

CONTRACT FORMATION OBJECTIVE THEORY OF ASSENT

- **Reasonable, objective, reasonable person standard that looks at outward manifestations, not inner thoughts, to determine if there was an offer (R § 19)**
 - Exception: if either party has special knowledge that the other party does not intend to be bound (i.e. joking)
- **Policy:** evidentiary difficulty of proving subjective intentions, fairness of having speaker bear costs of his misunderstanding, Kaldor-Hicks efficiency considerations
- **Lucy v. Zehmer:** contract for sale of land negotiated in bar upheld even though offeror thought it was a joke; offeree thought it was serious, **outward manifestations indicated seriousness**, and there was no fraud, so joke was not an excuse
- **Specht v. Netscape:** browse/scroll-wrap licensing terms on a webpage; a reasonable person would not be expected to assent because they were not obviously visible, **lacked notice**

OFFER

- **Mutually binding promise that become binding when offeree accepts (R § 24)**
- Offeror must reasonably convey intent to be legally bound to offeree (R § 24), *Lucy v. Zehmer*
- **Cannot be merely an invitation to treat or preliminary negotiations**
 - **Lefkowitz:** advertisements are generally not considered offers but this particular one was because it had limiting language (“first come, first served”), and clear quantity (definiteness); not open to negotiation or unlimited liability

ACCEPTANCE

- A **manifestation of assent to the terms of an offer**, as defined by the offeror, either a **promise or a performance** (R § 50)
 - Once offeree accepts offer, A **BINDING CONTRACT EXISTS**
- **No mutual assent** if parties attach *materially different meanings* to their manifestations of assent (and neither/both know) (R § 20)
 - **Peerless:** contract to buy bales of cotton arriving on *Peerless* ship; two ships with that name, parties meant different ships; no contract for failure of mutual assent, no “meeting of the minds”
 - BUT if A knows of the meaning attached by B, then B’s meaning governs
- **BY PROMISE** (bilateral contract)
 - Offer inviting acceptance by promise requires offeree to exercise due diligence to notify offeror of acceptance (R § 59)
 - Exception – parties can contract around general requirement of notice
 - **Int’l Filter v. Conroe Gin:** Intl. sent proposal for purchase of machinery to company: “become a contract when accepted and approved by purchased and approved by executive officer”; C wrote “accepted” and returned (offer); Intl. exec OK’ed and sent confirmation letter next day (acceptance); court held that notice was not required because it was not specified in the contract and the proposal stated that it would become a contract upon exec’s signature
- **BY PERFORMANCE** (unilateral contract)
 - **Only when invited to do so by the offeror** can an offeree accept by performance (R § 53)
 - **White v. Corlies:** builder sent office estimate, office sent note that “upon agreement to finish in two weeks,” builder could start work “at once” (offer); builder commenced wood work/purchase of lumber, office revoked, saying that “upon agreement” invited acceptance by promise, builder said “at once” invited performance; court said **this offer sought a return promise, not acceptance by performance**, at least w/o notice and so was unenforceable; performance could have been appropriate if builder had somehow notified office, plus builder’s prep could have applied to any job, *compare with:*
 - **Ever-Tite:** signed roofing agreement stated that it would become binding upon written acceptance of contractor OR commencement of the work (offer); once credit check cleared 9 days later, Ever-Tite loaded material and went to house (acceptance); discovered that Greens had contracted with another contractor; offer had not lapsed since no time was specified in contract and 9 days was reasonable according to circumstances; **acceptance by performance** was valid
 - **Notice is generally not required UNLESS** offeree knows that offeror will likely not know of performance, then offeror’s duty is discharged unless (i) he learns of it in reasonable time, (ii) offeree tries reasonably to notify him, or (iii) offer specifically said that notification was not required (R § 54)

- **Carlill v. Carbolic Smoke Ball Co.:** offer/promise (even by ad) that one who used influenza ball and still contracted the flu was entitled to £100 was binding based on offeree's performance; no notice was required since it was a unilateral contract, also offer itself did not specify notice
- **Bishop v. Eaton:** a unilateral contract involving a loan between one party in Illinois and another in Nova Scotia; did require reasonable notice of acceptance because the offeror was not likely to find out about the performance quickly due to distance

• BY SILENCE

- Silence is not considered acceptance UNLESS i) offeree takes goods/services with opportunity to reject them, knowing compensation is expected, ii) offeror has given offeree reason to believe that silence can show assent and offeree does so intending to accept offer, or iii) prior dealings indicate that a history of offeree's silence as manifesting assent (R § 69)
 - **Hobbs v. Massasoit:** silent retention of eelskins constituted acceptance due to prior dealings between parties; offeree was required to reject offer by notifying the seller

• WITH DIFFERENT TERMS

○ "BATTLE OF THE FORMS"

- "Mirror Image Rule": Acceptance must be on the **exact** terms proposed by the offer for contract to binding; if not identical, treated as a rejection/counter-offer
- Disputes can arise pre-performance and post-performance
 - Post-performance: parties believed they had a contract, but their terms did not match
 - **"Last shot" rule – last form sent dictates terms of contract** (incentive effect)
- Applies in all scenarios not relating to sales of goods

○ UCC § 2-207

- Definite expression of acceptance/written confirmation can equal acceptance even if it has **additional or different terms**
- (1) Is acceptance **expressly conditional** on offeree's assent to additional or different terms?
 - (a) If yes, no contract without assent – treated as a rejection/counter-offer (unless parties perform, then in (3))
 - (b) If no, contract – move to step (2)
- (2) Interpreting **additional** terms as proposals to the contract
 - (a) If not merchants, additional terms are never part of contract
 - (b) If between merchants, additional terms become part of contract unless:
 - (i) Offer **expressly limits** acceptance to terms of offer
 - (ii) Additional terms **materially alter** the contract
 - Open-ended, indefinite liability indemnification term is material, *Union Carbide*
 - Burden is on party opposing incorporation of term, *Bayway*
 - Must result in **surprise** (subjective/objective) and hardship
 - Objective surprise: **reasonable merchant** would not have assented to term, *Bayway*
 - Ex: NY considers arbitration clauses *per se* alteration, *Marlene*
 - (iii) **Timely notification of objection** to terms has already been given
- *If **differing/conflicting terms**, no guide from statute
 - (a) Majority "knockout" rule – conflicting terms knock each other out and replaced with gap-fillers, *Northrop*
 - (b) Minority "first shot" rule – offeror's different terms become part of the contract; offeror is "master of offer"
 - (c) CA rule – treat them just like additional terms under (2)
- (3): **Conduct by both parties** that recognizes the existence of a contract can establish a contract when forms do not
 - Court "knocks out" forms and includes agreed-upon terms and gap-fillers
- **Dorton:** an oral purchase order for carpets followed by a written order form containing an arbitration clause did not contain an expressly conditional acceptance, triggering (2); arbitration clause is construed as a proposal that will become part of the contract unless it "materially alters" it; unclear what the exact content of the oral agreement was, remanded
- **C. Itoh:** steel coils purchase; seller's form contained express condition to acceptance of all terms, including an arbitration clause; buyer never expressly assented or rejected; dispute over quality of coils and timing of delivery; contract implied from conduct (3) (since forms do not establish a contract b/c buyer never expressly assented to term) and arbitration knocked out since it's not an agreed term or a gap-filler
- **Bayway:** dispute over a tax clause in Bayway's forms that was never objected to by Oxygenated; involves the application of (2) and the material alteration standard; burden is on party objecting to incorporation of the term; material alteration is one that would result in "surprise (subjective and objective, via "reasonable merchant") or hardship"; evidence that such tax clauses were standard fare in oil industry, tax clause becomes part of the contract
- **Northrop:** problem of "different" terms not addressed by statute; 90 day v. unlimited warranty provisions; dispute arose over return of goods past 90 days; court likes CA rule, but uses knockout rule (what Illinois would adopt) on different terms and applies gap-fillers of a "reasonable time" (b/w 30-180 days) to reject goods

○ ROLLING CONTRACT FORMATION

- **Contract (offer/acceptance) first, then followed by additional terms**
- How to incorporate terms that follow?
 - Assent through failure to return goods: § 2-606 (*ProCD, Hill*)
 - Buyer can reject the offer by returning the goods
 - Agreeing to terms up front without knowing them (*Klocek v. Gateway*)
 - Buyer can reject offer up front
 - Treat written terms that follow as a “confirmation” under § 2-207 (*Klocek*)
 - Only come into contract if both parties are merchants, no material alteration, no timely objection given
- **ProCD:** offer of ProCD selling product, consumer purchased it; did not accept until clicking on the “click-wrap” licensing agreement; disregarded agreement and used for profit; Easterbrook did not apply § 2-207 (because there was only one form), but said that assent was implied by § 2-204 (“a contract for sale of goods may be made *in any manner* sufficient to show agreement”) by agreeing to license terms and also by § 2-606 (buyer accepts goods after failing to reject them after a reasonable time)
- **Hill:** Gateway sells computer over phone (offer), Hills not bound until they keep the computer past 30 days; Easterbrook applies *ProCD* analysis (§ 2-606) to hold Hills bound to arbitration clause in the agreement since they kept the computer past 30 days; applies even if buyer was unaware of terms

