

## Contracts (2<sup>nd</sup> Semester)

- I. Interpretation of terms of K
  - A. Goal: to get at the intent of the parties
  - B. Modified Objective Theory: R2d \_ 201(2) / UCC \_ 201-2- A party is bound by the other party's meaning if the first party knew or had reason to know of the second party's meaning while the second party did not know or have reason to know of the first party's meaning.
  - C. Main methods used (in order of weight given) R2d \_ 203 / UCC \_ 2-208
    1. **Express Terms**
    2. **Course of Performance**- A party always performs a certain way after K is formed. (R2d \_ 202- Applies where an agreement involves repeated occasions of performance by one party with the knowledge of it and opportunity for objection by the other- who did not previously object).
    3. **Course of Dealing**- this is the way it has always been done between the two parties before this K was formed. (R2d \_ 223- Previous conduct between the parties to an agreement which establishes a common basis of understanding)
    4. **Usage of trade**
  - D. When evidence of implied-in-fact terms are admissible
    1. Courts are divided
      - a. Restrictive view: such evidence is inadmissible if it appears to contradict the express terms.
      - b. Liberal view: such evidence is almost always admissible, even if it appears that the evidence "cuts down" the express terms (see e.g. Nanakuli below).
  - E. Other methods used
    1. Negotiation history
    2. Purpose of parties
    3. Government or statutory interpretations
    4. Subsequent conduct
    5. Construe against drafter rule
    6. Plain meaning rule:
      - a. If an express term has a plain meaning, court should not look at anything else but will interpret according to this plain meaning.
      - b. Major doubts about the validity of this rule. Most scholars say it is a bad idea, and the courts are split.
    7. Overall context
  - F. Patent (inherent) and latent ambiguity
    1. **Patent ambiguity**: Some courts require inherent ambiguity in a term before looking at the contextual evidence to interpret the term. This coincides with the Plain Meaning Rule.
    2. **Latent ambiguity**: While a term might not be inherently ambiguous, it may be ambiguous within the context of the K. Some courts allow the use

of any extrinsic evidence to support a parties claim of latent ambiguity, but this evidence must show that the term is ambiguous, not that the parties intended something different not incorporated into the K. (*Corbin approach*)

3. **Middle ground:** Some courts allow only “objective” (testimony of a 3<sup>rd</sup> party or trade usage, etc) rather than “subjective” (testimony about what the parties believed the K meant) evidence to show latent ambiguity.

G. Reasonable Expectations Doctrine: R2d \_ 211- The objectively reasonable expectations of applicants and intended beneficiaries regarding the terms of *insurance or adhesion Ks* will be honored.

1. Undermines the duty to read rule.
2. Not all courts accept this doctrine.
3. Some courts accept it broadly, as the court in C & J does.
4. Some accept more narrowly and require ambiguity in the terms. But there is already the construe against drafter rule so this approach doesn't do much.

H. Adhesion K:

1. Standard form agreement
2. One party has bargaining power and frequently enters such transactions while the other doesn't, and
3. It is presented on a “take it or leave it basis”

I. Cases

1. *Frigalment*- Example of latent ambiguity. Court had to interpret the word “chicken,” which is not on its face ambiguous. Plaintiff said “chicken” meant chicken suitable for frying & broiling. Defendant believed that considering the weights ordered at prices fixed by the parties that the order could be filled with a mixture of young chicken and older stewing chicken (“fowl” not “chicken” according to plaintiff). Court:
  - a. looked at K itself
  - b. usage of trade
  - c. negotiation of parties
  - d. market price v. contract price
  - e. course of performance—allowed 2d shipment
  - f. definitions from other resources—USDA
  - g. Found that P had not proved that “chicken” was used in the narrower rather than broader sense.
2. *C & J Fertilizer*- Court did not require ambiguity of terms to apply reasonable expectations doctrine. Definition of burglary in agreement said must have external damage (to prove it was an outside job). Damage was only internal. The agent had a sense that must have damage, but did not seem to know it must be external. Looked like neither agent nor P read the policy, Court said that terms should not apply because they undermine what was negotiated and what the insurance policy was reasonably expected to cover. Strong dissent said court should follow “Plain Meaning.”

## II. Parol Evidence Rule

- A. Effect: Bars supplementation to a final writing.
- B. Underlying Policy: When parties reduce the agreement to a final writing, the final writing is the best evidence as to what terms the parties agreed to.
- C. Rule: Other terms presented during oral agreements or earlier writings are superceded (excluded) by evidence of a final complete integrated writing.
- D. Analysis:
  - 1. Did the parties intend to produce a final writing? Only applies when there is a final writing.
  - 2. Is that final writing intended to be a complete integration? Two approaches as to how this is determined: Four Corners (Williston) and Contextual (Corbin).
  - 3. If yes, cannot supplement the final writing.
  - 4. If it is a partial integration, consistent additional terms (C.A.T.) left out of the writing can be added.
    - a. Cannot add terms that contradict the terms of the writing (**R2d \_ 215**).
    - b. Must be consistent, some courts say “reasonable harmony.”
    - c. Necessary included- some courts might exclude it even if it is a C.A.T. rationalizing that if the parties had agreed to it, they would have put it in the writing.
- E. Determining Partial v. Complete Writing:
  - 1. **Four Corners Approach (Williston)**- If there is nothing obviously missing from the writing, than the court assumes it is complete.
  - 2. **Contextual Approach (Corbin) R2d \_ 210**- The court, not acting as finder-of-fact, can take a preliminary look at extrinsic evidence to see if it can be submitted to a trier-of-fact to show it wasn't complete, or that there is another reasonable interpretation of a term. A writing by itself cannot illustrate its own completeness.
  - 3. **Merger Clauses**-
    - a. Williston approach believes merger clauses are conclusive or nearly conclusive evidence showing that the writing is fully integrated.
    - b. Corbin approach views it as evidence of a complete writing. integration.
    - c. **R2d \_ 216**- merger clause does not control the question of integration.
- F. **UCC \_ 2-202**- Final writing may not be contradicted by parol evidence, but may be explained or supplemented
  - 1. By course of performance, course of dealing, or usage of trade (interpretation) and
  - 2. By evidence of C.A.T. unless the court finds that the writing is a complete and exclusive statement of the terms of the agreement.

G. When PE rule does not apply

1. **Interpretation** of terms.
  - a. Some courts say even to interpret terms, evidence cannot be allowed if the “plain meaning” of the term is clear and “unambiguous.”
  - b. Others criticize plain meaning approach and use Corbin/R2d approach which asks whether the language is susceptible to more than one reasonable interpretation. **(R2d \_ 214(c))**
2. **Modification**- something that comes after the final writing.
3. **Oral precondition** (thin line)- a party can argue that the writing should not be enforced because it was subject to an oral precondition that was not satisfied.
4. **Discharge** (agreement is unenforceable)- evidence of fraud, duress, unconscionability etc. can always be presented.
5. **Equitable relief**- Drafter’s error. Must have clear and convincing evidence.
6. **Collateral Agreement**- Can have a separate K with separate consideration.

H. CISG (International Sale of Goods)

1. No statute of frauds
2. No PE rule- goes to jury to figure out whether the buyer or seller is lying about previous oral agreements.

I. Cases

1. *Thompson v. Libby*- Writing agrees to sale of logs for a certain price. D (buyer) didn't pay claiming breach of warranty based on an oral promise as to the quality of the logs. Court used “four corners” approach and did not allow parol evidence to show that it was a partial integration.
2. *Taylor v. State Farm*- Car accident, P sued insurance company for not settling with other party and alleges bad faith. There was final writing that included a release, D says P gave up all claims he might have had. P says the release only included contractual issues, not his claim of bad faith. The issue is interpretation of the release agreement, thus the PE rule does not apply.
3. *Sherrodd, Inc. v. Morrison-Knudsen*- Subcontractor puts in a bid based on incorrect info about amount of work to be done. Starts work, finds job to be much bigger. Signs written K w/ original amount of work and bid, says he had an oral agreement that the amounts would be adjusted and that he wouldn't get paid unless he signed K. P tries to prove fraud to get K thrown out- but he signed the final writing and fraud was disclaimed by the writing (courts are split on the effect of this). He can't supplement- the merger clause is big evidence that it is a complete integration. Perhaps P could have raised duress or mistake.
4. *Nanakuli Paving v. Shell Oil*- UCC case. K said Shell's price would be the posted price at the time of delivery. P said there was an understanding of price protection; that the price offered at the time the bid was made applied. Court found evidence of price protection agreement through usage of trade and course of performance, but this evidence cannot contradict an express term in the writing. Court says that it doesn't really contradict, b/c a full negotiation would be if Nanakuli were to set the

price. Court takes a very liberal view in finding evidence of price protection consistent with writing. **Courts will bend over backwards to find ways to make evidence of Course of dealing or Usage of Trade apply, even though express terms are to be given more weight and even if they could be construed to contradict an express term (here, the court says the term is consistent). Idea is that they may be more dependable as evidence of what the parties intended than the writing itself.**

### III. Implied Terms

#### A. Implied in fact

1. Obligation to use reasonable efforts- courts will say this is implied to prevent an indefinite promise from being illusory. (e.g. Wood v. Lady Duff- D gave P exclusive right to put her name on fashion designs by others, ct says P had implied promise to use reasonable efforts)
  - a. Prof. Eisenberg says if you bargain for an illusory promise (other side can back out) you should be bound to it. But the court in Lady Duff held that she did not bargain for an illusory promise but an implied promise.
  - b. UCC \_ 2-306- imposes a duty to use “best efforts.”

