves the law.” And if C and H sticks to the letter of the bond, it must like Shylock end by losing; a court of justice will not be so vindictive. Breach of contract entitles the wronged party only to fair compensation.
12. Seductive as Sun's argument is, it does not carry the day. Represented by sophisticated representatives, C and H and Sun reached the agreement that \$17,000 a day was the reasonable measure of the loss C and H would suffer if the barge was not ready. Of course they assumed that the tug would be ready. But in reasonable

anticipation of the damages that would occur if the tug was ready and the barge was not, Article 8 was adopted. As the parties foresaw the situation, C and H would have a tug waiting connection but no barge and so no shipping. The anticipated damages were what might be expected if C and H could not transport the Hawaiian sugar crop at the height of the season. Those damages were clearly before both parties. As Joe Kleschick, Sun's chief negotiator, testified, he had “a vision” of a “mountain of sugar piling up in Hawaii”—a vision that C and H conjured up in negotiating the damage clause. Given the anticipated impact on C and H's raw sugar and on C and H's ability to meet the demands of its grocery and industrial customers if the sugar could not be transported, liquidated damages of \$17,000 a day were completely reasonable.

13. The situation as it developed was different from the anticipation. The barge was not ready but neither was the tug. C and H was in fact able to find other shipping. The crop did not rot. The customers were not left sugarless. Sun argues that, measured by the actual damages suffered, the liquidated damages were penal.
14. We look to Pennsylvania law for guidance. Although no Pennsylvania case is squarely on point, it is probable that Pennsylvania would interpret the contract as a sale of goods governed by the Uniform Commercial Code. *Belmont Industries, Inc. v. Bechtel Corp.*, 425 F. Supp. 524, 527 (E.D.Pa.1976). The governing statute provides that liquidated damages are considered reasonable “in the light of anticipated or actual harm.” 12A Pa. Cons. Stat. Ann. 2-718(1) (Purdon 1970) (Pennsylvania's adoption of the Uniform Commercial Code).
15. The choice of the disjunctive appears to be deliberate. The language chosen is in harmony with the Restatement (Second) of Contracts § 356 (1979), which permits liquidated damages in the light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss. Section 356, Comment b declares explicitly: “Furthermore, the amount fixed is reasonable to the extent that it approximates the loss anticipated at the time of the making of the contract, even though it may not approximate the actual loss.”
16. Despite the statutory disjunctive and the Restatement's apparent blessing of it, the question is not settled by these authorities which must be read in the light of common law principles already established and accepted in Pennsylvania. *Carpel v. Saget Studios, Inc.*, 326 F. Supp. 1331, 1333 (E.D. Pa.1971); 13 Pa. C.S.A. § 1103. Prior to the adoption of the Uniform Commercial Code, Pennsylvania enforced liquidated

damage clauses that its courts labeled as nonpenal, but equitable considerations relating to the actual harm incurred were taken into account along with the difficulty of proving damages if a liquidated damage clause was rejected, e.g. *Emery v. Boyle*, 200 Pa. 249, 49 A. 779 (1901). We do not believe that the *U.C.C.* overrode this line of reasoning. Indeed, in a lower court case, decided after the *U.C.C.*'s enactment, it was stated that if liquidated damages appear unreasonable in light of the harm suffered, “the contractual provision will be voided as a penalty.” *Unit Vending Corp. v. Tobin Enterprises*, 194 Pa. Super. 470, 473, 168 A.2d 750, 751 (1961). That case, however, is not on all fours with our case: *Unit Vending* involved an adhesion contract between parties of unequal bargaining power; the unfair contract was characterized by the court as “a clever attempt to secure both the penny and the cake” by the party with superior strength. *Id.* at 476, 168 A.2d at 753. Mechanically to read it as Pennsylvania law governing this case would be a mistake. The case, however, does show that Pennsylvania courts, like courts elsewhere, attempt to interpret the governing statute humanely and equitably.

