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Contracts
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Outline

I. Introduction

II. Discussion

- A. The Elements and Nature of a Contract
- B. Written and Oral Contracts
- C. Remedies for Breach of Contract

III. Article 2 of the Uniform Commercial Code

IV. Comments/Examples

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Introduction

- What is a contract?
 - Another simple definition is "A legally enforceable promise"
 - The fact that it is legally enforceable makes all the difference in the world otherwise who would trust other people enough to do business with them?
 - Once you are in a contract it is very difficult, if not impossible, to get out of



Contracts: Basic Principles

- Contracts are only binding upon the parties that entered into the contract
 - I cannot enter you into a contract without your permission
- Contracts can be created by words or even by conduct
- Not all agreements must be in writing in order to create a contract
- Some agreements must be in writing in order to create a contract

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Contracts: Elements

There are five required elements for a contract:

1. Legally competent parties
2. Proper subject matter
3. Offer
4. Acceptance
5. Consideration

****If you are missing any of these then you do not have an enforceable contract!

Legally Competent Parties

Each party must be "competent" to enter into a contract

- o Which really is not as high a bar as you probably think that it is

There are two basic areas involved:

1. Age
2. Sufficient mental capacity
 - Mental illness
 - Intoxication

Legally Competent Parties

Age

- The magic age is 18
 - o If you are under 18, can you even enter into a contract?
 - o Sure, but the minor can rescind a contract if they want to unless they are purchasing a necessity (food, clothing, shelter, medical care, etc...)
- If they enter into a contract when they are a minor then they have the chance to "ratify" the contract when they turn 18 and if they do it then it is binding just as if they entered into it after they turned 18

Legally Competent Parties

Hypotheticals:

- Parrison Hitman is 17, but because of his extreme amount of facial hair he looks to be about 30. He buys a used truck and wrecks it. What can he do?
- Same facts, but this time he checks into a motel room and the clerk did not check to see if he was over 18 and Parrison refuses to pay because he is a minor.

Legally Competent Parties

Intoxication:

- It is almost never allowed to use the fact that one of the parties was intoxicated to void a contract. Why?
- Because it's their fault that they got intoxicated (barring some weird scenario where they forced or drugged).

Ex. A person is falling down drunk and some one comes up to them and offers to buy their car for a bag of Skittles...what should happen?

Legally Competent Parties

Mental Illness:

- In some ways it works a lot like being a minor and entering into a contract.
- A court has to find that a person is incompetent or there is something like an involuntary commitment in that person's recent past.
- If a person is judged to be mentally incompetent then that contract can be ratified either by that person when they become sane or if their guardian ratifies it.

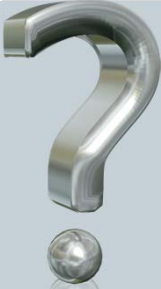
Proper Subject Matter

Every contract is a contract for *something*

- i.e., goods, land, services

That something must be “proper”

- In general, this means it must be legal.
 - i.e. you cannot take out a contract on somebody's life.



Proper Subject Matter

Examples:

- Parrison finally reaches age 18 and agrees to rob a gas station.
- I agreed to broilers under a production contract...does it matter that this isn't a tangible good?
- Steve wants to purchase famous paintings of Chuck Norris in action poses...

Offer

For an agreement to be considered a valid contract, there must be an offer

What is an offer?

- An offer is a statement that creates a power of acceptance in the **offeree** and a corresponding liability on the part of the **offeror**

Offer

To constitute an offer, a statement must:

- Create a reasonable expectation in the offeree that the person making the offer is willing to enter into a contract.

Ex. My truck breaks down for the 3rd time this week and while I'm cussing at the truck I make the statement that "I'd sell this piece of crap to the first person that offers me \$5!" A bystander that is watching me make a scene pulls out a \$5 bill and says "I accept"

Acceptance

In order for an agreement to be a valid contract, there must be acceptance by the offeree of the offer made by the offeror

Example: A says to B, "I'll sell you that tractor for \$5,000, as is."

- B says, "would you take \$4,000"? - What is this?
- B says, "for that piece of \$#%&"?
- B reaches out and shakes A's hand and says, "you got yourself a deal."

Offer + Acceptance

The offer and acceptance has to match up exactly for a contract to be formed

- One does not really matter without the other
- If they don't match up exactly then there is no agreement.
 - In the example about the tractor suppose that the people are talking about different tractors or that the buyer only wants to pay \$4,999 instead of the \$5,000.

Together they create the required "meeting of the minds" or mutual assent

Offer + Acceptance

- A “meeting of the minds” occurs when the offeror has clearly manifested a willingness to enter into a contract in such a manner that the offeree knows that assent is all that is necessary to conclude the bargain
- The acceptance must occur before the offer expires or is revoked
 - Offers can be revoked at any time before acceptance unless you have something that holds the offer open.