#### B. Implied in law

##### 1. Duty of Good Faith

- a. **R2d \_ 205 /UCC \_ 1-203**- every K imposes on each party a duty of good faith and fair dealing in its performance and enforcement.
  - (1) UCC comments- Parties must act consistently with the K’s purpose. A party cannot evade the responsibilities of performance.
  - (2) UCC \_ 2-103- “good faith” means
    - (a) honesty in fact
    - (b) the observance of reasonable commercial standards of fair dealing. (Protecting benefits the other side reasonably expects to receive).
- b. **Effect**
  - (1) Sets up affirmative duties on parties to a K, and prevents parties from doing certain things in “bad faith.”
  - (2) Protects the reasonable expectations of the parties.
  - (3) Prevents a party from frustrating the right of the other party of benefitting from the K.
- c. Should be employed where one party’s actions were such as to undermine the “spirit” of the K, either by enabling that party to realize gains that in making that K he had implicitly agreed to surrender, or by unfairly denying to the other party the fruits of the K she reasonably expected to receive.
- d. **Examples of good faith:**

- (1) fully disclosing material facts
  - (2) substantially performing w/o knowingly deviating from specifications.
  - (3) refraining from abuse of bargaining power
  - (4) acting cooperatively
  - (5) acting diligently.
  - (6) interpreting K language fairly
- e. **Express rights v. Duty of good faith**
- (1) If one party has bargained for the express right to do something, most courts say this right cannot be cut down by the duty of good faith.
  - (2) Some courts will draw fine line distinctions between actions that are covered exclusively by express terms and those that are also subject to the implied duty of good faith. (See e.g. *Locke*- express right to reject Ps proposals, but D had duty to evaluate them in good faith).
- f. **Lender liability**
- (1) Lenders often demand express right to
    - (a) cut off a line of credit
    - (b) demand immediate repayment
  - (2) Courts are split on the effect of the duty of good faith in these agreements:
    - (a) some say still subject to duty
    - (b) others say duty cannot cut down express terms
    - (c) UCC \_ 1-208 says duty of good faith does not apply- does not have any application to “demand instruments.”
- g. **Requirements K/Output K**
- (1) Requirements K is a promise from a buyer to buy all of some good from seller, in exchange for a good deal from the seller.
  - (2) An output K is where the seller agrees to sell all its output to a buyer.
  - (3) Both have open or estimated quantity of goods.
    - (a) Overdemand (UCC \_2-306)- Not allowed. The amount over cannot be unreasonably disproportionate to the estimate.
    - (b) Underdemand (UCC \_2-306)- As long as it is done in “good faith” the amount needed could go all the way down to zero. Difficulty is in figuring out when there is a good faith reason.
      - i) Change of thoughts not good enough
      - ii) economic difficulty- miscalculation not enough but sometimes severe economic



- (a) If an employee can show he was let go to deny compensation already earned (bonus/commission) than that is a breach of the duty of good faith.
- (b) Parties may expressly agree that termination must have cause, even if no set duration.
- (c) If there is a duration, than it is not an at-will K and employer must have cause.
- (2) Manner of termination
  - (a) There are limits on how the employer can terminate- the termination is never a breach of good faith, but may be a breach in how employee is treated up until termination.
- (3) Duty of good faith does apply to all other aspects of employment K
- (4) Exceptions to no-cause for termination rule-
  - (a) Public Policy- must involve a clear mandate of public policy founded on constitutional, legislative, administrative, or established judicial authority.
 

Examples:

    - i) An employer cannot fire employee for refusal to commit a crime.
    - ii) cannot fire employee for complying with a statutorily imposed duty (i.e. OSHA)
    - iii) cannot discharge an employee when specifically prohibited to do so by statute.
    - iv) Whistleblowers not protected
  - (b) Additional Consideration
    - i) Kind of looks like reliance- quitting current job and moving b/c of new employer's recruiting efforts.
  - (c) Promissory Estoppel
  - (d) Employee Manual- courts clearly split on this.
    - i) If the employer in a published manual gives assurances that the employee will only be let go for cause or after certain procedures, read as part of the K.

### 3. Warranties

- a. The seller need not have the intent to create a warranty.
- b. **Express Warranties** - UCC \_ 2-313(1) can be created by:
  - (1) an affirmation of fact or promise by the seller
    - (a) Commendation or "puffery" by seller does not create an express warranty (see *Bayliner*)
  - (2) a description of the goods which is made part of the basis

- of the bargain
    - (3) A sample or a model made part of the basis of the bargain.
- c. **Implied warranty of merchantability - UCC \_ 2-314**
  - (1) If the seller is a merchant with respect to a particular type of goods
  - (2) Goods must have good quality
    - (a) pass without objection in the trade
    - (b) fit for the ordinary purpose (meets the reasonable expectations of the buyer).
- d. **Implied warranty of fitness for a particular purpose- \_ 315**
  - (1) Buyer has a particular need/purpose
  - (2) seller knows buyer's purpose
  - (3) seller knows buyer is relying on seller to choose goods for that purpose
  - (4) buyer does rely
  - (5) seller does not have to be a merchant
  - (6) (some courts say that it must not be the ordinary purpose of the goods- this is not expressed in UCC).
- e. **Implied warranty of Title - UCC \_ 2-312**
  - (1) Title is good and transfer is rightful
  - (2) Goods free from security interest or lien which buyer at time of contracting has no knowledge
  - (3) unless specific language or circumstances give buyer reason to know seller does not claim title in himself
- f. **Implied Housing Merchant Warranty**
  - (1) Construction of house is done in a "skillful manner"
    - (a) Strict interpretation- must be some defect that makes house uninhabitable
    - (b) Intermediate- doesn't meet the standards of skillful construction; doesn't have to be uninhabitable.
  - (2) Justification- reasonable expectations of buyer to buy a house that is habitable.
  - (3) *Caceci v. DiCanio*- 4 years after buyer moved in, found problems with foundation. Ct found implied housing merchant warranty.
- g. **Time frame in bringing suit for breach of warranty**
  - (1) UCC = 4 years
  - (2) Some legislatures have codified time frame, and there is always SOL.
- h. **Disclaimer and exclusion of warranties - UCC \_ 2-316**
  - (1) Seller can disclaim implied warranties
  - (2) Limits:
    - (a) cannot disclaim express warranties (by PE rule may be a problem with express oral warranties and

- written disclaimers)
- (b) Must be in writing and conspicuous
- (c) Housing merchant warranties can also be disclaimed but most courts view disclaimers with suspicion say must be conspicuous, specific, and the result of mutual agreement.
- (3) can use language such as “as is”
- (4) When a buyer examined or refused to examine the goods, there is no implied warranty regarding the defects which an examination ought to have been revealed to him
- (5) implied warranty can also be excluded or modified by course of dealing or performance.
- i. *Bayliner Marine Corp v. Crow*
  - (1) No express warranty, because there was a disclaimer that the boat would go 30 miles per hour only under certain conditions. Ct says P did not buy the boat as described, so no breach.
  - (2) Line in brochure “this boat delivers the kind of performance you need to get to offshore fishing grounds” is mere puffery.
  - (3) No breach as to merchantability because not enough evidence that it was not fit for ordinary purposes.
  - (4) No breach as to particular purpose because seller did not know buyer had a particular purpose (needed boat to go at least 30 miles per hour).

#### IV. Modification

- A. Pre-existing duty rule- merely promising to perform an existing obligation will not serve as valid consideration for additional return compensation from the other party. Must give new consideration.
  - 1. Small consideration (not nominal, still have to bargain for it) suffices.
  - 2. Exceptions:
    - a. **R2d \_ 89(a)**- if the modification is fair and equitable based on *unforeseen circumstances*, no new consideration is required.
    - b. **R2d \_ 73/74**- A party’s good faith belief that it is not bound by the original K can be good consideration.
    - c. **R2d \_ 89(b)**- *statute*: refers to **UCC \_ 2-209(1)** which does not require new consideration for modification. No pre-existing duty rule with the sale of goods, but modification must be made in good faith.
    - d. **R2d \_ 89(c)**- *reliance*: modification is binding to the extent that justice requires enforcement in view of material change of position in reliance on the promise.
    - e. *Mutual recession* and formation of new K- but cts are suspicious

when they see something that looks like duress followed by mutual recession and a new K.

