

## CONTRACTS

Final Examination  
Santa Barbara College of Law  
Spring 2001  
Instructor: Craig Smith

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Time Allotted - Three Hours

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An answer should demonstrate your ability to analyze the facts presented by the question, to select the material from the immaterial facts, and to discern the points upon which the case turns. It should show your knowledge and understanding of the pertinent principles and theories of law, their relationship to each other, and their qualifications and limitations. It should evidence your ability to apply the law to the facts given, and to reason logically in a lawyer-like manner to a sound conclusion from the premises adopted. Try to demonstrate your proficiency in using and applying legal principles rather than a mere memory of them.

An answer containing only a statement of your conclusions will receive little credit. State fully the reasons that support them. All points should be thoroughly discussed. Although your answer should be complete, you should not volunteer information or discuss legal doctrines that are not necessary or pertinent to the solution of the problem.

Unless a question expressly asks for California law, it should be answered according to legal theories and principles of general application.

### QUESTION 1

Larry, Moe and Curly jointly owned Blackacre. Larry and Moe, who lived in California, entered into negotiations with Shep, who also lived in California, to sell Blackacre to Shep. Contract documents were drawn up. The price was set at \$600 per acre. (1000 acres were being conveyed.) The contract documents specifically provided that once Shep paid \$600,000 into escrow and the contract documents were signed by Larry, Moe and Curly, title to Blackacre would pass to Shep and a deed evidencing title would be delivered to him.

Shep signed the contract documents and he promptly deposited the \$600,000 into escrow. The contract documents were signed by Larry and Moe and then mailed to Curly who lived in New York. Before Curly received the documents and could act on the matter, Larry and Moe were struck by a serious case of "seller's remorse" and called Curly and asked him not to sign the contract. It was the intention of Curly to execute these documents and he would have done so when the contract was sent to him except for the pressures put upon him by Larry and Moe to withhold his signature. Larry and Moe intended to use that fact as grounds to repudiate the contract. Curly suffered great uncertainties of mind concerning what his proper course of action should be. He went so far as to tell Moe that he felt that he should sign the contract but he didn't quite know what to do and he asked Moe to tell him directly not to sign as that would relieve his conscience. Moe obliged with this request. As a result, Curly refused to sign. Moe and Larry are refusing to deliver title.

The sellers are now repudiating the contract. The buyer, Shep desires to enforce the contract. It can be shown that as of the date Blackacre was to be conveyed it had a fair market value of \$700 per acre.

- 1). Is there an enforceable contract?
- 2). Assuming there is an enforceable contract, what is Shep entitled to by way of enforcement?

## QUESTION 2

Debbie negotiated an oral agreement with Paul, whereby Paul was to design and construct a house on property in Malibu. Paul was an unlicensed contractor, a fact which Debbie was at all times aware of.

Debbie consented to pay Paul the sum of \$4,000,000 for Paul's provision of design, construction, general contracting and supervision services. She further agreed that Paul would "be paid progress payments upon periodic percentages of project completion." The parties' oral agreement was subsequently memorialized in a written contract bearing an August 1997 date, which was delivered to Debbie in early October 1997. Debbie never signed the contract, despite her promise to do so. Between June 1996 and November 1997, Debbie assured Paul that the contract would be honored and that Paul would receive full compensation for the construction services he provided under the contract. Paul timely commenced work on design and construction of the house. Although the contract called for progress payments, Debbie never made any payments and Paul did not insist upon them being made.

In November 1997, when construction was almost 90% complete, Debbie terminated her agreement with Paul without paying him for any of the services he had provided under the Contract.

Is there an enforceable contract?

Regardless of whether or not there is an enforceable contract, is Paul entitled to any compensation for his work on the Malibu house?

### QUESTION 3

After his second marriage, Moe brought home from the office a folder containing two certificates of insurance on his life and placed it in a dresser drawer. His former wife, Margaret was named as beneficiary on these certificates and that designation was never changed. Yet when he brought them home Moe said to his wife, Edith: "the beneficiaries are changed . . . and he also said that he didn't want that women (Margaret) to have any more of his money." Edith promptly notified the issuer of the policies, Stooze Insurance Company, that the proceeds of the policies were to be paid to her. Six months later Moe's house burns down and Stooze Insurance, who also issued the fire insurance policy, pays off on the loss. One year later, Moe dies. Both Edith and Margaret are claiming entitlement to all of the proceeds of the life insurance policies.

Stooze Insurance Company comes to you and asks the following questions:

Who should it pay the proceeds (\$1,000,000) of the life insurance policies to, Edith or Margaret?

It turns out that after Stooze paid off on the fire insurance policy they discovered that Moe had not made premium payments on that policy for several years. Can anything be done to recover the \$25,000 in unpaid premiums on the fire insurance policy?

Would it make a difference in Stooze's ability to recover if the \$25,000 in unpaid premiums related to the life insurance policies rather than the fire insurance policy?

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### Sample Answer to Question 1

Larry, Moe and Curly have promised to sell Blackacre. Promises can be categorized as being either absolute or conditional. In the instant case, the promise was conditional, i.e., would only become effective upon the happening of certain events. A condition is an act or event not certain to occur, which affects a duty of performance. Conditions can be either precedent or subsequent. The occurrence of a condition precedent triggers the obligation to perform some act or duty. The occurrence of a condition subsequent discharges the performance of a duty that has already arisen.