LIMITATIONS ON OFFEREE’S POWER OF ACCEPTANCE

- R § 36: Offeree **cannot accept** offer if –
 1. **Time period lapses** (either fixed by offeror or a “reasonable” time)
 2. Offeree **rejects** it or issues a **counter-offer** (last-shot rule)
 3. Offeror/offeree **dies** or is **incapacitated**
 4. Offeror **revokes** it – can revoke until acceptance UNLESS an option contract is created
 - Notice of revocation is generally required, but can be contracted around
- **OPTION CONTRACTS ARE IRREVOCABLE**
 - Four ways to create an option contract
 1. A common law “**option contract**” supported by consideration (R § 25, 37)
 - Example: A pays B \$10 to hold offer open for 10 days
 2. Made irrevocable by statute (do not need consideration)
 - A “**firm offer**” under UCC § 2-205 for written sale of goods contracts
 - Irrevocable during time stated or for a reasonable time not to exceed 3 months
 - N.Y. Gen. Oblig. Law § 5-1109 for all written contracts if so specified
 - Irrevocable during time stated or for a reasonable time
 3. Offer that seeks acceptance by performance (unilateral contract) is irrevocable after the **tender** or **beginning** of performance (R § 45)
 - Creates an **option contract** when offeree begins performance
 - But offeror is only bound to fulfill his part of the contract if the offeree completes the performance
 - Example: “I promise to give you \$100 to cross the Brooklyn Bridge”
 - If one begins to cross the bridge, then the offer is irrevocable
 4. Offer that reasonably induces **substantial reliance** on the offeree prior to acceptance is irrevocable to the extent necessary to avoid injustice (R § 87)
 - Applies promissory estoppel (R § 90) to make offer irrevocable
 - **Baird:** Hand held that promissory estoppel applies only to reliance on promises, not offers; promissory estoppel only applies to non-bargained (gift) situations that one relied on, not bargained-for exchanges in the contracting business *Rejected in:*
 - **Drennan:** Traynor applied promissory estoppel and made subcontractor’s bid irrevocable when contractor had reasonably relied on it in bidding for the job; solves holdup problem, but leaves open unilateral situation of general contractors being able to shop around
 - Per *Holman Erection*, SCs cannot claim reliance on GC’s use of bids
 - **CONTRACT AROUND:** make a firm offer under UCC or NY law/option contract with consideration, or make it conditional (“I [GC] will grant SC this bid if I get the main bid from the builder”)

DEFINITENESS

- **Terms must be reasonably certain** – must provide a **basis** for determining the existence of a **breach** and for giving an appropriate **remedy** (R § 33)
 - UCC § 2-204 is more extreme –if terms (even price) are left open, **as long as parties intend to be bound** and there’s a **basis for a remedy**, the contract does not fail for indefiniteness
- **INDEFINITE LONG-TERM AGREEMENTS**
 - Contracts are incomplete (do not provide for all contingencies) because:

- Prefer the gap-fillers and it saves them time
 - Afraid of contract falling through by raising tough issues
 - Do not foresee problems (i.e. sudden market changes)
 - Choose to withhold information for business advantage
- **Oglebay**: a long-term requirements contract for iron ore with a primary (regular season rate in publication) and secondary (mutually agreed-upon rate) price mechanism; both failed and dispute arose; court found that both parties intended to be bound due to long-term nature of contract and dependence (relational-specific investments – stock, capital improvements); used gap-filler § 2-305 to set a “reasonable price” and salvaged contract
- **INDEFINITE PRELIMINARY AGREEMENTS** – “subject to contract,” missing terms
 - No underlying duty to negotiate in good faith absent an express agreement to do so
 - **Tribune Type I**: a fully binding preliminary agreement with all essential terms agreed-upon, only step left is formality of signing the contract
 - Factors that weight against holding these agreements as binding: disclaimer of intent to be bound, complexity of agreement (billion dollar merger),
 - **Tribune Type II**: a binding preliminary commitment to negotiate in good faith with some essential terms still open for negotiation, does not bind parties to obligations
 - **Channel**: a letter of intent promising to negotiate in good faith the leasing agreement after withdrawing store from market; court found this to be a **binding preliminary Tribune Type II agreement** because parties intended to be bound (took actions relying on letter), the letter was definite, and consideration existed
 - If agreement is too indefinite (“agreement to agree”):
 - **Dixon**: an indefinite promise by bank to consider Dixon’s eligibility for a loan modification, court cannot find breach, but allows Dixon to recover in *promissory estoppel* because of detrimental reliance on promise for policy reasons
 - **Cyberchron**: an unsigned purchase order because no agreement on weights, but buyer urged manufacturer to perform its contractual duties as if issue had been resolved; buyer terminated; court could not allow recovery for breach because **agreement was too indefinite** but allowed reliance damages in *promissory estoppel*
 - **PRECONTRACTUAL LIABILITY**: claimants sometimes can claim recovery in restitution
 - **Songbird**: negotiations to sell jet to TX oil baron failed, Songbird sought recovery from Amax for its efforts; court denied recovery because such activities (tax saving devices) are commonly engaged in during negotiations and didn’t unjustly enrich Amax because they also helped Songbird
 - **Kenyon**: court allowed recovery for extensive technical and certification work for cars because Kenyon was unjustly enriched, and the work didn’t benefit Ellis at all (differentiated *Songbird*)
 - **Markov**: because lessor had engaged in misrepresentation (expressed interest in re-negotiating lease but was seeking buyers at the same time) and thus breached duty to negotiate in good faith the lease, court allowed reliance damages to lessee

CONSIDERATION

- Consideration must be a **bargained-for** (sought by promisor in exchange for promise and given by promisee in exchange for promise) **performance or return promise** (R § 71)
 - **Hamer**: Uncle promised to pay nephew \$5000 to forbear from drinking, gambling, smoking until 21; promise enforceable because **forbearance of a legal right is valid as consideration**
- Adequacy of consideration (R § 79)
 - If bargained-for, no additional requirements of:
 - Benefit to promisor/detriment to promisee (abandoned benefit-detriment theory), **Hamer**
 - Equivalence of values exchanged (nominal/peppercorn – unclear)
 - Mutuality of obligation
- Promises lack consideration when:
 - **Nothing is given in return** – gratuitous promise (a gift), firm offer, contract modifications, illusory promise (one party can withdraw at its leisure)
 - Gratuitous promises are not enforceable
 - **Kirksey: Conditional gratuitous promise** from brother-in-law to brother’s widow to give up land and live with him; after a while, kicks her off land, promise not enforceable, missing bargained-for element
 - **CONTRACT AROUND**: Illusory promises (R § 77, UCC § 2-306) can be changed to contain consideration
 - 1) Making them **exclusive dealings** contracts, which imply a duty of reasonable/good faith/best efforts that counts as consideration
 - **Wood**: Agent granted exclusive right to place endorsements and sell fashions for designer, splitting profits; agreement enforceable because Wood’s promise contains **implied duty of reasonable efforts** to market designs
 - 2) **Requirements/output** contracts contain implied duty of good faith that counts as consideration

- **Structural Polymer**: SP entered agreement to buy prepreg from Zoltek with a price protection clause allowing SP to go elsewhere if Zoltek did not match competitor's price; promise enforceable because **requirements contracts contain an implied duty of good faith** (UCC § 2-306); price protection clause as minimum floor for consideration (if Zoltek did match, SP could not go elsewhere without acting in bad faith)
- 3) Adding a **satisfaction clause**, which implies a duty of good faith in making that judgment
 - **Mattei**: Developer entered agreement with owner for purchase of land, subject to developer obtaining leases satisfactory to developer; leases obtained, developer offered to pay balance of purchase price, owner refused to tender deed; agreement enforceable because **satisfaction clauses imply duty to exercise judgment in good faith**, which is adequate consideration
- NY Gen Oblig. § 5-1103 (contract modifications) and § 5-1109 (firm offers) allows these to be enforceable lacking consideration if written down
- NY Gen. Oblig § 5-1115 – no consideration needed in real estate deals
- Involves **past consideration or performance**
 - A promise to reward/give something for an act already completed, not valid for consideration because it did not induce the promise
 - **Feinberg**: Company promised employee \$200/month for life after she retired to reward her for 37 year tenure; received payments for a few years, new president reduces to \$100, then terminates completely; promise not enforceable because **past benefit not valid as consideration**, did not induce employee to quit or work longer; recovered in promissory estoppel
 - NY Gen. Oblig. § 5-1105 allows past consideration to count as consideration for written contracts
- Policy for: makes sure that contracts are efficient and fair, serve formality functions of evidentiary (evidence that a promise was made), cautionary (makes parties aware of significance of acts), channeling (evidences intention to be legally bound)
- Policy against: promises can be efficient without it, consideration does not have to be equal, hampers contract modification

STATUTE OF FRAUDS

- Ancient **writing requirement** that renders certain categories of contracts unenforceable if not commemorated in writing
 - *Only need writing on party that you are seeking to bind
 - **CONTRACT AROUND**: put a signature requirement in contract
- Policy for: evidentiary, cautionary, channeling functions for these important types of contracts
- Policy against: increases transaction costs, prejudices unsophisticated parties
- **CATEGORIES OF CONTRACTS** subject to Statute of Frauds (R § 110)
 - 1. Executor-administrator – to answer for duty of decedent
 - 2. Suretyship – a contract to answer for the debt of another
 - 3. Marriage – upon consideration of marriage
 - **4. Land contract – for sale of an interest in land**
 - 5. One-year – cannot be completed within one year of formation
 - **6. Sale of goods over \$500 (covered by UCC § 2-201)**
- **REQUIREMENTS UNDER STATUTE OF FRAUDS**
 - Writings must be **signed**
 - Almost any writing will suffice
 - Must contain **essential terms**
 - UCC § 2-201 for sale of goods only requires that writings “indicate that a contract for sale has been made between the parties”
 - **Even if missing certain terms like price, still enforceable** but “not beyond the quantity of goods shown in such writing”
- **RELIANCE-BASED EXCEPTIONS UNDER COMMON LAW**
 - **Part-performance for sale of land contracts** (R § 129)
 - If party **reasonably relied** on contract due to **continuing assent** by the other party and injustice can only be avoided by **specific performance**
 - Drastic remedy used only when party seeks specific performance
 - If restitution is adequate, courts will avoid using this exception
 - Uses heightened evidentiary standard of “clear and convincing”
 - **Beaver**: oral agreement to sell land, Beavers spent \$85,000 improving \$10,000 piece of land relying on sellers’ assurances that they would work out a written contract, sellers reneged upon discovery of a due on sale clause in mortgage; contract enforceable despite statute of frauds due to part-performance; restitution is inadequate since land is unique, granted SP
 - **Estoppel** (R § 139)
 - Applies exact language of R § 90 to circumvent statute of frauds

