

**Contracts in United States Common
Law**

By

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**September 29-October 1, 2017
University of Szeged
Szeged, Hungary**

Note from the Professor to the Students

Please find enclosed my course pack for the common law contracts class we will have together. In order to assist you I have broken the course into two main parts: 1) Making Contracts and 2) Breaking Contracts. We will spend about half our time on each of these areas.

The course packet is designed to provide you a basic understanding of the United State Common Law of Contracts. For each aspect of contracts, the essential sections of the common law (in the form of the Restatement Second of Contracts synthesis of the rule from the common law) is provided. After several of the key sets of rules, cases are provided to help illustrate the rules as they are applied by American courts.

I encourage you to have read the entire course pack before the class so that we can profit the most from our time together. Please look at the rules and, as appropriate, look at the application of the rules in the small group of cases that are provided.

I intend that we will discuss these rules, the cases, and hypotheticals that I will present to you to help ground you in the United States Common Law of Contracts.

**Looking forward to working with you,
Sincerely,**

**Benjamin G. Davis
Professor of Law
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September 8, 2017**

**I. Making Contracts –
Friday and Saturday**

**II. Breaking Contracts –
Saturday and Sunday**

Table of Contents

I. Making Contracts	Pages
• What is a contract?	5
• Classic Contract	6-39
• Statute of Frauds	40
• Promissory Estoppel	41-49
• Restitution	50
• Meaning and Interpretation	51
• Parol Evidence Rule	52-57
• Implied Terms – Good Faith	58
• Warranties – Express or Implied	58
II. Breaking Contracts	
• Conditions	61-69
• Performance and Breach	70-82
• Anticipatory Repudiation	83
• Request for Assurances	84
• Remedies	
• Damages	86-99
• Alternatives to Damages	100
• Avoiding Enforcement	102
• Justifications for Non-Per- formance	103
• Miscellaneous	104

Making Contracts (cnt'd)

What is a Contract (or K)?

§1. Contract Defined

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

§2. Promise; Promisor; Promisee; Beneficiary

(1) A promise is a manifestation of intention to act or refrain from acting in a specified way, so made as to justify a promisee in understanding that a commitment has been made.

(2) The person manifesting the intention is the promisor.

(3) The person to whom the manifestation is addressed is the promisee.

(4) Where performance will benefit a person other than the promisee, that person is a beneficiary.

§4. How a Promise May Be Made

A promise may be stated in words either oral or written, or may be inferred wholly or partly from conduct.

Making Contracts (cnt'd) A. Classic Contract

K = Manifestation of Mutual Assent (MMA) + Consideration

§17. Requirement of a Bargain

(1) Except as stated in Subsection (2), the formation of a contract requires a bargain in which there is a *manifestation of mutual assent* to the exchange and a consideration.

(2) Whether or not there is a bargain a contract may be formed under special rules applicable to formal contracts or under the rules stated §§82-94.

§21. Intention to Be Legally Bound

Neither real nor apparent intention that a promise be legally binding is essential to the formation of a contract, but a manifestation of intention that a promise shall not affect legal relations may prevent the formation of a contract.

**Making Contracts
(cnt'd)
A. Classic Contract
MMA (usually) =
Offer and Acceptance**

§22. Mode of Assent: Offer and Acceptance

(1) The manifestation of mutual assent to an exchange ordinarily takes the form of an offer or proposal by one party followed by an acceptance by the other party or parties.

(2) A manifestation of mutual assent may be made even though neither offer nor acceptance can be identified and even though the moment of formation cannot be determined.

Making Contracts (cnt'd)

A. Classic Contract

Offer and Acceptance

§24. Offer Defined

An offer is the manifestation of willingness to enter into a bargain, so made as to justify another person in understanding that his assent to that bargain is invited and will conclude it.

§25. Option Contracts

An option contract is a promise which meets the requirements for the formation of a contract and limits the promisor's power to revoke an offer.

§26. Preliminary Negotiations

A manifestation of willingness to enter into a bargain is not an offer if the person to whom it is addressed knows or has reason to know that the person making it does not intend to conclude a bargain until he has made a further manifestation of assent.

§32. Invitation of Promise or Performance

In case of doubt an offer is interpreted as inviting the offeree to accept either by promising to perform what the offer requests or by rendering the performance, as the offeree chooses.

§33. Certainty

(1) Even though a manifestation of intention is intended to be understood as an offer, it cannot be accepted so as to form a contract unless the terms of the contract are reasonably certain.

(2) The terms of a contract are reasonably certain if they provide a basis for determining the existence of a breach and for giving an appropriate remedy.

(3) The fact that one or more terms of a proposed bargain are left open or uncertain may show that a manifestation of intention is not intended to be understood as an offer or as an acceptance

Making Contracts (cnt'd)

A. Classic Contract Offer and Acceptance

§36. Methods of Termination of the Power of Acceptance

- (1) An offeree's power of acceptance may be terminated by
 - (a) rejection or counter-offer by the offeree, or
 - (b) lapse of time, or
 - (c) revocation by the offeror, or
 - (d) death or incapacity of the offeror or offeree.
- (2) In addition, an offeree's power of acceptance is terminated by the non-occurrence of any condition of acceptance under the terms of the offer.

§38. Rejection

- (1) An offeree's power of acceptance is terminated by his rejection of the offer, unless the offeror has manifested a contrary intention.
- (2) A manifestation of intention not to accept an offer is a rejection unless the offeree manifests an intention to take it under further advisement.

§39. Counter-Offers

- (1) A counter-offer is an offer made by an offeree to his offeror relating to the same matter as the original offer and proposing a substituted bargain differing from that proposed by the original offer.
- (2) An offeree's power of acceptance is terminated by his making of a counter-offer, unless the offeror has manifested a contrary intention or unless the counter-offer manifests a contrary intention of the offeree.

§40. Time When Rejection or Counter-Offer Terminates the Power of Acceptance

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

Making Contracts (cnt'd) A. Classic Contract Offer and Acceptance

§43. Indirect Communication of Revocation

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

§45. Option Contract Created by Part Performance or Tender

(1) Where an offer invites an offeree to accept by rendering a performance and does not invite a promissory acceptance, an option contract is created when the offeree tenders or begins the invited performance or tenders a beginning of it.

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

Making Contracts (cnt'd)

A. Classic Contract Offer and Acceptance

§50. Acceptance of Offer Defined; Acceptance by Performance; Acceptance by Promise

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

(2) Acceptance by performance requires that at least part of what the offer requests be performed or tendered and includes acceptance by a performance which operates as a return promise.

(3) Acceptance by a promise requires that the offeree complete every act essential to the making of the promise

§58. Necessity of Acceptance Complying with Terms of Offer

An acceptance must comply with the requirements of the offer as to the promise to be made or the performance to be rendered.

§59. Purported Acceptance Which Adds Qualifications

A reply to an offer which purports to accept it but is conditional on the offeror's assent to terms additional to or different from those offered is not an acceptance but is a counter-offer.

§60. Acceptance of Offer Which States Place, Time, or Manner of Acceptance

If an offer prescribes the place, time or manner of acceptance its terms in this respect must be complied with in order to create a contract. If an offer merely suggests a permitted place, time or manner of acceptance, another method of acceptance is not precluded.

Making Contracts (cnt'd)

A. Classic Contract Offer and Acceptance

§63. Time When Acceptance Takes Effect

Unless the offer provides otherwise,

(a) an acceptance made in a manner and by a medium invited by an offer is operative and completes the manifestation of mutual assent as soon as put out of the offeree's possession, without regard to whether it ever reaches the offeror; but

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

§69. Acceptance by Silence or Exercise of Dominion

(1) Where an offeree fails to reply to an offer, his silence and inaction operate as an acceptance in the following cases only.

(a) Where an offeree takes the benefit of offered services with reasonable opportunity to reject them and reason to know that they were offered with the expectation of compensation.

(b) Where the offeror has stated or given the offeree reason to understand that assent may be manifested by silence or inaction, and the offeree in remaining silent and inactive intends to accept the offer.

(c) Where because of previous dealings or otherwise, it is reasonable that the offeree should notify the offeror if he does not intend to accept.

(2) An offeree who does any act inconsistent with the offeror's ownership of offered property is bound in accordance with the offered terms unless they are manifestly unreasonable. But if the act is wrongful as against the offeror it is an acceptance only if ratified by him.

In the discussion of the five types of option contracts (“Five Fingers of Death”) I will mention the Restatement 25 ordinary option contract and the Restatement 45 option contract by part performance. To a lesser extent I draw your attention to three other types of options: Option Contracts under Restatement 87(1)(a), Restatement 87(1)(b) and Restatement 87(2).

The language of Restatement 87 is as follows:

§87 Option Contract

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

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

(b) is made irrevocable by statute

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

Restatement 87(1)(a)

An effort has been made to suggest a rule for the common law that mirrors what is called the firm offer rule in Article 2 of the Uniform Commercial Code which is a statute that applies only in cases of sales of goods. As a statute, Article 2 of the Uniform Commercial Code is not the common law. The current state of the rule in Restatement 87(1)(a) is that the recital of a purported consideration under the terms of Restatement 87(1)(a) is not enough to create an option contract. Thus, if the option contract was “I pay \$10 for the right to purchase this land over the next three months.” The majority view is that the recital of a consideration like this recital (\$10 paid for the right to purchase over the next three months) is not enough to create the option. The majority view is that the \$10 would have had to actually been paid to create the option contract. Failing the payment, this situation would not be viewed as an option contract but as only an offer which could be revoked at any time. A more minority view would be that the “I pay \$10” might be viewed as a promise to pay \$10 and that might be sufficient consideration.

Restatement 87(1)(b)

This section of the Restatement notes the possibility of an option contract being created by a statute. This situation is typically imagined to cover UCC Section 2-205 Firm Offers which are a specialized form of offer in the setting of sales of goods that are allowed by statute to operate as option contracts.

Restatement 87(2)

This is a third type of option contract which represents an effort to generalize an option contract that is recognized in the construction contract setting to protect the general contractor's reliance on a subcontractor's bid until after the owner of the construction project has made the decision to award the contract. There are several exceptions that may apply in which this reliance based option contract will not be recognized to protect the general contractor's reliance on the subcontractor's bid (the subcontractor's bid terms excluding this possibility, no possibility of the general contractor shopping around to other subcontractors after the award by the owner (called bid shopping), no possibility of the general contractor pressuring the subcontractor to lower his price after the award by the owner (called bid chopping), no mistake by the subcontractor being obvious to the reasonable person). Note the rule does not protect the subcontractor's reliance on the general contractor's use of their bid – the protected reliance is in the other direction. There are efforts to expand the use of this type of option contract, but it is mainly centered in this particular aspect of construction contracts.

Cases

Second, when parties are in a bargaining relationship, it is also possible that one party can incur legal obligations to another person even though they have not entered into a contract. The doctrines of *restitution* and *promissory estoppel*, which we will examine in Chapter 3, involve liability between parties even though no contract has been formed or even contemplated. We will consider the policy reasons why contract law has come to recognize these additional bases of obligation.

Third, even if a contract has been formed, that is far from the end of the analysis. As we will see in subsequent chapters, a party who has entered into a contract may be relieved of that obligation if the other party has engaged in some form of bargaining misconduct, such as fraud, duress, or undue influence (to name just three), or if circumstances that existed at the time of the contract have changed sufficiently to justify nonperformance.

1. Intention to be Bound: The Objective Theory of Contract

In applying the concept of mutual assent, some courts state that the formation of a contract requires a "meeting of the minds" between the parties. A subtle but important distinction exists, however, between the ideas of "mutual assent" and "meeting of the minds." Suppose S and B sign a written document in which B agrees to buy a condominium in a new development. B later claims that he did not understand that he was signing a contract and that he did not intend to buy the condo. B might claim that he thought that the document he signed simply "reserved" the condo for him but did not obligate him to buy the property. The case goes to a trial before a jury. Suppose the jury believes that B is telling the truth and that he honestly did not understand that he was obligated to buy the property. If contract law requires a "meeting of the minds" for contract formation, then the jury should find for B. This view of contract formation has been described as "subjective" in that the actual intention of a party, rather than that party's conduct, determines the party's legal obligations. On the other hand, if contract law requires a manifestation of mutual assent, then (absent some fraud or other misconduct by S) the jury should find for S because both S and B manifested their assent by signing the document of sale. This approach has been described as "objective," in that it looks at the conduct of the parties from the perspective of a reasonable person rather than their actual, subjective intentions. Which approach should contract law use? Consider the following case.

Ray v. William G. Eurice & Bros., Inc.

Maryland Court of Appeals
201 Md. 115, 93 A.2d 272 (1952)

HAMMOND, Judge.

In an action in the Circuit Court for Baltimore County by the owners of an unimproved lot against a construction company for a complete breach of a written contract to build a house, the court, sitting without a jury, found for the defendant and the plaintiffs appealed.

13a

Calvin T. Ray and Katherine S. J. Ray, his wife, own a lot on Dance Mill Road in Baltimore County. Late in 1950, they decided to build a home on it, and entered into negotiations with several builders, including William G. Eurice & Bros., Inc., the appellee, which had been recommended by friends. They submitted stock plans and asked for an estimate—not a bid—to see whether the contemplated house was within their financial resources. John M. Eurice, its President, acted for the Eurice Corporation. He indicated at the first meeting that the cost of the house would be about \$16,000. Mr. Ray then employed an architect who redrew the plans and wrote a rough draft of specifications. Mr. Ray had copies of each mechanically reproduced, and in January, 1951, arranged a meeting with Mr. Eurice to go over them so that a final bid, as opposed to an estimate, could be arrived at. In the Ray living room, Mr. Ray and Mr. John Eurice went over the redrawn plans dated January 9, 1951, and the specifications prepared by the architect, consisting of seven pages and headed "Memorandum Specifications, Residence for Mr. and Mrs. C. T. Ray, Dance Mill Road, Baltimore County, Maryland, 9 January, 1951," and discussed each item. Mr. Eurice vetoed some items and suggested change in others. For example, foundation walls were specified to be of concrete block. Mr. Eurice wanted to pour concrete walls, as was his custom. Framing lumber was to be fir. Mr. Eurice wanted this to be fir or pine. In some instances, Mr. Eurice, wanting more latitude, asked that the phrase "or equivalent" be added after a specified product or brand make. All the changes agreed on were noted by Mr. Ray in green ink on the January 9th specifications, and Mr. Eurice was given a set of plans and a set of the specifications so that he could make a formal bid in writing. On February 14, the Eurice Corporation submitted unsigned, its typewritten three-page proposed contract to build a house for \$16,300 "according to the following specifications." Most of the three pages consisted of specifications which did not agree in many, although often relatively unimportant, respects with those in the January 9th seven-page specifications. Mr. Ray advised Mr. Eurice that he would have his own lawyer draw the contract. This was done. In the contract, as prepared and as finally signed, the builder agrees to construct a house for \$16,300 "strictly in accordance with the Plans hereto attached and designated residence for Mr. and Mrs. C. T. Ray, Dance Mill Road, Baltimore County, Maryland, Sheets 1 through 7 dated 9 January 1951 . . . and to supply and use only those materials and building supplies shown on the Specifications hereto attached and designated Memorandum Specifications—Residence for Mr. C. T. Ray, Dance Mill Road, Baltimore County, Maryland, Sheets 1 through 5 dated 14 February 1951 it being understood and agreed that any deviation from the said Plans shall be made only with the prior assent of the Owner. Deviations from the Specifications shall be made only in the event any of the items shown thereon is unavailable at the time its use is required, and then only after reasonable effort and diligence on the part of the Builder to obtain the specific item has failed and the owner has given his prior approval to the use of a substitute item."

The Memorandum Specifications referred to in the contract, consisting of five pages and dated February 14, 1951, had been prepared by Mr. and Mrs. Ray, the night of the day the Eurice Corporation delivered its three-page proposal, and after Mr. Ray had said that his own lawyer would draw the

contract. On the 14th of February the January 9 seven pages, as they had emerged from the green ink deletions and additions made at the meeting in January, were retyped and from the stencil so cut at the Ray apartment, Mr. Ray had many copies mechanically reproduced at the Martin Plant where he is an aeronautical engineer. The rewritten specifications were identified as they are designated in the contract, namely as ". . . Sheets 1 through 5, dated 14 February 1951."

On February 22, at the office of the Eurice Corporation, on the Old Philadelphia Road, the contract was signed. Present, at the time, were Mr. Ray—Mrs. Ray was absent and had signed the contract earlier because she could not get a babysitter—Mr. John Eurice and Mr. Henry Eurice, who is Secretary of the Eurice Corporation. Mr. Ray relates the details of the meeting, as follows:

I had copies, plans and specifications before me, as well as two copies of the contract. We sat down, Mr. John Eurice and I sat down and went over all of the items in the specifications. I volunteered to show him I had in fact changed the specifications to reflect their building idiosyncrasies, such as wanting to build the house with a poured cellar. We also went over the contract document item by item. Following that, we each signed the contract and Mr. Henry Eurice, being the other party there at the time, witnessed our signature. He was in the room during the entire discussion or review of the contract.

After the contract had been signed, Mr. Ray says he asked that the Eurice brothers help him fill out the F.H.A. form of specifications (required to obtain the mortgage he needed) since he was not familiar with the intricacies of that form. This they did, with Mr. Henry Eurice giving most of the aid. They used the memorandum specifications of February 14 where they corresponded with the F.H.A. form and in other instances, as where the memorandum specifications were not adequate, Mr. Henry Eurice gave the necessary information. After the F.H.A. specifications were completed, the meeting broke up and a copy of the signed contract and copies of the Plans and Specifications were retained by the Eurice Corporation.

Mr. Ray then obtained a loan from the Loyola Savings & Loan Association. To do this it was necessary that he furnish it with his copy of the contract as well as copies of the Plans, the specifications of February 14 and the F.H.A. specifications. Neither the plans nor specifications which were left with the Building Association were signed by the Eurice Corporation, nor, through a misunderstanding, had they been signed by either Mr. or Mrs. Ray. When they applied for the loan, Mr. and Mrs. Ray did sign the reverse side of each page of the drawings and of the contract specifications. Thereafter, in response to a call from the Building Association, Mr. John Eurice went to its office and signed the reverse side of each page of the contract, each page of the specifications of the five-page specifications of February 14, referred to in the contract, and each page of the plans dated January 9, and referred to in the contract, although he says that he did not look at any of these prior to signing them.

Settlement of the mortgage loan was made on April 19 and thereafter, Mr. Ray phoned Mr. John Eurice repeatedly in order to set a starting date for the construction work. He finally came to the Ray home on April 22 and

indicated that he would start construction sometime about the middle of May. Other details of the work were discussed and Mr. Ray was given the names of a plumber and a supply company so that he could pick out and buy direct various products which would be incorporated in the house. Mr. Eurice, at that time, brought up the question of a dry well which had not been noted in the specifications, and which was required by the Baltimore County Building Code, and Mr. Ray agreed that he would make allowance for this, as he felt it was an honest mistake.