Legally competent parties + Proper subject matter + Offer + Acceptance + Consideration

=

Contract

Consideration

For an agreement to be a valid contract, there must be consideration

What is “consideration”?

- something of value such as money, services, a promise to do or not to do something
- If there is no consideration then you just have a promise to make a gift...which is probably not enforceable

Contracts: Elements

There are five required elements for a contract:

1. Legally competent parties
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Types of Contracts

There are two basic types of contracts:

1. Express
 - formed by express language, either in writing or verbally
2. Implied
 - Created over a course of dealing between the parties

Types of Contracts

Examples:

- Rusty contracts to have his soybeans custom harvested
- Rusty's grandmother hates beer and offers him \$10,000 to give it up permanently
- You rent a house to live in for the year.

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General Principles

1. Not all agreements must be in writing to form a valid contract.

- McDonald's drive through...walk me through it

2. Some agreements must, by law, be in writing in order to form a valid contract

3. Sometimes, there are exceptions to the principle that some agreements must be in writing in order to form a valid contract

Statute of Frauds

- All states have adopted some version of the original statute of frauds
- Original statute was enacted in 1677 by English Parliament
- The 1677 law required that certain types of oral agreements could not be enforceable unless the agreement had been reduced into writing
 - Why?

Statute of Frauds

The 1677 English statute set forth five main areas:

- Promise to pay any debt or damages out of an estate
- Promise to pay for the debt of another person (i.e., guarantee a loan)
- Marriage/Bethrothal contracts

(cont'd)

Statute of Frauds

- Promise that cannot be performed within 1 year of the date of the promise
- Promise concerning an interest in land/real property

In general, each of these has been adopted into each states' laws in some form.

- There's not a whole lot of bethrothal contracts floating around anymore though

General Principles


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2. Some agreements must, by law, be in writing in order to form a valid contract
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Statute of Frauds: Exceptions

There are two exceptions to know:

1. Partial performance
2. Promissory estoppel

These are common law doctrines (judge made) so it is up to the Judge to determine if they want to apply it.



Partial Performance

This exception arises when a person undertakes conduct in furtherance of an alleged promise

Example: Homeowner who promises to sell property to neighbor upon a certain date so long as neighbor takes care of property until that date.

Promissory Estoppel

- What is promissory estoppel?
- PE is a legal concept that prevents a party from using the statute of frauds as a defense
 - This is usually a question of fairness. Did one party try to use the statute of frauds to put the other party into a bad situation?

Promissory Estoppel

Example:

- A owns a theater. B is a set designer. A promises to pay B a percentage of profits from upcoming production that will go on for more than one year, if B will design set for production.
- B performs promise, but A refuses to pay because his lease on building expired.
- A argues that the promise was not enforceable. Court **could** step in decide it was enforceable via PE.

Promissory Estoppel

Example:

- Landowner promises to rent farmland to Rusty for longer than one year if Rusty helps out with several projects on Landowner's farm and residence.
- Rusty performs his part of bargain, and Landowner later refuses to rent farmland to Rusty and says statute of frauds renders any promises unenforceable
 - What will the court say?

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Common Contract Issues

- **What happens in these situations?**
 - “Form” Contracts
 - Modification of the contract
 - Death of a party
 - Breach of a covenant
 - Breach of the contract
 - Termination

“Form” Contracts

- Form contracts are used everyday...there is nothing wrong with using them
- There are issues that you need to be aware of...
 - EVERYTHING in the contract is binding
 - The fact that you (and the other party) do not even know what all of the clauses mean does not matter



Standard Form Contracts

- Read them carefully and ask questions about clauses that you do not understand
- Modify them (covered in a minute)
 - and get written approval from authorized representative
- Use attachments if necessary
 - e.g., letters, memos, specifications
- Ambiguities interpreted against the drafter/person that provided the contract.
 - What does this mean?

Parol Evidence Rule

- Court will not permit evidence of prior or contemporaneous oral statements if there is a complete written agreement. What does this mean?
 - The exception – ambiguities in written statement
- Moral of the story
 - READ THE CONTRACT CAREFULLY!
 - GET IT IN WRITING!

Modification of the Contract

You can change a contract form before it is signed, but can you modify a contract **after** it has been signed?


- Absolutely...so long as all of the parties to the contract agree then you can change it.
- If the contract is written then the changes must be in writing as well (the Parol Evidence Rule)
 - This rule is not absolute, but it is very difficult to prove that the contract has been modified.

