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CONTRACTS

CASES AND MATERIALS

EIGHTH EDITION

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CHAPTER 1

BASES FOR ENFORCING PROMISES

SECTION 1. ENFORCEABLE PROMISES: AN INTRODUCTION

Most people have an informal sense of contracts. Almost everyone of consenting age has entered into a contract, often with little hesitation or ceremony. Consider, for example, the arrangement you have with your cell phone company or the agreement established when you accepted the offer of admission from your law school. You are no doubt already familiar with such common-sense notions of contracts. The aim of this book is to provide more formal content to those general understandings. We are interested in what “contract” means as a matter of law.

The Restatement of Contracts, Second, defines contract as “a promise or set of promises for the breach of which the law gives a remedy, or the performance of which the law in some way recognizes as a duty.” Restatement § 1. Not all promises are legally binding; the law does not provide a remedy for every broken promise. There may, of course, be moral or social sanctions for breaking a promise, but our primary inquiry here concerns the distinctive contributions of *law*. How does the law determine which promises to enforce?

We take up that question with two cases that focus on the promise itself. The first considers whether a binding (or enforceable) promise was created by a doctor’s assertion that he would make a young man’s injured hand “one hundred percent perfect.” The second case queries whether an enforceable promise should be found in the printed materials of a boat manufacturer stating that its boats could attain a “maximum speed of 30 miles per hour.” These cases begin our consideration of why some promises are found to be legally enforceable and others not. The section concludes with a brief introduction to theories of why some promises *should* be legally enforceable. In Section 2 we turn to the issue of how the law enforces promises, by taking an initial look at remedies for breach.

Beyond the “why” and “how” of promissory enforcement, these opening materials also serve as an introduction to the question of “where” the law of promissory obligation is to be found: the basic sources and authorities that govern most contractual relationships. We have already mentioned the influential Restatement of Contracts, a comprehensive statement of general common law contract principles first promulgated by the American Law Institute (ALI) in 1932. The Restatement, Second, appeared in 1979. In this book, unless otherwise indicated, a reference to the “Restatement” refers to the Restatement, Second. While not enacted law itself, the Restatement has been aptly described by a former ALI director as “common law ‘persuasive authority’ with a high degree of persuasion.” Herbert Goodrich, *Restatement and Codification*, in DAVID DUDLEY FIELD: CENTENARY ESSAYS 241, 244-45 (Alison Reppy ed., 1949). For more on the history of the Restatements, see the *Selections for Contracts*.

Beyond the persuasive force of the Restatement, statutes are a distinctive and direct source of authority, particularly Article 2 of the Uniform Commercial Code, which as we shall see in our second case, applies in cases involving the sale of goods. We will highlight various other sources of contract law as we encounter them in the cases that follow. Of course, the primary sources relied on in most casebooks, including this one, are cases—the judicial opinions that constitute the common law. We begin our study of promises with an old chestnut from the American common law of contracts, *Hawkins v. McGee*.

Hawkins v. McGee

New Hampshire Supreme Court, 1929.

84 N.H. 114, 146 A. 641.

■ BRANCH, J. The operation in question consisted in the removal of a considerable quantity of scar tissue from the palm of the plaintiff's right hand and the grafting of skin taken from the plaintiff's chest in place thereof. The scar tissue was the result of a severe burn caused by contact with an electric wire, which the plaintiff received about nine years before the time of the transactions here involved. There was evidence to the effect that before the operation was performed the plaintiff and his father went to the defendant's office, and that the defendant, in answer to the question, "How long will the boy be in the hospital?" replied, "Three or four days, not over four; then the boy can go home and it will be just a few days when he will go back to work with a good hand." Clearly this and other testimony to the same effect would not justify a finding that the doctor contracted to complete the hospital treatment in three or four days or that the plaintiff would be able to go back to work within a few days thereafter. The above statements could only be construed as expressions of opinion or predictions as to the probable duration of the treatment and plaintiff's resulting disability, and the fact that these estimates were exceeded would impose no contractual liability upon the defendant. The only substantial basis for the plaintiff's claim is the testimony that the defendant also said before the operation was decided upon, "I will guarantee to make the hand a hundred per cent perfect hand or a hundred per cent good hand." The plaintiff was present when these words were alleged to have been spoken, and, if they are to be taken at their face value, it seems obvious that proof of their utterance would establish the giving of a warranty in accordance with his contention.

The defendant argues, however, that, even if these words were uttered by him, no reasonable man would understand that they were used with the intention of entering "into any contractual relation whatever," and that they could reasonably be understood only "as his expression in strong language that he believed and expected that as a result of the operation he would give the plaintiff a very good hand." It may be conceded, as the defendant contends, that, before the question of the making of a contract should be submitted to a jury, there is a preliminary question of law for the trial court to pass upon, i.e. "whether the words could possibly have the meaning imputed to them by the party who founds his case upon a certain interpretation," but it cannot be held that the trial court decided this question erroneously in the present case. It is unnecessary to determine at this time whether the argument of the defendant, based upon "common knowledge of the uncertainty which attends all surgical operations," and the improbability that a surgeon would ever contract to make a damaged part of the human body "one hundred per cent perfect," would, in the ab-

sence of countervailing considerations, be regarded as conclusive, for there were other factors in the present case which tended to support the contention of the plaintiff. There was evidence that the defendant repeatedly solicited from the plaintiff's father the opportunity to perform this operation, and the theory was advanced by plaintiff's counsel in cross-examination of defendant that he sought an opportunity to "experiment on skin grafting," in which he had had little previous experience. If the jury accepted this part of plaintiff's contention, there would be a reasonable basis for the further conclusion that, if defendant spoke the words attributed to him, he did so with the intention that they should be accepted at their face value, as an inducement for the granting of consent to the operation by the plaintiff and his father, and there was ample evidence that they were so accepted by them. The question of the making of the alleged contract was properly submitted to the jury.

[The Court then discussed the proper measure of damages and, finding that the trial court's charge to the jury was erroneous (the trial court had instructed that the jury could consider the "(1) pain and suffering due to the operation; and (2) positive ill effects of the operation upon the plaintiff's hand"), it ordered a new trial on the calculation of damages. We take up the question of damages in such a case—what it means for the law to give a remedy—in Section 2.]

NOTES

(1) *One Hundred Percent*. Although Dr. McGee made a number of statements to the boy's father regarding the outcome of treatment, it does not appear that he actually used the word "promise." What then makes a statement a promise? Consider the role of language, its context, and the nature of the transaction in *Hawkins*. See Restatement §§ 2 and 4. What result if, before performing reconstructive knee surgery, a surgeon tells the patient that "the operation could give you a knee that was stronger than before" and that the patient would, "if committed, play basketball again"? See [Anglin v. Kleeman, 665 A.2d 747 \(N.H. 1995\)](#).

(2) *Policy Considerations*. In a well-known case involving plastic surgery gone wrong, the court observed that "[i]t is not hard to see why the courts should be unenthusiastic or skeptical about contract theory [in such a case]." [Sullivan v. O'Connor, 296 N.E.2d 183 \(Mass. 1973\)](#). (The Sullivan case is presented on p. 15 below.) Is judicial skepticism about recovery in contract specially warranted in a medical setting? Why?

Might an aggrieved plaintiff try other theories of recovery? What factors contribute to a decision to bring one type of claim rather than another? The availability of certain kinds of damages available in tort, for example, but not in contract? The application of the relevant statute of limitations?

The questions highlight structural limitations of the traditional law school curriculum. Although first year courses are sometimes taught as though they had little substantive relation to one another, the connections among them are many. Contracts for the sale of property, for example, require an underlying understanding of what counts as property and is therefore subject to transfer. Land obviously qualifies, but what about leaseholds, or ideas, or embryos? These questions are sometimes resolved in the context of a contract action, as we will see in connection with commercial surrogacy at p. 613 below. More often, however, contract law proceeds against the background of existing rules of

property, civil procedure, torts, and so on. We will from time to time point out the significance of these other foundational areas for the contract issue at hand, and urge you to keep an eye on the connections between contract law and your other subjects throughout this course.

(3) *Statutory Override*. Common-law rulings by courts sometimes give way to contrary judgments by legislatures. Consider the following example. In 1971, the Michigan Supreme Court affirmed a judgment for damages for breach of contract against a surgeon who, according to his patient's testimony, had said before a stomach operation, "After this operation, you can throw your pillbox away" and "Once you have an operation it takes care of all your troubles." [Guilmet v. Campbell, 188 N.W.2d 601 \(Mich. 1971\)](#). Three years later, the Michigan legislature enacted a statute providing that an "agreement, promise, contract, or warranty of cure relating to medical care or treatment" is void unless evidenced by a signed writing. Mich.Comp.L. Ann. 566.132(1)(g). How might this statute have come about?

We note the interplay between courts, legislatures, and other law-making bodies such as regulatory agencies at various points throughout this book. As you read, think about the strengths and advantages of each with regard to making or reforming contract law. Keep in mind such factors as institutional competence, legitimacy, and the practical necessities of law-making.

Bayliner Marine Corp. v. Crow

Supreme Court of Virginia, 1999.
[257 Va. 121, 509 S.E.2d 499.](#)

■ KEENAN, JUSTICE. In this appeal, the dispositive issue is whether there was sufficient evidence to support the trial court's ruling that the manufacturer of a sport fishing boat breached an express warranty and implied warranties of merchantability and fitness for a particular purpose.

In the summer of 1989, John R. Crow was invited by John Atherton, then a sales representative for Tidewater Yacht Agency, Inc. (Tidewater), to ride on a new model sport fishing boat known as a 3486 Trophy Convertible, manufactured by Bayliner Marine Corporation (Bayliner). During an excursion lasting about 20 minutes, Crow piloted the boat for a short period of time but was not able to determine its speed because there was no equipment on board for such testing.

When Crow asked Atherton about the maximum speed of the boat, Atherton explained that he had no personal experience with the boat or information from other customers concerning the boat's performance. Therefore, Atherton consulted two documents described as "prop matrixes," which were included by Bayliner in its dealer's manual.

Atherton gave Crow copies of the "prop matrixes," which listed the boat models offered by Bayliner and stated the recommended propeller sizes, gear ratios, and engine sizes for each model. The "prop matrixes" also listed the maximum speed for each model. The 3486 Trophy Convertible was listed as having a maximum speed of 30 miles per hour when equipped with a size "20x20" or "20x19" propeller. The boat Crow purchased did not have either size propeller but, instead, had a size "20x17" propeller.

At the bottom of one of the "prop matrixes" was the following disclaimer: "This data is intended for comparative purposes only, and is available without reference to weather conditions or other variables. All testing was

done at or near sea level, with full fuel and water tanks, and approximately 600 lb. passenger and gear weight.”

Atherton also showed Crow a Bayliner brochure describing the 1989 boat models, including the 3486 Trophy Convertible. The brochure included a picture of that model fully rigged for offshore fishing accompanied by the statement that this model “delivers the kind of performance you need to get to the prime offshore fishing grounds.”

In August 1989, Crow entered into a written contract for the purchase of the 3486 Trophy Convertible in which he had ridden. The purchase price was \$120,000, exclusive of taxes. The purchase price included various equipment to be installed by Tidewater including a generator, a cockpit cover, a “Bimini top,” a winch, a spotlight, radar, a navigation system, an icemaker, fishing outriggers, an automatic pilot system, extra fuel gauges, a second radio, and air conditioning and heating units. The total weight of the added equipment was about 2,000 pounds. Crow did not test drive the boat after the additional equipment was installed or at any other time prior to taking delivery.

When Crow took delivery of the boat in September 1989, he piloted it onto the Elizabeth River. He noticed that the boat’s speed measuring equipment, which was installed in accordance with the contract terms, indicated that the boat’s maximum speed was 13 miles per hour. Crow immediately returned to Tidewater and reported the problem.

During the next 12 to 14 months, while Crow retained ownership and possession of the boat, Tidewater made numerous repairs and adjustments to the boat in an attempt to increase its speed capability. Despite these efforts, the boat consistently achieved a maximum speed of only 17 miles per hour, except for one period following an engine modification when it temporarily reached a speed of about 24 miles per hour. In July 1990, a representative from Bayliner wrote Crow a letter stating that the performance representations made at the time of purchase were incorrect, and that 23 to 25 miles per hour was the maximum speed the boat could achieve.

In 1992, Crow filed a motion for judgment against Tidewater, Bayliner, and Brunswick Corporation, the manufacturer of the boat’s diesel engines. Crow alleged, among other things, that Bayliner breached express warranties, and implied warranties of merchantability and fitness for a particular purpose.

At a bench trial in 1994, Crow, Atherton, and Gordon W. Shelton, III, Tidewater’s owner, testified that speed is a critical quality in boats used for offshore sport fishing in the Tidewater area of Virginia because of the distance between the coast and the offshore fishing grounds. According to these witnesses, a typical offshore fishing site in that area is 90 miles from the coast. Therefore, the speed at which the boat can travel to and from fishing sites has a major impact on the amount of time left in a day for fishing.

Crow testified that because of the boat’s slow speed, he could not use the boat for offshore fishing, that he had no other use for it, and that he would not have purchased the boat if he had known that its maximum speed was 23 to 25 miles per hour. . . .

The trial court entered judgment in favor of Crow against Bayliner on the counts of breach of express warranty and breach of implied warranties of merchantability and fitness for a particular purpose. . . . On appeal, we review the evidence in the light most favorable to Crow, the prevailing party at trial.

Crow argues that the “prop matrixes” he received created an express warranty by Bayliner that the boat he purchased was capable of a maximum speed of 30 miles per hour. We disagree.

Code § 8.2–313 provides, in relevant part:

Express warranties by the seller are created as follows:

(a) Any affirmation of fact or promise made by the seller to the buyer which relates to the goods and becomes part of the basis of the bargain creates an express warranty that the goods shall conform to the affirmation or promise.

(b) Any description of the goods which is made a part of the basis of the bargain creates an express warranty that the goods shall conform to the description.

The issue whether a particular affirmation of fact made by the seller constitutes an express warranty is generally a question of fact. See *id.*, Official Comment 3; [Daughtrey v. Ashe](#), 243 Va. 73, 78, 413 S.E.2d 336, 339 (1992). In *Daughtrey*, we examined whether a jeweler’s statement on an appraisal form constituted an express warranty. We held that the jeweler’s description of the particular diamonds being purchased as “v.v.s. quality” constituted an express warranty that the diamonds were, in fact, of that grade. *Id.* at 77, 413 S.E.2d at 338.

Unlike the representation in *Daughtrey*, however, the statements in the “prop matrixes” provided by Bayliner did not relate to the particular boat purchased by Crow, or to one having substantially similar characteristics. By their plain terms, the figures stated in the “prop matrixes” referred to a boat with different sized propellers that carried equipment weighing substantially less than the equipment on Crow’s boat. Therefore, we conclude that the statements contained in the “prop matrixes” did not constitute an express warranty by Bayliner about the performance capabilities of the particular boat purchased by Crow.

Crow also contends that Bayliner made an express warranty regarding the boat’s maximum speed in the statement in Bayliner’s sales brochure that this model boat “delivers the kind of performance you need to get to the prime offshore fishing grounds.” While the general rule is that a description of the goods that forms a basis of the bargain constitutes an express warranty, Code § 8.2–313(2) directs that “a statement purporting to be merely the seller’s opinion or commendation of the goods does not create a warranty.”

The statement made by Bayliner in its sales brochure is merely a commendation of the boat’s performance and does not describe a specific characteristic or feature of the boat. The statement simply expressed the manufacturer’s opinion concerning the quality of the boat’s performance and did not create an express warranty that the boat was capable of attaining a speed of 30 miles per hour. Therefore, we conclude that the evidence does not support the trial court’s finding that Bayliner breached an express warranty made to Crow.

[The Court also found that Bayliner had not violated the “implied warranty of merchantability” provided in UCC § 2–314. Discussion of implied warranties is left to Chapter 5.]

Reversed and final judgment.

NOTES

(1) *Express Warranties.* According to Crow, what promise had Atherton broken? By what means had the supposed promise been made? Why should an express warranty result even if the seller did not intend to make one? What if Atherton had told Crow during their negotiations that “in my opinion this boat will go 30 miles per hour no trouble”? See UCC § 2–313(2).

(2) *Implied Warranties.* Suppose that another purchaser contracted with a boat manufacturer for the sale of a speed boat and that as in the principal case, the contract was silent with regard to the boat’s speed. Assuming that there had been no brochure or any discussion of speed between the parties prior to the sale, would any promise have been broken if when the purchaser revved the engine of his new boat, it was able to achieve a maximum speed of only two miles per hour? See UCC § 2–314 (2). Which of the provisions of that subsection might apply? How do implied warranties alter the force or applicability of the familiar saying *caveat emptor*? We discuss implied warranties, including disclaimers of warranties, in greater detail in Chapter 6.

(3) *UCC Primer.* Article 2 of the Uniform Commercial Code (UCC or “the Code”) is the primary source of law for transactions involving the sale of goods in the United States. The Code itself is the product of the American Law Institute and the National Conference of Commissioners on Uniform State Laws (NCCUSL). Versions of the Code have been enacted across the country by state legislatures, and by Congress for the District of Columbia. Article 2 is fundamental to the study of contract law, and cases exploring its structure and how it differs from the common law appear throughout this book. For now, however, a few basics are in order.

Transactions covered by Article 2 include not only sales between merchants but also those between merchants and consumers, as in *Bayliner*. As we shall see, in a number of areas Article 2 provides special rules for merchants, who are assumed to be more sophisticated and more familiar with commercial practices than are consumers. Determining whether a party is a merchant is therefore an important preliminary question. Article 2 defines merchant to include not only “a person who deals in goods of the kind” but also one who “by his occupation holds himself out as having knowledge or skill peculiar to the goods involved in the transaction.” UCC § 2–104(1). Comment 2 to that section lists special Article 2 merchant provisions which treat merchants differently from nonmerchants; we return to the significance of a party’s status as a merchant at various points.

A second basic matter concerns the definition of “goods.” The starting point is UCC § 2–105(1). What are “things . . . which are movable”? Is land “goods”? Is a 10-ton printing press “goods”? What if in the case above, Crow had custom-ordered his boat so that at the time of the contract the boat had not been built? See UCC § 2–105(2). The application of Article 2 is often called into question in contracts that involve both goods *and* services. Article 2 does not apply, for example, to a contract to paint the exterior of a house, even though a small amount of paint (goods) will be transferred, because the goods component of the contract is incidental. But what about other kinds of “hybrid contracts” such as contracts involving the sale of goods *and* the provision of services, or contracts involving the sale of goods *and* the sale of property other than goods, such as real estate? Should Article 2 apply to a contract that includes both the sale and installation of an appliance such as a washing machine? What about a

catering contract in which the customer is paying both for food and for food preparation? We look more closely at the problem of hybrid contracts in Chapter 8.

Finally, it is important to keep in mind that the Code does not wholly supplant the common law. UCC § 1–103(b) states that “[u]nless displaced by the particular provisions of [the Code], the principles of law and equity . . . supplement its provisions.” UCC § 1–103(b) provides a lengthy list of principles of law and equity that may supplement the Code, including such principles as capacity to contract, duress, and mistake. For a helpful discussion of the concept of supplementation, see Comment 2 to UCC § 1–103.

THEORIES OF CONTRACT ENFORCEMENT

The law of contract is the law of enforceable promises. But why should law enforce promises? In a well known article from the last century, legal philosopher Morris Cohen suggested that “[t]he simplest answer is that of the intuitionists, namely, that promises are sacred per se, that there is something inherently despicable about not keeping a promise, and that a properly organized society should not tolerate this.” At the same time, Cohen thought it very doubtful that

“many of us would want to live in an entirely rigid world in which one would be obliged to keep all one’s promises instead of the present more viable system, in which a vaguely fair proportion is sufficient. Many of us indeed would shudder at the idea of being bound by every promise, no matter how foolish, without any chance of letting increased wisdom undo past foolishness. Certainly, some freedom to change one’s mind is necessary for free intercourse between those who lack omniscience.” [Morris Cohen, *The Basis of Contract*, 46 *Harv.L.Rev* 553, 571–74, 580–583 \(1932\).](#)

Few would argue with the notion that promises carry moral force. So evident, it is almost tautological. Yet, when the force of law is brought to bear on promises, commonsense notions become more complicated and more contested. “Nowhere,” declared Oliver Wendell Holmes,^a “is the confusion between legal and moral ideas more manifest than in the law of contract.” [The Path of the Law, 10 *Harv. L. Rev.* 457 \(1897\).](#)

Conceding that law is justified in enforcing some, but not all, promises, the pertinent question then becomes, what distinguishes the promises that law will enforce from those it will not? To address this question, a number of theoretical arguments have been proposed, some more compelling than others. Pursuing these lines of argument in any detail would take us well beyond the scope of this casebook: our primary focus is contract doctrine—the basic rules and practices that comprise contract law. However, as we shall see, theoretical perspectives on promises can usefully inform the application of doctrine. For example, as the court observed in *Mills v. Wyman*, p. 52 below, “[g]eneral rules of law established for the protection and security of honest and fair-minded men, who may inconsiderately make promis-

^a Oliver Wendell Holmes, Jr. (1841–1935) practiced law in Boston, served briefly as professor of law at Harvard, and then for twenty years as justice and later chief justice of the Supreme Judicial Court of Massachusetts. In 1902 President Theodore Roosevelt appointed him to the Supreme Court of the United States, where the quality of his dissenting opinions won him the title of the “Great Dissenter.” He resigned because of his great age in 1932. His most famous work is *The Common Law* (1881), based on a series of lectures.

es without any equivalent, will sometimes screen men of a different character from engagements which they are bound in foro conscientiae to perform.”

Every theoretical argument justifying promissory liability emphasizes certain underlying values served by contract doctrine. Take, for instance, two competing theories that ground legal enforcement in the promisor’s autonomy or will. The “contract as promise” thesis holds that law is justified in enforcing a promise when an individual “intentionally invoke[s] a convention whose function is to give grounds—moral grounds—for another to expect the promised performance.” See, Charles Fried, *Contract as Promise*, at p. 16. Morality alone, however, won’t tell us which promises are or ought to be legally enforceable, since all promises carry some moral force. The competing “consent theory” grounds enforcement less in a general moral duty to keep one’s promises than in consensual undertakings that reveal an “intention to create a legally enforceable obligation.” See [Randy E. Barnett, A Consent Theory of Contract, 86 Colum. L. Rev. 269, 300 \(1986\)](#).

Both “contract as promise” and the “consent theory” look to the promisor’s will—in making a promise or voluntarily taking on a legal duty—in locating the basis for judicial enforcement. A third theoretical basis of promissory obligation flips the focus from the promisor’s will to the promisee’s reliance. When a promisee reasonably relies on a promise to his detriment, law may and in many cases does enforce the promise, even against the promisor’s will, in order to protect the promisee. Reliance theories are most clearly implicated in the various estoppel doctrines that enforce promises where the promise has triggered reasonable, foreseeable and justifiable detrimental action by the promisee.

Still other rival theoretical arguments for legal enforceability focus less on the interests of the parties, whether promisors or promisees, and more on broader criteria such as economic efficiency, predictability, fairness, social justice and distribution to justify legal enforcement of doctrine. For example, as Morris Cohen observed, “[t]here can be no doubt that from an empirical or historical point of view, the ability to rely on the promises of others adds to the confidence necessary to social intercourse and enterprise.” Whether or not these broader criteria undergird the whole of contract law, there is no doubt that aspects of each are reflected in the various doctrines we will study. As you read the cases going forward, be alert to the competing normative values that justify the legal enforcement of promises. Predictability, for instance, is a central motivating feature of the consideration doctrine, the topic of Section 3, and fairness, social justice and distribution run through doctrine of unconscionability discussed in Chapter 6. Theories of economic efficiency have been most effective, and perhaps also most controversial, in the doctrines involving contract remedies, the topic to which we now turn.

SECTION 2. REMEDYING BREACH

We all know what it means to keep a promise. Simply put, it means doing what was promised. But what does it mean to *enforce* a promise that has not been kept? Restatement § 1 defines a contract in terms of both a legal duty to perform a promise and the provision of a remedy if performance does not occur. How does the law determine the appropriate remedy? Although the answer is taken up in detail in Chapter 7, some consider-

ation of remedies is useful at the outset to get a sense of what is at stake practically and conceptually when a promise is broken.

The cases that follow introduce two fundamental assumptions made by courts in the development of remedies. The first is that the law is primarily concerned with relief of aggrieved promisees and not with punishment of promisors. The second assumption is that the primary purpose of the remedy is to give promisees “the benefit of the bargain” by protecting expectation interests. As expressed in Restatement § 344(a), the objective of protecting a promisee’s expectation interest is to put the promisee “in as good a position as he would have been in had the contract been performed.” While easily stated, the complexities of figuring out just how to measure that interest are tested in our next case, *Naval Institute*, wherein the court seeks to compensate Naval by calculating the extent of profits it lost on account of Berkley’s breach of promise. This amount, and no more, constituted Naval’s expectation interest.

United States Naval Institute v. Charter Communications, Inc

United States Court of Appeals, Second Circuit, 1991.
[936 F.2d 692.](#)

■ KEARSE, CIRCUIT JUDGE: This case returns to us following our remand in *United States Naval Institute v. Charter Communications, Inc.*, 875 F.2d 1044 (2d Cir.1989) (“*Naval I*”), . . . for the fashioning of relief in favor of plaintiff *United States Naval Institute* (“*Naval*”) against defendant *Charter Communications, Inc.*, and *Berkley Publishing Group* (collectively “*Berkley*”), for breach of an agreement with respect to the publication of the paperback edition of *The Hunt For Red October* (“*Red October*” or the “*Book*”). On remand, the district court awarded Naval \$35,380.50 in damages [and] \$7,760.12 as profits wrongfully received by Berkley. . . . Naval appeals from so much of the judgment as failed to award a greater amount as profits. . . . Berkley cross-appeals from the judgment as a whole and from such parts of it as awarded moneys to Naval. For the reasons below, we reverse the award of profits; we affirm the award of damages. . . .

I. Background

. . . Naval, as the assignee of the author’s copyright in *Red October*, entered into a licensing agreement with Berkley in September 1984 (the “*Agreement*”), granting Berkley the exclusive license to publish a paperback edition of the *Book* “not sooner than October 1985.” Berkley shipped its paperback edition to retail outlets early, placing those outlets in position to sell the paperback prior to October 1985. As a result, retail sales of the paperback began on September 15, 1985, and early sales were sufficiently substantial that the *Book* was near the top of paperback bestseller lists before the end of September 1985.

Naval commenced the present action when it learned of Berkley’s plans for early shipment, and it unsuccessfully sought a preliminary injunction. After trial, the district judge dismissed the complaint. He ruled that Berkley had not breached the *Agreement* because it was entitled, in accordance with industry custom, to ship prior to the agreed publication date. On appeal, we reversed. Though we upheld the district court’s finding that the *Agreement* did not prohibit the early shipments themselves, we concluded that if the “not sooner than October 1985” term of the *Agreement*

had any meaning whatever, it meant at least that Berkley was not allowed to cause such voluminous paperback retail sales prior to that date, and that Berkley had therefore breached the Agreement. Naval I, 875 F.2d at 1049–51. Accordingly, we remanded for entry of a judgment awarding Naval appropriate relief.

On the remand, Naval asserted that it was entitled to recovery for copyright infringement, and it sought judgment awarding it all of Berkley's profits from pre-October 1985 sales of the Book; it estimated those profits at \$724,300. . . . Berkley, on the other hand, [contended] that Berkley could not be held liable for copyright infringement . . . ; it argued that Naval therefore had at most a claim for breach-of-contract [and] argued that the profits attributed to it by Naval were inflated. . . . [On remand, the district judge] concluded that Naval was entitled to recover damages for copyright infringement, comprising actual damages suffered by Naval plus Berkley's profits "attributable to the infringement," 17 U.S.C. § 504(b).

The court calculated Naval's "actual damages from Berkley's wrongful pre-October 'publication' " as the profits Naval would have earned from hardcover sales in September 1985 if the competing paperback edition had not then been offered for sale. July 17 Order at 8. Noting the downward trend of hardcover sales of the Book from March through August 1985, the court found that there was no reason to infer that Naval's September 1985 sales would have exceeded its August 1985 sales. The court calculated Naval's lost sales as the difference between the actual hardcover sales for those two months, and awarded Naval \$35,380.50 as actual damages.

The district judge held that Berkley's profits "attributable to the infringement" were only those profits that resulted from "sales to customers who would not have bought the paperback but for the fact it became available in September." July 17 Order at 10. He found that most of the September paperback sales were made to buyers who would not have bought a hardcover edition in September, and therefore only those September sales that displaced hardcover sales were attributable to the infringement. Berkley's profit on the displacing copies totaled \$7,760.12, and the court awarded that amount to Naval. . . .

II. Discussion

A. *Naval's Claim of Copyright Infringement*

[The court rejected this claim because an exclusive licensee cannot be liable for infringing the copyright conveyed to it, even though it is liable for breach of contract.]

B. *Contract Damages . . .*

Since the purpose of damages for breach of contract is to compensate the injured party for the loss caused by the breach, 5 Corbin On Contracts § 1002, at 31 (1964), those damages are generally measured by the plaintiff's actual loss, see, e.g., Restatement (Second) of Contracts § 347 (1981). While on occasion the defendant's profits are used as the measure of damages, see, e.g., [Cincinnati Siemens–Lungren Gas Illuminating Co. v. Western Siemens–Lungren Co.](#), 152 U.S. 200, 204–07 (1894), . . . this generally occurs when those profits tend to define the plaintiff's loss, for an award of the defendant's profits where they greatly exceed the plaintiff's loss and there has been no tortious conduct on the part of the defendant would tend to be punitive, and punitive awards are not part of the law of contract damages. See generally Restatement (Second) of Contracts § 356 comment *a*

(“The central objective behind the system of contract remedies is compensatory, not punitive.”); *id.* comment *b* (agreement attempting to fix damages in amount vastly greater than what approximates actual loss would be unenforceable as imposing a penalty); *id.* § 355 (punitive damages not recoverable for breach of contract unless conduct constituting the breach is also a tort for which such damages are recoverable).

Here, the district court found that Berkley’s alleged \$724,300 profits did not define Naval’s loss because many persons who bought the paperback in September 1985 would not have bought the book in hardcover but would merely have waited until the paperback edition became available. This finding is not clearly erroneous, and we turn to the question of whether the district court’s finding that Naval suffered \$35,380.50 in actual damages was proper.

In reaching the \$35,380.50 figure, the court operated on the premise that, but for the breach by Berkley, Naval would have sold in September the same number of hardcover copies it sold in August. Berkley challenges that premise as speculative and argues that since Naval presented no evidence as to what its September 1985 sales would have been, Naval is entitled to recover no damages. It argues alternatively that the court should have computed damages on the premise that sales in the second half of September, in the absence of Berkley’s premature release of the paperback edition, would have been made at the same rate as in the first half of September. Evaluating the district court’s calculation of damages under the clearly erroneous standard of review, . . . we reject Berkley’s contentions.