3. At-will Ks- some cts say an employer cannot take away employee benefits in an employee manual deemed binding through the unilateral K formation process without new consideration.
  - a. In CA, employers have the right to change benefits, provided they give adequate notice. It is not modification, but employer policy.
4. Protest- Courts are split on whether a party has to protest the modification at the time it is done in order to seek recession under the pre-existing duty rule.
5. *Alaska Packers v. Domenico*- P = fishing crew contracted with D. P quit working and threatened not to continue unless D payed more \$\$\$. D protested and was not authorized to okay more \$\$\$, but no replacement so he promises more \$\$\$. Not enforceable due to pre-existing duty rule.

B. Modification under the UCC 2-209

1. No new consideration required.
2. New K must be formed in good faith.
3. No oral modification clauses- Under the UCC, these are not enforceable, because parties can orally wave the clause and then modify the agreement.
4. Protest of a bad faith modification- Some cts hold that a party agreeing to an assertedly coerced modification has a *good faith duty to make plain that it is acting under protest*, so that the other party will not be deceived as to its intention to eventually resist enforcement. Duty of good faith ties both the party seeking enforcement and the party resisting it.
5. *Kelsey-Hayes v. Galtaco*- 3 year requirement K, P bought castings from D at a fixed price. D says won't continue operations unless P agrees to price increases. P protested but had no other option. P refuses to pay, claiming economic duress. Ct agrees that new K was not formed in good faith, P protested enough to preserve its rights.

v. Excuses/Justifications for non-performance

A. Lack of capacity

1. Minors- Ks with minors are voidable at the election of the minor. The minor must do something to affirmatively void it.
  - a. **Return**
    - (1) *Majority rule*- minor must restore to other party whatever he received from K or whatever he has left from K, and he will get \$\$ (or whatever he exchanged) back.
    - (2) *Minority rule (Dodson v. Shrader)*- where there is no undue influence, minor cannot be permitted to recover the amount actually paid, without giving the seller reasonable compensation for the use of, depreciation of, or the willful/negligent damage to article purchased.
      - (a) Many say this only applies to things purchased with cash. So, if minor pays with credit, does not have to

make restitution.

- b. **Lack of knowledge** as to age is no excuse, but misrepresentation/fraud is.
  - c. **Disaffirmance**- minor has a certain period of time to disaffirm K.
    - (1) Some place it at a “reasonable time” after reaching majority, others set the time period.
  - d. **Ratify**- If minor does not disaffirm, he has implicitly ratified K. Always voidable while still a minor, even if the minor has ratified it.
  - e. **Exceptions**
    - (1) Necessaries- If minor Ks for food, shelter, clothing, medical care etc, the minor must pay reasonable value for them (not the K price).
    - (2) Minor commits tort- such as misrepresentation of age or willful destruction of property.
    - (3) Statutory- student loans, certain types of insurance Ks
    - (4) Emancipation- in some jurisdictions
  - f. Releases (that parents sign)- not an exception, most jx say that adults cannot bind the minor to a pre-injury release. Post-injury release has to be approved by court.
2. **Mental Incapacity**- K *voidable* if person lacks mental capacity to contract. If someone has been placed under court ordered guardianship, their Ks are *void* (**R2d \_ 13**).
- a. **Determining status:**
    - (1) *Cognitive test*
      - (a) Person is incapable of understanding K at the time it was made.
      - (b) Law presumes person is competent, he has burden of proof.
    - (2) *Volitional test*-
      - (a) Person is unable to act in a manner in relation to the transaction
      - (b) Other party has reason to know of his condition (not all courts require this).
    - (3) **R2d \_ 15**- adopts both of the tests.
  - b. **Return:**
    - (1) *General rule*- Can disaffirm only if you can restore other party to status before K was made.
    - (2) *Exceptions*-
      - (a) Other side knew or had reason to know of mental incapacity.
      - (b) K not made on fair terms.
      - (c) K was not made in good faith.
  - c. **Disaffirm**- must do so within a reasonable time.

d. *Hauer v. Union State Bank*- Ct found that D knew or had reason to know P was mentally incompetent to understand the nature of the loan (which she in turn loaned to someone else who lost it all). Thus, the bank also failed to act in good faith. Bank ordered to return P's collateral.

3. Economic Duress- Ks made under economic duress are *voidable*.

a. Elements **R2d \_ 175**:

- (1) Wrongful or improper threat
- (2) lack of reasonable alternatives
  - (a) availability of legal action *if* in the circumstances that is a viable option
  - (b) availability of supplies from other sources.
- (3) actual inducement or overcome of will (if the first two elements are found, this one usually is).
- (4) Majority of cts say D must also have caused the financial hardship, others say knowledge and taking unfair advantage is enough- R2d supports the latter view.

b. Third person **R2d \_ 175**:

- (1) If a party's manifestation of assent is induced by an improper threat of a person not a party to the transaction
- (2) the K is voidable
- (3) *unless* the other party in good faith and without reason to know of the duress
- (4) gives value or relies materially on the transaction.

c. Improper threats **R2d \_ 176**:

- (1) crimes and torts
- (2) threats of criminal prosecution
- (3) bad faith threats of use of civil process
- (4) threats that are breaches of duties of good faith
- (5) threat is improper if the resulting exchange is not on fair terms and
  - (a) threatened act would harm the recipient and not significantly benefit party making the threat
  - (b) prior unfair dealing by party making the threat
  - (c) it is otherwise a use of power for illegitimate ends.

d. *Totem v. Alyeska*- P K'd to haul goods from TX to Alaska. When P arrived, there were more goods than bargained for and not ready to load- took 30 days rather than projected 3. After unloading, D terminated K. D did not act in good faith and allow P to enjoy the "fruits" of K. P attempted to recover costs \$275,000. P signed settlement of \$97,000 in exchange for release. P was in dire financial straits (company about to collapse, could not wait for legal remedy) and D was threatening to withhold payment. Release voidable by P because of economic duress.

4. Physical Duress **R2d \_ 174**- If the K is signed under the threat of physical force, that K is *void*.

5. Undue Influence **R2d \_ 177**

a. Elements

- (1) Overpersuasion
  - (a) coercive in nature
  - (b) overcomes will of other person
- (2) One party is weak or subservient in some way
- (3) Other party is strong or dominant applying excessive pressure.
- b. Third person
  - (1) If a party's manifestation of assent is induced by one not a party to the transaction
  - (2) It is voidable *unless*
  - (3) the other party in good faith and without reason to know of the undue influence
  - (4) gives value or relies materially on the transaction.
- c. Factors in determining overpersuasion:
  - (1) discussion or consummation of transaction at an unusual or inappropriate time
  - (2) insistent demand that the business be finished at once
  - (3) extreme emphasis on consequences of delay
  - (4) the use of multiple persuaders by the dominant side against a single servient party
  - (5) absence of third party advisers to the servient party
  - (6) statements that there is no time to consult financial advisors or attorneys.
- d. *Odorizzi*- teacher arrested, charged with homosexual activity. School officials persuaded him to resign on the day he was released from bail. Had no time to consult an attorney, was told that he needed to sign now, that if he didn't sign, his reputation would be ruined, he hadn't slept in hours when they showed up at his door (inappropriate time and place), and he was in weaker position. K voidable due to undue influence.

## 6. Misrepresentation

- a. Actual Fraud R2d \_ 164(1)
  - (1) False representation
  - (2) knowledge of falsity
  - (3) fraudulent intent *or* innocent but material fact
    - (a) 162- fraudulent also includes an assertion made recklessly or negligently as to whether it is true or false.
  - (4) reasonable justifiable reliance
  - (5) resulting damage
- b. R2d \_ 164(2)- misrepresentation by third person
  - (1) If a party's manifestation of assent is induced by a fraudulent or material misrepresentation by the other party
  - (2) upon which that party is justified in relying
  - (3) the K is voidable
  - (4) *unless* the other party in good faith and without reason to

know of the misrepresentation gives value or relies materially on transaction.

- c. Statements of opinion
  - (1) **R2d \_ 168**- an opinion is the expression of a belief, without certainty, as to the existence of a fact.
  - (2) Reliance on Opinion **R2d \_ 168** - usually not justified *unless*,
    - (a) special relationship of trust and confidence (fiduciary relationship).
    - (b) expert on matters covered by the opinion
    - (c) renders the opinion to one who, because of age or other factors, is particularly susceptible to misrepresentation.
- d. Constructive Fraud
  - (1) where there is a confidential or fiduciary relationship
  - (2) courts may construe an innocent but false statement as fraud.
- e. Active concealment R2d \_ 160
- f. Nondisclosure R2d \_ 161- Usually a presumption that there is no duty to speak. But, a person's non-disclosure is equivalent to an assertion that the fact does not exist if:
  - (1) he knows that disclosure is necessary to prevent a previous assertion from being a misrepresentation -circumstances have changed.
  - (2) he knows that disclosure would correct a mistake not readily discoverable
    - (a) of a writing
    - (b) or of the other party in making an assumption
  - (3) the nondisclosure amounts to a failure to act in good faith
  - (4) there is a relationship of trust and confidence (fiduciary).
- g. Fraud in execution R2d \_ 163 (Park 100 case)
  - (1) A misrepresentation as to the character or essential terms of K
  - (2) which induces a party to assent
  - (3) but that party does not know or have reasonable opportunity to know the true character or terms of K
    - (a) than no MA and no K.
- h. Effect of Disclaimer or merger clause - 3 views
  - (1) *Hill* said evidence of fraud is never barred
  - (2) *Sherrod* said it is barred by P.E. rule
  - (3) NY takes an intermediate position and say a specific disclaimer bars evidence of fraud.
- i. *Hill v. Jones*- K for sale of home, buyers asked if ripple in wood floor was caused by termites. Sellers said it was water damage. Ended up being termites. Plants and boxes were

covering damage in other areas- could be active concealment but have to prove sellers intentionally put stuff there. There is actual fraud because (1) false representation about ripple in floor (2) even if no intent, it was a material fact (3) reasonable reliance because relying on seller's statement and termite inspection.