17. The Restatement § 356 Comment b, after accepting anticipated damages as a measure, goes on to say that if the difficulty of proof of loss is slight, then actual damage may be the measure of reasonableness: “If, to take an extreme case, it is clear that no loss at all has occurred, a provision fixing a substantial sum as damages is unenforceable. See Illustration 4.” Illustration 4 is a case of a contractor, A, agreeing to build B's race track by a specific date and to pay B \$1,000 a day for every day's delay. A delays a month, but B does not get permission to operate the track for that month, so B suffers no loss. In that event, the Restatement characterizes the \$1,000 per day as an unenforceable penalty. Sun contends that it is in the position of A: no actual loss was suffered by C and H because C and H had no tug to mate with the barge.
18. This argument restates in a new form Sun's basic contention that the liquidated damage clause was meant to operate only if the integrated tug barge was not delivered. The argument has been rejected by us as a misinterpretation of the contract. But in its new guise it gains appeal. If Illustration 4 is the present case, Sun is home scot-free. The Restatement, however, deals with a case where the defaulting contractor was alone in his default. We deal with a case of concurrent defaults. If we were to be so literal-minded as to follow the Restatement here, we would have to conclude that because both parties were in default, C and H suffered no damage until one party performed. Not until the barge was ready in March 1982 could C and H

hold Halter for damages, and then only for the period after that date. The continued default of both parties would operate to take each of them off the hook. That cannot be the law.

19. Sun objects that Halter had a more absolute obligation to deliver than Sun did. Halter did not have to deliver the integrated tug, only the tug itself; it was not excused by Sun's default. Hence the spectacle of two defaulting contractors causing no damages would not be presented here. But Sun's objection does not meet the point that Halter's unexcused delivery would, on Sun's theory, have generated no damages. The tug by itself would have been no use to C and H.
20. We conclude, therefore, that in this case of concurrent causation each defaulting contractor is liable for the breach and for the substantial damages which the joint breach occasions. Sun is a substantial cause of the damages flowing from the lack of the integrated tug; Sun cannot be absolved by the absence of the tug.
21. Sun has a final argument. Even on the assumption that it is liable as a substantial cause of the breach of contract, Sun contends that the actual damages suffered by C and H for lack of the integrated tug boat were slight. Actual damages were found by the district court to consist of "interest on progress payments, unfavorable terms of conversion to long-term financing, and additional labor expense." No dollar amount was determined by the district court in finding that these damages "bore a reasonable relationship to the amount liquidated in the Barge Contract."
22. The dollar value of the damages found by the district judge is, to judge from C and H's own computation, as follows:

| | |
|----------------------------------|-------------|
| Additional Construction Interest | \$1,486,000 |
| Added Payments to J.J. Henry | 161,000 |
| Added Vessel Operating Expenses | 73,000 |
| C and H Employee Costs | 109,000 |
| TOTAL | \$1,829,000 |

But "actual damages" have no meaning if the actual savings of C and H due to the nondelivery of the integrated tug barge are not subtracted. It was clearly erroneous for

the district judge to exclude these savings from his finding. These savings, again according to C and H's own computation, were:

| | |
|------------------------|-------------|
| Transportation savings | \$525,000 |
| Lay-up costs | \$936,000 |
| TOTAL | \$1,461,000 |

The net actual damages suffered by C and H were \$368,000. As a matter of law, Sun contends that the liquidated damages are unreasonably disproportionate to the net actual damages.

23. C and H urges on us the precedent of *Bellefonte Borough Authority v. Gateway Equipment & Supply Co.*, 442 Pa. 492, 277 A.2d 347 (1971), forfeiting a bid bond of \$45,000 on the failure of a contractor to perform a municipal contract, even though the loss to the municipality was \$1,000; the disproportion was 45 to 1. But that decision is not decisive here. It did not purport to apply the Uniform Commercial Code. Rules appropriate for bids to the government are sufficiently different from those applicable between private parties to prevent instant adoption of this precedent. A fuller look at relevant contract law is appropriate.
24. Litigation has blurred the line between a proper and a penal clause, and the distinction is “not an easy one to draw in practice.” *Lake River Corp. v. Carborundum Co.*, 769 F.2d 1284, 1290 (7th Cir.1985) (per Posner, J.). But the desire of courts to avoid the enforcement of penalties should not obscure common law principles followed in Pennsylvania. Contracts are contracts because they contain enforceable promises, and absent some overriding public policy, those promises are to be enforced. “Where each of the parties is content to take the risk of its turning out in a particular way” why should one “be released from the contract, if there were no misrepresentation or other want of fair dealing?” *Ashcom v. Smith*, 2 Pen. & W. 211, 218-219 (Pa. 1830) (per Gibson, C.J.). Promising to pay damages of a fixed amount, the parties normally have a much better sense of what damages can occur. Courts must be reluctant to override their judgment. Where damages are real but difficult to prove, injustice will be done the injured party if the court substitutes the requirements of judicial proof for the parties' own informed agreement as to what is a reasonable measure of damages. Pennsylvania acknowledges that a seller is bound to pay consequential damages if the seller had reason to know of the buyer's special circumstances. *Keystone Diesel*