The record showed that, though there was a declining trend of hardcover sales of the Book from March through August 1985, Naval continued to sell its hardcover copies through the end of 1985, averaging some 3,000 copies a month in the latter period.^b It plainly was not error for the district court to find that the preponderance of the evidence indicated that Berkley’s early shipment of 1,400,000 copies of its paperback edition, some 40% of which went to retail outlets and led to the Book’s rising close to the top of the paperback bestseller lists before the end of September 1985, caused Naval the loss of some hardcover sales prior to October 1985.

As to the quantification of that loss, we think it was within the prerogative of the court as finder of fact to look to Naval’s August 1985 sales. Though there was no proof as to precisely what the unimpeded volume of hardcover sales would have been for the entire month of September, any such evidence would necessarily have been hypothetical. But it is not error to lay the normal uncertainty in such hypotheses at the door of the wrongdoer who altered the proper course of events, instead of at the door of the injured party. See, e.g., [Lamborn v. Dittmer](#), 873 F.2d 522, 532-33 (2d Cir. 1989); [Lee v. Joseph E. Seagram & Sons, Inc.](#), 552 F.2d 447, 455-56 (2d Cir. 1977). . . . See generally . . . Restatement (Second) of Contracts § 352 comment *a* (“Doubts are generally resolved against the party in breach.”). The court was not required to use as the starting point for its calculations Naval’s actual sales in the first half of September, *i.e.*, those made prior to the first retail sale of the paperback edition. Berkley has not called to our attention any evidence in the record to indicate that the sales in a given month are normally spread evenly through that month. Indeed, it concedes that “[t]o a large degree, book sales depend on public whim and are notori-

^b It is unclear where Judge Kearse got the figure of only “some 3,000 copies a month” used in the paragraph after the next, but it might be a misprint for 30,000, an approximation of the August figure.

ously unpredictable. . . .” (Berkley brief on appeal at 31 n. 15.) Thus, nothing in the record foreclosed the possibility that, absent Berkley’s breach, sales of hardcover copies in the latter part of September would have out-paced sales of those copies in the early part of the month. Though the court accurately described its selection of August 1985 sales as its benchmark as “generous[],” it was not improper, given the inherent uncertainty, to exercise generosity in favor of the injured party rather than in favor of the breaching party.

In all the circumstances, we cannot say that the district court’s calculation of Naval’s damages was clearly erroneous. . . .

Conclusion

. . . For the foregoing reasons, we reverse so much of the judgment as granted Naval \$7,760.12 as an award of Berkley’s profits. In all other respects, the judgment is affirmed.

NOTES

(1) *Measuring Promisee’s Loss*. How did the district court go wrong in awarding Berkley’s profits on pre-October paperback sales to Naval Institute? How does that award square with protecting Naval’s expectation interest? How does it square with the assumption that the law’s concern is with relief of promisees and not punishment of promisors?

(2) *Conceptualizing Disgorgement*. Are there any cases where “the defendant’s profits . . . tend to define the plaintiff’s loss,” as Judge Kearse put it? Professor E. Allan Farnsworth^c described such cases, like *Cincinnati Siemens-Lungren* cited in *Naval Institute*, as follows:

“Suppose that a seller of a business makes a valid contract not to compete with the buyer and then breaks the covenant by operating a competing business. If the buyer claims damages . . . , the court will often receive evidence of the profits that the seller made from the competing business as evidence of the profit that the buyer lost as a result of the breach. But a court will not assume that the buyer could have made the same sales that the seller did. . . .” [Your Loss or My Gain? The Dilemma of the Disgorgement Principle in Breach of Contract Cases](#), 94 *Yale L.J.* 1339, 1366 (1985).

In other words, where the breaching promisor’s profits match the amount the promisee would have gained had the promise been performed, disgorgement and expectation produce the same figure, and disgorgement may be ordered. Nonetheless, the purposes of the two measures of recovery are distinct. Protecting the promisee’s expectation interest “undoes” the breach with regard to the promise; the effect of disgorgement is to “undo” the breach with regard to the promisor, who must forego the gains of the breach.

(3) *Reconsidering Disgorgement*. The disgorgement of profits is not uncommon in non-contract cases; as the district judge concluded in *Naval Insti-*

^c E. Allan Farnsworth (1928–2005) was an eminent contract law scholar, and from 1965 until his death, an editor of this casebook. He taught for fifty years at the Columbia Law School, from which he graduated in 1952. He represented the United States in matters of international trade law at the United Nations and at UNIDROIT. In 1971, following Professor Robert Braucher, Farnsworth became the Reporter for the Restatement, Second, of Contracts. His treatise *Farnsworth on Contracts*, kept current by Larry Garvin, is a standard text. In 1998, Prof. Farnsworth published *Changing Your Mind: The Law of Regretted Decisions*, and in 2004, *Alleviating Mistakes: Reversal and Forgiveness for Flawed Perceptions*.

tute, “Naval was entitled to recover damages for copyright infringement, comprising actual damages suffered by Naval *plus Berkley’s profits* ‘attributable to the infringement.’ 17 U.S.C. § 504(b).” This provision of the Copyright Act requires the infringer to disgorge profits to prevent the infringer from unfairly benefiting from a wrongful act.

If the measure of disgorgement damages is conceptualized not from the perspective of the *promisee* but from the perspective of the breaching promisor, then disgorgement even in contract cases may not be quite so uncommon. From this perspective, the consequence of disgorgement is to put breaching promisors (rather than injured promisees) in the position they would have been in had the contract been performed. See Steven Thel and Peter Siegelman, *You Do Have to Keep Your Promises: A Disgorgement Theory of Contract Remedies*, 52 *Wm. & Mary L. Rev.* 1181 (2011). Examples include specific performance (where disgorgement and expectation clearly merge) and the UCC remedy of cover, discussed in Chapter 7.

(4) *Fault*. As we saw in *Naval Institute*, the plaintiff in a contract action must prove the actual amount of damages it has suffered in order to recover, and this Naval had some trouble doing: the amount of profits it would have earned was uncertain. In finding that Naval had come close enough, Judge Kearse stated that “it is not error to lay the normal uncertainty . . . at the door of the wrongdoer who altered the proper course of events, instead of at the door of the injured party.” Should the reason a party fails to perform matter in the assessment of damages? Should the law care if the breach is willful or innocent, deliberate or unavoidable? Look for instances where fault appears to signify in the application of a contract rule despite the fundamental assumption mentioned earlier that the law is not generally concerned with the punishment of promisors.

(5) *Puzzler*. Why was the transaction in *Naval Institute* not governed by Article 2 of the Code?

THREE PROTECTED INTERESTS

When determining a remedy for a breach of contract, courts typically seek to put the promisee in the position it would have been in had the promise been kept. One way to accomplish this aim is for courts to compel performance of exactly what was promised, using the remedy known as specific performance. However, specific performance is often unavailable (promised goods may be no longer available) or undesired (would young Hawkins have wanted Dr. McGee to give it another try?). In addition, ordering a party to do what was promised might require continuing judicial supervision, a task courts are reluctant and perhaps ill-equipped to take on, especially when the performance involves a service or extends over time. These considerations lead to another assumption animating contract remedies in the United States: the appropriate form of relief is compensation for the breach, rather than requiring the promisor to perform. Courts order specific performance only sparingly, and in cases where monetary compensation is “inadequate.” See Restatement § 359. The classic case for specific enforcement concerns the sale of land, since courts have traditionally regarded each tract of land as unique and therefore not susceptible to substitution.

If the law seeks to remedy breach by compensating the promisee, what amount of money should the promisor pay? We have already encountered one answer: whatever it takes to protect the promisee's expectation interest. In that case the award should be just enough money to make the promisee as well off as actual performance would have made her. On this account, the promisee's injury consists in being worse off than if the promise had been performed, and expectation damages "undo" the effect of breach on the promisee.

Two other commonly pursued interests are *reliance* and *restitution*. A promisee has a reliance interest if he has changed his position to his detriment by relying on the promise. The promisee may, for example, have incurred expenses in preparing to perform his part of the deal. The promisee's injury consists of being worse off than if the promise had not been made in the first place. Reliance damages protect the promisee's interest in "being reimbursed for loss caused by reliance." Restatement § 344(b). As that section explains, reliance damages put the promisee "in as good a position as he would have been in had the contract not been made."

The promisee has a restitution interest to the extent that the promisee conferred a benefit on the promisor. The promisee may, for example, have given the promisor a down payment or performed some work before being paid anything. Restatement § 344(c) describes the restitution interest as the promisee's "interest in having restored to him any benefit that he has conferred on the other party." Judicial remedies that protect this interest have the effect of "unwinding" the promise by putting the *promisor* in the position in which she would have been had the promise not been made. These may include damages for the amount of the unjust enrichment, rescission of the contract, or even disgorgement of any profits made as a result of the breach. See Restatement (Third) of Restitution and Unjust Enrichment §§ 37–39. For more on these interests, see the pioneering article cited by the court in the following case, [Lon Fuller & William Perdue, Jr., The Reliance Interest in Contract Damages, 46 Yale L.J. 52, 53–57 \(1936\)](#). For criticism and expansion, see [Richard Craswell, Against Fuller and Perdue, 67 U. Chi. L. Rev. 99 \(2000\)](#) and [Avery Katz, Reflections on Fuller and Perdue's The Reliance Interest in Contract Damages: A Positive Economic Framework, 21 U. Mich. J.L. Reform 541, 542–47 \(1988\)](#).

In the next case, *Sullivan v. O'Connor*, the Supreme Judicial Court of Massachusetts considered how the three interests—expectation, reliance, and restitution—play out in the context of an action brought against a cosmetic surgeon for his failure to improve the plaintiff's appearance as he had promised to do. Our focus in *Sullivan* is not on the promise, as it was in *Hawkins*, but on the nature of the remedy.

Sullivan v. O'Connor

Supreme Judicial Court of Massachusetts, 1973.
[363 Mass. 579, 296 N.E.2d 183.](#)

[Alice Sullivan alleged she had entered into a contract with Dr. James O'Connor for plastic surgery "to enhance her beauty and improve her nose," but that as a result of the surgery, her appearance had been worsened. She charged him with negligence and with breach of contract. A jury awarded her \$13,500 on the latter count, rejecting her charge of negligence. The evidence provided support for findings as follow. O'Connor had promised Sul-

livan that, in two operations, he would make her nose shorter and more pleasing in relation to her other features. Having failed in that, he performed a third operation. Sullivan remained disfigured; and her appearance could not be improved by further surgery. Sullivan had paid a fee to O'Connor, and hospital expenses, for a total of \$622.65. She was a professional entertainer, as O'Connor had known. She failed to demonstrate, however, that she had lost employment by reason of her change of appearance.

O'Connor appealed, contending that the trial judge had erred in instructing the jury about the issue of damages. Sullivan had also objected to those instructions, on the ground that the judge had not instructed the jury that she was entitled to the difference between the value of her nose as promised and the diminished value of her nose after the operations. However, Sullivan indicated on appeal that she was willing to waive that objection if the appellate court denied O'Connor's appeal.

The opinion describes the instructions about damages given to the jury, and O'Connor's objections to them.]

■ KAPLAN, JUSTICE. . . . The judge instructed the jury, first, that the plaintiff was entitled to recover her out-of-pocket expenses incident to the operations. Second, she could recover the damages flowing directly, naturally, proximately, and foreseeably from the defendant's breach of promise. These would comprehend damages for any disfigurement of the plaintiff's nose—that is, any change of appearance for the worse—including the effects of the consciousness of such disfigurement on the plaintiff's mind, and in this connection the jury should consider the nature of the plaintiff's profession. Also consequent upon the defendant's breach, and compensable, were the pain and suffering involved in the third operation, but not in the first two. As there was no proof that any loss of earnings by the plaintiff resulted from the breach, that element should not enter into the calculation of damages.

By his exceptions the defendant contends that the judge erred in allowing the jury to take into account anything but the plaintiff's out-of-pocket expenses (presumably at the stipulated amount). The defendant excepted to the judge's refusal of his request for a general charge to that effect, and, more specifically, to the judge's refusal of a charge that the plaintiff could not recover for pain and suffering connected with the third operation or for impairment of the plaintiff's appearance and associated mental distress.

The plaintiff on her part excepted to the judge's refusal of a request to charge that the plaintiff could recover the difference in value between the nose as promised and the nose as it appeared after the operations. However, the plaintiff in her brief expressly waives this exception and others made by her in case this court overrules the defendant's exceptions; thus she would be content to hold the jury's verdict in her favor.

We conclude that the defendant's exceptions should be overruled . . .

[In an omitted part of the decision, the Court discussed whether a doctor's promise should be unenforceable on policy grounds, concluding that the law allows "actions based on alleged contract, but insist[s] on clear proof . . . that a given result was promised." The Court then turned to the question of damages.]

If an action on the basis of contract is allowed, we have next the question of the measure of damages to be applied where liability is found. Some

cases have taken the simple view that the promise by the physician is to be treated like an ordinary commercial promise, and accordingly that the successful plaintiff is entitled to a standard measure of recovery for breach of contract—“compensatory” (“expectancy”) damages, an amount intended to put the plaintiff in the position he would be in if the contract had been performed, or, presumably, at the plaintiff’s election, “restitution” damages, an amount corresponding to any benefit conferred by the plaintiff upon the defendant in the performance of the contract disrupted by the defendant’s breach. See Restatement: Contracts § 329 and comment *a*, §§ 347, 384(1). Thus in *Hawkins v. McGee*, 84 N.H. 114, 146 A. 641, the defendant doctor was taken to have promised the plaintiff to convert his damaged hand by means of an operation into a good or perfect hand, but the doctor so operated as to damage the hand still further. The court, following the usual expectancy formula, would have asked the jury to estimate and award to the plaintiff the difference between the value of a good or perfect hand, as promised, and the value of the hand after the operation. (The same formula would apply, although the dollar result would be less, if the operation had neither worsened nor improved the condition of the hand.) If the plaintiff had not yet paid the doctor his fee, that amount would be deducted from the recovery. There could be no recovery for the pain and suffering of the operation, since that detriment would have been incurred even if the operation had been successful; one can say that this detriment was not “caused” by the breach. But where the plaintiff by reason of the operation was put to more pain than he would have had to endure, had the doctor performed as promised, he should be compensated for that difference as a proper part of his expectancy recovery. It may be noted that on an alternative count for malpractice the plaintiff in the *Hawkins* case had been nonsuited; but on ordinary principles this could not affect the contract claim, for it is hardly a defense to a breach of contract that the promisor acted innocently and without negligence. The New Hampshire court further refined the *Hawkins* analysis in *McQuaid v. Michou*, 85 N.H. 299, 157 A. 881, all in the direction of treating the patient-physician cases on the ordinary footing of expectancy. . . .

Other cases, including a number in New York, without distinctly repudiating the *Hawkins* type of analysis, have indicated that a different and generally more lenient measure of damages is to be applied in patient-physician actions based on breach of alleged special agreements to effect a cure, attain a stated result, or employ a given medical method. This measure is expressed in somewhat variant ways, but the substance is that the plaintiff is to recover any expenditures made by him and for other detriment (usually not specifically described in the opinions) following proximately and foreseeably upon the defendant’s failure to carry out his promise. *Robins v. Finestone*, 308 N.Y. 543, 546, 127 N.E.2d 330. . . . This, be it noted, is not a “restitution” measure, for it is not limited to restoration of the benefit conferred on the defendant (the fee paid) but includes other expenditures, for example, amounts paid for medicine and nurses; so also it would seem according to its logic to take in damages for any worsening of the plaintiff’s condition due to the breach. Nor is it an “expectancy” measure, for it does not appear to contemplate recovery of the whole difference in value between the condition as promised and the condition actually resulting from the treatment. Rather the tendency of the formulation is to put the plaintiff back in the position he occupied just before the parties entered upon the agreement, to compensate him for the detriments he suffered in reliance upon the agreement. This kind of intermediate pattern of

recovery for breach of contract is discussed in the suggestive article by Fuller and Perdue, [The Reliance Interest in Contract Damages](#), 46 *Yale L.J.* 52, 373, where the authors show that, although not attaining the currency of the standard measures, a “reliance” measure has for special reasons been applied by the courts in a variety of settings, including noncommercial settings. See 46 *Yale L.J.* at 396–401.¹

For breach of the patient-physician agreements under consideration, a recovery limited to restitution seems plainly too meager, if the agreements are to be enforced at all. On the other hand, an expectancy recovery may well be excessive. The factors, already mentioned, which have made the cause of action somewhat suspect, also suggest moderation as to the breadth of the recovery that should be permitted. Where, as in the case at bar and in a number of the reported cases, the doctor has been absolved of negligence by the trier, an expectancy measure may be thought harsh. We should recall here that the fee paid by the patient to the doctor for the alleged promise would usually be quite disproportionate to the putative expectancy recovery. To attempt, moreover, to put a value on the condition that would or might have resulted, had the treatment succeeded as promised, may sometimes put an exceptional strain on the imagination of the fact finder. As a general consideration, Fuller and Perdue argue that the reasons for granting damages for broken promises to the extent of the expectancy are at their strongest when the promises are made in a business context, when they have to do with the production or distribution of goods or the allocation of functions in the market place; they become weaker as the context shifts from a commercial to a noncommercial field. 46 *Yale L.J.* at 60–63.

There is much to be said, then, for applying a reliance measure to the present facts, and we have only to add that our cases are not unreceptive to the use of that formula in special situations. We have, however, had no previous occasion to apply it to patient-physician cases.²

The question of recovery on a reliance basis for pain and suffering or mental distress requires further attention. We find expressions in the deci-

¹ Some of the exceptional situations mentioned where reliance may be preferred to expectancy are those in which the latter measure would be hard to apply or would impose too great a burden; performance was interfered with by external circumstances; the contract was indefinite. See 46 *Yale L.J.* at 373–386; 394–396.

² In *Mt. Pleasant Stable Co. v. Steinberg*, 238 *Mass.* 567, 131 *N.E.* 295, the plaintiff company agreed to supply teams of horses at agreed rates as required from day to day by the defendant for his business. To prepare itself to fulfill the contract and in reliance on it, the plaintiff bought two “Cliest” horses at a certain price. When the defendant repudiated the contract, the plaintiff sold the horses at a loss and in its action for breach claimed the loss as an element of damages. The court properly held that the plaintiff was not entitled to this item as it was also claiming (and recovering) its lost profits (expectancy) on the contract as a whole. Cf. *Noble v. Ames Mfg. Co.*, 112 *Mass.* 492. (The loss on sale of the horses is analogous to the pain and suffering for which the patient would be disallowed a recovery in *Hawkins v. McGee*, 84 *N.H.* 114, 146 *A.* 641, because he was claiming and recovering expectancy damages.) The court in the *Mt. Pleasant* case referred, however, to *Pond v. Harris*, 113 *Mass.* 114, as a contrasting situation where the expectancy could not be fairly determined. There the defendant had wrongfully revoked an agreement to arbitrate a dispute with the plaintiff (this was before such agreements were made specifically enforceable). In an action for the breach, the plaintiff was held entitled to recover for his preparations for the arbitration which had been rendered useless and a waste, including the plaintiff’s time and trouble and his expenditures for counsel and witnesses. The context apparently was commercial but reliance elements were held compensable when there was no fair way of estimating an expectancy. See, generally, annotation, 17 *A.L.R.2d* 1300. A noncommercial example is *Smith v. Sherman*, 4 *Cush.* 408, 413–414, suggesting that a conventional recovery for breach of promise of marriage included a recompense for various efforts and expenditures by the plaintiff preparatory to the promised wedding. . . .

sions that pain and suffering (or the like) are simply not compensable in actions for breach of contract. The defendant seemingly espouses this proposition in the present case. True, if the buyer under a contract for the purchase of a lot of merchandise, in suing for the seller's breach, should claim damages for mental anguish caused by his disappointment in the transaction, he would not succeed; he would be told, perhaps, that the asserted psychological injury was not fairly foreseeable by the defendant as a probable consequence of the breach of such a business contract. See Restatement of Contracts, § 341, and comment *a*. But there is no general rule barring such items of damage in actions for breach of contract. It is all a question of the subject matter and background of the contract, and when the contract calls for an operation on the person of the plaintiff, psychological as well as physical injury may be expected to figure somewhere in the recovery, depending on the particular circumstances. The point is explained in *Stewart v. Rudner*, 349 Mich. 459, 469, 84 N.W.2d 816. Cf. *Frewen v. Page*, 238 Mass. 499, 131 N.E. 475; *McClellan v. University Club*, 327 Mass. 68, 97 N.E.2d 174. Again, it is said in a few of the New York cases, concerned with the classification of actions for statute of limitations purposes, that the absence of allegations demanding recovery for pain and suffering is characteristic of a contract claim by a patient against a physician, that such allegations rather belong in a claim for malpractice. See *Robins v. Finestone*, 308 N.Y. 543, 547, 127 N.E.2d 330; *Budoff v. Kessler*, 2 A.D.2d 760, 153 N.Y.S.2d 654. These remarks seem unduly sweeping. Suffering or distress resulting from the breach going beyond that which was envisaged by the treatment as agreed, should be compensable on the same ground as the worsening of the patient's condition because of the breach. Indeed it can be argued that the very suffering or distress "contracted for"—that which would have been incurred if the treatment achieved the promised result—should also be compensable on the theory underlying the New York cases. For that suffering is "wasted" if the treatment fails. Otherwise stated, compensation for this waste is arguably required in order to complete the restoration of the status quo ante.³

In the light of the foregoing discussion, all the defendant's exceptions fail: the plaintiff was not confined to the recovery of her out-of-pocket expenditures; she was entitled to recover also for the worsening of her condition,⁴ and for the pain and suffering and mental distress involved in the third operation. These items were compensable on either an expectancy or a reliance view. We might have been required to elect between the two

³ Recovery on a reliance basis for breach of the physician's promise tends to equate with the usual recovery for malpractice, since the latter also looks in general to restoration of the condition before the injury. But this is not paradoxical, especially when it is noted that the origins of contract lie in tort. See Farnsworth, *The Past of Promise: An Historical Introduction to Contract*, 69 Col. L. Rev. 576, 594–596; Breitel, J. in *Stella Flour & Feed Corp. v. National City Bank*, 285 App.Div. 182, 189, 136 N.Y.S.2d 139 (dissenting opinion). A few cases have considered possible recovery for breach by a physician of a promise to sterilize a patient, resulting in birth of a child to the patient and spouse. If such an action is held maintainable, the reliance and expectancy measures would, we think, tend to equate, because the promised condition was preservation of the family status quo. . . .

It would, however, be a mistake to think in terms of strict "formulas." For example, a jurisdiction which would apply a reliance measure to the present facts might impose a more severe damage sanction for the wilful use by the physician of a method of operation that he undertook not to employ.

⁴ That condition involves a mental element and appraisal of it properly called for consideration of the fact that the plaintiff was an entertainer. Cf. *McQuaid v. Michou*, 85 N.H. 299, 303–304, 157 A. 881 (discussion of continuing condition resulting from physician's breach).

views if the pain and suffering connected with the first two operations contemplated by the agreement, or the whole difference in value between the present and the promised conditions, were being claimed as elements of damage. But the plaintiff waives her possible claim to the former element, and to so much of the latter as represents the difference in value between the promised condition and the condition before the operations.

Plaintiff's exceptions waived. Defendant's exceptions overruled.

NOTES

(1) *Applying the Interests.* Assign the following round numbers to Sullivan's claim: doctor's fee \$300; hospital fee per operation \$100; pain and suffering per operation \$3,000; increase in value of appearance if enhanced as promised \$20,000; loss in value of appearance due to disfigurement \$10,000. What would be the amount of Sullivan's claim if based on her restitution interest? On her reliance interest? On her expectation interest? How did the trial court calculate her damages?

(2) *Lost Opportunities as Reliance.* It can be argued that by relying on O'Connor, Sullivan lost the opportunity to deal with another doctor, who would have done a competent job so that she would have been in the same position as if O'Connor had performed as promised. How should this form of loss be characterized? If compensable, how should it be measured?

Suppose Sullivan could prove she had lost professional engagements as a result of Dr. O'Connor's operations. Are these lost opportunities in the same sense as losing the opportunity to engage a more competent surgeon? Should they be recoverable as reliance damages? Are they too speculative? Keep your eyes open for the relatively rare instances where courts take account of lost opportunities.

(3) *The Case of the Request for Restitution.* Not all plaintiffs have shared the view of the court in *Sullivan* that "a recovery limited to restitution seems plainly too meager." When two oil companies sued the United States for its breach of lease contracts giving them rights to explore for and develop oil off the North Carolina coast, what they sought was restitution of \$156 million that they had paid in return for the contracts. Their award of summary judgment was reversed by the Court of Appeals. The Supreme Court reversed and remanded.

The Court observed that when the United States makes contracts, its rights and duties are governed generally by the law applicable to contracts between private individuals, as reflected in the Restatement.

We agree that the Government broke its promise . . . and it must give the companies their money back. . . . And it must do so whether the contracts would, or would not, ultimately have proved financially beneficial to the companies. The Restatement illustrates this point as follows:

A contracts to sell a tract of land to B for \$100,000. After B has made a part payment of \$20,000, A wrongfully refuses to transfer title. B can recover the \$20,000 in restitution. The result is the same even if the market price of the land is only \$70,000, so that performance would have been disadvantageous to B. . . .

If a lottery operator fails to deliver a purchased ticket, the purchaser can get his money back—whether or not he eventually would have won the lottery. And if one party to a contract . . . advances the other party money, principles of restitution normally require the latter, upon repudiation, to refund that money.

[Mobil Oil Exploration & Producing Southeast v. United States](#), 530 U.S. 604, 624 (2000) (Breyer, J.).

THE ECONOMICS OF REMEDIES: AN INTRODUCTORY NOTE

As noted on p. ____, Justice Holmes, Jr. expressed his concern about the confusion of law and morality in no uncertain terms. Holmes advocated an approach to contracts informed more by external legal sanctions than by moral intuitions: “The duty to keep a contract at common law means a prediction that you must pay damages if you do not keep it, and nothing else.” Oliver Wendell Holmes, Jr., *The Path of the Law*, 10 Harv. L. Rev. 457, 458 (1897). The promisor’s obligation under this approach was reduced to a choice between performing a specified act and paying for its non-performance.

Though often characterized as immoral, Holmes’s “perform-or-pay” approach might be better understood as an *amoral* system, where “[p]rices do the work of morals” in guiding behavior.^d Holmes joins a long line of political theorists—including Hobbes, Bentham and Adam Smith—all of whom understood sanctions as useful means of enlisting self-interested individual behavior to promote social welfare. Consider in this regard this excerpt from Adam Smith in *The Wealth of Nations*:

[M]an has almost constant occasion for the help of his brethren, and it is vain for him to expect it from their benevolence only. He will be more likely to prevail if he can interest their self love in his favour, and shew them that it is for their own advantage to do for him what he requires of them. Whoever offers to another a bargain of any kind, proposes to do this: Give me that which I want, and you shall have this which you want, is the meaning of every such offer; and it is in this manner that we obtain from one another the far greater part of those good offices which we stand in need of. . . . We address ourselves, not to their humanity but to their self love, and never talk to them of our own necessities but of their advantages. Nobody but a beggar chooses to depend chiefly upon the benevolence of his fellow citizens.

Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations* 11 (1811 ed., bk. 1, ch. II).

Building on Smith’s claim to mutual gain through self-interested motivations and Holmes’s perform-or-pay vision of contracts, scholars from a school of thought known as law and economics have developed a distinctive approach to contract remedies. This school of thought, which has achieved considerable influence over the past several decades, emphasizes the incentive effects of legal remedies. Most notably, law and economics scholars observe that a promisor will exercise an “option” to breach and pay expecta-

^d Samuel Bowles, *Policies Designed for Self-interested Citizens May Undermine “The Moral Sentiments”*: Evidence from Economic Experiments, 320 *Science* 1605 (2008).

tion damages instead of performing only when it is economically efficient to do so. That is, she will breach when her gain from breaching exceeds the amount of damages she will have to pay to leave the promisee just as well off as he would have been had the promisor performed. In principle, then, breaches of this sort make promisors better off without making promisees worse off.

This observation, known as the “efficient breach hypothesis,” may be illustrated with a simple example. Say a promisor has promised to sell a piece of machinery to a promisee. The machinery will cost the promisor \$300 to produce and is worth \$1,000 to the promisee (the maximum amount the promisee is willing to pay for it). Exchange will produce \$700 of surplus since the promisee’s value of the machinery (\$1,000) is greater than the promisor’s costs to produce it (\$300). Say they agreed on a price of \$600. This means the promisor gets \$300 of the surplus (the \$600 price minus her costs of \$300) and the promisee gets \$400 (the \$1000 value to him of the machinery minus the \$600 price). At the time they enter into the contract, the performance is mutually advantageous.

Now the twist. Assume that at some date before performance a second buyer approaches the promisor and offers \$1200 for the machinery. The promisor has only one unit and cannot procure another. Suppose further that the promisee and the second buyer are unable to transact with each other, perhaps because neither knows of the other’s existence and it would be too costly for them to identify each other. The question then becomes, should the promisor sell the machinery to the first buyer (the promisee) as agreed or should he sell the machinery to the second buyer at the higher price? The efficient breach hypothesis says the latter course is the better economic option for all parties involved. Why? The promisee will be fully compensated for his expectation by the payment of \$400 in damages (since that is the amount that the promisee would have gained from the promisor’s full performance). The second buyer gets the machinery that she values at least as much as \$1200. Finally, if the promisor had performed the original contract she would have gained \$300 (\$600 sale price minus \$300 cost to produce), but by breaching the contract and selling to the second buyer the promisor is left with a gain of \$500, after paying expectation damages to the promisee (\$1200 sale price minus \$300 cost to produce minus \$400 damages paid to the promisee). This suggests that, under the assumptions of this example, the promisor can break her promise and enjoy a gain, without leaving the promisee any worse off.

Transactions that make no one worse off, while making someone else better off, are called Pareto-improving, so named after the 19th century Italian economist Vilfredo Pareto. Pareto-improvement is an important measure of what economists identify as efficiency, but it is not the only measure. Suppose that, in the example above, the promisor breaks her promise to the promisee and sells the machinery for \$1200. As we noticed, the machinery then ends up in the hands of the second buyer, who values it more than the promisee. At this point, even *without* compensating the promisee, the result satisfies another conception of efficiency known as Kaldor–Hicks efficiency. Note, however, that unless the promisee receives at least his expectation damages, this outcome would not be Pareto-improving. Without this compensation, the promisee is worse off on account of the breach. Compensating the promisee for the breach is irrelevant under the Kaldor–Hicks approach, so long as the promisor’s gains from the breach exceed the promisee’s loss. Yet we should not lose sight of distinc-

tions between economic theories and rules of law. The irrelevance of compensating the promisee may be a plausible feature of economic efficiency—it is certainly not irrelevant to law.

Our discussion of efficiency thus far has focused only on the moment when a party decides whether to breach. Economics, however, is the study of incentives broadly conceived and the question of whether parties have incentive to act efficiently will arise at every point where contracting parties make choices. These include searching for contractual partners, entering into a contract, relying on a contract, and so forth. Economic analysis cannot identify a single remedy, whether money damages or specific performance, that satisfies the demands of efficiency at all points concerning the transaction. This does not deprive economic analysis of value, however; it merely highlights the inevitable trade-offs that occur even within the singular perspective of efficiency.