7. **Unconscionability UCC 2-302 / R2d 208**- Designed to police Ks for extreme unfairness. K must be both procedurally and substantively unconscionable (but the more you have of one, the less you need of the other).
  - a. Examples of Procedural unconscionability:
    - (1) lack of meaningful choice
    - (2) defect in bargaining process
    - (3) unequal bargaining power
  - b. Examples of substantive unconscionability:
    - (1) unfair, hidden, or unintelligible terms.
  - c. Merchants must have a really good case to have the doctrine applied to them- usually isn't applied to commercial transactions.
  - d. Either the K as a whole or a particular term may be deemed unconscionable.
  - e. Must be unfair at the time K was made
  - f. In CA, an adhesion K is per se procedurally unconscionable.
  - g. Remedial options:
    - (1) cts can refuse to enforce K as a whole
    - (2) strike a particular clause
    - (3) or enforce K but limit the unconscionable effect.
  - h. *Williams v. Walker-Thomas*- P bought goods from D, D had right to repossess all good previously purchased upon default. Unconscionable K because: (1) door-to-door sales made it unlikely P would find out about clause (2) standard adhesion form not read (3) unintelligible clause (4) D knew of Ps bad financial situation- bad faith (5) unfair terms.
  - i. *Adkins v. Labor Ready*- **Sanctity of K** Employee sues temp agency, agency says must submit claims to arbitration per clause in K. Probably procedurally unconscionable- disparity in bargaining power, take-it-or-leave-it K. But ct says no substantive unconscionability. Fed law strongly favors arbitration. P argues unfair terms b/c he would have to pay arbitration fees not able to afford. This may be enough but P did not present any evidence as to costs.
  - j. *Cooper v. MRM Investment*- **Protecting Ps rights** Facts very similar to Adkins. Procedurally unconscionable b/c the average person wouldn't understand they are waiving their right to a jury trial and lack of meaningful choice. Substantively unconscionable b/c lack of bilaterality (i.e. both parties have to submit to arbitration) and costs of arbitration would be more than Ps annual income, thus barring P from protecting her rights.
8. **Public Policy R2d 178**- the substance of the agreement might go against public policy making it unenforceable.
  - a. Sources
    - (1) Constitutions

- (2) Statutes
- (3) Judicial precedent
- b. Examples
  - (1) **R2d \_ 187/188**- some types of restraints on free trade and covenants not to compete
  - (2) **R2d \_ 191**- A promise affecting the right of custody of a child unless it is consistent with the best interest of the child.
  - (3) Family relationships
  - (4) Ks to commit a crime
  - (5) exculpation agreements (limits liability)
    - (a) cannot engage in willful or reckless conduct and then exculpate oneself. If just ordinary negligence, than maybe it will be upheld.
  - (6) Ks that negatively affect the administration of justice.
  - (7) Ks that undermine a fiduciary duty.
- c. Covenants not to compete
  - (1) Usually disfavored by courts
  - (2) **R2d \_ 188**- Not valid if unreasonable:
    - (a) the restraint is greater than is needed to protect the promisee's legitimate interest, or
      - i) The interest must not be to avoid competition. Can be to protect current clients or referrals.
    - (b) the promisee's need is outweighed by the hardship to the promisor and the likely injury to the public.
  - (3) Severance
    - (a) **Blue pencil approach**- Allows severance or reduction only if the objectionable term can literally be lined out and the remainder enforced.
    - (b) **R2d \_ 184**- more flexible, allows reduction of the effect or scope of a covenant to make it reasonable. Only allowed when the clause was not made in bad faith and no evidence of deliberate overreaching.
    - (c) Some cts refuse to sever and enforce a flawed covenant in any case.
  - (4) Per se rule that covenants not to compete in the case of lawyers are not enforceable.
  - (5) *Valley Medical v. Farber*- P (a doctor) had an agreement with former employer not to practice within a 5 mile radius of any of Ds offices for 3 years after terminating employment. Ct held not reasonable because of excessive duration, geographic scope, and scope of restricted activity too broad (couldn't perform any medical services- even emergencies). Ct adopted blue pencil approach, but said nothing could be lined out so the entire covenant was

unenforceable.

- d. Remedial options
- (1) Leave parties where they find them
  - (2) Fully enforce (rare)
  - (3) Partially enforce- restitution
  - (4) **R2d \_ 178**- Factors used to determine which option is appropriate:
    - (a) the parties' justified expectations
    - (b) any forfeiture that would result if enforcement were denied
    - (c) any special public interest in enforcement of a particular term
    - (d) the strength of the policy as manifested by legislation or judicial decisions
    - (e) the likelihood that refusal to enforce the term will further that policy
    - (f) the seriousness of the misconduct involved and whether it was deliberate.
- e. *Borelli v. Brusseau*- P claims oral K between her and her husband before his death: promise to take personal care of him after stroke in exchange for interests in property and business. Ct says on the basis of marriage statutes spouses have a duty to take care of each other, and you cannot K for what you are already obligated to do (no consideration).
- f. *R.R. v. M.H.*- Surrogacy agreement. P and wife paid 10,000 for pregnancy fees and custody. Ct looks to adoption statutes and says it is against public policy to sell babies. Also K includes pre-birth surrender, adoption statutes say can't give up baby any sooner than 4 days after birth.

## 9. Mutual Mistake

- a. Elements **R2d \_ 152**
- (1) Shared mistake (basic assumption)
  - (2) Material mistake
  - (3) K can be avoided by the adversely affected party unless:
  - (4) He bears the risk of mistake.
- b. When a party bears the risk of mistake **R2d \_ 154**
- (1) the risk is allocated to him by agreement of the parties
  - (2) he is aware, at the time the K was made, that he only has limited knowledge with respect to the facts to which the mistake relates.
  - (3) the risk is allocated to him by the court on the ground that it is reasonable in the circumstances to do so.
- c. *Lenawee County v. Messerly*- D sold P land on which apartments were built. Soon discovered that sewage system on land was not adequate (neither knew about this at the time property was sold). P could not make \$\$ off land because property was condemned. First three elements exist, but court says the allocation of risk is on the buyer because of disclaimer/merger "as is" clause in K.

## 10. Unilateral Mistake R2d \_ 153

- a. Elements
    - (1) Mistake of one party
    - (2) material- severe enough to cause substantial loss *or*
    - (3) The other party had reason to know of, or was responsible for causing, the mistake.
    - (4) The mistaken party must not bear the risk of mistake.
    - (5) Must be able to return to status quo ante.
  - b. If a party is **grossly negligent**, unilateral mistake defense may not be allowed. However, **R2d \_ 157** negates any requirement that the mistaken party be non-negligent, requiring only that conduct be done in good faith and fair dealing.
  - c. *Wilfred's v. Metropolitan Sanitary*- P relied on subcontractor bid when placed bid with D. Subcontractor was mistaken in calculations, P attempted to revoke bid but D wouldn't allow it. Ct found for P because it was a material mistake (would cost P \$150,000), P had used reasonable care in relying on subcontractor bid, and the parties would be able to return to status quo ante. Subcontractor could not have sued P because there would be no way to return to status quo ante- P would eat the loss.
11. Impossibility- after K was made, supervening circumstances make it impossible for the K to be performed.
- a. Types of circumstances:
    - (1) **R2d \_ 262**- Death or incapacity of an essential person:
    - (2) **R2d \_ 264**- Illegality (prevention by government regulation or order)
    - (3) **R2d \_ 263**- Destruction of subject matter essential to performance of K.
12. Impracticability- the nature of the performance has so changed that it has become impractical.
- a. People rarely succeed on this defense.
  - b. Elements **R2d \_ 261**:
    - (1) Substantial reduction in the value of K
    - (2) basic assumption of non-occurrence of event
    - (3) the event happens
    - (4) without the party's fault
    - (5) the party does not bear the risk of that occurrence either under the language of K or the surrounding circumstances
    - (6) (foreseeability)-
      - (a) some courts require a showing that the event complained of was at unforeseen
      - (b) some say must be unforeseeable.
      - (c) Most do not require either.
  - c. Force Majeure Clauses- provide for specific excuses where performance is prevented or delayed by circumstances beyond the control of the party.
  - d. Change in market conditions- usually not enough to be granted

