

CONTRACTS
Santa Barbara College of Law
Mid-Term Examination
Fall 1991
Instructor: Craig Smith

Time Allotted - Two Hours (Essay Portion)

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

Bert orally agreed to buy 30 tons of Chardonnay grapes from Ernie with an option to purchase 70 more tons. Nothing was said as to price although the parties orally agreed that if Ernie failed to deliver the total amount of grapes ordered, he would pay Bert a \$10,000 penalty. Afterward Bert entered into numerous contracts to sell 125 tons of Chardonnay grapes to other wineries.

Unexpectedly cold weather and high winds caused the grapes to shrivel up and dehydrate resulting in Ernie's inability to deliver the total amount of grapes called for in the contract and the option. After delivering 37 tons, Ernie told Bert that he would not ship any more grapes unless Bert agreed to a modification of their contract waiving the penalty clause. Bert was unaware of any place he could obtain replacement grapes at that late date. Reluctantly, Bert orally agreed to the modification. Ernie had the modification written up, signed it and sent it to Bert for his signature. Bert neither signed nor responded to the modification in any way. Ernie delivered a total of 82 tons of grapes to Bert under the contract. Ernie presented Bert with an invoice for \$67,000, which represented the balance due without penalty. Bert sends Ernie a "payment-in-full" check in the amount of \$57,000, the balance due less the penalty discount. Ernie writes on the back of the check "not payment in full" and endorses and cashes the check.

Ernie then filed a lawsuit alleging breach of contract and seeking to recover \$10,000.

In the lawsuit between Bert and Ernie who will prevail? Discuss.

QUESTION 2

On July 4, 1990, Moe mailed to Larry a written offer to sell ten shares of an unlisted stock at \$60.00 per share. Larry was given four days from the date of the letter to accept. The offer was received on July 6 at 2 p.m. At 3 p.m. on July 6, Larry mailed a letter to Moe which stated in part: "will purchase ten shares at \$55.00 per share. . . ." At 11 a.m. on July 6, however, Moe had sold the ten shares to Curly for \$65.00 and at 1 p.m. of the same day had mailed a letter to Larry revoking the offer. Larry who was blissfully unaware of Moe's activity, learned at 4 p.m. on July 6 that the market price of the shares might increase and, at 5 p.m. on the same day, telegraphed Moe to "disregard letter . . . will take offered stock for \$60.00 per share." Larry's telegram of July 6 was received by Moe at 9 a.m. on July 7. Larry's letter of July 6 was received by Moe at 2 p.m. on July 8. Moe's letter of July 6 was received by Larry at 2 p.m. on July 8.

Larry claims that he has a contract with Moe for the purchase of the stock. Is this contention correct? discuss fully and in your answer deal with the following:

- (a) The legal right of Moe to revoke his offer before it is accepted.
- (b) The legal effect, if any, of Larry's letter of July 6.
- (c) The legal effect, if any, of Moe's sale of the stock to Curly.
- (d) The legal effect, if any, of Moe's letter of July 6.
- (e) The legal effect, if any of Larry's telegram of July 6.

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"MODEL ANSWER"

QUESTION 1

STATUTE OF FRAUDS

Who prevails depends upon whether the oral promise to modify and waive the penalty clause is enforceable. The original contract of the parties was an oral one for the sale of goods for a price of \$500 or more. Hence it was within the statute of frauds (UCC 2-201) and has to be evidenced by some writing signed by the party to be charged in order to be enforceable. The writing need only be sufficient to indicate that a contract has been made and that it state a quantity term. The quantity term need not be accurately stated by the contract but is not enforceable beyond the quantity stated. The price term may be ommitted from the writing.

Nonobjecting Merchant Rule

Here, the only writing between the parties is the memorandum regarding the modification. It would appear to indicate that a contract has been made. However it does not appear to state a quantity and it is only signed by Ernie and not by Bert who is the party to be charged. It may nevertheless be a sufficient memorandum under the "nonobjecting merchant rule." (UCC 2-201(2).) That rule states that where a confirming memorandum, sufficient against the sender is sent to the opposing party, and the opposing party, having reason to know of its contents, fails to object to it within a reasonable time, the contract is enforceable against the receiving party just as if he had signed it.