On May 8, Mr. Ray received urgent messages from the Eurice Corporation that his presence was desired for a conference. As he walked into the office, Mr. Henry Eurice picked up the drawings, specifications and the contract, and threw them across the desk at him, and onto the floor, with the announcement that he had never seen them, and that if he had to build according to those specifications he did not propose to go ahead. Attempts were made at the meeting to iron out the differences which apparently caused Mr. Henry Eurice to state that he would not live up to the contract. A second meeting was held at the Ray apartment several days later, and these efforts were continued by Mr. John Eurice, and that was the last contact that the Ray family had with any officer or agent of the Eurice Corporation. Realization that to build according to contract specifications would cost more than their usual "easy going, hatchet and saw manner" as Judge Gontrum described it, undoubtedly played a part in the refusal of the Eurice brothers to build the Ray house, although they testified that the excess cost would be only about \$1,000. More decisive, in all probability, was Mr. Ray's precision and his insistence on absolute accuracy in the smallest details which certainly made the Eurices unhappy, and to them was the shadow cast by harassing and expensive events to come. For example, at the meeting where the specifications were thrown across the desk, Mr. Ray agreed that certain millwork and trim which the Eurices had on hand was the equal of the specified Morgan millwork. Mr. Henry Eurice testified as to this:

He said that he thought ours were better I said "if we put that in your house how will we determine it was right or not?" He said he would bring a camera and take a picture of the moldings in our shed and when they were constructed in the house take another picture, and see if it would correspond. I said, "Man we can't build you a house under those conditions It is not reasonable." It created a heated argument for a while.

After written notice by Mr. Ray's lawyer to the lawyer for Eurice Corporation, that Mr. and Mrs. Ray considered that the contract had been breached and unless recognized within the week they would hold the Eurice Corporation "for any additional amount necessary to construct the house over and above the price called for in the agreement which has been breached by your client" had been ignored, suit was filed.

Mr. John Eurice agrees, in his testimony, that the Memorandum Sheets 1 to 7, dated January 9, had been gone over by him with Mr. and Mrs. Ray, but only as he says, to pick up "pointers." He also agrees that he had been told that the contract was to be drawn by Mr. Ray's lawyer, but says that he agreed only "so long as it is drawn up to our three page contract." He says that no specifications were attached to the contract which was signed, at the time it

was signed, and Mr. and Mrs. Ray cannot say definitely that the specifications were physically attached, although both say that they were unquestionably in existence and Mr. Ray is unequivocal and positive in his statement that they were present, stapled together, and discussed at the time of signing the contract. Mr. John Eurice says that the first time he saw the specifications was when his brother Henry "chucked them out," and in response to a question as to where they came from, said: "They were laying on the desk on the opened mail." This, he says, was some two weeks after the signing of the contract. No effort has been made by the appellee to show how the specifications arrived in the office at this time, with the opened mail. No envelope, with what could be a significant postmark, was introduced. No stenographer or clerk was brought into court to say that the specifications had been received in the mail, or to say that they had been delivered by messenger, or by Mr. Ray. Mr. John Eurice does not deny that he signed the plans and specifications, as well as the back of the contract at the office of the Loyola Building and Loan Association, but dismisses this as a practice necessary in all cases where financing is to be obtained, which has no relation to or significance in connection with the actual agreement between builder and owner.

Mr. Henry Eurice says that, although he was present at the time the contract was signed, and signed as a witness, that no specifications were attached to either copy of the signed contract, and that he did not see Specifications 1 to 5 until "right smart later, maybe a month." When he did first see them "they were laying on the desk on the opened mail."

Mr. John Eurice says in his testimony that the contract which was signed February 22 was not the proposal the Eurice Corporation had made. He sets forth that he read the contract of February 22 before he signed it, and he admits that he read paragraph B, whereby the builder agreed to construct the building strictly in accordance with the plans and specifications identified by description and date. He says he thought that the specifications, although they referred to pages 1 through 5, were those in his proposal which covered only three pages. Mr. Henry Eurice says that he read the contract of February 22, and that he read the paragraph with respect to the plans and specifications, but that he, too, thought it referred to the three-page proposal. Both agree that the plans were present at the time of the signing of the contract.

On the basis of the testimony which has been cited at some length, Judge Gontrum found the following:

The plaintiff, Mr Ray, is an aeronautical engineer, a highly technical, precise gentleman, who has a truly remarkable memory for figures and dates and a meticulous regard for detail. Apparently, his profession and his training have schooled him to approach all problems in an exceedingly technical and probably very efficient manner. He testified with an exceptional fluency and plausibility His mastery of language and recollection of dates and figures are phenomenal.

The defendants in the case are what might be termed old fashioned country or community builders. Their work is technical but it doesn't call for the specialized ability that Mr Ray's work demands. They conduct their business in a more easy going, hatchet and saw manner, and have apparently been successful in a small way in their field of home construction

The contract in question was entered into, in my judgment, in a hasty and rather careless fashion.

Judge Gontrum then cites the testimony of the Eurice Brothers that they had not seen Specifications 1 through 5 when they signed, and then says:

There is real doubt in my mind about the matter. Why the defendants signed the agreement without checking up on the specifications, I do not know, but they clearly were under the impression that the specifications referred to in the agreement were the specifications they had submitted some time prior and which they had permitted to be redrafted by the attorney for Mr. Ray. They both stated with absolute emphasis, and I do not question their veracity, that they were under the impression that the specifications in the agreement were the same which they had prepared

He concludes by saying that he feels that Mr. and Mrs. Ray were under one impression, and that the Messrs. Eurice were under another impression, saying:

In my opinion there was an honest mistake, that there was no real meeting of the minds and that the plaintiffs and defendants had different sets of specifications in mind when this agreement was signed. The minds of the parties, so different in their approach, to use a mechanical phrase, did not mesh.

It is unnecessary to decide, as we see it, whether there was or was not a mistake on the part of the Eurice Corporation. It does strain credulity to hear that the Messrs. Eurice, builders all their adult lives and, on their own successful builders for fifteen years of some twenty houses a year, would sign a simple contract to build a house, after they had read it, without knowing exactly what obligations they were assuming as to specifications requirements. The contract clearly referred to the specifications by designation, by number of pages and by date. It permits, in terms, no deviations from the specified makes or brands to be incorporated in the house, without the express permission of the owner. This would have been unimportant if the Eurice three-page specifications had been intended, since generality and not particularity was the emphasis there. Again, the contract could scarcely have intended to incorporate by reference the specifications in the three-page proposal because they were not set forth in a separate writing, but were an integral part of a proposed contract, which itself was undated, and which was of *three* pages, while the specifications designated in the contract were dated and were stated to be in the contract, *five* pages. Further, it is undisputed that the five pages of February 14th were the seven pages of January 9, corrected to reflect the deletions and changes made and agreed to by Mr. Ray and Mr. John Eurice. The crowning challenge to credulity in finding mistake is the fact that admittedly the contract, the plans and the specifications were all signed at one sitting by the President of the Eurice Corporation at the Loyola Building Association, after they had been signed by Mr. and Mrs. Ray.

If we assume the view as to mistake held by Judge Gontrum, in effect the mistake in the written agreement which prevented its execution by the Eurice Corporation from making it a contract was an unilateral one. It consisted, in the opinion of the Court, in the Eurice Corporation thinking it was assenting to its own specifications, while in form it was assenting to the Ray

1 specifications. If there was such a mistake, the legal result the Court found to follow, we think does not follow.

The law is clear, absent fraud, duress or mutual mistake, that one having the capacity to understand a written document who reads and signs it, or, without reading it or having it read to him, signs it, is bound by his signature in law, at least. . . .

Neither fraud nor duress are in the case. If there was mistake it was unilateral. The Rays intended their specifications to be a part of the contract, and the contract so stated, so the misconception, if it existed, was in the minds of the Messrs. Eurice.

Williston, Contracts (Rev. Ed.), Sec. 1577, says as to unilateral mistake:

But if a man acts negligently, and in such a way as to justify others in supposing that the terms of the writing are assented to by him and the writing is accepted on that supposition, he will be bound both at law and in equity. Accordingly, even if an illiterate executes a deed under a mistake as to its contents, he is bound if he did not require it to be read to him or its object explained.

In Maryland there may be exceptions in proceedings for specific performance, but otherwise the rule is in accord. . . . See also the Restatement, Contracts, Section 70, where it is said:

One who makes a written offer which is accepted, or who manifests acceptance of the terms of a writing which he should reasonably understand to be an offer or proposed contract, is bound by the contract, though ignorant of the terms of the writing or of its proper interpretation.

It does not lie in the mouth of the appellee, then, to say that it intended to be bound to build only according to its specifications. First, its claimed intent is immaterial, where it has agreed in writing to a clearly expressed and unambiguous intent to the contrary. Next, it may not vary that clearly expressed written intent by parol. And, finally, it may not put its own interpretation on the meaning of the written agreement it has executed. The Restatement, Contracts, Section 20, states the first proposition:

A manifestation of mutual assent by the parties to an informal contract is essential to its formation and the acts by which such assent is manifested, must be done with the intent to do those acts, but neither mental assent to the promises in the contract nor real or apparent intent that the promises shall be legally binding, is essential

Williston (work cited), Sec. 21, states the rule as follows: "The only intent of the parties to a contract which is essential, is an intent to say the words and do the acts which constitute their manifestation of assent." Judge Learned Hand expressed it in this wise: "A contract has, strictly speaking, nothing to do with the personal, or individual, intent of the parties. A contract is an obligation attached by the mere force of law to certain acts of the parties, usually words, which ordinarily accompany and represent a known intent. If, however, it were proved by twenty bishops that either party, when he used the words, intended

something else than the usual meaning which the law imposes upon them, he would still be held, unless there were some mutual mistake, or something else of the sort." *Hotchkiss v. National City Bank*, D.C., 200 F. 287, 293.

. . . The test in such case is objective and not subjective. Restatement, Contracts, Sec. 230. . . . Williston (work cited), Sec. 94, page 294, says: "It follows that the test of a true interpretation of an offer or acceptance is not what the party making it thought it meant or intended it to mean, but what a reasonable person in the position of the parties would have thought it meant." . . .

We conclude that the appellee wrongfully breached its contract to build the plaintiffs a house for \$16,300. The measure of damage in such a case presents no difficulty. *Keystone Engineering Corp. v. Sutter*, Md., 78 A.2d 191, 195. Here Judge Marbury said for the Court: "When a contractor on a building contract fails to perform, one of the remedies of the owner is to complete the contract, and charge the cost against the wrongdoer. Williston on Contracts, Rev. Ed. Vol. 5, §1363, p.3825, Restatement Contracts, ch. 12, §346, Subsec. (1) (a)(i), p.573 and Comment 1, p.576." See also, *Carrig v. Gilbert-Varker Corp.*, 314 Mass. 351, 50 N.E.2d 59, 62, 147 A.L.R. 927. There the court said: "The owner was entitled to be put in the same position that he would have been in if the contractor had performed its contract We think the proper measure of damages was the cost in excess of the contract price that would be incurred by the owner in having the houses built" That figure is ascertainable with sufficient definiteness in the instant case. . . .

Judgment reversed with costs and judgment entered for appellants against appellee in the sum of \$5,993.40.

Notes and Questions

1. *Credibility of the parties.* Does it appear to you that Judge Hammond, the author of the Maryland Court of Appeals' opinion in *Ray*, believed the Eurice brothers' testimony? Do you? Under the view of the case taken by the court, is the question of their veracity material to the outcome of the case? Should it be?

2. *Nature of the parties.* Although classical contract law typically assumes the interaction of hypothetical individuals (see the ubiquitous *A*, *B*, and sometimes *C* of the illustrations to both Restatements), in modern life it is of course more typical for at least one of the contracting parties to be a business enterprise, conducting its affairs through the medium of a corporation. This was true in the *Ray* case, where the defendant was a corporation, although it seems to have been essentially the creature of the two Eurice brothers, John and Henry. Do you think John and Henry Eurice were equally involved in and aware of the negotiations with Calvin and Katherine Ray? If not, what effect might that fact have had on the progress of those negotiations?

3. *The objective theory of contractual intent.* At one point the law may have looked for a true, or "subjective" intention on the part of the promisor. (See, however, Professor Joseph Perillo's historical study, *The Origins of the Objective Theory of Contract Formation and Interpretation*, 69 *Fordham L. Rev.* 427

offer. The thing offered was described with fairness and verity. The defendant's response to the offer was that—

"We will be interested in your official report of the different changes in the handling of freight, and would ask that you put our name down for a copy of same."

The defendant's letter does not describe the official report with exactness. Considered by itself, its meaning in that respect might be doubtful. But viewed in the light of the plaintiff's offer the reply is responsive and relevant. Plaintiff described and offered but one official report. Defendant referred to and requested a copy of "your official report," etc., which phrase in ordinary commercial practice would be understood to sufficiently identify the matter referred to. The additional descriptive words used, "of different changes in the handling of freight," while lacking in precision, are fairly referable to the subject of the plaintiff's offer. Especially is this true, since it is not made to appear that there was any other official report known to the parties to which the acceptance could refer. Under the circumstances, we think the communications of the parties above referred to, judged by a reasonable standard, manifest an intention to agree upon the same thing, and that the evidence was sufficient, as a matter of law, to support the finding of the trial court that the plaintiff's offer was accepted by the defendant. . . .

The later complaints of defendant were that the reports were of no value to defendant, that it could not use them, and that the price charged was surprising. No objection upon the grounds that the defendant did not contract for the particular reports furnished was made until this action was filed. There is no claim of misrepresentation or fraud against the plaintiff. It may well be that the reports proved useless and of no value to defendant, and that in volume and price they exceeded its expectations, but, in the absence of some misconduct on the part of the plaintiff, the defendant cannot be relieved from the consequences of its improvidence, merely because the bargain is burdensome and unprofitable.

Judgment affirmed.

WEBER, C. J., and GIDEON, THURMAN, and FRICK, JJ., concur.

Feldman v. Google, Inc.
United States District Court
513 F. Supp. 2d 229 (E.D. Pa. 2007)

James T. GILES, J

MEMORANDUM

I. INTRODUCTION

Before the court is Defendant Google, Inc.'s Motion to Dismiss Plaintiff's Amended Complaint, or in the alternative, to Transfer, which motion the court

131

converted to a Motion for Summary Judgment. Also before the court is Plaintiff Lawrence E. Feldman's Cross-Motion for Summary Judgment. The ultimate issues raised by the motions and determined by the court are whether a forum selection clause in an internet "clickwrap" agreement is enforceable under the facts of the case and, if so, whether transfer of this case to the Northern District of California is warranted. The court finds in the affirmative as to both issues and, therefore, denies Plaintiff's Motion for Summary Judgment, grants Defendant's Motion to Transfer, and transfers this case to the Northern District of California, San Jose Division. The reasons follow.

Defendant's motion seeks to enforce the forum selection clause in an online "clickwrap" agreement, which provides for venue in Santa Clara County, California, which is within the San Jose Division. In his original complaint, Plaintiff based his claims on a theory of express contract. In his Amended Complaint, however, Plaintiff offers a wholly new legal theory. He argues that no express contract existed because the agreement was not valid. Withdrawing his express contract allegations, Plaintiff advanced the theory of implied contract. Because he argues he did not have notice of and did not assent to the terms of the agreement and therefore there was no "meeting of the minds." Plaintiff also argues that, even if the agreement were controlling, it is a contract of adhesion and unconscionable, and that the forum selection clause is unenforceable.

The court will address these arguments in turn. . . .

II. FACTUAL BACKGROUND

A. GENERAL BACKGROUND

On or about January 2003, Plaintiff, a lawyer with his own law firm, Lawrence E. Feldman & Associates, purchased advertising from Defendant Google, Inc.'s "AdWords" Program, to attract potential clients who may have been harmed by drugs under scrutiny by the U.S. Food and Drug Administration.

In the AdWords program, whenever an internet user searched on the internet search engine, Google.com, for keywords or "AdWords" purchased by Plaintiff, such as "Vioxx," "Bextra," and "Celebrex," Plaintiff's ad would appear. If the searcher clicked on Plaintiff's ad, Defendant would charge Plaintiff for each click made on the ad.

This procedure is known as "pay per click" advertising. The price per keyword is determined by a bidding process, wherein the highest bidder for a keyword would have its ad placed at the top of the list of results from a Google.com search by an internet user.

Plaintiff claims that he was the victim of "click fraud." Click fraud occurs when entities or persons, such as competitors or pranksters, without any interest in Plaintiff's services, click repeatedly on Plaintiff's ad, the result of which drives up his advertising cost and discourages him from advertising. Click fraud also may be referred to as "improper clicks" or, to coin a phrase, "trick clicks." Plaintiff alleges that twenty to thirty percent of all clicks for which he was charged were fraudulent. He claims that Google required him to pay for all clicks on his ads, including those which were fraudulent.

Plaintiff does not contend that Google actually knew that there were fraudulent clicks, but alleges that click fraud can be tracked and prevented by computer programs, which can count the number of clicks originating from a single source and whether a sale results, and can be tracked by mechanisms on websites. . .

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Plaintiff alleges Google charged him over \$100,000 for AdWords from about January 2003 to December 31, 2005. Plaintiff seeks damages, disgorgement of any profits Defendant obtained as a result of any unlawful conduct, and restitution of money Plaintiff paid for fraudulent clicks.

B. THE ONLINE AGREEMENT AND FORUM SELECTION CLAUSE

This cross-summary judgment battle turns entirely on a forum selection clause in the AdWords online agreement. It is undisputed that the forum selection clause provides: "*The Agreement must be construed as if both parties jointly wrote it, governed by California law except for its conflicts of laws principles and adjudicated in Santa Clara County, California.*" (Def. Mot. to Dismiss, Ex. A, at P. 7 (emphasis added).)

Annie Hsu, an AdWords Associate for Google, Inc., testified by affidavit that the following procedures were in place at the time that Plaintiff activated his AdWords account in about January 2003. (Hsu Decl. P 7.) Although Plaintiff claims that the AdWords Agreement "was neither signed nor seen and negotiated by Feldman & Associates or anyone at his firm" (Pl. Opp. to Mot. to Dismiss at 2) and that he never "personally signed a contract with Google to litigate disputes in Santa Clara County, California" (Pl. Reply at 1). Plaintiff does not dispute that he followed the process outlined by Hsu.

It is undisputed that advertisers, including Plaintiff, were required to enter into an AdWords contract before placing any ads or incurring any charges. (Hsu Decl. P 2.) To open an AdWords account, an advertiser had to have gone through a series of steps in an online sign-up process. (Hsu Decl. P 3.) To activate the AdWords account, the advertiser had to have visited his account page, where he was shown the AdWords contract. (Hsu Decl. P 4.)

Toward the top of the page displaying the AdWords contract, a notice in bold print appeared and stated, "**Carefully read the following terms and conditions.** If you agree with these terms, indicate your assent below." (Hsu Decl. P 4.) The terms and conditions were offered in a window, with a scroll bar that allowed the advertiser to scroll down and read the entire contract. The contract itself included the pre-amble and seven paragraphs, in twelve-point font. The contract's pre-amble, the first paragraph, and part of the second paragraph were clearly visible before scrolling down to read the rest of the contract. The preamble, visible at first impression, stated that consent to the terms listed in the Agreement constituted a binding agreement with Google. A link to a printer-friendly version of the contract was offered at the top of the contract window for the advertiser who would rather read the contract printed on paper or view it on a full-screen instead of scrolling down the window. (Hsu Decl. P 5.)

At the bottom of the webpage, viewable without scrolling down, was a box and the words, "**Yes, I agree to the above terms and conditions.**" (Hsu Decl. P 4.) The advertiser had to have clicked on this box in order to proceed to the next step. (Hsu Decl. P 6.) If the advertiser did not click on "**Yes, I agree . . .**" and instead tried to click the "Continue" button at the bottom of the webpage, the advertiser would have been returned to the same page and could not advance to the next step. If the advertiser did not agree to the AdWords contract, he could not activate his account, place any ads, or incur any charges. Plaintiff had an account activated. He placed ads and charges were incurred. . . .