The economics of remedies is essential to the study of contracts. Contract remedies provide incentives that guide behavior. At the same time, of course, other principles, such as morality and fairness, also guide contractual behavior. For example, the promisor who has been offered \$1200 by the second buyer might decide that the harm to her reputation and self-esteem of breaking her promise to sell the machinery to the promisee is worth more to her than the \$200 gain. On some accounts, this may be factored into her economic calculation of the cost to her of the breach. On other accounts, her decision is guided by independent moral considerations not reducible to an economic calculus. Cf. Lon L. Fuller, *The Law in Quest of Itself* 93 (1940), on the Holmesian “bad man”: “[I]t will be noted that it is a peculiar sort of bad man who is worried about judicial decrees and is indifferent to extra-legal penalties, who is concerned about a fine of two dollars but apparently not about the possible loss of friends and customers.” We do not have to choose one approach over the other for our study of contracts; behavior is guided by many considerations. Whether economic efficiency is compatible with other normative objectives, like fairness, is an interesting question, but one we needn’t answer here. See [Richard R.W. Brooks, *The Efficient Performance Hypothesis*, 116 *Yale L.J.* 568 \(2006\)](#), [Daniel Friedmann, *The Efficient Breach Fallacy*, 18 *J. Legal Stud.* 1, 13–14 \(1989\)](#).

NOTES

(1) *Efficient Breach and the Bench*. How has the concept of efficient breach been received in practice by judges? Since the early 1980s, there have been a hundred or so cases that expressly employ the term. For example, Judge Richard Posner,^e discussing efficient breach in relation to an award of punitive damages, observed that “if the promisor has discovered that his performance is worth more to someone else,” then “efficiency is promoted by allowing him to break his promise, provided he makes good on the promisee’s actual losses. If he is forced to pay more than that, an efficient breach may be deterred, and the law doesn’t want to bring about that result.” [Patton v. Mid-Continent Systems, Inc.](#), 841 F.2d 742, 750 (7th Cir. 1988).

^e Richard Allen Posner (1939–), after clerking for Justice William Brennan and occupying several legal positions in the federal government, taught briefly at Stanford University Law School and then for more than a decade at the University of Chicago Law School. In 1981 he was appointed to the United States Court of Appeals for the Seventh Circuit, where from 1993 to 2000 he served as Chief Judge. His many books include the influential *Economic Analysis of Law*. Judge Posner maintains a personal website, <http://home.uchicago.edu/~rposner/>.

Other courts have also taken account of the concept. In refusing to enforce a contract upon a finding that one company had struck too hard a bargain with another, a California court stated: "Hard bargaining, 'efficient' breaches and reasonable settlements of good faith disputes are all acceptable, even desirable, in our economic system. That system can be viewed as a game in which everybody wins, to one degree or another, so long as everyone plays by the common rules. Those rules are not limited to precepts of rationality and self-interest. They include equitable notions of fairness and propriety which preclude the wrongful exploitation of business exigencies to obtain disproportionate exchanges of values. Such exchanges make a mockery of freedom of contract and undermine the proper functioning of our economic system." *Rich and Whillock, Inc. v. Ashton Development, Inc.*, 157 Cal.App.3d 1154, 1159 (Ct. App. 1984).

How should "notions of fairness and propriety" guide the law of remedies? Have you seen examples of this in the cases so far?

(2) *The Economics of Naval Institute*. Suppose that in August, noting the downward trend in Naval's hardcover sales, Berkley had estimated that by jumping the gun and shipping its paperback edition early as it did, it would gain at least \$100,000 from pre-October sales while the loss to Naval would be no more than \$40,000. Assuming that its estimates were accurate, and that Naval receives an award for its expectation damages, what is the gain to Berkley by breaching its contract with Naval? What factors, financial and other, might affect Berkley's decision about whether or not to ship the paperbacks early and breach the contract?

PUNITIVE DAMAGES

White v. Benkowski

Supreme Court of Wisconsin, 1967.

37 Wis.2d 285, 155 N.W.2d 74.

[In 1962, Virgil and Gwynneth White bought a house that lacked its own water supply but was connected by pipes to a well on the adjacent property of Paul and Ruth Benkowski. The Whites entered into a written contract with the Benkowskis under which the Benkowskis promised to supply water to the Whites' home for ten years unless the municipality supplied it, the well became inadequate, or the Whites drilled their own well. In exchange, the Whites agreed to pay the Benkowskis \$3 a month and half the cost of any future repairs or maintenance. Although the relationship between the neighbors began as a friendly one, by 1964 it had deteriorated and become hostile. During March and June, the Benkowskis shut off the water supply on nine occasions for periods in the late afternoon and early evening that were, according to Mrs. White's records, well under an hour. Mr. Benkowski claimed this was done either to allow accumulated sand in the pipes to settle or to remind the Whites that their water use was excessive. The Whites sued the Benkowskis for breach of contract, seeking compensatory and punitive damages. The jury found the Benkowskis had shut off the water maliciously in order to harass the Whites. It awarded the Whites compensatory damages of \$10 and punitive damages of \$2,000. On motions after the verdict, the award was reduced to \$1 in compensatory damages and no punitive damages. The Whites appealed.]

■ WILKIE, JUSTICE. Two issues are raised on this appeal.

1. Was the trial court correct in reducing the award of compensatory damages from \$10 to \$1?
2. Are punitive damages available in actions for breach of contract?

Reduction of Jury Award

The evidence of damage adduced during the trial here was that the water supply had been shut off during several short periods. Three incidents of inconvenience resulting from these shut-offs were detailed by the plaintiffs. Mrs. White testified that the lack of water in the bathroom on one occasion caused an odor and that on two other occasions she was forced to take her children to a neighbor's home to bathe them. Based on this evidence, the court instructed the jury that:

“... in an action for a breach of contract the plaintiff is entitled to such damages as shall have been sustained by him which resulted naturally and directly from the breach if you find that the defendants did in fact breach the contract. Such damages include pecuniary loss and inconvenience suffered as a natural result of the breach and are called compensatory damages. In this case the plaintiffs have proved no pecuniary damages which you or the Court could compute. In a situation where there has been a breach of contract which you find to have damaged the plaintiff but for which the plaintiffs have proven no actual damages, the plaintiffs may recover nominal damages.

“By nominal damages is meant trivial—a trivial sum of money.”

Plaintiffs did not object to this instruction. In the trial court's decision on motions after verdict it states that the court so instructed the jury because, based on the fact that the plaintiffs paid for services they did not receive, their loss in proportion to the contract rate was approximately 25 cents. This rationale indicates that the court disregarded or overlooked Mrs. White's testimony of inconvenience. In viewing the evidence most favorable to the plaintiffs, there was some injury. The plaintiffs are not required to ascertain their damages with mathematical precision, but rather the trier of fact must set damages at a reasonable amount. Notwithstanding this instruction, the jury set the plaintiffs' damages at \$10. The court was in error in reducing that amount to \$1.

The jury finding of \$10 in actual damages, though small, takes it out of the mere nominal status. The award is predicated on an actual injury. This was not the situation present in *Sunderman v. Warnken*.¹ Here there was credible evidence which showed inconvenience and thus actual injury, and the jury's finding as to compensatory damages should be reinstated.

Punitive Damages

“If a man shall steal an ox, or a sheep, and kill it, or sell it; he shall restore five oxen for an ox, and four sheep for a sheep.”²

Over one hundred years ago this court held that, under proper circumstances, a plaintiff was entitled to recover exemplary or punitive damages.³ In Wisconsin compensatory damages are given to make whole the damage or injury suffered by the injured party. On the other hand, punitive damag-

¹ (1947), 251 Wis. 471, 29 N.W.2d 496.

² Exodus 22:1.

³ *McWilliams v. Bragg* (1854), 3 Wis. 377 (*424).

es are given “. . . on the basis of punishment to the injured party not because he has been injured, which injury has been compensated with compensatory damages, but to punish the wrongdoer for his malice and to deter others from like conduct.”⁴

Thus we reach the question of whether the plaintiffs are entitled to punitive damages for a breach of the water agreement. The overwhelming weight of authority supports the proposition that punitive damages are not recoverable in actions for breach of contract. In *Chitty on Contracts*, the author states that the right to receive punitive damages for breach of contract is now confined to the single case of damages for breach of a promise to marry.⁵

Simpson states: “Although damages in excess of compensation for loss are in some instances permitted in tort actions by way of punishment . . . in contract actions the damages recoverable are limited to compensation for pecuniary loss sustained by the breach.”⁶ Corbin states that as a general rule punitive damages are not recoverable for breach of contract.⁷

In Wisconsin, the early case of *Gordon v. Brewster*⁸ involved the breach of an employment contract. The trial court instructed the jury that if the nonperformance of the contract was attributable to the defendant’s wrongful act of discharging the plaintiff, then that would go to increase the damages sustained. On appeal, this court said that the instruction was unfortunate and might have led the jurors to suppose that they could give something more than actual compensation in a breach of contract case. We find no Wisconsin case in which breach of contract (other than breach of promise to marry) has led to the award of punitive damages.

Persuasive authority from other jurisdictions supports the proposition (without exception) that punitive damages are not available in breach of contract actions. This is true even if the breach, as in the instant case, is willful. Although it is well recognized that breach of a contractual duty may be a tort, in such situations the contract creates the relation out of which grows the duty to use care in the performance of a responsibility prescribed by the contract. Not so here. No tort was pleaded or proved.

Reversed in part by reinstating the jury verdict relating to compensatory damages and otherwise affirmed. Costs to appellant.

NOTES

(1) *Questions*. Why was only \$10 awarded to the Whites as compensatory damages? What did that amount represent? How was it calculated? How did the jury come up with the \$2,000 punitive damage award?

Why shouldn’t punitive damages be awarded in such a case? What effect would the availability of punitive damages have on parties tempted to breach their contracts? Would it make sense to award punitive damages in cases where the breach was malicious, as in *White*, or should the law be indifferent as to why a party fails to perform? Might the possibility of a punitive damage

⁴ *Malco, Inc. v. Midwest Aluminum Sales* (1961), 14 Wis.2d 57, 66, 109 N.W.2d 516, 521.

⁵ 1 *Chitty, Contracts*, (22d ed. 1961), p. 1339.

⁶ *Simpson, Contracts*, (2d ed. hornbook series), p. 394, sec. 195.

⁷ 5 *Corbin, Contracts*, p. 438, sec. 1077.

⁸ (1858), 7 Wis. 309 (*355).

award affect a party's decision not only whether to breach a contract, but also whether to enter it in the first place?

(2) *Nominal Damages*. A plaintiff who, like the Whites in the case above, proves a breach of contract but fails to prove damages is traditionally awarded nominal damages (six cents or one dollar); Judge Posner has observed that “for reasons we do not understand every victim of a breach of contract, unlike a tort victim, is [so] entitled.” [Chronister Oil Co. v. Unocal Ref. & Mktg.](#), 34 F.3d 462, 466 (7th Cir. 1994). Yet such an award serves as a declaration of the plaintiff's rights and may also carry with it an award of court costs.

(3) *Flirting with Punitive Damages*. Although not traditionally granted for breach of contract, punitive or exemplary damages may be granted for tortious conduct that is sufficiently “outrageous.” See [Restatement, Second, of Torts § 908](#) (1979). Some courts have departed from the strict rule that denies punitive damages for breach of contract when the breach is accompanied by “fraudulent” conduct or by an “independent” tort sufficiently outrageous to justify such damages. See generally [Restatement § 355](#); 3 *Farnsworth on Contracts* § 12.8 (3d ed.2004 & Supp.2013). The use of punitive damages has been noticeable, for example, in connection with claims against insurers for their regular refusal to provide coverage to or settle claims with their insured. See [Comunale v. Traders & Gen. Ins. Co.](#), 328 P.2d 198 (Cal. 1958); [Vernon Fire & Cas. Ins. Co. v. Sharp](#), 349 N.E.2d 173 (Ind. 1976).

In 1984, the Supreme Court of California suggested that a new tort of “bad faith breach” might extend beyond insurance cases to other contractual breaches. [Seaman's Direct Buying Service v. Standard Oil Company of California](#), 686 P.2d 1158 (Cal. 1984). While the suggestion triggered much litigation and academic discussion, four years later a differently composed state Supreme Court refused to apply *Seaman's* to an employer's discharge of an at-will employee, and denounced the “uncritical acceptance . . . of the insurance model into the employment context, without careful consideration of the fundamental policies underlying the development of tort and contract law in general or of significant differences between the insurer/insured and employer/employee relationships.” [Foley v. Interactive Data Corp.](#), 765 P.2d 373 (Cal. 1988). The following year, the Ninth Circuit stated that *Foley* “solidly reaffirms the notion that the bad faith denial of the existence of a contract is a cause of action wholly distinct from the breach of the covenant of good faith and fair dealing.” [Air-Sea Forwarders, Inc. v. Air Asia Co.](#), 880 F.2d 176, 187 (9th Cir. 1989).

Nonetheless, there are other distinct circumstances where a promisor's breach of promise may result in punitive damages. For example, when a promisor, at the time a promise is made, has no intention of performing the promise, the promisee may bring an action for promissory fraud. This cause of action is discussed more fully in Chapter 4 in the section on misrepresentation.

REMEDIES IN PRACTICE

In providing promisees relief through money damages, the law by and large ignores the costs of obtaining that relief. Of course, to some extent the cost of obtaining relief in court is subsidized by the availability of the public machinery of justice. Litigants are not charged, except as taxpayers, for the services of judges or juries in resolving their disputes. In addition, the suc-

successful claimant may ordinarily recover its court costs, such as filing fees, court reporter fees, and charges for the serving of process or subpoenas. Such costs are typically set by statute and are often modest in scope. See, for example, Col. Rev. Stat. Ann. § 13–17–202. But in contrast to the situation in many countries, the successful claimant in the United States is not generally allowed to recover its attorney’s fees from the losing party. Unless specifically provided for by the contract itself, even winning parties are left to pay their own, often substantial, lawyers’ fees, as well as other costs of litigation such as the cost of *enforcing* a judgment against an obdurate defendant. If litigation costs are not part of the typical damage recovery, expectation damages will not put the plaintiff in the same position as if the contract had been performed. See Restatement § 344(a). The inability to recover litigation costs helps explain why many contractual disputes are either settled out of court or not brought in the first place.

The reluctance to enlist law to settle disputes also introduces us to the concept of the “law in action” a phrase associated with the law and society approach to the study of contracts. A central premise of this more sociological approach is that doctrine and theory only get us so far in understanding how contract law actually works: “law in action” is contrasted with “law on the books.” As Stewart Macaulay discovered in his important 1963 study of practices among disputing businesses, much of what occurs following a breach of contract is “non-contractual”:

Disputes are frequently settled without reference to the contract or potential or actual legal sanctions. There is a hesitancy to speak of legal rights or to threaten to sue in these negotiations. Even where the parties have a detailed and carefully planned agreement which indicates what is to happen if, say, the seller fails to deliver on time, often they will never refer to the agreement but will negotiate a solution when the problem arises apparently as if there had never been any original contract.

Stewart Macaulay, *Non-Contractual Relations in Business: A Preliminary Study*, 28 *Am. Soc. Rev.* 55, 61 (1963).

Of course, non-contractual practices such as negotiation and modification tell only part of the story. In each of the cases in this book, the parties, or at least one of them, has chosen to litigate. Where the transaction is a substantial one between business firms, litigation is often justified because its costs are small in relation to the amount in dispute or because of the precedential value of a judicial decision. But what of the typical consumer transaction in which the stakes are often smaller, whether the aggrieved party is the merchant (often trying to collect) or the consumer (perhaps refusing to pay)?

Between the two, the merchant is typically in the better position. The merchant is more likely to engage professionals such as lawyers or trade associations to draft its contract, which may provide for liquidated damages and attorney’s fees. The merchant may also be able to provide for security, such as by taking a deposit where goods have not been delivered or by preserving the right to repossess goods that have been delivered. In contrast, the ordinary consumer is less likely to know or be able to afford a lawyer, and less likely to have specifically bargained for favorable contract terms or even to know what terms are favorable. For the argument that the more sophisticated “repeat players” in the legal system tend to acquire and maintain structural advantages over one-shot players, who infrequently participate in litigation and legal strategy, see [Marc Galanter, Why the “Haves”](#)

Come Out Ahead: Speculations on the Limits of Legal Change, 9 *Law & Society Review* 95 (1974). Of course, it is important to recognize that the big-guy/little-guy story of merchant versus consumer is not always an accurate dividing line for determining party sophistication and advantage. Small businesses, for example, typically behave like consumers (little guys) but are treated at law like large businesses. See Larry T. Garvin, *Small Business and the False Dichotomies of Contract Law*, 40 *Wake Forest L. Rev.* 295 (2005).

A variety of solutions, many procedural in nature, have been put forth to even out disparities in at least a consumer's ability to bring or to defend claims. One solution is to "sweeten the pot" by increasing the successful consumer's recovery through statutes that allow civil penalties, multiple (e.g., treble) damages, or attorney's fees. Other solutions include allowing consumers to join as claimants in class actions, providing free or inexpensive legal services, or authorizing public agencies, such as the Federal Trade Commission (FTC), to bundle and investigate bundled claims and to distribute any recovery to the aggrieved consumers; see discussion of Administrative Measures on p. 518. In 2012, as part of the Dodd-Frank Wall Street Reform and Consumer Protection Act, the Bureau of Consumer Protection was created within the FTC. Its stated aim is to "enhance consumer confidence by enforcing existing federal consumer protection laws" and to "empower consumers" by providing information about their statutory rights. See Bureau of Consumer Protection, <http://www.ftc.gov/bcp/consumer.shtm> (last visited Apr. 3, 2013).

Still other mechanisms for reducing the costs and complexities of litigation focus on the forum. Take, for instance, the provision of small claims, such as the New York Civil Court which has jurisdiction over civil matters not exceeding \$25,000. As stated on the Court's website:

"Our court is where everyday people come to resolve their everyday legal problems. Whether you are a local merchant, a consumer, a debtor, or a creditor, the Civil Court is dedicated to providing access to fair and efficient justice." <http://www.courts.state.ny.us/courts/nyc/smallclaims/index.shtml>.

Parties who seek redress in such courts typically represent themselves, appearing *pro se* (without the formal assistance of counsel). Another procedural mechanism, as suggested above, is the class action suit, in which multiple claimants come together to sue a common defendant. While the details of class litigation are left mainly for procedure courses, we consider some aspects of them in Chapter 6 in connection with mandatory arbitration clauses that *prohibit* their use.

Firms too have sought to simplify dispute resolution. One approach is the turn away from courts to methods of alternative dispute resolution (ADR). The most important of these is arbitration. According to Soia Mentschikoff, an early scholar of commercial arbitration in the United States, the four essential aspects of arbitration are that "(1) it is resorted to only by agreement of the parties; (2) it is a method not of compromising disputes but of deciding them; (3) the person making the decision has no formal connection with our system of courts; but (4) before the award is known it is agreed to be 'final and binding.'" Soia Mentschikoff, *The Significance of Arbitration—A Preliminary Inquiry*, 17 *Law & Contemp. Probs.* 698, 699 (1952). Arbitration is therefore a "creature of contract": parties choose their own scheme of dispute resolution. Proponents of arbitration claim speed, flexibility, increased confidentiality, decreased costs, and deci-

sion-maker expertise among its advantages. While these claims are sometimes contested, arbitration undeniably is becoming more important in dispute resolution. For example, international commercial arbitration has become the main way to resolve transnational commercial disputes.

In addition to its use in commercial disputes, transnational and domestic, arbitration clauses are increasingly incorporated into ordinary consumer and employment contracts by companies and employers. A series of recent U.S. Supreme Court cases interpreting these *mandatory* arbitration clauses has caused some commentators to fear that whatever the benefits of arbitration in general, mandatory arbitration may now be less an alternative mode of dispute resolution than the dominant mode, and that this in turn may endanger access to courts by would-be litigants. See [Jean R. Sternlight, *Tsunami: AT & T Mobility LLC v. Concepcion Impedes Access to Justice*, 90 Or. L. Rev. 703 \(2012\)](#). We will come back to the questions raised by mandatory arbitration in Chapter 6, when we discuss standard form contracts and unconscionability.

Finally, in addition to varying the forum in which disputes are resolved, certain industries have also created private, trade-specific codes to govern their disputes. Professor Lisa Bernstein has explained that in the cotton industry, for example, disputes are subject to arbitration in merchant tribunals that not only apply rules that are sensitive to the particularities of the cotton industry, but are quick and inexpensive. The cotton industry “has succeeded in creating and maintaining a private legal system in which transaction costs . . . and collection costs are low.” [Lisa Bernstein, *Private Commercial Law in the Cotton Industry: Creating Cooperation through Rules, Norms, and Institutions*, 99 Mich. L. Rev. 1724 \(2001\)](#).

NOTES

(1) *Efficient Breach and the Costs of Enforcement*. The efficient breach hypothesis ignores the cost to the parties of enforcing rights. But what if it is very costly for the promisee to hire an attorney in order to prove the promisor’s performance was defective, or to prove the amount of its own damages? How might taking those costs into account change the analysis?

(2) *The “Work of the Law Machine at the Margin.”* Professor Karl Llewellyn^f concluded “that the real major effect of law will be found not so much in the cases in which law officials actually intervene, nor yet in those in which such intervention is consciously contemplated as a possibility, but rather in contributing to, strengthening, stiffening attitudes toward performance as what is to be expected and what ‘is done’ This work of the law machine at the margin, in helping keep the level of social practice and expectation up to where it is, as against slow canker, is probably the most vital single aspect of contract law. For in this aspect each hospital case is a case with significance for the hundreds of thousands of normal cases.” [Llewellyn, *What Price Contract?—An Essay in Perspective*, 40 Yale L.J. 704, 725 n. 47 \(1931\)](#). For a discussion of the nonlegal sanctions that may encourage promisors to keep their promises, see

^f Karl Nickerson Llewellyn (1893–1962) practiced law in New York for two years, and taught law at Yale, Columbia, and Chicago law schools. One of the school of “legal realists,” Llewellyn was well-known for his contributions to the field of jurisprudence, and also to the fields of commercial law and contracts. He was Chief Reporter of the Uniform Commercial Code, and the author of many books, including *The Bramble Bush: On Our Law and Its Study*, which was written especially for first-year law students.

David Charny, [Nonlegal Sanctions in Commercial Relationships](#), 104 *Harv. L. Rev.* 373 (1990).

(3) *Bargaining in the Shadow of Law*. In considering “the work of law,” Llewellyn referred to cases in which legal intervention is “not consciously contemplated as a possibility.” But what is the work of law when legal action is contemplated or has already been commenced by one of the parties? Does law matter when parties decide to settle a dispute outside the courtroom? In an important 1979 article, Professors Robert Mnookin and Lewis Kornhauser suggested disputing parties often bargain with one another against the knowledge, or “in the shadow,” of what the law is likely to do if they do not agree. See Mnookin and Kornhauser, [Bargaining in the Shadow of the Law: The Case of Divorce](#), 88 *Yale L.J.* 950 (1979). In this way, the background legal rule—say, that fault will not be penalized—provide parties with certain bargaining chips, or “endowments,” and that these endowments, among other factors, enhance a party’s negotiating power. The concept of bargaining in the shadow of law provides another example of a behavioral or socio-legal approach, as law hovers over the process of dispute settlement.

SECTION 3. CONSIDERATION AS A BASIS FOR ENFORCEMENT

(A) FUNDAMENTALS OF CONSIDERATION

Departing from the premise that not all promises are legally enforceable, we quickly arrive at the basic question of how to determine which ones are. To address this question, we must begin with an historical perspective. Enforceability under early English law was closely tied to the common law actions of covenant, debt, and assumpsit and, even today, no adequate answer to our basic question can ignore this aspect of legal history.

The first of these actions, *covenant*, was used to enforce contracts made under seal. Once a written promise was sealed and delivered, the action of covenant was available to enforce it, and it made no difference whether the promisor had bargained for or received anything in exchange for the promise, or whether the promisee had in any way changed position in reliance on it. In medieval England, the seal was a piece of wax affixed to the document and bearing an impression identifying the person who had executed it. At first its use was confined to the nobility, but later it spread to commoners. With the growth of literacy and the use of the personal signature as a means of authentication, the requirement of formality was so eroded that a seal could consist of any written or printed symbol intended to serve as a seal. The word “Seal” and the letters “L.S.” (*locus sigilli*) were commonly used for this purpose.

Three functions performed by such legal formalities as the seal have been described by Professor Lon Fuller.[§] The first is “evidentiary,” that is, providing trustworthy evidence of the existence and terms of the contract in

[§] Lon L. Fuller (1902–1978) had a long teaching career at Oregon, Illinois, Duke, Columbia, and, for the last three decades of his life, at Harvard, where he taught contracts and jurisprudence. In philosophical works he presented alternatives to positivist attitudes toward law, sometimes using partly-fanciful cases in imaginary and contrasting opinions. See, e.g., Fuller, [The Case of the Speluncean Explorers](#), 62 *Harv. L. Rev.* 616 (1949). His article, with one of his students, William Perdue, on the reliance interest in contracts prompted an extensive reexamination of the subject. It is cited on p. 15 above.

the event of controversy. The second function is “cautionary,” that is, bringing home to the parties the significance of their acts—inducing “the circum-spective frame of mind appropriate in one pledging his future.” The third function of seal, or of any other form, is “channeling,” or marking the promise as one intended to be legal and therefore to be resolved within the system of laws. Using the seal as the example, Fuller explained: “The seal not only insures a satisfactory memorial of the promise and induces deliberations in the making of it. It serves also to mark or signalize the enforceable promise; it furnishes a simple and external test of enforceability.” See Lon L. Fuller, *Consideration and Form*, 41 *Colum. L. Rev.* 799, 800–801 (1941); Lon L. Fuller, *Anatomy of the Law* 36–37 (1968). Of course, the ability of the seal to perform these functions and its distinctive effect on the enforceability of promises have declined as its legal status has changed. The seal has been abolished in roughly half of the states and seriously curtailed in the rest. The enactment of the Uniform Commercial Code dealt another significant blow to the seal with its announcement that “every effect of the seal which relates to ‘sealed instruments’ as such is wiped out insofar as contracts for sale are concerned.” Comment 1 to UCC § 2–203. Where the seal still retains some effect, it is often limited to raising a rebuttable presumption of consideration or making applicable a longer period of limitations.

What supplanted the seal as the primary criterion of the enforceability of a promise was the circumstance that the promise was, or was not, given in exchange for something. This development is reflected in the second of the three common law actions, debt, which was used to enforce some types of unsealed promises to pay a definite sum of money. These included a promise to repay money that had been loaned and a promise to pay for goods that had been delivered or for work that had been done. Since these were situations in which the contemplated exchange was completed on one side, they appealed to the primitive notion that the promisor (or debtor) had something belonging to the promisee (or creditor) that the former ought to surrender. The proprietary element present in this notion is reflected in the popular expression that a depositor who is owed money by a bank “*has* money in the bank.” What the promisee had given the promisor was sometimes called the “*quid pro quo*” and, as the underlying principles of contract law developed, the promisor’s obligation in debt was considered to rest upon receipt of a *benefit* from the promisee.

The third and ultimately the most important common-law action, *assumpsit*, grew out of cases in which the promisee sought to recover damages for physical injury to person or property on the basis of a consensual undertaking. In one such case a ferryman who undertook to carry the plaintiff’s horse across a river was held liable when he overloaded the boat and the horse drowned. In another a carpenter who undertook to build a house for the plaintiff was held liable when he did so unskillfully. The underlying theme of these decisions was that of misfeasance—the promisor, having undertaken (*assumpsit*) to do something, had done it in a manner inconsistent with that undertaking to the detriment of the promisee. The decisions did not go so far as to impose liability for nonfeasance—where the promisor had done *nothing* in pursuance of the undertaking—for example, where the carpenter in the case just put had failed to build the house at all. It was not until the latter half of the fifteenth century that the common-law courts began to make this extension. When they did, they imposed a requirement, analogous to that in the misfeasance cases, that the promisee must have incurred a *detriment* in reliance on the promise—as where the

owner had changed position by selling an old house in reliance on the carpenter's promise to build a new one.

Finally, by the end of the sixteenth century, the courts made a second major extension of the action of assumpsit and held that a party that had given only a promise in exchange for the other's promise had incurred a detriment by having its freedom of action fettered, since it was bound in turn by its own promise. By this circular argument, the common-law courts began to enforce exchanges of promises. Here is the opinion in what is said to be the earliest case recognizing that a promise, not even partly performed, could be consideration for a return promise:

Note, that a promise against a promise will maintain an action upon the case, as in consideration that you do give me £10 on such a day, I promise to give you £10 such a day after.

Strangborough v. Warner, 74 Eng. Rep. 686 (Q.B. 1588). See [Holdsworth, Debt, Assumpsit and Consideration](#), 11 Mich. L. Rev. 347, 351 (1913).

Eventually the action of assumpsit was allowed to supplant that of debt for the enforcement of promises. By the beginning of the seventeenth century, the common-law courts had succeeded in developing the action of assumpsit as a general basis for the enforcement of promises. By that time, the term "consideration" had come to be used as a word of art to express the sum of the conditions necessary for such an action to lie. It was therefore a tautology that a promise, if not under seal, was enforceable only where there was "consideration," for this was to say no more than that it was enforceable only where the action of assumpsit would lie. Bound up in the concept of consideration were several elements. Most important, from the *quid pro quo* of debt came the idea that there must have been an exchange arrived at by way of bargain. To the extent that debt inspired the concept of consideration, there was the notion that there must be a *benefit* to the promisor. To the extent that assumpsit inspired it, there was the notion that there must be a *detriment* to the promisee.

The cases that follow refine our understanding of the doctrine of consideration and of its development into this century. Consideration is now a fundamental feature of a contractual relationship, "the glue that binds the parties to a contract together." [In re Owen](#), 303 S.E.2d 351 (N.C.App. 1983). The concept of benefit and detriment have receded but the centrality of a bargained-for exchange between the parties remains, lending at least some support to the claim of the English legal historian, F.W. Maitland, that "[t]he forms of action we have buried, but they still rule us from their graves." Frederic W. Maitland, *The Forms of Action at Common Law* 2 (1936 ed.). For a thorough treatment of this historical background, see A.W. Brian Simpson, *A History of the Common Law of Contract* (1975). See also Patrick S. Atiyah, *The Rise and Fall of Freedom of Contract* (1979); [Farnsworth, The Past of Promise: An Historical Introduction to Contract](#), 69 Colum. L. Rev. 576 (1969). To be sure, the criterion of consideration as the *sine qua non* for promissory enforcement has, like the seal, been partially supplanted in its turn, by other criteria of enforceability, such as reliance. These too are developed in the following sections in this chapter. For now, however, our focus is on consideration: its logic, its vocabulary, and its development. Before doing so, a brief word on the categories or types of cases in which our investigation proceeds.