- Originally only covered equitable estoppel (a misrepresentation by breaching party) until *Monarco*, which expanded it to include promises
 - *Monarco*: stepfather reneges on promise to hold property in joint tenancy with wife so that upon death, land would pass to stepson Christie; meanwhile, Christie has relied on this promise by staying on family land venture, passing up opportunities; promise enforceable under estoppel exception which Traynor expands to include promises as well as misrepresentations
- **EXCEPTIONS FOR SALES OF GOODS CONTRACTS**
 - **Reliance-based exceptions: part-performance**
 - UCC § 2-201(3)(a): seller has commenced for custom-made goods
 - *Can recover in restitution
 - UCC § 2-201(3)(c): buyer and seller have paid for and delivered goods
 - **“Read your mail” exception**
 - UCC § 2-201(2): contract is enforceable if a written confirmation of it is sent between merchants in a reasonable time and recipient has a reason to know its contents UNLESS recipient objects to it in writing within 10 days of receiving it
 - *St. Ansgar Mills*: oral agreement for purchase of corn over the phone followed by written confirmation left in office for buyer to sign when he came in to pay balance, as was customary between the parties; price of corn fell, buyer pled statute of frauds as a defense to not performing; court applied “read your mail” exception to make it enforceable, reasonable time of receipt of written confirmation depends on circumstances of situation, including prior dealings
 - **“Laughing defendant” exception**
 - UCC § 2-201(3)(b): cannot admit in court the existence of a contract and then rely on statute of frauds to block its enforcement
 - Unclear whether estoppel exception applies to sales of goods
 - UCC § 1-103(b): “Unless displaced by particular provisions of UCC, the principles of law and equity including...estoppel...shall supplement it” VS.
 - UCC § 2-201(1): “Except as otherwise provided in this section...” suggesting that only exceptions to statute of frauds are in that section (no estoppel there)
 - Majority view – estoppel exception DOES apply to sales of goods

ALTERNATIVE METHODS OF RECOVERY

PROMISSORY ESTOPPEL

- Equitable remedy **used to enforce promises lacking consideration** and that would otherwise fail in breach (gratuitous promises, gifts to charity, firm offers, preliminary negotiations, contract modifications)
- Promissory Estoppel (R § 90) – **replaces consideration with reasonable reliance**
 - A **promise** that will **reasonably induce reliance** (action/forbearance)
 - Promisee **actually relies** on the promise
 - **Injustice** can only be avoided by enforcing the promise
 - *Exception – marriage agreements and charitable donations do not need actual reliance
- **Usually results in reliance damages**, but “remedy can be adjusted as justice requires” (sometimes expectation or restitution)
 - Policy for: enforce promises that promisor intended to be binding OR protect promises who behave reasonably from harm of detrimental reliance (more tort-oriented)
 - Policy against: concern that PE would swallow up contract law, has not occurred
- *Ricketts*: Grandfather promised granddaughter \$2K + 6% annual interest so she no longer had to work, she quit, grandfather died two years later and had not yet paid the balance; promise enforceable under promissory estoppel **because promise reasonably induced her to rely on it by quitting her job**; would be unjust to deny recovery due to lack of consideration
- *Feinberg*: No consideration because employer’s promise was gratuitous, but recovered in promissory estoppel because **employee reasonably relied on it by quitting her job**; unjust to deny enforcement since she had cancer and could not return to work
- *D&G*: Manufacturer promised distributor it would not take line elsewhere; relying on promise, D turned down offer to sell company, then M took line elsewhere; D lost opportunity to sell at higher price; promise enforceable though exact promise could not be pinpointed, D can recover **reliance damages** (lost opportunity price differential from first offer) in promissory estoppel; assurance of continuing relationship sufficient to induce reliance, even though terms of relationship were terminable at-will

RESTITUTION – see *infra* in REMEDIES

- **Restores to injured party any benefit that he has conferred on the breaching party**
 - Prevents unjust enrichment of breaching party
 - *Quantum meruit* – law of quasi-contract
- A non-contractual, flexible remedy based on foundation of **unjust enrichment** used:

- When it provides greatest measure of damages for injured party (down payments, market value has fallen dramatically)
- Seller has made custom-made goods (part-performance/reliance-based exception for statute of frauds in sale of goods contracts, UCC § 2-201(3))
- A **losing contract** (*Algernon*) – discussed *infra* in REMEDIES
- “**Guilty party**” **restitution** (*Britton*) – discussed *infra* in CONDITIONS
- **Impracticability** – discussed *infra* in EXCUSES FOR NON-PERFORMANCE (if conferred benefit to other party)
- No contract, but **unjust enrichment**
 - Benefits conferred in precontractual settings, *Kenyon*
 - An agreement existed but unenforceable due to technicalities (statute of frauds, capacity, public policy)
 - No agreement – **mistake/emergency**
 - Painter paints wrong house, owner watches but does not correct, painter can recover in restitution
- Exceptions: if one **voluntarily/gratuitously** confers a benefit, cannot recover in restitution
- Policy for: do not want to allow breaching parties to be unjustly enriched (corrective justice), moral disapproval
- Policy against: discourages efficient breach

INVALIDITY OF A CONTRACT

CONTRACT MODIFICATIONS

• **PRE-EXISTING DUTY RULE (R § 73)**

- Cannot modify a contract to charge more money for performing a legal duty already owed to a party because it lacks consideration UNLESS duty changed significantly, so not mere pretense of bargain
 - How to circumvent this rule:
 - **Mutual promises to rescind a contract** supported by consideration, *Schwartzreich*
 - Modification supported by **even minimal consideration** will be enforceable
- **Alaska Packers**: Workmen contract with fishing company to can salmon for fishing season; get to Alaska, stop working, demand more money for same service; company could not obtain other workers, so agree; **modification not enforceable** because of pre-existing duty rule
- **Watkins**: Excavator and owner orally agreed to raise originally agreed price by 9x for when excavator encountered solid rock when digging cellar; modification valid because implicit mutual agreement to rescind original contract, also modification to meet change in circumstances valid especially when it’s fair and no protest is made; **showing shift from § 73 to § 89**

• **GOOD FAITH AND FAIR DEALING (R § 89)**

- Modification of a not-yet performed (executory) contract is allowed (even lacking consideration) if:
 - Modification is fair and equitable in light of **unanticipated circumstances**, *Watkins*
 - To extent provided by **statute**
 - NY Gen. Oblig. § 5-1103 eliminates consideration for modifications as long as they’re written down
 - **UCC § 2-209** eliminates consideration for signed/written modifications for sales of goods contracts but cannot be coercive or in bad faith
 - Must pass test of good faith and fair dealing that looks at “reasonable commercial standards of fair dealing in the trade” (cmt. 2)
 - Enforces **no-oral modification clauses**, must satisfy statute of frauds, attempted modification can operate as a waiver; waivers can be retracted at any time UNLESS someone has materially changed position relying on it (estoppel)
 - **CONTRACT AROUND**: no-oral-modification clause, send written reminder each time you do other party a favor that this is not waiver/modification of any kind
 - To extent **justice requires due to material reliance** on modification (estoppel-type exception)

• **DURESS**

- Manifestation of assent induced by **physical/improper threat** that renders contract modification invalid; can occur when one party has already relied on contract (i.e. sunk costs), and other party “holds up” to modify to its benefit
- Physical compulsion (R § 174)
- Improper threat that **leaves the victim no reasonable alternative** (R § 175, 176)
 - Crime/tort, criminal prosecution, civil suit in bad faith
 - **Breach of duty of good faith and fair dealing**, *Austin*
 - UCC § 2-209 (cmt. 2): threat for no “legitimate commercial reason” voids it
 - If resulting exchange **is not on fair terms** and
 - Harms victim without significantly benefitting threatening party
 - Threat’s effectiveness is enhanced by prior unfair dealing, OR
 - Use of power for illegitimate ends

- *Alaska (reprise)*: modification void because of **duress/holdup problem**; cannery had sunk costs in venture, no alternate sources of labor in remote Alaska, *no real choice* unless it wanted to lose investment and future revenue
- *Austin*: Loral awarded Navy contract to build radar sets, hires subcontractor suppliers, gives first contract to Austin; meanwhile awarded second Navy contract; Austin demands it be given second contract and a price increase on first contract or else it would stop performance on first contract; Loral unable to find other suppliers to fill needs in time, so agrees; modification not enforceable because Loral was *deprived of free will* (no reasonable alternative) facing reputational loss with Navy and hefty liquidated damage clauses for not delivering goods on time
 - NOTE – case decided on common law duress, not UCC § 2-209 that takes into account dramatic increases in labor and material costs that led Austin to ask for modification

