

PEARCE MICRO REVIEW
Contracts

I. Formation of Contracts

A. Mutual Assent

1. Offer – Creates the Power of Acceptance in the Offeree
 - a. intent of the offeror to be bound
 1. content of the offer
 2. parties
 3. subject matter
 4. quantity
 5. price
 - b. communication of offer to offeree
 - c. termination of offer
 1. by offeror – revocation – effective upon receipt by offeree
 2. by offeree – rejection – effective upon receipt by offeror or lapse of time
 3. by operation of law – death or insanity of a party, destruction of subject matter, supervening illegality
2. Acceptance
 - a. offeree with power of acceptance
 - b. unequivocal terms of acceptance
 1. common law – mirror image rule
 2. U.C.C. – acceptance that does not mirror the offer is not necessarily a rejection and counter offer
 - a. non-merchants – terms of offer govern

- b. merchants – acceptance terms usually included
 - c. communication of acceptance – mail box rule says properly addressed and stamped acceptance is effective when sent
- 3. Consideration
 - a. bargain and exchange
 - b. adequacy of consideration
 - 1. mutuality of obligation
 - 2. implied promises
 - 3. disproportionate exchanges
 - c. substitutes for consideration
 - 1. moral obligation – invalid absent new promise or where past act performed at the promisor's request
 - 2. detrimental reliance – estoppel
 - a. promisor should reasonably expect reliance
 - b. of a definite and substantial nature
 - c. reliance is induced in fact
 - 3. statutory substitutes
 - d. modification of contracts – preexisting duties
 - 1. common law – requires consideration, but no writing
 - 2. U.C.C. – requires a writing, but no consideration
 - e. compromise and settlement of claims – valid consideration

- B. Defenses to Formation
 - 1. Incapacity
 - a. infancy
 - b. insanity
 - c. duress and coercion
 - 2. Illegality
 - 3. Unconscionability – judged at the time of formation
 - 4. Fraud
 - 5. Statute of Frauds
 - 6. Mistake
 - a. mutual mistake – prevents contract formation
 - b. unilateral mistake – does not invalidate contract unless other party knew or should have known about the mistake

- II. Terms of the Contract
 - A. Express Terms
 - B. Implied Terms
 - 1. Prior Dealings
 - 2. Custom and Usage
 - C. Parol Evidence Rule
 - 1. prior or contemporaneous communications that vary from the terms of a contract are inadmissible if the contract is a complete and final expression of the agreement
 - 2. there are many exceptions, none of which are counter-intuitive

- D. Interpretation of Contracts
 - 1. Is there a Present Duty to Perform?
 - a. promise vs. condition
 - b. classification and excuse of conditions
 - 2. Has the duty to perform been discharged?

- III. Rights of Non Contracting Parties
 - A. Third Party Beneficiaries
 - 1. Intended and Incidental Beneficiaries
 - 2. Creditor and Donee Beneficiaries
 - 3. Impairment or Extinguishment of Third Party Rights by Contract Modification or Mutual Rescission
 - 4. Enforcement by the Promisee
 - B. Assignment of Rights (may create third party beneficiaries)
 - C. Delegation of Duties (always creates third party beneficiaries)

- IV. Conditions
 - A. Express
 - B. Constructive
 - 1. Conditions of Exchange: excuse or suspension by material breach
 - 2. Immaterial Breach and Substantial Performance
 - 3. Independent Covenants
 - 4. Constructive Conditions
 - a. non-prevention

- b. non-hindrance
 - c. affirmative cooperation
 - C. Obligations of Good Faith and Fair Dealing in Performance and Enforcement of Contracts
 - D. Suspension or Excuse of Conditions by Waiver, Election or Estoppel
 - E. Prospective Inability to Perform and the Effect on the Other Party
- V. Breach
 - A. Minor Breach
 - 1. Substantial Performance of the Contract by the Breaching Party
 - 2. Remedy: Contract Price Minus Damages
 - B. Material Breach
 - 1. Some Performance, but Less than Substantial Performance
 - 2. Remedy: Damages or the Right to Cure, but No Right to Terminate the Agreement
 - C. Total Breach
 - 1. The Non Breaching Party May Terminate
 - 2. Caveats: Divisibility and Rescission
 - D. Anticipatory Repudiation – The Non Breaching Party May Elect substantive rights and remedies.
- VI. Defenses to Breach
 - A. Impossibility
 - B. Impracticability
 - C. Frustration of Purpose

