Law Student Steven Lang Brief

of

Brown Machine, Inc. v. Hercules, Inc., 770 S.W.2d 416 (1989)

CONCEPTS: Application of UCC when goods predominate over services, UCC §2-207 addressing nonmatching forms/communications with conflicting terms, qualified/varying acceptance, acceptance by performance, acceptance resulting in counter-offer (see UCC §2-207(1), Restatement (Second) of Contracts §59 (1981)).

PARTIES: PLAINTIFF-RESPONDENT: Brown Machine, Inc.
DEFENDANT-APPELLANT: Hercules, Inc.

ISSUE: If Party A submits a purchase order (constituting the offer) without an indemnity provision, and Party B's acknowledgment contains an indemnity provision, is Party B's acknowledgment a counteroffer or an acceptance with different or additional terms? Is there a contract with an indemnity provision?

HOLDING AND RULE: As long as there is no unwillingness by the parties to proceed with the transaction, the acknowledgment will constitute an acceptance with additional/different terms and, therefore, there is no indemnity provision in the contract. Pursuant to the UCC, additional/different terms (such as an indemnity provision) become part of a contract between merchants unless (1) the additional/different terms materially alter the contract; (2) the offer expressly limits acceptance to the offer's terms; and/or (3) notification of objection to the additional/different terms is provided within a reasonable time. The Missouri Court of Appeals reversed the trial court's jury verdict and judgment in favor of Plaintiff Brown Machine, Inc. in its action against Defendant Hercules, Inc. for indemnification.

FACTS: The Missouri Court of Appeals reversed the trial court's jury verdict and judgment in favor of Plaintiff Brown Machine, Inc. in its action against Defendant Hercules, Inc. for indemnification. In 1975, Defendant asked Plaintiff for a price quote for a trim press. Plaintiff then provided Defendant with a price quote proposal, which included an indemnification clause. Defendant subsequently submitted a purchase order to Plaintiff. However, Defendant's purchase order expressly limited its assent only to the terms stated in Defendant's purchase order. Moreover, Defendant's purchase order rejected any of Plaintiff's different terms. Furthermore, Defendant's purchase order did not contain an indemnity provision. Plaintiff then initiated performance on the work order, as well as returned Plaintiff's own order-acknowledgment form to Defendant. Plaintiff's own order-acknowledgment form contained an indemnity provision. After receiving the trim press, Defendant paid Plaintiff. Subsequently, an employee of Defendant sustained injuries while operating Plaintiff-supplied trim press. Said employee of Defendant sued Plaintiff. Plaintiff demanded that Defendant defend the lawsuit, however, Defendant refused. Plaintiff eventually settled the lawsuit. Plaintiff then initiated

action against Defendant for indemnification. Whether or not Plaintiff/Defendant's contract contained an indemnification provision was the dispositive issue on appeal.

ANALYSIS

LEGAL DISCUSSION: From the start, it should be pointed out that the business contract, like many business contracts, appears to contain a goods/services mix; however, the contract is governed by the UCC, since the predominant factor of the contract is a transaction for the sale of goods, with labor incidentally involved (see *Bonebrake v. Cox*, 499 F.2d 951 (8th Cir. 1974)). Therefore, the common law of contract (and classical contract law) doctrines of "mirror image" and "last shot" are not followed, as the "mirror image" and "last shot" rules are contrary to the intentions of the drafters of UCC §2-207 (Professor Karl Llewellyn, architect of the UCC, and principal drafter of Article 2; UCC widely adopted in the 1960s). The Missouri Court of Appeals' first order of business was to identify the offer (Note: The term "offer" is undefined in the UCC and, therefore, the common law definition was utilized.). While the Missouri Court of Appeals acknowledged that price quotations have the ability to be considered offers, at the same time, the Missouri Court of Appeals concluded that Plaintiff's price quotation proposal was not the offer in this instant issue and, instead, merely a negotiation invitation – for several reasons, including: (1) Plaintiff's price quotation proposal contained the words "No...offer to sell...shall be binding upon BROWN unless accepted by BROWN...on BROWN standard 'Order Acknowlegment' [sic] form."; (2) Plaintiff's price quotation contained the words "...written proposals...shall expire...thirty (30) calendar days from date issued...." However, Defendant's purchase order was well beyond the expiration of this price quotation proposal and, therefore, no timely acceptance (even if Plaintiff's price quotation proposal were ruled an offer). The Missouri Court of Appeals ruled that Defendant's purchase order constituted the offer (and not the acceptance), even though Defendant's purchase order uses the words "EXPRESSLY LIMITS ACCEPTANCE." The next question the Missouri Court of Appeals had to decide was whether Plaintiff's order-acknowledgment form containing the indemnity provision constituted a counter-offer or an acceptance with additional/different terms. Under UCC §2-207(1), an offeree's "definite and seasonable expression of acceptance" to an offer operates as a valid acceptance of the offer even though it contains additional/different terms from the terms of the offer unless the "acceptance is expressly made conditional" on the offeror's assent to the additional/different terms. (Note how UCC §2-207(1) clearly departs from the "mirror image" common law rule.) Accordingly, under UCC §2-207(1), a counter-offer results when the offeree's response to the offer is an acceptance "expressly conditional" on the offeror's assent to the offeree's additional/different terms (see Restatement (Second) of Contracts §59 (1981)). (Note: Under UCC §2-207(1), an acceptance containing terms that materially differ from the terms of the offer does not, in and of itself, result in an expressly conditional acceptance and thus a counter-offer [as would occur under the "mirror image" common law rule]; that is, an expressly conditional acceptance does not result merely by the presence of materially differing terms (see *Ionics, Inc. v. Elmwood Sensors, Inc.*, 110 F.3d 184 (1st Cir. 1997). Only very clear language [even if boilerplate] will be able to indicate if the offeree's assent is expressly

conditional [A few courts even go beyond the language, and examine additional evidence, such as facts and circumstances, trade usage, course of dealing, course of performance, etc.].) However, the majority of states hold that to convert an acceptance to a counter-offer under UCC §2-207(1), it is necessary that the offeree clearly expresses to the offeror that the offeree is unwilling to perform unless the offeree's additional/different terms are included in the contract. Accordingly, the Missouri Court of Appeals determined that Plaintiff's response to Defendant's offer, i.e., Plaintiff's order-acknowledgment form – as well as Plaintiff's pertinent conduct – did not clearly express to Defendant that Plaintiff was unwilling to proceed unless Defendant assented to Plaintiff's indemnification terms. That is, the Missouri Court of Appeals concluded that Plaintiff's acceptance should not be converted to a counter-offer pursuant to UCC §2-207(1), since Plaintiff's acceptance to Defendant's offer was not "expressly made conditional" on Defendant's assent to Plaintiff's indemnification terms. Therefore, the Missouri Court of Appeals argued that Plaintiff's order-acknowledgment form constituted an acceptance with additional or different terms from the offer, specifically, the indemnity provision. Pursuant to UCC §2-207(2) and UCC §2-207 Comment 3, the Missouri Court of Appeals concluded that Plaintiff's indemnification provision failed to be included in the contract (The Missouri Court of Appeals further noted that express assent under UCC §2-207(2) cannot be presumed by silence or mere failure to object.). Note: Even if the Missouri Court of Appeals had ruled that Plaintiff's order-acknowledgment form was an "expressly conditional" acceptance and thus a counter-offer, since the parties proceeded to performance (even without Defendant's definite acceptance of the counter-offer's terms), a contract would then be formed consisting of the terms on which the parties' communications agree, "together with any supplementary terms incorporated under any other provisions of [the UCC]," pursuant to UCC §2-207(3).

Law Student Steven Lang Brief

of

Webb v. McGowin, 27 Ala. App. 82, 168 So. 196, 232 Ala. 374 (1936)

CONCEPTS: Promissory restitution principle, material benefit rule, moral obligation as consideration.

PARTIES: PLAINTIFF-APPELLANT: Joe Webb
DEFENDANT-APPELLEE: N. Floyd McGowin and Joseph F. McGowin, as executors of the estate of J. Greeley McGowin

ISSUE: If there was no original duty or liability resting on the promisor, can a moral obligation support a subsequent promise to pay where the promisor has received a material benefit?