III. LEGAL STANDARD FOR SUMMARY JUDGMENT

[The court noted that summary judgment is appropriate under the federal rules of civil procedure if there is no genuine issue as to any material fact and the moving party is entitled to a summary judgment as a matter of law.—Eds.]

IV. DISCUSSION

A. CHOICE OF LAW

Defendant argues that the court must apply California law. The AdWords Agreement contains a choice of law clause, specifying that the Agreement must be governed by California law. (Def. Mot. to Dismiss, Ex. A, at P 7.) Defendant and Plaintiff both rely upon Pennsylvania and California substantive law in their briefs and arguments. . . .

Most [federal] circuit courts, however, have found that federal, and not state law, applies in the determination of the effect given to a forum selection clause in diversity cases. . . . The Third Circuit has held that federal law controls because "questions of venue and the enforcement of forum selection clauses are essentially procedural, rather than substantive, in nature." *Jumara v. State Farm Ins. Co.*, 55 F.3d 873, 877 (3d Cir. 1995) (quoting [*Jones v. Weibrecht*, 901 F.2d 17, 19 (2d Cir. 1990)]) Thus, this court follows the Third Circuit precedent set out in *Jumara* and applies federal law in determining the validity of the forum selection clause at issue here.

B. THE ONLINE ADWORDS AGREEMENT IS A VALID EXPRESS CONTRACT.

1 *The Clickwrap Agreement is Enforceable.*

Plaintiff contends that the online AdWords Agreement was not a valid, express contract, and that the law of implied contract applies. In support of this contention, Plaintiff argues that he did not have notice of and did not assent to the terms of the Agreement. Implying that the contract lacked definite essential terms, but failing to brief the issue, Plaintiff argues that the contract did not include fixed price terms for services. He further argues that the AdWords Agreement presented does not set out a date when Plaintiff may have entered into the contract. As to the latter argument, the unrebutted Hsu Declaration states that the AdWords Agreement and online process presented went into effect at the time that Plaintiff activated his AdWords account. (Hsu Decl. P 7.) Plaintiff has not presented any evidence to the contrary, nor does he allege that any agreement he made was different from the one presented through the Hsu Declaration. Thus, there is undisputed evidence that the AdWords Agreement presented is the same that Plaintiff activated with Defendant. . . .

The type of contract at issue here is commonly referred to as a "click-wrap" agreement. A clickwrap agreement appears on an internet webpage and requires that a user consent to any terms or conditions by clicking on a dialog box on the screen in order to proceed with the internet transaction.¹ *Specht v.*

¹ A clickwrap agreement is distinguishable from a "browsewrap" agreement, which "allow[s] the user to view the terms of the agreement, but do[es] not require the user to take any affirmative action before the Web site performs its end of the contract," such as simply providing a link to view the terms and conditions. James J. Tracy, Case Note, Legal Update: Browsewrap Agreements: Register.com, Inc. v. Verio, Inc., 11 B.U.J. Sci. & Tech. L. 164, 164-65 (2005)

130

Netscape Comms. Corp., 306 F.3d 17, 22 (2d Cir. 2002); . . . Even though they are electronic, clickwrap agreements are considered to be writings because they are printable and storable. See, e.g., *In Re RealNetworks, Inc., Privacy Litigation*, No. 00-c-1366, 2000 U.S. Dist. LEXIS 6584, at *8-11, 2000 WL 631341, at *3-4 (N.D. Ill. May 11, 2000).

To determine whether a clickwrap agreement is enforceable, courts presented with the issue apply traditional principles of contract law and focus on whether the plaintiffs had reasonable notice of and manifested assent to the clickwrap agreement. See, e.g., *Specht*, 306 F.3d at 28-30; *Forrest v. Verizon Communications, Inc.*, 805 A.2d 1007, 1010 (D.C. Cir. 2002); *Barnett v. Network Solutions, Inc.*, 38 S.W.3d 200 (Tex. App. 2001); . . . Absent a showing of fraud, failure to read an enforceable clickwrap agreement, as with any binding contract, will not excuse compliance with its terms. See, e.g., *Specht*, 306 F.3d at 30; *Lazovick v. Sun Life Ins. Co. of Am.*, 586 F. Supp. 918, 922 (E.D. Pa. 1984); *Barnett*, 38 S.W.3d at 204.

a. There was Reasonable Notice of and Mutual Assent to the AdWords Agreement.

Plaintiff claims he did not have notice or knowledge of the forum selection clause, and therefore that there was no "meeting of the minds" required for contract formation. In support of this argument, Plaintiff cites *Specht v. Netscape Comms. Corp.*, in which the Second Circuit held that internet users did not have reasonable notice of the terms in an online agreement and therefore did not assent to the agreement under the facts of that case. 306 F.3d at 20, 31.

The facts in *Specht*, however, are easily distinguishable from this case. There, the internet users were urged to click on a button to download free software. *Id.* at 23, 32. There was no visible indication that clicking on the button meant that the user agreed to the terms and conditions of a proposed contract that contained an arbitration clause. *Id.* The only reference to terms was located in text visible if the users scrolled down to the next screen, which was "submerged." *Id.* at 23, 31-32. Even if a user did scroll down, the terms were not immediately displayed. *Id.* at 23. Users would have had to click onto a hyperlink, which would take the user to a separate webpage entitled "License & Support Agreements." *Id.* at 23-24. Only on that webpage was a user informed that the user must agree to the license terms before downloading a product. *Id.* at 24. The user would have to choose from a list of license agreements and again click on yet another hyperlink in order to see the terms and conditions for the downloading of that particular software. *Id.*

The Second Circuit concluded on those facts that there was not sufficient or reasonably conspicuous notice of the terms and that the plaintiffs could not have manifested assent to the terms under these conditions. *Id.* at 32, 35. The Second Circuit was careful to differentiate the method just described from clickwrap agreements which do provide sufficient notice. *Id.* at 22 n.4, 32-33. Notably, the issue of notice and assent was not at issue with respect to a second agreement addressed in *Specht*. *Id.* at 21-22, 36. In that clickwrap agreement, when users proceeded to initiate installation of a program, "they were automatically shown a scrollable text of that program's license agreement and were not permitted to complete the installation until they had clicked on a 'Yes' button to indicate that they had accepted all the license terms. If a user attempted to install [the program] without clicking 'Yes,' the installation would be aborted." *Id.* at 21-22.

Through a similar process, the AdWords Agreement gave reasonable notice of its terms. In order to activate an AdWords account, the user had to visit a webpage which displayed the Agreement in a scrollable text box. Unlike the impermissible agreement in *Specht*, the user did not have to scroll down to a submerged screen or click on a series of hyperlinks to view the Agreement. Instead, text of the AdWords Agreement was immediately visible to the user, as was a prominent admonition in boldface to read the terms and conditions carefully, and with instruction to indicate assent if the user agreed to the terms. . . .

A reasonably prudent internet user would have known of the existence of terms in the AdWords Agreement. Plaintiff had to have had reasonable notice of the terms. By clicking on "Yes, I agree to the above terms and conditions" button, Plaintiff indicated assent to the terms. Therefore, the requirements of an express contract for reasonable notice of terms and mutual assent are satisfied. Plaintiff's failure to read the Agreement, if that were the case, does not excuse him from being bound by his express agreement.

b. The AdWords Agreement is Enforceable Despite Its Lack of a Definite Price Term.

Plaintiff's argument that the AdWords Agreement is unenforceable because of failure to supply a definite, essential term as to price is without merit. Under California and Pennsylvania law, the price term is an essential term of a contract and must be supplied with sufficient definiteness for a contract to be enforceable. . . . If the parties, however, have agreed upon a practicable method of determining the price in the contract with reasonable certainty, such as through a market standard, the contract is enforceable. See, e.g., *Portnoy v. Brown*, 430 Pa. 401, 243 A.2d 444 (1968); 1 *Witkin Sum. Cal. Law Contracts* §142 (2006) ("[T]he complete absence of any mention of the price is not necessarily fatal: The contract may be interpreted to mean the market price or a reasonable price.").

The AdWords Agreement does not include a specific price term, but describes with sufficient definiteness a practicable process by which price is determined. . . . The court concludes that the AdWords Agreement is enforceable because it contained a practicable method of determining the market price with reasonable certainty.

[The court proceeded to find that neither the AdWords Agreement nor its terms, including the forum selection clause, were unconscionable and therefore unenforceable. — Eds.]

V. CONCLUSION

For the foregoing reasons, Defendant's motion to transfer is granted and Plaintiff's motion for summary judgment is denied. An appropriate Order follows.

Notes and Questions

1. *Relevant legal standards.* You will soon study in more specific detail the law of contract formation and the meaning of the phrase "meeting of the minds." At this point does it appear to you that the courts in *Allen* and *Feldman* applied the same legal standard concerning the making of an enforceable agreement? Would you expect that the technological evolution that occurred between 1923 and 2007 would require that there be changes in the law as well?

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3. *Scholarly Commentary.* In a 1994 article, Professor Melvin Eisenberg asserted that the traditional rule does not conform to the reasonable expectations of most readers, who would assume that an advertiser does indeed commit itself to sell on a first-come-first-served basis until its supply of the advertised goods is exhausted. Eisenberg also claims that a majority of modern cases have followed *Lefkowitz* in imposing liability on the advertiser. Melvin A. Eisenberg, *Expression Rules in Contract Law and Problems of Offer and Acceptance*, 82 *Cal. L. Rev.* 1127, 1166-1172 (1994). Jay Feinman and Stephen Brill go even further than Eisenberg:

Courts and scholars uniformly recite the contract law rule familiar to all first-year students: An advertisement is not an offer. The courts and scholars are wrong. An advertisement is an offer. This article explains why the purported rule is not the law, why the actual rule is that an advertisement is an offer, and what this issue tells us about contract law in particular and legal doctrine in general.

Jay M. Feinman & Stephen R. Brill, *Is an Advertisement an Offer? Why It Is, and Why It Matters*, 58 *Hastings L.J.* 61 (2006).

Normile v. Miller

Supreme Court of North Carolina
313 N.C. 98, 326 S.E.2d 11 (1985)

FRYE, Justice.

Defendant Hazel Miller owned real estate located in Charlotte, North Carolina. On 4 August 1980, the property was listed for sale with a local realtor, Gladys Hawkins. On that same day, Richard Byer, a real estate broker with the realty firm Gallery of Homes, showed the property to the prospective purchasers, Plaintiffs Normile and Kurniawan. Afterwards, Byer helped plaintiffs prepare a written offer to purchase the property. A Gallery of Homes form, entitled "DEPOSIT RECEIPT AND CONTRACT FOR PURCHASE AND SALE OF REAL ESTATE," containing blanks for the insertion of terms pertinent to the purchasers' offer, was completed in quadruplicate and signed by Normile and Kurniawan. One specific standard provision in Paragraph 9 included a blank that was filled in with the time and date to read as follows: "OFFER & CLOSING DATE: Time is of the essence, therefore this offer must be accepted on or before 5:00 P.M. Aug. 5th 1980. A signed copy shall be promptly returned to the purchaser."

Byer took the offer to purchase form to Gladys Hawkins, who presented it to defendant. Later that evening, Gladys Hawkins returned the executed form to Byer. It had been signed under seal by defendant, with several changes in the terms having been made thereon and initialed by defendant. The primary changes made by defendant were an increase in the earnest money deposit (\$100 to \$500); an increase in the down payment due at closing (\$875 to \$1,000); a decrease in the unpaid principal of the existing mortgage amount (\$18,525 to \$18,000); a decrease in the term of the loan from seller (25 years to 20 years); and a purchaser qualification contingency added in the outer margin of the form.

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That same evening, Byer presented defendant's counteroffer to Plaintiff Normile. Byer testified in his deposition that Normile did not have \$500 for the earnest money deposit, one of the requirements of defendant's counteroffer. Also, Byer stated that Normile did not "want to go 25 [sic] years because he wanted lower payments." Byer was under the impression at this point that Normile thought he had first option on the property and that "nobody else could put an offer in on it and buy it while he had this counteroffer, so he was going to wait awhile before he decided what to do with it." Normile, however, neither accepted or rejected the counteroffer at this point, according to Byer. When this meeting closed, Byer left the pink copy of the offer to purchase form containing defendant's counteroffer with Normile. Byer stated that he thought that Normile had rejected the counteroffer at this point.

At approximately 12:30 A.M. on 5 August, Byer went to the home of Plaintiff Segal, who signed an offer to purchase with terms very similar to those contained in defendant's counteroffer to Plaintiffs Normile and Kurniawan. This offer was accepted, without change, by defendant. Later that same day, at approximately 2:00 P.M., Byer informed Plaintiff Normile that defendant had revoked her counteroffer by commenting to Normile, "[Y]ou snooze, you lose; the property has been sold." Prior to 5:00 P.M. on that same day, Normile and Kurniawan initialed the offer to purchase form containing defendant's counteroffer and delivered the form to the Gallery of Homes' office, along with the earnest money deposit of \$500.

Separate actions were filed by plaintiff-appellants and appellee seeking specific performance. Plaintiff Segal's motion for consolidation of the trials was granted. Defendant, in her answer, recognized the validity of the contract between her and Plaintiff Segal. However, because of the action for specific performance commenced by Plaintiffs Normile and Kurniawan, defendant contended that she was unable to legally convey title to Plaintiff Segal. Both plaintiffs filed a motion for summary judgment. Plaintiff Segal's motion for summary judgment was granted by the trial court, and defendant was ordered to specifically perform the contract to convey the property to Segal. Plaintiffs Normile and Kurniawan appealed to the Court of Appeals from the trial court's denial of their motion for summary judgment. That court unanimously affirmed the trial court's actions. Discretionary review was allowed by this Court on petition of Plaintiffs Normile and Kurniawan.

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 . . . [We] begin with a brief description of how a typical sale of real estate is consummated. The broker, whose primary duty is to secure a ready, willing, and able buyer for the seller's property, generally initiates a potential sale by procuring the prospective purchaser's signature on an offer to purchase instrument. J. Webster, *North Carolina Real Estate for Brokers and Salesmen*, §8.03 (1974). "An 'offer to purchase' is simply an offer by a purchaser to buy property, . . ." J. Webster, *supra*, §8.03. This instrument contains the prospective purchaser's "offer" of the terms he wishes to propose to the seller. *Id.*

Usually, this offer to purchase is a printed form with blanks that are filled in and completed by the broker. Among the various clauses contained in such an instrument, it is not uncommon for the form to contain "a clause stipulating that the seller must accept the offer and approve the sale within a

certain specified period of time, . . . The inclusion of a date within which the seller must accept simply indicates that the offer will automatically expire at the termination of the named period if the seller does not accept before then." *Id.*, §8.10. Such a clause is contained in Paragraph 9 of the offer to purchase form in the case *sub judice*.

In the instant case, the offerors, plaintiffs-appellants, submitted their offer to purchase defendant's property. This offer contained a Paragraph 9, requiring that "this offer must be accepted on or before 5:00 P.M. Aug. 5th 1980." Thus the offeree's, defendant-seller's, power of acceptance was controlled by the duration of time for acceptance of the offer. Restatement (Second) of Contracts §35 (1981). "The offeror is the creator of the power, and before it leaves his hands, he may fashion it to his will . . . if he names a specific period for its existence, the offeree can accept only during this period." Corbin, *Offer and Acceptance, and Some of the Resulting Legal Relations*, 26 *Yale L.J.* 169, at 183 (1917); see Restatement, *supra*, §41; S. Williston, *A Treatise on the Law of Contracts* §53 (1957).

This offer to purchase remains only an offer until the seller accepts it on the terms contained in the original offer by the prospective purchaser. *J. Webster, supra*, §8.10. If the seller does accept the terms in the purchaser's offer, he denotes this by signing the offer to purchase at the bottom, thus forming a valid, binding, and irrevocable purchase contract between the seller and purchaser. However, if the seller purports to accept but changes or modifies the terms of the offer, he makes what is generally referred to as a qualified or conditional acceptance. *Richardson v. Greensboro Warehouse & Storage Co.*, 223 N.C. 344, 26 S.E.2d 897 (1943); *Wilson v. W. M. Storey Lumber Co.*, 180 N.C. 271, 104 S.E. 531 (1920); 17 *Am. Jur.* 2d *Contracts* §62 (1964). "The effect of such an acceptance so conditioned is to make a new counter-proposal upon which the parties have not yet agreed, but which is open for acceptance or rejection." (Citations omitted.) *Richardson*, 223 N.C. at 347, 26 S.E.2d at 899. Such a reply from the seller is actually a counteroffer and a rejection of the buyer's offer. *J. Webster, supra*, §8.10.

These basic principles of contract law are recognized not only in real estate transactions but in bargaining situations generally. It is axiomatic that a valid contract between two parties can only exist when the parties "assent to the same thing in the same sense, and their minds meet as to all terms." *Goeckel v. Stokely*, 236 N.C. 604, 607, 73 S.E.2d 618, 620 (1952). This assent, or meeting of the minds, requires an offer and acceptance in the exact terms and that the acceptance must be communicated to the offeror. . . . "If the terms of the offer are changed or any new ones added by the acceptance, there is no meeting of the minds and, consequently, no contract." *G. Thompson, supra*, §4452. This counter-offer amounts to a rejection of the original offer. *S. Williston, supra*, §51. "The reason is that the counter-offer is interpreted as being in effect the statement by the offeree not only that he will enter into the transaction on the terms stated in his counteroffer, but also by implication that he will not assent to the terms of the original offer." *Id.*, §36.

The question then becomes, did defendant-seller accept plaintiff-appellants' offer prior to the expiration of the time limit contained within the offer? We conclude that she did not. The offeree, defendant-seller, changed the original offer in several material respects, most notably in the

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he seller accepts it on prospective purchaser. terms in the purchaser's contract at the bottom, thus act between the seller accepted but changes or orally referred to as a contract. *Ansboro Warehouse & Storey v. W. M. Storey*, 223 N.C. 2d Contracts §62. Defendant is to make a new contract agreed, but which is *Richardson*, 223 N.C. 2d actually a counteroffer §8.10.

contracted not only in real estate. It is axiomatic that a contract between the parties "assent to the contract as to all terms." *Restatement (Second) of Contracts* §33 (1952). This assent, however, is in the exact terms of the offeror. . . . "If the contract is an acceptance, there is no contract." G. Thompson, *supra*, of the original offer. Defendant's offer is interpreted as though he will enter into the contract so by implication that §36.

offeror accept plaintiff's offer. Defendant's offer contained within the offer, defendant-seller, most notably in the

terms regarding payment of the purchase price. S. Williston, *supra*, §77 (any alteration in the method of payment creates a conditional acceptance). This qualified acceptance was in reality a rejection of the plaintiff-appellants' original offer because it was coupled with certain modifications or changes that were not contained in the original offer. G. Thompson, *supra*, §4452. Additionally, defendant-seller's conditional acceptance amounted to a counter-offer to plaintiff-appellants. "A counter-offer is an offer made by an offeree to his offeror relating to the same matter as the original offer and proposing a substituted bargain differing from that proposed by the original offer." Restatement, *supra*, §39. Between plaintiff-appellants and defendant-seller there was no meeting of the minds, since the parties failed to assent to the same thing in the same sense.

In substance, defendant's conditional acceptance modifying the original offer did not manifest any intent to accept the terms of the original offer, including the time-for-acceptance provision, unless and until the original offeror accepted the terms included in defendant's counteroffer. The offeree, by failing to unconditionally assent to the terms of the original offer and instead qualifying his acceptance with terms of his own, in effect says to the original offeror, "I will accept your offer, provided you [agree to my proposed terms]." *Rucker v. Sanders*, 182 N.C. 607, 609, 109 S.E. 857, 858 (1921). Thus, the time-for-acceptance provision contained in plaintiff-appellants' original offer did not become part of the terms of the counter-offer. And, of course, if they had accepted the counteroffer from defendant, a binding purchase contract, which would have included the terms of the original offer and counteroffer, would have then resulted. J. Webster, *supra*, §8.03. . . .