FRAUD & MISREPRESENTATION

- A statement not in accord with the facts that can void a contract (R § 159, 164)
- Fraud is *never* efficient; everyone agrees that courts should void contracts due to fraud, but allowed in following three contexts
- **Fraudulent misrepresentation** (R § 162) – a tort action
 - Knowing or reckless false statement + justifiable reliance by other party
 - Plaintiff excused from performance
 - *Punitive damages*
- **Promissory fraud** – a tort action
 - Promise that was never intended to be performed
 - *Punitive damages*
- **Innocent misrepresentation** – a contract action, *Kannavos*
 - Materially false statement + justifiable reliance
 - Allows for *rescission* of contract
 - *Plaintiff excused from performance*, but no damages
- **Breach of warranty** – contract claim used in sales of goods
 - Affirmation of fact/promise turns out to be untrue that was basis of bargain
 - If breach is sufficiently material, *plaintiff excused from performance*
 - Expectation damages
- **NONDISCLOSURE**
 - Lack of a statement
 - Classical view: **caveat emptor**, “buyer beware” no liability for bare nondisclosure
 - *Swinton*: seller knew but did not disclose that house was infested with termites; buyer cannot recover for repairs because no liability for bare nondisclosure; creates inefficient outcome of every buyer doing “due diligence”
 - Modern view: Nondisclosure of known fact is equivalent to an assertion in: (R § 161)
 - **Concealment** (R § 160): action intended/likely to prevent one from learning a fact
 - Ex. putting flowerpot over termite damage before showing the house
 - **“Half-truth”**: disclosure necessary to prevent a previous assertion from being misrepresented
 - *Kannavos*: broker represented a building as an investment rental property, knowing it violated city ordinance; buyer bought building due to this representation, failed to investigate city law; buyer can rescind because broker moved beyond bare nondisclosure to half-truths; if one speaks, must be a complete representation
 - Disclosure would correct **mistake as to basic assumption** AND **violates duty of good faith and fair dealing**
 - Disclosure would correct mistake as to contents/effects of a writing
 - Disclosure is necessary in a **fiduciary relationship**
 - **CONTRACT AROUND**: include “*As Is*” clause disclaiming all implied warranties
 - **Policy for**: immorality of deception, information asymmetry problem (for buyer), economic value of preventing mistaken transactions, efficiency (seller is in better place to investigate)
 - **Policy against**: cost of disclosure, scope of disclosure, want to protect investments in special knowledge
- **OPINION & PUFFING**
 - Generally cannot rely on opinion or puffing to bring a claim of misrepresentation
 - An opinion expresses belief, without certainty, or a judgment of quality, value, etc. (R § 168)
 - *Speakers*: talent agency’s promise to get \$2 million in endorsements cannot reasonably be relied on since it constitutes **sales talk or mere “puffing”**, not a warranty; such talk is not actionable since no reasonable person would rely on it
 - Cannot reply on opinion only, UNLESS (R § 169)
 - Relationship of **trust or confidence**
 - **Special skill**, judgment, or objectivity with respect to subject matter
 - Person is particularly **susceptible** to a misrepresentation

- **Vokes:** widow paid \$31K in dance lessons because instructors heaped praise upon her to induce her to buy more lessons; widow was bad at dancing, instructors knew it; contract voidable because instructor had superior knowledge of subject matter and widow is vulnerable
- **DISCLAIMING LIABILITY FOR FRAUD**
 - Generally courts are reluctant to allow disclaimers for fraud for moral/efficiency reasons, but concerns for party autonomy, reduction of costs lead some states (NY) to allow it
 - Other states refuse to uphold them on grounds of public policy
 - **Borat Release:** combination of *waiver of right to sue* with *no-reliance clause* in release to be filmed for the movie is upheld under NY law; excludes all parol evidence to show fraud; policy concerns for party autonomy
 - **CONTRACT AROUND:** waiver of right to sue coupled with no-reliance clause

STANDARD FORM/ADHESION CONTRACTS

- Not negotiated (take-it-or-leave-it), one side lacks notice, terms are substantively unfair, drafter has substantial market power
- Policy for: reduce drafting costs, results in lower prices for goods, reduce uncertainty, risk calculation
- Policy against: disparity in market power, no opportunity to bargain, disparity in knowledge/skill
- Standard form contracts can become **ADHESION CONTRACTS** in consumer context if market power is substantively large and consumer can only take-it-or-leave-it
 - Adhesion contracts are valid UNLESS 1) violate reasonable expectations doctrine, 2) unconscionable/public policy
- Implicated doctrines of mutual assent, interpretive rules (parol evidence, reasonable expectations, duty of good faith, contra proferentem, unconscionability, public policy, equitable remedies, statutes
- **LAISSEZ-FAIRRE:** contract doesn't matter (even if substantively unfair) because of market alternatives and competition
 - Market creates incentives to draft welfare-maximizing contracts ("small informed minority" doctrine)
 - No invalidation of contracts outside of fraud/duress
- **LIBERTARIAN PATERNALISM:** understand market's exploitation of uninformed consumers, aimed at requiring disclosure through statutes to render consumer aware and thus make better decisions for himself
- **PATERNALISM:** market takes advantage of vulnerable consumers who lack information, state's role to step in and make decision for the consumer (embodied in doctrine of unconscionability)
- **REASONABLE EXPECTATIONS DOCTRINE (R § 211)**
 - (1) Starts out with proposition that **one is bound by all terms** of standard form contract upon signature
 - (3) EXCEPT if the drafter knows that, if the consumer knew that a certain term(s) were there, **the consumer would not assent** – that particular term(s) is OUT
 - Term violates reasonable expectations if inconsistent with other conspicuous terms of contract, with prior negotiations, with prior dealings, with prior dealings with other firms, with other firms' terms
 - (2) **Equality of treatment:** writing should be interpreted **regardless** of the party's actual knowledge of understanding of the standard terms of the writing
 - Controversial provision that is not widely adopted – treats lawyer and garbage man alike
 - Policy for: incentivizes drafters to draft very clear/explicit assent to certain terms
 - Policy against: discourages people from reading fine print
 - **Scissor-Tail:** involved the enforceability of a adhesion contract in musical concert industry mandating arbitration by union's international executive board; did not violate reasonable expectations because plaintiff was a member of the trade and had signed many such contracts before (did not use "equality of treatment"), but failed on unconscionability
- **Henningsen:** injury when steering failed; back of contract had provision limiting liability for breach of warranty in 6 pt. type; clause invalid because it violated reasonable expectations doctrine, but further because of gross inequality in bargaining positions (Big Three controlled 93.5% of market, used same form), consumer had no real choice *compare with:*
- **O'Callaghan:** defective paving in building injured tenant, lease contained exculpatory clause; despite argument that housing shortage gave landlords unequal bargaining power, court upheld clause, more **laissez-faire approach** (could have looked for apartments elsewhere), only invalid if against public policy or special social relationship (common carriers, master/servant, telegraph company), plus **legislature can deal with this issue better** than courts

UNCONSCIONABILITY

- Involves doctrines of duress, fraud, undue influence, infancy, incompetence arising in consumer contracts
- UCC § 2-302/R § 208: allows courts to set aside/modify/sever ("blue pencil rule") unconscionable contracts
 - "Whether, in light of **general commercial background and commercial needs of trade**, the clause is **so one-sided** as to be unconscionable **under the circumstances existing at the time of formation**
- Policy for: to enforce substantive fairness, to address inequalities in society
- Policy against: disregards individual autonomy, violates freedom of contract, inefficient since parties are best judges of what is beneficial for themselves, courts are not best institution to deal with this problem (let legislature do it)

- **PROCEDURAL** – “absence of *meaningful choice* on the part of one party”
 - No reasonable opportunity to understand the terms (no explanation given, low education level, no cooling off period)
 - Gross inequality of bargaining power
 - No market alternative
- **SUBSTANTIVE** – “contract terms which are *unreasonably favorable* to the other party”
 - Must be extreme in light of business practices of time and place
- **Williams**: sold furniture to poor black woman in contract with a cross-collateralization clause (balance kept on all items ever purchased by buyer, so if buyer defaulted on one, seller could repossess all); not enforceable because of absence of meaningful choice (**procedural** unconscionability) and terms that are unreasonably favorable to seller (**substantive** unconscionability); dissent argued that this would result in higher interest rates on credit for consumers, legislature should deal with it, not courts
- **Jones**: consumer on welfare bought freezer for \$900 from salesman who knew it was only worth \$300; void on **substantive** (price) **unconscionability alone** (not procedural) because of disparity between price and value; no need to pay rest (but had already paid \$600)

PUBLIC POLICY

- **Contracts that violate public policy are unenforceable (R § 178)**
 - **Criminal** law, licensing requirements, **legislative/judicial policy** against exculpatory clauses, restraint of trade, antitrust statutes, waiver of obligations to family members
- Balance public policy and interest in enforcement – parties’ expectations, possibility of forfeiture, public interest, importance of policy, relative culpability of parties
 - **In pari delicto** – position of defendant is most compelling (let losses lie where they fall)
- Can order **restitution** if a contract is voided on public policy grounds (“clean hands”)
- **Policy for**: enhances deterrence, conserves prosecutorial resources, maintains integrity of courts
- **Policy against**: disproportionate punishment, illegitimate punishment, exclusion from benefits of contract law
- **ILLEGAL CONTRACTS**: violate specific criminal laws
 - Illegal formation, illegal performance, formation is product of illegal activity, performance will promote illegal activity
 - **Bovard**: contract for sale of horse corporation involved in manufacturing drug paraphernalia; contract void because public policy against drug paraphernalia was **implicit** in statute criminalizing marijuana use
 - **XLO**: subcontractor sought payment owed by Rivergate (general contractor), who refused to pay alleging antitrust defense under Donnelly Act saying contract was a feature of extortion/labor bribery operation by Italian mob; remanded to trial to see if enforcement of contract will promote very illegalities abhorred by Donnelly Act, reluctant to void contracts on antitrust defenses because it benefits party that receives benefits and doesn’t have to pay
 - “All or nothing” rule: whole contract is either enforceable or void
- **CONTRACTS RELATED TO PUBLIC POLICY**: “protect some aspect of the public welfare”
 - **Covenants “not to compete”**: unenforceable on grounds of public policy if it (R § 188)
 - Is not ancillary to an otherwise valid transaction OR
 - Is broader in time, geographic area, and scope than is needed to protect the employer
 - Imposes **undue hardship** on the promisor
 - Is **injurious** to the **public** (i.e. physicians)
 - Remedy is an **INJUNCTION**
 - *NOTE: virtually unenforceable in CA (why Silicon Valley is competitive economic environment)
 - **Policy for**: incentivizes transfer of information to collaborators, acquisition of assets from competitors
 - **Policy against**: economic freedom of promisor, dissemination of info, competition, benefits to consumer
 - **Hopper**: non-compete to not practice small animal medicine for 3 years within 5 miles of city; ignored it, opened practice, employer lost business; covenant enforceable, but reduced to one year
 - **If non-compete is overly broad**:
 - “All or nothing”: enforce as written or reject entirely (old approach)
 - “Blue pencil”: cross/strike out offensive terms to extent possible (form over substance)
 - “Reasonableness”: enforce covenant to extent necessary to protect employer, used in *Hopper*
 - **Arbitration**: FAA represents federal policy in enforcing arbitration, preempts state policy, *Concepcion*
 - **Italian Colors**: contractual waiver of class arbitration under FAA is valid even though the plaintiff’s cost of individually arbitrating an antitrust claim exceeds potential recovery