TYPICAL CATEGORIES OF AGREEMENTS

Throughout the nineteenth century, text-writers on contract law devoted considerable attention to specific types of agreements, such as contracts with common carriers and innkeepers, and for pawns and pledges, that were on the periphery of general contract law. When, in 1920, Samuel Williston^h launched the first edition of his magisterial contracts treatise, he announced that he sought to “treat the subject of contracts as a whole, and to show the wide range of application of its principles.” This conception of a body of contract law generally applicable to agreements of all sorts was confirmed in 1932, when the ALI promulgated its original Restatement of Contracts, for which Williston served as Reporter. Half a century later, a federal court of appeals affirmed this view. In response to a party’s plea to limit an earlier holding involving the sale of software in the case of *ProCD v. Zeidenberg*, p. 227 below, the judge responded, “Where’s the sense in that? *ProCD* is about the law of contracts, not the law of software.” *Hill v. Gateway 2000, Inc.*, 105 F.3d 1147 (7th Cir.1997). Consistent with this conception, this book seeks to show how contract principles apply to a wide variety of transactions.

At the same time, many transactions fall into recognizable categories with distinctive rules and practices. These distinctive features derive from historical practice or common business sense; others reflect larger policy concerns. We note five such categories here: contracts for sales of goods, real estate transactions, construction contracts, employment agreements, and family contracts. When a case involving one of these categories appears, it is preceded by a description of some of the common features of the category. As other types of agreements appear throughout the book—franchise and distributorship contracts, publishing contracts, government contracts, consumer contracts, and so on—you may detect and organize distinctive features of these categories as well.

And now to the first of our five typical categories: family contracts.

FAMILY CONTRACTS

The agreement in the following venerable case—an uncle’s promise to a nephew made during a family celebration—is typical of agreements between relatives and others in close personal relationships. Unlike most commercial agreements, family agreements are frequently informal and oral, lacking in detail, and may not be preceded by significant bargaining. Whatever their importance within a particular family, family agreements are rarely of great moment to the economy, although in certain historical periods the accumulation and protection of family capital was often secured by keeping it “in the family” through elaborate contractual formalities.

Yet family agreements may involve matters long understood to be outside the proper scope of judicial intervention. An initial question is therefore whether a promise made between family members is enforceable at all,

^h Samuel Williston (1861–1963) joined the faculty of the Harvard Law School in 1890, after practicing law for a short period in Boston, and taught there until his retirement in 1938. His principal fields were contracts and sales. His multi-volume work, *A Treatise on the Law of Contracts*, was first published in 1920 and became one of the most widely used legal treatises in the United States. He was the Reporter for the Restatement of Contracts and the draftsman of several uniform laws, including the Uniform Sales Act.

a question that explains the presence of a number of such cases in this chapter.

The traditional answer has been: No. Goods or services given or pledged by one family member to another were assumed to be motivated by altruism or by domestic obligation (not always the same thing), and were decidedly *not* bargains motivated by gain. Policy concerns, such as family privacy and domestic harmony, further explained judicial reluctance to find a bargain between intimates. As an English court explained in denying a wife recovery on her husband's promise of a stated monthly allowance, "it would be the worst possible example to hold that agreements such as this resulted in legal obligations which could be enforced in the Courts," for "each house is a domain into which the King's writ does not run and to which his officers do not seek to be admitted." *Balfour v. Balfour*, [1919] 2 K.B. 571, 579 (C.A.). An American court justified a similar decision by declaring that to enforce such a promise would "open an endless field for controversy and bickering." *Graham v. Graham*, 33 F.Supp. 936 (E.D.Mich.1940).

In recent years, the differences between family agreements and commercial ones have narrowed as contractual relationships among relatives and other intimates have found greater legal acceptance. Sophisticated contracts, now often drafted by lawyers, are used to order matters once considered wholly unsuited for private agreement or public enforcement. Parties, married and unmarried, now arrange aspects of their relationships from start to finish through pre-nuptial agreements, cohabitation contracts, mid-marriage agreements and divorce and property settlements. People increasingly contract with one another for the purpose of creating and ordering vertical relationships—that is, between parents and children. For example, contract has come to play a role in parental acquisition of children, whether through surrogacy contracts, open adoption agreements, or the sale of genetic material. We explore such agreements in later chapters, but begin here with a relatively straightforward promise from uncle to nephew.

Hamer v. Sidway

Court of Appeals of New York, 1891.
124 N.Y. 538, 27 N.E. 256.

Appeal from an order of the general term of the supreme court in the fourth judicial department, reversing a judgment entered on the decision of the court at special term. The plaintiff presented a claim to the executor of William E. Story, Sr., for \$5,000 and interest from the 6th day of February, 1875. She acquired it through several mesne assignments from William E. Story, 2d. The claim being rejected by the executor, this action was brought.

It appears that William E. Story, Sr., was the uncle of William E. Story, 2d; that at the celebration of the golden wedding of Samuel Story and wife, father and mother of William E. Story, Sr., on the 20th day of March, 1869, in the presence of the family and invited guests, he promised his nephew that if he would refrain from drinking, using tobacco, swearing, and playing cards or billiards for money until he became 21 years of age, he would pay him the sum of \$5,000. The nephew assented thereto, and fully performed the conditions inducing the promise. When the nephew arrived at the age of 21 years, and on the 31st day of January, 1875, he wrote to his uncle, informing him that he had performed his part of the agreement, and

had thereby become entitled to the sum of \$5,000. The uncle received the letter, and a few days later, and on the 6th day of February, he wrote and mailed to his nephew the following letter:

Buffalo, Feb. 6, 1875.

“W.E. STORY, JR.:

“DEAR NEPHEW—Your letter of the 31st ult. came to hand all right, saying that you had lived up to the promise made to me several years ago. I have no doubt but you have, for which you shall have five thousand dollars as I promised you. I had the money in the bank the day you was 21 years old that I intend for you, and you shall have the money certain. Now, Willie, I do not intend to interfere with this money in any way till I think you are capable of taking care of it and the sooner that time comes the better it will please me. I would hate very much to have you start out in some adventure that you thought all right and lose this money in one year. The first five thousand dollars that I got together cost me a heap of hard work. . . . It did not come to me in any mysterious way, and the reason I speak of this is that money got in this way stops longer with a fellow that gets it with hard knocks than it does when he finds it. Willie, you are 21 and you have many a thing to learn yet. This money you have earned much easier than I did besides acquiring good habits at the same time and you are quite welcome to the money; hope you will make good use of it. I was ten long years getting this together after I was your age. Now, hoping this will be satisfactory, I stop. . . .

Truly Yours,
“W.E. STORY.

“P.S.—You can consider this money on interest.”

The nephew received the letter and thereafter consented that the money should remain with his uncle in accordance with the terms and conditions of the letters. The uncle died on the 29th day of January, 1887, without having paid over to his nephew any portion of the said \$5,000 and interest.

■ PARKER, J. The question which provoked the most discussion by counsel on this appeal, and which lies at the foundation of plaintiff's asserted right of recovery, is whether by virtue of a contract defendant's testator William S. Story became indebted to his nephew William E. Story, 2d, on his twenty-first birthday in the sum of five thousand dollars. The trial court found as a fact that “on the 20th day of March, 1869, . . . William E. Story agreed to and with William E. Story, 2d, that if he would refrain from drinking liquor, using tobacco, swearing, and playing cards or billiards for money until he should become 21 years of age, then he, the said William E. Story, would at that time pay him, the said William E. Story, 2d, the sum of \$5000 for such refraining, to which the said William E. Story, 2d, agreed,” and that he “in all things fully performed his part of said agreement.”

The defendant contends that the contract was without consideration to support it, and, therefore, invalid. He asserts that the promisee by refraining from the use of liquor and tobacco was not harmed but benefited; that that which he did was best for him to do independently of his uncle's promise, and insists that it follows that unless the promisor was benefited, the contract was without consideration, a contention which, if well founded, would seem to leave open for controversy in many cases whether that

which the promisee did or omitted to do was, in fact, of such benefit to him as to leave no consideration to support the enforcement of the promisor's agreement. Such a rule could not be tolerated, and is without foundation in the law. The Exchequer Chamber, in 1875, defined consideration as follows: "A valuable consideration in the sense of the law may consist either in some right, interest, profit, or benefit accruing to the one party, or some forbearance, detriment, loss, or responsibility given, suffered, or undertaken by the other." Courts "will not ask whether the thing which forms the consideration does in fact benefit the promisee or a third party, or is of any substantial value to any one. It is enough that something is promised, done, forbore, or suffered by the party to whom the promise is made as consideration for the promise made to him." Anson's Prin. of Con. 63.

"In general, a waiver of any legal right at the request of another party is a sufficient consideration for a promise." Parsons on Contracts, 444.

"Any damage, or suspension or forbearance of a right, will be sufficient to sustain a promise." Kent, Vol. 2, 465, 12th Ed.ⁱ

Pollock, in his work on contracts, page 166, after citing the definition given by the Exchequer Chamber already quoted, says: "The second branch of this judicial description is really the most important one. Consideration means not so much that one party is profiting as that the other abandons some legal right in the present or limits his legal freedom of action in the future as an inducement for the promise of the first."

Now, applying this rule to the facts before us, the promisee used tobacco, occasionally drank liquor, and he had a legal right to do so. That right he abandoned for a period of years upon the strength of the promise of the testator that for such forbearance he would give him \$5000. We need not speculate on the effort which may have been required to give up the use of those stimulants. It is sufficient that he restricted his lawful freedom of action within certain prescribed limits upon the faith of his uncle's agreement, and now having fully performed the conditions imposed, it is of no moment whether such performance actually proved a benefit to the promisor, and the court will not inquire into it, but were it a proper subject of inquiry, we see nothing in this record that would permit a determination that the uncle was not benefited in a legal sense. Few cases have been found which may be said to be precisely in point, but such as have been support the position we have taken.

In *Shadwell v. Shadwell*, 9 C.B.N.S. 159, an uncle wrote to his nephew as follows:

"MY DEAR LANCEY—I am so glad to hear of your intended marriage with Ellen Nicholl, and as I promised to assist you at starting, I am happy to tell you that I will pay you 150 pounds yearly during my life and until your annual income derived from your profession of a chancery barrister

ⁱ James Kent (1763–1847) began practice after three years as an apprentice and was active in Federalist politics. Hamilton introduced him to the writings of European authors on the civil law, which were to influence his later work. In 1793, largely through his Federalist connections, he was made Professor of Law in Columbia College. He attracted few students, and soon resigned to become a judge on the New York Supreme Court, then the highest court in the state. In 1814 he became Chancellor. Upon his retirement in 1823, he lectured again at Columbia for three years. Out of these lectures grew the "Commentaries on American Law," in four volumes, which became one of the most important American law books of the century. (It is the source of the quotation above.) Kent lived to prepare six editions; subsequent ones were revised by others. For his work on the Court of Chancery, he has been called the creator of equity in the United States.

shall amount to 600 guineas, of which your own admission will be the only evidence that I shall require.

“Your affectionate uncle,
“CHARLES SHADWELL.”

It was held that the promise was binding and made upon good consideration.

In *Lakota v. Newton*, an unreported case in the Superior Court of Worcester, Mass., the complaint averred defendant’s promise that “if you (meaning plaintiff) will leave off drinking for a year I will give you \$100,” plaintiff’s assent thereto, performance of the condition by him, and demanded judgment therefor. Defendant demurred on the ground, among others, that the plaintiff’s declaration did not allege a valid and sufficient consideration for the agreement of the defendant. The demurrer was overruled.

In *Talbott v. Stemmons*, 89 Ky. 222, the step-grandmother of the plaintiff made with him the following agreement: “I do promise and bind myself to give my grandson, Albert R. Talbott, \$500 at my death, if he will never take another chew of tobacco or smoke another cigar during my life from this date up to my death, and if he breaks this pledge he is to refund double the amount to his mother.” The executor of Mrs. Stemmons demurred to the complaint on the ground that the agreement was not based on a sufficient consideration. The demurrer was sustained and an appeal taken therefrom to the Court of Appeals, where the decision of the court below was reversed. In the opinion of the court it is said that “the right to use and enjoy the use of tobacco was a right that belonged to the plaintiff and not forbidden by law. The abandonment of its use may have saved him money or contributed to his health; nevertheless, the surrender of that right caused the promise, and having the right to contract with reference to the subject-matter, the abandonment of the use was a sufficient consideration to uphold the promise.” Abstinence from the use of intoxicating liquors was held to furnish a good consideration for a promissory note in *Lindell v. Rokes*, 60 Mo. 249. The cases cited by the defendant on this question are not in point. . . .

[In an omitted part of the opinion the court held that the action was not barred by the statute of limitations because under the uncle’s letter he held the money in trust and not merely as a debtor.] Order reversed and judgment of special term affirmed.

NOTES

(1) *Benefit, Detriment, and Bargain*. What was the consideration for the uncle’s promise to pay \$5,000? How did the court’s definition of detriment differ from that urged by the defendant? What role do benefit and detriment play under Restatement §§ 71 and 79? Was there consideration for the uncle’s promise under those sections? What if the uncle had promised his nephew \$5,000 in exchange for the young man’s promise to foreswear illegal substances?

How clear is it that there was consideration for promise of the affectionate uncle in *Shadwell v. Shadwell* (“My dear Lancey . . .”), cited by the court as being “precisely on point.”

(2) *Holmes and the “Bargain Theory” of Consideration*. Oliver Wendell Holmes, Jr., an early advocate of the “bargain theory” of consideration later

espoused in the Restatement, spoke of “reciprocal conventional inducement”: “It is said that consideration must not be confounded with motive. It is true that it must not be confounded with what may be the prevailing or chief motive in actual fact. A man may promise to paint a picture for five hundred dollars, while his chief motive may be a desire for fame. A consideration may be given and accepted, in fact, solely for the purpose of making a promise binding. But, nevertheless, it is the essence of a consideration, that, by the terms of the agreement, it is given and accepted as the motive or inducement of the promise. Conversely, the promise must be made and accepted as the conventional motive or inducement for furnishing the consideration. The root of the whole matter is the relation of reciprocal conventional inducement, each for the other, between consideration and promise.” Holmes, *The Common Law* 293–94 (1881).

Holmes reaffirmed this when he went on the bench: “[T]he promise and the consideration must purport to be the motive each for the other, in whole or at least in part. It is not enough that the promise induces the detriment or that the detriment induces the promise if the other half is wanting.” Holmes, J., in [Wisconsin & Michigan Railway Co. v. Powers](#), 191 U.S. 379 (1903). Compare Restatement § 71(2) with § 81(1).

(3) “*Sufficiency of Consideration*.” The term “sufficient consideration” appears at several points in *Hamer v. Sidway*. The original Restatement (“the Restatement”), embodied a concept of the “sufficiency” of consideration. Although consideration did not have to be “adequate,” it had to be “sufficient.” See the Restatement, §§ 76–81. The Restatement Second abandoned this concept. Under its terminology the question is simply whether there is “consideration,” with no qualifying adjective. See Restatement § 79. In declining to assess whether a particular lease provision was inadequate, one court relied on the “time-honored principle” that an informed decision by a party “that what it is receiving is worth what it is giving may not later be second-guessed by that party, nor may the party ask a court to engage in such post-hoc revisionism.” [GLS Development v. Wal-Mart Stores](#), 944 F.Supp. 1384 (N.D.Ill. 1996). Whether or not consideration can ever be so paltry as to suggest impermissible overreaching by one of the parties is taken up in Chapter 4.

(4) *The Peppercorn*. Under the bargain theory of consideration, can a gratuitous promise be made enforceable by a mere token payment, arranged by the parties for the sole purpose of satisfying the requirement of consideration? Holmes concluded that since courts would not in general “inquire into the amount of such consideration . . . , consideration is as much a form as a seal.” [Krell v. Codman](#), 28 N.E. 578 (Mass. 1891). The term “peppercorn” is often used to describe consideration that is of trifling value.

Will such a device be given effect? There is some authority, most of it old, that it will be. *E.g.*, *Thomas v. Thomas*, 2 Q.B. 851, 114 Eng.Rep. 330 (1842). Illustration 1 to the Restatement § 84 states:

A wishes to make a binding promise to his son B to convey to B Blackacre, which is worth \$5,000. Being advised that a gratuitous promise is not binding, A writes to B an offer to sell Blackacre for \$1. B accepts. B’s promise to pay \$1 is sufficient consideration.

In contrast, the Restatement Second, takes the opposite view. Illustration 5 to § 71 states:

A desires to make a binding promise to give \$1,000 to his son B. Being advised that a gratuitous promise is not binding, A offers to buy from B for \$1,000 a book worth less than \$1. B accepts the offer knowing that the purchase of the book is a mere pretense. There is no consideration for A's promise to pay \$1,000.

Why should promisors not be able to bind themselves through the pro forma use of consideration? Why might parties want to bind themselves legally in the absence of a bargain? Ought the law differentiate between a peppercorn inserted for the purpose of tying the promisor to the mast, and cases in which the consideration is intended as a sham from a promisory point of view? See [Meyer v. South Dakota Dept. of Social Services, 581 N.W.2d 151 \(S.D. 1998\)](#), in which the owner of a ranch sought to reduce his estate for purposes of Medicaid eligibility through a series of "gift/lendback" transactions with his adult children. The owner wrote checks to his children who endorsed the checks and gave them back to the owner, who deposited them into his account uncashed. The owner then gave the children a mortgage on the ranch to secure the "loans" they had made him. The court quoted Williston: "nothing can be treated as consideration that is not intended as such by the parties." 3 Williston on Contracts § 7.2 (4th ed. 1992).

(5) *Promise for Performance or Promise for Promise?* In the principal case, the uncle promised to pay his nephew in exchange for his nephew's *refraining* from various vices, and not for his nephew's *promise* to refrain. See Restatement § 71(1). Why might the uncle have sought actual performance rather than his nephew's promise? Distinctions between contracts in which the promise is exchanged for performance and those in which two promises are exchanged are discussed at p. 71 below and again in Chapter 2 in connection with contract formation. Agreements in which only one party makes a promise are often called *unilateral* contracts; agreements in which each party makes a promise to the other are often called *bilateral*. Bilateral contracts are much more common and economically significant than unilateral contracts. Why might this be?

(6) *Hamer Lives*. In [Dahl v. HEM Pharmaceuticals, 7 F.3d 1399, 1404 \(9th Cir. 1993\)](#), a drug company promised a year's free supply of an experimental drug to subjects who participated in a one-year clinical trial to test the drug's efficacy. Dahl participated for the full year, at which time HEM refused to supply the drug any further, claiming its promise to do so was unsupported by consideration. On appeal, the court said: "Somehow the category of unilateral contracts appears to have escaped HEM's notice. The deal was, 'if you submit to our experiment, we will give you a year's supply of Ampligen at no charge.' This form of agreement resembles that in the case taught in the first year of law school, *Hamer v. Sidway* . . ."

PROBLEM

Discounting Retirement. Thomas Hurley has worked as general superintendent for Marine Contractors for eight years, during which Marine has made annual payments into an Employee Retirement Plan and Trust Fund, a legally-separate entity whose sole trustee is also the president of Marine. Hurley now plans to leave Marine, and is entitled under the terms of the trust to payment of his vested share after a five-year waiting period. Marine wants Hurley to make a binding promise to Marine not to compete with it after he leaves its employ. In return, Marine's president, as trustee, is willing to have the trust

pay Hurley his vested share immediately. Will payment by the trust to Hurley be consideration for Hurley's promise to Marine? Does the answer depend on whether you are looking for a benefit, a detriment, or a bargain? See [Marine Contractors Co., Inc. v. Hurley](#), 310 N.E.2d 915 (Mass. 1974).

GRATUITOUS PROMISES

Suppose that the uncle in *Hamer* had given his nephew \$5,000 in cash at the golden wedding anniversary and had told him that it was a gift that he could keep on condition that he refrain from drinking, smoking, swearing, and gambling until he was twenty-one. Surely the nephew, having met the condition, could have kept the money if the uncle's executor had attempted to get it back.

If the law recognizes gratuitous *transfers*, with or without strings attached, why should it not recognize gratuitous *promises*? Why did the court have to find that there was consideration? What explains the reluctance to create a regime of enforceable gift promises? We have already seen the suggestion that social cooperation might best be achieved by a system of "free enterprise." Is it the fact that gratuitous promises serve no useful economic function? Do gift promises raise dangers as to proof? See Richard A. Posner, *Gratuitous Promises in Economics and Law*, 6 J. Legal Stud. (1977).

What sorts of rules or legal mechanisms would you suggest if it were thought desirable to enable promisors to make enforceable gratuitous promises? To what extent should those rules take account of such factors as the promisor's motives, the social utility of the promise, the formality with which it was made and the availability of alternate means of making gifts?

NOTES

(1) *Sweetheart Stadium?* In the 1990s, a group of taxpayers in Washington State sought to enjoin a bond ordinance enacted to raise money for a new stadium for the Seattle Mariners, a baseball team. The taxpayers argued that the consideration received by the city under the terms of the stadium lease between the city and the team was so "grossly inadequate" as to make the lease a gift, one prohibited under the state constitution, which forbids gifts of public monies to private organizations. The taxpayers pointed to such provisions as profit-sharing (with little expectation of profit), nominal rent, and easy-out terms for the team.

Noting that "courts do not inquire into the adequacy of consideration," the Washington Supreme Court found consideration in the Mariners' obligations to play home games, maintain the stadium, and share profits. It affirmed the trial court's declaratory order validating the bonds. [King County v. Taxpayers of King County](#), 949 P.2d 1260 (Wash.1997).

Is the traditional rule regarding consideration appropriate in the context of a constitutional challenge? A dissent in the stadium case argued that it is not:

If a public official may transfer \$100 of the taxpayer property for a \$5 return to the taxpayer, they are \$95 poorer. The return is inadequate regardless of the legal sufficiency of the consideration. The purpose of

the [constitutional] provision is to avoid transactions which plunder the public purse to the benefit of private corporate wealth.

Id. at 1278. The dissenting justices would have required a trial on the question of the adequacy of the return. The Arizona Supreme Court agreed. In 2010, the Court held that although “courts do not ordinarily examine the proportionality of consideration between parties contracting at arm’s length, leaving such issues to the marketplace,” a different test applies when the adequacy of consideration is challenged under the Gift Clause of the state constitution. [Turken v. Gordon](#), 224 P.3d 158 (Ariz, 2010). In that case, the City of Phoenix had agreed to pay a private developer an extraordinary price of over \$97,000,000 for the use of parking spaces over a specified period of time. Applying the new test prospectively, the Court held that the Gift Clause “prohibits subsidies to private entities, and paying far more than the fair market value . . . would plainly be a subsidy.” *Id.* at 166.

(2) *Changing One’s Mind*. One argument against enforcing gratuitous promises is that enforcement leaves no room for a promisor’s regret or for changed circumstances. But might not some reasons for changing one’s mind be anticipated and accommodated? French and German laws, for example, permit the revocation of *gifts* by means of implied conditions in cases where the donor is subsequently impoverished (German law), or cases of “donee ingratitude” (French law). See John P. Dawson, *Gifts and Promises* (1980) at 53, 140–141; see also Richard Hyland, *Gifts: A Study in Comparative Law* (2009). Professor Larry Garvin notes that we need not go so “far afield to see revocation for ingratitude at work.” Louisiana, a civil law jurisdiction, provides for revocation of an *inter vivos* gift where the donee “has attempted to take the life of the donor” or “has been guilty. . . of cruel treatment, crimes, or grievous injury.” Farnsworth on Contracts: 2013–2 Cumulative Supplement § 2.18a, n.21 (Larry T. Garvin ed., 2012).

Consider also an Israeli rule that permits revocation of a gift *promise*, even after reliance by the promisee, “if the retraction is warranted by disgraceful conduct towards the [promisor or the promisor’s family],” 22 Laws of State of Israel 113. Is it significant in these latter cases that the promisee appears to have had some responsibility for the promisor’s regret? For a thorough investigation of the subject, see E. Allan Farnsworth, *Changing One’s Mind: The Law of Regretted Decisions* (2000).

SETTLEMENT AGREEMENTS

Despite the well-known, perhaps well-deserved reputation for litigiousness in the U.S., only a tiny percentage of civil cases actually go to trial. See [John H. Langbein, The Disappearance of Civil Trial in the United States](#), 122 *Yale L.J.* 522 (2012). Most parties settle their cases, and for a variety of reasons: risk aversion, trial costs, privacy. When a plaintiff gives up a valid claim in exchange for something, consideration is no obstacle to the settlement. But what if the plaintiff’s claim turns out to be invalid? Has the defendant in such a case given up something for nothing?

Dyer v. National By-Products, Inc.

Supreme Court of Iowa, 1986.

[380 N.W.2d 732.](#)

■ SCHULTZ, JUSTICE. The determinative issue in this appeal is whether good faith forbearance to litigate a claim, which proves to be invalid and unfounded, is sufficient consideration to uphold a contract of settlement. The district court determined, as a matter of law, that consideration for the alleged settlement was lacking because the forborne claim was not a viable cause of action. We reverse and remand.

On October 29, 1981, Dale Dyer, an employee of National By-Products, lost his right foot in a job-related accident. Thereafter, the employer placed Dyer on a leave of absence at full pay from the date of his injury until August 16, 1982. At that time he returned to work as a foreman, the job he held prior to his injury. On March 11, 1983, the employer indefinitely laid off Dyer.

Dyer then filed the present lawsuit against his employer claiming that his discharge was a breach of an oral contract. He alleged that he in good faith believed that he had a valid claim against his employer for his personal injury. Further, Dyer claimed that his forbearance from litigating his claim was made in exchange for a promise from his employer that he would have lifetime employment. The employer specifically denied that it had offered a lifetime job to Dyer after his injury.

Dyer then filed the present lawsuit against his employer claiming that his discharge was a breach of an oral contract. He alleged that he in good faith believed that he had a valid claim against his employer for his personal injury. Further, Dyer claimed that his forbearance from litigating his claim was made in exchange for a promise from his employer that he would have lifetime employment.

The district court sustained the employer's motion on the basis that: (1) no reciprocal promise to work for the employer for life was present, and (2) there was no forbearance of any viable cause of action, apparently on the ground that workers' compensation provided Dyer's sole remedy. On appeal, Dyer claims that consideration for the alleged contract of lifetime employment was his forbearance from pursuing an action against his employer.

The employer, on the other hand, maintains that workers' compensation benefits are Dyer's sole remedy for his injury and that his claim for damages is unfounded. It then urges that forbearance from asserting an unfounded claim cannot serve as consideration for a contract. For the purpose of this discussion, we shall assume that Dyer's tort action is clearly invalid and he had no basis for a tort suit against either his employer or his fellow employees. We recognize that the fact issue, as to whether Dyer in good faith believed that he had a cause of action based in tort against the employer, remains unresolved. The determinative issue before the district court and now on appeal is whether the lack of consideration for the alleged promise of lifetime employment has been established as a matter of law.

Preliminarily, we observe that the law favors the adjustment and settlement of controversies without resorting to court action. [Olson v. Wilson & Co.](#), 244 Iowa 895, 899, 58 N.W.2d 381, 384 (1953). Compromise is favored by law. [White v. Flood](#), 258 Iowa 402, 409, 138 N.W.2d 863, 867

(1965). Compromise of a doubtful right asserted in good faith is sufficient consideration for a promise. *Id.*

The more difficult problem is whether the settlement of an unfounded claim asserted in good faith is consideration for a contract of settlement. Professor Corbin presents a view favorable to Dyer's argument when he states:

[F]orbearance to press a claim, or a promise of such forbearance, may be a sufficient consideration even though the claim is wholly ill-founded. It may be ill-founded because the facts are not what he supposes them to be, or because the existing facts do not have the legal operation that he supposes them to have. In either case, his forbearance may be a sufficient consideration, although under certain circumstances it is not. The fact that the claim is ill-founded is not in itself enough to prevent forbearance from being a sufficient consideration for a promise. Corbin on Contracts § 140, at 595 (1963).

Further, in the same section, it is noted that:

The most generally prevailing, and probably the most satisfactory view is that forbearance is sufficient if there is any reasonable ground for the claimant's belief that it is just to try to enforce his claim. He must be asserting his claim "in good faith"; but this does not mean he must believe that his suit can be won. It means that he must not be making his claim or threatening suit for purposes of vexation, or in order to realize on its "nuisance value."

Id. § 140, at 602 (emphasis added).

Indeed, we find support for the Corbin view in language contained in our cases. See [White v. Flood](#), 258 Iowa at 409, 138 N.W.2d at 867 ("[C]ompromise of a doubtful right asserted in good faith is sufficient consideration for a promise."); . . . [Messer v. Washington National Insurance Co.](#), 233 Iowa 1372, 1380, 11 N.W.2d 727, 731 (1943) ("[I]f the parties act in good faith, even when they know all the facts and there is promise without legal liability on which to base it, the courts hesitate to disturb the agreements of the parties. . . .") [additional citations omitted].

The Restatement (Second) of Contracts section 74 (1979), supports the Corbin view and states:

Settlement of Claims

- (1) Forbearance to assert or the surrender of a claim or defense which proves to be invalid is not consideration unless
 - (a) the claim or defense is in fact doubtful because of uncertainty as to the facts or the law, or
 - (b) the forbearing or surrendering party believes that the claim or defense may be fairly determined to be valid.

The Comment states:

b. Requirement of good faith. The policy favoring compromise of disputed claims is clearest, perhaps, where a claim is surrendered at a time when it is uncertain whether it is valid or not. Even though the invalidity later becomes clear, the bargain is to be judged as it appeared to the parties at the time; if the claim was then doubtful, no inquiry is necessary as to their good faith. Even though the invalidity should have been clear at the time, the settlement of an honest dispute is upheld. But a mere assertion or denial of liability does not make a

claim doubtful, and the fact that invalidity is obvious may indicate that it was known. In such cases Subsection (1)(b) requires a showing of good faith.

(Emphasis added.)

However, not all jurisdictions adhere to this view. Some courts require that the claim forborne must have some merit in fact or at law before it can provide consideration and these jurisdictions reject those claims that are obviously invalid. See *Bullard v. Curry–Cloonan*, 367 A.2d 127, 131 (D.C.App.1976) (“[A]s a general principle, the forbearance of a cause of action advanced in good faith, which is neither absurd in fact nor obviously unfounded in law, constitutes good and valuable consideration.”); *Frasier v. Carter*, 92 Idaho 79, 437 P.2d 32, 34 (1968) (The forbearance of a claim which is not utterly groundless is sufficient consideration to support a contract.); *Charles v. Hill* 260 N.W.2d 571, 575 (Minn.1977) (“[A] wholly baseless or utterly unfounded claim is not consideration for a contract.”); *Agristor Credit Corporation v. Unruh*, 571 P.2d 1220, 1224 (Okla.1977) (In order to constitute consideration for a contract, “claim forborne must be reasonably doubtful in law or fact.”).

In fact, we find language in our own case law that supports the view which is favorable to the employer in this case. See *Vande Stouwe v. Bankers’ Life Co.*, 218 Iowa 1182, 1190, 254 N.W. 790, 794 (1934) (“A claim that is entirely baseless and without foundation in law or equity will not support a compromise.”); *Peterson v. Breitag*, 88 Iowa 418, 422–23, 55 N.W. 86, 88 (1893) (“It is well settled that there must at least be some appearance of a valid claim to support a settlement to avoid litigation.”); . . . *Sullivan v. Collins*, 18 Iowa 228, 229 (1865) (A compromise of a claim is not a sufficient consideration to sustain a note, when such claim is not sustainable in law or in equity, or, at least doubtful in some respect.). Additionally, Professor Williston notes that:

While there is a great divergence of opinion respecting the kind of forbearance which will constitute consideration, the weight of authority holds that although forbearance from suit on a clearly invalid claim is insufficient consideration for a promise, forbearance from suit on a claim of doubtful validity is sufficient consideration for a promise if there is a sincere belief in the validity of the claim. 1 Williston on Contracts § 135, at 581 (3rd ed. 1957) (emphasis added).