Satisfaction of the Writing Requirement

Here, Bert never objected to the memorandum within a reasonable time. It is enforceable against him as if he had signed it provided that it would have been enforceable against the sender. Although the memorandum was signed by Ernie there is no indication it stated a quantity term. A memorandum sufficient to satisfy the writing requirement of the UCC need not state much but it must state a quantity term. It would not have been enforceable against Ernie. This is fatal to the effectiveness of the memorandum in satisfying the writing requirement.

Partial Performance

Another exception to the statute of frauds is for contracts where the goods have been delivered and paid for. (UCC 2-101(3).) Even in the absence of satisfaction of the writing requirement an oral contract within the statute of frauds is enforceable to the extent it has already been performed. Here, Ernie delivered and Bert paid for in excess of the 30 tons of grapes called for under the contract. To that extent the contract is enforceable notwithstanding lack of compliance

with the statute of frauds. The remaining issues of enforceability relate to the "option" for an additional 70 tons.

ENFORCEABILITY OF OPTION CONTRACT

An option contract is an offer which cannot be revoked for a stated period of time. At common law an option, to be enforceable, had to be supported by separate consideration. Once again however, this contract is governed by the UCC. Under UCC 2-205 an option needs no consideration to be binding if a merchant in a signed writing states that the offer will remain open for a specific period of time. Although this rule would otherwise apply to this situation, there is no signed writing which states that the offer is "firm." Ernie is free to revoke his offer to sell an additional 70 tons any time prior to acceptance. Under this analysis the offer to sell 70 additional tons subject to the \$10,000 penalty was revoked when Ernie refused to deliver additional quantities unless the penalty was removed. He in effect made a new offer to sell 70 tons with no additional penalties.

VALIDITY OF MODIFICATION

Even if the portion of the agreement relating to the 70 tons was deemed nevertheless enforceable Bert would argue that the modification of the contract waiving the penalty is unenforceable. At common law a modification of a contract had to be supported by new consideration. To do otherwise would violate the preexisting duty rule which states that promising to do what one is already legally obliged to do is not consideration. Once again the UCC liberalizes this common law rule. Section 2-209 provides that parties to a contract for a sale of goods may modify free of the constraints of the preexisting duty rule so long as the modification is sought in good faith. Ernie will argue that the modification was in good faith as the result of unanticipated extreme weather conditions. Bert will argue that he was forced to assent to the modification by virtue of coercion or duress. While the simple threat to break a contract does not amount to duress the fact that the promisor has no other viable alternatives may result in duress. Here, Bert was unsuccessful in obtaining comparable goods elsewhere and was committed to making his own deliveries. Bert will argue that he was forced to capitulate to the modification as the result of an unlawful threat to break the contract. Hence, the modification is not enforceable.

DEFINITENESS

The terms of a contract must be sufficiently definite to be enforced. Here, there was nothing said as to price. Price is generally considered to be a material term and at common law the omission of a material term rendered a contract unenforceable.

However, as discussed above, this contract for the sale of goods is within the provisions of Article 2 of the UCC. Section 2-305 provides that the parties can conclude a contract for the sale of goods even though they have left the price term open. In such a case it is assumed that the parties bargained in terms of a "reasonable" price. I.e., the market price at the time and place of delivery of the goods. The absence of a price term is not fatal to the enforceability of this contract.

ACCORD & SATISFACTION

What the case really boils down to is whether there was an effective accord and satisfaction. An accord and satisfaction is the offering of some performance different from that which was originally called for and the acceptance of that performance as a full performance.