It is generally recognized that "[a]n 'option' is a contract by which the owner agrees to give another the exclusive right to buy property at a fixed price within a specified time." 8A G. Thompson, *Commentaries on the Modern Law of Real Property*, §4443 (1963); *Sandlin v. Weaver*, 240 N.C. 703, 83 S.E.2d 806 (1954). In effect, an owner of property agrees to hold his offer open for a specified period of time. G. Thompson, *supra*, §4443. This option contract must also be supported by valuable consideration. *Id.* Disregarding the issue of consideration, it is more significant that defendant's counteroffer did not contain any promise or agreement that her counteroffer would remain open for a specified period of time.

Several of the cases cited by plaintiff-appellants are useful in illustrating how a seller expressly agrees to hold his offer open. For instance, in *Ward v. Albertson*, 165 N.C. 218, 81 S.E. 168 (1914), this Court stated, "An option, in the proper sense, is a contract by which the owner of property agrees with another that he shall have the right to purchase the same at a fixed price within a certain time." *Id.* at 222-23, 81 S.E. at 169. In that case, defendant-seller had agreed in writing as follows: ". . . I agree that if [prospective purchaser] pays me nine hundred and ninety five dollars prior to January 1, 1913, to convey to him all the timber and trees. . . ." *Id.* at 219, 81 S.E. at 168. . . . And finally, in *Kidd v. Early*, 289 N.C. 343, 222 S.E.2d 392 (1976), defendant-sellers agreed in writing: ". . . we C.F. Early and Bessie D. Early, hereby irrevocably agree to convey to [prospective purchasers] upon demand by him within 30 days from the date hereof, . . . a certain tract or parcel of land. . . ." *Id.* at 346, 222 S.E.2d at 396.

In each of these . . . cases, this Court recognized that the sellers had given the prospective purchasers a contractual option to purchase the seller's property. In the present case we find no comparable language within defendant-seller's counteroffer manifesting any similar agreement. There is no language indicating that defendant-seller in any way agreed to sell or convey her real property to plaintiff-appellants at their request within a specified period of time. There is, however, language contained within the prospective purchasers' offer to purchase that does state, "DESCRIPTION: I/we Michael M. Normile and Wawie Kurniawan hereby agree to purchase from the sellers, . . ." and "this offer must be accepted on or before 5:00 P.M. Aug. 5th 1980." (Emphasis added.) Nowhere is there companion language to the effect that Defendant Miller "hereby agrees to sell or convey to the purchasers" if they accept by a certain date.

Therefore, regardless of whether or not the seal imported the necessary consideration, we conclude that defendant-seller made no promise or agreement to hold her offer open. Thus, a necessary ingredient to the creation of an option contract, i.e., a promise to hold an offer open for a specified time, is not present. Accordingly, we hold that defendant's counteroffer was not transformed into an irrevocable offer for the time limit contained in the original offer because the defendant's conditional acceptance did not include the time-for-acceptance provision as part of its terms and because defendant did not make any promise to hold her counteroffer open for any stated time.

II

The foregoing preliminary analysis of both the Court of Appeals' opinion and plaintiff-appellants' argument in their brief prefaces what we consider to be decisive of the ultimate issue to be resolved. Basic contract principles effectively and logically answer the primary issue in this appeal. That is, if a seller rejects a prospective purchaser's offer to purchase but makes a counteroffer that is not accepted by the prospective purchaser, does the prospective purchaser have the power to accept after he receives notice that the counteroffer has been revoked? The answer is no. The net effect of defendant-seller's counteroffer and rejection is twofold. First, plaintiff-appellants' original offer was rejected and ceased to exist. *S. Williston, supra*, §51. Secondly, the counteroffer by the offeree requires the original offeror, plaintiff-appellants, to either accept or reject. *Benya v. Stevens & Thompson Paper Co., Inc.*, 143 Vt. 521, 468 A.2d 929 (1983).

Accordingly, the next question is did plaintiff-appellants, the original offerors, accept or reject defendant-seller's counteroffer? Plaintiff-appellants in their brief seem to answer this question when they state, "At the time Byer presented the counteroffer to Normile, Normile neither accepted nor rejected it. . . ." Therefore, plaintiff-appellants did not manifest any intent to agree to or accept the terms contained in defendant's counteroffer. Normile instead advised Byer that he, though mistakenly, had an option on the property and that it was off the market for the duration of the time limitation contained in his original offer. As was stated by Justice Bobbitt in *Howell v. Smith*, 258 N.C. 150, 128 S.E.2d 144 (1962): "The question whether a contract has been made must be determined from a consideration of the expressed intention of the

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parties — that is from a consideration of their words and acts." Id. at 153, 128 S.E.2d at 146. Although Normile's mistaken belief that he had an option is unfortunate, he still failed to express to Byer his agreement to or rejection of the counteroffer made by defendant-seller. . . .

Plaintiff-appellants in the instant case . . . did not accept, either expressly or by conduct, defendant's counteroffer. In addition to disagreeing with the change in payment terms, Normile stated to Byer that "he was going to wait awhile before he decided what to do with [the counteroffer]." Neither did plaintiffs explicitly reject defendant's counteroffer. Instead, plaintiff-appellants in this case chose to operate under the impression, though mistaken, that they had an option to purchase and that the property was "off the market." Absent either an acceptance or rejection, there was no meeting of the minds or mutual assent between the parties, a fortiori, there was no contract. *Horton v. Humble Oil & Refining Co.*, 255 N.C. 675, 122 S.E.2d 716 (1961); *Goeckel*, 236 N.C. 604, 73 S.E.2d 618 (1952).

It is evident from the record that after plaintiff-appellants failed to accept defendant's counteroffer, there was a second purchaser, Plaintiff-appellee Segal, who submitted an offer to defendant that was accepted. This offer and acceptance between the latter parties, together with consideration in the form of an earnest money deposit from plaintiff-appellee, ripened into a valid and binding purchase contract.

By entering into the contract with Plaintiff-appellee Segal, defendant manifested her intention to revoke her previous counteroffer to plaintiff-appellants. "It is a fundamental tenet of the common law that an offer is generally freely revocable and can be countermanded by the offeror at any time before it has been accepted by the offeree." E. Farnsworth, *Contracts*, §3.17 (1982); *Restatement, supra*, §42. The revocation of an offer terminates it, and the offeree has no power to revive the offer by any subsequent attempts to accept. *G. Thompson, supra*, §4452.

Generally, notice of the offeror's revocation must be communicated to the offeree to effectively terminate the offeree's power to accept the offer. It is enough that the offeree receives reliable information, even indirectly, "that the offeror had taken definite action inconsistent with an intention to make the contract." E. Farnsworth, *supra*, §3.17 (the author cites *Dickinson v. Dodds*, 2 Ch. Div. 463 (1876), a notorious English case, to support this proposition); *Restatement, supra*, §43.

In this case, plaintiff-appellants received notice of the offeror's revocation of the counteroffer in the afternoon of August 5, when Byer saw Normile and told him, "[Y]ou snooze, you lose; the property has been sold." Later that afternoon, plaintiff-appellants initialed the counteroffer and delivered it to the Gallery of Homes, along with their earnest money deposit of \$500. These subsequent attempts by plaintiff-appellants to accept defendant's revoked counteroffer were fruitless, however, since their power of acceptance had been effectively terminated by the offeror's revocation, *Restatement, supra*, §36. Since defendant's counteroffer could not be revived, the practical effect of plaintiff-appellants' initialing defendant's counteroffer and leaving it at the broker's office before 5:00 P.M. on August 5 was to resubmit a new offer. This offer was not accepted by defendant since she had already contracted to sell

her property by entering into a valid, binding, and irrevocable purchase contract with Plaintiff-appellee Segal.

For the reasons stated herein, the decision of the Court of Appeals is modified and affirmed.

Notes and Questions

1. *Classical Principles of offer and acceptance.* The court in *Normile* cites and applies many classical rules of offer and acceptance embodied in the first Restatement of Contracts and carried forward in the Restatement (Second), including the following: The power of acceptance created by an offer will be terminated by the offeree's rejection (as well as by other events, such as revocation by the offeror, or his death or incapacity). Restatement (Second) of Contracts §36. An acceptance must be unequivocal and unqualified in order for a contract to be formed. Restatement (Second) §§57 and 58. (Note that silence by the offeree rarely amounts to acceptance, but in some limited circumstances an offeree's silence may result in the formation of a contract. See Restatement (Second) §69; James J. White, *Autistic Contracts*, 45 *Wayne L. Rev.* 1693 (2000).) A "qualified acceptance" constitutes a counter-offer, Restatement (Second) §59, and as such will have the same effect as a rejection, insofar as the original power of acceptance is concerned. Restatement (Second) of Contracts §39. See Melvin A. Eisenberg, *The Revocation of Offers*, 2004 *Wis. L. Rev.* 271 (discussing classical and modern principles of offer and acceptance and arguing that contract law has partially but not completely broken away from doctrinal restrictions of classical contract law). See also Charles L. Knapp, *An Offer You Can't Revoke*, 2004 *Wis. L. Rev.* 309 (criticizing Eisenberg for failing to take into account many of the principles of modern contract law). For an argument that the rules of offer and acceptance have developed to promote efficient reliance see Richard Craswell, *Offer, Acceptance, and Efficient Reliance*, 48 *Stan. L. Rev.* 481 (1996).

2. *Policy analysis of classical rules.* What policy justifies the rule that the offeree's power of acceptance is terminated by his rejection of the offer? Does that policy apply with equal force to the case where the offeree makes a counter-offer? Professor Melvin Eisenberg has argued that the counter-offer-equals-rejection rule of Restatement (Second) §39(2) is not congruent with the normal understanding of most bargainers, and ought to be either abandoned entirely, or "dropped to the form of a maxim." Melvin A. Eisenberg, *Expression Rules in Contract Law and Problems of Offer and Acceptance*, 82 *Cal. L. Rev.* 1127, 1158-1161 (1994). Note, however, that the rule of termination-by-counter-offer is not stated as an inflexible one: Restatement (Second) §39(2) indicates that effect should be given to the expressed intention of either offeror or offeree to the contrary.

3. *Option contracts.* Plaintiff Normile testified that when he received the defendant's counter-offer he believed he had "first option" on the property, that Miller had bound herself to sell to no one else until Normile had accepted or rejected that counter-offer. The court indicates, however, that the defendant had made no promise to keep her offer open, and that Normile

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thus could not have had such an option. Even if Miller's counter-offer had been accompanied by an express promise on her part to keep that offer open for a stated period of time, Normile and Kurniawan would still not have had an enforceable option contract because they did not provide "consideration" for Miller's promise to hold the offer open. We will examine both the doctrine of consideration and option contracts in more detail in part B of this chapter. For now it is sufficient for you to know that under the modern theory of consideration a promise is generally enforceable only if the promisee has given either a promise or a performance in exchange for the promise that that promisee seeks to enforce. Normille and Kurniawan did not give anything to Miller to hold the offer open.

4. *Possibility of multiple acceptances.* In the course of its opinion in *Normile*, the North Carolina Supreme Court indicates that because the parties "failed to assent to the same thing in the same sense" there was "no meeting of the minds," and hence no contract. Suppose the plaintiffs had signed and returned Miller's counter-offer before they learned from Byer that Miller had in the meantime contracted to sell the property to Segal. Would a binding contract between Miller and plaintiffs have been formed? And, if so, what about the contract between Miller and Segal?

3. Offer and Acceptance in Unilateral Contracts

Perhaps no aspect of the classical contract law system was more vividly impressed on the minds of generations of law students than the distinction between bilateral and unilateral contracts. As we have seen, a bilateral contract is formed when the parties exchange promises of performance to take place in the future: Each party is both a promisor and a promisee; the offeree's communicated acceptance also constitutes in effect her promise to perform. However, if the offeror should offer to exchange his promise of a future performance only in return for the offeree's actual rendering of performance, rather than her mere promise of future performance, then the transaction would give rise to a unilateral contract. In that case, only one party (the offeror) would be a promisor, and the offeree's rendering of performance would also constitute her acceptance of the offer.

This view of the unilateral contract affords maximum protection to the offeror, who would not be bound unless and until he had received the performance he sought. For the offeree, however, it carries certain risks. If the offeror should revoke his offer at a time when the offeree had commenced but not yet completed the requested performance, classical theory denied the offeree any remedy on the contract because the offer was revoked before the proposed contract ever came into being. In 1916, Professor Maurice Wormser stated the classical view of this situation:

Suppose *A* says to *B*, "I will give you \$100 if you walk across the Brooklyn Bridge," and *B* walks—is there a contract? It is clear that *A* is not asking *B* for *B*'s promise to walk across the Brooklyn Bridge. What *A* wants from *B* is the act of walking across the bridge. When *B* has walked across the bridge there is a contract, and *A* is

then bound to pay to *B* \$100. At that moment there arises a unilateral contract *A* has bartered away his volition for *B*'s act of walking across the Brooklyn Bridge.

When an act is thus wanted in return for a promise, a unilateral contract is created when the act is done. It is clear that only one party is bound. *B* is not bound to walk across the Brooklyn Bridge, but *A* is bound to pay *B* \$100 if *B* does so. Thus, in unilateral contracts, on one side we find merely an act, on the other side a promise. . .

It is plain that in the Brooklyn Bridge case . . . , what *A* wants from *B* is the act of walking across the Brooklyn Bridge. *A* does not ask for *B*'s promise to walk across the bridge and *B* has never given it. *B* has never bound himself to walk across the bridge. *A*, however, has bound himself to pay \$100 to *B*, if *B* does so. Let us suppose that *B* starts to walk across the Brooklyn Bridge and has gone about one-half of the way across. At that moment *A* overtakes *B* and says to him, "I withdraw my offer." Has *B* then any rights against *A*? Again, let us suppose that after *A* has said, "I withdraw my offer," *B* continues to walk across the Brooklyn Bridge and completes the act of crossing. Under these circumstances, has *B* any rights against *A*?

. . . What *A* wanted from *B*, what *A* asked for, was the act of walking across the bridge. Until that was done, *B* had not given to *A* what *A* had requested. The acceptance by *B* of *A*'s offer could be nothing but the act on *B*'s part of crossing the bridge. It is elementary that an offeror may withdraw his offer until it has been accepted. It follows logically that *A* is perfectly within his rights in withdrawing his offer before *B* has accepted it by walking across the bridge — the act contemplated by the offeror and the offeree as the acceptance of the offer. *A* did not want *B* to walk half-way across or three-quarters of the way across the bridge. What *A* wanted from *B*, and what *A* asked for from *B*, was a certain and entire act. *B* understood this. It was for that act that *A* was willing to barter his volition with regard to \$100. *B* understood this also. Until this act is done, therefore, *A* is not bound, since no contract arises until the completion of the act called for. Then, and not before, would a unilateral contract arise. Then, and not before, would *A* be bound.

The objection is made, however, that it is very "hard" upon *B* that he should have walked half-way across the Brooklyn Bridge and should get no compensation. This suggestion, invariably advanced, might be dismissed with the remark that "hard" cases should not make bad law. But going a step further, by way of reply, the pertinent inquiry at once suggests itself, "Was *B* bound to walk across the Brooklyn Bridge?" The answer to this is obvious. By hypothesis, *B* was not bound to walk across the Brooklyn Bridge. . . . If *B* is not bound to continue to cross the bridge, if *B* is will-free, why should not *A* also be will-free? Suppose that after *B* has crossed half the bridge he gets tired and tells *A* that he refuses to continue crossing. *B*, concededly, would be perfectly within his rights in so speaking and acting. *A* would have no cause of action against *B* for damages. If *B* has a *locus poenitentiae*, so has *A*. They each have, and should have, the opportunity to reconsider and withdraw. Not until *B* has crossed the bridge, thereby doing the act called for, and accepting the offer, is a contract born. At that moment, and not one instant before, *A* is bound, and there is a unilateral contract. . . . So long as there is freedom of contract and parties see fit to integrate their understanding in the form of a unilateral contract, the courts should not interfere with their evident understanding and intention simply because of alleged fanciful hardship.

I. Maurice Wormser, *The True Conception of Unilateral Contracts*, 26 *Yale L.J.* 136, 136-138 (1916). Professor Wormser's argument, with its pointed if somewhat redundant disdain for "alleged fanciful hardship," may suggest why it has been sometimes said that "taught law is tough law." (And it may have

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some bearing on the fact that the fictional Professor Kingsfield of *The Paper Chase* was a contracts teacher.) The next case, *Petterson v. Pattberg*, illustrates the problem faced by an offeree in attempting to accept an offer for a unilateral contract when the offeror changes his mind and attempts to withdraw his offer.

Petterson v. Pattberg

New York Court of Appeals

248 N.Y. 86, 161 N.E. 428 (1928)

KELLOGG, J. The evidence given upon the trial sanctions the following statement of facts: John Petterson, of whose last will and testament the plaintiff is the executrix, was the owner of a parcel of real estate in Brooklyn, known as 5301 Sixth Avenue. The defendant was the owner of a bond executed by Petterson, which was secured by a third mortgage upon the parcel. On April 4th, 1924, there remained unpaid upon the principal the sum of \$5,450. This amount was payable in installments of \$250 on April 25th, 1924, and upon a like monthly date every three months thereafter. Thus the bond and mortgage had more than five years to run before the entire sum became due. Under date of the 4th of April, 1924, the defendant wrote Petterson as follows: "I hereby agree to accept cash for the mortgage which I hold against premises 5301 6th Ave., Brooklyn, N.Y. It is understood and agreed as a consideration I will allow you \$780 providing said mortgage is paid on or before May 31, 1924, and the regular quarterly payment due April 25, 1924, is paid when due." On April 25, 1924, Petterson paid the defendant the installment of principal due on that date. Subsequently, on a day in the latter part of May, 1924, Petterson presented himself at the defendant's home, and knocked at the door. The defendant demanded the name of his caller. Petterson replied: "It is Mr. Petterson. I have come to pay off the mortgage." The defendant answered that he had sold the mortgage. Petterson stated that he would like to talk with the defendant, so the defendant partly opened the door. Thereupon Petterson exhibited the cash and said he was ready to pay off the mortgage according to the agreement. The defendant refused to take the money. Prior to this conversation Petterson had made a contract to sell the land to a third person free and clear of the mortgage to the defendant. Meanwhile, also, the defendant had sold the bond and mortgage to a third party. It, therefore, became necessary for Petterson to pay to such person the full amount of the bond and mortgage. It is claimed that he thereby sustained a loss of \$780, the sum which the defendant agreed to allow upon the bond and mortgage if payment in full of principal, less that sum, was made on or before May 31st, 1924. The plaintiff has had a recovery for the sum thus claimed, with interest.

Clearly the defendant's letter proposed to Petterson the making of a unilateral contract, the gift of a promise in exchange for the performance of an act. The thing conditionally promised by the defendant was the reduction of the mortgage debt. The act requested to be done, in consideration of the offered promise, was payment in full of the reduced principal of the debt prior

Like §90, its more celebrated sibling (dealing with "promissory estoppel"), a concept we will discuss in the next chapter, §45 of the first Restatement appears to have reflected the view of Professor Arthur Corbin rather than that of Professor Samuel Williston. Compare 1 Williston on Contracts §60 (1920) with Arthur L. Corbin, Offer and Acceptance, and Some of the Resulting Legal Relations, 26 Yale L.J. 169, 191-196 (1917). In that respect Restatement §45 may have been part of what Professor Gilmore has referred to as the "Corbinization" of the first Restatement. Grant Gilmore, *The Death of Contract* 165 (1974).