HOLDING AND RULE: The subsequent promise to pay is enforceable pursuant to the "material benefit" rule, a principle of promissory restitution. Plaintiff filed suit, and the demurrers to Plaintiff's complaint were sustained. Grounds of demurrer: "(1) It states no cause of action; (2) its averments show the contract was without consideration; (3) it fails to allege that [Defendant] had, at or before the services were rendered, agreed to pay [Plaintiff] for them; (4) the contract declared on is void under the statute of frauds." On appeal, the Alabama Court of Appeals reversed and remanded.

FACTS: Plaintiff was employed at the same lumber mill as Defendant. Plaintiff was in the process of dropping a seventy-five pound pine block off of the upper floor of the lumber mill onto the ground, in accordance with his job description. However, just before Plaintiff released the pine block, Plaintiff saw Defendant standing on the ground where the pine block would have fallen. In order to keep the pine block from striking Defendant, Plaintiff held onto the pine block, and then Plaintiff diverted the downward direction of the pine block by falling to the ground with the pine block. Defendant avoided injuries, however, Plaintiff sustained serious injuries causing Plaintiff to be permanently incapable of working. For Plaintiff's care, Defendant then promised to provide bi-monthly funds to Plaintiff for the remainder of Plaintiff's life. These bi-monthly funds were paid by Defendant to Plaintiff for more than eight years. Shortly after Defendant's death, Plaintiff stop receiving the funds. Plaintiff filed suit, and the demurrers to Plaintiff's complaint were sustained. Grounds of demurrer: "(1) It states no cause of action; (2) its averments show the contract was without consideration; (3) it fails to allege that [Defendant] had, at or before the services were rendered, agreed to pay [Plaintiff] for them; (4) the contract declared on is void under the statute of frauds." On appeal, the Alabama Court of Appeals reversed and remanded.

ANALYSIS

LEGAL DISCUSSION: The Alabama Court of Appeals spent considerable effort discussing how "a moral obligation is a sufficient consideration to support a subsequent promise to pay where the promisor has received a material benefit, although there was no original duty or liability resting on the promisor...." That is, the subsequent promise to pay is enforceable pursuant to the "material benefit" rule, a principle of promissory restitution. (Note: Under the "material benefit" rule, the material benefit is not conferred gratuitously. This, alone, creates a legal debate about this case: That is, on the one hand, it could be argued that Plaintiff's services were rendered gratuitously; on the other hand, it could be argued that Plaintiff simply did not have time to ponder whether his services would be gratuitious. The Alabama Court of Appeals insisted that the payments by Defendant to Plaintiff for more than eight years verified that the services rendered by Plaintiff were not gratuitous.) In this type of case, the "moral obligation" is connected to the "material benefit." (The Alabama Court of Appeals noted how this was different from cases where the moral obligation, in and of itself, constitutes the consideration [and the moral obligation is not connected to any material benefit received by the promisor].) The Alabama Court of Appeals also argued how a promisor's subsequent promise to pay out of

a moral obligation for the material benefit received is an "affirmance or ratification" of the promisee's services rendered in providing the material benefit and, moreover, reflects a "presumption" that a previous request (by the promisor to the promisee) for the material benefit had been made. The Alabama Court of Appeals argued that the material benefit in this instant issue was Plaintiff saving Defendant from serious bodily injury or death. The Alabama Court of Appeals' discussion of the material value of human life involved pecuniary examples of surgeons charging for operations, personal injury lawyers arguing earnings and life expectancies, and life insurance companies analyzing physical health. On the topic of consideration and contractually enforcing Defendant's promise to pay, the Alabama Court of Appeals stated that the contractual consideration could be viewed in either of two ways: (1) Defendant's benefit resulting from Plaintiff saving Defendant from serious bodily injury or death or (2) Plaintiff's detriment of serious injury for the purpose of saving Defendant from serious bodily injury or death. In terms of promissory restitution cases in general, it should be noted that with promissory restitution, the obligation involves the assent of the person incurring liability and, therefore, promissory restitution has characteristics of classical contract law. At the same time, with promissory restitution, there is no bargained-for exchange and, yet, there is still liability, which, thus, has characteristics of pure restitution (unjust enrichment liability in the absence of promises/agreements/contracts/mutual assent) (Note: While many restitution claims arise out of contract disputes, and while the origins of restitution have contractual roots, in the twentieth century, restitution became its own distinct body of law, separate from contract law [Restatement of Restitution published by ALI in 1937].). Even though there is no bargained-for exchange involved in promissory restitution, there is still scholarly defense for these types of promises – the scholarly defense is based on principles of morality (see writings of Lon Fuller and Charles Fried), as well as on economics (see writings of Richard Posner [For example, in *Gratuitous Promises in Economics and Law*, 6 J. Legal Stud. 411, 418-419 (1977), Posner cites the example of how a promisor paying a debt barred by technicality thus "enhances the promisor's reputation for credit-worthiness and may induce people...to extend credit to him in the future."]).

Law Student Steven Lang Brief

of

Wood v. Lucy, Lady Duff-Gordon, 222 N.Y. 88, 118 N.E. 214 (1917)

CONCEPTS: Implied-in-law terms, implied-in-fact terms, UCC §2-306(2) provision imposing a "reasonable" or "best efforts" obligation with exclusive contract, implied obligation to use reasonable efforts which, thus, keep promises from being regarded as illusory (and, accordingly, provide consideration).

PARTIES: PLAINTIFF-APPELLANT: Otis F. Wood
DEFENDANT-RESPONDENT: Lucy, Lady Duff-Gordon

ISSUE: When does an implied obligation to use reasonable efforts exist within a contract? Is a contract illusory and, thus, lack consideration when there is an implied obligation to use reasonable efforts?

HOLDING AND RULE: An implied obligation to use reasonable efforts may be implied from the entire circumstances surrounding the contract. An implied obligation to use reasonable efforts may serve as valuable consideration. The Special Term court denied a motion by Defendant for judgment in Defendant's favor. The Appellate Division then reversed the Special Term court. The New York Court of Appeals then reversed the Appellate Division and, thus, affirmed the Special Term court.

FACTS: Defendant Lucy, Lady Duff-Gordon, a preeminent fashion designer, entered into an exclusive marketing contract with Plaintiff Wood. The contract provided Defendant with one-half of all the profits generated from Plaintiff's marketing contracts. Defendant then entered into a marketing contract without using Plaintiff's marketing agency; Defendant did not provide Plaintiff with any of the profits. Plaintiff filed a lawsuit against Defendant for breach of the exclusive marketing contract. The Special Term court denied a motion by Defendant for judgment in Defendant's favor. The Appellate Division then reversed the Special Term court. The New York Court of Appeals then reversed the Appellate Division and, thus, affirmed the Special Term court.