- relief.
- e. Increases in costs/loss of profitability- are not basic assumption. They are foreseeable and assumed risks, and do not render Ks impractical.
  - f. Natural disaster/war- have a times been enough to grant relief, but not usually.
  - g. *Karl Wendt v. International Harvester*- P has K to be exclusive distributor of Ds farm equipment. D sold farm equipment line due to dramatic decrease of market value. P does not get K from new owner, sues D for breach of K. K had termination provision specifying how each party could terminate K. Ct says mutual profitability is not a basic assumption of Ks. Ct focuses on Ds selling farm equipment as event, and says it is Ds fault. (Ct could have focused on change of market as event- not Ds fault). P prevails.
13. Frustration R2d \_ 265- Something happens that frustrates the principle purpose of the K.
- a. Also rare for parties to succeed on this defense.
  - b. K must be rendered almost totally valueless to succeed on this defense.
  - c. Elements- essentially has same elements as impracticability  
(1) basic assumption here refers to the principle purpose of K.
  - d. *Mel Frank v. Di-Chem*- D rents building from P to store chemicals. Gov. inspects after enactment of new regulation, finds building insufficient to store hazardous materials. D says "we're outta here." P sues for breach. Ct says new regulation not enough to excuse non-performance, because K has not been rendered *totally* worthless. D can still store all of its non-hazardous materials there.
  - e. Restitution is the remedy for frustration, impracticability, and impossibility.

## VI. Third Party Beneficiaries

- A. General rule- 3<sup>rd</sup> party beneficiaries are allowed to sue for damages based on a breach of a contract they are not a party to, as long as the parties *intended* the 3<sup>rd</sup> party to benefit. Cannot be an incidental beneficiary.
- B. R2d \_ 302- A beneficiary of a promise is intended if recognition of a right to performance in the beneficiary is appropriate to effectuate the intention of the parties and either:
  1. The performance of the promise will satisfy an obligation of the promisee to pay money to the beneficiary or
  2. The circumstances indicate that the promisee intends to give the beneficiary the benefit of the promised performance.
- C. Whose intent is important- Cts are split and restatement is unclear:
  1. Some cts say that both the promisor and promisee must intend to give the 3<sup>rd</sup> party rights under the K.
  2. Others say the intention of the promisee controls.
  3. Best approach- some cts focus on the promisee's intent, but it cannot be a "hidden" intent. Must be an intent that the promisor knows or has reason

to know about.

- D. Negligent will drafting- most cts allow 3<sup>rd</sup> party intended beneficiaries to sue for errors in drafting wills, unless the party signed as a witness.
- E. Vesting v. Variation of a duty to a beneficiary- issue is whether the parties who made the K have the right to change the terms of the K, or if they cannot because the rights have vested in the 3<sup>rd</sup> party beneficiary.
1. **R2d \_ 311**
    - a. Cannot discharge or modify a duty to an intended beneficiary if there is a term in the promise that does not allow it.
    - b. If no such term, discharge or modification is allowed *unless*
      - (1) The beneficiary has materially changed his position in justifiable reliance on the promise or
      - (2) Has brought suit on it or
      - (3) Has manifested his assent to it at the request of the promisor or promisee.
- F. Government Ks R2d \_ 313-
1. A promisor who contracts with a governmental agency to render a service for the public is not liable to the public for the consequential damages resulting from performance or failure to perform *unless*
    - a. the terms of the promise provide for such liability
    - b. the promisee is subject to liability to the member of the public for damages and an action against the promisor is consistent with the K and with the policy of the law authorizing the K and prescribing remedies for its breach.
  2. Policy concerns- In these types of Ks, the potential class of 3<sup>rd</sup> party beneficiaries is huge.
    - a. If there is a gov. K with an individual, \_313 should be deemed irrelevant.
- G. Express disclaimer of 3<sup>rd</sup> party beneficiaries- parties can expressly agree in K that there will be no third party standing to sue, even if 3<sup>rd</sup> parties were intended beneficiaries.
- H. Lawrence v. Fox- B owes money to A, B subsequently loans money to C. B says don't pay me when money is due, pay A. C does not pay A. A can sue C directly.
- I. Vogan v. Hayes Appraisal- P received a loan from bank to build a house. D had a K with bank to observe progress of house so bank knew how much money to release to builder. D said house was 90% complete. Builder defaulted, house was not 90% complete. Ct says P can sue D directly, because D had reason to know that the bank intended P to be a third party beneficiary of Ds services.
- J. Zigas v. Superior Court- landlord has K with HUD (gov. agency), promises to keep rents low in exchange for gov. subsidies and benefits. Landlord breaches K, and tenants sue landlord directly. Ct finds for tenants, saying \_313 was intended only to preclude lawsuits for consequential damages arising out of breaches of gov. Ks, not the breach itself. Some courts reject this reasoning and hold that tenants are only incidental beneficiaries of HUD Ks.

## VII. Assignment and Delegation of Rights and Duties

A. Assignment of a right

1. Assignment = present transfer of an existing right
  - a. Not a promise to transfer at a later date.
  - b. Has to be a right under an existing K or obligation.
  - c. Does not require any manifestation of assent by the obligor.
  - d. Once the obligor receives notice, the assignment vests.
2. Law favors assignment of rights as well as assignment of entire Ks.
  - a. It is almost impossible to prohibit assignment of rights to receive money.
3. Limits on the ability to assign; **R2d \_ 317**
  - a. Adverse affect on other party
  - b. Goes against public policy/statute
  - c. K itself (????)
    - (1) may preclude assignment, but courts don't always uphold such clauses.
      - (a) Often construed to be a promise not to assign
      - (b) but this does not render the assignment ineffective
      - (c) the party can sue for breach of this promise later.
      - (d) Sometimes, a party can use strong enough words to actually prohibit assignment of rights (i.e. assignment shall be void or invalid, assignee shall acquire no rights, non-assigning party shall not recognize such assignment.
    - (2) **R2d \_ 322-** a term prohibiting assignment of rights, unless a different intention is manifested
      - (a) does not forbid assignment of a right to damages for a breach of the whole K or a right.
      - (b) gives the obligor a right to damages for breach of the terms forbidden assignment but does not render it ineffective.
      - (c) does not prevent the assignee from acquiring rights against the assignor or the obligor from discharging his duty as if there were no such prohibition.
4. Partial assignment of a right
  - a. most courts enforce partial assignments in the same manner as a full transfer.
  - b. Some courts say partial assignments must be made with obligor's consent to be valid
  - c. the splitting of rights into many partial assignments could be found to impose a material adverse burden on the obligor and therefore be ruled ineffective.
5. Assignment of lawsuits
  - a. Can assign the proceeds from a pending claim
  - b. But cannot assign the cause of action itself, because it promotes

champerty (stirring up lawsuits by financing litigation).

B. Delegation of a duty

1. **R2d \_ 318(1) and (2)**- An obligor can delegate the performance of his duty unless:
  - a. It is contrary to public policy or
  - b. It is contrary to the terms of his promise or
  - c. The obligee has a substantial interest in having that person perform or control the acts promised
2. **R2d \_ 318(3)**- Does not release the obligor from the K.
  - a. The obligor becomes a guarantor
  - b. Obligee can go after either the guarantor or the delegate for breach of K.
  - c. But, the obligee can assent to the obligor being released from the K. Called a novation.
    - (1) **R2d \_ 280**- a novation is a substituted K that includes as a party one who was neither the obligor nor the obligee of the original duty.
3. **UCC \_ 2-210**- a party may perform his duty through a delegate
  - a. unless otherwise agreed to or
  - b. unless the other party has a substantial interest in having his original promisor perform or control the acts required by the K.

C. Cases

1. *Herzog v. Irace*- Jones got a settlement from a car accident, and assigned part of the settlement to P (a doctor) who rendered services for unrelated injuries. Jones gave notice of this to D (his lawyers). Jones later told D not to pay P. P sued D. Ct finds assignment valid: it was a present transfer of an existing right (right of potential recovery from lawsuit), and Jones gave notice to D do the assignment vested.
2. *Sally Beauty v. Nexxus*- Best has K with D to be exclusive distributor of Ds products. Best merges with P, and delegates its duties under the K with D to P. D argues it is a personal services K, not a good argument. But court, relying on UCC \_ 2-210, says this delegation is against the obligee's (Ds) best interests because D and P are direct competitors. Ct says there is an adverse impact on the obligee in having a direct competitor distribute products. Strong dissent says P has every incentive to distribute both its products and Ds products equally, and it already distributes products of direct competitors.

VIII. Consequences of Non-performance

A. Order of performance R2d \_ 234

1. When one of the party's performance will take a longer period of time than the other's, the longer performance must be rendered first.
2. If they both would take an equal amount of time, they must be rendered simultaneously.

