

K Checklist

John Won 2003 Knapp

MEANING OF THE AGREEMENT

Principles of interpretation

- subjective approach (mutual assent)
- objective approach (four corners)

Modified objective approach (Corbin R2d§201)

- Whose meaning controls?
- What was that meaning?
 - Same meaning
 - either party knew/ had reason to know
 - both parties knew/had reason to know

Maxims of interpretation

Plain Meaning rule

Old: no extrinsic evidence **unless** ambiguous on its face

New: all relevant circumstances **limited** by PER

When is K ambiguous?

- four corners rule
- extrinsic ambiguity doctrine
 - objective evidence preferred
 - Subjective evidence not preferred

Reasonable Expectation Doctrine (Insurance K)

Application to adhesion Ks generally

Definition of “Adhesion K”

Parol Evidence Rule

Full Integration or Partial Integration? (R2d§210)

[full = complete + final/ partial = incomplete + final]

Traditional / Restrictive View (Williston)

- Four Corners Rule
- Merger clause conclusively establishes integration
- In absence of Merger Clause assume integration

Modern / Restatement View (Corbin)

- Not limited to four corners
- Consider all facts and circumstances
- Integration is a matter of intent, not formality

- Merger clause is one factor to consider –not conclusive

What evidence is considered?

Traditional / Restrictive View (Williston)

- see Plain Meaning above

Modern / Restatement View (Corbin)

- No need for ambiguity to look at extrinsic evidence
- Accept evidence if K is “reasonably susceptible” to the interpretation

What evidence is barred? (both views)

- Full integration = no contradict/no supplement (explain OK)
- Partial integration = no contradict (supplement or explain OK)

Exceptions

- Explain the meaning of the K
- Agreements made after the K
- ORAL condition precedent (R2d§217)
- K invalid for any reason: fraud, duress, undue influence, incapacity, mistake, or illegality (R2d§214(d))
- Promissory Estoppel (Minority)
- Equitable remedy: rescission, reformation, or specific performance (R2d§241(e))
- “Collateral” agreement: separate consideration or naturally omitted from the writing (R2d§216(2))

UCC PER (§2-202)

Terms set forth in writing intended as the final expression of those terms **May not be contradicted** by oral or contemporaneous agreements, **but may be explained or supplemented** by:

- Course of performance, course of dealing, trade usage
- Consistent additional terms unless the parties intended the writing to have been complete + exclusive statement of the terms (full integration)

SUPPLEMENTING THE AGREEMENT

Implied Terms:

Best Efforts / Reasonable Efforts (UCC§2-306(2))

- Exclusive dealing in the kind of goods concerned
- Obligation by seller to use best efforts to supply
- Obligation by buyer to use best efforts to promote their sale

Possible Exceptions (where consideration would exist)

- Bargain for a “chance” at showing goods attractive
- Bargain for credibility by represented by the agent

Reasonable Notice of Termination (UCC§2-309(3))

- Termination of a K by one party (except on the happening of an agreed event) requires that the party receive reasonable notification
- Agreement not to notify is void if unconscionable.

Reasonable Notice = time to:

- Recoup reasonable initial or continuing investment
- Close out product line
- Minimize losses
- Find a substitute arrangement

Other UCC implied terms (Place of delivery, time of payment, risk of loss, buyer’s right to inspect)

Implied Warranties:

Caveat Emptor

Applicability of UCC & C/L Warranties

- UCC applies to “goods” not services or real estate (§2-102)
- Key element of good is “movable” (§2-105(1))

Mixture of Goods and Services

Majority: Predominant Factor Test

- Relative costs of goods / services
- K language: whether parties were bargaining primarily for goods OR services

Minority: Gravamen of Harm Test (whether source of breach is goods portion or services portion)

Leases, software, blood products, commercial services

Express Warranties (UCC§2-313)

- Seller can make an express warranty by: words, description, sample, model
- “Puffing” → sales talk, opinions of value ≠ warranties
- Consider
 - Specificity of representations
 - Degree of hedging or qualifying
 - Experimental nature of the product
 - Buyer’s knowledge or expertise
- Reliance by buyer (SPLIT): most courts hold that UCC eliminates requirement for buyer’s reliance (but still the representations must be part of the “basis of the bargain”)

Implied Warranty of Merchantability (UCC §2-314)

- Sale of goods that are not of good quality or fit for the ordinary purposes for which they are used:
- Seller is merchant w/respect to goods of that kind; AND
- Defect in goods caused damages

Disclaimer of Warranties / “As Is” Clause (UCC§2-316)

- Merchantability warranty can be specifically disclaimed if language mentions “merchantability” and is conspicuous
- Fitness warranty can be waived w/conspicuous writing
- General Disclaimer (“As Is” / “With all Faults”):
- Disclaims all implied warranties
- May not disclaim express warranties
- Tort liability might not be disclaimed
- INSPECTION (or failure to inspect) waives warranties on defects that examination should have revealed
- Course of performance/dealing, trade use may exclude warranties