ANALYSIS

LEGAL DISCUSSION: Defendant insisted that the marketing contract was never a contract, as Defendant attempted to argue that Plaintiff's contractual promise was illusory – performance is entirely optional with the promisor – and, therefore, the promise (even if bargained-for) cannot serve as consideration for a promise in return. Defendant pointed out that the contract obligated Defendant to give Plaintiff exclusive marketing rights to Defendant's fashion products. However, the gist of Defendant's illusory-contract argument was that the very words contained in the exclusive marketing contract never once obligated Plaintiff to anything in return for Defendant's promise/obligation – that is, according to Defendant, Plaintiff was free to do as much work, or free to do as little work, or free to do no work at all for Defendant ("plaintiff does not bind himself to anything"). In agreeing with Defendant's illusory-promise claim, the Appellate Division argued that Plaintiff was "under no duty to try to market designs." The New York Court of Appeals disagreed with the Appellate Division's and Defendant's Classical contract theory argument, as the New York Court of Appeals pointed out that the "law has outgrown its primitive stage of formalism when the precise word was the sovereign talisman, and every slip was fatal. It takes a broader view to-day [sic]. A promise may be lacking, and yet the whole writing may be 'instinct with an obligation,' imperfectly expressed....If that is so, there is a contract." Contrary to the arguments of Defendant and the

Appellate Division, the New York Court of Appeals argued that Plaintiff had, in fact, assumed an implied obligation to use "reasonable efforts" to perform marketing work for Defendant. The New York Court of Appeals found Plaintiff's obligation to use reasonable efforts to perform to be an implied-in-law term of the exclusive marketing contract. The New York Court of Appeals argued that Plaintiff's implied obligation to perform reasonable efforts was guided by an economic analysis of the law that there was a "business efficacy" that both parties must have intended in their agreement. The New York Court of Appeals further argued that Plaintiff's implied obligation to perform reasonable efforts was also guided by the legal principle that one party should not be "placed at the mercy of the other." The New York Court of Appeals indicated that Plaintiff's implied obligation to use reasonable efforts was evidenced by the following: (1) Defendant approved of Plaintiff's agency to market Defendant's fashions; (2) Plaintiff accepted an exclusive marketing agency right; (3) Defendant agreed that its only compensation from the marketing contract would be from one-half of all the profits generated by Plaintiff's performance; (4) Plaintiff agreed to make a monthly accounting of the profits; (5) Plaintiff agreed to perform all necessary work pertaining to patents, copyrights, and trademarks (Note: Given these five facts, an argument could be made that Plaintiff's reasonable-efforts obligation was both an implied-in-fact term as well as an implied-in-law term.). From the New York Court of Appeals' point of view, the most important of these items of evidence was the fact that Defendant was well aware that it had agreed that its only compensation from the marketing contract would be from one-half of all the profits generated by Plaintiff's performance. Therefore, the New York Court of Appeals concluded that there was an implied promise – which both parties intended – that Plaintiff would make reasonable efforts to perform. Of scholarly interest, according to Professor Melvin Eisenberg, writing in *The Principles of Consideration*, 67 Cornell L. Rev. 640, 649-651 (1982), many agreements involving illusory promises should be enforced, since these types of agreements frequently involve a rational bargaining process and, moreover, the party making the non-illusory promise is bargaining for the chance to show that its performance is attractive (such as a company promising a money-back guarantee to potential consumers, so that the company has a better chance of showing consumers that the company's product [that is, the company's performance] is attractive). According to Eisenberg, as long as a party knows that it is bargaining for the illusory promise of the other party, the contract should be enforced (because the first party knew what it was bargaining for). By following Eisenberg's argument, Defendant entered into a rational bargaining process with Plaintiff (even though Defendant was well aware that Plaintiff's promise was illusory – that is, Defendant knew what it was bargaining for), so that Defendant would have a better chance of showing consumers that its performance (as a fashion designer) was attractive for these consumers. In addition to Eisenberg's argument, present-day court decisions continue to agree with *Wood v. Lucy, Lady Duff-Gordon*, *supra*, that a promise can be kept from being regarded as illusory as long as there is an implied obligation to use reasonable efforts – that is, the implied obligation to use reasonable efforts has a non-illusory "value" and, thus, provides contractual consideration (see Emerson Radio Corp. v. Orion Sales, Inc., 253 F.3d 159 (3rd Cir. 2001); Magruder Quarry & Co., L.L.C. v. Briscoe, 83 S.W.3d 647

(Mo. Ct. App. 2002). (The New York Court of Appeals therefore disagreed with the Appellate Division's argument that Plaintiff's promise was "valueless," since [according to the Appellate Division] Plaintiff "was under no duty to try to market designs.") Accordingly, in the *Wood* case, the contract would have been unenforceable for lack of consideration if Plaintiff had not performed with "reasonable" or "best efforts." (On the consideration subject of "value," it should also be noted that the court in *Wood* pointed out that Defendant's endorsement to various fashions created a "new value in the public mind.") In terms of the UCC, it's also important to note that this *Wood* case is one of the legal bases for the UCC §2-306(2) provision that imposes a "reasonable" or "best efforts" obligation when there is an exclusive contract (For interesting examples of "exclusive" contracts under UCC §2-306(2), see *MDC Corp. v. John H. Harland Co.*, 228 F.Supp. 387, 393 n.3 (S.D.N.Y. 2002); *Tigg Corp. v. Dow Corning Corp.*, 962 F.2d 1119, 1125, (3d Cir. 1992).).

Law Student Steven Lang Brief

of

Hadley v. Baxendale, 156 Eng. Rep. 145 (1854)

CONCEPTS: Consequential damages vis-à-vis knowledge and foreseeability at contract formation.

PARTIES: Plaintiff-Respondent: Hadley
Defendant-Appellant: Baxendale

FACTS: Plaintiff's mill had to be shut down due to a broken crank shaft. Plaintiff therefore had to send the broken shaft (to be used as a pattern) to the manufacturers in Greenwich so that a new shaft could be made. Well-known transportation company Defendant told Plaintiff that next-day delivery to Greenwich could be done. Plaintiff definitely wanted next-day delivery ("The Plaintiffs' servant told the [Defendant's] clerk that the mill was stopped, and that the shaft must be sent immediately...."). Due to Defendant's neglect, the delivery of the shaft was delayed. The delay resulted in Plaintiff's mill not being operational and, therefore, Plaintiff lost profits it otherwise would have had if Defendant had not neglectfully delayed the transport of the shaft.

ISSUE: Should a breaching party be liable for consequential damages when the breaching party was not aware that the damages would be incurred from a breach of contract?

DECISIONS: The lower court jury awarded Plaintiff 25 pounds beyond the amount already paid to the court. Defendant appealed. The Court of Exchequer vacated and remanded for new trial.

REASONING: The Court of Exchequer first discussed the rule that when there is a breach of contract, the non-breaching party is entitled to recovery of an amount that should place the non-breaching party in the same position as if the breaching party had performed. In furthering the concept of this rule as it applies to *Hadley v. Baxendale*, *supra*, the Court of Exchequer then stated that if there is a breach of contract, the non-breaching party should recover damages reasonably considered to arise naturally from the breach (general or direct damages), or the non-breaching party should recover breach-of-contract damages that arise from special circumstances reasonably known and reasonably contemplated by both parties at the time of contract formation (consequential damages). On the other hand, the Court of Exchequer stated that if the special circumstances are unknown to the breaching party, and if the great multitude of similarly situated cases are not affected by the pertinent special circumstances, then the breaching party is only liable for those damages that arise generally, and the breaching party would not be liable for those proposed special damages.

SEPARATE OPINIONS: None.

ANALYSIS: The Court of Exchequer insisted that – at the time of contract formation – all that was known to Defendant was that Plaintiff operated a mill, and that Plaintiff had a broken shaft that needed to be transported. The Court of Exchequer therefore argued that Defendant had no way of knowing that an unreasonable delay by Defendant would cost Plaintiff lost profits. The Court of Exchequer stated that in the great multitude of cases of millers sending off broken shafts, the consequences that befell Plaintiff would not occur. The Court of Exchequer argued that (1) Plaintiff could have had another shaft in its possession with which to operate the mill, and that Plaintiff was sending the broken shaft back to the manufacturer (perhaps for a refund, or perhaps so that Plaintiff could have a back-up shaft made); or (2) that Plaintiff's mill could be not operational for other reasons in addition to the broken shaft (That is, while Plaintiff told Defendant that Plaintiff's mill was not operational, the Court of Exchequer concluded that Plaintiff did not effectively and directly communicate to Defendant that the shaft was the sole reason that Plaintiff's mill was not operational.). For either of those two reasons, the Court of Exchequer stated that any unreasonable delay by Defendant would not result in lost profits to Plaintiff. In other words, the Court of Exchequer was not convinced that Defendant had reasonably known (that is, been served notice by Plaintiff at the time of contract formation) that any unreasonable delay by Defendant would cost Plaintiff lost profits – the loss of profits were not reasonably contemplated by both parties at contract formation. While it is obvious that Plaintiff had an extreme dependence on the shaft, the Court of Exchequer argued that Plaintiff's special circumstances were never thoroughly communicated to Defendant – Plaintiff did not serve notice on Defendant concerning Plaintiff's special circumstances. Accordingly, these special, consequential damages were never fairly and reasonably contemplated by the parties during contract formation. The modern-day principle that resulted from *Hadley v. Baxendale*, *supra*, is foreseeability of loss. Modern-day foreseeability is determined as follows: (1) the consequential damages must be contemplated by the parties during contract formation; (2) it is only necessary that the type of loss be foreseeable, not the manner in which the loss

occurs; (3) the focus of foreseeability is on the breaching party; (4) the standard for foreseeability is at least in part objective; (5) the loss must be foreseeable as a "probable" result of the breach (liability does not extend to remote losses). Finally, on a historical note, it has been generally accepted that this *Hadley* case was motivated by the interest in protecting new, or small, businesses in the early stages of the industrial revolution (see Richard Danzig, *Hadley v. Baxendale, A Study in the Industrialization of the Law*, 4 J. Legal Stud. 249, 262-263 (1975)).