We believe, however, that the better reasoned approach is that expressed in the Restatement (Second) of Contracts section 74. Even the above statement from Williston, although it may have been the state of the law in 1957, is a questionable assessment of the current law. In fact, most of the cases cited in the cumulative supplement to Williston follow the “good faith and reasonable” language. 1 Williston on Contracts § 135B (3rd ed. 1957 & Supp.1985). Additionally, Restatement (Second) of Contracts section 74 is cited in that supplement. *Id.* As noted before, as a matter of policy the law favors compromise and such policy would be defeated if a party could second guess his settlement and litigate the validity of the compromise. The requirement that the forbearing party assert the claim in good faith sufficiently protects the policy of law that favors the settlement of controversies. Our holdings which are to the contrary to this view are overruled.

In the present case, the invalidity of Dyer’s claim against the employer does not foreclose him, as a matter of law, from asserting that his forbear-

ance was consideration for the alleged contract of settlement. However, the issue of Dyer's good faith must still be examined. In so doing, the issue of the validity of Dyer's claim should not be entirely overlooked: Although the courts will not inquire into the validity of a claim which was compromised in good faith, there must generally be reasonable grounds for a belief in order for the court to be convinced that the belief was honestly entertained by the person who asserted it. Sufficient consideration requires more than the bald assertion by a claimant who has a claim, and to the extent that the validity or invalidity of a claim has a bearing upon whether there were reasonable grounds for believing in its possible validity, evidence of the validity or invalidity of a claim may be relevant to the issue of good faith. [15A Am.Jur.2d Compromise and Settlement § 17](#), at 790. We conclude that the evidence of the invalidity of the claim is relevant to show a lack of honest belief in the validity of the claim asserted or forborne.

Under the present state of the record, there remains a material fact as to whether Dyer's forbearance to assert his claim was in good faith. Summary judgment should not have been rendered against him. Accordingly, the case is reversed and remanded for further proceedings consistent with this opinion.

REVERSED AND REMANDED.

NOTES

(1) *Questions.* What was the problem with the claim Dyer agreed not to pursue? Was any aspect of it doubtful as a matter of fact or law? How can forbearing on a legally non-existent claim satisfy the requirement of bargained-for exchange? Does the impossibility of Dyer's tort suit bear at all on the question of whether his forbearance complied with the factors set out in Restatement § 74?

Why might parties in general prefer to settle valid claims rather than litigate them? What broader policies are promoted by settlement? Private ordering? Efficiency? Fairness? See [Michael Moffitt, Three Things to be Against "Settlement" Not Included](#), 78 *Fordham L. Rev.* 1203 (2009).

(2) *The Claimant's Belief.* In *Dyer*, what factual issue was the trial court to determine on remand? How does a claimant prove a good-faith belief? Is the good-faith belief in the validity of the claim measured by an objective or subjective standard?

Consider the following case. In 1951, Hilda Boehm, an unmarried woman, gave birth to a baby girl. After informing Louis Fiege that he was the father, the parties then entered into an agreement: Boehm promised not to file a paternity action against Fiege in exchange for Fiege's promise to pay child support during the child's minority. In 1953, Fiege learned from Boehm's physician that blood tests indicated he could not have been the father. Fiege stopped paying support, and Boehm sued for breach of their settlement agreement. A jury found for Boehm, and Fiege appealed on the ground that the contract lacked consideration because Boehm's forbearance was based on an invalid claim. [Fiege v. Boehm](#), 123 A.2d 316 (Ct. App. Md. 1951). Held: for Boehm.

The appellate court found that Boehm's promise to forbear was good consideration. Not only did Boehm honestly believe her claim to be well-founded (subjective), but the claim also had a reasonable basis of support (objective).

What facts might warrant Boehm's good faith belief in the validity of her claim? Could she have enforced promises for child support against two promisors?

How does Boehm's claim against Fiege differ from that of Dyer in the principal case?

(3) *Settlement Agreements and Legal Ethics.* While *Dyer* concerned forbearance in the context of a personal injury claim, the settlement of doubtful claims also arises in connection with nuisance litigation or "strike suits." These are defined as lawsuits with a sufficiently low chance of prevailing at trial that they would not have been brought but for the prospect of settlement. Why are frivolous suits not always met with blanket refusals to negotiate? A legal economist has observed that "since refusing to take a valid claim seriously can be quite costly, a frivolous plaintiff may be able to take advantage of the defendant's uncertainty regarding the claim's validity to extract a substantial settlement." Avery Katz, *The Effect of Frivolous Lawsuits on the Settlement of Claims*, 10 *Intl. Rev. L. & Econ.* 3, 4 (1990).

What is a lawyer's responsibility with regard to filing dubious pleadings? Rule 11(b) of the Federal Rules of Civil Procedure provides that by presenting a pleading to a court, an attorney certifies that to the best of his or her knowledge, after a reasonable inquiry, the pleading "is not being presented for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation." An attorney further certifies, by virtue of signing a pleading, that there is evidentiary support for any fact it asserts. Courts may order sanctions against attorneys who violate Rule 11(b). Comparable rules govern state court pleadings; see, for example, the Signing of Pleadings in Texas Code Annotated § 9.01.

(4) *Plea Bargains.* Settlement agreements are not only a common aspect of civil litigation; they also play a significant role in the criminal justice system. Consider that only five percent of federal and state felony prosecutions are resolved by trial; the remainder are settled through plea bargains entered into between criminal defendants and prosecutors. See [Padilla v. Kentucky](#), 130 S. Ct. 1473, 1485 (2010). Typically, the defendant agrees to plead guilty in exchange for some concession by the prosecutor, such as a sentencing recommendation or a dismissal of other charges. Who is giving up what in this arrangement? What are the advantages for prosecutors, for defendants, and for the administration of justice? Ought the law have particular concerns when a party's forbearance has a constitutional dimension? If the government fails to make the promised sentencing recommendation, what remedy might the defendant seek? See *United States v. Ramsey*, 503 F. Supp.2d 554 (N.D.N.Y. 2007).

(5) *Forbearing Political Participation.* Community benefits agreements (CBAs) are contracts negotiated and executed between real estate developers and community groups. Typically these agreements require the developer to provide benefits to the community, such as local hiring, living wages and affordable housing, in exchange for the community groups' promise to not oppose the project. Is a promise to refrain from political participation valid consideration? What if the community group or a renegade member of the community group had a change of heart and sought to organize protests after the agreement was formed? Would the developer have a remedy and how might it be enforced? Citizens cannot offer their votes as consideration. How are CBAs distinguishable from vote-selling? See Vicki Been, *Community Benefits Agree-*

ments: New Local Government Tool or Another Variation on the Exactions Theme?, 77 U. Chi. L. Rev. 5, 5–6 (2010); Naved Sheikh, Community Benefits Agreements: Can Private Contracts Replace Public Responsibility?, 18 Cornell J. L. & Pub. Pol’y 223, 233-40 (2009).

(B) THE REQUIREMENT OF EXCHANGE: ACTION IN THE PAST

Feinberg v. Pfeiffer Co.

Saint Louis Court of Appeals, Missouri, 1959.
[322 S.W.2d 163.](#)

Action on alleged contract by defendant to pay plaintiff a specified monthly amount upon her retirement from defendant’s employ. The Circuit Court, City of St. Louis, rendered judgment for plaintiff, and defendant appealed.

■ **DOERNER, COMMISSIONER.** This is a suit brought in the Circuit Court of the City of St. Louis by plaintiff, a former employee of the defendant corporation, on an alleged contract whereby defendant agreed to pay plaintiff the sum of \$200 per month for life upon her retirement. A jury being waived, the case was tried by the court alone. Judgment below was for plaintiff for \$5,100, the amount of the pension claimed to be due as of the date of the trial together with interest thereon, and defendant duly appealed.

The parties are in substantial agreement on the essential facts. Plaintiff began working for the defendant, a manufacturer of pharmaceuticals, in 1910, when she was but 17 years of age. By 1947 she had attained the position of bookkeeper, office manager, and assistant treasurer of the defendant, and owned 70 shares of its stock out of a total of 6,503 shares issued and outstanding. Twenty shares had been given to her by the defendant or its then president, she had purchased 20, and the remaining 30 she had acquired by a stock split or stock dividend. Over the years she received substantial dividends on the stock she owned, as did all of the other stockholders. Also, in addition to her salary, plaintiff from 1937 to 1949, inclusive, received each year a bonus varying in amount from \$300 in the beginning to \$2,000 in the later years.

On December 27, 1947, the annual meeting of the defendant’s Board of Directors was held at the Company’s offices in St. Louis, presided over by Max Lippman, its then president and largest individual stockholder. The other directors present were George L. Marcus, Sidney Harris, Sol Flammer, and Walter Weinstock, who, with Max Lippman, owned 5,007 of the 6,503 shares then issued and outstanding. At that meeting the Board of Directors adopted the following resolution, which, because it is the crux of the case, we quote in full:

“The Chairman thereupon pointed out that the Assistant Treasurer, Mrs. Anna Sacks Feinberg, has given the corporation many years of long and faithful service. Not only has she served the corporation devotedly, but with exceptional ability and skill. The President pointed out that although all of the officers and directors sincerely hoped and desired that Mrs. Feinberg would continue in her present position for as long as she felt able, nevertheless, in view of the length of service which she has contributed provision should be made to afford her retirement privileges and benefits which

should become a firm obligation of the corporation to be available to her whenever she should see fit to retire from active duty, however many years in the future such retirement may become effective. It was, accordingly, proposed that Mrs. Feinberg's salary which is presently \$350.00 per month, be increased to \$400.00 per month, and that Mrs. Feinberg would be given the privilege of retiring from active duty at any time she may elect to see fit so to do upon a retirement pay of \$200.00 per month for life, with the distinct understanding that the retirement plan is merely being adopted at the present time in order to afford Mrs. Feinberg security for the future and in the hope that her active services will continue with the corporation for many years to come. After due discussion and consideration, and upon motion duly made and seconded, it was—

“Resolved, that the salary of Anna Sacks Feinberg be increased from \$350.00 to \$400.00 per month and that she be afforded the privilege of retiring from active duty in the corporation at any time she may elect to see fit so to do upon retirement pay of \$200.00 per month, for the remainder of her life.”

At the request of Mr. Lippman his sons-in-law, Messrs. Harris and Flammer, called upon the plaintiff at her apartment on the same day to advise her of the passage of the resolution. Plaintiff testified on cross-examination that she had no prior information that such a pension plan was contemplated, that it came as a surprise to her, and that she would have continued in her employment whether or not such a resolution had been adopted. It is clear from the evidence that there was no contract, oral or written, as to plaintiff's length of employment, and that she was free to quit, and the defendant to discharge her, at any time.

Plaintiff did continue to work for the defendant through June 30, 1949, on which date she retired. In accordance with the foregoing resolution, the defendant began paying her the sum of \$200 on the first of each month. Mr. Lippman died on November 18, 1949, and was succeeded as president of the company by his widow. Because of an illness, she retired from that office and was succeeded in October, 1953, by her son-in-law, Sidney M. Harris. Mr. Harris testified that while Mrs. Lippman had been president she signed the monthly pension check paid plaintiff, but fussed about doing so, and considered the payments as gifts. After his election, he stated, a new accounting firm employed by the defendant questioned the validity of the payments to plaintiff on several occasions, and in the Spring of 1956, upon its recommendation, he consulted the Company's then attorney, Mr. Ralph Kalish. Harris testified that both Ernst and Ernst, the accounting firm, and Kalish told him there was no need of giving plaintiff the money. He also stated that he had concurred in the view that the payments to plaintiff were mere gratuities rather than amounts due under a contractual obligation, and that following his discussion with the Company's attorney plaintiff was sent a check for \$100 on April 1, 1956. Plaintiff declined to accept the reduced amount, and this action followed. Additional facts will be referred to later in this opinion. . . .

Appellant's next complaint is that there was insufficient evidence to support the court's findings that plaintiff would not have quit defendant's employ had she not known and relied upon the promise of defendant to pay her \$200 a month for life, and the finding that, from her voluntary retirement until April 1, 1956, plaintiff relied upon the continued receipt of the pension installments. The trial court so found, and, in our opinion, justifiably so. Plaintiff testified, and was corroborated by Harris, defendant's

witness, that knowledge of the passage of the resolution was communicated to her on December 27, 1947, the very day it was adopted. She was told at that time by Harris and Flammer, she stated, that she could take the pension as of that day, if she wished. She testified further that she continued to work for another year and a half, through June 30, 1949; that at that time her health was good and she could have continued to work, but that after working for almost forty years she thought she would take a rest. Her testimony continued:

“Q. Now, what was the reason—I’m sorry. Did you then quit the employment of the company after you—after this year and a half? A. Yes.

“Q. What was the reason that you left? A. Well, I thought almost forty years, it was a long time and I thought I would take a little rest.

“Q. Yes. A. And with the pension and what earnings my husband had, we figured we could get along.

“Q. Did you rely upon this pension? A. We certainly did.

“Q. Being paid? A. Very much so. We relied upon it because I was positive that I was going to get it as long as I lived.

“Q. Would you have left the employment of the company at that time had it not been for this pension? A. No.

“Mr. Allen: Just a minute, I object to that as calling for a conclusion and conjecture on the part of this witness.

“The Court: It will be overruled.

“Q. (Mr. Agatstein continuing): Go ahead, now. The question is whether you would have quit the employment of the company at that time had you not relied upon this pension plan? A. No, I wouldn’t.

“Q. You would not have. Did you ever seek employment while this pension was being paid to you—A. (interrupting): No.

“Q. Wait a minute, at any time prior—at any other place? A. No, sir.

“Q. Were you able to hold any other employment during that time? A. Yes, I think so.

“Q. Was your health good? A. My health was good.”

It is obvious from the foregoing that there was ample evidence to support the findings of fact made by the court below.

We come, then, to the basic issue in the case. While otherwise defined in defendant’s third and fourth assignments of error, it is thus succinctly stated in the argument in its brief: “. . . whether plaintiff has proved that she has a right to recover from defendant based upon a legally binding contractual obligation to pay her \$200 per month for life.”

It is defendant’s contention, in essence, that the resolution adopted by its Board of Directors was a mere promise to make a gift, and that no contract resulted either thereby, or when plaintiff retired, because there was no consideration given or paid by the plaintiff. It urges that a promise to make a gift is not binding unless supported by a legal consideration; that the only apparent consideration for the adoption of the foregoing resolution was the “many years of long and faithful service” expressed therein; and that past services are not a valid consideration for a promise. Defendant argues further that there is nothing in the resolution which made its effectiveness conditional upon plaintiff’s continued employment, that she was not under contract to work for any length of time but was free to quit

whenever she wished, and that she had no contractual right to her position and could have been discharged at any time.

Plaintiff concedes that a promise based upon past services would be without consideration, but contends that there were two other elements which supplied the required element: First, the continuation by plaintiff in the employ of the defendant for the period from December 27, 1947, the date when the resolution was adopted, until the date of her retirement on June 30, 1949. And, second, her change of position, i.e., her retirement, and the abandonment by her of her opportunity to continue in gainful employment, made in reliance on defendant's promise to pay her \$200 per month for life.

We must agree with the defendant that the evidence does not support the first of these contentions. There is no language in the resolution predicated plaintiff's right to a pension upon her continued employment. She was not required to work for the defendant for any period of time as a condition to gaining such retirement benefits. She was told that she could quit the day upon which the resolution was adopted, as she herself testified, and it is clear from her own testimony that she made no promise or agreement to continue in the employ of the defendant in return for its promise to pay her a pension. Hence there was lacking that mutuality of obligation which is essential to the validity of a contract. . . .

Consideration for a promise has been defined in the [Restatement of the Law of Contracts, Section 75](#), as:

“(1) Consideration for a promise is

- (a) an act other than a promise, or
- (b) a forbearance, or
- (c) the creation, modification or destruction of a legal relation, or
- (d) a return promise,

bargained for and given in exchange for the promise.”

As the parties agree, the consideration sufficient to support a contract may be either a benefit to the promisor or a loss or detriment to the promisee. . . .

[The rest of the opinion is set out at p. 97, below. There Feinberg prevails on her contention that the defendant's promise resulted in a “change of position” on her part.]

NOTES

(1) *The Missing Ingredient.* Feinberg conceded “that a promise based on past services would be without consideration.” Why was it so clear to everyone that her 37 years of service, prior to the resolution of December 27, 1947, could not be consideration for Pfeiffer's promise?

(2) *Drafting.* Suppose that Max Lippman had called in his lawyer in December, 1947, and said, “I want you to draw up a resolution that will make sure that Mrs. Feinberg will get a pension of \$200 a month as long as she lives.” How might the lawyer have drafted such a document? Would it have helped to include the words, “*in consideration of* her many years of long and faithful service”?

PROBLEM

In 1985, the Prentis family entered into an endowment contract, or gift agreement, with Wayne State University (“WSU”) under which the Prentis’s family foundation would give \$1,500,000 to WSU and WSU would name its cancer center the Meyer L. Prentis Comprehensive Cancer Center. The payments were completed in 1990. In 1995, the Karmanos family offered WSU a significant gift on the condition that the center be renamed the Barbara Ann Karmanos Cancer Institute. The center accepted. The Prentis family sued for breach of contract. Should they prevail?

In answering, consider the following language. In paragraph 1 of the agreement, the foundation agreed to contribute the money. In paragraph 2, WSU stated as follows:

In recognition of the significant and long-standing commitment of and leadership and support by the Prentis Foundation in the fields of cancer education, detection and research and the generous financial contributions made over many years by the Prentis Foundation in furtherance thereof; and in further recognition of and appreciation to the Prentis Foundation for the fund it is hereby creating, [WSU and the other parties] do hereby agree that Center shall be renamed and henceforth be known as the Meyer L. Prentis Comprehensive Cancer Center of Metropolitan Detroit.

See *Prentis Family Found. v. Barbara Ann Karmanos Cancer Inst.*, 698 N.W.2d 900 (Mich. Ct. App. 2005).

MORAL OBLIGATION

Mills v. Wyman

Supreme Judicial Court of Massachusetts, 1825.
3 Pick. 207, 20 Mass. 207.

[Levi Wyman, age 25, fell ill on his return from a sea voyage and, being poor and in distress, was cared for by Daniel Mills for about two weeks. A few days later, after all Mills’s expenses had been incurred, Seth Wyman, Levi’s father, wrote Mills promising to pay those expenses. When Seth Wyman decided not to pay, Mills sued him. From a direction of nonsuit, Mills appealed.]

■ PARKER, C.J. General rules of law established for the protection and security of honest and fair-minded men, who may inconsiderately make promises without any equivalent, will sometimes screen men of a different character from engagements which they are bound in *foro conscientiae* to perform. This is a defect inherent in all human systems of legislation. The rule that a mere verbal promise, without any consideration, cannot be enforced by action, is universal in its application, and cannot be departed from to suit particular cases in which a refusal to perform such a promise may be disgraceful.

The promise declared on in this case appears to have been made without any legal consideration. The kindness and services towards the sick son of the defendant were not bestowed at his request. The son

was in no respect under the care of the defendant. He was twenty-five years old, and had long left his father's family. On his return from a foreign country, he fell sick among strangers, and the plaintiff acted the part of the good Samaritan, giving him shelter and comfort until he died. The defendant, his father, on being informed of this event, influenced by a transient feeling of gratitude, promises in writing to pay the plaintiff for the expenses he had incurred. But he has determined to break this promise, and is willing to have his case appear on record as a strong example of particular injustice sometimes necessarily resulting from the operation of general rules.

It is said a moral obligation is a sufficient consideration to support an express promise; and some authorities lay down the rule thus broadly; but upon examination of the cases we are satisfied that the universality of the rule cannot be supported . . .

A deliberate promise, in writing, made freely and without any mistake, one which may lead the party to whom it is made into contracts and expenses, cannot be broken without a violation of moral duty. But if there was nothing paid or promised for it, the law, perhaps wisely, leaves the execution of it to the conscience of him who makes it. It is only when the party making the promise gains something, or he to whom it is made loses something, that the law gives the promise validity . . .

[T]here seems to be no case in which it was nakedly decided, that a promise to pay the debt of a son of full age, not living with his father, though the debt were incurred by sickness which ended in the death of the son, without a previous request by the father proved or presumed, could be enforced by action.

For the foregoing reasons we are all of opinion that the nonsuit directed by the Court of Common Pleas was right, and that judgment be entered thereon for costs for the defendant.

NOTES

(1) *The Case Against "Moral Obligation."* Mills v. Wyman accurately reflects the traditional common law view that a promise made in recognition of a "moral obligation" arising out of a benefit previously received is not enforceable. A benefit conferred before a promise is made can hardly be said to have been given in "exchange" for the promise. Williston noted further that "it is essential that the classes of promises which are [enforceable by law] shall be clearly defined. The test of moral consideration must vary with the opinion of every individual. Indeed, as has been said, since there is a moral obligation to perform every promise, it would seem that if morality was to be the guide, every promise would be enforced and if the existence of a past moral obligation is to be the test, every promise which repeats or restates a prior gratuitous promise would be binding." 1 Williston, *Treatise on the Law of Contracts* § 148 (1st ed. 1920).

(2) *Immoral without Obligation?* Suppose the letter from Seth Wyman to Daniel Mills had read as follows:

I received a line from you relating to my Son Levi's sickness and requesting me to come up and see him, but as the going is very bad I cannot come up at the present, but I wish you to take all possible care of him and if you cannot have him at your house I wish you to remove him to some convenient place and if he cannot satisfy you for it I will.

What, if anything, would Wyman have promised by such a letter? Would this language change your views of the elder Wyman? What if, in contradiction of court's statement, Levi Wyman had in fact not died? For more on the *Mills* case, see [Geoffrey R. Watson, In the Tribunal of Conscience: Mills v. Wyman Reconsidered](#), 71 Tul. L. Rev. 1749 (1997).

(3) *Recognized Exceptions*. As the court acknowledged in *Mills*, in certain exceptional situations the common law does enforce certain promises made in recognition of what could be viewed as a "moral obligation." These include a promise to pay a debt no longer legally enforceable because the statutory period of limitations has run, and a promise by an adult reaffirming a promise made when the promisor was a minor and that could have been avoided on that ground. A promise to pay a debt that has been discharged in bankruptcy constitutes a third exception. See Restatement §§ 82 and 83. What appears to explain these exceptions? (The enforceability of a promise to pay a debt unenforceable because of the promisor's discharge in bankruptcy is now subject to additional requirements under the Bankruptcy Code. 11 U.S.C. § 524(c)-(d) (2006).)

Webb v. McGowin

Court of Appeals of Alabama, 1935.
[27 Ala.App. 82, 168 So. 196.](#)

Action by Joe Webb against N. Floyd McGowin and Joseph F. McGowin, as executors of the estate of J. Greeley McGowin, deceased. From a judgment of nonsuit, plaintiff appeals.

■ BRICKEN, PRESIDING JUDGE. This action is in assumpsit. The complaint as originally filed was amended. The demurrers to the complaint as amended were sustained, and because of this adverse ruling by the court the plaintiff took a nonsuit, and the assignment of errors on this appeal are predicated upon said action or ruling of the court.

A fair statement of the case presenting the questions for decision is set out in appellant's brief, which we adopt.

"On the 3d day of August, 1925, appellant while in the employ of the W.T. Smith Lumber Company, a corporation, and acting within the scope of his employment, was engaged in clearing the upper floor of Mill No. 2 of the company. While so engaged he was in the act of dropping a pine block from the upper floor of the mill to the ground below; this being the usual and ordinary way of clearing the floor, and it being the duty of the plaintiff in the course of his employment to so drop it. The block weighed about 75 pounds.

"As appellant was in the act of dropping the block to the ground below, he was on the edge of the upper floor of the mill. As he started to turn the block loose so that it would drop to the ground, he saw J. Greeley McGowin, testator of the defendants, on the ground below and directly under where the block would have fallen had appellant turned it loose. Had he turned it loose it would have struck McGowin with such force as to have caused him serious bodily harm or death. Appellant could have remained safely on the upper floor of the mill by turning the block loose and allowing it to drop, but had he done this the block would have fallen on McGowin and caused him serious injuries or death. The only safe and reasonable way to prevent this was for appellant to hold to the block and divert its direction in falling from the place where McGowin was standing and the only safe way to di-

vert it so as to prevent its coming into contact with McGowin was for appellant to fall with it to the ground below. Appellant did this, and by holding to the block and falling with it to the ground below, he diverted the course of its fall in such way that McGowin was not injured. In thus preventing the injuries to McGowin appellant himself received serious bodily injuries, resulting in his right leg being broken, the heel of his right foot torn off and his right arm broken. He was badly crippled for life and rendered unable to do physical or mental labor.

“On September 1, 1925, in consideration of appellant having prevented him from sustaining death or serious bodily harm and in consideration of the injuries appellant had received, McGowin agreed with him to care for and maintain him for the remainder of appellant’s life at the rate of \$15 every two weeks from the time he sustained his injuries to and during the remainder of appellant’s life; it being agreed that McGowin would pay this sum to appellant for his maintenance. Under the agreement McGowin paid or caused to be paid to appellant the sum so agreed on up until McGowin’s death on January 1, 1934. After his death the payments were continued to and including January 27, 1934, at which time they were discontinued. Thereupon plaintiff brought suit to recover the unpaid installments accruing up to the time of the bringing of the suit.

“The material averments of the different counts of the original complaint and the amended complaint are predicated upon the foregoing statement of facts.” . . .

The action was for the unpaid installments accruing after January 27, 1934, to the time of the suit. . . .

1. The averments of the complaint show that appellant saved McGowin from death or grievous bodily harm. This was a material benefit to him of infinitely more value than any financial aid he could have received. Receiving this benefit, McGowin became morally bound to compensate appellant for the services rendered. Recognizing his moral obligation, he expressly agreed to pay appellant as alleged in the complaint and complied with this agreement up to the time of his death; a period of more than 8 years.

Had McGowin been accidentally poisoned and a physician, without his knowledge or request, had administered an antidote, thus saving his life, a subsequent promise by McGowin to pay the physician would have been valid. Likewise, McGowin’s agreement as disclosed by the complaint to compensate appellant for saving him from death or grievous bodily injury is valid and enforceable.

Where the promisee cares for, improves, and preserves the property of the promisor, though done without his request, it is sufficient consideration for the promisor’s subsequent agreement to pay for the service, because of the material benefit received. . . .

In *Boothe v. Fitzpatrick*, 36 Vt. 681, the court held that a promise by defendant to pay for the past keeping of a bull which had escaped from defendant’s premises and been cared for by plaintiff was valid, although there was no previous request, because the subsequent promise obviated that objection; it being equivalent to a previous request. On the same principle, had the promisee saved the promisor’s life or his body from grievous harm, his subsequent promise to pay for the services rendered would have been valid. Such service would have been far more material than caring for his bull. Any holding that saving a man from death or grievous bodily harm is

not a material benefit sufficient to uphold a subsequent promise to pay for the service, necessarily rests on the assumption that saving life and preservation of the body from harm have only a sentimental value. The converse of this is true. Life and preservation of the body have material, pecuniary values, measurable in dollars and cents. Because of this, physicians practice their profession charging for services rendered in saving life and curing the body of its ills, and surgeons perform operations. The same is true as to the law of negligence, authorizing the assessment of damages in personal injury cases based upon the extent of the injuries, earnings, and life expectancies of those injured.

In the business of life insurance, the value of a man's life is measured in dollars and cents according to his expectancy, the soundness of his body, and his ability to pay premiums. The same is true as to health and accident insurance.

It follows that if, as alleged in the complaint, appellant saved J. Greeley McGowin from death or grievous bodily harm, and McGowin subsequently agreed to pay him for the service rendered, it became a valid and enforceable contract.

2. It is well settled that a moral obligation is a sufficient consideration to support a subsequent promise to pay where the promisor has received a material benefit, although there was no original duty or liability resting on the promisor. [Cases cited.]

The case at bar is clearly distinguishable from that class of cases where the consideration is a mere moral obligation or conscientious duty unconnected with receipt by promisor of benefits of a material or pecuniary nature. . . . Here the promisor received a material benefit constituting a valid consideration for his promise.

3. Some authorities hold that, for a moral obligation to support a subsequent promise to pay, there must have existed a prior legal or equitable obligation, which for some reason had become unenforceable, but for which the promisor was still morally bound. This rule, however, is subject to qualification in those cases where the promisor having received a material benefit from the promisee, is morally bound to compensate him for the services rendered and in consideration of this obligation promises to pay. In such cases the subsequent promise to pay is an affirmance or ratification of the services rendered carrying with it the presumption that a previous request for the service was made. . . .

4. The averments of the complaint show that in saving McGowin from death or grievous bodily harm, appellant was crippled for life. This was part of the consideration of the contract declared on. McGowin was benefited. Appellant was injured. Benefit to the promisor or injury to the promisee is a sufficient legal consideration for the promisor's agreement to pay. . . .

5. Under the averments of the complaint the services rendered by appellant were not gratuitous. The agreement of McGowin to pay and the acceptance of payment by appellant conclusively shows the contrary. . . .

From what has been said, we are of the opinion that the court below erred in the ruling complained of; that is to say in sustaining the demurrer, and for this error the case is reversed and remanded.

Reversed and remanded.

■ SAMFORD, JUDGE (concurring). The questions involved in this case are not free from doubt, and perhaps the strict letter of the rule, as stated by judges, though not always in accord, would bar a recovery by plaintiff, but following the principle announced by Chief Justice Marshall in [Hoffman v. Porter](#), Fed.Cas. No. 6,577, 2 Brock. 156, 159, where he says, “I do not think that law ought to be separated from justice, where it is at most doubtful,” I concur in the conclusions reached by the court.

[Part of the short opinion of the Supreme Court of Alabama, denying certiorari, is set out next.]

■ FOSTER, JUSTICE. . . . The opinion of the Court of Appeals here under consideration recognizes and applies the distinction between a supposed moral obligation of the promisor, based upon some refined sense of ethical duty, without material benefit to him, and one in which such a benefit did in fact occur. We agree with that court that if the benefit be material and substantial, and was to the person of the promisor rather than to his estate, it is within the class of material benefits which he has the privilege of recognizing and compensating either by an executed payment or an executory promise to pay. The cases are cited in that opinion. The reason is emphasized when the compensation is not only for the benefits which the promisor received, but also for the injuries either to the property or person of the promisee by reason of the service rendered.

Writ denied.

Harrington v. Taylor

Supreme Court of North Carolina, 1945.
225 N.C. 690, 36 S.E. 2d 227.

■ PER CURIAM.

The plaintiff in this case sought to recover of the defendant upon a promise made by him under the following peculiar circumstances:

The defendant had assaulted his wife, who took refuge in plaintiff's house. The next day the defendant gained access to the house and began another assault upon his wife. The defendant's wife knocked him down with an axe, and was on the point of cutting his head open or decapitating him while he was laying on the floor, and the plaintiff intervened, caught the axe as it was descending, and the blow intended for defendant fell upon her hand, mutilating it badly, but saving defendant's life.