Engine Co. v. Irwin, 411 Pa. 222, 191 A.2d 376 (1963). The liquidated damage clause here functions in lieu of a court's determination of the consequential damages suffered by C and H.

25. These principles inform a leading common law case in the field, *Clydebank Engineering & Shipbuilding Co. v. Yzquierdo y Castaneda*, 1905 A.C. 6. The defendant shipyard had agreed to pay 500 pounds per week per vessel for delay in the delivery of four torpedo boat destroyers to the Spanish Navy in 1897. The shipyard pointed out that had the destroyers been delivered on schedule they would have been sunk with the rest of the Spanish Navy by the Americans in 1898. The House of Lords found the defense unpersuasive. To prove damages the whole administration of the Spanish Navy would have had to have been investigated. The House of Lords refused to undertake such a difficult investigation when the parties had made an honest effort in advance to set in monetary terms what the lack of the destroyers would mean to Spain.
26. C and H is not the Spanish Navy, but the exact damages caused its manifold operations by lack of the integrated tug boat are equally difficult of ascertainment. C and H claimed that it suffered \$3,732,000 in lost charter revenues. Testimony supported the claim, but the district court made no finding as to whether the claim was proved or unproved. The district court did find that the loss of charter revenues had not been anticipated by the parties. But that finding has no bearing on whether the loss occurred. Within the general risk of heavy losses forecast by both parties when they agreed to \$17,000 per day damages, a particular type of loss was pointed to by C and H as having happened.
27. Proof of this loss is difficult—as difficult, perhaps, as proof of loss would have been if the sugar crop had been delivered late because shipping was missing. Whatever the loss, the parties had promised each other that \$17,000 per day was a reasonable measure. The court must decline to substitute the requirements of judicial proof for the parties' own conclusion. The *Moku Pahu*, available on June 30, 1981, was a great prize, capable of multiple employments and enlarging the uses of the entire C and H fleet. When sophisticated parties with bargaining parity have agreed what lack of this prize would mean, and it is now difficult to measure what the lack did mean, the court will uphold the parties' bargain. C and H is entitled to keep the liquidated damages of \$3,298,000 it has already received and to receive additional liquidated damages of \$1,105,000 with interest thereon, less setoffs determined by the district court.

28. On the comparatively minor issue as to whether C and H is entitled to arbitration of its claim for a contract price reduction, Article 32 of the contract provides for arbitration of all disputes arising out of the contract with exceptions not applicable here. But no dispute remains for arbitration. The district court found that Sun was excused from performing its mating obligations because the tug was not made available on March 11, 1982 when the barge was ready. C and H is not entitled to reimbursement from Sun for the costs it incurred in having the mating performed later by others. C and H was entitled to reimbursement for what it had paid Sun itself for the mating. But on the point system agreed to by the parties, this work represented 100 points out of possible 10,000 or 1 percent of the contract price. According to testimony offered on behalf of C and H, Sun credited C and H with a sum representing these 100 points. C and H's claim has been met. Arbitration is unnecessary.
29. Sun has counterclaimed against C and H and Halter for misrepresentation, charging that the two companies had concealed from Sun the true progress on the tug. The alleged damages consist in the expenses Sun incurred trying to meet its own contractual obligations to build the barge. This counterclaim lacks plausibility on its face. No damage is inflicted on a party which is induced to perform its own contract. The cases Sun invokes to support its position involve "active interference" by one party with another party's performance. They have no applicability here.
30. Uncontradicted testimony indicates, moreover, that Sun was aware of the delay. Employees of Sun were in touch with Halter. It would have been surprising if they had not been. Sun attempts to get around its actual knowledge by contending that it was not officially informed of the tug's progress. But the kind of knowledge that precludes the possibility of fraud does not have to be officially conveyed. Sun's counterclaim is meritless.