GOOD FAITH IN PERFORMANCE

*Only attaches at moment of contract *formation* – no duty to negotiate in good faith

- **Obligatory** duty in every contract (R § 205, UCC § 1-304) that CANNOT be contracted out of
 - UCC § 1-302: can define contours of good faith as long as not manifestly unreasonable

- **Definition of the duty**
 - R § 205: excludes “*bad faith*,” faithfulness to an *agreed common* purpose, consistent with *justified* expectations
 - UCC § 2-103: “*honesty in fact*,” observance of *reasonable commercial standards of fair dealing* in the trade”
- Arises in **discretionary** contracts that would have been illusory under old contract law for lack of consideration
 - Output/requirements contracts, exclusive agency agreements (*Wood v. Lucy*) “if satisfied” clauses (*Mattei*)
- Examples of **bad faith**: opportunism (ex. holdup – try to wring advantage from fact that other party is vulnerable because it has sunk costs in venture already & to take advantage of party in a way not contemplated at drafting), dishonesty
 - **Market Street**: lessee did not disclose ¶ 34 in letter to lessor requesting more financing in a sale-and-leaseback agreement, possibly knowing that if lessor did not agree to financing, lessee could purchase property back for less than market value; Posner remanded to find out if lessee’s state of mind was “tricky” or “sharp dealing,” intending to take advantage of lessor’s oversight; duty of good faith is about “*a stab at approximating the terms the parties would have negotiated had they foreseen the circumstances that have given rise to this dispute*”
- **Policy for**: protect parties’ expectations at low cost (don’t have to put it in contract), promote efficiency (gap-fillers), fair play
- **Policy against**: uncertainty, increased litigation costs, courts could get it wrong and parties are stuck with an unwanted term, so they try to opt out of it (increased drafting costs)
- **Dalton**: alleged testing service did not use good faith effort in considering his proffered evidence explaining score increase; contract breached because good faith implies promise not to act arbitrarily or irrationally, ETS did not exercise its discretion and test taker is entitled to **good faith consideration** of evidence; court’s analysis colored by fact of contract of adhesion nature
- **Bloor**: Falstaff bought Ballantine, contracted to use **best efforts** to promote and maintain high volume of sales; new management came, sales declined for label, but profits up for Falstaff overall; breached best efforts because Falstaff did not treat Ballantine **equally with its own products** or take advantage of opportunities to distribute it; best efforts doesn’t require bankrupting yourself, but remedy (expectation damages of lost sales using comparable brands) suggests it means **comparable efforts in industry standard**

INTERPRETATION OF A CONTRACT

PAROL EVIDENCE RULE

- Written agreement supersedes all other agreements; prevents admittance of parol/extrinsic evidence about previous agreements
 - **MERGER CLAUSES**: “There are no promises, verbal understandings, or agreements of any kind, pertaining to this contract other than specified herein”
 - *Parol evidence rule does not bar evidence of **subsequent** oral or written agreements
 - No-oral-modification clauses are not generally enforced at common law
 - But UCC § 2-209 and NY Gen. Oblig. Law § 15-301 make them more enforceable
- Step 1: Classify written agreements according to level of **integration** (R § 209, 210)
 - **Integrated**: writing constitutes *final expression* of one or more terms of agreement
 - **Completely integrated**: writing constitutes *complete and exclusive* statement of all the terms of the agreement
 - *No parol evidence admitted at all*
 - **Partially integrated**: writing constitutes *final expression* of some terms of the agreement, but not all terms
 - **Not integrated if omitted consistent additional term might “naturally” be omitted from writing**
 - *Parol evidence for consistent additional terms admitted as to the non-integrated terms ONLY*
- If agreement is integrated (either partially or completely), conflicting parol/extrinsic evidence is never allowed (R § 215)
- Parol/extrinsic evidence can ALWAYS come in to show (R § 214):
 - **Whether agreement is integrated** – completely/partially – or not integrated
 - **Meaning of the writing** (if ambiguous)
 - Illegality, fraud, duress, **mistake**, lack of consideration, or other invalidating cause
 - Grounds for rescission, reformation, specific performance, or other remedy
- **Policy for**: encourages people to put agreements in writing, less evidence in record, lower litigation costs, jury less likely to be confused, judicial control of interpretive process
- **Policy against**: increased drafting costs, prejudice against unsophisticated parties

DETERMINING LEVEL OF INTEGRATION OF AGREEMENT

- **Strict/NY rule**: if written contract embraced scope of oral contract, parol evidence excluded
 - Courts looked at contract and applied own common sense about what would naturally be included in such a contract
 - **Gianni**: rented space in office building, lease prohibited selling tobacco; when another store started selling soft drinks, Gianni tried to admit parol evidence that lessor had promised him exclusive right to sell soft drinks; no parol evidence allowed; **if subject is dealt with at all** in written contract, the **writing presumes to represent the entirety** of the transaction on subject
- **Liberal/CA rule**: “**A document itself cannot prove its own completeness**”
 - R § 214 – exception that allows parol evidence to show **if** writing is integrated or not

- **Masterson:** sellers granted deed to ranch to sister with an option to buy it back; seller went bankrupt, trustee wanted to purchase it back; sister wanted to admit parol evidence to show that right was not assignable; consistent/additional parol evidence admissible because *deed is partially integrated*; deed alone cannot prove complete integration, issue of assignability is not one that is “natural” to a deed
- **Bollinger:** Construction co. and landowner contract to dump waste on property if sandwiched between topsoil; topsoil part not included in written contract by mistake, but company originally complied; parol evidence admissible due to *mistake exception* to allowing parol evidence

DETERMINING WHETHER AGREEMENT IS AMBIGUOUS

- Extrinsic evidence CANNOT be used to explain unambiguous agreements; but can extrinsic evidence be used to determine *whether* an agreement is ambiguous?
 - *Generally used only for *completely integrated agreements*
- **NY’s “Plain Meaning”/ “Four Corners” Rule:** 1) is language ambiguous? – if no, no extrinsic evidence; 2) if yes, then extrinsic evidence is in per R § 214(c) to explain the ambiguous term
 - **Pros:** honors written contracts, promotes stability in law, encourages better drafting, better evidence (writing > testimony), lowers litigation costs, lowers reading costs
 - **Cons:** higher drafting costs, prejudice to unsophisticated parties
 - **Greenfield:** Ronettes signed contract with Phil Specter, signing away ownership rights to recordings of performance and got royalties in return; Specter later earned \$ on licensing and sales from synchronization but paid no royalties; Ronettes wanted to admit extrinsic evidence to prove that use for synchronization was not meant to be included in terms; inadmissible, silence does not equal ambiguity, “four corners of contract” were not ambiguous
 - **WWW:** Contract with reciprocal cancellation and merger clause; one party wants to introduce extrinsic evidence to show that reciprocal cancellation was really only for them; inadmissible because contract is not ambiguous on its face
- **CA’s “Anything Goes” Rule:** *preliminary consideration* of all extrinsic evidence in order to determine *if* agreement is ambiguous (i.e. if language is reasonably susceptible to alternate meaning)
 - **Pros:** honors intentions of parties, protects unsophisticated parties
 - **Cons:** destabilizes written contracts, sub-par evidence, huge litigation costs, sloppy drafting
 - **CONTRACT AROUND:** Sophisticated parties prefer NY over CA rule – opt out using **choice-of-law** provision, **NOT merger clause** (could use extrinsic evidence to knock it out)
 - **PG&E:** contract for work on a steam turbine with indemnity clause; during work, part of turbine damaged, company doing work sought to admit extrinsic evidence showing that clause covered third party property only; evidence admissible, must do **preliminary consideration of parol evidence** to find the parties’ intent and decided that language was fairly susceptible of either of the asserted interpretations
 - **Delta Dynamics:** contract with minimum quantities for trigger locks with termination clause and recovery for attorney’s fees; upon breach, Delta sued for damages; Pixey wants to include extrinsic evidence showing that sole remedy was termination; admissible as preliminary matter
 - **Trident:** contract between two sophisticated parties not allowing pre-payment for first 12 years; one party wants to introduce extrinsic evidence allowing it to prepay; admissible as a matter of CA law, but Kozinski is upset about the destabilizing effect this has on contract law in CA

DETERMINING WHETHER EVIDENCE OF COMMERCIAL CONTEXT CAN EXPLAIN OR SUPPLEMENT A WRITTEN AGREEMENT

- **Extrinsic evidence of commercial context admissible to supplement or give meaning to terms as long as it doesn’t contradict express terms;** basically Traynor’s super liberal approach even if term is clear
 - **CONTRACT AROUND:** include a clause knocking out usage of trade/course of performance/course of dealing as an interpretive tool (merger clauses are not adequate generally under UCC’s liberal approach)
- UCC § 1-303: Types of extrinsic evidence in order of weight accorded by courts (following express terms)
 - **Course of performance:** past conduct in current contract
 - Can be evidence of a **waiver** (ex. consistently accept delivery late)
 - But waivers can be **retracted** upon notice to other party
 - Unless relied upon by the other party (UCC § 2-209)
 - Can be evidence of a **contract modification** of an express term, which, unlike a waiver, is binding, even if it is inconsistent with that term (UCC § 1-303(f))
 - **CONTRACT AROUND:** 1) anti-waiver clause in initial contract, 2) send written reminder each time you do other party a favor that this is not waiver/modification of any kind
 - **Course of dealing:** conduct in past contracts
 - **Usage of trade:** conduct by other parties in a particular vocation
 - Needs regularity as to justify expectation that it will be observed in the contract in question