Law Student Steven Lang Brief

of

Lenawee County Board of Health v. Messerly, 417 Mich. 17, 331 N.W.2d 203 (1982)

CONCEPTS: Mutual mistake as justification for nonperformance/rescission, failure of consideration.

PARTIES: PLAINTIFF: Lenawee County Board of Health.
DEFENDANTS-APPELLEES: Carl and Nancy Pickles.
DEFENDANTS-APPELLANTS: William and Martha Messerly.
DEFENDANTS-APPELLEES: James Barnes and wife.

FACTS: In 1971, William and Martha Messerly purchased from Mr. Bloom approximately one acre plus 600 square feet of land. A three-unit apartment building was situated on the 600 square foot portion. Prior to the transfer, Mr. Bloom had installed a septic tank on the property without a permit and in violation of health code. In 1973, Messerly sold the property to Barnes. Barnes defaulted. Messerly reacquired the property. In 1977, after inspecting the property, Pickles purchased the property for $25,500. Five or six days later, Pickles discovered raw sewage seeping out of the ground, although it was determined that the septic system was defective prior to Pickles signing the contract. Plaintiff condemned the property; Plaintiff then initiated the lawsuit *Lenawee County Board of Health v. Messerly*, *supra*. A cross-complaint, counterclaim, and third-party complaint were subsequently filed. The issue the Michigan Supreme Court decided was whether or not Pickles was entitled to a rescission of the land contract.

ISSUE: Can a land contract can be rescinded on the basis of mutual mistake?

DECISIONS: Lenawee Circuit Court granted Plaintiff a permanent injunction against Messerly and Pickles (proscribing human habitation of the property until brought into code conformance). After this injunction was granted, Plaintiff was permitted to withdraw from the lawsuit. Messerly filed a cross-complaint against Pickles seeking foreclosure, sale of the property, and a deficiency judgment. Pickles then counterclaimed for rescission against

Messerly, and filed a third-party complaint against Barnes. In its claims, Pickles (1) alleged failure of consideration and (2) charged Barnes with willful concealment and misrepresentation (also holding Messerly liable for Barnes). After a bench trial, the trial court ruled no fraud or misrepresentation, as the court concluded that the sanitation problem was not known and not caused by either of the parties. Foreclosure and judgment was ordered against Pickles. Pickles appealed. Court of Appeals affirmed with respect to Barnes, however the Court of Appeals reversed with respect to Messerly. The Court of Appeals insisted that the mutual mistake between Messerly and Pickles went to a basic (not collateral) element of the contract – that is, the parties' intent was to transfer something of $25,500 in value (with income-earning potential), as opposed to something basically valueless. The Michigan Supreme Court ruled that Pickles was not entitled to rescission (reversing the Court of Appeals).

REASONING: The buyers had the opportunity to thoroughly inspect the property, and the property was purchased "as is." The property's "negative...value cannot be blamed upon an innocent seller."

SEPARATE OPINIONS: None.

ANALYSIS: The Michigan Supreme Court was well aware that the equitable remedy of rescission was available – indeed, appropriate (at the reasonable discretion of the court) – in cases of mutual mistake where the "basic assumption on which the contract was made has a material effect on the agreed exchange of performances" (Restatement (Second) of Contracts §152). At the same time, the Michigan Supreme Court clearly understood that voiding a contract for mutual mistake was not available if the adversely affected party bears the risk of the mistake (see Restatement (Second) of Contracts §154, "A party bears the risk of a mistake when (a) the risk is allocated to him by agreement of the parties, or (b) he is aware, at the time the contract is made, that he has only limited knowledge with respect to the facts to which the mistake relates but treats his limited knowledge as sufficient, or (c) the risk is allocated to him by the court on the ground that it is reasonable in the circumstances to do so."). In the instant issue, Pickles bore the risk of the mistake by contractual agreement – (1) Pickles contractually agreed that he inspected the property and (2) Pickles contractually agreed that he purchased the property "as is." Implied warranties protect against latent, unknown defects, and an "as is" clause serves to waive those implied warranties; accordingly, the "as is" clause imposes upon the purchaser the assumption of risk of latent, unknown defects, even in the absence of implied warranties. That is, in general, through contractual agreement, both parties to a contract can determine risk-allocation and, accordingly, both parties can contractually agree what will happen in the event of mutual mistake. In the instant issue, Pickles contractually agreed to bear the risk in the event of a mutual mistake and, therefore, the Michigan Supreme Court was justified in denying rescission even in the presence of mutual mistake. Even though there was no express contractual provision of the risk of the property becoming uninhabitable, the Michigan Supreme Court concluded that the agreed-upon "as is" clause allocated the risk to Pickles. (Note: Even in the presence of an "as is" clause, an adversely affected party may still

demand rescission by alleging fraud or misrepresentation.) (Note: The Michigan Supreme Court was thoroughly convinced that its risk-of-loss analysis reasoning hereinabove was clearly superior for mutual-mistake cases than that employed by the two pertinent leading cases of *A & M Land Development Co. v. Miller*, 354 Mich. 681, 94 N.W.2d 197 (1959) [discussing collateral mistakes relating only to value and, thus, not justifying rescission] and *Sherwood v. Walker*, 66 Mich. 568, 33 N.W. 919 (1887), "the barren cow case," [discussing the very essence of the consideration and, thus, justifying rescission].)

Law Student Steven Lang Brief

of

Ray v. William G. Eurice & Bros., Inc., 201 Md. 115, 93 A.2d 272 (1952)

This case discusses several important legal concepts in the area of contract law: Reasonably informed observer, subjective vs. objective theory of contractual intent, unilateral mistake, meeting of the minds, manifestation of acceptance.

PARTIES: PLAINTIFF-APPELLANT: Calvin T. Ray, Katherine S. J. Ray
DEFENDANT-APPELLEE: William G. Eurice & Bros., Inc.

ISSUE: Is a contract enforceable if a party who signs the contract did not intend to agree to the contractual terms?

HOLDING AND RULE: A party (with the capacity to understand a contract) is contractually bound by his signature (absent fraud, duress, or mutual mistake). Intent to agree (assent) is determined by objective (not subjective) criteria, using the reasonable-person standard. Unilateral mistake, in and of itself, does not create a breach. Judgment reversed and judgment entered for Appellants.

FACTS: Plaintiff appealed to the Maryland Court of Appeals from the Circuit Court for Baltimore County. Plaintiff Ray owned a vacant lot in Baltimore country; Plaintiff contracted with house-builder Defendant William G. Eurice & Bros., Inc. to build a house on the vacant lot. On January 9, 1951, Plaintiff and Defendant discussed Plaintiff's seven-page list of architectural specifications. Defendant objected to some of the items in this seven-page list. On February 14, Defendant then delivered to Plaintiff a three-page list of architectural specifications. However, also on February 14, Plaintiff prepared a five-page list of architectural specifications (also dated February 14, 1951). On February 22, Plaintiff and Defendant signed a contract with Plaintiff's five-page list of architectural specifications. Defendant signed each page of the five-page list of specifications, however, Defendant insisted that he did not look at the specifications prior to signing them. On May 8, Defendant then informed Plaintiff that Defendant had never seen the five-page list of architectural specifications and, therefore, Defendant argued that he was not obligated to build Plaintiff's new house. Defendant argued that he should only be required to build that house according to Defendant's three-page list of specifications because, according to Defendant, he believed that he had signed a contract involving Defendant's three-page list of specifications. In the Circuit Court for Baltimore County, Judge Gontrum ruled for Defendant: Judge Gontrum concluded that there had been an "honest mistake" by Defendant in signing the contract, that there had never been a meeting of the minds involving the contract with the five-page list of architectural specifications and, therefore, Defendant was not required to build Plaintiff's house according to the five-page list of architectural specifications.