Even Professor Wormser—the prototypical proponent of a hard-shelled approach to unilateral contract offers—ultimately acquiesced in the rule of §45. See I. Maurice Wormser, Book Review, 3 J. Legal Ed. 145, 146 (1950). Would the application of either §32 or §45 of the Second Restatement have changed the result of the *Petterson* case?

Cook v. Coldwell Banker/Frank Laiben Realty Co.

Missouri Court of Appeals
967 S.W.2d 654 (1998)

KATHIANNE KNAUP CRANE, Presiding Judge.

Defendant real estate brokerage firm appeals from a judgment entered on a jury verdict awarding defendant's former salesperson \$24,748.89 as damages for breach of a bonus agreement. Defendant claims that the salesperson failed to make a submissible case in that she did not accept the bonus offer before it was revoked. Defendant also asserts trial court errors relating to instructions, evidence, and closing argument. We affirm.

Plaintiff, Mary Ellen Cook, a licensed real estate agent, worked as a real estate salesperson or agent pursuant to a verbal agreement for defendant Coldwell Banker/Frank Laiben Realty Co. and its predecessors. Plaintiff listed and sold real estate for defendant as an independent contractor. Frank Laiben was a co-owner of defendant.

At a sales meeting in March, 1991, defendant, through Laiben, orally announced a bonus program in order to remain competitive with other local brokerage firms and to retain its agents. The bonus program provided that an agent earning \$15,000.00 in commissions would receive a \$500.00 bonus payable immediately, an agent earning \$15,000.00 to \$25,000.00 in commissions would receive a twenty-two percent bonus, and an agent earning above \$25,000.00 in commissions would receive a thirty percent bonus. Bonuses over the first \$500.00 were to be paid at the end of the year. The first year of the program would be January 1, 1991 to December 31, 1991 and it would continue on an annual basis after that. Laiben kept track of the agents' earnings in a separate bonus account.

At the end of April, 1991, plaintiff surpassed \$15,000.00 in earnings, entitling her to a \$500.00 bonus which defendant paid to her in September, 1991. By September, 1991 plaintiff surpassed \$32,400.00 in commissions.

At another sales meeting in September, 1991, Laiben indicated that bonuses would be paid at a banquet to be held in March of the following year instead of at the end of the year. Plaintiff asked if that meant that an agent had

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to be "here" in March in order to collect the bonus. Laiben indicated that was what it meant. Plaintiff testified that, at the time of the change in the bonus agreement, she had no intention of leaving defendant, but stayed with defendant until the end of 1991 in reliance on the promise of a bonus.

During 1991 plaintiff was contacted about joining Remax, another real estate brokerage firm. Although she was not initially interested, in January, 1992 she accepted a position with Remax and advised Laiben of her departure. Laiben informed her that she would not be receiving her bonus. At the end of 1991, plaintiff had total earnings of \$75,638.47, which made her eligible for a combined bonus of \$17,391.54. After placing her license with Remax, plaintiff finished closing four or five contracts that she had been working on prior to leaving defendant. In March, 1992 plaintiff sent a demand letter to defendant, seeking payment for the bonus she believed she had earned. Defendant did not pay plaintiff.

On December 17, 1992 plaintiff filed an action against defendant for breach of a bonus contract, seeking damages in the amount of \$18,404.31. She amended this petition to include prejudgment interest. At trial Laiben denied that at the March meeting he had stated the bonuses would be paid at the end of the year and testified that at that meeting he had told the agents the bonuses would not be paid until the following March. The jury returned a verdict in favor of plaintiff and awarded her damages in the amount of \$24,748.89. The court entered judgment in this amount.

In its first point defendant contends that the trial court erred in overruling its motions for directed verdict because plaintiff failed to make a submissible case of breach of the bonus agreement. In particular, defendant argues that plaintiff did not adduce sufficient evidence to establish a reasonable inference that 1) she tendered consideration to support defendant's offer of a bonus, or that 2) she accepted defendant's offer to give a bonus.

A directed verdict is a drastic action and should only be granted where reasonable and honest persons could not differ on a correct disposition of the case. *Seidel v. Gordon A. Gundaker Real Estate Co.*, 904 S.W.2d 357, 361 (Mo. App. 1995). In determining whether a plaintiff has made a submissible case in a contract action, we view the evidence in a light most favorable to plaintiff, presume plaintiff's evidence is true, and give plaintiff the benefit of all reasonable and favorable inferences to be drawn from the evidence. *Gateway Exteriors Inc. v. Suntide Homes Inc.*, 882 S.W.2d 275, 279 (Mo. App. 1994).

Plaintiff adduced evidence of a unilateral contract offered in March, 1991 to pay a bonus under certain conditions at the end of the year. She also adduced evidence that in September, 1991 defendant attempted to revoke that offer and make the bonus contingent upon the agent's remaining until March of the following year.

A unilateral contract is a contract in which performance is based on the wish, will, or pleasure of one of the parties. *Klamen v. Genuine Parts Co.*, 848 S.W.2d 38, 40 (Mo. App. 1993) A promisor does not receive a promise as consideration for his or her promise in a unilateral contract. *Id.* A unilateral contract lacks consideration for want of mutuality, but when the promisee performs, consideration is supplied, and the contract is enforceable to the extent performed. *Leeson v. Etchison*, 650 S.W.2d 681, 684 (Mo. App. 1983). An offer to make a unilateral contract is accepted when the requested performance is rendered. *Nilsson v. Cherokee Candy & Tobacco Co.*, 639

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S.W.2d 226, 228 (Mo. App. 1982). A promise to pay a bonus in return for an at-will employee's continued employment is an offer for a unilateral contract which becomes enforceable when accepted by the employee's performance. *Id.* at 228.

In the absence of any contract to the contrary, plaintiff could terminate her relationship with defendant at any time and was not obligated to earn a certain level of commissions. There was sufficient evidence that the bonus offer induced plaintiff to remain with defendant through the end of 1991 and to earn a high level of commissions for the court to submit the issue of acceptance by performance to the jury.

Defendant next argues that it was free to revoke the first offer with the second offer because, as of the time the second offer was made, plaintiff had not yet accepted the first offer. Defendant maintains that, because plaintiff did not stay until March, 1992, she did not accept the second offer and thus, did not earn the bonus.

Generally, an offeror may withdraw an offer at any time prior to acceptance unless the offer is supported by consideration. *Coffman Industries, Inc. v. Gorman-Taber Co.*, 521 S.W.2d 763, 772 (Mo. App. 1975). However, an offeror may not revoke an offer where the offeree has made substantial performance. *Id.* (citing 1 Williston on Contracts, Third Edition Section 60A (1957)). *Coffman* set out the general rule of law as follows:

Where one party makes a promissory offer in such form that it can be accepted by the rendition of the performance that is requested in exchange, without any express return promise or notice of acceptance in words, the offeror is bound by a contract just as soon as the offeree has rendered a substantial part of that requested performance.

1 Corbin on Contracts Section 49 (1952), quoted in *Coffman*, 521 S.W.2d at 772. The court stated the rationale for the rule as follows:

The main offer includes a subsidiary promise, necessarily implied, that if part of the requested performance is given, the offeror will not revoke his offer, and that if tender is made it will be accepted. Part performance or tender may thus furnish consideration for the subsidiary promises. Moreover, merely acting in justifiable reliance on an offer may in some cases serve as sufficient reason for making a promise binding. (Emphasis supplied.)

Restatement [First] of Contracts Section 45 cmt. b (1932), quoted in *Coffman*, 521 S.W.2d at 772. Thus, in the context of an offer for unilateral contract, the offer may not be revoked where the offeree has accepted the offer by substantial performance. *Id.* at 771-72.

In this case there was evidence that, before the offer was modified in September, 1991, plaintiff had remained with defendant and had earned over \$32,400.00 in commissions, making her eligible for the offered bonus. This constitutes sufficient evidence of substantial performance.

Plaintiff adduced evidence that defendant offered to pay a bonus at the end of 1991 if she would continue to work for it, that she stayed through 1991 with an intent to accept the offer, that she sold and listed enough property to qualify for all three bonus levels, that defendant knew of plaintiff's performance, that defendant paid \$500.00 of the bonus but did not pay the

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plaintiff could terminate the contract without being obligated to earn a bonus. The evidence indicates that the bonus was not earned by the end of 1991 and the plaintiff should submit the issue of

the first offer with the bonus was made, plaintiff had a duty to accept it, because plaintiff did not offer and thus, did not

at any time prior to the contract. *Coffman Industries, Inc.*, 377 N.W.2d 100 (Minn. App. 1975). However, the court has made substantial modifications to the Restatement (Second) of Contracts Section 60A:

it can be accepted by the offeree, without any express promise, and the offeror is bound by a contract just as if the offeree had requested performance.

Coffman, 521 S.W.2d at 100:

applied, that if part of the offer is accepted, the offeror may thus furnish a contract, and the offeror may rely acting in justifiable reliance on the offer as a reason for making a

§32), quoted in *Coffman*, 521 S.W.2d at 100. In a unilateral contract, the offeror is bound by the offer if the offer is accepted by sub-

stantial performance. The offer was modified in the contract and had earned over the offered bonus. This is the case.

plaintiff was to pay a bonus at the end of 1991. The plaintiff stayed through 1991 and did not list enough property to satisfy the tax. The plaintiff knew of plaintiff's tax situation but did not pay the

remainder, and that she was damaged. This evidence was sufficient to make a prima facie case for breach of a unilateral contract. Point one is denied.

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MARY RHODES RUSSELL and JAMES R. DOWD, JJ., concur.

Notes and Questions

1. *Continuing evolution of unilateral contract theory* We have already noted that §§31 and 45 of the first Restatement were aimed at minimizing the importance of the unilateral contract concept. Writing in 1938, Professor Karl Llewellyn sharply criticized the common law emphasis on the dichotomy between bilateral and unilateral contracts. He declared that "true" unilateral contracts—where the offeror seeks only performance and *not* a promise—were in fact so few in proportion to the ordinary run of commercial contracts that they should be viewed not as one-half of the contracting universe (as the classical categories would appear to suggest) but rather as aberrations—just a sideshow to the center ring of the contract circus. There were, Llewellyn conceded, a few types of true unilateral contracts; these would include offers of commissions to real estate brokers and the like, offers of rewards, etc. What these offers had in common, however, was not merely that acceptance could be made by performing, but the speculative nature of the offeror's performance. Where it is not at all certain that the offeree will be able to perform, *even if she wants to*, an offeror is unlikely to be interested in a mere promissory acceptance. What he wants is the specified performance; for that, and that alone, he is willing to pay the promised price. Professor Llewellyn's thesis is set forth throughout his article, *On Our Case-Law of Contract: Offer and Acceptance* (Pts. 1 & 2), 48 *Yale L.J.* 1, 779 (1938-1939), and is quoted and summarized in an article by Professor Mark Pettit, Jr., *Modern Unilateral Contracts*, 63 *B.U. L. Rev.* 551, 552-556 (1983). Influenced greatly by Professor Llewellyn's argument, the drafters of the Second Restatement abandoned the terminology he had attacked. Henceforth, they suggested, the terms *unilateral contract* and *bilateral contract* should generally be avoided, as "productive of confusion." See the Reporter's Note to Restatement (Second) §1, Comment *f*. Glimpses of the old unilateral contract can still be caught here and there in the revised Restatement, however. E.g., §32 (successor to former §31), Comment *b*: "Language or circumstances sometimes make it clear that the offeree is not to bind himself in advance of performance. . . . In such cases, the offer does not invite a promissory acceptance. . . ."

2. *Application to Cook*. Would the transaction in *Cook* fall within Professor Llewellyn's category of the "true" unilateral contract? Note that the court, referring to both Professors Williston and Corbin, indicates that in order to prevent revocation of the defendant's offer, plaintiff Cook had to have rendered "substantial" performance. Does §45 impose this requirement? Should it? (The phrase "substantial performance" has another application in determining remedies for breach of contract, which we will encounter later, in Chapter 10.)

3. *Modern use of unilateral contract analysis*. In his 1983 article, cited in Note 1, Professor Mark Pettit suggested that the obituary for the unilateral contract delivered in Restatement (Second) may have been a trifle premature. Despite the strictures of Professor Llewellyn and others, Pettit noted, judges persist in

27

**Making Contracts
(cnt'd)
A. Classic Contract
Consideration = 2
tests**

**Test 1 – benefit to promisor or detriment to promisee?
(Hamer v/ Sidway)**

Promise induces the consideration, consideration induces the promise

Court in role of policing the bargain (Where's the benefit?
Where's the detriment?)

Test 2 – Bargained for exchange – Rst 71

Promise for the promise, Promise for the performance –
importance of bargain element

More freedom in promise for promise. Little policing of the
bargain by the court.

With both tests, we are worried about a legal right.

Remember:

Usually the result is the same under benefit to promisor or
detriment to promisee test and bargain for exchange test for
consideration.

Making Contracts (cnt'd)

A. Classic Contract

Consideration = 2 tests

Test 1 – Benefit to Promisor or Detriment to Promisee

“A valuable consideration in the sense of the law may consist either in some right, interest, profit or benefit accruing to one party, or some forbearance, detriment, loss or responsibility given, suffered or undertaken by the other.” –
Hamer v/ Sidway

Test 2 – Bargained for exchange

§71. Requirement of Exchange; Types of Exchange

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

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

(3) The performance may consist of

(a) an act other than a promise, or

(b) a forbearance, or

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

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

29

Contracts in U.S. Common Law

Cases

to consideration as a basis for enforcement, however, the historical primacy of consideration doctrine in the classical contract system makes it of fundamental importance to our understanding of contractual obligation.

1. Defining Consideration

Hamer v. Sidway

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

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.

This action was brought upon an alleged contract.

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 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. . . . 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

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William E. Story, Sr., for 1875. She acquired it ory, 2d. The claim being appears that William E. at the celebration of the d mother of William E. sence of the family and l refrain from drinking, ds for money until he of \$5,000. The nephew inducing the promise. s and on the 31st day of t he had performed his d to the sum of \$5,000. n the sixth of February,

Buffalo, Feb. 6, 1875

nd all right, saying that go. I have no doubt but promised you I had the d for you, and you shall fere with this money in sooner that time comes e you start out in some ne year. . . . Willie, you you have earned much time and you are quite is 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 mcome 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.

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. 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."

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

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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 his 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). . . .

[The defendant also argued that even if the uncle's promise had originally given rise to an enforceable obligation, the plaintiff's action to enforce that promise was barred by the statute of limitations—too much time had passed since the cause of action arose. The court held, however, that the uncle's letter amounted to a "declaration of trust," making the uncle himself a "trustee" of the promised sum on behalf of his nephew as "beneficiary." The case thus was viewed not as the mere attempt to enforce an executory promise, but as an action to compel the delivery of a sum of money held in trust; the uncle's original promise was viewed as having in a legal sense already been performed. — Eds.]

The order appealed from should be reversed and the judgment of the Special Term affirmed, with costs payable out of the estate.

All concur.

Order reversed and judgment of Special Term affirmed.

Notes and Questions

1. *Hypothetical variations of Hamer.* (a) Recall our discussion of *Lucy v. Zehmer*, in the notes following the *Ray v. William G. Eurice & Bros., Inc.* case. Suppose that when young Mr. Story turned 21 and wrote his uncle, the uncle had responded (truthfully) that his "promise" of \$5000 had not been seriously intended, that it had been made only as a boast to impress the guests at the golden wedding celebration. Should the outcome of the case have been different?

(b) Suppose a modern-day *Hamer* case, in which the uncle, concerned about the effects of drug abuse, promises his fifteen-year-old nephew \$5000 if he refrains from using such drugs as marijuana, heroin, or cocaine at least until the age of 21. Suppose the nephew initially promises to refrain, and keeps that promise until age 21, but by that time the uncle has died, and his estate resists payment. Should the promise be enforced? What would be the legal arguments for and against enforcement? What would the policy arguments be? If consulted by the uncle at the outset, could you suggest ways in which the eventual enforcement of such a promise might be made more likely?

33

illusory promise doctrine is reserved the right to terminate without any period of notice to give notice a relatively long period, for example seven years, an illusory promise by definition that person or party cannot serve as other consideration. *Reyno Co.*, 64 F.2d 224 (9th Cir. 1934) (contractor's promise to construct bridge without consideration when time).

These doctrines are worth noting. Under a unilateral contract

If a promisor offers to perform a unilateral contract without seeking a return promise, performance constitutes both consideration for that promise. The defendant company argued that its promise was unenforceable because it gave the plaintiff the right to discharge him at any time. The court agreed with the plaintiff, but it still found the contract enforceable because the company continued to work for the plaintiff. In the instant case, the Company's promise to perform and ignore the fact of its own performance, is equally enforceable. *Durbin Food Corp.* case is frequently used where there is no return consideration in *Peterson v. Peterson*, above.)

These contracts do not impose a duty on the parties to make. See, e.g., *Restatement (Second) of Contracts* § 57 (Mont. 1999) (even if a dealer and defendant purchase contracts from plaintiff, agreement never sufficient to constitute a contract under HUD regulations if plaintiff in return for consideration provided by defendant for

enforcement of such output contracts, now

generally regarded as being enforceable despite the indefiniteness of commitment involved. See UCC § 2-306, discussed further in Chapter 6.

5. "Mutuality of obligation." Courts have sometimes also subjected contracts to a "mutuality of obligation" test, usually articulated as "both parties must be bound or neither is bound." As a broad generality, that is clearly an overstatement: We have already seen that unilateral contracts lack mutuality. A promisee under a unilateral contract is free to perform or not, while the promisor becomes bound once the promisee tenders a beginning of performance. As we shall see, many a promise is enforceable by a party who is not herself bound to performance in return. (E.g., the "promissory estoppel" case, where the relying promisee may be protected even in the absence of any commitment on her part.) The Restatement (Second) strongly asserts the absence of any "mutuality of obligation" test for contract enforcement; if the consideration requirement is met, it declares, that is enough. Restatement (Second) § 79(c). Nevertheless, some courts continue to apply a "mutuality of obligation" test for enforceability. E.g., *Pick Kwik Food Stores, Inc. v. Tenser*, 407 So. 2d 216 (Fla. Dist. Ct. App. 1981) (gasoline company could not enforce agreement for operation of pump on food store's premises where company had right to remove pump at any time); *Gull Laboratories, Inc. v. Diagnostic Technology, Inc.*, 695 F. Supp. 1151 (D. Utah, 1988) (distributorship agreement unenforceable against manufacturer for lack of consideration or mutuality; agreement did not bind distributor to order any goods).

Plowman v. Indian Refining Co.

United States District Court
20 F. Supp. 1 (E.D. Ill. 1937)

LINDLEY, District Judge.

Thirteen persons and the administrators of five deceased persons brought this suit, alleging that defendant, in 1930, made separate contracts to pay each of the individual plaintiffs and each of the deceased persons whose administrators sued, monthly sums equal to one-half of the wages formerly earned by such parties as employees of the defendant for life. Each of the claimants had been employed for some years at a fixed rate of wages, usually upon an hourly basis but payable monthly or semimonthly.

The theory of plaintiffs is that on July 28, 1930 (with two exceptions), the vice-president and general manager of the refinery plant called the employees, who had rendered long years of service separately into his office and made with each a contract, to pay him, for the rest of his natural life, a sum equal to one-half of the wages he was then being paid. The consideration for the contracts, it is said, arose out of the relationship then existing, the desire to provide for the future welfare of these comparatively aged employees and the provision in the alleged contracts that the employees would call at the office for their several checks each pay-day.