- If parties are in the trade, are aware of usage, or are performing in area where usage is used
- Policy for: reflects intentions of parties, lower drafting costs, generates fair outcomes
- Policy against: undermines written contracts, court could err, higher litigation costs, higher reading costs (especially on newcomers to trade)
- **Frigaliment**: conflict over whether contract for only young chickens or for any kind, including stewing chicken; court looked at express term, relation to price, Dept. of Agriculture's regulation, negotiations, trade usage; plaintiff did not meet burden to narrow term than is regularly used in trade
 - Argue failure of mutual assent (R § 20) like in Peerless if parties attached materially different meanings to "chicken"
- **Hurst**: 50% protein in horse meat term did not exclude 49.53 to 49.96% from receiving market value because of usage of trade; even though 50% is not ambiguous, extrinsic evidence still comes in
- **Nanakuli**: dispute over whether contract included price-protection for paving contractors in asphalt industry; court admitted extrinsic evidence showing usage of trade, Shell's past price-protection of Nanakuli was a course of performance that went to show the intentions of the parties with respect to the original agreement
- **Columbia Nitrogen**: extrinsic evidence admitted to show that express price and quantity terms in mixed fertilizer industry are just projections subject to market forces; merger clause did not prevent court from considering usage of trade or course of dealing

CHOOSING AMONG AMBIGUOUS MEANINGS

- **Contra proferentem (R § 206)**: interpret terms *against* drafter of the contract
- **Ejusdem generis**: "of the same kind" (cars, motor bikes, vehicles – vehicles excludes airplanes)
- **Expressio unius est exclusion alterius**: "the expression of one thing is the exclusion of another"
- **Noscitur a sociis**: "it is known from its associates" (to determine meaning of ambiguous word from rest of statute)
- **Purpose and intention of parties**
- **Interpretation that favors the public (R § 207)**
- **Advice of counsel** – takes sophistication of parties into account

EXCUSES FOR NON-PERFORMANCE

EXPRESS CONDITIONS

- **CONDITION: an event that is not certain to occur, but that must occur before other party's performance becomes due (R § 224)**
 - STRICT COMPLIANCE WITH EXPRESS CONDITIONS IS REQUIRED
 - **Luttinger**: contract to purchase premises with down payment of \$8500, subject to condition that buyers exercise due diligence to obtain financing from a bank/lending institution for \$45K, 20 years, 8.5% apr; could not find it, sought down payment back, Rosens offered to compensate them for .25% interest gap, Luttingers refused; Luttingers not in breach (Rosens are) because **Luttingers' performance was conditional** upon obtaining adequate financing, did not have to accept Rosens' offer because they are not a bank/lending institution
- **EXPRESS CONDITION OR DUTY?**
 - **R § 227: when a clause could be either a condition or a duty, courts prefer to impose a DUTY rather than a condition in order to mitigate harsh effects of non-occurrence of a condition (i.e. forfeiture)**
 - Duty: "ship owner promises to sail with the next wind"
 - Failure to do so = breach of contract (expectation damages)
 - Condition: "If, on condition that ship owner sails with next wind, cargo owner will pay 10% premium"
 - Failure to do so = no 10% premium, but no damages
 - Duty + Condition/Promissory Condition: "Ship owner promises to sail with the next wind; and if, on condition that he does so, cargo owner will pay a 10% premium"
 - Failure to do so = breach of contract (expectation damages) + no 10% premium
 - **Peacock**: GC/SC contract specifying that final payment would be made within 30 days after completion of work, written acceptance by architect, and final payment by owner of condo; owner went bankrupt, GC refused to pay SCs; GC is in breach, "full payment by owner" was NOT a condition precedent, but **an absolute promise to pay merely specifying a reasonable amount of time to do so**; since ambiguous, interpreted it as a duty to protect SCs, GCs are in better position to assume risk, norms of the business favor SCs
 - **CONTRACT AROUND**: "No payment shall be made until..." courts that do not categorically bar these conditions on grounds of public policy will honor them (if they do, use choice-of-law)
 - **SATISFACTION CLAUSES**
 - Must be reasonable, not arbitrary or capricious in commercial matters (*Mattei*)
 - Must be **honest** in matters of taste (*Gibson*)
 - Third-party satisfaction (i.e. architect) – most states use good faith standard

- EXCEPT NY: architect's claim of dissatisfaction must be *reasonable* (not independent agents, interests are aligned with one of the parties)
- **MITIGATING DOCTRINES** of harsh effects when an express condition does not occur
 - **PREVENTION:** cannot prevent the occurrence of a condition of one's own duty and then later assert the non-occurrence of that condition as a reason for non-performance
 - Such "sabotage" violates duty of good faith
 - Methods whereby *nonoccurrence of a condition can be EXCUSED* by party whose performance is conditional
 - **WAIVER:** party repeatedly ignores the condition
 - *McKenna:* Buyer repeatedly ignored condition that payments were conditional upon certificate of architect; builder sued for breach for nonpayment, buyer had waived condition
 - **Waivers can be retracted before the time for occurrence UNLESS other party has materially relied on it (ESTOPPEL)**
 - *CONTRACT AROUND:* 1) anti-waiver clause in initial contract, 2) send written reminder each time you do a favor that this is not waiver/modification of any kind
 - **MODIFICATION:** *binding* change to contract moving forward
 - Need consideration under common law, but not under UCC or NY law
 - **If courts have a choice between waiver and modification, they will choose waiver*
 - **ELECTION:** when time for occurrence of a condition has expired, party whose duty is conditional faces a choice: 1) take advantage of other party's failure to perform and *treat your duty as discharged* OR 2) disregard other party's failure to perform condition and *perform your duty anyway*
 - Once choice is made, it is *binding*
 - **INTERPRETATION TO AVOID FORFEITURE**
 - *Hicks:* completely integrated written merger agreement, prior parol condition about obtaining funds that applies to both parties and doesn't contradict written terms; **evidence of a condition precedent to the performance of BOTH parties can be used to supplement even a completely integrated agreement**
 - *CONTRACT AROUND:* Merger clause stipulating that nothing is contingent on outside conditions and that "there are no conditions to the effectiveness of this agreement"

CONSTRUCTIVE CONDITIONS OF EXCHANGE: conditions implied by law

- Can you *withhold your own performance* because other party did not complete his condition to satisfaction?
 - Makes "dependent covenants" as opposed to independent ones
- **MATERIAL BREACH:** if A doesn't substantially perform, excuses B's performance and B can get damages
 - *A lot depends on the order of performance/breach – who breached first?*
 - **R § 241: When is breach material? (COMPLETE OPPOSITE OF SUBSTANTIAL PERFORMANCE)**
 - Extent of *injured party's deprivation* of what they had been promised (i.e. half the house)
 - Extent to which injured party can be adequately compensated (*Kingston*)
 - Extent to which party in default will suffer *forfeiture* (i.e. if they had built the whole house)
 - Different if owner could reject performance (a moveable garden shed) that builder could resell later
 - If party in default will cure his failure and actually perform
 - If party in default is acting in *good faith* (if breach is "willful," almost always material breach)
 - *Kingston v. Preston:* silk mercer promised to give business to apprentice, who promised monthly payments backed by collateral; Kingston did not pay (since he was broke), Preston refused to give up business, so Kingston sued for breach; Preston not in breach because *Kingston's payments/collateral was a condition precedent to Preston handing over business*; not handing \$ over was a *material breach* (unreasonable to make Preston go out on a limb and hand over business to a broke Kingston, could not recover anything)
 - Policy for: protects promisee from going out on a limb (not going to make them perform and sue later when they might not recover anything), incentives promisor to take precautions against breach
 - Policy against: unjust enrichment of promisee (rectified by "guilty party" restitution), incentivizes promisee to induce breach (situation like *Britton* – mistreat employee 11 months into contract)
- **PERFORMANCE OF WORK PRECEDES PAYMENT** (absent language to contrary)
 - Theory that employers are more responsible than employees paid in advance
 - *Stewart:* builder walked off job, owner did not pay; question of who breached first; court found no evidence of owner's agreement to pay incrementally; absent such an express agreement, implied condition that *substantial performance of work precedes payment*, owner excused from payment
 - *CONTRACT AROUND:* specify that payment is to be made on a progress basis, or before completion of work
- **SIMULTANEOUS PERFORMANCE/CONCURRENT CONDITIONS**

- Applies in sale of goods, real estate deals
- **Perfect tender: tendering performance (showing you're ready to perform) is a condition of each party's duty**

MITIGATING HARSHNESS OF CONSTRUCTIVE CONDITIONS

• SUBSTANTIAL PERFORMANCE

- **SUBSTANTIAL PERFORMANCE REQUIRED WITH CONSTRUCTIVE CONDITIONS**
 - NOT STRICT COMPLIANCE; done to mitigate harsh effects of *forfeiture* on breaching party
- If B substantially performs but commits minor breach, A must still perform but can sue later and get damages
 - **Jacob & Youngs**: builder's oversight in not using Reading pipe was not willful (which always precludes finding of substantial performance), not every minutiae of contract is a dependent condition when **departure from the specification is not substantive but insignificant**, will not allow departures to be excused when they would *frustrate purpose of the contract itself*, justice demands that forfeiture not be allowed when departure is minute in comparison
- **CONTRACT AROUND**: make explicitly clear that use of Reading pipe is a condition precedent to payment, *not* a duty (as the original language of the contract said), discussion in recitals of contract of why use of the pipe is subjectively valuable (model home)

• DIVISIBILITY: if one party's performance consists of several distinct items and the price to be paid is apportioned to each item (corresponding pairs of part-performances)

- A's non-performance of one part of the contract only excuses B's performance of the corresponding part of the contract, NOT B's entire duties under the contract
 - **Protects breaching party by making other party pay for the part of the contract that was substantially performed**
- **Gill**: contract to drive logs downstream but flood came and swept many downstream; Gill sought payment of logs already driven downstream; contract was severable since payment was apportioned per 1000 feet of logs driven

• "GUILTY PARTY" RESTITUTION: Breaching party is entitled to restitution for any benefit conferred by part performance