Modification of the Contract

- For simple modifications (such as changing a date or getting rid of a clause) some will just strike through the language they do not want:
 - Example: ~~Not to assign this contract in whole or in part without the written consent of the seller.~~
- And have all parties sign/initial beside it and write in the date of modification
- For major changes (or lots of small changes) it is easier and safer to just write up a new contract

Modification of the Contract

- Use an attorney to modify contracts!
 - Typically not expensive
 - It is worth a couple of hundred \$ to modify a contract worth tens of thousands of \$
 - Every word matters in a contract so it is important to have an expert look at it
 - If you provided the contract then the ambiguities are held against you



Death of a Party


- What happens when either the landowner or the buyer dies?
- Usually nothing changes! The estate of the decedent (usually their family) will continue the contract until it runs its course.
- Most contracts remain relatively unaffected by the death of one of the parties.
 - The exception is for contracts that involve a personal service
 - This means that if something happens to you a court will not make your children complete your duties as a forester under the contract.
 - Does this make sense?

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Breach of Covenant

- If the seller or buyer breaks one of their promises in the contract is there a right to terminate the agreement?
 - Generally, No!
 - Unless the contract specifically allows for it. The normal remedy is to sue and either get damages or an injunction against further breaches.
- Office lease example



Breach of Contract



- Breach of Contract:
 - Very similar to the breach of a covenant in a contract, but instead of just one portion of the contract being broken, the violation here is severe enough that the contract itself is broken.
- Can you stop performing if the other party breaches the contract?
 - Sometimes you can, but only if the breach warrants your nonperformance as well. Minor problems arise in contracts all of the time and courts realize the fact that the world isn't perfect.

Breach of Contract, continued

- The problem that often arises in these cases is where you entered into a contract and something happens which causes you to want to get out of the agreement.
 - Timber values skyrocket, you find out some things that you did not know about the other party in the contract, etc...
- You will need to go to an attorney **BEFORE** assuming that a contract is broken

Remedies for Breach of Contract

Scenario:

- There is a valid contract, but one of the parties has failed, for whatever reason, to satisfy their end of the bargain
- So, now what?
 - Excused performance **OR**
 - Breach of contract

Excused Performance

There are three possibilities for “excused performance”:

1. Impossibility of performance
2. Impracticability
3. Purpose of contract has been frustrated

Impossibility of Performance

Basically, an event occurs that makes impossible the performance of a contract

Examples:

- Farmer contracts to sell bull that dies before delivery
- Rusty contracts to sell farm equipment but it is destroyed by tornado
- Rusty agrees to transfer poultry litter to another farmer, but a federal district court issues an injunction prohibiting all spreading of poultry litter

Impracticability

- Impracticability occurs when a contract could still theoretically be performed, but an event has occurred that makes it impracticable to do so
- Must result in a situation where, if the contract were performed, it would result in extreme and unreasonable difficulty

Impracticability

- Examples:
- Farmer contracts to have crops custom harvested. Custom harvester's equipment is destroyed by vandals and he is unable to perform on time.
 - Court might excuse nonperformance on grounds of impracticability. They could also say that they should rent some equipment and do their job.
- I'm contracted to build a house beside the Mississippi River and a flood changes the course of the river so that the property is now under the river. Is it possible to divert the river (Yes), but is it practical?

Purpose of Contract Has Been Frustrated

Occurs when a contract is not performed, and it would be neither impossible or impracticable to perform the contract

Example:

- Farmer contracts with aerial applicator to spray cotton crop. Mississippi River floods, crop is destroyed before it is sprayed. Farmer's promise to pay most likely not enforceable b/c subject of contract is destroyed.

Remedies for Breach of Contract

Scenario: There is a valid contract and one of the parties refuses to or fails to perform, and there is no basis for “excused performance”

There are 4 basic options:

1. Damages
2. Liquidated Damages
3. Specific performance
4. Rescission and restitution

Damages

In the event of a breach of contract, one party will seek money damages sufficient to make the injured party “whole”

- The general rule is that money makes almost every thing better.
- Stipulated or liquidated damages are sometimes called for *in the contract*
 - Typically damages are not meant to punish, but to make “whole”...this is an exception



Liquidated Damages

- Some contracts have provisions in them calling for “liquidated damages.”
- This is where the contract itself will set forth the damages for breach of contract.

Example: “If either party breaches the contract then they will pay \$100,000 and the attorney fees for the prevailing party”

- Even if the actual damage was only \$1,000 the breaching party has to pay the liquidated damages

Specific Performance

In addition, or instead of, seeking damages, a party may seek to have the contract performed as agreed, known as "specific performance"

Examples:

- Sale of land
- Buying a racehorse
- Having your portrait painted by a famous artist

Rescission and Restitution

This remedy arises when it is in the injured party's interest that neither damages be sought nor specific performance

Rescission: "cutting" the contract; termination of contract; declaring that it does not exist or that parts of it do not exist anymore

Restitution: Injured party is made whole, typically payment for benefits already transferred

- I sold you land and you didn't pay for it so I want my land back

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Comments/Examples/Questions