B. Material Breach v. Immaterial breach

1. A breach is material if the breaching party did not substantially perform.
  - a. Substantial performance means the non-breaching party received

- essentially what it bargained for.
- b. If there is a material b
2. If one party did substantially perform, the other party must perform as well.
    - a. Minor deviations from terms of K constitute immaterial breaches.
    - b. Non-breaching party can still recover damages based on this, but it is not discharged from its obligations under K.
      - (1) If the party decided not to perform based on the other party's immaterial breach, than the first party is the one that commits a material breach.
  3. Factors in determining whether a failure is material: **R2d \_ 241**
    - a. The extent to which the injured party will be deprived of the benefit which he reasonably expected
    - b. The extent to which the injured party can be adequately compensated for the part of that benefit of which he will be deprived
    - c. The extent to which the party failing to perform will suffer forfeiture
    - d. The likelihood that the party failing to perform will cure his failure, taking into account all the circumstances including reasonable assurances
    - e. The extent to which the behavior of the party failing to perform comports with standards of good faith and fair dealing.
    - f. (The breaching party's willfulness in breaching may also be considered by courts, as opposed to a party's negligent mistake)
  4. Total breach
    - a. If there is a material breach, question becomes whether it is total, which would allow the non-breaching party to be discharged from its obligations under the K.
      - (1) In most courts, material and total breaches are the same.
        - (a) The non-breaching party has the *option* of treating the breach as total and walking away from K.
          - i) This means he does not have to perform his duties under K
          - ii) And can enter into other Ks.
          - iii) Can still seek damages for total breach- even if injured party has not performed obligations.
        - (b) Or the party can treat it as partial and seek enforcement/damages
          - i) For a total breach, the injured party is entitled to recover actual damages as well as any future damages that will reasonably flow from breach

- ii) If it was a partial breach, injured party would only be able to recover damages for the actual harm that has resulted to date, not for future harm.
  - (2) Different view- **R2d \_ 242**: A material breach may or may not be a total breach depending on whether there can be a cure or correction by the breaching party without harming the non-breaching party. Factors considered:
    - (a) The extent to which further delay appears likely to prevent or hinder the making of substitute arrangements by the non-breaching party
    - (b) The degree of importance that the terms of the agreement attach to performance without delay.
  - b. An immaterial breach is never a total breach. It is a partial breach which does not discharge the non-breaching party from the K.
- 5. Recovery
  - a. For immaterial breaches, the non-breaching party usually recovers the **cost of completion**.
    - (1) Sometimes the courts will say that in this case, it would be wasteful to give amount for cost of completion
    - (2) In such a case, **diminution (difference) in value** will be used.
  - b. If the breach is material, the breaching party cannot recover based on the K price (i.e. if he performed 40% of K, does not get 40% of money promised him).
    - (1) He may be able to recover based on restitution- the value of the benefit conferred *minus* the harm caused by the breach.
- 6. *Jacob & Youngs v. Kent*- owner to pay P to build country home. K specified that builder use Reading brand wrought iron pipe. Owner found out after he moved in that not all the pipe used was Reading (but all were wrought-iron). Owner refused to pay outstanding balance. Architect said house not complete, and K had express condition that architect must certify before builder would be paid. Builder said it would cost too much \$\$ to be replaced and sued for remaining balance. Ct said builder had substantially performed, and that it was an immaterial breach that was the result of a negligent mistake. Ct said awarding the cost of completion (tearing up the walls and replacing pipes) would be wasteful and instead awarded diminution of value (which would be close to zero in this case).
- 7. *Sackett v. Spindler*- K for the sale of stock in three installment payments, the biggest chunk of money due on the third payment date. Buyer makes first payment on time and in full. Second payment was one week late and \$200 short (risky for seller at this point not to perform, probably is an immaterial breach of buyer). The check for the 3<sup>rd</sup> payment bounced. Although he received assurances from buyer, seller never received third payment and it was uncertain if he ever would. So now the breach is material and seller can walk away from K (sell to someone else).

### C. Anticipatory Repudiation

1. Definition **R2d \_ 250**- Before performance, a party indicates (by statement

or a voluntary affirmative act) that it is not going to perform.

2. Must be a clear, definite, unequivocal indication.
    - a. Financial difficulty- if one party hears that the other is having financial difficulty, that in itself is not enough to constitute an anticipatory repudiation.
      - (1) The party can ask for *adequate assurances* that the other will perform. This strengthens his position (only after he asked for assurances and party did not perform did he abandon K)
      - (2) **R2d \_ 251**- demand for adequate assurances
        - (a) Where reasonable grounds arise to believe that the obligor will not perform, the obligee may demand adequate assurance of due performance and may suspend any performance which he owes until he receives such assurance.
        - (b) the obligee may treat as a repudiation the obligor's failure to provide within a reasonable time such assurance.
    - b. Additional conditions- a clear statement that a party is only going to perform subject to an additional condition the parties didn't agree to can be treated as a repudiation.
  3. Effect of repudiation **R2d \_ 251**
    - a. The repudiation alone gives rise to a claim for damages for total breach.
    - b. Discharges the other party's remaining duties to render performance.
  4. Retraction **R2d \_ 256**- the repudiating party can retract, provided that the other party:
    - a. Has not sued
    - b. Hasn't materially relied on the repudiation
    - c. Hasn't announced that it is treating the repudiation as final.
  5. *Truman v. Schupf*- Express condition in K, \$\$ for land so long as city approves zoning. Public opposition to zoning, so buyers propose lower alternative price. Seller says no. Buyer then offers original price. Seller says buyer repudiated original K and it is void. Ct says buyers offer to change price was equivocal statement, not enough to equal an intention not to perform. Ct says even if it was a repudiation, the buyers retracted it because it was timely and sellers did not materially change their position or manifest an intention not to be bound.
- D. Ks subject to Express Conditions
1. Parties can expressly agree that the duty of one party (or both of them) depends on the happening of one or more specified events.
  2. Parties must strictly comply with express conditions. Substantial performance rule does not apply.
  3. Possible excuses:
    - a. Forfeiture **R2d \_ 229**- if it would lead to unfair disproportionate

- forfeiture, the court can excuse the fact that an express condition was not met.
- b. Waiver- parties can waive the condition
  - c. Estoppel- party reasonably relied on explicit and implicit expressions by other party (e.g. that oral rather than written notice would suffice).
4. **R2d \_ 225** Effects of non-occurrence of conditions:
    - a. Performance of a duty subject to an express condition cannot become due unless the condition occurs or its non-occurrence is excused.
    - b. Unless it has been excused, the non-occurrence of a condition discharges the duty when the condition can no longer occur.
    - c. Non-occurrence of a condition is not a breach by a party *unless* he is under a duty that the condition occur.
  5. Interpretive Preference- If language could be construed as a promise or an express condition, court prefers for it to be interpreted as a promise: a “promissory condition”
    - a. If it is so construed, the non-occurrence of it discharges the other party *and* allows that party to recover damages due to breach of the first party’s duty to make the condition occur.
  6. Lease agreements/options to renew
    - a. Failure to renew can be excused if the tenant will suffer unfair forfeiture.
    - b. Exceptions:
      - (1) If the owner has a risk of loss because of the tenant’s failure to renew.
      - (2) Gross negligence on the part of the tenant (in some jurisdictions).
      - (3) Intentional delay by tenant.
  7. Satisfaction as an express condition
    - a. Issue: what standard should be used?
      - (1) **Subjective standard**- For art (e.g. self portrait) the standard is the good faith of the person judging.
      - (2) **Objective standard**- For contracts not expressly for aesthetic purposes (e.g. construction Ks) an objective standard is used.
        - (a) thus, the Q is not whether the owner was satisfied, but whether the owner, as a reasonable person, should have been satisfied.
      - (3) **Satisfaction of an independent third person**- if a third person not a party to the K is judging, than the standard is usually just good faith.
  8. *Oppenheimer v. Oppenheim*- K for sublease subject to an express condition: D must receive written consent, by a certain date, from landlord to make changes to property. P contacted D by telephone

on that date and said that landlord gave oral consent. D contacted P the next day calling K off due to the fact that written consent was not given. Because it was an express condition, it must be strictly adhered to. D is discharged because P did not strictly adhere to condition, even though P did substantially perform.

9. *J.N.A. Realty Corp v. Cross Bay Chelsea*- D had in its lease K that it must give notice to renew the lease 6 months before it expires (express condition). They had bargained for a longer renewal when they purchased the lease from the previous tenants. P (lessor) gave them regular notice about taxes and other requirements, but not of the need to renew. D failed to renew and P tried to kick them out. Ct said because the tenant made valuable improvements on property and would suffer forfeiture if kicked out, tenant is entitled to equitable relief unless it would prejudice the landlord.
10. *Morin Building Products Co. v. Baystone*- P was subcontracted by D to install aluminum siding for a factory building. Payment was expressly conditioned on the satisfaction of GM, the owner of the building. GM not satisfied. P sues for payment. Because this was a commercial K for the construction of a building, and objective standard of satisfaction is used. The ct concluded that a reasonable person would have been satisfied by Ps work, thus it is entitled to payment.