- Party has **materially** breached (cannot sue in contract), but can sue in restitution for *market value* of work done
 - Measure of restitution is usually capped at total contract price
 - **Policy for**: eliminates bad incentive effect of employers mistreating employees after 11 months in a 12 month contract to get employee to leave, and reap benefits of 11 months of free labor
- *If injured party rejects the goods, and thereby derives no benefit from them, breaching party cannot recover anything because there has been no unjust enrichment
- **Britton v. Turner**: plaintiff walked off the job after nine months, defendant refused to pay; concluding that barring recovery altogether results in unjust enrichment where employer has derived months benefits of labor, *court allowed breaching party to recover in restitution* for market value of work performed
- **Kirkland**: due to plaintiff's mistake in using wood lath instead of rock lath (material breach, so can't recover in contract based on substantial performance), defendant made him stop working; court allowed plaintiff to recover in restitution for value of work performed

MISTAKE & IMPRACTICABILITY

• Results in excusal of **both** parties' contractual duties and recovery in restitution for both parties

- Can be used to excuse the non-occurrence of an express condition to avoid forfeiture

• MISTAKE

- Involve an existing, but unknown fact at the time of contract formation
 - Results in material adverse effect
 - Risk has not been allocated
- **UNILATERAL MISTAKE**: only one party is mistaken about an existing fact that was **basic assumption** (something parties never imagined would be different) of contract
 - Difficult to result in excusal unless it's unconscionable to hold one to duties or other party caused mistake
- **MUTUAL MISTAKE**: both parties are mistaken about an existing fact that was **basic assumption** of contract

• EXISTING IMPRACTICABILITY

- Involves an existing, but unknown fact at the time of contract formation
- **ELEMENTS OF EXISTING IMPRACTICABILITY CLAIM (R § 266)**
 - 1. A fact which party had no reason to know
 - 2. Non-existence of which was a basic assumption of contract
 - 3. Made performance impracticable (“excessive and unreasonable cost”)
- **Mineral Park**: contract to build bridge in which defendant was to take all necessary gravel and earth for construction from plaintiff’s land; only half was taken because other half was below water level; court excused performance because it would be “unreasonable and excessive” to remove rest of gravel
- **SUPERVENING IMPRACTICABILITY**
 - Involves facts that arise after time of contract formation (one of most difficult claims to win)
 - Originally very restricted to only “acts of God;” slowly expanded by English judges to include *implied conditions* that the occurrence would not happen
 - Classical categories (death/incapacity of person, destruction of a specific thing, prohibition/prevention by law)
 - **Taylor v. Caldwell**: performers rented out music hall, but it was destroyed by fire before the time of performance at no fault of either party; both parties excused because in contracts where performance depends on the continued existence of a given thing, there is an *implied condition* that *impossibility of performance arising from its destruction excuses performance* of respective duties
 - **ELEMENTS OF SUPERVENING IMPRACTICABILITY CLAIM (R § 261/UCC § 2-615)**
 - 1. Occurrence of event (contingency)
 - CANNOT be breaching party’s fault
 - 2. Non-occurrence of which was basic assumption of contract
 - “Not fairly to be regarded as within risks assumed under contract”
 - Mere foreseeability is NOT enough to assume party assumed that risk, Transatlantic
 - 3. Made performance impracticable
 - “A thing is *impossible* in legal contemplation when it is not practicable; and a thing is *impracticable* when it can only be done at an *excessive and unreasonable cost.*” *Transatlantic*
 - Mere price increase is never enough UNLESS the “the rise in cost is due to some unforeseen contingency which alters the essential nature of the performance” (cmt. 3)
 - **Transatlantic**: Ship transporting wheat to Iran had to take alternate route around the Cape of Good Hope because the Suez Canal had been closed due to Egyptian government nationalizing it; shipper wanted restitution for price differential from US government; performance was not impracticable, even if it lowered profit; *alternatives available and risk foreseen, ship owner superior risk-bearer; not treated as sale of goods, but UCC used as persuasive evidence*
 - How to decide if party assumed risk under contract?
 - Implied terms, surrounding circumstances, custom, and usage of trade
 - **SUPERIOR RISK-BEARER**: Posner & Rosenfeld article (*Transatlantic*)
 - Best situated to either control *probability* of risk materializing or insure against this risk by minimizing *magnitude* of loss
 - If can’t insure or control: who has diversified assets and can better *spread* risk
 - Foreseeability does NOT prove allocation, but is suggestive
 - Should parties reasonably have foreseen it? (i.e. changes in market value, concert hall could be closed)
 - Did parties *actually* anticipate it? (Suez canal closing in *Transatlantic*)
 - Did parties “tacitly agree” on it?
 - **Force majeure clauses**: party anticipates events that it cannot readily prevent and might impede its performance, so it introduces a clause excusing it from performance if the impediment arises
 - Must be careful not to be too broad or courts will just ignore them
 - *Ejusdem generis* – courts can interpret “or any additional events” like previous events listed
 - UCC § 2-615, cmt. 8: suggestion that *force majeure* clause cannot broaden too much the excuses available under the existing impracticability rule, and that “hell or high water” clauses can be manifestly unreasonable
 - **CONTRACT AROUND**: **force majeure clause** to expressly disclaim liability for a supervening event; **hell or high water clause** to expressly assume liability for a supervening, unforeseeable event (used in leases)
- **RECOVERY** for losses incurred in reliance on contract when party excused from performance due to impracticability
 - If contract is *divisible* – party is excused only to that part of their performances
 - If losses incurred in reliance have *conferred a benefit* to other party – courts allow recovery in *restitution*, usually capped at contract price
 - If party *rejects* the partial performance, then much harder to argue unjust enrichment
 - Work done “must have *become so far identified with contract* such that but for the destruction, it would have gone to the other party as contemplated by the contract”
 - **Young v. Chicopee**: contract for bridge repair specifying that work could not begin until half of all material was present to prevent hindering travel, plaintiff piled lumber along bridge/river bank; bridge

- burned down, destroying piled lumber as well; recovery allowed in restitution but not for damaged lumber because it had not yet become identified with the bridge, still in exclusive control of plaintiff
- Courts have discretion under § 272 to award reliance/partial expectation, but rarely do so (*Alcoa*—exception)

REMEDIES

SPECIFIC PERFORMANCE

- Equitable remedy compelling performance of contract available when *remedy at law* (money damages) is *inadequate* (i.e. land)
 - Injured party has “**clean hands**” and has not delayed (“laches”)
 - Contract is not too indefinite, **not for personal services** (indentured servitude), *Bliss*
 - Promisor would receive security for performance (i.e. promisee will actually pay)
 - Compelling performance will not be unjust, oppressive, or impossible, or unduly burdensome on court to supervise
 - Will not force party to break another existing contract
- Reasons for traditional rule against SP
 - Deters efficient breach by encouraging overinvestment
 - People don’t want to work together
 - Hard to enforce, supervise by courts
 - Money easy to calculate and almost always adequate
- Reasons in favor of SP
 - Hard to calculate \$ value
 - Forces parties to have private negotiation better at setting price
 - Can implement negative injunction preventing similar work (not forced servitude)
 - Some goods are unique (land, heirlooms) and money isn’t adequate
- Contemporary trend: follows Posner’s theory and expands SP using cost-benefit analysis
 - If costs and benefits are equal, then give damages
 - If costs are less for SP, then give SP, *Walgreen*
 - Coase theorem: absent transaction costs, parties will bargain to an allocatively efficient outcome under ANY remedy
- **Klein**: purchase of a jet to resell at profit, seller backed out; SP not appropriate because monetary damages (expectation of potential profit) are adequate, jet was not unique enough
- **Morris**: breach of promise to give horse to Sparrow; SP appropriate despite evidence of a robust market for roping horses because Sparrow had invested time and effort in training Keno to be a roping horse, giving it a “peculiar and unique value”
- **Laclede**: breach of long-term requirements contract to provide propane; SP appropriate because of the difficulty in calculating expectation damages, **public policy** in providing gas, difficult to **cover** (OPEC embargo)
- **Walgreen**: Sara Creek breached promised not to lease space to competing pharmacy; injunction appropriate, Posner says parties will *negotiate*, Walgreen will give up its right to injunction for a payoff, leads to **allocatively efficient outcome** regardless

RESTITUTION

- **Restores to injured party any benefit that he has conferred on the breaching party**
 - Returns breaching party to position had contract never been entered into
- **FORMULA: Recover reasonable/market value of services/benefits conferred at the time of breach**
 - **Not diminished by any loss that would have been sustained by complete performance**
- **LOSING CONTRACTS**
 - Valid contract exists, but **expectation damages would be zero or negative**
 - Allow recovery in restitution or else breaching party would be **unjustly enriched**
 - Policy for: fairness and prevents unjust enrichment, moral theory of corrective justice
 - Policy against: discourage efficient breach
 - **Algernon**: SC had contracted to erect steel and do other work for GC’s contract for naval hospital; SC would have *lost* \$37K if GC had performed by paying for crane use and K was completed; GC breached by refusing to pay for crane use; restitution available instead of expectation since this was a losing contract, equal to market value of performance

RELIANCE

- **Returns injured party to position as if contract had never been made**

- **FORMULA: (Expenses incurred in preparation for or by performance) – (any loss breaching party can prove with reasonable certainty that injured party would have suffered had contract been performed)**
- *Subject to avoidability and foreseeability limitations*
- Rarely used (since expectation damages swallow up reliance damages):
 - Expectation damages are too **UNCERTAIN** (discussed *infra* in certainty)
 - But cap to not exceed plausible measure of expectation damages
 - Expectation seems like too much (rough justice), *Sullivan*
 - Doubts about liability, *Sullivan*
 - Policy reasons (*Sullivan* court not wanting to discourage doctors from performing surgeries)
 - Usually used in **promissory estoppel** (but not always – *Ricketts, Feinberg*)
- **Sullivan:** multiple nosejobs left entertainer disfigured; restitution too meager, expectation too harsh especially where doubts about negligence, difficult to assign \$ value in noncommercial field, policy concerns about doctors; awarded **reliance** damages