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SUPPLEMENTING THE AGREEMENT (Cont'd)

Implied Warranties (Cont'd)

Warranty of Fitness for Particular Purpose (UCC§2-315)

- Buyer relies on seller's skill or judgment to select goods
- Seller has reason to know of this reliance
- Does not require that goods are defective – just that they are not fit for buyer's particular purpose (most courts hold that this particular purpose must be other than ordinary use)

Implied Warranties of Title (UCC§2-312)

- Warranty of good Title
- Warranty of freedom from encumbrances
- Warranty against infringement

Warranties in Leases

- In finance leases, buyer gets warranty from supplier rather than financier (UCC§2a-209)
- Similar warranties (express, merchantability, fitness) as sales

Warranty of Habitability

- Implied warranty of habitability in residential leases (Majority)

Housing Merchant Warranties

- Implied Warranty of Quality in Sale of New Home (Maj)
- By builder / vendor
- House will be constructed in skillful manner / free from material defects

Warranty of Habitability

- House will not have any major defects to render it unsuitable for habitation

Warranty of Skillful construction

- Focuses on manner in which works is done (might still be habitable)

Disclaiming the Warranties:

- May be modified or disclaimed (Maj)
- Court may require disclaimer to be conspicuous, specific, result of mutual agreement
- "As Is" clause may be ineffective if seller has duty to disclose
- "As Is" clause may be effective if buyer fails to inspect
- Tort liability might not be disclaimed

SUPPLEMENTING THE AGREEMENT (Cont'd)

Implied Obligation of Good Faith:

Every K has an obligation of good faith in its performance (R2d§205; UCC §1-203)

Tort Action under Insurance K's

- Bad faith refusal to honor obligations
- See Expectation Damages

Requirement / Output Ks (UCC§2-306)

- In addition to duty to use reasonable / best efforts (b/c of exclusivity), there may be duty to act in good faith:
- *OVER-Demanding*: buyer may not order unreasonably disproportionate to the estimate or buy so much as to re-sell in competition w/seller or "stockpile" goods
- *UNDER-Demanding*: buyer may reduce his requirements to zero in good faith (shut-down of division, drop in demand for products) not bad faith (second thoughts, to curtail losses), even though the K contained an estimate of those requirements – as long as he does not buy from anyone else. (Empire Gas v. American Bakeries)

Discretionary Rights (*Locke v. Warner Bros.*)

- K gives one party discretionary powers affecting the rights of the other party
- Duty to exercise that discretion w/honesty and good faith (subjective standard of honest satisfaction)
- Not to frustrate the other party's right to receive K benefits

Exception: K can give parties the express right to act in a way that would otherwise be prohibited by the duty of good faith

Lender Liability

- When lender may "at will" accelerate debt (except demand instruments), terminate credit or an obligation to extend funds, or foreclose on collateral, it may be required to exercise good faith in that right (some courts say express terms of K govern)

Employment at-Will

- What kind of K?
- At Will
- Term
- "Permanent" (no term, but "good cause" required / usually unenforceable except w/additional consideration)

Implied in Fact Good Cause Provision

- Some courts allow employment manuals or other public statements to be offers for unilateral K

Termination of At-Will Employment

- W/O cause, regardless of motive (business reasons or personal dislike, hatred, or ill will) as long as not in BAD FAITH (Maj)
- **Bad Faith**:
 - Violation of public policy (may also be a tort)
 - Fraud, deceit, subterfuge, misrepresentation (falsifying employment file – *DuPont v. Pressman*)
 - Discharging employee before being paid a commission OR to avoid paying benefits

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AVOIDING ENFORCEMENT

Infants (R2d§14)

- All minors' Ks are voidable at their election up to the beginning of the day before they party's 18th birthday. (regardless of whether the court views them as to his benefit or prejudice)
- Power to Affirm: at majority, party can affirm (or must disaffirm in a reasonable time after achieving majority)

Mental Incapacity (R2d§15)

- K is voidable by incompetent party if:
 - At date of transaction, party was not able to understand in a reasonable manner the nature and consequences of the transaction.
 - Unable to act in reasonable manner in relation to the transaction AND other party has reason to know his condition
- EXCEPT:
 - If made on fair terms and in good faith, AND
 - Other party has no reason to know of incompetence
 - K is not voidable if parties cannot be restored to status quo ante
- Person does not have the power to enter into Ks if his property is under guardianship (R2d§13)

Duress

Physical Compulsion

- K is void if:
 - Threat to life or limb

Non-Physical (Economic) Duress (R2d§175:

- K is voidable by victim if:
 - Improper threat (wrongful, unlawful, or coercive act OR threat) (R2d§176)
 - No Reasonable Alternatives (subjective test); AND
 - Actual inducement of K by threat

Clean Hands (Split)

Undue Influence (R2d§177)

- K is voidable by victim if:
 - Unfair persuasion of a party (inappropriate time OR place, no time to consult advisers, multiple persuaders)
 - Who is under the domination of person exercising the persuasion OR
 - Who, by virtue of the relation between them, is justified in assuming that the person will not act inconsistent w/his welfare

Fraud OR Material Misrepresentation

- Tort C/A
- K cause of action: defense OR rescission / restitution

K is voidable by the recipient of a misrepresentation if:

- Inducement of assent by...
- Fraudulent OR Material Misrepresentations
- Justifiable Reliance (R2d§164)

FRAUDULENT:

- Intent to induce Assent, AND
 - Knowledge or belief that representation is false,
 - Lack of confidence stated OR implied in the truth of the assertion
- OR
- Knowledge that the party does not have the basis that he states or implies for the assertion

MATERIAL MISREPRESENTATION:

- Would be likely to induce a reasonable person to manifest his assent, OR
- If maker knows that it would be likely to induce the recipient to do so

AVOIDING ENFORCEMENT CONT'D

Non-Disclosure (R2d§161)

- A person's non-disclosure of a fact known to him is equivalent to an assertion that the fact does not exist ONLY IF:
 - Necessary to prevent some previous assertion from being a misrepresentation OR from being fraudulent or material;
 - Correct a mistake of the other party as to a basic assumption on which that party is making the K (if non-disclosure of the fact amounts to a failure to act in good faith and in accordance w/reasonable standards of fair dealing);
 - Correct a mistake of the other party as to the contents OR effect of a writing, evidencing or embodying an agreement in whole or in part; **OR**
 - Relation of trust and confidence between the parties

Unconscionability (UCC§2-302)

- A court may refuse to enforce a K (or a part thereof) that it finds unconscionable at the time it was made:
 - Procedural: Absence of meaningful choice
 - Substantive: Harsh, one-sided, unreasonable terms ("Shock the Conscience" OR reasonable standard)

Sliding Scale:

Many courts say defensive only, a few allow damages, rescission / restitution

Public Policy (R2d§178)

- All or part of a K may be unenforceable on grounds of public policy OR by "illegality" if:
 - Legislation provides that it is unenforceable (generally regulatory, maybe not revenue-raising), OR
 - The interest in its enforcement is clearly outweighed by a public policy against enforcement

Weigh the parties' interests against public's interest

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JUSTIFICATIONS OF NON-PERFORMANCE

Mistake

There is a general rule against avoiding a K b/c of regret (Ks are made to assign/avoid risk)

Mistake = erroneous belief that is not in accordance w/ the facts in existence at the time the K is executed

Mutual Mistake (R2d§152)

- Mistake of both parties at the time the K was made
- As to a basic assumption on which the K was made
- Material effect on the agreed exchange of performances
- K is voidable by the adversely affected party UNLESS he bears the risk of the mistake:

(R2d§154) When the party bears the risk of a Mistake:

- Risk is allocated to him in the agreement
- He is aware that he has limited knowledge at the time K is made but treats it as sufficient, OR
- Risk is allocated to him by the court b/c it is reasonable

-“As Is” clause may indicate intent to allocate risk to the purchaser (SPLIT)

Unilateral Mistake (R2d§153)

Avoidance of K for mistake of one party is allowed if:

- Mistake of one party at the time K was made
- As to a basic assumption on which K was made
- Material effect on the agreed exchange of performances
- K is voidable by adversely affected party UNLESS he bears the risk or mistake (see Mutual Mistake), AND
 - The mistake is such that enforcement of the K would be unconscionable (sever enough to cause substantial loss); OR
 - The other party either had reason to know of, or was responsible for causing the mistake.

Clean Hands: Many courts hold that the mistaken party must be non-negligent

Status Quo: Some courts hold that the other party must be able to be placed in the status quo

Changed Circumstances

Impossibility

Traditionally, K liability was “strict liability” (no excuse for not performing)

A party’s duty to perform is excused if:

- A person or thing necessary for performance of the agreement:
 - Dies OR is incapacitated (R2d§262)
 - Is destroyed OR damaged (R2d§263)
 - Is prohibited by governmental action (R2d§264)

Frustration of Purpose (R2d§265)

Seldom applied in the U.S.

- Where after the K is made, a party’s principal purpose
- Is substantially frustrated
- Without his fault
- By the occurrence of an event, the non-occurrence of which was a basic assumption on which the K was made,
- His remaining duties to render performance are discharged UNLESS the language OR the circumstances indicated the contrary (that he expressly assumed the risk)

The other party’s performance under the K has lost all value to one party

- The object must be so clearly the basis of the K that both parties understand that w/o it, the K makes little sense.
- Economic return / profitability may not be the reason (that is the purpose of every K).