On appeal, however, the Maryland Court of Appeals reversed Judge Gontrum's lower court decision.

ANALYSIS

LEGAL DISCUSSION: While the Maryland Court of Appeals agrees that a mistake had been made by Defendant, at the same time, the Maryland Court of Appeals concludes that the mistake was unilateral. Accordingly, the Maryland Court of Appeals wrote, "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...." Further, on the subject of unilateral mistake, the Maryland Court of Appeals then cites Williston, Contracts (Rev. Ed.), Sec. 1577: "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." Restatement, Contracts, Section 70, "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." According to the strict legal objectivist Judge Learned Hand, writing in *Hotchkiss v. National City Bank, D.C.*, 200 F. 287, 293: "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 will still be held, unless there were some mutual mistake, or something else of the sort." The Maryland Court of Appeals then goes on to discuss subjective vs. objective theory of contractual intent, as well as the reasonably informed observer test: Williston, Contracts (Rev. Ed.), Sec. 94, page 294: "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 parties would have thought it meant." Also significantly cited are the 1881 lectures by Oliver Wendell Holmes; in these lectures, Holmes stated, "The law has nothing to do with the actual state of the parties' minds. In contract, as elsewhere, it must go by externals, and judge parties by their conduct." Finally, in *The Theory of Legal Interpretation*, 12 Harv. L. Rev. 417, 419 (1899), Holmes wrote, "If it turns out that one meant one thing and the other another, speaking generally, the only choice possible...is either to hold both parties to the judge's interpretation of the words in the sense which I have explained, or to allow the contract to be avoided because there has been no meeting of the minds. The latter course not only would greatly enhance the difficulty of enforcing contracts against losing parties, but would run against a plain principle of justice."

Law Student Steven Lang Brief

of

Normile v. Miller, 313 N.C. 98, 326 S.E.2d 11 (1985)

CONCEPTS: Real estate option contract, consideration and option contract, counter-offer-equals-rejection rule, mutual assent, meeting of the minds, manifestation of intent to agree.

PARTIES: PLAINTIFF-APPELLANT: Normile and Kurniawan
DEFENDANT-APPELLEE: Hazel Miller

ISSUE: Can a prospective purchaser accept a counteroffer after receiving notice of the counteroffer's revocation? When does an option contract exist?

HOLDING AND RULE: A counteroffer constitutes a rejection of the prospective purchaser's original offer. A prospective purchaser may not accept a counteroffer once it has been revoked. A counteroffer may be revoked with notice (even through indirect communication) any time before acceptance. An option contact is supported by consideration and grants an exclusive right to purchase for a fixed price within a specified period of time. Plaintiff Normile, Plaintiff Segal, and Defendant initiated court action seeking specific performance. The trial court granted Plaintiff Segal's motion for consolidation. Plaintiff Normile and Plaintiff Segal both motioned for summary judgment. The trial court granted Plaintiff Segal's motion for summary judgment, and Defendant was ordered to specifically perform the contract to Plaintiff Segal. Since the trial court denied Plaintiff Normile's motion for summary judgment, Plaintiff Normile appealed to the Court of Appeals; the Court of Appeals unanimously affirmed the trial court. Plaintiff then appealed to the Supreme Court of North Carolina. The Supreme Court of North Carolina modified and affirmed the Court of Appeals.

FACTS: Defendant Miller sought to sell her real estate property and listed the property with realtor Hawkins. Real estate broker Byer showed the property to Plaintiff Normile, prospective purchaser. Plaintiff then submitted a written offer to purchase Defendant's property; Plaintiff's offer contained the words "this offer must be accepted on or before 5:00 P.M. Aug. 5th." This offer was seen by Defendant, however, Defendant returned the written offer to Plaintiff with Defendant's changes in the terms; Plaintiff received Defendant's counteroffer. However, Plaintiff – in possession of Defendant's counteroffer – was now under the impression that he (Plaintiff) had the first option on the property and, therefore, Plaintiff now believed that no other prospective purchasers could now purchase the property as long as Plaintiff had Defendant's counteroffer. As a result, Plaintiff decided to take some time to think over Defendant's counteroffer, and so Plaintiff neither accepted nor rejected the counteroffer. On August 5, at 12:30 a.m., another Plaintiff, Segal, then offered to purchase Defendant's property

for terms very similar to Defendant's counteroffer to Plaintiff Normile. On that same day, Defendant accepted Plaintiff Segal's offer without requiring any changes to the terms of Plaintiff Segal's offer. On that same day, at 2:00 p.m., Byer communicated to Plaintiff Normile Defendant's acceptance of Plaintiff Segal's offer (and, consequently, the revocation of Defendant's counter-offer to Plaintiff Normile). Then, on that same day (August 5), prior to 5:00 p.m., Plaintiff Normile then accepted Defendant's counter-offer. Plaintiff Normile, Plaintiff Segal, and Defendant initiated court action seeking specific performance. The trial court granted Plaintiff Segal's motion for consolidation. Plaintiff Normile and Plaintiff Segal both motioned for summary judgment. The trial court granted Plaintiff Segal's motion for summary judgment, and Defendant was ordered to specifically perform the contract to Plaintiff Segal. Since the trial court denied Plaintiff Normile's motion for summary judgment, Plaintiff Normile appealed to the Court of Appeals; the Court of Appeals unanimously affirmed the trial court. Plaintiff then appealed to the Supreme Court of North Carolina. The Supreme Court of North Carolina modified and affirmed the Court of Appeals.

ANALYSIS

LEGAL DISCUSSION: The Supreme Court of North Carolina cited J. Webster, North Carolina Real Estate for Brokers and Salesman, §8.10, indicating that the offer to purchase remains only an offer until the seller accepts it on the terms contained in the original offer by the prospective purchaser. However, if the seller purports to accept the offer with modifications to the terms, then this would be viewed as a counter-offer and a rejection of the buyer's offer. The Supreme Court of North Carolina then cited *Goeckel v. Stokely*, 236 N.C. 604, 607, 73 S.E.2d 618, 620 (1952): "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 the terms.'" The Supreme Court of North Carolina further cited S. Williston, *A Treatise on the Law of Contracts*, §51, indicating that the Defendant-Appellee's counter-offer is tantamount to a rejection of the original offer; S. Williston, *supra*, §36: "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 counter-offer, but also by implication that he will not assent to the terms of the original offer." See also S. Williston, *supra*, §77, any alteration in the method of payment creates a conditional acceptance; Restatement (Second) of Contracts §39 (1981): "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." A "qualified acceptance" constitutes a counter-offer...and as such will have the same effect as a rejection, insofar as the original power of acceptance is concerned. *Id.* See also Melvin A. Eisenberg, *The Revocation of Offers*, 2004 Wis. L. Rev. 271 (discussing classical contract law); Charles L. Knapp, *An Offer You Can't Revoke*, 2004 Wis. L. Rev. 309 (criticizing Eisenberg *vis-à-vis* modern contract law). The Supreme Court of North Carolina then pointed out that Defendant's conditional acceptance modifying Plaintiff Normile's original offer did not manifest an intent to agree to the terms of Plaintiff Normile's original offer. Moreover, prior to the acceptance by Plaintiff Segal, Plaintiff Normile did not manifest (either expressly or by

conduct) an intent to agree to the terms in Defendant's counter-offer. See Restatement, *supra*, §§57-58, An acceptance must be unequivocal an unqualified in order for a contract to be formed. The Supreme Court of North Carolina concluded that there was never any mutual assent ("meeting of the minds") between Defendant and Plaintiff Normile. Even though Plaintiff Normile accepted Defendant's counter-offer, the Supreme Court of North Carolina concluded that there was an effective revocation of this counter-offer – and that Plaintiff Normile's power of acceptance had been terminated – given that Plaintiff Normile was well aware that Defendant had accepted the offer of Plaintiff Segal. While Plaintiff Normile insisted that he was in possession of a real estate option contract, the Supreme Court of North Carolina concluded that Defendant's counter-offer did not constitute a real estate option contract, since there was never a promise by Defendant to hold the counter-offer open for a specified time: "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." Moreover, even if Defendant's counter-offer legally constituted a real estate option contract indicating the offer would be held open for a specified period of time, it is also very important to point out that Plaintiff Normile did not provide any consideration to hold the offer open and, therefore, the real estate option contract would have been unenforceable.