Subsequently, defendant orally promised to pay the plaintiff her damages; but, after paying a small sum, failed to pay anything more. So, substantially, states the complaint.

The defendant demurred to the complaint as not stating a cause of action, and the demurrer was sustained. Plaintiff appealed.

The question presented is whether there was a consideration recognized by our law as sufficient to support the promise. The Court is of the opinion that, however much the defendant should be impelled by common gratitude to alleviate the plaintiff's misfortune, a humanitarian act of this kind, voluntarily performed, is not such consideration as would entitle her to recover at law.

The judgment sustaining the demurrer is
Affirmed.

NOTES

(1) *The Case for “Moral Obligation.”* “Courts have frequently enforced promises on the simple ground that the promisor was only promising to do what he ought to have done anyway. These cases have either been condemned as wanton departures from legal principle, or reluctantly accepted as involving the kind of compromise logic must inevitably make at times with sentiment. I believe that these decisions are capable of rational defense. When we say the defendant was morally obligated to do the thing he promised, we in effect assert the existence of a substantive ground for enforcing the promise. . . . The court’s conviction that the promisor ought to do the thing, plus the promisor’s own admission of his obligation, may tilt the scales in favor of enforcement where neither standing alone would be sufficient. If it be argued that moral consideration threatens certainty, the solution would seem to lie, not in rejecting the doctrine, but in taming it by continuing the process of judicial exclusion and inclusion already begun in the cases involving infants’ contracts, barred debts, and discharged bankrupts.” Fuller, *Consideration and Form*, 41 *Colum. L. Rev.* 799, 821–822 (1941).

(2) *Reconciling Webb and Harrington.* These two cases are less than ten years apart. What factors might explain the difference in outcome?

(3) *Reform by Statute.* New York law does not recognize “moral obligation” as an equivalent of consideration, but a New York statute enacted in 1941 and now found in General Obligations Law § 5–1105 provides: “A promise in writing and signed by the promisor or by his agent shall not be denied effect as a valid contractual obligation on the ground that consideration for the promise is past or executed, if the consideration is expressed in the writing and is proved to have been given or performed and would be a valid consideration but for the time when it was given or performed.”

How would the New York statute have affected the preceding cases? Would the common recital “for value received” satisfy the New York statute? Would you favor the adoption of that statute by other states? What about the adoption of a statute enacting Restatement § 86?

(C) THE REQUIREMENT OF BARGAIN**Kirksey v. Kirksey**

Supreme Court of Alabama, 1845.

8 Ala. 131.

The plaintiff was the wife of defendant’s brother, but had for some time been a widow, and had several children. In 1840, the plaintiff resided on public land, under a contract of lease, she had held over, and was comfortably settled, and would have attempted to secure the land she lived on. The defendant resided in Talladega County, some sixty or seventy miles off. On the 10th October, 1840, he wrote to her the following letter:

“Dear Sister Antillico,—Much to my mortification, I heard that brother Henry was dead, and one of his children. I know that your situation is one of grief and difficulty. You had a bad chance before, but a great deal worse now. I should like to come and see you, but cannot with convenience at pre-

sent. . . . I do not know whether you have a preference on the place you live on or not. If you had, I would advise you to obtain your preference, and sell the land and quit the country, as I understand it is very unhealthy, and I know society is very bad. If you will come down and see me, I will let you have a place to raise your family, and I have more open land than I can tend; and on account of your situation, and that of your family, I feel like I want you and the children to do well.”

Within a month or two after the receipt of this letter, the plaintiff abandoned her possession, without disposing of it, and removed with her family, to the residence of the defendant, who put her in comfortable houses, and gave her land to cultivate for two years, at the end of which time he notified her to remove, and put her in a house, not comfortable, in the woods, which he afterwards required her to leave.

A verdict being found for the plaintiff, for \$200, the above facts were agreed, and if they will sustain the action, the judgment is to be affirmed, otherwise it is to be reversed.

■ ORMOND, J. The inclination of my mind is that the loss and inconvenience which the plaintiff sustained in breaking up and moving to the defendant's, a distance of sixty miles, is a sufficient consideration to support the promise to furnish her with a house, and land to cultivate, until she could raise her family. My brothers, however, think that the promise on the part of the defendant was a mere gratuity, and that an action will not lie for its breach. The judgment of the court below must therefore be reversed, pursuant to the agreement of the parties.

NOTES

(1) *Conditional Gift or Bargained-For Exchange?* How did the court read the words, “If you will come down and see me, I will let you have a place to raise your family”? As words of bargain for an exchange or as a condition to a gratuitous promise? What factors (language, circumstances, indications of intent) make the sentence appear more like the promise of a gift? More like a proposal of a bargain?

(2) *Lunchtime at Tiffany's.* A father and his daughter became estranged after her mother divorced the father, and the daughter refused to see her father. The father then wrote to his daughter: “If you will meet me at Tiffany's next Monday at noon, I will buy you the emerald ring advertised in this week's *New Yorker*.” The daughter met her father at Tiffany's, but he did not buy her the promised ring. Bargained-for exchange or conditional gratuitous promise?

Williston put this case: “If a benevolent man says to a tramp, ‘If you go around the corner to the clothing shop there, you may purchase an overcoat on my credit,’ no reasonable person would understand that the short walk was requested as the consideration for the promise; rather, the understanding would be that in the event of the tramp going to the shop the promisor would make him a gift.” This first appeared in 1 Williston, *A Treatise on the Law of Contracts* § 112 (1st ed. 1920). Is the situation of the daughter distinguishable from that of the tramp?

(3) *The Million Dollar Swipe.* While vacationing at Atlantic City, New Jersey, Rena Gottlieb went to a promotional booth at the Tropicana Casino and joined the Tropicana's Diamond Club by filling out a simple application. She received a card that club members swipe before playing any machine. The

swipe provides information about members' gambling habits, which is then used by the casino's marketing department to tailor its promotions. Diamond Club members are entitled to one free spin daily of the Fun House Million Dollar Wheel. After swiping in, Gottlieb spun the wheel, which landed on the million dollar mark. Tropicana refused to pay on the ground that there was no consideration for her participation in the Diamond Club promotion. She sued the Tropicana Casino and Resort for \$1,000,000. Bargained-for exchange, conditional gift, or gratuitous promise? *Held*: For plaintiff. [Gottlieb v. Tropicana Hotel and Casino, 109 F.Supp.2d 324 \(E.D. Pa. 2000\)](#):

Ms. Gottlieb had to go to the casino to participate in the promotion. She had to wait in line to spin the wheel. By . . . allowing her [Diamond Club card] to be swiped into the casino's machine, she was permitting the casino to gather information about her gambling habits. Additionally, by participating in the game, she was a part of the entertainment that casinos, by their very nature, are designed to offer to all of those present. All of these detriments . . . were 'the requested detriment[s] to the promisee induced by the promise' of Tropicana to offer her a chance to win \$1 million. Tropicana's motives in offering the promotion were 'in nowise altruistic.' Tropicana offered the promotion in order to generate patronage of and excitement within the casino. In short, Ms. Gottlieb provided adequate consideration to form a contract with Tropicana.

Id. at 329-30. The case was remanded to determine the factual question of whether the marker firmly landed on the million-dollar mark, or immediately fell off, as the Casino claimed.

PROBLEMS

(1) *Jailhouse Rock*. Steve Jennings, a prisoner in Texas, was a faithful listener to radio station KSCS, which regularly broadcast that it played "at least three-in-a-row, or we pay you \$25,000. No bull, more music on KSCS." Jennings sued KSCS, alleging that each time it played "five-in-a-row" it played only three songs, followed by a brief commercial, and then only *two* songs, but that when he notified KSCS on specific occasions of this they refused to pay him \$25,000. He also alleged that he then stopped listening to KSCS. KSCS has moved to dismiss on the ground that there was no consideration for its promise. What decision? See [Jennings v. Radio Station KSCS, 96.3 FM, Inc., 708 S.W.2d 60 \(Tex.App.1986\)](#).

(2) *Open and Shut*. Joshua Gnaizda, the three-year-old son of a prominent San Francisco-area public-interest attorney, received what he (or his mother) thought was a tantalizing offer from Time, Inc. The front of the envelope contained two see-through windows. One window showed Joshua's name and address. The other revealed the following statement: "JOSHUA A. GNAIZDA, I'LL GIVE YOU THIS VERSATILE NEW CALCULATOR WATCH FREE just for opening this envelope before Feb. 15, 1985." Beneath the offer was a picture of the watch itself. Joshua's mother opened the envelope and realized she had been deceived by a ploy to get her to open a piece of junk mail. The see-through window had not revealed the full text of Time's offer. Printed below the picture of the watch, and not visible through the see-through window, were the following additional words: "AND MAILING THIS CERTIFICATE TODAY!" The certificate itself clearly required that Joshua purchase a subscription to Fortune magazine in order to receive the watch. Joshua's father sued Time on behalf of

Joshua and two others who had been similarly bamboozled. Time moved to dismiss for want of consideration. What result? See [Harris v. Time, Inc.](#), 237 Cal. Rptr. 584 (Ct. App. 1987).

(3) *One Person's Trash*. Pennsy Supply, a paving subcontractor, was hired to pave the parking lot of a new high school. The project specifications stated that the paving contractor could use AggRite, a treated ash by-product, as part of the base. AggRite was available from American Ash. American Ash made AggRite available free so that it could save the cost of disposal. Pennsy picked up and used 11,000 tons of AggRite. The work had to be redone, however, partly because the AggRite was not suited for use as a base for paving. Pennsy thus had to dig up the AggRite. Pennsy asked American Ash to arrange for its removal and disposal (AggRite is considered a hazardous waste material). American Ash declined. Pennsy paid for the disposal itself and then sued American Ash for breach of contract, requesting damages that included its disposal costs. American Ash has asserted a good many defenses, including that Pennsy received the AggRite as a conditional gift, not as part of a contract supported by consideration. What result? See [Pennsy Supply v. Am. Ash Recycling Corp.](#), 895 A.2d 595 (Pa. Super. 2006).

EMPLOYMENT AGREEMENTS

The next case introduces the category of personal service or employment agreements. For more than six centuries, important aspects of the employment relationship were governed by statute. For example, the Statute of Laborers, 23 Edw. 3 (1349), imposed a duty to work on most able-bodied adults, and later Elizabethan enactments established a minimum one-year duration for all employment contracts. Agreements between master and servant, as the parties were then called, shifted to a contractual model as industrialization and the philosophy of *laissez faire* took hold. A detailed account of the rise of bargaining, including collective bargaining, and of current statutory regimes such as minimum-wage, safety, and anti-discrimination law, is left to courses on labor and employment law. As you read the employment cases that follow, consider how background policies regarding the right to work or the prevention of idleness have influenced the development of common-law contract doctrine.

Our interest here is how basic contract principles play out in the circumstances of employment, including decisions about hiring and firing. We focus particularly on “at-will” employment, which is a category of employment that is terminable by either party at any time. We begin with the problem of bargained-for exchange between employers and employees when, as is often the case, the terms of the agreement are not entirely settled at a single moment. Determining these terms is crucial to deciding whether an employee has been wrongfully fired. In our first case, however, it is the *employer* who seeks to enforce the promise of an at-will employee. The term at issue concerns post-employment conduct, specifically the employee’s promise not to compete with his former employer.

Lake Land Employment Group of Akron, LLC v. Columber

Supreme Court of Ohio, 2004.
101 Ohio St.3d 242, 804 N.E.2d 27.

■ MOYER, C.J. Lake Land Employment Group of Akron, LLC (“Lake Land”), appellant, initiated this action by filing a complaint asserting that its ex-employee, appellee Lee Columber, had breached a noncompetition agreement the parties had executed. The agreement provided that for a period of three years after his termination of employment Columber would not engage in any business within a 50-mile radius of Akron, Ohio, that competed with the business of Lake Land. Lake Land further claimed that Columber’s employment with Lake Land terminated in 2001 and that he thereafter violated the terms of the noncompetition agreement. Lake Land sought money damages and an order prohibiting Columber from engaging in any activities that violated the noncompetition agreement.

Columber answered and admitted that he had been employed by Lake Land from 1988 until 2001. He further admitted that he had signed the noncompetition agreement and that following his discharge from Lake Land he had formed a corporation that is engaged in a business similar to that of Lake Land. Columber pled lack of consideration in his answer. Columber moved for summary judgment, claiming that the noncompetition agreement was unenforceable . . . and that the restrictions in the agreement were overly restrictive and imposed an undue hardship on him.

Columber could remember very little about the presentation or execution of the noncompetition agreement. He could not remember whether he had been told that his continued employment was dependent upon execution of the agreement or whether he had posed questions about the restrictions it contained. He testified that he vaguely remembered signing the agreement after his employer presented it to him and told him to read and sign it. He acknowledged that he had read the agreement, but had not talked to an attorney or anybody else about it. The at-will relationship of the parties continued for ten years thereafter.

The trial court granted summary judgment in Columber’s favor. It found no dispute that Columber had been employed by Lake Land beginning in 1988 and that Columber signed the agreement in September 1991. It further found no dispute that there “was no increase of salary, benefits, or other remunerations given as consideration for Columber signing the non-competition agreement” and “no change in his employment status in connection with the signing of the noncompetition agreement.” The trial court concluded that the noncompetition agreement lacked consideration, and was unenforceable. The trial court therefore found it unnecessary to determine the reasonableness of the temporal and geographical restrictions in the noncompetition agreement.

The court of appeals affirmed. It certified a conflict, however, between its decision and [those of other Ohio district courts of appeals]. The certified issue is “Is subsequent employment alone sufficient consideration to support a covenant-not-to-compete agreement with an at-will employee entered into after employment has already begun?”

I

Legal Background

Generally, courts look upon noncompetition agreements with some skepticism and have cautiously considered and carefully scrutinized them. [Ingram, Covenants Not to Compete \(2002\)](#), 36 *Akron L. Rev.* 49, 50. Under English common law, agreements in restraint of trade, including noncompetition agreements, were disfavored as being against public policy, although partial restraints supported by fair consideration were upheld . . . In a society in which working men entered skilled trades only by serving apprenticeships, and mobility was minimal, restrictive covenants precluding an ex-employee from competing with his ex-employer “either destroyed a man’s means of livelihood, or bound him to his master for life.” [Raimonde v. Van Vlerah \(1975\)](#), 325 *N.E.2d* 544.

Modern economic realities, however, do not justify a strict prohibition of noncompetition agreements between employer and employee in an at-will relationship. “The law upholds these agreements because they allow the parties to work together to expand output and competition. If one party can trust the other with confidential information and secrets, then both parties are better positioned to compete with the rest of the world. . . . By protecting ancillary covenants not to compete, even after an employee has launched his own firm, the law ‘makes it easier for people to cooperate productively in the first place.’” [KW Plastics v. United States Can Co \(Feb. 2, 2001\)](#), *M.D. Ala. Nos. Civ. A. 99–D–286–N and 99–D–878–N*, 2001 *WL* 135722, quoting [Polk Bros., Inc. v. Forest City Ent., Inc. \(C.A.7, 1985\)](#), 776 *F.2d* 185, 189. . . .

Jurisdictions throughout the country are split on the issue presented by the certified question. See, generally, [Annotation, Sufficiency of Consideration for Employee’s Covenant Not to Compete, Entered into after Inception of Employment \(1973\)](#), 51 *A.L.R.3d* 825. As summarized by the Supreme Court of Minnesota, “cases which have held that continued employment is not a sufficient consideration stress the fact that an employee frequently has no bargaining power once he is employed and can easily be coerced. By signing a noncompetition agreement, the employee gets no more from his employer than he already has,¹ and in such cases there is a danger that an employer does not need protection for his investment in the employee but instead seeks to impose barriers to prevent an employee from securing a better job elsewhere. Decisions in which continued employment has been deemed a sufficient consideration for a noncompetition agreement have focused on a variety of factors, including the possibility that the employee would otherwise have been discharged, the employee was actually employed for a substantial time after executing the contract, or the employee received additional compensation or training or was given confidential information after he signed the agreement.” (Citations omitted.) [Davies & Davies Agency, Inc. v. Davies \(Minn. 1980\)](#) 298 *N.W.2d* 127, 130.

More recently, some courts have found sufficient consideration in an at-will employment situation where a *substantial* period of employment ensues after a noncompetition covenant is executed, especially when the continued employment is accompanied by raises, promotion, or similar tangible benefits. 6 *Lord, Williston on Contracts (4th Ed.1995)*, Section 13:13.

¹ Note, however, that an at-will employee does not already have a right to come to work in the future at all, let alone under past terms of employment. Although both parties may very well contemplate continuation of the relationship, either may terminate it at any time.

These courts thereby implicitly find that the execution of a noncompetition agreement changes the prior employment relationship from one purely at will. *Id.* at 577–584. In effect, these courts infer a promise on the part of the employer to continue the employment of his previously at-will employee for an indefinite yet substantial term. Under this approach, however, neither party knows whether the agreement is enforceable until events occur after its execution.

This diversity of approach to the issue is reflected in opinions of the courts of appeals of this state. . . .

II. Formation of Binding Contract

[In a passage omitted here the court reviewed some elementary characteristics of contract law, and of at-will employment agreements.]

. . . [E]ither an employer or an employee in a pure at-will employment relationship may legally terminate the employment relationship at any time and for any reason. *Mers v. Dispatch Printing Co.* (1985), 19 Ohio St.3d 100, 103, 19 OBR 261, 483 N.E.2d 150. In the event that an at-will employee quits or is fired, he or she provides no further services for the employer and is generally entitled only to wages and benefits already earned.

It follows that either an employer or an employee in an at-will relationship may propose to change the terms of their employment relationship at any time. If, for instance, an employer notifies an employee that the employee's compensation will be reduced, the employee's remedy, if dissatisfied, is to quit. Similarly, if the employee proposes to the employer that he deserves a raise and will no longer work at his current rate, the employer may either negotiate an increase or accept the loss of his employee. In either event the employee is entitled to be paid only for services already rendered pursuant to terms to which they both have agreed. Thus, mutual promises to employ and to be employed on an ongoing at-will basis, according to agreed terms, are supported by consideration: the promise of one serves as consideration for the promise of the other.

The presentation of a noncompetition agreement by an employer to an at-will employee is, in effect, a proposal to renegotiate the terms of the parties' at-will employment. Where an employer makes such a proposal by presenting his employee with a noncompetition agreement and the employee assents to it, thereby accepting continued employment on new terms, consideration supporting the noncompetition agreement exists. The employee's assent to the agreement is given in exchange for forbearance on the part of the employer from terminating the employee.

We therefore hold that consideration exists to support a noncompetition agreement when, in exchange for the assent of an at-will employee to a proffered noncompetition agreement, the employer continues an at-will employment relationship that could legally be terminated without cause.

III. Caveat

We concur in the view that in cases involving noncompetition agreements, "as in other cases, it is still believed to be good policy to let people make their own bargains and their own valuations." 15 Corbin on Contracts (Interim Ed.2002) 96–97, Section 1395. Professor Corbin suggests that courts should inquire into the sufficiency of consideration in cases involving noncompetition agreements by examining the extent and character

of the consideration received by the promisor-employee, “even though we do not do so in ordinary contract cases.” *Id.* at 94–95.

Our decision today does no more than recognize that consideration exists where an at-will employer and an at-will employee continue their employment relationship, rather than terminate it, after the employer imposes a new requirement for employment, i.e., execution of a noncompetition agreement by the employee. While we are not prepared to abandon our long-established precedent that courts may not inquire into the adequacy of consideration, we do not disagree with Corbin’s conclusion that the validity of a restraining contract such as a noncompetition agreement should be “determined by weighing as best we can the sum-total of all factors standing together.” *Id.* at 97. We simply recognize that weighing of these factors should not be performed in the context of an inquiry concerning the sufficiency of consideration. That balancing instead should occur in the context of our established precedent recognizing that only reasonable noncompetition agreements are enforceable. . . .

Our refusal to sanction judicial inquiry into the adequacy of consideration in cases similar to the one at bar does not exclude consideration of other requisites of a contract. It remains the law that noncompetition agreements, like other purported contractual arrangements, may be voidable or unenforceable for reasons other than lack of consideration. . . .

IV. Disposition

Both Columber and his employer had a legal right to terminate their at-will employment relationship when Columber was presented with the noncompetition agreement in 1991. Neither party exercised that legal right to terminate the employment relationship, and, in fact, Columber continued working for the appellant for an additional ten years. Accordingly, the noncompetition agreement is not void for lack of consideration, and summary judgment in Columber’s favor should not have been entered on that basis.

Although the trial court erred in entering summary judgment based on its determination that the noncompetition agreement lacked consideration, it must yet determine whether the noncompetition agreement is reasonable pursuant to controlling precedent. We therefore reverse the judgment of the court of appeals and remand the cause for further proceedings.

Judgment reversed and cause remanded.

■ RESNICK, J., DISSENTING. Courts everywhere are sharply divided on the present certified issue. However, I adhere to the principle that continued employment in an at-will situation does not by itself constitute consideration. I respectfully dissent.

As the majority confirms, “a contract is not binding unless supported by consideration,” which is generally defined as “a detriment to the promisee or a benefit to the promisor.” Thus, in order for the September 1991 noncompetition agreement executed between appellant, Lake Land Employment Group of Akron, LLC, and appellee, Lee Columber, to be binding, either Lake Land must have given something for it or Columber must have received something in return. Yet, when all is said and done, the only difference in the parties’ employment relationship before and after September 1991 is the noncompetition agreement.

The majority’s holding that “[c]onsideration exists to support a noncompetition agreement when . . . the employer continues an at-will em-

ployment relationship . . .” belies itself. If the same at-will employment relationship continues, where is the consideration? The employer has relinquished nothing, since it retains exactly the same preexisting right it always had to discharge the employee at any time, for any reason, for no reason, with or without cause. The employee has gained nothing, for he has not been given or promised anything other than that which he already had, which is “employment which need not last longer than the ink is dry upon [his] signature.” *Kadis v. Britt* (1944), 224 N.C. 154, 163, 29 S.E.2d 543. It is precisely because the same at-will employment relationship continues that there is no consideration.

In fact, the majority endeavors to transform this mutual exchange of nothing into consideration by formulating such artful euphemisms as “forbearance on the part of an at-will employer from discharging an at-will employee,” “mutual promises to employ and to be employed on an ongoing at-will basis,” and “a proposal to renegotiate the terms of the parties’ at-will employment.” But in the end, the employer simply winds up with both the noncompetition agreement and the continued right to discharge the employee at will, while the employee is left with the same preexisting “nonright” to be employed for so long as the employer decides not to fire him. The only actual “forbearance,” “proposal,” or “promise” made by the employer in this situation is declining to fire the employee until he executes the noncompetition agreement.

Moreover, the majority’s holding and supporting rationale would allow the enforcement of a noncompetition agreement that was exacted from an employee who, at the time of execution, had already acquired all the knowledge his or her position affords and who was fired the day after affixing his or her signature to the document. In cryptic fashion, the majority is essentially holding that a restrictive covenant may henceforth be exacted from an at-will employee without any supporting consideration . . .

Since the noncompetition agreement in this case lacked consideration and therefore was unenforceable, I would affirm the judgment of the court of appeals.

■ PFEIFER, J., DISSENTING. I concur with Justice Resnick’s dissent—an employer’s agreement not to terminate an employee if the employee signs a noncompetition agreement does not constitute consideration. It constitutes coercion.

But the majority has found otherwise. In doing so, the majority must acknowledge that the execution of a noncompetition agreement for which forbearance from discharge is the consideration alters the at-will nature of the employment relationship. Any promise of continued employment removes the employment from the realm of an at-will relationship. For some undefined time, the employer must continue to employ the signer of the agreement. How long a period is enough? The absence of a specified term for the forbearance from discharge will leave courts to determine what period is reasonable.

Employers could prevent noncompetition agreements from intruding into the at-will relationship by not tying consideration to continued employment. A separate, monetary consideration could ensure that the noncompetition agreement stays a separate arrangement.

NOTES

(1) *Questions.* What is the significance of Columber's status as an at-will employee in the court's determination that his promise not to compete was supported by consideration? Do you agree with Chief Justice Moyer or Justice Resnick (a "mutual exchange of nothing")? Does the majority opinion rest on policy considerations, the straightforward application of doctrine, or both? What policy considerations weigh in favor of Columber? In favor of Lake Land Employment?

(2) *Dueling Dissents.* Although Justice Pfeifer professed to agree with Justice Resnick, the two dissents appear to disagree with regard to the effect of the court's ruling. Justice Resnick concludes that "in the end, the employer simply winds up with both the noncompetition agreement and the continued right to discharge the employee at will." Contrast Justice Pfeifer's understanding that "the execution of the noncompetition agreement . . . alters the at-will nature of the employment relationship." How does it do so? If Justice Pfeifer is right, how would a court go about deciding what period of time is reasonable? If these are opposing views, which is the more favorable to employees?

(3) *Jurisdictional Differences.* The Supreme Court of Minnesota has held that "where no raises or promotions resulted, where other employees with similar access were not asked to sign, the mere continuation of employment . . . is not enough." *Jostens, Inc. v. National Computer Systems, Inc.*, 318 N.W.2d 691, 703–04 (Minn.1982). The decision typifies judicial hostility in a number of states to promises not to compete. For additional helpful analyses, see Cynthia Estlund, *Between Rights and Contract: Arbitration Agreements and Non-Compete Covenants as a Hybrid Form of Employment Law*, 155 U. Pa. L. Rev. 379 (2006), and Katherine Stone, *Revisiting the At-Will Employment Doctrine: Imposed Terms, Implied Terms, and the Normative World of the Workplace* 36 *Industrial L.J.* 84 (2007).

Only a few months after *Jostens*, the same court said: "We look upon restrictive covenants with disfavor, carefully scrutinizing them because they are agreements in partial restraint of trade." *National Recruiters, Inc. v. Cashman*, 323 N.W.2d 736, 740 (Minn.1982). Judicially imposed constraints on such agreements are discussed further in the materials on public policy in Chapter 4.

PROBLEM

A Revolting Development. In 1997, American Energy Services (AES) was in financial trouble. The AES employees, all of them at-will, knew of the situation and informed officers of AES that they doubted whether the company would survive. In order to keep the employees from resigning, an AES vice-president promised the employees that, "in the event of sale or merger of AES, the original [eight] employees remaining with AES at that time would get 5% of the value of any sale or merger of AES." Seven of the eight were still with AES in 2001 when another company bought it. The seven demanded their proceeds; when they did not get them, they sued. AES defended in part on the grounds that the promise was illusory, because the employees were not bound to do anything under the alleged contract. What result? Would it matter if the employees were not at-will, but rather were hired under long-term employment agreements in force both when AES made the promise and when AES was bought? What if the eight original employees had each signed a document stating that

any one who leaves AES's before a sale or merger would not share in the proceeds of that transaction? See [Vanegas v. American Energy Servs.](#), 302 S.W.3d 299 (Tex. 2009).

EMPLOYEE HANDBOOKS

In *Lake Land Employment*, the question was whether or not the *employee's* promise not to compete was supported by consideration. Questions about the term of employment also arise with regard to the enforceability of *employers'* promises, often in the context of employee handbooks. Typically, and often some time after they have been hired, employees receive handbooks setting out company policies on matters ranging from vacation schedules to job security. Is the employer bound by these policies? Most employees do not bargain for the policies, and many may not have read or in some cases have even received a handbook. The following case is illustrative.

Mettille, a loan officer and at-will employee at the Pine River State Bank, was fired by the bank president, Griffith, for serious deficiencies in processing over \$600,000 worth of loans. Griffith had earlier prepared and distributed a printed Employee Handbook with information on various bank policies including "job security" and "disciplinary policy." In firing Mettille, Griffith failed to follow Handbook rules relating to "disciplinary policy." Mettille argued that Griffith was bound by those policies. Griffith countered that the handbook was intended only as a source of information for employees on bank procedures and that, in any case, it could not be part of an employee's employment contract because it was unsupported by consideration. In an action by Mettille against the bank, he won a money judgment. The Supreme Court of Minnesota affirmed the judgment, stating:

An employer's offer of a unilateral contract may very well appear in a personnel handbook as the employer's response to the practical problem of transactional costs. Given these costs, an employer, such as the bank here, may prefer not to write a separate contract with each individual employee. . . . Mettille's continued performance of his duties despite his freedom to quit constitutes an acceptance of the bank's offer and affords the necessary consideration for that offer, with the bank gaining the advantages of a more stable and, presumably, more productive work force.

[Pine River State Bank v. Mettille](#), 333 N.W.2d 622, 627–30 (Minn.1983).

The Court compared this approach with its cases holding that employee noncompete covenants signed after the initial employment contract "are not enforceable absent a showing of independent consideration involving something more than just continued services." *Id.* at 630 n.5. The Court noted that, with regard to the covenants not to compete, "a different public policy is at play, namely, the law's disfavor with restraints on trade, so that noncompete covenants are treated as a special circumstance and, therefore, these cases are not decided strictly according to the principles of contract formation." *Id.*

NOTES

(1) *Promise or Policy?* Not all representations in a handbook become terms of an at-will employee's contract. The court found that Pine River State Bank's statements about job security, as distinguished from its disciplinary policy, were "no more than a general statement of policy" in contrast to the "definite language" used to set out the disciplinary policy. *Id.* at 630. Consider the following paragraph from another Employee Handbook:

ACKNOWLEDGMENT: This employee handbook describes important information about the Company and I understand that I should consult the Business Manager regarding any questions not answered in the handbook. The provisions contained in this handbook are presented as a matter of information only and do not constitute an employment contract. I have entered into my employment relationship with the Company voluntarily and acknowledge that there is no specified length of employment. At any time, either I or the Company can terminate the relationship at-will, with or without cause or notice, as long as there is no violation of applicable federal or state law. I also understand that because business judgments and needs may change from time to time, the guidelines described herein are not conditions of employment. The Company has the right to change this handbook at any time and without advance notice. I have received a copy of Pflueger Group's Employee Handbook and I have read and understand the information outlined in the handbook. I have asked any questions I may have concerning its contents and will comply with all policies and procedures to the best of my ability.

What purposes is it intended to serve? (The paragraph is taken from *Douglass v. Pflueger*, found at p. 342 below.)

(2) *Modifications of Employee Handbooks.* To the extent that the terms of an employee handbook become part of an employment contract, can an employer unilaterally change or modify its terms so as to reduce the employee's rights? Several courts have answered No. "If the disclaimer modifies an existing employment contract requiring termination for cause, the employer must provide consideration to make the disclaimer effective." *Worley v. Wyoming Bottling Company, Inc.*, 1 P.3d 615, 621 (Wyo.2000); see also *Doyle v. Holy Cross Hospital*, 708 N.E.2d 1140 (Ill.1999). Would a clause in a handbook addressing "the Company's right to change this handbook," as in the form provided in Note 1 above, change the employer's right to modify? The modification of contract terms is examined more generally in Chapter 4.

(3) *An Administrative Law Model?* In *In re Certified Question (Bankey v. Storer Broadcasting)*, 443 N.W.2d 112 (Mich.1989), the court held that an employer *may* alter the terms of employment for existing employees by unilaterally changing its written policy statements even without prior notification to the employees that it has reserved the right to do so. In that case, the employer had replaced an existing "discharge for cause" provision with a term providing for employment "at the will of the company." The court held that as long as the new policy was applied consistently, the employees were bound. Explaining that the purpose of the change was "to promote an environment conducive to collective productivity," the court stated that it is "[t]he benefit to the employer of promoting such an environment, rather than the traditional contract-forming

mechanisms of mutual assent or individual detrimental reliance, [that] gives rise to a situation ‘instinct with obligation.’” 443 N.W.2d at 118.