- D. Modification – Novation
- E. Discharge of Contractual Duties

VII. Remedies

- A. Damages
 - 1. U.C.C. contracts
 - a. where buyer breaches, seller may withhold delivery and / or get damages
 - b. where seller breaches, buyer may reject non conforming goods, cancel, cover, resell, or get damages for non delivery
 - 2. land sales contracts – damages measured by difference between contract price / fair market value
 - 3. construction contracts
 - a. where owner breaches, builder gets profits plus costs, or full price plus interest where construction complete
 - b. where builder breaches, owner gets costs to complete plus reasonable compensation for delay, usually with an offset to prevent unjust enrichment
 - 4. punitive damages are not available for breach of contract
 - 5. nominal damages are awarded where there is a breach but no actual loss is shown by the plaintiff
- B. Consequential Damages – Must Be Foreseeable at the Time of Formation
- C. Duty to Mitigate Damages – Avoidable Consequences
- D. Liquidated Damages Clauses – Must be Reasonable, not a Penalty
- E. Quasi-Contractual Relief
 - 1. Failed Contract with One Party Unjustly Enriched at the Other's Expense

2. No Contract Between the Parties
 - a. one party confers a benefit on the other
 - b. with a reasonable expectation of being compensated
 - c. at the express or implied request of the other person
 - d. unjust enrichment would result without the relief sought

F. Reformation

1. Mistake – Unilateral or Mutual
2. Misrepresentation – Innocent or Fraudulent
3. Defenses to Reformation
 - a. laches
 - b. sale to b.f.p.
 - c. parol evidence rule

G. Rescission

1. Mistake that goes to the Heart of the Agreement
2. Fraud or Misrepresentation
3. Non Breaching Party may Rescind and Sue for Restitution Damages

H. Equity – Specific Performance

1. Inadequate Legal Remedy
 - a. land
 - b. unique goods
 - c. not available for services
2. Definite and Certain Contract

3. Feasibility
4. Mutuality
5. Defenses
 1. laches
 2. unclean hands
 3. sale to a bona fide purchaser

VIII. Sales

- A. Introductory Thoughts – U.C.C. Article 2 vs. the Common Law
 1. Merchant's Firm Offer Irrevocable Without Consideration
 2. Proposal of Additional Terms is not Rejection, and New Terms may become Part of the Contract
 3. Modifications in writing are binding without Consideration
 4. Perfect Tender Rule
 5. Merchants and Non Merchants
- B. Formation
 1. Offer and Acceptance
 - a. merchant's firm offers
 - b. battle of the forms vs. mirror image rule
 - c. open terms
 2. Auctions
- C. Defenses to Formation
 1. Statute of Frauds
 2. Unconscionability

- D. Modification
 - 1. By Agreement
 - 2. By Operation of Law
- E. Parol Evidence Rule – Contract may be Supplemented or Explained by:
 - 1. Consistent Additional Terms
 - 2. Course of Dealing
 - 3. Use and Custom of the Industry
 - 4. Course of Performance
- F. Performance
 - 1. Seller's Obligation of Tender and Delivery
 - a. carrier contracts
 - b. non-carrier contracts
 - 2. Buyer's Obligation to Pay and Right to Inspect
- G. Obtaining an Interest in Goods
 - 1. Buyer Obtains an Interest when Goods can be Identified
 - 2. Buyer has an Insurable Interest in Identified Goods
- H. Allocating the Risk of Loss
 - 1. Risk without Breach
 - 2. Risk with Breach
- I. Warranties
 - 1. Warranty of Title and Against Infringement
 - 2. Implied Warranty of Merchantability
 - 3. Implied Warranty of Fitness for a Particular Purpose

4. Express Warranties

- J. Remedies

1. Buyer's Remedies

- a. acceptance
- b. rejection prior to acceptance
- c. revocation of acceptance
- d. replevy of specific goods
- e. specific performance
- f. damages
 1. for non delivery, rejection, revocation of acceptance
 2. for accepted goods

2. Seller's Remedies

- a. withhold goods
- b. recover goods
- c. force goods on buyer and get full price
- d. damages
 1. resell and recover the difference between the contract price and the resale price
 2. recover the difference between the market price and the contract price
 3. recover the difference between the contract price and the seller's costs, excluding overhead

3. Remedies used by Buyer and Seller

- a. anticipatory repudiation

- b. right to demand assurances
 - c. retraction of repudiation
 - d. right to sue third parties
 - e. liquidated damages
4. Statute of Limitations – four years from the time of breach

Contracts Hypothetical #1

Joe had a wealthy brother, Steve, who owned an aging, unoccupied house situated on a large, tree-covered lot. Joe asked Steve if he would sell the property and, if so, at what price. Steve replied that he would not sell, but would let Joe have possession of the property free of charge if Joe would maintain it. A few days later, Joe wrote Steve and asked permission to go on and take possession of the property for the purpose of making the substantial repairs and renovations necessary to make the house habitable and to take up residence there. Steve wrote back: "Of course you may go on the property we discussed. I promise that if you make the house habitable, it is yours for at least the next ten years."