EXPECTATION DAMAGES

- **Puts injured party in position as if contract had been successfully performed**
- **FORMULA: (Loss in value due to other party's failure/deficiency of performance) + (other loss – incidental or consequential) – (cost and loss avoided by injured party stopping its performance)**
 - Loss in value – difference in value expected and value received
 - Other loss – incidental damages (costs incurred trying to find substitute); consequential damages (damages to person/property caused by breach)
 - Costs avoided – expense that would have incurred in party's own performance
 - Loss avoided – loss saved by getting substitute (cover/resale)
 - **Hawkins:** doctor promised 100% perfect hand, patient left permanently disfigured and suffered through extended recovery; expectation damages, awarded loss in value of perfect hand and additional pain recovery
- **MEASURING LOSS IN VALUE OF PERFORMANCE (R § 348)**
 - **SUBJECTIVE VALUE:** amount *promisee* is willing to pay for performance or willing to accept to surrender entitlement to performance
 - Which approach – cost of performance or diminution in market value – will approximate this value?
 - **CONTRACT AROUND:** specify in contract whether cost of performance or diminution in market rule will be used to calculate expectation damages (run risk of court viewing it as a penalty clause – to get around that, show sentimental/subjective value or purpose in the RECITAL of the contract)
 - **DIMINISHED (MARKET) VALUE:** amount *others* (not the promisee) are willing to pay for performance
 - Used when the **difference between cost of performance and actual value of that performance is too great**
 - Would result in “*economic waste*” – tearing down a building to complete desired performance
 - **Policy for:** minimizes harsh effect on breaching party, avoids disproportionality, limits litigation costs, doesn't unjust enrich injured party for performance they might not actually value that much
 - **Policy against:** “windfall” for breaching party, doesn't reprimand morally reprehensible breaches
 - **Peevyhouse:** couple leases land to coal mine company for 5 years, specified restorative and remedial work on land; work would have cost \$29K and only would increase value of land by \$300; default rule is cost of performance but this case used diminished value rule because cost to remedy was **grossly disproportional** to benefit to be attained, plus provision was merely **incidental** to contract
 - **Counter:** Peevyhouses bargained for this provision, sentimental value of land, gave up royalty up front, their subjective valuation was much higher than mere diminution in market value
 - **Jacob & Youngs:** construction contract specified Redding pipe; different brand, but equal quality pipe used, and owner did not discover mistake until after construction completed; damages limited to the diminution of market value (\$0) because cost of performance would be **grossly disproportional** to desired benefit (tear down wall, economic waste), use of wrong pipe was accidental (Cardozo does not want to punish builder so harshly)
 - **Plante:** contract for construction of a house, builder misplaced wall by one foot to dissatisfaction of owners; damages limited to diminished value rule (\$0) because cost of performance means tearing down wall (**gross economic waste**)
 - **COST OF PERFORMANCE:** amount needed to *compensate* promisee to *hire someone else* to complete the job satisfactorily
 - Generally the default rule, especially in “thick market” scenarios where goods are involved, more problematic in construction scenarios
 - **Policy for:** condemn morally reprehensible breaches, holds parties to contract terms, if someone has to benefit it should be the injured party (not breaching party)

- Policy against: windfall for injured party, performance might not be valued that much, disproportional
- **Groves**: contract to remove sand and gravel for 7 years, return promise to regrade land (would have cost \$60K, only increase value of land by \$12K); damages are cost of performance due to *willful/deliberate nature* of breach regardless of disproportion, economic waste only applies to tearing down of completed structures

LIMITATIONS ON EXPECTATION DAMAGES

- **AVOIDABILITY: damages are not recoverable for loss that the injured party could have avoided after breach or repudiation without undue risk, expense, burden or humiliation (R § 350)**
 - Incentives *efficient mitigation* – makes injured party better off without making breaching party any worse off
 - Types of avoidable losses:
 - Costs of continuing to perform, *Rockingham*
 - Expenditures in reliance on contract
 - Losses from failing to arrange substitute transactions (“cover”/ “resale”) – damages reflect difference between market value (at time of breach) and contract price (UCC § 2-713)
 - **Avoidability limitation only kicks in at moment of unequivocal breach/repudiation by other party**
 - **Does not bar recovery for losses incurred as a result of reasonable but unsuccessful efforts to avoid loss*
 - Incentives promisees: to mitigate losses efficiently, clarify if a statement/action is a repudiation/breach
 - Incentives promisors: to repudiate as early as possible (easier for promisee to mitigate losses)
 - **Rockingham**: county notified construction company not to proceed building under the contract (moment of repudiation/breach), but company kept building bridge, racking up losses of \$18K; once contract is broken, plaintiff has to stop performing and not rack up losses that “need not have been incurred”
 - **Parker**: actress agreed to be in a musical, studio breached but offered job in western film; actress need not mitigate damages with a job that is *different or inferior in kind*, but only with a job that is *comparable or substantially similar*
- **FORESEEABILITY: damages are not recoverable for unforeseeable losses (Hadley, R § 351)**
 - (1) Damages “*arising naturally*” from the usual course of things – ALWAYS recoverable
 - (2) Damages “*arising from special circumstances*” reasonably supposed to be in the contemplation of *both* parties as a *probable* result of breach
 - **Hadley v. Baxendale**: mill operator wanted to recover lost profits from common carrier for delayed delivery of mill part, resulting in 5-day shutdown; carrier not liable because such damages do not “naturally arise” and were not in contemplation of both parties since shutdown and urgency was not communicated to carrier
 - **CISG variant: possible** (not probable) result of breach – expands scope of recovery
 - **Delchi**: allowed recovery for lost profits based on Delchi taking orders based on number of compressors ordered from Rotorex and shipping/customs costs
 - **NY’s Tacit Agreement Test**: liability is limited to what the parties would have concluded had they considered the subject; would the defendant have assumed liability? – limits scope of recovery
 - **Kenford**: county enters contract for some of Kenford’s land to be used for a new stadium; county breaches, seeks damages for lost appreciation of value of the surrounding land; recovery denied because no contemplation that county would assume risk of paying loss appreciation of value of land were stadium not to be built
 - Historical policy reasons: distribute wealth to promisors (world of limited shareholder liability, thin insurance markets), control juries sympathetic to “little guy,” reduce litigation costs
 - Incentives promisors: to breach inefficiently (since expectation damages are altered)
 - Incentivizes promises: to take precautions against losses associated with breach, purchase insurance, disclose information about potential losses, just stipulate damages up front
 - **CONTRACT AROUND**: disclaim liability for consequential losses
- **CERTAINTY: damages are not recoverable for loss beyond an amount that the evidence permits to be established with reasonable certainty (R § 352)**
 - 1) If too uncertain, courts will award RELIANCE DAMAGES as an alternative
 - Cap to make sure they don’t exceed probable measure of expectation damages
 - If a losing contract, damages lowered based on amount promisee would have lost in course of completion
 - 1) If too uncertain, courts will award pre-contractual and contractual expenses as a proxy for expectation damages
 - Assuming parties would have made it back had contract been performed (i.e. not a losing contract)
 - Doubts are resolved against the party in breach
 - **Minority new business rule**: lost profits are too uncertain, *Evergreen*

- Policy for: incentivizes promisees to take precautions against breach, purchase insurance, stipulate damages up front, reduces litigation costs
- Policy against: favors established businesses, induces inefficient breach,
- **MAJORITY rule**: lost profits can be awarded to new businesses if they present evidence and testimony to support claims
 - **Fera**: 10 year lease for a book-and-bottle shop, landlord breached before term began; jury award for lost profits sustained as reasonable given the amount of evidence presented
 - Policy for: doesn't disfavor new enterprises

LIQUIDATED & STIPULATED DAMAGES

- **Damages for breach may be stipulated up front but must be reasonable in the light of the anticipated or actual loss caused by breach and the difficulties of calculating actual loss (R § 356)**
 - Reasonable/difficult to calculate at moment of formation (ex ante) or moment of breach (ex post) (UCC § 2-718)
 - **Gustafson**: contract to re-surface highway, provision that each day of delay would trigger a \$210 fine, state withheld \$14,070 from payment due to delay; liquidated damages clause honored as an *ex ante* reasonable attempt to fix a fair compensation for unexcused delay, was **clearly broken down for each day** and not inflated, and uncertainty was a factor since it was difficult to prove exact loss
- Looked on with suspicion by courts as **PENALTY CLAUSES**, which are unenforceable on grounds of public policy
 - Generally a presumption of reasonableness; burden on other party to show punitive nature of clause
 - Must be reasonable across every potential breach point
 - Do regular damages analysis (*Hadley*) and then compare to see if relatively the same
 - If a fixed sum that will overcompensate in certain scenarios (as one party performs), probably a penalty clause
 - **Lake River**: minimum guarantee clause triggered liquidated damages clause, which just guaranteed loss in value (\$533K) as a lump sum without any deduction for any costs that LR would have incurred to earn those payments or avoidable losses (resold bagging equipment); *ex ante* unreasonable because it systematically overcompensates LR every time; constitutes a penalty clause, thus unenforceable
 - **Wasserman**: storeowner leased land from township with termination provision/stipulated damages clause mandating that township would pay 25% of average gross receipts for a year; *ex ante or ex post* unenforceable as a penalty clause due to fixed nature of gross receipts measure, doesn't account for actual losses or profits at all
 - Cannot disguise penalty clause as a bonus – courts look through form to substance
- True liquidated damages are a GOOD THING: reduce litigation costs, avoid judicial error, can contract around limitations on damages (foreseeability, certainty, avoidability), reflects true intentions of parties
- Prohibition on penalty clauses:
 - Policy for: clause resulted from unequal bargaining power, court aiding in oppression, **deter efficient breach**, incentivizes promisees to induce breach, purpose of contract law is not punishment
 - Policy against: sophisticated parties will calculate the risks/benefits of a penalty clause, makes transaction credible (signal you're a good actor), a form of insurance for risk-averse promisee
- **CONTRACT AROUND** – Characterize payment as an **alternative mode of performance** rather than a penalty
 - Pay-or-play contracts with actors, take-or-pay gas purchase contracts, severance pay in employment contracts ONLY