Law Student Steven Lang Brief

of

Cook v. Coldwell Banker/Frank Laiben Realty Co., 967 S.W.2d 654 (1998)

CONCEPTS: Classical theory of unilateral contracts, Professor Karl Llewellyn (architect of the UCC and principle drafter of Article 2 [Sales article]) rejecting classical theory of unilateral contracts, modern theory and acceptance of unilateral contracts, substantial performance binding unilateral contracts.

PARTIES: PLAINTIFF-APPELLEE: Mary Ellen Cook
DEFENDANT-APPELLANT: Coldwell Banker/Frank Laiben Realty Co.

ISSUE: Can a party to a unilateral contract revoke the offer after the opposing party has completed substantial performance?

HOLDING AND RULE: In a unilateral contract, substantial performance constitutes acceptance (substantial performance also furnishes consideration). Once a party to a unilateral contract has completed substantial performance, the opposing party may not revoke the offer. The

Missouri Court of Appeals affirmed the decision of the trial court where a jury verdict awarded Plaintiff Cook (real estate agent) monetary damages for breach of contract.

FACTS: The Missouri Court of Appeals affirmed the decision of the trial court where a jury verdict awarded Plaintiff Cook (real estate agent) monetary damages for breach of contract. Defendant Coldwell Banker/Frank Laiben Realty Co. asserts, in appeal, trial court errors relating to instructions, evidence, and closing argument, and, additionally, that Plaintiff failed to make a submissible case. Defendant, at a sales meeting in March, 1991, offered a bonus program to the Defendant's real estate agents who earned a specific amount of commissions, and these bonuses (that exceeded the first $500.00 in bonuses) would be paid at the end of 1991. However, at another sales meeting in September 1991, Defendant then informed the Defendant's real estate agents that the bonuses (that exceeded the first $500.00 in bonuses) would now be paid in March, 1992; moreover, Defendant insisted that the real estate agents must still be working for Defendant in March, 1992 in order to collect theses bonuses. Plaintiff testified that she deliberately continued working for Defendant until the end of 1991 in reliance on Defendant's promise of the bonuses. However, in January, 1992, Plaintiff accepted a real estate agent job at another company. As a result, Defendant refused to pay the bonus to Plaintiff. Plaintiff sued for breach of contract seeking specific monetary damages (to also include prejudgment interest); the trial court entered a judgment for Plaintiff. In its appeal, Defendant argued that the trial court erred in overruling its motions for directed verdict: Defendant asserted that Plaintiff failed to make a submissible case of breach of the bonus agreement since, argued Defendant, Plaintiff did not adduce sufficient evidence to establish a reasonable inference that (a) Plaintiff tendered consideration to support Defendant's offer of a bonus or (b) Plaintiff accepted Defendant's offer to give a bonus.

ANALYSIS

LEGAL DISCUSSION: On the matter of directed verdict, the Missouri Court of Appeals, citing *Seidel v. Gordon A. Gundaker Real Estate Co.*, 904 S.W.2d 357, 361 (Mo. App. 1995), stated, "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." Moreover, as to Defendant's contention that Plaintiff failed to make a submissible case on evidential grounds, the Missouri Court of Appeals first pointed out that evidence is to be viewed in a light most favorable to Plaintiff. In addition to this, the Missouri Court of Appeals then proceeded to discuss the evidence as it related to Plaintiff's unilateral contract. However, on the subject of Plaintiff's unilateral contract, perhaps a brief historical discussion of unilateral contracts may be in order: A bilateral contract is formed when the offeror and offeree exchange promises of future performance. A unilateral contract, on the other hand, is formed when the offeror's promise of future performance is in exchange for the offeree's rendering of performance (not just a promise of future performance). The offeree's rendering of performance constitutes the acceptance of the offer. Moreover, the offeree's rendering of performance also constitutes the necessary consideration for binding contract (That is, until performance is rendered, a proposed

unilateral contract lacks consideration for want of mutuality.). According to the classical theory of unilateral contracts, the offeree was denied any remedy on the unilateral contract if the offeror revoked its offer prior to the offeree rendering performance (even if the offeree had commenced performance but not yet completed full performance). See I. Maurice Wormser, *The True Conception of Unilateral Contracts*, 26 Yale L.J. 136, 136-138 (1916). The obvious debate resulting from unilateral contract classicists, such as Wormser, was the inevitable unfairness issue to offerees who did not complete full performance, and yet had taken substantial steps in reliance of the offer. The Restatements have attempted, in several ways, to protect offerees faced with this type of legal predicament. For example, Restatement (Second) of Contracts §45 provides that, under a unilateral contract, when the offeree commences the requested performance, the offer then becomes irrevocable as long as the offeree completes performance. On the historical subject of unilateral contracts, it's also significant to point out that Professor Karl Llewellyn criticized the unilateral contract classicists for believing that classical-view unilateral contracts played a significant role in the law of contracts – that is, Llewellyn viewed "true" (classical-view) unilateral contracts as aberrations and, thus, having a rather small role in the domain of commercial contracts. See *On Our Case-Law of Contract: Offer and Acceptance* (Pts. 1 & 2), 48 Yale L.J. 1, 779 (1938-1939). In fact, Llewellyn's criticism of classical-view unilateral contracts was so significant that the drafters of the Restatement (Second) of Contracts suggested that the terms "unilateral contract" and "bilateral contract" should be avoided. However, in the 1983 article *Modern Unilateral Contracts*, 63 B.U. L. Rev. 551, 552-556, Professor Mark Pettit, Jr. discussed how modern-day judges continue to employ unilateral contract anaylsis, despite the criticism of unilateral contracts by Llewellyn and other scholars. Pettit discusses how modern unilateral contract analysis is used to enforce liability where no promissory acceptance was invited or required, and where the offeree is not necessarily committed to full performance. In any event, back to the subject of Plaintiff Cook's unilateral contract: Defendant argued that it had revoked the offer of a bonus to Plaintiff prior to Plaintiff tendering consideration to support Defendant's offer, and prior to Plaintiff accepting Defendant's offer. The Missouri Court of Appeals then discussed the significance of "substantial performance" by citing *Coffman Industries, Inc. v. Gorman-Taber Co.*, 521 S.W.2d 763, 772 (Mo. App. 1975) (citing 1 *Williston on Contracts*, Third Edition Section 60A (1957); 1 *Corbin on Contracts* §49 (1952)): "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." The Missouri Court of Appeals then cited *Coffman*'s rationale: "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." The Missouri Court of Appeals concluded that Plaintiff's earning a specific amount of commissions constituted sufficient evidence of substantial performance.

The Missouri Court of Appeals further maintained that Plaintiff remaining in Defendant's employ until the end of 1991 (even though Defendant modified its offer in September 1991) was sufficient evidence for a submissible case for breach of a unilateral contract.

Law Student Steven Lang Brief

of

Pennsy Supply, Inc. v. American Ash Recycling Corp. of Pennsylvania, 895 A.2d 595 (2006)

CONCEPTS: Benefit/detriment test for consideration, bargain theory of consideration, consideration vs. condition to a gift.