In answer to a similar certified question from the Ninth Circuit, the Arizona Supreme Court held that an employer *cannot* unilaterally change a handbook provision. The Arizona court rejected *Bankey* as using an “administrative law model.” The court stated: “We do not agree that a party to a contract containing a term that proves to be inconvenient, uneconomic, or unpleasant should have the right, like an administrative agency, ‘to change the rules prospectively through proper procedures.’” *Demasse v. ITT Corp.*, 984 P.2d 1138, 1149 (Ariz.1999).

REWARDS

The sheriff of Dallas County, A.H. Ledbetter, offered a reward of \$500 for the capture and return of Holly Vann, an escaped convict. A bounty hunter, S.H. Broadnax, captured Vann, brought him in, and sued for the reward. The trial court dismissed the petition, believing that it omitted a fact essential to the claim. On appeal, this question was certified to the Texas Supreme Court: “Was notice or knowledge to plaintiff of existence of the reward when the recapture was made essential to his right to recover?” The answer given was “Yes”: A reward offer “may be accepted by anyone who performs the service called for when the acceptor knows that it has been made and acts in performance of it, but not otherwise.” *Broadnax v. Ledbetter*, 99 S.W. 1111 (Tex.1907). Put in terms of Restatement § 71(2), the service that Broadnax rendered was not given by him in exchange for Ledbetter’s promise. Although the details of offer and acceptance are not taken up until the next chapter, it may be useful to think now about the relationship between consideration and offer and acceptance. Offer and acceptance can be understood as the mechanism by which the parties exchange consideration. In *Broadnax*, for example, the issue might have been framed in terms of offer and acceptance. Contract formation requires a manifestation of mutual assent. Restatement § 2(1). Broadnax could have manifested his assent by bringing in Vann, but when he brought Vann in he was not assenting to anything. Restatement § 23. More on this in Chapter 2.

Could Broadnax have recovered if he had captured Vann while ignorant of the reward but had learned of it before returning Vann to jail? Is his solution to release Vann and recapture him? See Restatement § 51. Could Broadnax have recovered if he had known of the reward but had captured Vann and turned him in because he was a close friend and wished to save him from mob violence? See Restatement § 81(2). For a case where three sets of claimants—including the attorney with whom the outlaw had conferred—sought unsuccessfully to recover the same reward, see *Taft v. Hyatt*, 180 P. 213 (Kan.1919).

NOTES

(1) *Comparative Perspective.* Under the law of some countries, such as Germany, a promise of reward is treated “not as an offer which would require acceptance in order to ripen into a contract, but as a unilateral jural act which as such is effective and binding without acceptance.” 1 Rudolf B. Schlesinger

(ed.), *Formation of Contracts: A Study of the Common Core of Legal Systems* 101–02 (1968). Would such a concept be a desirable one in the United States? See [Choice v. City of Dallas](#), 210 S.W. 753 (Tex.Civ.App.1919).

(2) *Employment Cases As Analogous?* As pointed out in the Note on Employee Handbooks, p. 68, an employee may not have read, or even received, the employer's handbook. Is that fatal to a claim by the employee based on a provision in the handbook? Reviewing the general requirement of reward cases that the promise must induce the performance, the Supreme Court of Iowa declined to follow it in a case in which the employee had received but not read the handbook provisions in question: "Although this holding is a departure from the traditional 'bargain-theory' contract analysis, we think it produces 'the salutary result that all employees, those who read the handbook and those who didn't, are treated alike.'" [Farnsworth, Developments in Contract Law During the 1980's: The Top Ten](#), 41 Case W. Res. L. Rev. 203, 209 (1990). [Anderson v. Douglas and Lomason Co.](#), 540 N.W.2d 277, 285 (Iowa 1995). What if the employee had not received the handbook?

PROBLEM

The One that Didn't Get Away. Diamond Jim III, a rockfish, was tagged and placed in the Chesapeake Bay in June by the American Brewery in connection with its Third Annual American Beer Fishing Derby. Under the Derby's well-publicized rules, the person who caught Diamond Jim III would receive a cash prize of \$25,000. In August, William Simmons went fishing in the Bay. He had heard of the contest, but did not have it in mind on that day. He caught Diamond Jim III and, although at first Simmons took little notice of the tag, he realized upon reexamining it a half hour later that he had caught the prize fish. Is Simmons entitled to the prize? See [Simmons v. United States](#), 308 F.2d 160 (4th Cir.1962). Note that Simmons, not the brewery, contended that the prize was a gift. Does the identity of the other party suggest a reason for that?

(D) PROMISES AS CONSIDERATION

The cases presented so far have focused on contracts in which the promisor has sought performance in exchange for a promise. As mentioned in Note 5, p. 40 above, these are called unilateral contracts. In contrast, contracts in which *both* parties make promises are called bilateral contracts. See Restatement § 71. Courts recognize that the consideration for a promise may be found in a return promise, even in one not even partly performed. Indeed, Comment *a* to Restatement § 75 informs us that "the promise is enforced by virtue of the fact of the bargain, without more."

This raises an underlying question regarding enforceability. What rationale lies behind the enforcement of a promise when the promisee has neither conferred a benefit upon the promisor nor acted in reliance on the promise? If one of the parties to an exchange of promises has second thoughts about the transaction the instant after the exchange has occurred, why should that party not be allowed to retract its promise? Consider again the various theories of contract enforcement described above at pp. 8–9.

Before looking more closely at the question of what constitutes a promise, we pause for a moment to introduce two concepts that enrich our understanding of promising more generally.

NOTES

(1) *Conditional Promises.* A promisor who seeks a *promise* in return is not, to be sure, unconcerned with the performance of the return promise. Suppose for example, that a buyer promises to pay \$100,000 in exchange for a seller's promise to convey a tract of land. The difference between this buyer's situation and that of a promisor such as Sheriff Ledbetter in *Broadnax v. Ledbetter*, p. 70 above, is that the promisor wants a return promise from the seller in *addition* to the transfer of land. Ledbetter's assurance that he would not have to pay the reward unless Vann is returned to captivity follows from the doctrine of consideration itself. His promise to pay the reward was not enforceable unless Vann was captured and returned: that is what he bargained for. How can one who bargains for a return promise, as the buyer above has done, be assured that its performance (paying the money in this instance) will not be due until the other party has performed (executing the deed)?

The solution involves the concept of a *condition*. A promise is conditional if its performance will become due only if a particular event, known as a "condition," occurs. This does not mean that the promise is not binding until the event occurs, but only that the event must occur before the promisor must perform. Insurance contracts provide good examples of *express* conditions. If a home owner pays \$1,000 to an insurance company in exchange for the company's promise to pay the owner \$100,000 if the owner's house suffers serious fire damage, the company has made an enforceable promise. But the company will owe nothing unless the house suffers serious fire loss within the year. Fire damage to the house is a condition of the company's promise to pay.

When a party makes a promise in exchange for a return promise, it can be protected by making its promise conditional on performance by the other party. Even if the contract does not so provide, the court may impose a condition by implication. Under such an implied condition—in this instance the condition is called a "constructive condition of exchange"—one party's duty to perform is not triggered until the other party has performed. For example, where promises are not typically performed at the same time, as in personal service contracts, the usual rule is that the work is made a condition of payment. Had Sheriff Ledbetter promised the reward in exchange for Broadnax's *promise* to capture and return Vann, when would the reward be due? Chapter 8 addresses the issue of conditions in more detail.

(2) *Rights and Duties.* The relationships between the parties in unilateral and bilateral contracts can be analyzed in terms of *right* and *duty*. A is said to have a *right* that B shall do an act when, if B does not do the act, A can initiate legal proceedings against B, and B in such a situation is said to have a *duty* to do the act. *Right* and *duty* are correlatives. In this strict sense there can never be a *right* without a *duty*, nor a *duty* without a *right*. The *right-duty* relationship is one between two parties. The *right* describes the relationship from one end and the *duty* from the other. Since, in a "unilateral" contract, there is a promise on one side only, there is a *duty* on one side only, and a *right* on the other side; and since in a "bilateral" contract there is a promise on each side, there is a *right* and a *duty* on each side.

For the precise use of terms such as *right* and *duty*, the legal profession is indebted to the work of Professor Wesley Newcomb Hohfeld,^a whose system of “Hohfeldian terminology” is set forth in *Fundamental Legal Conceptions* (1923). Review the language of Restatement § 1. How does it incorporate the language of right and duty?

WHAT CONSTITUTES A PROMISE?

It has long been clear that the consideration for a promise can be found in a return promise. The Restatement informs us that, with some exceptions, “a promise that is bargained for is consideration if the promised performance would be consideration.” Restatement § 75. But what exactly counts as a promise? The following cases explore how courts determine from language and context whether a performance has in fact been promised or whether only the *illusion* of performance has been held out.

Strong v. Sheffield

Court of Appeals of New York, 1895.

144 N.Y. 392, 39 N.E. 330.

[Action on a promissory note. A judgment for plaintiff, Benjamin B. Strong, against defendant, Louisa A. Sheffield, was reversed by the General Term of the Supreme Court.

Benjamin Strong brought this action against Louisa Sheffield, his niece. Strong had sold a business to her husband, Gerardus (“Rard”), on credit. Later, the buyer’s debt was embodied in a promissory note, payable on demand. Mrs. Sheffield endorsed the note, an act which the law treats as a promise to pay if her husband, the “maker” of the note, did not. What, if anything, she got in exchange for that was a matter in issue.

The trial court gave judgment for Strong. That was reversed on a first appeal. Then Strong appealed.]

■ ANDREWS, C.J. The contract between a maker or endorser of a promissory note and the payee forms no exception to the general rule that a promise, not supported by a consideration, is nudum pactum. The law governing commercial paper which precludes an inquiry into the consideration as against bona fide holders for value before maturity, has no application where the suit is between the original parties to the instrument. It is undisputed that the demand note upon which the action was brought was made by the husband of the defendant and endorsed by her at his request and delivered to the plaintiff, the payee, as security for an antecedent debt owing by the husband to the plaintiff. The debt of the husband was past due at the time, and the only consideration for the wife’s endorsement,

^a Wesley Newcomb Hohfeld (1879–1918) practiced law briefly in San Francisco before joining the Stanford law faculty in 1905. In 1914 he left Stanford to teach at Yale until his death at the age of thirty-nine. He made a lasting contribution to legal literature through his development of the eight terms of “Hohfeldian terminology” in his book *Fundamental Legal Conceptions*. Corbin wrote, “He was a severe taskmaster, requiring his students to master his classification of ‘fundamental conceptions’ and to use accurately the set of terms by which they were expressed. They found this, in the light of the usage of the other professors [at Yale], almost impossible.” Their resistance resulted in a petition to the President of Yale that Hohfeld’s appointment not be extended. The petition was ignored and generations of law students have continued to master Hohfeld’s terms.

which is or can be claimed, is that as part of the transaction there was an agreement by the plaintiff when the note was given to forbear the collection of the debt, or a request for forbearance, which was followed by forbearance for a period of about two years subsequent to the giving of the note.

[According to the record in the case, Mrs. Sheffield was reluctant to endorse the note.^j Strong testified that he had said: "Rard, I will give you my word as a man . . . that if you will give me a note, with your wife's endorsement . . . I will not pay that note away; I will not put it in any bank for collection, but I will hold it until such time as I want my money. . . ." Strong testified also that Gerardus had said, on delivering the note, "You won't pay this note away?", and that Strong answered, "No, I will keep it until such time as I want it." An example of "paying the note away" would have been for Strong to sell the note, giving the buyer the right to collect it on demand.]

There is no doubt that an agreement by the creditor to forbear the collection of a debt presently due is a good consideration for an absolute or conditional promise of a third person to pay the debt or for any obligation he may assume in respect thereto. Nor is it essential that the creditor should bind himself at the time to forbear collection or to give time. If he is requested by his debtor to extend the time, and a third person undertakes in consideration of forbearance being given to become liable as surety or otherwise, and the creditor does in fact forbear in reliance upon the undertaking, although he enters into no enforceable agreement to do so, his acquiescence in the request, and an actual forbearance in consequence thereof for a reasonable time, furnishes a good consideration for the collateral undertaking. In other words, a request followed by performance is sufficient, and mutual promises at the time are not essential unless it was the understanding that the promisor was not to be bound, except on condition that the other party entered into an immediate and reciprocal obligation to do the thing requested. . . . The note in question did not in law extend the payment of the debt. It was payable on demand, and although being payable with interest it was in form consistent with an intention that payment should not be immediately demanded, yet there was nothing on its face to prevent an immediate suit on the note against the maker or to recover the original debt. . . .

In the present case the agreement made is not left to inference, nor was it a case of request to forbear, followed by forbearance, in pursuance of the request, without any promise on the part of the creditor at the time. The plaintiff testified that there was an express agreement on his part to the effect that he would not pay the note away, nor put it in any bank for collection . . . [The court then quoted Strong's testimony as recited above.] Upon this alleged agreement the defendant endorsed the note. It would have been no violation of the plaintiff's promise if, immediately on receiving the note, he had commenced suit upon it. Such a suit would have been an assertion that he wanted the money and would have fulfilled the condition of forbearance. The debtor and the defendant, when they became parties to the note, may have had the hope or expectation that forbearance would follow, and there was forbearance in fact. But there was no agreement to for-

^j The record on appeal indicates that Benjamin Strong was Louisa Sheffield's uncle. He had sold his business on credit to Louisa's husband, Gerardus, and then sought Gerardus' note with Louisa's endorsement as security for the debt. Louisa was reluctant to endorse her husband's note because she had her own successful business and did not want to hurt her credit by having it known that she had undertaken a debt of her husband.

bear for a fixed time or for a reasonable time, but an agreement to forbear for such time as the plaintiff should elect. The consideration is to be tested by the agreement, and not by what was done under it. It was a case of mutual promises, and so intended. We think the evidence failed to disclose any consideration for the defendant's endorsement, and that the trial court erred in refusing so to rule.

The order of the General Term reversing the judgment should be affirmed, and judgment absolute directed for the defendant on the stipulation with costs in all courts.

Ordered accordingly.

NOTES

(1) *Questions.* Restatement § 77 mentions the “illusory” or “apparent” promise as a type that is not consideration. Did Strong make any promise of substance? Could he have been held liable for breach of contract in any circumstances? If there is no consideration when Strong refrains from calling the note, why is there consideration when Lake Land refrains from firing Columber?

(2) *Drafting.* Suppose that Louisa Sheffield had written to Strong: “I will be responsible for my husband's debt if you will not bother him about it for two years.” Would she have been liable to Strong if he had done nothing about the note for that period? What difference is there between this situation and the case as it stands? The precise rule of this case is reversed by UCC § 3-303(a)(3).

(3) *Sexually Transmitted Debt.* Why might Louisa have agreed to endorse Gerardus' note in the first place? Empirical studies suggest that spouses, and perhaps particularly wives, commonly co-sign or otherwise act as sureties for the debts of the other spouse, and many of them may be less experienced in financial matters than was Louisa Sheffield. For a study of surety spouses in England, see Belinda Fehlberg, *Sexually Transmitted Debt* (1997), suggesting that spousal promises to act as sureties should be subject to special scrutiny. Do you agree? See also *Barclay's Bank v. O'Brien*, [1993] 4 All E.R. 417 (H.L.). We return to the question of pressuring in bargaining in Chapter 4.

PROBLEM

The Case of the Unexpected Heir. Under the terms of their divorce settlement agreement, Gerald kept the family farm and Nancy took mortgages on the farm to secure periodic payments that Gerald was to make to her. Gerald later had financial difficulties and sought to refinance previous bank loans, but he found that he could not do so because of Nancy's mortgages. Nancy agreed to give up her right to any additional payments and to satisfy the mortgages in return for Gerald's promise to make a will leaving the farm to their son Ronn, reserving the right to sell a portion of the land in order to continue farming if “future economic exigencies require.” Although Gerald made a will and obtained refinancing as promised, Nancy began foreclosure proceedings. She argued that Gerald's promise was illusory because he had reserved a right to convey the farm. Should Nancy prevail? See [Harrington v. Harrington, 365 N.W.2d 552 \(N.D.1985\)](#).

CONTRACTS FOR THE SALE OF REAL ESTATE

Sales of land and other real estate transactions, including leases, are often quite complex. The following case, in which a developer sought to buy land in order to construct a shopping center, is an example. A commercial transaction of this kind typically involves not only the buyer (often called “purchaser”) and at least one seller (often called “vendor”) and their agents, but also third parties such as lenders, title companies, and potential lessees of the completed development. Each contributes to the intricacy of the transaction. This structural complexity explains in part why contracts for the sale of real estate have been characterized by more formality than, say, contracts for the sale of goods. Even in residential sales, the parties are frequently represented by lawyers and the required documents are lengthy and detailed.

In both residential and commercial real estate transactions, a number of intervening activities commonly take place between the contract signing and the formal “closing,” at which a deed is exchanged for the payment of the price. These typically include verifying the seller’s title to the property, the buyer’s obtaining financing, and—as in the case that follows—the buyer lining up enough satisfactory tenants to make the prospective shopping center viable. It is not uncommon for a deal to fall apart during this period (formally called the executory interval).

Real property is a uniquely valuable form of wealth and real estate transactions are of great salience to the economy in general as well as individual homeowners, current and prospective. For many, the most financially significant transaction of a lifetime is the purchase or sale of a home. In recent years, individual interests in home ownership and its broader economic implications have become deeply entwined. Shoddy lending practices associated with the most basic home loans contributed greatly to the worldwide financial crisis in the fall of 2008 and the ensuing economic recession, the worse since the Great Depression of the 1930s. The mortgage crisis of 2008 has put new demands on contract doctrine as homeowners have turned to courts for redress, and as legislatures attempt to police transactional aspects of the problem. We will look more closely at these issues when we take up the case of *Dixon v. Wells Fargo* in Chapter 2. We turn now, however, to a more ordinary category of dispute, one between a real estate developer and a recalcitrant seller.

Mattei v. Hopper

Supreme Court of California, 1958.
[51 Cal.2d 119, 330 P.2d 625.](#)

■ SPENCE, JUSTICE. Plaintiff [Mattei] brought this action for damages after defendant [Hopper] allegedly breached a contract by failing to convey her real property in accordance with the terms of a deposit receipt which the parties had executed. After a trial without a jury, the court concluded that the agreement was “illusory” and lacking in “mutuality.” From the judgment accordingly entered in favor of defendant, plaintiff appeals.

Plaintiff was a real estate developer. He was planning to construct a shopping center on a tract adjacent to defendant’s land. For several months, a real estate agent attempted to negotiate a sale of defendant’s property under terms agreeable to both parties. After several of plaintiff’s proposals had been rejected by defendant because of the inadequacy of the

price offered, defendant submitted an offer. Plaintiff accepted on the same day.

The parties' written agreement was evidenced on a form supplied by the real estate agent, commonly known as a deposit receipt. Under its terms, plaintiff was required to deposit \$1,000 of the total purchase price of \$57,500 with the real estate agent, and was given 120 days to "examine the title and consummate the purchase." At the expiration of that period, the balance of the price was "due and payable upon tender of a good and sufficient deed of the property sold." The concluding paragraph of the deposit receipt provided: "Subject to Coldwell Banker & Company obtaining leases satisfactory to the purchaser." This clause and the 120-day period were desired by plaintiff as a means for arranging satisfactory leases of the shopping center buildings prior to the time he was finally committed to pay the balance of the purchase price and to take title to defendant's property.

Plaintiff took the first step in complying with the agreement by turning over the \$1,000 deposit to the real estate agent. While he was in the process of securing the leases and before the 120 days had elapsed, defendant's attorney notified plaintiff that defendant would not sell her land under the terms contained in the deposit receipt. Thereafter, defendant was informed that satisfactory leases had been obtained and that plaintiff had offered to pay the balance of the purchase price. Defendant failed to tender the deed as provided in the deposit receipt.

Initially, defendant's thesis that the deposit receipt constituted no more than an offer by her, which could only be accepted by plaintiff notifying her that all of the desired leases had been obtained and were satisfactory to him, must be rejected. Nowhere does the agreement mention the necessity of any such notice. Nor does the provision making the agreement "subject to" plaintiff's securing "satisfactory" leases necessarily constitute a condition to the existence of a contract. Rather, the whole purchase receipt and this particular clause must be read as merely making plaintiff's performance dependent on the obtaining of "satisfactory" leases. Thus a contract arose, and plaintiff was given the power and privilege to terminate it in the event he did not obtain such leases. (See 3 Corbin, *Contracts* (1951), § 647, pp. 581-585.) This accords with the general view that deposit receipts are binding and enforceable contracts. (Cal.Practice Hand Book, *Legal Aspects of Real Estate Transactions* (1956), p. 63.)

However, the inclusion of this clause, specifying that leases "satisfactory" to plaintiff must be secured before he would be bound to perform, raises the basic question whether the consideration supporting the contract was thereby vitiated. When the parties attempt, as here, to make a contract where promises are exchanged as the consideration, the promises must be mutual in obligation. In other words, for the contract to bind either party, both must have assumed some legal obligations. Without this mutuality of obligation, the agreement lacks consideration and no enforceable contract has been created. . . . Or, if one of the promises leaves a party free to perform or to withdraw from the agreement at his own unrestricted pleasure, the promise is deemed illusory and it provides no consideration. . . . Whether these problems are couched in terms of mutuality of obligation or the illusory nature of a promise, the underlying issue is the same—consideration. . . .

While contracts making the duty of performance of one of the parties conditional upon his satisfaction would seem to give him wide latitude in avoiding any obligation and thus present serious consideration problems,

such “satisfaction” clauses have been given effect. They have been divided into two primary categories and have been accorded different treatment on that basis. First, in those contracts where the condition calls for satisfaction as to commercial value or quality, operative fitness, or mechanical utility, dissatisfaction cannot be claimed arbitrarily, unreasonably, or capriciously . . . , and the standard of a reasonable person is used in determining whether satisfaction has been received. . . . However, it would seem that the factors involved in determining whether a lease is satisfactory to the lessor are too numerous and varied to permit the application of a reasonable man standard as envisioned by this line of cases. Illustrative of some of the factors which would have to be considered in this case are the duration of the leases, their provisions for renewal options, if any, their covenants and restrictions, the amounts of the rentals, the financial responsibility of the lessees, and the character of the lessees’ businesses.

This multiplicity of factors which must be considered in evaluating a lease shows that this case more appropriately falls within the second line of authorities dealing with “satisfaction” clauses, being those involving fancy, taste, or judgment. Where the question is one of judgment, the promisor’s determination that he is not satisfied, when made in good faith, has been held to be a defense to an action on the contract. . . . Although these decisions do not expressly discuss the issues of mutuality of obligation or illusory promises, they necessarily imply that the promisor’s duty to exercise his judgment in good faith is an adequate consideration to support the contract. None of these cases voided the contracts on the ground that they were illusory or lacking in mutuality of obligation. Defendant’s attempts to distinguish these cases are unavailing, since they are predicated upon the assumption that the deposit receipt was not a contract making plaintiff’s performance conditional on his satisfaction. As seen above, this was the precise nature of the agreement. Even though the “satisfaction” clauses discussed in the above-cited cases dealt with performances to be received as parts of the agreed exchanges, the fact that the leases here which determined plaintiff’s satisfaction were not part of the performance to be rendered is not material. The standard of evaluating plaintiff’s satisfaction—good faith—applies with equal vigor to this type of condition and prevents it from nullifying the consideration otherwise present in the promises exchanged.

Moreover, the secondary authorities are in accord with the California cases on the general principles governing “satisfaction” contracts. . . . “A promise conditional upon the promisor’s satisfaction is not illusory since it means more than that validity of the performance is to depend on the arbitrary choice of the promisor. His expression of dissatisfaction is not conclusive. That may show only that he has become dissatisfied with the contract; he must be dissatisfied with the performance, as a performance of the contract, and his dissatisfaction must be genuine.” (Restatement, Contracts (1932), § 265, comment *a*.)

If the foregoing cases and other authorities were the only ones relevant, there would be little doubt that the deposit receipt here should not be deemed illusory or lacking in mutuality of obligation because it contained the “satisfaction” clause. However, language in two recent cases led the trial court to the contrary conclusion. The first case, [Lawrence Block Co. v. Palston](#), 123 Cal.App.2d 300, 266 P.2d 856, 858, stated that the following two conditions placed in an offer to buy an apartment building would have made the resulting contract illusory: “O.P.A. Rent statements to be ap-

proved by Buyer” and “Subject to buyer’s inspection and approval of all apartments.” These provisions were said to give the purchaser “unrestricted discretion” in deciding whether he would be bound to the contract and to provide no “standard” which could be used in compelling him to perform. 123 Cal.App.2d at pages 308–309, 266 P.2d at pages 861–862. However, this language was not necessary to the decision. . . .

The other case, *Pruitt v. Fontana*, 143 Cal.App.2d 675, 300 P.2d 371, 377, presented a similar situation. The court concluded that the written instrument with a provision making the sale of land subject to the covenants and easements being “approved by the buyers” was illusory. It employed both the reasoning and language of *Lawrence Block Co.* in deciding that this clause provided no “objective criterion” preventing the buyers from exercising an “unrestricted subjective discretion” in deciding whether they would be bound. 143 Cal.App.2d at pages 684–685, 300 P.2d at page 377. But again, this language was not necessary to the result reached. The buyers in *Pruitt* refused to approve all of the easements of record, and the parties entered into a new and different oral agreement. The defendant seller was held to be estopped to assert the statute of frauds against this subsequent contract, and the judgment of dismissal entered after the sustaining of demurrers was reversed.

While the language in these two cases might be dismissed as mere dicta, the fact that the trial court relied thereon requires us to examine the reasoning employed. Both courts were concerned with finding an objective standard by which they could compel performance. This view apparently stems from the statement in *Lawrence Block Co.* that “The standard ‘as to the satisfaction of a reasonable person’ does not apply where the performance involves a matter dependent on judgment.” 123 Cal.App.2d at page 309, 266 P.2d at page 862. By making this assertion without any qualification, the court necessarily implied that there is no other standard available. Of course, this entirely disregards those cases which have upheld “satisfaction” clauses dependent on the exercise of judgment. In such cases, the criterion becomes one of good faith. Insofar as the language in *Lawrence Block Co.* and *Pruitt* represented a departure from the established rules governing “satisfaction” clauses, they are hereby disapproved.

We conclude that the contract here was neither illusory nor lacking in mutuality of obligation because the parties inserted a provision in their contract making plaintiff’s performance dependent on his satisfaction with the leases to be obtained by him.

The judgment is reversed.

NOTES

(1)*Satisfied?* If, after signing the deposit receipt, Mattei had changed his mind about the purchase, could he have avoided liability simply by saying that he was “dissatisfied” with the deal? Would Hopper have been bound if Mattei had inserted a clause permitting him to do this? The meaning of “good faith” is explored further in later chapters.

After negotiations, parties often leave some matters for their lawyers. Do you see a difference in legal effect between a provision that says “subject to my lawyer’s approval of our agreement” and one that says “subject to my lawyer’s approval of documents tendered when the deal is closed”?

(2) *Holdouts*. Why might Hopper have refused to sell? Perhaps she came to regret the price she had agreed to and was seeking a way out of the contract? Why might this be?

One possibility is that Hopper was a “holdout,” or at least a would-be holdout. Holdouts are parties who seek to extract gains by delaying or otherwise raising the costs of, contractual formation. The paradigmatic context of holdouts occurs when a real estate developer attempts to assemble adjacent parcels of land for the site of a new project. See Andrew Alpern & Seymour B. Durst, *Holdouts!* (1984). From an economic perspective, the developer should be able to buy the desired parcels at their current value and still find it worthwhile to proceed with the project. When, however, the parcels are held by multiple separate owners, efficient trade becomes significantly less likely due to the “holdout problem.” The last landowner to sell (or perhaps in Hopper’s case, the last one to find out about the project) may be able to demand a higher price knowing that the developer is, to some extent, locked in by virtue of the earlier purchases.

When developers encounter a holdout, they have several options: they can go elsewhere (preferably to a site that has a single owner); they can pay the price demanded; they can discretely purchase the land through false fronts and straw buyers; or they can fix a total price that they will pay for the land and let the landowners deal with splitting the pie themselves. They might also, under certain circumstances, appeal to a state or municipal government to exercise its power of eminent domain on their behalf; see [Kelo v. City of New London](#), 545 U.S. 469 (2005).

(3) *Property and Contract*. We noted earlier that the substantive connections among first year courses are many. Consider for a moment connections between contract formation and the doctrine of eminent domain mentioned at the end of Note 2 above. Assume that in the principal case, the county (rather than a private developer) had sought Hopper’s land to use for a new highway but that Hopper refused to sell because she thought the price offered was too low. Might the availability of eminent domain influence negotiations over price between Hopper and the county? Might the availability of eminent domain, as provided for by the Fifth Amendment, influence negotiations over price between Hopper and the private developer? Do property owners in such circumstances bargain under the shadow of constitutional law? For one study about how prices are set generally in takings cases, see Curtis Berger, *The Nassau County Study: An Empirical Look into the Practices of Condemnation*, 67 *Colum. L. Rev.* 430 (1967).

CONTRACTS FOR THE SALE OF GOODS

You have already been introduced to this category of Contracts in the *Bayliner* case on p. 4 above. Contracts for the sale of goods have long been regarded as distinctive, as evidenced by the reduction of the common law of sales to statutory form in England in 1893 by the Sale of Goods Act and in the United States in 1906 by the Uniform Sales Act, later replaced by the UCC. The law of international sales has now also been codified in the United Nations [Vienna] Convention on the International Sale of Goods (CISG). (The Convention is found in Selections for Contracts.)

Article 2 of the UCC reflects the characteristics of commercial sales transactions in a number of ways. Because agreements to buy and sell goods are often made quickly and informally, the requirements for contract formation tend to be less demanding than in contracts for the sale of real property. The parties to sales contracts are often “repeat players” who have dealt with similar goods and often with each other over time, so that their particular understandings as well as customs and practices within the trade may give added content to their agreements. Terms and entire forms are often standardized.

The nature of goods is also significant with regard to remedies. Unlike land where every parcel is regarded as unique, goods are considered *fungible*: one item of a particular sort is understood to be as good as any other. (“Widgets” have been the inevitable law school example.) Because it is generally assumed that goods of all sorts are available on the market, market price plays an inescapable role in the calculation of damages under Article 2.

Structural Polymer Group, Ltd. v. Zoltek Corp.

United States Court of Appeals for the Eighth Circuit, 2008.

[543 F.3d 987.](#)

■ COLLOTON, CIRCUIT JUDGE.

A jury awarded Structural Polymer Group and Structural Polymer Systems (together SP) \$36,044,895 in lost profits from Zoltek Corporation for breach of a requirements contract for the sale of carbon fiber. The district court reduced the award to \$21,138,518, finding the remainder of the award duplicative. Zoltek appeals the district court’s denial of its motion for a new trial and motion for judgment as a matter of law. Structural Polymer cross-appeals the district court’s modification of the jury’s damages award. We affirm.