Most of the employees were participants in group insurance, the premiums for which had been paid approximately one-half by the employee

and one-half by the company, and, according to plaintiffs, their parts of the premiums were to be deducted from their payments as formerly. This procedure was followed.

The employees were retained on the pay roll, but, according to their testimony, they were not to render any further services, their only obligation being to call at the office for their remittances. Most of them testified that it was agreed that the payments were to continue throughout the remainder of their lives. But two testified that nothing was said as to the time during which the payments were to continue. As to still others the record is silent as to direct testimony in this respect.

The payments were made regularly until June 1, 1931, when they were cut off and each of the employees previously receiving the same was advised by defendant's personnel officer that the arrangement was terminated.

Defendant does not controvert many of these facts, but insists that the whole arrangement was included in a letter sent to each of the employees as follows:

Confirming our conversation of today, it is necessary with conditions as they are throughout the petroleum industry, to effect substantial economies throughout the plant operation. This necessitates the reducing of the working force to a minimum necessary to maintain operation. In view of your many years of faithful service, the management is desirous of shielding you as far as possible from the effect of reduced plant operation and has, therefore, placed you upon a retirement list which has just been established for this purpose.

Effective August 1, 1930, you will be carried on our payroll at a rate of \$_____ per month. You will be relieved of all duties except that of reporting to Mr. T. E. Sullivan at the main office for the purpose of picking up your semi-monthly checks. Your group insurance will be maintained on the same basis as at present, unless you desire to have it cancelled. (Signed by the vice-president.)

It contends and offered evidence that nothing was said to any employee about continuing the payments for his natural life; that the payments were gratuitous, continuing at the pleasure and will of defendant; that the original arrangement was not authorized, approved, or ratified by the board of directors, the executive committee thereof, or any officer endowed with corporate authority to bind the company; that there was no consideration for the promise to make the payments; and that it was beyond the power of any of the persons alleged to have contracted to create by agreement or by estoppel any liability of the company to pay wages to employees during the remainders of their lives, if they did not render actual services. Defendant admits the payments as charged and the termination of the arrangement on June 1, 1931.

The employees assert that there was ample authority in the vice-president and general manager to make a binding contract of the kind alleged to have existed; that, irrespective of the existence or nonexistence of such authority, the conduct of the company in making payment was ratification of the original agreement and that defendant is now estopped to deny validity of the same.

Plaintiff Kogan, an employee aged 72, testified that for some years prior to July 28, 1930, he had been employed as a drill pressman and in general repair work in the machine shops; that on July 28, 1930, he talked to Mr. Anglin, the vice-president and general manager, in the latter's private office; that Anglin

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paid at a rate of \$_____ per month to Mr. T. E. Sullivan at monthly checks. Your group unless you desire to have it

as said to any employee that the payments were made by defendant; that the original arrangement was approved by the board of directors and was not subject to the power of any of the directors or by estoppel during the remainders

Defendant admits the arrangement on June 1, 1931. Defendant's testimony in the vice-president's deposition of such authority, the invalidity of the original arrangement for some years prior to 1931 and in general repair work done at Mr. Anglin, the private office; that Anglin

said then that the oil industry was in a deplorable condition; that the management found it necessary to cut down expenses, and therefore, to lay off certain employees; that the witness was to be relieved of his duties, but that he would receive one-half of his salary and would be retained upon the pay roll; that this was being done because of the witness' many years of services; that the company did not desire to discharge him without further compensation; that he would be excused from all labor and required only to report to the main office to get his checks; that the company would carry his insurance in accord with previous practice; and that he would have all the privileges of hospitalization and in other respects of regular employees. The witness said he expressed his preference to work, but was told that that was impossible. He says that he was told that the arrangement was permanent, that is, for as long as he lived; that he would receive a letter confirming this conversation, which he should keep; that his labor would end on July 31, 1930; that he received the letter within a day or two; that thereafter he reported regularly at the office and obtained the checks until May 29, 1931, when he was told by the personnel department that the check then received would be the last one. This action, he said he was then told, was taken because of the necessity for further retrenchment. He testified that he sought no other employment; that nothing was said to him about working or not working for other parties, and that when he received the letter he kept it without comment or objection.

Other claimants testified substantially the same. . . .

In behalf of defendant, the assistant secretary testified that there were no minutes showing any corporate action with regard to the arrangement and that there was nothing in the records of the corporation, in bylaws, resolution or minutes authorizing, directing, or ratifying the payments or giving anybody authority to make the same. Anglin, vice-president and general manager in charge of manufacturing at the Lawrenceville Refinery where these men were employed, testified that he said to Kogan that, due to depressed conditions the company found it necessary to reduce expenses and lay off certain men; that it had no pension plan; that in an effort to be perfectly fair the company would keep him on the pay roll but relieve him of all duties except to pick up his check; that he said that the arrangement was voluntary with the company, and terminable at its pleasure, and that he hoped it would last during Kogan's lifetime, but that there might be a change in the policy of the company. His testimony as to the other employees was the same. He denied promising any of them that the payments would persist so long as they lived. He sent the letters as he promised confirming the arrangement. He testified that the letters were in compliance with what he had said; that no complaint or demand for any additional provisions was thereafter made; that he himself was employed orally; that he had no written contract; that he had no authority from the directors to make the arrangement; that he hired and fired men in Lawrenceville upon recommendation of the foreman; that a change in the management occurred when the Indian Refining Company was purchased by the Texas Company between October, 1930, and January, 1931; and that after the latter date he was not general manager at Lawrenceville. . . .

The present vice-president and general manager testified that he came into office January, 1931; and that no complaint was received by him by any plaintiff until suit was started.

Thus it is undisputed that a separate arrangement was made by the office with each of the claimants, most of them on July 28, 1930, to continue them upon the pay roll, deliver to them semimonthly a check, upon the calling for same, for one-half of the former wages; that this was done until June 1, 1931. It is also undisputed that the letters sent out said nothing about how long the payments should continue but were wholly silent in that respect. It is also undisputed that insurance payments were deducted from the checks which were delivered; that the employees were retained on the pay roll; that they did no active work after August 1, 1931 [sic; 1930?]; that they received the checks as mentioned; that the payments terminated on June 1, 1931; that most of them called at the office for their checks and received same; and that in at least two instances the checks were mailed. The controverted question of fact arises upon the testimony of most of the plaintiffs that each of them was told that the payments would continue until their death. This is denied.

Let us assume, without so deciding, for the purpose of disposition of this case, that each of the employees was told that the payments would continue for his lifetime. Then the questions remaining are legal in character. The arrangement was made by no corporate officer having authority to make such a contract. Under the bylaws, corporation transactions as recorded in the minutes, there was no authorization or ratification of any such contract. It is urged, however, that by continuing to pay the checks the corporation ratified the previously unauthorized action. The facts render such conclusion dubious. I am unable to see how knowledge of the mere fact that men's names were on the pay roll and checks paid to them could create any estoppel to deny authority, in the absence of proof of knowledge upon the part of the duly authorized officers of the company that the men were not working but were receiving in effect pensions or that they had been promised payments for life. Consequently, there was no ratification express or implied and no estoppel.

Presented also is the further question of whether, admitting the facts as alleged by plaintiffs, there was any consideration for a contract to pay a pension for life. However strongly a man may be bound in conscience to fulfill his engagements, the law does not recognize their sanctity or supply any means to compel their performance, except when founded upon a sufficient consideration. Volume 6, American & English Encyclopedia of Law, p.673 (2d Ed.)

The long and faithful services of the employees are relied upon as consideration; but past or executed consideration is a self-contradictory term. Consideration is something given in exchange for a promise or in a reliance upon the promise. Something which has been delivered before the promise is executed, and, therefore, made without reference to it, cannot properly be legal consideration. Williston on Contracts, vol. 1, §142; 13 Corpus Juris, 359; *Shields v. Clifton Hill Land Co.*, 94 Tenn. 123, 28 S.W. 668, 26 L.R.A. 523, 45 Am. St. Rep. 700; Restatement of the Law of Contracts, vol. 1, p.88.

It is further contended that there was a moral consideration for the alleged contracts. The doctrine of validity of moral consideration has received approval in some courts, but quite generally it is condemned because it is contrary in character to actual consideration. . . . Thus in *Hart v. Strong*, 183 Ill. 349, 55 N.E. 629, 631, the court said: "The agreement to receive less than the amount due on the note was made upon the purely moral consideration that John W. Hart, believing himself about to die, thought he ought not to have

ment was made by the local July 28, 1930, to continue monthly a check, upon their at this was done until June 1, but said nothing about how silent in that respect. It is deducted from the checks that on the pay roll; that they [?]; that they received their ted on June 1, 1931; that nd received same; and that re controverted question of tiffs that each of them was death. This is denied. pose of disposition of this yments would continue for legal in character. The ing authority to make such ctions as recorded in the of any such contract. It is ks the corporation ratified r such conclusion dubious. that men's names were on ate any estoppel to deny upon the part of the duly ere not working but were romised payments for life, implied and no estoppel. aer, admitting the facts as a contract to pay a pension n conscience to fulfill his ity or supply any means to on a sufficient considera- of Law, p.673 (2d Ed.) yees are relied upon as a self-contradictory term. a promise or in a reliance ered before the promise is to it, cannot properly be [42; 13 Corpus Juris, 359; W. 668, 26 L.R.A. 523, 45 acts, vol. 1, p.88. nsideration for the alleged nsideration has received condemned because it is us in Hart v. Strong, 183 sment to receive less than rely moral consideration ight he ought not to have

exacted so large a consideration for the reconveyance. But such an obligation does not form a valid consideration unless the moral duty were once a legal one. 'But the morality of the promise, however certain or however urgent the duty, does not, of itself, suffice for a consideration.' 1 Pars. Cont. 434."

Upon the same ground, appreciation of past services or pleasure afforded the employer thereby is not a sufficient consideration. . . . So Williston says (Contracts, vol. 1, p.230): ". . . if there be no legal consideration, no motive, such as love and respect, or affection for another or a desire to do justice, or fear of trouble, or a desire to equalize the shares in an estate, or to provide for a child, or regret for having advised an unfortunate investment, will support a promise."

Plaintiffs have proved that they were ready, willing, and able to travel to and report semimonthly to the main office. But this does not furnish a legal consideration. The act was simply a condition imposed upon them in obtaining gratuitous pensions and not a consideration. The employees went to the office to obtain their checks. Such acts were benefits to them and not detriments. They were detriments to defendant and not benefits. This is not consideration. Williston on Contracts, vol. 1, pp.231-235, and cases cited; Restatement of Contracts, par. 75, Illus. 2.

In the absence of valid agreement to make payments for the rest of their natural lives, clearly the arrangement was one revocable at the pleasure of defendant. If defendant agreed to make the payments for life, then, fatal to plaintiffs' cases is the lack of consideration. We have merely a gratuitous arrangement without consideration, and therefore, void as a contract.

In this enlightened day, I am sure, no one controverts the wisdom, justice, and desirability of a policy, whether promoted and fostered by industry voluntarily or by state or federal government, looking to the promotion and assurance of financial protection of deserving employees in their old age. We have come to realize that the industry wherein the diligent worker labors for many years should bear the cost of his living in some degree of comfort through his declining years until the end of his life. To impose this expense upon the industry, to the creation of whose product he has contributed, is not unfair or unreasonable, for, eventually, obviously, under wise budgeting and cost accounting systems, this element of cost is passed on to the consumer of the product. The public bears the burden—as, indeed, it does eventually of all governmental expenditures and corporate costs, either in taxes or price of products purchased. Surely no one would have the temerity to urge that such a policy is not more fair and reasonable, more humane and beneficent, than the poorhouse system of our earlier days. The recognition of the soundness of this proposition is justified by the resulting contribution to the advance of standards of living, hygienic and sanitary environment, and, in some degree at least, of culture and civilization.

But, in the absence of statute creating it, such a policy does not enter into the relationship of employer or employee, except when so provided by contract of the parties. The court is endowed with no power of legislation; nor may it read into contracts provisions upon which the parties' minds have not met.

Viewing the testimony most favorably for the plaintiffs, despite the desirability of the practice of liberality between employer and employee, the court must decide a purely legal question—whether under plaintiffs' theory

there were valid contracts. The obvious answer is in the negative. Consequently, there will be a decree in favor of defendant dismissing plaintiffs' bill for want of equity. The foregoing includes my findings of fact and conclusions of law.

Notes and Questions

1. *Consideration or condition?* The court holds that the plaintiffs' travel to the defendant's office, to pick up their checks, did not constitute consideration; it was "simply a condition imposed upon them in obtaining gratuitous pensions." Do you agree? Recall the analysis in *Pennsy Supply*, above.

2. *Hypothetical variations of Plowman.* The judge also dismisses (quoting Williston) the possibility that "love and respect, . . . affection for another or a desire to do justice" could amount to consideration; "legal consideration," he says, is necessary. It is frequently stated, however, that where bargained-for consideration is present, the fact that the promisor may have had some other motive or inducement for making the promise will not of itself defeat the agreement. See Restatement (Second) §81, and Comment *b*. Assuming that the principal motive for the defendant's promise may have been the welfare of its senior employees, should the promise have been enforceable if any of the following had also been part of the case?

- (a) Each promisee was required to pick up his check in person at the office of the defendant, at a time when the employees of the defendant would be picking up their regular paychecks.
- (b) Each pensioned employee was required, before receiving any payments, to submit a signed resignation, waiving all right to future employment with the defendant and any claim to wages or payments other than the promised "pension."
- (c) Each promisee was required, before receiving payments, to sign an agreement that he would, on request, assist in training new employees of the defendant (Would it matter whether the employees had ever been called on to do so?)

3. *"Past consideration."* The court also rejects the possibility that the "long and faithful service" of the plaintiffs could constitute consideration, using two related arguments. Services already performed could be, at best, only "past consideration," which is a "self-contradictory" term: Something already done cannot constitute consideration for a later promise. Nor can any "moral obligation" arising out of past faithful service constitute consideration, unless the "moral" duty was also a "legal" one. If this is indeed the law, *should* it be? Professor Charles Fried has argued that the making of a promise is an act that of itself creates a moral obligation that the law should respect and enforce.

The obligation to keep a promise is grounded not in arguments of utility but in respect for individual autonomy and in trust. Autonomy and trust are grounds for the institution of promising as well, but the argument for *individual* obligation is not the

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Making Contracts (cnt'd)

A. Classic Contract Formal Requirements

Statute of Frauds

§110. Classes of Contracts Covered

(1) The following classes of contracts are subject to a statute, commonly called the Statute of Frauds, forbidding enforcement unless there is a written memorandum or an applicable exception:

- (a) a contract of an executor or administrator to answer for a duty of his decedent (the executor-administrator provision);
- (b) a contract to answer for the duty of another (the suretyship provision);
- (c) a contract made upon consideration of marriage (the marriage provision);
- (d) a contract for the sale of an interest in land (the land contract provision);
- (e) a contract that is not to be performed within one year from the making thereof (the one-year provision).

(2) The following classes of contracts, which were traditionally subject to the Statute of Frauds, are now governed by Statute of Frauds provisions of the Uniform Commercial Code:

- (a) a contract for the sale of goods for the price of \$500 or more (Uniform Commercial Code §2-201);
- (b) a contract for the sale of securities (Uniform Commercial Code §8-319);
- (c) a contract for the sale of personal property not otherwise covered, to the extent of enforcement by way of action or defense beyond \$5,000 in amount of value of remedy (Uniform Commercial Code §1-206).

(3) In addition the Uniform Commercial Code requires a writing signed by the debtor for an agreement which creates or provides for a security interest in personal property or fixtures not in the possession of the secured party.

(4) Statutes in most states provide that no acknowledgment or promise is sufficient evidence of a new or continuing contract to take a case out of the operation of a statute of limitations unless made in some writing signed by the party to be charged, but that the statute does not alter the effect of any payment of principal or interest.

(5) In many states other classes of contracts are subject to a requirement of a writing.

§144. Effect of Unenforceable Contract as to Third Parties

Only a party to a contract or a transferee or successor of a party to the contract can assert that the contract is unenforceable under the Statute of Frauds.

Making Contracts (cnt'd) Alternatives to Classic Contract B. Promissory Estoppel

§90. Promise Reasonably Inducing Action or Forbearance

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

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

§139. Enforcement by Virtue of Action in Reliance

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

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

(a) the availability and adequacy of other remedies, particularly cancellation and restitution;

(b) the definite and substantial character of the action or forbearance in relation to the remedy sought;

(c) the extent to which the action or forbearance corroborates evidence of the making and terms of the promise, or the making and terms are otherwise established by clear and convincing evidence;

(d) the reasonableness of the action or forbearance;

(e) the extent to which the action or forbearance was foreseeable by the promisor.

41

Cases

some be fired or laid off. The stress and emotional trauma inherent in such a supervisory position cannot be measured in purely financial terms. Therefore, the presence of detrimental reliance in this case is a sufficiently disputed issue for the trier of fact that summary judgment cannot be granted to American Can Company

Id. at 919.

3. *Katz compared with Hayes.* Not all employees have been as successful as Mr. Katz. In *Hayes v. Plantations Steel Co.*, 438 A.2d 1091 (R.I. 1982), the plaintiff Hayes, after 25 years of employment, announced his decision to retire, effective in six months. One week before his actual date of retirement, Hayes met with an officer of the defendant company, who promised him that the company "would take care" of him. After Hayes's retirement, the company paid him a pension for four years but stopped doing so because of financial conditions and a change of ownership. The trial court ruled that the company was contractually bound to pay Hayes his pension, but the Supreme Court reversed. The Court first held that even if the company had made a promise, the promise was not supported by consideration. Citing the classical requirement of consideration as bargained-for exchange, the Court concluded that Hayes's retirement could not constitute consideration because he announced his decision before the company made its promise. For similar reasons the court rejected Hayes's promissory estoppel theory. Under that theory Hayes was required to show that the promise induced detrimental reliance, and he could not do so because his decision to retire preceded the promise. Do you think the factual differences between *Katz* and *Hayes* warrant different legal results? For further discussion and comparison of *Katz* and *Hayes*, see Charles L. Knapp, *Rescuing Reliance: The Perils of Promissory Estoppel*, 49 *Hastings L.J.* 1191, 1254-1261 (1998).

4. *Federal law governing benefit plans.* In 1974 Congress enacted the Employee Retirement Income Security Act of 1974 (commonly known as ERISA), 29 U.S.C. §1001 et seq. ERISA is a highly specialized body of law, but for our purpose it is sufficient to know that the act applies to an "employee benefit plan," a term that is broadly defined to include both retirement benefits and welfare benefits, such as medical insurance. Id. at §1002. Danny Dare's promise to Katz would not have been covered by ERISA because it did not amount to a "plan." To be an ERISA plan, the obligation requires the creation of an ongoing administrative program. A one-time obligation is not sufficient to amount to a plan. See *Fort Halifax Packing Co. v. Coyne*, 482 U.S. 1, 12 (1987).