PARTIES: PLAINTIFF-APPELLANT: Pennsy Supply, Inc.
DEFENDANT-APPELLEE: American Ash Recycling Corp. of Pennsylvania

ISSUE: Can materials provided free-of-charge constitute consideration (that is, as opposed to the free materials serving as a gratuitous promise and, thus, no contract)?

HOLDING AND RULE: Free materials may constitute consideration if Party A's promise to provide the free materials induced Party B's detriment of collecting (and taking title of) the free materials and, moreover, if Party B's detriment of collecting the free materials induced Party A to make the promise of providing the free materials. The Pennsylvania Superior Court reversed the decision (and remanded for further proceedings) the trial court's granting of preliminary objections in the nature of a demurrer in favor of Defendant American Ash Recycling Corp. of Pennsylvania.

FACTS: The Pennsylvania Superior Court reversed the decision (and remanded for further proceedings) the trial court's granting of preliminary objections in the nature of a demurrer in favor of Defendant American Ash Recycling Corp. of Pennsylvania. Plaintiff Pennsy Supply, Inc. (a subcontractor of general contractor Lobar, Inc.) was contracted to pave the driveways and parking lot of Northern York High School. For this paving project, the contract Project Specifications allowed the use of free AggRite from Defendant (It appears that Defendant was giving away free AggRite, since Defendant had an excess amount of AggRite and did not need the AggRite and, at the same time, Defendant did not want to pay the costs of disposing of the AggRite.). Plaintiff then collected 11,000 tons of Aggrite from Defendant; Plaintiff proceeded to use the AggRite to complete the paving work. Unfortunately, the AggRite turned out to be defective, as evidenced by extensive cracking in the pavement. Since Defendant refused to remove and dispose of the AggRite, Plaintiff was then required to remedy the defective work, which included removing and disposing of the AggRite. Plaintiff then filed a five-count complaint against Defendant: Breach of contract (Count I); breach of implied warranty of

merchantability (Count II); breach of express warranty of merchantability (Count III); breach of warranty of fitness for a particular purpose (Count IV); and promissory estoppel (Count V). The trial court sustained Defendant's demurrers and dismissed Plaintiff's complaint, as the trial court stated, *inter alia*, that "any alleged agreement between the parties is unenforceable for lack of consideration."

ANALYSIS

LEGAL DISCUSSION: Contract classicists view consideration as the most obvious *sine qua non* of contractual obligation. From a historical perspective, the roots of the modern consideration doctrine go back at least as far as thirteenth-century English law (involving actions of covenant and debt, wax seals, wager-of-law oath helpers, etc.), and then evolving further during the fifteenth and sixteenth centuries of English law (involving assumpsit, trespass action, quid pro quo, misfeasance, nonfeasance, etc. [During this early era of assumpsit, defendants would plead the factors considered when making promises – that is, plead "considerations."]). Moving into the modern era of law, in the Anglo-American legal system, consideration has become a necessary and integral requirement of contract formation and, consequently, promises alone are insufficient to contract formation. (Although, interestingly enough, international contract law does, in fact, permit contract formation without consideration. See UNIDROIT Principles of International Commercial Contracts (2004), Article 2.1.1; CISG Art. 23, Art. 11.) In any event, in the instant issue, the Pennsylvania Superior Court, on the subject of reversing the trial court's granting of preliminary objections in the nature of a demurrer and dismissing Plaintiff's complaint: "When reviewing the dismissal of a complaint based upon preliminary objections in the nature of a demurrer, we treat as true all well-placed material, factual averments and all inferences fairly deducible therefrom. Where the preliminary objections will result in the dismissal of the action, the objections may be sustained only in cases that are clear and free from doubt...Any doubt should be resolved by a refusal to sustain the objections." The Pennsylvania Superior Court then discussed the classic formula for consideration, stated by Justice Oliver Wendell Holmes, Jr., as "the promise must induce the detriment and the detriment must induce the promise." Consequently, there is no consideration – and, rather, only a conditional gift – if the promisor did not seek to induce detriment in exchange for the promise, even if the promisee still suffered a detriment induced by the promise. However, in the instant issue, the Pennsylvania Superior Court – consistent with the Holmesian consideration formula – concluded that there was sufficient consideration since Defendant's promise (to provide free AggRite) induced Plaintiff's detriment (collecting and taking title of the 11,000 tons of AggRite from Defendant) and, moreover, Plaintiff's detriment (collecting the AggRite from Defendant) induced Defendant to make the promise (providing AggRite for free [so that Defendant could avoid the substantial cost of disposing of the AggRite that Defendant didn't need]). The Pennsylvania Superior Court also cited *Weavertown Transport Leasing, Inc v. Moran*, 834 A.2d 1169, 1172 (Pa. Super. 2003): "It is not enough, however, that the promisee has suffered a legal detriment at the request of the promisor. The detriment incurred must be the "quid pro quo", or the "price" of the promise,

and the inducement for which it was made....If the promisor merely intends to make a gift to the promisee upon the performance of a condition, the promise is gratuitous and the satisfaction of the condition is not consideration for a contract. [Also citing *Williston on Contracts*, Rev. Ed., Vol. 1, §112]." Further, in discussing the distinction between consideration and condition to a gift, the Pennsylvania Superior Court then cited *American Jurisprudence*: "...an inquiry into whether the occurrence of the condition would benefit the promisor. If so, it is fair inference that the occurrence was requested as consideration." 17A Am. Jur. 2d §104 (2004 & 2005 Supp.). In addition to the benefit/detriment test for consideration, the Pennsylvania Superior Court also discussed the bargain theory of consideration by citing *Stelmack v. Glen Alden Coal Co.*, 339 Pa. at 414, 14 A.2d at 129 (1940) ("Consideration must actually be bargained for as the exchange for the promise."), and by citing Restatement (Second) of Contracts §71 (note comment c ["the distinction between bargain and gift may be a fine one, depending of the motives manifested by the parties"]). The Pennsylvania Superior Court insisted that consideration requires a benefit/detriment that is bargained for. The Pennsylvania Superior Court concluded that there had, in fact, been a bargaining process between the parties. Accordingly to *Transcript of Proceedings*, Feb. 1, 2005, at 14-15, Plaintiff's attorney stated that "it was understood by everybody that this [i.e., avoidance of disposal costs] was what American Ash was getting in return for [providing the AggRite for free]." The Pennsylvania Superior Court discussed how the bargain theory of consideration does not require actual bargaining, citing bargain theory advocate Justice Holmes who stated that for consideration to exist, the promise and the consideration must be in "the relation of reciprocal conventional inducement, each for the other." *The Common Law*, 293-94 (1881). See also *Farnsworth on Contracts* §2.6 (1990); Restatement (Second) of Contracts §71(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."). Accordingly, the Pennsylvania Superior Court concluded that bargaining had existed between the parties. It should also be pointed out that the doctrine of promissory estoppel may also protect a party who suffered detrimental reliance even in the absence of a bargaining process. Therefore, while this brief has focused on the doctrine of consideration, it should also be noted that the Pennsylvania Superior Court reversed the trial court on the matter of promissory estoppel (as well as breach of warranty under Article 2 of the UCC). Two final notes: (1) Promises of future performance (in and of themselves, even without the immediate payment of any money) may also pass the consideration tests of benefit/detriment and bargaining – and, therefore, result in binding contract – since promises of future performance may be bargained for and, moreover, promises of future performance bind each party to a promise of future performance, resulting in benefit and detriment to the parties; (2) The benefit/detriment test and the bargain test may not necessarily both apply in all cases (see *Newman & Snell's Bank v. Hunter*, 220 N.W. 665 (Mich. 1928)).

of

Drennan v. Star Paving Co., 51 Cal. 2d 409, 333 P.2d 757 (1958)

CONCEPTS: Part performance as consideration for the implied subsidiary promise of unilateral and bilateral contracts, consideration not fatal to promissory estoppel, irrevocable offers, option contracts.

PARTIES: PLAINTIFF-APPELLANT: Drennan
DEFENDANT-APPELLEE: Star Paving Co.