I.

Zoltek is a Missouri corporation that manufactures and sells carbon fiber. SP are British corporations that manufacture a strong, light-weight building material produced using carbon fiber called “prepreg.” Prepreg is made by weaving carbon fiber into textile-like sheets and then impregnating the sheets with liquid resin. The prepreg sheets are then sold to builders who can mold them into different shapes for a variety of applications. Used in this way, prepreg is a common substitute for fiberglass. One common application for prepreg is the manufacture of wind energy turbine blades.

The parties entered into a Supply Agreement in November 2000. Under the disputed agreement, Zoltek promised to manufacture and sell to SP all of SP’s requirements between November 6, 2000, and December 31, 2010, for “Large Filament Count Carbon Fibers (Carbon Fibers) as defined by PANEX 33 specifications,” at “then-current market price.” SP, in turn, promised to “obtain their total requirements for suitable quality, in the reasonable opinion of [SP], Carbon Fibers from [Zoltek],” the volume not to exceed “the amount actually purchased by [SP] in the preceding Contract Year plus one million (1,000,000) pounds.” “Large Filament Count,” or large-tow carbon fiber, contains 48,000 or more filaments per bundle.

“Small-tow” carbon fiber, by contrast, contains fewer than 48,000 filaments per bundle, commonly 24,000 or fewer filaments per bundle. Small-tow is more expensive to produce, but superior in quality.

When the Supply Agreement was formed, most manufacturers used small-tow carbon fiber. The purpose of the agreement was to develop a new market for large-tow fiber as a less expensive alternative to small-tow fiber in the wind-energy industry.

Before April 2002, Zoltek produced a large-tow carbon fiber product called Panex 33. SP purchased 28,219.17 and 20,943.91 pounds of Panex 33 from Zoltek under the Supply Agreement in 2000 and 2001, respectively. SP placed an order for 1,763.70 pounds of Panex 33 in 2002, but returned it due to alleged quality defects. In April 2002, Zoltek stopped manufacturing Panex 33, and started making a large-tow carbon fiber product called Panex 35. SP ordered no Panex 33 or 35 in 2003. SP ordered and received 548,935 pounds of Panex 35 in 2004.

The dispute in this case centers on two orders that SP placed with Zoltek in 2005 and 2006 that were never filled. SP ordered 1,480,138 pounds of Panex 35 in 2005, and claims that it was entitled to 2,480,138 pounds of Panex 35 in 2006.

On February 22, 2005, SP sued Zoltek for breach of contract alleging lost profits through December 31, 2006, and future lost profits through December 31, 2010. Because the parties disputed whether the Supply Agreement entitled SP to both Panex 33 and Panex 35, SP’s damages expert made alternative lost profit calculations: \$21,138,518 in then-current lost profits under Count I corresponding to 3,960,276 pounds of Panex 35, and \$14,906,377 in then-current lost profits under Count II corresponding to 3,000,000 pounds of Panex 33.

On November 29, 2006, a jury awarded SP lost profits under both counts through December 31, 2006, but declined to award SP future lost profits. The district court vacated the award under Count II as duplicative, giving SP a final sum of \$21,138,518. Zoltek filed motions under [Federal Rule of Civil Procedure 59\(a\)](#) for a new trial, and under Rule 50(b) for judgment as a matter of law, in connection with both the liability and damages phases of the proceedings, and the district court denied both motions. Zoltek appeals the district court’s denial of those motions. SP cross-appeals the district court’s vacation of the jury’s award under Count II of the complaint.

II.

Zoltek argues that the district court erred in four ways. First, Zoltek argues that the district court erred by refusing to allow it to raise two arguments to the jury. Zoltek sought to urge that the Supply Agreement was void for lack of mutuality of obligation. The district court concluded that Zoltek’s argument was an affirmative defense, which Zoltek waived by failing to plead it, and the district court then denied as untimely Zoltek’s motion to amend its complaint to add a mutuality defense. Second, the district court ruled that Zoltek failed to make a submissible case that SP had abandoned the Supply Agreement. Third, Zoltek argues that the district court failed to remedy unfairly prejudicial testimony at trial. Fourth, Zoltek argues that the jury’s damages award to SP was not based on adequate evidence, that the district court erred by allowing SP to amend its damages calculations twenty-two days before trial, that SP’s revised damages calculations were inadequate as a matter of law, and that the district court in-

structed the jury incorrectly in connection with the damages phase of the proceedings.

A.

We first consider Zoltek's objection to the district court's resolution of arguments concerning mutuality of obligation. Zoltek urged that the Supply Agreement was "unenforceable as a requirements contract due to a lack of mutuality," which is in essence an argument that SP failed to show that the Supply Agreement was supported by valid consideration. See Restatement (Second) of Contracts § 79 (1981) ("If the requirement of consideration is met, there is no additional requirement of . . . 'mutuality of obligation.'"); [USA Chem, Inc. v. Lewis](#), 557 S.W.2d 15, 24 (Mo.Ct.App.1977); [Famous Brands, Inc. v. David Sherman Corp.](#), 814 F.2d 517, 521 (8th Cir.1987). . . .

[W]e agree with the district court that the Supply Agreement was supported by adequate consideration as a matter of law. Under Missouri law, "whether consideration is sufficient to establish a contract is normally a question of law for the court and not a question of fact for the jury." [Allison v. Agribank, FCB](#), 949 S.W.2d 182, 188 (Mo.Ct.App.1997). Missouri law long has followed a rule that "[w]hen a party relies upon a writing or a number of writings to establish a contract, it is unquestionably the province of the court to determine from the writing or writings whether or not a contract was entered into." [Nelson v. Cal Hirsch & Sons' Iron & Rail Co.](#), 102 Mo.App. 498, 77 S.W. 590, 594 (1903).

Zoltek advances three reasons why the contract lacked mutuality of obligation. All three are based on an allegation that SP's requirements under the agreement are "hopelessly manipulable" and determined by SP's subjective preferences, rather than by objective criteria outside of SP's control. Specifically, Zoltek argues that "SP could at all times order or not order Zoltek fiber as it wanted" because (1) SP had zero requirements for large-tow fiber when the contract was formed, (2) the price protection clause gave SP the option "to purchase carbon fibers from other producers" whenever SP wanted to, and (3) SP was free to buy small-tow fiber, which Zoltek alleges is "interchangeable" with large-tow fiber, in place of large-tow whenever it pleased.

First, we disagree with Zoltek that the Supply Agreement lacks mutuality if SP had zero requirements for large-tow fiber when the contract was formed. A duty of good faith is implied in requirements contracts under Missouri law, see [Mo.Rev.Stat. § 400.2–306\(1\)](#) (1994); [Home Shopping Club, Inc. v. Roberts Broad. Co.](#), 989 S.W.2d 174, 179 (Mo.Ct.App.1998), and this "implied obligation of good faith is enough to avoid finding a contract null and void due to an illusory promise." [Magruder Quarry & Co. v. Briscoe](#), 83 S.W.3d 647, 650–51 (Mo.Ct.App.2002); see also [National Refining Co. v. Cox](#), 227 Mo.App. 778, 57 S.W.2d 778, 781 (1933). The Supply Agreement bound SP to order product from Zoltek in good faith, and if SP failed to purchase anything from Zoltek during the term of the agreement, then the contract allowed Zoltek to allege that SP acted in bad faith by failing to make purchases. An assertion of bad faith, however, is an argument that SP breached the agreement, not that the agreement lacked mutuality or consideration in the first place. The district court's ruling on Zoltek's proposed defense did not foreclose it from arguing to the jury that SP breached the agreement.

Second, we disagree with Zoltek that the price protection clause in the contract made SP's obligation illusory. The price protection clause gave

Zoltek a right of first refusal to sell large-tow carbon fiber to SP for the same price as offered by a third party seller. If Zoltek offered to match the price offered by another supplier, then SP was obligated to purchase from Zoltek. We think the Missouri courts are likely to agree with the observation in a leading treatise that this mechanism does not render the contract illusory:

The seller may not promise to meet such prices, but the seller may be given the option of doing so. If the seller meets such prices, the buyer must buy of the seller or not at all. If the seller does not meet such prices, the buyer has the privilege of buying elsewhere. Such promises are not illusory and the contract is valid. Arthur Linton Corbin, et al., 2–6 Corbin on Contracts § 6.8.

Zoltek’s authorities do not persuade us to the contrary. They demonstrate only that if SP had an unfettered option to purchase from another supplier during the term of the contract, then this option would destroy the exclusivity of the arrangement, and demonstrate lack of consideration. E.g., [In re Modern Dairy of Champaign, Inc.](#), 171 F.3d 1106, 1108 (7th Cir.1999); [Harvey v. Fearless Farris Wholesale, Inc.](#), 589 F.2d 451, 459 (9th Cir.1978); [Loizeaux Builders Supply Co. v. Donald B. Ludwig Co.](#), 144 N.J.Super. 556, 366 A.2d 721, 724 (1976); [Propane Indus., Inc. v. General Motors Corp.](#), 429 F.Supp. 214, 221 (W.D.Mo.1977). The inclusion in the Supply Agreement of a right of first refusal for Zoltek to retain its exclusive right to supply SP, so long as it matched a market price offered by another supplier, is sufficient to create mutuality of obligation and consideration.

Third, we do not agree with Zoltek that if small-tow and large-tow fiber are “interchangeable,” then the Supply Agreement lacked mutuality. There was a good deal of evidence at trial that small-tow and large-tow fiber are distinct products, with different qualities and applications. But assuming for the sake of argument that a jury could find that small-tow and large-tow fibers are in fact “interchangeable,” as Zoltek contends, the authorities cited by Zoltek do not establish that the Supply Agreement is void for lack of mutuality. These cases illustrate, rather, that when a buyer contracts to purchase its requirements for a product from a particular seller, but then—without a “good faith” basis to do so—purchases an interchangeable product from a third party instead, the buyer may have breached the requirements contract. E.g., [Fike Corp. v. Great Lakes Chemical Corp.](#), 332 F.3d 520, 524 (8th Cir.2003); [Empire Gas Corp. v. American Bakeries Co.](#), 840 F.2d 1333, 1339–41 (7th Cir.1988); [Loudenback Fertilizer Co. v. Tenn. Phosphate Co.](#), 121 F. 298, 303 (6th Cir.1903). Zoltek was free to argue on this basis that SP’s purchase of small-tow fiber from parties other than Zoltek was a breach of the agreement to purchase large-tow fiber exclusively from Zoltek, but the jury found that SP performed its obligations under the contract. SP’s obligation to purchase in good faith all of its requirements for large-tow fiber exclusively from Zoltek was sufficient consideration to make the contract valid.

For these reasons, we agree with the district court’s alternative holding that “on the face of the agreement, there is mutuality of obligation and, therefore, consideration.” . . .

III.

In its cross-appeal, SP argues that the district court erred by granting Zoltek’s motion to alter or amend judgment pursuant to [Federal Rule of Civil Procedure 59\(e\)](#). The verdict form submitted to the jury included al-

ternative damages calculations corresponding to 3,000,000 pounds of Panex 33 and 3,960,276 pounds of Panex 35. The jury awarded SP damages under both calculations. The district court concluded that SP had argued throughout the case that the Supply Agreement entitled them to “either Panex 33 or Panex 35,” but not to both, and therefore vacated the lesser of the two awards as duplicative.

We conclude that the district court did not abuse its discretion. SP’s complaint pleaded Counts I and II in the alternative, demanding that Zoltek “supply the unfulfilled quantities of PANEX 35 or, in the alternative, PANEX 33,” and alleging that the contract was modified to “substitute” Panex 35 for Panex 33. SP’s damages expert presented “alternative” damages calculations—one that assumed the Supply Agreement encompassed both Panex 33 and Panex 35, and a second that assumed that only Panex 33 was covered. The Supply Agreement referred to Panex 33 only, and established a maximum quantity that SP was entitled to order. The jury evidently accepted SP’s contention that it also was entitled to order Panex 35 under the agreement, because it was an improved version of Panex 33, but the agreement did not provide that SP could order the maximum quantity of both Panex 33 and Panex 35.

Under the Supply Agreement, SP was entitled to order the quantity of carbon fiber ordered in the immediately preceding year, plus one million pounds. Thus, between 2004 and 2005, SP was entitled either to 3,960,276 pounds of Panex 35, or 3,000,000 pounds of Panex 33, but not both. The jury’s award under both Count I and Count II gave SP profit corresponding to 6,960,276 pounds of large-tow carbon fiber when at most SP was entitled to 3,960,276 pounds. Therefore, the district court acted within its discretion when it determined that the jury’s award under both counts was duplicative and altered the judgment accordingly.

For these reasons, the judgment of the district court is affirmed.

NOTES

(1) *Drafting and Price Fluctuations.* Under a fixed-price requirements contract, the seller runs a risk that if the market price rises, the buyer’s requirements will escalate. Does the Code suggest any drafting techniques that a seller might use to reduce this risk? Did Gulf succeed in avoiding this risk by making a flexible-price requirements contract?

(2) *Output Contracts.* In contrast to a “requirements” contract, an “output” contract is one that calls on the seller to deliver and the buyer to take all of the goods, or all of a certain sort, that may be produced by the seller. Note the common characteristic of exclusivity in both requirement and output contracts. What protections does the Code provide for buyers and for sellers under these circumstances?

If a buyer announces it will not make any purchases at all, prior to the seller having commenced or completed its manufacture of the goods, how should the court measure the quantity for the purposes of assessing damages?

PROBLEM

This Contract is Toast. Suppose the Staehl Bread Company and Walker Cattle Farms had a ten-year contract for the sale of all the toasted bread crumbs Staehl made (Walker used the bread crumbs to feed its prize cows).

After a year or two, Staehl Bread gave notice to Walker that making the bread crumbs had become unprofitable, so it would cease their manufacture four weeks hence. Walker sued for breach of contract. Has Staehl Bread breached the contract? Isn't losing money a good reason not to continue in a line of business? Or must Staehl Bread continue making bread crumbs for Walker, even as Staehl Bread's losses become ruinous? See UCC § 2-306 cmt. 2. And if the seller is in breach, how would we measure the damages for breach, given the need to predict what the seller's output will be eight or so years after the trial? How might the parties draft their agreement to protect the buyer against the seller's decision to stop making the product? Cf. *Feld v. Henry S. Levy & Sons, Inc.*, 335 N.E.2d 320 (N.Y. 1975).

INTRODUCTION TO WOOD V. LUCY, LADY DUFF-GORDON

The cases so far have focused on statements that at least one of the parties regarded as an express promise. The following case concerns a promise that the court agrees was not "expressed in so many words" but instead, was "fairly to be implied." What was it implied from? In the discussion of *Hawkins v. McGee* in Note 1, p. 3 above, you were asked to consider the language, context, and nature of the transaction in determining whether Dr. Hawkins's statement was a promise. As you read Judge Cardozo's famous opinion below, consider how those factors contribute to the court's conclusion that, despite the absence of an explicit statement or promise, the writing is nonetheless "instinct with obligation."

Wood v. Lucy, Lady Duff-Gordon

Court of Appeals of New York, 1917.
222 N.Y. 88, 118 N.E. 214.

Appeal from Supreme Court, Appellate Division, First Department.

Action by Otis F. Wood against Lucy, Lady Duff-Gordon. From a judgment of the Appellate Division (177 App.Div. 624, 164 N.Y.Supp. 576), which reversed an order denying defendant's motion for judgment on the pleading, and which dismissed the complaint, plaintiff appeals. Reversed.

■ CARDOZO, J.^k The defendant styles herself "a creator of fashions." Her favor helps a sale. Manufacturers of dresses, millinery, and like articles are glad to pay for a certificate of her approval. The things which she designs, fabrics, parasols, and what not, have a new value in the public mind when issued in her name. She employed the plaintiff to help her to turn this vogue into money. He was to have the exclusive right, subject always to her approval, to place her indorsements on the designs of others. He was also to have the exclusive right to place her own designs on sale, or to license others to market them. In return she was to have one-half of "all profits and revenues" derived from any contracts he might make. The exclusive right was to last at least one year from April 1, 1915, and thereafter from year to year unless terminated by notice of 90 days. The plaintiff says that he kept the contract on his part, and that the defendant broke it. She placed her

^k Benjamin Nathan Cardozo (1870-1938) practiced in New York City after law school. He served as judge and later chief judge of the New York Court of Appeals, for which most of his significant opinions were written. President Hoover appointed him to the Supreme Court of the United States in 1932, upon Holmes's retirement. Cardozo's best-known jurisprudential work is a series of lectures entitled *THE NATURE OF THE JUDICIAL PROCESS* (1921).

indorsement on fabrics, dresses, and millinery without his knowledge, and withheld the profits. He sues her for the damages, and the case comes here on demurrer.¹

The agreement of employment is signed by both parties. It has a wealth of recitals. The defendant insists, however, that it lacks the elements of a contract. She says that the plaintiff does not bind himself to anything. It is true that he does not promise in so many words that he will use reasonable efforts to place the defendant's indorsements and market her designs. We think, however, that such a promise is fairly to be implied. The law has outgrown its primitive stage of formalism when the precise word was the sovereign talisman, and every slip was fatal. It takes a broader view today. A promise may be lacking, and yet the whole writing may be "instinct with an obligation," imperfectly expressed (Scott, J., in *McCall Co. v. Wright*, 133 App.Div. 62, 117 N.Y.S. 775; *Moran v. Standard Oil Co.*, 211 N.Y. 187, 198, 105 N.E. 217). If that is so, there is a contract.

The implication of a promise here finds support in many circumstances. The defendant gave an exclusive privilege. She was to have no right for at least a year to place her own indorsements or market her own designs except through the agency of the plaintiff. The acceptance of the exclusive agency was an assumption of its duties. *Phoenix Hermetic Co. v. Filtrine Mfg. Co.*, 164 App.Div. 424, 150 N.Y.S. 193; *W.G. Taylor Co. v. Bannerman*, 120 Wis. 189, 97 N.W. 918; *Mueller v. Mineral Spring Co.*, 88 Mich. 390, 50 N.W. 319. We are not to suppose that one party was to be placed at the mercy of the other. *Hearn v. Stevens & Bro.*, 111 App.Div. 101, 106, 97 N.Y.S. 566; *Russell v. Allerton*, 108 N.Y. 288, 15 N.E. 391. Many other terms of the agreement point the same way. We are told at the outset by way of recital that:

"The said Otis F. Wood possesses a business organization adapted to the placing of such indorsements as the said Lucy, Lady Duff-Gordon, has approved."

The implication is that the plaintiff's business organization will be used for the purpose for which it is adapted. But the terms of the defendant's compensation are even more significant. Her sole compensation for the grant of an exclusive agency is to be one-half of all the profits resulting from the plaintiff's efforts. Unless he gave his efforts, she could never get anything. Without an implied promise, the transaction cannot have such business "efficacy, as both parties must have intended that at all events it should have." Bowen, L.J., in *The Moorcock*, 14 P.D. 64, 68. But the contract does not stop there. The plaintiff goes on to promise that he will account monthly for all moneys received by him, and that he will take out all such patents and copyrights and trademarks as may in his judgment be necessary to protect the rights and articles affected by the agreement. It is true, of course, as the Appellate Division has said, that if he was under no

¹ In dismissing the complaint, the Appellate Division explained that "the plaintiff by this contract promises to collect the revenues derived from the indorsements, sales and licenses and to pay the cost of collecting them out of his half thereof, and to account to the defendant each month. But this promise on his part is not binding on him unless he places indorsements, makes sales or grants licenses, and nowhere in the contract has he bound himself to get these indorsements, or make the sales or grant the licenses. . . . It is quite apparent that in this respect the defendant gives everything and the plaintiff nothing and there is a lack of mutuality in the contract. . . . In fact the plaintiff in the nature of the case could not perform any of his various dependent agreements unless he placed indorsements, made sales or granted licenses to manufacture. And as the contract did not bind him to do any of these things, there is no provision of the contract which the defendant could enforce against him." 164 N.Y.S. at 577.

duty to try to market designs or to place certificates of indorsement, his promise to account for profits or take out copyrights would be valueless. But in determining the intention of the parties the promise has a value. It helps to enforce the conclusion that the plaintiff had some duties. His promise to pay the defendant one-half of the profits and revenues resulting from the exclusive agency and to render accounts monthly was a promise to use reasonable efforts to bring profits and revenues into existence. For this conclusion the authorities are ample. . . .

The judgment of the Appellate Division should be reversed, and the order of the Special Term affirmed, with costs in the Appellate Division and in this court.

[Three judges dissented.]

NOTES

(1) *Questions.* What is the rationale for the implication of a promise? To what extent does it turn on the fact that Lady Duff–Gordon gave Wood “an exclusive privilege”? Or on other of the “many circumstances” referred to by Cardozo? What were these circumstances? For a detailed comparison of the contract between Wood and Lucy, and an explicit exclusive dealings contract between Wood and another entrepreneur, see Victor P. Goldberg, [Desperately Seeking Consideration: The Unfortunate Impact of U.C.C. Section 2-306 on Contract Interpretation](#), 68 Ohio St. L.J. 103 (2007).

How does the statement of the rule in UCC § 2–306(2) guide your analysis of the case? (Would the UCC, if enacted at the time, have applied?)

(2) *What if Wood Wouldn't?* Might there be consideration even without the duty of reasonable efforts implied by Cardozo? Certainly the usual answer is No. But suppose Wood was the top agent in New York, one who could make the fortune of anyone he chose to take on as a client. Indeed, he would not even consider adding a client unless the potential client agreed in advance that, if he did, Wood would have the exclusive right to market the client's name and image, and that he would pay the client whatever portion of the revenue he thought appropriate. Illusory? Or, if this is the only way to become one of Wood's clients, isn't the potential client bargaining for the chance to be represented by Wood? Is it sufficient to rely upon the contractual duty of good faith and fair dealing?

(3) *Corbin and Llewellyn on Cardozo.* Professor Arthur Linton Corbin^m wrote this of Cardozo:

It cannot be said that he made any extensive changes in the existing law of contract. To state the facts of the cases, the decision, and the reasoning of the opinion will not show the overthrow of old doctrine or the establishment of new. Instead, it will show the application of existing doctrines with wisdom and discretion; an application that does not leave those doctrines wholly unaffected, but one that carries on their evolution as is reasonably required by the new facts before the court. When

^m Arthur Linton Corbin (1874–1967) practiced law in Colorado for four years after his graduation from law school in 1899. He taught at the Yale Law School from 1903 until his retirement in 1943, and became a leading authority on the law of contracts. His eight-volume treatise, *Corbin on Contracts*, which began to appear in 1950, ranks as one of the great legal treatises. He also served as Special Advisor, and as Reporter for the Chapter on Remedies, for the First Restatement of Contracts.

Cardozo is through, the law is not exactly as it was before, but there has been no sudden shift or revolutionary change.

Arthur L. Corbin, *Mr. Justice Cardozo and the Law of Contracts*, 39 Colum. L. Rev. 56, 56–57, 52 Harv. L. Rev. 408, 408–09, 48 Yale L.J. 426, 426–27 (1939).

Professor Karl Llewellyn used *Wood v. Lady Duff-Gordon* to illustrate Cardozo’s mastery in presenting the facts of a case.

You must remember that Cardozo was a truly great advocate, and the fact that he became a great judge didn’t at all change the fact that he was a great advocate. And if you will watch, in the very process of your listening to the facts, you will find two things happening. The one is that . . . you arrive at the conclusion that the case has to come out one way. And the other is, that it fits into a legal frame that says, ‘How comfortable it will be, to bring it out that way. No trouble at all. No trouble at all.’

Karl Llewellyn, *A Lecture on Appellate Advocacy*, 29 U. Chi. L. Rev. 627, 637–38 (1962). Llewellyn quoted the first five sentences of the opinion, noting how the defendant “is subtly made into a nasty person,” and then continued:

Does this sound . . . like a business deal? Does a business deal sound like a legally enforceable view? Nothing is being said about that. But watch it grow on you. And if I hadn’t stopped to tell you about it, it would have grown until you just took it, without a word.

Id. Can you give a similar reading to other parts of the opinion?

Might Cardozo have drawn his characterization of the defendant from the contract drafted by Lady Duff–Gordon’s lawyer?

(4) *Termination Clauses*. Parties often use termination clauses to reduce the risks that they assume by contracting. The contract in *Wood v. Lady Duff-Gordon* was, for example, terminable by either party without liability after one year. (As Judge Richard Posner has noted, “a year can be a long time in the fashion business.” Richard A. Posner, *Cardozo: A Study in Reputation* 96 (1990).)

If a termination clause is read as giving a party the power to terminate at any time at will, without more, that party’s promise will be held to be illusory. For example, a license agreement for the manufacture of Orange Crush gave the licensee the exclusive right and the duty to manufacture the soft drink in a specified territory, but provided that the licensee could terminate the contract at any time. In a suit by the licensee against the licensor, the court held that the licensee’s promise was not consideration for the licensor’s because the licensee “did not promise to do anything and could at any time cancel the contract.” *Miami Coca-Cola Bottling Co. v. Orange Crush Co.*, 296 F. 693 (5th Cir.1924).

If, however, a termination clause is read as requiring that notice be given some period of time before the termination becomes effective, or be given in writing, or in some other way restricts the right of termination, the promise will not be held to be illusory.

(5) *Termination Under the Code*. UCC § 2–309(3) requires “reasonable notification” for termination, except on the happening of an agreed event. Suppose a termination clause explicitly negates any duty of notification. Does that leave the agreement without consideration? Comment 8 to the section says: “An agreement dispensing with notification or limiting the time for the seeking of a

substitute arrangement is, of course, valid under this subsection unless the results of putting it into operation would be the creation of an unconscionable state of affairs.”

SUBSTITUTES FOR CONSIDERATION

The doctrine of consideration has been subjected to attacks for more than two centuries. Why, critics ask, should a promisor not be able to make a binding promise without receiving something in return from, and without reliance by, the promisee? Attempts at reform have focused on this problem, particularly with regard to gratuitous promises, and various substitutes have been suggested.

As long ago as 1765, in a case involving past consideration, Lord Mansfieldⁿ declared that a writing might substitute for consideration: “The ancient notion about the want of consideration was for the sake of evidence only: for when it is reduced into writing . . . there was no objection to the want of consideration. . . . In commercial cases amongst merchants, the want of consideration is not an objection.” *Pillans and Rose v. Van Mierop and Hopkins*, [1765] 97 Eng. Rep. 1035 (K.B.). His rule was short lived, for thirteen years later it was rejected by the House of Lords, which concluded that, “All contracts are, by the laws of England, distinguished into agreements by specialty [i.e., agreements under seal], and agreements by parol; nor is there any such third class as some of the counsel have endeavored to maintain, as contracts in writing. If they be merely written and not specialties, they are parol, and a consideration must be proved.” *Rann v. Hughes*, [1788] 101 Eng. Rep. 1014 (H.L.). Nonetheless, the view that the formality of putting a promise in writing should operate as an alternative to consideration continued to have appeal, and gained new vitality—particularly in connection with gratuitous promises—when the abolition of the seal raised the doctrine of consideration to even greater prominence.

A few states have general statutes that facilitate the making of binding gratuitous promises by recognizing some form of writing as a substitute for consideration. California, for example, makes a writing presumptive evidence of consideration. [Cal.Civ.Code § 1614 \(West 2001\)](#). In addition, Article 2 of the Uniform Commercial Code dispenses with the requirement of consideration in certain limited circumstances, as indicated on p. 185 and Note 2, pp. 361–362 below.

Civil law countries commonly have procedures by which a promisor may appear before a notary, a lawyer who holds an appointment from the state and who has no counterpart in common law countries, and make an irrevocable gratuitous promise. See [Arthur T. von Mehren, *Civil Law Analogues to Consideration: An Exercise in Comparative Analysis*, 72 *Harv. L. Rev.* 1009, 1057–62 \(1959\)](#). One explanation offered for the refusal by the American legal system to provide a similar mechanism is paternalism, the

ⁿ William Murray, first Earl of Mansfield (1705–1793), was a rival of William Pitt the Elder in school, in Parliament and in politics. He favored strict measures with the American rebels. His friend Alexander Pope helped him practice advocacy and later praised his eloquence in verse. Dr. Johnson said of him, “much can be made of a Scot if caught young.” Mansfield achieved greatness as a judge, being Lord Chief Justice from 1756 to 1788. One of his chief services was in rationalizing mercantile law. In commercial cases he made effective use of special “juries” of merchants, whose advice about their practices was sometimes instrumental in transforming custom into law.

view that a promisor's preferences regarding the enforceability of the promise should be disregarded for the promisor's own good. See Farnsworth, *Promises and Paternalism*, 41 *Wm. & Mary L. Rev.* 385 (2000). We consider the general question of whether legal constraints on a party's ability to contract are better understood as paternalism or protection in Chapters 4 and 6.

In a provocative article, Professors Daniel Farber and John Matheson proposed a rule that would enforce any promise "made in furtherance of an economic activity." See Daniel A. Farber & John H. Matheson, *Beyond Promissory Estoppel: Contract Law and the Invisible Handshake*, 52 *U. Chi. L. Rev.* 903, 929 (1985); see also Edward Yorio & Steve Thel, *The Promissory Basis of Section 90*, 101 *Yale L.J.* 111 (1991). Farber and Matheson argued that because firms commonly make promises for which they expect economic benefits—the promise to keep a plant open, for example—without receiving any specific bargained-for exchange but with the expectation of eventual economic benefit, such promises should be enforced. They concluded that a "rule that enforces promises designed 'to induce the creation of economic activity' simply 'reinforces the traditional free-will basis of promissory liability, albeit in an expanded context of relational and institutional interdependence.'" Farber and Matheson suggest that courts are already implementing the proposed rule using reliance to enforce commercial promises in cases where the plaintiff has shown little or no reliance at all; see *Vastoler v. American Can Co.*, cited in Note 2, p. 104 below. For criticism of the empirical basis of their argument, see [Robert Hillman, Questioning the New Consensus on Promissory Estoppel: An Empirical and Theoretical Study](#), 98 *Colum. L. Rev.* 580 (1998).

In their proposal Farber and Matheson drew a clear line between gratuitous promises that further economic activity and those that don't. "Unlike promises made in an economic setting, [non-commercial gratuitous promises] are not generally made to coordinate activities or generate reliance beneficial to the promisor. The presumption of utility that underlies our proposed enforcement of promises in furtherance of economic activity thus does not apply" Why is it that non-commercial gift promises find no haven, even among proposals that would abandon consideration in commercial dealings?

Consider also Judge Posner's view regarding the economic value of gratuitous promises. See [Richard A. Posner, Gratuitous Promises in Economics and Law](#), 6 *J. Legal Stud.*, 411 (1977). On this account, a promise's value depends in part on how likely it is that the promise will be kept. A rational promisee therefore discounts the promise to take the possibility of breach into account. This can work to the disadvantage of both the promisor and the promisee. If the promisor is reliable, she would like the prospective promisee to know that; the more valuable the promise, the greater the effect the promise will have on the promisee's actions.

One way to make a gratuitous promise worth more is to provide a means of enforcing it that the promisor may elect or not as she pleases. A low-risk promisor would commit herself readily; a high-risk promisor might want to keep her options open. It thus makes sense for courts to enforce gratuitous promises, because doing so makes the promises more valuable.