Shoemaker v. Commonwealth Bank

Pennsylvania Superior Court
700 A.2d 1003 (1997)

JOHNSON, Judge:

We are asked to determine whether a mortgagor who is obligated by a mortgage to maintain insurance on the mortgaged property can establish a cause of action in promissory estoppel based upon an oral promise made by

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have been as successful as in *2d 1091 (R.I. 1982)*, the court pronounced his decision to be based on the actual date of retirement, not the date of retirement, who promised him that at retirement, the company would pay so because of financial distress. The court ruled that the company had made a promise, but the Supreme Court overruled that. Citing the classical contract law, the Court concluded that the promisee's consideration because he relied on its promise. For similar reasons, the court applied the promissory estoppel theory. Under that theory, if a promise induced detrimental reliance on to retire preceded the promise, as in *Katz and Hayes* warrant a comparison of *Katz* and *The Perils of Promissory*

the Congress enacted the ERISA (commonly known as the Employee Retirement Income Security Act of 1974) which created a specialized body of law, but it applies to an "employee" who is not an employee. Both retirement benefits and ERISA at §1002. *Danny Dare's* ERISA because it did not require the creation of a trust. The Supreme Court held that the ERISA preemption is not sufficient to preempt state law. *482 U.S. 1, 12 (1987)*.

or who is obligated by a contract to convey property can establish a claim for a oral promise made by

the mortgagee to obtain insurance. We find no merit in those portions of the instant case sounding in fraud and breach of contract. We conclude, nevertheless, that a mortgagee's promise to obtain insurance can be actionable on a theory of promissory estoppel. Accordingly, on this appeal from the order granting summary judgment to the mortgagee, we affirm in part, reverse in part and remand for further proceedings.

Lorraine and Robert S. Shoemaker obtained a \$25,000 mortgage on their home from Commonwealth Bank (Commonwealth). The mortgage agreement provided that the Shoemakers were required to "carry insurance" on the property. By January 1994, the Shoemakers had allowed the home-owners' insurance policy covering their home to expire. In 1995, the Shoemakers' home, still uninsured, was destroyed by fire. The parties disagree as to the series of events that occurred after the insurance had lapsed.

The Shoemakers allege that Commonwealth sent a letter to them, dated January 20, 1994, that informed them that their insurance had been cancelled and that if they did not purchase a new insurance policy, Commonwealth might "be forced to purchase [insurance] and add the premium to [their] loan balance." The Shoemakers further allege that Mrs. Shoemaker received a telephone call from a representative of Commonwealth in which the representative informed her that if the Shoemakers did not obtain insurance, Commonwealth would do so and would add the cost of the premium to the balance of the mortgage. The Shoemakers assert that they assumed, based on the letter and phone conversation, that Commonwealth had obtained insurance on their home. They also contend that they received no further contact from Commonwealth regarding the insurance and that they continued to pay premiums as a part of their loan payments. Only after the house burned, the Shoemakers allege, did they learn that the house was uninsured.

Commonwealth, on the other hand, admits that it sent the letter of January 20, but denies the Shoemakers' allegations regarding the contents of the alleged conversation between its representative and Mrs. Shoemaker. Commonwealth further claims that it obtained insurance coverage for the Shoemakers' home and notified them of this fact by a letter dated February 4, 1994. Commonwealth also asserts that it elected to allow this coverage to expire on December 1, 1994, and that, by the letter dated October 25, 1994, it informed the Shoemakers of this fact and reminded them of their obligation under the mortgage to carry insurance on the property. The Shoemakers deny receiving any letter from Commonwealth regarding the insurance other than the letter dated January 20, 1994, that informed them that their policy had expired.

After the house burned down, Mrs. Shoemaker sued Commonwealth, alleging causes of action in fraud, promissory estoppel and breach of contract; the basis for all three causes of action was Commonwealth's alleged failure to obtain insurance coverage for the Shoemaker home. By order of the court, Mr. Shoemaker was joined as an involuntary plaintiff. Commonwealth then filed a motion for summary judgment.

The trial court granted Commonwealth's motion. The court noted that, even if Commonwealth had promised to obtain insurance on the Shoemakers' home, it made no representation regarding the duration of that coverage. The court concluded that because Commonwealth had actually obtained insurance,

44

even though the policy later expired, it had fulfilled its promise to the Shoemakers. Thus, the court reasoned that because Commonwealth had made no misrepresentation and breached no promise, the Shoemakers could not prevail on any of their causes of action. Mrs. Shoemaker now appeals. . . .

[The court first ruled that the trial court was correct in granting summary judgment for the bank on the Shoemakers' fraud claim. While Mrs. Shoemaker testified that the bank's representative had "said that they would acquire insurance for me," summary judgment was proper because as a matter of law "the breach of a promise to do something in the future is not actionable in fraud." — Eds.]

Mrs. Shoemaker next argues that the trial court erred by granting summary judgment on their promissory estoppel claim. The doctrine of promissory estoppel allows a party, under certain circumstances, to enforce a promise even though that promise is not supported by consideration. See *Thatcher's Drug Store of West Goshen, Inc. v. Consolidated Supermarkets, Inc.*, 535 Pa. 469, 476, 636 A.2d 156, 160 (1994); Restatement (Second) of Contracts §90. To establish a promissory estoppel cause of action, a party must prove that: (1) the promisor made a promise that he should have reasonably expected would induce action or forbearance on the part of the promisee; (2) the promisee actually took action or refrained from taking action in reliance on the promise; and (3) injustice can be avoided only by enforcing the promise. *Holewinski v. Children's Hospital of Pittsburgh*, 437 Pa. Super. 174, 178, 649 A.2d 712, 714 (1994), appeal denied, 540 Pa. 641, 659 A.2d 560 (1995); *Cardamone v. University of Pittsburgh*, 253 Pa. Super. 65, 74, 384 A.2d 1228, 1233 (1978).

In their complaint, the Shoemakers allege that Commonwealth promised that it would purchase "adequate insurance" and add the cost of the premium to the cost of their loan. They further allege that they relied on this promise by not purchasing the insurance on their own and that injustice can be avoided only by enforcing Commonwealth's promise. Commonwealth, on the other hand, argues that the Shoemakers cannot enforce their claim through promissory estoppel because of the Shoemakers' contractual obligation to maintain insurance under the mortgage. Further, Commonwealth argues that even if such a promise was actionable, the facts alleged by the Shoemakers are insufficient to support their claim because they have not alleged that Commonwealth promised to maintain such insurance for a particular duration.

Our research has not discovered any Pennsylvania cases that have addressed the question of whether a mortgagor who is obligated by a mortgage to maintain insurance on their property can establish a cause of action in promissory estoppel based upon an oral promise made by the mortgagee to obtain insurance. We have, however, discovered cases from other jurisdictions that have addressed this question, and the weight of this authority holds that such promises are actionable.

In *Graddon v. Knight*, 138 Cal. App. 2d 577, 292 P.2d 632 (1956), a California appellate court considered whether homeowners, who were obligated under a deed of trust to procure and maintain fire insurance on their home, could establish a cause of action based upon an oral promise by a bank to obtain the insurance on the homeowners' behalf. The court first

considered whether the bank's promise was inconsistent with its obligation to maintain the insurance; the court concluded that the bank's promise was not inconsistent with its obligation to maintain the insurance; the court then considered whether the bank's promise was sufficient to support the plaintiffs' claim. The court concluded that the bank's promise was sufficient to support the plaintiffs' claim. The court then considered whether the bank's promise was enforceable under the doctrine of promissory estoppel. The court concluded that the bank's promise was enforceable under the doctrine of promissory estoppel.

The mortgagee's promise to obtain insurance on the mortgagor's behalf is enforceable under the doctrine of promissory estoppel.

Restatement (Second) of Contracts §90. To establish a promissory estoppel cause of action, a party must prove that: (1) the promisor made a promise that he should have reasonably expected would induce action or forbearance on the part of the promisee; (2) the promisee actually took action or refrained from taking action in reliance on the promise; and (3) injustice can be avoided only by enforcing the promise.

We must first determine whether the bank's promise to obtain insurance on the mortgagor's behalf is enforceable under the doctrine of promissory estoppel. The bank's promise to obtain insurance on the mortgagor's behalf is enforceable under the doctrine of promissory estoppel because the bank's promise was sufficient to support the mortgagor's claim. The bank's promise to obtain insurance on the mortgagor's behalf is enforceable under the doctrine of promissory estoppel because the bank's promise was sufficient to support the mortgagor's claim. The bank's promise to obtain insurance on the mortgagor's behalf is enforceable under the doctrine of promissory estoppel because the bank's promise was sufficient to support the mortgagor's claim.

fulfilled its promise to the Commonwealth had made the Shoemakers could not make now appeals. . . . It is not correct in granting summary judgment on the fraud claim. While Mrs. Shoemaker had "said that they would not sue because as a matter of course the future is not actionable

the court erred by granting summary judgment on the fraud claim. The doctrine of promissory estoppel, in certain circumstances, to enforce a promise not made by consideration. See *Restatement (Second) of Contracts* § 336(1); *Restatement (Second) of Contracts* § 336(1); *Restatement (Second) of Contracts* § 336(1). Cause of action, a party must show that he should have reasonably expected the part of the promisee to take action in reliance on the promise. *Restatement (Second) of Contracts* § 336(1); *Restatement (Second) of Contracts* § 336(1); *Restatement (Second) of Contracts* § 336(1). See also *Murphy v. Burke*, 454 Pa. 391, 398, 311 A.2d 904, 908 (1973) (adopting section 90 of the Restatement (Second) of Contracts).

Commonwealth promised to add the cost of the premium on the mortgage. The Shoemakers relied on this promise because that injustice can be avoided. Commonwealth, on the other hand, would force their claim through the courts. Commonwealth's contractual obligation to add the cost of the premium on the mortgage is not a promise. Commonwealth argues that the Shoemakers are not bound by the Shoemakers' promise because they have not alleged that the bank promised to add the cost of the premium on the mortgage for a particular

Pennsylvania cases that have held that a promisee who is obligated by a promise can establish a cause of action for promissory estoppel. *Restatement (Second) of Contracts* § 336(1); *Restatement (Second) of Contracts* § 336(1); *Restatement (Second) of Contracts* § 336(1). See also *Murphy v. Burke*, 454 Pa. 391, 398, 311 A.2d 904, 908 (1973) (adopting section 90 of the Restatement (Second) of Contracts). The Shoemakers allege that they actually relied upon Commonwealth's promise and, thus, failed to obtain insurance. In support of this allegation, Mrs. Shoemaker testified in her deposition and swore in her affidavit that she instructed Commonwealth's representative to acquire insurance on her behalf.

considered whether the bank's promise to obtain fire insurance was inconsistent with the term of the deed of trust that required the homeowners to [maintain the insurance. The court] concluded that the bank's promise was not inconsistent with the homeowners' obligation under the deed of trust because the deed required only that the homeowners procure and maintain insurance; the deed did not bar them from making a separate agreement under which another party would procure the insurance on their behalf. *Id.* at 635-36. The court then held that the evidence presented by the plaintiffs was sufficient to establish a cause of action in promissory estoppel because the plaintiffs relied to their detriment on the bank's promise to obtain insurance. *Id.* at 636-37. . . . In accord with these cases, illustration 13 to comment e of section 90 of the Restatement (Second) of Contracts provides:

"A, a bank, lends money to B on the security of a mortgage on B's new home. The mortgage requires B to insure the property. At the closing of the transaction A promises to arrange for the required insurance, and in reliance on the promise B fails to insure. Six months later the property, still uninsured, is destroyed by fire. The promise is binding.

Restatement (Second) of Contracts §90, cmt. e, illus. 13. See also *Murphy v. Burke*, 454 Pa. 391, 398, 311 A.2d 904, 908 (1973) (adopting section 90 of Pennsylvania law). We find this authority persuasive and thus we reject Commonwealth's claim that the Shoemakers cannot maintain a cause of action because of their obligation under the mortgage to maintain insurance on the property.

We must next determine whether the Shoemakers' allegations and the evidence that they have presented are sufficient to create genuine issues of material fact with regard to each element of a promissory estoppel cause of action and thus survive Commonwealth's motion for summary judgment. The first element of a promissory estoppel cause of action is that the promisor made a promise that he should reasonably have expected to induce action or forbearance on the part of the promisee. *Holewinski*, supra, at 178, 649 A.2d at 714. The Shoemakers have alleged that the bank promised to obtain insurance on their behalf and that it would add this cost to their mortgage payment. Mrs. Shoemaker testified in her deposition and swore in an affidavit that a representative from Commonwealth stated that the bank would acquire insurance if she did not and that she instructed the representative to take that action. Because the Shoemakers claim that Commonwealth's promise to obtain insurance was, essentially, conditioned upon the Shoemakers' course of conduct, i.e., that Commonwealth would obtain insurance if they did not, we conclude that this evidence, if believed, would be sufficient to allow a jury to find that Commonwealth made a promise upon which it reasonably should have expected the Shoemakers to rely. See *Holewinski*, supra.

The second element of a promissory estoppel cause of action is that the promisee actually relied upon the promise. *Id.* at 178, 649 A.2d at 714. The Shoemakers allege that they actually relied upon Commonwealth's promise and, thus, failed to obtain insurance. In support of this allegation, Mrs. Shoemaker testified in her deposition and swore in her affidavit that she instructed Commonwealth's representative to acquire insurance on her behalf.

46

We conclude that this evidence, if believed, would be sufficient to allow a jury to find that the Shoemakers relied upon Commonwealth's promise to obtain insurance. See *Holewinski*, supra.

The final element of a promissory estoppel cause of action is that injustice can be avoided only by enforcement of the promise. *Id.* at 178, 649 A.2d at 714. One of the factors that a court may consider in determining whether a promisee has satisfied this element is "the reasonableness of the promisee's reliance." *Thatcher's Drug Store*, supra, at 477, 636 A.2d at 160, quoting Restatement (Second) of Contracts §90, cmt. b. Mrs. Shoemaker testified that she and her husband received no communication from Commonwealth regarding their insurance after her conversation with a Commonwealth representative in early 1994. Commonwealth, on the other hand, asserts that it sent the Shoemakers letters informing them that their house would be uninsured after December 1, 1994. We conclude that this evidence is sufficient to create a genuine issue of material fact regarding the reasonableness of the Shoemakers' reliance. Accordingly, we hold that the trial court erred by granting summary judgment on the Shoemakers' promissory estoppel claim.

...

We therefore reverse that portion of the trial court's order that granted summary judgment on the Shoemakers' promissory estoppel claim and remand for trial on that claim. We affirm the grant of summary judgment on the Shoemakers' fraud and breach of contract claims.

...

Notes and Questions

1. *Analyzing Shoemaker*. Consider the following questions:

- Although the court does not focus on this fact, Mrs. Shoemaker testified at her deposition that she could not have gotten home owners' insurance on her own: "I told them go ahead and do so because at that point I was in no financial situation to do so on my own." 700 A.2d at 1006. Is this fact legally significant? Why?
- The court mentions but does not address the bank's argument that a cause of action for promissory estoppel did not lie because, even if the bank made a promise to obtain insurance for the Shoemakers, the promise did not have a duration. What response would you give to this argument?
- A significant issue in the case revolves around the alleged letter from the bank dated October 25, 1994. The bank claims that in this letter it informed the Shoemakers that they would be required to maintain insurance on their home after December 1, 1994. Mrs. Shoemaker testified that she never received this letter. What lawyering lessons can you learn from this factual dispute?
- Suppose the mortgage documents signed by the Shoemakers stated that no agreement or modification would be legally binding on the bank unless set forth in a writing signed by the bank. Should such a

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is sufficient to allow a jury to find that the bank's promise to obtain

provision have been relevant to the Shoemakers' claim? Why? Should it have been conclusive? Why?

of action is that injustice. See, e.g., *Id.* at 178, 649 A.2d at 160. In determining whether a breach of promise is actionable, see 36 A.2d at 160, quoting *Shoemaker*. Shoemaker testified that the bank's promise to obtain a loan from Commonwealth Bank with a Commonwealth Bank guarantee. On the other hand, she asserts that the bank's promise that their house would be sold at this evidence is sufficient to find the reasonableness of the bank's promise. The trial court erred by granting promissory estoppel claim.

The court's order that granted promissory estoppel claim and summary judgment on the merits.

Legal questions:

On this fact, Mrs. Shoemaker did not have gotten home to see them go ahead and do so in a similar situation to do so on my own. Is this significant? Why?

The bank's argument that a promise is not binding because, even if the promise is for the Shoemakers, the bank's response would you give to

and the alleged letter from the bank claims that in this letter it would be required to maintain the promise. See, e.g., *Jones v. Best*, 1994. Mrs. Shoemaker: What lawyering lessons can be learned from this case?

by the Shoemakers stated. Is the promise legally binding on the bank? Should such a

2. *Promissory fraud.* The court states that the Shoemakers' allegations against the bank were legally insufficient to establish fraud because they had alleged nothing more than a breach of promise by the bank to do something in the future. As the court states, while a breach of promise may be actionable under either a contract or promissory estoppel theory, it is not normally actionable as fraud because fraud requires a misrepresentation of a present fact rather than a promise to do something in the future. In some cases, however, a breach of promise may be fraudulent—if the promisor did not intend to perform the promise at the time the promise was made. In such a case, the promisor has misrepresented a present fact, namely the promisor's intention to perform the promise. Restatement (Second) of Torts §530 provides as follows: "A representation of the maker's own intention to do or not to do a particular thing is fraudulent if he does not have that intention." See, e.g., *Gerhardt v. Harris*, 934 P.2d 976 (Kan., 1997) (client stated cause of action for fraud against lawyer when client alleged that lawyer promised to abide by decision of fee dispute board without intention of doing so).

3. *The functions of form.* Recall Professor Fuller's suggestion that legal "forms" (in which category he suggested "consideration" might be placed) serve a variety of functions in a legal system, among them the "cautionary" function of "acting as a check against inconsiderate action," and also the "channeling" function of distinguishing conduct that has legal consequences from conduct that does not. Does the promissory estoppel cause of action as applied by the court in *Shoemaker* serve these purposes?

4. *Other commercial cases.* Since its promulgation in the 1930s, §90 has been applied to enforce a wide variety of promises in commercial situations. See, e.g., *Cohen v. Cowles Media Co.*, 479 N.W.2d 387 (Minn., 1992) (news source allowed to recover on promissory estoppel theory from newspaper that breached promise of confidentiality); *Chesus v. Watts*, 967 S.W.2d 97 (Mo. Ct. App., 1998) (homeowners association had standing to bring promissory estoppel claim against developers to enforce promise to turn over common areas in good repair).

On the other hand, it should not be thought that the mere mention of promissory estoppel will cause a court to roll over and play dead. Courts have typically denied recovery when the defendant failed to make a promise on which liability could be based or when the plaintiff failed to establish detrimental reliance. See, e.g., *Creative Demos, Inc. v. Wal-Mart Stores, Inc.*, 142 F.3d 367 (7th Cir., 1998) (food demonstration contractor failed to establish detrimental reliance element of promissory estoppel claim against grocery store chain for refusal to honor promise to retain contractor's services through specific date when contractor continued to earn substantial profit after promise was made); *Jones v. Best*, 950 P.2d 1 (Wash., 1998) (en banc) (vendor's promissory estoppel defense against real estate agent failed because evidence showed that real estate agent did not make promise to accept reduced commission).

5. *The Restatement (Second) view of promissory estoppel.* In light of the widespread acceptance of promissory estoppel as enunciated in §90 of the first Restatement, it is not surprising that the drafters of the Restatement (Second)

48

chose to retain and expand the doctrine. As we noted earlier, the new §90 has an additional subsection providing for enforcement of charitable subscriptions even without a showing of detrimental reliance. In addition, the drafter revised the text of §90 by adding a reference to the possibility of third-party reliance, by indicating that the remedy to be awarded "may be limited as justice requires," and by deleting the requirement that reliance to be protectible must be "definite and substantial." Various aspects of the Restatement (Second) approach to promissory estoppel are considered in Charles L. Knapp, *Reliance in the Revised Restatement: The Proliferation of Promissory Estoppel*, 81 Colum. L. Rev. 52 (1981). On the issue of third-party recovery, see Michael B. Metzger & Michael J. Phillips, *Promissory Estoppel and Third Parties*, 42 Sw. L.J. 931 (1988).