Here, the duty to convey Blackacre did not arise until the \$600,000 was deposited into escrow and all three owners signed. Here, only two of the three owners signed. Normally, failure of a condition excuses performance. However, Larry and Moe by influencing Curly not to sign, actively procured the failure of a condition. A party may not assert failure of a condition as a defense when they caused that condition not to occur. The contract is enforceable in spite of the fact it lacked Curly's signature.

Shep's entitlement to damages or other relief. The objective of contract damages is to put the injured party in the position they would have been in had the contract been fully performed. In this case, that means Shep would have title to Blackacre. If Shep were purchasing Blackacre for investment purposes or to resell then monetary damages would be an adequate remedy. That could be measured as the difference between the contract price and the market price at the time of the breach.

On the other hand, if Shep wanted to live on Blackacre monetary damages are probably not sufficient. Shep would be entitled to specific performance. Every piece of real property is unique with respect to its location and hence Shep would be entitled to a court order conveying Blackacre to him.

## Sample Answer to Question 2

Here we have an oral agreement to design and build a house. Is it within the Statute of Frauds? The Statute of Frauds requires that certain types of contracts be evidenced by some written note or memorandum thereof, signed by the party to be charged. Here, there is no such note or memo, Debbie, the welching party, having never signed. But is it within the Statute of Frauds? The only possible clause that might bring it within the statute would be that provision that says a contract not to be performed within the space of one year from the making thereof is within the statute. The important language of that clause is "by its terms." Even though it may be unlikely to complete a \$4,000,000 house within one year it is not impossible. There was nothing in the terms of the contract that would require performance in excess of one year, hence, the Statute of Frauds is not brought into play. The oral contract is enforceable.

Paul's status as an unlicensed contractor might be a defense that Debbie could assert. Court's will not enforce illegal bargains. Whether a licensing statute can be asserted as a defense depends upon the underlying purpose of the statute. If the purpose of requiring a license is to insure a minimum level of skill or competence, then the statute is to protect the public and the unlicensed individual cannot enforce the contract. On the other hand, if the purpose of requiring a license is merely to raise revenue, then the fact that a party is not licensed is not a defense. Here, the underlying purpose would appear to be to insure that contractors who undertake construction projects are competent. Hence, Debbie could successfully assert Paul's lack of a license as a defense. Furthermore, even though the contract called for periodic progress payments, Paul may have waived his right to them. Waiver is a relinquishment of a known right. Paul, by his conduct, led Debbie to believe he would not insist upon periodic payments.

Although there is no enforceable contract Paul may be entitled to compensation on a quasi contract theory. Allowing Debbie to retain the benefit of a \$4,000,000 house for nothing would result in unjust enrichment. To avoid this, the court may allow Paul to recover in quantum meruit or the reasonable value of his services. This may be less than the \$4,000,000 contract price. However, the quantum meruit measure would set the contract price as a ceiling on recovery.

### Sample Answer to Question 3

Moe's former wife Margaret, is a third party beneficiary of the contract between Moe and the insurance company. A third party who is not in privity of contract can have enforceable rights if she can show that the original promisee intended to confer a benefit upon her either in the form of a gift (donee beneficiary) or to discharge a debt (creditor beneficiary) and the promisor reasonably understood that intention. Moe, by contracting with the insurance company for its promise to pay Margaret a monetary benefit upon his death obviously intended to confer a gift benefit upon Margaret. As a result, she would have enforceable rights under the contract. Normally, the original parties to the contract are free to modify or eliminate the third party's rights. However, their ability to do so terminates once the third party's rights have vested. Vesting takes place when the third party learns of the contract and assents to it or changes their position in reliance on it. Here, there are no facts to suggest that Margaret assented to the contract or detrimentally relied upon it. Hence, Moe would be free to terminate her rights as a beneficiary.

Having terminated Margaret's rights as a beneficiary, it appears that Moe attempted to assign the benefits to Edith. An assignment is a transfer of rights. The general rule is that contract rights may be freely assigned. Was the assignment effective? No particular words are necessary to create an assignment. All that is required is some manifestation that the assignor is making a present transfer of an existing right. Margaret notified the insurance company of the change. Once notified, Stooze Insurance became duty bound to deal with the assignee. If they made payment of the proceeds to the assignor (or Margaret the original third party benny) they put themselves at risk for having to pay twice. Based on this analysis Stooze should pay the proceeds to Edith.

The assignee stands in the shoes of the assignor. They take the assignment subject to all the claims and defenses that could have been asserted against the assignor. In other words, the promisor may assert against the assignee any claims and defenses that could have been asserted against the assignor. Here, Stooze could have asserted its claim of failure to pay the fire insurance premiums against Moe. However, notice of assignment cuts off the right to set-off claims and defenses that do not arise out of the right being assigned and that accrues after notice was given. Since Margaret gave notice of assignment Stooze has lost its right to set off this unrelated claim.

The same is not true for claims that arise out of the right being assigned. These claims can be recouped regardless of when they arose. Stooze is entitled to recover the \$25,000 in unpaid life insurance premiums since they relate to the very right that was being assigned.