E. The “efficient breach”

1. Discussed by scholars, not courts.
2. Holmes said no one is punished for breaching Ks, no punitive damages
3. Posner said because of no punishment, we are effectively encouraging breaches by persons who enter into more profitable bargains, thereby performing an “efficient breach.”

IX. Remedies

A. Equitable relief

1. **R2d \_ 359-** specific performance only granted when damages will not give a party adequate relief.
2. **R2d \_ 360- Factors used to determine adequacy of \$\$ damages**
  - a. The difficulty of proving damages with reasonable certainty
  - b. The difficulty of procuring a suitable substitute performance by means of money damages
  - c. The likelihood that an award of damages could not be collected.
3. **R2d \_ 361- Effect of provision for liquidated damages**
  - a. Specific performance may be granted despite the provision.
4. **R2d \_ 362- Effect of uncertainty of terms**
  - a. Specific performance will not be granted unless the terms of the K are sufficiently certain to provide a basis for an appropriate order.
5. **Clean Hands-** He who seeks equitable relief must have “clean hands”- courts will not grant such relief if it would result in unfairness, even to the party in breach.
6. **R2d \_ 364- Effect of unfairness**
  - a. Specific performance will be refused if such relief would be unfair because:
    - (1) the K was induced by mistake or by unfair practices
    - (2) the relief would cause unreasonable hardship or loss to the party in breach or to third persons

- (3) the exchange is grossly inadequate or the terms of the K are otherwise unfair.
  - b. Specific performance will be granted if denial of such relief would be unfair because it would cause unreasonable hardship or loss to the party seeking relief or to third persons.
7. **R2d \_ 365- Effect of public policy**
- a. Specific performance will not be granted if it would be contrary to public policy.
8. **R2d \_ 366- Effect of difficulty in enforcement or supervision**
- a. No specific performance if the character and magnitude of the performance would impose on the court burdens in enforcement or supervision that are disproportionate to the advantages to be gained from enforcement and to the harm to be suffered from its denial.
9. **R2d \_ 367- Ks for personal service or supervision**
- a. No specific performance for Ks to render personal services (would kind of be like involuntary servitude/slavery).
    - (1) However, a promise to render a personal service exclusively for one employer may be enforced by an injunction against serving another
    - (2) unless the result would be to leave the employee without other reasonable means of making a living.
  - b. *ABC v. Wolf*- D promised to engage in good faith negotiations for new employment K 90 days before K was up. D breached by entering into K with someone else before 90 days were up. Court would never order specific performance of new employment K, but will issue injunctions against breaches of covenants not to compete (although such covenants are disfavored). Dissent said there was a 90 day covenant not to compete that should be enforced (an Prince agrees). But majority said injunctions are usually given where party is still under K with covenant not to compete. Once K is over, must show express covenant or that there will be irreparable harm to employer if not enforced.
10. **Land Ks-** specific performance usually given.
- a. Reasoning- land is considered to be so unique that \$\$ damages would be inadequate.
  - b. But equitable relief is always discretionary.
11. *City Stores v. Ammerman*- P gave a letter of support in order to approve zoning for D, in exchange for an option to get store in Ds mall (yet to be built). Express conditions that (1) D get zoning approved (2) D enter in with leases with other stores to provide terms of lease for Ps store. D satisfies above conditions, but does not want to give P store. Issue: would damages be sufficient here? It is important for P to get store in that location b/c of suburban boom. Also, how would you measure \$\$ damages/lost profits? Would not be unfair to order specific performance, D would not go out of business. No unfairness to any third parties (D did not enter into other Ks). Ct weighed the difficulty of enforcement with the harm done to P if not enforced and found for P.

B. Expectation Damages- protects the benefit of the bargain

1. General measure **R2d \_ 347**: loss in value + other loss - cost avoided - loss avoided.
2. Direct or immediate damages
  - a. Measure of damages if there has been substantial performance:
    - (1) Cost of completion- usually applied
    - (2) Demunition in value- often applied if cost of completion would be wasteful (Jacob & Young).
    - (3) **R2d \_ 348**- states this a little differently:
      - (a) If a breach results in defective or unfinished construction and the loss in value to the injured party cannot be proved with sufficient certainty, he may recover damages based on:
        - i) the dimunition in the market price of the property caused by breach or
        - ii) the reasonable cost of completing performance or of remedying defects if that cost is not clearly disproportionate to the probable loss in value to him.
  - b. Measure of direct damages in real estate Ks:
    - (1) If the buyer breeches, the measure is the difference between K price and the fair market value of the house.
    - (2) If the seller breeches:
      - (a) English rule (majority)- only liable for restitution and reliance damages, not expectation damages *unless* the seller breached in bad faith.
      - (b) American rule (minority)- expectation damages awarded for any unexcused failure to convey, regardless of the good or bad faith of the seller.
      - (c) If seller sells to a different buyer, the 1<sup>st</sup> buyer will be able to recover the additional value seller made on 2<sup>nd</sup> transaction.
3. Indirect or consequential damages
  - a. Requirements:
    - (1) **R2d \_ 351**- Must be *reasonably foreseeable* at time K was made.
      - (a) Must be a probable result- not necessary and not possible, something in between.
    - (2) **R2d \_ 352**- Must show with *reasonable certainty* the amount of damages suffered as a result of the breach
      - (a) But courts will bend over backwards to find a measure of damages for the non-breaching party, even if uncertain.
    - (3) **R2d \_ 350**- Non-breaching party has a *duty to mitigate*

damages

- (a) damages are not recoverable for that the injured party could have avoided without undue risk, burden, or humiliation
  - (b) the injured party is not precluded from recovery if it has made reasonable but unsuccessful efforts to avoid loss.
  - (c) Minority view- if both the breaching and non-breaching party have the opportunity to mitigate the damages, than the non-breaching party does not have to.
- (4) *Causation*- the breach must actually have caused the harm the party is seeking \$\$ for.
- b. Damages that cannot be recovered (usually):
- (1) Emotional distress damages *unless* (**R2d \_ 353**)
    - (a) bodily harm results
    - (b) it is a special K where emotional distress is particularly likely to result. Examples:
      - i) Ks to care for the deceased
      - ii) Ks of common carriers
      - iii) Ks for the delivery of messages concerning death.
  - (2) Punitive damages *unless* (**R2d \_ 355**)
    - (a) The breach of the K is also a tort- may be able to get it under tort law.
    - (b) It is a wrongful or bad faith denial of a claim or failure to defend under an insurance K- this also amounts to a tort.
  - (3) Attorney's fees *unless*
    - (a) There is a provision in the K allowing for it if one party breaches.
      - i) Cts are likely to enforce this
      - ii) Cts will read one party's attorney's fees rights as reciprocal.
    - (b) There is a statutory provision (e.g. consumer protection, antitrust etc.)
    - (c) It is allowed under court made rules such as FRCP.
    - (d) They are fees for collateral litigation (of collateral Ks) that the party incurred as a result of the breach.
- c. Lost profits **R2d \_ 351**- can recover lost profits if they are reasonably foreseeable as a result of the breach at the time the K was made.
- (1) but if this would result in disproportionate compensation,

- R2d says cts may not allow or may limit recovery.
- d. Parties can specify in the K that they won't be responsible for consequential damages if K is breached.
    - (1) But if there is a statute against it (e.g. consumer protection) or if the K would be unconscionable as a result, cts won't enforce it.
  4. Credits against damages
    - a. But for the breach, non-breaching party would not have made or saved this money (cost avoided and loss avoided).
    - b. When there is doubt, the non-breaching party is favored.
  5. Measure of damages in sale of goods: **UCC \_ 2-708**
    - a. If the buyer breaches, the measure is the difference between the K price and the market price at the time and place of tender
    - b. plus any incidental or consequential damages
    - c. but less expenses saved in consequence of the buyer's breach.
  6. Measure of damages in employment Ks
    - a. Breach of K by employee: measure is the cost of obtaining other services equivalent to that promised but not performed, plus any foreseeable consequential damages.
    - b. Breach of K by employer/wrongful termination:
      - (1) Front pay- how much money a person would have made up until the time of retirement
      - (2) Back pay- amount of salary from time of wrongful termination to judgement.
      - (3) Duty to mitigate-
        - (a) injured party only has to take work that is comparable or substantially similar
        - (b) Employer has burden of proof that former employee failed to mitigate.
        - (c) Some cts say not only does the employer have to prove that former employee failed to look for a job, but have to prove that it is reasonably likely she would have found a new comparable job if she had looked.
        - (d) If a person takes a non-comparable job courts look to see if she could have done both this job and former job at same time.
          - i) if so, does not mitigate damages
          - ii) if not, the back of the first job is a but/for cause of 2<sup>nd</sup> employment K, thus the damages will be mitigated by the salary received under the 2<sup>nd</sup> K.
  7. Cases
    - a. *Turner v. Benson*- buyer breached K to buy house. Here, fair market value equaled K price, so seller could not recover

direct damages. Seller could recover consequential damages: (1) loss of profit from home daycare- court says no foreseeability and no causation, seller would have sold the daycare even if no breach, loss must be the result of breach. (2) Interest paid on funds borrowed to buy new house- direct result of breach, wouldn't have had to borrow if buyer did not breach. (3) utilities, plumbing damages, insurance on home, advertising expenses to sell home all recoverable. D asked for credits: (1) credit for rental income P realized- ct said this is proper, but can be offset by any expenses P incurred from renting property.