Over the next several months, Joe spent more than 300 hours of his free evenings and weekends working on the house, expended \$6,000 for materials, and paid out another \$5,000 for plumber and electrician help. Joe often slept overnight at the house on occasions when he worked late.

Just as the house became habitable and ready for Joe to take up permanent residence on the property, Steve told him that Buyer had offered \$200,000 for the house for immediate possession, that Steve had accepted Buyer's offer, and that Steve would compensate Joe for his out-of-pocket expenses (\$11,000) but not for his time and labor. The rental value of the property, as restored by Joe, is \$800 per month, and Joe's time is worth \$15 an hour.

What are Joe's rights and remedies? Discuss.

- I. Joe v. Steve
 - A. Formation: When was the contract formed?
 - B. Statute of Frauds Defense to Formation
 - 1. Steve signed a confirming letter.
 - 2. Joe's part performance satisfies the statute.
 - C. Breach: Steve's agreement with Buyer: Voluntary Disablement
 - D. Remedies
 - 1. Damages: Rental value of \$800 per month for the duration of the contract.
 - 2. Restitution:
 - a. \$11,000 out of pocket expenses
 - b. \$4,500 for Joe's labor
 - c. Increase in value of the repaired house
 - 3. Specific Performance
 - a. Definite and certain contract
 - b. Inadequate legal remedy: land unique
 - c. Feasibility
 - d. Mutuality: present under modern view
 - e. Defense: Sale to Buyer, a BFP.
- II. Joe v. Buyer
 - A. Joe's only theory of recovery is in tort.
 - B. The key issue is whether or not Buyer had notice.

Contracts Hypothetical #2

Neptune is an upscale seafood restaurant that opened in a convenient downtown location six months ago. It has become well known for the quality of its food and service. It has several dishes featuring salmon that are particularly popular with patrons.

Neptune entered into a valid written contract with Seafood Uptown Providers (SUP) under which SUP agreed to supply Neptune with 250 pounds per week of fresh Pacific salmon at \$4.00 per pound for the next year.

Three months after the making of the contract, a large widely publicized oil spill occurred in Pacific coast waters. The spill greatly reduced the catch of salmon. Salmon began selling on the open market for at least \$5.00 per pound. SUP then told Neptune that it would supply salmon only at a price of \$6.00 per pound. Neptune refused to pay more than the contract price. In fact, SUP has found a new customer willing to pay \$6.00 per pound, and it is selling its entire supply (about 450 pounds of salmon per week) to that customer.

Neptune, faced with the prospect of having to obtain salmon for its daily restaurant menu and also for special events that it caters, found a supplier willing to meet about one-half of Neptune's weekly requirement for salmon at \$5.00 per pound. With further effort, Neptune might have filled a portion of the remaining weekly requirement for salmon at \$6.00 per pound, but it was uncertain to what extent salmon would continue to be obtainable and how high the price might go. Neptune decided instead to reduce its menu offerings of salmon and to cancel several catering contracts.

Within a month after reducing its menu offerings of salmon, Neptune experienced a 25% decline in its restaurant business from the previous month. It also had a 75% decline in new bookings for catering jobs.

Neptune still has the immediate and long-term problem of how to obtain a reliable source of salmon, and wants to sue SUP.

What rights and remedies does Neptune have against SUP, what damages, if any, might Neptune recover, and what defenses, if any, should SUP assert? Discuss.

- I. Neptune's Rights: Contract
 - A. The contract was valid.
 - B. The UCC applies to these merchants.
 - C. SUP breached the contract.