JUSTIFICATIONS OF NON-PERFORMANCE (cont’d)

Impracticability (R2d§261)

- Where after K is made, a party’s performance is made impracticable
- Without his fault
- By the occurrence of an event, the non-occurrence of which was a basic assumption on which the K was made,
- His duty to render performance is discharged UNLESS the language OR circumstances indicate the contrary (that he expressly assumed the risk).

Performance may not be literally or subjectively impossible but impeded OR sufficiently different from what the parties had both contemplated at the time of contracting

Change in economic conditions that makes the K less profitable may not be a reason.

Some courts require the event to be unforeseeable – or at least unforeseen (Minority)

Modification

C/L Modification Rules

Pre-existing Duty Rule (R2d§73) (need consideration for modification
barring waiver)

EXCEPTIONS:

- Unanticipated Difficulties Rule (R2d§89(a))
- Surrender of a defense (R2d74)
- Detrimental reliance (R2d89(c))
- Surrender of a better offer

At-will employment K’s may be modified (3 approaches)

No Oral Modification (NOM) clause: at C/L not enforceable as a restraint on parties’ freedom to K

Accord and Satisfaction: may bar further claims

UCC Rules

- No consideration (and no formal requirements) needed (UCC§2-209(1))
- Obligation of Good Faith (acts as a bar to extortion OR duress)
- Notice of Protest: some courts require a party who feels it is being coerced to make plain that it is acting under protest.

SOF and Modification

- If K was subject to SOF, so must the modification

NOM (“private SOF”)

- NOM is generally valid (must have been separately signed in the K if between merchant and customer)

Exceptions to SOF:

- Immaterial changes
- Promissory estoppel
- Goods accepted and received OR payment made
- Waiver by actual later conduct
- Waiver by attempted modification (may require detrimental reliance)
- Actual performance can overcome NOM, like SOF
- Accord and Satisfaction (even cashing a check “under protest” or with “reservation of rights” may not work)

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WHAT ARE THE 3RD PARTY'S RIGHTS & DUTIES?

Standing of 3rd Parties

- Promisor, Promisee, 3rd Party
- Intended v. Incidental Beneficiaries (R2d§302)
- Outline pg 19

Assignment of Rights (R2d§317(2))

- Restrictions on Assignments
- Assignable K rights notwithstanding K Provisions to the Contrary
- Non-assignment clauses
- See Outline pg19/20

Delegation of Duties (R2d§318(1); UCC§2-210(1))

- Personal Services K
- Unsatisfactory Delegate to a Sale of Goods K
- Delegation to a Direct Competitor
- Non-Delegation clauses
- Original Obligor still Liable
- Release
- See outline pg 19/20

WHAT ARE THE CONSEQUENCES OF NONPERFORMANCE?

Breach of K (R2d§235(2)):

- Express Conditions
- Implied in-fact Conditions
- Constructive conditions
- See outline pg 21

Substantial Performance

- (*Jacob & Youngs*)

Total v. Partial Breach:

- Is the other party's breach material? (R2d§241)
- Has the material breach become total?

Anticipatory Repudiation:

- See outline pg 25
- Retracting repudiation

Demand for Adequate Assurances (R2d§251; UCC§2-609)

- See outline pg. 25

Express Conditions

- See outline pg 21
- Strict performance
- Effect of Non-occurrence (R2d§225)
- Interpretation
- Waiver (Material v. Non-material conditions)
- Retraction of Waiver
- Prevention
- Avoidance of Forfeiture
- Satisfaction of a Party (Subjective v. Objective Test)

WHAT ARE THE DAMAGES?

Expectation Damages

- See Outline pg 25
- Benefit of the Bargain Rule
- Expectation Damages Formula
- UCC Damages
- Interest on Damages

Restrictions on Recovery of Expectation Damages

- Foreseeability

Mitigation

- Lost Volume
- See Outline pg 28

Non-recoverable Damages:

- Attorney's fees
- Tort Damages

Reliance Damages (R2d§349)

- When expectation is too speculative
- See Outline pg 29

Restitutionary Damages (R2d§271)

- Unjust enrichment OR impoverishment
- See outline pg. 30

Specific Performance:

- Unique subject matter
- Adequacy Rule
- Personal Service (Positive/Negative Injunction)
- See outline pg 31

Agreed Remedies

- Liquidated Damages Provision (enforceable)
- Penalty (unenforceable)
- Objective Reasonableness Test (R2d§356(1); UCC§2-718(1))
- Time for determining reasonableness
- See Outline pg 31/32