ISSUE: Even in the absence of a contract, can an offer become irrevocable based on promissory estoppel (resulting from reasonable and foreseeable reliance)?

HOLDING AND RULE: Even in the absence of consideration, and even if the absence of a contract (such as a bilateral contract or an option contract), an offer can still become irrevocable based on promissory estoppel. Promissory estoppel can result when the offeror is silent on revocation of the offer and, at the same time, the offeror's promise is 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 [and, therefore, the promise] is binding if injustice can be avoided only by enforcement of the promise." Restatement (Second) of Contracts §90. The reliance should be reasonable and detrimental, and the action or forbearance should be of a reasonable and substantial character. The California Supreme Court affirmed the trial court's judgment for Plaintiff general contractor Drennan resulting from Defendant subcontractor Star Paving Co. refusing to do paving work in accordance with Defendant's bid.

FACTS: The California Supreme Court affirmed the trial court's judgment for Plaintiff general contractor Drennan resulting from Defendant subcontractor Star Paving Co. refusing to do paving work in accordance with Defendant's bid. Defendant submitted a bid to Plaintiff in the amount of $7,131.60. After Plaintiff was awarded the contract, Defendant then informed Plaintiff that Defendant had made a mistake in its bid, and that Defendant would only complete performance for $15,000.00. Plaintiff then attempted to mitigate its loss by identifying another subcontractor who agreed to complete the requested performance for $10,948.60. The trial court then entered a judgment for Plaintiff of the difference of $3,817.00, plus costs.

ANALYSIS

LEGAL DISCUSSION: Defendant argued that it had made a revocable offer and revoked this offer prior to Plaintiff's acceptance and, therefore, no contract may be enforced. Defendant further argued that Plaintiff's own general-contractor bid did not constitute acceptance of Defendant's subcontractor bid-offer to Plaintiff. Therefore, Defendant insisted that there was neither a bilateral contract nor an option contract supported by consideration. On the other

hand, Plaintiff argued that it was in detrimental reliance on Defendant's offer thereby making Defendant's offer irrevocable. In aligning with the arguments set forth by Plaintiff, the California Supreme Court discussed the concepts of reliance and promissory estoppel, and how Defendant was able to "reasonably expect" that its bid to Plaintiff would "induce action...of a definite and substantial character" by Plaintiff, citing §90 of the first Restatement of Contracts, as well as 1 Williston, *Contracts* (3d ed.), §24A, p.56, §61, p.196. The California Supreme Court pointed out that Defendant's bid did not indicate whether or not it was revocable prior to acceptance. The California Supreme Court then cited §45 of the first Restatement of Contracts, discussing how, in a unilateral contract, a promisee's part performance (as the promisee is in reliance on the promisor's offer) therefore results in the promisor's offer now becoming an irrevocable contract, as long as the promisee completes full performance (thereby tendering full consideration). Comment *b* to said §45 states how the "main offer includes as a subsidiary promise, necessarily implied, that if part of the requested performance is given, the offeror will not revoke his offer, and that if tender is made it will be accepted. Part performance or tender may thus furnish consideration for the subsidiary promise. Moreover, merely acting in justifiable reliance on an offer may in some cases serve as sufficient reason for making a promise binding (see §90)." The Supreme Court of California then concluded that the implied "subsidiary promise" of unilateral contracts also applied to bilateral contracts. The Supreme Court of California then discussed how promissory estoppel does not require consideration to still make the promissor's offer binding. The Supreme Court of California argued that Defendant placed its bid with Plaintiff not for some idle purpose, but for the serious purpose – and with the serious intent and serious self-interest – of obtaining the subcontract ("Defendant had reason not only to expect plaintiff to rely on its bid but to want him to. Clearly defendant had a stake in plaintiff's reliance on its bid."). The Supreme Court of California was also unimpressed with Defendant's attempt to argue that its bid to Plaintiff was a mistake and therefore unenforceable: The Supreme Court of California indicated that Defendant's cited case law described unrelated circumstances where the bidder's mistake was known, or should have been known, to the general contractor. In the instant issue, however, the Supreme Court of California stated that Plaintiff general contractor had no rational basis to reasonably believe that Defendant's bid-offer was a mistake. Moreover, Defendant had a duty to exercise reasonable care in preparing its bid-offer and, accordingly, "the loss resulting from the mistake should fall on the party who caused it." For the purpose of comparative case law discussion, this case of *Drennan v. Star Paving Co., supra,* is often compared – as a matter of contentious scholarly discussion – to the earlier similar-circumstances case of *James Baird Co. v. Gimbel Bros., Inc.*, 64 F.2d 344 (2d Cir. 1933), the decision written by Judge Learned Hand, affirming the lower court's ruling in favor of subcontractor Defendant. Note that this *Baird* case was decided in 1933, well before the widespread adoption of the UCC in the 1960s, and just one year after the first Restatement of Contracts was adopted by the ALI in 1932 (Restatement (Second) of Contracts not adopted until 1979). In *Baird*, Judge Hand acknowledged the doctrine of promissory estoppel in §90 of the first Restatement of Contracts for cases involving charitable donations, as well as for cases involving "harsh results" reliance by the promisee. However,

Judge Hand insisted that promissory estoppel did not apply in *Baird*, since Defendant had made a contractual offer for an exchange, thereby requiring consideration, such as a counter-promise of future performance, that is, a bilateral contract. Judge Hand insisted that Defendant's offer was in exchange for Plaintiff's acceptance, not Plaintiff's bid ("However, it seems entirely clear that the contractors did not suppose that they accepted the offer merely by putting in their bids."). Judge Hand argued that Plaintiff – even though relying on Defendant's offer to place a bid – had never communicated acceptance of Defendant's offer prior to Defendant's revocation (Defendant's offer: "[W]e are offering these prices...prompt acceptance after the general contract has been awarded.") and, therefore, no consideration was received by Defendant and, hence, no contract (citing Restatement of Contracts §35). Judge Hand pointed out that Plaintiff never once insisted upon a contract with Defendant prior to using Defendant's offer to then place a bid ("[I]n commercial transactions it does not in the end promote justice to seek strained interpretations in aid of those who do not protect themselves."). In addition to all this, Judge Hand also concluded that Defendant's offer should not be construed as an option contract (and that Defendant never had the intent to create an option contract with Plaintiff). It should be noted that while the *Drennan* versus *Baird* debate has clearly been judicially won by *Drennan* – even Restatement (Second) of Contracts §87(2) (see Comment *e* and Illustration 6) supports *Drennan* over *Baird* – there is, however, interesting legal research that questions all this: For example, see Franklin Schultz, *The Firm Offer Puzzle: A Study of Business Practice in the Construction Industry*, 19 U. Chi. L. Rev. 237 (1952), and Joe C. Creason, Jr., *Note, Another Look at Construction Bidding and Contracts at Formation*, 53 Va. L. Rev. 1720 (1967), discussing surveys of general contractors and subcontractors which concluded that general contractors do not, in fact, usually place very much reliance on the "firmness" of subcontractor offers. Therefore, it is rather ironic that there should be so much legal debate on this subject of general contractors versus subcontractors when, in reality, the vast majority of general contractors have never really had very much reliance on the "firmness" of subcontractors' offers in the first place. Most general contractors and subcontractors have never once read through §90 of the first Restatement of Contracts, or read through Comment *e* and Illustration 6 of §87(2) of Restatement (Second) of Contracts, or read through scholarly judicial decisions such as *Drennan v. Star Paving Co., supra*, or *James Baird Co. v. Gimbel Bros., Inc., supra*, and, therefore, there is a certain ironic element to all the legal debate on this subject. Indeed, it's rather fascinating – and even somewhat amusing – that there should be such a lengthy scholarly debate on the legal subject involving general contractors and subcontractors, when most general contractors and subcontractors don't really even care about all this lengthy scholarly debate, or place much reliance on any of it. Yet, at the same time, the legal debate on this subject does, nevertheless, provide a very lively discussion on extremely important legal concepts such as part performance as consideration for the implied subsidiary promise of unilateral and bilateral contracts, consideration not fatal to promissory estoppel, irrevocable offers, and option contracts.