6. *The CISG and promissory estoppel*. In *Geneva Pharmaceuticals Technology Corp. v. Barr Laboratories*, 201 F. Supp.2d 236 (S.D.N.Y. 2002), plaintiff pharmaceutical manufacturer asserted a variety of claims against defendant competitor and raw material supplier, including antitrust, breach of contract, and tort. Because the plaintiff was an American corporation and the defendant Canadian, the CISG governed their contractual relations, and preempted the plaintiff's state law contract claims. Plaintiff's tort claims, on the other hand, were clearly not preempted. The plaintiff also asserted a promissory estoppel claim, however, and the court had to decide whether that was preempted along with the contract claim. Noting that the CISG in Article 16(2)(b) recognizes reliance, the court indicated that perhaps a reliance claim intended to establish a "firm offer" would be preempted by that provision (Compare CISG Art. 16(2)(b) to Restatement (Second) §87(2), which we considered in the previous chapter.) Here, however, the plaintiff's claim of promissory estoppel was a more general one asserted to make a promise binding, and the court held such a claim not to be preempted by the CISG.

Comment: The Status and Future of Promissory Estoppel

In its infancy, promissory estoppel was generally regarded as a principle to which the court should resort only after conventional contract analysis had failed to produce recovery; its function was to serve as a "substitute" for some element of the classical system that was insufficiently satisfied by the case at hand. As the doctrine developed over the years, it came to have an independent significance, to be viewed not just as a subcategory of "contract" but as a distinct theory of action—one not necessarily grounded in the principles of contract or circumscribed by its limitations. An exploration of this development can be found in an article by Professors Michael Metzger and Michael Phillips, *The Emergence of Promissory Estoppel as an Independent Theory of Recovery*, 35 Rutgers L. Rev. 472 (1983). See also Kevin M. Teeven, *A History of Promissory Estoppel: Growth in the Face of Doctrinal Resistance*, 72 Tenn. L. Rev. 1111 (2005).

The remarkable growth and expansion of promissory estoppel since its incorporation in the first Restatement led Professor Knapp to conclude in 1981 that promissory estoppel had become "perhaps the most radical and

expansive development" (Charles L. Knapp, *Reliance in the Revised Restatement: The Proliferation of Promissory Estoppel*, 81 Colum. L. Rev. 52 (1981)). Professor Knapp suggests that the 1980 Restatement may have been a "rescue" (Charles L. Knapp, *Rescue in Contract Law During the 1980s*, 219-220 (1990) (favoring developments). Two appraisals of the current state of the doctrine, commentary, and relative importance of the doctrine.

Since the early 1980s, the foundations of promissory estoppel have been re-examined and has instead become a more prominent feature in contract cases. Jay M. Byrnes, *Contract Law: A Modern and Judicial Method*, 97 (1985) and the various modes of decision-making produce either certain or uncertain results. Contending that Karl Llewellyn believed that reliance should be a more significant theory of action (Michael Gibson, *Promissory Estoppel (Third) of the Restatement (Third) of Contracts*, 1985). Professors Daniel and Jay Byrnes, *Promissory Estoppel Case Law: A Survey of the Courts Enforcing the Doctrine in the Absence of Reliance*, 1985.

The traditional view of promissory estoppel is based on the idea of reliance. By far the most common category of promises for other consideration is the promise of reliance, in order to produce a result governed by present contract law. Promissory estoppel. Here, the promisee who has relied on the promise. Based on our survey of the cases, promissory estoppel is less commonly enforced with only the few cases based on the idea of reliance. The damages are the same as for promissory estoppel. Promissory estoppel is not a separate theory of action. Enforcing promises differs from enforcing contracts. Sharing a common goal of economic actors. Trust is

Making Contracts (cnt'd) Alternatives to Classic Contract C. Restitution

1. Restitution in the absence of a promise

a) Implied in Fact

“Where a person performs services at another’s request, or
Where services are rendered by one person for another without his expressed request, but
with his knowledge, and under circumstances fairly raising the presumption that the
parties understood and intended that compensation was to be paid. In these
circumstances the law implies the promise to pay a reasonable amount for the services..”
Commerce Partnership 8098 Limited Partnership v/ Equity Contracting Co. Inc

b) Implied in Law

- 1) the plaintiff has conferred a benefit on the defendant;
- 2) the defendant has knowledge of the benefit
- 3) the defendant has accepted or retained the benefit conferred, and
- 4) the circumstances are such that it would be inequitable for the defendant to retain the benefit without paying fair value for it.

2. Promissory Restitution

a) **Moral Obligation + Promise** Rst 82, Rst 83 (debts of bankrupts, tolled by statute of limitations and infants)

b) **Material benefit rule = Material benefit + promise (Rst 86)**

Making Contracts (cnt'd)

Meaning and Interpretation

§201. Whose Meaning Prevails

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

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

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

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

(3) Except as stated in this Section, neither party is bound by the meaning attached by the other, even though the result may be a failure of mutual assent.

§203. Standards of Preference in Interpretation

In the interpretation of a promise or agreement or a term thereof, the following standards of preference are generally applicable:

(a) an interpretation which gives a reasonable, lawful, and effective meaning to all the terms is preferred to an interpretation which leaves a part unreasonable, unlawful, or of no effect;

(b) express terms are given greater weight than course of performance, course of dealing, and usage of trade, course of performance is given greater weight than course of dealing or usage of trade, and course of dealing is given greater weight than usage of trade;

(c) specific terms and exact terms are given greater weight than general language;

(d) separately negotiated or added terms are given greater weight than standardized terms or other terms not separately negotiated.

Making Contracts (cnt'd)

Parol Evidence Rule

§213. Effect of Integrated Agreement on Prior Agreements (Parol Evidence Rule)

(1) A binding integrated agreement discharges prior agreements to the extent that it is inconsistent with them.

(2) A binding completely integrated agreement discharges prior agreements to the extent that they are within its scope.

(3) An integrated agreement that is not binding or that is voidable and avoided does not discharge a prior agreement. But an integrated agreement, even though not binding, may be effective to render inoperative a term which would have been part of the agreement if it had not been integrated.

§214. Evidence of Prior or Contemporaneous Agreements and Negotiations

Agreements and negotiations prior to or contemporaneous with the adoption of a writing are admissible in evidence to establish

- (a) that the writing is or is not an integrated agreement;
- (b) that the integrated agreement, if any, is completely or partially integrated;
- (c) the meaning of the writing, whether or not integrated;
- (d) illegality, fraud, duress, mistake, lack of consideration, or other invalidating cause;
- (e) ground for granting or denying rescission, reformation, specific performance, or other remedy.

§215. Contradiction of Integrated Terms

Except as stated in the preceding Section, where there is a binding agreement, either completely or partially integrated, evidence of prior or contemporaneous agreements or negotiations is not admissible in evidence to contradict a term of the writing.

Cases

in its present version by evidence may also be embodied in evidence, which are applied in its commonly employed mode is considered by authorities of evidence, but a rule of evidence, §7.2 (4th ed. 2004). This although it does have some primary rules of evidence, the not asserted at the time when case with evidence admitted. See Estate of Parker, v. evidence rule is matter of rule, even though without de before case submitted to e required to follow state cases involving diversity of f the parol evidence rule. sociates, Inc., 44 F.3d 572

various sources, and the nt (Second) of Contracts he gist of it can be stated agreed to incorporate (or ment in a writing, neither nt that written agreement greements or negotiations inal only with respect to a ontradicted, but it may be t discussions of the parol Contracts §§7.2 -7.6 (4th llo on Contracts §§3.2-3.8 ical origins of the rule, as for present-day contract ment: A New Historicist nder in Mind, 13 Am.

parol evidence rule, it is rule does not define what es to *exclude* evidence onally probative of some n a given situation, it has y into court extrinsic (or the written agreement at evidence is offered to the parol evidence rule executed such a written ithin some exception to n the body of rules that

collectively make up the law of evidence. Of course, even if the offered parol evidence is ruled admissible and received into evidence, that alone may not prove decisive; Like any other evidence, it may still be rejected as not credible by the trier of fact.

To begin our examination of the parol evidence rule in action, let us first envision the procedural setting in which a parol evidence issue arises. Suppose the owner of an apartment project enters into a written contract with a painting contractor calling for the painting of the "interior of the building, including walls, ceilings, and trim." Later, a dispute develops about whether the contract requires the contractor to paint the common areas (hallways, etc.). When the parties are unable to resolve the dispute through negotiation, the owner discharges the contractor, who then brings suit against the owner claiming that the discharge constitutes a breach of contract. At trial the contractor offers to introduce evidence (either oral testimony or correspondence) that the owner was informed (at or before the time of contracting) that the contractor's bid for the work did not include common areas, and the owner agreed to that. The owner objects to such evidence being considered by the fact finder because of the parol evidence rule. If the matter were being tried before a jury, the judge would hold an "in camera" hearing, that is, out of the presence of the jury, in which the party offering parol evidence would outline what the evidence would show, both parties would make legal arguments about the application of the parol evidence rule, and the judge would decide if the evidence were admissible under the rule. (Such in camera hearings are not unique to contract law but are employed whenever evidence of doubtful admissibility is being offered by one of the parties; another common example is the determination of the admissibility of an alleged confession by a defendant in a criminal case.) If the matter were being tried by a judge sitting without a jury, the in camera hearing would be unnecessary, but the judge would still be required to rule on the admissibility of the evidence. You may wonder why in nonjury cases the judge must rule on the admissibility of the evidence since the judge will have heard the evidence no matter how he rules. Even in nonjury cases, however, the admissibility of evidence can be important. If a judge reaches a decision based on evidence that was not properly admitted, the judge's decision could be reversed on appeal under the "clearly erroneous" rule for appellate review of trial court factual determinations.

We will see that both courts and commentators differ widely over the scope and application of the parol evidence rule. The following case illustrates the classical approach.

Thompson v. Libby
Minnesota Supreme Court
 34 Minn. 374, 26 N.W. 1 (1885)

MITCHELL, J. The plaintiff being the owner of a quantity of logs marked "H. C. A.," cut in the winters of 1882 and 1883, and lying in the Mississippi river, or on its banks, above Minneapolis, defendant and the plaintiff, through

54

his agent, D. S. Mooers, having fully agreed on the terms of a sale and purchase of the logs referred to, executed the following written agreement:

AGREEMENT

Hastings, Minn., June 1, 1883.

I have this day sold to R. C. Libby, of Hastings, Minn., all my logs marked "H. C. A.," cut in the winters of 1882 and 1883, for ten dollars a thousand feet, boom scale at Minneapolis, Minnesota. Payments cash as fast as scale bills are produced.

[Signed] J. H. Thompson,
Per D. S. Mooers,
R. C. Libby

This action having been brought for the purchase-money, the defendant—having pleaded a warranty of the quality of the logs, alleged to have been made at the time of the sale, and a breach of it—offered on the trial oral testimony to prove the warranty, which was admitted, over the objection of plaintiff that it was incompetent to prove a verbal warranty, the contract of sale being in writing. This raises the only point in the case.

No ground was laid for the reformation of the written contract, and any charge of fraud on part of plaintiff or his agent in making the sale was on the trial expressly disclaimed. No rule is more familiar than that "parol contemporaneous evidence is inadmissible to contradict or vary the terms of a valid written instrument," and yet none has given rise to more misapprehension as to its application. It is a rule founded on the obvious inconvenience and injustice that would result if matters in writing, made with consideration and deliberation, and intended to embody the entire agreement of the parties, were liable to be controlled by what Lord Coke expressively calls "the uncertain testimony of slippery memory." Hence, where the parties have deliberately put their engagements into writing in such terms as to import a legal obligation, without any uncertainty as to the object or extent of such engagement, it is conclusively presumed that the whole engagement of the parties, and the manner and extent of their undertaking, was reduced to writing. 1 Greenl. Ev. §275. Of course, the rule presupposes that the parties intended to have the terms of their complete agreement embraced in the writing, and hence it does not apply where the writing is incomplete on its face and does not purport to contain the whole agreement as in the case of mere bills of parcels, and the like.

But in what manner shall it be ascertained whether the parties intended to express the whole of their agreement in writing? It is sometimes loosely stated that where the whole contract be not reduced to writing, parol evidence may be admitted to prove the part omitted. But to allow a party to lay the foundation for such parol evidence by oral testimony that only part of the agreement was reduced to writing, and then prove by parol the part omitted, would be to work in a circle, and to permit the very evil which the rule was designed to prevent. The only criterion of the completeness of the written contract as a full expression of the agreement of the parties is the writing itself. If it imports on its face to be a complete expression of the whole

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terms of a sale and written agreement:

Minn., June 1, 1883.

all my logs marked thousand feet, boom bills are produced,

J. H. Thompson,

Per D. S. Mooers

R. C. Libby

e-money, the defense logs, alleged to have been offered on the trial oral over the objection of y, the contract of sale

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agreement,—that is, contains such language as imports a complete legal obligation,—it is to be presumed that the parties have introduced into it every material item and term; and parol evidence cannot be admitted to add another term to the agreement, although the writing contains nothing on the particular one to which the parol evidence is directed. The rule forbids to add by parol where the writing is silent, as well as to vary where it speaks,—2 Phil. Evidence, (Cow. & H. Notes,) 669; Naumberg v. Young, 44 N.J. Law, 331; Hei v. Heller, 53 Wis 415,—and the law controlling the operation of a written contract becomes a part of it, and cannot be varied by parol any more than what is written. 2 Phil. Ev. (Cow. & H. Notes,) 668; La Farge v. Rickert, 5 Wend, 187; Creery v. Holly, 14 Wend. 26; Stone v. Harmon, 31 Minn. 512.

The written agreement in the case at bar, as it appears on its face, in connection with the law controlling its construction and operation, purports to be a complete expression of the whole agreement of the parties as to the sale and purchase of these logs, solemnly executed by both parties. There is nothing on its face (and this is a question of law for the court) to indicate that it is a mere informal and incomplete memorandum. Parol evidence of extrinsic facts and circumstances would, if necessary, be admissible, as it always is, to apply the contract to its subject-matter, or in order to a more perfect understanding of its language. But in that case such evidence is used, not to contradict or vary the written instrument, but to aid, uphold, and enforce it as it stands. The language of this contract "imports a legal obligation, without any uncertainty as to its object or the extent of the engagement," and therefore "it must be conclusively presumed that the whole engagement of the parties, and the manner and extent of the undertaking, was reduced to writing." No new term, forming a mere incident to or part of the contract of sale, can be added by parol. . . .

[W]e are referred to a few cases which seem to hold that parol evidence of a warranty is admissible on the ground that a warranty is collateral to the contract of sale, and that the rule does not exclude parol evidence of matters collateral to the subject of the written agreement. It seems to us that this is based upon a misapprehension as to the sense in which the term "collateral" is used in the rule invoked. There are a great many matters that, in a general sense, may be considered collateral to the contract; for example, in the case of leases, covenants for repairs, improvements, payment of taxes, etc., are, in a sense, collateral to a demise of the premises. But parol evidence of these would not be admissible to add to the terms of a written lease. So, in a sense, a warranty is collateral to a contract of sale, for the title would pass without a warranty. It is also collateral in the sense that its breach is no ground for a rescission of the contract by the vendor [*sic*; vendee?], but that he must resort to his action on the warranty for damages. But, when made, a warranty is a part of the contract of sale. The common sense of men would say, and correctly so, that when, on a sale of personal property, a warranty is given, it is one of the terms of the sale, and not a separate and independent contract. To justify the admission of a parol promise by one of the parties to a written contract, on the ground that it is collateral, the promise must relate to a subject distinct from that to which the writing relates. Dutton v. Gerrish, 9 Cush. 89; Naumberg v. Young, supra; Taylor, Ev. §1038. See Lindley v. Lacey, 34 Law J., C. P., 7.

We have carefully examined all the cases cited in the quite exhaustive brief of counsel for defendant, and find but very few that are at all in conflict with the views

56

already expressed, and these few do not commend themselves to our judgment. Our conclusion therefore is that the court erred in admitting parol evidence of a warranty, and therefore the order refusing a new trial must be reversed.

Notes and Questions

1. *Rationale for parol evidence rule.* The court states that the parol evidence rule is "founded on the obvious inconvenience and injustice" that would result if extrinsic evidence were admissible to contradict or vary the terms of a written agreement. What specific "inconvenience" and "injustice" can result from the introduction of extrinsic evidence?

2. *Meaning of "integration."* As the *Thompson* court indicates, at the core of the parol evidence rule is the concept that parties typically arrive at contract terms through a process of preliminary negotiations and then produce a writing containing the final terms that have been mutually adopted. (As you are well aware, however, adhesion contracts do not fit this pattern.) The final writing is then considered the best evidence of the contract and displaces any earlier agreement or proposals, whether oral or written. See E. Allan Farnsworth, *Contracts* §7.2, at 418 (4th ed. 2004) (the useful purpose of parol evidence rule is to replace negotiations and superseded understandings with a final authoritative statement of the agreement). Both classical and modern contract law use the term *complete integration* to refer to a writing that is intended to be a final and exclusive expression of the agreement of the parties. First Restatement §228; Restatement (Second) §210. Both classical and modern contract law also recognize the possibility of a *partial integration*, a writing that is intended to be final but not complete because it deals with some but not all aspects of a transaction between the parties. The correct application of the parol evidence rule thus requires that the court first determine whether the writing in question is intended to be a final expression of the parties agreement and, if so, whether it is a complete or partial statement of the contract terms. How would you assess the writing in *Thompson* in light of these standards?

3. *Determining integration.* The *Thompson* court states that the written contract does not appear on its face to be either an "informal or incomplete" memorandum, and therefore the court concludes that the writing is a completely integrated agreement. The court's determination is based on an approach often identified with Professor Williston who argued that the question of integration must be determined from the "four corners" of the writing without resort to extrinsic evidence. 4 Williston on Contracts §633, at 1015. Moreover, Williston asserted that the inclusion in the writing of a "merger clause" would conclusively establish that the writing was integrated. 4 Williston on Contracts §633, at 1014. A merger clause states that the writing is intended to be final and complete; all prior understandings are deemed to have been "merged" into or superseded by the final writing. The following is an example of a typical merger clause:

Entire Agreement. This document constitutes the entire agreement of the parties and there are no representations, warranties, or agreements other than those contained in this document.

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Making Contracts (cnt'd)

Implied Terms – Good Faith

§205. Duty of Good Faith and Fair Dealing

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

Warranties – Express or Implied

Making Contracts on One page

Box 1

What law applies? UCC or Common Law (mixed contract only – predominant purpose test)

Objective Theory of Contracts

Manifestation of Mutual Assent in all its permutations (UCC or Common Law)

Consideration (Two Tests)

Statute of Frauds (UCC and Common Law and exceptions)

Interpretation (UCC and Common Law)

Parol Evidence Rule (UCC and Common Law)

Implied Terms (UCC and Common Law)

Box 2

Promissory Estoppel (Rest 90/1)

Pre-acceptance Reliance (Rest 87/2)

Exceptions to PER above (I put both places) - Rest 129 and 139

Box 3

Restitution in Absence of a Promise

- Implied-in-fact
- Implied-in-law

Promissory Restitution

- Moral Obligation + Promise (infants, debts discharged in bankruptcy, or after statute of limitations)
- Material Benefit + Promise

Making Contracts (cnt'd)

END