- b. *Handicapped Children's Educ. Bd. v. Lukaszewski*- 1-year employment K, breached by employee. P had to replace employee, only one qualified applicant who had more experience, D had to pay her a higher salary. P gets the difference of costs between paying more to replacement and salary of D.
- c. *American Standard v. Schectman*- Builder pays \$275,000 and a promise to regrade land to a certain level for right to salvage equipment from owner. Builder regrades land but not to the correct depth as specified by K. Land was sold by owner for \$180,000. If it had been regraded correctly, it would be worth \$183,000. Difference of \$3,000. Cost of regrading equals \$90,000. Ct uses cost of completion measurement and awards 90,000. Prince thinks diminution of value should have been used because it is such an ext. Compare with Jacob & Youngs.
- d. *Hadley v. Baxendale*- May 11- shaft breaks in mill. May 13- asks carriers how long it would take to get replacement, said 1 day. May 14- delivered shaft to carrier. May 20- shaft arrives (5 day delay). P seeks K price and lost profits from mill not running for 4 days. Ct says can't recover lost profits, because not reasonably foreseeable; carriers weren't on notice that mill wasn't running, mill could have had a replacement shaft. But opinion states that miller told carrier that mill was stopped. If this was true, than the case was decided incorrectly.
- e. *Rockingham County v. Luten Bridge Co*- County repudiates K for building of bridge. This is a total and material breach, and the builder should treat K as being discharged and sue for recovery. But builder begins to build bridge anyway- the money spent on building the bridge was avoidable and not a direct consequence of breach. So breaching party not responsible for it and builder has to eat loss. Builder can still recover profit would have realized based on K price (but he ends up losing out- because this is just the profit he would have realized, he eats cost of building bridge).
- f. *Boehm v. American Broadcasting*- wrongful termination. D argues that P did not mitigate his damages because he failed to accept Ds offer of employment. But Ct found that this offer of a new position was not comparable to former position- Different compensation, rank, would have had to report to person who replaced him (undue humiliation).
- g. *Erlich v. Menezes*- D negligently builds house, leaks everywhere, falling apart. P claims emotional distress. Ct says no bodily injury and not a K where emotional distress is particularly likely to result. Policy concerns about allowing recovery in Ks for construction of homes: (1) financial risks not predictable for builders (2) cost of housing market would rise (3) would make commercial Ks affairs unstable and unpredictable.
- h. *Roth v. Speck*- Employee breach 1-yr employment K. Employer could not find a replacement comparable to D. Ct used cost of replacement to measure damages, but this was uncertain since D could not find a replacement. Ct determined that Ds new salary was indicative of how much it would cost to

replace him.

C. Reliance damages

1. **Definition-** an alternative to expectation damages. Non-breaching party recovers out-of-pocket expenses incurred in reliance on the performance of the K.
  - a. Usually out-of-pocket expenses only
  - b. But in very rare circumstance courts take into account the gains P would have made had she no relied on the promises of D.
  - c. *Dialist Co. v. Pulford-* After breach of an exclusive territory provision, P permitted to recover not only initial franchise fee but also the amount of lost salary after quitting his original job until reemployed.
2. **R2d \_ 349**
  - a. The injured party has the right to damages based on reliance interest, including expenditures made in preparation for performance or in performance
  - b. Less any loss that the party in breach can prove with reasonable certainty the injured party would have suffered had the contract been performed.
3. Subject to same limitations as consequential damages: foreseeability, certainty, duty to mitigate, causation.
4. *Wartzman v. Hightower Productions-* flag pole sitting case. Attorneys breached K to create corporation that would enable P to sell stock and fund project. Uncertain as to how much P would have made if Woody succeeded in breaking flag pole sitting record- therefore would not be able to recover expectation damages. Ps sue for reliance damages. P could not afford to mitigate damages by hiring another attorney to fix problem, asked D to pay attorneys fees, and D refused (MA takes minority position that says if D had opportunity to mitigate, P does not have to).
5. **Essential v. incidental reliance damages R2d \_ 333**
  - a. Essential = expenses incurred as part of expense in performing the K
  - b. Incidental = expenses incurred in collateral Ks in reliance that the original K would be performed.
6. **Pre-contract reliance-** courts are split as to whether a party can be awarded reliance costs before the K was made.
7. **When the theory of obligation is not breach of K, but PE**
  - a. Courts have the discretion to award expectation damages, or reliance damages, or something in between.
  - b. *Walser v. Toyota-* D contacted P about prospective Lexus dealership. Parties began negotiating. No mutual assent, but P argues that he relied on promise made by D that they would get letter of intent for dealership. After this promise, P bought land for dealership. D rescinded promise and never sent letter of intent. Jury awarded \$232,131 for land bought in reliance on promise. P argued should have been awarded 7,600,000 for lost profits. Court limited reliance damages here because:
    - (1) Not certain that P would get dealership, may not have been able to satisfy conditions of letter of intent.

(2) Short opportunity to rely, promise was rescinded quickly.

D. Restitution- an alternative to expectation damages.

1. **R2d \_ 371- Measuring restitution**

- a. Reasonable value- to the other party of what he received in terms of what it would have cost him to obtain it elsewhere *or*
- b. Enrichment- the extent to which the other party's property has been increased in value.
- c. Courts favor non-breaching party in deciding which measurement to use.

2. **\_ 373- Restitution when other party is in breach**

- a. (1) In the event of a total breach or repudiation, the injured party is entitled to restitution for any benefit that he has conferred on the other party by way of performance or reliance.
- b. (2) The injured party has no right to restitution if he has performed all of his duties under the K and no performance by the other party remains due other than payment of \$\$ for that performance.

3. **\_ 374- Restitution in favor of party in breach**

- a. (1) The party in breach is entitled to restitution for any benefit that he has conferred by way of part performance or reliance in excess of the loss that he has caused by his own breach.
- b. Limitations:
  - (1) Restitution cannot exceed ratable portion of K price
  - (2) If there is a valid liquidated damage clause, than no restitution.
  - (3) Specific performance- given readily in land sale transactions.
  - (4) R2d comment- restitution might be denied in exceptional cases involving a scheming, bad faith, intentional breach.
  - (5) In MA and NY, no restitution allowed for breaching party.

4. **\_ 375- Restitution and SOF**

- a. A party is not barred from restitution for the reason that the K is unenforceable by him because of the SOF
- b. unless the statute provides otherwise or its purpose would be frustrated by allowing restitution.

5. **\_ 376- Restitution when K is voidable**

- a. A party who has avoided a K on the ground of lack of capacity, mistake, misrepresentation, duress, undue influence or abuse of fiduciary relation is entitled to restitution.

6. **\_ 377- Restitution in cases of impracticability etc.**

- a. A party whose duty of performance does not arise or is discharged as a result of impracticability of performance, frustration of purpose, non-occurrence of a condition or disclaimer by a beneficiary is entitled to restitution.

7. **Restitution can be recovered even if full performance would have**

**resulted in loss.**

- a. Recovery for restitution is allowed “off the K” as if the K had never been formed.
- b. *Coastal Steel Erectors v. Algernon Blair*- P performs part of work, but D fails to pay for crane rentals per agreement. P stops work and sues for restitution. If P had continued would have lost \$\$\$. P put in \$60,000, and had been paid \$23,000, so is owed \$37,000. But if it had fully performed, would have lost rather than gained money. So P wins by failing to perform, because it breaks even.
- c. But a party cannot recover for restitution if it has fully performed, then must go off the K price.

8. **When restitution rather than breach of K is theory for recovery-** restitution is the way to measure damages, follow R2d \_ 371.

E. Liquidated Damages

1. **Definition-** A fixed or determinable sum of \$\$ has been specified in advance as the remedy for a particular type of breach.
2. **Determining validity-** not always enforced by courts.
  - a. Cannot be aimed at penalizing, must be aimed at compensation.
  - b. Must be reasonable forecast of just compensation
    - (1) Courts are split on whether to analyze its reasonableness at time K was made or
    - (2) at time of breach in light of actual harm suffered (**R2d \_ 356** takes this view).
    - (3) The greater the difficulty of estimating or proving damages, the more likely the stipulated damages will appear reasonable.
3. **R2d \_ 356**
  - a. Damages for breach by either party may be liquidated in the agreement but only at an amount that is reasonable in light of the anticipated or actual loss caused by the breach and the difficulties of proof of loss.
  - b. A term fixing unreasonably large liquidated damages is unenforceable on grounds of public policy as a penalty.

F. Prejudgment Interest = interest on money owed from the time of breach to the time of judgement.

1. If the amount the breaching party owes is uncertain, court will not allow prejudgment interest.
2. Otherwise, it is generally awarded.