A "payment in full" check operates as an accord and satisfaction when the creditor negotiates the check with awareness of the terms upon which it was offered. Bert was certainly aware that the check was offered on a "payment-in-full" basis (after all he scratched the condition out). Nevertheless he negotiated the check. Traditionally, a creditor could write all manner of disclaimer over the check to no avail. If she negotiated the check aware of the basis on which it was offered she entered into a valid accord and satisfaction. Once again the UCC liberalizes that traditional rule. One may now cash a check under protest by indicating on the instrument a reservation of rights and no accord and satisfaction is entered into. This is exactly what Ernie did. As discussed earlier, the only remaining defense to liability for the \$10,000 penalty is whether removal of it was assented to in good faith as opposed to being the product of duress or coercion. On this issue Ernie will prevail as he had no reasonable commercial alternative other than to capitulate to the modification.

QUESTION 2

Larry's contention that he has a contract to purchase the stock is correct.

The legal right of Moe to revoke his offer before it is accepted.

An offer may be revoked anytime prior to acceptance. The only exceptions to this rule are situations of option contracts or detrimental reliance. An option contract is an offer that is irrevocable for a stated period of time. However, an option contract must be supported by separate consideration. Otherwise, the promise to keep the offer open, in this case for four days from the date of the letter, is merely gratuitous. This offer is subject to the usual rule that it may be withdrawn any time prior to acceptance.

An offeror may lose the power to revoke the offer prior to acceptance where it is foreseeable that the making of the offer will result in substantial action or forbearance on the part of the offeree, such action or forbearance actually results, and injustice can only be avoided by enforcing the promise. None of these conditions exist. This was not an offer which invited acceptance by performance (a unilateral contract) but rather invited acceptance by the making of a promise. No substantial action or forbearance was foreseeable on the part of the promisee as a result of the promisor merely making the offer.

The legal effect, if any, of Larry's letter of July 6.

Larry's letter of July 6 was a counteroffer. At common law an acceptance had to be the mirror image of the offer. If it varied from the terms of the original offer in any manner, no matter how trivial or insignificant, it operated as a counteroffer or rejection. I.e., a counteroffer has the same effect as an outright rejection. It terminates the power of acceptance. The offeree cannot revive the negotiations by later attempting to accept the original offer. Since a counteroffer is a rejection it is governed by the rule that a rejection is effective upon receipt. Hence, it was effective at 2 p.m. July 8.

The legal effect, if any, of Moe's sale of the stock to Curly.

The power of acceptance is terminated when the offeror takes any action inconsistent with keeping the offer open and the offeree receives reliable information to that effect. This is sometimes called "indirect revocation."

Here, Moe certainly took action inconsistent with keeping the offer open (he sold the stock to someone else). The problem is there are no facts to indicate that Larry learned of this fact from any reliable source (or from any source at all for that matter.)

The legal effect, if any, of Moe's letter of July 6.

The power of acceptance is terminated by express notice of revocation. Moe's July 6 letter was certainly such express notice. However, a revocation is not effective until it is received. If this were the only circumstance then the revocation did not take effect until 2 p.m. July 8 when it

was received. Coincidentally, this is the same time that Larry's counteroffer and rejection was received.

The legal effect, if any of Larry's telegram of July 6.

An acceptance is an unequivocal assent to the terms of the offer made in the manner or mode invited or required by the offeror. Acceptance results in a contract with the consequence that neither party can withdraw from the bargain without incurring liability to the other.

The acceptance in this case is unequivocal. ("Will take offered stock for \$60.00 per share." No manner or mode of acceptance was suggested or required therefore any reasonable manner or mode under the circumstances is effective. Considering that the offer was made by mail, telegram is at least as expedient if not a more efficient mode of communication and hence is reasonable. Under the "mailbox rule" of Adams v. Lindsell acceptance is effective upon dispatch. I.e., when it is put out of the control of the offeree. Hence acceptance was effective at 5 p.m. July 6th. This was prior to the rejection by counteroffer becoming effective (2 p.m. July 8) and prior to the express revocation becoming effective (2 p.m. July 8). And as stated before Larry never received reliable information that Moe had already sold the stock so there was never an effective indirect revocation.

There is an enforceable contract for the sale of the stock between Moe and Larry.