- II. Neptune's Remedies
 - A. Expectation Damages
 - B. Consequential Damages
 - 1. 25% decline in restaurant business
 - 2. 75% decline in new bookings for catering jobs
 - C. Neptune's Duty to Mitigate
 - D. Specific Performance

- III. SUP's Defenses
 - A. Defenses to Breach
 - 1. Impossibility
 - 2. Impracticability
 - B. Defenses to Specific Performance

Contracts Hypothetical #3

National Bank is located in a state which has the following statute: "Employment which is not for a specified term is terminable at the will of either party and without notice." National Bank offered Pam a job as Vice President and Manager/Pension Funds, a job in which she would be principally responsible for managing large pension funds for private and public employees. In response to her concerns about job security, National Bank assured her in writing that she would be a "permanent" employee, although no specified term was recited in the writing. Pam accepted the offer at a starting annual salary of \$37,000 and commenced working in March 1989.

In October 1989, National Bank issued and gave all employees, including Pam, an employees' handbook describing its employment policies. The handbook stated, "Reasonable cause will be required for the termination of any employee, and procedures will be applied in a fair and consistent manner." The handbook, which specified that insubordination is reasonable cause for termination, concluded with the statement, "The procedures described herein are applicable to all persons now in our employ or hereafter hired and may be changed at any time, without notice."

In October 1991, Pam noticed in National Bank's pension accounting procedures some practices which constituted potentially serious violations of statutes designed to protect and preserve pension funds. When she reported them to National Bank's president, the president told her, "Cover them up and we'll fix them after the next visit by Federal Bank Examiners. Pam flatly refused. The president immediately fired her for "gross insubordination."

Pam has searched diligently for an equivalent job but has not been able to find one. She has turned down a number of jobs as pension clerk and pension assistant at salaries of about \$15,000 per annum. Pam has sued National Bank for breach of contract, wrongful discharge, and breach of the covenant of good faith and fair dealing.

What are Pam's rights and what types of damages, if any, may she recover? Discuss.

- I. Pam's Breach of Contract Claim
 - A. Pam's Contract with National Bank
 - B. The Employee Handbook
 - C. Breach by National Bank
 - D. Conclusion

- II. Pam's Wrongful Discharge Claim

- III. Did National Bank breach the covenant of good faith and fair dealing?

- IV. Pam's Damages
 - A. Compensatory
 - B. Punitive

- V. Conclusion

Contracts Hypothetical #4

Delta is the owner of an equipment installation company. In May 1992, Pratt, a meat market owner, called Delta and asked whether Delta could install six used coolers which Pratt had recently purchased. The coolers were to be installed in a new meat market that Pratt was opening. Pratt emphasized the need to complete the installation by July 1 in time for the new market's opening on that day for the Fourth of July holiday.

On May 31, Delta met with Pratt and after a brief discussion Pratt signed a form entitled "Authorization Agreement." The document provided that:

"In consideration of \$12,000 to be paid on completion of the work, Delta will install in Pratt's market six used coolers, including pressurizing all cooling lines, and calibrating the equipment for proper temperature within 30 days from the making of the contract."

Delta told Pratt that Delta would send Pratt the executed contract as soon as Delta had verified that Delta had the necessary compatible fittings for the valves on the used coolers. On June 4, having verified that the compatible equipment was on hand, Delta dated, signed and sent the executed contract to Pratt.

Delta's crew began installing the equipment on June 20, and by June 28 had installed five of the six coolers with pressurization and calibration complete. The crew was having trouble with installation of the last cooler and the crew chief decided that a special valve fitting was needed to complete the job. The crew chief ordered the fitting from a supplier, and stopped work on the installation of the last cooler, pending arrival of the fitting. It arrived on July 2 and the chief and his crew went immediately to Pratt's new meat market. Pratt refused to allow the crew to finish installation of the last cooler.

Pratt had arranged the grand opening of his new market for July 1 and 2, in anticipation of the high demand for beef, fish and chicken for Fourth of July weekend barbecues. Pratt claims that the opening was "ruined" because of the messy appearance of the partly assembled cooler, and that he had lost sales because the cooler was unavailable for the fresh fish display he had planned for the opening. Pratt had ordered his butcher to discard the fresh fish, for which he had paid \$1500, because he could find no cold storage for it. He had tried unsuccessfully to contact Delta on July 1.

Pratt claims that Delta has breached their contract. Pratt refuses to pay Delta any sum of money and plans to sue Delta to recover \$2500 which was to be the retail price of the fish that were discarded.

What are Delta's rights and liabilities, if any? Discuss.

I. Formation

- A. Offer, Acceptance, Consideration - No Problems.
- B. Vague Term: The Completion Date.
- C. Parol Evidence Rule
- D. Conclusion

II. Performance

- A. Delta did not complete performance when it was due.
- B. Pratt did not allow Delta to complete performance.

III. Remedies

- A. Delta's Demand: Restitution
- B. Pratt's Demand: Damages
- C. Conclusion

Contracts Hypothetical #5

Technical University (Tech) solicited an offer from Data Equipment Company (Data), headquartered in State A, for the supply, installation and testing of air-quality monitoring equipment for Tech's floating Ocean Research Station in the mid-Pacific Ocean. Identical equipment, uninstalled, was available for \$20,000 from several of Data's competitors, but only Data had the means to install and test the equipment in the mid-Pacific Ocean.

At a meeting on April 3, 1990, Data's president, Dan, offered to do the job for \$28,000 by July 30, 1991, and Tech accepted. On April 4, 1990, Tech sent Data a letter confirming their April 3 discussions.

One month later, Tech called Data to ask if the work could be completed by May 1, 1991, so that Tech could participate in a U.S. Navy experiment. Dan said that the work would be completed by May 1, 1991, at no additional charge.

On May 15, 1990, Data signed a lucrative contract with a major oil company and wanted to have all installation personnel available for work on that contract. Then, on June 1, 1990, Dan informed Tech by telephone that Data would not be able to install the air-quality monitoring equipment at all.

On June 15, 1990, after having searched unsuccessfully for a substitute to supply, install and test the equipment, Tech sued Data in State A court for specific performance, demanding that Data be required to supply, install and test the equipment by May 1, 1991.

What legal arguments could Data raise as defenses, and how should the court rule on each of them? Discuss.

- I. Data's Defense to Formation: The Statute of Frauds
 - A. The one year rule requires a writing.
 - B. Data did not sign the confirming letter.

- II. Data's Defenses to the Modification
 - A. The modification lacked consideration.
 - B. The modification was not in writing.

- III. Data's Defense to Breach: Tech's Suit is Premature.

- IV. Data's Defenses to Specific Performance
 - A. Legal remedies are adequate.
 - B. The court lacks jurisdiction to order performance.
 - C. The contract is for personal services.
 - D. Conclusion

Contracts Hypothetical #6

Clark is a wholesale distributor of office supplies. Jones operates a novelty supply company. On May 1, Clark received a written order from Jones for 30,000 pens at 50 cents each, the price listed in Clark's catalog. The order from Jones stated that the pens were to be specially imprinted by Jones with a political slogan and were being purchased for resale by Jones to Davis, a candidate for the United States Senate. The order specified for delivery of half of the pens by August 1 and the remainder by October 1.

On May 5, Clark sent to Jones a written confirmation which acknowledged the quantity, price, delivery dates, and purpose of the purchase. Both the order and the confirmation were on forms containing a number of printed clauses. The printed clauses were substantially the same on both forms, except that Clark's confirmation included an additional clause stating that all disputes about the transaction were to be resolved by arbitration.

On June 30, Jones telephoned Clark and told him that another distributor had offered Jones the same pens at 45 cents each and that Jones intended to switch his order to the other distributor unless Clark agreed to lower his price. Rather than lose the sale, Clark grudgingly agreed to lower the price to 45 cents for Jones' order.

On July 30, Clark shipped the first 15,000 pens and, on August 2, Clark accepted Jones' payment for them at 45 cents each. On August 10, Jones wrote to Clark canceling the second half of the order because Davis had withdrawn from the senatorial race due to poor health. When he received the letter of cancellation, Clark had not yet ordered the second shipment of pens from the manufacturer.

Clark sued Jones for breach of contract in state court, seeking damages based on the original 50 cent price for the remaining 15,000 pens.

What arguments should each party make, and how should the case be decided? Discuss.

- I. Clark v. Jones: Breach of Contract
 - A. Formation
 - 1. Offer and Acceptance
 - 2. The Arbitration Clause: UCC Section 2-207
 - 3. Conclusion: Binding Contract without Arbitration Clause
 - C. Modification: Price Cut from 50 cents to 45 cents
 - 1. Jones threatens to breach.
 - 2. Clark “grudgingly agreed.”
 - 3. Clark accepted Jones payment.
 - 4. Conclusion: Modification Binding
 - D. Jones cancellation of the second half of the order
 - 1. Davis quit the campaign.
 - 2. Clark had notice of the purpose of the order.
 - 3. Jones’ Impracticability and Commercial Frustration Defenses to Breach
 - 4. Conclusion: The cancellation is not a breach of contract.
- II. Conclusions
 - A. Jones’ cancellation of the second half of the order is justified.
 - B. If Clark were found to be the winner, he would get lost profits on the second half of the order, based on the modified price of 45 cents per pen.